

Debunking the “Tax Thee, But Not Me” Myth: Five Reasons Why Non-Smokers Should Oppose High Tobacco Taxes

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Introduction

Smokers are easy targets for elected officials looking to increase government revenue and score political points by punishing “unpopular” activities. The sheer number of recent tobacco tax hikes vividly illustrates this trend: Cigarettes taxes were increased 72 separate times in 43 states from 2000 to 2007.¹

Broad-based tax increases (e.g., sales tax hikes) are often opposed by wide swaths of the population precisely because they directly affect many people. On the other hand, significant segments of the non-smoking population go along with efforts to raise tobacco excise taxes because these taxpayers believe they can avoid the resulting pinch by simply not buying cigarettes. It’s a classic case of a “tax thee, but not me” mentality backed up by the logic of “if the government is going to spend the money anyway, let them take it from someone else.”

However, this kind of approach doesn’t hold up to scrutiny. Analyses of state fiscal habits from 2000 and onward show that tobacco tax hikes have very real fiscal implications for non-smoking taxpayers. This Issue Brief explores the following five reasons tax-sensitive non-smokers should oppose high cigarette taxes:

1. States with low cigarette taxes tend to have lower overall tax burdens;
2. Tobacco tax hikes are rarely used to cut other taxes;
3. Tobacco tax hikes don’t forestall other tax increases;
4. Tobacco tax hikes may encourage other tax hikes down the road; and
5. Tobacco taxes don’t spur economic growth.

Granted, the research presented in this paper won’t mean much for those who favor higher taxes no matter what, but these findings should resonate with non-smoking individuals who prefer to retain more of their own money.

1. States with Low Cigarette Taxes Tend to Have Lower Overall Tax Burdens

Along with raising revenue for government spending, the Tax Code is often used for social engineering purposes. Tobacco tax increases are touted as a way to “discourage” smoking by artificially boosting related costs. Under this same line of reasoning, one would also look to the states to use tax law to promote favored activities. “Productive” behavior, such as earning an income and owning a home, should therefore be rewarded with low taxes.

However, the “tax behavior we don’t like, reward what we do like” outlook doesn’t hold true when comparing the relationship between tobacco taxes and a state’s total tax burden. States with higher cigarette taxes tend to have higher-than-average combined tax burdens when all state and local taxes are taken into account. Preferred behavior – along with the “undesirable” – tends to be punished with higher taxes! Conversely, states with low cigarette tax rates tend to have lower-than-average total state and local tax burdens.

Table 1. Per Capita State and Local Tax Burden for High Cigarette Tax States (as of 1/1/07)

State	Tax Burden	Cigarette Tax
Ohio	\$4,332	\$1.250
Pennsylvania	\$4,057	\$1.350
Texas	\$3,368	\$1.410
New York	\$5,734	\$1.500
Connecticut	\$6,018	\$1.510
Massachusetts	\$5,047	\$1.510
Hawaii	\$4,496	\$1.600
Montana	\$3,108	\$1.700
Vermont	\$4,118	\$1.790
Alaska	\$2,598	\$1.800
Arizona	\$3,350	\$2.000
Maine	\$4,719	\$2.000
Michigan	\$3,965	\$2.000
Washington	\$4,334	\$2.025
Rhode Island	\$4,629	\$2.460
New Jersey	\$5,234	\$2.575
Weighted Average	\$4,417	
Weighted U.S. Average	\$4,072	
Difference	\$345	

Source: compiled from Federation of Tax Administrators² and Tax Foundation³ data

Specifically, residents of states with the 16^a highest per-pack cigarette taxes (as of January 1, 2007) had an average per capita state and local tax burden for fiscal year 2006 that was \$345 more

^a This paper analyzed the highest and lowest 16 states because both Delaware and West Virginia have per-pack cigarette taxes of \$0.55, tying for 15th-lowest place.

than the national average. In other words, the general tax bill for residents of high-tobacco tax states is 8 percent above the national average.

On the other hand, residents in the 16 states with the lowest per-pack cigarette tax (as of January 1, 2007) had a state and local tax burden for fiscal year 2006 that was \$616 less than the national average. In other words, the general tax bill for residents of low-tobacco tax states is 15 percent below the national average.

