

2011 HOUSE FINANCE AND TAXATION

HCR 3030

2011 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee Fort Totten Room, State Capitol

HCR 3030
February 14, 2011
#14482

☐ Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

A concurrent resolution directing the Legislative management to study the feasibility and desirability of requiring use of cigarette tax stamps to ensure compliance with tobacco products tax laws.

Minutes:

Ch. Belter: We will open the hearing on HCR 3030.

Rep. Craig Headland: Introduced Concurrent Resolution 3030. Support. We've all seen similar bills like this in prior sessions. We've never been able to get them passed. I think it is time that we look at this, study it and see if we do have a problem in the area of cigarettes that are not company supported, pirated cigarettes. There are others to testify on this bill.

Ch. Belter: Thank you. Further testimony in support of HCR 3030.

Allan Stenehjelm, Reynolds American: Support. Please refer to attached testimony #1.

Rep. Shirley Meyer: When you talk about contraband cigarettes, is there something bad in them or are they old, stolen from another cigarette company. What are contraband cigarettes.

Allan Stenehjelm: One example of contraband cigarettes, came from 2005, where Rep. Porter got on the internet and ordered cigarette from Russia; they were delivered here to his desk, actually in the Chamber. They weren't produced by the companies that take great care and concern in making sure the cigarettes that they sell are real. There are contraband cigarettes put on and the quality is not the same. That is what my company is most concerned about. We believe that stamping cigarettes would help ensure that that does not happen.

Rep. Wrangham: Would a stamping law stop that company from Russia from shipping the cigarettes into the state.

Allan Stenehjem: The stamps would require that anything that was sold in the state of ND, would have a stamp on it. We have laws in place to make sure that we're protecting sales of cigarettes on the internet. Can there still be cigarettes brought in, certainly. But at least we would have a mechanism saying that if there is no stamp on it, we know that 1) they haven't paid the tax on it; and 2) that it's not a legitimate cigarette that should be brought into the state. We're one of three states that do not stamp cigarettes; North and South Carolina and North Dakota. I believe that North Carolina is now putting in a bill during this session to require stamping of cigarettes.

Rep. Hatlestad: Obviously there is a cost involved to the wholesaler. Do you have any idea what it costs to buy a machine to stamp the cigarettes.

Allan Stenehjem: I have a representative here from the wholesalers that can give you the specific number. I have looked at their operation and how they stamp the cigarettes. It is quite impressive how they do it. He has the numbers of the equipment and what is involved in it.

Ch. Belter: Thank you. Further testimony in support of HCR 3030.

John Job, Northern Division Mgr., AMCON Distributing Company: Support. Please refer to attached testimony #2.

Rep. Zaiser: What are the benefits for the state of North Dakota in having cigarettes stamped? Basically, we're already dealing with a drug. What are the benefits that the state derives from having the cigarettes stamped.

John Job: I can't speak on behalf of the state what the benefits are for having the stamps on there; but as a wholesaler, it marks the product. The stamps have a number on it and it will tell investigators or people who are researching it, what distribution center that product came out of. It gives us the ability to track.

Rep. Zaiser: How does that benefit the state? Is there any health benefit?

John Job: I'm not sure how that would benefit the state.

Rep. Owens: Before we go considering raising taxes on cigarettes, we need to find out if we are actually collecting the ones we've already instituted. That would be the big advantage to the state personally and to the taxpayers. You went back and forth. Are you for the resolution or against it.

John Job: I'm for the study.

Rep. Owens: You said that currently you're working four shifts, 10 hours a day stamping cigarettes. Did I understand you to say that you do it for South Dakota, Montana, and Minnesota. Then what I found very unique was, that out of those three states, you said it would be an increase in employees because over 50% of the remaining cigarettes were in ND that you would then have to stamp. Did I hear that correctly.

John Job: That is correct. Our share in the states is slightly less than 50% goes into MN, MT, and SD and hit a sliver of WI. It's an excess of 50% that's North Dakota. In ND you process the orders, pull the orders, and go right on down the line to the loading line and onto the truck. The other ones they go on the conveyor over to the stamping machine and have to go through the stamping machine to have the stamps put on there. That's a two-person operation.

Rep. Owens: I never saw anything in your materials talking about duty-free locations at the border. I know people drive 50 miles to buy cigarettes at the duty-free just to take them back home to Minnesota. Do they still have stamps at the duty-free shops.

John Job: We do sell to some duty free but they are assessed the tax. As a matter of fact, our company, in order to sell to any retailer in the state of ND or any of the other states that we serve, we must have documentation that they do, in fact, have a cigarette license. We don't sell to anybody that doesn't have a cigarette license so that we do assess the tax.

Rep. Hatlestad: You currently pay the tax before you ship the product out, is that correct?

John Job: In all the states except in ND. All of the states we sell to, we either pay via automatic clearing house or we pay with a check with the order and that's an advance. In ND, it's an accounting, administrative procedure. We sell the product, at the end of the month, total it up and we send a check to the Tax Dept.

Rep. Hatlestad: You send out your cigarettes, you send out the invoice with the tax included.

John Job: Absolutely.

Rep. Hatlestad: Do you COD your cigarettes so that you're getting your check, or at the end of the month, do you send them an invoice and they hopefully send you a check.

