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## FISCAL IMPACT REPORT

**ORIGINAL DATE** 01/27/10

**SPONSOR** Harden **LAST UPDATED** \_\_\_\_\_ **HB** \_\_\_\_\_

**SHORT TITLE** No Tribal Cigarette Tax Break for Non-Members **SB** 158

\_\_\_\_\_  
**ANALYST** Gutierrez

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	FY11	FY12		
	\$16,584.0	\$16,584.0	Recurring	General Fund
	\$315.0	\$315.0	Recurring	County & Muni Recreation Fund
	\$627.0	\$627.0	Recurring	County & Muni Cigarette Fund
	\$315.0	\$315.0	Recurring	UNM Cancer Center
	\$471.0	\$471.0	Recurring	NMFA
	\$3,348.0	\$3,348.0	Recurring	NMFA for UNM Health
	\$1,410.0	\$1,410.0	Recurring	NMFA for DOH
	\$233.0	\$233.0	Recurring	Rural County Cancer Treatment

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to SB30, SB121, and HB35

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Taxation and Revenue Department (TRD)

Indian Affairs Department (IAD)

Department of Health (DOH)

### SUMMARY

#### Synopsis of Bill

Senate Bill 158 eliminates the state cigarette tax exemption which currently allows cigarettes to be exempted from the cigarette tax for those cigarettes sold on tribal land to non-tribal members. The bill provides that the Taxation and Revenue Department, in conjunction with each tribe, shall determine the number of tax exempt stamps needed to be provided to distributors for cigarettes sales to tribal members on tribal land.

The effective date of this bill's provisions is July 1, 2010.

## **FISCAL IMPLICATIONS**

TRD:

The presumed consumption of cigarettes by tribal members, assuming standard national consumption patterns, is estimated to be about 5,379 thousand packs per year (see Attachment 1). The estimated state tax loss associated with the federal preemption from taxing tribal members on their own tribal land is estimated to amount to about \$4,895 thousand per year. The Estimated Revenue Impact represents estimated sales of cigarettes that are currently tax-exempt to non-tribal persons.

The "Cigarette Inventory Tax" (Section 7-12-3.1 NMSA 1978) is distinctly separate from the "Cigarette Tax" and is distributed entirely to the State General Fund. The estimate has assumed that less than one-half of the first month of additional revenue may be collected as inventory tax, and that retailer purchases in the first month will be weaker than normal after stocking to capacity in June to beat the tax increase. Thus, some strength in FY2010 June revenue may be expected, but that impact has not been included in the estimated revenue.

Cigarette Tax revenue to the NMFA Credit Enhancement Account is ultimately forwarded to the State General Fund. The total General Fund impact with inclusion of the NMFA Credit Enhancement Account is shown as "General Fund". The direct impact on the NMFA Credit Enhancement Account is (111) thousand (negative) per year.

Cigarette demand is responsive to price changes and it is important to recognize that when prices go up, demand will go down, affecting the fiscal impact. Due to price elasticity, cigarette sales on tribal lands are estimated to decrease by 2.5 – 3 million packs a year based solely on imposing the cigarette tax on non-tribal members. In addition to this loss, the tribal sales of cigarettes could decrease significantly if there is no longer an incentive for non-tribal members to travel to tribal lands to buy their cigarettes.

## **SIGNIFICANT ISSUES**

TRD:

The Cigarette Tax rate was last increased in 2003 when the rate was increased from \$0.21 per pack to \$0.91 per pack. Prior to that, the tax rate was increased from \$0.15 per pack to \$0.21 per pack in 1993. The \$0.15 per pack tax had been in effect from 1986 through 1993.

The state tax exemption for cigarettes sold by tribal entities was granted in 1992 when the state cigarette tax rate was \$0.15 per pack. At that time, tribal sellers were beginning to purchase cigarettes from other out-of-state tribal sellers, and state tax law did not explicitly impose the incidence of the tax on the consumption (consumer) of cigarettes.

On March 31, 2009 the federal cigarette tax rate increased from 39 cents per pack to \$1.01 per pack, which was expected to decrease cigarette consumption by about 8%. The federal tax increase was expected to affect the volume of both state taxable cigarettes and tax-exempt Tribal sales.

## ADMINISTRATIVE IMPLICATIONS

TRD:

The extent of the administrative impact would depend on whether, and how, the Technical Issues are addressed. Tax compliance issues may be especially problematic.

## RELATIONSHIP

Senate Bill 158 relates to:

- SB30 which increases the cigarette and tobacco taxes and distributes the additional revenue to the county-supported Medicaid fund;
- SB121 which increases the cigarette tax and distributes the additional revenue to the general fund; and
- HB35 which increases the cigarette and tobacco taxes and distributes the additional revenue to the public school fund.

## TECHNICAL ISSUES

TRD:

The mechanism for providing untaxed cigarettes to tribal members may prove unworkable. Section 4, Subsection B (on page 6, line 23 through page 7, line 1) provides for a “*number of tax exempt stamps needed to be provided to distributors for cigarette sales to tribal members on tribal land.*” Distributors (cigarette stampers) would need to maintain a separate inventory of tax exempt stamps for each tribe, and tribal retailers would need to maintain separate inventories of cigarettes intended for sale to tribal members and non-members. Since all cigarette packages are required to bear some type of tax stamp, and since the tax exempt status (federal preemption) cannot be determined until the pack is sold to a tax exempt entity, administration would be difficult. Tribal sellers probably would not be equipped to affix heat-transfer stamps at the time of sale to a tribal member, so problems with shortages of particular cigarette brands that bear a tax exempt stamp would probably occur.

