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Senate Bill 720 through 722 (as introduced 11-3-21)
Sponsor: Senator Jim Runestad
Committee: Finance

Date Completed: 11-10-21

CONTENT

Senate Bill 720 would amend the Tobacco Products Tax Act to do the following:

- **Modify various terms and definitions.**
- **Prohibit an unlicensed person from importing tobacco products into the State.**
- **Increase all license fees to \$200 and update requirements for licensees.**
- **Allow a creditor that acquired a tobacco product in the State as a result of exercising a security interest to sell that tobacco product without being licensed under the Act if the creditor received written approval from the Department of Treasury to do so.**
- **Modify the requirements for transportation of tobacco products out of the State and require transporters to obtain a license.**
- **Allow the Department to delist a manufacturer and establish a procedure by which the Department could remove a tobacco product manufacturer or affiliated brand family of a tobacco product manager from the State's directory**
- **Modify the distribution of proceeds from tobacco products taxes.**

Senate Bill 721 would amend the Health and Safety Fund Act to require the State Treasurer to credit the Health and Safety Fund with the portion of proceeds from the cigarette excise tax authorized to be deposited into the Fund under the Tobacco Products Tax Act.

Senate Bill 722 would amend Public Act 244 of 1999, which requires tobacco product manufacturers to place funds in escrow for medical expenses incurred by the State due to tobacco-related illnesses, to modify references to the Tobacco Products Tax Act to be consistent with the amendments proposed under Senate Bill 720.

Senate Bill 721 is tie-barred to Senate Bill 720.

Senate Bill 720 is discussed in greater detail below.

Definition Changes

Under the Act, "cigarette" means a roll for smoking made wholly or in part of tobacco, irrespective of size or shape and irrespective of the tobacco being flavored, adulterated, or mixed with any other ingredient, which roll has a wrapper or cover made of paper or any other material. Under the bill, the term also would mean a roll for smoking *or heating that is* made wholly or in part of tobacco, irrespective of size or shape and irrespective of the tobacco

being flavored, adulterated, or mixed with any other ingredient, which roll has a wrapper or cover made of paper or any other material.

The bill would remove the definition for "Commissioner".

"Remote retail sale" would mean a sale of a tobacco product to a consumer in the State if either of the following applied: a) 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; or b) if 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.

"Retailer" means a person other than a transportation company who operates a place of business for the purpose of making sales of a tobacco product at retail. Under the bill, the term would mean a person other than a transportation company who operates a place of business for the purpose of making, *or who does make*, sales of a tobacco product at retail *other than a remote retail sale*.

"Secondary wholesaler" means a person who sells a tobacco product for resale, who purchases a tobacco product from a wholesaler or unclassified acquirer licensed under this act, and who maintains an established place of business in this state where a substantial portion of the business is the sale of tobacco products and related merchandise at wholesale, and where at all times a substantial stock of tobacco products and related merchandise is available to retailers for resale. Under the bill, the term would mean 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. The term also would include 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.

"Stamping agent" means a wholesaler or unclassified acquirer other than a manufacturer who is licensed and authorized by the Department to affix stamps to individual packages of cigarettes on behalf of themselves and other wholesalers or unclassified acquirers other than manufacturers. The bill would remove the phrase "other than a manufacturer".

Under the bill, "unclassified acquirer" would include a person located within or outside of the State that makes a remote retail sale of a tobacco product to a consumer in the State.

"Vending machine operator" means a person who operates one or more vending machines for the sale of a tobacco product and who purchases a tobacco product from a manufacturer, licensed wholesaler, or secondary wholesaler. Under the bill, the term would mean a person who operates one or more vending machines for the sale of a tobacco product.

The Act defines "wholesale price" and allows the Department to establish the wholesale price for a tobacco product under certain circumstances. Under the bill, the Department could establish the wholesale price if a wholesaler or unclassified acquirer failed to keep or maintain the records as required under Section 6 (which details records those entities are required to keep and maintain). If an unclassified acquirer made a remote retail sale and failed to keep or maintain those records for a remote retail sale, the Department could determine the wholesale price of the tobacco product sold to the consumer in that remote retail sale based on the average price paid, during the immediately preceding calendar year, by the unclassified acquirer to acquire or purchase the same type of tobacco product if that information were made available to the Department by the unclassified acquirer.

