



Single Stick, Inc.

Mr. Frank Foote
Regulations and Rulings Division
Alcohol and Tobacco Tax and Trade Bureau
P.O. Box 14412
Washington, D.C. 20044

RE: Notice No. 65, Tax Classification of Cigars and Cigarettes, 71 Fed.Reg.
No. 206 (October 25, 2006)

Comments of Single Stick, Inc. and Affiliate

Dear Mr. Foote:

These comments are made on behalf of Single Stick, Inc. (hereafter "SSI") and its distribution subsidiary, USA Tobacco Distributing, Inc. (hereafter "USA" and collectively referred to as "SSI" or the "Company" as the context warrants). SSI is a manufacturer of tobacco products, predominantly cigars, but also manufactures cigarettes and roll your own tobaccos operating under permits issued by the Alcohol and Tobacco Tax and Trade Bureau (hereafter referred to as the "TTB"). SSI's primary manufacturing facility is located at 7427 NC Hwy 58 South, Stantonsburg, NC 27883, with a packaging facility and executive offices located at 2019 West Lone Cactus Dr., Phoenix, Arizona 85027. USA, a wholly owned subsidiary of SSI, distributes products manufactured by SSI in 39 states, Canada, and other foreign countries. SSI manufactures little cigar products under the trademarks Prime Time®, Smoker's Choice®, Gold Rush®, Happy Hour®, and Bullseye®. SSI manufactures large cigars under the Prime Time® and Smokers Choice® trademarks. The Companies were incorporated in 1993

and began the manufacture of their own proprietary products after issuance of their original permit in 1999.

SSI is a member of the Cigar Association of America (hereafter the "CAA") and supports fully its efforts to encourage clarity in the regulations governing the manufacture and sale of cigar products. SSI participated in the drafting of the comments submitted by the CAA and fully supports those comments, including the changes sought by the CAA in the proposed regulations. SSI strongly supports the proposed website suggested by the CAA on which the TTB is encouraged to post the certifications made by compliant companies for the benefit of the states.

SSI supports the goal of the TTB to clarify its administrative practice and guidance to the industry in a single regulatory framework subject to statutory requirements. These comments are intended to assist in this effort. The comments herein are presented solely on behalf of the SSI Companies and should not be attributed to any other entity.

I. THE PROPOSED REGULATIONS, AS WRITTEN, DO NOT COMPLY WITH THE REGULATORY FLEXIBILITY ACT OR WITH EXECUTIVE ORDER 12866.

SSI opposes adopting the proposed regulations because certain provisions of the regulations substantially change the requirements for classification as a cigar and will eliminate SSI's entire line of both little cigars and large cigars by reclassifying them as cigarettes. See, Section V, below. The change in the classification

criteria for cigars wrapped in a substance containing tobacco will, according to estimates by the CAA, eliminate approximately 97% of the little cigars currently marketed today with irreparable adverse economic impact on a substantial number of small manufacturers¹ together with their suppliers and customers.

Based on its knowledge of the industry and the projected impact of the application of the Proposed Regulation on its own operations if adopted in its present form, SSI disputes the certification by the TTB that “this notice of proposed rulemaking will not have a significant economic impact on a substantial number of small entities”. SSI is further concerned by the conclusory statement that the “proposed rule is not a significant regulatory action as defined by Executive Order 12866”. As described below, certain departures by the Proposed Regulation from longstanding administrative practice are exactly the type of actions requiring a thorough analysis of alternative approaches and economic impacts. SSI submits that changes can be made in the regulation as finally adopted which would both accomplish TTB’s goal to “clarify the application of existing statutory definitions... to provide clearer and more objective product classification criteria”, and avoid the economic disruption which will inevitably occur upon adoption of the Proposed Regulations in their present form. See Sections V, VI, and IX below. We urge the TTB to adopt modifications in the final regulations which will not eliminate large classes of currently compliant cigar products. The adoption of certain modifications, along the lines of those

¹ Manufacturers qualifying as a small business pursuant to 13 CFR Sec. 121.201 and falling within the criteria of the Small Business Administration.

proposed by the CAA, will eliminate the need for compliance by the TTB with the Regulatory Flexibility Act and Executive Order 12866.

