

# Tobacco Taxes: Federal Revenue Implications of Tax Rate Differences and Drawback Refunds

GAO-25-107903

Q&amp;A Report to Congressional Committees

August 20, 2025

## Why This Matters

By increasing gaps in tax rates for smoking tobacco products that are similar to each other, the Children's Health Insurance Program Reauthorization Act (CHIPRA) of 2009 created opportunities for tax avoidance through the substitution of lower-taxed tobacco products for higher-taxed ones. Specifically, CHIPRA increased the federal excise tax rate on cigarettes and set equivalent tax rates on roll-your-own tobacco and small cigars, which can be close substitutes for factory-made cigarettes. As a result, the tax rates for these products are generally higher than the tax rates for pipe tobacco and large cigars. In addition, consumers have increasingly purchased e-cigarettes and oral nicotine pouches that are not federally taxed.

We reported in 2012, 2014, and 2019 that sales of lower-taxed pipe tobacco and large cigars saw immediate and significant growth following CHIPRA, and we estimated the amount of revenue lost by the federal government because of these market shifts. To address this issue, we recommended that Congress consider equalizing tax rates on pipe tobacco and roll-your-own tobacco. We also recommended that Congress, in consultation with the Department of the Treasury, consider options for reducing tax avoidance related to the different tax rates for small and large cigars. As of July 2025, Congress has not passed legislation to eliminate these tax differentials among smoking tobacco products.

For this report, as part of our work on duplication, overlap, fragmentation, cost savings, and revenue enhancement in response to a provision in section 21 of public law 111-139, we reviewed the markets for cigarettes, roll-your-own tobacco, pipe tobacco, small cigars, and large cigars. We also reviewed how certain new products affected markets for these traditional smoking tobacco products. In addition, we examined how much additional revenue the federal government could collect over the next 5 fiscal years if tobacco tax rate disparities were eliminated as of fiscal year 2025. Further, we examined how much revenue the federal government refunded to companies through drawback claims for taxes paid on tobacco imports that were substituted with similar, qualifying products later exported or destroyed.

## Key Takeaways

- Federal revenue from tobacco excise taxes has decreased since fiscal year 2014 as sales of smoking tobacco products have declined.<sup>1</sup> The extent to which the increased use of e-cigarettes and oral nicotine pouches has affected sales for traditional smoking tobacco products is unknown.
- Tax rate disparities created by CHIPRA in 2009 led to market shifts from higher-taxed roll-your-own tobacco to lower-taxed pipe tobacco and from higher-taxed small cigars to lower-taxed large cigars, and these trends have continued since then.<sup>2</sup>

- Federal revenue would likely increase if Congress were to eliminate the tax differences among similar smoking tobacco products. For instance, if the tax rate for pipe tobacco were increased to the roll-your-own tobacco rate, the federal government could collect at least \$1.5 billion in additional revenue for both products from fiscal year 2025 through fiscal year 2029. Similarly, revenue would likely increase if Congress were to establish a minimum tax rate for large cigars equal to the small cigar rate.
- The requested and approved amounts of drawback refunds for smoking tobacco products have both generally increased in recent years. Drawbacks are refunds of up to 99 percent of duties, taxes, or fees paid on imports and may be requested by companies that export similar, qualifying goods. From fiscal year 2019 through fiscal year 2024, the federal government refunded approximately \$312 million in excise taxes for smoking tobacco products.

## How did CHIPRA change the federal tax rates for smoking tobacco products?

In 2009, CHIPRA increased the federal excise tax rates for cigarettes, roll-your-own tobacco, and small cigars more than it increased the tax rates for pipe tobacco and some large cigars.<sup>3</sup> Cigarettes and small cigars are taxed on a per stick basis, while roll-your-own tobacco and pipe tobacco are taxed by weight.<sup>4</sup> The tax rate on large cigars is ad valorem—calculated as a percentage of the manufacturer’s or importer’s sale price—up to a maximum tax per cigar.<sup>5</sup> Figure 1 shows a sample of these smoking tobacco products.

**Figure 1: Examples of Cigarette and Cigar Products**

Small cigars and hand-rolled cigarettes are close substitutes for factory-made cigarettes.



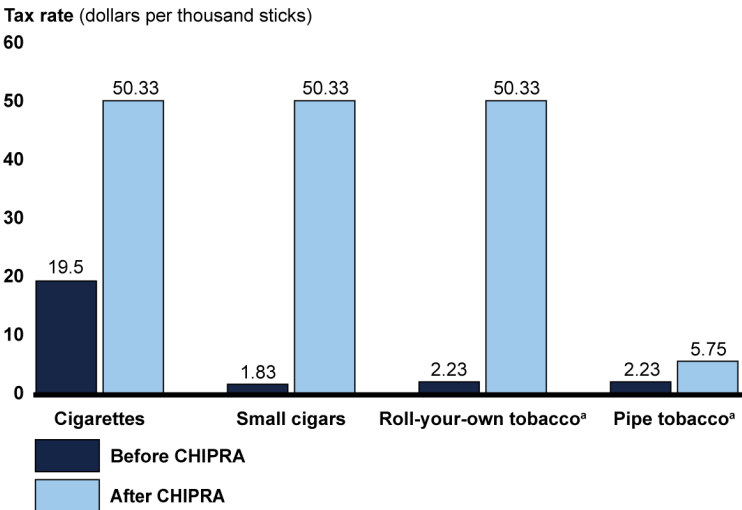
Source: GAO (photo). | GAO-25-107903

Note: The small cigar (number 3) and the large cigar (number 4) are similar in appearance but are categorized differently for tax purposes based on their weight. Under the Internal Revenue Code, small and large cigars are differentiated by a weight threshold. Small cigars are defined as weighing 3 pounds or less per thousand sticks and large cigars are defined as weighing more than 3 pounds per thousand sticks. To qualify as a small cigar, cigar number 3 must fall under the weight threshold differentiating small and large cigars, while cigar number 4 must be over this weight threshold.

CHIPRA equalized—on a comparable per stick basis—federal excise tax rates for cigarettes, small cigars, and roll-your-own tobacco but not for pipe tobacco, as shown in figure 2. As a result, a hand-rolled cigarette made with pipe tobacco (marked as number 1 in figure 1) has a lower applicable tax rate than either the

factory-made cigarette (number 2) or a hand-rolled cigarette made with roll-your-own tobacco.

**Figure 2: Federal Excise Tax Rates for Tobacco Products Before and After the Children’s Health Insurance Program Reauthorization Act (CHIPRA) of 2009**



Source: GAO analysis of the Internal Revenue Code. | GAO-25-107903

Notes: The tax rate on large cigars is ad valorem—calculated as a percentage of the manufacturer’s or importer’s sale price—up to a maximum tax per cigar. CHIPRA increased the tax rate on large cigars from 20.72 percent of the manufacturer’s or importer’s sale price with a maximum tax of 4.875 cents per cigar to 52.75 percent of this sale price with a maximum of 40.26 cents per cigar (\$402.60 per thousand sticks). CHIPRA increased the federal excise tax rate for large cigarettes up to 6.5 inches long from \$40.95 to \$105.69 per thousand sticks. Large cigarettes over 6.5 inches long are taxed at the rate for small cigarettes but counting each 2.75 inches or fraction thereof in the length of each such cigarette as a separate stick.

<sup>a</sup>Because roll-your-own tobacco and pipe tobacco are taxed based on weight, we converted weight to cigarette stick equivalent using the Tobacco Master Settlement Agreement conversion rate that is based on the weight of 0.0325 ounces of roll-your-own tobacco per cigarette stick. In 1998, 46 states signed the Tobacco Master Settlement Agreement with the four largest U.S. tobacco companies to settle state tobacco-related lawsuits and recover billions in costs associated with smoking-related illnesses.

**What challenges do federal agencies face in collecting taxes on tobacco products?**

Treasury’s Alcohol and Tobacco Tax and Trade Bureau (TTB) has reported facing challenges when collecting federal excise taxes on smoking tobacco products. TTB collects taxes on domestic tobacco products when these products leave manufacturing facilities, while Customs and Border Protection (CBP), within the Department of Homeland Security, collects taxes on imported tobacco products after those products are released from Customs custody.<sup>6</sup>

TTB faces challenges in distinguishing between roll-your-own tobacco and pipe tobacco for tax collection purposes, in part, because the statutory definitions do not specify physical characteristics that would differentiate them. Rather, roll-your-own tobacco and pipe tobacco are defined in the Internal Revenue Code by such factors as the use for which the product is suited and how the product is offered for sale, as indicated by its appearance, type, packaging, or labeling (see table 1).<sup>7</sup> TTB officials said that these very similar products have historically been marketed as both kinds of tobacco by manufacturers.

**Table 1: Definitions of Smoking Tobacco Products in the Internal Revenue Code**

Product	Definition
<b>Cigarette</b>	(1) Any roll of tobacco wrapped in paper or in any substance not containing tobacco, and (2) any roll of tobacco wrapped in any substance containing tobacco which, because of its appearance, the type of tobacco used in the filler, or its packaging and labeling, is likely to be offered to, or purchased by, consumers as a cigarette described in (1).
<b>Roll-your-own tobacco</b>	Any tobacco which, because of its appearance, type, packaging, or labeling, is suitable for use and likely to be offered to, or purchased by, consumers as tobacco for making cigarettes or cigars, or for use as wrappers thereof.
<b>Pipe tobacco</b>	Any tobacco which, because of its appearance, type, packaging, or labeling, is suitable for use and likely to be offered to, or purchased by, consumers as tobacco to be smoked in a pipe.
<b>Small cigar</b>	Any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco (other than any roll of tobacco which is a cigarette) that weighs 3 pounds or less per thousand.
<b>Large cigar</b>	Any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco (other than any roll of tobacco which is a cigarette) that weighs more than 3 pounds per thousand.

