

Proposition EE: Taxes on Nicotine Products

1 **Proposition EE, if approved, would:**

- 2 • increase taxes on cigarettes and tobacco products;
- 3 • create a new tax on nicotine products, including vaping products; and
- 4 • distribute the new revenue to expanded preschool programs, as well as to
- 5 K-12 education, rural schools, affordable housing, eviction assistance,
- 6 tobacco education, and health care.

7 **What Your Vote Means**

YES

A “yes” vote increases taxes on cigarettes and other tobacco products, and creates a new tax on nicotine products, including vaping products. The new tax revenue will be spent on education, housing, tobacco prevention, health care, and preschool.

NO

A “no” vote means taxes on cigarettes and other tobacco products will stay the same, and there will be no new taxes on nicotine or vaping products.

1 **Summary and Analysis for Proposition EE**

2 **Why is Proposition EE on the ballot?**

3 Earlier this year, the state legislature passed a law to raise taxes on cigarettes and
 4 tobacco products, create a state tax on nicotine products, and modify the regulation
 5 of these products. The new law takes effect only if Proposition EE is approved by
 6 voters, as all tax increases require voter approval under the Colorado Constitution.
 7 This analysis discusses the changes that will occur if Proposition EE passes.

8 **How are cigarettes, other tobacco products, and nicotine products currently**
 9 **taxed?**

10 Cigarettes are currently taxed at 4.2¢ per cigarette, which is 84¢ per pack of
 11 20 cigarettes. Tobacco products include chewing tobacco, cigars, and snuff and are
 12 currently taxed at 40 percent of the manufacturer’s list price, which is the price at
 13 which a manufacturer sells the product to a distributor. Nicotine products, which
 14 include vaping products, are not currently subject to any existing cigarette or tobacco
 15 tax. All three products are currently subject to the state sales tax.

16 Cigarette and tobacco taxes are required to be paid by the distributor that first
 17 receives products in the state, which may include local manufacturers. The business
 18 pays taxes to the state, but may keep a portion of the tax as compensation for work
 19 associated with filing taxes.

20 **Current revenue distributions.** Current cigarette and tobacco tax revenue is
 21 distributed to a variety of health care, tobacco education, and disease prevention
 22 programs, as well as for general state programs and services.

23 **How does Proposition EE change taxes on those products?**

24 Proposition EE raises taxes on cigarettes and tobacco products, and establishes a
 25 new tax on nicotine products. The new taxes increase incrementally until they are
 26 fully phased in by 2027. Table 1 lists the current tax rates and the new rates under
 27 the measure. The new revenue is exempt from constitutional spending limits.

28 **Table 1**
 29 **Changes to Cigarette, Tobacco, and Nicotine Products Taxes**

Product	Current Tax Rates	New Rates Under Proposition EE*							Tax Rate Increase 2021 to 2027
		2021	2022	2023	2024	2025	2026	2027	
Cigarettes <i>Tax per pack</i>	\$0.84	\$1.94	\$1.94	\$1.94	\$2.24	\$2.24	\$2.24	\$2.64	\$1.80
Tobacco Product <i>Percent of price**</i>	40%	50%	50%	50%	56%	56%	56%	62%	22%
Nicotine Products <i>Percent of price**</i>	None	30%	35%	50%	56%	56%	56%	62%	62%

30 * Rate increases begin January 1, except in 2024 and 2027, when rate increases begin July 1.
 31 ** Manufacturer’s list price.

1 If approved, the measure also:

- 2 • sets new tax rates for modified risk tobacco products, which are federally
3 designated as having lower health risks compared to existing commercial
4 products. Currently, there is only one type of tobacco product that has received
5 this designation for sale nationwide. This product would be taxed at 35 percent of
6 the manufacturer's list price, while a regular tobacco product would be taxed at
7 50 percent in 2021;
- 8 • establishes a minimum tax for moist snuff products at \$1.48 per 1.2 ounce
9 container, increasing to \$2.26 by 2027-28. Moist snuff is a type of cut,
10 smokeless tobacco that can be loose or pouched and is intended to be placed in
11 the mouth rather than sniffed;
- 12 • sets the minimum after-tax price of cigarettes for consumers at \$7.00 per pack
13 beginning in January 2021, and \$7.50 per pack beginning in July 2024;
- 14 • makes online sales from out of state retailers to Colorado consumers subject to
15 the new taxes; and
- 16 • reduces the portion of the taxes that distributors may keep as compensation for
17 the work associated with filing taxes from 4.0 percent to 0.4 percent for cigarette
18 distributors, from 3.33 percent to 1.6 percent for tobacco distributors, and sets
19 this rate at 1.1 percent for nicotine distributors.

