

MICROFILM DIVIDER

OMB/RECORDS MANAGEMENT DIVISION

SFN 2053 (2/85) 5M



ROLL NUMBER

DESCRIPTION

1522

2005 HOUSE HUMAN SERVICES

HB 1522


2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1522

House Human Services Committee

☐ Conference Committee

Hearing Date January 26, 2005

| Tape Number | Side A | Side B | Meter # |
|---|--------|--------|-----------|
| Number One | x | | 3027-6055 |
| | | | |
| | | | |
| Committee Clerk Signature  | | | |

Minutes:

Chairman Price opened the hearing on HB 1522,

Rep. Carlson, District 41. There are two major parts to this bill, one deals with the sales to minors and Internet sales and the other deals with stamps (indicia) putting back on the packs of cigarettes. Last session, Rep. Porter decided to see if he could get cigarettes over the Internet, and they came from Russia. There is a large amount of cigarettes being sold over the Internet and in many cases there are not enough safeguards put into place as to who can buy them. They can be sold directly to minors and be delivered directly to their homes and no one ever checks up on that. The bill covers in the first part, the prohibition of sales to minors, requirements of when you mail/ship the product, copy of the valid government issued document with name, address and birth date. Scenario: Dropping off the product, resident didn't order it, etc.(Page 3), Then it deals with the stamping. In 1991, dropped the stamping. Two reasons for bringing it back is:

We have decided that cigarettes are taxed at 44 cents a pack, then it is our responsibility to collect that tax on all the cigarettes that are sold in the state. This bill says you cannot sell cigarettes without stamps indicia attached. Members of the industry will be testifying, as this will require more work for them, as they will have to open cartons of cigarettes and stamp each pack. The tax dept. becomes involved because they will have to issue these stamps. I do have an amendment, because when I sponsored this last session, it became a study, because it there was cost involved to do it. Some of distributors are already delivering to other states and they are required to stamp, so some are already set up to stamp, some aren't. I believe there are 15 distributors, 4 of them are not set up to stamp. Another question is the method of payment for the stamps. As, I understand this, you used to have to pay for the stamps up front. This amendment allows them to get the stamps from the tax dept. and then pay for those on a quarterly basis, so they can collect the tax to repay for the stamps. When I just showed them this, they have some comments on the process. We have several areas that we might not be able to collect the tax, one is the Internet and the other would be sales at the casinos, being resold at our retailers. I honestly cannot give you any figures on how much money this would bring in, because at this point, I don't think anyone could project that.

Rep. Porter: The cigarettes that I ordered last session, came by US Postal Service, they dropped them off at LC and they delivered them to my desk. How would we make the postal service accountable. I see that is being one of the biggest barriers we have.

Rep. Carlson: On page 2, there is an explanation. Some of the people that are here from the tobacco industry may have the answer for that.

Rep. Carlson: We found out that those Russian cigarettes were Marlboro's, not counterfeit, and mailed directly from St. Petersburg, Russia. and by passed customs because they were less than the customs fee requirements, plus it was an international sales. Is there anything that we can do in regards to customs..

Rep. Carlson: I am not sure, but I am sure if there is a way around this, they will find a way. We have a legal product, we are supposed to be able to expect a revenue stream from it and we should be able to collect the tax. 47 states stamp cigarettes, 1 other is in the process now, so would leave only one that doesn't. The logistics will have to be worked out but I ask that you give this a do pass.

Rep. Potter: How do we know how many cigarettes are sold in ND.

Rep. Carlson: The companies know how many are sold, but at 44 cents a pack, \$4.44 are every carton is saved by not buying in state, and doing it over the Internet. If retailers could buy cigarettes over the Internet, resell those cigarettes over their counter, without anyone knowing, the temptation would be there to do that. You hear stories about cigarettes being sold out of cars in parking lots.

John Walstad, Legislative Council.

I am here with a neutral position to answer some of the questions that have come up.

Rep. Kreidt: Who did draft this bill.

J. Walstad: I am not sure who drafted the bill.

Chairman Price: Rep. Carlson had an old bill dusted off and there would additions. Do you remember when the stamps were eliminated.

J. Walstad: In 1991, the intent of this amendment that distributors may acquire the stamps from the Tax Dept. on a quarterly period. Then pay for the indicia, at the end of the quarterly period, so they don't have the outlay before they actually sell the product.

Rep. Weisz: I am assuming that none of these provisions will apply to sales on the reservations.

J. Walstad: As you know, we can't reach across tribal boundaries.

Rep. Weisz: What happens if someone buys cigarettes on the reservation and then sells them off of the reservations, that would not have the stamp.

J. Walstad: There is no problem if you have un-stamped cigarettes that you purchased on the reservation and your off the reservation, but if you take un-stamped products off the reservation and try to sell them off the reservation, then you have a problem.

Rep Porter: Is that against the law now, to resell cigarettes off of the reservation but there is no way to track them.

J. Walstad: That is right, it is illegal now, but every pack of cigarettes look the same.

Chairman Price: Rep. Carlson referred to a study, has there ever been anything done on that?

J. Walstad: I don't know that we have had an interim study on that, but the tax dept. did do an extensive auditing to see if there were illegal sales going on, and found that there weren't very many illegal sales.

Mr. Jon Olson: Altria Corporate Services.

We have invited Christopher Beard, Phillip Morris USA. to give you some information about Internet sales and why it is so important that ND join the other states in this stamping effort.

Christopher Beard, Public Policy Manager, Phillip Morris USA.

See attached testimony.

Side B: Christopher Beard Testimony continued:

Chairman Price: Which other states don't stamp?

C. Beard: North and South Carolina.

Rep. Potter: How do we know that illegal cigarettes are in ND?

C. Beard: It is hard to track. California, New York and New Jersey did studies 5 years ago, they have seen increasing illegal sales the last few years and feel it will probably see it increase.

Rep. Potter: How do we know that stamping will "fix" the problem.

C. Beard: This bill will send message that it is illegal to purchase cigarettes over the Internet. The states of Michigan and Washington sent letters to consumers. Stamping might not solve the complete problem, but other parts addressed in this bill will help.

Rep. Sandvig: What about the reservation areas?

C. Beard: The message we are getting is that this is only the tip of the iceberg. We were also told that some funds derived from the sales of cigarettes in North and South Carolina were given to a terrorist organization.

Rep. Ugem: Would we have any success with the US postal service?

C. Beard: Trying to put on boundaries on international items that come into the US Postal Service.

Gary Anderson, Directive Specialist, ND State Tax Dept.

There were some questions concerning the Fiscal Note and I have passed around a break down for your information.

John Quinlan, Administrator ND Tobacco Products Tax Law Div, of the ND State Tax Dept. (SEE ATTACHED TESTIMONY)

Testimony Attached:

Rep. Kaldor: In regards to the amendment, do you think this will improve tribal relations?

J. Quinlan: In 1993, we signed a compact with the Standing Rock tribe, we do the tax work for them so we can collect the taxes.

Rep. Kaldor: I guess I thought that would be a lever to try and get the tribes to collect the tax.

Chairman Price: What about those that sell off the reservation? Would the numbers/stamps collect tax then?

J. Quinlan: They are allowed 1 carton tax free now and it is the sovereign nations responsibility.

Rep. Weisz: How do you know where the cigarettes come from?

J. Quinlan: Through the retail sales and sales tax.

Chairman Price: Because we are a low tax state, that is now as much of a problem, we are losing money from 2 areas, Internet/reservation sales.

J. Quinlan: We would agree if ND was looking at a tax increase, we would compliment that with a tax program, depending if it would be a significant increase, a penny or two, we don't believe that would be advisable, however if the increase would be, for instance, raising the tax to 70 cents per pack, without the stamping process, we feel that has been a proven vehicle for smuggling. The stamping program/increasing per pack tax should go hand in hand. States have taken it upon themselves to do this stamping to assist with the actions of the federal government to work to stop the Internet/reservation illegal sales. We want the committee to know that we are not opposed to stamping, but feel that the time is not here at this. We feel at some point, the stamping process will be necessary. Previously, there was a question concerning the US Postal

Service, if I could comment. The last annual meeting of the tax administrators, the US Postal Service gave a presentation regarding the Internet specifically. Currently, under Federal law, anything that is shipped first class mail, they have an obligation to deliver. It cannot be interfered with, That is the method, that most of the Internet sales companies have gone too. In the advent of legislation of face to face deliveries that the states of NY, MI, AL and a few others. Those Internet companies are circumventing that law by using the USPS. There is nothing at this point that the USPS can do, however there is federal legislation that is being considered as part of the PACT act, HB 1177 on the federal level, that does address some of these concerns, unfortunately, it is stalled in congress.

Gary Anderson: The FN is initially drafted without the amendments, we indicated there would be a \$14,000 addition to the general fund. The reason that occurs is right now the distributors receive up to \$100 discount, when they report each month. So this would be reflective of that reduction because it is repealed in HB 1522. The \$468,000 expenditure is based on the intent of HB 1522, creates an additional administration. We would envision our field activity due to stamping would increase and the field work involved, we are looking at two FTE's as well as the cost of the stamps. The stamps alone would cost out at \$160,000. There is additional \$100,000 dedicated to the Internet aspect. In regard to the amendments, in quickly looking at it, it seems there would be a significant revenue lose, what happens is that the last quarter of the bi-annium, the due date, the distributors would actually have 10 days into the next bi-annium to pay it. The last quarters revenue we would receive, would actually be reported in the following bi-annium. There would be approximately a 2 1/2 million to 4 million dollar lose of revenue that would be projected by that amendment.

Brad Borkhuis, Wholesale Supply Co. Inc.

See attached testimony.

Rep. Kaldor: The amendment probably solves that last comment.

B. Borkhuis: Yes, I presume it would. But anything that is stamped within that 72 hours, that product we have maintain that in a cash flow, we have to maintain a dual inventory, to keep up with that inventory, separate states, separate tax jurisdictions, now that inventory doesn't turn as fast, and manufacturers require, on a one day electronic funds transfer so we have already paid for that. We are incurring financing costs the second that hits our doors.

Rep. Kaldor: So even with that, you still have a financial burden. Does your company distribute to MT or SD.

B. Borkhuis: We go into SD and MN. We do hand stamp those. But if ND went to stamping, we would have to go to machines.

Chairman Price: I understand the issue of the machine, but the other is the 72 hours?

B. Borkhuis: That and the labor regarding the individual stamping.

Chairman Price: Do you have any cost breakdowns for your company?

B. Borkhuis: No, not at this time.

Chairman Price: I know this is not in the bill, but we have had discussions on what type of reimbursements there would be for companies of your size.

B. Borkhuis: Per the bill, it is just scary, other states have a way to absorb that cost, but it would hit our bottom line, we have no other way to absorb that.

Rep. Porter: In 1991, when the stamping program was dropped, how many employees did you lay off?

B. Borkuis: I don't have any information, we are a family company so we try to maintain our employees.

Chairman Price: Do you have any suggestions or recommendations for us.

B. Borkuis: Part of the concern, is that smuggling/contraband issue that came from the manufactures stand point. We would face that too, but unfortunately when they do that they will find a more blanketed issue. The counterfeiter now, has to stamp each pack by hand, with stamping, he would only have to get a stamp. If stamping should be done in the future, we would have to done so we could find a way to absorb the cost. It was very efficient, as far as our state. In regards to the reservations, there could be something done to verify their cigarettes. My feeling is that you need to tax all cigarettes. This way the tribes could receive some money back to assist with their social structure, if that agreement could be reached.

Chairman Price: What if we told you that you had to collect the tax at the time of the sale and the tribe had to go back to Tax Dept. to collect their money?

B. Borkuis: We currently do that, we pass it back on the 15th of the month.

Chairman Price: Do you charge all retailers on the reservations?

B. Borkuis: No, but if your scenario came to be, we would certainly be glad to do that.

Rep. Uglem: The 72 hours of receipt, what would be your solution to that?

B. Borkuis: Stamp upon sale.

Henry J. Kroll, Frank McKone Cigar, Fargo, ND. Testimony attached.

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House Human Services Committee

Bill/Resolution Number HB 1522

Hearing Date January 26, 2005

Chairman Price: What is your compensation from MN.

H. Kroll: 4% of the cost.

Close Hearing on HB 1522.

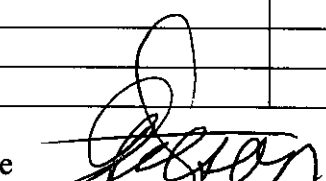
2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1522

House Human Services Committee

☐ Conference Committee

Hearing Date Feb. 1, 2005

| Tape Number | Side A | Side B | Meter # |
|--|--------|--------|-----------|
| 2 | | x | 3800-4337 |
| | | | |
| | | | |
| Committee Clerk Signature  | | | |

Minutes:

Chairman Price opened the discussion on HB 1522.

Rep. Porter: I know that this particular bill is from the tax stamp stand point, I do think that the portion about prohibiting tobacco sales to minors and the Internet sales portion is an important piece because we have more and more problems in that area. We have been dealing with this and there are other bills this session indirectly affecting this. I know that everyone laughed about the cigarette purchase I did last session, but I did it with a credit card, it was delivered up to LC, and it ended up on my desk and there was not at any point in time, did anyone ask for an ID. So if you give a kid a cash card, there will be no one that will check an ID there.

Chairman Price: What about reducing the one carton to zero for untaxed cigarettes?

Rep. Porter: I don't have a problem with that.

Page 2

House Human Services Committee

Bill/Resolution Number HB 1522

Hearing Date February 1, 2005

Chairman Price: The problem is with enforcement, no one is enforcing to the guy that is selling out of his trunk right now.

Rep. Weisz: I don't have a problem with eliminating that, but it has been pointed out to me that it may be unfair as we have exemption on liquor, on the reservation and in airports, etc.

Chairman Price: Anyone else with comments? If not, the hearing is adjourned.


2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1522

House Human Services Committee

☐ Conference Committee

Hearing Date Feb. 14, 2005

| Tape Number | Side A | Side B | Meter # |
|---|--------|--------|-----------|
| 2 | | x | 3800-4337 |
| | | | |
| | | | |
| Committee Clerk Signature  | | | |

Minutes:

Chairman Price opened discussion on HB 1522.

Sandy Tabor, Deputy Attorney General, State of North Dakota

In regards to HB 1522, our office has concerns about how you would enforce the proposed legislation, and as you remember, when the tobacco settlement was reached several years ago, one of the requirements was that the state would duly enforce all of the different laws concerning tobacco sales and tobacco usage. If this would have been law at that time, the dept. would not have funding for international investigating and prosecutions. We also feel there is a great potential for challenge, should this legislation be incited.

Chairman Price: I recieved an Email from the Attorney General so when Doug walked in the room, I thought we could bring it up now, instead of later. This is very much of a concern that we could lose funds under the master settlement if we enacted this section.

S. Tabor: This issue is really a potential for a challenge, when we are not enforcing a law that is on the books. We have reviewed this a couple of times internally and find it would be difficult to enforce.

Chairman Price: As I understand it, to enforce this, there would almost have to be someone able to go to places like Indonesia, to prosecute and funding for that would be exorbitant amount.

Rep. Porter: In the Internet component, where it covers the common carriers and making sure that they are carding people, is that OK?

S. Tabor: I don't believe that it was discussed specifically as a problem, however, it would probably be a practical problem.

Rep. Porter: We do it for alcohol, if someone is enrolled in a wine of the month club, the outside of the package indicates that ID is needed to receive the package.

Chairman Price: Sec 1, paragraph 5, would have limited enforcement and as the AG indicated, the rest of the bill would be almost impossible to enforce.

Chairman Price: Close discussion.

Chairman Price: Opened discussion on HB 1522.

Rep. Nelson moved to accept the amendments.

Rep. Weisz: Second

Chairman Price: Is there any more discussion?

Rep. Porter: Do Pass as Amended

Rep. Pietsch: second

Vote: 10-1-1 Carrier: Rep. Weisz

FISCAL NOTE
Requested by Legislative Council
03/23/2005

Amendment to: Engrossed
 HB 1522

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.*

| | 2003-2005 Biennium | | 2005-2007 Biennium | | 2007-2009 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.*

| 2003-2005 Biennium | | | 2005-2007 Biennium | | | 2007-2009 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 1522 with Senate Amendments provides for the regulation of the sale and delivery of tobacco products over the Internet and through the mail. All cigarette and tobacco taxes apply to these sales, and the bill authorizes penalties for failure to comply with North Dakota's laws. There is no direct 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: | Office of Tax Commissioner |
| Phone Number: | 328-3402 | Date Prepared: | 03/24/2005 |

FISCAL NOTE

Requested by Legislative Council
02/16/2005

Amendment to: HB 1522

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.*

| | 2003-2005 Biennium | | 2005-2007 Biennium | | 2007-2009 Biennium | |
|----------------|--------------------|-------------|--------------------|-------------|--------------------|-------------|
| | General Fund | Other Funds | General Fund | Other Funds | General Fund | Other Funds |
| Revenues | | | \$116,500 | | | |
| Expenditures | | | | | | |
| Appropriations | | | | | | |

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

| 2003-2005 Biennium | | | 2005-2007 Biennium | | | 2007-2009 Biennium | | |
|--------------------|--------|------------------|--------------------|---------|------------------|--------------------|--------|------------------|
| Counties | Cities | School Districts | Counties | Cities | School Districts | Counties | Cities | School Districts |
| | | | | \$8,500 | | | | |

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

Engrossed HB 1522 removes the provision that allows individuals to possess one carton of untaxed cigarettes.

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.*

Engrossed HB 1522 is expected to increase revenues by an estimated \$125,000 during the 2005-07 biennium.

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: | Office of Tax Commissioner |
| Phone Number: | 328-3402 | Date Prepared: | 02/16/2005 |

FISCAL NOTE
Requested by Legislative Council
01/18/2005

Bill/Resolution No.: HB 1522

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.*

| | 2003-2005 Biennium | | 2005-2007 Biennium | | 2007-2009 Biennium | |
|-----------------------|--------------------|-------------|--------------------|-------------|--------------------|-------------|
| | General Fund | Other Funds | General Fund | Other Funds | General Fund | Other Funds |
| Revenues | | | \$45,000 | | | |
| Expenditures | | | \$468,000 | | | |
| Appropriations | | | | | | |

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

| 2003-2005 Biennium | | | 2005-2007 Biennium | | | 2007-2009 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 1522 reinstates the requirement that all cigarettes sold in the state must be stamped. Section 13 of HB 1522 repeals the deduction to licensed distributors for administrative expenses.

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.*

The repeal of the deduction for distributors is estimated to result in increased state general fund revenues of \$45,000 for the 2005-07 biennium.

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.*

The stamping requirements of HB 1522 would cause an increase in expenditures estimated to total \$368,000 for the 2005-07 biennium. These expenses include stamps, stamp cylinders, insured delivery of stamps, computer system expenses, and two FTE.

Additionally, there will be expenses associated with the regulation provisions of Section 1, requiring one FTE for investigative purposes. This is estimated to result in an additional \$100,000 of expenditures for the 2005-07 biennium.

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: | Office of Tax Commissioner |
| | | | |

Phone Number: 328-3402

Date Prepared: 01/25/2005

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1522

Page 8, line 10, after the underscored period insert "A licensed distributor may acquire sufficient indicia from the tax commissioner as reasonably may be expected to be used during the current or next calendar quarterly period and the licensed distributor shall pay the tax commissioner for the indicia within ten days after the end of the calendar quarterly period for which the indicia were acquired."

Page 8, line 21, remove "Any manufacturer or distributor marking cigarettes with a"

Page 8, remove line 22

Renumber accordingly

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1522

Page 1, line 1, remove "two new subsections to section 57-36-01,"

Page 1, remove line 2

Page 1, line 3, remove "Dakota Century Code," after "products" insert a semi-colon, and after the second "and" insert "to amend and reenact section 57-36-27 of the North Dakota Century Code, relating to consumer's use tax."

Page 1, remove lines 4 through 7

Page 4, replace lines 24 through 31 with:

"SECTION 2. AMENDMENT. Subsection 3 of section 57-36-27 of the North Dakota Century Code is amended and reenacted as follows:

57-36-27. Consumer's use tax - Cigarettes - Reports - Remittances.

~~3. This tax does not apply to the use or storage of cigarettes in quantities of two hundred or less in the possession of any one consumer nor to cigarettes exempt pursuant to section 57-36-24."~~

Page 5, remove lines 1 through 31

Page 6, remove lines 1 through 30

Page 7, remove lines 1 through 31

Page 8, remove lines 1 through 31

Page 9, remove lines 1 through 31

Page 10, remove lines 1 through 6

Renumber accordingly

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1522

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact section 57-36-27 of the North Dakota Century Code, relating to consumer's use tax.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-36-27 of the North Dakota Century Code is amended and reenacted as follows:

57-36-27. Consumer's use tax - Cigarettes - Reports - Remittances.