Section 2, Subsection C (page 5, line 12) – it is not clear who the “*person in possession of the cigarettes*” is that has the burden of proof that cigarettes are not taxable. If it is the consumer, this provision would make enforcement of the bill difficult. Since the cigarette tax is collected through the sale of stamps, and enforced through the requirement that cigarettes must be stamped with either a tax or tax-exempt stamp, and since the stamps are placed on the cigarettes by the distributor, the Department would be unable to ascertain that a tax-exempt stamp was properly placed on cigarettes once the cigarettes are in possession of the consumer.

## OTHER SUBSTANTIVE ISSUES

### DOH:

The U.S. Supreme Court, in Oklahoma Tax Comm. v. Potawatomi Tribe, 498 U.S. 505 (1991), ruled that "under the doctrine of tribal sovereign immunity" a state is "free to collect taxes on sales to nontribal members" that occur on tribal lands within state borders (but may not tax tribal-land sales to tribal members). But the Court also ruled that because of Indian tribes' sovereign immunity, a state cannot enforce any such tax collection laws against a tribe through a lawsuit in court unless specifically authorized by Congress to do so.

## ALTERNATIVES

### IAD:

An alternative to repealing the tribal cigarette tax exemption could be to form a Tribal-State Work Group, similar to the Gasoline Tax Working Group established in 2003, to investigate the issues raised by the cigarette tax and develop possible solutions that are supported by both state and tribal governments.

BLG/mt

***The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:***

- 1. Adequacy:*** revenue should be adequate to fund government services.
- 2. Efficiency:*** tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.
- 3. Equity:*** taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.
- 4. Simplicity:*** taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.
- 5. Accountability/Transparency:*** Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.

***More information about the LFC tax policy principles will soon be available on the LFC website at [www.nmlegis.gov/lcs/lfc](http://www.nmlegis.gov/lcs/lfc)***

**Illustration of Tax Reimbursement to Native American Smokers Living on Reservations  
(calculated at the current \$0.91 per pack tax rate)**

Geographic Area	Total Population (2000 Census)	Native American (1) Population (2000 Census)	Estimated 2010 Total Population	Native American Population age 18 and over	Native American Adult Smokers (2)	Estimated Cigarette Tax that would be paid by Native American Smokers (3)
<b>AMERICAN INDIAN RESERVATION AND OFF-RESERVATION TRUST LAND — FEDERAL All areas</b>	<b>138,839</b>	<b>104,823</b>	<b>114,705</b>	<b>70,764</b>	<b>14,577</b>	<b>\$4,894,940</b>
Acoma Pueblo and Off-Reservation Trust Land, NM	2,802	2,724	2,981	1,932	398	\$133,642
Cochiti Pueblo, NM	1,502	695	761	561	116	\$38,806
Isleta Pueblo, NM	3,166	2,675	2,927	1,985	409	\$137,308
Jemez Pueblo, NM	1,958	1,940	2,123	1,380	284	\$95,458
Jicarilla Apache Reservation, NM	2,755	2,474	2,707	1,635	337	\$113,097
Laguna Pueblo and Off-Reservation Trust Land, NM	3,815	3,670	4,016	2,671	550	\$184,760
Mescalero Reservation, NM	3,156	2,888	3,160	1,849	381	\$127,900
Nambe Pueblo and Off-Reservation Trust Land, NM	1,764	455	498	365	75	\$25,248
Navajo Nation Reservation and Off-Reservation Trust Land, NM (part)	69,524	67,369	73,720	44,011	9,066	\$3,044,361
Picuris Pueblo, NM	1,801	166	182	132	27	\$9,131
Pojoaque Pueblo, NM	2,712	263	288	210	43	\$14,526
Sandia Pueblo, NM	4,414	499	546	370	76	\$25,594
San Felipe Pueblo, NM	3,185	2,465	2,697	1,718	354	\$118,839
San Ildefonso Pueblo, NM	1,524	527	577	405	83	\$28,015
San Juan Pueblo, NM	6,748	1,329	1,454	1,015	209	\$70,210
Santa Ana Pueblo, NM	487	473	518	335	69	\$23,173
Santa Clara Pueblo, NM	10,658	1,332	1,458	1,057	218	\$73,116
Santo Domingo Pueblo, NM	3,166	3,084	3,375	2,079	428	\$143,810
Taos Pueblo and Off-Reservation Trust Land, NM	4,492	1,330	1,455	1,131	233	\$78,234
Tesuque Pueblo and Off-Reservation Trust Land, NM	806	355	388	264	54	\$18,262
Ute Mountain Reservation and Off-Reservation Trust Land, NM (part)	0	n/a	n/a	n/a	n/a	n/a
Zia Pueblo and Off-Reservation Trust Land, NM	646	645	706	460	95	\$31,819
Zuni Reservation and Off-Reservation Trust Land, NM (part)	7,758	7,424	8,124	5,199	1,071	\$359,629
San Felipe/Santa Ana joint use area, NM	0	n/a	n/a	n/a	n/a	n/a
San Felipe/Santo Domingo joint use area, NM	0	n/a	n/a	n/a	n/a	n/a

(1) "Native American" based on Census definition of "American Indian and Alaska Native".

(2) "Smokers" assumed to be 20.6% of adult population.

(3) Estimated Cigarette Tax that would be paid by Native American smokers assumes average consumption of 369 packs per year per smoker.

Source: U.S. Census Bureau, Census 2000 Summary File 1, Matrix P8.

Source: U.S. Census Bureau, Census 2000 Summary File 1, Matrices PCT12 and P13.

Calculations by TRD/TAR&S Office from Census percentages of population for age and race.