

Tobacco, Alcohol, and Gambling Taxes

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In times of tight revenue, certain products or activities may be more acceptable to target for taxation than others. Consumption of tobacco or alcohol or partaking in gambling activities are targeted for taxation as they are specific behaviors of choice that not everyone partakes in and therefore may receive less outcry. These activities are restricted to adults, and prevention efforts are undertaken by many state and local agencies and organizations. The tax is only on those who consume the products or participate in the activity. In the past, these type of consumption taxes have been labeled "sin taxes" and can also be considered as sumptuary to the extent that they are intended to restrain or limit the expenditures of citizens on items such as tobacco.

Some of the revenue from these taxes is dedicated to the Department of Public Health and Human Services (DPHHS) for state programs that target prevention and treatment programs related directly to the use or abuse of these products. The table that follows provides a snapshot of these taxes. More information on the current rates, revenue collection and allocation, and a history of each tax follows the table.

Selected Consumption Taxes, Rates, Last Legislative Change

Product/Activity	Tax Rate	Enacted	Last Change	MCA Section
Cigarette: pack of 20	\$0.70	1947	2003	16-11-111
Tobacco products: wholesale price	25%	1969	2003	16-11-202
Moist snuff: ounce	\$0.35	2003	2003	16-11-202
Liquor excise: retail selling price more than 200,000 proof gallons 200,000 proof gallons or less	16% 13.8%	1937	1957 1985	16-1-401
Liquor license: retail selling price more than 200,000 proof gallons 200,000 proof gallons or less	10% 8.6%	1957	1977 1985	16-1-404
Beer: barrel of 31 gallons over 20,000/year 10,001 to 20,000/year 5,001 to 10,000/year up to 5,000/year	\$4.30 \$3.30 \$2.30 \$1.30	1933	1997 2000 2000 2000	16-1-406
Wine and hard cider: liter table wine hard cider table wine sold to agency liquor store	\$0.27 \$0.037 \$0.01	1978	1985 1997 1987	16-1-411 16-2-301

Product/Activity	Tax Rate	Enacted	Last Change	MCA Section
Video gambling machine: gross income	15% minus tax credit	1987	1987	23-5-610

The following is a list of the consumption taxes on tobacco, alcohol, and gambling and includes the current rate, revenue, allocation, and a history of the tax. The amounts include taxes only and do not include application processing or license fees, unless specified.

Tobacco

Since the awareness of the effects of tobacco on society raised by the Tobacco Settlement and its resulting coveted revenue stream, tobacco has been a target for increased taxation.

Cigarette¹

Tax: 70 cents a pack of 20 (2003 increase of the tax from 18 cents)

Insignia discount: 1.66% on first 2,580 cartons (reduced from 6%, 2003)
1.11% on next 2,580 cartons (reduced from 4%, 2003)
0.83% in excess of 5,160 cartons

Allocation: Revenue from taxes on cigarettes is distributed to operate and maintain the state veterans' nursing homes, to the long-range building program, and to the general fund after deductions for tribal refunds. In 2003, distribution was changed to guaranteeing 8.3% or \$2 million for the veterans' homes, 4.3% to long-range building, and the remainder to the general fund.

General Fund

Revenue:² FY 2003 actual: \$12.58 million FY 2004 forecast: \$34.9 million
Total Revenue: FY 2003 actual: \$16.09 million FY 2004 forecast: \$40.29 million

Wholesale tobacco products (except for moist snuff):

Tax: 25% of the wholesale price (2003 increase from 12.5%)

Moist snuff:

Tax: 35 cents an ounce on moist snuff (taxed separately and new rate in 2003)

Allocation: General Fund

General Fund

Revenue: FY 2003 actual: \$2.36 million FY 2004 forecast: \$3.22 million

- ◆ The cigarette tax began at 2 cents for a pack of 20 in 1947. Initiative No. 54 in 1951 added 2 cents a pack to fund an honorarium for World War II veterans (total 4 cents). This is when the veterans and the cigarette tax connection began. In 1957, the original tax was raised 3 cents and 1 cent was added to fund bonds for an honorarium for Korean War veterans (total 8 cents) and the insignia tax discount of 8% was added. In 1963, World War I veterans were offered the honorarium. In 1971, the original tax was increased to 9 cents a pack (total 12 cents) and the revenue was deposited 50% into the

general fund and the remainder to two funds in the long-range building program that continued to pay the bonds on any remaining veterans' honoraria. In 1981, the insignia discount was lowered to 3% and all of the proceeds of the cigarette tax went to the long-range building sinking fund and the bond proceeds and insurance clearance funds. In 1983, the tax rose to 16 cents. The 18-cent-a-pack tax was implemented in 1989, with the additional 2 cents dedicated to help fund the veterans' home. The tax experienced a brief increase to 19.26 cents a pack in 1992 for 1 year only (7% surtax), but returned to 18 cents a pack until 2003 when the tax was raised to 70 cents.

