

TOBACCO PRODUCTS TAX ACT

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Senate Bills 720 (S-2), 721, and 722 as passed by the Senate

Sponsor: Sen. Jim Runestad

House Committee: Tax Policy

Senate Committee: Finance

Complete to 2-9-22

Analysis available at
<http://www.legislature.mi.gov>

SUMMARY:

Senate Bill 720 would make several changes to the Tobacco Products Tax Act to account for remote retail sales and to revise provisions concerning manufacturers, wholesalers, and unclassified acquirers, among others. The bill would prohibit an unlicensed person from importing tobacco products into Michigan. It also would revise the disbursement of proceeds from the tax on cigarettes and on other tobacco products.

Definitions

The bill would revise the following defined terms as follows:

- Exclude **remote retail sales** from the definition of “retailer.”
- Amend the definition of **secondary wholesaler** to remove provisions that currently require maintenance of an established place of business in Michigan where a substantial portion of the business is tobacco sales. (These requirements would be added to nondefinitional provisions concerning secondary wholesalers elsewhere in the act, as described below.)
- Allow a “stamping agent” to be a wholesaler or unclassified acquirer that is also a manufacturer.
- Provide that an “unclassified acquirer” also includes a person located within or outside of Michigan that makes a remote retail sale of a tobacco product to a consumer in Michigan.
- Remove from the definition of “vending machine operator” a requirement that the person purchase a tobacco product from a manufacturer, licensed wholesaler, or secondary wholesaler.
- Add to the definition of “wholesale price” a provision allowing the Department of Treasury to determine the wholesale price of a tobacco product in a remote retail sale (based on the average price paid during the immediately preceding calendar year) if an unclassified acquirer makes a remote retail sale and fails to keep or maintain the required records.

Remote retail sale would mean the sale of a tobacco product to a consumer in Michigan to which either of the following applies:

- The consumer submits the order for the sale by means of a telephone or other method of voice transmission, the mail, or the internet or other online service or the seller is otherwise not in the physical presence of the purchaser when the request for purchase or order is made.
- The tobacco product is delivered to the purchaser by common carrier, private delivery service, or other method of remote delivery or the seller is not in the

physical presence of the purchaser when the purchaser obtains possession of the tobacco product.

Secondary wholesaler would mean either of the following:

- A person, other than a manufacturer or a person licensed under the act as a vending machine operator, wholesaler, or unclassified acquirer, who engages in the sale of a tobacco product for resale.
- A retailer, not otherwise licensed under the act, who transfers or exchanges a tobacco product from one place of business of the retailer to another place of business of the retailer.

Licensure under the act

Currently, a person may not purchase, possess, acquire for resale, or sell a tobacco product as a manufacturer, wholesaler, secondary wholesaler, vending machine operator, unclassified acquirer, transportation company, or transporter in Michigan unless licensed to do so.

The bill would additionally prohibit an unlicensed person from *importing* tobacco products into Michigan.

The bill also would prohibit a person from making a remote retail sale to a consumer in Michigan unless the person was licensed as an unclassified acquirer.

The bill would require a license application to state the applicant's regular business hours.

Additionally, if an unclassified acquirer applicant did not maintain a place of business where tobacco products were sold, brought, or kept, the Department of Treasury could issue a license based on the physical address of the applicant's nonresidential building, office, or other facility where required records would be kept and maintained.

The bill would extend the documentation that must accompany an initial license application to include proof that the applicant has a facility to receive, *store*, and distribute *tobacco products* (in addition to the currently specified proof of a facility to receive and distribute *cigarettes*.)

The bill would require each place of business of a retailer, and any place of business or other nonresidential building, office, or facility licensed under the act, to display the name and address of the retailer or licensee in a way that is readily visible to the general public from outside the place of business, building, office, or facility.

The following requirements would apply to a secondary wholesaler, vending machine operator, or wholesaler, as applicable:

- A secondary wholesaler could purchase or acquire a tobacco product for resale in Michigan only if that purchase or acquisition were directly from a wholesaler or unclassified acquirer that was licensed under the act and the tax imposed by the act had been paid on that tobacco product.
- A secondary wholesaler would have to maintain an established place of business in Michigan where a substantial portion of the business was the sale of tobacco products and related merchandise at wholesale and where, at all times, a substantial stock of tobacco products and related merchandise was available for sale to retailers for resale.

