

# MICROFILM DIVIDER

OMB/RECORDS MANAGEMENT DIVISION  
SFN 2053 (2/85) 5M



ROLL NUMBER

DESCRIPTION

1431

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Lolita Rickford  
Operator's Signature

10/16/03  
Date

2003 HOUSE FINANCE AND TAXATION

HB 1431

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Yolanda Richardson  
Operator's Signature

10/16/03  
Date

2003 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1431

House Finance and Taxation Committee

Conference Committee

Hearing Date February 5, 2003

Tape Number	Side A	Side B	Meter #
1	X		1.5

Committee Clerk Signature *Jamie Stein*

Minutes:

**REP. DAVID DROVDAL, VICE-CHAIR** Called the hearing to order.

**REP. WESLEY BELTER, DIST. 22**, Introduced the bill at the request of the industry. The bill allows for the stamping of cigarettes for taxing purposes. Instead of calling it stamping, it is now called indicia. He stated when he first came to the legislature in 1985, they were stamping cigarettes, then they went away from the stamping. Now, we are considering it again. This is being brought about by the differentials in taxing which is taking place throughout the country. There are also a lot of cigarettes sold right now, which are not being taxed. The intent here, is to make sure that cigarettes which are being sold, are being taxed properly.

Rep. Belter, submitted amendments to the bill.

**REP. WEILER** What was the reason that they went away from the stamping?

**REP. BELTER** I don't recall when it was, I think it was felt that it was an unnecessary cost at that time. There may be others that can information on that.

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*Sal Costa Richardson*  
Operator's Signature

*10/16/03*  
Date

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House Finance and Taxation Committee

Bill/Resolution Number HB 1431

Hearing Date February 5, 2003

**JOHN OLSON ON BEHALF OF PHILIP MORRIS USA** This bill was put in at the request of Philip Morris USA. We were working with the industry and the attorney general, the state tax commissioner and the wholesalers. The amendments presented to you, are primarily, designed to accommodate the wholesalers, in terms of their responsibilities. He explained all sections of the bill. He stated, we are one of four states, who do not have stamping. This stamping law was in effect until 1991.

**REP. WINRICH** Questioned the discount in Section 6, according to the fiscal note, this would decrease revenues by about 1.8 million, was a similiar discount in effect prior to 1991, when we did have this stamp in there, or is this something new about this particular version of the law?

**JOHN OLSON** Deferred the question.

**JACK HOLLERAN, VICE-PRESIDENT OF BRAND INTEGRITY AT PHILIP MORRIS USA.** Testified in support of the bill. See written testimony. During his testimony, he presented counterfeit cigarettes to committee members for their comparison to the approved cigarettes being sold. Most of the counterfeit cigarettes sold in the U.S. also have counterfeit stamps, therefore, the nation loses a large amount of money.

**REP. BELTER** Is there more of a problem with the importation then with trafficking out of a low tax state, where is the largest problem?

**JACK HOLLERAN** All of these problems are of equal weight. The difficulty is that it is all illegal activity. We can detect trends, but we can't find the scope or the magnitude of anyone of the problems, counterfeit versus illegal imports, versus diversion of unstamped illegal products.

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Hearing Date February 5, 2003

**JOHN JOB, DIVISION MANAGER OF AMCON DISTRIBUTING COMPANY,**

**BISMARCK,** Testified in support of the amended version of the bill. See written testimony.

**REP. DROVDAL** You mentioned, the 72 hours would be a problem, do you have a better time frame, or more lenient time frame?

**JOHN JOB** It is an unknowing situation. In order to have the brands, and there are numerous brands on the market right now, at the present time, we are stocking four hundred different brands, when you buy a case of thirty of them and are shipping it in four different packs, etc., the clock starts ticking as soon as the product arrives, and we have 72 hours to affix a tax stamp to that. Once we affix a tax stamp, it can be sold in any other state. I have to pay an inventory cost to have it on inventory, it is a guessing game for us. We pay a substantial amount of money for a security system, to insure our inventory is protected.

**REP. BELTER** The business that you do with other states, do you have businesses located in other states, or do you store cigarettes here in North Dakota and ship them to Montana or Minnesota, or

**JOHN JOB** We ship them right out of Bismarck into Montana, the orders are all processed right here in Bismarck. As the orders are pulled, they go on a conveyer line right up to the cigarettes stamping area, the order is then checked for accuracy and then it goes through the cigarettes stamping machine, where the tax is applied, then they go out to the loading area. We put the stamp on at the time that product is pulled to go to the customers.

**JOHN QUINLAN, NORTH DAKOTA TAX DEPARTMENT** Testified in a neutral position. He explained the bill as the tax department understands the bill. He stated they have a

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House Finance and Taxation Committee

Bill/Resolution Number HB 1431

Hearing Date February 5, 2003

concern in Section 3, line 29, which talks about rolling your own tobacco, that was changed last session, and currently, there are no stamps available to roll your own packages. We have options there. Prior to the last session, roll your own product was taxed at a twenty eight percent tobacco tax rate, because at the time we didn't stamp, and because of inflation, roll your own product was removed from the twenty eight percent category to treat it as a cigarette. It is an area of concern, however, we don't have an amendment at this time. The variable discount could cause some confusion both administratively and for the wholesaler. He suggested that a flat rate of discount be considered rather than a variable discount. There is a little confusion in Section 11 and then in Section 14, it repeals that section. The fiscal note prepared, takes into consideration the three percent which is listed in Section 11, page 6. In Section 12, under the bad debt deduction, as we understand it, the wholesaler could claim a credit from the tax department, if the retailer doesn't pay.

**REP. BELTER** The variable rate discount, is in Section 6?

**JOHN QUINLAN** Yes

**REP. BELTER** Do you know how other states handle it?

**JOHN QUINLAN** A number of other states, do use a fixed rate discount, which varies in several states. He submitted a handout to committee members which showed what the results are with fixed rate discounts and variable rate discounts. See attached copy.

**JACK HOLLERAN** Commented again regarding the counterfeit cigarettes, the fiscal note, and revenue impact from enforcement if this bill is enacted.

**KELLY KAISER, O.K. DISTRIBUTING, WILLISTON** Submitted testimony in opposition of the bill unamended.

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House Finance and Taxation Committee

Bill/Resolution Number HB 1431

Hearing Date February 5, 2003

With no further testimony, the hearing was closed.

**COMMITTEE ACTION**

**REP. BELTER** Asked for any input as to how committee members felt regarding the bill.

Discussion was held why stamping was stopped in 1991, it was felt it was a cost factor.

Questions were also raised whether cigarettes were stamped on the military bases and how it will get handled on the reservations.

The fiscal note was also discussed. The question was raised whether the amendments would affect the fiscal note. Committee members felt the seventy two hour requirement may have to be amended.

**REP. BELTER** decided to wait until later in the day to act on the bill.

**COMMITTEE ACTION Later in the day. Tape #1, Side B, Meter #37.0**

**REP. CLARK** Made a motion to adopt amendments #30633.0201 as presented.

**REP. KLEIN** Second the motion. Motion carried by voice vote.

**REP. GROSZ** Referred to page 8, line 20 of the bill and page 6, line 26, suggested that lines 20 and 21 of page 8 should be deleted.

**REP. GROSZ** Made a motion to further amend 30633.0201 to include the deletion of page 8, line 20 and 21.

**REP. IVERSON** Second the motion. Motion carried by voice vote.

**REP. CLARK** Made a motion for a **DO PASS AS AMENDED AND BE REREFERRED**

**TO APPROPRIATIONS**

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House Finance and Taxation Committee  
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**REP. GROSZ** Second the motion. **MOTION CARRIED**

14 YES      0 NO      0 ABSENT

**REP. GROSZ** Was given the floor assignment.

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Salvatore Riccardi  
Operator's Signature

10/16/03  
Date

**FISCAL NOTE**  
 Requested by Legislative Council  
 02/20/2003

Amendment to: HB 1431

1A. **State fiscal effect:** Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. **Narrative:** Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

HB 1431 Third Engrossment requires the stamping of all cigarettes for sale in the state. The discount to tobacco wholesalers has been removed and the stamping expenses are required to be paid by the distributors. Therefore, HB 1431 Third Engrossment has no fiscal impact.

3. **State fiscal effect detail:** For information shown under state fiscal effect in 1A, please:

A. **Revenues:** Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

B. **Expenditures:** Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.

C. **Appropriations:** Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

Name:	Kathryn L. Strombeck	Agency:	Tax Dept.
Phone Number:	328-3402	Date Prepared:	02/21/2003

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*Kathryn L. Strombeck*  
 Operator's signature

10/16/03  
 Date

**FISCAL NOTE**  
 Requested by Legislative Council  
 02/14/2003

Amendment to: HB 1431

**1A. State fiscal effect:** Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			(\$700,000)			
Expenditures			\$110,000			
Appropriations						

**1B. County, city, and school district fiscal effect:** Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

**2. Narrative:** Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

Re-engrossed HB 1431 requires the stamping of all cigarettes for sale in the state. It also authorizes the sale of stamps at a discount to tobacco wholesalers. We estimate the discount provisions will reduce state general fund revenues by \$700,000 during the 2003-05 biennium. Additionally, administrative expenses for the Office of Tax Commissioner are expected to increase by \$110,000 during the 2003-05 biennium. These expenses include computer changes, postage, and the cost of the stamps themselves.

**3. State fiscal effect detail:** For information shown under state fiscal effect in 1A, please:

**A. Revenues:** Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

**B. Expenditures:** Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.

**C. Appropriations:** Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

<b>Name:</b>	Kathryn L. Strombeck	<b>Agency:</b>	Tax Dept.
<b>Phone Number:</b>	328-3402	<b>Date Prepared:</b>	02/18/2003

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*K. Costa*  
 Operator's Signature 10/16/03  
Date

**FISCAL NOTE**  
 Requested by Legislative Council  
 02/07/2003

Amendment to: HB 1431

1A. **State fiscal effect:** Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			(\$1,800,000)			
Expenditures			\$110,000			
Appropriations						

1B. **County, city, and school district fiscal effect:** Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. **Narrative:** Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

Engrossed HB 1431 requires the stamping of all cigarettes for sale in the state. It also authorizes the sale of stamps at a discount to tobacco wholesalers. We estimate the discount provisions will reduce state general fund revenues by \$1,800,000 during the 2003-05 biennium. Additionally, administrative expenses for the Office of Tax Commissioner are expected to increase by \$110,000 during the 2003-05 biennium. These expenses include computer changes, postage, and the cost of the stamps themselves.

3. **State fiscal effect detail:** For information shown under state fiscal effect in 1A, please:

A. **Revenues:** Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

B. **Expenditures:** Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.

C. **Appropriations:** Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

Name:	Kathryn L. Strombeck	Agency:	Tax Dept.
Phone Number:	328-3402	Date Prepared:	02/12/2003

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*K. Costa*  
 Operator's Signature

10/16/03  
 Date

**FISCAL NOTE**  
 Requested by Legislative Council  
 01/21/2003

Bill/Resolution No.: HB 1431

**1A. State fiscal effect:** Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
<b>Revenues</b>			(\$1,800,000)			
<b>Expenditures</b>			\$110,000			
<b>Appropriations</b>						

**1B. County, city, and school district fiscal effect:** Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

**2. Narrative:** Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

HB 1431 requires the stamping of all cigarettes for sale in the state. It also authorizes the sale of stamps at a discount to tobacco wholesalers. We estimate the discount provisions will reduce state general fund revenues by \$1,800,000 during the 2003-05 biennium. Additionally, administrative expenses for the Office of Tax Commissioner are expected to increase by \$110,000 during the 2003-05 biennium. These expenses include computer changes, postage, and the cost of the stamps themselves.

**3. State fiscal effect detail:** For information shown under state fiscal effect in 1A, please:

**A. Revenues:** Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

**B. Expenditures:** Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.

**C. Appropriations:** Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

<b>Name:</b>	Kathryn L. Strombeck	<b>Agency:</b>	Tax Dept.
<b>Phone Number:</b>	328-3402	<b>Date Prepared:</b>	02/04/2003

Date: 2-5-03  
Roll Call Vote #: 1

2003 HOUSE STANDING COMMITTEE ROLL CALL VOTES  
BILL/RESOLUTION NO. HB1431

House FINANCE & TAXATION Committee

Check here for Conference Committee

Legislative Council Amendment Number 30633.0300

Action Taken Do Pass as amended +

Motion Made By Rep. Clark Seconded By Rep. Grosz

Representatives	Yes	No	Representatives	Yes	No
BELTER, CHAIRMAN	✓				
DROVDAL, VICE-CHAIR	✓				
CLARK	✓				
FROELICH	✓				
GROSZ	✓				
HEADLAND	✓				
IVERSON	✓				
KELSH	✓				
KLEIN	✓				
NICHOLAS	✓				
SCHMIDT	✓				
WEILER	✓				
WIKENHEISER	✓				
WINRICH	✓				

Total (Yes) 14 No 0

Absent 0

Floor Assignment Rep. Grosz

If the vote is on an amendment, briefly indicate intent:

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Salvatore Riccardi Date 10/16/03  
Operator's Signature

REPORT OF STANDING COMMITTEE (410)  
February 6, 2003 8:43 a.m.

Module No: HR-23-1789  
Carrier: Grosz  
Insert LC: 30633.0202 Title: .0300

REPORT OF STANDING COMMITTEE

HB 1431: Finance and Taxation Committee (Rep. Belter, Chairman) recommends AMENDMENTS AS FOLLOWS and when so amended, recommends DO PASS and BE REREFERRED to the Appropriations Committee (14 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1431 was rereferred to the Appropriations Committee.

Page 1, line 2, after "57-36-13.1" insert ", 57-36-13.2"

Page 1, line 3, after "indicia" insert "and unfair and deceptive business practices"

Page 1, line 5, remove "to repeal section 57-36-25.1 of the North Dakota Century Code,"

Page 1, remove line 6

Page 6, after line 11, insert:

"SECTION 10. Section 57-36-13.2 of the North Dakota Century Code is created and enacted as follows:

57-36-13.2. Unfair and deceptive business practices. The advertising, offering for sale, or sale of cigarettes below cost to the retailer or cost to the wholesaler is an unfair and deceptive business practice. It is the policy of the state to promote the public welfare and it is the purpose of this chapter to carry out that policy in the public interest, stabilize the sale of cigarettes, and maximize and protect state revenues from this chapter. For purposes of this section:

1. "Cost to the retailer" means the cost to the wholesaler from whom the cigarettes were purchased by the retailer plus the cost of doing business by the retailer as evidenced by the standards and methods of accounting regularly employed by the retailer in the retailer's determination of costs for income tax reporting purposes for the total operations of the retailer's establishment. Cost of doing business by the retailer includes costs of:
  - a. Labor, including salaries of executives and officers;
  - b. Rent;
  - c. Depreciation;
  - d. Selling;
  - e. Maintenance of equipment;
  - f. Delivery;
  - g. Licenses;
  - h. Business taxes;
  - i. Insurance;
  - l. Advertising;
  - k. Any rebates, patronage dividends, or concessions, no matter how defined;

- l. Expenses prior to opening for business, including costs of startup, land acquisition, construction, marketing studies, and similar expenses;
- m. Any district, central, regional, and national administrative and operation costs and expenses; and
- n. All other indirect or overhead costs with respect to the operation of the business of the retailer.

The cost of doing business by the retailer must be expressed as a percentage and applied to the cost to the wholesaler from whom the cigarettes were purchased.

A retailer who purchases directly from a manufacturer or from any other person at or at less than or about the price normally and usually charged for purchases in wholesale quantities shall, in determining the cost to the retailer, add the cost of doing business by the wholesaler, to the basic cost of cigarettes to the retailer, as well as the cost of doing business by retailer.

In the absence of the filing with the commissioner of satisfactory proof of a lesser or higher cost of doing business by the retailer making the sale, the cost of doing business by the retailer is presumed to be eight percent of the cost to the wholesaler.

2. "Cost to the wholesaler" means the basic cost of cigarettes purchased by the wholesaler from a manufacturer plus the cost of doing business by the wholesaler as evidenced by the standards and methods of accounting regularly employed by the wholesaler in the wholesaler's determination of costs for income tax reporting purposes for the total operation of the wholesaler's business. The cost of doing business by the wholesaler includes costs of:

- a. Labor, including salaries of executives and officers;
- b. Rent;
- c. Depreciation;
- d. Selling;
- e. Maintenance of equipment;
- f. Delivery;
- g. Licenses;
- h. Business taxes;
- i. Insurance;
- j. Advertising;
- k. Any rebates, patronage dividends, or concessions, no matter how defined;

- l. Expenses prior to opening for business, including costs of startup, land acquisition, construction, marketing studies, and similar expenses;
- m. Any district, central, regional, and national administrative and operation costs and expenses; and
- n. All other indirect or overhead costs with respect to the operation of the wholesaler.

The cost of doing business by a wholesaler must be expressed as a percentage and applied to the basic cost of cigarettes.

In the absence of the filing with the commissioner of proof that the commissioner declares to be satisfactory of a lesser or higher cost of doing business by the wholesaler making the sale, the cost of doing business by the wholesaler is presumed to be five percent of the basic cost of cigarettes to the wholesaler."

Page 8, remove lines 20 and 21

Renumber accordingly

2003 HOUSE APPROPRIATIONS

HB 1431

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Date

2003 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1431

House Appropriations Committee

Conference Committee

Hearing Date 02-11-03

Tape Number	Side A	Side B	Meter #
2	X		25.4 - end of tape
		B	0.0-16.3
Committee Clerk Signature <i>Chris I. [Signature]</i>			

Minutes:

**Chairman Svedjan** Opened HB 1431 for discussion. There was a quorum present.

**Rep. Wes Belter** This bill requires all tobacco and cigarettes to be stamped before they are sold in the state. When the product comes to the wholesaler, they are stamped within 72 hours because there are a lot of counterfeit tobacco products imported. The bill's purpose is to get a handle on this.

**Rep. Carlisle** Will these stamps be implemented on the reservations also?

**Rep. Belter** That is probably still not decided. I'm not sure if the tribes can avoid stamping.

**John Olson, Representing the Phillip-Morris USA.** The jury is still out on this. We do need reservation cooperation on this.