John Job: That would be in a perfect world to get COD. We do extend some terms based on the credibility of the account and the program we have the customer set up in. We try to do automated clearing house from our customers too, an electronic fund transfer to us to pay for it.

Rep. Hatlestad: If the state sets a minimum price isn't that price fixing?

John Job: It is a minimum price to pay for a highly regulated product. ND has minimum pricing on milk right now.

Rep. Trottier: This is called a cigarette tax, does it apply to cigars, chewing tobacco, etc.

John Job: They are two separate entities; cigarettes are 10 packs of 20 that go through the machine. Cigars and other tobacco products, that's totally separate, that would not be involved with the stamping.

Rep. Zaiser: I once knew an owner of a C-store in Fargo that sold a lot of cigarettes. He indicated to me that the cigarette distributor, wholesaler, whomever, liked to put them out on the counter, knowing full well that the cigarettes would get stolen and in that case, the objective was to get more people hooked on cigarettes. In that case, there wouldn't be a tax on those if you sell them based on the sale, whereas in the other states, you talked about how you paid the sales taxes upfront.

John Job: We pay the excise tax upfront but we also track how many we sell out of our building to any ND retailer. We assess the tax to the retailer, to our customer, and then we pay it to the State Tax Dept. There are all kinds of computerized reports I can generate for whatever month, or for whatever customer you'd like to know.

Brad Bourkes, Wholesale Supply Company, Minot, ND: Support. We are a family owned, in-state owned ND business that's been here since my grandfather started in the early 1950's. One of the things that we look at when we look at the stamping issue, we are in support of a study, but if it is done with a logical approach and a ND approach. A couple of concerns that we do have, we were a stamping state, as you may or may not know. We went away from that for logical reasons that are predecessors made a decision on. The purpose and logic on that still stands. The accounting process as Mr. Job explained vs. the policing of the stamp is much less a hindrance to the Tax Dept. When you look at the number of retail locations that you would need to manage the stamps at versus unfortunately now that the number of distributors in the state, I think there are around 12 operating in the state. You go to 12 locations and manage the books that are there that are coming through that accounting process, which as CPA's know it is a very effective process. Our concern is that 1) we'll support stamping, we'll support what is best for ND, but we want it to be logically done as well. We want to make sure that what is being asked for and requested, is logical. A perfect question was does the stamping make a difference. No, the only thing that makes a difference is the policing of it. If they can manage the policing through the distributor, they have 12 distributors that they have relationships with that they understand that they have to report back to the state. That is kept very transparent with the state. There was a question earlier, are we for

the stamping or not. No in the fact that we're concerned of where that goes as far as logic. In regards to the way in which contraband works, there were some good questions. The contraband that got in from Russia to the Chamber's desk did not pay tax. The Tax Dept isn't going to his desk to make sure that there is a stamp on it vs. no stamp on it. The conflict I have in understanding the stamping is that there is no logical support in the policing efforts to make this make sense. The one thing I would ask, if the study goes through, I ask that the study supports the focus on the people in the state of ND. From a manufacturer standpoint, their concern is not for us. Their concern is their brand and the black market and how that affects them. We believe that is very minimal; 1) just the population base, the value of doing it in a population base, and the tax value of it right now. If we do a stamp, if they are contraband the product right now; from a tax based standpoint, if they are contraband the product and you're not getting the stamp value of it, they are going to contraband the stamp and you still won't get the tax value of it. We look at it from that standpoint and have some concerns there as well. As John had mentioned, they are going to have to add 50% to theirs. Basically, we would have to add 100%. The amount of overhead invested, they have knowledge and stamps and what to do. Basically we have none. So the amount of overhead invested and training, ramp up would be unfairly assessed to an in-state distributor like us. If we were a national distributor, and ND was only a small piece of our pie, then it would be much less of a hindrance. We ask to be treated fairly; nothing more nothing less.

Rep. Trottier: Is what is going on now not working?

Brad Bourkes: I believe that it is working very well. It works well for the IRS. They assess us, audit us, they come and evaluate. We send reports. As John mentioned, we send reports every month, we've got detailed reports. I can tell them to you frontwards and backwards. We've got the information that they would need because we track the information coming in and going out. The comment about cigarettes being placed on the counter to be stolen; 1) a distributor doesn't set it anywhere in the store other than in their back room, the store owner would set it out to the front or wherever they decided to put it. In that same example, the tax is taxed before it gets to the store. So the tax is already collected. We've assessed that store's taxes, so whether it gets stolen or sold it doesn't matter. Regarding the stamping process, you made a good point. I think part of the challenge that so many other states have is that we are ND, we do drive down the road and we stop to help someone out. I have a sales manager who came in from Lincoln, NE. We do have security systems but he says I think we need more. Down in NE we had more of this and more of that; I said yes, but in the end does a security camera steal the product or does a person steal the product. Our focus is on hiring and making sure that the people are worthy of that trust.

Ch. Belter: Thank you. Further testimony in support of HCR 3030.