20 **Are vaping products taxed under Proposition EE?**

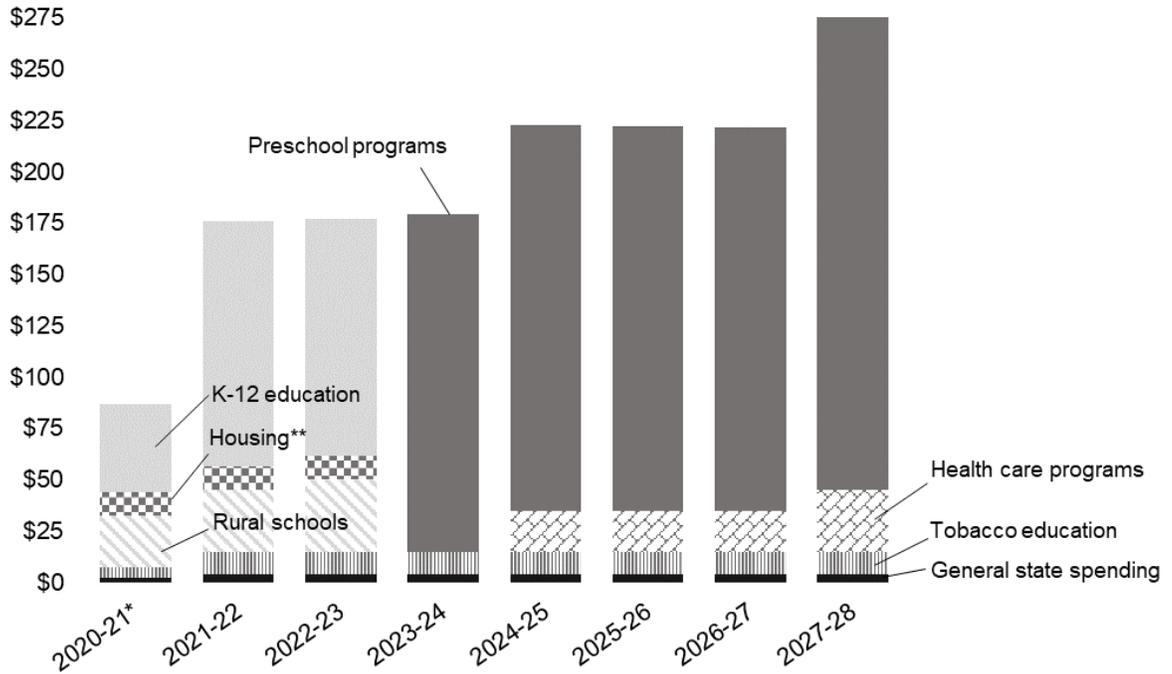
21 Yes, vaping products that contain liquid nicotine are subject to the nicotine tax
22 established by Proposition EE. Vaping products and devices that do not contain
23 nicotine are not subject to the tax. Vaping products are not eligible for the lower tax
24 rates for modified risk tobacco products, even if they are approved for this
25 designation by the federal government.

26 **How will the new tax revenue be spent?**

27 Proposition EE is expected to generate up to \$175.6 million in cigarette, tobacco,
28 and nicotine tax revenue in budget year 2021-22, the first full year the measure will
29 be in effect, and up to \$275.9 million beginning in budget year 2027-28 when the
30 new tax rates are fully phased in. Figure 1 shows the programs that will receive
31 funding as the new tax rates are phased in through budget year 2027-28. Programs
32 funded in budget year 2027-28 will continue to receive funding in future years.

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Figure 1
Distributions of New Tax Revenue
Millions of dollars, by budget year



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* Half-year impact.
** Includes housing development and eviction legal assistance.