License to Sell Tobacco

The Act prohibits a person from purchasing, possessing, acquiring for resale, or selling a tobacco product as a manufacturer, wholesaler, secondary wholesaler, vending machine operator, unclassified acquirer, transportation company, or transporter in the State unless licensed to do so. The bill would prohibit an unlicensed person from importing tobacco products into the State. Also, the bill would prohibit a person from making a remote retail sale to a consumer in the State unless the person was licensed as an unclassified acquirer.

The Act prescribes requirements for the application and issuance of licenses. The bill would require that a license application state the applicant's regular business hours. The bill would allow the Department, for unclassified acquirers that did not maintain a place of business where tobacco products were sold, brought, or kept, to issue a license based on the physical address of the applicant's nonresidential building, office, or other facility where the records required under the Act would be kept and maintained.

The Act prescribes the fees for different license types. The bill would raise all licensee fees to \$200.

The Act prohibits a person from possessing a machine for vending tobacco products for a period in excess of 72 hours unless there is a disc or marker attached as specified. The bill also would prohibit a person from operating a machine for vending tobacco products without a disc or marker. This requirement does not apply to a machine not containing a tobacco product. Under the bill, it also would not apply to a machine not used in selling a tobacco product.

A license application must be accompanied by satisfactory proof, as determined by the Department, of certain requirements, including the applicant owns, or has an executed lease for, a secure nonresidential facility for the purpose of receiving and distributing cigarettes and conducting its business. Under the bill, an application would have to be accompanied by satisfactory proof that an applicant owned, or had an executed lease for, a secure nonresidential facility for the purpose of receiving, *storing*, and distributing *tobacco products* and conducting business *in accordance with the Act*.

The bill would require each place of business of a retailer, and any place of business or other nonresidential building, office, or facility license to display the name and address of the retailer or licensee in a manner that was readily visible to the general public from outside the place of business, nonresidential building, office, or facility, as applicable.

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 the State 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 the State 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 the State 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.

Creditors Acquiring Tobacco Products as a Security Interest

A creditor that acquired a tobacco product in the State as a result of exercising a security interest could sell that tobacco product without being licensed under the Act if the creditor received written approval from the Department, and the creditor sold or transferred the tobacco product to a person in the State licensed under the Act as either a wholesaler or an unclassified acquirer. A creditor would have to apply for approval do so on a form and in a manner prescribed by the Department.

"Creditor" and "security interest" would mean those terms as defined under the Uniform Commercial Code.

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. Under the bill, this also would apply to tobacco products otherwise acquired.

The Act requires all statements and other records required above to be preserved for four years. Under the bill, this requirement would apply for a period of four years from the date of purchase or acquisition of the tobacco product. 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 the State

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 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 the State would have to bear either the name and address of the wholesaler or unclassified acquirer making that first purchase.

Under the bill, the point at which a shipping case or container would be considered to be received or acquired in the State would be determined based on the facts and circumstances including all of the following:

- Ownership of the shipping case or container when it entered the State's borders or when it was delivered to the wholesaler or unclassified acquirer.
- The risk of loss.
- The use of a common carrier or a vehicle owned or leased by the wholesaler or unclassified acquirer to import or transport the shipping case or container into the State or deliver the shipping case or container to the wholesaler or unclassified acquirer.

A wholesaler or unclassified acquirer, licensed under Act, would have to place or otherwise affix the markings prescribed by the Department on 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, in the State. If one of these markings were affixed by means of a mechanical or other device that applied the marking, the wholesaler or unclassified acquirer would need to obtain prior approval from the Department to purchase, possess, or otherwise be permitted 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 within 60 days of the revocation, termination, or expiration. 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 under the Act. Notwithstanding anything in the Act to the contrary, 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 under the Act on that product.