John Olson, Phillip Morris: Support. We are here to support the study. We've had a bill in several sessions in this decade. The House was pretty kind to the bill, got

over to the Senate and it was killed over there on a couple of occasions. One of the things that I've been told; of course, I'm not old enough to remember 40 years ago, when stamping was in the state, it was repealed as a result of the manufacture of the machines going out of business and they couldn't get parts, so I think that was the impetus for the repeal back then. Philip Morris is concerned about the language in the resolution. If you go to the third WHEREAS, it says application of tax stamps would demonstrate diligent enforcement of master settlement agreement provisions to ensure reliable collection of master settlement agreement payments due to states. That is only one element of diligent enforcement. We think that might be a problem with the language, and it's going to be solved by Doug Barr, who is going to be up here on behalf of the AG's office who's going to propose an amendment that will more or less make this neutral. Let's not decide right now the merits of whether stamping is appropriate or good for the state of ND. Let's let the study take its course. Have all the parties present and weigh in; the companies, manufacturers, distributors, the Tax Dept., the Attorney General's office, retailers, anyone with an interest in whether or not stamping would be good for the state of ND. You've already heard that ND's one of very few states that doesn't stamp, and there is probably going to be one on board in the Carolinas from what I've been told. From my company's perspective, stamping would be a good thing for the interest of the country in terms of having a national distribution identification. In terms of counterfeiting cigarettes, that happens. China was a country that was involved in a lot of counterfeiting, you heard the story about Russia, and also heard comments about counterfeiting the stamp. There is a lot of study and technology involved in that process as well, to come up with indicia, a stamp on a pack that would be more difficult to counterfeit. All of that is relevant to a study.

Rep. Trottier: I have a problem with your testimony, when you said that you cannot remember 45 years ago.

John Olson: I remember you from 45 years ago, I don't remember the stamping issue.

Ch. Belter: Thank you. Further testimony in support.

Mike Ruud, North Dakota Petroleum Marketers and ND Retail Association: Support. We too stand in support of the study. I have members obviously on both sides of this issue. We'd like to see once and for all just where the retail sector would land should the stamping be implemented. We have no problem at all with seeing the study move forward and seeing what those results would be.

Ch. Belter: Thank you. Further testimony in support of HCR 3030.

Myles Vosberg, Tax Commissioners Office: Support of study. This topic keeps surfacing every session. It is a very complex study, I don't think we've had time to adequately discuss all the issues, the pros and cons in previous sessions. We think it is important to have law enforcement also involved in this study. Whether the

result is stamping or not stamping, we think that's an important topic here as part of the consideration.

Rep. Shirley Meyer: Does the state of North Dakota have the authority to require the Tribes to tax their cigarettes; would you touch on that briefly.

Myles Vosberg: The state cannot require the Tribes to tax. Right now we have an agreement with Standing Rock. Standing Rock taxes their cigarette sales, the same as ND and then we share the revenue from the sales that are made on the reservation based on a ratio of population - enrolled members to non-members. The other tribes do not tax their cigarettes. We do not have the ability to be involved in their taxation or their enforcement of whatever they do with cigarettes.

Ch. Belter: Thank you. Further testimony in support. If not, any testimony in opposition.

Doug Barr, Director of Civil Litigation in the Attorney General's Office: In that capacity one of my functions is tobacco counsel, which is to help enforce the master settlement agreement as well as chapter 51-25, which was a statute implemented as a result of the master settlement agreement that has to do with tobacco companies who do not sign or become signatories to the master settlement agreement, being required to pay escrow based upon the number of cigarettes which they sell in the preceding years. I want to make it clear that AG does not take any position decision of whether or not to conduct a study regarding tobacco tax stamps. He does, however, strongly oppose the language in the current resolution, because that language is not neutral. To the contrary, it actually makes preliminary finding that would be the very purpose of the study. Please refer to attached testimony #3. It covers two different areas, on lines 2, 6, 7 and 18, the language in those lines provides that using tobacco tax stamps would ensure compliance. That is a finding that the study should determine; first of all whether the use of tobacco tax stamps would assist in compliance in any way; and whether, in fact, there is non-compliance to date. By including that language, it is implying that there isn't compliance at this time and that the use of tax stamping would ensure compliance. Again, we believe that if there is a study that is one aspect of that study. I believe Mr. Stenehjem and others who have testified, have noted that. That the degree of non-compliance is a factual issue and whether tax stamping would impact that positively or negatively is another issue that should be part of the study. Most importantly, the concern is, as Mr. Olson, mentioned, in the 3rd WHEREAS clause. That language, again, makes a finding by saying that using tax stamps, that those tax stamps would demonstrate diligent enforcement of the master settlement agreement. For the committee's information, a number of tobacco companies have withheld portions of their payments under the master settlement agreement. The states who are signatories to the master settlement agreement are currently in an arbitration involving \$1.2 billion just for the year of 2003. There could be similar arbitrations for each year after 2003. The very issue in that arbitration is whether the states diligently enforced their statutes. First of all, it's not whether they diligently enforced their tobacco tax

