

REVENUE ESTIMATING CONFERENCE

TAX: Cigarette Tax
ISSUE: Additional Tax for Non-Settling Manufacturers
BILL NUMBER(S): HB1207
SPONSOR(S): Rep. Tobia
MONTH/YEAR COLLECTION IMPACT BEGINS: July 1, 2011
DATE OF ANALYSIS: March 16, 2011

SECTION 1: NARRATIVE

- a. **Current Law:** Currently non-settling manufacturers do not pay any additional fees to ship their cigarettes into or within the state.
- b. **Proposed Change:** The bill creates s. 201.236, F.S., to provide a fee for non-settling manufacturers. The fee is set at 2.6 cents per cigarette, or 52 cents per pack. This fee is in addition to excise and sales taxes already imposed on the sale of cigarettes.

SECTION 2: DESCRIPTION OF DATA AND SOURCES

The projection of the number of packs sold under current law is based on the February 2011 conference on Tobacco Tax and Surcharge revenues. DBPR provided detailed information on shipments into Florida by manufacturer.

SECTION 3: METHODOLOGY (INCLUDE ASSUMPTIONS AND ATTACH DETAILS)

It is estimated that currently 20.7% of packs sold in Florida are from non-settling manufacturers (based on the shipment data). The high estimate assumes that this market share is maintained; the middle estimate assumes that non-settling manufacturers lose 25% of their market share; the low estimate assumes that non-settling manufacturers lose 50% of their market share.

SECTION 4: PROPOSED FISCAL IMPACT

State Impact: All Funds	FY 2011-12 Cash	FY 2011-12 Annualized	FY 2012-13 Cash	FY 2013-14 Cash	FY 2014-15 Cash
NSM Fee	92.0	100.4	99.8	99.5	99.3
High: Excise Tax	-3.9	-4.2	-4.0	-3.9	-3.7
Surcharge	-11.3	-12.3	-11.8	-11.4	-11.0
Sales Tax	1.6	1.8	1.7	1.7	1.7
Tobacco settlement fees	0	0	0	0	0
Middle: NSM Fee	69.2	75.5	75.1	74.9	74.7
Excise Tax	-2.8	-3.1	-3.0	-2.9	-2.8
Surcharge	-8.4	-9.2	-8.9	-8.6	-8.2
Sales Tax	1.2	1.3	1.3	1.3	1.3
Tobacco settlement fees	.1	.1	.1	.1	.1
Low: NSM Fee	46.3	50.5	50.2	50.1	50.0
Excise Tax	-1.9	-2.1	-2.0	-1.9	-1.9
Surcharge	-5.6	-6.1	-5.9	-5.7	-5.5
Sales Tax	0.8	0.9	0.9	0.9	0.9
Tobacco settlement fees	.1	.1	.1	.1	.1

SECTION 5: CONSENSUS ESTIMATE (ADOPTED 3/25/11)

- The REC reviewed the Brattle Group’s *Final Determination Pursuant to the NPM Procedures Agreement* dated March 27, 2006. The Group was jointly retained by Philip Morris, R.J. Reynolds, Lorillard and the forty-six settling states to review the non-participating manufacturers’ adjustment. In the course of its work, the Group received expert testimony, economic analyses and data from both sides. Each side was allowed to question and comment on the opposing side’s materials, as well as make adjustments to its own work. The Group also developed its own econometric models and analyses that encompassed the most reasonable specifications and econometric approaches provided by the opposing parties. The REC finds that this analysis offers an unbiased view and can be relied upon to guide the development of impacts for HB 1207.
- Own-Price Elasticity gives the responsiveness of the quantity demanded of a good or service to a change in its price. More precisely: the percentage change in quantity demanded in response to a one percent change in price. Based on the Group’s hybrid analyses of the individual work performed by Gruber and Pindyck; Hausman; Bresnahan; and Murphy, the NPM’s own-price elasticities using AIDS or AIDS-like specifications are in the range of -2.9486 to -4.9044. This

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yields a result not inconsistent with the proposed 50% market share reduction and the actual natural experiment changes seen in Minnesota and Michigan. To incorporate these findings, the REC adopts the 50% market share reduction.