Source: 26 U.S.C. §§ 5701, 5702. | GAO-25-107903

TTB officials have discussed the complexity of administering the federal excise tax on large cigars because it is calculated as a percentage of the manufacturer's or importer's sale price, up to a maximum tax per cigar. TTB guidance states the sale price that determines the amount of excise tax for large cigars is generally the price that a manufacturer or importer sells the cigar in an arm's length transaction to an unrelated party, typically a distributor or wholesaler.<sup>8</sup>

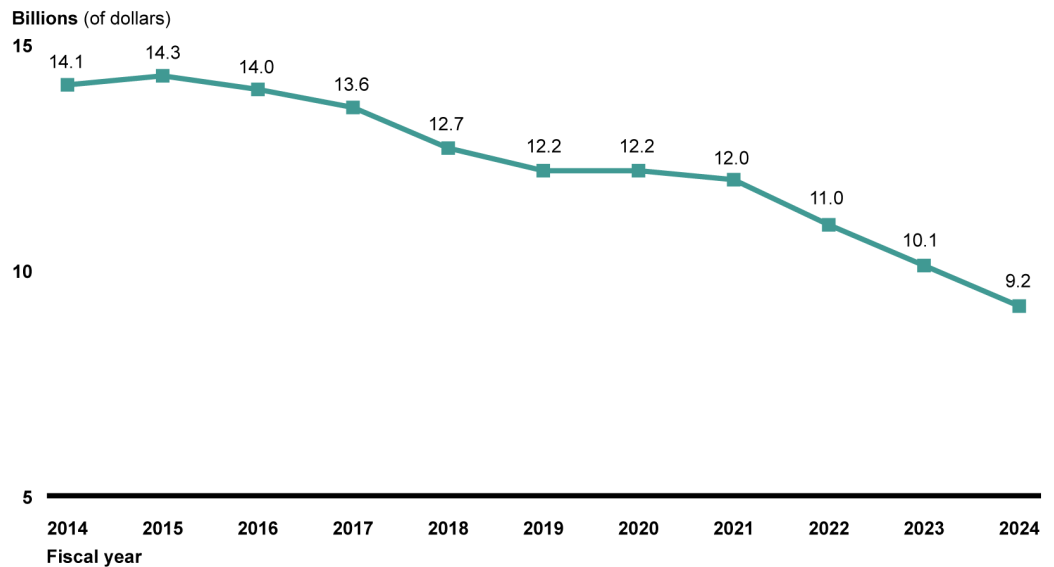
However, TTB officials said it can be challenging to establish the fair-market price and relationships among businesses. Some manufacturers and importers may restructure their market transactions to lower this sales price, according to TTB officials. For example, TTB officials have said that manufacturers or importers may "layer" sales transactions by including a preliminary transaction at a low price before the sale to the wholesaler or distributor and using this low initial price to calculate the tax.<sup>9</sup>

### How has federal tobacco tax revenue changed over the past 10 years?

Revenue from federal excise taxes on cigarettes, roll-your-own tobacco, pipe tobacco, and cigars decreased from approximately \$14 billion in fiscal year 2014 to \$9 billion in fiscal year 2024 (see fig. 3). Taxes on cigarettes account for most of this revenue, although the percentage has decreased from about 94 percent of total tobacco tax revenue in fiscal year 2014 to 90 percent in fiscal year 2024. The percentage of tobacco tax revenue collected from roll-your-own tobacco and pipe tobacco has remained between 1.3 and 1.5 percent annually, while the percentage of revenue from cigars has increased from 5 percent in fiscal year 2014 to nearly 9 percent in fiscal year 2024.

**Figure 3: Revenue from Federal Excise Tobacco Taxes Has Declined, Fiscal Years 2014–2024**

Tax revenue has decreased as sales of smoking tobacco products have declined.



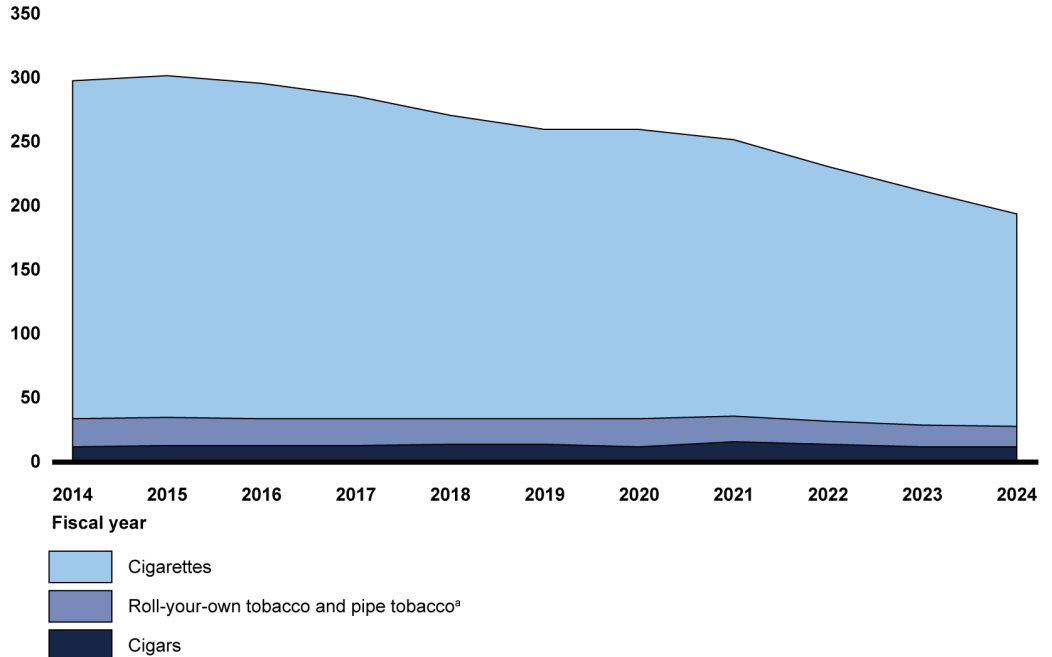
Source: GAO analysis of Department of the Treasury and Customs and Border Protection data. | GAO-25-107903

Notes: These amounts include tax revenue from cigarettes, roll-your-own tobacco, pipe tobacco, and cigars, but not smokeless tobacco products. Treasury could not provide data about pipe tobacco imports for fiscal years 2018 and 2020 because of taxpayer privacy considerations. We estimated the amount of revenue from pipe tobacco imports for these years by averaging the amount collected the year before and the year after. In this figure, “sales” of smoking tobacco products refers to the amount of these products removed from a factory for distribution in the U.S. or released from Customs custody.

The decline in tobacco tax revenue over the past 10 years has coincided with decreasing U.S. sales of smoking tobacco products over the same period (see fig. 4). Overall smoking rates have declined for various reasons, according to industry experts. One reason given for the decline is that some states and localities, such as California and Massachusetts, have a ban on the sale of most tobacco with flavor additives, including menthol.<sup>10</sup> Increased investment in national media campaigns against smoking has also contributed to declining smoking rates, according to researchers from a nongovernmental organization focused on tobacco use.

**Figure 4: U.S. Sales of Cigarettes, Roll-Your-Own Tobacco, Pipe Tobacco, and Cigars Declined, Fiscal Years 2014–2024**

Number sold (per year in billions of sticks)



Source: GAO analysis of Department of the Treasury and Customs and Border Protection data. | GAO-25-107903

Note: In this figure, “sales” are represented by the amount of these products removed from a factory for distribution in the U.S. or released from Customs custody. Treasury could not provide data about pipe tobacco imports for fiscal years 2018 and 2020 because of taxpayer privacy considerations. We estimated the amount of pipe tobacco imports for these years by averaging the ratio of imports to domestic sales from the prior and following years.

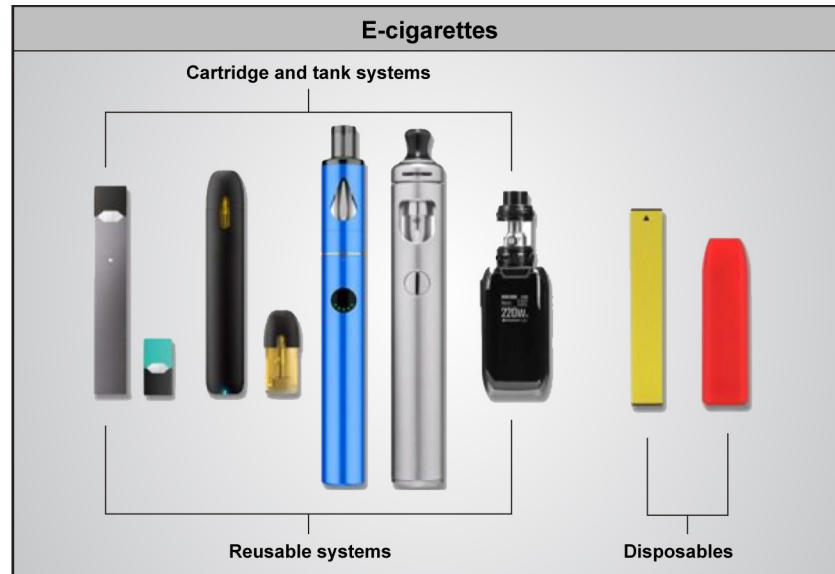
<sup>a</sup>Because roll-your-own tobacco and pipe tobacco are taxed based on weight, we converted weight to cigarette stick equivalent using the Tobacco Master Settlement Agreement conversion rate that is based on the weight of 0.0325 ounces of roll-your-own tobacco per cigarette stick. In 1998, 46 states signed the Tobacco Master Settlement Agreement with the four largest U.S. tobacco companies to settle state tobacco-related lawsuits and recover billions of dollars in costs associated with smoking-related illnesses.

