

**SWISHER INTERNATIONAL, INC.**

December 10, 2004

John M. Truluck III  
Director, Tobacco Division  
Farm Service Agency  
United States Department of Agriculture (USDA)  
STOP 0514, Room 4080-S  
1400 Independence Avenue, SW  
Washington, DC 20250-0514

Dear Director Truluck:

Attached please find written comments submitted on behalf of Swisher International, Inc. in relation to the implementation of the Fair and Equitable Tobacco Reform Act of 2004. These comments are submitted pursuant to the November 17, 2004 *Federal Register* Notice (69 F.R. 67298) published by the Commodity Credit Corporation.

We look forward to working with you in the weeks ahead as several key decisions are made with respect to the administration of this important legislation. Thanks for your attention to this matter.

Sincerely,

A handwritten signature in blue ink that reads "Tom Ryan". The signature is fluid and cursive, with the first name "Tom" being particularly prominent.

Tom Ryan  
Executive Vice President  
Swisher International, Inc.

Comments of Swisher International, Inc.  
On the Implementation of the  
Fair and Equitable Tobacco Reform Act of 2004

Before the Department of Agriculture  
Commodity Credit Corporation  
Farm Service Agency

December 10, 2004

Submitted to:  
Director, Tobacco Division  
Farm Service Agency  
United States Department of Agriculture  
STOP 0515, Room 4080-S  
1400 Independence Ave., SW  
Washington, D.C. 20250-0514

## I. Background

Swisher International, Inc. ("Swisher") is one of the largest manufacturers of cigars and smokeless tobacco products in the world. Swisher is headquartered in Jacksonville, Florida and has been in operation for 141 years. Its products include quality cigars and smokeless items in all price categories, including popular priced cigars, handmade and imported cigars, moist snuff and loose leaf chewing tobacco brands. Swisher is a member of the Cigar Association of America ("CAA"), and fully supports the views expressed in the written comments submitted today by the CAA regarding the implementation of the Fair and Equitable Tobacco Reform Act ("FETRA") of 2004 (Pub. L. 108-357). The additional comments herein are intended to supplement those views.

FETRA was enacted on October 22, 2004. The Act provides for the assessment of tobacco manufacturers and importers of up to \$10.14 billion to fund payments to tobacco quota holders and farmers and to offset any losses incurred in disposing of surplus tobacco resulting from the termination of the federal tobacco supply management program. The payments to tobacco quota holders and growers are commonly referred to as "tobacco buyout" payments, as they are being made in conjunction with the elimination of the federal program. In order to fund the payments, the Secretary is required to impose quarterly assessments on each manufacturer and importer of tobacco products sold in the United States.

## II. The assessments in FETRA are based on the federal excise tax code

The 108th Congress debated the tobacco buyout issue extensively, with legislative proposals introduced from the earliest weeks of the Congress in January, 2003. Various approaches were suggested as a means of funding a tobacco buyout. Some advocated that no special funding mechanism be provided, instead financing a tobacco buyout from *general revenues*. This was the approach taken in the version of FETRA that initially passed the U.S. House of Representatives on June 17, 2004.

Others advocated that the tobacco buyout be funded through assessments on manufacturers and importers based on the amount of *domestic quota type tobacco used* in each tobacco product class. For several years, cigar manufacturers and importers have used only de minimus amounts of domestic quota tobacco, with most using none whatsoever. Largely because of this, the version of FETRA that initially passed the Senate on July 15, 2004 *did not include any assessment at all on cigar manufacturers and importers*. It did, however, impose assessments to fund the tobacco buyout on

manufacturers and importers of cigarettes, snuff, chewing tobacco, pipe tobacco, and roll-your-own tobacco.

A third approach to funding the tobacco buyout was to impose assessments on tobacco product classes based upon the *relative excise tax burdens*. Under this approach, a distinction was made between large and small cigars, which are classified and taxed differently under the federal excise tax code. So for example, S.1490, the leading Senate tobacco buyout proposal prior to the passage of FETRA, imposed assessments on large cigars at 1.095 percent of the total assessment and small cigars at 0.011 percent of the total assessment. H.R. 3160, a House bill with 43 cosponsors, took an identical approach to S.1490, distinguishing between large and small cigars.

