CAMPAIGN for TOBACCO-FREE Kids

THE BEST WAY TO TAX SMOKELESS TOBACCO
[A Simple Weight-Based Tax Hurts State Revenues and Increases Youth Use]

To protect state revenues, promote tax equity, and most effectively prevent and reduce tobacco use, especially among youth, states must avoid simple weight-based tax systems for moist snuff or smokeless tobacco. Taxing smokeless tobacco at a percentage of wholesale price better accommodates the many varieties of smokeless tobacco products, keeps up with inflation and product pricing over time, better promotes public health, and is much fairer than a simple weight-based tax. A simple percentage-of-price tax could allow brands sold at low predatory or anti-competitive prices to evade reasonable taxation, but adding a minimum tax can solve that problem. Switching to a simple weight-based tax, however, would create a host of new tax loopholes, reduce revenues, and cause other problems for the state.

Percentage-of-Price Taxes (and How to Make Them Even Better)

The most common practice among the states is to tax smokeless tobacco – and all other tobacco products other than cigarettes – at a percentage of their wholesale price (sometimes referred to as the manufacturer's price) tax. These state tax rates on other tobacco products (OTPs) range from a low of five percent (SC) to 100 percent (WI).

A percentage-of-price tax is one of the simplest and most effective ways to tax OTPs because it establishes an identical percentage tax rate, or flat tax, on all the different types, brands, weights, and packages of OTPs, and it keeps up with inflation over time. But state percentage-of-price taxes have come under attack by UST (the largest U.S. smokeless tobacco company, now owned by Altria, the parent company of Philip Morris USA) for subjecting UST's higher-priced, premium brands of regular moist snuff to a larger tax, per can or package, than brands with much lower prices. A higher per-can tax on higher-priced premium products (when all products pay the same flat-tax percentage rate) actually makes sense because those premium products bring in much larger amounts of income and profits per can. However, states can effectively address the problem of some smokeless brands being sold at bargain-basement or predatory prices not paying an adequate tax per can by supplementing the state's percentage-of-price tax with a reasonable minimum tax.

An effective minimum tax could simply state that any smokeless product with a wholesale price of less than $2.50 per ounce shall be taxed as if its price were $2.50 per ounce. Or even better, the minimum tax could set the tax rate on smokeless to be the higher of the percentage-of-price tax, or an amount equal to the state's tax on a pack of 20 cigarettes for each 1.2 ounces (a standard can of smokeless, roughly equal to a pack of cigarettes, weighs 1.2 oz.).

The Problems with A Simple Weight-Based Tax (and How to Fix Them)

Some states tax moist snuff tobacco products (a subset of all smokeless tobacco) on a per-weight basis. This approach has been pushed aggressively for years by UST. The advantages to UST and Altria from a state switching to a simple weight-based tax are enormous. It will sharply increase the tax on the lower-priced moist snuff smokeless sold by UST's competitors; and, over time (if not immediately), it will reduce the tax on UST's and Philip Morris's own premium smokeless products. In fact, getting a weight-based tax established is so beneficial to UST and Altria that they often design the tax-switch proposals to be especially attractive to states to make state moist snuff tax revenues increase in the year following the switch. But UST and Altria fail to inform the states that the switches they propose will, over time, actually increase overall smokeless tobacco use, especially among kids, and significantly reduce state revenues.

In fact, the simple weight-based proposals and laws supported by UST and Altria suffer from several major structural flaws:

- ***Unlike a percentage-of-price tax, a simple weight-based tax will not keep up with inflation or product price increases.*** As a result, the weight-based tax will erode over time, bringing the state increasingly lower revenues than a percentage-of-price tax. This problem can be fixed by adding in automatic inflation adjustment to the weight-based tax or by setting the weight-based tax amount to equal the state's tax on a pack of 20 cigarettes (so that the weight-based tax will go up every time the state increases its cigarette tax).
- ***Unlike a percentage-of-price tax, a simple weight-based tax will grossly under-tax the new generation of super-light-weight moist snuff products, sharply reducing future state revenues.*** The newest trend in smokeless is toward very low weight spit-less, pre-packed, single-dose units – such as UST's Skoal Dry, Philip Morris's Marlboro Snus, and RJ Reynolds Camel Snus and new Camel Dissolvable Orbs, Sticks, and Strips. Weighing as little as one-eighth as much per dose as standard moist snuff that comes in a can, these emerging new products pay almost nothing under a weight-based tax. This problem can be fixed by making sure that any weight-based tax applies only to conventional moist snuff (e.g., moist snuff that has a moisture content no lower than 45%) and not to any smokeless tobacco products that come in discrete, single-use units or doses.
- ***The weight-based tax proposals being pushed by UST and Altria require states to rely on whatever weight the manufacturer lists on the can or package when calculating the tax owed, leaving the door wide open door to fraud and abuse.*** This problem can be fixed by applying any weight-based tax to the weight listed in good faith by the manufacturer, as periodically confirmed by the state department of finance.
- ***A simple weight-based tax increases youth tobacco use and related public health harms****.* UST's best-selling premium smokeless tobacco products are among the most popular with youth, with just two of its brands (Copenhagen and Skoal) accounting for roughly half of all youth consumption. By reducing the taxes and prices on these brands, either immediately or over time, the simple weight-based taxes supported by UST and Altria directly increase youth smokeless initiation and use, dooming even more kids to a lifetime of tobacco addiction and related harms. This problem can be largely avoided by implementing the fixes described above; but a more effective solution would be to set the state's tax on smokeless to be the higher of a percentage-of-price tax or the fixed weight-based tax.

Simple weight-based tax systems for moist snuff or smokeless contradict tax equity, create tax loopholes, and are bad for state revenues and public health. Fortunately, these problems can be fixed quite easily with common sense modifications. Similarly, the concerns raised by UST and Altria regarding percentage-of-price tax systems can be effectively addressed (without causing any new problems) by adding a minimum tax. Moreover, adding minimum tax will also bring the state new revenues (and public health benefits) both in the short term and over time.[*]

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For more information: http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=18.

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[*] The Campaign for Tobacco-Free Kids has model legislative language to fix existing weight-based taxes or proposals or to establish the optimal system for taxing moist snuff, all smokeless, or all tobacco products. For more information, please contact factsheets@tobaccofreekids.org.

Model legislation is also available for: a) establishing strong minimum price laws for all tobacco products, both to prevent the kind of predatory and anti-competitive bargain-basement pricing by some manufacturers that UST complains about, and to block youth initiation into tobacco use and otherwise promote public health; and b) requiring smokeless tobacco companies that have not signed onto the Smokeless MSA (UST is the only signer) to make special payments to the states – just like the existing state laws that require payments from the nonparticipating cigarette companies (NPMs) that have not signed onto the cigarette MSA.