Cigarette sales continue to dominate the smoking tobacco products market, but sales have decreased 37 percent since 2014. Other smoking tobacco products—roll-your-own tobacco, pipe tobacco, and cigars—have become a slightly larger share of the market. From fiscal year 2014 through fiscal year 2024, combined sales of cigars, roll-your-own tobacco, and pipe tobacco increased from 12 percent to 14 percent of total smoking tobacco product sales.

### What effect have e-cigarettes had on the market for traditional smoking tobacco products?

The use of electronic cigarettes, often called “e-cigarettes,” has grown in recent years, but how much this has affected the market for traditional smoking tobacco products is unknown.<sup>11</sup> E-cigarettes are a type of electronic nicotine delivery system (ENDS) product, a category of products that also includes vapes, vape pens, e-cigars, and similar products that use an “e-liquid” usually containing nicotine derived from tobacco as well as flavorings and other ingredients, according to the U.S. Food and Drug Administration. ENDS products may be rechargeable (or reusable) if they contain parts such as refillable cartridges. Some ENDS products are disposable, or intended to be disposed not refilled, once the e-liquid is consumed (see fig. 5).

**Figure 5: Examples of Electronic Cigarette, or “E-cigarette,” Products, Which Are Not Federally Taxed**



Source: U.S. Food and Drug Administration. | GAO-25-107903

Whether e-cigarettes are substitutes for traditional smoking tobacco products or if they lead to dual use among consumers of those products is unclear, according to industry experts and relevant studies. Comprehensive data for e-cigarette sales are limited, making it challenging to determine the overall effect of these products on the traditional smoking tobacco market. For example, a researcher from a nongovernmental organization specializing in tobacco and nicotine research said that estimating the size of the overall e-cigarette market is difficult because reliable data are not available about the size of the market share of specialty vape, cigar, and tobacco shops nor about the size of the online market. However, available sales data cited in literature provide some insights into the prevalence of e-cigarettes.

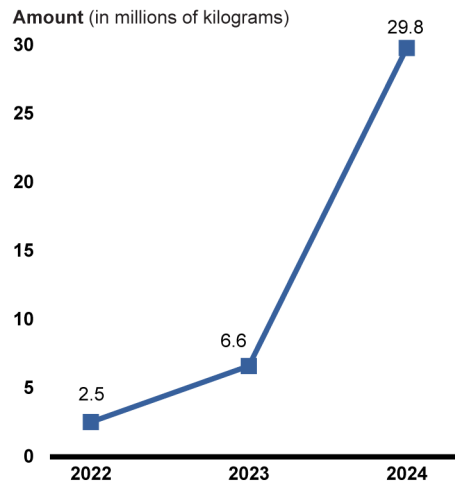
According to literature about e-cigarettes, data show that the use of all types of e-cigarettes, which are not currently taxed under the Internal Revenue Code as tobacco products, has increased in recent years.<sup>12</sup> The first e-cigarettes became available in 2007 and initially experienced slow market growth, but have since gained popularity.<sup>13</sup> As of 2021, e-cigarettes were the second most common tobacco product in the U.S.<sup>14</sup> A 2024 study found that between 2019 and 2023, e-cigarette sales increased 47 percent—from about 211 million units to about 309 million units.<sup>15</sup>

In particular, research has shown that notable increases in sales of disposable e-cigarettes occurred after the U.S. Food and Drug Administration announced guidance in 2020 to prioritize enforcement against certain flavors of prefilled cartridges for reusable e-cigarettes, among other ENDS products.<sup>16</sup> An expert explained disposable e-cigarettes became more popular in part because of this ban on most flavored reusable e-cigarettes. According to industry experts, most e-cigarettes are imported, and CBP data show disposable e-cigarette imports increased 1,080 percent from 2022 through 2024 (see fig. 6).



**Figure 6: Imports of Disposable E-Cigarettes Dramatically Increased, 2022–2024**

In 2024, more than 90 percent of imported, disposable e-cigarettes were from China, according to trade data.



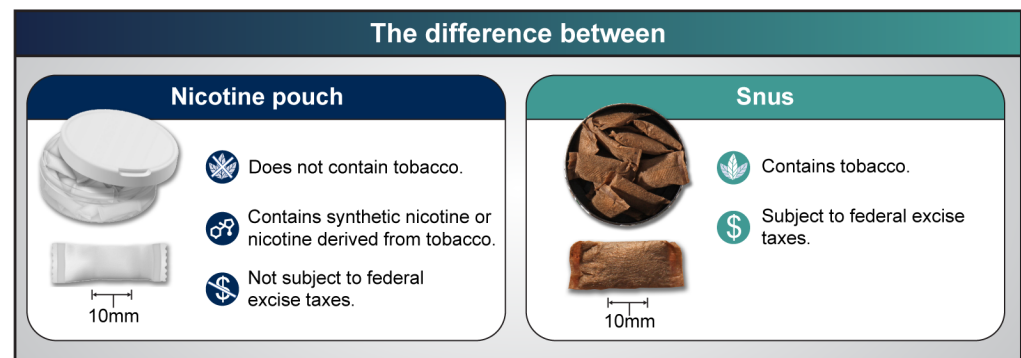
Source: GAO analysis of data from the USA Trade Online database maintained by the U.S. Census Bureau (accessed May 2025). | GAO-25-107903

### What effect have oral smokeless products had on the market for traditional smoking products?

The use of oral smokeless products, particularly nicotine pouches, has grown in recent years, but how much these products have affected the market for traditional smoking tobacco products is unclear. Oral smokeless products include snuff and chewing tobacco as well as tobacco and nicotine pouches, which are marketed as safer products and have been popularized by brands such as ZYN, Velo, and On!.<sup>17</sup>

Some oral smokeless products that contain tobacco, specifically chewing tobacco and snuff, are taxed under the Internal Revenue Code as tobacco products. Other products that have grown in popularity, such as nicotine pouches, may contain synthetic nicotine or nicotine derived from tobacco and are not taxed under the Internal Revenue Code as tobacco products. Figure 7 shows the difference between oral smokeless pouches that contain tobacco (also known as snus) and oral nicotine pouches.<sup>18</sup>

**Figure 7: Examples of Oral Smokeless Pouches**



Source: GAO (data); GAO (icons); U.S. Food and Drug Administration (photo); Arra Vais/stock.adobe.com.(photo) | GAO-25-107903

The U.S. market for oral smokeless products, particularly nicotine pouches, has grown since 2019, according to sales data, industry stakeholders, and company shareholder reports. According to one study, overall sales of nicotine pouches increased from about 126 million units during the last 5 months of 2019 to about



808 million units during the first 3 months of 2022.<sup>19</sup> Sales have continued to increase since then, according to industry experts. In March 2024, sales of nicotine pouches surpassed the combined sales of the top two e-cigarette brands, according to a nongovernmental organization specializing in tobacco and nicotine research.

According to tobacco industry experts, oral smokeless products have gained popularity in part because they are marketed as a safer alternative to traditional smoking tobacco products. For instance, an expert said that oral pouches containing synthetic nicotine are marketed as being designed to introduce the least amount of harmful particles into the body. Another expert told us that social media videos may likely normalize the use of oral nicotine pouches in youth while driving sales and market growth.

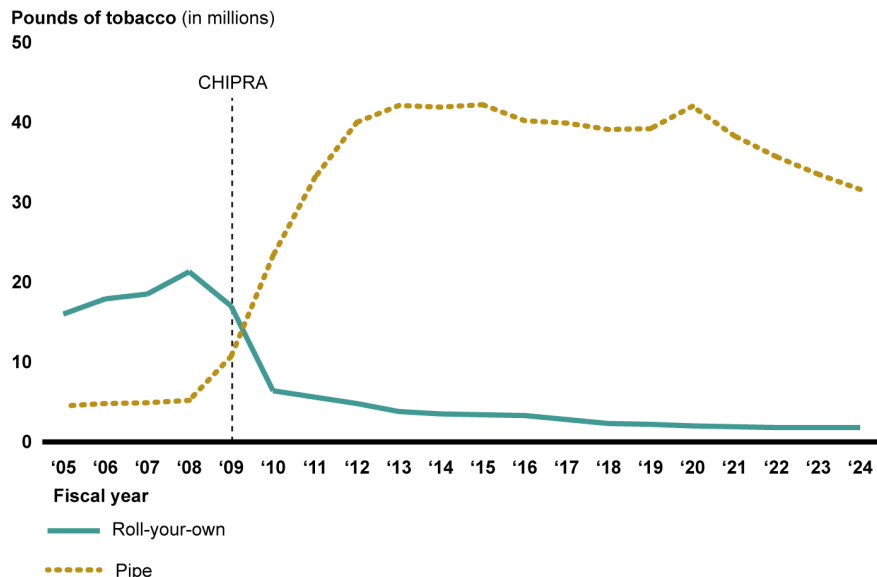
However, the extent to which oral smokeless products has affected the market for traditional smoking tobacco products is unclear because the data are not available. Determining the effect of these products is also complicated because consumers of oral smokeless products may be dual- or triple-users of other tobacco products (such as cigarettes and e-cigarettes), according to industry experts.

### How has the market for pipe tobacco and roll-your-own tobacco changed since CHIPRA?

CHIPRA's disparity in tax rates for similar types of tobacco created opportunities for tax avoidance and led to market shifts from the higher-taxed roll-your-own tobacco to the lower-taxed pipe tobacco that have continued through fiscal year 2024.<sup>20</sup> Following CHIPRA's enactment in 2009, pipe tobacco sales increased while roll-your-own tobacco experienced a steep drop in sales (see fig. 8). Roll-your-own tobacco's share of the combined roll-your-own and pipe tobacco market decreased from approximately 78 percent in fiscal year 2008 (before CHIPRA) to 5 percent in fiscal year 2024.