---Brattle Group Hybrid AIDS Model Own-Price Elasticity: Combination

Own-Price Elasticity	-2.9486 to -4.9044
Average	-3.9265
% Cost Increase	11% to 12%
Average % Cost Increase	11.5%
Impact on Market Share	-45.2%

*AIDS = Almost Ideal Demand System of Equations

- The REC finds that other discount or value cigarette brands provide a near-perfect substitute for the products produced by non-settling manufacturers. This means that no loss of tobacco users or demand was assumed within the overall market setting for cigarettes. To incorporate this finding, the REC eliminates the proposed -0.7 elasticity effects on packs.
- Like the Brattle Group, the REC finds that product branding has importance. Further, the REC believes that product loyalty to a particular discount brand and inertia can slow the response to a price change, much as Murphy found in his Price Response Model and first Structural Demand Model. For these reasons, the REC does not believe that market shares adjust instantly to price changes. To incorporate these findings, the REC altered the long-run theoretical elasticity to produce short-term market share losses by non-settling manufacturers equal to 40% in the first year, 45% in the second year, and a long-run steady state of 50% thereafter.
- Finally, the REC assumes that issues with rule-making will have no effect on the timing of implementation.

	FY 2011-12 Cash	FY 2011-12 Annualized	FY 2012-13 Cash	FY 2013-14 Cash	FY 2014-15 Cash
General Revenue	55.9	50.9	55.6	50.4	50.2
Tobacco Settlement TF	.1	.1	.1	.1	.1
Total State Impact	56.0	51.0	55.7	50.5	50.3
Total Local Impact	0	0	0	0	0
Total Impact	56.0	51.0	55.7	50.5	50.3

HB1207
 Non-settling Manufacturers' Fee
 \$.52 per pack

	High estimate, assumes no change in market shares				
	Cash 2011-12	2011-12	2012-13	2013-14	2014-15
Packs Current Law (Millions)		944.9	938.7	936.0	933.6
Average pre-sales tax price		5.80	5.98	6.18	6.40
% Packs NSM's		20.7%	20.7%	20.7%	20.7%
Packs NSM's (Millions)		195.6	194.3	193.8	193.3
Average price with \$.52 fee		5.91	6.09	6.29	6.51
Packs using -.7 elasticity effect		932.6	926.9	924.6	922.6
NSM packs		193.1	191.9	191.4	191.0
\$.52 collections	92.0	100.4	99.8	99.5	99.3
Excise Tax	-3.9	-4.2	-4.0	-3.9	-3.7
Surcharge	-11.3	-12.3	-11.8	-11.4	-11.0
Sales Tax Impact	1.6	1.8	1.7	1.7	1.7

	Middle estimate, NSM's lose 25% of their packs				
		2011-12	2012-13	2013-14	2014-15
Packs Current Law (Millions)		944.9	938.7	936.0	933.6
Average pre-sales tax price		5.80	5.98	6.18	6.40
% Packs NSM's		15.5%	15.5%	15.5%	15.5%
Packs NSM's (Millions)		146.7	145.7	145.3	144.9
Average price with \$.52 fee		5.88	6.06	6.26	6.48
Packs using -.7 elasticity effect		935.7	929.8	927.4	925.4
NSM packs		145.3	144.4	144.0	143.7
\$.52 collections	69.2	75.5	75.1	74.9	74.7
Excise Tax	-2.8	-3.1	-3.0	-2.9	-2.8
Surcharge	-8.4	-9.2	-8.9	-8.6	-8.2
Sales Tax Impact	1.2	1.3	1.3	1.3	1.3