**Chairman Svedjan** It exempts the tribes except for those products that are sold to tribal members.

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Operator's Signature

10/6/03  
Date

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House Appropriations Committee  
Bill/Resolution Number HB 1431  
Hearing Date 02-11-03

**John Olson** That is sort of a convoluted way of saying it, but it is correct. We only can control non-tribal entities. That is the premise.

**Rep. Rennerfeldt** Was there any concern voiced around interstate distributors?

**Olson** There was an e-mail from a distributor from Williston. It will be illegal to be in possession of cigarettes not stamped.

**Rep. Timm** 15-20 years ago we changed this for 2 reason, the costs to the state, and the warehouses didn't want to do this. Why did you introduce the bill?

**Rep. Belter** Phony cigarettes, we are 1 of 4 states that don't stamp currently.

**Rep. Timm** How many counterfeits are sold in ND?

**Rep. Belter** They don't think any have been.

**Rep. Carlson** If we are concerned about counterfeits, those people are not also paying in to the Tobacco Settlement Plan, correct? We build our revenues on the sales of tobacco.

**Rep. Belter** Correct.

**Rep. Monson** Its illegal to posses non-stamped cigarettes, but how many can a person have from a tribe while having non-stamped cigarettes?

**Rep. Belter** It is my understanding that if you have any in your possession you are in violation.

**Rep. Timm** Many people buy cigarettes over the Internet.

**Olson** That's why we're here. You're not going to get a handle on these counterfeit ones until the legitimate ones are stamped.

**Rep. Timm** Should the cigarette companies pay for this?

**Olson** I can support that, but there are already a lot of taxes on cigarettes.

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House Appropriations Committee  
Bill/Resolution Number HB 1431  
Hearing Date 02-11-03

**John Jove, Amcon Distributing Company** As far as the reservation question, you could buy a carton of cigarettes from anywhere and they look the same. This bill will attempt to have wholesaler affix the tax stamp on the bottom of the pack. The reservations would have their own stamp and they could not go off of the reservation.

**Rep. Carlson** Is this or is it not a problem?

**Jove** Yes, it is a problem. Nothing would be possible to detect this as of rows.

**Rep. Rennerfeldt** Couldn't they put counterfeit stamps on the counterfeit cigarettes?

**Jove** Yes, you could.

**Rep. Thoreson** It is going on in other parts of the country.

**Rep. Warner** Are we providing protection to other industries such as beer, wine, etc.?

**Rep. Timm** Would you have a problem with removing the penalty?

**Rep. Belter** The penalty may be too severe, but if we have laws there should be exceptions to them and the courts should look at the individual situations.

**Rep. Monson** Where is this new tax going?

**Rep. Belter** It is a discount distributor's receive, not a tax.

**Rep. Kroeber** Is that the way the states around us handle this?

**Rep. Belter** Yes.

**Rep. Brusegaard** How did this come out of the Finance and Tax Committee?

**Rep. Belter** It was a 14-0 Do Pass.

**Rep. Skarphol** Why should we do this?

**Rep. Belter** The Tax Commissioner stated we could capture our costs with this bill.

**Rep. Skarphol** I'd assume we'd sell these stamps. Isn't there revenue there?

Page 4  
House Appropriations Committee  
Bill/Resolution Number HB 1431  
Hearing Date 02-11-03

**Rep. Belter** Yes, but the difference will come in when we make up for illicit cigarettes.

**Rep. Timm** What are we repealing here in the law?

**Rep. Belter** It is section 11 of the bill.

**Jove** That is the administrative discount for license distributors. When the wholesalers of ND read this, they were amazed. They already are taxed \$100.00 per month.

**Rep. Brusegaard** I move the amendments 30633.0301 to HB 1431. 2nd by Rep. Carlisle.

**Motion Carries.**

**Rep. Timm** I propose an amendment to remove the penalty from the bill. It would be section 14 of the bill. 2nd by Rep. Carlson

**Rep. Warnke** What is the infraction carrying?

**Rep. Belter** A \$500 find and no jail time.

**Rep. Warnke** I move a substitute motion to remove "Class B misdemeanor" and replacing it with "infraction." 2nd by Rep. Wald. Motion Carries.

**Rep. Skarphol** I move a Do Not Pass As Amended. 2nd by Rep. Thoreson.

**Rep. Wald** I think we should resist this motion.

**Rep. Carlson** If we build one budget on cigarette taxes, then we should protect that and resist this motion.

**Rep. Timm** Its costing us money, so we should vote yes on this Do Not Pass. That's why it's here in the first place.

**Rep. Wald** This is a fairness issue.

**Rep. Skarphol** I agree on Wald and Carlson's philosophy, but its not going to realistically provide any revenue.

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10/16/03  
Date

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**Rep. Carlson** Look at the Tobacco Settlement Trust Fund. That will continue to decline if we don't enforce this.

**Rep. Martinson** Do Not Pass this. How can you possibly say that this will bring in money when the testimony indicates this is not even a problem in ND.

**Motion to Do Not Pass As Amended Carries 15 yeas, 7 nays, 0 A/NV. Rep. Skarphol will carry this bill.**

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10/16/03  
Date

2003 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1431

House Appropriations Committee

Conference Committee

Hearing Date 02-11-03

Tape Number	Side A	Side B	Meter #
2		X	-39.8
3	X		0.0-9.0
Committee Clerk Signature <i>Chris S. Nyhus</i>			

Minutes:

**Rep. Carlson** I move to reconsider our actions on HB 1431. 2nd by Rep. Aarsvold.

**Rep. Carlson** The major concern to this committee was that there was a \$700,000 fiscal note.

The cigarette companies would be willing to absorb the costs to the wholesalers.

**Rep. Timm** You move to take out the penalty?

**Rep. Carlson** I'm not sure.

**Rep. Aarsvold** The infraction is up to \$500 dollars.

**Rep. Bellew** I'd like clarification on parliamentary procedure. I believe only a person on the prevailing side can bring a bill back.

**Chairman Svedjan** Correct.

**Rep. Aarsvold** I was on the prevailing side and I move to reconsider our actions. 2nd by

**Rep. Glassheim.**

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Date

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House Appropriations Committee  
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Hearing Date 02-11-03

**Rep. Timm** I hope we resist this motion. We changed this 10-12 years ago because the wholesalers didn't want to do this any more.

**Rep. Carlson** We are one of only four states that don't stamp. The only way to know which cigarettes are black-market or reservation cigarettes is to stamp it.

**Motion Carries.**

**Rep. Carlson** I move to amend the bill. 2nd.

**Rep. Monson** Did all of the cigarette distributors buy off on this deal, or is it only the one that talked to Rep. Carlson?

**Rep. Carlson** I only talked to the distributor that was here. If others don't like it they'll work hard in the Senate to make sure that it dies.

**Rep. Delzer** When you reconsider a bill that was amended, don't you take the amendments off too?

**Chairman Svedjan** I don't think so.

**Motion Carries.**

**Rep. Delzer** It looks to me that subsection 2 of section 13 puts the penalty in there. If the distributors/wholesalers have agreed to do this, then I move to delete that subsection. 2nd by

**Rep. Thoreson.**

**Rep. Skarphol** It is subsection 2 of section 14 in the engrossed bill.

**Rep. Glassheim** If you have no penalty in this bill, it is useless.

**Rep. Wald** If you don't have a penalty, then Rep. Glassheim is right. Taking the penalty out defeats what we are trying to accomplish.

**Rep. Brusegaard** Resist this motion. Let's not act as the Judicial Committee.

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House Appropriations Committee  
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**Rep. Delzer** Isn't there a penalty in subsection #1 for the person selling the cigarettes?

**Rep. Timm** Lets support this and pass the bill.

**Rep. Monson** I relate this to being in possession of something illegal.

**Rep. Koppleman** This discussion has nothing to do with the fiscal impacts of the bill.

**Rep. Warner** There is no jail time with the infraction.

**Motion to amend Fails.**

**Rep. Koppleman** I move a Do Pass As Amended. 2nd by Rep. Carlson.

**Motion Carries 16-7-0. Rep. Koppleman will carry this bill.**

30633.0302  
Title.0400

Prepared by the Legislative Council staff for  
House Appropriations  
February 11, 2003

VK  
2/12/03

HOUSE AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1431 APP 2-13-03

Page 1, line 2, after the fifth comma insert "and" and remove ", and 57-36-25.2"

Page 1, line 4, remove "57-36-25.1,"

Page 1, line 5, after "indicia" insert "; to repeal section 57-36-25.1 of the North Dakota Century Code, relating to tobacco tax deductions for distributors"

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 2, line 27, after "tobacco" insert "and are not subject to the indicia requirements of this chapter"

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 3, line 29, after the period insert "A distributor shall provide minimum retail pricing on all invoices."

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 4, line 27, replace "computed as a percentage" with "three and one-half percent"

Page 4, line 28, replace "at the following rates:" with an underscored period

Page 4, remove lines 29 and 30

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 5, remove lines 1 through 6

Page 5, line 7, remove "5."

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 9, remove lines 5 through 30

HOUSE AMENDMENTS TO ENGROSSED HB 1431 APP 2-13-03

Page 10, remove lines 1 through 18

Page 10, line 30, replace "a class B" with "an infractor."

Page 10, replace line 31 with:

"SECTION 13. REPEAL. Section 57-36-25.1 of the North Dakota Century Code is repealed."

Renumber accordingly

REPORT OF STANDING COMMITTEE (410)  
February 13, 2003 1:26 p.m.

Module No: HR-28-2587  
Carrier: Koppelman  
Insert LC: 30633.0302 Title: .0400

REPORT OF STANDING COMMITTEE

HB 1431, as engrossed: Appropriations Committee (Rep. Svedjan, Chairman) recommends AMENDMENTS AS FOLLOWS and when so amended, recommends DO PASS (16 YEAS, 7 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1431 was placed on the Sixth order on the calendar.

Page 1, line 2, after the fifth comma insert "and" and remove ", and 57-36-25.2"

Page 1, line 4, remove "57-36-25.1,"

Page 1, line 5, after "indicia" insert "; to repeal section 57-36-25.1 of the North Dakota Century Code, relating to tobacco tax deductions for distributors"

Page 2, line 27, after "tobacco" insert "and are not subject to the indicia requirements of this chapter"

Page 3, line 29, after the period insert "A distributor shall provide minimum retail pricing on all invoices."

Page 4, line 27, replace "computed as a percentage" with "three and one-half percent"

Page 4, line 28, replace "at the following rates:" with an underscored period

Page 4, remove lines 29 and 30

Page 5, remove lines 1 through 6

Page 5, line 7, remove "5."

Page 9, remove lines 5 through 30

Page 10, remove lines 1 through 18

Page 10, line 30, replace "a class B" with "an infraction."

Page 10, replace line 31 with:

"SECTION 13. REPEAL. Section 57-36-25.1 of the North Dakota Century Code is repealed."

Renumber accordingly

30633.0401  
Title.0500

Prepared by the Legislative Council staff for  
Representative Carlson  
February 18, 2003

VR  
2/18/03

PROPOSED AMENDMENTS TO REENGROSSED HOUSE BILL NO. 1431

Page 4, replace lines 26 through 31 with:

"57-36-10.1. Indicia may be purchased at cost. A licensed distributor may purchase indicia for cigarettes at a cost not to exceed the cost of producing and distributing the indicia."

Page 5, remove lines 1 through 3

Renumber accordingly

Page No. 1

30633.0401

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La Costa Rickford  
Operator's Signature

10/16/03  
Date

REPORT OF STANDING COMMITTEE (410)  
February 19, 2003 7:37 a.m.

Module No: HR-32-3201  
Carrier: Grosz  
Insert LC: 30633.0401 Title: .0500

**REPORT OF STANDING COMMITTEE**  
HB 1431, as reengrossed: Appropriations Committee (Rep. Svedjan, Chairman)  
recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends  
**DO PASS** (13 YEAS, 4 NAYS, 6 ABSENT AND NOT VOTING). Reengrossed  
HB 1431 was placed on the Sixth order on the calendar.

Page 4, replace lines 26 through 31 with:

"57-36-10.1. Indicia may be purchased at cost. A licensed distributor may purchase indicia for cigarettes at a cost not to exceed the cost of producing and distributing the indicia."

Page 5, remove lines 1 through 3

Renumber accordingly

2003 SENATE FINANCE AND TAXATION

HB 1431

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2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1431

Senate Finance and Taxation Committee

Conference Committee

Hearing Date March 18, 2003

Tape Number	Side A	Side B	Meter #
1	X		30-end
		X	1-1365

Committee Clerk Signature *Mary Kay Wilcox*

Minutes:

Senator Urlacher opened the hearing on HB1431. All committee members are present. This bill relates to a tobacco tax indicia and unfair and deceptive business practices.

Representative Wes Belter (mtr #35) - Introduced the bill. This deals with the stamping of cigarettes (indicia). Briefly walked through the intent of the bill by each section. Distributed an amendment and explained its intent. This bill gives the distributors the authority to absorb the cost of the stamps and then will be reflected in the price of the cigarettes.

Senator Seymour (mtr #343) - Where did you get the idea for this bill?

Representative Belter (mtr #353) - This is an industry bill. Concerned about the counterfeit cigarettes coming in to the country. Two issues are important, one is to put a stop to the counterfeit cigarettes, and make sure the cigarettes that are not counterfeit are paying their tax.

John Olson, representing Phillip Morris USA (mtr #450) - Testified in support of HB1431.

Phillip Morris USA supports this bill to get ND in line with most of the country that already have

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*10/16/03*  
Date

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 18, 2003

stamping. ND is one of only four states that does not have stamping. Gave further answer to Senator Seymour's question and the history of stamping in ND. With the advent of the internet, there is more need for the stamp. This bill is related to HB1434. There is a growing concern of counterfeit sales, gray market and black market sales. Also concerned about sales to minors. In order to identify the legal product from the illegal product, you need stamping. That is part of a nationwide effort to get a handle on the distribution of this product. The amendment is an effort to get at the Internet sales that being made and the avoidance of taxes that these companies are doing.

Senator Nichols (mtr #846) - Regarding the Internet sales, do we have a reasonable guess on what percentage is coming in and do some of them, in fact, pay taxes.

Mr. Olson (mtr #868) - Referenced an example several weeks ago when an order was placed over the Internet and cigarettes purchased from Russia. Taxes had not been paid. Feels it is a large problem. Cited other examples of internet sales to avoid taxes.

Senator Syverson (mtr #1013) - Couple of questions on the bill. In reference to the bills description of tobacco products, includes all tobacco products and on page 5, it addresses just cigarettes, does not address other tobacco products that were addressed on page 1. Second question, on page 8, talks about a penalty of a Class A Misdemeanor and in another part it is a Felony. Also concerned about page 8 reference to penalties to any consumer that purchases a pack of cigarettes etc. Consumer in convenience store, is guilty of infraction because of a mislabeled product.

Mr. Olson (mtr #1165) - Why on only cigarettes? Because that is the only one that can be reasonably stamped. The issue of penalties, is a good concern, the bill is trying to get at those

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 18, 2003

distributors that are trying to violate the intent of the law, which is to get tax revenues to the state on legally marketed cigarettes. More serious penalties for people that are selling, need penalties for out of state companies, as far as the infraction, felt there needed to be something to prevent people from the illicit possession of these products.

Senator Syverson (mtr #1365) - Used the example of military personnel purchasing cigarettes on the base. Will these cigarettes be stamped.

Mr. Olson (mtr #1406) - Not sure if he has the answer to that question. We don't have state jurisdiction on federal property.

Senator Tollefson (mtr #1460) - The company you represent has products sold on the Internet.

Mr. Olson (mtr #1474) - Is correct to say they do have products for sold on the Internet, but the company does not sell on the Internet.

Senator Tollefson (mtr #1494) - Your company probably sells product on the Internet that is probably not taxed.

Mr. Olson (mtr #1542) - My company does not sell product on the Internet. Others do and that is the issue we are trying to address, that they are not taxed.

Toby Spangler, Regional Director of Government Affairs at Altria Corporate Services Inc. (mtr #1615) - Wants to address that last question regarding Internet sales. We are very aggressively going after a lot of the Internet companies that are selling over the Internet. We do not sell to these companies. This legislation offers the State of North Dakota an important opportunity to help eliminate tax evasion and other illegal activity related to cigarette sales. Feels HB1431 will address the counterfeit issue. Written testimony is attached. Urges the support of the committee.

Senator Seymour (mtr #2411) - Product can still be falsified with the tax stamp.

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Mr. Spangler (mtr #2427) - ND tax stamp should be unique. The solution to this issue includes litigation, law enforcement and legislation.

Senator Nichols (mtr #2532) - On the examples, there is a New York type of stamp. Is that supposed to be a stamp?

Mr. Spangler (mtr #2556) - That is an illegal stamp. In ND we have no idea, because there is no stamp.

Senator Nichols (mtr #2681) - With regard to the Native American reservations and the air bases. How would you envision what could be done to make that a better process.

Mr. Spangler (mtr #2714) - The air bases, will defer the question to the wholesalers. With regard to the reservations, we would work with the state coming up with some kind of equitable solution

Senator Tollefson (mtr #2819) - Talked of illegal and contraband in your testimony, does that have any relationship to quality.

Mr. Spangler (mtr #2840) - Absolutely, other problem is brand integrity. Product made by other manufacturer is of sub par quality.

Senator Syverson (mtr #2980) - Question regarding bogus cigarettes when you export for sales in foreign markets. Are cigarettes blended here or abroad and is the blend the same.

Mr. Spangler (mtr #3075) - We do manufacture all over the world. In foreign countries we license the brand, then its manufactured over seas. Our domestic product is manufactured in North Carolina and Virginia.

John F. Job, Division Manager, AMCON Distributing Co. and ND Candy and Tobacco

Wholesales Assoc. (mtr #3218) - Testified in support of HB1431. Feels the bill allows the state

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*10/16/03*  
Date

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Senate Finance and Taxation Committee  
Bill/Resolution Number HB1431  
Hearing Date March 18, 2003

of ND to ensure that all cigarettes sold in ND have had the taxes collected. Written testimony I attached.

Senator Nichols (mtr #3705) - What would be the approximate increase in cost to the consumer.

Mr. Job (mtr #3725) - Tough to estimate, feels it would be minimal. Guessing 3%-5%.

Russ Hanson, NDPMA (mtr #3841) - Testified in support of HB1431.

