

# Department of Finance and Administration

## Legislative Impact Statement

**Bill: HB1156**

**Bill Subtitle: TO IMPOSE A TAX ON E-CIGARETTES; AND TO CREATE THE E-CIGARETTES TAX ACT.**

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**Basic Change :** Sponsor: Representative Blake

The bill creates the E-Cigarettes Tax Act and levy a new tax on electronic cigarettes. The tax would be levied at the tax rate of 7½¢ per fluid milliliter of consumable nicotine liquid product. The tax would be imposed at the wholesale level and paid by the product wholesaler or distributor. If purchased by a retailer from a source other than a registered wholesaler, the retailer would be responsible for payment of the tax. The tax would be due on the 15<sup>th</sup> day of the month following the month of the product purchase by the wholesaler or retailer.

Revenues collected would be deposited into the State Treasury and be distributed as follows:

- Twenty-Five (25%) shall be credited to the Child Care and Early Childhood Education Fund Account of the Department of Human Services Fund.
- Twenty-five percent (25%) shall be credited to the Aging and Adult Services Fund Account of the Department of Human Services Fund.
- Twenty-five percent (25%) shall be credited to the Department of Veterans Affairs' cash fund deposited into the State Treasury.
- Twenty-five percent (25%) shall be General Revenues and shall be credited to the State Apportionment Fund.

The proposal would be effective on the first day of the second calendar month following the effective date of this act.

**Revenue Impact :**

\$1.5 Million Potential Annual Increase in State Tax Revenues

+ \$363,000 --- Child Care and Early Childhood Education Fund  
+ \$363,000 --- Aging and Adult Services Fund Account  
+ \$363,000 --- Department of Veterans Affairs' cash fund  
+ \$363,000 --- General Revenues  
+ \$ 33,000 --- State Central Services  
+ \$ 15,000 --- Constitutional Officers

[ Impact based on estimated consumption level of nicotine liquid solution using national consumption levels as provided in industry reports factored to the Arkansas population. ]

**Taxpayer Impact :**

E-Cigarette distributors and wholesalers would register with DFA and monthly report the taxes due. Taxpayer accounting records and systems would require modification to report the new tax.

**Resources Required :**

None

**Time Required :**

Adequate time is provided for implementation

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### Procedural Changes :

This proposal would require creation of tax reporting forms and instructions for taxpayers to use in filing the new tax reports. Modifications to DFA's computer systems for filing and remitting state taxes will also require modification to allow the paper and electronic tax return processing. Education of the staff and the adoption of rules for the new tax would also be necessary.

### Other Comments :

Page 2 Line 36 and Page 3 Lines 1 through 6 -- This proposal provides the director with the authority to assess a penalty of 10% of the tax due for failure to file and/or remit the excise tax due at the time required. State law currently provides for failure to file and failure to pay penalties for all other state taxes collected by DFA which are assessed at 5% per month, not to exceed 35%. Modifications to DFA computer system will be required if a different penalty levy is established. Continuing the penalty provisions that are applicable to other tax types collected by DFA would be preferred.

Page 3 -- Lines 14 through 18 -- This language requires taxpayers to maintain their accounting records for this tax for 3 years. State law currently requires all taxpayers to maintain their tax records for 6 years. The language conflicts with current law and is unnecessary.

At present, only Minnesota and North Carolina have adopted tax levies on e-cigarette products. Minnesota has levied the e-cigarette tax in the same manner as their taxes on tobacco products. The tax is levied at 95% of the sales price to the e-cigarette wholesaler, the same tax rate they apply to other tobacco products such as cigars, moist snuff, and chewing tobacco (Arkansas levies the tax on other tobacco products at 68% of the price paid by wholesalers). North Carolina will begin collecting their tax on July 1, 2015 at the rate of \$.05 per fluid milliliter of consumable nicotine liquid product. Other states have not adopted legislation at this time for a special excise tax on e-cigarette product. Comparing the tax amount due using the Minnesota and North Carolina methods as reflected in a report by industry representatives, for a product with a wholesale cost of \$7.00 the tax due in Minnesota would be \$6.65 versus the amount due in North Carolina would be \$.03.

### Legal Analysis :

HB1156 would require a license for any distributor, wholesaler, or manufacturer of "e-cigarettes" or "consumable products" that sell or offer e-cigarettes or consumable products for sale to retail dealers within Arkansas. A "consumable product" is a nicotine liquid solution or other material containing nicotine that is depleted as an e-cigarette is used. Retailers that purchase e-cigarettes or consumable products from unlicensed distributors, wholesalers, or manufacturers are also required to be licensed. The license is to be issued by DFA.

Several issues require consideration and are stated below.

1) The issues of penalties and record retention are already addressed in the Arkansas Tax Procedure Act (TPA). The provisions enunciated in the bill regarding these issues are contrary to the provisions of the TPA. The adoption of contrary procedures for different tax types is likely to create confusion for taxpayers. Unless the contrary provisions are deemed essential, those provisions should be removed from the bill and the TPA should govern.

2) A provision should be added to allow direct taxation of purchasers in possession of untaxed products to address online sales by out-of-state retailers.

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3) Page 4, Line 15, should be amended to provide that DFA "may" promulgate rules rather than "shall" adopt rules. This will prevent the need to issue an unnecessary rule if the Act is complete on its face.

4) The bill designates DFA to license entities to conduct business in Arkansas. Licensing of entities involved in the manufacture, distribution, and sale of tobacco-related products is generally handled by the Director of Tobacco Control. If licensing is intended, it would be more cost effective to have the Arkansas Tobacco Control Board with its existing enforcement infrastructure to administer licensure of distributors, wholesalers, manufacturers, and retailers of e-cigarettes or consumable products. It appears that HB1156 intends for DFA not to license the businesses to operate but simply to register the entities for tax collection purposes. Proposed § 26-57-1507 should be amended to clarify that the purpose of DFA's role in administration of HB1156 is for tax account registration and collection and not to license the conduct of business.