

2013 SENATE FINANCE AND TAXATION

SB 2106

2013 SENATE STANDING COMMITTEE MINUTES

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

SB 2106
1/16/2013
Job Number 17275

Conference Committee

Committee Clerk Signature

Angela K. Miller

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to create and enact sections 57-36-05.3, 57-36-05.4, and 57-36-06.1 of the North Dakota Century Code, relating to the operation of roll-your-own cigarette-making machines; to amend and reenact sections 57-36-01 and 57-36-33 of the North Dakota Century Code, relating to the definitions of cigarette and roll-your-own cigarette-making machine for tobacco products tax purposes; to provide a penalty; and to provide an effective date.

Minutes:

Testimony Attached

Chairman Cook opened the hearing on SB 2106.

Daniel L Rouse, Legal Counsel, ND Office of State Tax Commissioner - See attached testimony 1 in support of SB 2106 and proposed amendment (attachment 2).

Senator Oehlke - We found out where one of the potentially 3 machines was in, in the state, do you have any idea where the others may or may not be?

Daniel L Rouse - No.

Senator Oehlke - Might this be a predominant issue on reservations and can you do anything about it if it were?

Daniel L Rouse explained that any activity is unknown and if there would be, they have no authority on enforcement. He thinks it is more common in smoke shops.

Senator Burckhard - Are these cigarette making machines made in America?

Daniel L Rouse - Yes, the majority are.

Senator Dotzenrod - Did this come to the attention of the tax department because there was some situation in our state or is this more a result of communication around the country that this is showing up in other states and the tax department thought it was a good idea to do this, not so much because we've got particular situations here but because it's something they see coming.

Daniel L Rouse - It's a combination of both of those. We were aware this is a new phenomenon around the country, we were aware that there were machines entering into North Dakota, we were concerned that we didn't have any regulatory structure at the state level, to one, allow this type of business enterprise to take place if people so chose to do so, but to make sure they knew what the playing field looked like. So, I believe it was a combination, and we did receive some information from other states and industry and collected and coalesced all of that into what you see before you today. So the answer is yes and yes.

Vice Chairman Campbell - Approximate is \$.44 I believe for pack on tax so we are missing out on that full \$.44 I'm assuming, that is my first question, and second, smoke shops, I don't know about North Dakota, but in Minnesota most sell paraphernalia related with marijuana or illegal tobacco, are these cigarette machines doing that a well? Is that another reason this should be pursued?

Daniel L Rouse - With respect to your first question at a minimum right now the state is receiving the 28% tax that is applied at the whole sale level on the acquisition by the manufacturer of the pipe tobacco. It's just that there is such a disparity between that and the cigarette tax rate that you see the wide range. And again incidentally that's really not the primary focus for this bill; the focus is to establish the framework within which these manufacturers can operate. With respect to your second question, I suppose anything could happen, from the research I have done, I've not detected a sense of blending, although it could happen.

Senator Triplett - Are there health related issues for taking pipe tobacco and putting it in a cigarette? Does it smoke differently? Do you know the health implications?

Daniel L Rouse - I'm not a medical professional so I truly don't know what the research has shown if anything.

Daniel L Rouse then went on to explain that pipe tobacco is much more course than cigarette tobacco so there may be less tobacco going into a cigarette made with pipe tobacco.

Mike Rud, ND Retail Association and Petroleum Marketers Association briefly explained that they do not want any association with anything that may be illegal or that does not have good manufacturing practices.

Barbara Andrist, Center for Tobacco Prevention and Control - I am here just to offer support for SB 2106.

Chairman Cook asked for testimony opposed and then for neutral testimony.

Chairman Cook closed the hearing on SB 2106.

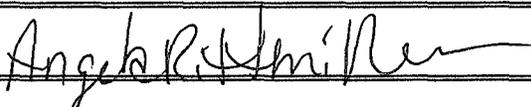
2013 SENATE STANDING COMMITTEE MINUTES

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

SB 2106
1/30/2013
Job Number 18001

Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

A BILL for an Act to create and enact sections 57-36-05.3, 57-36-05.4, and 57-36-06.1 of the North Dakota Century Code, relating to the operation of roll-your-own cigarette-making machines; to amend and reenact sections 57-36-01 and 57-36-33 of the North Dakota Century Code, relating to the definitions of cigarette and roll-your-own cigarette-making machine for tobacco products tax purposes; to provide a penalty; and to provide an effective date.