II. SCOPE AND DEFINITION OF THE PROBLEM.

The Preamble to the Propose Regulations states:

"The proposals contained in the document clarify the application of existing statutory definitions and update and codify administrative policy in order to provide clearer and more objective product classification criteria. These clarifications are intended to reduce possible revenue losses through the misclassification of cigarettes as little cigars."

The stated goal of the regulations, to prevent misclassification of cigarettes as cigars and thereby reduce possible revenue losses, is clearly desirable from both the industry and the government perspective. The protection of the federal revenue subject to the maintenance of the categories of tobacco products as established by Congress in the Internal Revenue Code² is the proper scope for these regulations. The establishment of clearly defined criteria which preserves the product categories as defined by statute also assists the industry by facilitating compliance with clearly stated objective criteria and by eliminating the confusion in the marketplace created by mislabeled product. SSI supports these objectives.

SSI is concerned, however, that the problem of misclassification of cigar products is overstated as it relates to mischaracterization of cigarette products and lost revenue.

² 26 USC § 5701(a)(1).

TTB has not provided actual figures (either on enforcement actions undertaken against misclassified product, reclassification of products, or lost revenue) to substantiate the stated concern over loss of tax revenue.

It is further submitted that the TTB's existing compliance and classification efforts have been extremely efficient in ensuring the proper classification of cigar products by domestic manufacturers. The TTB requires all domestic manufacturers to hold a permit. The TTB routinely audits these permit holders. At the inception of each audit of a company, TTB auditors routinely select samples of each of a manufacturer's cigars from the factory floor or from stocks on hand and send these samples to their National Laboratory for testing. These test results provide the basis for the classification of cigar products for purposes of the audit. At each audit of SSI, the Company's products have been tested and qualified as either large or little cigars. The Company has never had any cigar product reclassified as a cigarette due to an audit. Due to the substantial differentials in tax rates between little cigars and those for cigarettes, the Company has required its component suppliers to provide written assurances that the components they supply qualify as cigar tobacco, in the case of filler, and comply with the tobacco content requirements for reconstituted tobacco wrappers. The TTB has a program under which a manufacturer can voluntarily submit its cigar products to the National Laboratory for testing and receive a letter of determination as to their proper tax classification. SSI has submitted its cigar products in the past pursuant to this procedure for testing and has retained its product classification as cigars.

The wholesale reclassification of cigar products as cigarettes which would occur under the proposed regulations would not enhance the tax revenue. For reasons stated herein, the reclassification of little cigars as cigarettes would result in their elimination from the marketplace since consumers would be highly unlikely to accept a cigar product as a cigarette. See, Sections IV and VII, below. Even assuming the reclassified product could be remarketed as a cigarette, an assumption with which the Company strongly disagrees, the proposed regulation amounts to an unlegislated tax increase.

Losses in tax revenues due to misclassification of domestic cigar products as cigarettes should not be the motivating factor for the proposed regulation. No evidence has been cited to show that such misclassifications recur on more than an infrequent basis. Closer coordination of efforts between the TTB and US Customs and Border Protection Agency would serve to enhance existing compliance efforts and close any existing gaps in enforcement.

III. OVERVIEW OF THE CIGAR INDUSTRY AND COMPARISON WITH CIGARETTES

In terms of its relative size, the cigar industry in the United States is a fraction of the size of the cigarette industry. The following chart compares the relative size of the two industries:

2002-2005 (IN BILLIONS OF UNITS)

