

NLWJC - Kagan

DPC - Box 046 - Folder-012

**Tobacco-Tobacco Settlement:
Licensing**

Tobacco licensing

- smuggling outreach
- First-retailers

1. Our amendments to McCain -

not moved yet.

Feeney promised to meet, but when?

McC → Summers

Other p. will grab/take credit

Leahy mtg - Fri; McC has to come 1st!

2. St. licensing / First incentives

Lic sch. costs approx 50 m.

ent cost 200 m

} 250 across all states each yr.

NW: 50 is low

also decreases over time

states

changes:

have to have min age

not contingent on lookback; block grant

First 125 - I'm a ST + [I have a low probability sales to minors]

McC: 125 - I'm a ST + 1 license

Picking in unit list factors they have to do as part of license

bonus/pen - bonus - max value: in addition, 19 out of 20 buy

have to ~~get~~ get dinged → 10% bonus penalty - if more than 20% can buy between 80 - 95, happens

250

60

McCain - licensing/ent b.g.
- law - sales to minors
- law - licensing

First compliance bonus - e.g. 50 m.
upside/downside

- 1) First mtg of lookback - real #
- 2) specifying funding for b.g.
- 3) purposes?? - DG-availability

codifying study - 24) changing targets - start now; not in 2003.

Retail Licensing Options Paper
(April 29, 1998)

BACKGROUND

McCain licensing block grant -- sec.235 (p.134): Creates an optional block grant for states that voluntarily decide to license retailers. McCain does not specify block grant funding level and does not prescribe licensing requirements, but stipulates that states that receive grants must enforce compliance in a manner that can be expected to reduce the sale of tobacco products to minors. If a participating state fails to enforce their licensing laws, the Secretary can withhold any portion of the grant. For states that do not have their own licensing schemes, the Secretary may promulgate regulations for a federal licensing program and provide grants to any states which agree to participate in the program.

Frist compliance amendment: While the McCain bill retained the Synar inspection and penalty scheme (sec. 211, p.119), Frist repeals Synar and creates a separate block grant which is designed to reward or penalize states based on retailer compliance rates. This is funded through 5 percent of the lookback penalties. To qualify for the Frist grant, states must demonstrate a 95% compliance rate (ie. fewer than 5 percent of minors who attempt to purchase tobacco products in the state are successful). States that receive a grant must distribute half of it to retailers who do the best job complying with the restrictions on selling tobacco to minors. States which do not meet minimum compliance targets would lose 5 percent of their state share of lookback funding. It is important to note that in repealing Synar, Frist repealed the requirement that states have a law prohibiting the sale of tobacco products to minors.

ISSUES:

- 1) We need to provide sufficient funding for the McCain block grant such that states find the licensing option attractive.
- 2) We do not believe it is a good idea to tie the Frist amendment to the lookback penalty. If the industry does a good job in meeting youth smoking reduction targets, there will either be low or no funding available for the compliance bonus and therefore there will be no extra incentive for states to reduce tobacco purchasing by minors.

PROPOSAL

While HHS would prefer to strike the Frist amendment and retain Synar, the following options assume that we want to work within the Frist compliance scheme. We also assume that the estimated cost of licensing for the states would be \$50 million annually, and the cost of enforcement would be \$200 million, for a total of \$250 million.

McCain optional licensing block grant: retain optional licensing block grant and fund it at \$125 million. The block grant would provide funding for the following activities:

- 1) creating a list of outlets
- 2) conducting merchant education/training
- 3) issuing licenses
- 4) verifying completeness of the list
- 5) linking retailer non-compliance with licensing system

Frist compliance grants: Provide funding of \$125 million annually for grants to states to conduct enforcement through random inspections. Since Frist repealed Synar, we would condition the receipt of funds that states have a law prohibiting sales to minors (similar to Synar).

This section would also provide a bonus for states that reach the 95% compliance target as proposed by Frist. Specifically, a state that has a 95% or better compliance rate and participates in the McCain optional licensing block grant could get an additional 10% bonus. States would be required to distribute half of their bonus to retailers. States that do not meet minimum compliance targets would be penalized, regardless of whether they participate in the optional licensing block grant. HHS proposed that they lose a percentage of block grant funds based on number of years they are out of compliance, ie. 10% of funds in year 1, 20% in year 2, 30% in year 3, and 40% in year 4.

RATIONALE

This scheme builds in four incentives for licensing:

- 1) the optional licensing block grant far exceeds the cost to states to license;
- 2) the Frist compliance block grant does not fully cover states' inspection/enforcement costs so states will want to tap into the optional licensing funds;
- 3) states and retailers will only be able to tap into the Frist compliance bonus if the state participates in the McCain optional licensing block grant.
- 4) if states are required to keep an accurate list of retailers, they will basically have to license in order to meet their compliance targets -- HHS wants to require the retailer lists to be 90% accurate.

TECHNICAL ITEMS

From a technical standpoint, the Frist amendment retains some problematic provisions in the McCain bill such as an onerous sampling methodology, lower minimum compliance targets (compared to Synar) and a delayed penalty scheme -- HHS has recommended technical changes. HHS would also like the Secretary to have the authority to promulgate a model licensing scheme and has provided proposed changes to section 235.

Tob - act - smuggling
and
Tob - act - licensing

Tobacco Legislation Should Contain Tough Anti Black Market Provisions

An effective licensing and enforcement system will minimize the impact of tobacco smuggling and ensure that smuggling does not compromise the central goal of reducing youth smoking.

What does an effective licensing and enforcement system entail?

To prevent black market activity, tobacco products should be regulated in a manner similar to the way the federal government has regulated alcoholic beverages for over 60 years. In other words, a system of licensing and enforcement should be in place to close the distribution chain for tobacco products and prevent smuggling. And just as states currently regulate alcohol retailers, states should have primary responsibility for licensing tobacco retailers.

Under this system, only manufacturers, wholesalers, exporters, importers, distributors and retailers of tobacco products that hold a license or permit would be allowed to engage in those businesses. Licenses would be issued based on certain specified criteria and could be revoked or suspended for certain specified violations. Those conducting business without a license would be subject to penalties. Licensed entities would only be authorized to sell tobacco products to other licensed entities. The sale or distribution to any entity that is unlicensed would be unlawful.

Additionally, legislation should require the marking, branding and identification of packages of all tobacco products intended for domestic distribution and for export so that they may not be diverted or smuggled in circumvention of the legitimate channels for distribution. Finally, any regulatory proposal should include penalty and administrative provisions that would allow for effective, efficient, and uniform enforcement of controls over the distribution. These measures will help ensure that tobacco smuggling is minimized and youth smoking is reduced.

Why aren't existing laws adequate to address these issues?

Existing Federal laws are aimed at collecting Federal excise taxes imposed on tobacco and at assisting States in their efforts to collect state excise taxes imposed on certain tobacco products, not at preventing black market activity.

How does this closed distribution scheme prevent black market activity?

A closed distribution system will ensure that products moving outside the legal channels of distribution can be easily earmarked and targeted for prosecution. This system would limit drastically smugglers' ability to enter products into a legitimate distribution channel. Potential black marketeers would not be able to move products through legitimate wholesalers or distributors. Nor will they be able to sell products to retail consumers at the local convenience stores or other licensed retail outlets. Instead, without a way to place contraband in the market legally, smugglers would

have to sell cigarettes outside channels of legitimate distribution. This would be very risky and criminal provisions and penalties would act as a significant deterrent to persons contemplating the unlawful diversion of tobacco products.

Does this proposal address cross-border smuggling?

Ensuring that the distribution chain for tobacco products is closed at the border would also address cross-border smuggling. That is, the product may legally only be imported, exported, and sold by and through licensees. Recordkeeping provisions, which create an audit trail, and marking requirements will help ensure that smuggled tobacco products do not enter the legitimate domestic distribution chain. Also, specific criminal provisions should be aimed at deterring the unlawful cross-border smuggling of tobacco products.

Would this system work to reduce youth smoking?

Yes. Youth will be a primary target for black market distribution, as a result of increased restrictions on access. Creating a closed distribution scheme will ensure that tobacco products legally move only through the legitimate chain of distribution and will minimize black market distribution of these products.

How would this system be funded?

Industry licensing and registration fees would self-fund this system. Funding includes costs for administering the licensing system as well as investigating unlawful domestic and international trafficking in contraband tobacco products.

Canada experienced a smuggling problem when they raised their excise tax. Why won't a similar problem arise under the McCain bill?

In the early 1990s, Canada did have a problem with cigarettes being legally exported to the US and illegally smuggled back to Canada. There are several reasons to believe that this example does not apply to the US.

- First and foremost, Canada did not have in place an effective licensing and enforcement system, as proposed above.
- Second, smuggling became a problem in Canada because of the ease of access to alternative markets -- 80 percent of the Canadian population lives within a two hour drive of the U.S. border. The U.S. population is much more dispersed.
- Third, sizeable cigarette taxes existed in Canada both before and after Canada's smuggling difficulties in the early 1990s, and thus smuggling in Canada does not seem directly related to price.

STATES % LICENSING

AZ	NO
CO	OR
HI	SC
IA	SD
IN	TN
KY	VA
LA	WV
MI	

4/21 Licensing

Dropped ATF's involvement w/ retail level

McC has fed govt operate as backstop - (FDA auth to license retailers - if states do not)

McC requires lic. of others higher up in food chain.

a) provide incentives to states to pick up.

b) Then: FDA "may" to "shall"

Harkin-Chafee incentive pool?

Frist - conditioning lookback \$

on certain outcome meas-

ures. Add: condition on

Licensing

My food chain: need language making explicit that exporters must be licensed

also need better provision on record keeping

also need tougher penalties

add ~~to~~ as a cond. of licensing - compliance w/ other statutes

catch-all provision - allowing Secy to promulgate implementing regs.

Use fees? McC doesn't use
on wholesalers / manufs.

Take out bonding section - admin hassle / doesn't get you anything.

(Wyden Thing?)

Also too tough on letter-free.



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April 27, 1998

Honorable Orrin G. Hatch
 Chairman, Senate Committee on the Judiciary
 United States Senate
 Senate Russell Building, Room 131
 Washington, DC 20510

Dear Mr. Chairman:

On behalf of the approximately 14,000 members of the Federal Law Enforcement Officers Association (FLEOA) I am writing to you to express our concerns to S. 1415, the "Universal Tobacco Settlement Act", currently pending before your committee. FLEOA supports the goal of reducing youth smoking in this country, however, FLEOA's members also understand and, must plan for and deal with, the criminal black market enterprises that will arise up once this issue is finally settled.

Federal agents are disturbed that throughout the tobacco settlement talks no one has solicited law enforcement's opinion on the historic proposals now before Congress. FLEOA knows that you understand that law enforcement will be greatly affected by this legislation. Organized crime families, motorcycles gangs, and others will move into the lucrative contraband market for tobacco. The resultant rise in crime will not only effect federal law enforcement but also the state and local levels as well.

The emerging black market for tobacco will, in effect, be a new unfunded mandate for law enforcement. By reaching for the laudable goal of reducing youth smoking, Congress is setting up law enforcement for another battle. Congress should recognize this and put in motion proposals to strengthen and increase law enforcement, especially the U.S. Customs Service, the Bureau of Alcohol, Tobacco and Firearms, and multi-jurisdictional organized crime task forces. As S. 1415 is debated in Congress, the smuggling/black market problems that will arise must also be addressed. FLEOA knows that you will follow through with law enforcement's request of being provided the means to deal with whatever emerges.

If you have any questions or need further information, please feel free to contact me at (212) 264-8406 or (516) 368-6117.

Richard J. Gallo

Tob - sr - licensing



Cynthia A. Rice


04/20/98 04:10:24 PM

Record Type: Record

To: Laura Emmett/WHO/EOP

cc:

bcc:

Subject: Re: Erskine Q & A's & talking points 

Tell Elena the Q&A on licensing is fine.

She should know just for her own information -- I think she does already -- that to get a license, wholesalers and distributors would be required to identify whether they had previously been convicted of a felony or a federal crime related to tobacco; retailers would not be subject to such screening in order to register.

Laura Emmett



Laura Emmett

04/20/98 04:00:36 PM

Record Type: Record

To: Cynthia A. Rice/OPD/EOP

cc:

Subject: Erskine Q & A's & talking points



Q&A0420.W

LICENSING AND ANTI-SMUGGLING PROVISIONS

This provision would create a licensing, registration and enforcement system to prevent smuggling and discourage illegal sales to minors. Only those manufacturers, importers, exporters, and wholesalers of tobacco products licensed by the Bureau of Alcohol, Tobacco, and Firearms would be allowed to do business. In addition, only retailers registered with the ATF would be allowed to purchase tobacco products from licensed entities and only licensed entities could sell to registered retailers. Those conducting business without a license or registration would be subject to criminal and civil penalties, as well as seizure and forfeiture of property. The provision would authorize funds for ATF for investigative operations and prosecutions and for ATF and customs to prevent trafficking and contraband tobacco products, and would allow the Secretary of the Treasury to impose licensing and registration fees to recover the costs of administering the system.

This registration system would also help discourage illegal sales to minors. Current Food and Drug Administration regulations forbid retailers from selling tobacco products to anyone under age 18, and they require retailers to obtain verification of age for anyone appearing under age 27. FDA currently contracts with the states to do inspections of retailers of their compliance with these access restrictions, and trains and commissions state officials to conduct these inspections (and, in states that do not wish to contract, FDA will conduct its own inspections). Retailers who violate these rules are subject to monetary penalties. Under this provision, FDA would notify ATF of violations, and ATF would suspend or revoke the registrations of retailers that repeatedly violate these rules, thus preventing them from purchasing cigarettes from manufacturers or distributors. Registrations would be suspended for 30 days for a third violation, for 60 days for a fourth violation, and revoked for the fifth violation. This provision would not affect or supersede any state licensing schemes.

2 **SEC. 2. DEFINITIONS.**

3 (a) **CIGAR.**--The term "cigar" means any roll of tobacco wrapped in leaf tobacco
4 or in any substance containing tobacco (other than any roll of tobacco which is a cigarette
5 within the meaning of subsection (b)(2)).

6 (b) **CIGARETTE.**--The term "cigarette" means--

7 (1) any roll of tobacco wrapped in paper or in any substance not
8 containing tobacco; and

9 (2) any roll of tobacco wrapped in any substance containing tobacco
10 which, because of its appearance, the type of tobacco used in the filler, or its
11 packaging and labeling, is likely to be offered to, or purchased by, consumers as a
12 cigarette described in paragraph (1).

13 (c) **CONTRABAND TOBACCO PRODUCT.**-- The term "contraband tobacco product"
14 means any tobacco product that is manufactured, sold or offered for sale, shipped,
15 delivered, transferred, or possessed in violation of this chapter, Chapter 52 of Title 26,
16 United States Code, or Chapter 114 of Title 18, United States Code or any regulations
17 issued under those statutes.

18 (d) **DEALER.**--The term "dealer" means any person lawfully engaged in the
19 business of selling tobacco products.