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As shown in the above figure, the measure will provide funding for the following programs:

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- **Preschool programs.** Proposition EE provides funding for expanded preschool, including at least ten hours per week of free preschool for every child in their final year before kindergarten. A portion of the additional sales tax revenue from the minimum cigarette price is also used for this purpose.
- **Rural schools.** Of the money allocated for rural schools in the first three years, 55 percent goes to rural school districts with between 1,000 and 6,500 students, and 45 percent goes to rural school districts with fewer than 1,000 students. The funding is allocated on a per-student basis.
- **K-12 education.** In addition to the funding for rural schools, any revenue not allocated to other programs will be available for K-12 education funding for the first three years. Specific uses may include school finance funding to school districts statewide, including charter schools, as well as other education programs.
- **Housing development.** In the first three years, funding will be allocated as grants or loans to buy, renovate, and construct houses, or provide rental assistance, in an effort to increase the supply of affordable housing. Of the amount allocated for this purpose, \$5.0 million must be used in rural areas.
- **Eviction legal assistance.** Funding for this purpose is allocated in the first three years and will be awarded to organizations that provide legal assistance to low-income clients at risk of eviction.

- 1 • **Health care programs.** Funding allocated for health care programs will be used
2 for Medicaid, primary care, tobacco use prevention, children’s health and a
3 variety of other health care programs that currently receive cigarette and tobacco
4 tax revenue.
- 5 • **General state spending.** Of the amount allocated for this purpose, 27 percent
6 must be distributed to local governments, and the remainder used for general
7 state spending, which may include education, transportation, and health care,
8 and will be determined by the state legislature. A portion of the additional sales
9 tax revenue from the minimum cigarette price is also used for general state
10 spending.
- 11 • **Tobacco education programs.** Money allocated for this purpose is used for
12 grants for community-based and statewide programs to reduce tobacco use by
13 youth, encourage cessation, and reduce exposure to secondhand smoke.

14 **How would preschool availability and funding change?**

15 Currently, the Colorado Preschool Program funds 29,360 half-day preschool slots for
16 three- and four-year-old children who are from low-income families, in need of
17 language development, or who meet certain criteria indicating they may be in danger
18 of falling behind in school. About 9,000 low-income students also have access to
19 preschool through federal Head Start programs. The measure requires that the new
20 funding be used to offer at least 10 hours per week of free preschool to every child in
21 their final year before kindergarten. This is expected to begin in the 2023-24 school
22 year. Any remaining revenue must be used to expand preschool opportunities for
23 low-income families and children at risk of not being ready for kindergarten.

For information on those issue committees that support or oppose the measures on the ballot at the November 3, 2020, election, go to the Colorado Secretary of State’s elections center web site hyperlink for ballot and initiative information:

<http://www.sos.state.co.us/pubs/elections/Initiatives/InitiativesHome.html>

24 **Arguments For Proposition EE**

- 25 1) Colorado has one of the highest rates of youth vaping in the country, while also
26 having one of the lowest tax rates on cigarettes and tobacco products, and no tax
27 on vaping products. Cigarettes, tobacco, and nicotine products are addictive and
28 have negative health impacts, which can include cancer as well as heart and
29 lung disease. Tax increases usually result in higher prices, which deter smoking
30 and tobacco use, especially among youth and young adults. Higher taxes on
31 cigarettes, tobacco products, and vaping products could decrease consumption
32 while funding health care, and tobacco cessation, education, and prevention
33 programs.
- 34 2) Proposition EE provides needed funding for education. The impacts of the
35 COVID-19 pandemic on the state budget have resulted in a 10 percent decrease
36 in the state share of public school funding for the 2020-21 school year. Additional
37 federal funding has helped lessen the impact of this state budget cut in 2020;
38 however, it is not likely to be available next year and further cuts are expected.
39 The measure provides vital funding for schools as the economy recovers, and

1 additional assistance for small rural districts that are disproportionately impacted
2 by state funding cuts.

3 3) Providing access to free preschool gives all children the same foundation before
4 entering kindergarten. Currently, half of Colorado three- and-four-year-olds do
5 not attend any type of preschool. High quality preschool is shown to improve
6 educational, economic, and health outcomes throughout a child's life, including
7 higher wages, higher graduation rates, and fewer criminal convictions. Access to
8 preschool also supports working parents by giving them the option to enroll their
9 children in up to ten hours per week at no cost.

10 **Arguments Against Proposition EE**

11 1) Increasing taxes on cigarette, tobacco, and nicotine products imposes a financial
12 burden on people who choose to consume them, particularly low-income users.
13 Because these products are addictive, users may continue to purchase them
14 even after a tax increase. In addition, vaping products are used by many as a
15 way to quit using traditional cigarettes. Youth vaping should be addressed
16 through enforcement of existing age restrictions and additional education and
17 prevention, not through raising taxes on a product that some use as a cessation
18 device.