	Low estimate, NSM's lose 50% of their packs				
		2011-12	2012-13	2013-14	2014-15
Packs Current Law (Millions)		944.9	938.7	936.0	933.6
Average pre-sales tax price		5.80	5.98	6.18	6.40
% Packs NSM's		11.4%	11.4%	11.4%	11.4%
Packs NSM's (Millions)		107.9	107.2	106.9	106.6
Average price with \$.52 fee		5.86	6.04	6.24	6.46
Packs using -.7 elasticity effect		938.1	932.2	929.7	927.5
NSM packs		107.1	106.4	106.1	105.9
\$.52 collections	51.0	55.7	55.3	55.2	55.1
Excise Tax	-2.1	-2.3	-2.2	-2.1	-2.1
Surcharge	-6.2	-6.8	-6.5	-6.3	-6.1
Sales Tax Impact	0.9	1.0	1.0	1.0	1.0

	Adopted estimate, NSM's lose 40%, 45%, then 50% of their packs, no effect on total consumption				
	2011-12 Cash	2011-12	2012-13	2013-14	2014-15
Packs Current Law (Millions)		944.9	938.7	936.0	933.6
% Packs NSM's		12.4%	11.4%	10.4%	10.4%
Packs NSM's (Millions)		117.4	106.9	96.9	96.6
\$.52 collections	55.9	61.0	55.6	50.4	50.2
Recurring Estimate (50% loss)		50.9	50.5	50.4	50.2

Shipments into Florida

	2007-08		2008-09		2009-10		2010-11 *	
	Packs	%	Packs	%	Packs	%	Packs	%
Settling Manufacturers	940,774,656	81.7%	885,512,005	77.9%	680,999,133	79.0%	375,844,560	77.8%
Subsequent Participating Manufacturers	38,207,161	3.3%	16,724,753	1.5%	18,997,725	2.2%	7,138,265	1.5%
Non-settling Manufacturers	172,922,310	15.0%	234,263,250	20.6%	162,503,124	18.8%	100,154,297	20.7%
Total	1,151,904,127		1,136,500,008		862,499,982		483,137,122	

* partial year, July 2010-January 2011

Source: Department of Business and Professional Regulation

Impact on the Tobacco Settlement Trust Fund

For the High estimate, there is no loss of market share by the NSMs, so there is no shift to the participating manufacturers

For the middle estimate, there is a 25% loss in Market share

If it is all absorbed by Liggett or the SPMs, there is no impact on settlement payments

If it is all absorbed by the other participating manufacturers, the impact would be as below:

	Feb 2011 REC Florida Definition Volume (Millions)	Impact of 25% Demand shift To participating Manufacturers	Adjusted Florida Definition Volume (Millions)	Percentage Change in Volume	Feb 2011 REC Settlement Annual Payment (\$ Millions)	Impact on Settlement Annual Payment (\$ Millions)
FY 2011-12	247,566.8	47.8	247,614.6	0.019%	352.8	0.07
FY 2012-13	240,461.6	46.4	240,508.0	0.019%	353.4	0.07
FY 2013-14	234,426.0	45.3	234,471.3	0.019%	355.2	0.07
FY 2014-15	229,737.5	44.4	229,781.9	0.019%	358.8	0.07

For the low estimate, there is a 50% loss in Market share

If it is all absorbed by Liggett or the SPMs, there is no impact on settlement payments

If it is all absorbed by the other participating manufacturers, the impact would be as below:

	Feb 2011 REC Florida Definition Volume (Millions)	Impact of 50% Demand shift To participating Manufacturers	Adjusted Florida Definition Volume (Millions)	Percentage Change in Volume	Feb 2011 REC Settlement Annual Payment (\$ Millions)	Impact on Settlement Annual Payment (\$ Millions)
FY 2011-12	247,566.8	95.9	247,662.7	0.039%	352.8	0.14
FY 2012-13	240,461.6	93.1	240,554.7	0.039%	353.4	0.14
FY 2013-14	234,426.0	90.8	234,516.8	0.039%	355.2	0.14
FY 2014-15	229,737.5	89.0	229,826.5	0.039%	358.8	0.14