



USING STATE CIGARETTE TAX INCREASES TO REPLACE REDUCED TOBACCO SETTLEMENT PAYMENTS TO THE STATES

The cigarette companies' tobacco settlement payments to the states pursuant to the Master Settlement Agreement can fluctuate or decline for a variety of reasons – and the same holds true for the tobacco settlement payments received by Mississippi, Florida, Texas, and Minnesota, pursuant to their individual settlement agreements. First, the unadjusted base payment amounts used as a starting point for calculating each state's settlement receipts each year sometimes change. Second, the downward volume adjustment applied to these base payment amounts will continue to grow as the combined nationwide pack sales of the three major cigarette companies – Philip Morris, Reynolds American, and Lorillard – continue to decline because of consumption declines (and, possibly, from market share losses to other companies). And, third, the upward inflation adjustment applied to the unadjusted base payment amounts continues to grow (faster than actual inflation).¹

In addition, the settlement payments to the states can decline because various participating cigarette companies fail to make all or part of the settlement payments they owe in a particular year.² Most notably, in 2006 Reynolds American, Lorillard and many other MSA companies unilaterally withheld payments totaling more than \$800 million from the states based on an alleged Non-Participating Manufacturers adjustment linked to 2003, even though all the criteria for such a downward adjustment to their payments had not yet been met.³

States that would like to compensate for declining tobacco settlement receipts can easily do so through relatively small increases in their state excise tax rates on cigarettes and other tobacco products. No matter what else happens, the addictive power of cigarettes ensures that large amounts of cigarettes will continue to be sold by someone in each state for many years to come. That means that the states can always replace any lost, reduced, or delayed tobacco settlement payments by raising their cigarette tax rates. Put simply, the additional revenue per pack sold will easily make up for any declines in pack sales; and every state that has significantly raised its cigarette tax rate has experienced both reduced smoking levels and increased state revenues.

As an added bonus, any tobacco tax increases to offset declines in state tobacco settlement payments will also work directly and effectively to prevent and reduce tobacco use among kids; reduce adult smoking; decrease tobacco-caused death, disease, and suffering; and lock-in massive reductions to the wide range of tobacco-caused costs to government, business, and households.⁴

For illustrative purposes, the following table shows the size of the cigarette tax increase that would be needed in each state to compensate for the difference between what the state actually received in settlement payments in 2006 compared to the unadjusted base payment amount for that year.⁵

¹ For additional information on the state tobacco settlements, payments, and payment adjustments, see the Campaign materials at: <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=32> and <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=8>.

² Some state officials worry that one or more of the major cigarette companies might at some point declare bankruptcy – because of court rulings against them or other new legal obligations – further reducing or delaying total settlement payments to the states. But Wall Street tobacco industry analysts and other experts think that any such bankruptcy is highly unlikely – and that any significant decline in state settlement receipts because of a cigarette company bankruptcy is even more unlikely.

³ For more on the 2006 withholdings, see the Campaign factsheet, *The NPM Adjustment Threat to MSA Payments: How Real is It and How Can States Fight Back?*, <http://tobaccofreekids.org/research/factsheets/pdf/0293.pdf>.

⁴ For more on the power of tobacco tax increases to raise revenue and produce massive public health benefits and cost savings, see the Campaign website at: <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=18>.

⁵ Because the states never expected to receive as much as their full unadjusted base payment amount in any given year, because of the expected power of the downward volume adjustment, the tax increase amounts in the table would actually increase each state's tobacco revenues well beyond any unexpected declines in settlement payments.

Using State Cigarette Tax Increases to Replace Reduced Settlement Payments / 2

States	Current State Cigarette Tax Rate (cents/pack)	2006 Unadjusted Settlement Payment Amount (millions)	2006 Actual Settlement Payment Amount (millions)	2006 Downward Settlement Payment Adjustment (millions)	Increase to Cigarette Tax to Offset Downward Adjustment (cents/pack)
Alabama	42.5	\$113.2	\$93.4	\$19.8	7
Alaska	180	\$23.9	\$19.7	\$4.2	21
Arizona	118	\$103.2	\$85.2	\$18.1	13
Arkansas	59	\$58.0	\$47.9	\$10.1	7
California	87	\$894.0	\$737.6	\$156.4	20
Colorado	84	\$96.0	\$79.2	\$16.8	11
Connecticut	151	\$130.0	\$107.3	\$22.7	24
Delaware	55	\$27.7	\$22.9	\$4.8	6
Washington, DC	100	\$42.5	\$35.1	\$7.4	55
Florida	33.9	\$440.0	\$396.5*	\$43.5	5
Georgia	37	\$171.9	\$141.8	\$30.1	7
Hawaii	160	\$42.2	\$34.8	\$7.4	23
Idaho	57	\$25.4	\$21.0	\$4.4	8
Illinois	98	\$326.0	\$269.0	\$57.0	13
Indiana	55.5	\$142.9	\$117.9	\$25.0	7
Iowa	36	\$60.9	\$50.3	\$10.7	6
Kansas	79	\$58.4	\$48.2	\$10.2	11
Kentucky	30	\$123.4	\$101.8	\$21.6	5
Louisiana	36	\$158.0	\$130.3	\$27.6	9
Maine	200	\$53.9	\$44.5	\$9.4	25
Maryland	100	\$158.3	\$130.6	\$27.7	16
Massachusetts	151	\$282.9	\$233.4	\$49.5	30
Michigan	200	\$304.8	\$251.5	\$53.3	20
Minnesota	123	\$214.0	\$187.2*	\$26.8	18
Mississippi	18	\$136.0	\$122.5*	\$13.5	6
Missouri	17	\$159.3	\$131.4	\$27.9	9
Montana	170	\$29.8	\$24.5	\$5.2	15
Nebraska	64	\$41.7	\$34.4	\$7.3	10
Nevada	80	\$42.7	\$35.2	\$7.5	8
New Hampshire	80	\$46.6	\$38.5	\$8.2	9
New Jersey	257.5	\$270.8	\$223.5	\$47.4	34
New Mexico	91	\$41.8	\$34.5	\$7.3	17
New York	150	\$893.9	\$737.5	\$156.3	41
North Carolina	35	\$163.4	\$134.8	\$28.6	7
North Dakota	44	\$25.6	\$21.2	\$4.5	14
Ohio	125	\$352.8	\$291.1	\$61.7	14
Oklahoma	103	\$72.6	\$59.9	\$12.7	7
Oregon	118	\$80.4	\$66.3	\$14.1	13
Pennsylvania	135	\$402.5	\$332.1	\$70.4	17
Rhode Island	246	\$50.4	\$41.5	\$8.8	42
South Carolina	7	\$82.4	\$68.0	\$14.4	6
South Dakota	53	\$24.4	\$20.2	\$4.3	11
Tennessee	20	\$171.0	\$141.1	\$29.9	7
Texas	141	\$580.0	\$507.4*	\$72.6	16
Utah	69.5	\$31.2	\$25.7	\$5.4	11
Vermont	179	\$28.8	\$23.8	\$5.0	28
Virginia	30	\$143.2	\$118.2	\$25.0	6
Washington	202.5	\$143.8	\$118.7	\$25.2	25
West Virginia	55	\$62.1	\$51.2	\$10.9	9
Wisconsin	77	\$145.1	\$119.7	\$25.4	10
Wyoming	60	\$17.4	\$14.4	\$3.0	11

* Estimated