1. A tax is hereby imposed upon the use or storage by consumers of cigarettes in this state, and upon such consumers, at the following rates:
 - a. On cigarettes weighing not more than three pounds [1360.78 grams] per thousand, five mills on each such cigarette.
 - b. On cigarettes weighing more than three pounds [1360.78 grams] per thousand, five and one-half mills on each such cigarette.
2. This tax does not apply if the tax imposed by section 57-36-06 has been paid.
3. ~~This tax does not apply to the use or storage of cigarettes in quantities of two hundred or less in the possession of any one consumer nor to cigarettes exempt pursuant to section 57-36-24.~~
4. On or before the tenth day of each calendar quarter, every consumer who during the preceding calendar quarter has acquired title or possession of cigarettes for use or storage in this state, upon which cigarettes the tax imposed by section 57-36-06 has not been paid, shall file a return with the tax commissioner showing the quantity of cigarettes so acquired. The return must be made upon a form furnished and prescribed by the tax commissioner and must contain such other information as the tax commissioner may require. The return must be accompanied by a remittance for the full unpaid tax liability shown by it.
- ~~5.~~ 4. As soon as practicable after any return is filed, the tax commissioner shall examine the return and correct it, if necessary, according to the tax commissioner's best judgment and information.
- ~~6.~~ 5. In case any consumer required to pay the tax levied by this section fails to file a return or remit the tax as herein required, the tax commissioner has the authority to make an assessment of tax against the consumer according to the commissioner's best judgment and information.
- ~~7.~~ 6. All of the provisions of this chapter relating to corrections of returns, deficiency assessments, protests thereto, hearings thereon, interest and penalties, and collections of taxes are applicable to consumers under this section in like manner as though set out in full herein."

Renumber accordingly

Date: 2/14/05

Roll Call Vote #: 1) Do Pass on Amend
Rep Porter/Rep Devlin
2) Do Pass as Amend
Rep Porter/Rep Pietsch

2005 HOUSE STANDING COMMITTEE ROLL CALL
BILL/RESOLUTION NO. NB1522

House _____ Committee Human Services

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Pass as amend.

Motion Made By Rep. Porter Seconded By Rep. Pietsch

| Representatives | Yes | No | Representatives | Yes | No |
|---------------------|-----|----|-----------------|-----|----|
| Chairman C.S. Price | \ | | Rep.L. Kaldor | \ | |
| V Chrm.G. Kreidt | \ | | Rep.L. Potter | | \ |
| Rep. V. Pietsch | \ | | Rep.S. Sandvig | \ | |
| Rep.J.O. Nelson | \ | | | | |
| Rep.W.R. Devlin | \ | | | | |
| Rep.T. Porter | \ | | | | |
| Rep.G. Uglem | \ | | | | |
| Rep C. Damschen | \ | | | | |
| Rep.R. Weisz | AB | | | | |
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| | | | | | |
| | | | | | |

Total Yes 10 No 1

Absent 1

Floor Assignment Rep. Weisz

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

REPORT OF STANDING COMMITTEE

HB 1522: Human Services Committee (Rep. Price, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (10 YEAS, 1 NAY, 1 ABSENT AND NOT VOTING). HB 1522 was placed on the Sixth order on the calendar.

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact section 57-36-27 of the North Dakota Century Code, relating to consumer's use tax.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-36-27 of the North Dakota Century Code is amended and reenacted as follows:

57-36-27. Consumer's use tax - Cigarettes - Reports - Remittances.

1. A tax is hereby imposed upon the use or storage by consumers of cigarettes in this state, and upon such consumers, at the following rates:
 - a. On cigarettes weighing not more than three pounds [1360.78 grams] per thousand, five mills on each such cigarette.
 - b. On cigarettes weighing more than three pounds [1360.78 grams] per thousand, five and one-half mills on each such cigarette.
2. This tax does not apply if the tax imposed by section 57-36-06 has been paid.
3. ~~This tax does not apply to the use or storage of cigarettes in quantities of two hundred or less in the possession of any one consumer nor to cigarettes exempt pursuant to section 57-36-24.~~
4. On or before the tenth day of each calendar quarter, every consumer who during the preceding calendar quarter has acquired title or possession of cigarettes for use or storage in this state, upon which cigarettes the tax imposed by section 57-36-06 has not been paid, shall file a return with the tax commissioner showing the quantity of cigarettes so acquired. The return must be made upon a form furnished and prescribed by the tax commissioner and must contain such other information as the tax commissioner may require. The return must be accompanied by a remittance for the full unpaid tax liability shown by it.
5. 4. As soon as practicable after any return is filed, the tax commissioner shall examine the return and correct it, if necessary, according to the tax commissioner's best judgment and information.
6. 5. In case any consumer required to pay the tax levied by this section fails to file a return or remit the tax as herein required, the tax commissioner has the authority to make an assessment of tax against the consumer according to the commissioner's best judgment and information.
7. 6. All of the provisions of this chapter relating to corrections of returns, deficiency assessments, protests thereto, hearings thereon, interest and penalties, and collections of taxes are applicable to consumers under this section in like manner as though set out in full herein."

REPORT OF STANDING COMMITTEE (410)
February 15, 2005 12:24 p.m.

Module No: HR-30-2951
Carrier: Weisz
Insert LC: 58311.0102 Title: .0200

Renumber accordingly

2005 SENATE FINANCE AND TAXATION

HB 1522

2005 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. **HB 1522**

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date **March 9, 2005**

| Tape Number | Side A | Side B | Meter # |
|---|--------|--------|------------|
| #1 | | X | 5.5 - 61.3 |
| #2 | X | | 0.0 - 2.0 |
| Committee Clerk Signature <i>Aaron Benyon</i> | | | |

Minutes:

CHAIRMAN URLACHER CALLED THE COMMITTEE TO ORDER AND OPENED THE HEARING ON HB 1522.

The Clerk handed out written testimony from John Job of AMCON Distributing in support of the bill as it stands.

REP. CARLSON: Prime sponsor appeared in support stating this basically deals with sales of cigarettes over the Internet. More and more people are turning to the Internet obviously because of the tax that the State has imposed on cigarettes over the years, some as high as \$1.50 a pack. The problem is how do we keep track of that? I'm offering an amendment and handed out a chart entitled State Tax - Paid Cigarette Sales. The original bill that was sent to the House that I introduced put stamps back on cigarettes. I think originally we used to stamp cigarettes all the time, the amendments I have for you deal with not only the tax that is owed on the Internet but it also deals with taxes that would be owed that are sold into this State and would require stamping.

In 1991 we quit stamping and the best I can understand the reason why we quit stamping is I understand the machines broke and they were hard to replace and they cost too much money so we said we were going to quit stamping cigarettes. There's a lot of new technology available today that you can stamp cigarettes with and right now 47 States out of the 50 are stamping cigarettes, we are one of the three that is not. There's been some discrepancy Mr. Chairman about the number of cigarettes that are shipped into the State and the number of cigarettes that have been taxed. The numbers that I received and was given information on, there was about 47 million tax of cigarettes and last year were sent into the State and from what I understand there is a tax collected on about 41 million of those. The Tax Dept. Somehow those numbers have not coincided between the industry and the Tax Dept. And they can both address that issue. My point is that they are sold here, they should be taxed here. We have a unique situation obviously where we have reservations where cigarettes could be purchased on the reservations and resold. Now there are not supposed to do that, but I would care to wager that around the State that's happening. Adding up the numbers, what this bill does is there was some concern on the part if you stamp cigarettes, who pays for it? There was some concerns on the part of the industry that it costs money to do that. So this bill I believe gives 12 cents a carton to stamp those cigarettes, so its a reimbursement for the effort they do for stamping them. That's gonna cost about \$570,000.00 when we looked at the fiscal note, on the other hand if you actually take the difference in numbers between the cigarette packs that were brought into the State and those that the tax were collected on, I believe that there is about 3 million dollars worth of revenue that's been missed there.

I think as long as its a legal product, as long as its being sold, as long as we have a tax structure that said your supposed to pay a tax, then we should have a mechanism in place to allow tax to be collected on all those cigarettes. And that's why the bill before you deals with the Internet because its a serious problem and there are states right now and their are companies like UPS that will not deliver unless you can provide identification to show that your of proper age, their doing more checking but its still happening and its an easy way for the youth to buy cigarettes and I don't think any of us are in favor of that, so we need to keep that in mind as well, I think this bill brings back what should have probably been not drawn away from years ago and that's keeping track of the number of sales and the tax that's collected on cigarettes. For sure we need to make sure that we address the issue of Internet sales, the least we do and that's the bill in front of you, is it would make sure we address that, because I think that's crucial or I would like to see us stamp the cigarettes and tax again, Mr. Chairman and find the mechanism to work with the industry and I think we've addressed that on the compensation form for them to stamp those cigarettes and to collect the taxes on the ones that are actually sold in the State of ND. I know there's some disagreement over the number of packs, I think if you add the revenue up you'll see that what the industry says they've brought into the State and what the Tax Dept. Says was collected on, if you do the math, your gonna find out that there's probably some money short there. But I think there were packs that were missed that were actually sent here and there is the chart that I handed out and this doesn't deal with ND but it deals with other states that have been addressing the same issue and it talks about the state taxes paid on cigarettes and if you go to 1999 on the list and I believe it was Michigan that instituted putting the stamps back on the cigarettes and they saw revenue growth between 99 and 2000 of a hundred million dollars.

Obviously its a lot bigger state but the point is there were cigarettes that were being sold and distributed that were not being taxed and by them putting the stamps back on those cigarettes, they collected that much more revenue. Now I'm not saying that going to happen in ND, Alaska had the same type of results where they picked up an additional 2% when they went to stamping of their cigarettes. But what it is, is 3 million dollars and its paying a tax that's owed. And with that Mr. Chairman I would prefer to turn the rest of this over to the experts in the field, that's the logic behind the bill, its not the first time you've seen it. We tried to do this last time and it ended up being turned into a study, I think the problem still exists with the Internet sales and with the sale of cigarettes that are not being taxed from in our Indian Reservations and Casinos and I think that we need to address those issues to make sure that's collected. Any questions?

SEN. WARDNER: in your amendment it provides for 12 ½ cents a pack to the wholesaler?

ANSWER: 12 cents a carton. My understanding is you have to uncarton them and stamp them and it gives 12 cents a carton which is about 570,000.00 dollars for the biennium if you take the total number of cartons. About \$570,000.00 dollars total would be the cost of stamping them by having the 12 cents a carton. On the other hand I believe that there is a possibility of 3 to 3 ½ million dollars worth of revenue that's being missed on the tobacco sales in the State.

TOBY SPANGLER: District Director for Government Affairs for Altri Corporate Services, my client I'm representing today is Philip Morris USA and handed out some materials in support of the bill with written testimony. I've come here to testify in ND to talk about contraband and counterfeit cigarettes. Philip Morris believes that HB 1522 will benefit the State of ND in several ways. We believe that 1522 will help disrupt, reduce the trade and counterfeit cigarettes. As Rep. Carlson pointed out, ND is one of 3 states in the Country that does not tax cigarettes.

We're waiting for the state to discontinue taxing cigarettes (I'm trying to get a tax break here) stamping the cigarettes here in ND, we've been very aggressively going after a lot of the counterfeit sellers, the sellers that are selling illegal and counterfeit product over the Internet and we believe that putting stamps on cigarettes in ND will help the State Law Enforcement, its gonna help State collect the revenues that they have coming and we think that it's only gonna get worse before it gets better and basically the bottom line is, we think its a pretty good idea to put the stamps on, get the money that is owed to the State, it gives the Tax Dept. An opportunity to go in find out exactly where the product is coming from. If you went into a store in ND today and you went in and you grabbed a couple packs off the shelf, you have no way of knowing where those cigarettes came from. It could have come from the Indian Reservations, a low tax state like North Carolina, from the Internet, you just have no way, so if you put the stamps on, you can go in read the serial code, know exactly what wholesaler put that product out there, make sure that we know that the tax is being collected and if there's any problems from a quality issue or a tax issue you can go ahead and track it down. Obviously with the Tribes here in the state I think everybody acknowledges that a good number of sales coming off of the reservations and with the stamp at least people will know whether if it came off the reservation or if it came off from a legitimate wholesaler at the end of the day the retailers and wholesalers will benefit from having the tax stamp as will the State of ND with the increased revenue and that's pretty much. what our position is on the bill and I'd be happy to answer any questions.

SEN. TOLLEFSON: facetiously, who really cares if they buy a pack of cigarettes whether its stamped or not?

TOBY: the consumer? As long as its legitimate product, because what we've seen from China, is a lot of operators who are actually producing counterfeit Marlboros and they ship em over here and then they get into the distribution channel, honestly we haven't seen a lot of that in ND, its been primarily a problem in Florida, California but like anything else, it just takes a little while to get things to move into the heartland. As far as the consumer, if product tastes normal, then they are probably getting genuine product.

SEN. TOLLEFSON: Can care less.

TOBY; yes, but and if obviously now the appropriate taxes are being paid. And the other thing that the other representative was gonna talk about was you not only losing the state to 44 cent per pack excise tax, remember you also add another 5% sales tax on top of that and your you know your talking many many thousands of dollars. The opportunity to collect more revenues is certainly out there and think 47 other states are doing it.

SEN. WARDNER: Toby, Rep. Carlson mentioned that there is a discrepancy between the Tax Dept. And the industry, the industry feel they've sold x number of cigarettes in the state of ND and the Tax Dept. Has a whole different number, would you care to comment? Do you agree with him on that?

TOBY: I would say that we were at a hearing I believe 2 or 3 weeks ago and it was provided to the committee that the taxable sales in ND as far as collection had come to 41 million 6 or 7 hundred thousand dollars, that would be the collected tax, no on the taxable packs. We ran, its in the letter that we provided its known as the stars information it actually tracks industry volume, the number that we came up and its a pretty conservative number, its close to 48 million. Now since then the Tax Dept. Has come back and is reflecting I think there is close to 5 million packs

that they are showing as coming off the reservations, so that number will move up. The number we're working with at the last hearing was 41.7 million, so we were quite confident that that number was much higher and so we did something that we normally don't do and we provided some proprietary industry data so that everybody could have a clearer picture of what the situation is.

SEN. COOK: in your written testimony, you make a comment most counterfeit cigarette packs also carry counterfeit tax stamps, are these tax stamps easy to duplicate? To have a counterfeit stamp out there and if so, then how does it solve our problem?

TOBY: absolutely, there are packs that we've collected these stamps are duplicated, the packaging that they use for our packs of Marlboro I could set down 2 packs on the table and I guarantee you that one person in this room could tell the difference. So yes, they can duplicate they can counterfeit the stamps, its a very lucrative business, is this gonna solve all the problems, no but I would venture to guess that because the volume in ND isn't as heavy it is in some of the larger states, I don't know if it'd be cost effective to come in and produce the ND stamps, but absolutely, they can counterfeit the stamps.

SEN. BERCIER: Toby, are you saying that Tribal businesses and I'm using your language here would who are selling cigarettes are not or not law abiding businesses?

TOBY: nah, what I'm saying is that the in ND right now, the law in ND that enables a person to take off the Reservation 1 carton of cigarettes and that's the law, now according to the number that the Tax Dept. Has provided us that says there are 5 million packs coming off the Reservation. I don't know how many how the math adds up but I'm not saying that people are not breaking the law or breaking the law, we are just using the numbers.

SEN. URLACHER: anyone here in opposition of the bill.

JOHN QUINLAN, Tax Dept. handed out some handouts on ND Retail Cigarettes Sold. The numbers you've been given by the industry provided what we understand is retail packs that were sold in ND, the first copy I handed to you showed that were in that 48 million package ball park in ND between those sales which were taxed and those sales which were not taxed but still sold at retail. I feel that the numbers are pretty equal, you have to take into consideration from the report those products which were legally sold onto the union reservation to enroll tribal members and legally purchased by ND residents as well as those taxed products for which we give credit when returns are made to the manufacturer. So we feel confident that our numbers reflect the same basic total of retail packages available for sale in the State of ND that the industry provided. The second attachment that I handed to you this morning is just a recap of a major court case brought by another manufacturer in conjunction with the federal govt. on Internet sales. And from the handout you can see that Internet is primarily a problem in high tax states and stamping doesn't solve the Internet problem. Most other states as you've been told, you need stamp cigarettes they continue to have enforcement problems not just with Internet but within enforcement problems regarding counterfeit product and counterfeit stamps as Sen. Cook has indicated. I do have to give Philip Morris some credit, they have over the past years created a good brand integrity program, Mr. Hollam (sp) through the head of that had worked with the States they have very thoroughly worked with the States to help protect their market share. They come out and provide classes for the States so that counterfeit product can be identified and they go to great lengths to work with the States to make sure that their sales continue and that the tax is properly paid. In front of the Nevada legislature, Mr. Hollam (sp) indicated in testimony to

them that 95% of the packages of counterfeit product that they find have counterfeit stamps on.

My counterparts in other states spend a lot of time inspecting or verifying that products on the shelves are stamped and checking to see if the stamps are counterfeit. Right now that's an area that we don't have to worry about because we don't stamp. Anyone can walk into ND and look at packs on the shelf and if they are stamped, because we don't stamp they stand out and we get calls occasionally some product will come over from MN by accident and we get calls because the everyday citizen can take a look at a pack and realize whether or not its a legitimate package of cigarettes in ND. So in a perverse way that works for the State of ND in a reverse way because we don't stamp cigarettes currently. Otherwise anybody could go in and if they're all stamped you couldn't tell whether that was a legitimate stamp or not because of the success the counterfeiters have had with the product. Are their cigarettes that are purchased and brought off the Reservation? Under the existing law, people have the ability to buy one carton and bring it off legally, is that abused? It probably is, do we feel that there is a large retail contingent doing that? No we don't. We do a review every biennium of about 10% of the retailers and go through their records to determine where they are buying a product. We find in the last review that we have as many retailers purchasing particularly Marlboro cigarettes from other retailers than we do buying on the Reservation. Because the marketing structure you can go down to a local gas station here and buy Marlboros, its \$25.00 a carton, which is basically what they cost on the Reservation. Its my understanding that the Tribal store they cost between \$24 and \$25 a carton. So we have retailers instead of going to the Reservation and buying \$24 - \$25 dollar product, they are buying legally taxed right here in Bismarck, Fargo, Devils Lake, Minot or from a retailer who is because of pricing structure able to sell at that reduced price. Stamping doesn't stop

youth from going on and purchasing cigarettes on the reservation and stamping won't stop those individuals who chose to break state law and bring excess packages off the reservation. There are some things that stamping will do, stamping will increase enforcement costs and expenses for wholesalers, now the information that you received this morning on the 12 cent costs, basically that was a little bit low based on our numbers and the numbers provided by the industry, there were 48 million packages sold in 2004. Using that number it would be 576,000 per year and that doesn't include the initial stamp out by the wholesalers, so actually those costs would increase and based on some rough numbers this morning, the top 6 wholesalers would get over 7% of that discount. In fact, the largest distributor that we have would basically do about 200 million packs a year and received \$120,000.00 for stamping cigarettes. In 1991 when we discontinued stamping cigarettes we had capped the wholesaler at \$25,000.00 maximum for their discount for stamping so that would be an increase across the board for the largest wholesaler.

SEN. WARDNER: How does that work when a retailer buys cigarettes from another retailer and resells those as far as the tax, they don't pay tax twice on those?

ANSWER; no, because the tax was paid when the initial retailer bought it from the wholesaler, the tax has been paid, so it doesn't affect the taxable sales for the Tax Dept. It affects the wholesaler because they are not selling at the same price, they don't have as many customers.

SEN. WARDNER: so, if I was selling to another retailer, I just mark them up a little bit so I made a little bit more and I would have to remit the tax on those because I bought them from another retailer?

ANSWER; the tax would have already been paid, so you'll pay the sales tax on it but the \$4.40 a carton had been previously paid.

SEN. COOK: if somebody sets up a shop and they start remotely selling cigarettes into NY, there would be say, somebody from ND, is the person doing the selling breaking NY law or is it just the person doing the buying that would have a tax obligation? Would it be legal from some distributor in ND to ship and sell cigarettes into NY?

ANSWER: it would depend on the what the NY law states. Some states have changed their laws to require that products coming into their state be taxed with their state tax stamp. I don't know off hand if the state of NY has made that change, if they haven't there wouldn't be anything illegal in the interstate shipment of the cigarettes and it would then fall upon the purchaser in NY to pay the tax. NY does have a tougher sales law they call it face to face and they have made some changes but I'm not sure it would place a burden on the out of state seller.

SEN. COOK: there's quite a difference in tax, there could be a lucrative business _____. I'm surprised there isn't a whole lot of cigarettes being shipped illegally into NY, there obviously are.

ANSWER; there's a huge amount of cigarettes being shipped into NY, smuggled into NY, NY City itself has the highest tax rate at \$1.50 State and \$1.50 City for a combined rate of \$3.00 a pack and as the map shows you, that's why they are an Internet haven so to speak because of their high tax rate.

SEN. TOLLEFSON: (comment) Facetiously maybe we should introduce a predatory pricing bill on cigarettes.

