F I S C A L   I M P A C T   R E P O R T

SPONSOR Beam **DATE TYPED** 2-16-04 **HB** 84

SHORT TITLE Nonparticipating Tobacco Manufactures **SB**

ANALYST Neel

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY04	FY05			
		See Narrative	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates: Senate Bill 67, Nonparticipating Tobacco Manufactures

Relates to:

HB 59, Increase Tobacco Products Tax
HB 86, Tobacco Stamp Procedure Changes
HB 220, Tobacco Settlement Revenue Appropriation
SB 192, Smart Moves Smoking Cessation Program Funding
HM 1, Promote Cigarette Taxation Parity

SOURCES OF INFORMATION
LFC Files

Responses Received From
Human Services Department (HSD)
Department of Health (DOH)
Department of Finance and Administration (DFA)

No Response Received From:
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 84 amends Section 6-4-13 (the Model Tobacco Escrow Statute) to change the criteria whereby tobacco companies that do not participate in the tobacco Master Settlement Agreement (MSA) or nonparticipating manufactures (NPM) may receive an early release of monies they are required by state law to escrow to provide a fund for future claims the state may bring against them.

Additionally SB 67 enacts a new section of law regarding the severability of the amended language in Paragraph (2) of Subsection B of Section 6-4-13 NMSA 1978, should it be found to be unconstitutional.

Significant Issues

According to the AG, the amendment is necessary to fix a problem that has been costing the states under the MSA hundreds of millions in reduced settlement payments. It is estimate that the loss to New Mexico last year was effectively $2.6 million and the effective loss this year is anticipated to be $3.8 million. Current law allows NPM access to escrowed funds under three criteria one of which one is when it establishes the amount that it is required to place into escrow is greater than what the manufacturer would have been required to pay had it participated in the MSA or the individual state's allocable share (in NM 0.6 percent). Under SB 67, NPM would only obtain an early release of escrowed amounts in excess of an amount calculated on the basis of the actual units or cigarette sticks sold in New Mexico.

The intent of the Model Statute was twofold: To protect the public health gains achieved by the Master Settlement Agreement (MSA) and to create a level playing field between the forty some companies on the MSA who abide by the MSA' marketing restrictions and make settlement payments to New Mexico and the remaining tobacco companies who make no settlement payments and have no marketing restrictions by agreement. The AG states, the NPM have discovered that by strategically targeting states with low allowable share (i.e. New Mexico at 0.6 percent), they can receive refunds equaling most of the payments placed in escrow. This unforeseen outcome gives NPM a price advantage against the companies that have signed onto the agreement and undermines the intent of the settlement. The larger the leakage due to this activity the larger the adjustments to the state's payments.

If the OPMs lose market share and are able to show that the loss is a result of the agreement, the state's payments will be reduced by three-times the market share loss. Market share loss of the four major companies is currently at about 8-percent. If the OPMs are able to show that the model statute has not been diligently enforced and that the loss is due to the agreement, the state's annual payments will be reduced by an additional 24-percent, or $8.4 million each year and depending upon the application of the adjustment it could eliminate the entire annual settlement payment.

FISCAL IMPLICATIONS

There is no direct fiscal impact because the amendment changes the method by which NPM obtain early release of escrowed funds. However there is potentially a long-term positive fiscal impact with lower erosion rates for MSA payments.

OTHER SUBSTANTIVE ISSUES

DFA provided the following substantive issues:

Following the MSA, original participating manufactures (OPMs) will be making base payments totaling $229 billion through 2025. Since the agreement, the state has received payments totaling $176.3 million and collects about $37 million annually. Base payments are adjusted for volume. The adjustment reflects OPM sales volume losses since the agreement. Through 2003, the adjustment is approximately 27.8 percent, representing a cumulative loss of $52.6 million of revenue to the state since 2000. The volume adjustment was initially about three-percent a year, but has escalated to five and six percent in the last two years, respectively. Volume adjustment levels this high indicate that there is significant substitution away from OPM brand cigarettes.

SN/yr