

## Effective Taxation of Cigarettes and Other Tobacco Products

The American Cancer Society Cancer Action Network (ACS CAN) supports a comprehensive approach to tobacco control that includes regular, significant excise tax increases of \$1.00 or more per pack of cigarettes to effectively reduce the number of people who begin smoking and increase the number of people who quit. Taxing all other tobacco products, including e-cigarettes, at rates equivalent to the tax on cigarettes also helps prevent tobacco initiation among youth and promotes tobacco cessation among adults. Tax increases work best when tax revenues provide sustained funding for tobacco control programs that include hard-hitting earned and paid media campaigns, and evidence-based cessation services.

### Excise Taxes

Excise taxes are either “specific” or “ad valorem”

- A **specific excise tax** is a fixed monetary amount per quantity, volume, or weight of tobacco (or a combination of these).
- An **ad valorem excise tax** is a percentage of some measure of the value of tobacco products; retail, manufacturer or wholesale prices are often used as the base value.

### Taxing Cigarettes: By the Pack

All states currently have an excise tax on cigarettes at a rate per cigarette or per pack. In tax administration terms, this tax basis is known as a specific tax. In fact, since 2000, 48 states and the District of Columbia have increased their cigarette tax rates at least 149 times, always as a specific tax.<sup>i</sup>

According to the U.S. National Cancer Institute and World Health Organization, a specific tax on cigarettes better achieves public health objectives than an ad valorem excise tax because it increases retail prices of all products subject to the tax and does not perpetuate or increase price gaps between brands. Narrowing price gaps reduces consumers’ incentives to change from higher-priced to lower-priced brands or to other tobacco products.<sup>ii</sup>

Furthermore, specific taxes on cigarettes are easy to administer because cigarettes are uniform in their structure and packaging. Also important, specific taxes provide a more predictable revenue stream.

States that are interested in having cigarette taxes keep pace with inflation in real dollar terms can institute an inflation-based annual adjustment if they so choose, but these minor tax adjustments should not be in lieu of regular and significant cigarette tax increases of \$1.00 or more per pack. Tax revenue from ad valorem-based inflation increases would be (at best) pennies on the dollar which do not deter youth tobacco use, and they don’t encourage those who currently smoke to quit.

States should retain their current per-pack structural approach to taxing cigarettes. Switching the cigarette tax to a percent-of-price tax would produce the unintended consequence of creating larger price gaps between brands, resulting in a category of very low-cost cigarettes that appeal to youth, and furthermore encourage people who smoke cigarettes to simply switch to cheaper products rather than quit.

Additionally, changing the taxation on cigarettes to a price-based tax could add administrative complexity to efficient and effective enforcement of the Master Settlement Agreement as payments are based in part on tracking the quantity of cigarette sales and shipments which is easily tracked with a per-pack tax.

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## Taxing Other Tobacco Products: By Price

To maximize health and revenue gains, simplify tax collections, and make many dangerous and addictive products that are attractive to kids cost prohibitive, ad valorem excise taxes should be assessed on all other tobacco products including e-cigarettes. Taxing other tobacco products at a percent of the retail, manufacturer or wholesale price, with an accompanying minimum tax equal to the state's per-pack cigarette tax rate is the optimal way to tax these products. Instituting a minimum tax rate will reduce price gaps between tobacco products.<sup>iii</sup>

Other tobacco products, including chewing tobacco, cigars, hookah and e-cigarettes, vary widely in their structure and packaging unlike cigarette packs. This lack of uniformity makes an effective per-pack tax difficult to assess and collect on these types of products.

Tobacco companies favor weight-based or volume-based taxes on tobacco products to keep the price of their products cheaper for consumers. A weight-based or volume-based tax will not keep up with inflation or product price increases. As a result, a weight-based or volume-based tax will erode over time, bringing states lower revenue than percentage-of-price taxes.<sup>iv</sup> Taxing tobacco products by weight or volume is administratively complex, requiring independent verification of the quantity of taxable contents. Also, weight-based or volume-based taxes incentivize tax avoidance by tobacco manufacturers which could simply reduce the weight or change the composition of the product to keep the overall price low.

## The Bottom Line

Establishing a specific tax on cigarettes and a percent-of-price tax on other tobacco products will optimize the health, revenue collection, and enforcement aspects of the policy. ACS CAN supports regular and significant excise tax increases on all tobacco products. Ensuring that tobacco tax increases are equally applied across all product categories will maximize the health and revenue benefits of the tax increase. ACS CAN opposes tobacco industry attempts to complicate tax collection efforts by taxing cigarettes at a percent-of-price or by taxing other tobacco products by weight or volume. To further amplify health the benefits of the tax, ACS CAN also recommends that new tobacco tax revenues be directed to evidence-based tobacco prevention and cessation programs in accordance with Centers for Disease Control and Prevention best practices.<sup>v</sup>

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<sup>i</sup> Campaign for Tobacco-Free Kids. Cigarette Tax Increases by State per Year 2000-2023. Factsheet available at: <https://www.tobaccofreekids.org/assets/factsheets/0275.pdf>. Updated August 8, 2023.

<sup>ii</sup> U.S. National Cancer Institute and World Health Organization. The Economics of Tobacco and Tobacco Control. National Cancer Institute Tobacco Control Monograph 21. NIH Publication No. 16-CA-8029A. Bethesda, MD: U.S. Department of Health and Human Services, National Institutes of Health, National Cancer Institute; and Geneva, CH: World Health Organization; 2016. Section 3: Price Determinants of Demand: Chapter 5: Design and Administration of Taxes on Tobacco Products. [https://cancercontrol.cancer.gov/brp/tcrb/monographs/21/docs/m21\\_5.pdf](https://cancercontrol.cancer.gov/brp/tcrb/monographs/21/docs/m21_5.pdf). Accessed March 15, 2019.

<sup>iii</sup> Tobacco Control Legal Consortium. State Taxation of Non-Cigarette Tobacco Products. Last updated February 2012. Factsheet available at: <https://www.publichealthlawcenter.org/sites/default/files/resources/tclc-guide-state-tax-OTP-2012.pdf>. Accessed March 15, 2019.

<sup>iv</sup> Campaign for Tobacco-Free Kids. The Best Way to Tax Smokeless Tobacco: A Simple Weight-Based Tax Hurts State Revenues and Increases Youth Use. Washington, DC: Campaign for Tobacco-Free Kids; 2008.

<sup>v</sup> Centers for Disease Control and Prevention. Best Practices for Comprehensive Tobacco Control Programs—2014. Atlanta: U.S. Department of Health and Human Services, Centers for Disease Control and Prevention, National Center for Chronic Disease Prevention and Health Promotion, Office on Smoking and Health, 2014.