RICK CLAYBURGH: Tax Commissioner, maybe I should remind Sen. Tollefson that that was part of the bill two years ago that had the minimum pricing aspects in it that did recall a couple of out of state companies came in and testified against. I just want to address an issue that we are

researching in the Tax Dept. And I believe in the A.G's office as well is looking at it and it deals with the issue, and I have not seen the amendments today if they are similar to the way the bill had left or the bill that was originally introduced in the House, on the issue of the Internet side of the bill, there are some concerns that we have as the States in looking at that would that because of the difficulty in trying to enforce it, one of the areas and one of the people we came across last legislative session or groups we came across that also shipped tobacco products through the US Postal Service and the US Postal Service doesn't follow anybody's rules and regulations they just kinda say we're taking a first class product and we're shipping it to ya and whoever gets it, gets it, it doesn't matter.

HENRY KNOLL: with Frank McKone Cigar Company in Fargo, ND appeared in opposition with written testimony.

SEN. COOK: Would you have to have two stamping machines or could you use the same stamping machine for both MN and ND stamps?

ANSWER; you could, but if you've ever seen one of these stamping machines, you have to take the roll of stamps off and there is a lot of adjusting that has to be done every time you take them off and put them back on. If this were to go into effect, I think it would best as far as time and labor wise, I would have to get another machine.

SEN. BERCIER: Mr. Clayburgh, I do this as kind of targeting the Internet sales but Indian Tribes have been mentioned and also the military have been mentioned, if this were to pass, would this be enforceable.

MR. CLAYBURGH: the stamping aspect? Yes. The stamping aspect is a concern, our biggest issue as a state, if we look at the potential for revenue its North Dakotans going on the

Reservation and legally purchasing, they can purchase on the Reservation, our current law allows an individual to have one carton of untaxed cigarettes. Now the bill as it came over from the House eliminates that and so there is no longer that ability to have one carton of untaxed cigarettes. Part of that comes out to if you go up to Canada you can come back and purchase duty free, that would no longer apply in ND. You just could not have a carton of untaxed cigarettes anymore. So North Dakotans that would go onto the Reservation make a legal purchase could not come off the Reservation, how do you enforce that is the big question. Are we going to have the Highway Patrol start stopping people, those are the issues that make it very difficult to try to address that issue.

SEN. BERCIER: the question on Internet sales, would that be enforceable?

ANSWER; the Internet sale aspect of it and I need to double check and review again, I'm assuming its the same as it came out of the House. There's certain aspects of it that three are some businesses out there, Internet businesses that would probably lawfully comply and we would be able to deal with those individuals. But there is a lot of activity that's occurring in areas where States don't have the legal ability to reach. I don't know how we could fully enforce the Internet provisions and that's part of my concern in what I addressed on the issue of the MSA (Master Settlement Agreement) and that's the part we are still trying to get a handle on . I don't know we cold totally enforce the Internet provisions of the bill, its like trying to enforce Internet sales of clothing or any other taxable item, how do we do that? Are we gonna start going door to door or stopping cars, those are very difficult issues to enforce and we don't have the resources to fully enforce any of those Internet issues at the State level, not just ND but national.

ROGER BORKHAIS (SP) Wholesale Supply Company out of Minot, appeared in opposition stating we employ approximately 83 individuals, all but 1 are North Dakotans. We service the entire state of ND and part of western MN and a little bit of MT. We distribute candy, tobacco, wholesale products, tobacco, grocery food service and everything we can, we've acquired about three other distributors in the past 10 years and through attrition at the time we had about 120 combined employees and are now down to say 83. At one time we were the largest I think reporting cigarette distributor in the State and paying in excess of \$300,000 dollars a month. We have since dwindled down in that through out of state concerns and that's approximately where our 40 jobs have gone is competing with out-of-state. One of my concerns with stamping is we service about 3 to 4 of the Indian Reservations in the State selling unstamped audit to those customers and I think for the most part are sold legitimately to individuals purchasing their product, but we ran into a problem with the ICC I think it is or Federal Regulations that we couldn't at the time before 1992 or whatever it was when stamping _____. We could not transport unstamped product in the State of ND to sell to the Indian Reservations and so we were at a disadvantage, our out-of-state competitors could ship the interstate commerce on a private carrier and legally deliver that product to the Reservations and not be in violation of Federal Law. When this came about, obviously it created some more jobs because those sales were staying within the State of ND and I think better control through the Tax Commissioners Office of knowing where the reporting was coming from and it wasn't coming through the back door. I did some checking like Henry mentioned as far as the technology for stamping, I just came back from our trade show out in Las Vegas and there was a company there that's done and approved stamping system, the cost of the machine alone is \$50,000 and its called the red line. Right now

we've been coming under attack from both sides, the cigarette manufacturers obviously are tightening their belts, it used to be stale and damaged product was actually a money maker for us, we made more money handling it than we did selling it originally outright in the first place but since then they have eliminated doing that so even in your stamping damage now would be at our cost \$4.40 a carton plus the \$25 for a carton of cigarettes could put us out of business in not time, because the machinery that we've been using is just leaves a lot to be desired. This \$50,000 machine now their error rate is down to 1 in a 1,000 I think or something they're claiming that with 5 units in a complete stamp off region, but for \$50,000 for the equipment plus leasing upkeep and maintenance on it and then probably another \$50,000 for personnel to run the stamping machine, its beginning more cost prohibited that way. I guess my suggestion would be if Philip Morris wants to see this product stamped, they should stamp it at their level. They would see again, because right now its putting the burden to us as much as we'd appreciate the 12 cents a carton as opposed to nothing, I think Philip Morris would know what kind of a ____ We're trying to stamp or who knows how many thousands of tax jurisdictions there are across the country. Counterfeit stamps, that's the other thing that was addressed pretty well because in this day and age, there's more people that are doing a better job at doing counterfeit stamps than they are US postal stamps, so that really wouldn't solve the problem anyway, I don't see it because these guys if their smart enough to figure out a way to sell products illegally, they obviously could counterfeit a stamp pretty easy. Our business in most part is competing with out-of-state competitors too that are coming in or being the bigger and better servicing our national accounts whether its the Walmarts trying to sell the gas cheaper than anybody else out there, which I'm sure nobody has a problem with that other than the convenience stores out there that are trying to

make a living, but the same with cigarettes. I think cigarettes for the most part I think the Tax Commissioner's done a good job of monitoring keeping us honest and keeping us on our feet and watching our customers to see where the product is going too because, I'm glad somebody mentioned here that a lot of our competition has come from retail accounts, not from the Indian Reservations but its when the buy downs are \$6.50 and \$7.00 a carton they can go, my retailer that I used have to go out to Columbus, ND and sell him a carton of cigarettes and try to figure out how I'm gonna pay for his service up there to deliver that product, all of sudden now he can go into almost any major city and go in and products cheaper than I can sell it to him, the way the structure is set up with the discount. I guess everything else has pretty well been covered by that, if there's any questions, I'd be glad to answer them.

KELLY KISER: Owner of OK Distributing in Williston, ND appeared in opposition stating we are a candy and tobacco wholesaler that services NW North Dakota and parts of Eastern MT for over 50 years. I employ 15 people in Williston and 5 people in MT and I'm a third generation of the company. I'm not in favor of this bill with the proposed amendment for the most part on financial basis. A typical stamping machine costs a minimum of \$6,000 and that's just to lease it. I figure it will take 1 additional employee to oversee the stamping of the cigarettes at a cost of in Williston \$17,000 plus benefits. I think based on what Mr. Spangler had spoken about the amendments that 12 cents a carton that we'd be getting as a stamping allowance, I think it will take me about 45 weeks of the year to offset that \$6,000 in ND. The 72 hour stamping provision because I stamp in 3 different tax jurisdictions, I have ND, MT and the Tribal accounts, I'd have to carry 3 different inventories and I had for a rough figure, we're talking about \$100,000 dollars in added inventory which would be about 20% more inventory value that I'm already carrying

right now. The stamping technology has been spoken about a few times I'd like to give my spin on it because I work with it because we have a machine from MT. I call it an over growing retro set in the 1950's, the quality of the stamps is a price of this carton is marginal effect, you can sometimes get the stamp ID number on it, there are many times that we'll run a carton through and you either get a stamp put on 2 packs or no stamps on the last 2 packs, so your actually stamping 8 of the 10 packs. Also we would have to put a Tribal Stamp on ours as I understand it. I think that would give the Tribal accounts an opportunity to make them choose whether or not they thought our ____ have anything on it or to have a different type of stamp that would stand out. I think in general stamping cigarettes will create more of a problem than it will solve because of the counterfeiting, a financial investment for being a small wholesaler like myself will have to make a st____ing compared to the returns that it will bring. There is very little opportunity to pass these costs on to the customers in the industry because of the fact that out-of-state competitors are operating on a very large scales. I think that we do a very good job in ND collecting the tax on cigarettes and it does employ people in my community and I think my community would prefer having as many people employed as possible rather than having out-of-state concern handling the product. Today with no stamping in ND businesses can be audited and verified with no more effort than a State that has stamping, I deal with MT and the forms are very similar and basically all you do is right em down, how many stamps that you've placed on product and right now we write how many sales in cigarettes are sold in ND. In closing, I believe that any problems this proposed amendment is trying to addressed will not be fixed by putting a stamp on a pack of cigarettes.

Closed the hearing.

2005 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. **HB 1522**

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date **March 14, 2005**

| Tape Number | Side A | Side B | Meter # |
|--|--------|--------|------------|
| #1 | | X | 56.8 - END |
| #2 | X | | 0.0 - 0.7 |
| | | | |
| Committee Clerk Signature <i>Sharon Pennew</i> | | | |

Minutes:

COMMITTEE WORK

SEN. BERCIER: made a **MOTION FOR DO NOT PASS**, seconded by Sen. Every.

SEN. WARDNER: does it do anything, the way it is, we've spent so much time talking about stamping which is an amendment which isn't even on the bill , does it do anything as far as the Internet?

SEN. COOK: no

SEN. URLACHER: a do not pass means no stamping.

SEN. COOK: stamping isn't in the bill, they presented amendments and basically spoke to the amendments and the amendments would deal with stamping. The bill as is simply removes the 2 carton exemption. Right now its legal that you have 2 cartons in your possession that you may not have had to pay taxes on, the bill removes that exemption, that's all it does now. Most of the testimony was on the amendments that were presented by the prime sponsor of the bill and they deal with stamping.

SEN. WARDNER: I didn't think there was a very good argument for stamping and for anything. Even the Tax Dept. And the numbers of the industry, the Tax Dept. Knew within 200,000 packs or something like that which is a very small amount of just how many cigarettes were not taxed through the Reservation and stuff, so I guess I.

SEN. COOK: for what its worth, one other thing, the fiscal note if we went to stamping with something like 576,000, some information I got after the hearing on my own, right now we compensate sellers or people who collect and remit the cigarette tax, we compensate them 1 ½ % per month for 1 ½ % (tape ran out)

I think if we had a, if we were going to raise our cigarette tax then we could probably have a problem that would require us to look at stamping, but where our cigarette tax is located right now relative to other states, I don't think there's a boot legging problem. If we were in NYC, they got a bootlegging problem big time. With \$3.00 cigarette tax in the City of New York, \$3.00 a pack, they would need something to make this.

SEN. URLACHER: any further discussion? If not, call the roll for Do Not Pass.

ROLL CALL VOTE: 5-0-1 Sen. Bercier will carry the bill.

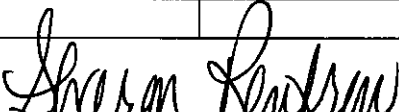
2005 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. **HB 1522**

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date **March 21, 2005**

| Tape Number | Side A | Side B | Meter # |
|---|--------|--------|-------------|
| #1 | X | | 33.1 - 61.5 |
| | | | |
| | | | |
| Committee Clerk Signature  | | | |

Minutes:

COMMITTEE WORK

SEN. COOK: made a **MOTION TO RECONSIDER OUR PREVIOUS ACTIONS**, seconded by Sen. Wardner. **VOICE VOTE:** 5-1-1, Sen. Bercier absent, motion carries.

SEN. URLACHER: John Olson will be here to explain the amendments stating one allows 1 carton of cigarettes and the other eliminates that and they both eliminate stamping.

JOHN OLSON: Altria, and they have Kraft & Philip Morris appeared to explain the amendments. As you regard we initially supported 1522 with several amendments, one being the stamping amendments which the committee has elected to not accept and we are not supporting those amendments today. The other set of amendments related to the Internet piece which does regulate and enforce the laws prohibiting Internet sales except under certain conditions. There were some reservations that were expressed about that bill I believe tat the State Tax Dept. Had problems with the Internet piece because of its relationship with the master settlement. We had encouraged the committee at that time that there were no real concerns with that. The Attorney

General had also some of those concerns, those concerns have been eliminated and I think I'll literally speak on behalf of the attorney general this morning. One of the things that has happened with the Internet piece is that recently the negotiation with attorneys general and the Federal agency, ATF, jointly reached an agreement with the major credit card companies that those credit card companies will no longer accept credit card sales for tobacco over the Internet. The best I can offer you on that recent announcement is the article that is off the web which relate to that. I can get the press release for you. In essence its the announcement struck by the major credit card companies with the US Bureau of Alcohol, tobacco and firearms and the state attorney general stress that they want to work together to prevent the unchecked use of credit cards to buy cigarettes over the Internet across the state line. That agreement is affective immediately, the result is that virtually all credit cards will no longer participate with web sites based in the United States and abroad in itself these products in every state. The card companies also agree to take action against Internet sellers that authorities identify as violating state and federal law regulating cigarette sales. The spokesman for ATF said that states lose more than 1 billion dollars a year in tax revenue from Internet tobacco sales because they're not paying those state sales taxes and so forth.

SEN. URLACHER: question was mentioned whether they would not accept credit cards in state for purchases or just Internet?

ANSWER; just Internet, that has no impact on locals being able to go down to the grocery store and produce a credit card for the sale for a purchase there. The amendments were drafted in this manner. One set of amendments will place the Internet restrictions as previously proposed together with an emergency clause and the emergency clause is at the request of the attorney

general. He believes its an important enough issue now that we should get on board as soon as possible. The other set of amendments I believe addresses the way the bill currently is written and the way the bill came over from the House, the only thing that was left in the bill after they stripped out the Internet piece and the stamping piece was to repeal the one carton exemption, whereby if you purchased a carton of cigarettes on an Indian Reservation, you would be able to have one carton of untaxed, unregulated purchase and that piece was not in the bill when it originally came in. Altria has no position on that, that's a matter of policy for your committee and whatever you want to do with that piece remains completely your decision. I know that the amendment addressed the difference. So one set of the amendments will put the Internet piece in with the emergency clause and repeal the one carton exemption which is currently in the bill and the other set of amendments would set that ____ aside and you would continue having the one carton exemption.

SEN. WARDNER: so the set of amendments that says after a bill, would mean you would clean it out and start fresh and that would repeal that one carton limit, so that's .0202 and then the other one is .0203, that one would leave that one carton limit.

ANSWER; absolutely correct.

SEN. URLACHER: who would administer this process.

ANSWER; Its a prohibited act, so I would assume that the enforcement would fall with the attorney general or whatever agency seeks to enforce the collection of state sales tax, I assume that the state tax dept. Would also be interested making sure that the taxable sales are reported and these provisions are enforced. The attorney general would be the primary law enforcement agency obliged to enforce the law.

SEN. EVERY: I'm looking at the testimony that came from the tax dept. on lots of tax collections between October 1999 and July 2004, it says that ND sold no cigarettes over the Internet and lost no revenue from that. If that the case and if this federal law is now or working federally on making this illegal to use your credit card to buy cigarettes over the Internet, why do we need the bill?

ANSWER; that's a good question, but I don't see how any one of us can really gage how many cigarettes are sold over the Internet, I don't think you can do that. I think we can guess or speculate.

SEN. EVERY: Well John, you just testified how much revenue was lost in NY, they must be able to gauge it?

ANSWER; they maybe can, but I don't think anybody really has a tremendous handle on how many cigarettes are lost over the Internet. I assume that ND is not in the same taxing position as NY so there's probably some differences there, but I think this bill is being adopted in more states all along, I think ND has an obligation, I think to join a national system of enforcement so I think it would help not only ND but would help a nation wide system of enforcement on Internet sales that should be prohibited. Who can be against the bill that prohibits minors from purchasing over the Internet.

SEN. URLACHER: 0202 is the one that is a hog house and eliminates Internet sales without the one carton,

SEN. COOK, .0203 adds another section to the bill it leaves the bill basically as we have before us intact, so that's 0203 would eliminate the one carton possession though.

SEN. EVERY: so I could go out to the Reservation and buy as many cartons of cigarettes as I want?

SEN. COOK; no, right now with existing law, you could have in your possession 1 carton of untaxed cigarettes. 02 would leave that.

SEN. EVERY; John, we already have a law now that says minors can't purchase cigarettes, don't we?

ANSWER; we do, but that's in state and violations are pretty much limited to in state enforcement. Now its certainly no convenience store can sell cigarettes to minors but we don't have much control over the Internet out of state.

RICK CLAYBURGH: Tax Commissioner, clarification of the amendments, from the dept.'s stand point, its purely a policy decision, we don't take a position on that, if that's what the legislature is interested in, that's just fine either way. The issue about the Internet, for the most part from our analyze shows that on main street ND, I many respects you can get a carton of cigarettes close to a similar price that you can on the Internet, with that being said, we are just reviewing these amendments for the first time but based on the initial analyze of it, I don't think we would have any concern with these amendments to the bill. Our initial concerns we've been in contact with the attorney generals office as well on this Internet side and my understanding too is it will be the attorney generals office that will be the agency being responsible for the administrative oversight and it appears their not concerned with it either.

SEN. COOK: clarification - 03 allows 1 carton untaxed, 02 would prohibit 1 carton of untaxed.

JOHN OLSON: Sen. Cook is absolutely correct, 02 is the hog house which takes the whole bill out which removes the repeal of the exemption, 02 starts all over, the law would be the same as it is now.

SEN. COOK; made a **MOTION TO MOVE THE AMENDMENTS 0203**, seconded by Sen. Wardner. This repeals 1 carton and adds Internet part, just adds language.

SEN. WARDNER: from your stand point, right now I can have 1 carton of untaxed cigarettes, is that a problem or would it be better if you can't have any, in your opinion?

RICK: is it enforceable, its a difficult issue to enforce, but I don't think there's any other section of code in tax law that you allow an exemption for somebody, unless your provide an exemption, there isn't anything else in code that allows you to possess something that tax shouldn't be applied to. Basically an exemption for 1 carton of cigarettes is the what the aspect is. Is it enforceable, I think the biggest thing that will come out of it, is the stand point that as if in just discussion points talking in the newspaper, talking about people being aware of it, certain retailers can talk about it to their customers and people realize that there isn't an exemption for a single carton of cigarettes, it may lead to some North Dakotans not purchasing untaxed cigarettes. Is it a good policy, in my opinion I think it is, I think it would not be a bad thing to do from a policy perspective, is it enforceable, it would be very difficult.,

SEN. EVERY: as I said earlier when we voted do not pass on this bill and it came in that this was nothing more than a wolf in sheep's clothing. We talked about it like it was designed to curb all this Internet sales that are going on and in reality its all about getting those taxed cigarettes off the reservation and I know that's where we are going with this, that's exactly where this is going, I don't think we should be taxing legislation without a hearing and allow the tribes to come in

and at least testify, because that's their revenue that this is going to affect. What this is, is putting into policy a whole new law without any hearing and any notification of hearing and I'm going to adamantly oppose this as even 02 which allows the carton as John had said earlier, we don't even need this bill, there's no sales on the Internet that we can account for and there's nothing that suggests that we are losing any revenue other than what is being sold on the reservation and to me that's what this bill is all about and that's what it was about when it was originated.

SEN. WARDNER: that was in the bill and there was a hearing on that part of it on the one carton because that was when it came over here that's the way it was, so there was an opportunity for a hearing.

SEN. EVERY: after that hearing we voted a do not pass recommendation for a do not pass for the whole body upstairs and now we're gonna go back on that and add it back in without the hearing. As far as I'm concerned there was no hearing the tribes had no chance to testify on this and that's the only person that this affects.

SEN. WARDNER: I agree that if we change our mind, we haven't yet, but if we would be changing our mind, but they did have an opportunity and no one really came in to testify on that but there was a hearing on that part, that's my point. Is there a possibility that we might change our mind, I guess there is.

SEN. COOK: the Internet portion which is basically what we just amended off of that, how does that affect tribes? Does it affect tribes differently than it does anybody else, I guess maybe I'm missing something here.

SEN. EVERY; as you heard when Mr. Quinlin testified this does this bill according to what's being sold on the Internet is not needed at all. The only reason that he suggested that it might be

needed is so that we can go along with what everybody else is already doing and what the federal legislation is going to do, we don't need the law. We don't need anything in this bill that has anything to do with the Internet and Mr. Quinlin testified to that.

SEN. COOK: but it fits us all the same your just saying it doesn't need, I'm trying to make the tribe connection with the Internet part. The Internet part your saying we don't need it but the Internet part does not in some way affect tribes differently than it does anybody else.

