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Federal Excise Taxes on Tobacco Products: Rates and Revenues

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Summary

This report examines increases in excise tax rates on tobacco products contained in the Balanced Budget Act of 1997 (P.L. 105-33). Under that Act, the increased rates on tobacco products became effective in two stages. The first scheduled increase in rates occurred on January 1, 2000, while the second increase in rates occurred two years later on January 1, 2002.

The increased rates apply to all tobacco products. In addition, the Act included a new excise tax on roll-your-own tobacco which became effective January 1, 2000. Also included in the Act were expanded compliance measures designed to ensure collections of tobacco excise tax monies. As a result of payments made by tobacco companies under the Master Settlement Agreement and the resulting increase in the cost of tobacco products, tobacco consumption declined. Thus, projected federal tobacco revenues have declined somewhat when compared to prior revenue estimates made at the time of the Balanced Budget Act's passage. This report will be updated as legislative developments warrant.

Tax Rates

The federal tax rate on cigarettes remained unchanged at 8 cents per pack from 1951 to 1982.¹ Since 1982 the rate has been increased by three federal tax acts. The rate was increased to 16 cents per pack as part of the Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97-248). In the General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982, the Joint Committee on Taxation indicated that the reason for this increase was that inflation had caused the effective level of the tax to decline by more than 70% in constant dollars because the tax was imposed as a set

¹ For a more detailed legislative history see CRS Report 94-474, *Federal Excise Taxes on Tobacco Products: A Summary of Present Law and a Legislative History*, by Thomas B. Ripy and Mildred C. Washington.

amount, rather than as a percentage of sales price. The doubling of the tax rate did not increase the per-pack tax, in real terms, above the 1951 level. Also, Congress felt that the broad-based increase in revenue required by the fiscal outlook through 1985 mandated an increase in the cigarette excise taxes.

Next, the rates were increased in two stages under the Revenue Reconciliation Act of 1990 (P.L. 101-508). One half of the increase (4 cents per pack) took effect on January 1, 1991 with the second half (an additional 4 cents) in effect as of January 1, 1993. Thus, the Revenue Reconciliation Act of 1990 raised the rates from 16 cents per pack to 24 cents per pack. The rates were increased because of large continuing federal budget deficits and the need for additional federal revenues.

The most recent increase in federal excise tax rates on tobacco products occurred in the Balanced Budget Act of 1997 (P.L. 105-33). Like the increases provided under the Revenue Reconciliation Act of 1990, the tax rates on all tobacco products increased in two stages. The rates first increased on January 1, 2000. The final increase in rates occurred on January 1, 2002. In the case of cigarettes, the first stage increased rates by 10 cents a pack to 34 cents. In the second stage, the rates increased an additional 5 cents a pack to make the federal excise tax 39 cents per pack. In addition, the Act established a tax rate for roll-your-own tobacco which is now in effect. **Table 1** provides details on the rate increases imposed on all tobacco products for the period 1990 to 2002.²

Revenues

The actual revenue yield from federal tobacco excise taxes remained relatively stable during the 1990s. After the statutory rate increase in 1993 the revenue yield jumped from just over \$5 billion in fiscal year 1992 to \$5.875 billion in fiscal year 1993. Fiscal year revenues over the 1993 to 1996 time period have ranged from a low of \$5.691 billion to a high of \$5.878 billion. The Joint Committee on Taxation estimated that the Balanced Budget Act of 1997 increase in tobacco tax rates would increase revenues beginning in fiscal year 2000 (the increased rate is effective for a nine month period during that fiscal year). At the time of the Balanced Budget Act of 1997's enactment, the Joint Tax Committee estimated that additional revenues of \$1.175 billion would be collected in fiscal year 2000 due to the first part of the rate increase. Further, the committee estimated that the increased rates would result in more than \$2 billion in additional annual revenue by fiscal year 2002. As indicated earlier, these projections were made prior to the tobacco Master Settlement Agreement. A detailed breakdown of actual and estimated tobacco tax receipts is provided in Table 2, which appears on the final page of this report.

² As originally enacted, increased revenue collections were to be credited against the total payments to be made under the tobacco industry settlement agreement. However, this provision was repealed under section 519 of the Fiscal Year 1998 Appropriations for Labor, Health and Human Resources (P.L. 105-78).

