



Agenda Item - 10.C.

Agenda MemorandumCity Council Meeting
October 26, 2020*Financially Sustainable Government Providing Excellence in City Services*

Subject: Councillor's Bill No 32 Re: Proposed Amendment to Title IV of the Westminster Municipal Code Eliminating the Sales and Use Tax Exemption for Cigarettes

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Recommended City Council Action:

Pass Councillor's Bill No. 32 on first reading, amending Title IV of the Westminster Municipal Code, eliminating the Sales and Use Tax exemption for cigarettes.

Summary Statement:

Sales and use tax is a critical source of revenue for Westminster, generating over \$100 million to provide essential services to the public, and accounts for over two-thirds of all General Fund revenues.

As a home rule city, Westminster is authorized, by State Constitution, to administer and collect its own sales and use taxes. Such local control over sales and use tax administration is crucial to home rule municipalities, including Westminster.

Staff is regularly looking at ways to simplify the tax code and maintain an ordinance that is relevant and harmonious with with meeting the needs of the businesses. Exemptions often create an added layer of complexity for taxpayers as taxation is the general rule and exemption the rare exception.

Repealing the exemption related to cigarettes will harmonize the taxability of all nicotine and tobacco products in the City. Similar products that are not currently exempt include vaping oils and devices, cigars, and smokeless tobacco items.

Fiscal Impact:

Estimated Increase in Sales Tax Revenue \$600,000 (Revenues net of state share back, should the City be required to forfeit these funds, would be \$400,000)

Source of Funds:

Sales and use tax on cigarettes

Policy Issue(s):

Should the City amend Title IV of the Westminster Municipal Code (the "Code") to repeal the exemption of cigarettes from sales and use tax?

Alternative(s):

City Council could direct Staff to leave the current exemption in place. This alternative is not recommended. Removing the exemption will harmonize the tax treatment of all nicotine products such as vaping oils and devices, and smokeless tobacco. This will make the taxation of these items simpler for retailers while contributing some revenue to the City.

Background Information:

Colorado municipalities, including Westminster, are heavily dependent on sales and use tax revenues. Approximately two-thirds of the City's General Fund revenue is generated by these taxes. Sales and use tax revenues fund crucial services for the public. In addition,

sales and use taxes are the primary funding source for the Parks, Open Space, and Trails Fund.

As a home rule city, Westminster maintains control over its tax administration, enforcement, and audit functions, as well as its tax base. The City of Westminster has exempted cigarettes from sales tax since Ordinance No. 533, which levied the retail sales and use tax in Westminster, was adopted and became effective in 1967.

Although cigarettes are tangible personal property, and thus normally would be subject to the City's sales tax, an exemption currently exists removing them from collection. Cigarettes are taxed at 4.2 cents per cigarette (\$.84 per pack of 20 cigarettes); this tax is made of two components, an original one cent per cigarette tax and an additional 3.2 cent tax that was added pursuant to Amendment 35. Twenty seven percent of the original one cent tax is distributed to local governments based on the amount of revenue collected within a given city or county. The City may receive marginal distribution from subsequent tax increases, but almost all of the additional taxes are dedicated to specific programs and not subject to the distribution.

Cigarettes are also subject to the 2.9 percent state sales tax. Historically, local governments that taxed cigarettes were not entitled to an allocation of state cigarette tax revenue and, in practice, no local taxes are levied.

HB 19-1033, which passed March 28, 2019, allows home rule cities to levy sales taxes on cigarettes, arguably, without forfeiting the distribution from the state. Previously, cities could not collect both their own sales tax and receive their share of the 27% state excise tax. Although the state currently disagrees, the passage of HB 19-1033 may allow cities like Westminster to collect both sets of tax revenue if it chooses. There is pending litigation involving another metro-area city regarding a city's ability to retain the share back while also subjecting cigarettes to a local sales tax. Regardless of Westminster's ability to continue to receive the share back from the state, the removal of the exemption would result in greater authority of the City to administer its own tax program, receive additional revenues, as well as harmonize the treatment of similar products.

In addition to harmonizing the taxation of cigarettes with other similar products, removing the exemption on cigarettes will serve the public interest in that raising costs of cigarettes may operate as a deterrent to using these products. The current city sales tax would result in an additional cost to the consumer of approximately \$.22 per pack of 20 cigarettes. Cigarette prices vary depending on the vendor, but the basis of the \$.22 tax estimate assumes an average taxable price of \$5.66 per pack of cigarettes per a June 2020 survey provided by Tobaccofree.kids.org. That same organization ranks Colorado 41st (with 1 being the highest) in state excise and sales taxes per pack in the U.S. According to Tobaccofreekids.org, annual healthcare costs in Colorado directly caused by smoking is \$1.89 billion. (Campaign for Tobacco-Free Kids, 2020).

The exemption repeal can be accomplished without triggering a TABOR election as supported by recent court cases including the State of Colorado, as well as the Regional Transportation District, each of which eliminated specific exemptions and were determined to have not required an election. The City may choose to rescind sales tax exemptions on goods largely on a discretionary basis because the resulting revenue increase, as a part of the total City revenue, is de-minimus. Past City Council's chose to exempt specific items, such as cigarettes, from being taxed via ordinance. Removal of the exemption will subject the sale of cigarettes to the City's 3.85% sales tax.

It should be noted that there will be a statewide vote on the November 2020 ballot, specifically Proposition EE. If passed, Proposition EE will increase the cigarette tax levied on wholesalers. Proposition EE also increases taxes on other tobacco products, and implements a new tax on nicotine products (e.g. vaping products), which are separate from the tobacco tax. Staff have reviewed Proposition EE and do not believe that the passage of Proposition EE would result in a noticeable change to the shared cigarette tax the City currently receives; as stated above, the City *may* receive a marginal distribution from subsequent tax increases, but almost all of the additional taxes are dedicated to specific programs and not subject to the distribution for local governments.

The proposed amending ordinance supports the City's Strategic Plan Goals of Financially Sustainable Government Providing Excellence in City Services, by making it easier for businesses to voluntarily comply with City tax laws, to accurately collect and remit taxes, and identify revenue opportunities within the state's legal framework to improve the quality of life in the provision of services to citizens through increased revenue generation.

Respectfully submitted,

Donald M. Tripp

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City Manager

ATTACHMENTS:

Description	Upload Date	Type
Councillor's Bill No. 32 Concerning Amendment to Title IV Tax Administration	10/20/2020	Ordinance