Minutes:

Committee Work

Chairman Cook opened discussion on SB 2106.

Senator Miller - I'll move the amendment.

Chairman Cook - We have a motion to change the first word on line 24 'must' to 'may'.

Seconded by **Senator Oehlke**.

Verbal Vote 7-0-0

Senator Miller - I'll move a **Do Pass as Amended**.

Seconded by **Vice Chairman Campbell**.

Discussion followed on the difference between personal use rolling machines and commercial use machines intended to sell the tobacco product.

Roll Call Vote 7-0-0

Carried by **Vice Chairman Campbell**.

FISCAL NOTE
Requested by Legislative Council
12/21/2012

Bill/Resolution No.: SB 2106

- 1 A. **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.*

	2011-2013 Biennium		2013-2015 Biennium		2015-2017 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

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

	2011-2013 Biennium	2013-2015 Biennium	2015-2017 Biennium
Counties			
Cities			
School Districts			
Townships			

- 2 A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

SB 2106 addresses requirements for the operation of roll-your-own cigarette-making machines.

- B. **Fiscal impact sections:** *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

SB 2106 requires permits and registrations of persons using roll-your-own cigarette machines. Cigarettes made on these machines are subject to wholesale tobacco taxes. If enacted, SB 2106 may have a small positive fiscal impact; however, the amount cannot be determined.

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, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*



Name: Kathryn L. Strombeck

Agency: Office of Tax Commissioner

Telephone: 701.328.3402

Date Prepared: 12/27/2012



13.8126.01001
Title.02000

Adopted by the Finance and Taxation
Committee

January 30, 2013

VJR
1/30/13

PROPOSED AMENDMENTS TO SENATE BILL NO. 2106

Page 4, line 19, overstrike "must" and insert immediately thereafter "may"

Renumber accordingly

Date: 1-30-13
Roll Call Vote #: 1

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 2106

Senate Finance & Taxation Committee

Check here for Conference Committee

Legislative Council Amendment Number 13.8126.01001 file 02000

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

Motion Made By Senator Miller Seconded By Senator Oehlke

Senators	Yes	No	Senator	Yes	No
Chariman Dwight Cook			Senator Jim Dotzenrod		
Vice Chairman Tom Campbell			Senator Connie Triplett		
Senator Joe Miller					
Senator Dave Oehlke					
Senator Randy Burckhard					

Total (Yes) 7 No 0

Absent 0

Floor Assignment _____

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

Verbal vote

Date: 1-30-13
Roll Call Vote #: 2

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 2106

Senate Finance & Taxation Committee

Check here for Conference Committee

Legislative Council Amendment Number 13.8126.01001 Title 02000

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

Motion Made By Senator Miller Seconded By Senator Campbell

Senators	Yes	No	Senator	Yes	No
Chairman Dwight Cook	X		Senator Jim Dotzenrod	X	
Vice Chairman Tom Campbell	X		Senator Connie Triplett	X	
Senator Joe Miller	X				
Senator Dave Oehke	X				
Senator Randy Burckhard	X				

Total (Yes) 7 No 0

Absent 0

Floor Assignment Senator Campbell

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

REPORT OF STANDING COMMITTEE

SB 2106: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). SB 2106 was placed on the Sixth order on the calendar.

Page 4, line 19, overstrike "must" and insert immediately thereafter "may"

Renumber accordingly

2013 HOUSE FINANCE AND TAXATION

SB 2106

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

SB 2106
March 11, 2013
Job #19678

Conference Committee

Committee Clerk Signature

Mary Bruecker

Explanation or reason for introduction of bill/resolution:

A Bill relating to the operation of roll-your-own cigarette-making machines; relating to the definitions of cigarette and roll-your-own cigarette-making machine for tobacco products tax purposes.

Minutes:

Attached testimony #1.

Chairman Belter: Opened hearing on SB 2106.

Dan Rouse, Legal Counsel for the North Dakota Office of State Tax Commissioner:

See attached testimony #1. Viewed a two minute You Tube video on roll your own cigarette making machines (<http://ryofillingstation.com/video.php>).

Vice Chairman Headland: Where is the closest place a person could use one of these machines and how much does it cost?