- A wholesaler would have to maintain an established place of business in Michigan where substantially all of the business was the sale of tobacco products and related merchandise at wholesale and where, at all times, a substantial stock of tobacco products and related merchandise was available for sale to retailers for resale.
- A vending machine operator could purchase a tobacco product only from a secondary wholesaler, wholesaler, or unclassified acquirer licensed under the act.

The act prohibits a person from possessing for more than 72 hours a machine for vending tobacco products unless there is a disc or marker attached as specified. This requirement does not apply to a machine that does not contain a tobacco product.

The bill would further prohibit a person from operating a machine for vending tobacco products without such a disc or marker. The requirement would not apply to a machine that is not used in selling a tobacco product.

Creditors acquiring tobacco products as a security interest

Under the bill, a creditor that acquired a tobacco product in Michigan as a result of exercising a security interest could sell that tobacco product without being licensed if the creditor received written approval from the Department of Treasury and the creditor sold or transferred the tobacco product to a person in Michigan licensed under the act as either a wholesaler or an unclassified acquirer.

Records

The act requires a manufacturer, wholesaler, secondary wholesaler, vending machine operator, transportation company, unclassified acquirer, or retailer to keep a complete and accurate record of each tobacco product manufactured, purchased, or otherwise acquired, and provides specific records that must be maintained for each entity type. Except for a manufacturer, the records must include the price paid for each tobacco product purchased. The act requires the statements and other records to be preserved for four years.

Under the bill, the record-keeping requirement described above also would apply to tobacco products otherwise acquired. The retention requirement would provide that it applies for a period of four years from the date of purchase or acquisition of the tobacco product. In addition, under the bill, a licensee or retailer in possession or control of a tobacco product that had not preserved the required statements and records would have the burden of proving that the product was purchased or acquired more than four years ago. A licensee or retailer that failed to do so would be in violation of the record-keeping requirements.

Transport outside of Michigan

Under the act, if a tobacco product other than cigarettes is received or acquired within Michigan by a wholesaler, secondary wholesaler, vending machine operator, unclassified acquirer, or retailer, each original manufacturer's shipping case must bear the name and address of the person making the first purchase or any other markings the Department of Treasury prescribes.

Under the bill, a shipping case or a container of a tobacco product other than cigarettes received or acquired by a wholesaler or unclassified acquirer from a manufacturer or any person located outside Michigan would have to bear either the name and address of the wholesaler or

unclassified acquirer making that first purchase or any other markings the Department of Treasury prescribes.

The point at which a shipping case or container would be considered to be received or acquired in Michigan would be determined based the ownership of the container when it entered Michigan, the risk of loss, and the use of a common carrier, among other factors.

A licensed wholesaler or unclassified acquirer would have to mark every shipping case or container of a tobacco product other than cigarettes that was sold, transferred, shipped, or delivered by the wholesaler or unclassified acquirer to a retailer or another licensee. If one of these markings were affixed mechanically, the wholesaler or unclassified acquirer would need to obtain prior approval from the Department of Treasury to use such a device. A wholesaler or unclassified acquirer whose license was revoked, terminated, or expired would have to return all of these devices in its possession to the Department of Treasury within 60 days. In addition to any other penalty, a wholesaler or unclassified acquirer would be liable for a fine of \$500 per device not timely returned. Markings could not be illegible and could not cover up information or markings required elsewhere in the act.

The act presumes that unmarked tobacco products found are in violation of the act.

The bill specifies that if unmarked tobacco products were acquired, imported, transferred, or sold (in addition to being found), they would constitute contraband subject to seizure and forfeiture. If any tobacco product were adjudicated by a court of competent jurisdiction to have been lawfully seized under the act, and if the adjudication of lawful seizure survived the exhaustion or lapse of any appeal rights, the tobacco product would be automatically forfeited to the state and the person from whom that tobacco product was seized would be liable for the tax imposed on that product.

Currently, if a tobacco product is shipped outside Michigan, the licensee shipping the tobacco product must include the name and address of the consignee or purchaser to whom the shipment is made on every shipping case or container.