20 (e) **ENGAGED IN THE BUSINESS.**-- The term "engaged in the business" means--

21 (1) as applied to a manufacturer of tobacco products, any person who
22 devotes time, attention, and labor to manufacturing tobacco products for sale or
23 distribution;

24 (2) as applied to an importer of tobacco products, any person who devotes
25 time, attention, and labor to importing tobacco products into the United States
26 from a place outside the United States for sale or distribution;

1 (3) as applied to an exporter of tobacco products, any person who devotes
2 time, attention, and labor to exporting tobacco products for sale or distribution
3 outside the United States;

4 (4) as applied to a wholesaler in tobacco products, any person who devotes
5 time, attention, and labor to the sale or distribution of tobacco products at
6 wholesale; and

7 (5) as applied to a retailer in tobacco products, any person who devotes
8 time, attention, and labor to the sale or distribution of tobacco products to
9 consumers.

10 (f) EXPORTER.--The term "exporter" means any person engaged in the business of
11 exporting tobacco products from the United States for purposes of sale or distribution;
12 and the term "licensed exporter" means any such person licensed under the provisions of
13 this chapter.

14 (g) IMPORTER.--The term "importer" means any person engaged in the business of
15 importing tobacco products into the United States for purposes of sale or distribution; and
16 the term "licensed importer" means any such person licensed under the provisions of this
17 chapter.

18 (h) INTENTIONALLY.--The term "intentionally" means doing an act, or omitting to
19 do an act, deliberately, and not due to accident, inadvertence, or mistake. An intentional
20 act does not require that a person knew that his act constituted an offense.

21 (i) MANUFACTURER.-- The term "manufacturer" means any person engaged in the
22 business of manufacturing a tobacco product for purposes of sale or distribution; and the
23 term "licensed manufacturer" means any such person licensed under the provisions of this
24 chapter, except that such term shall not include a person who produces cigars, cigarettes,
25 smokeless tobacco, or pipe tobacco solely for his own personal consumption or use.

26 (j) PACKAGE.--The term "package" means the innermost sealed container,
27 irrespective of the material from which such container is made, in which a tobacco

1 product is placed by the manufacturer and in which such tobacco product is offered for
2 sale to a member of the general public.

3 (k) PERSON.--The term "person" includes any individual, corporation, company,
4 association, firm, partnership, society, or joint stock company.

5 (l) PIPE TOBACCO.--The term "pipe tobacco" means any tobacco which, because
6 of its appearance, type, packaging, or labeling, is suitable for use and likely to be offered
7 to, or purchased by, consumers as tobacco to be smoked in a pipe.

8 (m) RETAILER.--The term "retailer" means any person engaged in the business of
9 distributing or selling tobacco products at retail; and the term "registered retailer" means
10 any such person registered under the provisions of this chapter.

11 (n) ROLL-YOUR-OWN TOBACCO.--The term "roll-your-own tobacco" means any
12 tobacco that, because of its appearance, type, packaging, or labeling, is suitable for use
13 and likely to be offered to, or purchased by, consumers as tobacco for making cigarettes.

14 (o) SECRETARY.--The term "Secretary" means the Secretary of the Treasury or his
15 delegate.

16 (p) SECRETARY OF HEALTH AND HUMAN SERVICES. The term "Secretary of Health
17 and Human Services means the Secretary of Health and Human Services or his delegate.

18 (q) SMOKELESS TOBACCO.--The term "smokeless tobacco" means any snuff or
19 chewing tobacco.

20 (1) The term "snuff" means any finely cut, ground, or powdered tobacco
21 that is not intended to be smoked.

22 (2) The term "chewing tobacco" means any leaf tobacco that is not
23 intended to be smoked.

24 (r) STATE.--The term "State" includes the several States, the District of Columbia,
25 the Commonwealth of Puerto Rico, and the possessions of the United States.

26 (s) TOBACCO PRODUCTS. --The term "tobacco products" means cigars, cigarettes,
27 smokeless tobacco, pipe tobacco, and roll-your-own tobacco.

1 (t) UNITED STATES.--The term "United States" means the several States, the
2 District of Columbia, the Commonwealth of Puerto Rico, and the possessions of the
3 United States.

4 (u) WHOLESALE.--The term "wholesaler" means any person engaged in the
5 business of purchasing tobacco products for resale at wholesale, or any person acting as
6 an agent or broker for any person engaged in the business of purchasing tobacco products
7 for resale at wholesale.

8 **SEC. 3. LICENSING AND RETAILER REGISTRATION.**

9 (a)(1) LICENSING.--No person shall engage in the business as a manufacturer,
10 importer, exporter, or wholesaler of tobacco products until such person has received a
11 license to do so from the Secretary. The application shall be in such form and contain
12 such information necessary to determine eligibility for licensing as the Secretary shall by
13 regulation prescribe. Each applicant shall pay an annual fee for obtaining and
14 maintaining such a license, a separate license and fee being required for each place in
15 which the applicant is to do business. Failure to pay this annual fee will result in the
16 automatic termination of the license.

17 (2) ELIGIBILITY.--A person shall be entitled to a license unless the
18 Secretary finds--

19 (A) that such person has been previously convicted of a Federal
20 crime relating to tobacco, including the taxation thereof;

21 (B) that such person has, within five years prior to the date of
22 application, been previously convicted of any felony under Federal or
23 State law; or

24 (C) that such person is, by virtue of his business experience,
25 financial standing, or trade connections, not likely to maintain such
26 operations in conformity with Federal law.

1 (3) ISSUANCE OF LICENSE.--Upon the filing of a proper application,
2 payment of the prescribed annual fee, and a finding that the person is entitled to a
3 license, the Secretary shall issue to a qualified applicant the appropriate license
4 subject to the provisions of this chapter and other applicable provisions of law,
5 which shall entitle the licensee to engage in the business of manufacturing,
6 importing, exporting, or wholesaling in tobacco products as the case may be.

7 (4) DURATION.--Any license issued under this chapter shall continue in
8 effect until revoked, suspended, or annulled as provided in this subsection, or
9 voluntarily surrendered, except that--

10 (A) if leased, sold, or otherwise transferred, the license shall be
11 automatically terminated; and,

12 (B) if transferred by operation of law or if actual or legal control of
13 the licensee is acquired, directly or indirectly, whether by stock-ownership
14 or in any other manner, by any person, then such license shall be
15 terminated after thirty days; provided, that if within a thirty-day period
16 application is made for a new license, then the outstanding license shall
17 continue in effect until such application is finally acted upon by the
18 Secretary.

19 (5) CONDITIONS.--All licenses issued under this chapter shall be
20 conditioned upon compliance with the provisions of this chapter, all Federal laws
21 relating to the taxation of tobacco products, the Contraband Cigarette Trafficking
22 Act, 18 U.S.C. Chapter 114, the Jenkins Act, 15 U.S.C. § 375, *et seq.*, and any
23 regulations issued pursuant to such statutes.

24 (b)(1) RETAILER REGISTRATION.--No person shall engage in the business as a
25 retailer of tobacco products until such person has registered with the Secretary and paid a
26 fee for obtaining such registration, a separate registration and fee being required for each
27 place in which the retailer is to do business. The registration shall be in such form and

1 contain such information deemed necessary as the Secretary shall by regulation prescribe.
2 Any registration issued under this chapter shall continue in effect for a period of one year.
3 Such registration may not be leased, sold, or transferred, by operation of law or
4 otherwise. The fee imposed by this subsection shall be paid in such form, manner, and at
5 such time as the Secretary by regulation shall prescribe. No fee shall be pro-rated if a
6 retailer commences operations any time after the first of the year. Any registration
7 issued under this chapter shall terminate when the registration is leased, sold, or
8 transferred, by operation of law, or otherwise to another person.

9 (2) ISSUANCE OF REGISTRATION.--Upon the filing of a proper registration
10 and payment of the prescribed fee, the Secretary shall register a qualified retailer
11 which, subject to the provisions of this chapter and other applicable provisions of
12 law, shall entitle the retailer to engage in the business as a retailer in tobacco
13 products, unless the Secretary finds that the person submitting a registration has
14 previously had a registration under this chapter revoked.

15 (3) CONDITIONS.--A retailer registration shall be conditioned upon
16 compliance with this chapter, all Federal laws relating to the taxation of tobacco
17 products; the Contraband Cigarette Trafficking Act, 18 U.S.C. Chapter 114, and
18 any regulations issued pursuant to such statutes.

19 (c) PROCEDURES.

20 (1) ANNULMENT.--The Secretary may, after providing notice, annul any
21 license or registration issued under this chapter if the Secretary finds that the
22 license or registration was procured through fraud, misrepresentation, or
23 concealment of material fact. If the Secretary annuls a license or registration, he
24 shall, upon request by the aggrieved party, promptly hold a hearing to review the
25 annulment of such license or registration.

26 (2) DENIAL.--The Secretary may, after providing notice, deny any
27 application for a license or reject any registration submitted under this chapter by

1 a person the Secretary has reason to believe is not entitled to receive such license
2 or registration. If the Secretary denies an application for a license or rejects a
3 registration, he shall, upon request by the aggrieved party, promptly hold a
4 hearing to review the denial, revocation, or suspension of such license or
5 registration.

6 (3) REVOCATION OR SUSPENSION.—The Secretary may, after providing
7 notice, revoke, or suspend any license or registration issued under this chapter if
8 the Secretary finds the person holding the license or registration has violated the
9 conditions of licensing or registration. If the Secretary revokes or suspends a
10 license or registration, he shall, upon request by the aggrieved party, promptly
11 hold a hearing to review the revocation or suspension of such license or
12 registration.

13 (4) VIOLATIONS OF YOUTH ACCESS RESTRICTIONS.—Upon the issuance of
14 a final order by the Secretary of Health and Human Services pursuant to section
15 321 *et seq.*, of Title 21, United States Code, that a registered retailer has violated
16 section 360j(e) of Title 21, United States Code, or the regulations issued
17 thereunder, and upon proper referral of such final order to the Secretary, a
18 registration issued under this chapter shall be automatically suspended or revoked
19 in accordance with the final order of the Secretary of Health and Human Services.
20 Upon receipt of such order, the Secretary shall, within 60 days, provide notice to
21 the registrant that his registration is suspended or revoked. The provisions of
22 subsections (d) and (e) of this section shall not apply with respect to the
23 revocation or suspension of any registration issued under this chapter resulting
24 from a final order from the Secretary of Health and Human Services.

25 (d)(1) PROCESS.—Any person whose application for a license is denied or
26 application for registration, is rejected, or any holder of a license or registration that is
27 revoked, suspended, or annulled shall receive a written notice from the Secretary stating

1 specifically the grounds upon which the application was denied or upon which the license
2 or registration was revoked, suspended, or annulled. Any notice of a revocation or
3 suspension of a license or registration shall be given to the holder of such license or
4 registration before the effective date of the revocation or suspension.

5 (2) NOTICE.--Written notice of any denial of application, rejection of
6 registration, suspension, revocation, annulment, or other proceedings, shall be
7 served--

8 (A) in person by any officer or employee of the Secretary
9 authorized for the purpose; or

10 (B) by mailing the order certified mail, addressed to the applicant
11 or respondent at his last known address in the records of the Secretary.

12 (c) APPEAL.--An applicant, registrant, or licensee may appeal any final order of
13 the Secretary denying an application for a license, rejecting a registration, or suspending,
14 revoking, or annulling, a license or registration. The aggrieved party may at any time
15 within sixty days after the date the notice of such final order was given file a petition in
16 the circuit court of appeals of the United States within any circuit in which such person
17 resides or has as a principal place of business, or in the United States Court of Appeals
18 for the District of Columbia, asking that the order of the Secretary be modified or set
19 aside in whole or in part. A copy of the petition shall forthwith be transmitted by the
20 clerk of the court to the Secretary, or any officer designated by him or her for that
21 purpose, and thereupon the Secretary shall file in court the record upon which the order
22 complained of was entered, as provided in section 2112 of Title 28, United States Code.
23 Upon the filing of such petition such court shall have exclusive jurisdiction to affirm,
24 modify, or set aside such order, in whole or in part. No objection to the order of the
25 Secretary shall be considered by the court unless such objection shall have been urged
26 before the Secretary or unless there were reasonable grounds for failure so to do. The
27 finding of the Secretary as to the facts, if supported by substantial evidence, shall be

1 conclusive. If any party shall apply to the court for leave to adduce additional evidence,
2 and shall show to the satisfaction of the court that such additional evidence is material
3 and there were reasonable grounds for failure to adduce such evidence in the proceeding
4 before the Secretary, the court may order such additional evidence to be taken before the
5 Secretary and to be adduced upon the hearing in such manner and upon such terms and
6 conditions as the court may deem proper. The Secretary may modify his findings as to
7 the facts by reason of the additional evidence so taken, and he shall file with the court
8 such new or modified findings, which, if supported by substantial evidence, shall be
9 conclusive, and his recommendation, if any, for the modification or setting aside of the
10 original order. The judgment or decree of the court affirming, modifying, or setting
11 aside, in whole or in part, any such order of the Secretary shall be final, subject to review
12 by the Supreme Court of the United States upon certiorari or certification as provided in
13 section 1254, Title 28, United States Code. The commencement of proceedings under
14 this subsection shall, unless specifically ordered by the court to the contrary, operate as a
15 stay of the Secretary's order.

16 **SEC. 4. UNLAWFUL ACTS.**

17 (a) It shall be unlawful for any person--

18 (1) except a licensed manufacturer, licensed exporter, licensed importer, or
19 licensed wholesaler to engage intentionally in the business of manufacturing,
20 exporting, importing or wholesaling any tobacco product; or

21 (2) except a registered retailer to engage intentionally in the business of
22 selling or offering for sale tobacco products at retail.

23 (b) It shall be unlawful for any licensed importer, licensed manufacturer, licensed
24 wholesaler intentionally to ship, transport, deliver or receive any tobacco products from
25 or to any person other than a person licensed or registered under this chapter.

26 (c) It shall be unlawful for any retailer registered under the provisions of this
27 chapter intentionally --

1 (1) to receive tobacco products from any person other than a licensed
2 manufacturer, licensed importer, or licensed wholesaler; or

3 (2) to sell or offer for sale to any person in a single transaction any tobacco
4 products in quantities of more than 50 packages, other than a direct return to a
5 licensee for credit.

6 (d) It shall be unlawful for any licensed exporter intentionally --

7 (1) to ship, transport, sell or deliver for sale any tobacco products to any
8 person other than a licensed manufacturer, licensed importer, licensed wholesaler,
9 or foreign purchaser; or

10 (2) to receive any tobacco products from any person other than a licensed
11 manufacturer, licensed importer, or licensed wholesaler; or

12 (3) to ship, transport, sell, deliver or otherwise transfer any tobacco
13 product intended for export unless the package containing the tobacco product is
14 marked "FOR EXPORT ONLY FROM THE UNITED STATES."

15 (e) It shall be unlawful for any person other than a licensed exporter intentionally
16 to ship, transport, receive or possess, for purposes of resale, any tobacco product in
17 packages marked "FOR EXPORT ONLY FROM THE UNITED STATES," other than
18 for direct return to the manufacturer or exporter for re-packing or for re-exportation.

19 (f) It shall be unlawful for any licensed manufacturer, licensed exporter, licensed
20 importer, or licensed wholesaler to make intentionally any false entry in, to fail willfully
21 to make appropriate entry in, or to fail willfully to maintain properly any record or report
22 that he is required to keep as required by this chapter or the regulations promulgated
23 thereunder.