Table 2. Per Capita State and Local Tax Burden for Low Cigarette Tax States (as of 1/1/07)

State	Tax Burden	Cigarette Tax
South Carolina	\$3,213	\$0.070
Missouri	\$3,509	\$0.170
Mississippi	\$2,924	\$0.180
Tennessee	\$2,979	\$0.200
Kentucky	\$3,383	\$0.300
Virginia	\$4,056	\$0.300
Florida	\$3,566	\$0.339
North Carolina	\$3,526	\$0.350
Iowa	\$3,709	\$0.360
Louisiana	\$3,463	\$0.360
Georgia	\$3,564	\$0.370
Alabama	\$2,881	\$0.425
North Dakota	\$3,421	\$0.440
South Dakota	\$3,177	\$0.530
Delaware	\$3,426	\$0.550
West Virginia	\$3,212	\$0.550
Weighted Average	\$3,456	
Weighted U.S. Average	\$4,072	
Difference	-\$616	

Source: compiled from Federation of Tax Administrators⁴ and Tax Foundation⁵ data

Americans hoping to keep their total state and local tax burden low should avoid states with high cigarette taxes. Elevated tobacco taxes may reflect a propensity to tax other types of activity and products, regardless of their positive or negative impact on society and the economy. Non-smokers looking to higher tobacco taxes for a “tax thee, but not me” policy will be disappointed, as living with high tobacco taxes correlates with a “tax we” mentality.

2. Tobacco Tax Hikes Are Rarely Used to Cut Other Taxes

The anti-tobacco lobby makes the case that approving higher tobacco taxes will allow for other tax reductions. One such group argues, “By reducing smoking rates, cigarette tax increases will reduce the large amounts low-income and other state households are already paying in state and federal taxes to cover smoking-caused government expenditures.”⁶

Do cigarette tax hikes really provide tax relief elsewhere? There are a limited number of cases where tobacco tax hikes helped to cover decreases in other taxes. For example, in fiscal year 2007 Hawaii saw a combination of tobacco and gas tax hikes offset by cuts in personal income and other taxes, for a net tax decrease of \$13 million. In fiscal year 2003, Louisiana increased tobacco taxes and cut sales, personal income, corporate income, and other taxes for a net tax decrease of \$30.8 million. Mississippi officials considered increasing their tobacco tax to reduce the 7 percent sales tax on groceries, but the plan was vetoed in 2006 and renewed attempts in 2007 were shelved without action. Tennessee lawmakers lowered the state grocery tax by 0.5 percent in 2008 by using a small portion of the new funds coming from a 42-cent jump in the tobacco tax.

However, it is far more common to find tobacco tax hikes either 1) married with other tax increases, or 2) paired with cuts worth less than the tobacco tax increase.

Table 3. States with Tobacco Tax Hikes and Same-Year Tax Cuts
(offsets of equal or more value)

Fiscal Year	Number of States with Tobacco Tax Hikes	Number of States with Complete Tax Cut Offsets
2008	8	0
2007	4	1
2006	10	0*
2005	10	0*
2004	15	0*
2003	19	1
2002	3	0
2001	2	0

*States with revenue actions that had a series of tax cuts and increases but ended with a net tax increase were considered not offset.

Source: compiled from National Association of State Budget Officers⁷ data

The record shows that higher tobacco taxes are not commonly used to lower net tax burdens. Most states that increase cigarette taxes don't refund the revenue elsewhere – they spend it.

3. Tobacco Tax Hikes Don't Forestall Other Tax Increases

If tobacco tax hikes don't lead to tax cuts, do they at least prevent other tax hikes that would hit non-smokers?

Once again, this isn't the case. By looking at past state government "revenue actions" – revisions in laws that affect taxpayer liability – it is clear that most states go on to raise additional taxes and fees (including sales, personal income, corporate income, motor fuels, alcohol, additional tobacco taxes, and/or fees) within just a few short years of a tobacco tax increase being approved.

Table 4. States Increasing Net Annual Tax/Fee Burden within Two Years of a Tobacco Tax Hike

Fiscal Year	Number of States with Tobacco Tax Hikes	Number of States with Subsequent Tax/Fee Hikes
2006	10	8
2005	10	4
2004	15	10
2003	19	15
2002	3	3
2001	2	1

Source: compiled from National Association of State Budget Officers⁸ data

As shown by the above chart, 41 of 59 state tobacco tax increases between fiscal years 2001 and 2006 were followed by tax hikes in the two-year period following enactment. In other words, taxpayers faced a 7 out of 10 chance of seeing another net annual tax hike within two years of a tobacco tax increase. Tobacco tax hikes don't serve as a permanent fix to the over-spending problem many states bring upon themselves, and new sources of revenue are often tapped even after a tobacco tax hike is put into place.