SEN. EVERY: my argument would be if the idea behind the bill is to get the lost revenue for those cigarettes that are being sold some other place than according to what the Tax Dept. Testified, there's been zero in the last 5 years. No need for the bill.

SEN. COOK: I think I would have to respectfully disagree, I think one of the things that the bill does is its going to remove the loop hole or the opportunity that somebody, a minor is trying to get cigarettes might use to get cigarettes and probably sell em to classmates and if it does that then I think its got some merit.

RICK CLAYBURGH: I should clarify this issue that Mr. Quinlin testified to. The information that we received and provided to the committee was based on activity that occurred within a couple of Internet companies and some states policing activity. They went in and looked at their records and provided that information that is not all Internet sales, that some specific companies and their activities and I think it showed a minimal amount in MN, zero amount in ND and SD and larger amounts in the higher tax states. We do know that Internet sales occurs but is that, we just think its that huge of an amount based on our tax rate and based on the fact that most of our sampling right now is showing our main street prices fairly similar to Internet pricing. Although Internet companies now, the pricing are coming down more and also they don't charge shipping

and some other things to try to make themselves competitive. Its the tax rate that are causing more of it than anything. I hope that you don't get the impression that we are saying that no Internet activity occurs in ND, obviously there's got to be some but the evidence we have seen on some of the larger sting type operations, that information that was provided showed no activity in North or South Dakota and limited into MN.

SEN. BERCIER: if this passes, the tribes are going to challenge it. It's only going to cause more ill will than its going to do any good. Now the Internet issue doesn't seem to be ____.

SEN. WARDNER: it's a matter of which set you want to put on in my opinion and where I'm coming from. Do we want to allow one carton of untaxed cigarettes like we always had then we would do the set that is not on the table now, to me that's where its at. I don't have a problem with the Internet thing, I really don't, so in my mind the debate is what set of amendments to put on.

SEN. TOLLEFSON: or no amendments and kill the bill.

SEN. URLACHER: Sen. Cook, why don't we call the Attorney General down if that's controversial why we want his opinion.

SEN. COOK: if the heartburn in the committee is with the amendments I moved, I did them for a starting point in this discussion, to me that was the cleanest thing to do we add it to the bill and that's what the House apparently wanted to do but if that's where the heartburn is I'm not married to that set of amendments I can certainly support the other set.

SEN. URLACHER: that's part of the process.

SEN. EVERY: the only way that we could remove the heartburn is to adopt the 02 and eliminate 03 and then we have no heartburn.

SEN. COOK: that's why I asked the question about the Internet part of it, so I would move that you call the question on 03 and then we can go from there.

ROLL CALL VOTE: 6-0-0 **MOTION FAILS**

SEN. COOK: made a **MOTION TO ADOPT AMENDMENTS 0202**, seconded by Sen. Wardner.

ROLL CALL VOTE: 6-0-0 **MOTION PASSES.**

SEN. COOK: made a **MOTION FOR DO PASS AS AMENDED**, seconded by Sen. Wardner.

SEN. URLACHER; someone from the tax dept. Want to explain the fiscal note?

SEN. COOK: there is no fiscal note, its like killing the bill.

RICK CLAYBURGH: based on our quick analysis here, we believe the fiscal note would change. Originally the way the bill was discussed in the House and I believe the amendments that Rep. Carlson presented had the tax dept. doing work on the Internet side and doing it forfeit work, we were going to need and FTE and expenditures in the dept. But since the fact, from our stand point its the attorney general's office that will be overseeing it, they'll probably be more litigation activity, but the fiscal note would change the way it was discussed in the House, there would be no fiscal impact in the tax dept. And I can't imagine, I would assume there would be some fiscal impact if there's been an agency oversight. I'd like to inquire that if that's the case, then I'm assuming that the bill gets re-referred to appropriations for a quick review and a new fiscal note.

SEN. URLACHER: well there's a question on whether it gets referred to appropriations.

SEN. COOK: we killed the bill that came over to us that had the fiscal note to it, we killed that.

This is a new bill, if there's going to be some fiscal impact on the attorney generals officer,
re-refer it and find out.

RICK CLAYBURGH: my advice as an administrative agency would be to just make the
re-referral and as its engrossed the fiscal note would be done and the Chairman can always kick it
out of appropriations.

SEN. URLACHER: so is that part of your motion?

SEN. WARDNER: yes, I'll second that.

ROLL CALL VOTE; 6-0-0 Sen. Bercier will carry the bill.

Date: 3-14-05
Roll Call Vote #: 1

2005 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1522

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Not Pass

Motion Made By Bercier Seconded By Every

| Senators | Yes | No | Senators | Yes | No |
|----------------|-----|----|--------------|-----|----|
| Sen. Urlacher | ✓ | | Sen. Bercier | ✓ | |
| Sen. Wardner | ✓ | | Sen. Every | ✓ | |
| Sen. Cook | ✓ | | | | |
| Sen. Tollefson | | | | | |
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Total (Yes) 5 No 0

Absent 1

Floor Assignment Bercier

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

REPORT OF STANDING COMMITTEE (410)
March 14, 2005 4:02 p.m.

Module No: SR-46-4918
Carrier: Bercier
Insert LC: . Title: .

REPORT OF STANDING COMMITTEE

HB 1522, as engrossed: Finance and Taxation Committee (Sen. Urlacher, Chairman)
recommends **DO NOT PASS** (5 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING).
Engrossed HB 1522 was placed on the Fourteenth order on the calendar.

Date: 3.21-05
Roll Call Vote #: 1

2005 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1522

| Senate | Finance and Taxation | Committee |
|--------|----------------------|-----------|
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☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken Reconsider previous action

Motion Made By Cook Seconded By Wardner

[illegible]

Total (Yes) 4 No 1

Absent /

Floor Assignment

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

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1522

Page 1, line 1, after "Act" insert "to create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products;"

Page 1, line 2, after "tax" insert "; and to declare an emergency"

Page 1, after line 3, insert:

"SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual;
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
 - (2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company; and
 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order.
3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.
4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.

5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
 - (2) Have an individual of legal minimum purchase age sign for delivery of the package; and
 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

51-30-03. E-mail addresses. Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses.

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. Before making delivery sales or shipping cigarettes in connection with those sales, every person shall file with the tax commissioner a statement setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.
2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:

- a. The name and address of the individual to whom the delivery sale was made;
- b. The brand or brands of the cigarettes that were sold in the delivery sale; and
- c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person."

Page 2, after line 11, insert:

"SECTION 3. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

Date: 3-21-05
Roll Call Vote #: 2

2005 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1522

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 0203

Action Taken Adopt Amendments

Motion Made By Cook Seconded By Wardner

| Senators | Yes | No | Senators | Yes | No |
|----------------|-----|----|--------------|-----|----|
| Sen. Urlacher | | ✓ | Sen. Bercier | | ✓ |
| Sen. Wardner | | ✓ | Sen. Every | | ✓ |
| Sen. Cook | | ✓ | | | |
| Sen. Tollefson | | ✓ | | | |
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Total (Yes) 0 No 6

Absent 0

Floor Assignment _____

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

March 18, 2005

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1522

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products; and to declare an emergency.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual;
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
 - (2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company; and
 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order.
3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.
4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.

5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
 - (2) Have an individual of legal minimum purchase age sign for delivery of the package; and
 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

51-30-03. E-mail addresses. Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses.

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. Before making delivery sales or shipping cigarettes in connection with those sales, every person shall file with the tax commissioner a statement setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.
2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:

- a. The name and address of the individual to whom the delivery sale was made;
- b. The brand or brands of the cigarettes that were sold in the delivery sale; and
- c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person.

SECTION 2. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

Date: 3.21.05
Roll Call Vote #: 3

2005 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. *HB 1522*

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| Senate | Finance and Taxation | Committee |
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☐ Check here for Conference Committee

Legislative Council Amendment Number 0202

Action Taken Adopt 0202

Motion Made By Cook Seconded By Wardner

[illegible]

Total (Yes) 6 No 0

Absent 0

Floor Assignment

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

Date: 3-21-05
Roll Call Vote #: 3

2005 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1522

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Pass As Amended & Refer to Appropri's.

Motion Made By Cook Seconded By Wardner

| Senators | Yes | No | Senators | Yes | No |
|----------------|-----|----|--------------|-----|----|
| Sen. Urlacher | ✓ | | Sen. Bercier | ✓ | |
| Sen. Wardner | ✓ | | Sen. Every | ✓ | |
| Sen. Cook | ✓ | | | | |
| Sen. Tollefson | ✓ | | | | |
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Total (Yes) 6 No 0

Absent 0

Floor Assignment Bercier

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

REPORT OF STANDING COMMITTEE

HB 1522, as engrossed: Finance and Taxation Committee (Sen. Urlacher, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** and **BE REREFERRED** to the **Appropriations Committee** (6 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1522 was placed on the Sixth order on the calendar.

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products; and to declare an emergency.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual;
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
 - (2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company; and
 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order.
3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.

4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.
5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
 - (2) Have an individual of legal minimum purchase age sign for delivery of the package; and
 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

51-30-03. E-mail addresses. Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses.

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. Before making delivery sales or shipping cigarettes in connection with those sales, every person shall file with the tax commissioner a statement

setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.

2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:
 - a. The name and address of the individual to whom the delivery sale was made;
 - b. The brand or brands of the cigarettes that were sold in the delivery sale; and
 - c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person.

SECTION 2. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

2005 HOUSE HUMAN SERVICES

CONFERENCE COMMITTEE

HB 1522

2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. **HB 1522**

House ~~Human~~ Services Committee

☒ Conference Committee XX

Hearing Date **April 11, 2005**

| Tape Number | Side A | Side B | Meter # |
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| Committee Clerk Signature <i>Janice Stein</i> | | | |

Minutes:

REP. ROBIN WEISZ, CHAIRMAN Called the conference committee meeting to order.

Asked the Senators for the rationale for putting back the internet

SEN. COOK Gave an explanation of what happened on the Senate side. He stated they were in the process of killing the bill, and at the same time, the Attorney General had a meeting with the state AG officers and came back from that meeting and strongly suggested that we at least, put into the bill these provisions you see here. What you see is just the interest provisions.

REP. PRICE Asked if it was identical to the language the Attorney General asked to have taken out on the House side?

SEN. COOK Didn't know. He said it may very well be, he said they didn't see the language when the bill came to the Senate side. Maybe he went to that meeting and had a change of heart. I don't want to speak for him. I think his concerns were that, people who would ship this product to a potential youth buyer, of cigarettes or tobacco, and that there were some changes in UPS and

some agreements that were taking part in the shipping industry, that all of a sudden, may have impacted his change of heart.

REP. PRICE Stated she thought it was the US Postal Service, you cannot interfere with the US Postal Service delivery route.

SEN. COOK Stated those are questions that should be asked of the Attorney General.

JAN OLSON, ATTORNEY GENERAL'S OFFICE Stated he visited with the Attorney General this morning. He stated he would be glad to answer questions, he spoke for the Attorney General at the hearing in the Senate. A couple of things did happen, when the National Association of Attorney General's met, they eliminated their concern about the master settlement agreement. In terms of what has happened in the industry, UPS and others are getting on board in terms of not handling tobacco, but more importantly, a recent announcement by major credit card companies in conjunction with the federal alcohol, tobacco and firearm provision, they decided they weren't going to handle tobacco sales anymore. A combination of all of that, precipitated the Attorney General's strong support of the internet provision. It was his idea to even put the emergency clause on the bill.

REP. WEISZ Asked what the issue was with the master settlement agreement.

JAN OLSON Stated, from our standpoint, there never was an issue, from their standpoint, the comfort of other Attorneys General, were proliferating with language. South Dakota just passed a law and their governor signed it, which is more harsh then ours, in terms of penalties. It is taking place accross the country right now, but no one will solve the problem. The fact that the law is there, puts some pressure on.

SEN. BERCIER Asked how would you regulate that?

REP. WEISZ Stated being in possession of tax free cigarettes, isn't against the law.

SEN. BERCIER Would this be the principal if the tribe were to take an opposite position and took the state to court over it?

REP. WEISZ North Dakota residents have to pay the tax, they are obligated to pay the tax, not the reservation.

SEN. BERCIER What made it legal up to this point, and now all of a sudden, it makes it illegal? This one carton, was legal, when did that start?

REP. PRICE Answered, what we are looking at is, what is the difference if it is five cartons or one carton, if you are a resident of Fargo and not a member of any tribe, you go up and buy cigarettes, you still are a North Dakota citizen, you are supposed to pay those taxes, whether you get them over the internet or any other place. You bought something that North Dakota State law says, there is a tax.

SEN. COOK If I went to the reservation and bought a carton of cigarettes, would they be required to collect and remit that tax, or would I be required to go and remit the tax?

REP. PRICE We know people are doing that, we don't know how much it is happening, are they supposed to pay the tax, we won't change how they are doing business, there won't be a policeman standing at the border of the reservation. It is to send a message to the citizens that it is not right to send your neighbor up to buy for you, we are supposed to pay taxes on the cigarettes.

GARY ANDERSON, STATE TAX DEPARTMENT Under the sales tax law, you purchased a product and you have not been subject to tax for consumption in North Dakota, you would remit the tax voluntarily, we have a form which allows you to do so. With the one carton, if you

went to the reservation and purchased one carton of cigarettes, there is no reporting responsibility because that is what the law says, if you purchased five cartons, you should be reporting that.

SEN. COOK Stated they started their discussion on the Senate side regarding the degree of cigarettes being sold on the reservation which there weren't taxes being collected for, as they listened to testimony, the degree to which they thought it was happening, was greatly diminished. They reviewed two different sets of records one from the tax department and one shipping cigarettes into North Dakota, we came to the conclusion that, we don't have a big problem with tobacco tax not being collected. It is probably due to the fact that our taxes aren't as high as other states.

REP. PRICE Stated they saw a lot of different numbers too, and the philosophy that they took, was it is something that is a concern to the state of North Dakota. It is more of a forward looking thing. It is more of a message, it will not be more enforcement.

REP. WEISZ Stated it is more of an awareness issue.

WAYNE STENJHEM, ATTORNEY GENERAL Gave his concern. One of the things that the Attorneys General are responsible for is what is called "diligent enforcement" of escrow money of those companies that are not part of the original master settlement agreement. The group that were part of the settlement agreement, are very careful to make sure that we are making those other companies who didn't join the settlement, pay what they are supposed to pay. If we don't do that, we risk losing some or all of the monies that were due from these companies that did sign the original agreement. That was my concern, then I went off to the National Association of Attorneys General meeting, and at one of these sessions that we always had, on issues relating to the tobacco settlement, and I asked the question specifically and repeatedly, if

we adopt a bill regulating internet sales, are we ever going to get into a possible argument from the original participating members that we are not diligently enforcing, they assured me the answer was "no". You can adopt this provision and it will not create any kind of a problem.

Several other states have adopted this kind of language. Most of the major credit card companies have agreed they will not permit the use of credit cards for the purchase of cigarettes. I support this bill as it is now.

REP. PRICE Has there been any movement on the postal service delivering?

WAYNE STENJHEM I can't answer that specifically, I know they have been visiting with the postal service as well, but we don't have an agreement with them.

SEN. BERCIER Has there been a big problem of illegal trafficking of tobacco sales in the state of North Dakota?

WAYNE STENJHEM I wouldn't have that answer, possibly the state tax department would. There are problems in other states.

SEN. BERCIER How enforceable is this, how are we going to know if someone has three cartons of cigarettes?

WAYNE STENJHEM What I suspect would likely happen, we would probably work with other Attorneys General offices, taking action against a specific company where we can all join up, work together, and go after them.

The meeting was adjourned.


2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1522

House Human Services Committee

☐ Conference Committee

Hearing Date 4/12/05

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Minutes: 6 members present.

Rep. Weisz: Called the meeting to order. Attendance was taken. We have a quorum. We left off at the last meeting discussing the Internet section. We have the Attorney General here.

Sen. Urlacher: On the Internet.

Rep. Weisz: Yes, it would be section 1.

Sen. Cook: I am comfortable with the Internet language.

Rep. Weisz: How comfortable are you at putting the language back in. We took it out at the request of the AG and now he wants identical language back in again. And it appears that it is identical to what we took out. There doesn't seem to be any opposition on that, I guess we're only really left with the language that, the exemption for the single carton.

Sen. Bercier: Where in this bill, are we looking at .0300.

Rep. Weisz: .0300 is the Senate version. If you're questioning on that carton, in the House amendments, if you just have a copy of the House amendments, .0200, we took out the section

where it says that this tax does not apply to the use or storage of cigarettes in quantities of 200 or less. So that, in reality, is the carton of cigarette language, and then, of course, in your bill, that language was back in. Seeing you're not referenced 57.36 for any other reason, it just doesn't show up in the bill now. So it's just back to current law that's in your version. But in the House, that's what we did, on 57-36.27.3, we took out that language which would eliminate the exemption for one carton.

Rep. Price: The House position was that they would really like to see that exemption go away. There's really been no argument given for the need for a tax-free carton of cigarettes, it does not affect the tribal members or the reservation residents. They can still buy their cigarette at whatever, tax free if that's the tribe's choice. It's really for non-reservation and non-tribal members. Nobody is going to be sitting at the end of the reservation, nobody is going to be running around doing anything different than right now, obviously. I do see, however, that the Council says that it has a positive cash-flow for us of \$116,000. I don't know if that would be a volunteer type thing, obviously. Just like any of the other, above one carton is right now. The whole issue on it, has been that we don't really know exactly how many, we've got numbers on the cartons available for sale on the reservations, less what they are considering being consumed. How many packets a year they are taking a look at, if you look at what their carton numbers are from the first e-mail versus the fiscal note, there's definitely a difference between there. So it's a real fluid topic. But I guess I'm looking as much, to say I don't care whether you buy your tax-free products anywhere, if it's office supplies over the Internet or whatever, as a North Dakota resident, off the reservation, you're supposed to pay tax. That's our position.

Sen. Bercier: I know we are allowed exemptions for a lot of things, duty-free things. You pay it and then get a rebate. You get reimbursed. I just don't see how in the world, you put a law into effect that's probably never going to be enforced, and if you did work at enforcement, the cost of trying to buy two cartons of cigarettes, in this large state of ours, the cost of enforcing it is going to far outweigh the tax that you would collect, on even 50 cartons of cigarettes. Even the penalty wouldn't pay for the cost of enforcing cigarettes, when we've got meth and all these other problems. Not that cigarette smoking is all that healthy. I was a smoker at one time myself. It's hard to justify a law that is unenforceable. There was a mention made yesterday of the possibility of a casino coming up in a city in the state. I have no idea where that's going. I guess that's a possibility, but I don't, the probability may be way down the road; so anticipating an issue and legislating for the anticipation of a problem is not a good idea. I guess those are my general comments or remarks on this. The exemption, we have exemptions for a lot of things, many things, oil, tax, gas, coal, sales of merchandise, machinery, the carton of cigarettes, is it healthy, I don't agree with it. I don't think smoking is healthy, but at the same time, there are folks that do enjoy smoking. With regard to the law and enforcement and I guess in principal, on the other side to fairness, the exemptions are already in place for other things, and one carton of cigarettes, I don't know how many people will go in and turn in that second carton.

Rep. Weisz: I was just going to address the enforcement, if that's the logic, then why have anything in at all, because if you can't enforce one carton, you can't enforce one, or five or ten, you could make the argument then we don't care what you purchase at the time. It's not a matter of exemption, some things we charge sales tax on, and some things we don't. We charge sales tax, we charge cigarette excise tax on cigarettes. So the argument is why should any be exempt

to a non-reservation member. So that's what I think the House was looking at, 1) it's a conflicting message that some are exempt and some aren't, and we obviously don't plan to open it up just because law enforcement isn't able to enforce it, or it isn't cost effective. I don't think anyone has plans to say, let them buy as many packs as they want, over the Internet or wherever, why should we even bother.

Rep. Price: That was some of the things I was going to say, what's the difference just between one carton or unlimited tax-free. I don't necessarily think that, in fairness to the retailers who do collect the tax, that we should necessarily be allowing duty-free anywhere. I don't care if it's from Canada or South Dakota, or whatever. We also have responsibilities to our retailers, to have a fair playing field for them. That's one of the reasons the stamping piece was done on this bill, out of fairness to the retailers. We weren't ready to put the money in to reimburse them for the cost of going to the stamping. That was part of what we did as a compromise, that we would take away this one exemption, and it just kind of gives them a little bit more of level playing field, it doesn't affect the tribal members, we're not taking away their exemption. If the tribes don't choose to charge them tax, they're tax-free. But it's for the non-tribal members of our state, or any other state, who chooses to buy cigarettes there, we're trying to make it the same as any other product, we say if you're buying it, it's a tax product, it shouldn't matter whether you buy one combine or 20 combines, one carton of cigarettes or 20. Let's make it the same.

Sen. Urlacher: I don't think it is enforceable, but yet I see some value in being consistent, and providing the message that, even though we aren't consistent in a lot of ways, by a long shot, but is that to say we shouldn't start.