24 (g) It shall be unlawful for any registered retailer to make intentionally any false
25 entry in, to fail willfully to make appropriate entry in, or to fail willfully to maintain
26 properly any record or report that he is required to keep as required by this chapter or the
27 regulations promulgated thereunder.

1 (b) It shall be unlawful for any person intentionally to ship, transport, receive,
2 possess, sell, offer for sale, distribute, or purchase contraband tobacco products in or
3 affecting interstate commerce.

4 **SEC. 5. PENALTIES AND COMPROMISE OF LIABILITY.**

5 (a) CRIMINAL PENALTIES.--Any person violating any of the provisions of section
6 4 shall upon conviction be fined as provided in section 3571 of Title 18, United States
7 Code, imprisoned for not more than five years, or both.

8 (b) CIVIL PENALTIES.--The Secretary may, in lieu of referring violations of this
9 section for criminal prosecution, impose a civil penalty of not more than \$10,000 for each
10 offense.

11 (c) COMPROMISE OF LIABILITY.--The Secretary is authorized, with respect to any
12 violation of this chapter or any regulation issued thereunder, to compromise the liability
13 arising with respect to such violation upon payment of a sum for each offense prior to
14 referral to the Department of Justice for prosecution or defense; an Attorney General or
15 his delegate may compromise any such case after referral to the Department of Justice for
16 prosecution or defense.

17 (d) FORFEITURE.--

18 (1) The Secretary shall seize and forfeit, in accordance with section
19 9703(o) of Title 31, United States Code, any conveyance, tobacco products, or
20 monetary instrument (as defined in section 5312, Title 31, United States Code)
21 involved in a violation of this section or any property, real or personal, which
22 constitutes or is derived from proceeds traceable to a violation of this chapter.

23 (2) The court, in imposing sentence on a person convicted of violating this
24 section, shall order that person to forfeit to the United States any property
25 described in paragraph (1) involved in such violation. The seizure and forfeiture
26 of such property shall be governed by subsections (b), (c) and (e) through (p) of
27 section 853 of Title 21, United States Code.

1 **SEC. 6. GENERAL ADMINISTRATIVE PROVISIONS.**

2 (a) **RECORDS.--**

3 (1) Every manufacturer, importer, wholesaler, or exporter shall keep
4 records in such manner as the Secretary shall prescribe by regulations.

5 (2) Every retailer of tobacco products shall keep records in a manner as
6 the Secretary shall prescribe, including but not limited to records of tobacco
7 products received, and the person from whom such tobacco products were
8 received.

9 (3) The records required by this subsection shall be maintained
10 for a period of not less than five years and the Secretary may, by giving written
11 notice to the manufacturer, importer, wholesaler, exporter, or retailer require the
12 retention for an additional period of not more than two years.

13 (b) **PRESERVATION AND INSPECTION OF RECORDS.--**Any records or documents
14 required to be kept under subsection (a) or any regulations issued pursuant thereto shall
15 be preserved by the person required to keep such records or documents available for
16 inspection by the Secretary during business hours.

17 (c) **ENTRY OF PREMISES FOR INSPECTION.--**The Secretary may enter during
18 business hours the premises (including places of storage) of any manufacturer, importer,
19 wholesaler, exporter, or retailer for the purposes of inspecting such premises and for the
20 examination of any required record or inventory of tobacco products kept or stored by
21 such person on the business premises.
22

1 (d) EXAMINATION AND SUMMONS.--

2 (1) For the purpose of ascertaining whether any manufacturer, importer,
3 wholesaler, exporter, retailer, or any other person is in compliance with the
4 provisions of this Act, the Secretary is authorized at all reasonable times to
5 examine and copy any books, paper, records, or other data that may be relevant or
6 material to such inquiry.

7 (2) In order to conduct an inspection, investigation, or maintain an
8 enforcement action, the Secretary may summon any person having information on
9 the compliance of the provisions of this Act by any manufacturer, importer,
10 wholesaler, exporter, retailer, or any other person to appear before the Secretary at
11 a time and place named in the summons and to give testimony under oath or
12 produce such books, papers, records, or other data as may be relevant or material
13 to such inquiry.

14 (3) A summons shall be served by the Secretary, by an attested copy
15 delivered in hand to the person to whom it is directed, or left at such person's last
16 place of business or abode; and the certificate of service signed by the person
17 serving the summons shall be evidence of the facts it states on the hearing of an
18 application for the enforcement of the summons. When the summons requires the
19 production of books, papers, records, or other data, it shall be sufficient if such
20 books, papers, records, or other data are described with reasonable certainty.

21 (4) Any of the district courts of the United States within the
22 jurisdiction of which such inquiry is carried on may, in case of contumacy or
23 refusal to obey a summons, issue to a person an order requiring such person to
24 appear before the Secretary and give such testimony or produce such books,
25 papers, records, or other data relating to the inquiry; and any failure to obey such
26 order of the court may be punished by such court as a contempt thereof.

1 (e) INDUSTRY COMPLIANCE PROGRAM.-- The Secretary shall prescribe regulations
2 necessary to ensure each licensee establishes and maintains a compliance program. Such
3 program shall be designed to ensure that retailers comply with Federal laws and
4 regulations relating to the distribution of tobacco products to consumers.

5 (f) REPORTS TO THE SECRETARY.--The Secretary is authorized to require, in such
6 manner and form as shall be prescribed in regulations, such reports as are necessary to
7 carry out the powers and duties under this Act including any reports deemed necessary to
8 ensure the proper accounting of materials necessary to manufacture tobacco products.
9 Such reports will include detailed descriptions of licensee compliance programs that have
10 been developed by the licensees to ensure that retailers comply with the Federal laws and
11 regulations relating to the distribution of tobacco products to consumers.

12 (g) UTILIZATION OF OTHER GOVERNMENT AGENCIES.--The Secretary may, with
13 the consent of the department or agency affected, utilize the services of any department or
14 other agency of the Government to the extent necessary to carry out the powers and duties
15 under this Act and authorize officers and employees thereof to act as agents of the
16 Secretary.

17 (h) MARKINGS, BRANDING, IDENTIFICATION.-- Tobacco products shall be marked,
18 branded, packaged, or identified in such a manner as the Secretary shall prescribe by
19 regulations.

20 (i) PROCEEDS OF INVESTIGATIVE OPERATIONS.--With respect to any undercover
21 investigative operation of the Bureau of Alcohol, Tobacco and Firearms (hereinafter
22 "ATF") that is necessary for the detection and prosecution of offenses against the United
23 States under Titles ____ of the United States Code involving tobacco products which are
24 within the jurisdiction of the Secretary, and notwithstanding any other provision of law--

25 (1) sums authorized to be appropriated to ATF and the proceeds from such
26 operation may be deposited in banks or other financial institutions;

1 (2) the proceeds from such operation may be used to offset necessary and
2 reasonable expenses incurred in such operation;

3 (3) sums authorized to be appropriated to ATF may be used to purchase
4 property, building, and other facilities, and to lease space within the United States,
5 the District of Columbia, and the territories and possessions of the United States,
6 and to establish or acquire proprietary corporations or business entities and
7 operate such corporations or business entities on a commercial basis; and

8 (4) ATF shall comply with liquidation, deposit, audit, and reporting
9 provisions in 19 U.S.C. § 2081 (b) - (d) to the extent applicable and not
10 inconsistent with this subsection;

11 provided, however, that the Director or his delegate has certified in writing the actions
12 authorized by paragraphs (1), (2), and (3) are necessary for the conduct of such operation.

13 **SEC. 7. FUNDING.**

14 (a) LICENSING AND REGISTRATION FEES.--The Secretary may, in the
15 Secretary's sole discretion, set the licensing and registration fees required by this chapter,
16 in such amounts as are necessary to recover the costs of administering the provisions of
17 this Chapter, including preventing trafficking in contraband tobacco products.

18 (b) DISPOSITION OF FEES.--Fees collected by the Secretary under this chapter shall
19 be deposited in an account with the Treasury of the United States that is specially
20 designated for paying the costs associated with the administration of this chapter. The
21 Secretary is authorized and directed to pay out of any funds available in such account any
22 expenses incurred by the Federal Government in administering this chapter (including
23 expenses incurred for the salaries and expenses of individuals employed to provide such
24 services). None of the funds deposited into such account shall be available for any
25 purpose other than making payments authorized under the preceding sentence.

26 **SEC. 8. TRANSITIONAL RULES.**

27 (a) GENERAL RULES.--

1 (1) Any manufacturer or export warehouse proprietor, who, on the date of
2 enactment of this Act, is a permittee under chapter 52 of the Internal Revenue
3 Code of 1986, and who submits an application pursuant to the provisions of this
4 chapter before (date), may continue to engage in such business pending final
5 action on such application.

6 (2) Any person engaged in the business of importing, exporting,
7 wholesaling, or retailing tobacco products on the date of enactment of this Act,
8 who submits an application pursuant to the provisions of this chapter before
9 (date), may continue to engage in such business pending final action on such
10 application.

11 **SEC. 9. RULES AND REGULATIONS.**

12 The Secretary shall prescribe all needful rules and regulations for the enforcement
13 of this chapter, including all rules and regulations that are necessary to ensure the lawful
14 distribution of tobacco products in interstate or foreign commerce.

15 **SEC. 10. SEVERABILITY.**

16 If any provision of this chapter or the application thereof to any person or
17 circumstance is held invalid, the validity of the remainder of this title and this chapter and
18 of the application of such provision to other persons and circumstances shall not be
19 affected thereby.

Section 11, STATE AND LOCAL PROGRAMS.

Nothing in this chapter shall be construed to limit or constrain state and local programs that impose registration and/or licensing requirements that are in addition to, or different from, the requirements under this chapter.

Section 303 of the Federal Food Drug Cosmetic Act (21 U.S.C. 333) is amended by adding a new provision—

"(h)(1) Any person who is subject to section ___ of Title __, United States Code, as a retailer under that Title who violates Section 520(e) or regulations issued thereunder respecting tobacco products shall, in addition to any applicable penalties elsewhere in this Act, be liable to an order of the Secretary suspending or revoking a registration issued pursuant to section ___ of Title __, United States Code, in accordance with paragraph (2). Such revocation or suspension shall be adjudicated in accordance with the procedures provided in section 303(f)(3)(A), (4). If civil penalties pursuant to section 303(f)(1)(A) are being sought for the same violation or violations, such violation will be adjudicated in a single proceeding for purposes of both subsections.

"(2)(A) In issuing an order for a violation of a regulation issued under section 520(e) involving age or identification restrictions, the Secretary may—

- (i) Order a 30 day registration suspension for a third violation;**
- (ii) Order a 60 day registration suspension for a fourth violation; or**
- (iii) Order registration revocation for a fifth violation.**

"(B) With respect to any violation not encompassed by subparagraph (A), the Secretary shall establish when orders for a 30 day registration suspension, a 60 day registration suspension, and registration revocation are appropriate."

(3) Upon receiving a final order issued by the Secretary suspending or revoking a registration issued under section ___ of Title __, United States Code, the Secretary of the Treasury shall notify the registrant that such registration has been suspended or revoked in accordance with this subsection.

Tobacco -
enforcement -
licensing

RETAILER REGISTRATION/LICENSING ISSUES

Elements of a Registration System

- Retailers of tobacco products will be required to "register" with AFT prior to engaging in the retail sale of tobacco products. AFT would be responsible for ensuring that only registered retailers sell tobacco products. Manufact + distribute tob?
- Manufacturers, importers and wholesalers may distribute tobacco products only to registered retail dealers. AFT would be responsible for enforcing this requirement.
- Registration will be conditioned upon compliance with Federal laws regulating the distribution of tobacco products, including payments of industry payments/taxes. condition of revenue?
- AFT would be responsible for taking action against retailers who violate distribution requirements (e.g., sell to unregistered retailers). ? Same as bullet 2?
- Registration would be subject to suspension and/or revocation automatically upon a determination by FDA that retailer's violations warrant such action. when? by doing what?
- FDA would continue its national enforcement strategy of contracting with state and local agencies to conduct compliance checks.
- FDA would have authority to develop a penalty schedule under which retailers who sell to minors would be subject to escalating civil money penalties and registration suspension and/or revocation (e.g., civil money penalties start with first violation; registration subject to 30 day suspension after 3 violations). not in statute?
- HHS/FDA would be responsible for providing administrative process for retailers charged with violations of access provisions. Statutory provisions should be structured so that suspension/revocation would be automatic once the HHS/FDA process is complete.
- Treasury proposes to pay for ATF system/activities through the imposition of either registration fees or occupational taxes.
- HHS/FDA state contract contracting program and its staffing of the enforcement process would be funded through annual appropriations.

- ▶ Unresolved issue: Because retailers can appeal the administrative actions of AFT and HHS/FDA to the court of appeals, there could be significant delay before the suspension goes into effect. Should there be expedited procedures?
- ▶ Unresolved issue: How will registration suspension be policed? Will AFT monitor all suspensions/revocations, or will monitoring need to be included in FDA's contracts with the states? ?
- ▶ Unresolved issue: Should registrations be subject to suspension and/or revocation for violations of access requirements other than the prohibition on sale to minors (e.g., repeated violations of the prohibition on self-service modes of sale)?

Role of State Licensing

- At minimum, state and local licensure requirements should not be preempted. State and/or local licensure programs would provide additional mechanism to help reduce sales to minors.
- Although state and local licensing programs would add value, it is not clear that the benefits of [requiring] states to enact such programs would outweigh the costs (e.g., the need to provide the states something in return, federalism concerns, administrative responsibilities of ensuring that states have appropriate programs in place). recom?
- ▶ Unresolved issue: Some legislative proposals, although not the current McCain draft, contain provisions that would fine clerks who sell to minors and/or minors themselves. As a general matter, FDA does not enforce against individual users/recipients of a product. In addition, its current enforcement approach does not record the identity of the clerk. If adopted by Congress, these requirements — particularly fines against minors who purchase tobacco products — should be administered and enforced at the state or local level, and should not be made part of the FDA program or statute. leave out

how diff from current leg?

Licensing of Retailers: A Federal Standards Administered by the States Approach

Public health purpose:

A mandatory retailer licensing under this approach would allow license suspension or revocation for repeated violations of the prohibition on sales to minors (and possibly also for violations of in-store access and advertising restrictions). This program would not take the place of existing or enhanced regulation of the chain of distribution of tobacco products from the manufacturer or importer to the wholesaler and/or the retailer for taxation or other non-public health purposes. The focus is instead on those facilities that sell tobacco products to the consuming public in order to prevent sales to minors. Because tobacco product sales increase overall sales for most retailers, the threat of losing the ability to sell tobacco products would be a powerful incentive on retailer compliance.]

Concept:

- Retailers would be required by statute to have a Federal license (issued by a State or locality under the authority of the Federal program, or the Federal government).
- The Federal authority would be authorized to suspend and/or revoke a license for particular violations of Federal law.
- Federal penalties would be available against retailers who sell tobacco products without a license.
- The Federal agency would have authority to establish minimum standards for the operation of a licensing program. (These standards would include standards for notification of retailers and issuance, authorization to collect fees from retailers to pay for administrative costs, and standards for ensuring compliance with license requirements).
- The Federal agency would have authority to establish a schedule for the circumstances in which the suspension penalty would be imposed and the length of time the license would be suspended. If revocation is an option, the Federal agency should also have authority to establish procedures for retailers to apply for reinstatement.
- The Federal agency would conduct the administrative and/or judicial processes required to impose these penalties, as well as the fines for selling

tobacco products without a license.