statutes, which this implies that it was. It was whether they diligently enforced their statutes that are called model statutes, which is our chapter 51-25. So this statement appears to make a legislative finding; first of all that by having cigarette tax stamps we would have diligently enforced, which means by not having tax stamps, we did not diligently enforce. I would submit that that legal issue, as well as that factual issue, if it is an issue at all, is appropriate for the arbitration panel and that this committee and the legislative assembly should not get involved into that very technical issue that is under the MSA as to what diligent enforcement is. Again, Mr. Olson acknowledged that that is an issue they don't want to just be resolved or addressed in here either. The AG's office proposes an amendment, the handout's first page are the amendments and the second page shows if those are adopted, what the resolution would look like. We believe that it makes the resolution neutral, rather than findings that could be attempted to be used against the state in this very expensive arbitration; an arbitration that could result in millions and millions of dollars that the tobacco companies are currently refusing to pay. In our position, contrary to the MSA, of course, they take the position that they don't have to pay it, and that's why we are in arbitration. The language that we included, provides neutrally that it would study both the benefits and the detriments of requiring tax stamps instead of falsely, prematurely stating that it will ensure compliance and it will demonstrate diligent enforcement under the MSA. In summary, we do not oppose the study in any way, but we oppose language that prematurely makes legislative determinations that could adversely impact the state's position in the current diligent enforcement arbitration and that implies that currently the process is failing and that somehow by simply passing the tax stamp as a requirement, there would be perfect compliance, that it could in some way ensure compliance.

Ch. Belter: Thank you. Any further testimony in opposition. Any neutral testimony.

Allan Stenehjem, Reynolds American: Exactly what happened is what we do not to happen. We want the focus on stamping the cigarettes, not the master settlement agreement or any other implications that that is associated with. We want the focus on should we stamp cigarettes and when we had this drafted, this is not company language, and this was drafted by Legislative Council, thinking this is what should be in here. We have no problem taking this language out. I want to make sure that we focus on the issues that we need to focus on. This just regressed and we don't need to go there. As far as the amendments, I would encourage you to adopt the amendments to make sure that the language is taken out so that we focus on the real issue.

Ch. Belter: Thank you. We will close the hearing on HCR 3030. Let's take a look at HCR 3030. What are the committee's wishes.

Rep. Headland: It appeared that everybody was in agreement that the amendment is a good addition to the bill, I move the proposed amendment from the AG's office.

Rep. Owens: Second the motion.

Ch. Belter: We will take a voice vote. Motion carried. We now have the bill before us as amended. What are the committee's wishes.

Rep. Headland: I move a Do Pass as amended on HCR 3030 and when so amended be placed on the Consent calendar.

Rep. Owens: Second the motion.

Ch. Belter: The clerk will call the roll.

14 YES 0 NO 0 ABSENT

DO PASS AS AMENDED AND PLACED ON CONSENT CALENDAR

CARRIER: Rep. Headland

February 14, 2011

VR
2/14/11

PROPOSED AMENDMENTS TO HOUSE CONCURRENT RESOLUTION NO. 3030

Page 1, line 2, remove "to ensure compliance with tobacco products"

Page 1, line 3, remove "tax laws"

Page 1, remove lines 6 through 11

Page 1, line 12, replace "effects" with "feasibility and desirability"

Page 1, line 13, replace "effects" with "benefits and detriments"

Page 1, line 13, replace "the requirement" with "requiring cigarette tax stamps"

Page 1, line 18, remove "to ensure compliance with tobacco products tax laws"

Renumber accordingly

Date: 2/14/11
Roll Call Vote # 1

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 3030

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment
☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Headland Seconded By Rep. Owens

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley R. Belter			Scot Kelsh		
Vice Chair. Craig Headland			Shirley Meyer		
Glen Froseth			Lonny B. Winrich		
Bette Grande			Steven L. Zaiser		
Patrick Hatlestad					
Mark S. Owens					
Roscoe Streyle					
Wayne Trottier					
Dave Weiler					
Dwight Wrangham					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

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

Voice Vote / Motion Carried.

Date: 2/14/11
Roll Call Vote # 2

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 3030

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 11.3064.01001 .02000

Action Taken: ☒ Do Pass ☐ Do Not Pass ☒ Amended ☐ Adopt Amendment
☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Headland Seconded By Rep. Owens

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley R. Belter	✓		Scot Kelsh	✓	
Vice Chair. Craig Headland	✓		Shirley Meyer	✓	
Glen Froseth	✓		Lonny B. Winrich	✓	
Bette Grande	✓		Steven L. Zaiser	✓	
Patrick Hatlestad	✓				
Mark S. Owens	✓				
Roscoe Streyle	✓				
Wayne Trottiér	✓				
Dave Weiler	✓				
Dwight Wrangham	✓				

Total (Yes) 14 No 0

Absent 0

Floor Assignment Rep. Headland

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

*When so amended, be placed
on Consent Calendar.*

REPORT OF STANDING COMMITTEE

HCR 3030: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (14 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HCR 3030 was placed on the Sixth order on the calendar.