Sen. Cook: First off, regarding being consistent, if we want to start somewhere, maybe we should start by listing all the places, we're not. We're not going to start at all of them at the same time, but if we get focused on tobacco sales here, that I think are being made on the reservation, but how about sales that are being made, and you touched on this Rep. Price, in MN, MT, across the borders, somebody living in Fargo, they go across to Moorhead, they recognize they need some cigarettes, so they buy a carton. Now they come back home and immediately then, are you saying that they should somehow say, gosh I got to pay tax on these cigarettes in ND now. I look back to how we got this in the first place. Individuals who smoke, they have buying habits. Some people buy a pack at a time, when they need them. Other people, when they realize they need cigarettes, will buy a carton. These are innocent people who have a dirty habit, should we say. That's why I'm sure the 200 cigarettes are there, but that of course, is in a carton. If somebody is going to bootleg, which is why we would want to have a law at all, that we would hope to enforce, if they're bootlegging, they're going to buy a trunkful. That's who we want to be looking after and going after. I don't think we want to, in any way, try to impose some sort of a burden on the individual who came across the border from another state, with a carton of cigarettes in their possession. I don't even know how we could enforce that.

Rep. Price: We have Mr. Anderson here from the Tax Department, but I would assume that would be much like, I buy certain products in Canada. If I pay the Canadian tax or if I choose not to pay the Canadian, the GST and all those kinds of things. If I don't pay it up there, then I pay it down here. I'm assuming there are some of those cross-border things. If I'm in MN and I buy a CD player, and I pay tax on it, I don't think you are required to come across the border and pay it again, it has to do with, if you've gotten it tax-free over there, you've got some responsibilities.

I'm not the tax expert, we've got one here. It's a message, as much as anything, this was just in response to yours. If you want to have Mr. Anderson answer.

Mr. Anderson: Under most laws, there are reciprocity provisions, if you paid tax in another state, we'll recognize the tax payment here. Really the only issue is what is the rate of tax. Most times, it is credit for credit given. When you are talking about, most of our laws are based on state to state. We don't have that same privilege with Canada. If you buy something Canadian, you are subject to their tax. You would continue to be taxed in ND, as well. There is a refund process available for ND resident to Canada and we have reciprocative refund process similar to what they use. Credit for credit reciprocity would generally apply to most taxes in that regard. Cigarette is interesting, there isn't a reciprocity provision. Again, I am assuming that part of the reason it hasn't been, is probably because of what the Senator pointed out, the one carton situation. Again, it would be a matter from an administrative standpoint, whether to just simply recognize the fact that they were purchased in another state, as long as they could prove that they paid taxes on the cigarettes. That would be the issue. The one thing I would point out, our neighboring states have a higher tax rate, and probably the only reason for picking up a carton or two, is because they are traveling through the area. If they need to make a purchase, they probably would, but most times they would probably wait until they were back in ND, which has a lower rate than neighboring states.

Sen. Cook: Somebody from Fargo goes across the river and shops in Moorhead, and they buy a bike. They're going to pay sales tax to the state of MN for buying that bike and that is the state that legally gets the sales tax, because it was purchased in that state. If you take that bike across the river into ND, you are perfectly legal. You are breaking no laws. However, if you go across

Moorhead, and you buy a suit or any piece of clothing, which is tax exempt in MN, you don't pay any sales tax in MN, but the minute you cross the river with that clothing, now you owe ND use tax. There is nobody who pays that use tax. If you order from a store in MN and they ship it to you, with streamline sales tax, if we get that in place, then that store in MN will collect and remit the sales tax to ND. But again, if you go across the river yourself and pick it up, trust me, I walked up to the Tax Commissioner's office to pay the use tax on two pairs of shoes, and I think I was the only one who ever did it.

Rep. Weisz: Why don't we exempt that suit then, because, why should the ND citizen be required to pay ND tax on one suit, if he only buys one suit. What's the difference between that and the carton of cigarettes.

Sen. Cook: It still goes to the enforcement issue though. But we don't allow an exemption for you buying a few clothes in MN, you don't have to worry about it, because we can't enforce it. We say, clothes are a taxable item, if you purchase clothes, you pay tax in ND. We've said that with cigarettes, except now we're going to exempt one carton.

Rep. Weisz: Why don't we exempt one suit of clothes or one pair of shoes, or whatever.

Sen. Cook: The obvious question is you can go across and buy clothes, so you could buy a \$1 item, you could buy a \$500 item and anything in between. Cigarettes, basically the price is pretty constant. A carton of cigarettes is, it's a fairly constant price. Like I said earlier, you look at the way smokers buy their cigarettes. They either buy them one pack at a time or they buy them a carton at a time. I guess this isn't a big issue to me here, it's a good, sweet bill. It deals with one issue and that's Internet sales of tobacco.

Sen. Bercier: Not to belabor it, but I've got two things. One, Rep. Price mentioned that if a non-tribal member went on the reservation, they bought 3 cartons of cigarettes, and then you're saying that the retailer in Belcourt, that person should be collecting the tax on a non-tribal member and then reporting it. Is that correct.

Mr. Anderson: Is it an Indian retailer.

Sen. Bercier: Yes.

Mr. Anderson: The federal government preempts the state from applying or enforcing an Indian retailer on a reservation from collecting ND taxes, whether it be cigarettes or sales tax. There is a preemption of almost all taxes that a tribal retailer would have to collect. A non-Indian retailer, located on the reservation, is subject to ND's laws, with the exception of member customers.

Rep. Price: How did you distinguish between the tribal and non-tribal customer.

Mr. Anderson: That's a good question. When we talked to retailers, to deal with that issue, the most common answer is that they're familiar with the population base within their community and if they don't, they ask for identification. There are tribal enrollment numbers that are provided to tribal members, and that type of information or card can be provided to the retailer. But again, the most common thing we hear is identification. That they know who their neighbors are, they know their customer base.

Rep. Price: Both of those retailers are located on the reservation. Correct.

Mr. Anderson: Correct.

Rep. Price: So now a distinction between whether they are allowed to sell tax-free cigarettes, or how it's owned.

Mr. Anderson: Basically, who owns the store location, correct. If it is an Indian member, tribal member, who is the owner of the facility, the State has no jurisdiction. If it is a non-Indian member, we have jurisdiction, but again, sometimes the problem you have then is our enforcement authority on the reservation, whether we can actually go on the reservation or not. We have a pretty good working relationship with all of the tribes, so we're generally comfortable there.

Rep. Price: Can they sell one carton tax-free to anyone, they're on the reservation.

Mr. Anderson: The non-Indian retailer is not able to purchase tax-free cigarettes. When they purchase from the wholesalers in ND, it is a taxed product already. The only product the ND wholesaler, licensed distributor in ND, whether they are located in ND or not, but they are licensed, the only way they could sell the product, is if it's been taxed to a non-Indian owner. If it is an Indian owner they can sell it tax-free.

Rep. Price: Section 57-36-24, has to do with the seller then, whether...

Mr. Anderson: Yes, we have very few, and on some reservations, I'm not even aware of a non-Indian retailer, we have very few that actually operate on them. The Three Affiliated Tribes does, because it has the situation with New Town, we have more situations occurring. Most of the other reservations, you don't have the frequency of the non-Indian retailer operating.

Sen. Bercier: With regard to that, particularly for a non-tribal person, I know they know the folks in the community, but you know, we've been intermarrying so much, I would challenge you to go back home, or to any of the reservations and pick out an "Indian". I'm pretty noticeable, but there are some in my own family, if my sister walked up to the car, she would be taken for a non-tribal member. Then you get into racial profiling. Who's an Indian and who isn't an Indian.

Somebody is going to end up in court. They're going to say, well I'm being accused of not being an Indian, or I'm being accused of being Indian, and they're not believing me. Of course, we do have enrollment cards, we do have an enrollment number, we're registered. We do have an enrollment card where we can prove we are a member of a federally recognized tribe. There are tribes, tribal members, who are not members of a federally recognized tribe, but these folks do not have the same rights and privileges from the federal government that federally recognized tribes do, at this point.

Mr. Anderson: I can't speak to that.

Sen. Bercier: We don't have that issue in ND. I wouldn't lose sleep over this negotiation. If this is a make or break deal, I'm going to say that I wouldn't lose sleep over letting it go. I just need to make sure that you understood some of what the implications might be, the ramifications to the local business owners, as well as purchaser and folks coming around who all of a sudden find themselves in a position where there's a law now that preempts me from having an extra carton of cigarettes, which I guess their conscious will dictate to them how they'll report or not report the extra carton, or two cartons that they purchased because of them passing through or whatever. This was just for discussion, but there could be some issues that come up.

Rep. Price: This whole discussion on the tribal versus non-tribal retailers interesting, but not really part of the bill. Sen. Cook, if they came in front of our committee, there would be other exemptions gone on the sales tax too. But these, they don't all come in front of our committee.

Sen. Urlacher: We just got to move the tax committee.

Rep. Price: It's a message, I don't think our population realizes. I think their conscience is going to be whether it's to cross into MN to buy that suit of clothes, or that bike over the Internet

or catalog. Everyone is going to have to deal with it the way they want to. I'm just interested in being a little bit more consistent, and it's like, if you purchased them and you're non-tribal, take a pack.

Sen. Urlacher: I'm not worried about that carton, or two cartons. I guess when there's a truckload coming over, or a trunk load, maybe we would be in a better position to enforce a tax collection when it was possible to enforce. But recognizing that if there was a major movement or a block, there might be some advantage.

Sen. Cook: You're talking about putting that back in, about the carton of cigarettes.

Rep. Price: We'll have both pieces, we'll have the Internet language and do away with these exemptions.

Sen. Bercier: That one carton is not going to be a big enough issue to overshadow the Internet sales. I don't have a copy of it, if you want to put the words in, I'll make the motion.

Rep. Weisz: It would be for the Senate to recede from their amendments and to amend, and then that would be the language that you adopted on the Internet bill.

Rep. Price: And our language.

Rep. Weisz: No, because our language is already in there.

Rep. Price: That's right.

Rep. Weisz: So that's what we have to do to get it in there. Because our language is already in the bill, all we have to do is add the amendments the Senate put in. The Internet language goes back in that was in the original bill and was adopted by the Senate.

Sen. Cook: Why don't you just get all those printed up and then we come back down here and call a meeting.

Rep. Price: Both of these pieces would be in, .0102 and .0202. Correct.

Rep. Weisz: Was there a second to that.

Sen. Cook: We'll make the motion for that.

Rep. Weisz: We'll get them drafted and then reschedule.

Sen. Bercier: I will withdraw my motion.

Rep. Weisz: So everybody is clear, the language on .0102 at the end and the language on .0202 be put in there. What you put in there and the repeal of the exemption. We're adding all that, not hoghousing it. Committee is adjourned.

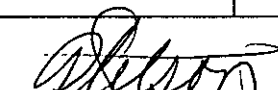
2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1522

House Human Services Committee

☒ Conference Committee

Hearing Date 4/13/05

| Tape Number | Side A | Side B | Meter # |
|---|--------|--------|-----------|
| 1 | xx | | 0-0.2 |
| 1 | xx | | 30.4-33.2 |
| Committee Clerk Signature  | | | |

Minutes: Attendance was taken: 5 members present, 1 member absent (Rep. Sandvig).

Rep. Weisz: Called the meeting to order. We have a quorum. Committee, you have a set of amendments, in front of you that I believe, say what it was we had agreed to this morning. We'll give everybody a chance to look them over.

Rep. Price: Just so we're all clear then, we're taking the House version of the bill, which had the repeal of the exemption of one carton, and we're adding to it, the Internet sales to minors, that the Senate put in the bill. So we'll have both pieces if we make this motion.

Rep. Weisz: That is correct, that is what this amendment will do, it will retain the House version, and add the Internet language that the Senate put in.

Sen. Bercier: The only reason it's got extra pages, is because it's printed bigger.

Rep. Weisz: Correct, I double-checked the language, it is identical to what you had adopted.

Rep. Price: Yes, it's Senate recede and amend as follows. So we go back to the House version and amend on the Senate version.

Page 2
House Human Services Committee
Bill/Resolution Number HB 1522
Hearing Date 4/13/05

Sen. Bercier: I move the Senate recede, and adopt amendments.

Sen. Cook: Seconded.

Rep. Weisz: Any further discussion. The clerk will call the vote.

5 YES 0 NO 1 ABSENT MOTION CARRIED.

SENATE WILL RECEDE AND ADOPT AMENDMENTS.

Rep. Weisz: Thank you. The committee is dissolved.

That the Senate recede from its amendments as printed on pages 1260-1262 of the House Journal and pages 953-955 of the Senate Journal and that Engrossed House Bill No. 1522 be amended as follows:

Page 1, line 1, after "to" insert "create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products;"

Page 1, line 2, after "tax" insert "; and to declare an emergency"

Page 1, after line 3, insert:

"SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:

a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual;

b. A signed statement from the individual providing a certification that the individual:

(1) Is a smoker of legal minimum purchase age in the state;

(2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company;
and

(3) Understands that providing false information may constitute a violation of law.

2. Before mailing or shipping the product, the person:

a. Verifies the date of birth or age of the individual against a commercially available data base; or

b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order.

3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.

4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.

Page No. 1 58311.0202

5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:

(1) Be the addressee;

(2) Have an individual of legal minimum purchase age sign for delivery of the package; and

(3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.

b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.

6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

51-30-03. E-mail addresses. Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses.

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;

2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;

3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and

4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. Before making delivery sales or shipping cigarettes in connection with those sales, every person shall file with the tax commissioner a statement setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.

2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:

a. The name and address of the individual to whom the delivery sale was made;

b. The brand or brands of the cigarettes that were sold in the delivery sale; and

c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.

2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.

3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.

4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.

5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person."

Page 1, line 4, replace "1." with "2."

Page 2, after line 11, insert:

"SECTION 3. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1522

That the Senate recede from its amendments as printed on pages 1260-1262 of the House Journal and pages 953-955 of the Senate Journal and that Engrossed House Bill No. 1522 be amended as follows:

Page 1, line 1, after "to" insert "create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products; to"

Page 1, line 2, after "tax" insert ^{*to provide a penalty;*} "; and to declare an emergency"

Page 1, after line 3, insert:

"SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual; and
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
 - (2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company; and
 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order. *individual*
3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.

4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.
5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
 - (2) Have an individual of legal minimum purchase age sign for delivery of the package; and
 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

^a **51-30-03. E-mail addresses.** Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses ^{for the purchaser}

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. ^a Before making delivery sales or shipping cigarettes in connection with these sales, every person shall file with the tax commissioner a statement setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.
2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale

during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:

- a. The name and address of the individual to whom the delivery sale was made;
- b. The brand or brands of the cigarettes that were sold in the delivery sale; and
- c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person."

Page 2, after line 11, insert:

"SECTION 3. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

REPORT OF CONFERENCE COMMITTEE
(ACCEDE/RECEDE)

Bill Number HB 1522 (, as (re)engrossed):

Date: 4-13-05

Your Conference Committee Human Services

For the Senate:

For the House:

| | YES / NO | | | YES / NO | |
|--------------|----------|--|--------------|----------|--|
| Sen Cook | ✓ | | Chm. Willis | ✓ | |
| Sen Unlacker | ✓ | | Rep Price | ✓ | |
| Sen Bersier | ✓ | | Rep Sandberg | ✓ | |

recommends that the (SENATE/HOUSE) (ACCEDE to) (RECEDE from)

the (Senate/House) amendments on (SJ/HJ) page(s) 1240 -- 1262

_____, and place _____ on the Seventh order.

✓, adopt (further) amendments as follows, and place HB 1522 on the Seventh order:

_____, having been unable to agree, recommends that the committee be discharged and a new committee be appointed.

((Re)Engrossed) HB 1522 was placed on the Seventh order of business on the calendar.

DATE: 4/13/05

CARRIER: Rep Willis

| | |
|-----------------------------------|----------------|
| LC NO. <u>58311.0204</u> | of amendment |
| LC NO. | of engrossment |
| Emergency clause added or deleted | |
| Statement of purpose of amendment | |

MOTION MADE BY: Sen Bersier

SECONDED BY: Sen Cook

VOTE COUNT 4 YES 0 NO 0 ABSENT

Revised 4/1/05

REPORT OF CONFERENCE COMMITTEE

HB 1522, as engrossed: Your conference committee (Sens. Cook, Urlacher, Bercier and Reps. Weisz, Price, Sandvig) recommends that the **SENATE RECEDE** from the Senate amendments on HJ pages 1260-1262, adopt amendments as follows, and place HB 1522 on the Seventh order:

That the Senate recede from its amendments as printed on pages 1260-1262 of the House Journal and pages 953-955 of the Senate Journal and that Engrossed House Bill No. 1522 be amended as follows:

Page 1, line 1, after "to" insert "create and enact chapter 51-30 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products; to"

Page 1, line 2, after "tax" insert "; to provide a penalty; and to declare an emergency"

Page 1, after line 3, insert:

"SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

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1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual; and
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
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 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the individual placing the order.

3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.
4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.
5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
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 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

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51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

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2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:
 - a. The name and address of the individual to whom the delivery sale was made;
 - b. The brand of the cigarettes that were sold in the delivery sale; and
 - c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain a violation of this chapter by any person."

Page 2, after line 11, insert:

"SECTION 3. EMERGENCY. This Act is declared to be an emergency measure."

Renumber accordingly

Engrossed HB 1522 was placed on the Seventh order of business on the calendar.

2005 TESTIMONY

HB 1522

2

TESTIMONY BEFORE THE NORTH DAKOTA
HOUSE HUMAN SERVICES COMMITTEE
IN SUPPORT OF HOUSE BILL NO. 1522

JANUARY 26, 2005

Madam Chairman, members of the committee, good morning. My name is Christopher Beard, and I am a Public Policy Manager working with the Brand Integrity Department of Philip Morris USA. Thank you for giving me this opportunity to present our views in support of House Bill 1522. This legislation offers the State of North Dakota an important opportunity to help disrupt and reduce illegal activity related to cigarette sales.

I've come here today because contraband cigarettes- an umbrella term we use to define various types of illegal activity related to cigarettes - are a growing problem in this country, and a growing problem for our business that we take very seriously.

Philip Morris USA believes House Bill 1522 will benefit the State of North Dakota in several ways. Specifically, HB 1522 will help to disrupt and reduce the trade in contraband cigarettes in North Dakota. It will make it more difficult for minors residing in North Dakota to purchase cigarettes thereby furthering North Dakota's efforts to prevent youth smoking. Finally it will make it more difficult for smokers to avoid excise tax payments and ensure that all applicable taxes are collected, thereby increasing the amount of excise tax revenues North Dakota collects.

My testimony is designed to provide you with some context as to why this bill is necessary and why it is necessary now. I will provide some background on the contraband problem, who it impacts, and why this legislation is a critical part of the solution.

January 26, 2005



We think it is important to first provide background on recent changes in the cigarette industry and the existing industry environment. In recent years there have been dramatic increases across the country in state cigarette excise taxes. Such increases have created incentives for adult 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 contributed to an increase in illegally sold or "contraband" cigarettes, as well as an increase in Internet cigarette sales that often occur without the proper payment of excise taxes or mandatory escrow payments, without effective age verification, and in violation of trademark and other laws.

House Bill 1522 would help prevent contraband cigarette sales. There are three types of contraband cigarettes that this bill would help address:

- Untaxed and under-taxed cigarettes, which are genuine cigarettes intended for sale typically in a low tax state, but illegally sold often in states and localities with higher excise taxes, over the Internet or through direct mail. Untaxed cigarettes also include those cigarettes sold without a tax stamp or with an altered or counterfeit tax stamp.
- Counterfeit cigarettes, which are not of the same quality as genuine cigarettes, but are difficult to identify before consumption because the external packaging is very similar to legitimate product.
- Illegally imported cigarettes, which are intended for sale outside the United States but which are sold illegally in the United States.



According to the U.S. Customs Service, the number of seizures of counterfeit cigarettes for trademark infringement has jumped significantly in the last few years. U.S. Customs and Border Protection valued the cigarettes they seized in FY 2004 at \$24.2 million. By contrast, in FY 2001, U.S. Customs and Border Protection had valued the cigarettes similarly seized at only \$4.5 million.¹

Philip Morris USA has already identified the existence of counterfeit cigarettes at retail in 19 states, with suspected counterfeit cigarettes in 23 more. Most counterfeit cigarette packs also carry counterfeit tax stamps, if they have a tax stamp at all.

Illegal sales negatively impact Philip Morris USA trademarks, as adult smokers may unknowingly purchase substandard, counterfeit cigarettes that they believe are authentic. This tarnishes our trademarks and brand reputations. It also distorts the legitimate market, hurting those legitimately engaged in the trade, including businesses located here in North Dakota.

Illegal cigarette sales harm not only Philip Morris USA, but also the State of North Dakota in the form of increased crime and lost revenue that, if collected, could help ensure that North Dakota is collecting the tax revenue to which it is entitled. In a 2002 report, the General Accounting Office 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).) Additionally, these illegal sales could lead to reduced payments for the State of North Dakota under the tobacco settlement agreement.