— The Federal agency would have authority to contract with States (and localities) to operate licensing programs. The Federal agency would retain authority to operate programs in States that choose not to participate. }

— Annual appropriations would be available for Federal agency to contract with States for purpose of developing and maintaining a licensing scheme, with appropriations also available for the Federal agency to undertake these responsibilities in States that choose not to contract with the Federal authority. The amount received by the States would be determined through a contract negotiation process and would be in proportion to the scope of the licensing program proposed by the State.

Discussion:

Under this approach, the Federal authority would have the ability to set the standards for licensing programs and would have available the important tool of license revocation, while administrative responsibilities would rest with the States that choose to participate in the contracting process.

Because States would opt in through the contracting process, and the monies received would be in proportion to the States' activities under the contracts, this approach would likely avoid the Tenth Amendment issues that may be present in some other proposals, such as those which tie all of the monies to be received by a State under "settlement" legislation to compliance with the Federally proscribed licensing program requirements. In last term's ruling on the Brady Act, the Supreme Court made clear that the Tenth Amendment bars the Federal government from requiring States to enact or enforce a Federal mandate. Printz v. United States, 117 S. Ct. 2365 (1997). Although Congress may condition the receipt of Federal funds on the States' undertaking certain responsibilities, Supreme Court "decisions have recognized that in some circumstances the financial inducement offered by Congress might be so coercive as to pass the point at which 'pressure turns into compulsion.'" South Dakota v. Dole, 483 U.S. 203, 211 (1987), quoting Steward Machine Co. v. Davis, supra, 301 U.S. 548, 590 (1937). As a result, linking the receipt of any Federal monies under tobacco legislation to compliance with Federal standards for a licensing program may be considered an impermissible coercion on the States, particularly if the area of retailer licensing is deemed to be a core State function.

PROPOSAL RELATING TO TOBACCO LICENSING

- Treasury

I. Scope

This paper provides ideas to combat the anticipated growth in the "black market" distribution of cigarettes and smokeless tobacco in the event the provisions of the tobacco settlement are enacted into law. As explained below, preventing the black market distribution of tobacco products may have the effect of reducing youth smoking. These proposals appear to complement the Department of Health and Human Services' (HHS) proposals relating to licensing entities which sell tobacco products directly to the consuming public.

II. Background

The Secretary of the Treasury, through the Bureau of Alcohol, Tobacco and Firearms (ATF), is responsible for the administration of Chapter 52 of the Internal Revenue Code of 1986 (IRC), which imposes Federal excise taxes on the manufacture of tobacco products. In connection with the collection of these taxes, ATF enforces the permit and record keeping requirements imposed upon manufacturers of tobacco products. These requirements are primarily concerned with protection and collection of the revenue, not the regulation of the distribution of tobacco. Additionally, ATF is responsible for enforcing the Contraband Cigarette Trafficking Act (18 U.S.C. §§ 2341 *et seq.*) which prohibits the shipment, transportation, or possession of more than five cases of cigarettes (60,000 cigarettes) into a State without required evidence of payment of that State's taxes. ATF also has ancillary jurisdiction to enforce the reporting requirements of the Jenkins Act (15 U.S.C. §§ 375 *et seq.*), which requires tobacco distributors to report on a monthly basis to State tobacco tax administrators information about every shipment of cigarettes into a State in which the distributor is not licensed. Finally, ATF works closely with officials from foreign governments, *e.g.*, Canada, to assist in the investigation and prevention of unlawful trafficking in cigarettes from the United States to those countries.

Domestic commerce in cigarettes, which accounts for the largest portion of commerce in tobacco products, is generally conducted through a multi-tiered chain of distribution that can involve a manufacturer or importer, multiple wholesale distributors (including jobbers and stamping agents), and retail dealers. Generally, tax-paid cigarettes are shipped after production to one of several remote manufacturer's warehouses located throughout the country. Most cigarettes are then shipped to one or more wholesale distributors for further distribution to retail dealers. However, some retail dealers purchase cigarettes directly from producers. With respect to exportation, tobacco products can lawfully be exported through either an export warehouse proprietor or a Customs bonded warehouse.

The proposed tobacco settlement requires the tobacco industry to make "payments" on the cigarettes and smokeless tobacco produced in the United States for domestic consumption. The settlement contemplates that these industry payments will be passed on to consumers through increased retail prices for cigarettes. Analysts believe this could result in an increase

of up to \$1.50 in the retail price of a pack of cigarettes.¹ If youth smoking levels are not reduced to certain established levels, the settlement requires the industry to pay penalties, which could increase the retail price of cigarettes even further.

The proposed settlement does not appear to reach products produced abroad and imported into the United States, nor does it reach products exported from the United States. In other words, the industry payments contemplated by the settlement would not be made on cigarettes imported into, or exported from the United States. This "loophole" in the settlement could provide a means for cigarette manufacturers to avoid the industry payments required by the settlement simply by moving operations outside the United States. Moreover, this "loophole" would make the importation and exportation of cigarettes particularly vulnerable to unlawful diversion to the black market.

Based on ATF's experiences gained from investigating the unlawful trafficking of cigarettes and alcohol, it has learned that any action that artificially increases the market price of a commodity (*i.e.*, a tax increase, industry payments or prohibition) tends to give rise to the "black market" distribution of that commodity. At the current level of regulation, the increases contemplated by the settlement would assuredly result in a significant diversion of cigarettes into the black market. Such distribution could grow to a point where the illicit products will be sold at a price significantly lower than the retail price of legitimate products.

Studies show that price is a primary factor young people consider when deciding whether to smoke. These studies support the proposition that the increase in retail price for cigarettes as a result of settlement payments will reduce youth smoking. If this proposition is true, then young people will be a significant market for black market distributors and, if black market distribution grows to a point where the illicit products are widely available, youth smoking could remain static or actually increase. Canada experienced a similar phenomenon after it significantly increased its excise taxes on tobacco in the early 1990s. Ironically, if this were to occur, the legitimate domestic consumption of cigarettes could appear to decrease. Consequently, under the settlement, the industry would appear to be attaining reduced levels of overall consumption and, under the original settlement would have faced lower payments. This would occur despite the fact that youth smoking remained static or actually increased as a result of black market distribution.

III. Regulation of the Tobacco Distribution System on the Alcohol Model

One way to help prevent the unlawful diversion of tobacco products to the black market would be to regulate commerce in tobacco products on a model similar to that in place for

¹While other proposals advocate actual per pack increases of this nature, the effect of the original settlement as written is \$0.58 to \$0.67 per pack in real terms (*i.e.*, controlling for inflation), depending on the size of the youth look back surcharge.

alcohol beverages for over sixty years. This model includes Federal regulation of all levels of the distribution chain for tobacco products -- from manufacturer to retail dealer.

As we understand it, HHS' proposal for the licensing aspects of the tobacco settlement envisions a Federal/State partnership in which the State would enforce the Federal standards relating to the advertising, labeling, promotional schemes, and distribution of cigarettes and smokeless tobacco through a State retail dealer licensing scheme. These State licensing schemes would be funded primarily by the Federal government. The following model complements HHS' proposal in that it imposes controls on the distribution of tobacco products from manufacture or importation up to the retail dealer -- even providing the Federal government a means to put retail dealers who violate Federal laws relating to the regulation of tobacco out of business. Regulation of the sale to the actual consumer would be picked up by HHS' proposal.

Because a licensing/permit system is the most practical way to control the distribution of a commodity, a permit system (similar to that imposed on the alcohol industry by the Federal Alcohol Administration Act (27 U.S.C. §§ 201 et seq.)) should be proposed. This system should require all manufacturers, importers, exporters, and wholesale distributors (including brokers) of tobacco products to obtain a permit. Additionally, all retail dealers in tobacco products should be required to register with the Federal agency designated to administer the program.² The system should include the authority for the designated Federal agency to suspend or revoke any permit or registration, and/or levy fines if the entity holding the permit or registration violates any Federal law relating to the regulation or distribution of tobacco products. Sales of tobacco products to consumers should only be allowed in "non-commercial" quantities. In whole or in part, the funding for this proposal could be derived from a special (occupational) tax/ or registration fee imposed on each level of the distribution chain.

This system should allow manufacturers, importers, or wholesale dealers to deliver, sell, ship, or transfer tobacco products only to permitted or registered entities. Exporters should be allowed to deliver, sell, ship, or transfer tobacco products only to permitted manufacturers, other exporters, or to foreign purchasers. In that regard, all tobacco products intended for export should be marked "FOR EXPORT FROM THE UNITED STATES ONLY." Re-importation of exported cigarettes should not be permitted, except for re-exportation, or for direct return to a manufacturer for repackaging. It should be unlawful to distribute or possess for domestic resale tobacco products in packages marked for export only in the United States.

²Retail dealers would register by filing a "Notice of Registration" with the designated Federal agency. Unless there is evidence that the retail dealer had previously violated Federal laws relating to tobacco, the Notice would be approved. An application for a permit would be investigated much more thoroughly.

Manufacturers, importers, exporters, and wholesale distributors should be required to keep records of production, importation, acquisition, and distribution. Retailers should be required to keep records only of acquisition, since such records are sufficient for enforcement purposes. The designated Federal agency should have adequate inspection authority for both the permitted or registered premises and required records.

Adequate criminal penalties should be imposed for any violations of these provisions. Additionally, the designated Federal agency should be given the authority to impose civil monetary penalties for violation of the proposed system, and the ability to compromise said violations. The designated Federal agency should also be given the authority to seize and forfeit tobacco products, conveyances, and proceeds associated with and derived from any violation of the proposed system.

Finally, the Contraband Cigarette Trafficking Act currently contains loopholes which make enforcement difficult in certain jurisdictions. For example, that Act currently applies only to cigarettes not bearing a tax stamp demonstrating payment of the State tobacco tax. However, five states do not require tax stamps for cigarettes. By closing this loophole, the entire system would have greater integrity, which would generally make it more difficult to divert tobacco products from the lawful distribution chain.

IV. Costs to Implement and Maintain a Comprehensive Tobacco Program

Given the nature of the settlement as outlined, provisions in this proposal could change based on the scope of the legislation resulting from the settlement. However, failure to enact a comprehensive scheme to regulate the distribution of tobacco products will have a substantial impact on the ability of the designated Federal agency to ensure compliance with the proposals. In any event, no proposals will succeed without adequate funding for administration and enforcement.

Assuming a regulatory model similar to the Federal Alcohol Administration Act is adopted, and applying existing workload and cost data for Federal regulation of the alcohol industry, a period of three years would be required to phase-in all aspects of the program. We estimate that costs would exceed \$88 million during each of the first three years of the program. This amount includes processing permit applications, issuing those permits, collecting a special (occupational) tax or registration fee from permitted entities and retailers and necessary enforcement actions. This also assumes a floor stocks tax program (payment of tax on existing tobacco products inventory) would be required.

After the phase-in period, annual costs of \$38 million would be required to collect annual special tax or registration fees, to conduct industry audits to ensure compliance with the law and for necessary enforcement actions.

An annual fee of \$75 for each permittee and retail registrant would cover these costs. This fee could be enhanced to allow flexibility for reimbursement to State/local enforcement

authorities in a Federal/State partnership at the retail level. Also, this fee schedule could be significantly impacted by changes in a proposed regulatory system and would need to be reconsidered in light of those changes.

Current

tobacco - settlement -
licensing

Taxation - Product
wholesale > fed permit-syst -
same line as alcohol

Retail level - 1 to 1.5 ⁱⁿ retailers - registration - system
wholesalers couldn't sell to anyone
without reg #

basic info

reg fee - \$75
will offset

Revoke retail reg ^{cap} state finding
that violates state law (e.g. in
cigarette sales)

last 3 yrs - 8 yrs - then drop to 2 yr

HHB - Above is good complement to FDA plans for
product reg + access

On access - re environ - fed-st licensing schemes
some states have weak licensing systems
fed part sets minimum licensing standards
could be implemented + enforced either on fed or
state level. -

Access and Licensing

This Administration is committed to taking effective action to prevent youth access to tobacco. The FDA rule contains numerous provisions to limit youth access, including establishing 18 as the federal minimum age of sale, requiring retailers to check photo identification of anyone under 27, and eliminating free samples and the sale of single cigarettes. These provisions will help parents to keep their children safe from tobacco products.

The Administration supports legislation that will advance this effort still further. This legislation, in addition to incorporating access restrictions from the FDA rule, shall ban all cigarette vending machines and require tobacco products to be placed out of reach of consumers in any facility that children may enter.

In addition and even more important, the Administration supports legislation to establish an effective licensing scheme to enforce these access restrictions. This scheme shall prohibit any unlicensed person from selling tobacco products to consumers; institute a strict scheme of criminal and civil penalties, including license suspension or revocation, for violations of licensing laws; and impose licensing fees to cover the costs of administering the licensing system.

The Administration will work with Congress on the appropriate distribution of responsibility between the federal and state governments for administering this scheme and imposing penalties. In addition, the Administration will work with Congress on the appropriate level of penalties for violating licensing laws, including by selling tobacco products to minors. These penalties cannot impinge on any existing powers of the FDA to impose civil penalties and must be sufficiently stringent to deter violations; in particular, the threshold for permanently revoking licenses should not be set so high as to lost its power to deter retailers from selling tobacco to minors.

Internal notes:

The above statement embraces the settlement's provisions on youth access restrictions. These provisions, which codify and then go beyond the FDA rule, significantly advance the effort to limit youth access to tobacco products.

Even more important to that effort is the provision for establishing a retail licensing system. FDA and Treasury agree that such a system is necessary for adequate enforcement of youth access provisions. Assuming adequate funding, legislation creating a licensing system would count as one of the principal virtues of the settlement agreement.

The proposed settlement is vague as to who -- state authorities, federal authorities, or some combination of the two -- should administer the licensing scheme. We are not yet in a position to make a concrete recommendation on this question. FDA's current inclination is to

give responsibility for running the scheme to the states, but to retain the power to revoke licenses. We are not sure whether such an approach would work (or even how it could be done); the above statement therefore says only that we will work with Congress on this issue.

The statement also indicates that the penalty structure attached to the licensing scheme needs further thought and strengthening, but does not now commit ourselves to a particular set of penalties. The statement includes language about preserving FDA authority as a safeguard, in light of the settlement's failure to make this point explicit. More meaningfully, the statement suggests that the penalty scheme set out in the settlement is too lenient. The settlement provides for permanent license revocation only after a licensee's tenth offense within two years. Because licensing officials are unlikely to conduct ten compliance checks on a single retailer in a two-year time frame, this provision is essentially meaningless. The above statement indicates that we want mandatory revocation to be a real weapon, without getting into a level of detail unsuitable at this stage of the process.

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8/11/97

Licensing

Licensing generally effective

← fewer retailers / also other restrictions -
good to have list e.g. location
deterrent device

One caveat - resource issues.

How much? see 38 m. stat. But may be that
lessor scheme is approx.