Tom Kelsch, representing the McLane Company (mtr #3977) - Testified in opposition to HB1431. Distributed an amendment and introduced McLane Company to explain the amendment. Also handed out ND's Unfair Trade Practices Law, Chapter 51-10 (exhibit A). Talked about the amendment taking out section 10 of the bill.

Charles Sulak, Manager of Corporate Tax for McLane Company (mtr #4140) - Testified in opposition to HB1431. Explained the amendment. Written testimony is attached.

Matt Bjornson (mtr #5744) - Testified in opposition to HB1431. Feels the bill is a well intentioned effort to stop problems that effects his business, but will cause serious problems in the cigarette market. Is concerned about sales on reservations. Most sales on the reservation are to non reservation members. This bill will not stop that. Feel the cigarette companies could limit the number of sales to reservation stores.

Tape 1, Side B

Mr. Bjornson (mtr #1) - Concerned about the huge shift of cigarette sales to reservation stores, which would significantly hurt his business. A good step in getting this problem solved, cigarette manufacturers would promote on a national basis, a stamp at the manufacture level. Feels that

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 18, 2003

would fix the inequities that retailers suffer. Feels this bill will put small retailers at a distinct competitive disadvantage.

Senator Wardner (mtr #230) - So you are objecting to the minimum pricing?

Mr. Bjornson (mtr #242) - Objects to the whole concept, in that it is not going to stop anything.

Adding the burden of the additional stamping, nobody has talked about how we are going to enforce this.

Rick Clayburgh, State Tax Commissioner (mtr #350) - Is neutral on the bill. Written testimony includes the administrative costs of this bill. Talked about the administrative costs associated with cigarette stamping. As bill was amended and moved out of the house, there is no specific provision for funding of the Tax Department's additional administrative costs. Again, as is, there is no appropriation to the Tax Department. Do need an appropriation attached to this bill to address the administration of the Tax Department. If bill remains unchanged and you maintain the minimum pricing section, then the appropriation will be a special fund appropriation allowing Tax Dept to receive the approximately \$130,000 for the biennium. If minimum pricing section is removed, we would need a general fund appropriation for that administration. Went over exactly what the additional costs would be to the Department. Asked that the administrative costs of the bill be attached to the bill at the request of the House Appropriations Chairman. Two specific issues raise concern, not only dealing with Native American sales, but also deals with military sales and sales at National Guard installations. These issues create a tremendous loophole.

Gary Anderson, State Tax Department (mtr #700) - In regards to the taxing provision, not opposed to it, it certainly provides an incentive to prevent the smuggling of cigarettes. Largest

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 18, 2003

concern the Tax Department has, as an enforcement agency, is the complaints received on purchases occurring through the reservations or military installations. Want to address that briefly, section 12 of the bill, has a penalty provision. In looking at that process, an individual should not have an unstamped pack with them, would be the intent of the Tax Department to create an indicia for a tribal stamp, which would ask wholesalers to use when selling to tribes. That will work for licensing distributors, but if purchased out of state and shipped interstate commerce, there will be some cigarettes that will go unstamped. Also looked at military aspect, in looking at reports, their cigarettes are supplied directly by the manufacturers. May need to create a military stamp and look to Phillip Morris to stamp before shipping. If we can stamp as much of the product as possible, including that going to tribal reservations and military installations, that makes the job of enforcement much easier.

Senator Seymour (mtr #1032) - The sponsors didn't come to you initially to talk about the issue of stamping?

Mr. Anderson (mtr #1044) - The proponents of the bill have talked to us throughout the process. But the issues of military and reservations specifically, did not come up. Agreed that the state doesn't have total policing authority in regards to the enforcement of cigarettes, if purchased out of state from a supplier and ship interstate commerce, the state can not interfere with that.

Senator Urlacher (mtr #1136) - How complicated will it be switching stamps from one location to another.

Mr. Anderson (mtr #1149) - Talked the number of distributors and manufacturers and the number of those that are already stamping for another state. Some cases it wouldn't be difficult.

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One thing ND has looked at, there is a company out there that is trying to develop an electronic stamping operation which intrigues us because it removes all of the necessity of handling rolls of stamps etc. Problem is that the system is very new.

Senator Urlacher (mtr #1365) - Given no further testimony, closed the hearing.

March 19, 2003 Tape 1, Side A

Senator Urlacher (mtr #4037) - Amendments are coming in on this as well. Will hold.

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*10/16/03*  
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2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1431

Senate Finance and Taxation Committee

Conference Committee

Hearing Date March 24, 2003

Tape Number	Side A	Side B	Meter #
1	X		2755-end
1		X	1-1623
Committee Clerk Signature <i>[Handwritten Signature]</i>			

Minutes:

Senator Urlacher opened discussion on HB1431. All committee members are present. This bill relates to tobacco tax indicia and unfair and deceptive business practices.

John Olson, representing Phillip Morris USA(mtr #2856) - Distributed amendment .0502 and explained the changes it would make to the bill and the resulting impact on the state general fund. Expanded on the amendment. Minimum pricing without any cost to the state is something the committee should consider. Concerned about untaxed sales. Distributed hard copy of article that talked about the stamping law and revenues in the state of Michigan. Copy attached.

Feels it makes sense to identify the product to be able to identify the problem.

Senator Wardner (mtr #3722) - Question regarding the states around us, do they stamp?

Mr. Olson (mtr #3742) - They do. Only four states in the country that do not stamp.

Senator Wardner (mtr #3795) - Can enact a law, not to buy over the Internet, but how would it be enforced?

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*10/16/03*  
Date

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 24, 2003

Mr. Olson (mtr #3828) - Not sure, but need to lay back drop to try and get a handle on it.

Senator Seymour (mtr #3949) - Question on stamping, talked about autos and textbooks being stamped at the place of origin, why not stamp cigarette packs at the manufacturer.

Mr. Olson (mtr #3996) - Can't really address that. Each state stamps and can determine the origin of the cigarettes to that state. Would need to federalize the issue if you want stamping at the manufacturer level.

Senator Wardner (mtr #4156) - Are you disputing the McClane information that indicated an increase of \$4.51 per carton?

Mr. Olson (mtr #4200) - That is not my issue.

Senator Wardner (mtr #4227) - With the 2%, do you have any idea what the fiscal note would be to the state?

Mr. Olson (mtr #4255) - Doesn't really know.

Senator Tollefson (mtr #4279) - What effect is contraband cigarettes on Phillip Morris?

Mr. Olson (mtr #4294) - Suspects contraband includes counterfeit cigarettes from China, which are coming over by ship container. Issues with brand integrity.

Senator Tollefson (mtr #4410) - Contraband cigarettes would probably come into the market unstamped.

Mr. Olson (mtr #4427) - Yes, could be counterfeit stamps as well.

Representative Belter (mtr #4530) - In response to Senator Seymour's question regarding stamping at the manufacturer, wouldn't work to stamp at the national level unless you were going to have a national federalized tax rate for all states. Point with this bill, the untaxing of

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 24, 2003

cigarettes will become a greater problem due to counterfeit and tax rates being raised here and in other states.

Senator Urlacher (mtr #4725) - Why did we stop stamping?

Representative Belter (mtr #4735) - Believes it was cost.

John Job, Amcon Distribution (mtr #4802) - Referenced a fact sheet that was distributed earlier.

Copy attached. It is common practice to have minimum pricing in place in neighboring states.

Senator Wardner (mtr #5210) - Question regarding the 5% & 8% minimum pricing. Need to reduce?

Mr. Job (mtr #5255) - Initially minimum pricing is based on Montana information, set the price at a middle of the road rate on the wholesale side and at the low end on the retail side.

Senator Wardner (mtr #5410) - What was the fiscal note when the bill was in the House.

Gary Anderson, State Tax Department (mtr #5488) - Regarding the fiscal note, was originally -700,000.00 for the biennium. Regarding the bill, concerned with making sure all cigarettes are stamped. Referenced stamping issues with Michigan and New York. Do not have information from manufacturer regarding a problem with counterfeit cigarettes. In ND military and reservation transactions a concern because of the inability to identify those sales. Concerned about how to regulate military personnel purchases. If these issues could be clarified would be a step forward in moving into a stamping process.

Senator Wardner (mtr #25) - Do businesses on the reservations buy their product from local wholesalers.

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Mr. Anderson (mtr #46) - In looking at information from wholesalers, we feel a significant portion of the cigarettes are being purchased from the wholesalers. The exception is the Hankinson Reservation.

Senator Wardner (mtr #185) - As we move forward and stamp the cigarettes, that means that the retailers on the reservation are going to have stamped cigarettes. Will they have to charge more?

Mr. Anderson (mtr #218) - The cost is insignificant, will have untaxed stamps.

Senator Syverson (mtr #258) - Is there a possibility that an agreement could be reached with the rest of the tribes, where they would be selling stamped cigarettes. Was it difficult to achieve with the Standing Rock Tribe?

Mr. Anderson (mtr #293) - In that case the tribe came to us and worked with us to initial the cigarette tax. Gave further information on working with tribes on taxing issues.

Senator Urlacher (mtr #394) - Would be to their benefit as well as ours to implement those arrangements.

Senator Seymour (mtr #410) - What are some of your ideas for enforcement of this?

Mr. Anderson (mtr #435) - That is part of the administrative process. Cost is built in. Would work if everybody stamped cigarettes.

Senator Urlacher (mtr #524) - Question regarding penalties to individuals that are in violation.

Mr. Anderson (mtr #530) - Is an infraction.

Senator Syverson (mtr #566) - Has a reasonable value been established to the amount of revenue that is lost to Internet sales or to importation of untaxed cigarettes.

Mr. Anderson (mtr #608) - It is not possible to identify that. Not sure to what degree the Internet creates a problem.

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Senate Finance and Taxation Committee

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Senator Tollefson (mtr #680) - Questions on the enforcement of Internet sales or contraband sales or a combination of. Is almost unenforceable.

Mr. Anderson (mtr #699) - That is correct. We have no restrictions over the postal service.

Senator Wardner (mtr #797) - With the 2% discount, are we looking approximately 400,000-500,000 negative fiscal note?

Mr. Anderson (mtr #822) - Is guessing a \$400,000 negative impact.

Senator Wardner (mtr #883) - Comment, feels we need to do something. This is a work in progress. All states around us do it. Feels it would increase revenue. Only question in the minimum pricing or the 2% discount. Will support cigarette stamping. Not ready to make a motion, needs time to look at the amendment and think about it.

Senator Nichols (mtr #1136) - With regard to the military and reservation sales, do you think that we would need some kind of stamp affixed to those cigarettes as well?

Senator Wardner (mtr #1167) - Yes, does feel that is important. As long as those retailers are buying from instate wholesalers, they will be stamped.

Senator Nichols (mtr #1243) - Those stamps would be different wouldn't they?

Senator Wardner - That is my understanding.

Senator Seymour (mtr #1342) - Feels we need a different attitude regarding Internet sales. Need to see as a positive rather than a negative.

Senator Wardner (mtr #1402) - Agrees with Senator Seymour.

Senator Tollefson (mtr #1440) - Hard to see how we will gain by stamping.

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Senator Wardner (mtr #1490) - It probably will be tough to start with, but we do have money in there for administration. Big thing we are looking at is contraband cigarettes coming to the reservation stores. Feels it is a work in progress.

Senator Urlacher (mtr #1600) - Given no further comments, closed the discussion.

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2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1431

Senate Finance and Taxation Committee

Conference Committee

Hearing Date March 25, 2003

Tape Number	Side A	Side B	Meter #
1	X		1225-4840

Committee Clerk Signature *Mary K. [unclear]*

Minutes:

Senator Urlacher opened the discussion on HB1431. All committee members are present. This bill relates to tobacco indicia and unfair and deceptive business practices.

Senator Wardner (mtr #1245) - In talking to wholesalers, the 2% discount doesn't do it.

Question for Tax Department - When the discount was at 3.5%, did the wholesalers have a problem with that?

Gary Anderson, State Tax Department (mtr #1302) - At 3.5% nobody spoke negatively towards the administrative fee. The fiscal effect was 700,000.00. Did some work last night, ran some numbers on 2% with a 25,000 cap as well as unlimited, no cap. Referenced handout. (exhibit A).

Senator Wardner (mtr #1530) - Comment, the 2% would probably hurt those below the \$14,000 on the chart. Are the costs the same regardless of the size of your company?

Mr. Anderson (mtr #1594) - The cost will escalate with the larger volume. Would need more than one stamping machine. Would envision the larger the wholesaler, the larger the cost. The

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 25, 2003

smaller wholesalers may have costs that larger wholesalers would not have.

Senator Wardner (mtr #1729) - Question on the cost of the basic equipment. Once purchased, what is the life of the equipment.

John Quinlan, State Tax Department (mtr #1760) - The equipment rental costs the wholesaler about \$5700.00 per year. Gave further information on the type of equipment that amount would cover. Feels smaller wholesalers would probably rent.

Senator Wardner (mtr #1861) - Question using an example of the Super Value store in Fargo. Would you foresee them renting this equipment and what would labor costs be.

Mr. Quinlan (mtr #1896) - Does not have answers regarding labor. Super Value is large and may have multiple machines.

Senator Wardner (mtr #1952) - Your guess would be that of retailers listed, many would already have the stamping machines?

Mr. Quinlan (mtr #1972) - The majority yes, in looking at the list of the top fifteen, just two or three that may not have the equipment.

Senator Wardner (mtr #2092) - Then basically it is labor and equipment that is going to cost the wholesaler to do the stamping.

Mr. Quinlan (mtr #2104) - Agreed. Gave further information on the availability of equipment rental and the options included in the contracts.

Senator Urlacher (mtr #2214) - When we stopped stamping, why was there no gain?

Mr. Quinlan (mtr #2248) - At the time Pitney Bowes had a monopoly on the stamp equipment market, they gave a two year notice that they would be discontinuing that service. At that time

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the wholesalers came forward, we looked at the expense of stamping and determined, after reviewing their request, to end stamping in ND.

Senator Urlacher (mtr #2470) - Could this cycle repeat itself?

Mr. Quinlan (mtr #2483) - There are new companies trying to break into the industry. Feel that other alternatives will be available in the future. Talked about companies that are working on different types of stamping that would be paperless.

Senator Urlacher (mtr #2608) - We can stamp, but we can not enforce regarding Internet sales, reservation sales and military sales.

Mr. Quinlan (mtr #2635) - That is correct, we are able to stamp, in the past have stamped reservation cigarettes with a tribal non taxed stamp. But the military cigarettes are shipped directly from the manufacturer and have never been taxed.

Senator Urlacher (mtr #2725) - Concerned about a shift in purchases, and losing the tax base we have now.

Senator Seymour (mtr #2750) - Still feels something should be done at a national level.

Mr. Quinlan (mtr #2790) - Feels Phillip Morris is doing as much as can be done, have created their brand integrity division and litigating just about every case they where they find counterfeit product.

Senator Tollefson (mtr #3006) - State of ND can't do anything about the issues just talked about.

The present system is a paper system for tax reporting. Would 1431 improve that situation?

Won't give anymore enforcement over the areas that you discussed now.

Mr. Quinlan (mtr #3063) - That is correct.

Senator Tollefson - So 1431 really doesn't do a lot for the State of North Dakota.

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Senate Finance and Taxation Committee

Bill/Resolution Number HB1431

Hearing Date March 25, 2003

Gary Anderson, State Tax Department (mtr #3094) - Responded to Senator Tollefson's remarks.

Talked about enforcement and how that would work in the Tax Department. In essence enforcement will take people away from enforcing other taxes.

Senator Tollefson (mtr #3268) - Commented, without additional staff you are going to take people away from other duties, to expand the staff is going to take more state dollars. Still seeking whether 1431 will do anything for North Dakota beyond what we are doing now.

Mr. Anderson (mtr #3327) - Would agree, feels the solution would be a company that could do electronic stamping.

Mr. Quinlan (mtr #3542) - Talked about stamp on demand on other states and the benefit of that system.

Senator Wardner (mtr #3578) - In this bill, 8% discount for retailers and 2% discount for wholesalers is that still in the bill?

Mr. Quinlan (mtr #3638) - The 8% retail and 5% wholesale was in the unfair trade practices, that is separate from the 2% discount. Is a separate issue.

Senator Syverson (mtr #3739) - Does anybody have a speculative number on the percentage of cigarette sales in ND that are currently not taxed. Excluding Indian reservations and military installations.

Mr. Quinlan (mtr #3789) - Guess about 1%-2%, feels that would be a high number. Don't know the extent of the Internet sales.

Mr. Anderson (mtr #3872) - Look to the distributors for information on buying patterns of their customers. Wholesalers do a good job of policing a lot of the activity out there.

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Senate Finance and Taxation Committee

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Senator Syverson (mtr #3963) - An observation, in 2001 had about 20 millions dollars in revenue generated in the State of North Dakota from cigarette tax sales, 1% of that is not a whole lot and we may spend more than that on enforcement.

Mr. Anderson (mtr #4024) - That is correct.

Senator Urlacher (mtr #4039) - Would simplified sales tax eventually come into any advantage here? And whether the Federal government reacts to Internet sales? Can you relate to that?

Mr. Anderson (mtr #4089) - The streamlined sales tax won't have an effect on this.

Mr. Quinlan (mtr #4155) - Federal attention is starting to be paid to this issue.

Senator Wardner (mtr #4202) - What do the wholesalers and retailers charge now for the cost of doing business.

Mr. Quinlan (mtr #4219) - Believes wholesaler stated yesterday that they are at about 3.5% in that business operation. As long as they are complying with the Unfair Practices Act and selling about cost, there is no violation.

Senator Wardner (mtr #4373) - Will support the bill the way it is. We are one of four states that don't stamp, feels we need to get started.

Senator Urlacher (mtr #4473) - Question if there is much gain and if it is enforceable.

Senator Tollefson moves to amend with .0502. Motion dies for lack of a second.

Tollefson moves a Do Not Pass. Second by Senator Seymour.

Roll call vote 4 yea, 2 nay, 0 absent. Carrier is Senator Tollefson.

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30633.0501  
Title.

Prepared by the Legislative Council staff for  
Representative Belter  
March 17, 2003

PROPOSED AMENDMENTS TO REENGROSSED HOUSE BILL NO. 1431

Page 1, line 2, after "57-36-12.1" insert ", 57-36-12.2"

Page 2, line 9, remove "Indicia under this chapter may be sold to and affixed only in North Dakota by licensed"

Page 2, line 10, remove "distributors."