**Figure 8: U.S. Sales of Roll-Your-Own and Pipe Tobacco Before and After the Children's Health Insurance Program Reauthorization Act (CHIPRA) of 2009**

CHIPRA created tax disparities that led to an increase in sales of pipe tobacco and a decrease in sales of roll-your-own tobacco.



Source: GAO analysis of Department of the Treasury and Customs and Border Protection data. | GAO-25-107903

Notes: CHIPRA was signed in February 2009 and the tobacco tax provisions took effect in April 2009. Pub. L. No. 111-3, § 701(i), 123 Stat. 8, 108.

In this figure, “sales” are represented by the amount of these products removed from a factory for distribution in the U.S. or released from Customs custody. The information above reflects two different datasets. In 2021, Treasury’s Alcohol and Tobacco Tax and Trade Bureau (TTB) changed its methodology for capturing the quantities of imported roll-your-own tobacco and pipe tobacco to be more precise. However, data prior to 2013 were no longer available. One dataset used the previous methodology for fiscal year 2005 through fiscal year 2012 and the other used the updated methodology for fiscal year 2013 through fiscal year 2024. TTB could not provide data about pipe tobacco imports for fiscal years 2018 and 2020 because of taxpayer privacy considerations. We estimated the amount of pipe tobacco imports for these years by averaging the ratio of imports to domestic sales from the prior and following years.

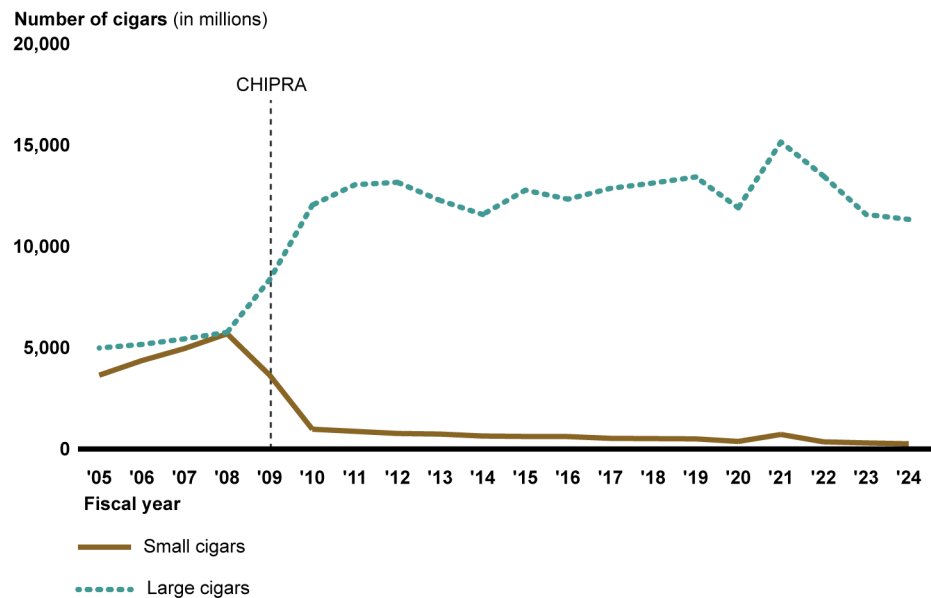
Although pipe tobacco and roll-your-own tobacco are similar, pipe tobacco is taxed at a lower rate; therefore, consumers who hand roll cigarettes may have an incentive to use pipe tobacco. The tax disparity is the primary reason the markets for the two tobacco types shifted in 2009, according to experts from a nongovernmental organization. In fiscal year 2024, the average price of pipe tobacco was \$2.90 per ounce including excise tax, while roll-your-own tobacco averaged \$4.53 per ounce.<sup>21</sup> By purchasing pipe tobacco rather than roll-your-own tobacco, consumers would save more than \$1.50 per ounce. The tax disparity also provided an incentive for manufacturers to switch from manufacturing roll-your-own tobacco to pipe tobacco. One expert told us the change in labeling tobacco packages as pipe tobacco rather than roll-your-own tobacco seemed to happen “overnight.”

## How has the market for cigars changed since CHIPRA?

CHIPRA’s disparity in tax rates between types of cigars also created opportunities for tax avoidance and led to market shifts from small cigars to large cigars that have continued through fiscal year 2024.<sup>22</sup> Large cigar sales increased from approximately 50 percent of the combined cigar market in fiscal year 2008 (before CHIPRA) to approximately 98 percent by the end of fiscal year 2024 (see fig. 9).

**Figure 9: U.S. Sales of Large and Small Cigars Before and After the Children’s Health Insurance Program Reauthorization Act (CHIPRA) of 2009**

CHIPRA created tax disparities that led to an increase in sales of large cigars and a decrease in sales of small cigars.



Source: GAO analysis of Department of the Treasury and Customs and Border Protection data. | GAO-25-107903

Notes: CHIPRA was signed in February 2009 and the tobacco tax provisions took effect in April 2009. Pub. L. No. 111-3, § 701(i), 123 Stat. 8, 108.

In this figure, “sales” are represented by the amount of these products removed from a factory for distribution in the U.S. or released from Customs custody. The information above reflects two different datasets. In 2021, Treasury’s Alcohol and Tobacco Tax and Trade Bureau changed its methodology for capturing the quantities of imported large and small cigars to be more precise. However, data prior to 2013 were no longer available. One dataset used the previous methodology for fiscal year 2005 through fiscal year 2012 and the other used the updated methodology for fiscal year 2013 through fiscal year 2024.

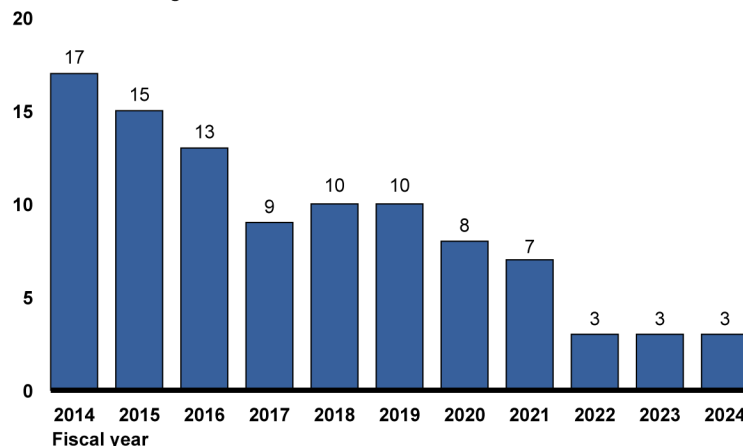
To reduce the amount of federal excise taxes they need to pay, manufacturers of inexpensive small cigars have an incentive to add weight to their product so that they qualify as lower-taxed large cigars.<sup>23</sup> Although small cigars and large cigars can be similar in appearance, they may be taxed at significantly different rates, depending on the price of the large cigar. For example, a manufacturer of cigars with a sale price of \$50 per thousand would pay \$50.33 per thousand in taxes if the cigars qualified as small cigars compared to \$26.38 per thousand if they qualified as large cigars. Consequently, this manufacturer would experience a tax savings of \$23.95 per thousand if its product qualified as a large cigar.

The number of domestic manufacturers of small cigars has decreased with the decline in small cigar sales, as shown in figure 10. In fiscal year 2014, 17 domestic manufacturers reported producing small cigars to TTB. Since fiscal year 2022, three domestic manufacturers have reported doing so.

**Figure 10: The Number of Domestic Small Cigar Manufacturers Has Decreased Since Fiscal Year 2014**

Over this time period, U.S. sales of small cigars have declined.

Domestic small cigar manufacturers



Source: Department of the Treasury data. | GAO-25-107903

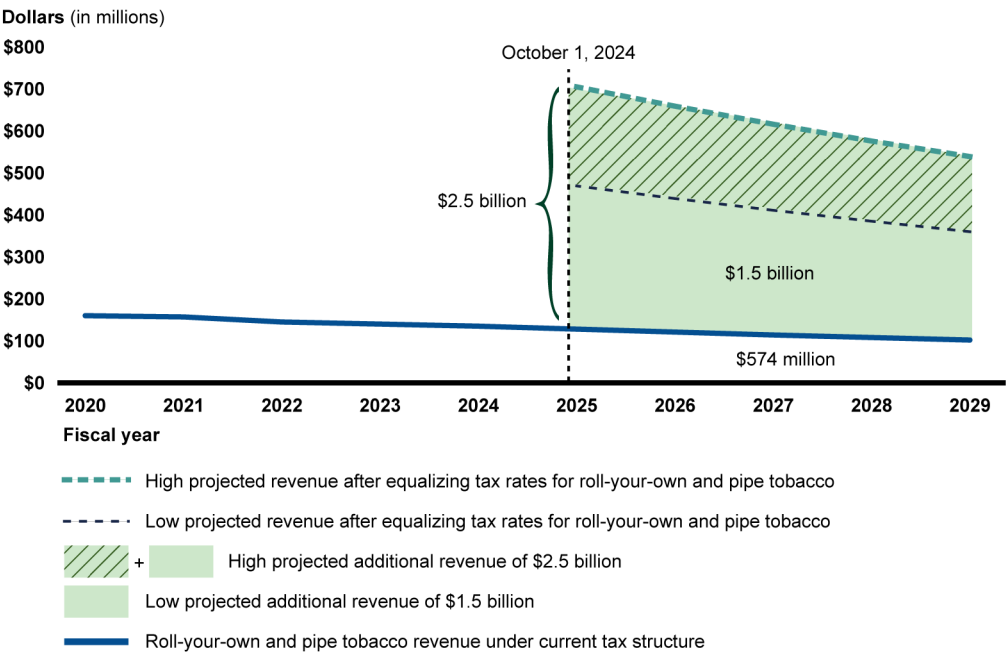
The makeup of large cigar sales also changed after CHIPRA, with imports replacing domestic cigars as the main contributor to the large cigar market. When CHIPRA took effect in 2009, domestic cigars made up more than 93 percent of the large cigar market. After CHIPRA, the large cigar market began to shift in favor of imports, and imported cigars consistently became the majority product in the large cigar market by 2017. In fiscal year 2024, imported cigars made up 76 percent of the large cigar market. According to CBP data, 79 percent of imported large cigars in 2024 had an importer’s sale price of less than 15 cents per stick, the least expensive value category of imported large cigars.