1. Distribution between state + feds?

enforcement schemes? may be easiest -

Admin burden?

← Will to revoke license? > see separate sheet

→ can do this by its entered into w/ states?

or as a condition of some of the \$?

Option 3
best -
FDA
w/ certifying/
contracting

FDA doesn't want to do licensing.

Would prob rather do through certifying
w, if nec, contracting than license
directly.

"Not who we are." // Also - b/c ans of \$.

(license)
User fees - to capture costs of scheme.

Do DOT -

But cuts off policy
from enforcement

APP III A

Pros and Cons of a Licensing Scheme

Present Licensing of Tobacco, Alcohol, and Firearms

- All states and the District of Columbia license retail dealers in alcoholic beverages and wholesalers and producers of alcoholic beverages within their jurisdiction. (In addition, 17 states control either parts of the retail sale of alcohol or all or part of wholesale distribution.)
- Thirty states license retail sales of tobacco products and 28 states license vending machine sales.
- In addition, ATF licenses tobacco and alcohol at the manufacturing and export level (approximately 140 tobacco manufacturers and 200 export warehouse proprietors; 3,800 alcohol beverage manufacturers and 14,500 wholesalers and importers) as well as firearms at all levels of the distribution chain-- nearly 135,000 firearms and explosives licensees. Wholesalers and producers of alcoholic beverages are thus licensed by both the state and the federal government.

Possible New Licensing Schemes for Tobacco Products

The pros and cons of a licensing scheme vary to some extent depending on the particular licensing system used. The proposed tobacco settlement seems to envision some role for both the federal and the state governments. There is a spectrum of constitutionally permissible options:

- the federal government establishes and enforces a nationwide licensing program
- 2 • the federal government allows states to set up and enforce licensing programs that meet federal standards as an alternative to being subject to the federal program
- 3 • the federal government conditions receipt of federal funds (the Industry Payments) on the states' enacting and enforcing a licensing scheme that meets federal standards
- 4 • the state and federal governments establish and enforce separate and concurrent retail licensing schemes; a retailer would be required to have both licenses to operate
- the states license tobacco with advisory input from the federal government.

no

Admin
burden

Gives a bit
to FDA to
revolve
license
Admin
burden

no

Pros and Cons of a Licensing System

ATF and the FDA have contacted state officials involved in state licensing of alcohol and tobacco, respectively, to collect their impressions of the pros and cons of a licensing scheme and

other observations regarding licensing. States have cited the following as specific benefits of a licensing system:

- *The license application process limits the distribution system, saving enforcement resources and helping ensure the integrity of the licensing and regulatory system.* The state observations correspond with ATF's experience in federal firearms licensing: several years ago, when firearms licenses cost only \$10 per year and there was almost no enforcement of the requirement that licensees actually engage in business, the number of licensees blossomed to over 260,000, making enforcement of the gun control laws difficult. Raising the fee to \$200 and strictly enforcing the licensing requirements has led to a decrease of about 60% in the number of licensees over a four year period, greatly enhancing ATF's ability to enforce the gun control laws.

However, the effectiveness of a licensing scheme in ensuring against illegal sales and noncompliance depends in part on the extent to which it covers the distribution chain. Record keeping requirements must be sufficient to enable the licensing agency to trace the commodity from the manufacturer to the retailer. Because the system proposed does not license manufacturers and wholesalers, potential for diversion to illegal consumption or for noncompliance with regulatory requirements would be great, particularly when effective controls are imposed at the retail level.

- *Licensing facilitates identification of retailers for compliance inspections, training and educational programs.* Most states that license alcohol or tobacco products have departments or agencies specifically devoted to enforcing laws relating to the distribution of alcohol or tobacco products and the licensing of dealers in these products. Many jurisdictions also charge these agencies with educating retail dealers on how to comply with the distribution laws. For example, the Illinois Liquor Control Commission (which also regulates the distribution of tobacco products in Illinois) has a program called "Kids Can't Get 'Em Here," designed to educate retail dealers in tobacco products on the regulations relating to distribution of tobacco products, how to assist the Commission in the enforcement of those provisions, how to identify underage purchasers and how properly to check identification. According to the Commission, this program has resulted in a significant increase in retail dealer compliance with Illinois tobacco distribution regulations.
- *The threat of suspending or revoking a license helps to ensure that the retail dealer complies with the State and local laws regulating the product.* Short of revocation, a sensible range of meaningful sanctions for non-compliance gives the licensing agency the needed flexibility to deal with different types of violations. While most states use the threat of suspension or revocation of the license as a way to coerce compliance, many States have added "civil or administrative" fines which are less drastic yet effective ways to achieve compliance. States report that administrative sanctions that can be imposed through an expedited procedure are particularly cost-effective because they can be imposed promptly by the licensing agency.

- *Licensing can. be used to restrict the location of retail dealers.* For example, Massachusetts restricts alcohol licenses from locations near churches or schools.

States have cited the following as the primary difficulties posed by a licensing system:

- *An effective licensing system is expensive and time-consuming to administer and enforce.* An agency charged with administering a licensing system must have adequate resources to process and investigate applications for licenses to ensure that ineligible persons do not improperly receive them. ATF's experience shows that time spent investigating applicants is repaid many fold by avoiding later enforcement actions. Significant resources must also be devoted to inspection, education, and data processing support. Costs of a licensing system are particularly high when enforcement is at the retail level, given the number of potential licensees involved, the frequency of turnover, and the diverse locations where business is conducted. For example, lists of retailers have to be constantly updated or they are useless, but states report that given the number of tobacco product retailers, maintaining the quality and the accuracy of a licensing list in this area requires significant resources.

FDA estimates that there are on the order of 700,000 retail dealers in tobacco products in the United States. Given that ATF taxes 450,000 retail liquor dealers (stores, bars, restaurants, etc.), almost all of whom sell tobacco products, this may be an underestimate. By way of comparison, ATF regulates nearly 135,000 firearms licensees, using nearly 430 inspectors and roughly 50 people to process license applications. The cost of administering this licensing system is approximately \$38 million per year. This estimate does not include the costs of establishing a new system from scratch, nor does it include litigation costs associated with defending challenges to the system; actions to suspend or revoke licenses; or criminal investigations and prosecutions.

The proposal states that enforcement of the licensing scheme would be funded through industry payments, and that licensing fees would cover the administrative costs of issuing State licenses. However, the agreement does not mention any audit authority to account for payments used to enforce the system, nor does it specify whether the federal government or Indian tribes would recover the costs of non-enforcement aspects of licensing programs they administer.

- *Inadequate or uneven enforcement results in a breakdown of the entire system.* All states surveyed noted the need for adequate enforcement authority. States also noted that proper enforcement can be jeopardized by turf battles between different agencies involved in the process: for example, in some states, lists of tobacco retailers are maintained by the revenue collecting agency but tobacco control public health measures are the responsibility of a different agency, and the exchange of information is less than ideal.

The enforcement authority envisioned by the proposed agreement appears deficient in some respects. There is no mention of an investigative authority to determine whether an applicant is eligible for a license or is maintaining compliance. The penalty set out in the proposal for unlawful sale of tobacco products without a license is a misdemeanor. A criminal misdemeanor is not a great deterrent -- particularly if the illicit sale of tobacco products becomes highly profitable. Moreover, it is very difficult to obtain prosecution of a misdemeanor given scarce prosecutorial resources. Similarly, it is unclear whether the sanctions imposed for the sale of tobacco products to underage persons are criminal or civil in nature. They appear to be less severe than sanctions the FDA can impose under its present authority.

- *Licensing can be perceived as an economic barrier to competition.* Licensing imposes a burden on the retail dealer. The process of getting a license is burdensome, intrusive and costly. Moreover, government limitation of the number of licensed retailers benefits those retailers at the expense of those who do not have a license.

Options other than Licensing

There are other mechanisms besides licensing available to enforce regulations governing the sale of tobacco products. Because they do not involve a licensing scheme, they may be less intrusive on law-abiding manufacturers, wholesalers or retailers and less of an administrative burden on the regulating agency. However, significant enforcement resources would have to be expended to ensure compliance.

- Even without a licensing scheme, the enforcing agency could be authorized to seek civil or criminal sanctions for violations from a court. *Have um.*
- The agency could be authorized to impose administrative sanctions, or even issue a "cease and desist" order, when the agency learns of violations. However, due process concerns would likely require the agency to establish a procedure under which notice and a hearing are provided to the violator either prior to the imposition of the sanctions or shortly after. Additionally, the agency would have to rely on enforcement by a court in the event the violator did not comply with the sanctions.

LICENSING

I. Introduction

ATF has extensive experience in licensing the alcohol, tobacco, and firearms industries for specified statutory purposes. ATF licenses approximately 3,800 distilled spirits plants, wineries, and breweries; 140 manufacturers of tobacco products and cigarette papers; 14,500 alcohol beverage wholesalers and importers; 200 tobacco export warehouse proprietors; and nearly 135,000 firearms and explosives licensees.

II. Issues to Consider in Evaluating the Licensing Provisions of the Proposed Agreement

A. A comprehensive regulatory scheme for retailers requires licensing at all levels of the distribution chain.

Any licensing scheme should be tailored to meet its specific goals. For example, ATF's licensing of tobacco manufacturers serves the primary purpose of collecting and protecting the revenue generated by a production tax collected from the manufacturer. To achieve this goal, there is no need to license wholesalers or retailers. In contrast, ATF licenses the entire distribution chain of the firearms industry because the primary purpose of the gun control laws is to prevent sales of guns to particular classes of persons, such as felons, and comprehensive record keeping on all transactions is essential to the national firearms tracing system.

The proposed settlement suggests that the primary goals of a licensing system are to facilitate FDA regulation with respect to access, advertising, and labeling. These goals require a comprehensive licensing scheme that will provide accountability for compliance with the licensing scheme. Record keeping requirements must be sufficient at each level to enable the licensing agency to trace the commodity from the manufacturer to the retailer. Without these controls, there is a "weak link" in the distribution chain that can result in the diversion of the commodity into the stream of unlicensed commerce or noncompliance with regulatory requirements.

However, the system proposed does not license all levels of the distribution chain. Manufacturers and wholesalers that do not sell to consumers would not require a license. Potential for diversion from points earlier in the distribution chain to illegal consumption or for noncompliance with regulatory requirements would be great, particularly when effective controls are imposed at the retail level.

B. The licensing scheme should have enforceable criteria for obtaining a license.

Setting criteria to limit the distribution system has the prophylactic effect of saving enforcement resources and helping ensure the integrity of the licensing and regulatory system. To avoid illicit trading, licenses should be given only to persons who actually intend to engage in the business the license authorizes. Keeping ineligible persons out of the business can also be achieved through licensing fees and inspections. Several years ago, when firearms licenses cost only \$10 per year and there was almost no enforcement of the requirement that licensees actually engage in business, the number of licensees blossomed to over 260,000, making enforcement difficult. Raising the fee to \$200 and strictly enforcing the licensing requirements has led to a decrease of about 60% in the number of licensees over a four year period, greatly enhancing ATF's ability to enforce the gun control laws.

The proposed scheme makes compliance with the proposed legislation a condition of obtaining and holding that license. However, there is no mention of an investigative authority to determine whether an applicant is eligible for a license or, for that matter, to determine whether a licensee is maintaining compliance with the proposed legislation.

C. The licensing system needs an effective enforcement arm.

Because a licensing system produces an incentive to traffic unlawfully in the licensed commodity, a sophisticated enforcement arm is needed to investigate unlawful commerce outside the licensed distribution channels. An effective and fair enforcement arm raises the level of voluntary compliance through education of the licensees and deterrence; in contrast, uneven application leads to resentment and non-compliance on the part of licensees, and ultimately, to litigation.

Certain enforcement tools are necessary to effective licensing enforcement. Periodic inspections ensure that the licensees comply with the system. A sensible range of meaningful sanctions for non-compliance give the licensing agency the needed flexibility to deal with different types of violations. These sanctions can include suspension or revocation of the license, civil fines or penalties, or criminal penalties.

The penalty set out in the proposal for unlawful sale of tobacco products without a license is a misdemeanor. A criminal misdemeanor is not a great deterrent -- particularly if the illicit sale of tobacco products becomes highly profitable. Moreover, it is very difficult to obtain prosecution of a misdemeanor given scarce prosecutorial resources.

It is unclear whether the penalties and other sanctions imposed for the sale of tobacco products to underage persons are criminal or civil in nature. Moreover, it is not clear how to count violations for purposes of imposing these sanctions.

D. The proposal leaves unresolved critical funding and resource issues.

An agency charged with administering a licensing system must have adequate resources to process and investigate applications for licenses to ensure that ineligible persons do not improperly receive them. ATF's experience shows that time spent investigating applicants is repaid many fold by avoiding later enforcement actions. Significant resources must also be devoted to the education and inspection of licensees. Costs associated with data processing support are also significant. Costs of a licensing system are particularly high when enforcement is at the retail level, given the number of potential licensees involved, the frequency of turnover, and the diverse locations where business is conducted.

Resources needed for the proposed scheme will be very substantial. FDA estimates that there are on the order of 700,000 retail dealers in tobacco products in the United States. Given that ATF taxes 450,000 retail liquor dealers (stores, bars, restaurants, etc.), almost all of whom sell tobacco products, this may be an underestimate. Costs relating to the processing and investigation of applications alone will be extensive. Costs associated with investigating violations and taking action against violators could even be greater. For example, ATF regulates nearly 135,000 firearms and explosives licensees, using nearly 430 inspectors and roughly 50 people to process license applications. The cost of administering this licensing system is approximately \$38 million per year. This estimate does not include the costs of establishing a new system from scratch, nor does it include litigation costs associated with defending challenges to system; actions to suspend or revoke licenses; or criminal investigations and prosecutions.

The proposal states that the enforcement of the licensing scheme would be funded through industry payments, and that licensing fees would cover the administrative costs of issuing State licenses.

However, the agreement does not appear to contemplate any audit authority to account for payments of monies used to enforce the system, nor does it specify whether the federal government or Indian tribes would recover the costs of non-enforcement aspects of licensing programs they administer.

E. The proposal will require cooperation between the federal government and the States.

In order to avoid confusion, misinformation and duplication of efforts, it is necessary to vest responsibility for licensing in one agency. However, cooperation and communication with other agencies is often essential to ensure the licensing agency has all relevant information. In particular, commodities licensed by the Federal government may also be regulated by State and local governments. Cooperation, information sharing and communication with those State and local agencies is essential in order to regulate a commodity effectively. This is particularly true when enforcement resources are stretched to the limit at both the Federal and State level. ATF has entered into approximately 40 memoranda of understanding with States calling for the exchange of information pertaining to alcohol and tobacco products.

III. Legal Issues

A. Tenth Amendment Concerns with the Imposition of Federal Standards on the States

According to the proposed agreement, Federal legislation would mandate "minimum Federal standards" for a retail licensing scheme. The agreement is ambiguous about how this would be done, but presumably the following are possibilities:

- The Federal government could be the licensor, exercising its power under the commerce clause;
- The Federal government could preempt the field, but allow the states to adopt and enforce their own regulations conforming to the Federal standard;
- The States could design their own licensing schemes with advisory Federal guidance; or
- The spending power could be used to give incentives to the States to comply with the Federal standard.

