

Finding of Emergency

Statement Regarding Compliance With Government Code section 11346.1(e)

As explained herein, the Department of Justice (Department) has made substantial progress and proceeded with diligence toward compliance with Government Code section 11346.1(e). Specifically, in addition to monitoring compliance with the California Tobacco Directory, we have been successfully implementing the initial emergency regulations with many companies. The Department submitted the Certificate of Compliance for the regular rulemaking to the Office of Administrative Law in August 2019 and is currently working towards completion of the rulemaking process.

Statement Regarding Emergency Circumstances Since the Initial Adoption of Emergency

The Department finds it is necessary to re-adopt these emergency regulations because the circumstances demonstrating the existence of an emergency are unchanged since the emergency regulations' initial adoption.

The Department finds that an emergency exists and an immediate amendment of sections 999.12 and 999.13 of chapter 16, division 1, of title 11 of the California Code of Regulations and the Approved Tobacco Escrow Agreement, JUS-TOB6 (Rev. 1/2019), which is incorporated by reference into section 999.12, is necessary for the preservation of public health, safety, and general welfare. Immediate amendments to the California Approved Tobacco Escrow Agreement and implementing regulations are necessary to secure compliance with California's Qualifying Statute (Health & Saf. Code, §§ 104555-104557) and California's beneficial interest in funds deposited pursuant to California's Qualifying Statute.

Government Code section 11346.1, subdivision (a)(2), requires that, at least five working days prior to submission of the proposed emergency rulemaking to the Office of Administrative Law (OAL), the Department provide a notice of the proposed emergency action to every person who has filed a request for notice of regulatory action with the Department. To this end, the Department will post the proposed emergency regulation amendments on its public website and simultaneously disseminate notice of the proposed emergency action to all persons who have filed a request for notice.

After submission of the proposed emergency rulemaking to the OAL, the OAL shall allow interested persons five calendar days to submit comments on the proposed emergency regulation amendments as set forth in Government Code section 11349.6. Comments must be in writing only and contain a notation identifying the topic of the emergency rulemaking, and must be received by both the Department and the OAL within five days of the Department's filing with OAL. To determine the Office of Administrative Law's five day comment period, please visit <http://www.oal.ca.gov>.

Specific Facts Demonstrating the Need for Immediate Action:

- 1) In 1998, 46 states entered into a Tobacco Master Settlement Agreement (“MSA”) with the four largest tobacco manufacturing companies in the United States to settle certain claims against manufacturers arising out of the sale, advertising, and consumption of certain tobacco products. (Health & Saf. Code, § 104555, subd. (e).)
- 2) Tobacco manufacturers that elect not to join the MSA are required by California and almost all other states to deposit funds into qualified tobacco escrow accounts. (Health & Saf. Code, § 104557; Rev. & Tax. Code, § 30165.1.) Deposit amounts are based on sales of cigarettes and roll-your-own tobacco. Unless specific conditions are satisfied, such manufacturers may not access the principal on deposit for 25 years.
- 3) The Department is responsible for ensuring that tobacco manufacturers that have not joined the MSA deposit funds into the qualified tobacco escrow accounts. The escrow accounts for the Non-Participating Manufacturers (“NPMs”) are governed by an escrow agreement, which must be approved by the Attorney General’s Office. (Rev. & Tax Code, § 30165.1, subds. (b)(3)(B)(2) and (c)(2)(A).)
- 4) Until all of the escrow principal is eligible for release pursuant to Health and Safety Code sections 104555 through 104557, the Department must monitor the compliance of the tobacco escrow accounts. Currently, there is over 80 million dollars of tobacco escrow funds on deposit for the benefit of California.
- 5) Since the Department’s most recent revision to Sections 999.12 and 999.13 and the California Approved Tobacco Escrow Agreement, JUS-TOB6, in 2004, some NPMs have prematurely accessed escrow principal in violation of Health and Safety Code section 104557.
- 6) Furthermore, some NPMs have abandoned their reversionary interest in the escrow accounts without resolving the status of the funds with California or the escrow bank.
- 7) The emergency revisions to Regulations 999.12 and 999.13 and the Approved Tobacco Escrow Agreement, JUS-TOB6 (Rev. 1/2019) protect the public health and welfare by providing clear guidance to NPMs and escrow banks to ensure successful compliance with the law.
- 8) The regulations are being amended pursuant to Revenue and Taxation Code section 30165.1, subd. (o):

The regulations adopted to effect the purposes of this section are emergency regulations in accordance with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code. For purposes of that chapter, including Section 11349.6 of the Government Code, the adoption of the regulations shall be considered by the Office of Administrative Law to be necessary for the immediate preservation of the public peace, health and safety, and general welfare.