Page 1, line 2, remove "to ensure compliance with tobacco products"

Page 1, line 3, remove "tax laws"

Page 1, remove lines 6 through 11

Page 1, line 12, replace "effects" with "feasibility and desirability"

Page 1, line 13, replace "effects" with "benefits and detriments"

Page 1, line 13, replace "the requirement" with "requiring cigarette tax stamps"

Page 1, line 18, remove "to ensure compliance with tobacco products tax laws"

Renumber accordingly

2011 SENATE FINANCE AND TAXATION

HCR 3030

2011 SENATE STANDING COMMITTEE MINUTES

Senate Finance and Taxation Committee
Lewis and Clark Room, State Capitol

HCR 3030
3/7/2011
Job Number 15048

☐ Conference Committee

A. Bittmiller

Explanation or reason for introduction of bill/resolution:

A concurrent resolution directing the Legislative Management to study the feasibility and desirability of requiring use of cigarette tax stamps

Minutes:

Written Testimony Attached

Chairman Cook opened the hearing on HCR 3030.

Representative Headland – I'm here to ask you for your favorable consideration of engrossed HCR 3030 which is a simple bill that will study stamping of cigarettes in the state of North Dakota.

Allan Stenehjelm, Reynolds American – (See attached testimony A in favor of HCR 3030)

Senator Triplett – I don't have any problem with studying just about anything, but just in general do you have ideas as how this study might approach the issue of Indian reservations and do you expect cooperation from the Indian reservations? I think without that this wouldn't prove very much.

Allan Stenehjelm, Reynolds American – Standing Rock is the only reservation that does do the stamping of the cigarettes. It is our hope that we can get this discussion to that point where we can open the dialog and figure out a way to work with the tribes and the state and the Tax Department and all of those entities. It's complicated; it's not something that is easy to do during the session. You have all these parties come together and say; now we want to resolve this in 3 months. It's something that needs to be done and either we do it and stamp cigarettes or we figure out through this study that we are not going to do it and then we are done with it and move on.

John Olson, Philip Morris USA Inc. – I just distributed testimony from Michael Thorne-Begland (attachment B). I don't intend to read it; I will just give it to you for your consideration.

Mike Rud, The North Dakota Petroleum Marketers Association – We too are in favor of this study. I've got members on both sides of this issue and we would like to see some resolution to it. I think the Native American issue is a huge issue that we need to resolve.

Myles Vosberg, Tax Department – Commissioner Fong asked me to throw in our support for this study. It's a complicated issue that has come up every session for several sessions. There are a lot of groups involved and we think there has not been adequate time to study so we too think it would be a good idea to study this issue and include law enforcement in that study as to if there is stamping, how the enforcement would take place as part of that.

Chairman Cook – When you say include law enforcement do you mean, make sure they are there, or are you saying amend the bill?

Myles Vosberg, Tax Department – I think they should be part of the discussion and part of the study as to how they could contribute to enforcement if stamping is put in to place.

Chairman Cook asked for testimony opposed to HCR 3030. No one came forward.

Chairman Cook asked for neutral testimony for HCR 3030. No one came forward.

Chairman Cook closed the hearing on HCR 3030.

Vice Chairman Miller – I'll move a Do Pass.

Seconded by **Senator Triplett**.

Chairman Cook – All in favor say yea. (4-0-3)

Carried by **Vice Chairman Miller**.

Date: 3-7-11
Roll Call Vote # 1

2011 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 3030

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken: ☒ Do Pass ☐ Do Not Pass ☐ Amended ☐ Adopt Amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Senator Miller Seconded By Senator Triplett

Senators	Yes	No	Senators	Yes	No
Dwight Cook – Chairman			Jim Dotzenrod		
Joe Miller – Vice Chairman			Connie Triplett		
Randy Burckhard					
David Hogue					
Dave Oehlke					

Total (Yes) 4 No 0

Absent 3

Floor Assignment Senator Miller

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

REPORT OF STANDING COMMITTEE

HCR 3030, as engrossed: Finance and Taxation Committee (Sen. Cook, Chairman)
recommends **DO PASS** (4 YEAS, 0 NAYS, 3 ABSENT AND NOT VOTING).
Engrossed HCR 3030 was placed on the Fourteenth order on the calendar.

2011 TESTIMONY

HCR 3030

Mr. Chairman, members of the committee my name is Allan Stenehjelm. I appear here today on behalf of Reynolds American. This resolution was put in at their request. Thank you, for giving me the opportunity to present their views in support of HCR 3030.

The issue of stamping cigarettes is not new to this committee. Bills have been introduced since 2003 to address the need to stamp cigarettes in North Dakota. This is a complex issue that needs to be worked out between all parties. The Tobacco Industry, wholesalers, retailers, Tax Department and certainly the State Legislature, who sets the policy to collect a tax on all cigarettes sold in the State.

Reynolds American and the other leading tobacco companies are concerned about illegally sold or "contraband" cigarettes.

Illegal sales negatively impact Reynolds American 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.

Two issues are important here, one is to put a stop to the sale of counterfeit cigarettes, the second is to make sure the tax on cigarettes sold in the state are paid.

While most in the industry agree on the need to stamp cigarettes in North Dakota, there have been differences amongst the various groups over the years on how best to accomplish this.

This study would go a long way in resolving issues such as:

#1 p. 2

- Define the time period in which wholesalers would be required to stamp cigarettes
- How to promote state-tribal collection agreements that would encourage the application of a tax stamp.
- At what rate should wholesalers be reimbursed for their efforts?
- Should North Dakota implement minimum pricing for cigarettes?
- Does North Dakota have a contraband cigarette problem?
- Are there instances where cigarette taxes are not collect?
- What burden would this place on the Tax Department?