The language of the proposed tobacco settlement agreement appears to contemplate legislation under which the Federal government would set minimum standards for licensing laws that states would be required to adopt as state law and required to enforce through funding provided by the tobacco industry. In its recent decision striking down certain portions of the Brady act, the Supreme Court made clear that the Tenth Amendment bars the Federal government from requiring states to enact or enforce a Federal mandate. *Printz v. United States*, No. 95-1478, 1997 U.S. LEXIS 4044 (June 27, 1997). Thus, the licensing scheme cannot be implemented simply by the passage of a Federal law requiring states to adopt Federal prescribed licensing laws and to enforce them.

However, there are other constitutionally permissible models for Congress to encourage state participation in a Federal scheme. Congress can make compliance with Federal standards a precondition for continued state regulation in an otherwise preempted field. *Printz, supra.* at 27, discussing *Hodel v. Virginia Surface Mining & Reclamation Assn., Inc.*, 452 U.S. 264 (1981) and *FERC v. Mississippi*, 456 U.S. 742 (1982); see also *New York v. United States*, 505 U.S. 144, 161-3 (1992). There is no question that under its Commerce Clause authority Congress could establish a nationwide Federal licensing system for tobacco products, to be administered by Federal agencies. Under *Hodel*, Congress could then allow states to adopt and enforce their own regulations if they

complied with Federal standards. If the agreement provides for industry payments to the Federal government for licensing, Congress could finance a Federal licensing system through such payments.

A somewhat more difficult question is whether Congress could through Federal legislation condition the receipt of payments from the tobacco industry to the states, or some portion of those payments, on the states' adoption of licensing laws that complied with Federal standards. Under the Spending Clause, Congress may condition the receipt of Federal funds on the States' undertaking certain action. *Printz, supra*, (O'Connor, J. concurring). In *South Dakota v. Dole*, 483 U.S. 203 (1987), the Supreme Court upheld, as a valid exercise of the Spending Power, a Federal law reducing the percentage of Federal highway funds received by States that failed to enact a law barring consumption of alcohol by persons under 21. Likewise, in *New York v. United States, supra*, the Supreme Court upheld financial incentive provisions of a Federally mandated waste disposal law applying to the States but struck down provisions forcing the State to take title involuntarily to such wastes.

However, the Court has cautioned that if the Federal financial incentive is too powerful it may be deemed not to be a condition but to be impermissible coercion. *South Dakota v. Dole*, 483 U.S. at 211, citing *Stewart Machine Co. v. Davis*, 301 U.S. 548, 590 (1937). The Fourth Circuit, sitting en banc, recently struck down a funding condition imposed by the Department of Education on the receipt of funds under the Individuals with Disabilities Education Act (IDEA). *Comm. of Virginia Dept. of Education v. Riley*, 106 F. 3d 559 (4th Cir. 1997). While the majority held only that the statute did not clearly and expressly authorize the condition imposed, six judges joined an opinion holding that the threat of withdrawal of all IDEA funds if the state did not change its policy of refusing to provide tutors to disabled students expelled from school "begins to resemble impermissible coercion, if not forbidden regulation," in violation of the Tenth Amendment. *Id.* at 569-72. The six seemed moved not only by the size of the amount at issue but also by the area in which the Federal government had sought to influence the state's choice.

Some aspects of the proposed settlement might prove problematic to Federal regulation of state licensing under a Spending Clause approach. First, the industry payments may not be Federal funds subject to the Spending Power -- if, for example, the agreement itself provides for licensing-related payments from the tobacco companies to the states, or otherwise constrains the Federal government's use of the licensing funds. Second, the size of the payments involved may be quite large, so that even in the unlikely event that the states were willing to have industry payments for licensing made to the Federal government and doled out to the states under Federal law, the courts might find the legislation coercive. Finally, not all states are participating in this settlement, and the courts might be particularly skeptical of the legislation as applied to a non-signatory state.

B. Due Process Concerns with Suspension and Revocation

The licensing scheme also provides for a suspension of the retail license (after the first offense) and revocation (after the sixth or subsequent offense). Since a license is a property interest protected by the Fifth Amendment, Due Process requires that the licensees be afforded an opportunity for a hearing before the license may be suspended or revoked. See *Bell v. Burson*, 402 U.S. 535 (1971). This applies to both state and Federal licensing procedures because the due process clause is made applicable to the states by the Fourteenth Amendment. Accordingly, the enabling legislation must establish a procedure (administrative and/or judicial) giving the licensee notice of the charges and an opportunity to be heard.

C. Licensing on Native American Lands

Using a framework adopted from the Clean Air Act (a *Hodel* - model scheme), the proposed agreement provides for licensing provisions governing sales on Native American lands and

commerce in tobacco products by members of Indian tribes. The proposed agreement provides that the federal government would decide for each tribe whether the licensing provisions would be set by the federal government, set by the state subject to federal standards, or set by the tribe subject to federal standards which incorporate state law. (See Appendix III.)

These provisions do not appear to raise additional Constitutional concerns. First, as discussed above, the *Hodel* model of federal-state interaction appears to have been reaffirmed in the Printz case. We are not aware of any constitutional concerns that would arise from the imposition of a federal licensing system or federal standards on Indian tribes, even if the federal standards incorporated state law. The state could also set the licensing requirements: it is well-established that State taxation and regulatory laws can apply to members of Indian tribes and can apply in Indian country. See, e.g., *New York State Department of Taxation v. Attea*, 114 S. Ct. 2028 (1994) (State can require Indian cigarette traders to register with state and tax cigarettes intended for off-reservation consumption). For example, State liquor licensing laws apply to Indians. See *id.*; *Rice v. Rehner*, 463 U.S. 713 (1983).

Also, the agreement states that federal taxes or fees (such as the tobacco excise tax) would apply to commerce in tobacco by members of Indian tribes or on tribal lands. Again, this does not seem to raise significant legal concerns. Federal statutes of general applicability apply with equal force to Indians unless the law touches on exclusive rights of self-governance in purely intramural matters, the application of the law would abrogate treaty rights, or Congress intended to exclude Indians. *U.S. v. Baker*, 63 F.3d 1478, 1484-1485 (9th Cir.) cert. den., 116 S.Ct. 824 (1996). For example, the Contraband Cigarette Act applies to Indian tribes. *U.S. v. Gord*, 77 F.3d 1192 (9th Cir. 1996).

However, it might be difficult for a Federal agency or State to enforce a licensing scheme given current sovereignty issues or the volatile nature of investigations occurring on these lands.

105TH CONGRESS
1ST SESSION

H. R. 2034

To amend section 1926 of the Public Health Service Act to encourage States to strengthen their efforts to prevent the sale and distribution of tobacco products to individuals under the age of 18, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

JUNE 25, 1997

Mr. BISHOP (for himself, Mr. BAESLER, Mr. BONO, Mr. BILBRAY, Mr. CAMP, Mr. CRAMER, Mrs. EMERSON, Mr. JOHN, Mr. PETERSON of Minnesota, Mr. PETERSON of Pennsylvania, Mr. PICKERING, Mr. STEARNS, Mr. STIMKUS, and Mr. TAYLOR of Mississippi) introduced the following bill; which was referred to the Committee on Commerce

A BILL

To amend section 1926 of the Public Health Service Act to encourage States to strengthen their efforts to prevent the sale and distribution of tobacco products to individuals under the age of 18, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the "Tobacco Use by Minors
5 Deterrence Act of 1997".

1 **SEC. 2. AMENDMENT TO SECTION 1926 OF THE PUBLIC**
2 **HEALTH SERVICE ACT.**

3 Section 1926 of the Public Health Service Act (42
4 U.S.C. 300x-26) is amended to read as follows:

5 **"SEC. 1926. STATE LAWS REGARDING SALE OF TOBACCO**
6 **PRODUCTS TO INDIVIDUALS UNDER THE AGE**
7 **OF 18.**

8 **"(a) MODEL LAW.—**

9 **"(1) IN GENERAL.—**Subject to paragraph (2),
10 for fiscal year 1998 and each subsequent fiscal year,
11 the Secretary shall reduce, as provided in subsection
12 (d), the amount of any grant under section 1921
13 that does not have in effect a law with the following
14 provisions:

15 **'SECTION 1. DISTRIBUTION TO MINORS.**

16 **'(a) IN GENERAL.—**No person shall distribute a to-
17 bacco product to an individual under 18 years of age. A
18 person who violates this subsection is liable for—

19 **'(1)** a civil money penalty of \$25 for the first
20 violation of this subsection;

21 **'(2)** a civil money penalty of \$50 for a second
22 violation of this subsection; and

23 **'(3)** a civil money penalty of \$150 for a third
24 or subsequent violation of this subsection.

25 **'(b) EMPLOYERS.—**The employer of an employee who
26 has violated subsection (a) more than twice while in the

1 employ of the employer is liable for a civil money penalty
2 of \$150 for each violation by such employee. An employer
3 who pays a civil money penalty under this subsection shall
4 not, for purposes of section 11, be considered as having
5 violated this Act.

6 '(c) DEFENSES.—It shall be a defense to a charge
7 brought under subsection (a) that—

8 '(1) the defendant—

9 '(A) relied upon proof of age that appeared
10 on its face to be valid, or

11 '(B) had complied with the requirements of
12 section 7, or

13 '(2) the individual to whom the tobacco product
14 was distributed was at the time of the distribution
15 employed in violation of section 9(b).

16 '(d) ENFORCEMENT.—A person who violates sub-
17 section (a) shall not be liable for a civil money penalty
18 unless the individual who received the tobacco product is
19 proceeded against under section 2(a), except that such a
20 person shall be liable for such penalty if such individual
21 was not proceeded against because such individual was
22 testing compliance with this Act under section 9(b).

1 **SEC. 2. PURCHASE, RECEIPT, OR POSSESSION BY MINORS**
2 **PROHIBITED.**

3 (a) IN GENERAL.—An individual under 18 years of
4 age shall not purchase or attempt to purchase, receive or
5 attempt to receive, possess or attempt to possess, smoke
6 or attempt to smoke, or otherwise use or consume or at-
7 tempt to use or consume a tobacco product in a public
8 place. An individual who violates this subsection is liable
9 for a civil money penalty of not less than \$25 and not
10 more than \$150 for each violation and shall be subject
11 to suspension of the individual's authorization to operate
12 a motor vehicle or a requirement to perform community
13 service or both. Upon the second or subsequent violation
14 of this subsection, the authorization of such individual to
15 operate a motor vehicle shall be suspended for a period
16 of not less than 30 days and such individual shall be re-
17 quired to perform community service.

18 (b) NOTICE.—A law enforcement agency, upon de-
19 termining that an individual under 18 years of age alleg-
20 edly purchased, received, possessed, smoked, or otherwise
21 used or attempted to purchase, receive, possess, smoke,
22 or otherwise use, a tobacco product in violation of sub-
23 section (a) shall notify the individual's parent or parents,
24 custodian, or guardian as to the nature of the violation
25 if the name and address of a parent, guardian, or custo-
26 dian is reasonably ascertainable by the law enforcement

1 agency. The notice required by this subsection shall be
2 made not later than 48 hours after the individual who al-
3 legedly violated subsection (a) is cited by such agency for
4 the violation. The notice may be made by any means rea-
5 sonably calculated to give prompt actual notice, including
6 notice in person, by telephone, or by first-class mail.

7 '(c) EMPLOYMENT.—Subsection (a) does not prohibit
8 an individual under the age of 18 from possessing a to-
9 bacco product during regular working hours and in the
10 course of such individual's employment if the tobacco
11 product is not possessed for such individual's consump-
12 tion.

13 **'SEC. 3. SAMPLING.**

14 'It shall be unlawful for any person to distribute to-
15 bacco product samples in any face-to-face transaction
16 without first procuring, from any prospective purchaser or
17 recipient who appears to be under the age of 18, proof
18 of age establishing that such prospective purchaser or re-
19 cipient is 18 years of age or older. A person who violates
20 this section is liable for a civil money penalty of \$150 for
21 each violation. This section does not apply to distributions
22 of tobacco products in an area or establishment that indi-
23 viduals under the age of 18 are not permitted to enter.

1 **'SEC. 4. OUT-OF-PACKAGE DISTRIBUTION.**

2 'It shall be unlawful for any person to distribute ciga-
3 rettes or smokeless tobacco products other than in an un-
4 opened package originating with the manufacturer that
5 bears the health warning required by Federal law. A per-
6 son who distributes a cigarette or smokeless tobacco prod-
7 uct in violation of this section is liable for a civil money
8 penalty of \$150 for each violation.

9 **'SEC. 5. SIGNAGE.**

10 'It shall be unlawful for any person who sells tobacco
11 products over-the-counter to fail to post conspicuously a
12 sign communicating that—

13 '(1) the sale of tobacco products to individuals
14 under the age of 18 is prohibited by law,

15 '(2) the purchase of tobacco products by indi-
16 viduals under the age of 18 is prohibited by law, and

17 '(3) proof of age may be demanded.

18 A person who fails to post a sign in violation of this section
19 is liable for a civil money penalty of \$150 for each viola-
20 tion.

21 **'SEC. 6. DISPLAYS.**

22 '(a) GENERAL RULE.—It shall be unlawful for any
23 person who sells tobacco products over the counter to
24 maintain packages of such products in any location acces-
25 sible to customers that is not within the line of sight, or

1 under the control, of a cashier or other employee, during
2 regular business hours.

3 '(b) PENALTY.—Any person who violates subsection
4 (a) is liable for a civil money penalty of \$150 for each
5 violation.

6 **'SEC. 7. NOTIFICATION OF EMPLOYEES.**

7 '(a) NOTICE TO EMPLOYEES.—Within 180 days of
8 the effective date of this Act, every person engaged in the
9 business of distributing tobacco products at retail shall im-
10 plement a program to notify each employee employed by
11 that person who distributes tobacco products that this
12 Act—

13 '(1) prohibits the distribution of tobacco prod-
14 ucts to any individual under 18 years of age and the
15 purchase, receipt, possession, smoking, or other use
16 or consumption of tobacco products by any individ-
17 ual under 18 years of age,

18 '(2) prohibits out-of-package distribution of
19 cigarettes and smokeless tobacco products, and

20 '(3) permits a defense to a charge of distribu-
21 tion of a tobacco product to an individual under 18
22 years of age based on evidence that the defendant
23 relied upon proof of age that appeared on its face
24 to be valid. Any employer failing to provide the re-

1 required notice to any employee shall be liable for a
2 civil money penalty of \$150 for each violation.

3 ‘(b) STATEMENT.—It shall be a defense to a charge
4 that an employer violated subsection (a) of this section
5 that the employee acknowledged receipt, either in writing
6 or by electronic means, of a statement in substantially the
7 following form:

8 “I understand that State law prohibits the distribu-
9 tion of tobacco products to individuals under 18
10 years of age and out-of-package distribution of ciga-
11 rettes and smokeless tobacco products and permits
12 a defense based on evidence that a prospective pur-
13 chaser’s proof of age was reasonably relied upon and
14 appeared on its face to be valid. I understand that
15 if I sell, give, or voluntarily provide tobacco products
16 to an individual under the age of 18, I may be found
17 responsible for a civil money penalty of \$150 for
18 each violation. I promise to comply with this law.”

