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**HB 20-1427**

# FINAL FISCAL NOTE

**Drafting Number:** LLS 20-1329  
**Prime Sponsors:** Rep. Caraveo, McCluskie  
 Sen. Fields; Moreno  
**Date:** September 29, 2020  
**Bill Status:** Signed into Law  
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**Bill Topic:** **CIGARETTE, TOBACCO, AND NICOTINE PRODUCTS TAX**

**Summary of Fiscal Impact:**

- ☒ State Revenue (*conditional*)
- ☒ State Expenditure (*conditional*)
- ☒ State Transfer (*conditional*)
- ☐ TABOR Refund
- ☒ Local Government (*conditional*)
- ☐ Statutory Public Entity

Conditional on voter approval, this bill raises taxes on cigarettes and tobacco products and establishes a new tax on nicotine products. It establishes a minimum price for cigarettes and a minimum tax for moist snuff. Revenue from the taxes is distributed to fund K-12 schools, housing, preschool, health care, tobacco education, and other programs. With voter approval, the bill increases state revenue and expenditures on an ongoing basis.

**Appropriation Summary:** No appropriation is required. See State Appropriations section.

**Fiscal Note Status:** This final fiscal note reflects the enacted bill.

**Table 1**  
**Conditional State Fiscal Impacts Under HB 20-1427**

		FY 2020-21	FY 2021-22
<b>Revenue</b>	General Fund	\$91.6 million	\$185.2 million
	Cash Funds	(\$4.3 million)	(\$8.2 million)
	<b>Total</b>	<b>\$87.4 million</b>	<b>\$177.1 million</b>
<b>Expenditures</b>	General Fund	\$2.2 million	\$4.4 million
	State Education Fund	\$42.4 million	\$118.9 million
	Cash Funds	\$42.7 million	\$53.7 million
	Centrally Appropriated	\$0.01 million	\$0.03 million
	<b>Total</b>	<b>87.4 million</b>	<b>\$177.1 million</b>
	<b>Total FTE</b>	<b>0.4 FTE</b>	<b>1.3 FTE</b>
<b>Transfers</b>	2020 Tax Holding Fund	(\$86.5 million)	(\$175.6 million)
	General Fund	\$1.4 million	\$3.0 million
	Cash Funds	\$85.1 million	\$172.6 million
	<b>Total</b>	<b>\$0</b>	<b>\$0</b>
<b>TABOR Refund</b>		-	-

\*Totals may not sum due to rounding.

**Summary of Legislation**

This bill refers a ballot measure, designated as Proposition EE, to voters at the November 2020 statewide election to increase cigarette and tobacco taxes and create a new tax on nicotine products. Table 2 lists cigarette and tobacco product (excluding modified risk tobacco products) tax rates under current law and the bill, beginning January 1, 2021. Table 3 does the same for nicotine product taxes. The tax rate increases and new taxes are phased in through 2027. Revenue from the new taxes is exempt from TABOR as a voter-approved revenue change.

**Table 2  
Cigarette and Tobacco Product Tax Rate Changes Under HB 20-1427**

	<b>FY 2020-21 to FY 2023-24</b>	<b>FY 2024-25 to FY 2026-27</b>	<b>Beginning FY 2027-28</b>
<b>Cigarettes (per pack)</b>			
Current Law*	\$0.84	\$0.84	\$0.84
Increase from Current Law	\$1.10	\$1.40	\$1.80
<b>New Total Rate Under HB 20-1427</b>	<b>\$1.94</b>	<b>\$2.24</b>	<b>\$2.64</b>
<b>Tobacco Products (% of MLP)</b>			
Current Law*	40%	40%	40%
Increase from Current law	10%	16%	22%
<b>New Total Rate Under HB 20-1427</b>	<b>50%</b>	<b>56%</b>	<b>62%</b>

\* Includes statutory and Constitutional tax rates  
MLP = Manufacturer's list price.  
Excludes modified risk tobacco products.

**Table 3  
Nicotine Product Taxes Under HB 20-1427**

<b>Nicotine Products (% of MLP)</b>	<b>2021</b>	<b>2022</b>	<b>Jan. 2023 - June 2024</b>	<b>July 2024 - June 2027</b>	<b>Beginning July 2027</b>
Current Law	None	None	None	None	None
<b>New Total Tax Rate</b>	<b>30%</b>	<b>35%</b>	<b>50%</b>	<b>56%</b>	<b>62%</b>

MLP = Manufacturer's list price.

