

# HOUSE BILL REPORT

## ESHB 2272

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### As Amended by the Senate

**Title:** An act relating to transferring the enforcement of existing cigarette and tobacco taxes from the department of revenue to the liquor control board.

**Brief Description:** Transferring enforcement of cigarette and tobacco taxes to the liquor control board.

**Sponsors:** By House Committee on Appropriations (originally sponsored by Representatives Huff, Clements, Alexander, Wensman, Sehlin and Mitchell).

**Brief History:**

**Committee Activity:**

Appropriations: 3/25/97, 4/5/97 [DPS].

**Floor Activity:**

Passed House: 4/10/97, 58-37.

Senate Amended.

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### HOUSE COMMITTEE ON APPROPRIATIONS

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 24 members: Representatives Huff, Chairman; Alexander, Vice Chairman; Clements, Vice Chairman; Wensman, Vice Chairman; H. Sommers, Ranking Minority Member; Gombosky, Assistant Ranking Minority Member; Benson; Cooke; Crouse; Dyer; Grant; Keiser; Kessler; Lambert; Linville; Lisk; Mastin; McMorris; Parlette; Poulsen; D. Schmidt; Sehlin; Sheahan and Talcott.

**Minority Report:** Do not pass. Signed by 7 members: Representatives Doumit, Assistant Ranking Minority Member; Carlson; Chopp; Cody; Kenney; Regala and Tokuda.

**Staff:** Jeff Olsen (786-7157).

**Background:** The state of Washington imposes a tax on the sale, use, consumption, handling, possession and distribution of cigarettes and tobacco products. Cigarettes are taxed at the rate of \$0.825 per pack. Tobacco products are taxed at the rate of 74.9 percent of the wholesale price. In addition to the cigarette and tobacco tax, sales tax and business and occupation tax are also applicable to the sale of cigarettes and tobacco products.

According to an estimate from the Department of Revenue (DOR), the state will lose \$109 million in tax revenue in fiscal year 1997 from the illegal sale of untaxed cigarettes. Revenue losses occur from casual smuggling from states with lower cigarette tax rates than Washington, and from cigarettes purchased from tax-free outlets such as military post exchanges and Indian smoke shops.

Under federal law, the cigarette tax does not apply to cigarettes sold on an Indian reservation to an enrolled tribal member for personal consumption. However, sales made by a tribal cigarette outlet to nontribal members are subject to the tax. The United States Supreme Court has affirmed that the state may impose a cigarette tax on sales made within reservations to nontribal members and have upheld the imposition of minimal burdens on the tribal seller to assist in collecting the tax. Those burdens have included affixing the appropriate stamp to individual cigarette packages and keeping records that distinguish between exempt sales and taxable sales. The ability of the state to take enforcement action on-reservation and off-reservation has been the subject of several lawsuits, leaving uncertain the extent of enforcement authority the state may exercise.

In 1996, the Legislature established the Cigarette Tax and Revenue Loss Advisory Committee to study and analyze cigarette tax revenues lost during 1992-95. The study included an analysis of lost cigarette tax revenue and an analysis of the revenue losses attributable to cigarette tax increases. The study also analyzed the feasibility of reducing lost revenue through negotiated agreements between the state and federally recognized Indian tribes in Washington. The committee did not reach consensus. The majority recommendation supported a cooperative approach that included negotiated agreements with the tribes. The minority recommendation opposed any agreements with the tribes and suggested that more scrutiny should have been given to enforcing the law against the purchase of untaxed cigarettes by non-Indian consumers.

The DOR is charged with enforcing the cigarette and tobacco products tax laws and administering and collecting the taxes. Department employees do not have general police powers and must appoint local law enforcement officers or the state patrol officers as agents for certain enforcement activity such as search and seizure activity.

The Liquor Control Board enforces the Minors' Access to Tobacco law and may suspend or revoke retail or wholesale licenses of licensees who violate this law. The board does not enforce cigarette or tobacco product tax laws. Liquor enforcement officers have general police powers to enforce the state's liquor laws.

**Summary of Bill:** Primary enforcement authority for cigarette and tobacco tax laws is transferred from the DOR to the Liquor Control Board. It is the intent of the Legislature that the cigarette and tobacco tax laws of the state of Washington be actively enforced. The DOR will continue to administer and collect cigarette and tobacco taxes. The DOR must appoint enforcement officers of the Liquor Control

Board as the department's authorized agents to allow both the department and the board to engage in certain enforcement activities. These officers are not considered employees of the DOR. The Liquor Control Board is given authority to adopt rules necessary to enforce cigarette and tobacco tax laws.

A schedule is established to require the Liquor Control Board to reduce lost revenue due to cigarette and tobacco tax evasion by 50 percent within five years.

The bill contains provisions addressing the rule-making powers of an agency.

**EFFECT OF SENATE AMENDMENT(S):** The Governor is given authority to execute cooperative agreements with federally recognized Indian tribes or nations concerning the sale of cigarettes and tobacco. The Liquor Control Board is required to negotiate the cooperative agreements. The rate of tax imposed on tobacco and cigarette products under the cooperative agreement must be at the same rate as currently applied to these products, but the amount of taxes that may be retained by the Indian tribe or nation may be negotiated.

Fifty percent of the cigarette and tobacco tax revenue received by the state through cooperative agreements with Indian tribes or nations shall be deposited into the Violence Reductions and Drug Enforcement Account and fifty percent shall be deposited into the Health Services Account. The sales and use tax, cigarette tax, and tobacco products tax do not apply to the sale, use, consumption, handling, possession, or distribution of cigarettes or tobacco by Indian nations or tribes during the effective period of the cooperative agreements.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill contains an emergency clause and takes effect immediately.

**Testimony For:** The state of Washington needs to enforce the law and collect taxes that are legally due to the state. Tribal smoke shops that do not charge state excise taxes have an unfair competitive advantage over retailers that pay their taxes. It is wrong for retailers to have to compete against illegal sales.

**Testimony Against:** The DOR recognizes the problems with enforcing cigarette and tobacco tax laws. Enforcement is resource intensive, and often results in legal action being taken against the state. Since the state does not have enforcement authority on tribal reservations, increased enforcement will not solve the problem. Government to government cooperation (compact) is preferred over increased enforcement.

The Liquor Control Board did not request the enforcement authority for cigarette and tobacco tax laws. However, if enforcement is transferred to the board, they request that the Legislature provide adequate resources to implement the bill. The board has established working relationships with the tribes, and they have concerns that the bill does not allow them the ability to negotiate agreements.

**Testified:** Gary Gilbert, Liquor Control Board (concerns); Fred Kiga and Gary O'Neil, Department of Revenue (con); Jerry Blanton, small business owner (pro); T.K. Bentler, Washington Association of Neighborhood Stores (pro); Stuart Cloud, retailer (pro); Randy Scott, Puyallup Tribal Council and Quinalt Indian Nation (con); and Dawn Vyvyon, Yakima Nation (concerns).