19 ‘(c) VICARIOUS LIABILITY.—If an employer is
20 charged with a violation of subsection (a) and the em-
21 ployer uses as a defense to such charge the defense pro-
22 vided by subsection (b), the employer shall be deemed to
23 be liable for such violation if such employer pays the pen-
24 alty imposed on the employee involved in such violation

1 of this Act or in any way reimburses the employee for such
2 penalty.

3 **SEC. 8. VENDING MACHINES**

4 ‘(a) IN GENERAL.—It shall be unlawful for any per-
5 son to distribute tobacco products through a vending ma-
6 chine which is not equipped with a lockout device, except
7 in an establishment that individuals under the age of 18
8 are not permitted to enter. A person who violates this sec-
9 tion is liable for a civil money penalty of \$150 for each
10 violation.

11 ‘(b) DEFINITION.—For purposes of subsection (a),
12 the term “lockout device” means a device attached to a
13 vending machine which—

14 ‘(1) locks out sales from the machine unless it
15 is released by a trained employee who is at least 18
16 years of age;

17 ‘(2) is designed to ensure that only one sale of
18 a tobacco product occurs when the release mecha-
19 nism for the device is activated;

20 ‘(3) is not accessible to customers; and

21 ‘(4) will continue to lockout sales of tobacco
22 products when the power to the device is interrupted
23 or discontinued.

1 **SEC. 9. RANDOM UNANNOUNCED INSPECTIONS; REPORT-**
2 **ING; AND COMPLIANCE.**

3 ‘(a) ENFORCEMENT AND INSPECTION.—The State
4 Police of a State, or such local law enforcement authority
5 duly designated by the State Police, shall enforce this Act
6 in a manner that can reasonably be expected to reduce
7 the extent to which tobacco products are distributed to
8 individuals under 18 years of age and shall conduct ran-
9 dom, unannounced inspections in accordance with the pro-
10 cedures set forth in this Act and in regulations issued
11 under section 1926 of the Public Health Service Act (42
12 U.S.C. 300x-26) to ensure compliance with this Act.

13 ‘(b) USE OF INDIVIDUALS UNDER 18.—The State
14 may engage an individual under 18 years of age to test
15 compliance with this Act, except that such an individual
16 may be used to test compliance with this Act only if the
17 testing is conducted under the following conditions:

18 ‘(1) Prior to use of any individual under the
19 age of 18 years in a random, unannounced inspec-
20 tion, written consent shall be obtained from such in-
21 dividual’s parents or legal guardian.

22 ‘(2) An individual under 18 years of age shall
23 act solely under the supervision and direction of the
24 State during a random, unannounced inspection.

25 ‘(3) An individual under 18 years of age used
26 in random, unannounced inspections shall not be

1 used in any such inspection at a store in which such
2 individual is a regular customer.

3 '(4) If an individual under 18 years of age par-
4 ticipating in random, unannounced inspections is
5 questioned about such individual's age, such person
6 shall state such individual's actual age and shall
7 present a true and correct proof of age if requested
8 at any time during the inspection to present it.

9 '(c) PENALTY.—Any person who uses any person
10 under 18 years of age, other than as permitted by sub-
11 section (b), to test compliance with this Act, is liable for
12 a civil money penalty of \$150 for each violation.

13 '(d) USE OF PENALTY MONEY AND FEES.—Civil
14 money penalties collected for violations of this Act and
15 fees collected under section 10 may only be used to defray
16 the costs of administration and enforcement of this Act.

17 **SEC. 10. LICENSURE.**

18 '(a) IN GENERAL.—The State shall require that each
19 person engaged in the distribution of tobacco products
20 hold a license issued under this section. A separate license
21 shall be required for each place of business where tobacco
22 products are distributed at retail. A license issued under
23 this section is not assignable and is valid only for the per-
24 son in whose name it is issued and for the place of busi-
25 ness designated in the license.

1 ‘(b) FEE.—The annual license fee is \$25 for each
2 place of business where tobacco products are distributed
3 at retail.

4 ‘(c) APPLICATION.—Every application for a license,
5 including renewal of a license, under this section shall be
6 made upon a form provided by the State and shall set
7 forth the name under which the applicant transacts or in-
8 tends to transact business, the location of the place of
9 business for which the license is to be issued, the street
10 address to which all notices relevant to the license are to
11 be sent (in this Act referred to as ‘notice address’), and
12 any other identifying information that the State may re-
13 quire.

14 ‘(d) ACTION ON LICENSE.—The State shall issue or
15 renew a license or deny an application for a license or the
16 renewal of a license within 30 days of receiving a properly
17 completed application and the license fee. The State shall
18 provide notice to an applicant of action on an application
19 denying the issuance of a license or refusing to renew a
20 license.

21 ‘(e) SCOPE AND RENEWAL.—Every license issued by
22 the State shall be valid for 1 year from the date of issu-
23 ance and shall be renewed upon application except as oth-
24 erwise provided in this Act.

1 ‘(f) CHANGE OF ADDRESS.—Upon notification of a
2 change of address for a place of business for which a li-
3 cense has been issued, a license shall be reissued for the
4 new address without the filing of a new application.

5 ‘(g) NOTICE.—The State shall notify every person in
6 the State who is engaged in the distribution at retail of
7 tobacco products of the license requirement of this section
8 and of the date by which such person should have obtained
9 a license.

10 ‘(h) PENALTY.—

11 ‘(1) IN GENERAL.—Any person who engages in
12 the distribution at retail of tobacco products without
13 a license required by this section is liable for a civil
14 money penalty in an amount equal to two times the
15 applicable license fee and \$50 for each day on which
16 such distribution continues without a license.

17 ‘(2) SUSPENSION OR REVOCATION.—Any person
18 who engages in the distribution at retail of tobacco
19 products after a license issued under this section has
20 been suspended or revoked is liable for a civil money
21 penalty of \$100 per day for each day on which such
22 distribution continues after the date such person re-
23 ceived notice of such suspension or revocation.

24 ‘(i) TERM.—The term of a license shall be 1 year.

1 ‘(j) EFFECTIVE DATE.—No person shall engage in
2 the distribution at retail of tobacco products on or after
3 180 days after the date of enactment of this Act unless
4 the person is authorized to do so by a license issued pursu-
5 ant to this section or is an employee or agent of a person
6 who has been issued such a license.

7 **‘SEC. 11. SUSPENSION, REVOCATION, DENIAL, AND NON-**
8 **RENEWAL OF LICENSES.**

9 ‘(a) NOTICE.—Upon a finding that a licensee has
10 been determined by a court of competent jurisdiction to
11 have violated this Act during the license term, the State
12 shall notify the licensee in writing, served personally or
13 by registered mail at the notice address, that any subse-
14 quent violation of this Act at the same place of business
15 may result in an administrative action to suspend the li-
16 cense for a period determined by the State.

17 ‘(b) SUSPENSION.—Upon finding that a further vio-
18 lation by the licensee has occurred involving the same
19 place of business for which the license was issued and the
20 licensee has been provided notice under subsection (a), the
21 State may initiate an administrative action to suspend the
22 license for a period to be determined by the State. If an
23 administrative action to suspend a license is initiated, the
24 State shall immediately notify the licensee in writing at
25 the notice address of the initiation of the action and the

1 reasons therefor and permit the licensee an opportunity,
2 at least 30 days after written notice is served personally
3 or by registered mail upon the licensee, to show why sus-
4 pension of the license would be unwarranted or unjust.

5 ‘(c) REVOCATION.—The State may initiate an admin-
6 istrative action to revoke a license that previously has been
7 suspended under subsection (b) if, during the one year pe-
8 riod in which the license was issued, a further violation
9 of this Act is committed, after the suspension, by the li-
10 censee involving the same place of business for which the
11 license was issued. If an administrative action to revoke
12 a license is initiated, the State shall immediately notify
13 the licensee in writing at the notice address of the initi-
14 ation of the action and the reasons therefor and permit
15 the licensee an opportunity, at least 30 days after written
16 notice is served personally or by registered mail upon the
17 licensee, to show why revocation of the license would be
18 unwarranted or unjust.

19 ‘(d) OTHER VIOLATIONS.—No action with respect to
20 any license at a place of business may be taken based on
21 a violation that occurred subsequent to the occurrence of
22 another violation unless such other violation is fully adju-
23 dicated at the time the subsequent violation occurred.

24 ‘(e) FEE.—A person whose license has been sus-
25 pended or revoked with respect to a place of business pur-

1 suant to this section shall pay the State a fee of \$50 for
2 the renewal or reissuance of the license at that same place
3 of business.

4 '(f) EFFECT ON APPLICATION FOR NEW LICENSE.—
5 Revocation of a license under subsection (c) with respect
6 to a place of business shall not be grounds to deny an
7 application by that person for a new license with respect
8 to that place of business for more than 12 months subse-
9 quent to the date of such revocation. Revocation or sus-
10 pension of a license with respect to a particular place of
11 business shall not be the grounds to deny an application
12 for a new license, to refuse to renew a license, or to revoke
13 or suspend an existing license at another place of business.

14 '(g) JUDICIAL REVIEW.—A licensee may seek judicial
15 review of an action of the State suspending, revoking, de-
16 nying, or refusing to renew a license under this section
17 by filing a complaint in a court of competent jurisdiction.
18 A complaint shall be filed within 30 days after the date
19 on which notice of the action is received by the licensee.
20 The court shall review the evidence de novo.

21 '(h) REPORT.—The State shall not report any action
22 suspending, revoking, denying, or refusing to renew a li-
23 cense under this section to the Secretary of Health and
24 Human Services, unless judicial review, if any, of the ac-
25 tion has been completed.

1 **'SEC. 12. PREEMPTION.**

2 'No county, city, town, other political subdivision of
3 this State or agency of a political subdivision of this State
4 may enact or enforce any law, ordinance, or rule concern-
5 ing the distribution, display, use, or advertising or pro-
6 motion of tobacco products unless the requirements of
7 such law, ordinance, or rule are not inconsistent with the
8 requirements of this Act.

9 **'SEC. 13. SEVERABILITY.**

10 'If any provision of this Act or its application to any
11 person or circumstance is held invalid, such holding shall
12 not affect other provisions or applications of this Act that
13 can be given effect without the invalid application.

14 **'SEC. 14. NO PRIVATE RIGHT OF ACTION.**

15 'Nothing in this Act shall be construed to create a
16 right of action by any private person for any violation of
17 any provision of this Act.

18 **'SEC. 15. JURISDICTION AND VENUE.**

19 'Any action alleging a violation of this Act may only
20 be brought in a court of general jurisdiction in the city
21 or county where the violation is alleged to have occurred.

22 **'SEC. 16. REPORT.**

23 'The State shall prepare for submission annually to
24 the Secretary of Health and Human Services the report
25 required by section 1926 of the Public Health Service Act
26 (42 U.S.C. 300x-26) and otherwise shall be responsible

1 for the State's reporting of compliance with that section
2 and any implementing regulations promulgated by the
3 Secretary.

4 **'SEC. 17. DEFINITIONS.**

5 'For purposes of this Act:

6 '(1) PACKAGE.—The term "package" means a
7 pack, box, carton, pouch, or container of any kind
8 in which cigarettes or smokeless tobacco products
9 are offered for sale, sold, or otherwise distributed to
10 consumers.

11 '(2) PROOF OF AGE.—The term "proof of age"
12 means a driver's license or other form of identifica-
13 tion issued by a governmental authority or other
14 identification that includes a photograph and the
15 date of birth of the individual.

16 '(3) SAMPLE.—The term "sample" means a to-
17 bacco product distributed to members of the public
18 at no cost for the purpose of promoting the product,
19 but excludes tobacco products distributed—

20 '(A) in conjunction with the sale of other
21 tobacco products,

22 '(B) to consumer or market research pan-
23 els,

24 '(C) to persons employed in the trade, or

1 ‘(D) to customers or consumers, in re-
2 sponse to customer or consumer complaints.

3 ‘(4) TOBACCO PRODUCT.—The term “tobacco
4 product” means—

5 ‘(A) “tobacco products” as defined in sec-
6 tion 5702 of the Internal Revenue Code of
7 1986, or

8 ‘(B) any other product containing tobacco
9 as a principal ingredient which, because of its
10 appearance, type, or tobacco used in the prod-
11 uct, or its packaging and labeling, is likely to
12 be offered to, or purchased by, consumers as a
13 tobacco product as described in subparagraph
14 (A).

15 ‘(5) UNDER THE CONTROL.—The term “under
16 the control” means within the reach of the cashier
17 or protected by other security, surveillance, or detec-
18 tion methods, including electronic scanners.

19 ‘(6) VENDING MACHINE.—The term “vending
20 machine” means any mechanical, electric, or elec-
21 tronic self-service device which, upon insertion of
22 money, tokens, or any other form of payment, auto-
23 matically dispenses tobacco products.

24 ‘(7) WITHIN THE LINE OF SIGHT.—The term
25 “within the line of sight” means visible to a cashier

1 or other employee, whether directly or by means of
2 mirrors or monitors.’.

3 “(2) DELAYED APPLICABILITY FOR CERTAIN
4 STATES.—In the case of a State whose legislature
5 does not convene a regular session in fiscal year
6 1998, the requirement described in paragraph (1) as
7 a condition of avoiding a reduction in a grant under
8 section 1921 shall apply only for fiscal year 1999
9 and subsequent fiscal years.

10 “(b) ENFORCEMENT.—

11 “(1) IN GENERAL.—For the first applicable fis-
12 cal year and for each subsequent fiscal year, a fund-
13 ing agreement for a grant under section 1921 of the
14 Public Health Service Act is a funding agreement
15 under which the State involved will—

16 “(A) enforce the law described in sub-
17 section (a)(1) systematically and conscientiously
18 and in a manner that can reasonably be ex-
19 pected to reduce the extent to which tobacco
20 products are available to individuals under the
21 age of 18; and

22 “(B) certify that it requires such enforce-
23 ment of such law to be treated as a priority by
24 State and local law enforcement authorities.

1 “(2) ACTIVITIES AND REPORTS REGARDING EN-
2 FORCEMENT.—For the first applicable fiscal year
3 and for each subsequent fiscal year, a funding agree-
4 ment for a grant under section 1921 is a funding
5 agreement under which the State involved will—

6 “(A) conduct random, unannounced in-
7 spections to ensure compliance with the law de-
8 scribed in subsection (a)(1); and

9 “(B) annually submit to the Secretary a
10 report describing—

11 “(i) the activities carried out by the
12 State to enforce such law during the fiscal
13 year preceding the fiscal year for which the
14 State is seeking the grant;

15 “(ii) the steps taken by the State to
16 ensure that enforcement of such law was
17 treated as a priority by State and local law
18 enforcement authorities;

19 “(iii) the extent of success the State
20 has achieved in reducing the availability of
21 tobacco products to individuals under the
22 age of 18, including the results of the in-
23 spections conducted under subparagraph
24 (A); and

1 “(iv) the strategies to be utilized by
2 the State for enforcing such law during the
3 fiscal year for which the grant is sought.