Mr. Chairman and committee members, these are just a few of the questions and concerns I identified as I read the testimony of stamping legislation since 2003. In the process of moving forward with this legislation for the 2011 session I discovered that the same questions remain unanswered. The various parties are willing to work on a resolution to this issue and this study would provide the vehicle for that to happen.

Thank you for your time,

Allan Stenehjem

#2 p.1



February 14, 2011

Good Morning Mr. Chairman and member of the committee

My name is John Job. I am the Northern Division Manager for AMCON Distributing Company.

I have compiled some additional information for your review during the consideration of stamping cigarettes for the state of North Dakota. The information will be presented as follows:

1. About AMCON.
 2. Neighboring state information.
 3. Equipment needed.
 4. Labor requirements.
 5. Security provided
 6. Wholesaler questions.
-
1. AMCON Distributing Company is a leading wholesale distributor of consumer products, including beverages, candy, tobacco, groceries, foodservice, frozen and chill foods, and health and beauty products with locations and customers in the Great Plains and Rocky Mountain regions of the United States. AMCON is a publicly traded company on AMEX with DIT as its symbol. AMCON Distributing Company's North Dakota distribution center is located at 3125 East Thayer Avenue, Bismarck, ND 58501. We own and occupy the north half of the block between 31st street and Eastdale Drive. AMCON employs between 55 & 60 people, depending on the time of the year. Our 2011 budgeted salary expense is more than \$ 2,225,000. Please visit amcon.com for additional information.
 - 2 South Dakota has minimum pricing. The minimum pricing formula is manufacturer list price less any purchase discounts plus the stamp value plus 5.5% mark-up. South Dakota Department of Revenue administers the minimum pricing within the state by posting this information publicly on their web site. Their tax stamps are ordered using a form that is sent in with a check. They have a stamp pre-purchase discount of \$ 0.10 cents per carton.

3125 East Thayer Avenue -- Bismarck, ND 58501

Montana has minimum pricing. The minimum pricing formula is manufacturer list price to the wholesaler plus 5.75% markup. Montana Department of Revenue administers the pricing within the state by posting this information publicly on their web site. Their tax stamps are pre-purchased by creating an order and paid for by ACH payment. The stamps are then shipped to our location. They have a pre-purchase discount of decreasing percentages depending on the wholesaler's volume. We use \$.07 cents per carton in determining the value of the discount in Montana.

Minnesota has minimum pricing. The minimum pricing formula is manufacturer list price to the wholesaler plus the stamp value plus \$ 0.67 per carton. The Minnesota Department of Commerce administers the pricing within the state by posting this information publicly on their web site. Their tax stamps are pre-purchased by creating an order and paid for by ACH payment. The stamps are then shipped to our location. Minnesota has no stamping purchase discount.

- 3 AMCON Distributing Company would need to purchase additional equipment in order to stamp North Dakota cigarettes. There is a misconception that since we have a stamping machine it would be easy for us to stamp another state. At the present time our stamping crew is working four 10 hour shifts per week stamping slightly less than 50% of our cigarette volume. Our North Dakota volume is slightly more than 50% of our total cigarette volume in the Bismarck Distribution Center. We will need to acquire an additional stamping machine in order to stamp another state. We would need to stamp with both machines in order to satisfy our customer commitments. We have secured a price quote dated January 27, 2011 from United Silicone on Meyercord stamping and handling equipment. By analyzing the bid AMCON would have an additional minimum investment of \$145,000 to stamp North Dakota. We have also requested a bid on Red Stamp equipment, however, we have not received that bid as yet. Copies of the United Silicone bid are available.
- 4 In order to run the new equipment we would also need to hire and train two additional employees to stamp during the shifts. We would also need to invest some time of our maintenance people to install and service the equipment on a regular basis. We estimate approximately \$100,000 of additional annual salary and benefits to provide for the labor necessary to stamp North Dakota cigarettes.
- 5 AMCON has invested in a wide variety of security equipment in order to protect our inventory and property. We do keep our extra cigarette tax stamps locked up and very secure at all times. We do daily audits of cigarettes and stamps in order to make sure stamps and cigarettes are

accounted for. Having one more state to audit will add to our daily audit. We would need to re-evaluate security if we would have to carry and stamp cigarettes for the State of North Dakota instead of collecting and paying the State excise tax monthly.

- 6 The primary concerns of the wholesaler are the cost of labor and equipment we would be required to provide in order to stamp cigarettes. Our other concerns will need to be addressed during the rules writing from the department that administers stamping. When will the state require payment of the stamps? Who will stand the loss of damaged stamps? What will the value of the stamps affixed to products returned to the manufacturer on outdated products be? Will customer credits for returned product be allowed at full value? Will tribal stamps be a requirement for all sales sold on tribal land within the states boundaries? Will there be any cigarette excise tax relief for bankrupt ND retailers?.