YEAR	LARGE CIGARS	LITTLE CIGARS	CIGARETTES
2002	4.2	2.3	417.3
2003	4.5	2.5	459.2
2004	4.9	2.9	398.3
2005	5.1	4.0	381.0

Between 2002 and 2005 cigarette removals were down 36.3 billion units while little cigar removals were up only 1.7 billion units, and removals of all cigars were up only 2.6 billion units. Clearly the losses in volume in the cigarette industry are not the result of widespread substitution by consumers into cigar products as the result of the systematic mischaracterization of cigar products by the cigar industry. Similarly, we would expect a much closer concurrence between the gain in cigars and the losses in cigarettes if the alleged tax disparity or the MSA payments from the cigarette manufacturers were motivating factor. IRC Section 5701 establishes separate tax classifications and tax rates for cigars and cigarettes. IRC Section 5701(a)(1) establishes the current federal tax rate for little cigars at \$1.828 per thousand or \$.3656 per 200 count carton (IRC Section 5701(b)(1)). Cigarettes are taxed at \$19.50 per thousand or \$3.690 per 200 count carton (IRC Section 5701(b)(1)). The current (sales year 2006) contribution to escrow for cigarettes based on the tobacco Master Settlement Agreement is \$4.29 per 200 count carton. The differences in these rates, \$8.19 for cigarettes versus \$.3656 for small cigars have not, over time, resulted in an inversion in the size of the markets for cigarettes and little cigars. If tax and MSA payments were the motivating factor for cigarette smokers to change to cigars,

we would expect a complete reversal of volumes sold with cigars dominating the market and cigarettes sales of only a fractional amount.

The products sold by the cigar industry are broken down into large and luxury cigars weighing more than 3 pounds per thousand units and little cigars weighing less than 3 pounds per thousand units. Some companies, such as SSI, make both little and large cigars. The industry is composed predominantly of small companies. While exact figures are difficult to get on the number and size of the small companies, the USDA, as part of its administration of the Tobacco Transition Payment Program, must assess cigar companies according to their market shares to fund the government buyout of the farmer's tobacco entitlements. According to the Tobacco Assessment Summary published by the USDA for the period April-June, 2005, attached as Exhibit "A", out of 149 companies reporting, only 82 were assessed based on a market share cutoff of .01% or higher. Sixty seven reporting companies (all companies which make and sell cigars must be reporting companies) had less than a hundredth percent market share. The remaining 82 companies had assessable market shares. It is fair to conclude from this analysis, that the vast majority of companies in the cigar business are small businesses with minimal market shares.

IV. CIGAR PRODUCTS ARE DIFFERENT FROM CIGARETTE PRODUCTS

The reason that consumers have not substituted cigars for cigarettes on a wholesale basis are that cigar products are substantially different from cigarette products in a number of ways. Most of these differences are easily perceptible

by the consumer. There are differences in the characteristics of the tobaccos used, in the characteristics of the product as it is smoked, and in the way in which it is marketed. The preponderance of large cigars are clearly different in size and shape from cigarettes and there are substantial and detectable differences between the wrapper used in cigars and the paper in which cigarettes are wrapped.

The difference in the tobacco used as cigarette filler from that used as cigar filler gives each product distinctive flavor characteristics which are readily apparent to the consumer. Cigarettes, because of the massive volume of tobacco used, are made predominantly from flue cured tobaccos. In this process tobaccos are heated, which dries them more quickly. Cigarette tobaccos are chemically more acidic. Cigarette tobaccos also contain more sugar as the result of the heat applied in the flue curing process which destroys enzymes in the leaf. The lack of such enzymes in cigarette tobaccos result in a greater sugar content. Cigar tobaccos retain their natural enzymes during the curing process and the action of these enzymes on the sugars occurring in the tobacco result in a lesser sugar content in the cured cigar tobacco. In cigarette tobaccos, result is a greater sugar content. Cigars are made from predominantly air cured tobaccos or from fermented tobaccos. In this process the tobacco is not subjected to heat and as a consequence of the working of the enzymes in the tobacco, they have lower levels of sugars. The air cured tobacco is chemically alkaline. The wrapper of a cigar is required to be made of similar tobaccos to those of the filler.

The differences in smoking characteristics are similarly pronounced and appeal to different consumers. Most cigarette smokers smoke everyday. In contrast, as many as three-quarters of cigar smokers smoke only occasionally. Some may only smoke a few cigars a year. National Cancer Institute of the National Institutes of Health, Monograph 9 Cigars; Health Effects and Trends (1998). Cigarette smokers inhale their product. Cigar smokers do not inhale the smoke from their cigars. There are significant differences between cigarettes and cigars in taste, aroma, and draw.

Cigars are labeled and marketed differently from cigarettes. AFT Ruling 73-22 sets forth the requirement that packaging "conspicuously declare it to be a cigar" and that all "marketing materials and advertising clearly present the product to the consumers as a cigar and not as a cigarette". In the event that the product is packaged in 20 count packages comparable to the manner in which cigarettes are packaged, the declaration "cigar", "small cigar", or "little cigars" must appear "in direct conjunction with, parallel to, and in substantially the same conspicuousness of type and background as the brand name each time the brand name appears". Product labeling, therefore, clearly informs the consumers that the product is a cigar and not a cigarette.