Page 5, after line 16, insert:

**"SECTION 9.** Section 57-36-12.2 of the North Dakota Century Code is created and enacted as follows:

**57-36-12.2. Retail sales by remote sellers.** A person may not make a sale from a location outside this state for delivery to a consumer in this state of any cigarettes without indicia attached as required by this chapter.

Page 9, after line 2, insert:

**"3. A second or subsequent offense under section 57-36-12.2 is a class C felony."**

Renumber accordingly

30633.0502  
Title.

Prepared by the Legislative Council staff for  
Representative Belter  
March 24, 2003

3 24.03

PROPOSED AMENDMENTS TO REENGROSSED HOUSE BILL NO. 1431

Page 1, line 2, after the fourth comma insert "and" and remove ", and 57-36-13.2"

Page 1, line 3, remove "and unfair and deceptive business"

Page 1, line 4, remove "practices"

Page 4, replace lines 26 and 27 with:

"57-36-10.1. Indicia may be purchased at discount. Any licensed distributor may purchase indicia for taxed cigarettes at a discount. The tax commissioner may allow the discount in the settlement of the account of the wholesale distributor upon the payment to the tax commissioner of any moneys due by reason of the sale, delivery, or consignment to the distributor of the indicia. The discount is two percent of the face value of the indicia. The total discount under this section for any distributor may not exceed twenty-five thousand dollars for each fiscal year. A licensed distributor may purchase indicia for untaxed cigarettes at a cost not to exceed the cost of producing the indicia. A discount is not allowed for the purchase of untaxed cigarette indicia."

Page 5, remove lines 28 through 31

Page 6, remove lines 1 through 30

Page 7, remove lines 1 through 30

Page 8, remove lines 1 through 9

Renumber accordingly

Page No. 1

30633.0502

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REPORT OF STANDING COMMITTEE (410)  
March 25, 2003 12:40 p.m.

Module No: SR-53-5672  
Carrier: Tollefson  
Insert LC: . Title: .

**REPORT OF STANDING COMMITTEE**  
HB 1431, as reengrossed: Finance and Taxation Committee (Sen. Urlacher, Chairman)  
recommends **DO NOT PASS** (4 YEAS, 2 NAYS, 0 ABSENT AND NOT VOTING).  
Reengrossed HB 1431 was placed on the Fourteenth order on the calendar.

(2) DESK, (3) COMM

Page No. 1

SR-53-5672

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Date

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2003 TESTIMONY

HB 1431

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Yolanda Rickford 10/16/03  
Operator's Signature Date



**3125 East Thayer Avenue  
Bismarck, ND 58501**

AMCON Distributing Company of Bismarck distributes consumer products in North Dakota, South Dakota, Minnesota, and Montana.

I am in favor of HB 1431 with the amendments to remove from section 3, 57-36-07 number 2, or the 72 hour provision and a state minimum pricing amendment.

Our company ships cigarettes into several tax jurisdictions. At the present time we are stamping cigarettes on demand (by individual order) for the surrounding states. Approximately half of our volume is in ND and half is in MN, MT, and SD. By forcing the wholesaler to stamp all cigarettes within 72 hours of receipt we would be forced to increase our inventories to extremely large levels in order to anticipate any unforeseeable sales demands.

The minimum pricing amendment is taken from Montana state law. It is very similar to Minnesota, South Dakota, Nebraska, Iowa, and other states with minimum pricing. The minimum pricing allows the wholesaler to recover the cost of stamping machine equipment, labor to affix the stamp, and a return on the investment of stamp inventory. HB 1431 will require AMCON Distributing Company to acquire an additional cigarette stamping machine and the hire and training of an additional employee. We would also have to invest in a sufficient inventory of stamps to cover sales. Our Bismarck distribution center is cigarette tax stamping in MN, MT, & SD, and those states have had cigarette minimum pricing laws for a number of years. It is a common business practice to have minimum pricing of cigarettes set by the various states.

I also believe that all of the wholesalers of ND would agree that we need to stamp sales in ND. At the present time, no one can determine if a pack of cigarettes has had the ND tax applied just by looking at it. However we need the amendments to HB 1431. Without the amendments it would cause undue financial hardship on the wholesalers.

Testimony for amended HB 1431

John E. Job, Division Manager, AMCON Distributing Company, 701-258-3618  
Home address: 3115 Arizona Drive, Bismarck, ND 58503, 701-258-8167

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10/16/03  
Date

Variable Discount

36-19.1

John Guinlan  
HB 1431

JULSON JONES COMPANY

0720111111

		3.5	4	Variable Comp
		714,286	625,000	
1	Wholesale Supply	247713849	25000	25000
2	FLEMING	388153504	25000	25000
3	AMCON	242508761	25000	25000
4	FRANK McKONG	172392671	25000	25000
5	Schwab Wholesale	120996124	25000	25000
6	NASH FINCH - FARGO	90826124	25000	25000
7	GHC Merchandise Dist	69848271	24447	25000
8	FRANCIS Becken	65281938	22849	25000
9	HENRY'S FOODS	60366317	21128	24147
10	NASH FINCH MINOT	59872267	20955	23949
11	MCLANE Western Inc	51225680	17929	20490
12	FM Jobbing	47955961	16785	19182
13	MCLANE - MN	38981215	13643	15592
14	Super Valu - FARGO	37034360	12962	14814
15	Super Valu - Bis	32840564	11494	13136
16	World Wide	28274136	9896	11310
17	QUEEN City Candy	23771011	9320	9508
18	OK Dist	17807414	6233	7123
19	MASON Bros	6875832	2407	2750
20	HET - Moberge Candy	6416080	2246	2566
21	Fleming Supermarkets	5568640	1949	2227
22	Albertsons Dist Ctr	2494690	873	998
23	RE FRITZ	24090	843	964
24	S ABRAHAMSON	2123876	743	850
25	RJ REYNOLDS Tob Co	1909248	668	764
26	FRANCHISE WHOLESALE	1512720	529	605
27	PAPIOTRAC	631547	221	253
28	KRETEK INTL	322696	113	129
29	MCLANE SE	223080	78	89
30	PRAIRIE Wholesale	137280	48	55
31	SANTA FE Natural	123829	43	50
32	GA ANDERSON & CO	117927	41	47
33	SANTA FE INC	70055	25	28
34	Tobacco Row	68372	24	27
35	MHJ Wholesale	528	18	21
36	M+R Dist	51920	18	21
37	Lorillard Tobacco	9856	3	4
38	RJ REYNOLDS Smokeshop	8140	3	3
		347534	371702	358607.23

PREPARED BY STATE TAX COMMISSIONER (1/16/2003)

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10/16/03  
Date

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TESTIMONY BEFORE THE NORTH DAKOTA LEGISLATURE IN SUPPORT OF  
HOUSE BILL 1431  
February 5, 2003

Mr. Chairman, members of the committee, good morning. My name is Jack Holleran, and I am the Vice President of Brand Integrity at Philip Morris USA. Thank you for giving me this opportunity to present our views in support of House Bill 1431. This legislation offers the State of North Dakota an important opportunity to help disrupt, reduce and eventually eliminate illegal activity related to cigarette sales.

A weak economy, heightened consumer frugality, and dramatic increases across the country in state cigarette excise taxes and other costs have caused smokers across the nation to seek avenues for purchasing cigarettes at a lower price. While there is nothing wrong with looking for a bargain, unfortunately this purchasing behavior has led to a growing number of unintended consequences. These include an increase in illegally sold or "contraband" cigarettes.

This illegal activity hurts everyone, whether or not they are smokers or engaged in the tobacco trade. Like any illegal activity, contraband cigarette trafficking negatively affects our society. Illegal cigarette sales also deprive governments of tax revenue and can result in stolen products, hijacked cigarette trucks, tarnished trademarks and brand reputations, and distortions in the legitimate market. Illegal sales are currently posing a threat not only to Philip Morris USA, which makes about half of the cigarettes sold in the U.S., but also to the State of North Dakota in the form of increased crime and lost revenue that, if collected, could provide the state with additional tax revenue. It is currently estimated that billions of dollars in federal and state tax revenue is lost each year due to illegal activity related to cigarette sales. (See e.g. Opening Statement of Director Bradley A. Buckles to the International Conference on Illicit Tobacco Trade, United Nations (July 2002).)

NO. 231 P. 12

FEB. 5. 2003 8:51PM PM CORPORATE AFFAIRS

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*Jack Holleran*  
Operator's Signature

10/16/03  
Date

Illegal cigarette sales also hurt law-abiding businesses including wholesalers, retailers and manufacturers who are competing against those that have unfair economic advantages due to illegal activity.

Finally, illegal sales negatively impact our brands, including Marlboro, if adult smokers unknowingly purchase substandard, counterfeit cigarettes that they believe are authentic. Moreover, Internet sites often mislead consumers into violating State excise tax laws and the laws against re-importing versions of domestic brands that are not intended to be sold in the United States or are imported in violation of Federal law.

Philip Morris USA takes the issue of illegal cigarette sales very seriously, and we are pleased to support House Bill 1431. We commend Rep. Belter for his leadership in putting forth legislation that, if enacted and enforced, would help disrupt, reduce and ultimately eliminate illegal cigarette sales.

Let me tell you how, starting with the issue of contraband. There are four types of contraband cigarettes:

- Counterfeit cigarettes, which are of poor quality when smoked, but are difficult to identify before consumption because the external packaging is very similar to legitimate product.
- Illegally imported or illegally re-imported cigarettes, formerly known as "gray market" cigarettes, which are intended for sale outside the United States. These cigarette sales are illegal under federal law and under North Dakota law.

NO. 231 P. 13

FEB. 5. 2003 8:51PM PM CORPORATE AFFAIRS

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*10/16/03*  
Date

- **Untaxed and under-taxed cigarettes, which are genuine cigarettes that are intended for sale typically in a low tax state, but are illegally sold often over the Internet or through direct mail, in states and localities with higher excise taxes.**
- **And finally, stolen containers of cigarettes or cigarettes stolen from retail stores. According to the FBI there is \$12 - \$20 billion worth of cargo, including cigarettes, stolen every year in the U.S.**

According to the U.S. Customs Service, the number of seizures of counterfeit cigarettes jumped significantly in 2002, with the seized product representing a domestic value of \$37.6 million versus \$4.5 million in 2001. During fiscal year 2002 (October 2001 - September 2002), 34 containers of counterfeit cigarettes were seized - representing close to 300 million cigarettes. During the last three months of 2002, 16 containers of counterfeit cigarettes were seized - representing over 15 million cigarettes. Phillip Morris USA has already identified more than 60 counterfeit product codes and confirmed the existence of counterfeit cigarettes at retail in 6 states, with suspected counterfeit cigarettes in 10 more. Most counterfeit cigarette packs also carry counterfeit tax stamps.

Not only does illegal trafficking hurt those legitimately engaged in the trade by infiltrating the legal channels through which cigarettes are currently sold, causing lost sales and damage to valuable brand reputations, this illegal activity also occurs without full or any payment of taxes and escrow payments to the State and by its very nature disregard for the state and federal laws. The activity also supplants sales of genuine product by manufacturers such as Phillip Morris USA.

House Bill 1431 would help address these serious issues by providing better tools for law enforcement officials to eliminate contraband cigarettes, and by helping to trace product moving through the cigarette distribution channel, so that illegal product can be kept out and legitimate

NO. 231 P. 14

FEB. 9. 2003 8:52PM PM CORPORATE AFFAIRS

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*Richard Costa*  
Operator's Signature

*10/16/03*  
Date

product cannot be illegally diverted. By requiring that cigarettes sold in the state bear a tax indicia, law could help officials identify illegal product and ensure appropriate cigarette taxes are paid on cigarettes sold in North Dakota. This is a policy Philip Morris USA strongly supports, and it is currently required in 46 other states. North Dakota is one of just 4 states where cigarette wholesalers are not required by law to apply tax stamps to each pack of cigarettes they distribute. This bill would, among other things:

- Require tax indicia on each pack of cigarettes sold in the state. The indicia can only be sold to and affixed in North Dakota by licensed distributors and must be affixed to cigarettes sold in the state within 72 hours of receipt by the distributor.
- Require licensed dealers only to sell, buy or have in their possession cigarettes that have an indicia.
- Require the tax commissioner to keep a record of all indicia received and distributed.
- Require the seizure and forfeiture of cigarettes transported from place to place within the state without indicia, and the vehicles transporting them.

One area where the bill could go further is to require an indicia for product sold on Native American Reservations. Without impinging on the established rights of Native American tribes to be exempt from state excise taxes, controls should be put in place to ensure that this exemption is applied only as intended. Examples of measures that should be considered include a requirement that those shipping product from tribal lands be responsible for making sure that they deal only with licensed members of the trade who will pay all appropriate taxes due. Further, North Dakota should consider a system whereby Native American tribes are required to pay all state excise taxes for all sales, and the state

NO. 231 P. 15

FEB. 5. 2003 8:52PM PM CORPORATE AFFAIRS

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Department of Revenue can reimburse them for taxes paid on sales to tribal members. We would be happy to work with the committee to address this issue.

Conclusion

The issue of illegal cigarette sales is one that Philip Morris USA takes very seriously, and we are committed to working with you to help stop this growing problem. While Philip Morris USA will continue to work with law enforcement in North Dakota and elsewhere in order to provide intelligence information and cooperate with their investigations, there is a clear need for the existing laws to be strengthened so that law enforcement has the tools it needs to address this issue. House Bill 1431 is an important step toward solving this issue. We urge you to support it. Thank you.

NO. 231 P. 16

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10/16/03  
Date



"Kelly Kaiser"  
<kellyk@okdist.com>  
02/05/2003 12:28 AM

To: <ddrovdal@state.nd.us>, <bolark@state.nd.us>,  
<rfroello@state.nd.us>, <mpgrosz@state.nd.us>,  
<cheadland@state.nd.us>, <riverson@state.nd.us>,  
<skelsh@state.nd.us>, <fklein@state.nd.us>,  
<enichoia@state.nd.us>, <arschmid@state.nd.us>,  
<dweiler@state.nd.us>, <rwikenhe@state.nd.us>,  
<lwinrich@state.nd.us>, <wbelter@state.nd.us>  
cc: <erennerf@state.nd.us>  
Subject: HB 1431

Gentlemen,

I would like to introduce myself, I am Kelly Kaiser, I own O.K. Distributing in Williston. We are a candy and tobacco distributor. My wife is expecting and we have a doctor's appointment Wednesday morning and I will not be able to attend the committee hearing on HB 1431. Therefore, I would like to offer my thoughts on this bill.

HB 1431 as it stands, I am against it. I can understand why we need to stamp cigarettes. We need to know where ND taxed products are and where they end up. But in order to go back to stamping cigarettes would require additional employees and equipment costs. I feel that there are amendments that can be added that would be useful.

Page 2, line 20-23 should be deleted (72 hour stamping law). The majority of ND wholesalers stamp in multiple states. If we are required to stamp our inventory within 72 hours, we would have to carry separate inventories for each state. At 400 different kinds of cigarettes, it would require a substantial capital investment and physical warehouse space for each tax jurisdiction.

The addition of predatory pricing regulations to this bill would prevent large out of state distributors to lose money on tobacco products for a time to gain market share in this state and drive small local distributors out of business. I believe it is in the States best interest to have in-state distributors. We are the collectors for tobacco taxes. We can be easily audited and responsible for abiding by ND law. It would also help us defray the additional expense of stamping. We employ hundreds of North Dakotans. I myself employ twenty people. I believe that all of us grew up in ND and have an interest in this state. Personally, I am the third generation in this company. I was born here, educated in ND and have started a family here.

These changes and additions to this bill will allow us to stamp and collect the cigarette tax efficiently and prevent predatory pricing. It would be a "fair" law for both the State and the distributors.

In closing, I hope you will give weight to the distributors that will be testifying verbally Wednesday. I know they will communicate more effectively the points I have mentioned above and give additional reasons to amend this bill.

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Operator's Signature

10/16/03  
Date

Feel free to call me if you need any additional questions answered.

Thank you for your time and consideration on this bill.

Sincerely,

Kelly Kaiser

O.K. Distributing Co., Inc.

Williston, ND

701-572-9161

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*Yolanda Rickford*

10/16/03

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TESTIMONY BEFORE THE NORTH DAKOTA LEGISLATURE IN SUPPORT OF  
HOUSE BILL 1431  
March 18, 2003

Mr. Chairman, members of the committee, good morning. My name is Toby Spangler, and I am the Regional Director of Government Affairs at Altria Corporate Services Inc. I am here on behalf of our affiliate, Philip Morris USA, and want to thank you for giving me this opportunity to present our views in support of House Bill 1431. This legislation offers the State of North Dakota an important opportunity to help eliminate tax evasion and other illegal activity related to cigarette sales.

- A weak economy, heightened consumer frugality, and dramatic increases across the country in state cigarette excise taxes and other costs have caused smokers across the nation to seek avenues for purchasing cigarettes at a lower price.
- Unfortunately, this purchasing behavior has led to a growing number of unintended consequences, including an increase in illegal, or "contraband", cigarettes.
- This illegal activity hurts everyone, whether or not they are smokers, and whether or not they are engaged in the tobacco trade.
  
- Illegal sales are currently posing a threat to the State of North Dakota in the form of increased crime and lost revenue that, if collected, could help improve the state's budget situation. It is currently estimated that billions of dollars in federal and state tax revenues are lost each year nationwide due to contraband cigarettes.

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Toby Spangler  
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- In addition to depriving governments of tax revenue, illegal cigarette sales can result in stolen products, hijacked cigarette trucks, tarnished trademarks and brand reputations, and distortions in the legitimate market.
- Contraband cigarettes, including counterfeit versions of our genuine cigarettes, illegally imported cigarettes, and cigarettes that are purchased in low excise tax states and smuggled into and illegally re-sold in higher excise tax states, are a growing problem in this country.
- Illegal cigarette sales also hurt law-abiding businesses including wholesalers, retailers and cigarette companies who are competing against those that have unfair economic advantages due to illegal activity.
- And like any illegal activity, contraband cigarette trafficking negatively affects our society.
- Philip Morris USA takes the issue of illegal cigarette sales very seriously, and we are pleased to support House Bill 1431.
- We commend Rep. Belter for his leadership in putting forth legislation that, if enacted and enforced, would help North Dakota to disrupt, reduce and ultimately eliminate illegal cigarette sales.
- House Bill 1431 would help address these serious issues by requiring indicia that could help to trace product moving through the cigarette distribution channel, so that illegal product can be kept out and legitimate product cannot be illegally diverted.
- By requiring that cigarettes sold in the state bear a tax indicia, this law could help officials identify illegal product and ensure appropriate cigarette taxes are paid on cigarettes sold in North Dakota. This is a policy Philip Morris USA strongly supports, and it is currently required in 46 other states.