¹http://www.cbp.gov/ImageCache/cgov/content/import/communications_5fto_5frade/statistics/fy01pub_2epdf/v1/fy01pub.pdf (last accessed 4/15/04)



Illegal cigarette sales also hurt law-abiding businesses, including wholesalers, retailers and manufacturers that are competing against those that have unfair economic advantages due to illegal activity – for example, Internet sites that don't collect State excise taxes.

While online sales currently represent a small percentage of total cigarette sales, there are currently more than 1,500 web sites selling cigarettes. The cost to states in lost revenue is significant. One report cited by the U.S. General Accounting Office estimates that Internet tobacco sales alone will cost the States \$1.4 billion in tax revenue in 2005. (See Online Tobacco Sales Grow, States Lose, Forrester Research, Inc. (April 27, 2001); "Internet Cigarette Sales," U.S. General Accounting Office, August 2002.) Other observers believe that the cost to the States could reach \$4 billion by 2005. (See Testimony of Patrick Fleenor, Chief Economist Fiscal Economics Inc., before the Subcommittee on Courts, the Internet and Intellectual Property, Committee on the Judiciary, House of Representatives (May 1, 2003)). According to the U.S. General Accounting Office, three-quarters of all Internet tobacco sellers explicitly say that they will not report cigarette sales to tax collection officials and moreover, Internet sites often mislead consumers into violating State excise tax laws by claiming to be exempt from the Jenkins Act regulations. (See *e.g.* GAO Report: Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement (August 2002)).

Philip Morris USA takes the issue of illegal cigarette sales very seriously, and we have been making significant efforts to disrupt and reduce these illegal sales. We have been working closely with law enforcement at the federal and state level to support their efforts to address contraband by enforcing the laws already on the books. Additionally, under existing laws that give us certain



legal rights, such as trademark laws, we have filed lawsuits against those who are trafficking in contraband. To date these lawsuits have involved more than 2800 retailers, 4 wholesalers, and 18 internet operators. The existing laws in place to address contraband cigarette sales need to be expanded and toughened.

That is why House Bill 1522 is needed and why we are pleased to support it. We commend Representatives Carlson and Price and in the Senate, Senator Wardner, for their leadership in putting forth legislation that, if enacted and enforced, would help disrupt and reduce illegal cigarette sales.

House Bill 1522 would help address these serious issues by providing better tools for law enforcement officials to eliminate contraband cigarettes, and help ensure that all industry participants comply with the requirements governing the legitimate distribution and sale of cigarettes. The bill would, among other things:

- Ensure that only licensed distributors would be able to purchase and sell cigarettes.
- Require tax indicia on each pack of cigarettes sold in the state. The indicia can only affixed by licensed distributors.
- 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.
- Address the issues of inadequate age verification and non-payment of appropriate taxes, by imposing comprehensive new restrictions, including; age verification requirements, fiscal compliance measures,



penalties and enforcement mechanisms on sales of cigarettes to consumers via the Internet. These provisions would help in reducing tax evasion and in limiting the access of youth to cigarettes.

Conclusion

Contraband cigarette trafficking including tax-evasive Internet and Direct Mail Sales continue to present challenges for the domestic cigarette industry, and, as states raise excise taxes, the incidences of these problems likely will increase. North Dakota has an opportunity to play a key role in addressing an issue that negatively impacts not only compliant cigarette manufacturers, their trade partners and consumers, but also the government and its revenue collection efforts.

The issue of illegal cigarette sales is one that Philip Morris USA takes very seriously, and we are committed to working with the State of North Dakota to help stop this growing problem. While Philip Morris USA will look to work with law enforcement in North Dakota and elsewhere in order to provide information and support to 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 1522 is a significant step toward solving this issue. We urge you to support it.

Thank you.



TESTIMONY BEFORE THE HOUSE
HUMAN SERVICES COMMITTEE

HB 1522

Prepared by John Quinlan

January 26, 2005

Madam Chairman and members of the House Human Services Committee, my name is John Quinlan. I oversee the administration of the North Dakota Tobacco Products Tax Law for the Office of State Tax Commissioner.

Before addressing Section 1, I would like to first address Section 2 through Section 12 of House Bill 1522. These sections provide for the implementation of a cigarette tax stamp program in North Dakota. North Dakota is one of three states that currently does not apply a tax stamp on cigarettes. North Carolina and South Carolina are the other two states.

North Dakota did require a cigarette tax stamp program until 1991, at which time the requirement was repealed. This change resulted, in part, because the supplier of the stamping equipment discontinued the manufacture and support for their equipment. Instead of having distributors incur additional expense for new equipment; the decision was made by the legislature to remove the stamping requirement.

Since that time the Office of State Tax Commissioner has monitored the sales of cigarettes in North Dakota for possible tax avoidance. In response to these efforts, the Office of State Tax Commissioner has not encountered

smuggling activities in its compliance and enforcement efforts nor received complaints or information from cigarette manufacturers, from North Dakota cigarette distributors, from main-street businesses, from consumers in this state, or from the Federal Bureau of Alcohol, Tobacco, and Firearms, or the U.S. customs Office to support the fact that smuggling activities exist in North Dakota.

A tax stamp program does increase the enforcement challenges. With a tax stamp program, the importance of field reviews intensifies. For example, Philip Morris' website notes the existence of "ever-increasing problem of counterfeit product and counterfeit tax stamps." They cite an estimate of 100 billion counterfeit cigarettes being manufactured in China annually, and the difficulty industry and states share in identifying these products. They also speak to the expertise of these counterfeiters to copy a state's tax stamps.

Our office agrees a cigarette tax stamp program represents a vehicle to control cigarettes smuggling. However, states that are often identified as having smuggling problems are states having high cigarette tax rates, higher population bases or both; such as New Jersey (\$2.05), New York (\$1.50), Washington (\$1.425), Oregon (\$1.28), Michigan (\$1.25) and California (\$.87).

North Carolina (\$.05) and South Carolina (\$.07) have tax rates so low that smuggling is not an issue. North Dakota's tax rate (\$.44) continues to be lower than our

neighboring states, and represents a state having a small population base.

| | |
|--------------|-------------|
| North Dakota | \$.44/pack |
| Minnesota | \$.48/pack |
| South Dakota | \$.53/pack |
| Montana | \$1.70/pack |

Purchases of untaxed cigarettes do occur in North Dakota. Cigarettes sales occurring on Indian reservations and military locations are not subject to the state's cigarette taxes. Congress has provided sovereign rights to all sales occurring on an Indian reservation by Indian retailers or the tribe. Federal law provides a similar preemption of state taxes on sales that occur on military locations to active military, North Dakota National Guard members, and retired military personnel.

Despite the stamping requirement proposed by House Bill 1522, cigarettes purchased by Indian retailers located on Indian reservation from licensed distributors will not be subject to the state cigarette tax. We can, as we did years ago, require North Dakota cigarette distributors to place a special untaxed stamp on cigarettes intended for resale by Indian retailers. But we would note that it has recently been brought to our attention by a major distributor in North Dakota that some Indian retailers are purchasing cigarettes from out-of-state suppliers. House Bill 1522 will not provide authority to the state to interfere with these transactions or impose stamping requirements on such purchases, as federal law again provides preemption on shipments made in interstate commerce to Indian reservations. Should the state

implement a tax stamp program and require North Dakota licensed cigarette distributors to place a special untaxed stamp on cigarettes sold to an Indian retailer or tribe, the Indian retailer or tribe can simply avoid such purchases by instead legally purchasing all of there cigarette product from unlicensed out-of-state suppliers.

In the case of untaxed cigarettes sold on Indian reservations and military locations, the cigarette tax instead becomes a responsibility to the consumer having possession of these untaxed products to report and pay the state's cigarette tax, which is difficult, if not impossible to enforce. To add to the complexity of this situation, North Dakota Century Code, section 57-36-27, subsection 2, which is not addressed by House Bill 1522 allows a person to have in their possession at anytime one carton (10 packages) of untaxed cigarettes.

We would note that House Bill 1522 attempts to address the issue of untaxed cigarettes in a person's possession, as noted in Section 12, on page 9, lines 30 and 31; and on page 10, lines 1 and 2. This subsection states that a person, such as an active military or National Guard member, having untaxed cigarettes in their possession off a military base, is guilty of an "infraction," which we understand can represent a fine up to \$100. However, our legal counsel has stated that having both the exemption in NDCC 57-36-27 and the penalty provision in Section 12 of House Bill 1522 would generally be viewed as "ambiguous criminal laws that are held invalid by the courts" and as a result would not be enforceable.

We are in support of Section 1 of House Bill 1522. The sale of cigarettes over the Internet has become a significant issue in recent years for many states that have a high cigarette tax rate, high population base, or both. Matthew Myers, President of Campaign for Tobacco-Free Kids, testified before the U.S. House Judiciary Committee in May 1, 2003 stating "very few states have laws that explicitly apply to Internet sellers." Mr. Meyers further states "To be effective, legislation must require that Internet sellers maintain records of their sales for several years prohibit anyone from shipping tobacco products into the state who has not registered and give the state the authority to block the delivery of tobacco products who have not complied with the law." Section 1 speaks to these concerns and we believe would require additional enforcement efforts by our office to insure compliance by Internet sellers.

Several states experiencing significant Internet sales activity have passed legislation similar to that presented in Section 1. In addition, several states have become proactive in their enforcement efforts involving Internet sales. Oregon funds a Tobacco Tax Compliance Task Force made up of representative from various state agencies. The Attorney Generals for California and Washington have pursued civil action to enforce violations against several Internet sellers.

I have provide on page 9, findings from a recent federal Internet investigation of a large Internet seller, which identified a tax loss of \$2,388,021.80.

The Office of State Tax Commissioner has the responsibility to insure compliance with the cigarette tax laws. As noted previously, we continue to monitor the sales of cigarettes in North Dakota to prevent possible tax avoidance. It has always been our position that should actual smuggling activities be identified that we would request the implementation of a tax stamp program.

The requirement to stamp cigarettes as proposed by House Bill 1522

- Will not prevent adults or youth from driving to an Indian reservation for the purpose of purchasing cigarettes or other tobacco products
- Will not prevent the sale of unstamped and untaxed cigarettes on Indian reservations and military locations
- Will not prevent the sale of untaxed cigarettes on Indian reservations to non-members
- Will not prevent non-members from transporting untaxed cigarettes off the reservation for personal consumption
- Will not prevent a person from having in their possession at anytime, one carton of untaxed cigarettes
- Will not reduce the cost of administration, compliance and enforcement

In place of Sections 2 through 12, we suggest the following for your consideration:

- Repeal NDCC 57-36-27(2) that currently allows a person to have in their possession one carton of untaxed cigarettes.
- Require all licensed cigarette retailers to purchase cigarettes only from a licensed distributors
- Promote state-tribal collection agreements that would encourage the application of a tribal cigarette tax
- Promote and encourage cigarette manufacturers, like Philip Morris, to use alternative tracking methods for cigarettes based on new technology in place of stamping programs. Such technology is available, as noted by the radio frequency identification tags that are now available from manufacturers like Alien Technology of Fargo. We believe this technology has the possibility of providing more efficient and reliable solutions to the problems and concerns cited as reasons for House Bill 1522 and those cited in my testimony, such as counterfeit cigarettes and tax stamps. This technology may provide a low cost and yet secure approach to providing confidence in the cigarette market place to manufacturers, distributors, and state policy makers.

In closing, it should be noted that most states have implemented tax stamping programs for more than thirty years. Despite having such programs, most states having larger tax rates, larger population bases or both experience smuggling activities, counterfeit cigarettes, counterfeit tax stamps, and a continued increase in

Internet sales. The fact that all states impose a tax stamp program, with the exception of North Carolina and South Carolina provides North Dakota an opportunity to recognize illegal product without having to discern whether the stamp is in fact North Dakota's, another state's stamp, or a counterfeit product. This also provides opportunities for manufacturers and distributors' representatives, as well as customers, to more easily identify the inadvertent or intentional placement of out-of-state product on North Dakota retailer shelves, thereby sharing in the enforcement efforts completed by our office.

This concludes my testimony. I stand for any questions.

HOUSE BILL 1522 – ATTACHMENT

Testimony by John Quinlan

Office of State Tax Commissioner

Federal Internet Investigation

Affordablecigs.com and Cigoutlet.com

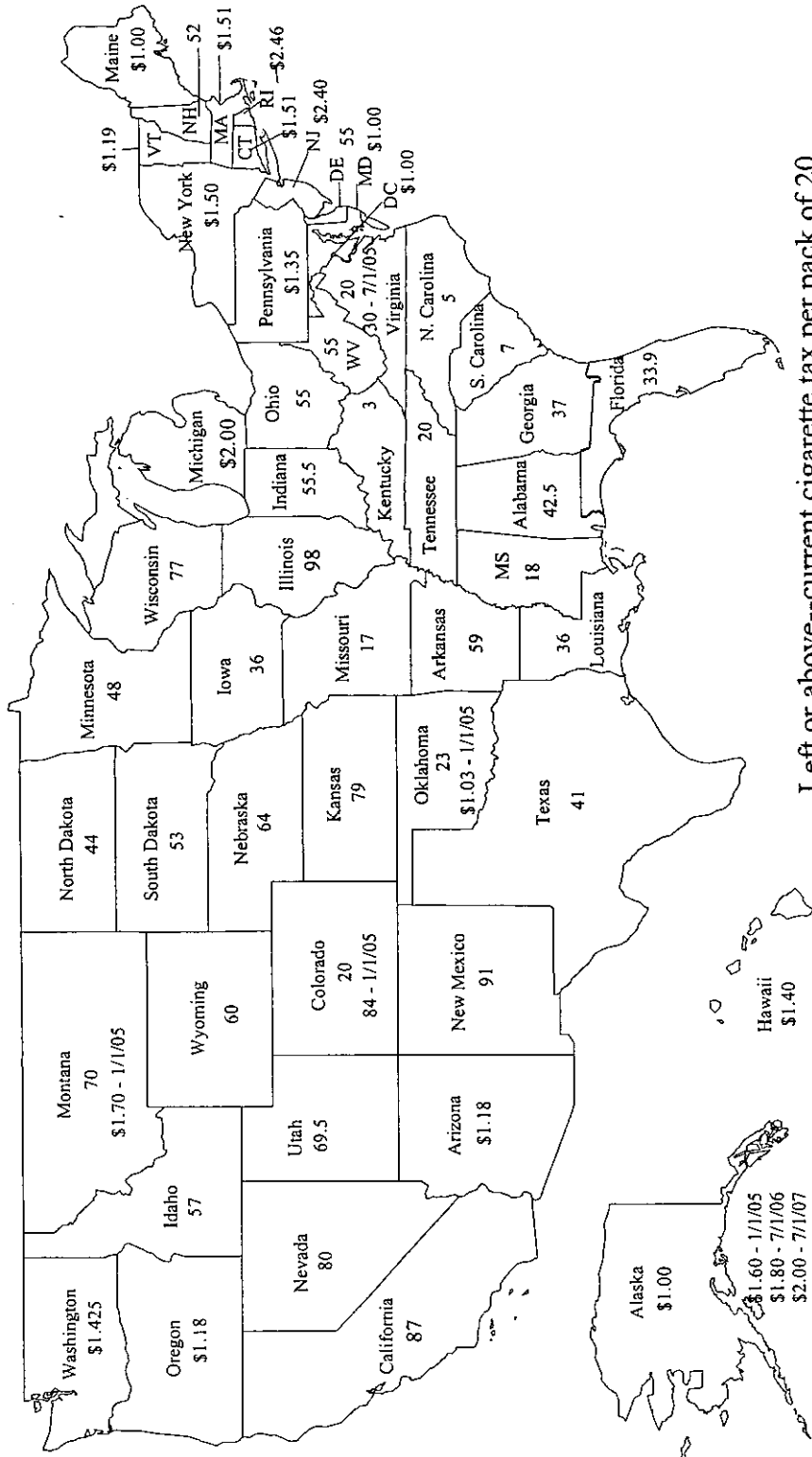
Total Revenue Loss \$2,388,021.80

Period October 1999 – July 2004

Sampling of Findings for States:

| <u>State</u> | <u>Cartons</u> | <u>Tax Rate</u> | <u>\$Loss</u> |
|---------------|----------------|-----------------|---------------|
| New York | 62,759 | 1.50/pack | \$941,385 |
| New Jersey | 21,554 | 2.05 | 441,857 |
| Massachusetts | 7,350 | 1.51 | 110,985 |
| Illinois | 5,591 | .98 | 54,792 |
| Michigan | 3,422 | 2.00 | 42,775 |
| Connecticut | 2,917 | 1.51 | 44,047 |
| Washington | 1,944 | 1.425 | 27,702 |
| ... | | | |
| ... | | | |
| Minnesota | 618 | .48 | \$ 2,966 |
| Montana | 88 | .70 | 616 |
| Colorado | 80 | .20 | 160 |
| Iowa | 41 | .36 | 148 |
| Oklahoma | 15 | .23 | 35 |
| South Dakota | 0 | .53 | 0 |
| North Dakota | 0 | .44 | 0 |

State Cigarette Tax Rate (per pack of 20)



Left or above--current cigarette tax per pack of 20
Right or below--future cigarette tax per pack of 20



Locations at Bismarck and Grand Forks
3500 Burdick Expy. East • P.O. Box 1948 • Minot, North Dakota 58702
Phone 701-857-8300 • Fax 701-857-8307

January 25, 2005

Testimonial; Impact of stamping on distributors

Dear Legislators:

It has come to our attention that a bill has again been introduced to allow for the stamping of cigarettes by wholesale distributors of cigarettes and tobacco products. I would like to address some of the issues that come to mind when considering what enactment of this bill would do for the state of North Dakota and what impact it would have on the distributors operations.

First of all, I could understand the concern if this was proposed by the State Tax Commissioners office over concerns that bootlegging operations are unchecked and millions of tax dollars are being lost to the illicit trade of contraband cigarettes. This simply just isn't the case! I would be more concerned about counterfeit stamping operations giving the impression of legal product given the technology we have today and the potential to reap large rewards in states like Montana with \$17.00 per carton state tax.

I can't see where anyone benefits from the proposed stamping bill but can think of a number of reasons that would affect both the wholesale and retail community negatively. I estimate that it would cost us an additional \$40,000 to \$65,000 per year in labor, equipment leasing and maintenance costs. The requirement that all product be stamped within 72 hours of receipt is simply unrealistic and out date. Many distributors sell product in more than one tax jurisdiction and would create an inventory nightmare trying to maintain pre-stamped inventory for each of those states, not to mention the cash flow implications of maintaining duplicate inventories combined with the fact that the manufactures no longer stand behind stale product returned from the trade. As the proposed bill reads, it would give out of state distributors an unfair advantage in that they are not required to stamp all product received within 72 hours and would be allowed to post stamp after the orders have been picked for shipping.

This bill would also give an unfair advantage to out of state distributors in that it would allow for the interstate transportation of non indicia bearing product leaving the local instate distributor unable to sell product to non taxable entities within the state (intrastate). This was the case prior to 1990 when the Indian Reservations were forced to by from out of state distributors that met the interstate commerce guidelines. This would in turn force us to lay off additional personnel due to the loss of volume to qualifying out of state distributors. We don't need anymore disadvantages to give our customers reason to go out of state!

It's also quite evident that given the dwindling population in western North Dakota and the increased responsibility that would be placed on the Tax Commissioners office in administering the stamping program that less time would be available to police the compliance thus resulting in more lost tax dollars with a stamping law. I think that they have done an outstanding job of administering the law and collecting revenue for the state and fail to see how adding more field inspectors will help them be more cost efficient.

The final issue is a mater of cash flow concern for our company in that it would require us to purchase stamps prior to sale with a potential impact of over \$500,000 due to the additional capital required to prepay opposed to remit tax due by the 15th of each month. Given the drastic changes our suppliers have forced on the wholesale community with reduced terms, increased inventory dollars, and impossible program requirements to qualify for value added services, this could very well be the stick that broke the camels back for one of the states largest collector of tobacco taxes and employer to 85 native North Dakotans! Thank you for your time and consideration given this matter.

Sincerely, Roger Borkhuis, President/CEO, Wholesale Supply Co. Inc.



**Henry J Knoll
Operations Manager
Frank McKone Cigar Co.
742 19th Street North
Fargo, ND 58102
1-701-235-4261**

January 26, 2005

Frank McKone Cigar is in the business of distributing wholesale candy and tobacco products to retail and business outlets.

As a representative of Frank McKone Cigar Co., representing the company as a whole, we oppose HB 1522.

Reasons of opposition:

The additional cost of applying the indicia(stamps) is not addressed anywhere in this bill. We would need another stamping machine to handle the extra stamping load. Another employee would be needed to run the extra stamping machine. The biggest expense for us would be to have to pay for the stamps up front, which would create a nightmare with our cash flow situation.

72 hour stamping provision: This is an unreasonable and costly provision. It would force us to carry duplicate inventories on most of our cigarette inventory. We are presently stamping Minnesota cigarettes. Other wholesalers in the state are servicing 3 to 4 states, and also servicing the Reservations, this would create a bigger problem for those wholesalers.

