

Legislative Analysis



INCREASE TOBACCO TAX

Mitchell Bean, Director
Phone: (517) 373-8080
<http://www.house.mi.gov/hfa>

House Bill 4389

Sponsor: Rep. Coleman Young

Committee: Tax Policy

Complete to 3-27-07

A SUMMARY OF HOUSE BILL 4389 AS INTRODUCED 3-1-07

The bill is intended to implement Governor Granholm's proposal to increase the tax on cigarettes from \$2.00 per pack to \$2.05 per pack and to double the tax on other tobacco products from 32 percent of the wholesale price to 64 percent of the wholesale price. This proposal accompanied the FY 2007-08 Executive Budget Recommendation.

The proposal also intends to direct the increase in revenues to the Medicaid Benefits Trust Fund and hold the other funding recipients from tobacco taxes harmless from any resulting reduction in revenue due to decreased consumption.

[As introduced, however, the bill would increase the tax on cigarettes from \$2.00 per pack to \$2.005 per pack. It increases the cigarette tax by one-quarter of one mill (0.25) rather than by 2.5 mills. The introduced version also directs increased revenues to the General Fund rather than the Medicaid Benefits Trust Fund. It is expected that technical amendments will be made to the bill to implement the Governor's proposal.]

The bill would amend the Tobacco Products Tax Act to increase the excise tax on cigars, cigarettes, noncigarette smoking tobacco, and smokeless tobacco beginning June 1, 2007. The bill would also require licensees and retailers to pay the additional tax for any inventory on hand as of June 1, 2007.

Also, the bill provides that the current 32% tax on other tobacco products would remain in place through May 30, 2007, and the 64% tax would take effect June 1, 2007. The bill would need to be amended to extend the current 32% tax to May 31, 2007.

MCL 205.427 and 205.432

FISCAL IMPACT:

House bill 4389 is part of the executive recommendation. This bill would increase tobacco tax revenue by an estimated \$18.1 million in FY 2006-07 and \$57.6 million in FY 2007-08. The estimate assumes a decline of 0.5% in consumption of packs of cigarettes and a 10.3% decline in the consumption of other tobacco products. Under the executive recommendation, this revenue would be earmarked to the Medicaid Benefits Trust Fund and the other funds that receive tobacco tax revenue would be held harmless.

Technical changes will be needed to ensure that the bill corresponds to the executive recommendation.

BACKGROUND INFORMATION:

The Executive Budget presentation states, "The current tax rate on other tobacco products (OTP) is 32 percent of the wholesale price – which is significantly lower than the current tax rate on cigarettes. The cigarette tax of \$2 per pack averages between 80 and 150 percent of the wholesale price on a percentage basis, depending on whether the cigarettes are a premium or a discount brand. This significant tax differential has created an incentive for consumers to substitute tobacco products taxed as OTP for cigarettes. In addition, manufacturers have created new products that share many of the characteristics of cigarettes (white wrapping paper, filters, and packs of 20) but are sold as 'little cigars.' These products have a considerable price advantage due to the different tax rates assessed on OTP compared to cigarettes, and it appears these little cigars have experienced increased sales while cigarette sales have declined."

History of Tobacco Tax Rates

The state's cigarette tax dates back to the enactment of 1947 PA 265, which first imposed at tax of 1.5 mills per cigarette (3¢ per pack). Over the next several decades, the tax rate remained relatively low; by 1988, the rate had reached 12.5 mills per cigarette (25¢/pack). Since 1994, the tax rate has been increased numerous times. The Tobacco Products Act, part of Proposal A of 1994, tripled the tax to 37.5 mills per cigarette (75¢/pack). The act also imposed a tax of 16% of the wholesale price of other tobacco products. Since passage of Proposal A, the tax on cigarettes and other tobacco products has increased twice, most recently in 2004.

