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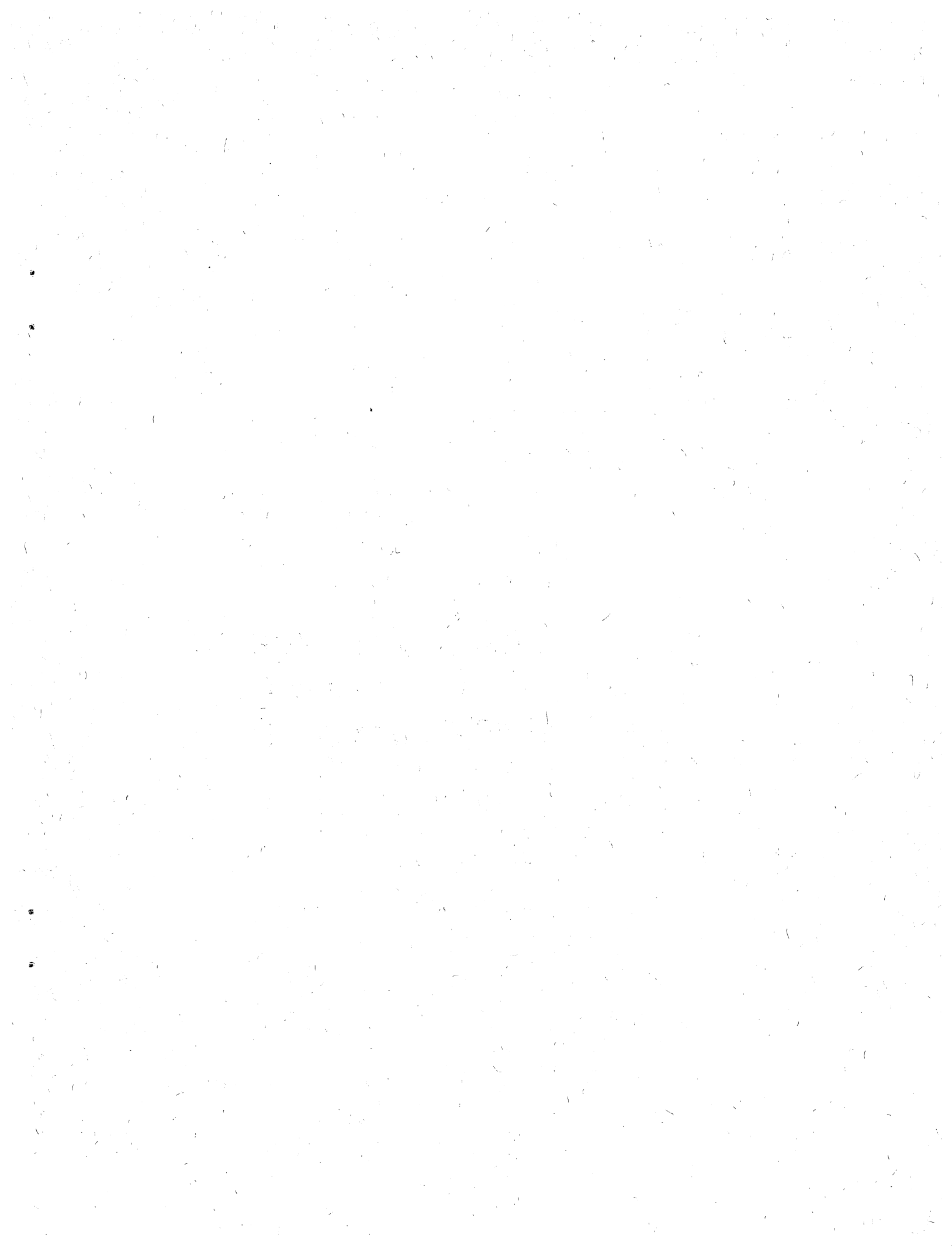
R E P O R T

OF THE

COMMISSION OF THE NEW JERSEY LEGISLATURE
CREATED UNDER THE PROVISIONS OF SENATE
CONCURRENT RESOLUTION NO. 8 OF THE 1957
SESSION OF THE LEGISLATURE.