Dan Rouse: At the last opportunity we had to verify it there is one in Dickinson, Williston, and Bismarck. It's considerably less than what you have to pay now for a pack or a carton of cigarettes. These things come out one at a time and you collect them in a tote and put them in whatever box you have. The tax rate is considerably different from what you would have to pay if you were going to a convenience store and purchasing cigarettes.

Representative Kelsh: Are we also going to tax the older machines that our grandfathers used if it's for personal use?

Dan Rouse: No. We specifically carve out personal consumption from this.

Representative Klein: You indicate there is tobacco that is exempt from federal tax?

Dan Rouse: There is a small amount of tobacco that is used for law enforcement training, investigatory purposes, and some of that is exempt from tax. That's not the focus of this but we have to include that as an exception to this so that we make sure we are covering all our bases.

Representative Schmidt: RYO does not sell the tobacco product, correct?

Dan Rouse: RYO is an acronym that is used for the roll your own machines. When you go into a facility that has one of these vending machines you pay a certain fee for the tobacco and then dump into the machine and it spits out the cigarettes for you.

Representative Schmidt: When I buy the tobacco as a separate item I pay the tax on the loose tobacco, correct?

Dan Rouse: That is correct.

Representative Schmidt: I pay the tax on the tobacco and put it into the machine and it spits out a completed cigarette. The bill proposes to increase the taxes to the company that owns the machine?

Dan Rouse: That's correct. This bill recognizes that what is happening in front of your eyes is the manufacturing of a cigarette not any other form of tobacco but a cigarette. Cigarettes have a specific rate of taxation that is different than a tax you would pay if you would have just gone into a smoke shop and bought a pouch of tobacco for chewing, snuff, or putting into your pipe. More commonly folks are buying pipe tobacco which is a much coarser cut but it still seems to be fitting within the confines of these machines into the process of turning it into a cigarette.

Representative Schmidt: When I buy that machine I would pay taxes on the machine when I bought it, correct?

Dan Rouse: There would be an incident of sales tax on the machinery.

Representative Schmidt: I pay sales tax on the machine then I pay another tax when the cigarettes go through it?

Dan Rouse: That's correct, just as like anyone who would have a vending machine of any other sort.

Representative Drovdal: How are you going to determine a licensing fee and what would that fee be? Are all machines treated equally?

Dan Rouse: The fee for the licensure is established by the attorney general's office. I would expect them to look around the country to see what the comparable fees would be. We are looking for an opportunity to measure the product that is being purchased by the consuming public then applying the cigarette tax rate to that purchase.

Representative Froseth: Is the sales tax collection method tracked to see who's buying them? Is the class C felony consistent with other states? It seems like that is a severe penalty for making an illegal cigarette.

Dan Rouse: Yes, payment of sales tax would require the person who is buying the machine to report it to us as well as the attorney general's office. That would be our

opportunity to track where those machines are. One of the primary purposes here is not to discourage this type of activity in the state but to make sure that the state, because we are in a regulatory capacity here, that we are aware of where those machines are and that they are registered, licensed and tracked for purposes of tax components as well. The class C felony is consistent with what other states are doing. A class C felony is indeed a serious offense, it is certainly not something where a person would see a long term imprisonment or fine but it is consistent with what other states are doing. These machines are putting out a lot of cigarettes and there is a lot of activity so if it is not treated appropriately it could be something that is easily disregarded.

Representative Owens: Map 21 identified these machines as manufacturing and set up a licensing for it. This bill is designed to duplicate that at the state level, is that correct?

Dan Rouse: Correct.

Representative Owens: It is our intent to then tax at a minimum the difference associated between cigarettes and that initial on a tax of just raw tobacco because of the manufacturer of cigarettes within the boundaries of the state, is that correct?

Dan Rouse: Because the federal law recognizes it as manufacture of cigarettes if this law is enacted the state would recognize this process as the manufacturing of cigarettes that it would ensure the appropriate level of tax is paid on that manufactured product.

Representative Owens: How is the tax department going to police this? How are you going to know how many cigarettes are made? Is there a counter of some sort?

Dan Rouse: Yes there is a counter on these and it tells how many cigarettes are put out. That's another reason, in conjunction with the attorney general's office with respect to the enforcement side of this, we would have a clear idea of what was being produced because those machines would have to be licensed, inspected on a routine basis, and we would ask for production of the manufacturing results from the manufacturer to us.

Chairman Belter: Can more than one individual own a machine?