Stamping Equipment: At this time, Meyercord stamping machines are our only options for applying the indicia(stamps). This equipment is old and outdated. It is difficult to get any kind of consistency applying the stamps with this machine. If we have to bring in additional equipment to handle stamping in North Dakota it will double and triple the amounts of problems we are having with daily stamping and downtime of the machines.

It is my opinion that passage of HB 1522 will create undue financial stress on Frank McKone Cigar and many of the other wholesalers in North Dakota. I suggest you give HB 1522 a DO NOT PASS.

#6

TESTIMONY BEFORE THE HOUSE

HUMAN SERVICES COMMITTEE

HB 1522

Review of Fiscal Note

Section 1: Require one FTE \$100,000**

Sections 2-12:

Require:

| | |
|--------------------------|-----------|
| Stamps | \$ 84,000 |
| Stamp cylinders | 6,000 |
| Delivery expense | 20,000 |
| Computer program rewrite | 30,000 |
| Require two FTEs | 228,000** |

Total Expenditures: \$468,000

**Cost include salary, training, equipment, and travel expenses.

Testimony provided by Gary Anderson
Office of State Tax Commissioner
January 26, 2005

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1522

Page 1, line 1, after "Act" insert "to create and enact chapter 51-30, two new subsections to section 57-36-01, and sections 57-36-08.1, 57-36-10.1, 57-36-11.2, 57-36-12.1, and 57-36-13.1 of the North Dakota Century Code, relating to regulation of sale and delivery of tobacco products and to tobacco tax indicia"; replace "section" with "sections 57-36-02, 57-36-07, 57-36-09, 57-36-18, 57-36-25.1," and after "57-36-27" insert ", and 57-36-33"

Page 1, line 2, after "to" insert "tobacco tax indicia and tobacco" and after "tax" insert "; to provide a penalty; and to provide an effective date"

Page 1, after line 3, insert:

"SECTION 1. Chapter 51-30 of the North Dakota Century Code is created and enacted as follows:

51-30-01. Prohibited acts regarding sale of tobacco products to minors. It is unlawful for any person in the business of selling tobacco products to take an order for a tobacco product, other than from a person who is in the business of selling tobacco products, through the mail or through any telecommunications means, including by telephone, facsimile, or the internet, if in providing for the sale or delivery of the product pursuant to the order, the person mails the product or ships the product by carrier, and the person fails to comply with each of the following procedures:

1. Before mailing or shipping the product, the person receives from the individual who places the order the following:
 - a. A copy of a valid government-issued document that provides the name, address, and date of birth of the individual;
 - b. A signed statement from the individual providing a certification that the individual:
 - (1) Is a smoker of legal minimum purchase age in the state;
 - (2) Has selected an option on the statement as to whether the individual wants to receive mailings from a tobacco company; and
 - (3) Understands that providing false information may constitute a violation of law.
2. Before mailing or shipping the product, the person:
 - a. Verifies the date of birth or age of the individual against a commercially available data base; or
 - b. Obtains a photocopy or other image of the valid, government-issued identification stating the date of birth or age of the person placing the order.

3. Before mailing or shipping the product, the person provides to the prospective purchaser, by electronic mail or other means, a notice that meets the requirements of section 51-30-04.
4. In the case of an order for a product pursuant to an advertisement on the internet, the person receives payment by credit card, debit card, or check for the order before mailing or shipping the product.
5. a. The person employs a method of mailing or shipping the product requiring that the individual purchasing the product:
 - (1) Be the addressee;
 - (2) Have an individual of legal minimum purchase age sign for delivery of the package; and
 - (3) If the individual appears to the carrier making the delivery to be under twenty-seven years of age, take delivery of the package only after producing valid government-issued identification that bears a photograph of the individual, indicates that the individual is not under the legal age to purchase cigarettes, and indicates that the individual is not younger than the age indicated on the government-issued document.
- b. The bill of lading clearly states the requirements in subdivision a and specifies that state law requires compliance with the requirements.
6. The person notifies the carrier for the mailing or shipping, in writing, of the age of the addressee as indicated by the government-issued document.

51-30-02. Rule of construction regarding common carriers. This chapter may not be construed as imposing liability upon any common carrier, or officer or employee of the carrier when acting within the scope of business of the common carrier.

51-30-03. E-mail addresses. Persons taking delivery sale orders may request that prospective purchasers provide their e-mail addresses.

51-30-04. Disclosure requirements. The notice required under subsection 3 of section 51-30-01 must include:

1. A prominent and clearly legible statement that cigarette sales to consumers below the legal minimum age are illegal;
2. A prominent and clearly legible statement that consists of one of the warnings set forth in section 4(a)(1) of the Federal Cigarette Labeling and Advertising Act [15 U.S.C. 1333(a)(1)] rotated on a quarterly basis;
3. A prominent and clearly legible statement that sales of cigarettes are restricted to those consumers who provide verifiable proof of age in accordance with section 51-30-01; and
4. A prominent and clearly legible statement that cigarette sales are subject to tax under sections 57-36-06 and 57-36-32, and an explanation of how the tax has been, or is to be, paid with respect to the delivery sale.

51-30-05. Registration and reporting requirements.

1. Before making delivery sales or shipping cigarettes in connection with those sales, every person shall file with the tax commissioner a statement

setting forth the person's name, trade name, and the address of the person's principal place of business and any other place of business.

2. Not later than the tenth day of each month, each person that has made a delivery sale or shipped or delivered cigarettes in connection with any sale during the previous calendar month shall file with the tax commissioner a memorandum or a copy of the invoice, which provides for each delivery sale:
 - a. The name and address of the individual to whom the delivery sale was made;
 - b. The brand or brands of the cigarettes that were sold in the delivery sale; and
 - c. The quantity of cigarettes that were sold in the delivery sale.

51-30-06. Taxes. Each person accepting a purchase order for a delivery sale of any tobacco product shall remit to the tax commissioner any taxes due under chapter 57-36 with respect to the delivery sale. This section does not apply if the person has obtained proof, in the form of the presence of applicable tax stamps or otherwise, that the taxes already have been paid to this state.

51-30-07. Penalties.

1. Except as otherwise provided in this section, a person that violates this chapter is subject to a fine of not more than one thousand dollars. In the case of a second or subsequent violation of this chapter, the person is subject to a fine of not less than one thousand dollars nor more than five thousand dollars.
2. Any person who knowingly violates any provision of this chapter is guilty of a class C felony.
3. Any individual who knowingly and falsely submits a certification under subdivision a of subsection 5 of section 51-30-01 in another individual's name is guilty of a noncriminal offense and is subject to the penalty provided under subsection 1.
4. Any person that fails to pay any tax required in connection with a delivery sale shall pay, in addition to any other penalty, a penalty of fifty percent of the tax due but unpaid.
5. Any cigarettes sold or attempted to be sold in a delivery sale that does not meet the requirements of this chapter are forfeited to the state and must be destroyed.

51-30-08. Enforcement. The attorney general or any person who holds a permit under 26 U.S.C. 5712 may bring an action in the appropriate court in the state to prevent or restrain violations of this chapter by any person or any person controlling that person.

SECTION 2. Two new subsections to section 57-36-01 of the North Dakota Century Code are created and enacted as follows:

"Delivery sale" means any sale of cigarettes to a consumer in the state if either the purchaser submits the order for such sale by means of a telephonic or other method of voice transmission, the mail or any other delivery service, or the internet or other online service or the cigarettes are delivered by use of the mail or other delivery service. A sale of cigarettes

is a delivery sale regardless of whether the seller is located within or without the state.

"Indicia" means the impression or mark made on the cigarettes or package containing the cigarettes approved by the tax commissioner under sections 57-36-08.1 and 57-36-11.2.

SECTION 3. AMENDMENT. Section 57-36-02 of the North Dakota Century Code is amended and reenacted as follows:

57-36-02. Distributors and dealers to be licensed. Each person engaged in the business of selling cigarettes, cigarette papers, snuff, cigars, or tobacco in this state, including any distributor or dealer, must secure a license from the attorney general before engaging or continuing to engage in business. A separate application and license is required for each distributor at each outlet or place of business within the state, and a separate dealer's license is required for each retail outlet when a person owns or controls more than one place of business dealing in cigarettes, cigarette papers, snuff, cigars, or tobacco. No retailer will be granted a distributor's license except a retailer who, in the usual course of business, performed a distributor's or wholesaler's function for at least one year prior to filing the license application. The application prescribed by the attorney general must include the name and address of the applicant, the address and place of business, the type of business, and other information as required for the proper administration of this chapter. Each application for a wholesale or distributor's outlet license must be accompanied by a fee of twenty-five dollars and a surety bond approved by the attorney general. Each application for a dealer's outlet license must be accompanied by a fee of fifteen dollars. A reinstatement fee of fifty dollars is required in addition to the annual license fee for each license renewal applied for after June thirtieth. The total reinstatement fee may not exceed five hundred dollars for any one licensee in any fiscal year. Indicia under this chapter may be sold to and affixed only in North Dakota by licensed distributors. Licensed dealers may sell, buy, or have in their possession only cigarettes upon which indicia were previously affixed. A distributor's license does not authorize the holder to make retail sales. Each license issued must be prominently displayed on the premises covered by the license.

SECTION 4. AMENDMENT. Section 57-36-07 of the North Dakota Century Code is amended and reenacted as follows:

57-36-07. Packaging - Presumption from possession - Indicia to be affixed. Cigarettes must be packaged and marked with indicia as follows:

1. All cigarettes sold or distributed in this state must be in packages containing twenty or more cigarettes each.
2. Within seventy-two hours of receipt by the licensee, each package of cigarettes, except as otherwise provided in this chapter, must have a securely affixed indicia denoting the tax, and each indicia must be properly canceled prior to sale or removal for consumption, under rules adopted by the tax commissioner.
3. Each package of cigarettes displayed, exhibited, stored, or possessed in original cartons or containers upon the premises where consumer sales are made is conclusively presumed to be for sale to consumers.
- ~~2-~~ 4. All packages of roll-your-own tobacco sold or distributed in this state must be in packages containing at least 0.60 ounces [17 grams] of tobacco and are not subject to the indicia requirements of this chapter.
5. Each package of cigarettes displayed, exhibited, stored, or possessed in original cartons or containers upon the premises where consumer sales are

made is conclusively presumed to be for sale to consumers. Each package of cigarettes, except as otherwise provided, must have a securely affixed indicia denoting the tax. Indicia must be canceled as provided in this chapter and possession of any unmarked package of cigarettes is prima facie evidence of a violation of this chapter.

SECTION 5. Section 57-36-08.1 of the North Dakota Century Code is created and enacted as follows:

57-36-08.1. Indicia prepared by commissioner. The tax commissioner shall prepare indicia for use on each kind of package under this chapter and keep an accurate record of all indicia received and delivered. The tax commissioner may sell the indicia only to a person holding a distributor's license. Wholesale distributors of cigarettes located outside of this state may apply for a distributor's license as provided in section 57-36-02 and may purchase indicia from the tax commissioner. The indicia must be affixed on cigarettes to be sold in this state and canceled pursuant to the tax commissioner's rules.

SECTION 6. AMENDMENT. Section 57-36-09 of the North Dakota Century Code is amended and reenacted as follows:

57-36-09. Records to be kept by distributors and reports made - Penalty. Distributors shall keep records and make reports relating to purchases and sales of cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products made by them, and must be punished for failure so to do, as follows:

1. Each distributor who shall dispose of cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products shall keep and preserve for one year all invoices of cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products and all receipts issued by the tax commissioner for indicia purchased by the distributor and shall permit the state tax commissioner, and assistants, authorized agents, or representatives of the state tax commissioner, to inspect and examine all taxable merchandise, invoices, receipts, books, papers, and memoranda as may be deemed necessary by the state tax commissioner, and assistants, authorized agents, or representatives of the state tax commissioner in determining whether the indicia required by this chapter have been purchased and used and the amount of the tax as may be yet due. Each person selling or otherwise disposing of cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products as a distributor shall keep a record of all sales made within the state showing the name and address of the purchaser and the date of sale. For sales of other tobacco products, the records must also include the net weight in ounces, as listed by the manufacturer.
2. On or before the fifteenth day of each month, each licensed distributor, on such form as the state tax commissioner shall prescribe, shall report to the tax commissioner all purchases and sales of cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products made from or to any persons either within or without this state during the preceding month. For sales of other tobacco products, each licensed distributor shall also report to the tax commissioner the net weight in ounces, as listed by the manufacturer. The tax levied by this chapter is payable monthly and must be remitted to the tax commissioner by each licensed distributor on or before the fifteenth day of the month following the monthly period.
3. Any person failing to file any prescribed form or return or to pay any tax within the time required or permitted by this section is subject to a penalty of five percent of the amount of tax due or five dollars, whichever is greater, plus interest of one percent of the tax per month or fraction of a month of delay except the first month after the return or the tax became due. The

tax commissioner, if satisfied that the delay was excusable, may waive all or any part of the penalty. The penalty must be paid to the tax commissioner and disposed of in the same manner as are other receipts under this chapter.

SECTION 7. Section 57-36-10.1 of the North Dakota Century Code is created and enacted as follows:

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.

SECTION 8. Section 57-36-11.2 of the North Dakota Century Code is created and enacted as follows:

57-36-11.2. Tax meter machines. In lieu of selling indicia, the tax commissioner may authorize any manufacturer or distributor to mark cigarettes with an indicia by a tax meter machine. The tax commissioner may adopt rules for leasing a tax meter machine to any manufacturer or distributor and for supervising the operation of the meter. Meters may not be used to mark untaxed cigarettes. The tax commissioner shall collect and receive the tax prescribed by this chapter on all cigarettes sold in or delivered to dealers in this state for sale, barter, gifts, or any other purpose. Any cigarette marked with the tax meter machine need not have the indicia sold by the tax commissioner affixed and may be possessed and sold by any wholesale or retail dealer in this state. Any manufacturer or distributor marking cigarettes with a tax meter machine under this section is entitled to the discount provided in section 57-36-10.1.

SECTION 9. Section 57-36-12.1 of the North Dakota Century Code is created and enacted as follows:

57-36-12.1. Distributors may not sell indicia. A distributor or wholesale dealer may not resell to any other distributor or dealer any indicia purchased from the tax commissioner. Any distributor who has on hand any unused and canceled indicia at the time of discontinuing the business of selling cigarettes may return such indicia to the tax commissioner and receive ninety-seven percent of the face value of the indicia.

SECTION 10. Section 57-36-13.1 of the North Dakota Century Code is created and enacted as follows:

57-36-13.1. Unlawful to transport cigarettes without indicia. A person may not transport into, receive, carry, or move from place to place in this state any cigarettes without indicia by any means of transportation, except in the course of interstate commerce. Any automobile, truck, boat, airplane, conveyance, vehicle, or other means of transportation in which any cigarettes are transported or carried in violation of this chapter, and any cigarettes and other equipment or personal property used as an incident to such transportation and found in such means of transportation, is subject to seizure by the tax commissioner or by any sheriff or other police officer, with or without process, and is subject to forfeiture as provided in section 57-36-14.

SECTION 11. AMENDMENT. Section 57-36-18 of the North Dakota Century Code is amended and reenacted as follows:

57-36-18. Tax commissioner to administer chapter. In administering this chapter, the tax commissioner and agents of the tax commissioner shall exercise the following powers:

1. The tax commissioner and authorized agents of the tax commissioner shall enforce the provisions of this chapter and have the powers of peace officers. They may arrest violators of the provisions of this chapter and enter complaint before any court of competent jurisdiction, and may seize

without formal warrant, and use as evidence, any forged, counterfeit, spurious, or altered license or indicia found in the possession of any person in violation of this chapter.

2. The tax commissioner may prescribe rules and regulations not inconsistent with the provisions of the chapter for its detailed and efficient administration.

SECTION 12. AMENDMENT. Section 57-36-25.1 of the North Dakota Century Code is amended and reenacted as follows:

57-36-25.1. Deduction to reimburse licensed distributor for administrative expenses.

- ~~1.~~ A licensed distributor who pays the tax due under this chapter within the time limitations prescribed may deduct and retain ~~one and one-half percent of twelve cents per carton of cigarettes from the tax due to reimburse the distributor for expenses incurred in affixing indicia, keeping records, preparing and filing returns, remitting the tax, and supplying information requested by the commissioner.~~
- ~~2. The total deduction allowed by this section may not exceed one hundred dollars per month for each licensed distributor."~~

Page 2, after line 11, insert:

"SECTION 14. AMENDMENT. Section 57-36-33 of the North Dakota Century Code is amended and reenacted as follows:

57-36-33. Penalties for violation of chapter. Except as otherwise provided in this chapter, ~~any:~~

1. Any person who violates any provision of this chapter is guilty of a class A misdemeanor. All cigarettes, cigarette papers, cigars, pipe tobacco, or other tobacco products in the possession of the person or in the place of business of the person must be confiscated and forfeited to the state.
2. Any consumer who purchases any package of cigarettes that does not bear the indicia placed on it under this chapter and any person who uses or consumes within this state any cigarette, unless it was taken from a package or container having attached the indicia required by this chapter, is guilty of an infraction.

SECTION 15. EFFECTIVE DATE. Sections 2 through 14 of this Act are effective for taxable events occurring after July 31, 2005."

Renumber accordingly

Mr. Chairman, members of the committee, good morning. My name is Toby Spangler, and I am a Regional Director at Altria Corporate Services. I appear here today on behalf of Philip Morris USA. Thank you for giving me this opportunity to present Philip Morris USA's views in support of House Bill 1522. This legislation -- in the form introduced in the House and currently before this Committee -- offers the State of North Dakota an important opportunity to help disrupt, reduce and eventually eliminate illegal activity related to cigarette sales.

I've come here today because contraband cigarettes -- an umbrella term that we use to define various types of illegal activity related to cigarettes -- are a growing problem in this country, and a growing problem for Philip Morris USA's business that it takes very seriously.

Philip Morris USA believes House Bill 1522 will benefit the State of North Dakota in several ways. Specifically, HB 1522 will help to disrupt and reduce the trade in contraband cigarettes in North Dakota. It will make it more difficult for minors residing in North Dakota to purchase cigarettes, thereby furthering North Dakota's efforts to prevent youth smoking. Finally it will make it more difficult for smokers to avoid excise tax payments and ensure that all applicable taxes are collected, thereby increasing the amount of excise tax revenues North Dakota collects.

My testimony is designed to provide you with some context as to why this bill is necessary and why it is necessary now. I will provide some background on the contraband problem, who it impacts, and why this legislation is a critical part of the solution.

In recent years there have been dramatic increases across the country in state cigarette excise taxes. Such increases have created incentives for adult 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 contributed to an increase in illegally sold or "contraband" cigarettes, as well as an increase in Internet cigarette sales that often occur without the proper payment of excise taxes or mandatory escrow payments, without effective age verification, and in violation of trademark and other laws.

House Bill 1522 would help prevent contraband cigarette sales. There are three types of contraband cigarettes that this bill would help address:

- Untaxed and under-taxed cigarettes, which are genuine cigarettes intended for sale typically in a low tax state, but sometimes illegally sold in states and localities with higher excise taxes, over the Internet, through direct mail, or by traveling across the state border. Untaxed cigarettes also include those cigarettes sold without a tax stamp or with an altered or counterfeit tax stamp.
- Counterfeit cigarettes, which are not of the same quality as genuine cigarettes, but are difficult to identify before consumption because the external packaging is very similar to legitimate product.
- Illegally imported cigarettes, which are intended for sale outside the United States but which are sold illegally in the United States, in violation of the Federal Imported Cigarette Compliance Act of 2000.

According to the U.S. Customs Service, the number of seizures of counterfeit cigarettes has jumped significantly in the last few years. U.S. Customs and Border Protection valued the



cigarettes they seized in FY 2004 at around \$24.2 million. By contrast, in FY 2001, U.S. Customs and Border Protection had valued the cigarettes similarly seized at only \$4.5 million.¹

Philip Morris USA has already identified the existence of counterfeit cigarettes at retail in 19 states, with suspected counterfeit cigarettes in 23 more. Most counterfeit cigarette packs also carry counterfeit tax stamps, if they have a tax stamp at all.

Illegal sales negatively impact Philip Morris USA trademarks, as adult smokers may unknowingly purchase substandard, counterfeit cigarettes that they believe are authentic. This tarnishes the Company's trademarks and brand reputations. It also distorts the legitimate market, hurting those legitimately engaged in the trade, including businesses located here in North Dakota.

Illegal cigarette sales harm not only Philip Morris USA, but also the State of North Dakota in the form of increased criminal activity and lost revenue. In a 2002 report, the General Accounting Office 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.* GAO Report: Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement (August 2002); Opening Statement of Director Bradley A. Buckles to the International Conference on Illicit Tobacco Trade, United Nations (July 2002).) Additionally, these illegal sales could lead to reduced payments for the State of North Dakota under the tobacco settlement agreement if the legitimate sales of manufacturers participating in the Master Settlement Agreement decrease.