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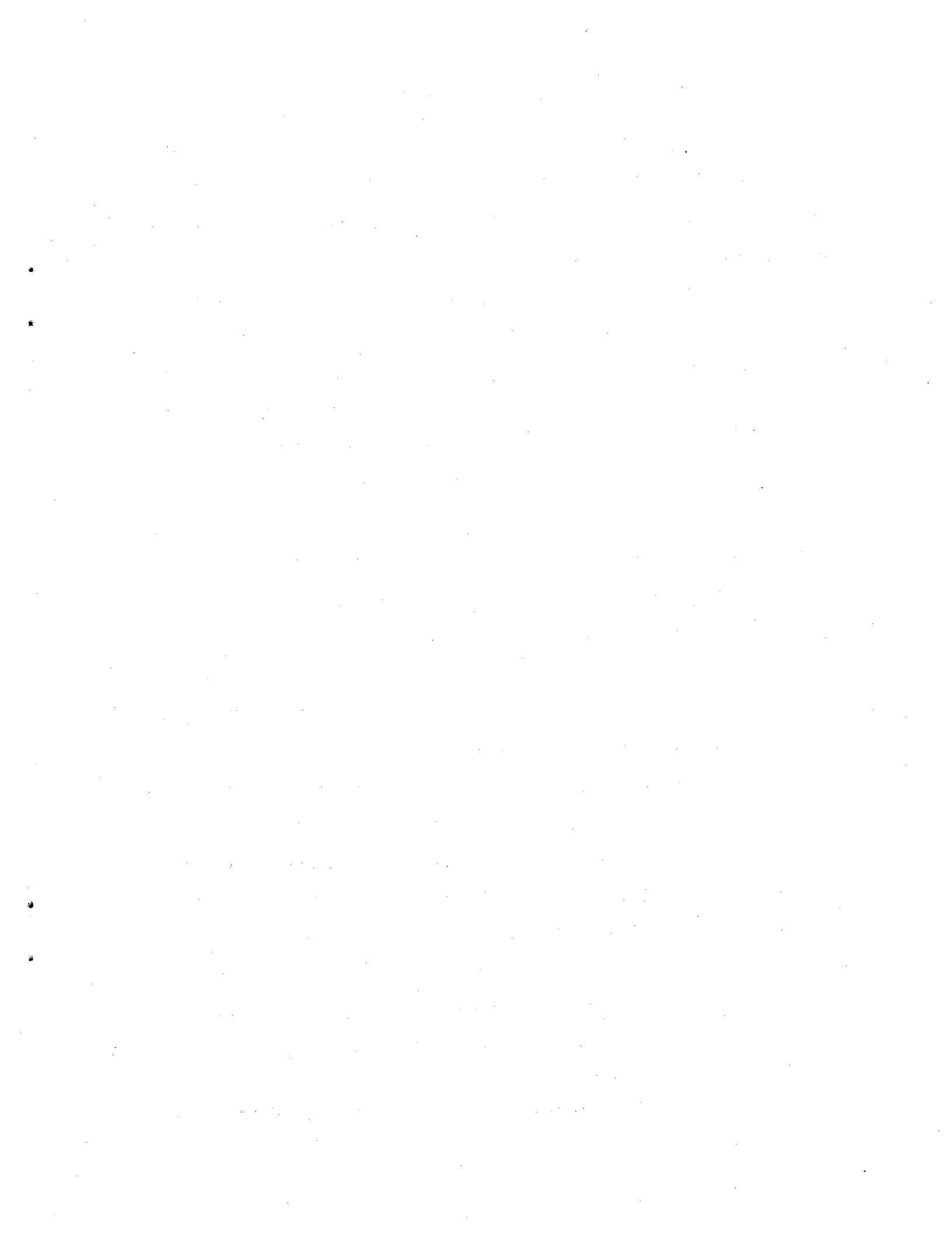
TO THE LEGISLATURE OF THE STATE OF NEW JERSEY:

As the result of Senate Concurrent Resolution No. 8 of the 1957 Session of the Legislature, the undersigned were appointed as members of a Commission "to study the cost of the service and expense imposed upon cigarette distributors in connection with the affixing and handling of State cigarette tax stamps as the same relates to the tax discount allowed therefor, and in connection therewith to examine the report of the Division of Taxation in the Department of the Treasury made pursuant to Joint Resolution No. 10 of the 1956 Session of the Legislature, dated September 7, 1956, and to hold a hearing to accord interested parties an opportunity to be heard."

The Commission examined the report of the Division of Taxation in the Department of the Treasury, dated September 7, 1956, from all of which the Commission has made the following findings of fact:

By Chapter 65 of the Laws of 1948, the Cigarette Tax Act was enacted as N.J.S.A. 54:40A-1, et seq.

Under that law a cigarette tax of \$.03 per package of 20 cigarettes was imposed. On the other hand, because it was found that the most expeditious and economical way for the State to collect this tax was to require the distributors to pre-pay the tax by purchasing the tax stamps and to place said tax stamps on the cigarette packages, a discount of 5% of the tax was allowed to the distributors to cover their expense in handling and affixing the tax stamps on the packages.



The testimony at the hearing showed that when the Cigarette Tax Act was adopted in 1948 by the State of New Jersey, it was determined that the most expeditious and economical manner of collecting the cigarette tax was by using the Tobacco Distributors as a tax collection agency. The procedure to be used was for the distributors to prepay the tax by purchasing tax stamps which they, the distributors, would then affix to all packs of cigarettes. To reimburse the distributors for the costs of this operation, it was determined that a discount of 5% should be allowed them on the purchase of the tax stamps from the State. This procedure and rate of discount was arrived at by a study of experiences in other States which then had cigarette taxes.

Between 1948 and 1957 the costs of the distributors' operation in affixing tax stamps increased considerably, especially in the field of labor which comprises about 70% of the distributors' costs. No increase had been allowed to the distributors despite these increased costs over the past nine years.

The distributors fall into three categories:

Group "A" - those who process up to 50 cases per day;

Group "B" - those who process between 50 to 100 cases per day;

Group "C" - those who process more than 100 cases per day.

It is to this Group "C", specifically, that the report of the Division of Taxation, dated September 7, 1956, is