The marketplace makes similar distinctions between cigarettes and cigars. Planograms (the design plans used for placement of products in convenience stores) are used by the large chain stores. These planograms always separate

cigar products from cigarette products in shelving and display areas. Other merchants follow this lead in separating cigarette and cigar products.

Finally, no cigars are line extensions of cigarettes. Camel® or Marlboro® cigars do not exist. In the case of cigars, it is frequently the case that little cigars are extensions of established large cigar brands.

The difference in the composition of cigar wrappers and cigarette paper also present gross differences:

CIGAR WRAPPER

Air and fermented tobacco
66-2/3% tobacco content
Color of tobacco
PH basic
Tobacco character and taste
Nicotine
Slightly rough texture

CIGARETTE WRAPPER

Paper
No tobacco
White (usually)
PH menthol
No taste
No nicotine
Smooth texture

V. THE PROPOSED REGULATIONS CHANGE EXISTING REQUIREMENTS FOR CLASSIFICATION AS A CIGAR AND PROVIDE FOR WHOLESALE RECLASSIFICATION OF LONGSTANDING CIGAR PRODUCTS AS CIGARETTES

The traditional tests for a cigar product are established in Sections 5702(a) and (b) of the Internal Revenue Code. Section 5702(a) defines a cigar as “any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco...” (emphasis supplied). A cigarette is defined in Section 5702(b) as “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...” The statute thus set up a three part test to differentiate between cigars and cigarette

products. That test requires examination of: (1) the wrapper (a substance containing tobacco), (2) the filler (type of tobacco used), and (3) disclosure of the product type (its packaging and labeling). The Bureau of Alcohol, Tobacco and Firearms (ATF), predecessor agency to TTB, further defined the required tests for a cigar in Revenue Ruling 73-22 by enhancing the statutory three part test. This ruling has served as the source of administrative guidance for the industry for 33 years since its publication. The ruling specifies that a cigar wrapper contain "approximately two thirds or more tobacco which did not in the reconstitution process lose its tobacco character (taste, aroma, identifiable chemical components)", and which is of "a color consistent with that of natural leaf tobaccos traditionally used as a wrapper for American cigars".

The second part of the test directed at the cigar filler requires that the filler be "substantially of tobacco unlike those in ordinary cigarettes and must not have any added flavorings which would cause the tobacco to have the taste or aroma generally attributed to cigarettes". The ruling goes on to state that "inclusion of flue-cured or aromatic (oriental) tobaccos" could make the product a cigarette. Various chemical tests have been developed over the years which provide clear and objective differentiation between cigars and cigarettes.

The third test, disclosure of product type, was also addressed in the ruling. Packaging "must conspicuously declare it to be a cigar". Further "all marketing

materials and advertising clearly present the product to the consumer as a cigar and not as a cigarette”.

Since its publication in 1973, the industry has relied on the tests supplied in this ruling and has developed products and packaging at substantial cost to create compliant products. All of these tests are substantive and address the essential elements of different components of the cigar product which make it different than a cigarette.

The Proposed Regulations represent a substantial change in the historical classification requirements for cigars wrapped in manufactured cigar wrappers and will eliminate a substantial portion of the 97% of machine wrapped cigars on the market today.

Section 40.12 of the Proposed Regulations sets forth classifications of cigars and cigarettes. The Proposed Regulations follow existing law in classifying the small percentage of the cigar market with leaf wrappers as cigars and in classifying products wrapped in paper as cigarettes. In the area of products wrapped in “a substance contain tobacco” (machine usable reconstituted tobacco wrapper) the Proposed Regulations ignore the longstanding three part test for a cigar and require a wholesale reclassification of existing products. Section 40.12(2) for the first time expresses a “cigarette classification precedence” Section 40.12(2)(b)(3)(ii) provides that a product wrapped in a “substance containing

tobacco” is classified as a cigarette if (1) “It has a typical cigarette size and shape, has a cellulose acetate or other cigarette type integrated filter”, or (2) “is put up in a traditional cigarette type package that does not bear all of the notice requirements for cigars specified in Section 40.214....”.