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Salvatore Riccio  
Operator's Signature

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- North Dakota is one of just 4 states where cigarette wholesalers are not required by law to apply tax stamps to each pack of cigarettes they distribute. In addition, this bill would:
- Require that tax indicia only be sold to and affixed in North Dakota by licensed distributors and must be affixed to cigarettes sold in the state within a reasonable period of receipt by the distributor.
- Require licensed dealers only to sell, buy or have in their possession cigarettes that have an indicia.
- Require the tax commissioner to keep a record of all indicia received and distributed.
- Require the seizure and forfeiture of cigarettes transported from place to place within the state without indicia, and the vehicles transporting them.
- One area where the bill could go further is to require an indicia for product sold on Native American Reservations. Without impinging on the established rights of Native American tribes to be exempt from state excise taxes, controls should be put in place to ensure that this exemption is applied only as intended. We would be happy to work with the committee to address this issue.
- The issue of illegal cigarette sales is one that Phillip Morris USA takes very seriously, and we are committed to working with you to help stop this growing problem.
- We urge you to support House Bill 1431. Thank you.

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10/16/03  
Date



P.O. Box 1472  
Bismarck, ND 58502-1472  
701-258-3618

Testimony in favor of HB 1431 by John F. Job, Division Manager, AMCON Distributing Company, 701-258-3618 Home address: 3115 Arizona Drive, Bismarck, ND 58503, 701-258-8167

AMCON Distributing Company of Bismarck distributes consumer products in North Dakota, South Dakota, Minnesota, and Montana. About half of our cigarette volume is to ND retailers.

HB 1431 allows the state of ND to ensure that all cigarettes sold in ND have had the taxes collected. As is it now you cannot look at a package of cigarette sold in ND and know that the tax has been paid. Tax stamping will solve that. The stamping section of the bill is very similar to other legislation that has been in effect for years in other states.

Section 10 of HB 1431 was taken from Montana state law. It is very similar to Minnesota, South Dakota, Nebraska, Iowa, and other states with minimum pricing. The minimum pricing allows the wholesaler to recover the cost of stamping machine equipment, labor to affix the stamp, and a return on the investment of stamp inventory. HB 1431 will require AMCON Distributing Company and most other wholesalers to acquire additional cigarette stamping machines (nearly \$15,000 per year lease) and to hire and train an additional employee (estimated at 30 to \$35,000 per year). We would also have to invest in a sufficient inventory of stamps to cover sales (based on our average cigarette inventory (\$100,000 at stamping start up). At the present time our Bismarck distribution center is cigarette tax stamping for MN, MT, & SD, and those states have cigarette minimum pricing laws and have had those laws for a number of years. It is a common business practice to have minimum pricing of cigarettes set by the various states.

When one looks at the negative revenue impact to the state of ND of a carton of cigarettes that was purchased on the internet, mail order, tribal, or out of state the results can be staggering. In addition to the lost excise tax the MSA (Master Settlement Agreement) sales are not tracked. The state will lose the \$4.40 per carton excise tax plus the nearly \$5.00 per carton MSA funding. Just a small percentage of sales that are untaxed and untracked will have a negative impact on our states revenue collections. By having all cigarettes sold in ND affixed with indicia, those excise tax revenues will be collected and the MSA payments will be tracked for payment.

I am testifying in favor of passage of HB 1431 on behalf of the 55 employees of AMCON Distributing Company – Bismarck and on behalf of the other members of the ND Candy and Tobacco Wholesalers Association and their employees.

FR

**PROPOSED AMENDMENTS TO  
REENGROSSED HOUSE BILL NO. 1431  
(Third Engrossment)**

Page 5, remove lines 28 through 31

page 6, remove lines 1 through 30

Page 7, remove lines 1 through 30

Page 8, remove lines 7 through 9

Renumber accordingly

Proposed by McLane Co.

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Yolanda Richardson  
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10/16/03  
Date

## CHAPTER 51-10

## UNFAIR TRADE PRACTICES LAW

Section	Section
51-10-01. Definitions.	51-10-07. Application of provisions of chapter.
51-10-02. Items advertised, offered for sale, or sold with other items at a combined price — Regulations governing.	51-10-08. No immunity from self-incrimination.
51-10-03. Unfair advertising, offer to sell, or sale.	51-10-09. Proof of intent — Cost surveys — Repealed.
51-10-04. Schemes or devices included within sales below cost.	51-10-10. Procedure for establishing cost survey — Hearing — Notice — Repealed.
51-10-05. Advertising, offering, or selling article at less than cost — Penalty.	51-10-11. Hearings and investigations — Contempts — Repealed.
51-10-05.1. Powers of attorney general.	51-10-12. North Dakota trade commission — Repealed.
51-10-05.2. Subpoena — Hearing — Rules.	51-10-13. Appointment and term of members — Repealed.
51-10-05.3. Failure to display information or obey subpoena.	51-10-14. Retailer's license — Penalty — Repealed.
51-10-06. Injunctive relief may be had in addition to other penalties — Duty to commence actions.	51-10-15. Disbursement of funds — Repealed.

**51-10-01. Definitions.** In this chapter, unless the context or subject matter otherwise requires:

1. "Cost" means the actual invoice cost of the merchandise or the replacement cost of the merchandise, whichever is the lower, less all trade discounts, advertising allowances, including customary discounts for cash, to which must be added transportation, including cartage cost, not otherwise included in the invoice cost or the replacement cost of the merchandise. Where a manufacturer publishes a list price, proof of such list price, less all discounts, is prima facie evidence of "cost".
2. "Replacement cost" means the cost per unit at which the merchandise sold or offered for sale could have been bought by the seller at any time prior to the date of sale or the date upon which it is offered for sale by the seller.
3. "Retailers" means and includes every person, partnership, corporation, limited liability company, or association engaged in the business of making sales at retail within this state. In the case of a person, partnership, corporation, limited liability company, or association engaged in the business of making sales at retail and sales at wholesale, such term must be applied only to the retail portion of such business.
4. "Sell at retail", "sales at retail", and "retail sale" mean and include any transfer for a valuable consideration, made in the ordinary course of trade or in the usual prosecution of the seller's business, of title to tangible personal property to the purchaser for consumption or use other than resale or further processing or manufacturing, except that sales to contractors or subcontractors engaged in any

type of building operation or the repair of buildings or other improvements upon real estate must be deemed sales for consumption and not for further processing or manufacturing. The terms include any transfer of such property where title is retained by the seller as security for the payment of the purchase price.

5. "Sell at wholesale", "sales at wholesale", and "wholesale sales" mean and include any transfer for a valuable consideration made in the ordinary course of trade or the usual conduct of the seller's business, of title to tangible personal property to the purchaser for purposes of resale or further processing or manufacturing, except that sales to contractors engaged in any type of building operation or the repair of buildings or other improvements upon real estate, regardless of further processing or manufacturing of the material sold, must be deemed retail sales and not wholesale sales. The terms include any transfer of such property where title is retained by the seller as security for the payment of the purchase price.
6. "Wholesaler" means and includes every person, partnership, corporation, limited liability company, or association engaged in the business of making sales at wholesale within this state. In the case of a person, partnership, corporation, limited liability company, or association engaged in the business of making both sales at wholesale and sales at retail, such terms must be applied only to the wholesale portion of such business.

Source: S.L. 1941, ch. 291, § 2, subss. 1, 2, 4, 5 to 7; R.C. 1943, § 51-1001; S.L. 1993, ch. 54, § 106.

**Cross-References.**

Unfair dairy trade practices, see § 4-14-09.

**Collateral References.**

Trade Regulation — 891-910.  
 32 Am. Jur. 2d, Fair Trade Laws, §§ 1, 2; 54 Am. Jur. 2d, Monopolies, Restraints of Trade, and Unfair Trade Practices, §§ 1077-1106.  
 87 C.J.S. Trade-Marks, Trade-Names, and Unfair Competition, §§ 240, 244, 245.  
 Delegation of legislative power by authorizing manufacturers of trade-marked articles to fix resale price, 3 A.L.R.2d 201.  
 Intoxicating liquors, state power to regulate price of, 14 A.L.R.2d 699.  
 Comment note: Validity of state "Fair Trade" Act as applied to nonsigning reseller, 19 A.L.R.2d 1139.  
 Trading stamps, premiums, or the like as violation of fair trade law, 22 A.L.R.2d 1212.  
 Validity, under state constitutions, of nonsigner provision of fair trade laws, 60 A.L.R.2d 420.

Who may fix resale price under Fair Trade Act specifying vendor or seller as stipulator of resale price, 64 A.L.R.2d 758.

Contract restrictions, enforceability, insofar as restrictions would be reasonable, of contract containing unreasonable restrictions on competition, 61 A.L.R.3d 397.

Scope and exemptions of state deceptive trade practice and consumer protection acts, 89 A.L.R.3d 399.

Delivery of merchandise, failure to deliver ordered merchandise to customer on date promised as unfair or deceptive trade practice, 7 A.L.R.4th 1257.

Validity, construction and application of state statutory provisions prohibiting sales of commodities below cost, 41 A.L.R.4th 612.

Validity, construction, and application of state statute forbidding unfair trade practice or competition by discriminatory allowance of rebates, commissions, discounts, or the like, 41 A.L.R.4th 675.

Coverage of insurance transactions under state consumer protection statutes, 77 A.L.R.4th 991.

Coverage of leases under statute consumer protection statutes, 89 A.L.R.4th 854.

**51-10-02. Items advertised, offered for sale, or sold with other items at a combined price — Regulations governing.** When one or more items are advertised, offered for sale, or sold with one or more other items at a combined price, or are advertised, offered as a gift, or given with the sale of one or more items, each and all of said items, for the purpose of this chapter, must be deemed to be advertised, offered for sale, or sold, and the price of each item named must be governed by the provisions of subsection 1 or 2 of section 51-10-01, respectively.

Source: S.L. 1941, ch. 291, § 2, subs. 3; R.C. 1943, § 51-1002.

**Franchise Fee.**

Where corporation marketed its product through distributors under a multi-level marketing plan, and to become a distributor a fee

was charged for a literature package and to become a direct distributor a fee entitled "booking entry fee" was charged, those charges constituted a franchise fee. *Meadow Fresh Farms, Inc. v. Sandstrom*, 333 N.W.2d 780 (N.D. 1983).

**51-10-03. Unfair advertising, offer to sell, or sale.** Any advertising, offer to sell, or sale of any merchandise, either by retailers or wholesalers, at less than cost as defined in this chapter, which has the intent or the effect of inducing the purchase of other merchandise or of unfairly diverting trade from a competitor or otherwise injuring a competitor, impairs and prevents fair competition, injures public welfare, and is unfair competition and contrary to public policy and the policy of this chapter, where the result of such advertising, offer, or sale is to tend to deceive any purchaser or prospective purchaser, or substantially to lessen competition, or unreasonably to restrain trade, or to tend to create a monopoly in any line of commerce.

Source: S.L. 1941, ch. 291, § 3; R.C. 1943, § 51-1003.

**Collateral References.**

Validity, construction, and application of state statute provision prohibiting sales of commodities below cost—modern cases, 41 A.L.R.4th 612.

Validity, construction, and application of state statute forbidding unfair trade practice or competition by discriminatory allowance of rebates, commissions, discounts, or the like, 41 A.L.R.4th 675.

**51-10-04. Schemes or devices included within sales below cost.** The inhibition against sales below cost, as defined in this chapter, shall embrace any scheme of special rebate, collateral contract, or any device of any nature whereby such result is, in substance or in fact, effected in violation of the spirit and intent of this chapter.

Source: S.L. 1941, ch. 291, § 3; R.C. 1943, § 51-1004.

**Collateral References.**

Validity, construction, and application of

state statute forbidding unfair trade practice or competition by discriminatory allowance of rebates, commissions, discounts, or the like, 41 A.L.R.4th 675.

**51-10-05. Advertising, offering, or selling article at less than cost — Penalty.** Any retailer or wholesaler who shall advertise, offer to sell,

51-10-05.1

SALES AND EXCHANGES

or sell any article of merchandise at less than cost to such retailer or wholesaler as defined in this chapter, or who gives, offers to give, or advertises the intent to give away any article of merchandise, with the intent, or with the effect of injuring competitors and destroying competition, is guilty of a class A misdemeanor.

Source: S.L. 1941, ch. 291, § 4; R.C. 1943, § 51-1005; S.L. 1975, ch. 106, § 555.

**Collateral References.**

Validity, construction, and application of state statutory provision prohibiting sales of commodities below cost--modern cases, 41 A.L.R.4th 612.

Validity, construction, and application of state statute forbidding unfair trade practice or competition by discriminatory allowance of rebates, commissions, discounts, or the like, 41 A.L.R.4th 675.

**51-10-05.1. Powers of attorney general.** When it appears to the attorney general that a person has engaged in, or is engaging in, any practice declared to be unlawful by this chapter or when the attorney general believes it to be in the public interest that an investigation should be made to ascertain whether a person in fact has engaged in, is engaging in, or is about to engage in, any such practice the attorney general may:

1. Require that person to file on forms prescribed by the attorney general, a statement or report in writing, under oath or otherwise, as to all the facts and circumstances concerning the sale or advertisement of merchandise at less than cost as defined in this chapter and any other data and information the attorney general may deem necessary.
2. Examine under oath any person in connection with the sale or advertisement of any merchandise at less than cost as defined in this chapter.
3. Examine any merchandise or sample of merchandise, record, book, document, account, or paper as the attorney general may deem necessary.
4. Pursuant to an order of a district court impound any record, book, document, account, paper, or sample of merchandise material to such practice and retain it until completion of all relevant proceedings under this chapter.

Source: S.L. 1991, ch. 525, § 1.

**51-10-05.2. Subpoena — Hearing — Rules.** The attorney general may issue subpoenas to any person, administer an oath or affirmation to any person, conduct hearings in the aid of any investigation of inquiry, prescribe forms, and adopt necessary rules.

Source: S.L. 1991, ch. 525, § 1.

**51-10-05.3. Failure to display information or obey subpoena.** If any person fails or refuses to file any statement or report, or obey any

subpoena issued by the attorney general, the attorney general may file in the district court a petition for an order directing the person to file the required statement or report or to obey the subpoena. The order may be granted by the district court after notice and hearing.

Source: S.L. 1991, ch. 525, § 1.

**51-10-06. Injunctive relief may be had in addition to other penalties — Duty to commence actions.** In addition to the penalties provided in this chapter, the courts of this state are invested with the jurisdiction to prevent and restrain violations of this chapter by injunctive proceedings. The attorney general and the several state's attorneys shall institute suits in behalf of this state, to prevent and restrain violations of the provisions of this chapter. Any person damaged, or who is threatened with loss or injury, by reason of a violation of the provisions of this chapter, is entitled to sue for and have injunctive relief in the district court against any damage or threatened loss or injury by reason of a violation hereof.

Source: S.L. 1941, ch. 291, § 5; R.C. 1943, action under state unfair or deceptive trade § 51-1006; S.L. 1965, ch. 330, § 1; 1973, ch. practices law, 54 A.L.R.5th 631. 387, § 1; 1991, ch. 525, § 2.

**Collateral References.**

Constitutional right to jury trial in cause of

**51-10-07. Application of provisions of chapter.** The provisions of this chapter do not apply to sales at retail or sales at wholesale, where:

1. Merchandise is sold in bona fide clearance sales, if advertised, marked, and sold as such.
2. Perishable merchandise must be sold promptly in order to forestall loss.
3. Merchandise is imperfect or damaged, or is being discontinued and is advertised, marked, and sold as such.
4. Merchandise is sold upon the final liquidation of any business.
5. Merchandise is sold for charitable purposes or to relief agencies.
6. Merchandise is sold on contract to departments of the government or government institutions.
7. The price of merchandise is made in good faith to meet legal competition.
8. Merchandise is sold by any officer acting under the order or direction of any court.

Any retailer or wholesaler claiming the benefits of any of the exemptions provided for in this section shall have the burden of proof of facts entitling such retailer or wholesaler to any of the benefits of said exemptions.

Source: S.L. 1941, ch. 291, § 6; R.C. 1943, § 51-1007.

**51-10-08. No immunity from self-incrimination.** No person subpoenaed or ordered may be excused from attending and testifying or from producing books, records, correspondence, documents, or other evidence in any civil action or proceeding instituted or brought, pursuant to the provisions of this chapter, upon the ground that the testimony or evidence required of that person may tend to incriminate that person or subject that person to a penalty or forfeiture. No person may be prosecuted or subjected to any penalty or forfeiture for or on account of any act, transaction, matter, or thing concerning which that person is compelled, after having claimed the privilege against self-incrimination, to testify or produce evidence. The provisions of this section do not exempt any person from prosecution or punishment for perjury.

Source: S.L. 1941, ch. 291, § 7; R.C. 1943, § 51-1008.

Privilege against self-incrimination, criminal proceedings, see N.D. Const., Art. I, § 12; § 31-01-09.

**Cross-References.**

Perjury, see § 12.1-11-01.

**51-10-09. Proof of intent — Cost surveys.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-10. Procedure for establishing cost survey — Hearing — Notice.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-11. Hearings and investigations — Contempts.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-12. North Dakota trade commission.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-13. Appointment and term of members.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-14. Retailer's license — Penalty.** Repealed by S.L. 1991, ch. 525, § 4.

**51-10-15. Disbursement of funds.** Repealed by S.L. 1991, ch. 525, § 4.

**CHAPTER 51-11**

**FAIR TRADE LAW**

[Repealed by S.L. 1979, ch. 516, § 1]

TESTIMONY  
OF  
MCLANE COMPANY, INC.