**Cigarette tax increase.** The bill increases the cigarette tax by \$0.055 per cigarette or \$1.10 per pack in the first four fiscal years, by \$0.07 per cigarette or \$1.40 per pack in fiscal years five through seven, and by \$0.09 per cigarette or \$1.80 per pack thereafter.

**Tobacco products tax increase.** The bill increases the tobacco products tax by 10 percent of the MLP in the first four fiscal years, by 16 percent of the MLP in fiscal years five through seven, and by 22 percent of the MLP thereafter.

**Nicotine products tax.** The bill establishes a new tax on nicotine products, defined as any ingestible product containing nicotine that is not a cigarette, a tobacco product, or a drug or device authorized for sale by the U.S. Food and Drug Administration. The tax is assessed at a rate of 30 percent of the MLP in 2021, 35 percent in 2022, 50 percent in 2023 and the first half of 2024, 56 percent of the MLP in fiscal years five through seven, and 62 percent thereafter.

**Modified risk tobacco products.** The bill establishes separate tax rates for modified risk tobacco products (MRTP), which must be certified by the U.S. Food and Drug Administration to reduce the risk of tobacco-related disease associated with commercially marketed tobacco products. MRTP are taxed at a lower rate than regular products. Regardless of any future federal certification, vaping products are excluded from MRTP status in Colorado.

**Moist snuff.** The bill establishes a minimum tax for moist snuff. Moist snuff is defined as any finely cut, ground, or powdered tobacco that is not intended to be smoked but does not include any tobacco that is intended to be placed in the nasal cavity. For the first four fiscal years, moist snuff is to be taxed at a minimum rate of \$1.48 per 1.2 ounce can. For fiscal years five through seven, moist snuff is taxed at a minimum rate of \$1.84 per 1.2 ounce can. Thereafter, it is taxed at a minimum rate of \$2.26 per 1.2 ounce can.

**Inventory tax.** The bill requires that importers and distributors remit taxes for products in inventory at the effective date of tax increases after January 1, 2022.

**Vendor fee.** Under current law, tobacco and cigarette distributors who file taxes on time are allowed to retain a portion of the tax due as a vendor allowance to cover the cost of tax collection. The bill reduces this allowance from 3.33 percent to 1.6 percent for tobacco distributors, and 4 percent to 0.4 percent for cigarette distributors. This vendor allowance applies to statutory taxes only. Nicotine distributors are permitted a vendor allowance of 1.1 percent for timely tax remittance.

**Regulation of nicotine product distribution.** The bill directs the Department of Revenue (DOR) to license nicotine tax distributors and to administer similar regulatory requirements as those that exist for tobacco product distributors, including a \$10 annual license fee, quarterly tax filings, late payments, and penalties. A distributor who is willfully noncompliant with the tax regime or who falsifies a tax return is guilty of class 5 felony tax evasion, subject to the tax evasion criminal penalty statute in existing law.

**Sales to Colorado consumers by out-of-state sellers.** The bill requires that out-of-state cigarette wholesalers and tobacco and nicotine product distributors who sell to Colorado consumers remit the appropriate taxes. Correspondingly, Colorado distributors who sell tobacco and nicotine products to out-of-state consumers are allowed a tax credit equal to the amount of tax paid when the products were brought into the state.

**Minimum price for cigarettes.** The bill establishes a minimum price for cigarettes of \$7 per pack and \$70 per carton until July 1, 2024, and \$7.50 per pack and \$75 per carton on and after July 1, 2024.

**Distribution of tax collected.** Via the Old Age Pension Fund and General Fund, the revenue from the new and increased taxes is deposited in the newly created 2020 Tax Holding Fund, and then distributed as follows:

- in FY 2020-21 through FY 2022-23, the bill specifies amounts to be distributed to the Tobacco Tax Cash Fund, Housing Development Grant Fund, Eviction Legal Defense Fund, General Fund, and the newly created Rural Schools Cash Fund, with the remainder deposited in the State Education Fund;
- in subsequent years, the bill specifies amounts to be distributed to the Tobacco Tax Cash Fund, General Fund, newly created Preschool Cash Fund, and the Tobacco Education Programs Fund.

The additional sales tax revenue from the minimum cigarette price is deposited in the Preschool Cash Fund (73 percent) and the General Fund (27 percent).

**Rural schools.** The bills creates the Rural Schools Cash Fund consisting of the following amounts transferred from the 2020 Tax Holding Fund: \$25.0 million in FY 2020-21, \$30.0 million in FY 2021-22, and \$35.0 million in FY 2022-23. The money is distributed by the Colorado Department of Education (CDE) on a per pupil basis to rural school districts and charter schools in those districts. Of the amount in the fund, 55 percent is distributed to large rural schools and 45 percent to the small rural schools. Each district and charter school that receives funds must report to CDE on how the funds are used.