These three requirements in the Proposed Regulations are stated in the disjunctive (“or”) so that if any one of them is violated, the product is classified as a cigarette. As has been noted, both little cigars and cigarettes are made on machines to the statutory standard of less than three pounds per thousand. If a little cigar meets all of the existing tests (a wrapper greater than 66-2/3% tobacco, a filler made of cigar type tobaccos, and is packaged in a package that clearly and conspicuously discloses the contents to be cigars) under the proposed regulations it will nevertheless be considered to be a cigarette solely because it has a “typical cigarette size and shape”. Based on the statutory requirements of IRC Section 5701(a)(1), the size and shape of these two products is virtually mandated. The criteria “typical cigarette size and shape” is neither probative of any essential characteristic of a cigar, nor is the size and shape of the product any more typical of a cigarette than it is of a little cigar. Little cigars have been manufactured in their current size and shape for over fifty years since the classification statute was enacted. The criteria “size and shape” has no value as a functional discrimination between the two products. Virtually all of the little cigar products on the market today meet the “typical cigarette size and shape” requirement and are thus summarily reclassified as cigarettes in the Proposed Regulations.

A second criteria for classification of a little cigar as a cigarette is that the product has "a cellulose acetate or other cigarette type integrated filter." Rev. Rule. 66-123 has for the past forty years provided guidance to the cigar industry by its approval of just such filters incorporated into cigar products. Once again, a cigar product which is wrapped in wrapper which is compliant with existing federal standards, has filler tobaccos which are compliant cigar type tobaccos, and is packaged in packaging which clearly and conspicuously discloses that the product is a cigar product will nevertheless be reclassified as a cigarette solely because it has "a cellulose acetate or other cigarette type integrated filter". The criteria "cigarette type integrated filter" is once again simply not probative of any essential characteristic of a cigar, nor is the existence of a filter more typical of a cigarette than a cigar. Cigars have been manufactured with integrated filters for at least 40 years based upon the publication of Rev. Rule 66-123 in 1966. The criteria has no value as a functional discriminator between cigars and cigarettes. Most of the little cigar products on the market today meet the criteria "cigarette type integrated filter" and are thus summarily reclassified. The proposed regulation thus concentrates on product features common to both cigarettes and little cigars but characteristic of neither. These tests, with a decisive role in recharacterizing little cigar products, focuses on trivial and non-probative features and depart from the traditional tripartite tests for filler, wrapper and disclosure of package contents which proceed from the enabling statute and historical regulations. We would propose that the final regulation concentrate on

clarifying existing requirements and not adopt new criteria which are found nowhere in existing law or regulations.

VI. OTHER COMMENTS ON THE PROPOSED REGULATIONS

a. **Manufacturer's Certification** – Proposed Rule 40.13 provides that manufacturers will certify to the TTB that their products comply with the regulations. Conceptually, we support this proposal but would suggest strongly that it needs to be modified in three respects. First, most if not all cigar companies buy their components, e.g. tobacco fillers and machine usable tobacco wrappers from existing and long established suppliers. Many of these suppliers supply these products to multiple manufacturers. As in the case of SSI, many companies must rely on the representations of their component manufacturers that the components supplied meet the required criteria. Testing equipment, such as that required to certify that wrappers contain the requisite percentages of tobacco, would be prohibitively expensive, and personnel qualified to use the equipment would add an additional level of continuing expense which cannot easily be amortized over existing market shares, especially those of small manufacturers. It would be both reasonable and cost effective to permit certifying manufacturers to rely on certification from their suppliers that such components are compliant with the criteria established in the regulation.

We are concerned that the recertification process will become unwieldy if the recertification is required for "any change in the composition or presentation of

that product". We would prefer that the regulation be drafted to deem the certifications filed as continuing in effect and to require recertification or withdrawal by the manufacturer of its certifications in the event that changes are made to the product or its presentation which would cause it to be reclassified. Due to the organic nature of the product, every load of tobacco used will have some variation. Although these variations are not enough to cause it to be reclassified, under the rule as proposed they would cause a company to file certifications on a continuing basis.

