

TENNESSEE GENERAL ASSEMBLY  
FISCAL REVIEW COMMITTEE



**FISCAL NOTE**

**SB 738 - HB 1419**

February 24, 2019

**SUMMARY OF BILL:** Increases, from 18 to 21, the minimum age of persons allowed to purchase and use tobacco or vapor products. Creates a Class C misdemeanor for selling or distributing flavored electronic cigarettes. Increases the tax rate on cigarettes by 1.25 cents (\$0.0125) per cigarette.

**ESTIMATED FISCAL IMPACT:**

**Increase State Revenue – Net Impact - \$85,025,900**

**Increase Local Revenue – Net Impact - \$349,800**

Assumptions:

*Current Law and Enforcement:*

- The Department of Agriculture (DOA) will enforce a minimum age limit of 21 years, instead of the current age limit of 18 years, for the purchase of tobacco and vapor products.
- Enforcement of the age limit of 21 for the purchase of tobacco and vapor products can be accomplished within existing DOA resources without an increased appropriation or reduced reversion.
- The Synar Amendment, enacted in 1992 as part of the federal Alcohol, Drug Abuse, and Mental Health Administration Reorganization Act (section 1926), requires states to enact and enforce laws prohibiting the sale or distribution of tobacco products to individuals under the age of 18.
- The Amendment requires each state and U.S. jurisdiction to conduct annual, random, unannounced inspections of retail tobacco outlets and to report the findings to the Secretary of the U.S. Department of Health and Human Services.
- States that do not comply with the requirements set forth in the Amendment are subject to a penalty of 40 percent of their federal Substance Abuse Prevention and Treatment Block Grant funding.
- It is assumed that the state will obtain approval from the Substance Abuse and Mental Health Services Administration's Center for Substance Abuse Prevention to implement the minimum age change, as proposed by this legislation, and that federal funding to the state will not be impacted by the proposed legislation.

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- Pursuant to Tenn. Code Ann. § 67-4-1004(a) and Tenn. Code Ann. § 67-4-1004(d)(1), cigarette tax is a \$0.62 tax per pack of 20 cigarettes.
- The average price per pack of 20 cigarettes in Tennessee is estimated to be \$5.00, which includes state cigarette tax of \$0.62 and a federal excise tax of \$1.01, but does not include state and local sales taxes.
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617 percent.
- The current Fiscal Review Committee staff estimate for tobacco tax collections in FY19-20 is \$238,700,000. This number is assumed to remain constant in subsequent years under current law.
- The number of 20-pack cigarettes estimated to be sold in FY19-20 and subsequent years under current law is 385,000,000 ( $\$238,700,000 / \$0.62$ ).
- Recurring state sales tax collections under current law are estimated to be \$129,876,093 [ $(385,000,000 \times \$5.00 \times 7.0\%) - (385,000,000 \times \$5.00 \times 7.0\% \times 3.617\%)$ ].
- Recurring local sales tax collections under current law are estimated to be \$52,998,908 [ $(385,000,000 \times \$5.00 \times 2.5\%) + (385,000,000 \times \$5.00 \times 7.0\% \times 3.617\%)$ ].

*Changes from Age and Cigarette Tax Increase:*

- Based on information provided by Department of Revenue, the recurring decrease in sales of tobacco products as a result of the minimum age limit increase is estimated to be approximately 1.89 percent.
- The number of 20-pack cigarettes sold is estimated to decrease by 7,276,500 packs ( $385,000,000 \times 1.89\%$ ), for a total of 377,723,500 pack sold each year ( $385,000,000 - 7,276,500$ ).
- The proposed legislation increases the tax rate on cigarettes by 1.25 cents (\$0.0125) per cigarette, or \$0.25 per pack of 20 cigarettes. The total state cigarette tax will become \$0.87 ( $\$0.62 + \$0.25$ ).
- The new price per cigarette pack is estimated to be \$5.25 ( $\$5.00 + \$0.25$ ), which translates into an increase of 5.0 percent ( $\$0.25 / \$5.00$ ). The increase in price of cigarettes will result in an additional decrease in the consumption of cigarettes.
- Based on various studies, the price elasticity of demand for cigarettes is estimated to be negative 0.35. The 5.0 percent increase in the price of cigarettes is estimated to result in a 1.75 percent decrease in the quantity of cigarettes consumed ( $5\% \times -0.35$ ).
- The number of 20-pack cigarettes sold at the new price is estimated to be 371,113,339 [ $377,723,500 \times (100.00\% - 1.75\%)$ ]. Taxable sales are estimated to be \$1,948,345,030 ( $371,113,339 \times \$5.25$ ). These numbers are assumed to remain constant into perpetuity.
- Recurring tobacco tax collections as a result of this legislation are estimated to be \$322,868,605 ( $371,113,339 \times \$0.87$ ).
- Recurring state sales tax collections as a result of this legislation are estimated to be \$131,451,137 [ $(\$1,948,345,030 \times 7.0\%) - (\$1,948,345,030 \times 7.0\% \times 3.617\%)$ ].
- Recurring local sales tax collections as a result of this legislation are estimated to be \$53,641,641 [ $(\$1,948,345,030 \times 2.5\%) + (\$1,948,345,030 \times 7.0\% \times 3.617\%)$ ].