In closing AMCON Distributing Company is committed to doing business in North Dakota. Collecting the cigarette excise tax for the state is one of those commitments. We will stamp North Dakota cigarettes, we just do not have a desire to commit to additional labor and equipment at our expense to complete this task. We feel a minimum price at the wholesale level similar to our surrounding states on cigarettes is necessary in order to continue our commitments to North Dakota. The minimum pricing should be administered by a state agency similar to our surround states. The formula should use manufacturer list price plus the stamp plus the markup to cover the wholesaler responsibility. In order to make sure all cigarettes are stamped and all excise taxes are collected a minimum amount on a highly regulated product should be a part of the stamping bill. I welcome this opportunity to address all of these concerns in a study to assist by providing information necessary for North Dakota.

Respectfully submitted,

John F. Job
Northern Division Manager

#3 p. 1

PROPOSED AMENDMENTS TO HOUSE CONCURRENT
RESOLUTION NO. 3030

Page 1, line 2, remove "to ensure compliance with tobacco products"

Page 1, line 3, remove "tax laws"

Page 1, remove lines 6 through 11

Page 1, line 12, replace "effects" with "feasibility and desirability"

Page 1, line 13, replace "effects of the requirement" with "benefits and detriments of
requiring cigarette tax stamps"

Page 1, line 18, remove "to ensure compliance with tobacco products tax laws"

Renumber accordingly

#3 p. 2

Sixty-second
Legislative Assembly
of North Dakota

HOUSE CONCURRENT RESOLUTION NO. 3030

Introduced by

Representatives Headland, Owens, S. Meyer

Senators Cook, Miller, Triplett

A concurrent resolution directing the Legislative Management to study the feasibility and desirability of requiring use of cigarette tax stamps.

WHEREAS, North Dakota is one of only three states that do not require tax stamps on cigarettes; and

WHEREAS, a study of the feasibility and desirability of requiring tax stamping on cigarettes will allow consideration of the benefits and detriments of requiring cigarette tax stamps on the state, wholesalers, the public, and administrative and law enforcement agencies;

NOW, THEREFORE, BE IT RESOLVED BY THE HOUSE OF REPRESENTATIVES OF NORTH DAKOTA, THE SENATE CONCURRING THEREIN:

That the Legislative Management study the feasibility and desirability of requiring use of cigarette tax stamps; and

BE IT FURTHER RESOLVED, that the Legislative Management report its findings and recommendations, together with any legislation required to implement the recommendations, to the Sixty-third Legislative Assembly.

Mr. Chairman, members of the committee my name is Allan Stenehjelm. I appear here today on behalf of Reynolds American. This resolution was put in at their request. Thank you, for giving me the opportunity to present their views in support of HCR 3030.

The issue of stamping cigarettes is not new to this committee. Bills have been introduced since 2003 to address the need to stamp cigarettes in North Dakota. This is a complex issue that needs to be worked out between all parties. The Tobacco Industry, wholesalers, retailers, Tax Department and certainly the State Legislature, who sets the policy to collect a tax on all cigarettes sold in the State.

Reynolds American and the other leading tobacco companies are concerned about illegally sold or "contraband" cigarettes.

Illegal sales negatively impact Reynolds American 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.

Two issues are important here, one is to put a stop to the sale of counterfeit cigarettes, the second is to make sure the tax on cigarettes sold in the state are paid.

While most in the industry agree on the need to stamp cigarettes in North Dakota, there have been differences amongst the various groups over the years on how best to accomplish this.

This study would go a long way in resolving issues such as:

- Define the time period in which wholesalers would be required to stamp cigarettes
- How to promote state-tribal collection agreements that would encourage the application of a tax stamp.
- At what rate should wholesalers be reimbursed for their efforts?
- Should North Dakota implement minimum pricing for cigarettes?
- Does North Dakota have a contraband cigarette problem?
- Are there instances where cigarette taxes are not collect?
- What burden would this place on the Tax Department?

Mr. Chairman and committee members, these are just a few of the questions and concerns I identified as I read the testimony of stamping legislation since 2003. In the process of moving forward with this legislation for the 2011 session I discovered that the same questions remain unanswered. The various parties are willing to work on a resolution to this issue and this study would provide the vehicle for that to happen.

Thank you for your time,

Allan Stenehjem

HCR 3030

**STATEMENT OF MICHAEL THORNE-BEGLAND
SENIOR DIRECTOR OF BRAND INTEGRITY
AND ASSISTANT GENERAL COUNSEL
ALTRIA CLIENT SERVICES INC.**

SUBMITTED ON BEHALF OF PHILIP MORRIS USA INC.

SENATE FINANCE AND TAX COMMITTEE

IN SUPPORT OF ND HCR 3030 – TAX STAMP STUDY RESOLUTION

Altria Client Services Inc., on behalf of Philip Morris USA Inc. (PM USA),¹ submits this testimony regarding HCR 3030, which would require North Dakota Legislative Management to study the feasibility and desirability of cigarette tax stamps and report any findings to the next Legislative Assembly.

PM USA supports the North Dakota Legislature's efforts to research the need for and value of applying state excise tax stamps to cigarette packs sold in the state. PM USA believes that the application of state excise tax stamps is an important component of a comprehensive approach to address the illicit cigarette trade. Because cigarette excise tax rates vary from state to state, it is important that each state require excise tax stamps that signify the tax paid status of the pack and identifies that the pack is for sale in that specific state.