Dan Rouse: That seems to be one of the more recent developments in this area where people are developing social clubs or some sort of interest groups and instead of treating them as a retail sale of a tobacco product they end up getting together to talk about cigarettes and tobacco and at the same time they are producing cigarettes. The way we have this bill designed we are looking at the retail production or the manufacturing component of this. I think this will continue to be an evolving area of law and at some point we may look at other ways to ensure the activity that is being done with these machines is being regulated and taxed at the appropriate level. Right now in the current language of the bill we are not interested in coming to your garage or house to see what you're doing on your own we are looking at the retail part of it.

Chairman Belter: If I'm an owner of one of these and I work at a business and have 25 friends who smoke then they each give me a bag of tobacco to take home to make cigarettes for them I could do that and not be in violation of the law?

Dan Rouse: I think if you look at the language that we've developed which states "consumed by the individual who owns the machine or by other persons whose consumption is incidental to that owner's personal use of the machine" I think there is a reasonableness factor that we would have to apply to this as well. We'd have to look and see what the intent was.

Representative Zaiser: Is it possible for an operator of a RYO machines to adjust the compaction rate of the tobacco or different sizes?

Dan Rouse: We have observed that they are relatively uniform as far as the size of any other cigarette. The compaction rate is going to be driven primarily by the machine itself. The puff of air in that machine is what drives that tobacco into that roll and then the paper is rolled into a cigarette. I assume you could change that compaction rate to whatever you wanted.

Representative Drovdal: The purpose of this bill isn't to collect a registration fee but to get a handle on the taxes that are due on cigarettes. You're going to have a tax for those cigarettes that this machine is going to make. Are these individuals who have already paid the tax on the tobacco product be allowed the credit that they've already paid or are they going to be charged the whole value of what a cigarette pack would have been?

Dan Rouse: The objective is to first define that this is a manufacturing process and the end result is a cigarette. According to state law cigarettes are taxed at a certain level and it is our objective to ensure a level playing field.

Chairman Belter: Further testimony in support of 2106?

Mike Rud, President of the North Dakota Petroleum Marketers: We stand in support of 2106. This can create some uncompetitive advantages in certain places with these machines and if we're not careful with this we could have a whole bunch of cigarette smuggling potential. We want to make sure the taxes are paid in a proper manner and the money goes where it belongs.

Vice Chairman Headland: Are you aware or have any of your retailers you represent entered into this area of business?

Mike Rud: No one to my knowledge has taken part in this but I believe there is a shop in Dickinson and a potential in Williston but none of our retail sites have bought into one of these machines at this time. It's \$35,000 investment so you need to have money and space and people who know what they are doing as far as monitoring the situation as well.

Chairman Belter: Any other testimony in support? Any opposition to 2106? Any neutral testimony? If not, we will close the hearing on 2106.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

SB 2106
March 12, 2013
Job #19787

Conference Committee

Committee Clerk Signature

Mary Brucher

Minutes:

Chairman Belter: Can we have discussion on 2106 the cigarette machine?

Representative Schmidt: Apparently the guy that has to live with the law is a lot smarter than the guy that wrote it.

Representative Froseth: I have a problem with that class c felony charge; it seems like it's a pretty harsh charge for making a cigarette. I always thought a class c felony was a penalty for some personal harm of some type not for some type of material offense that basically doesn't endanger anyone's life or well-being. A class a misdemeanor would be one year in prison and a \$2,000 fine or both so I would think a class a misdemeanor would be sufficient.

Representative Klein: I agree with Representative Froseth. That's a pretty severe penalty for this type of thing. I think we should take that out.

Representative Froseth: I would suggest changing it to a class a misdemeanor. **Made a motion to change line 14 page 4 the penalty is guilty of a class a misdemeanor rather than a class c felony.** I don't know about those numbers 57-36-05.3.4 and 57-36-6.1 I don't know if those pertain to the penalties but they may need to be changed as well.

Chairman Belter: We have a motion to change, on page 4 line 14, class c felony to class a misdemeanor. Is there a second?

Representative Klein: Seconded.

Representative Froseth: On line 21 are the same numbers so I don't know if those have to be changed too or not.

Chairman Belter: Will (legal intern), will you make sure those numbers are correct or have to be changed. **We will make that part of the motion to make any necessary code revisions to comply with the class a misdemeanor.**

VOICE VOTE: MOTION CARRIED.

