

SMOKESHOP

THE INDUSTRY AUTHORITY ON TOBACCO RETAILING

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E-CIGARETTES

No longer a fringe category, e-cigs are increasingly seen as playing a major role in the future of the tobacco industry.

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to Date; Retailers Pass 95.1% of them.

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Little Cigars are a Big Deal

Little cigars are often a cheaper alternative to cigarettes, at least for now, as states cast increasing scrutiny on the category as tax evaders.

>BY TROUTMAN SANDERS TOBACCO TEAM

A report issued this year by the Centers for Disease Control and Prevention, "Consumption of Cigarettes and Combustible Tobacco—United States, 2000-2011," states that despite a continuing decline in cigarette use, there has been, in recent years, a drastic increase in adult consumption of cigarette-like cigars. These cigars are often referred to as "filtered cigars," and generally look identical to a cigarette, except that they are brown in color, given that they are wrapped in tobacco or paper containing tobacco. In addition, they are often packaged similarly to cigarettes, in packs of 20, and in cartons containing 10 packs.

The CDC report also revealed that while total consumption of all smoked tobacco products declined by 27.5 percent between 2000 and 2011, large cigar consumption increased by 482 percent and 233 percent, respectively. The increase in consumption of filtered cigars is directly related to their lower cost, both due to lower federal excise taxes applicable to many filtered cigars and to the applicable state tax rates. For example, in an August 2012 press release, Alabama Tobacco Prevention and Control Branch Director Diane Beeson explained that, "In Alabama, we are seeing more interest in little cigars, which look almost exactly like cigarettes, but are wrapped in paper which contains tobacco."

Notably, the federal excise tax on "small cigars" weighing less than three pounds per thousand is exactly the same as that imposed on cigarettes: \$1.01 per pack of 20. However, by increasing the tobacco in filtered cigars so that they weigh just over three pounds per thousand, filtered cigars can be classified as a "large cigars." The federal excise tax on large cigars is calculated differently

from that imposed upon both cigarettes and small cigars, and is based upon the sales price of the product. The net effect is that "large" filtered cigars are generally subject to a lower federal excise tax rate, which results in a lower overall sales price.

A favorable excise tax differential exists for filtered cigars in many states as well; for instance, many states impose a flat tax rate upon cigarettes, while cigars are often classified as "other tobacco products," with tax rates are based upon a percentage of the price of the product. Such taxing schemes generally result in a lower state excise tax rate for filtered cigars. Notwithstanding, many states are starting to take notice of the increased consumption of filtered cigars, and many are changing their excise tax schemes in an attempt to tax filtered cigars at the same rate as cigarettes.

For example in Montana, a product classified as a cigar for federal excise tax purposes can be subjected to the state's cigarette tax if it meets two or more of the following criteria:

- *the product is sold in packs containing 20 or 25 sticks;*
- *the product is available for sale in cartons of ten packs;*
- *the product is sold in soft packs, hard packs, flip-top boxes, clam shells, or other cigarette-type boxes;*
- *the product is of a length and diameter found in commercially-manufactured cigarettes;*
- *the product has a cellulose acetate or other integrated filter;*
- *the product weighs less than three pounds per thousand sticks;*
- *the product is marketed or advertised to consumers as a cigarette or cigarette substitute; or*
- *other evidence that the product fits within the definition of cigarette.*

New Mexico has also taken steps to identify and regulate cigarette-like cigars. In August 2012, the state's Attorney General's office issued a notice to licensed cigarette distributors that stated "if there is any product that, because of its appearance, looks like a cigarette but is marked 'large cigar,' you must provide us with the brand and manufacturer name of these products in order for the Attorney General's office to make a determination as to the correct size."

By contrast, New York simply taxes cigars that contain a cellulose acetate or other integrated filter at the same tax rate as cigarettes. A little cigar, which is taxed at the same rate as a cigarette, is defined by New York as "any roll for smoking made wholly or in part of tobacco if the product is wrapped in any substance containing tobacco, other than natural leaf tobacco wrapper, with a cellulose acetate or other integrated filter." Other states vary the weight of products that are considered small cigars and are thus subject to tax treatment as a cigarette. Pennsylvania, for example, taxes any "small cigar" weighing less than four pounds per thousand at the same rate as a cigarette.

Because of the continued growing consumption of filtered cigars by consumers, due to their lower cost, States are expected to continue to crack down on these products in an attempt to subject filtered cigars to their State's higher cigarette tax rate. Any manufacturer, distributor, or retailer of these products is well-advised to stay abreast of the laws regarding filtered cigars and small cigars so that they understand the consequence of any failure to properly charge the applicable tax on these products. Many states impose significant criminal penalties and fines for such violations. **S**

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