19 2) Raising taxes and establishing a minimum purchase price hurts business
20 owners. This is particularly true for businesses that sell low-cost products, or that
21 are in areas of the state where local governments have already imposed
22 cigarette, tobacco, and nicotine taxes. Businesses selling these products may
23 see a decline in sales, which can be particularly harmful for small, local
24 businesses at a time when many are already struggling. Private businesses and
25 market competition are best suited to determine the prices at which products are
26 bought and sold.

27 3) The state should not be dependent on tax revenue from a specific, addictive
28 product to fund schools, preschool, and other state services. Once Proposition
29 EE is fully phased in, revenue from this tax is likely to decline over time as the
30 increased price results in fewer products being purchased. At the same time,
31 preschool funding needs are likely to grow. A tax intended to decrease
32 consumption is not a funding source on which the state should rely.

33 **Estimate of Fiscal Impact for Proposition EE**

34 **State revenue.** Proposition EE will increase state revenue from cigarette, tobacco
35 product, and nicotine product taxes by \$87 million in state budget year 2020-21 and
36 \$176 million in state budget year 2021-22, the first full year under the measure. The
37 amount of new revenue will increase as the measure is phased in, with \$276 million
38 expected to be generated in state budget year 2027-28.

In addition, the measure will also increase state revenue from sales taxes by \$0.8 million in state budget year 2020-21 and by \$1.5 million in state budget year 2021-22, the first full year under the measure. The amount of additional sales tax revenue will decline as the measure is phased in, with no new sales tax revenue expected in state budget year 2027-28.

State spending. Proposition EE will increase state spending by \$87 million in state budget year 2020-21 and by \$177 million in state budget year 2021-22. As the measure is phased in, state spending will increase, with \$276 million expected to be spent in state budget year 2027-28. Spending includes the amounts shown in Figure 1 for education, housing, preschool, tobacco and nicotine education and cessation programs and other programs, as well as costs for administrative and auditing purposes.

Taxpayer impacts. Proposition EE is expected to increase taxes paid by an average of \$38 per Colorado adult in state budget year 2021-22, and \$53 per Colorado adult in budget year 2027-28; however, the direct tax impact applies only to people who consume cigarette, tobacco products, and/or nicotine products. If the percentage of adult smokers remains constant at 14.5 percent, the measure is expected to increase the taxes paid by cigarette smokers by an average of \$222 in state budget year 2021-22 and by \$291 in state budget year 2027-28.

State Spending and Tax Increases

Article X, Section 20, of the Colorado Constitution requires that the following fiscal information be provided when a tax increase question is on the ballot:

- Estimates or actual amounts of state fiscal year (FY) spending for the current year and each of the past four years with the overall percentage and dollar change; and
- For the first full fiscal year of the proposed tax increase, estimates of the maximum dollar amount of the tax increase and of state fiscal year spending without the increase.

“Fiscal year spending” is a legal term in the Colorado Constitution. It equals the amount of revenue subject to the constitutional spending limit that the state or a district is permitted to keep and either spend or save for a single year. Table 2 shows state fiscal year spending for the current year and each of the past four years.

**Table 2
State Fiscal Year Spending**

	Actual FY 2016-17	Actual FY 2017-18	Actual FY 2018-19	Actual FY 2019-20	Estimated FY 2020-21
Fiscal Year Spending	\$12.89 billion	\$13.70 billion	\$14.36 billion	\$14.87 billion	\$12.70 billion
Four-Year Dollar Change in State Fiscal Year Spending: -\$0.19 billion					
Four-Year Percent Change in State Fiscal Year Spending: -1.5 percent					

Table 3 shows the revenue expected from the cigarette, tobacco product, and nicotine product tax increase for FY 2021-22, the first full fiscal year for which the tax increase would be in place, and an estimate of state fiscal year spending without the tax increase. The estimate in Table 3 differs from the amount in the ballot question for Proposition EE because it reflects a different fiscal year, FY 2021-22 rather than FY 2027-28.

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Table 3
Estimated State Fiscal Year Spending
and the Proposed Cigarette, Tobacco Product, and Nicotine Product Tax Increase

	FY 2021-22 Estimate
Fiscal Year Spending Without the Tax Increase	\$16.46 billion
Revenue from the Tax Increase	\$186.5 million