When the competing versions of FETRA were considered by a joint House-Senate conference committee in October, 2004, it was determined that neither of the initial funding approaches (through general revenues or based on domestic quota tobacco used) would be followed. Instead, the tobacco buyout would be funded based on the relative excise tax burden among tobacco products classes. This rationale has been confirmed in subsequent conversations with Members of Congress and key staff involved in writing the legislation (discussed further below).

Unfortunately, in the haste to draft a final version of the legislation, the statutory distinction between large and small cigars was not specifically mentioned. Notwithstanding the language of the federal excise tax code, large and small cigars were lumped together into a single category for purposes of assigning a percentage of the total assessments to be paid. [As noted in the CAA comments, we also take issue with the actual percentage chosen, which does not appear to be precisely based on excise tax revenue statistics from any known recent period.] In other words, FETRA imposes an assessment on cigar manufacturers and importers based on their share of federal excise taxes collected, initially set at 2.783 percent of the overall assessments to be paid.

### III. Small cigars and large cigars are treated differently under the federal tax code

26 U.S.C. 5701(a)(1) provides that “small” cigars (those “weighing not more than 3 pounds per thousand”) are to be taxed at \$1.828 per thousand. 26 U.S.C. 5701(a)(2) provides that “large” cigars (those “weighing more than 3 pounds per thousand”) are to be taxed at 20.719 percent of the price for which sold but not more than \$48.75 per thousand.”

This differentiation, which has existed for decades, takes into account the variety of shapes and sizes of cigar products in the marketplace. Unlike cigarettes

(which are fairly uniform in size and shape), cigars have traditionally been manufactured in a variety of ways. The sliding scale structure of the large cigar excise tax adjusts for this variety. In other words, a ten cent cigar should not be taxed at the same rate as a \$10 cigar.

#### IV. Small cigars and large cigars should be assessed differently under FETRA

The result of this excise tax structure produces an equitable distribution of the tax burden. For example, small cigars represented 34.7 percent of all cigars manufactured in 2003. Yet they represented just over two percent of cigar industry revenues and just over two percent of cigar excise taxes collected.

If the rationale for assessments on manufacturers and importers of tobacco products under FETRA is based on federal excise taxes paid, then small and large cigar manufacturers and importers must be treated differently. While the initial assessment on all cigars is fixed under FETRA for the first year at 2.783 percent of total assessments, small and large cigars should be assessed in relation to their respective tax burdens when imposing individual assessments to meet this overall amount.

#### V. Congress intended that small and large cigars be assessed differently under FETRA

Section 625(f) of FETRA requires the Secretary to assess manufacturers and importers based on their respective market share. "Market share" is defined in section 625(a)(3) in terms of the "total volume of domestic sales of the *class* of tobacco product..." The Secretary should logically interpret "class" for purposes of assigning market share to mirror the federal tax code, with large cigars and small cigars being treated as separate market share classes.

The term "class" is not limited in the definition of market share, nor is it given a definition under FETRA. While other provisions of FETRA limit the term "class" in the context of the categories for FETRA percentage allocations, no such limitation exists as used in the definition of market share. Therefore, the term "class" should not be so limited in interpreting the meaning of "market share." If Congress intended such a limitation on the meaning of "class," it would have specified such a limitation as it has in other parts of the statute.

Congressman Ander Crenshaw considered seeking a clarification of this provision prior to the completion of the FETRA negotiations, but was assured that none was required. As noted in the attached letter from Rep. Crenshaw, he had extensive discussions with Chairman Thomas and the staff of the House Ways and Means Committee prior to the passage of FETRA. After discussing the Congressional intent, the Congressman notes that the drafters of FETRA "made it abundantly clear that the

Department of Agriculture has ample authority to differentiate between large and small cigars and impose an equitable assessment structure.... In other words, since small cigars pay only about two percent of the excise taxes collected on all cigars, they should only pay about two percent of the new buyout assessments imposed on all cigars.”

