

Taxation of Emerging Tobacco Products - Executive Summary

Background

Over the past decade, new nicotine products have emerged in the marketplace requiring governments to adapt existing tobacco control policies and to develop new methods of regulation, standardization, and taxation. Taxation is one of the most effective public health strategies for reducing tobacco use and its associated health consequences. Each type of tobacco product is subject to its own tax rates and may vary in form (by weight, by pack, by wholesale price, etc.).

The emergence of new products such as e-cigarettes and other vaping products and heated tobacco products has added new complexity and challenges for efficient and effective taxation, given the diversity of the product categories, differing levels of nicotine, and the lack of product standardization. This has led to considerable variability in how these newer products are being taxed by states and localities.

Methodology

This report provides an analysis of current state tobacco product taxation, including the taxation of e-cigarettes, in the United States and a summary of qualitative interviews that elucidated the challenges to implementation states have faced and important lessons learned. The findings from this assessment have helped shape a set of recommendations for e-cigarette and other vaping product taxation going forward. As the market and regulations change, these recommendations may evolve.

Key Recommendations

Based on experiences of states and local jurisdictions taxing e-cigarettes, the following are recommendations for applying taxes equivalent to taxes on combustible cigarettes:

A) Specific vs. Ad Valorem Taxation:

The wide variety of available vaping products make *ad valorem* excise tax the most appropriate tax structure to avoid favoring certain products. Specific excise taxes are more beneficial to products that are highly homogenous and become problematic when applied to products that have significant differences.

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B) Ad Valorem Tax Base:

By levying an *ad valorem* excise tax based on the tax-inclusive retail price of e-cigarettes and other vaping products, the potential for tax-avoidance resulting from pricing schemes will be minimized and the effective tax will rise with inflation. This ensures the price paid by the consumer includes the tax and has a greater impact on consumer behavior.

C) Taxing Devices and/or Components:

Some vaping product devices are well defined, while others are not. Due to the diversity of devices and components on the market, it is not recommended that excise taxes be levied on the devices themselves.

D) Taxing E-Liquids:

The most effective method of taxing e-liquids is to include all liquids due to the difficulty in measuring and determining the presence of nicotine. For products that include the device and the e-liquid, taxes should be levied on the retail price of the product.

E) Where to Collect the Tax:

The non-traditional distribution chains for e-cigarettes and other vaping products make it difficult to determine where tax should be collected. State and local level excise taxes should be collected at the point-of-sale based on the retail price.

F) Tax Rates:

At this time, all e-cigarettes and other new tobacco products should be taxed at rates that achieve parity with the average cigarette tax rates in each state. Until more clarity is provided about the relative harms and risks of new tobacco product as determined by the FDA, it is appropriate to tax these products at the same rate as combustible cigarettes.

G) Heated Tobacco Products:

Given the relatively homogeneous ‘heat sticks’ used in heated tobacco products, levying a specific tax per stick appears most appropriate.

H) Federal Government:

Currently, the federal government does not tax e-cigarettes or heated tobacco products. However, alternative proposals for taxing these products have been introduced in the US Congress and, for e-cigarettes, the best approach may be a volume-based specific tax equivalent to the level of nicotine contained in cigarettes, assuming that there is nicotine testing conducted on the products.

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This Policy Brief is based on a larger Report titled the *Taxation of Emerging Tobacco Products* found on the [Tobacconomics](http://Tobacconomics.org) website [here](#).

About Tobacconomics

Tobacconomics is a collaboration of leading researchers who have been studying the economics of tobacco control policy for nearly 30 years. The team is dedicated to helping researchers, advocates and policymakers access the latest and best research about what’s working—or not working—to curb tobacco consumption and the impact it has on our economy. As a program of the University of Illinois at Chicago, Tobacconomics is not affiliated with any tobacco manufacturer. Visit www.tobacconomics.org or follow us on Twitter www.twitter.com/tobacconomics.