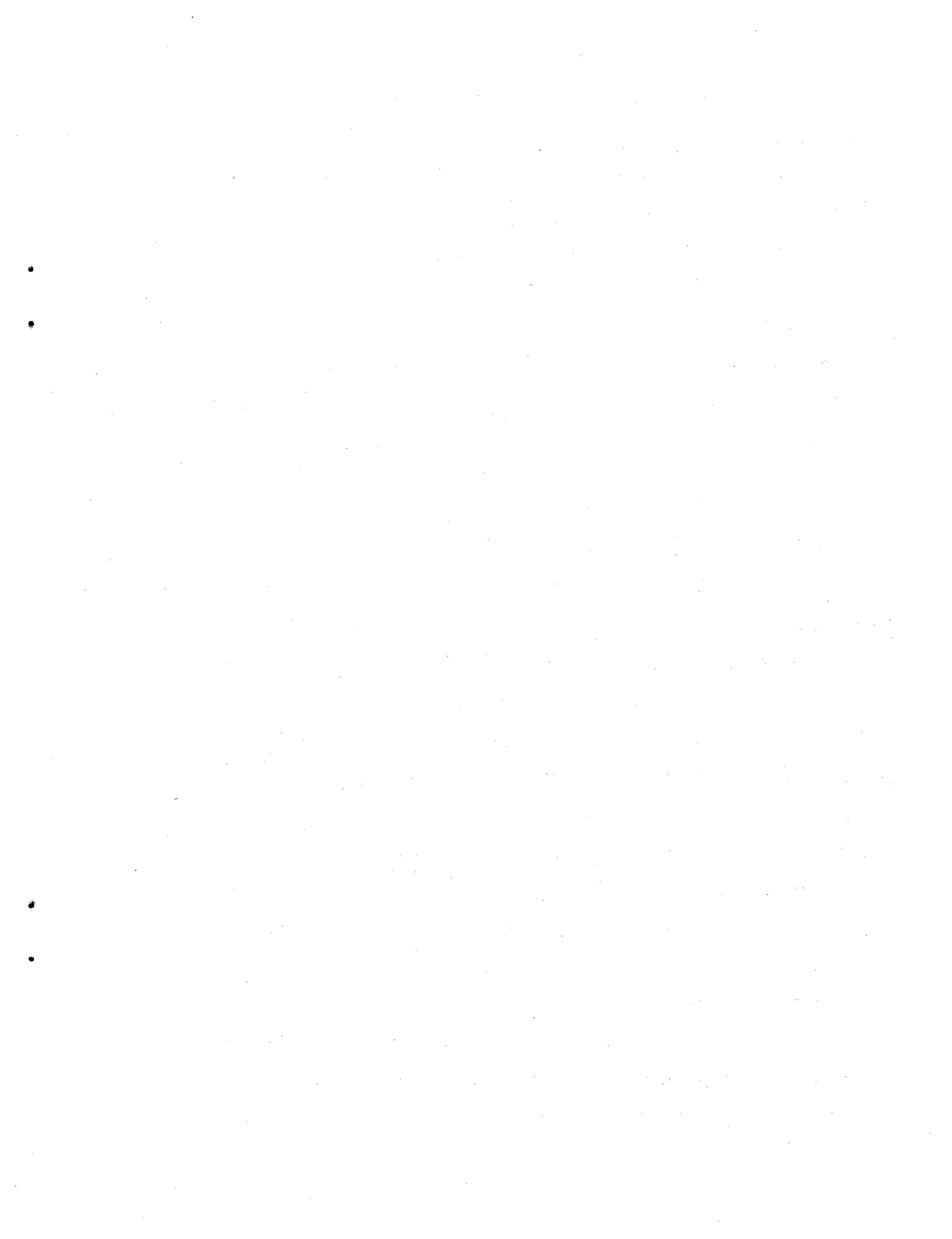


pertinent in so far as it relates to costs, because the basis upon which a "norm" was established by the Division was founded upon data supplied by this "C" group.

However, the evidence disclosed that those distributors who fall within Group "A" comprise approximately 90% of the distributors and process about 75% of the cigarettes sold. It is obvious not only that the "norm" of 160 cases per day cannot apply to this Group, but also that this is the particular Group which suffers the greatest hardship. Sufficient evidence has been adduced to support the claim of the distributors that, in the operation of handling and affixing tax stamps for the State, they have been operating at a loss because of the increase in labor costs and the inability of the distributors to obtain peak efficiency from manpower, which necessarily is only partially productive by virtue of the very nature of the operation.

The same problem exists in other States where the same system of collecting cigarette taxes is used, and it is shown that the other States met this problem by increasing the Cigarette Distributors' cash allowance by allowing the same percentage of discount to remain in the law at a time when cigarette taxes were increased. It was shown that of 28 States that increased cigarette taxes from 1948 to 1956, 21 of them increased distributors' discounts.