**Preschool funding.** The measure requires that revenue credited to the Preschool Programs Cash Fund be expended to expand and enhance the Colorado Preschool Program or a successor program in order to offer at least 10 hours per week of voluntary preschool, free of tuition, to any child in his or her final year before entry into kindergarten, subject to available funding.

**Tobacco education programs.** The bill broadens the permissible uses of money deposited in the Tobacco Education Programs Fund to allow the fund to be use for education, prevention, and cessation programs related to nicotine products.

**Audit.** The Office of the State Auditor (OSA) is required to conduct an annual financial audit of tax revenue collected and allocated under the bill.

## Background

Colorado assesses an excise tax on each cigarette sold and on the manufacturer's list price (MLP), or invoice price, of non-cigarette tobacco products. Cigarette taxes are assessed when cigarettes are sold by wholesalers. Tobacco product taxes are assessed when the products are manufactured, brought into the state, or shipped to retailers. No tax is currently assessed on nicotine products.

## State Revenue

Contingent upon voter approval, the bill is expected to generate about \$87.4 million in FY 2020-21, and \$177.1 million in FY 2021-22, the first full fiscal year under the measure, with higher amounts in future years as tax rates increase and consumption changes. These estimates are net amounts by which the measure is expected to increase revenue from new taxes and decrease revenue from

existing taxes because of reduced cigarette and tobacco product consumption. For example, in FY 2021-22, the measure increases taxes by \$186.5 million, but reduces existing taxes by \$9.4 million. These estimates include impacts of the minimum price per cigarette as well as the minimum tax for moist snuff. The estimate for FY 2020-21 represents a half-year impact. Increased tax revenue is retained and spent in excess of the state TABOR limit as a voter-approved revenue change. Revenue impact estimates are summarized in Table 4.

**Table 4**  
**Conditional State Revenue Impacts Under HB 20-1427**

	FY 2020-21	FY 2021-22	FY 2022-23
<b>Cigarette Taxes</b>			
Current Statutory Tax (General Fund)	(\$0.7 million)	(\$1.3 million)	(\$1.0 million)
Constitutional Tax (Tobacco Tax Fund)	(\$4.1 million)	(\$7.8 million)	(\$6.9 million)
New Statutory Tax (General Fund)	\$80.2 million	\$160.1 million	\$156.4 million
<b>Total Cigarette Taxes</b>	<b>\$75.5 million</b>	<b>\$151.1 million</b>	<b>\$148.4 million</b>
<b>Tobacco Product Taxes</b>			
Current Statutory Tax (General Fund)	\$0.02 million	\$0.01 million	(\$0.02 million)
Constitutional Tax (Tobacco Tax Fund)	(\$0.2 million)	(\$0.4 million)	(\$0.5 million)
New Statutory Tax (General Fund)	\$5.7 million	\$12.5 million	\$13.0 million
<b>Total Tobacco Product Taxes</b>	<b>\$5.5 million</b>	<b>\$12.1 million</b>	<b>\$12.5 million</b>
<b>Nicotine Product Tax</b>			
New Statutory Tax (General Fund)	<b>\$5.5 million</b>	<b>\$12.4 million</b>	<b>\$16.3 million</b>
<b>State Sales Tax Revenue</b>			
Additional State Sales Tax (General Fund)	<b>\$0.8 million</b>	<b>\$1.5 million</b>	<b>\$1.1 million</b>
<b>Net General Fund Revenue Impact</b>	<b>\$91.6 million</b>	<b>\$185.2 million</b>	<b>\$185.7 million</b>
<b>Tobacco Tax Cash Fund Revenue Impact</b>	<b>(\$4.3 million)</b>	<b>(\$8.2 million)</b>	<b>(\$7.4 million)</b>
<b>Total Net Revenue Impact</b>	<b>\$87.4 million</b>	<b>\$177.1 million</b>	<b>\$178.3 million</b>

*\*Totals may not sum due to rounding.*

**Cigarette and tobacco taxes.** The estimates in Table 3 assume the June 2020 Legislative Council Staff forecast for cigarette and tobacco product statutory and constitutional tax revenue. Based on observed changes in consumption following the enactment of Amendment 35, it is assumed that tax rate increases will decrease cigarette and tobacco product consumption by 0.28 percent for each percentage point by which the after-tax retail price is increased. To the extent that consumption is less than or greater than assumed, the revenue impact of the measure will be correspondingly lower or higher. For the current statutory taxes, the estimates in Table 3 represent the net impact of reduced consumption and the decrease of the current distributor allowance.