How much additional revenue could the federal government collect were Congress to tax pipe tobacco at the same rate as roll-your-own tobacco?

We estimated that federal revenue would increase by at least \$1.5 billion from fiscal year 2025 through fiscal year 2029 if the pipe tobacco tax rate were increased to the higher rate for roll-your-own tobacco and cigarettes.<sup>24</sup> We estimate that under current tax rates, the federal government would collect approximately \$574 million in federal excise taxes from domestic and imported roll-your-own tobacco and pipe tobacco from fiscal year 2025 through fiscal year 2029.

If Congress were to increase the federal excise tax rate on pipe tobacco from \$2.83 per pound to the higher roll-your-own tobacco rate of \$24.78 per pound, we estimate that the federal government could collect an additional \$1.5 to \$2.5 billion in revenue (see fig. 11). A total of between \$2.1 and \$3.1 billion could be collected for both products over 5 years if the tax rate for pipe tobacco were increased to the roll-your-own tobacco rate. These estimates depend on assumptions about how much less tobacco consumers would purchase in response to the price increase from higher taxes.<sup>25</sup>

Figure 11: Estimated Revenue over 5 Years Were Congress to Equalize Federal Excise Tax Rates for Roll-Your-Own and Pipe Tobacco as of Fiscal Year 2025



Source: GAO analysis of data from the Department of the Treasury, Customs and Border Protection, and Bureau of Labor Statistics. | GAO-25-107903

Note: The estimated tax revenue lines project tax revenue if federal excise tax rates on roll-your-own and pipe tobacco had been equalized on October 1, 2024. The projection of the current tax structure is based on extending into the future the most recent 5-year historic trend for roll-your-own and pipe tobacco sales. "Sales" of roll-your-own and pipe tobacco refers to the amount of these products removed from a factory for distribution in the U.S. or released from Customs custody. The projection of tax revenue after equalizing roll-your-own and pipe tobacco tax rates is adjusted downward based on the consumer response in quantity demanded to the tax increase and then follows the same 5-year historic trend. The high estimate uses a price elasticity of -0.2 while the low estimate uses a price elasticity of -0.9. The revenue differential is calculated as the annual difference between each scenario and the projected revenue under the current tax structure.

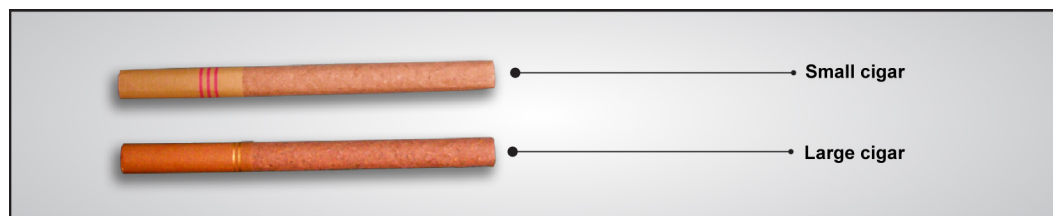
**How much additional revenue could the federal government collect were Congress to establish a minimum tax rate for large cigars equal to the small cigar rate?**

Federal revenue from tobacco taxes would likely increase if the minimum tax rate for large cigars were the same as the small cigar rate. However, a precise estimate is challenging to determine because of limited information about the retail prices of large cigars and consumer response to increased taxes. In particular, the average retail price of large cigars that are currently taxed at a lower rate than small cigars cannot be estimated because public data are limited. If the average retail price of these cigars were 12 cents a stick, we estimate that the federal government could collect \$374 to \$510 million in additional revenue from fiscal year 2025 through fiscal year 2029.<sup>26</sup>

Despite being similar in appearance, the ad valorem tax rate results in some large cigars having a lower tax rate than small cigars depending on their price (see fig. 12). Currently, small cigars are taxed at \$50.33 per thousand sticks. The tax rate on large cigars is calculated at a fixed percentage of the manufacturer's or importer's sale price—up to a maximum tax of 40.26 cents per cigar.<sup>27</sup> Because of these different tax rates, large cigars with a manufacturer's or importer's sale price of less than about 9.5 cents per cigar have a lower tax rate than small cigars. In fiscal year 2024, approximately 75 percent of domestic large cigars and 42 percent of imported large cigars were taxed at a lower rate than small cigars.

**Figure 12: Examples of Large and Small Cigars**

Although large and small cigars may appear similar, they are categorized differently for tax purposes based on their weight.



Source: GAO (photo). | GAO-25-107903

Note: Under the Internal Revenue Code, small and large cigars are differentiated by a weight threshold. Small cigars are defined as weighing 3 pounds or less per thousand sticks and large cigars are defined as weighing more than 3 pounds per thousand sticks.

Under current tax rates, we estimate the federal government would collect \$495 million over 5 years for this subset of large cigars—those taxed a rate lower than small cigars. If a minimum tax rate for large cigars were established equal to the small cigar rate as of fiscal year 2025, the federal government could collect additional tax revenue from these large cigars. For example, if the average retail price of these cigars were 12 cents per stick, the federal government could collect an additional \$374 to \$510 million over 5 years. These estimates depend on assumptions about how many fewer cigars consumers would purchase in response to the price increase from higher taxes.<sup>28</sup>

**How much revenue has been refunded through drawback claims for tobacco products since 2019?**

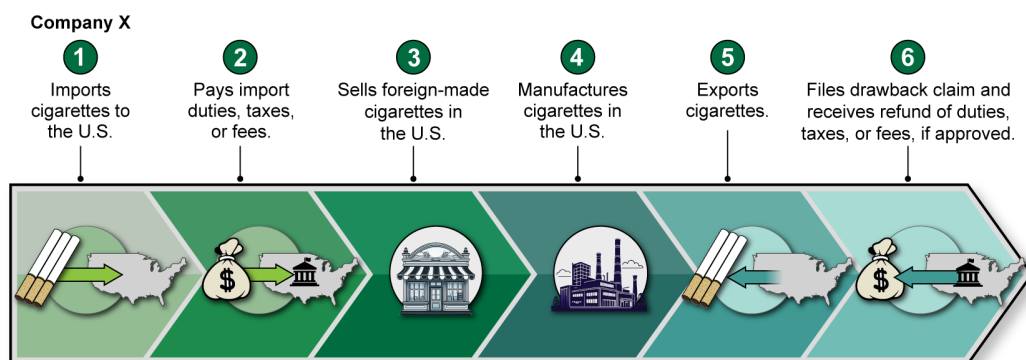
Both the requested and approved amounts of drawback refunds for smoking tobacco products have generally increased since fiscal year 2020. Overall, the federal government refunded about \$312 million in tobacco taxes through drawbacks from fiscal year 2019 through fiscal year 2024. A drawback refund is a remittance of up to 99 percent of duties, taxes, or fees previously paid by an importer.<sup>29</sup> We reported in 2019 that the Trade Facilitation and Trade Enforcement Act of 2015 modernized and expanded eligibility for the drawback

program, making it easier for companies to qualify for certain drawback refunds, according to CBP officials.<sup>30</sup>

Although various types of drawback refunds exist, tobacco companies primarily used substitution unused merchandise drawback for tobacco products from fiscal year 2019 through fiscal year 2024.<sup>31</sup> This type of drawback refund may be claimed on goods that were exported (or destroyed under CBP supervision) without being used and were substituted for imported merchandise meeting the appropriate criteria (see fig. 13).<sup>32</sup>

### Figure 13: Example of a Substitution Unused Merchandise Drawback Refund Claim upon Exportation

If a U.S. company imports and exports similar, qualifying goods, it generally may file a substitution unused merchandise drawback refund claim for the duties, taxes, or fees paid on the imported goods.

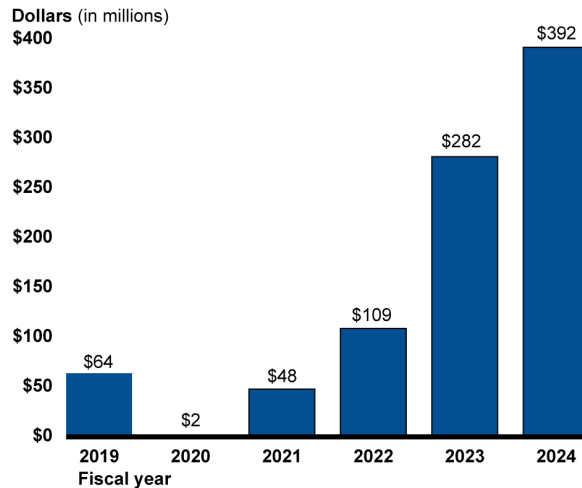


Source: GAO analysis of 19 U.S.C. § 1313 as amended by Pub. L. No. 114-125, § 906, 130 Stat. 124, 226-234 (Feb. 24, 2016) (data); GAO (icons). | GAO-25-107903

Note: Eligibility for payment of drawback claim depends on meeting statutory criteria in 19 U.S.C. § 1313.