In 1952 and continuing through 1956, legislation was proposed in New Jersey, the effect of which would be to increase the amount of the cigarette tax. In every bill submitted to the Legislature affecting the cigarette industry, the distributors' discount rate of 5% remained undisturbed. On March 26,



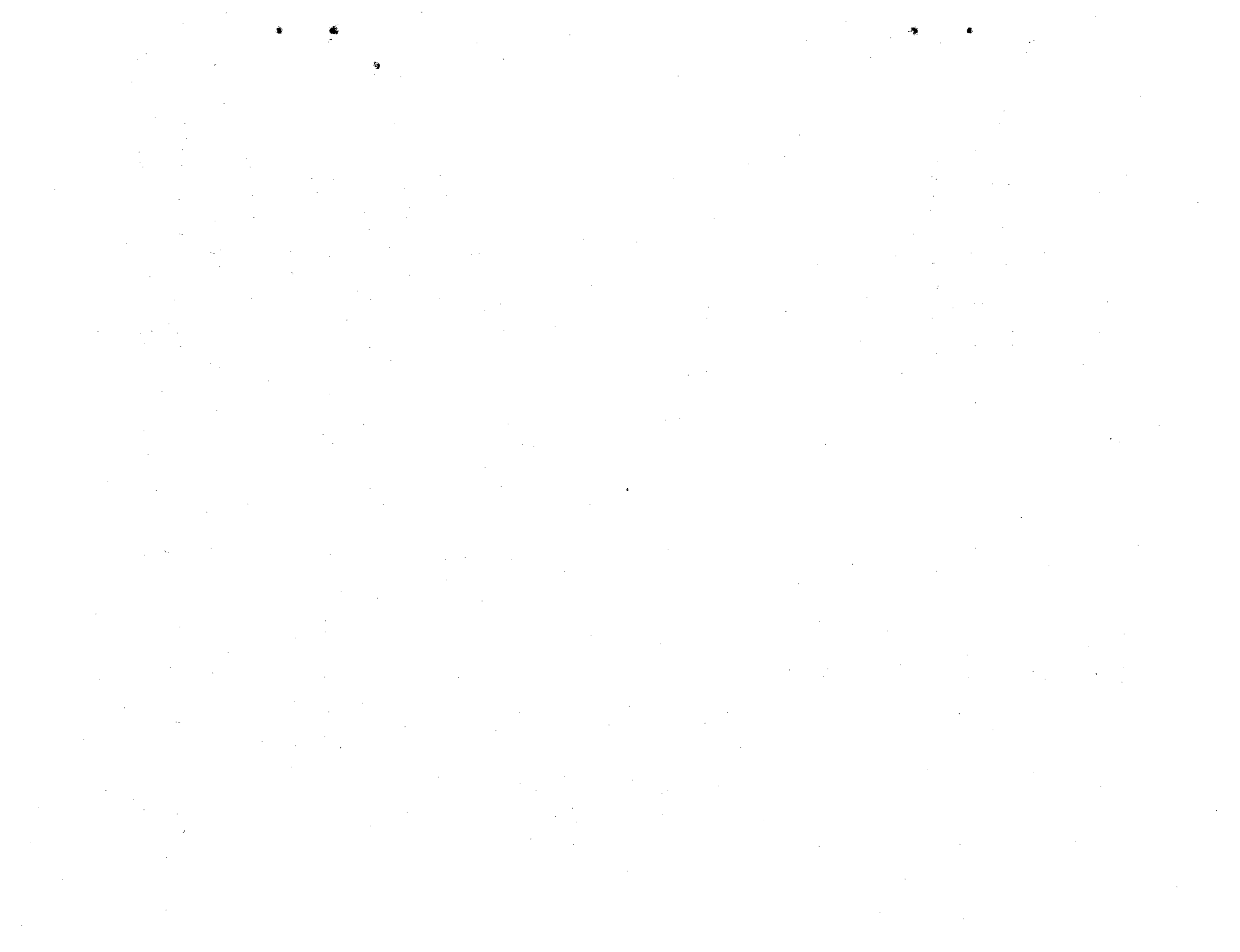
1956, Assembly Bill No. 455 was introduced in the Legislature and passed the very same day under suspension of rules. This bill, which became Chapter 10 of the Laws of 1956 and is now found in N.J.S.A. 54:40A-8 and 54:40A-11, reduced the distributors' discount from 5% to 3%.

