



AGENDA ITEM: 10
DATE OF MEETING: October 23, 2014
ACTION: _____
INFORMATION: X

ALTERNATIVE SOURCES FOR ADDITIONAL REVENUE

SUMMARY

Since Proposition 10 passed in 1998, California has seen a steady decrease in tobacco use, resulting in a corresponding downturn in revenue for First 5 California (F5CA). In fact, revenue has decreased an average of 3.1 percent per year over the last 14 years. First 5 counties have also experienced decreases in revenue.

In the spirit of long-term sustainability, the Commission requested staff to explore alternative sources for additional revenue to counteract this reduction. While many revenue-generating activities can be identified, staff outlines the following options that may be feasible in the next few years. Staff would invite any other ideas not identified here that would lead to increasing the revenue stream for F5CA.

It should be noted that any effort by F5CA to secure alternative sources for revenue would have the added value of benefiting First 5 counties, which are also reviewing options to restore declining revenue. F5CA will work with First 5 counties to coordinate any efforts to increase revenue.

OPTIONS

1. E-Cigarette Tax

E-cigarettes are made up of a heating element, a battery, a cartridge, and an atomizer, and can simulate the look of a cigarette. The cartridge contains liquid that forms an aerosol when heated. The aerosol is inhaled and drawn into the lungs.

E-cigarette aerosol contains nicotine, toxins and particles, some of which appear on California's Proposition 65 list of harmful chemicals. According to the California Department of Public Health (CDPH), people exposed to secondhand aerosol absorb nicotine at comparable levels to secondhand smoke from cigarettes. The secondhand aerosol contains ultrafine particles that may cause cancer and birth defects. In addition to the secondhand smoke effects, the California Poison Control System has reported a ten-fold increase in calls for children under 5 years of age from 2012 to 2013 due to e-cigarette poisoning.

E-cigarette usage in California has increased at a staggeringly rapid pace. CDPH reports E-cigarette use by young adults (18-29) has tripled in one year, and young adults are three times more likely to use e-cigarettes than adults 30 years and older. Nearly 20 percent of young adult e-cigarette users have never smoked cigarettes. For students in grades 6-12, a national polls shows that use of e-cigarettes have more than doubled from 2010 to 2011.

Further, CDPH reports no scientific evidence exists to show e-cigarettes help smokers quit smoking or reduce consumption. In fact, one study shows 89 percent of e-cigarette users are still using them after one year.

In three years, national spending on e-cigarette advertising has increased by 1,200 percent, topping \$80,000,000 in 2013, and is clearly targeting a younger market. E-cigarettes are being offered in flavors such as gummy bear, cotton candy, and vanilla cupcake. Provocative advertising campaigns are aimed to attract young users.

To date, only two states (Minnesota and North Carolina) tax e-cigarettes. The federal Food and Drug Administration is in the process of reviewing potential rules and restrictions on e-cigarettes. On August 8, 2014, CDPH filed comment on these proposed rules. Other states have either attempted to tax e-cigarettes, or are in the process of drafting legislation to address the issue.

The California Children and Families Act (the Act) currently defines taxable "tobacco products" as products containing at least 50 percent tobacco. Under this definition, F5CA cannot tax e-cigarettes. In order to impose a tax similar to the one imposed in Minnesota and North Carolina, Proposition 10 would need to be statutorily amended to define tobacco products as "products that use nicotine," or something to that effect.

CDPH also taxes tobacco products, using the same "50 percent tobacco" definition; any attempt to seek a legislative remedy should include partnering with CDPH.

2. Inclusion of F5CA in Any Initiative that Attempts to Legalize Recreational Marijuana Use

California has the distinction of being the first state to place a marijuana legalization measure on the ballot (in 1972). Although it did not pass, it opened the door to a series of efforts to legalize marijuana use. Since 1972, statewide ballots in 14 states have featured a total of 44 ballot measures related to marijuana. These ballot measures have played a major role in the increasing liberalization of statewide marijuana laws.

As of August 2014, medical marijuana is legal in 23 states and the District of Columbia, while four marijuana measures are certified for the November 2014 ballot, and one other marijuana-related measure is currently in circulation. Of the 23 states permitting medical marijuana, 11 states have achieved legalization via statewide ballot measure (including California) and 12 states have seen the state legislature

approve medical marijuana. In May 2014, the U.S. Congress voted to halt federal prosecutions of medical marijuana users in states that have legalized the drug's use with a doctor's prescription.

In 2012, Colorado and Washington became the first states to legalize commercial sale of marijuana to all adults over 21. Voters in Oregon, Alaska and the District of Columbia will weigh in on marijuana legalization in November. Both Colorado and Washington's initiatives include the imposition of excise taxes, but neither include funding to go to early childhood development. Instead, the tax revenue is dedicated to school districts, substance abuse treatment, school construction, deterrence efforts, research, and health care. Washington estimates tax revenue for 2014 to be between \$200-\$400 million, while Colorado expects to bring in an estimated \$98 million in revenue this year.

The first year in which a majority of Americans reported favoring legalized marijuana was 2013. In 2014, 73 percent of Americans report being in favor of medical marijuana, while 53 percent support decriminalizing marijuana possession. In a 2014 survey of likely voters, 40 percent of respondents said they would be "much more likely" to vote if marijuana legalization issues were on the ballot. An additional 30 percent said marijuana ballot initiatives would make them "somewhat" more likely to vote. Likewise, public commentary in support of legalization has been robust. For example, on July 27, 2014, the New York Times Editorial Board endorsed ending the national prohibition on marijuana, and on August 11, 2014, California Lieutenant Governor Gavin Newsom publically stated that he would back an appropriate initiative that would legalize recreational marijuana use.