**Nicotine product tax.** The estimates in Table 3 are based on 2018 retail sales data for nicotine products. Consumption of nicotine products is expected to grow by between 3 percent and 8 percent annually between 2018 and 2022. Additionally, modifications were made to accommodate online sales, which are believed to be underrepresented in available retail sales data. Demand for nicotine products is assumed to be more sensitive to changes in price than

demand for cigarettes and other tobacco products. It is assumed that the imposition of the new tax will decrease nicotine product consumption by 0.37 percent for each percentage point by which the after-tax retail price is increased.

Data from which to base an estimate of new nicotine tax revenue from the measure are limited. States that have enacted nicotine product taxes report tax revenues that suggest significantly different levels of consumption across states even after adjusting for differences in state populations and economic activity. Data from other states suggest that consumption grew significantly from year to year even after taxes were enacted. However, the market for nicotine and vaping products is expected to continue to evolve in coming years, and the pace of increasing consumption is expected to slow as federal, state, and local regulations on the industry tighten.

**Sales tax revenue.** Sales tax revenue is expected to increase due to the bill's minimum price per pack of cigarettes.

**License fees, fines, and penalties.** License fees will generate \$10 per taxpayer per year to the General Fund; relative to the tax impacts of the bill, fee impacts are assumed to be minimal. This revenue is subject to TABOR. Fines, penalties, and interest will depend on taxpayer compliance and DOR enforcement processes.

**Modified Risk Tobacco Products.** Tax rate increases for MRTP products are lower than for other cigarette, tobacco, and nicotine products under the bill. There is currently only one line of tobacco products designated as MRTP by the U.S. Food and Drug Administration. This fiscal note assumes that MRTP do not constitute a significant market share, and that revenue impacts from the lower taxation of these products will be minimal. Future designations of new MRTP would reduce revenue relative to the estimates in this fiscal note.

**Moist snuff.** The measure includes a minimum tax per 1.2 ounce can of moist snuff. The majority of moist snuff products are priced at a level such this provision will have no impact. For a relatively small share of moist snuff products, the minimum tax rate will increase taxes above the amounts that would have been collected by applying the increased tax rates alone. It is assumed that a maximum of 7 percent of moist snuff product sales will be affected by this provision, resulting in a revenue increase of \$279,000 per year on average during the first seven full fiscal years.

## State Transfers

Conditional on voter approval, the bill requires that the net additional revenue from cigarette, tobacco, and nicotine products tax be transferred to the 2020 Tax Holding Fund, where it is then transferred to the following funds:

- Tobacco Tax Cash Fund;
- General Fund;
- Rural Schools Fund, State Education Fund, Housing Development Grant Fund, and Eviction Legal Defense Fund (FY 2020-21 through FY 2022-23);
- Preschool Programs Cash Fund (beginning in FY 2023-24); and
- Tobacco Education Programs Fund (beginning in FY 2024-25).

Based on the revenue estimates in this fiscal note, transfers from the 2020 Tax Holding Fund will total \$86.5 million in FY 2020-21, \$175.6 million in FY 2021-22, and \$177.2 million in FY 2022-23, with ongoing transfers in future years based on the expected revenue growth.

In addition, sales tax revenue from the minimum cigarette price is transferred to the Preschool Programs Cash Fund. These transfers are estimated to be \$0.6 million in FY 2020-21 and \$1.1 million in FY 2021-22, and declining thereafter to \$0 by 2027-28.

**State Expenditures**

The measure increases state expenditures by \$87.4 million in FY 2020-21 and \$177.1 million in FY 2021-22, as shown in Table 5. This fiscal note assumes that expenditures increase by the same amounts by which the bill increases revenue.