BEFORE THE SENATE FINANCE AND TAXATION COMMITTEE  
NORTH DAKOTA LEGISLATIVE ASSEMBLY

ON

HOUSE BILL 1431

TUESDAY, MARCH 18, 2003  
9:00 AM

FOR MORE INFORMATION:

KIMBERLY A. WOODARD  
SENIOR MANAGER  
GOVERNMENTAL AFFAIRS AND CORPORATE COMMUNICATIONS

MCLANE COMPANY, INC.  
4747 MCLANE PARKWAY  
TEMPLE, TEXAS 76504  
(254) 771-7431  
[KWOODARD@MCLANECO.COM](mailto:KWOODARD@MCLANECO.COM)

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Operator's Signature

*Lo Costa Rickford*

Date

*10/16/03*

TESTIMONY OF MCLANE COMPANY, INC.  
BEFORE THE SENATE FINANCE AND TAXATION COMMITTEE  
NORTH DAKOTA LEGISLATIVE ASSEMBLY  
ON  
HOUSE BILL 1431

TUESDAY, MARCH 18, 2003

Good morning. My name is Charles Sulak, and I am Manager of Corporate Tax for McLane Company. On behalf of McLane Company, I want to thank you for the opportunity to speak with you today regarding House Bill 1431.

McLane Company strongly opposes this legislation, which includes a provision to impose minimum pricing constraints on the wholesale and retail sale of cigarettes. As a distributor of such products, McLane Company takes a keen interest in this legislation.

MCLANE COMPANY, INC. - BACKGROUND

McLane Company, Inc., headquartered in Temple, Texas, is a wholly-owned subsidiary of Wal-Mart Stores, Inc., and provides distribution services to multiple industries throughout the United States. We deliver food and non-food products to more than 50,000 customer locations around the world - including the convenience store, chain drug store, mass merchandise, quick service restaurant, and movie theater industries. We operate 19 grocery divisions and 18 foodservice distribution centers around the country. McLane employs more than 15,000 people in the United States.

Although McLane Company does not operate a distribution center in North Dakota, our parent corporation, Wal-Mart Stores, Inc., operates eight (8) discount stores and two (2) Sam's Club outlets - employing more than 2,000 people statewide.

McLane Company's North Dakota customers are serviced from our McLane Minnesota distribution center. We paid a total of approximately \$930,512 in cigarette excise taxes to the State of North Dakota in fiscal year ended January 1, 2003. Our market share in the state was approximately 4.87 percent in fiscal year ended January 1, 2003. In addition to our parent corporation, McLane Company sells cigarettes and tobacco products to three other customers in the State of North Dakota.

POSITION ON HOUSE BILL 1431

As previously stated, McLane Company strongly opposes House Bill 1431. The bill, among other things, would prohibit the sale of cigarettes without tax indicia. Although compliance of such a requirement will increase McLane Company's costs, we agree with the those who believe that requiring tax indicia to be affixed to packages of cigarettes would more than likely have the effect of reducing illegal activity related to cigarette sales.

However, we do not think that the costs of administering a tax for the state of North Dakota should be borne solely by wholesalers, as now provided for in House Bill 1431. As initially proposed, the bill would have helped to reduce expenses by providing licensed distributors a discount against purchases of tax indicia.

As originally drafted, House Bill 1431 provided distributors a discount that ranged from two percent to five percent of the face value of the tax indicia, based upon purchases, not to exceed \$25,000 each fiscal year. A discount against stamp purchases, commonly known as a cigarette excise tax administrative allowance, is provided to distributors by all 50 states and the District of Columbia - the stated purpose of which is to reimburse distributors for the expense of affixing tax indicia to packages of cigarettes.

Existing North Dakota statute, Section 57-36-25.1, titled "Deduction to Reimburse Licensed Distributor for Administrative Expenses," reads:

*"A licensed distributor who pays the tax due under this chapter..... may deduct and retain one and one-half percent of the tax due to reimburse the distributor for expenses incurred in keeping records, preparing and filing returns, remitting the tax, and supplying information requested by the commissioner. The total deduction allowed.....may not exceed one hundred dollars per month....."*

The expenses related to affixing tax indicia to packages of cigarettes are substantial, and are both fixed and variable. The fixed costs are labor and equipment, while the variable costs are in the areas of insurable risk, security, audit risk, stamping mistakes, bad debt risk, and shrinkage. There are also administrative costs, such as recordkeeping and reporting, obtaining and transporting the tax stamps, and meeting certain bonding requirements.

After several revisions, the discount provided for in House Bill 1431 went from a sliding scale based on purchases, not to exceed \$25,000 per year; to three and one-half percent, not to exceed \$25,000 per year; to no discount at all, but indicia can be purchased at cost.

It is unclear now whether the existing discount of one and one-half percent will still be provided to distributors. Instead, it appears as if the increased costs associated with further administering the North Dakota cigarette excise tax is to be borne by the wholesaler.

#### THE PROBLEMS WITH NORTH DAKOTA HOUSE BILL 1431

➤ **Minimum Pricing is Not the Means by Which to Reimburse Wholesalers for the Expense of Administering the State's Cigarette Excise Tax**

Language has been included in House Bill 1431 that effectively creates cigarette "price fixing." The bill now dictates the minimum price wholesalers and retailers can legally sell cigarettes based on costing computations required by the bill. The required formula for the determination of state mandated minimum pricing is set forth through the use of the definition "cost of doing business."

Essentially, this bill now imposes a "fixed" minimum price on cigarettes by requiring that the sales price be at a required percentage above a predetermined, manipulated and inflated cost, which is little more than "government price fixing." It is important to note that the Department of Revenue will not allow the use of this "cost" number in preparing North Dakota income tax returns.

In House testimony, it was stated that "minimum pricing allows the wholesaler to recover the cost of stamping machine equipment, labor to affix the stamp, and a return on the investment of stamp inventory." This statement is inaccurate. As previously mentioned, the cigarette excise tax administrative allowance, which is currently provided for under North Dakota statute, is for the purpose of reimbursing licensed distributors for the costs associated with administering the cigarette excise tax.

On the other hand, the minimum pricing constraints provided for in House Bill 1431 have nothing to do with off-setting costs associated with affixing tax indicia to packages of cigarettes. What it does, however, is benefit a handful of companies who claim that they cannot compete without government intervention.

It was also presented in House testimony that "it is common business practice to have minimum pricing of cigarettes set by the various states." That statement is inaccurate. While it is true that the states bordering North Dakota (Minnesota, Montana and South Dakota) impose minimum pricing constraints, it is hardly "common business practice" to do so. In fact, only 26 jurisdictions impose this type of inflated pricing scheme.

➤ **Wholesalers and Retailers are Guaranteed a Profit at the Expense of North Dakota Consumers**

House Bill 1431 statutorily eliminates a free market economy - with respect to cigarettes, and imposes higher prices on North Dakota consumers. If enacted, HB 1431 would force wholesalers and retailers to statutorily mark up the price of each carton of cigarettes by five percent and eight percent, respectively - pocketing a profit on each carton of cigarettes sold.

If House Bill 1431 is enacted, the per carton cigarette price to consumers will increase by \$4.51. Essentially, wholesalers will pocket \$1.60 per carton and retailers will realize a \$2.69 per carton profit. Both are at the expense of the consumer. (See attached chart.) This statutory profit will increase substantially if, as expected, cigarette prices continue to rise.

➤ **The State of North Dakota Will Lose Revenue Under House Bill 1431**

The presumptive cost of doing business is an artificial price that has no rational relationship to the actual cost of doing business by those involved in the cigarette trade. This "price fixing" scheme increases the price of cigarettes to consumers in North Dakota, without affecting the neighboring jurisdictions, which distorts the competitive marketplace in substantial ways - making it cost effective for smokers to purchase their cigarettes from alternative sources, including stores in neighboring states, e-tailers (Internet retailers), the black market, and Native American reservations.

The basic economic principle of "Price Elasticity of Demand" provides that when prices rise, quantity demanded can be expected to decline. These sensible consumer responses to higher prices in the state of North Dakota will have negative results, including lost tax revenue to the state, lost sales for taxpaying businesses in the state, and an increase in illegal black market activity. (See enclosed map.)

➤ **House Bill 1431 Represents Little More than Government "Price Fixing"**

The role of government should not be to engage in "price fixing," but rather to promote the free market principles upon which this nation was built. If House Bill 1431 is enacted, then businesses that sell cigarettes should not be the only group to receive "government protection." This measure allows for a guaranteed profit not provided for in most industries.

Thus, it begs the question: why not extend such protections for other commodities as well? If the state is not going to provide "price fixing" protection to wholesalers of bread, clothing, pharmaceuticals or any other commodity, why should cigarette wholesalers be given special treatment? HB 1431 is the beginning of a slippery slope toward government price controls on a variety of products.

➤ **Businesses Will Survive With or Without This Statute - Minimum Pricing Laws Do Not Keep Companies in Business**

Proponents of House Bill 1431 claim to need government imposed "price fixing," arguing that without this protection they will eventually be put out of business. This assumption is without merit or factual basis. While it is true that some inefficient wholesalers have seen their profits reduced or have been replaced by other more efficient wholesalers, that phenomenon is a function of the free market economy and not unfair trade practices.

As previously stated, our market share in the state was less than 5 percent in fiscal year ended January 1, 2003 - *hardly a monopoly*.

The real competitors whom proponents of this measure should fear are the owners of smoke shops set up on Native American reservations. These individuals do not pay the state excise tax, nor will they mark up the cost of cigarettes as required under House Bill 1431, and they certainly do not pay state sales tax. Essentially, a carton of cigarettes sold on Native American territory will sell for \$27.64, while traditional retailers all over the state will be forced to sell a carton of cigarettes for \$38.15. (See enclosed map.)

House Bill 1431 will encourage, not prevent, the movement of the cigarette distribution industry outside of North Dakota, with the attendant job loss and tax revenue loss. The increased prices necessitated by this bill mean fewer cigarettes will be legitimately sold in North Dakota - resulting in lower tax revenues and a detriment to the business base in the state.

➤ **House Bill 1431 is Redundant - Federal and State Law Already Prohibit Sales Below Cost**

Proponents of the minimum pricing provision indicate the need to eliminate sales of cigarettes below "cost" with the intent to harm competition. It is already illegal under federal law to sell any item below cost with the intent to harm competition. The Robinson-Patman Act (15 U.S.C. Section 13) provides the following with respect to this matter:

*"It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price.....where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition....."*

Furthermore, North Dakota has an "Unfair Trade Practices Law" (Title 51, Chapter 10) that is very similar to that of the federal Robinson-Patman Act, which reads as follows:

*"Any retailer or wholesaler who shall advertise, offer to sell, or sell any article of merchandise at less than cost to such retailer or wholesaler.....or who gives, offers to give, or advertises the intent to give away any article of merchandise, with the intent, or with the effect of injuring competitors and destroying competition, is guilty of a class A misdemeanor."*

North Dakota's "Unfair Trade Practices Law" also provides for "injunctive relief against any damage or threatened loss or injury by reason of a violation."

If there are sales occurring that are below cost, then the federal government and the state of North Dakota need to enforce the laws currently on the books, rather than layer a flawed statute on top of two existing statutes.

CONCLUSION

House Bill 1431 started as a well-intentioned piece of legislation, designed to reduce illegal activity related to cigarette sales. Instead, and with all due respect to the proponents of this bill, the measure has veered significantly off-track from its stated goal and will, in fact, increase illegal activity with respect to cigarette sales.

It is unfortunate that the state apparently does not have a funding source to reimburse distributors for affixing tax indicia to packages of cigarettes; however, engaging in governmental "price fixing" is not the answer.

For the reasons outlined, I respectfully urge you to oppose House Bill 1431. Thank you for your time. I am happy to answer any questions that you may have.

Impact of Proposed  
**North Dakota UNFair Trade Bill**  
 (HB 1431)

Calculation Sheet

	Premium	Generic
Manufacturer's Price	27.64	24.94
+ State Tax	<u>4.40</u>	<u>4.40</u>
Basic Cost	32.04	29.34
+ 5% Mark-up	<u>1.60</u>	<u>1.47</u>
Wholesale Price	33.64	30.81
+ 8% Mark-up	<u>2.69</u>	<u>2.46</u>
Retail Price	36.33	33.27
+ 5% Sales Tax	<u>1.82</u>	<u>1.66</u>
Final Price to Consumer	38.15	34.93

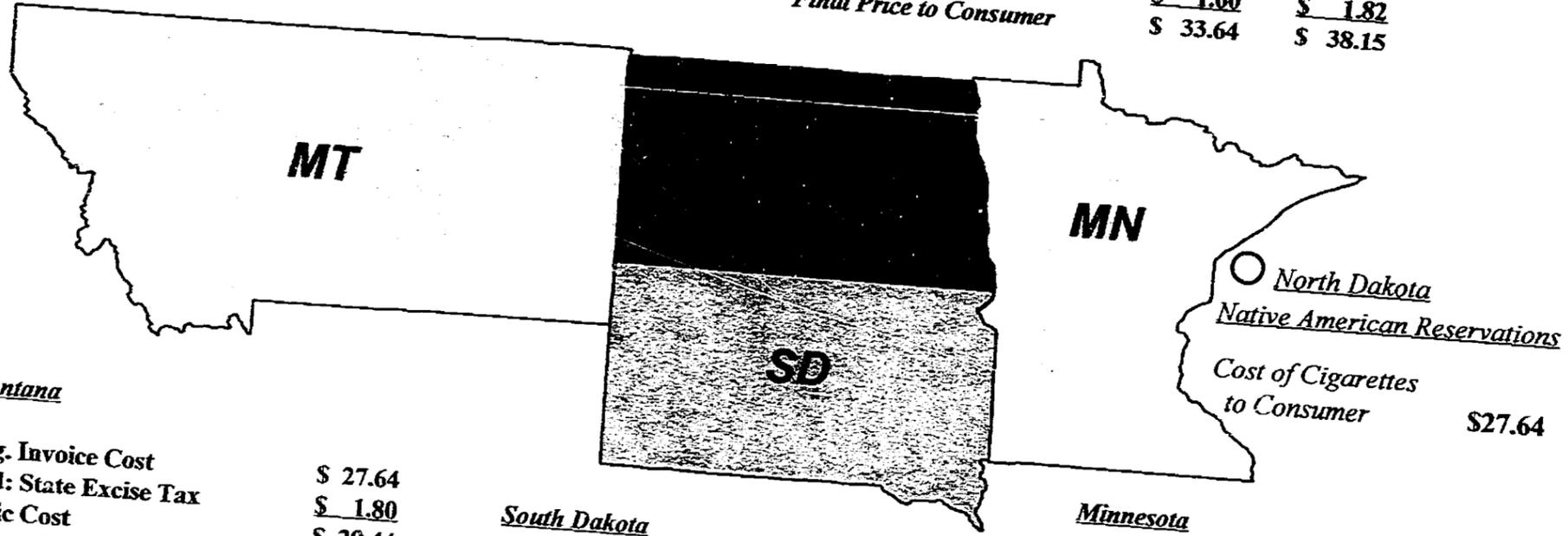
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Salvatore Riccardi  
 Operator's Signature

10/10/03  
 Date

Impact of Proposed  
**North Dakota**  
**UN Fair Trade Bill**  
 (HB 1431)

	Current	HB1431
Mfg. Invoice Cost		
Add: State Excise Tax	\$ 27.64	\$ 27.64
Basic Cost	\$ 4.40	\$ 4.40
Add: 5% Statutory Markup	\$ 32.04	\$ 32.04
Cost to Retailer		\$ 1.60
Add: 8% Retail Markup		\$ 33.64
Price to Consumer		\$ 2.69
Add: 5% State Sales Tax	\$ 1.60	\$ 1.82
Final Price to Consumer	\$ 33.64	\$ 38.15



Montana

Mfg. Invoice Cost	\$ 27.64
Add: State Excise Tax	\$ 1.80
Basic Cost	\$ 29.44
Add: 5.75% Statutory Markup	\$ 1.70
Cost to Retailer	\$ 31.14
Add: 10% Retail Markup	\$ 3.12
Price to Consumer	\$ 34.26
Add: 0% State Sales Tax	\$ 0.00
Final Price to Consumer	\$ 34.26

South Dakota

Mfg. Invoice Cost	\$ 27.64
Less: 2.75% Cash Discount	-\$ 0.76
Add: State Excise Tax	\$ 3.30
Basic Cost	\$ 30.18
Add: 5.5% Statutory Markup	\$ 1.68
Cost to Retailer	\$ 31.86
Add: 8% Retail Markup	\$ 2.55
Price to Consumer	\$ 34.41
Add: 4% State Sales Tax	\$ 1.38
Final Price to Consumer	\$ 35.79

Minnesota

Mfg. Invoice Cost	\$ 27.64
Add: State Excise Tax	\$ 4.80
Basic Cost	\$ 32.44
Add: 4.5% Statutory Markup	\$ 1.46
Cost to Retailer	\$ 33.90
Add: 8% Retail Markup	\$ 2.72
Price to Consumer	\$ 36.62
Add: 6.5% State Sales Tax	\$ 2.38
Final Price to Consumer	\$ 39.00

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Operator's Signature Yolanda Rickard  
 Date 10/6/83

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Testimony before the Senate Finance and Taxation Committee  
House Bill 1431

March 18, 2003

Presented by  
North Dakota Office of State Tax Commissioner

**Administrative Costs Associated with  
Cigarette Stamping for 2003-2005**

<b>Stamp Engraving Plates</b>		
Plates for packages of 20, 25, Tribal, & Military		\$ 6,000
<b>Stamps:</b>		
116 million stamps or 3,900 rolls (30,000 stamps/roll)		
3,900 rolls @ \$16.50		\$ 64,350
<b>Mail or Shipping Costs (Option – regular or registered mail):</b>		
US Postal Service – regular mail/Insured		\$ 21,000
<b>Compliance/Enforcement:</b>		
Travel Expense (Tax Department Compliance/Audit Staff)		\$ 15,000
<b>Computer/Programming Costs</b>		
Equipment/Programming		\$ 25,000
<b>Staff costs (absorbed by Tax Dept budget)</b>		
Order receipt/processing		
Sorting, opening, assembly	\$1,014	
Validation/cashiering	290	
Order preparation and mailing	\$7,800	
Compliance/Enforcement Staff Time	**	
Total Costs		\$ 9,004
Total Administrative Costs		\$140,354
Less Staff costs		<u>( 9,004)</u>
Net Administrative Costs		\$131,350

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La Costa Richard  
Operator's Signature

10/6/03  
Date

Information distributed to  
Senators by Sen. Sykeson.