- ◆ Tobacco products have been taxed since 1969 beginning at 12.5% of the wholesale selling price. The tax was raised briefly in 1992 to 13.38% for 1 year. In 2003, the tax was doubled to 25% of the retail selling price and a separate tax was created on moist snuff of 35 cents an ounce.
- ◆ After the 2003 change, Montana's cigarette tax rate ranks 23rd in the country, the overall average state cigarette tax per pack is 73.5 cents, but looking at the statistics a little deeper reveals that the six major tobacco states average a much lower tax of 12.4 cents, bringing the other average for the other states to 81.7 cents. The federal cigarette tax is 39 cents a pack. The lowest rate in the country is 3 cents a pack in Kentucky and the highest is \$2.05 a pack in New Jersey. In other states, localities are allowed to impose an additional tax. New York City imposes a tax of \$1.50 a pack on top of the New York State tax of \$1.50.
- ◆ The U.S. Center for Disease Control and Prevention estimates that smoking-caused health costs nationwide total \$7.18 for each pack sold in the U.S.

Alcohol

Liquor excise

Tax: 16% of retail selling price if more than 200,000 proof gallons
 13.8% if 200,000 proof gallons or less

Allocation: General Fund (less a small distribution to Indian tribes)

Total Revenue: FY 2003 actual: \$8.4 million

- ◆ Taxes on alcohol began in 1937 at 50 cents a gallon. In 1939, the tax was amended to 8% of the retail selling price. The tax was increased to 16% in 1957 and approved by a referendum in 1958. The differentiation of tax rate based on amount sold was placed in law in 1985 to foster small business growth and development and lowered the amount for 200,000 proof gallons or less to 13.8% of the retail selling price.

Liquor license

Tax: 10% of retail selling price if more than 200,000 proof gallons
 8.6% if 200,000 proof gallons or less

Allocation: 34 1/2% to General Fund, 65 1/2% to DPHHS for treatment, rehabilitation and prevention of alcoholism and chemical dependency

Total Revenue (excise and license):
 FY 2004 forecast: \$13.879 million

General Fund Revenue (excise and license):

FY 2003 actual: \$10,042,488

DPHHS (state special revenue - license only):

FY 2003 actual: \$5.2 million

- ◆ In 1957, the tax began at 4% of the retail selling price. It was changed in 1974 to 5% (with 4/5 of the tax going to counties). In 1977, it was raised to 10% and the new 5% was the beginning of the alcohol tax earmarked for treatment, prevention, and rehabilitation of alcoholics with a portion of the money going to the Department of Institutions and a portion to counties. The differentiation in tax based on amount sold was placed in law in 1985 for small business development.

Beer

Tax: Over 20,000 barrels a year: \$4.30 on each barrel of 31 gallons
10,001 and 20,000 barrels of beer, \$3.30
5,001 to 10,000, \$2.30
Up to 5,000 barrels, \$1.30 a barrel

Allocation: 23.26% to DPHHS and remainder to General Fund (minus a small portion returned to Indian tribes)

Total Revenue: FY 2003 actual: \$3.6 million

- ◆ In 2001, the changes to the schedule for 20,000 barrels or less was implemented. In 1997, the tax rate was raised to the current \$4.30 a barrel from \$3.00. The tax began in 1933 at 50 cents a barrel, but shortly thereafter was raised to \$1.00 a barrel in an Extraordinary Legislative Session in the same year. In 1959, it was raised to \$1.50 a barrel, and the 1969 Legislature temporarily raised it to \$3.00 barrel, which was made permanent in 1971.
- ◆ The beginning of the alcohol-earmark tax was in 1977 when an additional \$1.00 a barrel tax was placed on beer and earmarked for the Department of Institutions for the treatment, prevention, and rehabilitation of alcoholics. That additional amount was raised to \$1.30 in 1987. The allocation is now 23.26% to DPHHS for use for treatment, rehabilitation, and prevention of alcoholism and chemical dependency.