¹http://www.cbp.gov/ImageCache/cgov/content/import/communications_5fto_5trade/statistics/fy01pub_2epdf/v1/fy01pub.pdf (last accessed 4/15/04)



Illegal cigarette sales also hurt law-abiding businesses, including wholesalers, retailers and manufacturers that are competing against those that have unfair economic advantages due to illegal activity – for example, Internet sites that don't collect State excise taxes.

While online sales currently represent a small percentage of total cigarette sales, there are currently more than 1,500 web sites selling cigarettes. A report issued in 2000 estimated that, by 2010, at least one-fifth of annual U.S. cigarette sales would occur over the Internet.² Due to the illegal nature of most Internet cigarette sales, it is difficult to quantify the financial impact to the States. Philip Morris USA believes, however, that the cost to States in lost revenue is significant. While estimates vary, one report cited by the U.S. General Accounting Office estimates that Internet tobacco sales alone will cost the States \$1.4 billion in tax revenue in 2005.³ Other observers believe that the cost to the States could reach \$4 billion by 2005.⁴

According to the U.S. General Accounting Office, three-quarters of all Internet tobacco sellers explicitly say that they will not report cigarette sales to tax collection officials as required by Federal law under the Jenkins Act. Moreover, Internet sites often mislead consumers into violating State excise tax laws.⁵

Additionally, the problem appears to be growing. One source that tracks Internet traffic to websites selling cigarettes found there was a 25 percent increase in visitors to the sites nationally in 2004. Those visitors viewed the pages 51 percent more often than they did the year before.⁶

² Said, Carolyn "Online sale of tobacco drawing a fight. Critics say tax, age laws must apply to Web market." San Francisco Chronicle. 29 May 2000

³ Online Tobacco Sales Grow, States Lose, Forrester Research, Inc. April 27, 2001; "Internet Cigarette Sales," U.S. General Accounting Office, August 2002.

⁴ Testimony of Patrick Fleenor, Chief Economist, Fiscal Economics Inc., before the Subcommittee on Courts, the Internet and Intellectual Property, Committee on the Judiciary, House of Representatives (May 1, 2003))



Philip Morris USA takes the issue of illegal cigarette sales very seriously, and we have been making significant efforts to disrupt and reduce these illegal sales. It has been working closely with law enforcement at the federal and state level to support their efforts to address contraband by enforcing the laws already on the books. Additionally, under existing laws that give us certain legal rights, such as trademark laws, it has filed lawsuits against those who are trafficking in contraband. To date these lawsuits have involved more than 2800 retailers, 4 wholesalers, and 18 internet operators. The existing laws in place to address contraband cigarette sales need to be expanded and toughened.

That is why House Bill 1522 is needed and why Philip Morris USA is pleased to support it. I commend Representatives Carlson and Price for their leadership in putting forth legislation that, if enacted and enforced, would help disrupt and reduce illegal cigarette sales.

House Bill 1522 would help address these serious issues by providing better tools for law enforcement officials to eliminate contraband cigarettes, and help ensure that all industry participants comply with the requirements governing the legitimate distribution and sale of cigarettes. The bill would, among other things:

- Ensure that only licensed entities (other than consumers) may purchase and sell cigarettes.

⁵ "Internet Cigarette Sales," U.S. General Accounting Office, August 2002.

⁶ "Cigarette tax skirted online." Chuck Plunkett. Denver Post. February 7, 2005



- Require tax indicia on each pack of cigarettes sold in the state. The indicia can only affixed by licensed distributors.
- 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.
- Address the issues of inadequate age verification and non-payment of appropriate taxes, by imposing comprehensive new restrictions, including: age verification requirements, fiscal compliance measures, penalties and enforcement mechanisms on sales of cigarettes to consumers via the Internet. These provisions would help in reducing tax evasion and in limiting the access of youth to cigarettes.

Conclusion

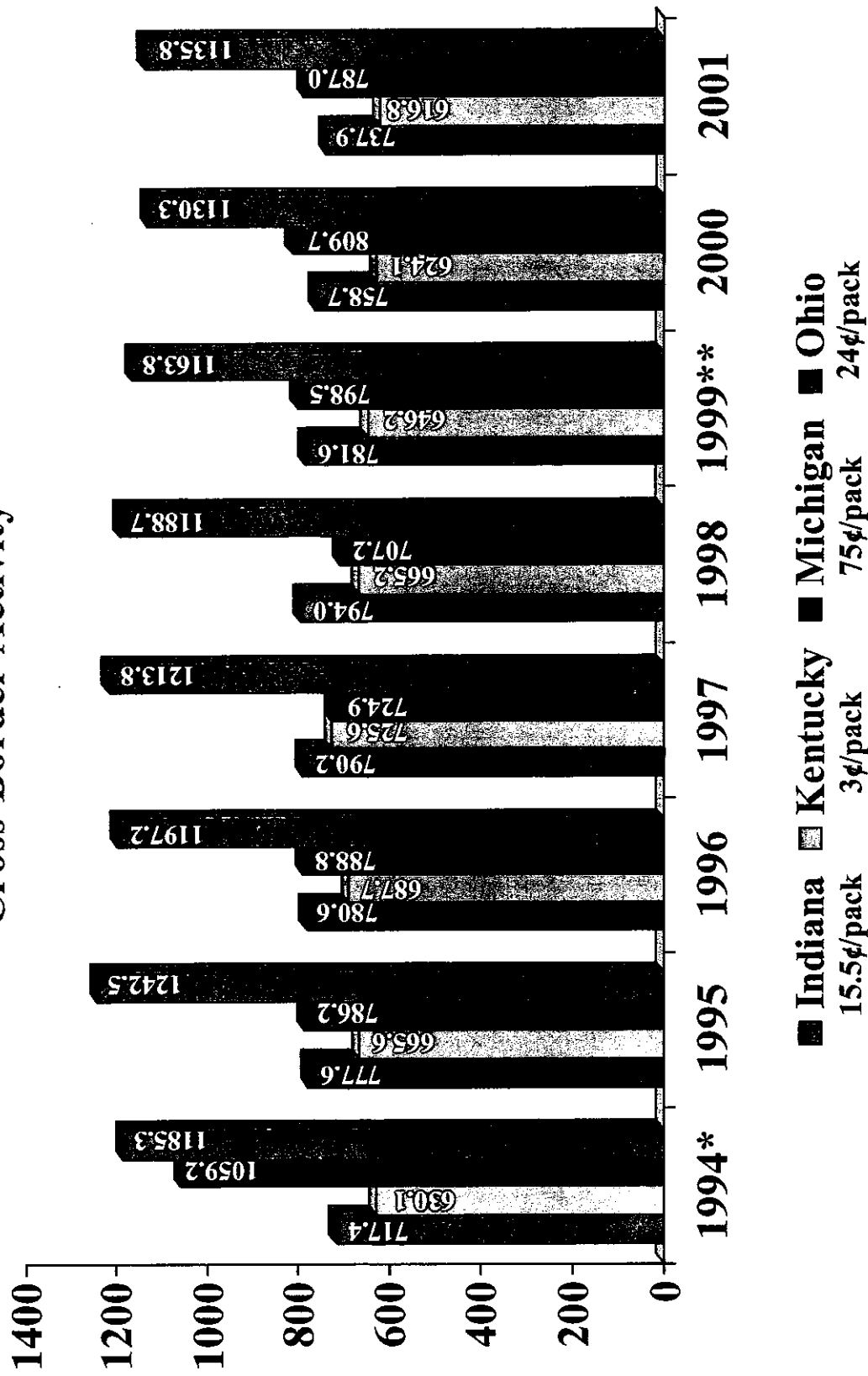
Contraband cigarette trafficking, including tax-evasive Internet and Direct Mail Sales, continues to present challenges for the legitimate domestic cigarette industry and for governments, including state revenue departments. North Dakota has an opportunity to play a key role in addressing an issue that negatively impacts not only law-abiding cigarette manufacturers, their trade partners and consumers, but also the government and its revenue collection efforts.

Philip Morris USA will continue to work with law enforcement in North Dakota and elsewhere. There is a clear need, though, for the existing laws to be strengthened so that law enforcement has the tools it needs to address this issue. House Bill 1522 is a significant step toward solving this issue. We urge you to support it. Thank you.



State Tax-Paid Cigarette Sales

(in millions of packs)
Cross-Border Activity



Source: The Tax Burden on Tobacco, Tobacco Institute Historical Compilation, Volume 36, 2001, page 29

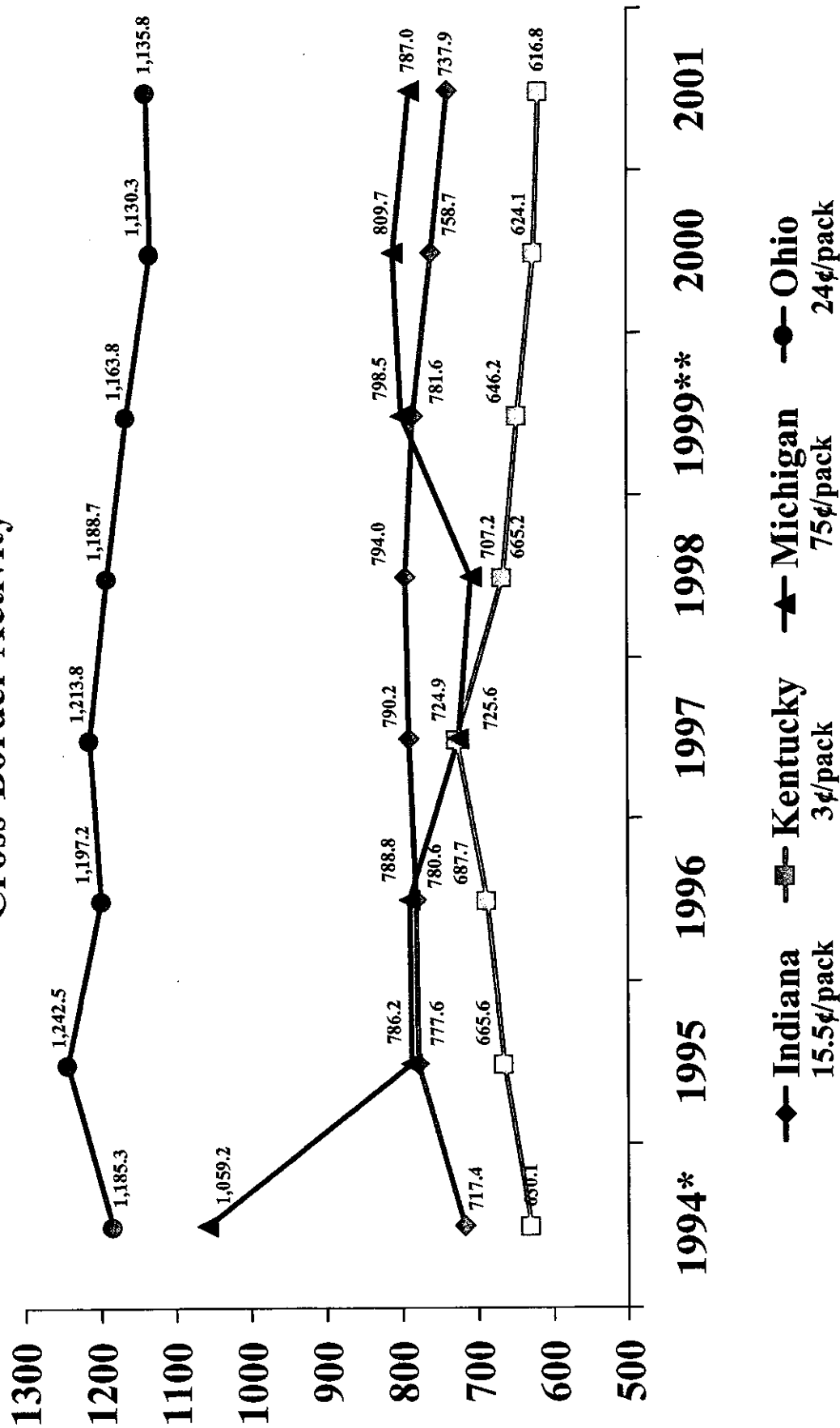
* Michigan increased \$.50 per pack in 1994

** First full year of Michigan tax stamping

State Tax-Paid Cigarette Sales

(in millions of packs)

Cross-Border Activity



Source: The Tax Burden on Tobacco, Tobacco Institute Historical Compilation, Volume 36, 2001, page 29

* Michigan increased \$.50 per pack in 1994

** First full year of Michigan tax stamping



PHILIP MORRIS USA

PO Box 26603 Richmond, VA 23261 (804) 274-2000

March 2, 2005

The Honorable Herbert Urlacher
State Senator
600 E. Boulevard Ave
Bismarck, ND 58505

Dear Mister Chairman and Members of the Committee:

Per your request, I provide below information on the volume of cigarettes shipped to retail outlets located in the State of North Dakota for calendar years 2003 and 2004. This information is provided to Philip Morris USA by Management Science Associates (MSA), a company that collects cigarette shipment volume from participating wholesalers and distributors.

By way of background, Philip Morris USA sells cigarettes to wholesalers ("direct accounts"). These wholesalers in turn sell to retailers and, on occasion, to other wholesalers (known as subjobbers). Philip Morris USA's direct accounts report to MSA their weekly shipments of all brands of cigarettes to retailers and to subjobbers. MSA aggregates the data and checks the quality. MSA then makes the data available to Philip Morris USA, and it is referred to internally as "STARS" data. The information provided below is drawn from the STARS data maintained by MSA.

It is important to understand two limitations with respect to the STARS data. First, although MSA checks the quality of the STARS data, the data is self-reported by wholesalers. Second, the STARS data includes information only from Philip Morris USA's direct accounts. Retailers in North Dakota may purchase cigarettes from other wholesalers, from non-reporting subjobbers or even from other out-of-state retailers, which purchases may not be captured in the STARS data.

This data is Confidential and Proprietary to Philip Morris USA, and we ask that this information not be distributed beyond this committee without express permission from PM USA. However we believe it would be beneficial information to your committee as you continue to examine the need for cigarette tax stamps in the State of North Dakota.

Wholesaler industry shipments to North Dakota retailers as reported by Management Science Associates to Philip Morris USA:

2003 – 48,239,340 packs of cigarettes

2004 – 47,804,660 packs of cigarettes

Wholesaler industry shipments to North Dakota retailers **excluding** classified Native American retail¹ volume as reported by Management Science Associates to Philip Morris USA:

2003 – 45,104,540 packs of cigarettes

2004 – 44,697,690 packs of cigarettes

Source: STARS Store Level Database as of Jan 22, 2005

If you have further questions regarding this information please contact me at (804) 484-8625.

Sincerely,

C. R. Beard

Christopher Beard
Public Policy Manager

¹ Philip Morris USA classifies certain retail accounts as Native American based on information reported to Philip Morris USA by those accounts. The classification may be inaccurate where the information was misreported. In addition, there may be accounts that are owned by Native American tribes or tribal members that have not been identified to Philip Morris USA.

Prepared for Senate Finance and Taxation
HB 1522

North Dakota Retail Cigarettes Sold*

2003

| | |
|---------------------------------------|------------------|
| Taxable sales by Licensed Wholesalers | 42,043,779 |
| Reservation Sales | <u>5,992,170</u> |
| Total packages of 20 cigarettes | 48,035,949 |

2004

| | |
|---------------------------------------|------------------|
| Taxable sales by Licensed Wholesalers | 41,667,649 |
| Reservation Sales | <u>5,780,410</u> |
| Total packages of 20 cigarettes | 47,550,318 |

*Does not include military cigarettes or Reservation purchases from unlicensed out of state distributors made in interstate commerce.

Source: North Dakota Distributor tax reports

Prepared by John Quinlan, March 2005
Office of the State Tax Commissioner

March 9, 2005

Henry J Knoll
Frank McKone Cigar Co.
742 19th Street N.
Fargo, ND 58102
1-701-235-4261

Chairman Urlacher & Senators,

Frank McKone Cigar is in the wholesale distribution business of selling candy and tobacco products to retail outlets. We are located in Fargo, ND. We are a family owned business. We primarily operate in eastern North Dakota and western Minnesota. At present, we have 23 full-time employees.

It has been brought to my attention that there will be amendments made to the First Engrossed HB 1522, to revive HB 1522 as it was originally presented in the House of Representatives, with all the stamping language put back in the bill. If this is true, as a representative for Frank McKone Cigar, we oppose HB 1522.


There are several cost that go along with the stamping process. We would need an additional stamping machine, these machines rent for \$6,000 to \$8,000 a year. An additional employee would be needed to run this machine, at a cost of \$24,000 to \$28,000 a year, plus benefits. The largest expense would be to have to pay for the stamps up front at a cost of anywhere from \$140,000 to \$180,000 a month. This would create a very serious problem with our cash flow.

The 72 hour stamping provision is unreasonable and a very costly provision. It would force us to carry duplicate inventories on most of our cigarette brand styles. We are presently stamping cigarettes in Minnesota. The Minnesota cigarette orders are stamped on demand, meaning as they come off the picking line. On average, our cigarette inventory is valued at \$375,000. Doubling this number creates an even bigger problem with our cash flow.

At this time, Meyercord stamping machines are our only option for applying stamps. The technology on these machines is old and outdated. It is difficult to get any kind of consistency applying stamps with these machines.

It is my opinion that passage of HB 1522 will create undue financial stress on Frank McKone Cigar and all the other wholesalers in the state of North Dakota. We need your help to keep North Dakota businesses financially strong. I suggest you give HB 1522 a DO NOT PASS.

Thank you,



Henry J Knoll

"John Job"
<JJOB@amcon.com>

To: "S Fin NDLA" <sfin@state.nd.us>
cc:
Subject: HB 1522 for Senator Urlacher

03/08/2005 08:40 PM

Sharon, Please forward to Senator Urlacher. Thank you.

Senator Urlacher,

I am sorry that I am unable to attend the Senate committee hearing on HB 1522. I am out of Bismarck on business. Please accept my e-mail as my testimony on HB 1522.

I manage a wholesale distribution center of consumer products located in Bismarck, ND. One of the consumer products we distribute is cigarettes. Upon reviewing the original version of HB 1522 we had some language issues within the bill and did not support the bill without extensive language cleanup. The bill was amended and cleaned up reappearing in a first engrossed version that we support. Recently I have had a discussion with a lobbyist. The lobbyist informed me that tax stamping language that was in the original HB 1522 will be offered as an amendment into the bill during your hearing. Based on the discussion with the lobbyist, we feel passage of HB 1522 will put unfair burden on in-state wholesale distribution operations such as AMCON Distributing Company and give out of state wholesale distribution companies unfair advantages. Without my knowledge of the exact wording of the amendment, and just using the spoken intent of the amendment, and the prior language of HB 1522, there may be a 72 hour provision in the amendment. My understanding is that section would require all product have indicia properly affixed to product within 72 hours of receipt of product. AMCON Distributing Company ships into 5 different tax jurisdictions. You would force us into stocking much more product as we would have to affix tax stamps to our entire product upon receipt of product rather than just prior to selling it. As it is now the jurisdictions that require stamping we affix the stamps after selling just prior to shipping and maintain our inventory as unstamped until sold. This would force AMCON Distributing Company to maintain 3 or 4 times the amount of cigarette inventory we now have, or move our cigarette stamping procedure out of state. We were also informed that there would be a wholesaler compensation of 12 cents per carton to implement stamping on North Dakota sold product. Without my knowing where this money is to come from, my assumption is it would come in the form of a stamp purchase discount from the tax department. We believe that the state of ND should not subsidize a wholesaler's stamping expense. The 58th session of the ND legislature had HB 1431 that addressed the cigarette stamping issues fairly and this bill passed both chambers, only to be recalled the following day and defeated in the Senate Chamber for reasons that remain unknown to me. That bill used language from Montana law and it put the expense of stamping cigarettes on the retail price of the product, not the state of ND. That bill had the proper language all parties could live with.

In conclusion, we are in support of the first engrossment of HB 1522, however we are opposed to HB 1522 as amended in the Senate Hearing scheduled for March 9, 2005. We feel the language of the amendment was hastily prepared, without any input from the in the state of ND wholesale distributors and to the benefit of the out of state distributors.

If you should have any questions of my testimony, please feel free to contact me via e-mail jjob@amcon.com or my cell phone 701-220-5977. I will be happy to further explain cigarette tax stamping from a wholesale distributor's perspective.

Thank you,

John F. Job
Division Manager
AMCON Distributing Company
3125 East Thayer Ave.
Bismarck, ND 58501
701-258-3618

1522

Page 4, after line 23, insert:

SECTION 2. AMENDMENT. Subsection 3 of section 57-36-27 of the North Dakota Century Code is amended and reenacted as follows:

57-36-27. Consumer's use tax – Cigarettes – Reports – Remittances.

Overstrike "3. This tax does not apply to the use or storage of cigarettes in quantities of two hundred or less in the possession of any one consumer nor to cigarettes exempt pursuant to section 57"

Page 4, remove lines 24 through 31

Page 5, remove lines 1 through 31

Page 6, remove lines 1 through 30

Page 7, remove lines 1 through 31

Page 8, remove lines 1 through 31

Page 9, remove lines 1 through 31

Page 10, remove lines 1 through 6