Under the bill, the licensee would have to satisfy this requirement if a tobacco product was to be or was being transported on a public highway, road, or street in Michigan for shipment out of state, as indicated by documentation related to that shipment. In addition, for tobacco products other than cigarettes, the shipping case or container would have to include the marking prescribed by the Department of Treasury unless it already bore that marking from the licensee.

A tobacco product that was located in Michigan would be considered to have been shipped outside Michigan for purposes of the above provisions if the tobacco product crossed the Michigan border, regardless of whether it was delivered to or accepted by the consignee or purchaser to whom the shipment was made outside of Michigan.

Except as otherwise provided by the act, a person transporting, possessing, or acquiring a tobacco product for the purpose of transport would be have to be licensed as a transporter unless otherwise licensed as an unclassified acquirer, wholesaler, transportation company, vending machine operator or secondary wholesaler under the act.

The act now requires a transporter to possess a permit for each load being transported, and that certain regulations be followed. This requirement, and the rules concerning a transporter with a permit, would be eliminated.

Under the bill, a retailer in Michigan or another person acting on behalf of a retailer in Michigan would not have to be licensed under the act to transport a tobacco product on a public highway, road, or street for the purpose of delivering it to a consumer if all of the following were met:

- The product was purchased by the consumer from the retailer at retail.
- The consumer paid for the tobacco product in full before its shipment and delivery.
- The retailer or other person making the delivery had in its possession while the tobacco product was being transported proof of the sale to the specific customer and other specified information concerning the product and the delivery.

Stamps

Under the act, before delivery, sale, or transfer to a person in Michigan, a wholesaler or unclassified acquirer that is not a manufacturer must include on each individual package or cigarettes a stamp provided by the Department of Treasury.

The bill would remove the exclusion of manufacturers from the above provision. In addition, under the bill, a stamp could be placed in a location other than the bottom of each individual package of cigarettes if approved by the Department of Treasury. Generally, a person could not sell a cigarette separately from its package.

The act authorizes the Department of Treasury to perform inspections of licensees during regular business hours.

Under the bill, the inspection would have to verify that shipping cases and containers of tobacco products other than cigarettes bear the markings required by the act. The bill also would describe what “regular business hours” means with respect to different licensees.

The bill would eliminate provisions that prescribe conditions that must be met before the Department of Treasury can issue stamps to a wholesaler or unclassified acquirer that it has determined not to be financially sound, as well as provisions concerning a wholesaler’s or unclassified acquirer’s remittal of unpaid tax in obtaining stamps from the department.

Directory

A new section 6f would establish a process by which the Department of Treasury could remove a tobacco product manufacturer or an affiliated brand family of a tobacco product manufacturer from the *directory* or refuse to list them on the directory. Section 6f would not apply to any tobacco product manufacturer that voluntarily requested removal from, or rescinded a request to be included on, the directory.

Directory would mean the lists established and described under sections 6c and 6d, separately or collectively, as applicable to a tobacco product manufacturer.¹

¹ For instance, see https://www.michigan.gov/documents/taxes/NPM_Directory_1-10-2019_649747_7.pdf

The Department of Treasury could not include or retain in the directory a manufacturer or a brand family of a manufacturer if any of the following applied:

- The manufacturer had not performed any of its obligations under the act.
- The manufacturer had been removed from a list maintained by another state that was equivalent to the directory based on actions or omissions that would serve as a basis for removal from Michigan's directory.
- The manufacturer, or any of its officers or directors, in any jurisdiction, had pled guilty or nolo contendere to, or been found guilty of, a felony relating to the sale, distribution, or taxation of a tobacco product.
- The manufacturer sold, transferred, or distributed a tobacco product to a wholesaler or unclassified acquirer that it knew or had reason to know was not licensed or whose license was suspended or revoked.

If the department intended to remove from the directory or not include in the directory a tobacco product manufacturer or an associated or affiliated brand family of a tobacco product manufacturer, the department would have to notify the manufacturer or, if applicable, its agent for the service of process. The notice would have to include the deficiencies, the actions that the manufacturer would have to take to cure the deficiencies, and a 15-day deadline for those actions. (The deadline could be extended for an additional 15 days.)