Rep. Crenshaw further described his conversations regarding the FETRA assessments. He stated that Chairman Thomas and his staff “believe that the intention of the legislation is (1) that the Secretary can differentiate the amount paid within a class so small cigars do not pay the same amount as large cigars; (2) there is no per unit assessment level for a product set by the bill... levels by type of cigar can be set by the Secretary; and (3) the Secretary can set the rate on small cigars and big cigars at different levels as long as the total amount to be collected from the industry segment (2.783% of the total from cigars) is received.” A full copy of the letter from Rep. Crenshaw is attached.

For all of the foregoing reasons, large and small cigars should be assessed at different rates to reflect the different levels at which these products are taxed under statutory provisions providing for federal tobacco excise tax collections.



UNITED STATES  
HOUSE OF REPRESENTATIVES

December 8, 2004

Mr. Tom Ryan  
Executive Vice President  
Swisher International, Inc.  
459 East 16<sup>th</sup> Street  
Jacksonville, Florida 32206

Dear Tom:

As you know, I feel strongly that cigar manufacturers were not treated fairly under the terms of the tobacco buyout assessment included in H.R.4520, the American Jobs Creation Act of 2004. Tobacco manufacturers are being assessed under the new law to pay for a tobacco farmer buyout. The assessments are allegedly based on the excise tax liabilities for each class of tobacco product. This bears no relationship to the amount of domestic quota tobacco actually used.

A more rational assessment would have been based on quota tobacco used by each segment of the tobacco industry, since the purpose of the assessment is to pay quota holders and growers of domestic quota tobacco. Unfortunately, a different mechanism was chosen that was not included in either the initial House or Senate versions of the bill. As a result, the bill imposes a 2.783 percent initial assessment on cigar manufacturers.

To make matters worse, it is unclear whether the bill makes any distinction between small cigar manufacturers and large cigar manufacturers as is done under the excise tax law. As you know, the tax code imposes excise taxes on small cigars at a fixed rate (\$1.828 per thousand), while large cigars are taxed at a much higher rate (20.719 percent, up to a cap of \$48.75 per thousand). I spoke extensively with Chairman Thomas and staff members from the House Ways and Means Committee in the hours before the H.R.4520 conference report passed the House of Representatives. As a result of those conversations, it is clear to me that they believe that the initial assessment percentages are based on an excise tax allocation and that the Secretary has the authority to adjust these percentages each year, as well as the market share allocations made each year within an industry segment.

As you know, small cigar manufacturers make approximately 35 percent of the cigars annually, but pay about two percent of cigar excise taxes because of the sliding scale nature of the federal excise tax structure, which imposes taxes based on price. They also made it abundantly clear that the Department of Agriculture has ample authority to differentiate between large and small cigars and impose an equitable assessment structure. At the very least, these new assessments should be imposed in a way that reflects the relative excise tax burden of small and large cigars. In other words, since small cigars pay only about two percent of the excise taxes collected on all

Mr. Tom Ryan  
December 8, 2004  
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cigars, they should only pay about two percent of the new buyout assessments imposed on all cigars.

As a result of my discussions with Chairman Thomas and his staff, it is clear to me that they believe that the intention of the legislation is (1) that the Secretary can differentiate the amount paid within the class so small cigars do not pay the same amount as large cigars; (2) there is no per unit assessment level for a product set by the bill... levels by type of cigar can be set by the Secretary; and (3) the Secretary can set the rate on small cigars and big cigars at different levels as long as the total amount to be collected from the industry segment (2.783% of the total from cigars) is received.

As the tobacco buyout is implemented, I will be closely monitoring the actions of the Department of Agriculture to see that this intent is followed. Assessments imposed on cigars should parallel the excise tax code, with small cigars assessed at a much lower rate. Florida small cigar manufacturers should not be penalized twice by an inequitable administrative decision. You can be assured that I will follow this process with great interest and with the interests of Swisher, its employees, and the entire Florida cigar manufacturing industry in mind.

Sincerely,

A handwritten signature in black ink that reads "Ander Crenshaw". The signature is written in a cursive, flowing style.

Ander Crenshaw  
Member of Congress