It's worth noting that many of the above revenue actions took place during a period of strong economic growth, high energy prices (important for states like Montana and Alaska that rely on mineral extraction fees), and hefty budget surpluses. Even in an "up" economy, tobacco taxes have not historically forestalled other tax increases.

4. Tobacco Tax Hikes May Encourage Other Tax Hikes Down the Road

Many recent tobacco tax hike plans have been tied to specific spending boosts, particularly in the area of health and education. If the program expansion of choice is related to state-provided health care (e.g., Oregon's defeated Measure 50), proponents argue that the higher tax is really just a "user fee" for smokers.

However, the non-smoker should look upon the dedication of tobacco tax funds to expensive new government programs with a wary eye. Once spending demands eventually outstrip revenues brought in from cigarette taxes, the non-smoker can expect to be called upon to fill in the budget gap.

Tobacco use rates are declining,⁹ and with it, potential tax collection earnings for the state. Even high-tax activists accept that cigarette tax revenues will be reduced over time as smoking declines. These same campaigners even argue that "the state can easily adapt"¹⁰ to such changing revenue dynamics. Non-smoking taxpayers should hope that "easily adapt" translates into proportional cuts in spending. Otherwise, to make up the difference the government will need to rely on a sudden burst of new smokers (unlikely) or tax hikes on other activities and products. Given that many states have balanced budget requirements, someone or something will likely be targeted for new taxes if spending eclipses tobacco tax intake.

Citizens are already seeing new taxes on the horizon in states that approved new spending in conjunction with higher tobacco taxes. Arizona Governor Janet Napolitano was quoted making a pitch to residents to buy cigarettes (but not smoke them) because “we need the money from cigarettes”¹¹ to fill a \$1.3 billion budget hole partly caused by new education spending mandates. Her request may have been tongue-in-cheek, but the need to cover the budget deficit is all too real.

Similar budget warnings helped to derail a 2008 California plan to tie a major run-up in the state’s health care spending to a tobacco tax increase of \$1.75 per pack. A fiscal examination from the California Legislative Analyst’s Office noted that the tobacco revenues connected to this plan “would decline over time because of the well-established ongoing erosion of smoking activity unrelated to this measure.”¹² The estimate found that funds from the new taxes would fall short of the program’s outlays by anywhere from \$300 million to \$1.5 billion in its fifth year. Other tax hikes (or, less plausibly, spending cuts) would have been needed fairly soon to cover the program’s costs.

This isn’t a concern that’s limited to the states. In 2006, proponents of expanding federal support for the State Children’s Health Insurance Program incorporated a 61-cent-per-pack hike in the federal tobacco tax to “pay” for their plan. However, a Heritage Foundation study¹³ found that in five years 9 million new smokers would be needed just to provide enough revenue to keep the program afloat. Over a 10-year outlook, 22.4 million new smokers would be required if the government didn’t want to rely on revenue from income taxes, etc., to fund the program. This potential burden to non-smokers was among the key reasons the plan was defeated.

Ironically, schemes that tie dedicated program funding to higher tobacco taxes would make government increasingly reliant on revenues extracted from the very product whose use among citizens it supposedly hopes to extinguish. Unless non-smokers want to pick up the tab later on, they should reject calls for tobacco tax hikes, especially when they are tied to specific high-cost spending programs.

Furthermore, if non-smokers accept tax hikes that target a minority of the population, they are tacitly opening the door for broad-based tax hikes that attack other “politically incorrect” activities, such as enjoying fast food. Once legislators see they can get away with this type of pinpointing, there’s no way of telling when and where they’ll stop.

5. Tobacco Taxes Don’t Spur Economic Growth

Another dubious claim made by pro-tax advocates is that the new revenue brought in from tobacco tax hikes somehow “helps” the economy. Says one such group, “Directing the new state government revenues generated by the cigarette tax increase to reduce state budget deficits or to fund economically productive programs or projects will further strengthen and improve the state’s economy.”¹⁴ Again, data shows this isn’t necessarily the case.

Nineteen states approved tobacco tax hikes in fiscal year 2003 (the largest one-year number in recent history). If the claim that revenue from tobacco tax hikes “improves the state’s economy,” these 19 states should experience greater-than-average economic growth within a few years

(providing enough time for the revenue to circulate through programs, etc.) than states that didn't adopt tobacco tax hikes.