We are optimistic that an in-depth analysis of the feasibility and desirability of cigarette tax stamps in North Dakota will support the enactment of tax stamp legislation during the next Legislative Assembly.

¹ PM USA, a leading domestic manufacturer of cigarettes, is a wholly-owned subsidiary of Altria Group Inc.



Background

PM USA commends the committee for holding hearings on legislation relating to the issue of the illicit cigarette trade. Illicit cigarette sales have dramatically increased in recent years² with the sharp rise in excise taxes throughout the United States.

Contraband cigarette smuggling has been linked to organized crime and terrorist organizations in the U.S.³ The illicit sale of cigarettes and other tobacco products has many costs:

- Illicit cigarette sales reduce tax revenues for federal, state and local governments.
- Illicit cigarette sales undermine efforts to prevent youth access to cigarettes.
- Illicit cigarette sales deprive revenue from local, law-abiding wholesalers and retailers who fully comply with all applicable laws and thereby find themselves at a competitive disadvantage.
- Contraband cigarette trafficking is used by organized crime syndicates as a source of income to support other criminal activity and is often associated with other more serious crimes.

Some criminals engaged in the illicit cigarette trade exploit the variance in state excise taxes to generate immense illegal profits at the expense of legitimate, tax-paying businesses. To help address this problem, PM USA believes that all states should require that a wax-based tax stamp be affixed to each pack of cigarettes. These stamps should include security features to aid law enforcement authentication and a serial number or, where applicable, a stamp that denotes that the cigarettes are tax-exempt (e.g. qualified

² Bureau of Alcohol Tobacco, Firearms & Explosives (ATF) March 2010 *ATF Tobacco Diversion Fact Sheet*

³ *International Journal of Comparative and Applied Criminal Justice*. Spring 2008, Vol. 32, No. 1- The Nexus of Organized Crime and Terrorism: Two Case Studies in Cigarette Smuggling



Native American sales). North Dakota is one of only three states that do not require tax stamps on cigarette packs.

In our experience, untaxed cigarettes are the most common form of contraband cigarettes. Untaxed cigarettes include those that are sold with no tax stamp in a jurisdiction that requires one, cigarettes with the wrong tax stamp for the jurisdiction in which it was sold, and cigarettes sold with counterfeit tax stamps. PM USA believes that this study bill will identify the risks of the illicit cigarette trade and the benefits of cigarette excise tax stamping, and thus support the enactment of tax stamping legislation. State cigarette excise tax stamps will help reduce the trade in untaxed cigarettes and will help address issues facing the legitimate North Dakota cigarette trade. Among other things, the study bill should consider:

- North Dakota requires a state excise tax to be paid for each pack of cigarettes for qualified sales. Without a state excise tax stamp there is no way to physically distinguish legitimate tax-free product from product that is subject to the state excise tax.⁴ Thus, North Dakota cigarette excise tax revenue is unprotected.
- Law enforcement information indicates that traffickers of contraband cigarettes are intent on buying unstamped cigarettes for their illegal operations.⁵ North Dakota's lack of state specific excise tax stamp on cigarette packs may attract

⁴ Native American cigarette sales not covered by a state tobacco tax compact in North Dakota are exempt from state excise taxes for sales to tribal members and sales of two-hundred cigarettes or less to non-tribal members.

⁵ April 28th, 2010 BNO news *Glendale, CA man sentenced for smuggling cigarettes*



criminal cigarette traffickers and organized crime syndicates into the state.

Businesses in North Dakota may unknowingly sell unstamped cigarettes to criminals who then re-sell the products to fund other criminal activity.

- As the illicit, unregulated channels grow, the effectiveness of underage access prevention measures in regulated retail trade channels would diminish and jeopardize progress on reducing underage initiation. In addition, with increased access to cigarettes through the illicit market comes the likely exposure of minors to other criminal activities associated with those markets.
- Wax-based cigarette excise tax stamps are currently in use in 45 states. They can cost as little as 50¢ per thousand.⁶
- Wax-based cigarette excise tax stamps typically use serial numbers that can enable law enforcement to determine the identity of the wholesaler that applied the tax stamp; a useful tool when attempting to investigate contraband issues.
- Authentication technology is available for wax-based tax stamps that provide law enforcement the ability to readily determine if the tax stamp is genuine or counterfeit.
- The majority of wholesalers who ship cigarettes to North Dakota retailers also ship to surrounding states that require tax stamps. Thus, these wholesalers have the machines necessary to apply the wax-based tax stamps currently utilized by other states.

⁶ June 3, 2008 letter from Patrick O'Conner, Assistant State Treasurer of New Jersey regarding Senate Bill No. 1545



Conclusion

PM USA supports North Dakota's efforts to study the feasibility and desirability of cigarette tax stamps and the resulting impact on the illicit cigarette trade. There is a wealth of information available that documents the scope and consequences of the illicit cigarette trade and the benefits of state cigarette excise tax stamps. We believe that if North Dakota decides to pursue the study, Legislative Management will discover the value of wax-based cigarette excise tax stamps far outweighs the minimal cost of introduction.

We welcome the opportunity to work with North Dakota to address its contraband cigarette issues.