- The recurring increase in tobacco tax collections is estimated to be \$84,168,605 (\$322,868,605 - \$238,700,000).
- The recurring increase in state sales tax collections is estimated to be \$1,575,044 (\$131,451,137 - \$129,876,093).
- The recurring increase in local sales tax collections is estimated to be \$642,733 (\$53,641,641 - \$52,998,908).

*Changes from Flavored E-cigarette Ban*

- Approximately 10,800,000 adults in the United States are estimated to currently use e-cigarettes, with more than half of them being under 35 years old.
- Tennessee represents approximately 2.069 percent of total U.S. population.
- The number of adults in Tennessee estimated to currently use e-cigarettes is 223,452 (10,800,000 x 2.069%).
- Eighty one percent of youth e-cigarette users cited the availability of “appealing flavors” as the primary reason for use. Adjusted for adult usage, we estimate that approximately 70 percent of Tennesseans, or 156,416 (223,452 x 70%) use fruit flavors.
- Assuming the average cost of these flavored pods is \$4.36 and that users of these flavored e-cigarettes purchase one pod a week, taxable sales are estimated to be \$35,462,636 (156,416 users x \$4.36 x 52 weeks).
- It is assumed that prohibiting the use of flavored e-cigarettes would result in a 30 percent decrease in such sales. The remaining 70 percent of users would switch to tobacco flavored e-cigarettes or cigarettes.
- The recurring decrease in taxable sales is estimated to be \$10,638,791 (\$35,462,636 x 30%).
- The recurring decrease in state sales tax collections are estimated to be \$717,779 [(\$10,638,791 x 7.0%) - (\$10,638,791 x 7.0% x 3.617%)].
- The recurring decrease in local sales tax collections are estimated to be \$292,906 [(\$10,638,791 x 2.5%) + (\$10,638,791 x 7% x 3.617%)].

*Net Impact and Other:*

- The net recurring increase in state revenue to the General Fund as a result of this legislation is estimated to be \$85,025,870 (\$84,168,605 + \$1,575,044 - \$717,779).
- The net recurring increase in local sales tax collections as a result of this legislation is estimated to be \$349,827 (\$642,733 - \$292,906).
- Pursuant to Tenn. Code Ann. § 39-17-1509(b), a person found to be in violation of selling or distributing tobacco or vapor products to an individual that has not reached the minimum age of 21 will receive a warning letter for a first violation, a civil penalty up to \$500 for a second violation, a civil penalty up to \$1,000 for third violations, and a civil penalty up to \$1,500 for fourth and subsequent violations.
- Given the majority of violations will likely be first time offenses, whereby a warning letter will be issued, no significant increase in civil penalty revenue is anticipated.

- There will not be a significant impact on the number of cases in the court system for state or local government to experience any significant impact on revenue or expenditures.

**IMPACT TO COMMERCE:**

**Decrease Business Revenue – \$57,436,800/Recurring**

**Increase Business Expenses – Exceeds \$30,000/One-Time**

**Jobs Impact – Not Significant**

Assumptions:

- Pursuant to Tenn. Code Ann. § 39-17-1506, all retail establishments selling tobacco products are required to post a sign stating that state law prohibits the sale of tobacco products or smoking paraphernalia to persons under the age of 18 years. Such signs will have to be updated as a result of this legislation to reflect the new minimum age of 21 years.
- According to the Tennessee Fuel and Convenience Store Association, there are approximately 6,000 retail outlets that offer tobacco products for sale in Tennessee.
- Assuming a minimum cost of \$5.00 per sign, the one-time increase in business expenses is estimated to be at least \$30,000 (6,000 businesses x \$5.00 per sign).
- The proposed legislation is estimated to result in a recurring decrease in the number of 20-pack cigarettes sold of 13,886,661 (385,000,000 - 371,113,339).
- Under the proposed legislation, the average price per pack of 20 cigarettes in Tennessee is estimated to be \$5.25, which includes state cigarette tax of \$0.62, the proposed tax of \$0.25, and a federal excise tax of \$1.01, but does not include state and local sales taxes.
- The recurring decrease in business revenue from an increase in the age limit and change in price is estimated to be \$46,798,048 [13,886,661 x (\$5.25 - \$0.25 - \$0.62 - \$1.01)].
- The additional recurring decrease in business revenue from the decrease in flavored e-cigarette sales is estimated to be \$10,638,791.
- The total recurring decrease in business revenue is estimated to be \$57,436,839 (\$46,798,048 + \$10,638,791).
- Assuming that such revenue loss is equally distributed over all retail establishments selling tobacco, the average recurring decrease in revenue per establishment is estimated to be less than \$9,573 (\$57,436,839 / 6,000).
- Based on the 2012 Economic Census, the average annual salary of gasoline station employees, or employees for other similar retail establishments that sell tobacco products in Tennessee, is estimated to be \$16,737.
- It is therefore assumed that any decrease in the total number of jobs in the state will be not significant.

**CERTIFICATION:**

The information contained herein is true and correct to the best of my knowledge.



Krista Lee Carsner, Executive Director

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