Under the Act, if a tobacco product is shipped outside the State, the licensee shipping the tobacco product must cause to be placed on every shipping case or container in which the tobacco product is shipped the name and address of the consignee or purchaser to whom the shipment is made outside of the State. Under the bill, the licensee would have to satisfy this requirement if a tobacco product were to be or was being transported on a public highway, road, or street in Michigan for shipment outside of the State, as indicated by documentation related to that shipment. For tobacco products other than cigarettes, the licensee would have to cause the marking specified above to be included. A tobacco product would be considered to have been shipped outside the State if it crossed the borders of the State, regardless of whether or not it was delivered to or accepted by the purchaser or consignee to whom the shipment was made outside the State.

Except as otherwise provided by the Act, a person who transports, possesses, or acquires for the purpose of transport of a tobacco product would be required to be licensed as a transporter unless otherwise licensed under the Act. The Act currently requires a transporter to possess a permit for each load being transported, and that certain regulations be followed as specified in the Act. This requirement, and the rules concerning a transporter with a permit, would be eliminated.

Under the bill, a retailer or other person acting on the behalf of a retailer in the State would not have to be licensed under the Act to transport a tobacco product upon a public highway, road, or street of the State for the purpose of delivering a tobacco product to a consumer if the tobacco product were purchased by the consumer from the retailer at retail, the consumer had paid for the tobacco product in full before the shipment and delivery of the tobacco product, the retailer or other person making the delivery had in its possession at all times during which the tobacco product was being transported, proof of the sale to the specific customer and other information as specified in the bill.

Stamps

Under the Act, before delivery, sale, or transfer to a person in the State, a wholesaler or unclassified acquirer must place or cause to be placed on each individual package or cigarettes to be sold in Michigan a stamp provided by the Department. Under the bill, if approved by the Department, a stamp could be placed in a location other than the bottom of each individual package of cigarettes. Except as otherwise provided, a person could not sell a cigarette separately from its individual package.

The Act allows the Department to inspect entities for compliance. Under the bill, the inspection would have to verify that shipping cases and containers of tobacco products other than cigarettes bore any markings required by the Act. An inspection would have to be conducted during the licensee's regular business hours. Unless otherwise approved, those business hours would be those disclosed on the entity's license application.

Manufacturers

Under the bill, if a manufacturer failed to provide the certification of compliance that it was not a participant in the master settlement agreement and that it had performed its obligation to established a qualified escrow account and deposited relevant funds, the Department could delist a manufacturer subject to Section 6f.

Section 6f would establish the process by which the Department could remove a tobacco product manufacturer or affiliated brand family of a tobacco product manager from a directory or refuse to list any of the above 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.

The Department could not include in the directory or retain a manufacturer or a brand family of a manufacturer in the director, if any of the following apply:

- The manufacturer had not performed any of its obligations under the Act.
- The manufacturer had been moved 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 under the Act or whose license was suspended or revoked under the Act.

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 all of the following:

- The factual and legal deficiencies upon which the Department's intended action rested.
- The action that the tobacco product manufacturer would have to take to cure those deficiencies.

- A statement that the tobacco product manufacturer would have 15 calendar days, from the date of the notice, to cure those deficiencies and submit documentation of its attempt to cure.

The Department could extend the 15-calendar-day period for good cause shown up to an additional 15 calendar 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 was made as provided by the Act, the Department would remove the tobacco product manufacturer or any of its brand families from or not include them in its directory.

A manufacturer, within 10 business days after the date of the service of the notice, could file with the State Treasurer a demand for a hearing before a representative of the Department to determine the legitimacy of the delisting. If, within 10 business days, no demand was filed, the Department would remove the manufacturer and its associated brands from the directory. After receiving a demand, the Department would have to hold a hearing within 15 business days, at which the manufacturer would be entitled to appear before the Department, to be represented by counsel, and to present testimony and argument. The hearing would not be a contested case proceeding and would not be subject to the Administrative Procedures Act. Within 10 business days after the hearing, the Department would have to declare, by order, that the manufacturer either be removed or not included on the directory or that it be retained or included. If the order were the former, the manufacturer would have to be removed immediately or refused inclusion on the directory. A manufacturer aggrieved by a Department decision of the Department could appeal the Department's order to the Ingham County Circuit Court within 30 days after the date the Department mailed the order to the aggrieved tobacco product manufacturer. The Department could not remove a manufacturer from the directory until all appeal rights had been exhausted.