Since fiscal year 2020, companies have requested increasing amounts of drawback refunds for smoking tobacco products, according to CBP data.<sup>33</sup> In fiscal year 2020, companies requested approximately \$2 million. The amounts requested have steadily increased since then, and companies requested about \$392 million in drawback refunds for smoking tobacco products in fiscal year 2024 (see fig. 14). From fiscal year 2019 through fiscal year 2024, companies requested approximately \$898 million in drawback refunds for smoking tobacco products.

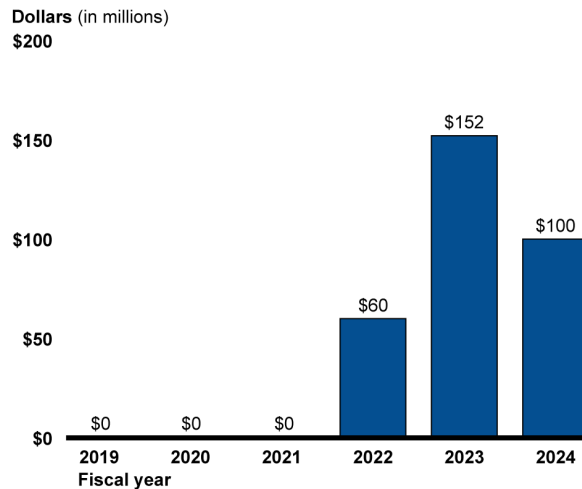
**Figure 14: Drawback Refunds Requested for Smoking Tobacco Products Have Generally Increased, Fiscal Years 2019–2024**



Source: GAO analysis of Customs and Border Protection data. | GAO-25-107903

From fiscal year 2019 through fiscal year 2024, the amount of taxes refunded through drawback claims for smoking tobacco products totaled about \$312 million (see fig. 15).<sup>34</sup>

**Figure 15: Amount of Taxes Refunded Through Drawback Claims for Smoking Tobacco Products, Fiscal Years 2019–2024**



Source: GAO analysis of Customs and Border Protection data. | GAO-25-107903

Note: The Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) modernized and generally expanded eligibility for the drawback program. See Pub. L. No. 114-125, § 906, 130 Stat. 122, 226-234. CBP began accepting TFTEA drawback claims in February 2018. According to officials, CBP did not liquidate any drawback refunds for tobacco taxes from May 2020 through October 2021 in response to a Court of International Trade injunction which paused the liquidation of certain claims for drawback of internal revenue tax. See *Nat'l Ass'n of Mfrs. v. U.S. Dep't of the Treasury*, No. 19-00053 (Ct. Int'l Trade May 22, 2020) (order enjoining liquidation of certain claims for drawback). Officials said the reason the data show no liquidated refunds prior to the injunction may be because drawback claims filed before February 24, 2019, when claims were required to be filed electronically, may not have included the same tariff information.

Processing drawback claims takes at least 18 months, according to CBP officials. This timeframe includes a year for CBP to classify and value the imported goods and validate the amount of duties, taxes, and fees as well as a 180-day period during which the drawback claimant can protest CBP's findings. Officials said that the process may be longer in some cases because of limited agency resources or a claim's complexities or size. In addition, importers generally have



5 years from the date of import to submit drawback claims, including claims for substitution unused merchandise.<sup>35</sup>

Further, drawback claims may be denied, or the total requested amount may not be approved, according to CBP officials.<sup>36</sup> Officials explained that drawback claims or requested refund amounts may be denied for various reasons, such as a lack of supporting documentation or insufficient proof of qualifying exports.

Although companies have requested increasing amounts of drawback refunds for smoking tobacco products, our analysis showed the potential amount of refunded taxes could not be more than \$600 million annually for fiscal year 2019 through fiscal year 2024 and would likely be less. Drawback refunds cannot exceed 99 percent of the duties, taxes, or fees paid by importers. In addition, nearly all the taxes refunded for smoking tobacco products through drawback claims during this time were for cigarettes, according to CBP data.<sup>37</sup> From fiscal year 2019 through fiscal year 2024, taxes collected on imported cigarettes averaged about \$441 million, ranging from about \$312 million in fiscal year 2023 to about \$595 million in fiscal year 2020, according to TTB data.

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## Agency Comments

We provided a draft of this report to CBP, Labor, and Treasury for review and comment. CBP and Treasury provided technical comments, which we incorporated as appropriate.

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## How GAO Did This Study

To address the questions in this study, we reviewed documents and interviewed agency officials from the Department of the Treasury's Alcohol and Tobacco Tax and Trade Bureau (TTB), the Department of Homeland Security's U.S. Customs and Border Protection (CBP), and the Department of Labor's Bureau of Labor Statistics (BLS). We also interviewed researchers from three nongovernmental organizations and representatives from three industry associations and customs brokers working on tobacco, taxation, and import and export issues to obtain information on markets, industry practices, and consumer trends for tobacco products. We identified these organizations, associations, and brokers by reviewing our prior work on the topics and using an expert referral process. We selected these groups to ensure a range of views.

To describe trends in the markets for cigarettes, roll-your-own tobacco, pipe tobacco, and cigars as well as the effect of e-cigarettes and oral smokeless products on these markets, we reviewed relevant studies, reports, and other documents. We searched research databases, including Scopus and ProQuest, to identify academic studies, industry articles, and think tank reports published about these topics since 2019 when we last reported on tobacco taxes. We analyzed TTB domestic removals data and CBP imports data to describe how sales trends for these products and associated federal revenue from excise taxes had changed over the past 10 years. The import data did not include personal imports or imports where \$10 or less in excise tax was paid. TTB officials said that these types of imports constituted less than 0.02 percent of tobacco imports in fiscal year 2024.

TTB could not provide data about pipe tobacco imports for fiscal years 2018 and 2020 because of taxpayer privacy considerations. We estimated the amount of pipe tobacco imports for these years by averaging the ratio of imports to domestic sales from the prior and following years. We estimated the amount of revenue from pipe tobacco imports for these years by averaging the revenue collected on these imports during the previous and following years. To assess

the reliability of these data, we reviewed the data for inconsistencies and completeness, interviewed knowledgeable agency officials, and reviewed data reliability assessments from our prior reports that used these data for similar purposes. We determined the data were sufficiently reliable for describing trends in U.S. sales of and federal revenue collected from excise taxes on smoking tobacco products.

We identified market shifts among smoking tobacco products by analyzing these sales data to identify trends before and after the tax rate changes from the Children's Health Insurance Program Reauthorization Act of 2009. Further, we analyzed federal taxes collected from these sales to describe how revenue had changed since fiscal year 2014. In addition, we reviewed price data from BLS for pipe tobacco and roll-your-own tobacco and data from TTB about the number of domestic, small cigar manufacturers.

To describe the size of the e-cigarette market, we examined data about e-cigarette devices and parts imported from 2022 through 2024. Sales data on e-cigarettes are limited, but imports make up most of the U.S. e-cigarette market, according to industry experts. We analyzed imports data that were available in May 2025 from the USA Trade Online database maintained by the U.S. Census Bureau.<sup>38</sup> Specifically, we analyzed the quantity of imports of the seven statistical reporting numbers for disposable e-cigarettes from 2022 through 2024. We assessed the reliability of these data by reviewing relevant documentation and examining the data for inconsistencies and completeness. We determined that the data were sufficiently reliable for describing trends about e-cigarette imports.

To calculate the potential effect on federal tax revenue from raising the tax rate for pipe tobacco to match that of roll-your-own tobacco, we adjusted the pipe tobacco tax rate to the roll-your-own tobacco tax rate of \$24.78 per pound. Our methodology draws from Dr. Frank Chaloupka's model calculating the effect of raising cigarette taxes in Illinois State.<sup>39</sup> This methodology projects the effect of a future tax increase based on the historic sales trend, amount of the tax, and price elasticity of demand. Under this model, when a tax increase is enacted, demand for the product is expected to decline based on the price elasticity and effect on prices. Following this initial decline, demand for the product is expected to continue at the rate of its historic sales trend.

Our model assumes that taxes would have been equalized as of October 1, 2024, and calculates the cumulative revenue differential for 5 fiscal years through September 2029. We assumed that these increased taxes would be fully passed onto consumers as increased prices. The model takes into account the additional reduction in consumption because of the tax increase and estimates potential revenue differentials. We used price elasticities of -0.2 and -0.9 to denote the range of potential tax revenue outcomes. In particular, the price elasticity of -0.9 was assumed to provide a conservative estimate. The higher elasticity of -0.9 would account for a larger drop in consumption including from shifts to other tobacco products. The range of elasticities is based on a literature review of studies published since 2019 and an interview with the Joint Committee on Taxation.

After the drop in demand because of the tax increase, future demand was projected linearly using the most recent 5-year historic trend. The projection of future sales under the current tax rate was calculated by applying the same historic trend to the fiscal year 2024 sales of roll-your-own and pipe tobacco.

Projected revenue was calculated by multiplying the applicable tax rates with the projected sales.

The BLS price data used in our analysis are a subset of the data used for calculating the Consumer Price Index for tobacco products. The data are collected from a sample of consumers representing over 90 percent of the urban population. The data do not include the spending patterns of people living in rural nonmetropolitan areas, farm households, institutions, religious communities, or on military installations. The BLS data contain retail price information collected each month throughout the U.S. These price data include excise taxes from federal, state, and local governments and exclude shipping, handling, sales tax, and fuel surcharges. Because the BLS data are at the retail level, there is an expected markup in addition to the charges mentioned above.