**Table 5. 2005-2006 Percentage Change in GDP Growth
for 2003 Tobacco Tax Hike States**

State	Percent GDP Growth
Connecticut	2.6
Hawaii	4.3
Illinois	3.0
Indiana	2.0
Kansas	3.4
Louisiana	1.7
Maryland	2.9
Massachusetts	2.9
Michigan	-0.5
Nebraska	2.2
New Jersey	2.9
New York	3.4
Ohio	1.1
Oregon	5.0
Pennsylvania	1.7
Rhode Island	1.8
Tennessee	3.0
Utah	7.2
Vermont	2.8
Average	2.8
U.S. Average	3.4
Difference	-0.6

Source: compiled from Bureau of Economic Analysis data¹⁵

Comparing the percent change in real (i.e., inflation-adjusted) gross domestic product (GDP) by state between 2005 and 2006 (estimated by the Bureau of Economic Analysis), states that adopted a tobacco tax hike in fiscal year 2003 actually had a lower average growth rate (0.6 percent less) than those states that did not adopt a tax increase.

It makes sense that tobacco taxes don't strengthen the economy because the very act of taxing extracts needed capital resources out of the private market and directs them to less efficient government uses. If elected officials actually had the ability to improve the economy with tax hikes, we'd never experience any economic downturns. As this isn't the case, state legislators can best create an environment favorable to economic growth by promoting noninvasive tax policies.

Conclusion

Whether or not an individual uses tobacco, tax hikes hurt everyone by encouraging the growth of government. As demonstrated in this Issue Brief, high cigarette taxes reflect a tendency to grow total tax burdens. Furthermore, tobacco tax hikes rarely precipitate tax relief elsewhere or even stave off future tax hikes. If tied to new spending, tobacco tax hikes can trigger future tax hikes once cigarette revenues decline. Finally, tobacco tax hikes don't correlate with economic growth.

While tobacco tax increases will assuredly come up as funding "solutions" in the future, taxpayers – smokers and non-smokers alike – would be better served by extinguishing such a notion and instead focusing on cutting the size of government.

About the Author

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Notes

¹ Federation of Tax Administrators, "Cigarette Tax Increases 2000-2007," http://www.taxadmin.org/fta/rate/cig_inc02.html.

² Federation of Tax Administrators, "State Excise Tax Rates on Cigarettes," January 1, 2007, <http://www.taxadmin.org/fta/rate/cigarette.html>.

³ Tax Foundation, "Facts & Figures Handbook: How Does Your State Compare?," March 1, 2007, <http://www.taxfoundation.org/publications/show/2181.html>.

⁴ Federation of Tax Administrators, "State Excise Tax Rates on Cigarettes," January 1, 2007, <http://www.taxadmin.org/fta/rate/cigarette.html>.

⁵ Tax Foundation, "Facts & Figures Handbook: How Does Your State Compare?," March 1, 2007, <http://www.taxfoundation.org/publications/show/2181.html>.

⁶ Campaign for Tobacco-Free Kids, <http://www.tobaccofreekids.org/research/factsheets/pdf/0227.pdf>.

⁷ National Governors Association and National Association of State Budget Officers, "The Fiscal Survey of the States," December 2000 through December 2007, <http://www.nasbo.org/publicationsReport.php>.

⁸ *Ibid.*

⁹ Centers for Disease Control and Prevention, "Targeting Tobacco Use: The Nation's Leading Cause of Preventable Death," May 24, 2007, <http://www.cdc.gov/nccdphp/publications/aag/osh.htm>.

¹⁰ Campaign for Tobacco-Free Kids, "Responses to Misleading and Inaccurate Cigarette Company Arguments Against State Cigarette Tax Increases," <http://www.tobaccofreekids.org/research/factsheets/pdf/0227.pdf>.

¹¹ Elizabeth Jackman, "Gov: AZ Must Go Forward Despite Deficit," *The Glendale Star*, January 25, 2008.

¹² Elizabeth Hill, California Legislative Analyst's Office, January 22, 2008.

¹³ Michelle C. Bucci and William W. Beach, "22 Million New Smokers Needed: Funding SCHIP Expansion with a Tobacco Tax," The Heritage Foundation, July 11, 2007, <http://www.heritage.org/Research/HealthCare/wm1548.cfm>.

¹⁴ Campaign for Tobacco-Free Kids, <http://www.tobaccofreekids.org/research/factsheets/pdf/0227.pdf>.

¹⁵ Bureau of Economic Analysis, "State Economic Growth Widespread in 2006," June 7, 2007, http://www.bea.gov/newsreleases/regional/gdp_state/gsp_newsrelease.htm.