**STATE CIGARETTE TAX RATES & RANK, DATE OF LAST INCREASE, ANNUAL PACK SALES & REVENUES, AND RELATED DATA**

Although 19 states (and Puerto Rico) have implemented higher cigarette tax rates in 2002, 27 states have not increased their cigarette tax for at least five years. Of these, seven have not increased their cigarette taxes since the 1980s, and four have not made any increase since the 1970s. Virginia has not increased its cigarette tax since 1960. As time passes, inflation erodes the real value of state tobacco tax rates and revenues – and state cigarette taxes now typically account for much smaller portions of the total retail price of a pack of cigarettes than when they were first enacted.

State cigarette tax increases can restore state tobacco tax revenues to historical levels.

State	Cigarette Tax (cents/pack)	National Rank (1 = high)	Date of Last State Tax Increase	FY 2001 Cigarette Pack Sales (millions)	FY 2001 Cigarette Tax Revenue (millions)	Retail Price Per Pack With All Taxes	Adult Smoking Rate	Adult Smoking Rank (1=low)
All States	58.8 avg.	///	///	20.73 billion	\$8.2 bill.	\$3.85 avg.	22.8 avg.	///
Alabama	16.5	45th	7/1/1984	402.3	\$62.50	\$3.48	25.20%	42
Alaska	100	9th	10/1/1997	40.9	\$40.90	\$4.55	25.00%	40
Arizona	58	22nd	11/29/1994	277.4	\$157.60	\$3.91	18.60%	3
Arkansas	34	32nd	7/1/2001	271.8	\$82.50	\$3.60	25.10%	41
California	87	15th	1/1/1999	1,287.60	\$1,110.70	\$4.38	17.20%	2
Colorado	20	39th	7/1/1986	302.9	\$58.10	\$3.18	20.00%	8
Connecticut	111	8th	4/3/2002	234	\$115.10	\$4.53	19.90%	7
Delaware	24	36th	1/1/1991	110.8	\$26.40	\$3.29	22.90%	24
Washington, DC	65	20th	7/1/1993	25.1	\$16.30	\$4.05	20.90%	13
Florida	33.9	33rd	7/1/1990	1,255.80	\$419.70	\$3.65	23.20%	25
Georgia	12	46th	4/1/1971	703.6	\$81.80	\$3.31	23.50%	30
Hawaii	120	7th	7/1/2002	51.8	\$51.80	\$4.65	19.70%	5
Idaho	28	35th	7/1/1994	86.3	\$23.30	\$3.33	22.30%	22
Illinois	98	13th	7/1/2002	833.9	\$470.20	\$4.26	22.30%	22
Indiana	55.5	23rd	7/1/1987	737.9	\$110.00	\$3.72	26.90%	48
Iowa	36	29th	6/1/1991	253	\$89.40	\$3.48	23.20%	25
Kansas	70	17th	6/1/2002	209.9	\$48.80	\$3.76	21.10%	15
Kentucky	3	50th	7/1/1970	616.8	\$16.80	\$3.23	30.50%	51
Louisiana	36	29th	7/1/2002	371.5	\$78.60	\$3.50	24.10%	35
Maine	100	9th	10/1/2001	103.6	\$74.40	\$4.25	23.80%	33

State Cigarette Tax Rates & Rank, Date of Last Increase And Related Data

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Operator's Signature: *Richard* 10/16/03  
Date

State Cigarette Tax Rates & Rank, Date of Last Increase And Related Data

State	Cigarette Tax (cents/pack)	National Rank (1 = high)	Date of Last State Tax Increase	FY 2001 Cigarette Pack Sales (millions)	FY 2001 Cigarette Tax Revenue (millions)	Retail Price Per Pack With All Taxes	Adult Smoking Rate	Adult Smoking Rank (1=low)
<b>Maryland</b>	100	9th	6/1/2002	307.8	\$197.70	\$4.36	20.50%	10
<b>Massachusetts</b>	151	1st	10/1/2002	347.8	\$263.90	\$4.32	20.00%	8
<b>Michigan</b>	125	6th	8/1/2002	787	\$583.00	\$4.68	24.10%	35
Minnesota	48	26th	7/1/1992	365	\$172.50	\$3.83	19.80%	6
Mississippi	18	41st	6/1/1985	267	\$45.00	\$3.43	23.50%	30
Missouri	17	43rd	10/1/1993	603	\$99.40	\$3.29	27.20%	49
Montana	18	41st	8/15/1993	67.5	\$11.80	\$3.21	18.80%	4
<b>Nebraska</b>	64	21st	10/1/2002	119.4	\$39.20	\$3.88	21.20%	16
Nevada	35	31st	7/1/1989	180.9	\$61.20	\$3.56	29.00%	50
New Hampshire	52	25th	7/1/1999	168.2	\$87.50	\$3.65	25.30%	43
<b>New Jersey</b>	150	2nd	7/1/2002	485.8	\$386.00	\$4.90	21.00%	14
New Mexico	21	38th	7/1/1993	97.7	\$20.00	\$3.49	23.60%	32
<b>New York</b>	150	2nd	4/3/2002	910.7	\$1,002.40	\$5.80	21.60%	19
North Carolina	5	49th	8/1/1991	806.1	\$38.80	\$3.15	26.10%	45
North Dakota	44	27th	7/1/1993	45	\$19.80	\$3.68	23.20%	25
<b>Ohio</b>	55	24th	7/1/2002	1,135.80	\$262.80	\$3.96	26.20%	47
Okahoma	23	37th	6/1/1987	373	\$61.10	\$3.40	23.30%	28
Oregon	68	19th	2/1/1997	234.6	\$157.90	\$3.74	20.80%	12
<b>Pennsylvania</b>	100	9th	7/15/2002	1,065.40	\$320.90	\$4.25	24.30%	38
<b>Rhode Island</b>	132	5th	7/1/2002	83.3	\$58.40	\$4.61	23.40%	29
South Carolina	7	48th	7/1/1977	387.6	\$24.90	\$3.30	24.90%	39
South Dakota	33	34th	7/1/1995	58.9	\$18.60	\$3.53	21.90%	20
<b>Tennessee</b>	20	39th	7/1/2002	588.9	\$74.20	\$3.38	25.70%	44
Texas	41	28th	7/1/1990	1,294.70	\$480.80	\$3.60	21.90%	20
<b>Utah</b>	69.5	18th	5/6/2002	86.3	\$42.70	\$3.83	12.90%	1
<b>Vermont</b>	93	14th	7/1/2002	57.4	\$24.60	\$4.37	21.50%	18
Virginia	2.5	51st	8/1/1960	666.3	\$15.10	\$3.20	21.40%	17
<b>Washington</b>	142.5	4th	1/1/2002	295.8	\$236.70	\$4.98	20.70%	11
West Virginia	17	43rd	8/1/1978	197.9	\$32.10	\$3.25	26.10%	45
Wisconsin	77	16th	10/1/2001	419.4	\$243.50	\$4.16	24.10%	35
Wyoming	12	46th	7/1/1989	45.9	\$5.50	\$3.35	23.80%	33
USA/U.S. Gov't	39 (fed. tax)	///	1/1/2002	21+ billion	\$7.1 bill.	\$3.85	23.30%	///

States in bold have increased tax in 2002.

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Operator's Signature

*Richard*

10/10/03  
Date

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## Tax Stamps: Cigarettes

This Act is based on Idaho Senate Bill 21, which became law in 2002. This Act prohibits stamping or paying taxes on cigarettes or roll-your-own tobacco products that are produced by manufacturers that are not participating in the Master Settlement Agreement.

On November 23, 1998 46 states, the District of Columbia and 6 territories reached the Master Settlement Agreement with the four Original Participating Manufacturers (OPMs). The OPMs represent the biggest tobacco companies in the industry. All together Philip Morris, RJ Reynolds, Brown & Williamson, and Lorillard constituted 99% of the cigarette market in 1997. Since 1998, 31 Subsequent Participating Manufacturers (SPMs), which are now subject to all of the terms of the agreement, have signed the MSA as well. The total estimated payout for the states was approximately \$206 billion spread over the next 25 years.

In addition to OPMs and SPMs, there are those tobacco manufacturers that have not signed the MSA. These companies are known as non-participating manufacturers or NPMs. In order to hold these companies accountable, all 46 MSA states passed legislation (Exhibit T of the MSA) that forces NPMs to place money in privately established escrow accounts in each state. These accounts ensure that money is available in the event that a state sues an NPM. If states do not win a lawsuit against the NPM, those monies put into the escrow will be released back to the originating company after the 25-year payout plan has expired.

Each of the participating states and territories has been allocated a percentage of the MSA agreement based on the state's population and the number of cigarette sold in their state. Each year, the payment is subject to a volume adjustment based on the number of cigarettes sold compared to the number of cigarettes sold in 1997.

In addition to the volume adjustment, the payment amount is also subject to an inflation adjustment using the consumer price index and an NPM adjustment. The NPM adjustment is calculated by multiplying the market share loss for the OPM from the previous year by 3 in those states that do not have the model statute in place to hold NPMs accountable or are not enforcing it. In other words a 2 percent loss of market share by the OPMs would result in a 6 percent reduction in the allocated payment to the settling states. Based on the MSA, a reduction in the total percentage of tobacco sales or a reduction in the market share held by the OPMs could reduce the amount given to the states.

Before the MSA was signed, OPMs manufactured an average 700 billion cigarettes a year, with a peak in 1996 of 754 billion. In addition, the overall consumption of cigarettes declined by 50 billion from 1997 to 2000. Since the MSA was signed, OPMs have begun to lose their dominance over the market. Their market share reduction, which can be attributed to many factors, has been just under 4% over the last three years.

The decline of the OPMs control in the tobacco market has enabled NPMs to garner greater control of the market share. OPMs have been forced to raise the price of their cigarettes to accommodate for the payments to the states, while NPMs that do not pay into escrow accounts have not. Therefore, NPMs have gained those consumers whose preferences are driven by finances.

Currently, states are actually receiving less money than previously forecasted. Reductions to the MSA payments are attributed to a reduction in cigarette sales by OPMs and SPMs, which was a desired result of the MSA, and an NPM adjustment based on the failure to enforce the model NPM statute provided in Exhibit T of the MSA. The MSA payments received by the states as of April 2001 were 10.7 percent below the originally estimated payments. Twelve percent of this reduction (approximately \$200 million according to the Kentucky Legislative Research Council), or just over 1 percent of the total estimated payment is due to the NPM adjustment, while the rest can be attributed to the decline in volume shipped by the OPMs. Thus, the majority of the reduction in settlement payments is a direct reciprocation of the decline in smokers in the United States, as well as a drop in the volume of cigarettes sold. If the trend continues states will not receive all of the money once thought to be guaranteed based on the MSA.

If current trends continue, the states could suffer \$14 billion in lost revenue over the next 9 years.

### The Council of State Governments

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Operator's Signature

*10/16/03*  
Date

According to a United States General Accounting Office report, states have received \$1.6 billion less than originally projected under the Master Settlement Agreement (MSA). Based on MSA projections states are expecting to receive nearly \$70 billion from the tobacco industry through 2010, but latest estimates show a 20% reduction in these payments. The decrease is attributed to continuing decline in the consumption of cigarettes at a rate of 1.5% each year, and NPMs garnering a .8% greater share of the market each year. By gaining market share at their current pace the NPMs could cost the states \$2.4 billion dollars. In an effort to stop NPMs from gaining market share, some states are proposing legislation that would levy an additional tax on the cigarettes sold by NPMs, e.g., South Dakota Senate Bill 21, 2002.

Submitted as:  
South Dakota  
SB 21 (enrolled version)  
Status: enacted into law in 2002.

### Suggested State Legislation

(Title, enacting clause, etc.)

1 Section 1. [*Short Title.*] This Act may be cited as "An Act to Prohibit Tax Stamping or Payment of  
2 Taxes on Cigarettes or Roll-Your-Own Tobacco Products Produced by Certain Nonparticipating  
3 Manufacturers and to Provide for the Creation of a Directory for Compliant Nonparticipating  
4 Manufacturers."  
5

6 Section 2. [*Conditions for Affixing a Cigarette Tax Stamp.*] No distributor or wholesaler may,  
7 directly or indirectly, affix the [state] cigarette tax stamp or imprint to a package of cigarettes, or pay the  
8 [state] cigarette tax on roll-your-own tobacco product, manufactured or sold by a tobacco product  
9 manufacturer unless:

10 (1) The manufacturer is a participating manufacturer as that term is defined in [insert  
11 citation]; or

12 (2) The manufacturer is a nonparticipating manufacturer in compliance with [insert  
13 citation].  
14

15 Section 3. [*Directory of Complying Manufacturers.*] The [secretary of revenue] shall annually, no  
16 later than [insert date], transmit to all licensed distributors and wholesalers, and post on the [department of  
17 revenue's] website, a directory of nonparticipating tobacco product manufacturers determined by the  
18 [secretary] to be in compliance with [insert citation]. The [secretary of revenue] shall amend the directory  
19 on the [department of revenue's] website, as necessary, to include any nonparticipating tobacco product  
20 manufacturer determined to be in compliance with [insert citation] after [insert date], or to remove any  
21 nonparticipating tobacco product manufacturer subsequently determined not to be in compliance with  
22 [insert citation]. The [secretary of revenue] may require distributors, wholesalers, and nonparticipating  
23 tobacco product manufacturers to submit such information as the [secretary] may determine is necessary to  
24 enable the [secretary] to determine whether a nonparticipating tobacco product manufacturer is in  
25 compliance with [insert citation].  
26

27 Section 4. [*Exclusions and Removals from Directory.*] Any nonparticipating tobacco product  
28 manufacturer excluded or removed from the directory may request a contested case hearing before the  
29 [secretary]. A request for hearing shall be made within [sixty (60)] days of the exclusion or removal or the  
30 date the manufacturer determined it was in full compliance with this Act and [insert citation], and shall  
31 contain the evidence supporting the manufacturer's compliance with [insert citation]. At the hearing, the  
32 [secretary] shall determine whether the nonparticipating tobacco product manufacturer is in compliance  
33 with [insert citation], and whether the manufacturer should be listed in the directory.

Suggested State Legislation, 2003 - Part II

Richard Costa  
Operator's Signature

10/16/03  
Date

34  
 35 Section 5. *[Violations.]* Any stamped cigarettes or roll-your-own tobacco on which taxes have  
 36 been paid in violation of this Act are contraband goods and may be legally seized, without a warrant, by  
 37 the [secretary of revenue], [department] agents or employees, or by any law enforcement officer of this  
 38 state if directed by the [secretary] to do so. Any tobacco products seized and forfeited under this Section  
 39 shall be destroyed. The [department of revenue] may allow a credit for tax paid on contraband cigarettes  
 40 and roll-your-own product returned to the manufacturer or distributor from which they were purchased. An  
 41 Act to prohibit tax stamping or payment of taxes on cigarettes or roll-your-own tobacco products produced  
 42 by certain nonparticipating manufacturers and to provide for the creation of a directory for compliant  
 43 nonparticipating manufacturers.  
 44

45 Section 6. *[Severability.]* [Insert severability clause.]  
 46

47 Section 7. *[Repealer.]* [Insert repealer clause.]  
 48

49 Section 8. *[Effective Date.]* [Insert effective date.]

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## STATE OPTIONS TO PREVENT AND REDUCE CIGARETTE SMUGGLING AND BLOCK OTHER ILLEGAL EFFORTS TO AVOID PAYING STATE CIGARETTE TAXES\*

Although the cigarette companies regularly overstate the amount of smuggling and tax-avoidance prompted by the large differences among different states' cigarette tax rates, many U.S. states may be annually losing millions of dollars of revenue because of both illegal cigarette smuggling by organized criminal syndicates and more informal tax-avoidance efforts by individual smokers, such as cross-border purchases in lower-tax states or internet purchases of cigarettes on which no state taxes are paid. Fortunately, there are a number of relatively simple and inexpensive measures that could minimize these state government revenue losses.

### The Nuts & Bolts of U.S. Interstate and International Cigarette Smuggling

U.S. interstate cigarette smuggling typically occurs when smugglers purchase cigarettes on which a low state cigarette tax has been applied and then illegally smuggle them into a higher-tax state for illegal resale to otherwise-legal retailers. The retailers purchase the cigarettes from the smugglers at prices that reflect the avoided state cigarette taxes, and they then sell the cigarettes to unknowing consumers. Because the retailers collect and keep all state-tax payments from the final customers – with no cigarette tax payments ever being made to the high-tax state on the sales – they (and the smugglers), and not the smokers, enjoy most of the tax-avoidance "savings." According to various studies, this kind of cigarette smuggling accounts for the majority of all state revenue losses.

In some cases, the cigarettes smuggled from the low-tax state are sold directly to final customers via black-market sales, but these black-market sales are quite small compared to the sales through otherwise legal retailers. Some smokers also avoid paying the cigarette tax in their state by going to a neighboring, lower-tax state to purchase their cigarettes, perhaps buying packs for family members and friends, as well. Another tax-avoidance strategy is to buy cigarettes over the internet, where in virtually all cases no state cigarette or sales taxes are applied. While federal law (the "Jenkins Act") requires internet sellers to report all sales into a particular state to that state's tax-collection authority (so the tax-collection authority can collect the taxes owed from the in-state buyers), very few internet sellers comply with that law -- and federal or state enforcement has been almost nonexistent.

### Measures to Make Smuggling More Difficult

**Improve state cigarette tax stamps.** Make them larger, easily distinguishable from other states' tax stamps, harder to counterfeit, highly visible, and, if technically possible, placed on two sides of the pack and under the cellophane wrapper on cigarette packs. States could also take advantage of the fast-growing technology re hard-to-counterfeit, easy-to-check-for-validity cigarette stamps, which can also provide information on each pack re what retailer or wholesaler originally purchased it from which distributor or manufacturer.

\* These ideas can be expanded or modified to reduce the smuggling of other tobacco products, besides cigarettes, and to block other illegal efforts to avoid paying state taxes on the other tobacco products.