4 “(c) FUNDING.—The law specified in subsection
5 (a)(1) may be administered and enforced by a State
6 using—

7 “(1) any amounts made available to the State
8 through a grant under section 1921;

9 “(2) any amounts made available to the State
10 under section 1901 (42 U.S.C. 300w);

11 “(3) any fees collected for licenses issued pursu-
12 ant to the law described in subsection (a)(1);

13 “(4) any fines or penalties assessed for viola-
14 tions of the law specified in subsection (a)(1); or

15 “(5) any other funding source that the legisla-
16 ture of the State may prescribe by statute.

17 “(d) NONCOMPLIANCE OF STATE.—Before making a
18 grant under section 1921 to a State for the first applicable
19 fiscal year or any subsequent fiscal year, the Secretary
20 shall make a determination whether the State has main-
21 tained compliance with subsections (a) and (b). If, after
22 notice to the State and an opportunity for a hearing, the
23 Secretary determines that the State is not in compliance
24 with such subsections, the Secretary shall reduce the

1 amount of the allotment under such section for the State
2 for the fiscal year involved by an amount equal to—

3 “(1) in the case of the first applicable fiscal
4 year, 10 percent of the amount determined under
5 section 1933 for the State for the fiscal year;

6 “(2) in the case of the first fiscal year following
7 such applicable fiscal year, 20 percent of the amount
8 determined under section 1933 for the State for the
9 fiscal year;

10 “(3) in the case of the second such fiscal year,
11 30 percent of the amount determined under section
12 1933 for the State for the fiscal year; and

13 “(4) in the case of the third such fiscal year or
14 any subsequent fiscal year, 40 percent of the amount
15 determined under section 1933 for the State for the
16 fiscal year.

17 “(c) DEFINITION.—For purposes of this section, the
18 term ‘first applicable fiscal year’ means—

19 “(1) fiscal year 1999, in the case of any State
20 described in subsection (a)(2); and

21 “(2) fiscal year 1998, in the case of any other
22 State.

23 “(f) APPLICATION.—For purposes of this section, ref-
24 erences to section 1921 shall include any successor grant
25 programs.”.

1 **SEC. 3. SALES BY INTERNET.**

2 No person may sell or otherwise distribute a tobacco
3 product to an individual under the age of 18 through the
4 internet. A person who violates this section shall be liable
5 for a civil money penalty of \$150.

6 **SEC. 4. EFFECTIVE DATE.**

7 This Act and the amendments made by this Act shall
8 take effect 180 days after the date of the enactment of
9 this Act.

○

Section -By-Section Analysis

H.R. 2034

The Tobacco Use by Minors Deterrence Act

AMENDMENT TO SECTION 1926 OF THE PUBLIC HEALTH SERVICE ACT

The legislation dovetails with and expands upon on what is popularly known as the "the Synar amendment" to the ADAMHA Reorganization Act of 1992 (relating to the sale or distribution of tobacco products to individuals under the age of 18), P.L. No. 102-321 Stat. 394 (1992). The Department of Health and Human Service issued proposed regulations to implement this legislation on August 26, 1993 and final regulations on February 19, 1996. The Substance Abuse and Mental Health Administration currently oversees and reports to Congress on this regulation.

The regulation promulgated to implement this legislation requires states (1) have in effect a state law prohibiting the sale and distribution of tobacco products to minors; (2) enforce such laws; (3) conduct annually, random, unannounced inspections of tobacco outlets; (4) negotiate a strategy and timeframe for achieving an inspection failure rate of no more than 20 percent; (5) identify a State agency responsible for enforcing the State law on tobacco sales/distribution. Reports are submitted annually to the Department of Health and Human Services. States that fail to comply with the enforcement requirements will be penalized 10 percent of their grant in the first applicable year, 20 percent in the second, 30 percent in the third, and 40 percent in the fourth, and thereafter.

PROHIBITION ON DISTRIBUTION TO MINORS

Prohibits distribution of tobacco products (including cigars and pipe tobacco) to anyone under 18 years of age. Prohibits an individual of legal age to purchase tobacco products with the intent of providing it to a minor. Retailer and employee penalties for violation include civil fines of \$25 for the first violation; \$50 for the second violation; \$150 for third and subsequent violations. In addition, employers of a retail establishment are fined \$150 if the same employee has sold a tobacco product to a minor more than once.

- An employee has a defense if he or she relied upon proof of age that appeared to be valid and if unannounced inspections are not conducted in accordance with the legislation; (a driver's license or another form of identification issued by a governmental authority that includes a photograph and date of birth will suffice)
- An employer has a defense if it can prove that it has trained its employees regarding the prohibition on sales to minors and the employee has acknowledged that he or she understands the law.

PURCHASE, RECEIPT, OR POSSESSION BY MINORS PROHIBITED

Prohibits a minor from purchasing, attempting to purchase, receiving or attempting to receive, possessing or attempting to possess, smoking or attempting to smoke or otherwise using or consuming or attempting to use or consume a tobacco product in a public place.

Penalties for a first violation include a civil money fine of between \$25 and \$150; community service; and suspension of the individual's driver's license. It is up to the discretion of the judge whether to impose all of these penalties. After the second violation, it is mandatory that a drivers license suspension be imposed for at least 30 days.

The law enforcement agency must notify the individual's parent, guardian, or custodian as to the nature of the violation within 48 hours. The notification can be made through any practicable means such as telephone, mail, or person-to-person. In addition, before an employee or owner can be prosecuted, law enforcement must also prosecute the minor.

LICENSURE

Any person engaged in the distribution at retail of tobacco products must apply and receive a license. A separate license is required for each place of business where tobacco products are sold to the public. A license fee of \$25 will be imposed for each license. The license is valid for 1 year from the date of issuance. Penalties for operating without a license will accrue at the amount of \$50 for each day. Any store that continues to sell tobacco products after the license has been suspended or revoked will be penalized at \$100 for each day after the store has received notice of suspension or revocation.

SUSPENSION, REVOCATION, DENIAL, AND NONRENEWAL OF LICENSES

Once a court has determined that a violation has occurred, the State shall notify the licensee in writing, that any subsequent violation at the same place of business may result in a suspension of the license for a period determined by the State.

- *Suspension of License:* If a further violation occurs at the same store, the State may initiate administrative action to suspend the license for a period to be determined by the State. Once the State notifies the licensee of the initiation of the suspension action, the licensee has 30 days to demonstrate why suspension of the license may be unwarranted or unjust.
- *Revocation of License:* The State may revoke the license that has been previously suspended during the one year period in which the license was issued if a further violation of the Act is committed involving the same store. The licensee, after being notified by the state, will have 30 days to demonstrate why revocations of the license would be unwarranted or unjust.
- *Fees:* When a license has been suspended or revoked, the licensee must pay the State \$50 for renewal or reissuance of the license at the same place of business.
- *New License Application:* Revocation or suspension of a license at one place a business shall not last longer than 12 months and may not be grounds to deny application at another place of business
- *Judicial Review:* A licensee has the option to seek judicial review of an action by the State to suspend, revoke, or deny a new license by filing a complaint in court with jurisdiction over the matter.

PREEMPTION

This Act would preclude a county, city, town, or other political subdivision of the State to enact separate measures that are inconsistent with this Act.

SALES BY THE INTERNET

Prohibits tobacco sales through the internet to minors.

USE OF PENALTY MONIES AND FEES

Civil money penalties for violations and license fees collected under this Act can only be used to defray the cost of administration and enforcement of the Act.

Side-By-Side Comparison

Tobacco Use By Minors Deterrence Act	FDA Regulations	Tobacco Industry Settlement
Requires retailers to adopt self-funding state licensing	Does not address	Requires retailers to adopt federal licensing funded by tobacco companies
Fines retailers for selling tobacco to minors	Does not address	Fines and suspends or revokes licenses for retailers selling tobacco to minors
Subjects minors caught buying or using tobacco to meaningful punishments	Does not address	Does not address
Contacts parents if minors caught with tobacco	Does not address	Does not address
Requires retail employee training	Does not address	Does not address
Provides local and state law enforcement authority to apply civil penalties	Does not address	Does not address
Controls sales of cigars and pipe tobacco to minors	Does not address	Does not address
Bans sale or distribution of tobacco to minors	Bans sale to minors and completely bans distribution of free samples	Adopts FDA regulations
Restricts all self-serve tobacco displays	Bans self-serve displays where minors permitted	Adopts FDA regulations
Requires retailers to check ID of all vending machine customers	Bans vending machines where minors permitted	Adopts FDA regulations
Requires verification of ID in accordance with applicable state law	Requires verification of ID for all customers under 27	Adopts FDA regulations

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ORGANIZATIONS SUPPORTING H.R. 2034

- **National Fraternal Order of Police**
- **National Association of Police Organizations**
- **Law Enforcement Alliance of America**
- **National Association of Convenience Stores**
- **Society of Independent Gasoline Marketers of America**
- **Amusement and Music Operators Association**
- **General Conference of Seventh Day Adventists**

DEPARTMENT OF COMMERCE
OF THE
UNITED STATES OF AMERICA

R. BRUCE JOSTEN
SENIOR VICE PRESIDENT
MEMBERSHIP POLICY GROUP

June 10, 1997

1615 H STREET, N.W.
WASHINGTON, D.C. 20062-2000
202/463-3310 202/887-3403 FAX

The Honorable Sanford Bishop
United States House of Representatives
Washington, D.C. 20515

Dear Representative Bishop:

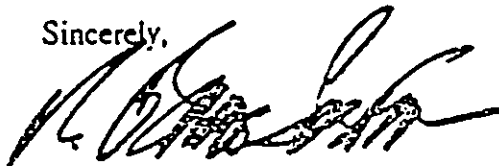
I would like to congratulate you on your leadership to provide a legislative solution to deter tobacco use by minors. Given the adverse ramifications of tobacco usage by minors for various industries and sectors of our country, there could be no more critical time to directly address this problem.

Your legislation appears to be more than willing to meet this charge because it recognizes clearly that any solution must be a collaborative one, involving retailers, law enforcement officials, and families and kids. This aggressive, targeted enforcement approach could make the difference in enhancing the quality of life for today's minors and future generations.

As reflected throughout our nation's history, the best solutions to the most challenging problems have come by way of a hands-on approach. In this case, the people who can make the greatest impact, communities, neighborhoods, and families, are given the tools necessary to combat an issue that has serious implications for the youth of our country and on our nation's health care system.

I wish you the best of luck in your efforts to advance this important piece of legislation.

Sincerely,



R. Bruce Josten

the Institute for Youth Development

August 28, 1997

The Honorable Sanford Bishop
United States House of Representatives
Washington, DC 20515

Dear Congressman Bishop,

I am writing today to commend your leadership in bringing forth the legislation, "Tobacco Use by Minors Deterrence Act of 1997," which offers solutions to the use of tobacco by minors. The Institute for Youth Development would like to congratulate you on your efforts.

Our nation needs a plan that will make a difference in enhancing the quality of life for today's youth and future generations. Your initiative does so by emphasizing the shared responsibility of communities and families to work together to find a long-term solution to the problem of underage tobacco use.

Your legislation provides many necessary tools to those who could make the greatest impact in our ongoing battle with teens and tobacco: retailers, law enforcement officials, and families. The bill not only levies fines on the retailers, but also places responsibility on our youth by instituting civil penalties, such as revoked drivers' licenses and community service.

Also, the bill will make underage tobacco users accountable by requiring parental and/or guardian notification of those youths caught using, purchasing, or in possession of tobacco. Finally, the legislation provides for community involvement by proposing incentives for states to establish stricter laws. Through these and other components, the "Tobacco Use by Minors Deterrence Act" offers solutions to an issue that has serious implications for our nation's youth.

Thank you for your leadership.

Sincerely,



Shepherd Smith
President



GEORGIA FRATERNAL ORDER OF POLICE

2860 East Point Street, Suite 225

P. O. Box 9122

East Point, Georgia 30344

FAX 404-767-9017

Ph 404-767-3311
1-800-305-0237

August 19, 1997

The Honorable Sanford Bishop
United States House of Representatives
Washington, D.C. 20515

Dear Representative Bishop:

The Georgia Fraternal Order of Police commends you on your recently proposed legislation, the Tobacco Use by Minors Deterrence Act, H.R. 2034. We congratulate you on your efforts to deter tobacco use by minors.

Given the rapidly growing numbers of minors using tobacco, it is time to address the problem of kids buying and using tobacco. And our membership knows from experience that any attempt to stop an issue involving minors and substances prohibited to them must involve everyone; law enforcement officers, local businesses, families, and kids. By asking for the commitment of the entire community, we believe you are offering a solution that could actually put a stop to underage tobacco use. We commend you on your leadership and concern for the welfare and health of our nation's youth.

The law enforcement officers of this state realize that our communities must work as teams to defeat underage tobacco use. We believe your legislation will provide our officers with the necessary tools to do our part in this battle. We wish you success in your endeavor. If the Georgia Fraternal Order of Police may be of assistance, please feel free to call on us.

Sincerely,

A handwritten signature in black ink that reads "Ricky H. Rich".

Ricky Rich
President

RR/bw

Bishop proposes

WASHINGTON (AP)—A Georgia congressman with extensive tobacco interests in his district proposed legislation Thursday to curb teen-age smoking through licensing of retail stores and penalties on both youthful offenders and businesses that sell them tobacco products.

Rep. Sanford Bishop, an Albany Democrat whose district includes Moultrie, said the legislation aims to deny teen-agers access to tobacco by helping local communities, businesses, parents and teens themselves present a united front against tobacco use.

"This bill is not designed to outlaw tobacco," said Bishop, whose south Georgia district encompasses all aspects of the tobacco industry, from growers to warehouses to a cigarette manufacturing plant.

"It's designed to limit access to tobacco by kids," he said.

Bishop said the legislation, developed with the cooperation of retailers, will be introduced in the next several days. Sen. Gordon Smith, R-Ore., is the sponsor of the Senate version of the bill.

A key feature of the measure is the creation of a state retail license to sell tobacco products, similar to the licenses businesses now must obtain to sell alcoholic beverages. States that did not adopt the model licensing law would lose federal public health funding.

Under the model law, Bishop said retailers would be required to obtain a license, pay fines of \$25 to \$150 for illegal sales of tobacco products to minors, train employees on tobacco laws, restrict access to tobacco displays, and electronically lockout

tobacco access bill

minors from tobacco vending machines.

The bill also would levy fines of \$25 to \$150 on teen-agers who illegally purchase cigarettes, and take away their driver's licenses after repeat offenses. It also would require that their parents be notified.

Bishop said money from the license sales and fines would be used exclusively to enforce the bill's prohibitions on underage smoking, including such police tactics as unannounced retail inspections and sting operations using minors.

Smith, a freshman, said the proposed legislation would "make it more difficult for retailers to profit from the illegal sale of tobacco to teens" and would "change the psychology" of smoking by licensing sales.

Smith and Bishop said their bill represents a more comprehensive approach to the problem of underage tobacco use than does a similar campaign by the Food and Drug Administration.

The FDA has proposed regulations that would ban the sale of

tobacco products to minors and prohibit self-serve tobacco displays and tobacco vending machines in establishments where minors are permitted. They also would require identification verification of all customers under 27 who seek to buy tobacco.

The legislation proposed by Smith and Bishop would permit vending machines in retail establishments, but would require the machines be electronically locked so purchases could not be made until the proprietor verified the customer's age.