Table 1. Comparison of Tobacco Excise Tax Rates

Commodity	Statutory Rate— 1990	Statutory Rate— 1991	Statutory Rate— 1993	Statutory Rate— 2000-01	Statutory Rate— 2002
Cigarettes, small (Class A) Rates are per thousand	\$8.00 (16 cents per pack)	\$10.00 (20 cents per pack)	\$12.00 (24 cents per pack)	\$17.00 (34 cents per pack)	\$19.50 (39 cents per pack)
Cigarettes, large (Class B) Rates are per thousand	\$16.80	\$21.00	\$25.20	\$35.70	\$40.95
Large cigars, wholesale price not more than \$235.294 per thousand	8.5% of wholesale price (but not more than \$20 per thousand)	10.625% of wholesale price (but not more than \$25 per thousand)	12.75% of wholesale price (but not more than \$30 per thousand)	18.063% of wholesale price (but not more than \$42.50 per thousand)	20.719% of wholesale price (but not more than \$48.75 per thousand)
Small cigars (per thousand)	75 cents	93.75 cents	\$1.125	\$1.594	\$1.828
Cigarette Papers (per 50)	0.500 cent	0.625 cent	0.750 cent	1.06 cents	1.22 cents
Cigarette tubes (per 50)	1.0 cent	1.25 cents	1.5 cents	2.13 cents	2.44 cents
Snuff (per pound)	24 cents	30 cents	36 cents	51 cents	58.5 cents
Chewing Tobacco (per pound)	8 cents	10 cents	12 cents	17 cents	19.5 cents
Pipe Tobacco (per pound)	45 cents	56.25 cents	67.5 cents	95.67 cents	\$1.0969
“Roll Your Own Tobacco”				95.67 cents per pound	\$1.0969 per pound

When the Joint Tax Committee estimated the projected increase in tobacco tax revenues, the Master Settlement Agreement between the states, the District of Columbia, U.S. territories, and the tobacco industry had not been signed. As a result of the Master Settlement Agreement, tobacco companies have raised prices a number of times so as to raise revenues with which to make the annual payments totaling \$204.5 billion through 2025. In apparent response to the increase in price, projected tobacco consumption has declined.³ Thus, the Joint Tax Committee's revenue estimates for tobacco receipts would be lower if made under current conditions. More recent projected federal tobacco tax estimates, prepared by the Treasury Department, are shown in the final column of Table 2, which appears on the final page of this report.

In addition to the excise taxes on various tobacco products, there is also an occupational tax. A manufacturer or exporter of taxable tobacco products with gross receipts of less than half a million dollars in the preceding taxable year must pay a tax of \$500 a year. For those whose gross receipts exceed that amount, the tax is \$1,000 a year per business premise. While the special occupational taxes brought in approximately \$102.8 million in fiscal year 2000, the tax applies to alcohol and firearms as well as tobacco, and it is believed that tobacco accounts for only a small part of the revenue. Occupational taxes collected from those dealing in alcohol and firearms make up the bulk of collection revenues. No breakdown of the special occupational taxes is available.

Tobacco excise taxes are paid into the General Fund of the U.S. Treasury. There continues to be no direct relationship between federal tobacco excise tax collections and any particular federal program. In those cases where other excise taxes are directly linked with spending programs (as through trust funds), there is usually a relationship between the taxed products and a program financed by the funding (such as the gasoline and diesel fuel excise taxes and the Highway Trust Fund). In some cases, excise taxes may be imposed in situations where those actually responsible for damages cannot be held directly accountable (such as the .01 cent excise tax on gasoline used for cleaning up underground leaking storage tanks). In those cases, taxes are levied on current production of a product associated with causing the damages that the government program is trying to rectify.

³ For a discussion of the Master Settlement Agreement effects on price, workers, suppliers, consumption, and income distribution see CRS Report 97-995, *The Proposed Tobacco Settlement: Effects on Prices, Smoking Behavior, and Income Distribution*, by Jane G. Gravelle.

Table 2. Tobacco Excise Tax Estimates and Actual Revenue Receipts
(Revenue Amounts in Billions)

Fiscal Year	Tobacco Excise Tax Revenues (Estimates Made Under Prior Tax Law) ^a	Joint Tax Committee Estimated Increase in Tobacco Excise Tax Receipts ^b	Tobacco Excise Tax Revenues (Actual for FY2000 and Estimates Under Current Tax Law) ^c
1992 (actual)	\$5.049		
1993 (actual)	\$5.875		
1994 (actual)	\$5.691		
1995 (actual)	\$5.878		
1996 (actual)	\$5.795		
1997 (estimate)	\$5.694		
1998 (estimate)	\$5.661		
1999 (estimate)	\$5.626		
2000 (estimate)	\$5.594	\$1.175	\$7.221
2001 (estimate)	\$5.563	\$1.720	\$7.548
2002 (estimate)	\$5.535	\$2.272	\$8.140
2003 (estimate)		\$2.280	\$8.175
2004 (estimate)		\$2.290	\$7.941
2005 (estimate)		\$2.300	\$7.778
2006 (estimate)		\$2.310	\$7.643
2007 (estimate)		\$2.320	

a. U.S. Office of Management and Budget. *Budget of the United States Government, Historical Tables, Fiscal Year 1998*. February 1997. p. 39.

b. U.S. Congress. Joint Committee on Taxation. *General Explanation of Tax Legislation Enacted in 1997*. Washington, U.S. Govt. Print. Off., 1997. p. 546.

c. U.S. Office of Management and Budget. *Budget of the United States Government, Analytical Perspectives, Fiscal Year 2002*. February 2001. p. 47.