To simplify the model, we assumed that the markup remained constant after the equalization of taxes. To calculate the fiscal year average price, we took the unweighted average of BLS's observed product prices. We used the average price from fiscal year 2020 through fiscal year 2024 to reduce the potential effects of inflation during the period. We assessed the reliability of these data by reviewing the data for inconsistencies and completeness, interviewing knowledgeable BLS officials, and reviewing data reliability assessments from our prior reports that used these data for similar purposes. We determined that the data were sufficiently reliable to create an average price of pipe tobacco from fiscal year 2020 to fiscal year 2024.

To calculate the potential effect on tax revenue from establishing a minimum tax rate for large cigars equal to the small cigar tax rate, we followed a similar methodology as for the pipe tobacco analysis. In particular, we examined the effect of establishing a minimum tax rate for large cigars currently taxed at less than the small cigar tax rate of \$50.33 per thousand sticks. Because the tax rate on large cigars is calculated at 52.75 percent of the manufacturer's or importer's sale price up to a maximum tax, large cigars with a sale price of less than about 9.54 cents per stick are taxed at lower rate than small cigars. From fiscal year 2020 through fiscal year 2024, these cigars constituted between approximately 70 percent and 78 percent of domestic large cigars and between approximately 42 and 71 percent of imported large cigars, according to data provided by TTB. We modeled changing the tax rate of these large cigars from the ad valorem rate to a uniform \$0.05033 unit tax.

We made similar assumptions for the timing of the tax rate change and the evolution of demand as in the pipe tobacco analysis. Because the retail prices of these large cigars were not publicly available, we used an average price of 12 cents to approximate these cigars' retail price without taxes. We projected the fiscal year 2025 through fiscal year 2029 sale price using the fiscal year 2020 through fiscal year 2024 growth rates in the average tax paid for such cigars. The model similarly uses price elasticities of -0.2 and -0.9. We calculated projected revenue under the current tax rate by multiplying the ad valorem tax rate with the estimated price and projected sales. The revenue in the alternate scenarios were calculated by multiplying the new tax rate with the projected sales.

To examine the amount of revenue refunded by the federal government via drawbacks for smoking tobacco products, we analyzed CBP data about drawbacks for cigarettes, roll-your-own tobacco, pipe tobacco, and cigars from fiscal year 2019 through fiscal year 2024. Specifically, we analyzed (1) the value of refunds for duties, taxes, or fees requested by tobacco companies; (2) the

amounts of duties, taxes, or fees approved for refunds by CBP; and (3) the final liquidated amounts of tobacco taxes refunded by CBP.

Although the Trade Facilitation and Trade Enforcement Act (TFTEA) of 2015 was enacted in 2016, drawback claims under this act were not accepted until 2018. The act allowed a one-year transition period (from February 24, 2018, until February 23, 2019) in which drawback claimants could file claims under either the TFTEA drawback process or the previous process. Therefore, we examined data on drawback claims and approved refunds for tobacco products from fiscal year 2019 through fiscal year 2024. To assess the reliability of these data, we reviewed the data for inconsistencies and completeness and interviewed knowledgeable CBP officials. We determined the data were sufficiently reliable to describe trends in drawback claims for smoking tobacco products and to estimate the amount of federal tax revenue refunded through drawback claims for smoking tobacco products.

We conducted this performance audit from October 2024 to August 2025 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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## List of Addressees

The Honorable Lindsey Graham  
Chairman  
Committee on the Budget  
United States Senate

The Honorable Jeff Merkley  
Ranking Member  
Committee on the Budget  
United States Senate

The Honorable Mike Crapo  
Chairman  
Committee on Finance  
United States Senate

The Honorable Ron Wyden  
Ranking Member  
Committee on Finance  
United States Senate

The Honorable Rand Paul  
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Committee on Homeland Security and Governmental Affairs  
United States Senate

The Honorable Gary Peters  
Ranking Member  
Committee on Homeland Security and Governmental Affairs  
United States Senate

The Honorable Jodey Arrington  
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The Honorable Brendan Boyle  
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Committee on the Budget  
House of Representatives

The Honorable James Comer  
Chairman  
Committee on Oversight and Government Reform  
House of Representatives

The Honorable Robert Garcia  
Ranking Member  
Committee on Oversight and Government Reform  
House of Representatives

The Honorable Jason Smith  
Chairman  
Committee on Ways and Means  
House of Representatives

The Honorable Richard Neal  
Ranking Member  
Committee on Ways and Means  
House of Representatives

We are sending copies of this report to the appropriate congressional committees and the Secretaries of Homeland Security, Labor, and the Treasury, as well as other interested parties. In addition, the report is available at no charge on the GAO website at <https://www.gao.gov>.

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**Staff Acknowledgments:** Jeremy Latimer (Assistant Director), Daniela Rudstein (Analyst in Charge), Pedro Almoguera, Marc Rockmore, Mario Tiberie, Steve Brown, Jieun Chang, Chris Keblitis, Donna Morgan, and Alexa Stechschulte.

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<sup>1</sup>In this report, “sales” of smoking tobacco products refers to the number of these products removed from a factory for distribution in the U.S. or released from Customs custody. “Cigarettes” refers to small cigarettes in the context of tax rates and to large and small cigarettes in the context of sales and revenue. Although the Internal Revenue Code distinguishes between large and small cigarettes for tax purposes, the federal excise tax return does not. Similarly, statistical reporting numbers for imports do not distinguish between large and small cigarettes. Since at least fiscal year 2013, no domestic manufacturers have reported producing large cigarettes, according to Treasury officials.

<sup>2</sup>The tax rate on large cigars is calculated at 52.75 percent of the manufacturer’s or importer’s sale price—up to a maximum tax of 40.26 cents per cigar. 26 U.S.C. § 5701. Depending on this sale price, large cigars may have a lower tax rate than small cigars.

<sup>3</sup>Children’s Health Insurance Program Reauthorization Act of 2009, Pub. L. No. 111-3, § 701, 123 Stat. 8, 106–07.

<sup>4</sup>Small cigarettes and small cigars are taxed at a rate of \$50.33 per thousand sticks, while roll-your-own tobacco is taxed at \$24.78 per pound and pipe tobacco is taxed at \$2.83 per pound. The federal excise tax rate for large cigarettes up to 6.5 inches long is \$105.69 per thousand sticks. Large cigarettes over 6.5 inches long are taxed at the rate for small cigarettes but counting each 2.75 inches or fraction thereof in the length of each such cigarette as a separate stick. 26 U.S.C. § 5701.

<sup>5</sup>The tax rate on large cigars is calculated at 52.75 percent of the manufacturer’s or importer’s sale price—up to a maximum tax of 40.26 cents per cigar. 26 U.S.C. § 5701.

<sup>6</sup>Domestic manufacturers and importers of tobacco products must obtain a permit from Treasury before engaging in business. See 26 U.S.C. §§ 5712–13. The federal excise taxes on domestic tobacco products are determined when these products leave the manufacturing facilities and are paid to TTB with semimonthly tax returns. 26 U.S.C. § 5703(b); 27 C.F.R. §§ 40.161–162 (2025).

<sup>7</sup>26 U.S.C. § 5702.

<sup>8</sup>Department of the Treasury, Alcohol and Tobacco Tax and Trade Bureau, *Importation of Tobacco Products and Calculating the Tax on Imported Large Cigars*, Industry Circular, No. 2011-03 (April 26, 2011).

<sup>9</sup>TTB officials said that investigations of these cases could result in (1) accepting the pricing rationale with no tax consequences; (2) a determination that tax was based on a sale otherwise than through an arm’s length transaction and at less than a fair market price, resulting in additional tax liability; or (3) criminal case referrals. Since 2019, TTB has initiated and completed seven investigations related to large cigar taxes, resulting in \$1.1 million in additional federal excise tax liabilities, according to agency officials.

<sup>10</sup>Cal. Health & Safety Code § 104559.5 (Deering 2024); Mass. Ann. Laws ch. 270, § 28 (LexisNexis 2024).

<sup>11</sup>In 2022, the Federal Food, Drug, and Cosmetic Act definition of “tobacco product” was amended to include products containing nicotine from any source. 21 U.S.C. § 321(rr). In 2023, the U.S. Food and Drug Administration updated its regulations to reflect this definition of tobacco products. 21 C.F.R. § 1100.3. However, the Internal Revenue Code still defines tobacco products as “cigars, cigarettes, smokeless tobacco, pipe tobacco, and roll-your-own tobacco.” 26 U.S.C. § 5702(c). GAO has previously reported on e-cigarettes. See GAO, *Science & Tech Spotlight: E-cigarettes*, GAO-20-610SP (Washington, D.C.: June 30, 2020).

<sup>12</sup>Some states tax ENDS products. As of September 2024, 33 states and the District of Columbia levied excise taxes on e-cigarettes or similar products, according to the U.S. Centers for Disease Control and Prevention.

<sup>13</sup>Richard O’Connor, et al., “Evolution of tobacco products: recent history and future directions,” *Tobacco Control* (2022).

<sup>14</sup>O’Connor, et al., “Evolution of tobacco products.”

<sup>15</sup>Truth Initiative and CDC Foundation, “Monitoring E-cigarette Trends in the United States” (2024).

<sup>16</sup>Fatma Romeh M Ali, et al., “E-cigarette Unit Sales by Product and Flavor Type, and Top-Selling Brands, United States, 2020–2022,” *Morbidity and Mortality Weekly Report* (2023). In 2020, the U.S. Food and Drug Administration described its intention to prioritize the agency’s enforcement against flavored e-cigarettes, excluding tobacco and menthol flavors, that are being marketed without the agency’s authorization. U.S. Food & Drug Admin., *Enforcement Priorities for Electronic Nicotine Delivery System (ENDS) and Other Deemed Products on the Market Without Premarket Authorization (Revised): Guidance for Industry* (2020).



