

Cigarette Tax and Tobacco Products Tax

Overview – Washington state taxes cigarettes and other tobacco products under two separate tax rates and statutes. Cigarettes are taxed at their own rate while other tobacco products such as cigars, chewing tobacco, and snuff are taxed at a different rate. These so called “sin” taxes have been a popular tax to increase in recent years to pay for more government spending. Washington currently has the third-highest cigarette tax in the nation and one of the highest taxes on other tobacco products.

Tax Rates

Cigarettes:	\$2.025/pack
Other tobacco products:	75 percent of the wholesale price (for cigars, 75 percent of the wholesale price or 50 cents/cigar, whichever is less)

Tax revenues from cigarettes and tobacco products are distributed mainly to the Health Services Account to pay for health care programs, including the Basic Health Plan, and education programs. The remaining receipts are distributed to the General Fund, water quality programs and drug and alcohol programs. Following is the current distribution of the cigarette tax:

➤ 24.68 cents	General Fund
➤ 9.02 cents	Water Quality Account
➤ 11.88 cents	Violence Reduction and Drug Enforcement Account (VRDE)
➤ \$1.1402	Health Services Account
➤ 42.9 cents	Education Legacy Trust Account

Legislative History – The cigarette tax was enacted in 1935 with an initial rate of 1 cent per pack. The other tobacco products tax was enacted in 1959 with an initial rate of 25 percent of the wholesale price. In 2001, I-773 raised the cigarette tax by 60 cents per pack and the tobacco products pack by 54.5 percent to a rate of 129.42 percent. All proceeds from I-773 revenues were to be used for new enrollments in the Basic Health Plan above 125,000. However, the 2003 Legislature eliminated this requirement and used the I-773 funding to help balance the operating budget.

The 2005 Legislature raised the cigarette tax by an additional 60 cents per pack, bringing the overall tax to the current rate of \$2.025/pack. Proceeds from most of this 60-cent tax are deposited in the Education Legacy Trust Account created at the same time to pay for I-728 allocations, higher education, and other education programs at the discretion of the Legislature. The 2005 Legislature also *lowered* the Other Tobacco Products Tax from 129.42 percent of the wholesale price to 75 percent, the pre I-773 level.

Tribal Compacts – Indian tribes have been a source of cheaper cigarettes because they are not subject to state cigarette and tobacco taxes. In 2001 the Legislature authorized the governor to enter into cigarette compacts with certain federally recognized Indian tribes. The compacts were designed to reduce cigarette tax evasion by non-tribal residents. To date, most of the federally recognized tribes in Washington have a compact or are negotiating one with the governor.

The compacts allow tribes to collect a tribal cigarette tax and sales tax for cigarettes sold to non-Indians. These tribal taxes are in lieu of the state cigarette tax, with the exception of the compact between the state and the Puyallup Indian tribe. Under the Puyallup compact, the tribe collects a tribal cigarette tax lower than the state tax, but shares 30 percent of the revenue with the state (an estimated \$10 million in state revenue per year).

Legislation passed in 2008 provided a separate cigarette tax compact for the Yakama Tribe. This compact requires the tribe to collect a cigarette tax rate equal to 80 percent for the first six years and increasing to 87.6 percent by the eighth year of the agreement. There was concern that this could become the standard rate when other tribal compacts are up for renegotiation in the coming years and lead to more cigarette tax evasion because tribal cigarettes would once again be cheaper than off-reservation.

Issues and Outlook – Cigarette and tobacco products tax evasion is prevalent because of the state's high tax rates. Smuggled cigarettes from tribal reservations, as well as increasing Internet purchases, remain an issue. Ironically, the 2005 Legislature raised the cigarette tax while lowering the tobacco products tax. Proponents of lowering the tobacco products tax argued that it would stimulate Washington business because fewer people would purchase their products over the Internet or from the black market. However, cigarette tax evasion is still high, and the Legislature raised the tax again. The Department of Revenue estimates that the state loses \$200 million in cigarette tax revenue to Internet purchases and smuggled products.