Chairman Belter: What are your wishes on this bill?

Representative Klein: Made a motion for a Do Pass as Amended.

Representative Dockter: Seconded.

Representative Dockter: The reason why I believe in this Do Pass is if, for example, you have a tobacco store and they are selling cigarettes and are paying higher they could put in a machine and pay a lower tax. I think it's more of an even playing field with the tax to make it level for everyone. It shouldn't hinder the people that have been in business and have a store front that people are going to their store and are already selling their product I don't think they should have a disadvantage by having a store front versus having a machine.

ROLL CALL VOTE: 10 YES 1 NO 3 ABSENT

Representative Froseth will carry this bill.

FISCAL NOTE
Requested by Legislative Council
12/21/2012

Amendment to: SB 2106

- 1 A. **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.*

	2011-2013 Biennium		2013-2015 Biennium		2015-2017 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

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

	2011-2013 Biennium	2013-2015 Biennium	2015-2017 Biennium
Counties			
Cities			
School Districts			
Townships			

- 2 A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

SB 2106 addresses requirements for the operation of roll-your-own cigarette-making machines.

- B. **Fiscal impact sections:** *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

SB 2106 requires permits and registrations of persons using roll-your-own cigarette machines. Cigarettes made on these machines are subject to wholesale tobacco taxes. If enacted, SB 2106 may have a small positive fiscal impact; however, the amount cannot be determined.

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, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*



Name: Kathryn L. Strombeck

Agency: Office of Tax Commissioner

Telephone: 701.328.3402

Date Prepared: 12/27/2012



13.8126.02001
Title.03000

Adopted by the Finance and Taxation
Committee

March 12, 2013

VIC
3/12/13

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL NO. 2106

Page 4, line 13, remove "In addition to the penalty in subsection 1, any person who violates sections"

Page 4, remove lines 14 through 16

Page 4, line 17, remove "3."

Renumber accordingly

Date: 3-12-13
Roll Call Vote #: 1

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 2106

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. Froseth Seconded By Rep. Klein

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter			Rep. Scot Kelsh		
Vice Chairman Craig Headland			Rep. Steve Zaiser		
Rep. Matthew Klein			Rep. Jessica Haak		
Rep. David Drovdal			Rep. Marie Strinden		
Rep. Glen Froseth					
Rep. Mark Owens					
Rep. Patrick Hatlestad					
Rep. Wayne Trottier					
Rep. Jason Dockter					
Rep. Jim Schmidt					

Vote - Motion Carried

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

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

*Line 14 page 4 - change to class A misdemeanors rather than class C felony.
Line 21 have the same numbers
Make any necessary code revisions
Voice Vote - Motion carried.*

Date: 3-12-13
 Roll Call Vote #: 2

**2013 HOUSE STANDING COMMITTEE
 ROLL CALL VOTES
 BILL/RESOLUTION NO. 2106**

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. Klein Seconded By Rep. Dockter

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter	✓		Rep. Scot Kelsh	✓	
Vice Chairman Craig Headland	✓		Rep. Steve Zaiser	✓	
Rep. Matthew Klein	✓		Rep. Jessica Haak	✓	
Rep. David Drovdal	AB		Rep. Marie Strinden	AB	
Rep. Glen Froseth	✓				
Rep. Mark Owens	AB				
Rep. Patrick Hatlestad	✓				
Rep. Wayne Trottier		✓			
Rep. Jason Dockter	✓				
Rep. Jim Schmidt	✓				

Total (Yes) 10 No 1
 Absent 3
 Floor Assignment Rep. Froseth

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

REPORT OF STANDING COMMITTEE

SB 2106, as engrossed: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (10 YEAS, 1 NAYS, 3 ABSENT AND NOT VOTING). Engrossed SB 2106 was placed on the Sixth order on the calendar.

Page 4, line 13, remove "In addition to the penalty in subsection 1, any person who violates sections"

Page 4, remove lines 14 through 16

Page 4, line 17, remove "3."

Renumber accordingly

2013 TESTIMONY

SB 2106

TESTIMONY OF THE OFFICE OF STATE TAX COMMISSIONER
BEFORE THE
SENATE FINANCE AND TAXATION COMMITTEE

SENATE BILL 2106

JANUARY 16, 2013

Good Morning, Chairman Cook and members of the Senate Finance and Taxation Committee. My name is Daniel L. Rouse, Legal Counsel for the North Dakota Office of State Tax Commissioner. I stand today on the Tax Commissioner's behalf, in support of Senate Bill No. 2106.