<sup>17</sup>In January 2023, the U.S. Food and Drug Administration authorized the marketing of three new heated tobacco products, which experts said are popular abroad. Heated tobacco products, sometimes marketed as “heat-not-burn” products, heat processed tobacco leaf which allows users to inhale nicotine into their lungs, according to the U.S. Centers for Disease Control and Prevention. Heated tobacco products may be classified as taxable tobacco products under the Internal Revenue Code depending on the characteristics of the product, according to TTB officials.

<sup>18</sup>According to TTB officials, snus is classified as snuff and is federally taxed at the same rate of \$1.51 per pound. See 27 U.S.C. § 5701(e)(1). TTB officials said that the agency does not require companies to distinguish between products within the same tax classification, so granular data for snus are not available. In fiscal year 2024, TTB collected approximately \$143 million in federal excise taxes for smokeless tobacco products, including chewing tobacco, snuff, and snus.

<sup>19</sup>Anuja Majmundar, et al., “Nicotine Pouch Sales Trends in the US by Volume and Nicotine Concentration Levels from 2019 to 2022,” *JAMA Network Open* (2022).

<sup>20</sup>We have previously reported on these market shifts. See GAO, *Tobacco Taxes: Large Disparities in Rates for Smoking Products Trigger Significant Market Shifts to Avoid Higher Taxes*, GAO-12-475 (Washington, D.C.: Apr. 18, 2012); *Tobacco Taxes: Disparities in Rates for Similar Smoking Products Continue to Drive Market Shifts to Lower-Taxed Options*, GAO-14-811T (Washington, D.C.: July 29, 2014); and GAO, *Tobacco Taxes: Market Shifts toward Lower-Taxed Products Continue to Reduce Federal Revenue*, GAO-19-467 (Washington, D.C.: June 13, 2019). We have also discussed tobacco taxes in our annual reports on fragmentation, overlap, and duplication as opportunities for cost savings and revenue enhancement. For example, see GAO, *Additional Opportunities to Reduce Fragmentation, Overlap, and Duplication and Achieve Billions of Dollars in Financial Benefits*, GAO-24-106915 (Washington, D.C.: May 15, 2024).

<sup>21</sup>These prices are based on a subset of the data used in the Consumer Price Index for Tobacco Products Other Than Cigarettes. These data, provided by the Department of Labor’s Bureau of Labor Statistics, should be interpreted with care because they do not meet the agency’s standard publication criteria. For more information, see “How GAO Did This Study.”

<sup>22</sup>We have previously reported on these market shifts. See GAO-12-475, GAO-14-811T, and GAO-19-467.

<sup>23</sup>Under the Internal Revenue Code, small and large cigars are differentiated by a weight threshold. Small cigars weigh 3 pounds or less per thousand sticks and large cigars weigh more than 3 pounds per thousand sticks. 26 U.S.C. § 5701(a). In 2012, we reported that small cigar manufacturers could add weight by packing the tobacco more tightly. GAO-12-475.

<sup>24</sup>In 2019, we estimated the federal government could collect an additional \$1.3 billion from fiscal year 2019 through fiscal year 2024 if the tax rate for pipe tobacco were equalized with that of roll-your-own tobacco and cigarettes as of fiscal year 2019. See GAO-19-467. The current estimate is higher because pipe tobacco prices have increased since fiscal year 2019 and therefore the same amount of tax increase would have less of an effect on the final price paid by consumers, leading to a smaller decrease in quantity demanded.

<sup>25</sup>Price elasticity measures the sensitivity of consumer demand to price changes. For example, a price elasticity of demand of -0.9 means that when prices increase by 10 percent, demand will decrease by 9 percent. Our analysis showed that the federal government could collect an additional \$1.5 billion in excise tax revenue assuming a price elasticity of -0.9 and could collect an additional \$2.5 billion assuming a price elasticity of -0.2. For this estimate, we assumed that the fiscal year 2025 through fiscal year 2029 demand for roll-your-own tobacco and pipe tobacco would continue to decrease at the same average rate as it decreased from fiscal year 2020 through fiscal year 2024. See “How GAO Did This Study” for more information about our methodology.

<sup>26</sup>For information about the selection of this assumed average retail price, see “How GAO Did This Study.”

<sup>27</sup>According to TTB guidance, the sale price that determines the amount of excise tax for large cigars is generally the price that a manufacturer or importer sells the cigar in an arm’s length transaction to an unrelated party, typically a distributor or wholesaler. Department of the Treasury, Alcohol and Tobacco Tax and Trade Bureau, *Importation of Tobacco Products and Calculating the Tax on Imported Large Cigars*, Industry Circular, No. 2011-03 (April 26, 2011).

<sup>28</sup>Price elasticity measures the sensitivity of consumer demand to price changes. For example, a price elasticity of demand of -0.9 means that when prices increase by 10 percent, demand will decrease by 9 percent. If the retail price of this subset of large cigars—those taxed at less than the small cigar rate—were 12 cents per stick, we estimate the federal government could collect an additional \$374 million in excise tax revenue assuming a price elasticity of -0.9. If price elasticity were -0.2, the federal government could collect an additional \$510 million in tobacco tax revenue.



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For this estimate, we assumed that the fiscal year 2025 through fiscal year 2029 demand for these large cigars would continue to decrease at the same average rate as it decreased from fiscal year 2020 through fiscal year 2024. See “How GAO Did This Study” for more information about our methodology.

<sup>29</sup>In 2019, we reported that the rationale for the drawback program was to encourage American commerce and manufacturing, according to CBP officials. GAO, *Customs and Border Protection: Risk Management for Tariff Refunds Should Be Improved*, GAO-20-182 (Washington, D.C.: Dec. 17, 2019). The drawback program permits American manufacturers to compete in foreign markets without the handicap of including in their costs, and consequently in their sales price, the duty they paid on imported merchandise. See Customs Regulations Revision Relating To Drawback; Specialized and General Provisions, 48 Fed. Reg. 46740, 46741 (Oct. 14, 1983).

<sup>30</sup>GAO-20-182. Although the Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) was enacted on February 24, 2016, TFTEA drawback claims were not accepted until February 24, 2018. Pub. L. No. 114-125, § 906(q), 130 Stat. 122, 233-34. Additionally, the act allowed a one-year transition period in which drawback claimants could file claims under either the previous or new drawback processes. In 2018, CBP and Treasury issued a rule that finalized regulations clarifying the prohibition on the filing of certain substitution drawback claims, which effectively exempted some products (e.g., alcohol and tobacco) from certain drawback refunds. See Modernized Drawback, 83 Fed. Reg. 64942 (Dec. 18, 2018). In 2020, the Court of International Trade held challenged provisions of the rule unlawful, which the U.S. Court of Appeals for the Federal Circuit later affirmed. *Nat’l Ass’n of Mfrs. v. U.S. Dep’t of the Treasury*, 432 F. Supp. 3d 1381, 1381 (Ct. Int’l Trade 2020), *aff’d* 10 F.4th 1279, 1288 (Fed. Cir. 2021).

<sup>31</sup>See 19 U.S.C. § 1313(j)(2) (describing substitution unused merchandise drawback).

<sup>32</sup>In general, if a U.S. company exports an item with a Harmonized Tariff Schedule code identical to that of an item that the company imported, the company may claim a substitution unused merchandise drawback on the duties, taxes, or fees paid on the imported item, according to CBP officials. From fiscal year 2019 through fiscal year 2024, CBP also refunded approximately \$92,000 to U.S. tobacco companies for direct identification unused merchandise drawbacks, mainly for cigars. This type of drawback may be claimed on imported merchandise that was exported or destroyed under CBP supervision, without having been used in the U.S. 19 U.S.C. § 1313(j)(1).

<sup>33</sup>Companies requested about \$64 million for drawback refunds for smoking tobacco products in fiscal year 2019, according to CBP data. Industry experts told us drawback claims for tobacco products were likely lower in fiscal year 2020 due to uncertainty about drawback eligibility for certain products, which was clarified in 2021. See *Nat’l Ass’n of Mfrs.*, 432 F. Supp. 3d at 1381, *aff’d* 10 F. 4th at 1288.

<sup>34</sup>Although the refunds requested through drawback claims include duties, taxes, and fees paid on imported goods, these data only reflect the amount of tobacco taxes liquidated by CBP as drawback refunds.

<sup>35</sup>19 U.S.C. § 1313(r).

<sup>36</sup>Once a drawback claim is submitted to CBP, qualified companies may receive bond-guaranteed, accelerated payments for the requested amount, according to CBP officials. Officials explained that if CBP processes the drawback claim and determines the final refund amount is less than the amount requested, companies are required to return the difference to the federal government.

<sup>37</sup>From fiscal year 2019 through fiscal year 2024, 98 percent of drawback refunds for tobacco taxes were for cigarettes. This percentage ranged from 91 percent in fiscal year 2022 to about 100 percent in fiscal year 2024. CBP did not liquidate certain claims for tobacco tax drawback refunds from May 2020 to October 2021 in response to a federal court injunction, according to officials. See *Nat’l Ass’n of Mfrs. v. U.S. Dep’t of the Treasury*, No. 19-00053 (Ct. Int’l Trade May 22, 2020) (order enjoining liquidation of certain claims for drawback).

<sup>38</sup>See <https://usatrade.census.gov/>.

<sup>39</sup>Frank Chaloupka and Jidong Huang, *A Significant Cigarette Tax Rate Increase in Illinois Would Produce a Large, Sustained Increase in State Tobacco Tax Revenues* (Chicago: University of Illinois at Chicago, Jan. 3, 2011).