Cigarette Taxes			Other Tobacco Products	
Public Act	Mills/Cigarette	\$/Pack	Public Act	% of Wholesale Price
1947 PA 265	1.5	\$0.03		
1959 PA 274	2.0	\$0.04		
1961 PA 156	2.5	\$0.05		
1962 PA 215	3.5	\$0.07		
1970 PA 11	5.5	\$0.11		
1982 PA 73	10.5	\$0.21		
1987 PA 219	12.5	\$0.25		
1993 PA 327	37.5	\$0.75	1993 PA 327	16%
2002 PA 503	62.5	\$1.25	2002 PA 503	20%
2004 PA 164	100.0	\$2.00	2004 PA 164	32%

Source: Citizens Research Council: Outline of the Michigan Tax System (January 2007)

State Excise Tax Rates on Cigarettes

State	Rate (¢/pack)	Rank	State	Rate (¢/pack)	Rank
New Jersey	257.5	1	New Hampshire	80	26
Rhode Island	246	2	Kansas	79	28
Washington	202.5	3	Wisconsin	77	29
Arizona	200	4	Utah	69.5	30
Maine	200	4	Nebraska	64	31
MICHIGAN	200	4	Wyoming	60	32
Alaska	180	7	Arkansas	59	33
Vermont	179	8	Idaho	57	34
Montana	170	9	Indiana	55.5	35
Hawaii	160	10	Delaware	55	36
Connecticut	151	11	West Virginia	55	36
Massachusetts	151	11	South Dakota	53	38
New York	150	13	North Dakota	44	39
Texas	141	14	Alabama	42.5	40
Pennsylvania	135	15	Georgia	37	41
Ohio	125	16	Iowa	36	42
Minnesota	123	17	Louisiana	36	42
Oregon	118	18	North Carolina	35	44
Oklahoma	103	19	Florida	33.9	45
Dist. of Columbia	100	20	Kentucky	30	46
Maryland	100	20	Virginia	30	46
Illinois	98	22	Tennessee	20	48
New Mexico	91	23	Mississippi	18	49
California	87	24	Missouri	17	50
Colorado	84	25	South Carolina	7	51
Nevada	80	26	U. S. Median	80	

Source: Federation of Tax Administrators (January 1, 2007)

1. Counties and cities may impose an additional per pack tax in AL (1¢-6¢); IL (10¢-15¢); MO (4¢-7¢); NYC (\$1.50); TN (1¢); and VA (2¢-15¢)
2. Dealers pay an additional enforcement and administrative fee of 0.1¢ per pack in KY and 0.05¢ in TN.
3. Tax rate is scheduled to increase to \$2./pack on 7/1/2007 in AK and on 9/30/2007 in HI.
4. Minnesota also adds a 25.5¢ sales tax on to the wholesale price of a tax stamp.
5. Michigan, Minnesota, and Utah also impose a 35¢ "equity assessment" on the cigarettes of manufacturers that did not participate in the tobacco settlement.

Distribution of Cigarette Tax Revenue

	Mills	\$/Pack	%
General Fund	19.7625	\$0.40	19.7625%
School Aid Fund	41.62	\$0.83	41.6200%
Healthy Michigan Fund	3.75	\$0.08	3.7500%
Health and Safety Fund	2.4375	\$0.05	2.4375%
Medicaid Benefits Trust Fund	31.875	\$0.64	31.8750%
Wayne County	0.555	\$0.01	0.5550%
Total	100	\$2.00	100.0000%

	Total Mills	%	Mills	
1993 PA 327	37.5	6.5%	2.4375	Health and Safety Fund
		24.1%	9.0375	General Fund
		63.4%	23.775	School Aid Fund
		6.0%	2.25	Healthy Michigan Fund
2002 PA 503	15.0	9.0%	1.35	General Fund
		56.3%	8.445	School Aid Fund
		6.0%	0.9	Healthy Michigan Fund
		3.7%	0.555	Wayne County
		25.0%	3.75	Medicaid Benefits Trust Fund
2002 PA 503	10.0	94.0%	9.4	School Aid Fund
		6.0%	0.6	Healthy Michigan Fund
2004 PA 164	37.5	75.0%	28.125	Medicaid Benefits Trust Fund
		25.0%	9.375	General Fund
		100.0%	37.5	

Legislative Analyst: Mark Wolf
Fiscal Analyst: Rebecca Ross
Jim Stansell

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.