CURRENT LAW

The Tax Department is responsible for administering the taxation of tobacco products. Our office shares regulatory responsibilities for the tobacco industry with the Office of Attorney General. However, our agency's primary function with respect to tobacco products is the enforcement of the tobacco taxes. As you may be aware, under N.D.C.C. Chapter 57-36, different forms of tobacco (i.e., cigarettes, cigars, and pipe tobacco) have different rates of taxes imposed on sale of those products. Tobacco in the form of cigarettes is taxed at a higher rate than loose tobacco, such as that used for pipe smoking.

That difference in rates has led on occasion to some creative solutions by those who want to smoke cigarettes but don't want to pay the higher rate of taxes imposed on cigarettes. One example of that is found with the emerging roll-your-own cigarette making machine industry. Please bear in mind these aren't the small table-top machines that your grandfather might have used to roll his own cigarettes. Rather, these are huge machines, costing nearly \$35,000 each. (Incidentally, if you care to see what one of these machines looks like, go to: <http://www.youtube.com/watch?v=nvdVSd7ZEVg> and you will find a short video showing a RYO machine). The intent behind the use of these machines is to allow the rapid manufacture of cigarettes. But the unique aspect of these machines is that the operator can use loose tobacco – such as pipe tobacco – to manufacture the cigarettes. The end result of the process is production of cigarettes costing considerably less than normally-manufactured cigarettes because the tax rates are considerably less for the pipe tobacco used in the RYO machine. And, as it is a relatively new industry, few regulations are in place to deal with it.

Due to this lack of regulation of this growing industry, this past July, Congress approved, and the President signed into law, the “Moving Ahead for Progress in the 21st Century” Act (or the “MAP-21” Act). One provision of the MAP-21 Act provided that any person who for commercial purposes makes available, for consumer use (including the consumer’s personal consumption or use), a machine capable of making tobacco products is considered a “manufacturer of tobacco products.” In other words, the person who makes the machine available for consumer use is the person liable for the Federal excise tax on the resulting tobacco products. For example, if a retail store purchased and made the machine available to consumers, the retailer is a manufacturer of tobacco products under the federal law.

At present, North Dakota law does not recognize RYO or cigarette-making machines in the same manner as the Federal government does. This inconsistency has raised compliance challenges at the state level.

PROPOSED CHANGE TO THE LAW

Accordingly, Senate Bill 2106 proposes to amend North Dakota law to recognize persons who make RYO machines available for commercial purposes to be manufacturers of tobacco products. Specifically, in **Section 1**, we propose defining a “cigarette-making machine” in accord with the definition of RYO machines at the federal level. We also propose defining a cigarette to include the product of the RYO manufacturing process. This would then make RYO produced cigarettes subject to the tax rate applicable to other cigarettes. In **Section 2**, we propose to require the owner or operator of a RYO machine to have the Federal tobacco product manufacturer permit now required under Federal law unless the machine is used strictly for personal purposes. **Section 3** will require the RYO machine to be registered with the Attorney General. **Section 4** proposes that the RYO manufacturer provide specific information to the state, pay the appropriate taxes on the product sold, comply with the master settlement agreement provisions under N.D.C.C. chapter 51-25, use fire-safe paper to form the cigarettes, and use only federal tax-paid RYO tobacco or tobacco exempt from federal tax under Internal Revenue Service provisions. **Section 5** proposes certain penalties that the Tax Commissioner may impose on RYO manufacturers for failure to comply with these new laws. Finally, **Section 6** of the bill pushes out the effective date of this bill, if enacted, to provide adequate time for notice and public education to take place.

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CONCLUSION

In order for the Tax Department to ensure compliance with the tobacco products tax laws, and ensure that the laws are equitable with respect to similar types of tobacco products, this bill is necessary. By bringing North Dakota's laws forward with this bill -- and making our law parallel to federal law in this area -- you will give the Tax Commissioner the tools needed to ensure that compliance and equity are achieved.

For these reasons, I respectfully request that the Senate Finance and Taxation Committee give Senate Bill 2106 favorable consideration. I'll be happy to answer any questions you may have.