**Require better record keeping by wholesalers.** Require wholesalers selling to retailers that sell cigarettes in the state to keep and maintain records of amounts sold, to whom, etc., and to regularly provide this information to state officials.

**Require better record keeping by retailers.** Require all retailers that sell cigarettes in the state to keep and retain accurate records regarding: a) their receipt of cigarettes for resale to final customers or others in the state (including date, quantity, from whom received, etc.); b) their total cigarette sales in the state (with monthly totals); and c) their sale of any tobacco products in quantities exceeding 2,000 cigarettes, or 10 cartons (including date, quantity, description, to whom sold, etc.).

**Block retail sales clearly not for personal use.** Prohibit all retail sales in the state or to state residents (e.g., by internet sellers) of cigarettes in amounts greater than 2,000 cigarettes (10 cartons) – with parallel limits for the sales of other tobacco products.

**Publicize toll-free phone numbers to encourage reports of smuggling or tax-avoidance activities.** Require state-based wholesalers, distributors, importers, exporters, and retailers of cigarettes and other tobacco products to post prominent signs that provide a toll-free number for reporting anyone suspected of smuggling cigarettes or buying or selling smuggled cigarettes. These or other signs could also provide information on how to identify legal versus smuggled cigarettes, notify smokers and others of the existing laws and penalties re buying smuggled cigarettes, bringing cigarettes into the state from other jurisdictions, etc., and inform employees of existing whistleblower protections. The toll-free number could also be included on the state tax stamps placed on cigarette packs sold in the state.

**Protect "Whistleblowers."** To encourage the reporting of smuggling activities and protect witnesses, protect the employees of retailers, distributors, wholesalers, importers, exporters, manufacturers, etc. who notify authorities or testify in court regarding their employers' smuggling-related wrongdoing from being fired or penalized by their employers.

**Work with Neighboring States.** To increase each state's cigarette tax revenues, groups of neighboring states can work together both to make their cigarette tax rates equal or similar to each other's (by the lower-tax states raising their rates) and to coordinate and expand their efforts to minimize cigarette smuggling and other tax avoidance.

**Support Federal Anti-Smuggling Legislation.** While each state can do a lot to minimize cigarette tax avoidance, the federal government can do more, especially to make it more difficult for low-tax states to serve as national suppliers of smuggled cigarettes. Most notably, the federal government could require all states to put tax stamps on their cigarettes, thereby stopping the sale in some low-tax states of blank packs that can easily be used for smuggling. The federal government can also create nationwide standards for tax stamps; cigarette labeling (e.g., requiring unique serial numbers or markings indicating where packs may be legally sold); record keeping by manufacturers, wholesalers, and retailers; maximum sales amounts; and the like. Federal legislation could also make tax-avoidance via internet sales much more difficult.

#### **Stronger Disincentives and Punishments for Smuggling**

**Expand definition of illegal smuggling subject to state prosecution and penalties.** To reach more illegal smuggling and tax avoidance through state law enforcement, reduce the

minimum number of cartons/packs/cigarettes that trigger smuggling violations or major smuggling penalties.

**Increase existing fines for cigarette smuggling.** Increase the minimum dollar amounts of existing fines and have no maximum amount so that meaningful fines can be levied against large economic entities involved in smuggling.

**Seize vehicles and properties used in cigarette smuggling.** Established new provisions to allow for the state's seizure of vehicles used in cigarette smuggling, putting liens on property for the value of smuggled goods, etc. (as with state laws pertaining to illegal drug trafficking).

**Withdraw right to sell tobacco products from retailers involved in smuggling.** State anti-smuggling laws could ensure that retail outlets in the state that buy smuggled cigarettes or knowingly sell smuggled cigarettes will lose their right to sell any cigarettes in the state for some period of time (e.g., from one to ten years depending on the severity of the violation).

**Include jail or even prison time for guilty large-scale smugglers.** Going beyond just fines and other economic disincentives, state laws could call for jail or prison sentences for persons participating in large smuggling efforts or who are guilty of repeatedly violating the states anti-smuggling or tax-avoidance laws.

**Implement periodic "stings" to catch state smokers making cross-border cigarette purchases.** While trying to stop state residents from going to neighboring lower-tax states to purchase their cigarettes would be a complicated and costly enterprise, making periodic highly publicized "stings" to catch some of these cross-border shoppers, seize their cigarettes, and issue fines could dampen many smokers' enthusiasm for this tax avoidance strategy. A similar strategy might work for dampening internet cigarette purchases.

#### **Special Measures to Stop Illegal Tax-Free Internet & Mail Order Sales of Cigarettes**

**Subject internet and other mail-order cigarette sellers to same anti-smuggling measures applied to in-state face-to-face sellers.** Make sure all anti-smuggling provisions that apply to in-state retail sellers of cigarettes also apply to internet or mail-order companies that sell cigarettes to persons in the state, including record-keeping requirements, applicable penalties, etc. When the anti-smuggling measures applied to in-state sellers cannot be directly applied to internet sellers, develop parallel versions. For example, rather than try to require internet sellers to post "signs" on their websites with a state toll-free whistle-blowers phone number and other information, state law could require that internet sellers include that information in all mailings or emails to customers or potential customers in the state.

**Make sure there are state laws that parallel and supplement the federal Jenkins Act.** The Jenkins Act law requires all internet cigarette sellers to provide each state with periodic reports listing residents of that state who have purchased cigarettes from the internet sellers (including the quantities sold to each and the residents' mailing addresses). Rather than rely just on this federal law, each state could establish its own laws requiring internet (and mail-order) retailers that sell cigarettes to state residents to provide the Jenkins Act information to the state and abide by other state requirements, with strong penalties for noncompliance.

**Directly contact internet cigarette sellers to notify them of applicable state and federal laws re their cigarette sales to state residents.** Although many internet sellers do not

regularly make the required Jenkins Act reports to all states, some states have substantially increased the Internet sellers' compliance rate simply by contacting them and demanding the reports. Currently, the number of active Internet sellers operating in the United States is still relatively small, making it possible for states to have a major impact by focusing their notification efforts on just the top 50 or so (and states could easily share these lists once developed).

**Establish systems for regularly notifying Internet buyers of cigarettes of the amount of state cigarette and sales taxes they owe.** Once more Internet sellers begin reporting the names of their customers from the state, the state can easily set up a system for mailing notices of taxes owed to these customers. Some states have already received substantial compliance (and additional revenue) simply by sending out such notices without further enforcement efforts.

**Enforce state laws pertaining to internet sellers and internet customers.** To the extent that notifying Internet sellers and internet customers of their legal obligations to the states does not prompt adequate compliance, states can follow up with additional notifications and other enforcement action. Beyond standard enforcement efforts, a state could try to get a court to order that: a) cigarette wholesalers not sell any cigarettes to internet sellers that have failed to comply with state and federal reporting requirements or other applicable state laws; and b) credit card companies withhold credit-card vending rights from non-complying Internet vendors.

**Require ID checks and record keeping by common carriers delivering cigarettes to state retail customers.** To make internet cigarette purchases less easy and convenient for state smokers trying to avoid taxes (and also make it hard for kids to purchase cigarettes via the internet), states can require common carriers delivering cigarettes into the state to get a signature from the person receiving the cigarettes and check a photo ID of the person to ensure both that they are over 18 and that they are the actual purchaser/recipient. Rhode Island already has such a law. To improve related tax collection efforts, states could also require that the common carriers delivering the cigarettes to retail customers provide the state with the names, addresses, and quantity received of all persons receiving such cigarette deliveries in the state -- with parallel laws that require any shippers of cigarettes into the state to end-user customers to provide that same information to the carriers.

**Require ID checks by Internet and other mail-order tobacco sellers.** Require that Internet sellers must verify the identify, age, and address of each customer against a government-issued ID database before making any internet or mail-order sales and before allowing any customer access to the seller's tobacco-selling website -- and require the sellers report this information to the state (along with information on the sales to each customer) for tax collection purposes.

**Require that those selling cigarettes into the state by mail or other delivery must be licensed by the state as a tobacco-product distributor that pays or collects applicable state cigarette taxes (e.g., is licensed to affix state tax stamps) on each pack sold into the state.** Besides regular enforcement efforts against non-complying sellers, the state could provide carriers with a list of all such licensed sellers and prohibit carriers from delivering cigarettes to persons in the state from any cigarette seller not on the list.

3 24 03

John Olson

From: Spangler, Toby J. [Toby.Spangler@Altria.com]  
Sent: Friday, March 21, 2003 3:33 PM  
Subject: 'jolson@olsonclchy.com'  
Helpful article

Cigarette tax revenue soars: Jump linked to stamp on packs to fight smuggling (The Detroit News) February 11, 1999

LANSING -- State tax receipts from cigarette sales jumped sharply in the five months since the state mandated each pack to carry a "Michigan" stamp designed to combat smuggling from low-tax states.

The additional \$46 million in revenue amounted to a 20-percent boost over the previous year. Cigarette money pays to educate Michigan's school students and to support health care and other state programs.

State officials are surprised by how much new money is flowing into state coffers. Last year, the tobacco tax generated about \$566 million.

When Gov. John Engler first called for the cigarette stamp two years ago, he estimated that smuggling was a \$17-million annual problem. State officials later upped the estimate to \$28 million. On Wednesday, armed with the latest tax receipt reports, they said the figure is even higher.

"Now based on what we're seeing on the reports and the money coming in, we think it was \$60 million and could be more," said Lyle Mather, administrator of the Motor Fuel and Tobacco Tax Division in the Treasury Department.

Smuggling became a problem in May 1994 when the cigarette tax was tripled from a quarter to 75-cents a pack as part of the Proposal A school refinance plan.

Before the stamp was required, it was difficult to determine, on its face, whether a pack or carton had paid Michigan taxes.

Michigan's 75-cent tax is the nation's seventh highest -- more than double the national average. That invited smugglers to buy cigarettes in states with lower taxes, turn around and sell them here.

The cigarette tax is 3 cents in Kentucky; a nickel in North Carolina; and 7 cents in South Carolina.

Michigan noticed a \$39-million drop-off in receipts between 1995 and 1996. They fell by another \$34 million in 1997.

That didn't jibe with smoking statistics that showed only a gradual decline in adult smoking during that time.

Today, 1.8 million Michigan adults -- a quarter of the population -- smoke. The state has the seventh-highest percentage of adults who smoke.

Confronted with an alarming increase in smuggled cigarettes, the Michigan State Police formed a Tobacco Tax Team. It has confiscated more than \$4 million in smuggled smokes.

Just last month, a Farmington Hills wholesaler agreed to pay the state \$1 million in unpaid taxes on 240,000 cartons of cigarettes he purchased in

*Tal Costa Richardson*  
Operator's Signature

10/16/03  
Date

FR

Kentucky for sale here between 1995 and 1997. The wholesaler still faces a possible 27-month prison sentence.

"It could be one individual who goes to four or five smoke shops and takes orders, drives out of state, buys the cigarettes and comes back to deliver," said Det. Lt. Lewis Langham of the tax team.

But smugglers were still getting through the state net. So the tobacco stamp was launched last September.

"The new tax stamp has been effective in reducing the smuggling of cigarettes into Michigan," said state Atty. Gen. Jennifer Granholm.

But she said criminals are still trying, with mixed success, to outsmart regulators.

The latest problem is counterfeit tobacco stamps.

"It's more sophisticated, not the mom and pop store owners going to other states and bringing back cigarettes," added Granholm, who could bring charges against a major counterfeiter next week.

Toby Spangler  
Director Government Affairs  
Altria Corporate Services  
Region 6  
Work (608) 285-4674  
Cell (608) 345-6035

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Date



3.25.03  
P.O. Box 1472  
Bismarck, ND 58502-1472  
701-258-3618

March 20, 2003

Senator Urlacher Chairman and members of the Senate Finance and Taxation Committee:

During the opposition testimony on HB 1431 I heard some testimony that is not accurate and I would like to make sure the committee has the facts.

During my testimony I was asked how much of a price impact the minimum pricing would have on the retail price of cigarettes, and I estimate 3 - 5 %. Mr. Charles Sulak testified 10% or more than \$4.00 per carton. Since the hearing I have done some research. AMCON Distributing Company's processes an end of day report every morning that lists all items sold, the value of those items, and % profit. The report shows those figures in a daily category and a monthly category. AMCON has totaled a month to date margin of 3.85% on cigarettes sold through our distribution center through this morning. The minimum pricing sets wholesale at 5%. This would increase cigarette prices by 1.15% at the wholesale level. That increase in price would offset the stamping costs incurred by the wholesalers. The retail price survey I did with our 50 customers that we have set the retailers to print on their invoices show a range of 8 to 15% of the wholesale cost. HB 1431 has minimum retail price of 8% and that would not change on the retail side based on my survey. Based on my research I estimated the increase higher than what would actually been. My actual estimate should have been between 1 and 2% or under a nickel a pack.

Mr. Charles Sulak of McClanes Company (a Wal Mart Subsidiary) testified that their tobacco market share was less than 5%. I talked with John Quinlan of the tax department and McClanes market share is much larger than 5%.

Finally, regardless of whose estimates we use HB 1431 will generate additional sales tax revenue. I estimated a nickel a pack increase times 70 million packs (fiscal year ND 2001 figures) would generate \$10,500 or \$1.4 million if we used McClane's number of a \$4.00 increase.

Thank you for the time

John

## Cigarette minimum price repeal attempt canceled

**David Phelps**

Star Tribune  
Published 03/20/2003

The Minnesota Commerce Department sought to repeal a state law that sets a minimum price for cigarettes but reversed itself late Wednesday when it became evident that the change would open the way for cut-rate pricing and make cigarettes more affordable for smokers, including price-conscious teens.

The department wanted to eliminate its small enforcement staff for the 40-year-old Unfair Cigarette Sales Act, although there would have been little, if any, budget savings because the staff is financed by fees paid by tobacco wholesalers and those fees would be eliminated with repeal of the law.

Public health advocates, who argue for higher prices for cigarettes as a smoking deterrent, were puzzled by the department's proposal and caught off guard.

"We did not know that this was happening," said Matt Flory of the American Cancer Society. "The intent of this law is to make sure there is not unfair competition. But one of the effects is it drives prices up."

The attempt to repeal the law was described as a budget-reducing decision, said Commerce Department spokesman Bruce Gordon.

"It's just a proposal in a bill, and it's coming out," Gordon said late Wednesday after the agency fielded questions about its plan to repeal.

Few with interest in the issue were aware of the repeal's inclusion in a large Commerce Department budget bill until this week. The bill is scheduled to be heard today in the House Commerce, Jobs and Economic Development Policy Committee, where the act will be reinstated.

Gordon said the department changed its plans after hearing from "members of the retail industry" who want the status quo and could challenge predatory pricing only through litigation if it were repealed.

Thomas Briant, executive director of the Minnesota Wholesale Marketers Association, estimated that cigarette prices would decline by \$3 to \$4 per carton, or 30 to 40 cents per pack, if the law were repealed. He based his estimate on sales in North Dakota, where there is no unfair-sales law.

"We are not talking about selling turkeys below cost at Thanksgiving," Briant said Wednesday. "We would be facing the prospect of allowing cigarettes to be sold at or below cost every day of the year in potentially over 10,000 retail stores statewide."

Marketers Association President Curt Dass, a wholesaler from Tyler, Minn., said repeal of the law would put him and a lot of smaller convenience stores out of business.

Mass merchandisers and chains would drop the price, he said, and "the mom-and-pop and independent stores" wouldn't be able to compete.

*Lo Costa Richardson*  
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3.25.03

Unfair-cigarette-sales laws exist in 24 other states.

Jeremy Hanson of the Minnesota Smoke-Free Coalition said his organization has not taken a position on the Unfair Cigarette Sales Act, although he added, "We generally support any legislation that increases the cost of cigarettes."

#### Prices and smoking

It is well known in public health circles that higher-priced cigarettes are one of the major factors leading people to quit smoking or discouraging teens from starting.

Several antismoking organizations this year have asked for a \$1 increase in the state cigarette excise tax as a smoking prevention measure. The current tax in Minnesota is 48 cents a pack. But the Pawlenty administration's no-tax-increase pledge gives that proposal little chance.

More than 60 wholesalers in the state pay up to \$2,500 a year to the state's general fund for enforcement of the Unfair Cigarette Sales Act, for a total of about \$110,000 a year. The Commerce Department's enforcement budget is \$92,000 a year.

A complicated formula is used to determine the lowest price that can be charged for cigarettes. The formula includes the manufacturer's price, the state excise tax, the wholesale cost of doing business and the retail cost of doing business.

Last year the Commerce Department fined an Iowa wholesaler \$20,000 for selling cigarettes at less than cost by providing rebates to retailers.

An attempt to repeal the Minnesota Unfair Cigarette Sales Act in 1997 died quickly when public health groups and wholesalers expressed their opposition.

**David Phelps is at [dphelps@startribune.com](mailto:dphelps@startribune.com).**

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2% Purchase Discount

3-25-03  
Exhibit A.

Company	Market Share	Forecast Packages	Tax Rate	2% unlimited	2% capped *25,000 1,250,000
FLEMING	21	8715000	3834600	76692	25000
Wholesale Supply	16	6640000	2921600	58432	25000
AMCON DIST	13	5395000	2373800	47476	25000
FRANK McKONE	9	3735000	1643400	32868	25000
Schwab Wholesale	6	2490000	1095600	21912	21912
NASH Finch - Fargo	5	2075000	913000	18260	18260
McLANE	5	2075000	913000	18260	18260
G.H.C. Merchandise	4	1660000	730440	14608	14608
FRANKE Bocken	3	1245000	547800	10956	10956
HENNYS	3	1245000	547800	10956	10956
NASH Finch - Minot	3	1245000	547800	10956	10956
FM Jobbing	3	1245000	547800	10956	10956
SUPER VALU - Fargo	2	830000	365200	7304	7304
SUPER VALU - Bis	2	830000	365200	7304	7304
	95%	39425000	17347000	*346940	*231472
Remaining Wholesalers	5%	2075000	913000	18260	18260
Totals		41500000	18260000	*365200	*249732
Premium Cost for 2% Disc.				*730400	*499444
Prepared by John Quinlan Office of State Tax Commissioner March 24, 2003					

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