Recognition was given at the time of the passage of A 455 to a possible revision of the discount rate because of the complaints registered by the distributors that this reduction was inequitable and that no opportunity had been afforded for a proper presentation of statistical data to support this view.

As a result, Senate Joint Resolution No. 10 was adopted on June 28, 1956, which directed the Tax Department to make a survey for the purpose of ascertaining the distributors' costs of handling and affixing cigarette tax stamps.

This survey was made and the written report thereof was submitted to the Legislature under date of September 7, 1956. The report is comprehensive and sets forth all types of costs and expenses incurred by the distributors in the operation of handling and affixing tax stamps. The distributors have not disputed any of the figures in the report except those which attempt to allocate labor costs. In this regard the distributors contend that this allocation of labor costs is improper and unsound because it is based upon a theory of percentages and "norms" and does not take into consideration the actual labor costs of the great majority of distributors.

The Tax Department admitted that its survey was conducted only in those establishments processing more than 100 cases per day and that no survey had been made of any



distributors in the Group "A" category. (See testimony of Aaron Neeld, page 49, line 5, of transcript).

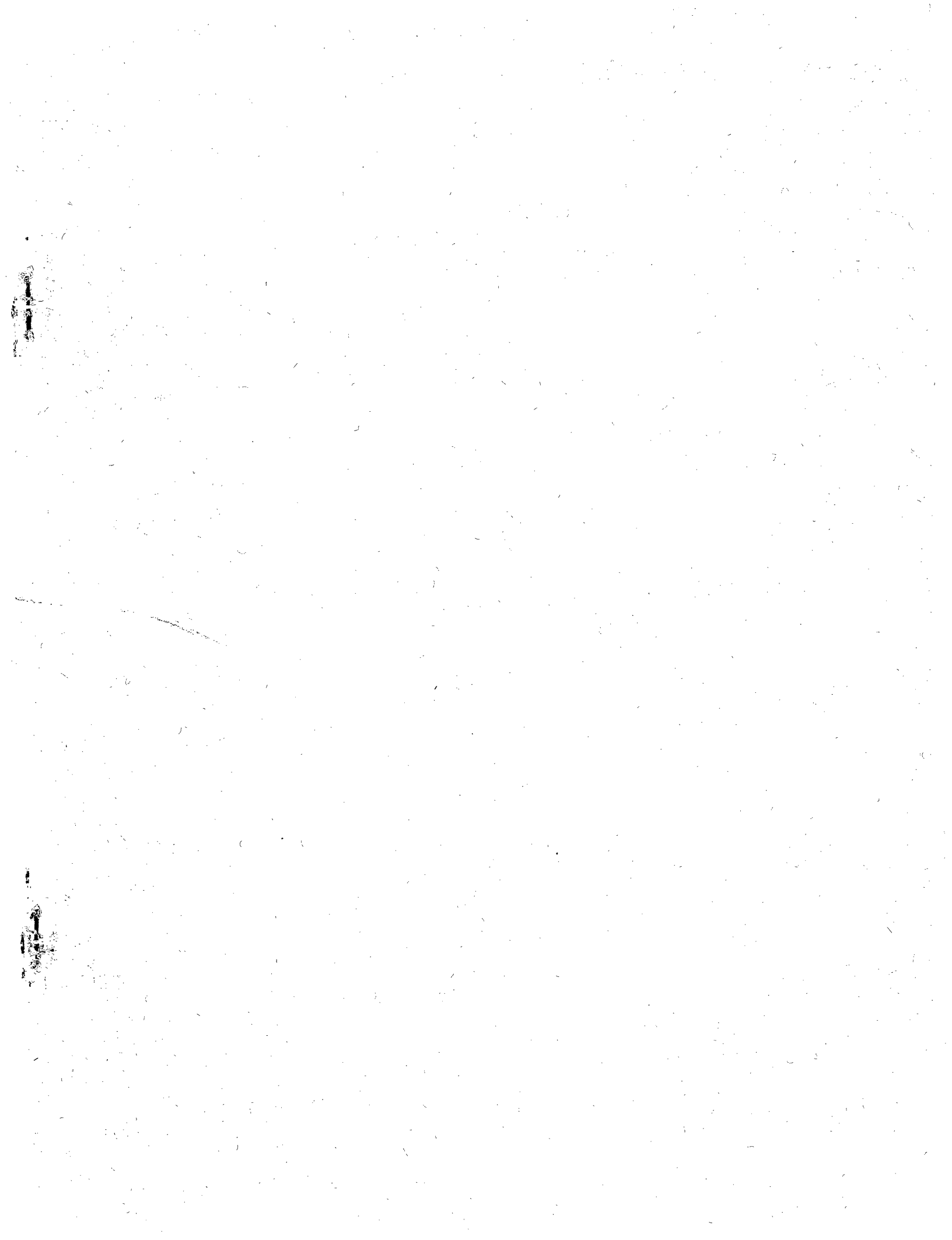
The Department's method of allocating labor costs is criticized by Edgar O. Edwards, Associate Professor of Economics at Princeton University, who also took issue with any allocation of labor costs based upon a so-called "norm."