Wine and hard cider

Tax: 27 cents a liter of table wine
3.7 cents a liter of hard cider
Additional 1 cent a liter on table wine sold by a table wine distributor to an agent (1987) - allocated to General Fund

Allocation: 2001 increased general fund allocation by 10% (from the repeal of cities and counties allocation reimbursed by the county entitlement share) to 69% and 31% to DPHHS

Total Revenue: FY 2003 actual: \$1.98 million

- ◆ The wine tax was first imposed in 1978 when the people of Montana approved selling table wine in stores. The tax began at 75 cents a gallon. In 1979, it was changed to 20

cents a liter, 16 cents of which went to the general fund and the remainder of which went to the Department of Institutions, counties, and cities for the treatment, prevention, and rehabilitation of alcoholics. In 1985, it was raised to 27 cents a liter with the additional 7 cents allocated to the Department of Institutions. In 1992, there was a 1-year surtax of 7% of the tax liability. In 1997, the sale of hard cider was authorized and a separate tax of 3.7 cents a liter was imposed. It was in that year that the allocation was changed to percentages.

General information

- ◆ After adjusting for inflation, the nationwide average state beer tax in 2000 was only around one-third as much as the beer tax in 1968, with Montana reporting approximately 25% to 49% erosion. The Montana state beer tax averages 1.3 cents per drink below the national average of 2.51 cents per drink versus the wine tax, which averages 3.99 cents per drink compared to 2.82 cents per drink nationally. (Hard liquor tax is not reported by average per drink.)³ Various alcoholic beverage taxes have been modified to accommodate small businesses, such as the liquor license tax and the beer tax, and the averages do not apply to the lower volume, lower taxed beverages.
- ◆ In 1979, the state began approval of treatment programs and the beer and liquor license taxes were distributed to both the state and counties to fund treatment, prevention, and rehabilitation for alcoholics.
- ◆ The 1999 state alcoholic beverages tax collections in Montana were \$18.26 per capita, 13th in the nation, compared to \$14.33 for the United States. Montana collects 8 cents per \$100 income, 12th in the nation, compared to 5 cents for the United States average.⁴
- ◆ In a 2001 study by the National Center on Addiction and Substance Abuse, it was estimated that 14.9% of spending in Montana on state programs was related to (legal and illegal) substance abuse (including justice, education, health, child/family assistance, mental health, developmental disability, public safety, and state workforce). In fiscal year 2002, 92 % of people admitted to state-approved treatment facilities identified one of three substances as their primary substance of abuse: alcohol, marijuana, and methamphetamine. Alcohol consumption among adults is legal, but 62 % of clients abuse two or more substances. For youth who are 12 to 17 years of age, alcohol is the most frequently used (hovering around or above 40%), cigarettes are second (20%), and marijuana is third (20%) (2002 Prevention Needs Assessment).
- ◆ A 2003 change in the allocation of revenue received from the taxation of alcoholic beverages resulted in more money for co-occurring mental illness and chemical dependency and discretionary money for counties (Ch. 140, L. 2003).

Gambling

Video gambling machine

Gross income tax: 15% of the gross income (minus any tax credit for connection to automated reporting system)

Allocation: General Fund

Total Revenue: FY 2003 actual: \$45.85 million

State Lottery

Tax: Net revenue of the state lottery constitutes the enterprise fund. Net revenue is gross revenue minus a minimum of 45% of the money paid for tickets that must be paid out as prize money and minus commissions and operating expenses.

