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STATE OF MICHIGAN
DEPARTMENT OF TREASURY
LANSING

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**NOTICE TO CIGARETTE STAMPING AGENTS
CONCERNING MICHIGAN'S IMPLEMENTATION OF
DIGITAL CIGARETTE TAX STAMPS**

February 21, 2014

OVERVIEW

This Notice applies to every licensed wholesaler and unclassified acquirer that is authorized by the Department to be a stamping agent under the Tobacco Products Tax Act ("TPTA") and in accordance with 1998 MR 3, R 205.454 ("Stamping Agent").

To implement 2012 PA 188, the State of Michigan is transitioning from heat-applied cigarette tax stamps to digital, pressure applied, cigarette tax stamps ("Digital Stamps"). Because the use of Digital Stamps will involve new technologies, processes and significant changes to the cigarette tax stamping requirements in Michigan, the Department will be implementing this transition through a phased-in rollout to Stamping Agents.

This means that the Department will select Stamping Agents to be transitioned to the use of Digital Stamps throughout 2014 and complete the rollout to all Stamping Agents by December 31, 2014. The Department will select a Stamping Agent for transition to the use of Digital Stamps based on several factors including the Stamping Agent's acquisition of its digital cigarette tax stamp machine ("Digital Stamping Machine") and successful completion of testing for its Digital Stamping Machine(s). The Department, primarily through Xerox State & Local Solutions, Inc., will assist Stamping Agents in this transition process.

As part of the transition process, the Department will establish a date by which the selected Stamping Agent must begin affixing Digital Stamps to packages of cigarettes to be sold in Michigan ("Implementation Date").

The Implementation Date is the triggering event by which a qualifying Stamping Agent may begin claiming reimbursement for the initial purchase of its Digital Stamping Machine(s) and for claiming "compensation" in the form of credits against its monthly tobacco tax liability for its costs for certain upgrades to technology and equipment necessary to affix Digital Stamps. These reimbursement and "compensation" opportunities for Stamping Agents are set forth under MCL 205.427(3)(d)-(e) and are summarized below.

REIMBURSEMENT FOR DIGITAL STAMPING MACHINE PURCHASE

As authorized by MCL 205.427(3)(e), Stamping Agents may claim monthly reimbursement for their direct costs actually incurred for the *initial* purchase of Digital Stamping Machines (that qualify as "eligible equipment" under MCL 205.427(13)) in an amount equal to 5.55% of the

total net purchase price. Reimbursement under this provision includes any sales or use tax due on the purchase, but excludes any shipping, installation and ongoing maintenance costs. For purposes of implementing this provision, reimbursement will be based upon Digital Stamping Machine configured as follows:

- Basic digital stamping machine
- TaxRight system for MSA verification
- Lake camera system

Note: The maximum amount of reimbursement which may be claimed for each Digital Stamping Machine qualifying as “eligible equipment” is \$169,749.00 plus any sales or use tax applicable to the purchase of that machine.

A Stamping Agent may be reimbursed for any number of Digital Stamping Machines purchased that qualify as “eligible equipment” up to the number of that Stamping Agent’s “existing equipment” as certified by the Stamping Agent on a form to be prescribed by the Department.

ELIGIBLE EQUIPMENT means a cigarette tax stamping machine that meets all of the following conditions:

- (i) Was purchased by a Stamping Agent who was licensed as a Stamping Agent as of December 31, 2011.
- (ii) Enables the Stamping Agent to affix Digital Stamps to individual packages of cigarettes in accordance with MCL 205.426a(2).
- (iii) Was purchased to be used for the primary purpose of permitting the Stamping Agent to affix Digital Stamps to individual packages of cigarettes to be sold in Michigan following the implementation of the use of Digital Stamps.

EXISTING EQUIPMENT means a cigarette tax stamping machine that meets all of the following conditions:

- (i) Was owned by a person who was licensed as a Stamping Agent as of December 31, 2011.
- (ii) Was a cigarette tax stamping machine used prior to January 1, 2012 by the Stamping Agent to apply stamps using stamp rolls of 30,000 stamps.

Note: For purposes of the TPTA, a “stamp” refers to the cigarette tobacco tax stamp authorized by the Department to be affixed to packages of cigarettes to be sold and/or consumed in Michigan to indicate that the tax imposed by the TPTA has been paid.

Reimbursement is to be claimed by the Stamping Agent as a monthly credit on its monthly tobacco tax return filed in the calendar month immediately following that Stamping Agent’s Implementation Date (and for the next succeeding 17 months) in order to receive the full amount of reimbursement authorized by the statute. If the amount of tax due on the Stamping Agent’s monthly tobacco tax return is less than the amount of this credit, the Stamping Agent will be eligible for a credit carryforward or refund of the difference.

Example: Stamping Agent ABC purchases an eligible Digital Stamping Machine on April 1, 2014 with a net purchase price of \$168,000 (including sales tax). The Implementation Date for Stamping Agent ABC is May 1, 2014. Stamping Agent ABC is eligible to claim a monthly credit equal to 5.55% of the net purchase price (e.g., \$9,324) beginning with its TPTA tax return

due June 20, 2014 (i.e., reporting its May 2014 TPTA tax) and for the next 17 (consecutive) monthly TPTA tax returns.

COMPENSATION FOR UPGRADES TO EQUIPMENT AND TECHNOLOGY

Under MCL 205.427(3)(d), a Stamping Agent may receive “compensation” in the form of an offset (e.g., credit) to its monthly tobacco tax liability for its direct costs actually incurred for “upgrades” to technology and equipment (excluding the Digital Stamping Machine reimbursed under MCL 205.427(3)(e)) that are “necessary to affix” Digital Stamps. The monthly compensation amount is limited to 0.5% of the total amount of TPTA tax due on cigarettes sold by the Stamping Agent for the month being reported. This includes cigarettes sold untaxed to Indian tribes which are treated as taxable sales for purposes of claiming this compensation.

The Department is currently reviewing equipment and technology upgrades that may be eligible for the 0.5% compensation and will provide guidance as soon as a determination is finalized. In addition, as Stamping Agents request reimbursement for additional upgrades, the Department will review those as well. The Department may require Stamping Agents to submit supporting documentation for any upgrades to equipment and technology for which compensation is claimed.

The 0.5% compensation is to be claimed by Stamping Agents as a credit against their monthly tax liability and is limited (for a particular month) by the amount of cigarette tax due that month. Compensation may be claimed no earlier than the first calendar month following the Stamping Agent’s Implementation Date and may continue to be claimed until the Stamping Agent is fully compensated for the eligible upgrade costs.

Example: Stamping Agent ABC purchases an eligible upgrade to technology or equipment for \$5,000 on April 1, 2014. The Implementation Date for Stamping Agent ABC is May 1, 2014 and its cigarette tax liability for the month of May 2014 is \$4,000. Stamping Agent ABC is eligible to begin claiming compensation for this upgrade purchase beginning with its TPTA tax return due on June 20, 2014 (i.e., reporting its May 2014 TPTA tax). Stamping Agent ABC is only eligible to claim \$200 (0.5% x \$4,000) in compensation on this return. Stamping Agent ABC is not eligible for a refund of the remaining \$4,800, but may continue to claim the applicable 0.5% compensation on its succeeding monthly cigarette tax returns until it is fully reimbursed.

CONTACT INFORMATION

If you have any questions or concerns about this Notice, please contact the Department of Treasury’s Tobacco Tax Unit at (517) 636-4630.

If you have questions about digital stamping technology or purchasing a digital stamping machine, please contact the Xerox State & Local Solutions, Inc. at (602) 412-2033.