Taxation

The Act levies a tax on the sale of tobacco products sold in the State as specified. The bill would require this tax to be levied on tobacco products sold for consumption in the State; consumption would be presumed when sold to a retailer or consumer.

The bill would eliminate much of the language pertaining to tax rates and, instead would specify the following rates:

- For cigarettes, 100 mills per cigarette.
- For cigars, noncigarette smoking tobacco, and smokeless tobacco, 32% of the wholesale price, with the exception that between November 1, 2012, and October 31, 2021, the amount of tax levied on cigars not exceed 50 cents per cigar.

However, if the Secretary of the United States Department of Health and Human Services issued an order for a product under 21 USC 387k(g) (i.e. an order that a modified risk product may be commercially marketed under certain circumstances) and the manufacturer had notified the Department of Treasury of that order on a form in a manner prescribed by the Department, the tax imposed on that product would be the following:

- 50% of the otherwise applicable rate, if the order were a modified risk tobacco product order.
- 25% of the otherwise applicable rate, if the order is issued under 21 USC387k(g)(2).

Under the Act, a licensee other than a retailer, unclassified acquirer licensed as a manufacturer, and a vending machine operator must file a return with the Department stating the wholesale price of each tobacco product other than cigarettes purchased and other information as specified in the Act. Under the bill, this provision would apply to a licensee other than a manufacturers and vending machine operators.

Penalties

The Act specifies that 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 also would apply to a person, other than a licensee, who offered to sell at retail, or did sell at retail, an individual package of cigarettes without a stamp or any tobacco product purchased or acquired from a person that was not licensed under the Act as secondary wholesaler, wholesaler, or unclassified acquirer, at the time of purchase or acquisition.

The bill would prohibit a consumer in the State from purchasing or otherwise acquiring a tobacco product through a remote retail sale unless the seller was licensed under the Act as an unclassified acquirer.

Other Provisions

The Act requires that all invoices, bills of lading, sales receipts, etc. related to tobacco product sales conducted online, by telephone, or in a mail-order transaction contain the current seller's information and whether relevant taxes have been paid. It also requires that all packages of tobacco products shipped from a seller to purchasers who reside in Michigan clearly print or stamp the word "TOBACCO PRODUCTS" on the outside of all sides of the package. The bill would require this for remote retail sales and remove the exemption for wholesalers or unclassified acquirers making remote retail sales.

"Sale conducted through the internet" would include a remote retail sale.

Disbursement of Tax Revenue

The bill abolishes many prior disbursement provisions. Those new and remaining would be as follows:

For the tax on cigarettes under Section 7(1)(a):

- Instead of 6.5% of the proceeds being credited to the Health and Safety Fund created by the Health and Safety Fund Act, 2.4375% would be credited accordingly.
- Instead of 63.4% of the proceeds being credited to the State School Aid Fund, 41.6200% would be credited accordingly.
- Instead of 6% of the proceeds being credited to the Healthy Michigan Fund, 3.75% would be credited accordingly.
- Instead of 24.1% of the proceeds being credited to the Michigan State Capitol Historic Site Fund, 19.7625% would be credited accordingly.
- 0.5550% of the proceeds would be paid to counties with a 2000 population of more than 2.0 million to be used for indigent health care.
- 31.8750% of the proceeds would be credited to the Michigan Medicaid Benefits Trust Fund Act.

MCL 205.422 et al. (S.B. 720)
141.473 (S.B. 721)
445.2051 & 445.2052 (S.B. 722)

Legislative Analyst: Christian Schmidt

FISCAL IMPACT

The bills would increase license revenue from tobacco licensees by less than \$100,000, based on the number of current licensees. The provisions regarding the taxes levied and the distribution of tax revenue are technical changes that would simplify the current language and would not alter the levy nor its distribution across different funds. Almost all of the remaining provisions in the bill would refine current regulations determining who is liable for taxes, securing stamps, and enforcement provisions. As such, any impact on revenue from those refinements likely would be minimal.

Fiscal Analyst: David Zin

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.