Allocation: General Fund

Total Revenue: FY 2003 actual: \$7.45 million

- ◆ The gross income tax on video gambling machines was implemented in 1987 at 15%. At the same time, there was a reduction in the video draw poker machine license fee from \$1,500 to \$100 and the tax applied to keno machines as well. A local license and fee was repealed in 1989. State license fees are currently at \$220 for each video gambling machine, which goes into a state special revenue fund for administering the law and to local governments. In addition, there is an annual permit surcharge fee of \$10 for each machine for less than 20 machines and \$20 for each machine if over 20 machines, and the proceeds go to the general fund.
- ◆ Taxes and permit and license fees for other forms of gambling (bingo, keno, sports games and tabs, casino nights) are not reported here as the revenue is not reported separately. Bingo and keno taxes are statutorily appropriated to the municipality or county where the games are located. Sport tabs collections are retained by the Department of Justice for administration.
- ◆ The 1998 Montana Gambling Study reported that 78% of Montanans gambled in some form and 3.6% of all Montanans are probable problem or pathological gamblers, up from 2.2% reported in a 1992 study. An estimated 3% to 6% of problem and pathological gamblers will eventually seek treatment. Ninety-three percent of gambling establishments hold alcohol licenses (only state residents may obtain a license to sell alcoholic beverages, and the remainder are owned completely or partially by nonresidents). (1998 Montana Gambling Study, Legislative Services Division, November 1998)

Summary

It is clear that through time, these taxes have been incrementally increased and it is not uncommon for them to be partially dedicated or earmarked for a specific activity. The cigarette tax was first dedicated to World War II veterans honoraria -- no necessary connection other than the near-universal distribution of tobacco by the military for those serving in war-time situations. In later years, the revenue assisted in the support of a state long-term care facility for veterans. In 1977, the earmarking of alcohol taxes for use by county and state programs for the prevention, treatment, and rehabilitation of alcoholism provided a direct link between the product taxed and the use of the revenue. There also have been proposals in the past to use gambling revenue for treatment of problem and pathological gamblers, which would be a direct link.

Dedicating or "earmarking" revenue for certain programs has been discouraged in the recent past. In 1993, the Legislature passed legislation requiring review of dedicated revenue, and in

1995, it promulgated the principles of revenue dedication. Some of the related principles include whether the person paying the tax is a direct beneficiary of the specific activity, whether the entire cost is paid by the beneficiary, whether the cost is commensurate with the cost of the activity, and whether there is a legal basis to designate funds for a specific purpose. On their face, these consumption taxes appear to qualify for dedication to substance use prevention and treatment.

Is the revenue accrued from the taxation of these products and activities commensurate with the costs to society involved in prevention and treatment, criminal justice, child abuse and neglect, and health care, and other costs correlated with the use or abuse of these legal products or services? Many costs to society are the result of illegal activity; however, the cost information does not separate out the differences for costs of substance use, abuse, or addiction for legal or illegal substances, at least a portion of the costs are for legal use of legal substances.

The National Center on Addiction and Substance Abuse at Columbia University surveyed state budgets for 1998 to determine the impact of substance abuse and addiction in 16 budget categories. They estimated that Montana spent 14.9% of the 1998 state budget on spending related to substance abuse, including health, social services, criminal justice, education, mental health, developmental disability, public safety, and public workforce.

Some of the tax rates have been increased more recently than others, most notably the tax hike on cigarettes and other tobacco products in 2003. Others have not been increased for a long period of time--most notably the liquor excise tax since 1957 and the liquor license tax since 1977. The beer tax top rate was raised in 1997, but a sliding tax was implemented that actually decreased some taxes. The wine tax was last changed in 1985. The questions arise of whether tax rates are keeping pace with inflation, and what level of tax rate is appropriate and commensurate with social costs.

There is also the conundrum of using taxation as a prevention tool -- the higher the rate of tax, the more it discourages the purchase of that product, especially by young people, and the decreased demand for a product will then reduce the revenue. The fiscal note for legislation increasing the cigarette tax in 2003 (SB 407) assumed that each penny increase in tax is translated directly to a penny increase in the price of a pack of cigarettes, which would result in a decrease in demand of 0.14%.

As state budgets become tighter and the needs in the area of alcohol, tobacco, and other drug prevention, treatment, and justice issues increase, these areas may provide sources of revenue.

ENDNOTES

1. Montana law provides an exception to tobacco taxes in the form of refunds, credits, or a quota for tax-free distribution for sale to members of federally recognized tribes of a specific reservation and for revenue sharing.

2. All revenue figures were obtained through the Legislative Fiscal Division sources.
3. Alcohol Policies in the United States, Highlights From the 50 States, University of Minnesota. November 2000.
4. NCSL website. Taxes: 1999 State Taxes, posted April 25, 2002, National Conference of State Legislatures Fiscal Affairs Program.

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