The distributors contend that the Tax Department's report allows to the distributors who fall into Group "A" category a sum equal to only 28% of the actual full labor costs incurred. (See testimony of Monroe Lewis, pages 49-52 of transcript).

It is clear from the evidence submitted that the present discount rate allowed to the distributors is inequitable and must be modified. It is equally apparent that the present 5% rate of discount should not be granted to all groups of distributors, because this will insure to the very large distributors, who fall into Group "C", a profit on the operation, and at the same time it will compel the small distributors in the Group "A" class to sustain a financial loss.

A practical solution might be the adoption of a progressive discount rate to fit each category.

We, therefore, recommend that Section C54:40A-11 of the Cigarette Tax Act of 1948 be amended to provide



for the following revision:

That the rates of discount to be allowed to a distributor on purchases of stamps, as made within any fiscal year commencing July 1, 1957, be 5% on the first \$250,000.00 face value of stamps; 3% on purchases in excess of \$250,000.00 but not more than \$450,000.00; 2% on purchases in excess of \$450,000.00 but not more than \$650,000.00; and 1% on all purchases in excess of \$650,000.00.

The 1955-56 sales of cigarette tax stamps totaled \$34,372,408.86.

The amount paid on the present 3% discount rate is the sum of \$1,031,172.27.

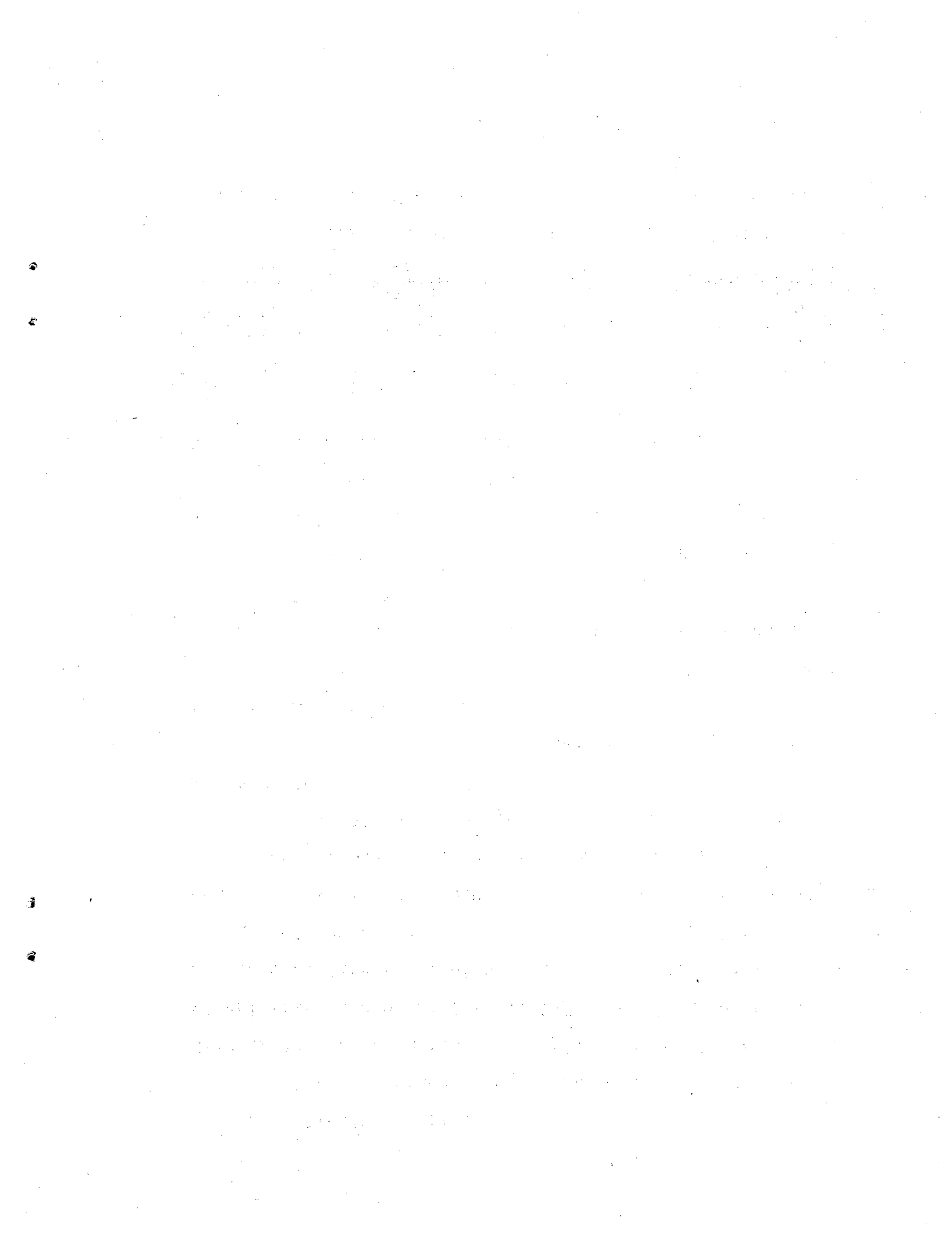
Under the recommended formula, the total discount would be \$1,372,018.02, as compared with the present amount totaling \$1,031,172.27.

The net increase is computed at \$340,845.75, or a figure slightly under 1% of the total 1955-56 sales.

A tabulation based on this formula furnished by the Statistical Bureau of the Tax Division follows:

5%	3%	2%	1%	Total
\$1.00- \$250,000.00	\$250,001.00- \$450,000.00	\$450,001.00- \$650,000.00	Over \$650,000.00	
\$575,000.00	\$193,307.50	\$59,352.20	\$26,560.68	\$854,220.38
389,747.00	615.30	--	--	390,362.30
107,381.16	14,355.00	5,599.18	100.00	127,435.34
<u>\$1,072,128.16</u>	<u>\$208,277.80</u>	<u>\$64,951.38</u>	<u>\$26,660.68</u>	<u>1,372,018.02</u>

We also recommend that the amendment make provision that, where more than one distributor is located at the



same place of business, the operation shall be deemed,
as a matter of law, to be a single distributor.

Respectfully submitted,

Frank S. Shershin, Chairman

John A. Lynch

Harold W. Hannold

C. William Haines

Bruno V. Krawczyk

Ruby V. Perfette

May 6, 1957.