If the manufacturer failed to cure the deficiencies within the time period, the department would have to notify the tobacco product manufacturer that, unless a demand for a hearing were made, the department would remove the tobacco product manufacturer or any of its brand families from the directory or not include them.

Within 10 business days of the service of the notice, a manufacturer could demand a hearing with the department to appeal the delisting. If no demand were filed, the department would have to immediately remove the manufacturer and its brands from the directory. The department would have to hold a hearing within 15 business days, at which the manufacturer could appear, be represented by counsel, and present testimony. The hearing would not be a contested case proceeding and would not be subject to the Administrative Procedures Act.

Within 10 business days, the department would have to order either that the manufacturer be removed from or not included on the directory or that it be retained or included. A manufacturer could appeal the department's order to the Ingham County Circuit Court within 30 days. The department could not remove a manufacturer until all appeal rights had been exhausted.

Taxation

The act levies a tax on the sale of tobacco products sold in this state. The bill would add that the tax applies to tobacco products sold for consumption in this state, which is presumed to apply when the products are sold to a retailer or consumer in this state.

The bill would remove language describing and implementing the step increases in tax rates for cigarettes over the last 20 years and specify that the tax on cigarettes is 100 mills per cigarette (the current rate). It also would include *any other tobacco product other than cigarettes* in products taxed at 32% of the wholesale price (the rate that now applies to cigars, noncigarette smoking tobacco, and smokeless tobacco).

Currently, a licensee other than a retailer, unclassified acquirer licensed as a manufacturer, and a vending machine operator must file a return with the Department of Treasury stating the wholesale price of each tobacco product other than cigarettes purchased and other information as specified.

Under the bill, this provision would apply to a licensee other than a manufacturer or a vending machine operator.

Disbursement of tax revenue

The bill would remove or revise many disbursement provisions, largely because marginal tax rate increases on cigarettes over the years often were given different disbursement percentages.

Under the bill, the proceeds collected from the tax on cigarettes would be disbursed as follows:

- 2.4375% to the Health and Safety Fund created by the Health and Safety Fund Act.
- 41.62% to the State School Aid Fund.
- 3.75% to the Healthy Michigan Fund.
- 19.7625% to the Michigan State Capitol Historic Site Fund and the general fund.
- 0.5550% to counties with a year 2000 population of more than 2.0 million, to be used for indigent care.
- 31.8750% to the Michigan Medicaid Benefits Trust Fund.

The proceeds collected from the tax on cigars, noncigarette smoking tobacco, and smokeless tobacco (and, under the bill, any tobacco product other than cigarettes) would remain at its current disbursement: 75% to the Michigan Medicaid Benefits Trust Fund and 25% to the general fund.

Other provisions

Currently, a person, other than a licensee, who is in control or in possession of a tobacco product contrary to the act, who is in control or in possession of an individual package of cigarettes without a stamp in violation of the act, or who offers to sell or does sell a tobacco product to another for resale without being licensed to do so, is personally liable for the tax imposed under the act, plus a penalty of 500% of the amount of tax due.

Under the bill, this liability would also apply to a person, other than a licensee, who offers to sell at retail, or does sell at retail, an individual package of cigarettes without a stamp or any tobacco product purchased or acquired from a person not licensed as secondary wholesaler, wholesaler, or unclassified acquirer at the time of the purchase or acquisition.

In addition, the bill would prohibit a consumer from purchasing or otherwise acquiring a tobacco product through a remote retail sale unless the seller is licensed as an unclassified acquirer.

Finally, the bill would extend provisions that now apply to sales of tobacco products conducted through the internet to also apply to remote retail sales.

MCL 205.422 et seq. and proposed MCL 205.423a and 205.426f

Senate Bill 721 would update the language and citations in the Health and Safety Fund Act to reflect changes proposed by SB 720.

The bill is tie-barred to SB 720, which means that it could not take effect unless SB 720 were also enacted.

MCL 141.473

Senate Bill 722 would likewise update citations in 1999 PA 244, which governs tobacco product manufacturers' escrow accounts.

MCL 445.2051 and 445.2052

FISCAL IMPACT:

As written, the bills would not alter current tax rates for cigarettes or other tobacco products or significantly adjust the distributions. Thus, they would have little, if any, impact on state revenues or tobacco tax distributions.

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