Prepared by the
Office of State Tax Commissioner
January 16, 2013

PROPOSED AMENDMENT TO SENATE BILL 2106

Page 4, line 22, replace "must" with "may"

Renumber accordingly

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**TESTIMONY OF THE OFFICE OF STATE TAX COMMISSIONER
BEFORE THE
HOUSE FINANCE AND TAXATION COMMITTEE**

ENGROSSED SENATE BILL 2106

MARCH 11, 2013

Good Morning, Chairman Belter and members of the House Finance and Taxation Committee. My name is Daniel L. Rouse, Legal Counsel for the North Dakota Office of State Tax Commissioner. I stand today on the Tax Commissioner's behalf, in support of Engrossed Senate Bill No. 2106.

CURRENT LAW

The Tax Department is responsible for administering the taxation of tobacco products. Our office shares regulatory responsibilities for the tobacco industry with the Office of Attorney General. However, our agency's primary function with respect to tobacco products is the enforcement of the tobacco taxes. As you may be aware, under N.D.C.C. Chapter 57-36, different forms of tobacco (i.e., cigarettes, cigars, and pipe tobacco) have different rates of taxes imposed on sale of those products. Tobacco in the form of cigarettes is taxed at a higher rate than loose tobacco, such as that used for pipe smoking.

That difference in rates has led on occasion to some creative solutions by those who want to smoke cigarettes but don't want to pay the higher rate of taxes imposed on cigarettes. One example of that is found with the emerging roll-your-own cigarette making machine industry. Please bear in mind these aren't the small table-top machines that your grandfather might have used to roll his own cigarettes. Rather, these are huge machines, costing nearly \$35,000 each. (Incidentally, if you care to see what one of these machines looks like, go to: <http://ryofillingstation.com/video.php> and you will find a short video showing a RYO machine). The intent behind the use of these machines is to allow the rapid manufacture of cigarettes. But the unique aspect of these machines is that the operator can use loose tobacco – such as pipe tobacco – to manufacture the cigarettes. The end result of the process is production of cigarettes costing considerably less than normally-manufactured cigarettes because the tax rates are considerably less for the pipe tobacco used in the RYO machine. And, as it is a relatively new industry, few regulations are in place to deal with it.

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Due to the lack of regulation of this growing industry, this past July, Congress approved, and the President signed into law, the “Moving Ahead for Progress in the 21st Century” Act (or the “MAP-21” Act). One provision of the MAP-21 Act provided that any person who for commercial purposes makes available, for consumer use (including the consumer’s personal consumption or use), a machine capable of making tobacco products is considered a “manufacturer of tobacco products.” In other words, the person who makes the machine available for consumer use is the person liable for the Federal excise tax on the resulting tobacco products. For example, if a retail store purchased and made the machine available to consumers, the retailer is a manufacturer of tobacco products under the federal law.

At present, North Dakota law does not recognize RYO or cigarette-making machines in the same manner as the Federal government does. This inconsistency has raised compliance challenges at the state level.

PROPOSED CHANGE TO THE LAW

Accordingly, Engrossed Senate Bill 2106 proposes to amend North Dakota law to recognize persons who make RYO machines available for commercial purposes to be manufacturers of tobacco products. Specifically, in **Section 1**, we propose defining a “cigarette-making machine” in accord with the definition of RYO machines at the federal level. We also propose defining a cigarette to include the product of the RYO manufacturing process. This would then make RYO produced cigarettes subject to the tax rate applicable to other cigarettes. In **Section 2**, we propose to require the owner or operator of a RYO machine to have the Federal tobacco product manufacturer permit now required under Federal law unless the machine is used strictly for personal purposes. **Section 3** will require the RYO machine to be registered with the Attorney General. **Section 4** proposes that the RYO manufacturer provide specific information to the state, pay the appropriate taxes on the product sold, comply with the master settlement agreement provisions under N.D.C.C. chapter 51-25, use fire-safe paper to form the cigarettes, and use only federal tax-paid RYO tobacco or tobacco exempt from federal tax under Internal Revenue Service provisions. **Section 5** proposes certain penalties that the Tax Commissioner may impose on RYO manufacturers for failure to comply with these new laws. Finally, **Section 6** of the bill pushes out the effective date of this bill, if enacted, to provide adequate time for notice and public education to take place.

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CONCLUSION

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