In the last year, two California initiatives were circulated to legalize recreational marijuana use, but neither generated sufficient signatures to qualify for the ballot. While the initiatives would have authorized the imposition of an excise tax, neither earmarked F5CA as a recipient of the tax. Instead, the initiatives listed public education, health care, fire services, drug abuse treatment, and law enforcement as recipients. To advocate for the inclusion of F5CA funding in any initiative, First 5 staff would need to work with supporters and authors of future initiatives to include early childhood funding. Strategists identify 2016 as the best year for success for a California marijuana initiative, since it is a presidential election year and turnout likely will be greater than for a non-presidential election year.

3. Cigarette Tax Increase for Early Childhood Education

California's tax on cigarettes total \$.87 per pack. Other than the \$.50 per pack tax defined by Proposition 10, current tobacco revenue is divided between the state General Fund (\$.10) and two special funds: 1) the Proposition 99 tax (\$.25), which support programs including health education, research into tobacco-related diseases, indigent health care, rural health services, and resource and environmental programs, and 2) the legislatively established breast cancer research and early detection tax (\$.02).

Comparing California's cigarette tax to other states/territories' tax is noteworthy. Only 18 states have a lower cigarette tax rate than California, including Alabama (\$.425 per pack), Georgia (\$.37), Louisiana (\$.36), and Virginia (\$.30).

By contrast, all 6 American territories and 16 states have at least double the level of California's cigarette tax. Some states, including New York (\$4.35 per pack), Massachusetts (\$3.51), Rhode Island (\$3.50), Connecticut (\$3.40), Hawaii (\$3.20), and Washington (\$3.00) tax cigarettes at a substantially higher rate than California.

To increase the cigarette excise tax would require legislation to amend the Act.

4. Specialized License Plates

Specialized California automobile license plates serve as a revenue source for a number of groups, including California firefighters, the Lake Tahoe Conservancy, Veterans and the Yosemite Conservancy. A specialty license plate currently exists that benefits the Child Health and Safety Fund, which California incorporates the symbol of a child's handprint, heart, star, or plus sign on its plate. This fund receives approximately \$4.1 million annually from license plate revenue, which is provided to the California Departments of Social Services and Public Health for programs that keep California children safe, including child care safety, child abuse prevention, and efforts to prevent childhood injuries. This license plate is the most successful of the specialized plates; revenue derived from other plates has been as low as \$38,000 per year per fund.

The authority for a specialized license plate begins with legislative action. The process requires state agencies to send an application to the Department of Motor Vehicles (DMV) to sponsor a specialized license plate program, along with 7,500 pre-paid applications for the agency's specialized license plates. The DMV reviews and approves applications, sets an annual fee for the program, and administers the process.

5. Voluntary Contributions on Income Tax Returns

State income tax returns provide an opportunity to voluntarily contribute to various funds, including such diverse causes as cancer research, animal shelters, sea otters, and senior citizens. Currently, three funds are child-related: school supplies for homeless children, child victims of human trafficking, and a children's trust for the prevention of child abuse.

Like the specialized license plate program, legislation is required to add language to the Revenue and Taxation Code that would allow First 5 California to take advantage of this revenue option. Currently, yearly revenue totals generated by the twenty funds soliciting voluntary contributions range from \$55,505 to \$476,933 per year.

6. Requesting Donations in F5CA Advertisements

At its April 2014 meeting, the Commission suggested the option of placing a request for donations at the end of the advertisements run by F5CA. While this option is permitted under the Act, staff is concerned with possible public perception associated with this approach.

One of F5CA's primary responsibilities is to provide for statewide dissemination of public information to members of the general public for the purpose of developing appropriate awareness and knowledge regarding early childhood development. In fact, First 5's largest allocation is to the Mass Media Communications Account for this purpose.

By placing a request for donation at the end of a F5CA advertisement, staff is concerned that the public may perceive the ad as being run for the purpose of fund-raising as opposed to its intended purpose of public awareness around early childhood development. Further, the message of the ad may be lost or diluted by the request for donations. Finally, the potential for negative publicity may be generated as a result of donation requests.

7. Applying for Federal, State and Philanthropic Grants

While First 5 has funded and co-funded various programs, projects and activities, opportunities may exist whereby F5CA could itself apply for grants from public and private partners to support its mission. F5CA is committed to continue to look for opportunities to secure grant funding in the private and public sectors. However, the downside of this option is grant funding is usually a one-time award, thus defeating the intent to identify sustainable, long-term revenue that would backfill lost taxes as a result of the decrease in smoking.

STAFF RECOMMENDATION

While all of the options create an opportunity to increase F5CA revenue, the Commission should focus on options that create sustainable, measurable funding opportunities, not only for F5CA, but for the First 5 counties as well. Of the listed options, taxation of e-cigarettes and F5CA inclusion in any marijuana initiatives appear to provide the significant, sustainable funding that would infuse long-term resources into First 5's declining revenue stream. Likewise, depending on the amount, an increase of the \$.87 per pack excise tax for cigarettes could substantially augment F5 revenue.

Obviously, each of these options would face resistance, and substantial groundwork would need to occur to successfully implement one or more of these proposals. Further, since Proposition 10 was passed as a state initiative, any statutory amendment to the Act would require a two-thirds vote of the Legislature.

While not as controversial, the other options may be less attractive for different reasons. The specialized license plates and the voluntary contribution on the tax returns currently have children programs receiving revenue, and F5CA's inclusion may create friction with those children programs. Further, the revenue associated with these efforts would likely not be substantial, and may not be sustainable. Due to the public perception concern, asking for donations through our media efforts may result in our message being lost or misperceived.

Finally, F5CA will continue to seek grants that will complement our mission, but due to their one-time nature, grants do not serve as a sustainable, long-term funding mechanism. Likewise, we will continue to explore additional ideas for long term financing.