Authority and Reference Citations

Authority: Section 30165.1, Revenue and Taxation Code; Sections 11110 through 11113, Government Code; Section 104557, Health and Safety Code; Article 5, Section 13 of the California Constitution.

Reference: Section 30165.1, Revenue and Taxation Code, Sections 104555 through 104558, Health and Safety Code.

Information Digest / Policy Statement Overview

Section 999.12

This regulation applies to NPMs whose cigarettes or roll-your-own tobacco (“RYO”) are sold to consumers within California, NPMs that previously sold cigarettes or RYO to consumers within California and must maintain escrow principal for the benefit of California and other releasing parties under the MSA pursuant to Health and Safety Code sections 104555 through 104557, and the financial institutions that serve as escrow agents for NPMs with tobacco escrow accounts for the benefit of California.

Section 999.12 will be amended to explain the requirements for establishing and maintaining qualified tobacco escrow accounts and will incorporate the revised form of the escrow agreement that will govern the escrow accounts. Approved Tobacco Escrow Agreement JUS-TOB6 (Rev. 1/2019), is revised to ensure that NPMs and escrow banks properly hold, track, and monitor tobacco escrow funds on deposit for the benefit of California. Section 999.12 provides that other than filling blank spaces and checking boxes, no deviation, amendments, or other changes to the escrow agreement shall be permitted without the prior written approval of the Attorney General.

The revised form of the escrow agreement addresses several issues that that have emerged since California’s most recent revision. The revised definitions of “principal” and “interest” will prevent NPMs from prematurely accessing escrow principal. The revised form clarifies provisions regarding account ledgers, NPMs that fail to appoint successor agents after their escrow bank resigns, and reports from NPMs to the states.

Section 999.13

Section 999.13’s operative terms will be consolidated into section 999.12. Thus, section 999.13 will be repealed.

Forms and Standards Incorporated by Reference

A revised form of the Approved Tobacco Escrow Agreement, JUS-TOB6 (Rev. 1/2019) is incorporated by reference into the revised text of Section 999.12.

Summary of Existing Laws and Regulations Related Directly to the Proposed Rulemaking

NPMs must deposit funds into qualified escrow funds governed by state law based upon their sales of cigarettes and RYO. Unless specific conditions are satisfied, NPMs are statutorily prohibited from accessing or using the principal on deposit in the tobacco escrow accounts for twenty-five years. (Health & Saf. Code, § 104557, subd. (b).) NPMs and their escrow banks must execute a California Attorney General approved escrow agreement and ensure the funds are held and monitored in compliance with California law. (Rev. & Tax. Code, § 30165.1, subd. (b)(3)(B)(2) and (c)(2)(A).)

The Office of the Attorney General is responsible for establishing and updating California's tobacco escrow agreement. (Rev. & Tax Code, § 30165.1, subdivisions (o).) California Code of Regulations, Title 11, Sections 999.12 and 999.13 are the current regulations governing tobacco escrow accounts and the Approved Tobacco Escrow Agreement, JUS-TOB6 (Rev. 1/2019).

Evaluation of the Proposed Regulation for Consistency and Compatibility with Existing Regulations

The Department has determined that revisions to Sections 999.12, 999.13, and California's Approved Tobacco Escrow Agreement JUS-TOB6 (Rev. 1/2019) are not inconsistent or incompatible with existing state regulations

Mandate on Local Agencies or School Districts

No mandates or other impacts are imposed on any local agencies or school districts.

Technical, Theoretical, and Empirical Study, Report, or Similar Document, if any, Upon Which the Department Relied

The Department relied upon Department staff's understanding of tobacco escrow accounts in determining that the proposed emergency revision is necessary to have the effect and accomplish the objective of ensuring that NPM escrow deposits remain in qualified escrow accounts for the requisite time period pursuant to California law. The Department did not rely upon any technical, theoretical, or empirical study, report or similar document in making that determination.

Cost Estimates / Impact of Regulatory Action

The Department has assessed the potential for significant statewide adverse impact that might result from the proposed emergency action and has determined:

- There will be no costs or savings to local agencies or school districts;
- There will be no costs or savings in federal funding to the State;
- There will be no effect on housing costs.

The Department has determined that the emergency revisions to Sections 999.12, 999.13 will neither save nor cost additional funds to the State.

All of the tobacco companies and escrow banks addressed by these emergency revisions currently have tobacco escrow accounts and tobacco escrow agreements. The Department anticipates that the emergency regulations will require approximately 50 NPMs to each spend approximately \$1,500 reviewing and executing the revised regulation and escrow agreement.

Moreover, the Department anticipates that approximately eight to ten escrow banks will each spend approximately \$2,500 reviewing and executing several revised escrow agreements with NPMs.