The CAA in its comments entitled "Proposed Regulatory Language (c) Cigar Certification and Tax Status" proposed that the certification form provide for a voluntary waiver on the part of the certifying company which would permit the TTB to publicly disclose the manufacturer's certifications on the TTB website. Concerns have been raised, both in the states' petition to the TTB and in state legislatures, regarding the proper distinction between little cigars and cigarette products. The states do not have the technical resources and in many cases the expertise to make the required determination. Most cigar products are sold on a national basis and a national standard is clearly appropriate as the submission of the states' petition recognizes. The creation of a national website and a certification system verifiable through the technical resources available to the TTB will provide needed assurances to all of the parties to the tobacco regulation process. SSI strongly supports the addition of a voluntary waiver to the proposed certification requirement.

b. Application of Labeling Requirements to Export Products – Proposed Sections 44.186 and 44.253 specify how packaging of cigars intended for export must be labeled. These provisions essentially repeat the labeling requirements set forth in proposed Section 40.214, applicable to cigars intended for sale in the U.S. market. The labeling provisions of Sections 44.186 and 44.253 attempt to impose U.S. labeling requirements on cigars intended for sale in foreign markets. The attempt to impose U.S. labeling requirements on cigars sold in foreign markets is both unnecessary to enforce internal revenue requirements and contrary to basic principles of U.S. law. Labeling requirements for cigars sold in foreign markets are imposed by the governments in the markets in which the cigars are sold. The only requirement that TTB should impose is that the cigars be labeled “for export only”, in a conspicuous place and manner, which would preclude their sale in the U.S. market.

It is a well-established principle of U.S. law, adopted by the Supreme Court and reiterated by numerous Federal Court of Appeals, that legislation enacted by the U.S. Congress is presumed to apply only within the territorial jurisdiction of the United States unless a contrary or affirmative intention of Congress is clearly expressed. *EEOC v. Arabian American Oil Co.*, 499 U.S. 244, 248 (1991); *Arc Ecology v. United States Department of the Air Force*, 411 F. 3d 1092 (9th Cir. 2005). In *EEOC v. Arabian American Oil*, the Supreme Court stated that it assumes that Congress legislates against the backdrop of the presumption against extraterritorially, and unless the “affirmative intention of the Congress” is expressed, the Court will presume that Congress is primarily concerned with

domestic conditions. *Id.*, at 248. The Supreme Court reiterated this position in *Small v. United States*, 125 S. Ct. 1752, 1755 (2005), where it stated that “in determining the scope of [a] statutory phrase we find help in the common sense notion that Congress generally legislates with domestic concerns in mind.” If Congress does not have the authority, as a general rule, to legislate extraterritorially, administrative agencies and their regulations also will be so limited.

In the case of the proposed TTB rules, there is no indication in the underlying legislation that Congress intended TTB to enact any rules or regulations which would be applied on an extraterritorial basis. Further, there is nothing to indicate that the presumption against extraterritoriality should not be applied, as in this case the failure to extend the labeling rules to foreign countries will have absolutely no effect in the United States.

The effort to extend U.S. labeling requirements for cigars beyond the borders of the United States is contrary to settled U.S. law, and must be rejected. We would urge that TTB amend proposed Sections 44.186 and 44.253 to simply require the packages of cigars intended for export be labeled with the statement “for export only” (or with other similar language). This would be consistent with labeling requirements adopted by other U. S. regulatory agencies with respect to goods which are intended for export only for sale in foreign markets.

c. Disclosure Requirement – The Proposed Regulation requires the words “cigars”, “little cigars”, or “small cigars” to appear in “conspicuous” type on the packaging. The use of the term “conspicuous “ is subjective. SSI supports the proposal in the CAA’s comments that specific font size be specified based on the area of the packaging. Precedent for this exists both in The Federal Cigarette Labeling and Advertising Act administered by the Federal Trade Commission (FTC) and in the language of the cigar Master Settlement as administered by the FTC.

VII. THE PROPOSED REGULATIONS, IF IMPLEMENTED, WILL CAUSE IRREVOCABLE ECONOMIC HARM TO SSI, ITS SUPPLIERS AND DISTRIBUTORS

The implementation of the Proposed Regulations reclassifying SSI’s core production, its little cigar products, as cigarettes will have a devastating and irrevocable economic impact on the Company. The impact of the reclassification will also have a profoundly negative impact on the Company’s suppliers and the distributors, transport and retailers in its supply chain. While we have no quantifiable economic information on our suppliers and other companies in our supply chain, the effect on eliminating virtually all little cigars, and a substantial market percentage of large cigars as referenced in the CAA’s comments, multiplies the expected impact on the marketplace.