**Table 5**  
**Conditional State Expenditures Under HB20-1427**  
*Millions of Dollars*

<b>Fiscal Year</b>	<b>2020-21</b>	<b>21-22</b>	<b>22-23</b>	<b>23-24</b>	<b>24-25</b>	<b>25-26</b>	<b>26-27</b>	<b>27-28</b>
Preschool Programs Cash Fund	\$0.6	\$1.1	\$0.8	\$164.7	\$188.6	\$187.7	\$186.7	\$230.9
State Education Fund	\$42.4	\$118.9	\$115.6	-	-	-	-	-
Rural Schools Cash Fund	\$25.0	\$30.0	\$35.0	-	-	-	-	-
Tobacco Education Programs Fund	-	-	-	-	\$20.0	\$20.0	\$20.0	\$30.0
Housing Development Grant Fund	\$11.2	\$11.2	\$11.2	-	-	-	-	-
Tobacco Tax Cash Fund	\$5.5	\$11.0	\$11.0	\$11.0	\$11.0	\$11.0	\$11.0	\$11.0
General Fund	\$2.2	\$4.4	\$4.3	\$4.2	\$4.3	\$4.2	\$4.1	\$4.1
Eviction Legal Defense Fund	\$0.5	\$0.5	\$0.5	-	-	-	-	-
<b>Total</b>	<b>\$87.4</b>	<b>\$177.1</b>	<b>\$178.3</b>	<b>\$179.9</b>	<b>\$223.9</b>	<b>\$222.8</b>	<b>\$221.7</b>	<b>\$275.9</b>

**Programmatic expenditures.** Expenditures will be made from cash funds to which moneys are credited.

*Rural schools.* The funding allocated to the Rural Schools Fund will be allocated on a per pupil basis to rural schools and charter schools within those districts. Funds will be distributed on a per pupil basis, with 55 percent distributed to large rural districts and charters, and 45 percent to small rural districts and charters.

*Preschool program.* Revenue in the preschool programs fund must be spent to provide at least 10 hours a week of free preschool to children in the year before they start kindergarten.

*Tobacco education programs.* Revenue credited to the Tobacco Education Programs Fund will be expended for tobacco and nicotine education, prevention, and cessation grants and for grant making administration. When tobacco education programs funding is made available beginning in FY 2024-25, the Colorado Department of Public Health and Environment (CDPHE) may require additional staff to administer grants. Expenditures for staff salaries and attendant operating, capital, and travel costs will be paid from the amounts transferred to the cash fund.

*Tobacco Tax Cash Fund.* Revenue transferred to the Tobacco Tax Cash Fund is distributed to programs administered in the Colorado Department of Health Care Policy and Financing and CDPHE, including Medicaid, Child Health Plan Plus (CHP+), immunization programs, primary care programs, cancer and chronic disease detection and treatment programs, tobacco education programs, and various other healthcare programs. Specific transfers to individual programs have not been estimated at this time.

*State Education Fund.* Any remaining revenue in the first three fiscal years will be deposited in the State Education Fund. It can be spent for the state share of total program funding, or for other programs related to education, as determined by the General Assembly.

*Affordable Housing and Eviction Assistance.* Revenue credited to the Housing Development Grant Fund, administered by the Department of Local Affairs, will be expended to improve, preserve, or expand the supply of affordable housing in Colorado. At least \$5 million of the funds must be used for affordable housing in rural areas. Revenue credited to the Eviction Legal Defense Fund, administered by the Judicial Department, will be expended to provide legal services to indigent parties facing eviction.

**Administrative expenses.** Expenditures in the DOR for tax administration are estimated at \$286,000 and 0.4 FTE in FY 2020-21 and \$71,000 and 1.0 FTE in FY 2021-22. Start-up costs include computer programming and testing, while ongoing costs include staff in the department's Taxpayer Services Division, reporting, and legal services. Beginning in FY 2021-22, the Office of the State Auditor will require an estimated \$25,000 and 0.3 FTE to conduct an annual financial audit of tax revenue collected and expended as a result of the measure.

**Election expenditure impact—existing appropriations.** This bill includes a referred measure that will appear before voters at the November 2020 general election. While no additional appropriation is required in this bill, certain election costs are incurred by the state when ballot measures are referred to voters, including reimbursements to counties from the Department of State Cash Fund in the Secretary of State's Office and newspaper publication of text and titles and inclusion in the statewide ballot information booklet, paid from the Ballot Analysis Revolving Fund in the Legislative Department.

## **Local Government**

Of the revenue designated for the General Fund, excluding additional sales tax revenue, 27 percent is distributed to local governments. This amount is expected to be \$1.1 million in the first full year of the measure. Of the money deposited in the Tobacco Tax Cash Fund, a portion is distributed to local governments. Additional revenue to the fund will result in higher distributions to local governments.



## Effective Date

This bill was signed into law by the Governor on July 8, 2020. If approved by voters at the November 2020 general election, the new tax and tax increases in the bill take effect upon proclamation of the Governor, or January 1, 2021, whichever is later.

## State Appropriations

No appropriation is required. If Proposition EE is approved by voters, appropriations will be addressed through the annual budget process

## State and Local Government Contacts

Education  
Human Services  
Public Health and Environment  
Counties

Health Care Policy and Financing  
Law  
Revenue  
Municipalities