SSI emphasizes in the strongest possible terms that the effect of the reclassification of the little cigar product will not be to cause it to be remanufactured as cigarettes, but to effectively eliminate little cigars from the marketplace. The economic inelasticity of cigar and cigarette products is

demonstrable. See, Section III, above. Product price differentials not accompanied by an inversion in the marketplace are evidence that the products are not interchangeable. The reason for this inelasticity is that the customers for cigarettes are different from the customers for cigars. See, Section IV, above. To require cigar products to be labeled as cigarettes will cause market confusion as customers purchase products labeled as cigarettes, and get instead, a product that smokes as a cigar. There is no known market for cigar products labeled as cigarettes. Lawsuits, by consumers and suppliers forced to refund the purchase price of products considered "defective" by cigarette smokers, will add to the confusion.

It has been shown that cigars are separated from cigarettes on the planograms used by major store chains to design their stores. Most of the space in the cigarette planogram is dedicated by contract and slotting agreements to the cigarette products of the major cigarette manufacturers. If cigars are reclassified as cigarettes, they would be effectively precluded from positions in retailers' cigarette displays by these contracts.

If the proposed regulations are finalized, and cigars reclassified as cigarettes, the companies would be subject to a number of state cigarette requirements. Requirements favoring mass cigarette consumption, in the form of limitations on package size less than 20 count, would be imposed on cigars which are often purchased and smoked by their customers in smaller quantities. A growing number of states have legislation which requires cigarettes to use low ignition

propensity paper. Whether cigars, reclassified as cigarettes could pass the required tests is unknown. If the wrappers of cigar products were required to be replaced by low ignition cigarette paper, the product would simply become unrecognizable to its customers. The result again is an entirely different product with no known market.

SSI has taken all reasonable steps available to it as a small company to ensure and maintain a compliant cigar program. It has invested in plant and equipment including packaging machinery for 20 count packages to make legal cigar products. These investments were made in reliance on the longstanding regulatory traditions establishing and providing guidance to the cigar market, and will be lost if the Proposed Regulations are adopted and destroy the little cigar market.

The impact of the export labeling requirements only exacerbates the destruction of the Company's domestic markets. The Company has a significant export market, particularly to Canada. Canada has its own extensive labeling requirements, including the characterization of little cigars as cigarillos. The direct effect of the adoption of the export regulations would be a conflict with the requirements of Canadian law. The Company could not export its product to Canada under such circumstances. Other export jurisdictions have other conflicting requirements.

VIII. EFFECTIVE DATE

If the Proposed Regulations are adopted as written there is no known market for such products which must be re-labeled as cigarettes contrary to the expectations of the consuming public. We are, accordingly, unable to speculate on any deferred effective date which would mitigate the adverse and irrevocable consequences we have clearly demonstrated above.

In the event that modifications to the Proposed Regulations are made which retain traditional classification criteria, but which make modifications to labeling requirements, a 9 – 12 month period would permit the use up of existing packaging.

IX. SUPPORT FOR CAA PROPOSED REGULATORY LANGUAGE

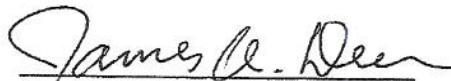
SSI supports in its entirety the regulatory language as proposed by CAA. These changes, if enacted, will provide clarity to the manufacturing companies to assist with compliance, provide a clear and non-subjective national standard to the states, and provide states with evidence of compliance by the cigar manufacturers. We strongly urge that the CAA's alternative regulatory language, including the voluntary waiver and website provisions for manufacturer's certificates be adopted as part of the final rule.

X. CONCLUSION

SSI hereby requests that the modifications to the proposed regulation as submitted by the CAA and as further supported herein be adopted.

Respectfully submitted,

Single Stick, Inc.. and Affiliate



James A. Deer
Secretary and Legal Counsel



Donald Stein, Esq.
Greenberg Traurig, LLC
Its Counsel