

## Excise Taxes

### Talking Points

- Adult smokers increasingly face higher prices for their cigarettes as the government raises cigarette excise taxes. In addition, because these taxes are based on the product and not on income level, cigarette excise taxes are regressive, impacting low-income smokers more than high-income smokers.
- The tax is unfair. Revenue from these tax increases often is used to fund general government spending that benefits all Americans. It is unfair to force one subsection of the population – adult tobacco users – to fund general government programs.
- Tobacco excise tax increases may be costly to retailers and small business owners. When users of tobacco products react to a tax increase by shifting their purchases across state lines or to other sources, such as Native American territories or over the Internet, where taxes are often not collected, in-state retailers lose sales & revenues. The impact of this purchasing shift on retailers becomes even more pronounced when tobacco purchases are bundled with other products, such as gasoline and groceries.
- The effect of tobacco excise tax increases is not limited to the tobacco segment of the retail community. The Joint Committee on Taxation (“JCT”) notes that “because smokers are paying more in aggregate to smoke, they consume less of other goods and services in the economy. This implies that incomes of producers and workers in other sectors will decline.” In fact, when estimating the revenue increase from a tobacco excise tax increase, the JCT offsets gross revenues by 25% to account for decreases in income and payroll tax revenues.
- Tobacco excise tax increases provide additional incentives for smuggling. As stated by John D’Angelo of the Bureau of Alcohol, Tobacco, Firearms and Explosives, “There is no doubt that there’s a direct relationship between the increase in a state’s tax and an increase in illegal trafficking.” It may also accelerate the growth of imports of counterfeit cigarettes manufactured in China and many other countries around the world.
- Cigarette excise taxes are a poor solution for state funding needs. States may receive less revenue than they anticipate from a cigarette tax increase, which can result in short and long-term fiscal problems for the state.
- In the short-term, the amount of revenue that a cigarette tax will raise can be very difficult to predict. This is illustrated by the fact that of the 57 state excise tax increases that were implemented between FY 2003 (which began July 1, 2003) and FY 2007 (which ended June 30, 2007), only 16 of them met or exceeded the projected revenues.
- Tax-paid cigarette sales in the U.S. continue to decline each year. According to data reported by Orzechowski & Walker, total state tax-paid sales have declined by an average of 3.0% per year from 1999-2008. In FY08, tax-paid sales declined by 5.0%. As a result, taxing jurisdictions that rely on cigarette taxes realize less and less revenue and may face gaps in funding in the long-term. Earmarking cigarette tax revenues for programs with growing costs compounds this problem.

1. Joint Committee on Taxation, Modeling the Federal Revenue Effects of Proposed Changes in Cigarette Excise Taxes, (JCT-101-07), October 19, 2007.

2. Maria Schultz, Raised Tax on Smokes May Stoke Illicit Sales, DETROIT NEWS, (July 21, 2002).

3 State Cigarette Excise Tax Increases: A Comparison of Projected versus Actual Revenue FY 2003 -2006, FISCAL PLANNING SERVICES, INC., (January 1, 2008); prepared for and funded by Altria Corporate Services, Inc.

5 Thomas Capehart, Tobacco Outlook, USDA-ECONOMIC RESEARCH SERVICE, TBS No. 254 (April 23, 2003).

5 Bill Orzechowski & Rob Walker, The Tax Burden on Tobacco, vol. 42 (February 2008); funded in part by Altria Client Services Inc. According to the Tax Burden on Tobacco Table 3 page 6, total cigarette consumption in 1981 was 633.3 billion cigarettes. In 2007, total cigarette consumption was 374.7. The average percentage change based on a compound annual growth rate calculation was approximately -2.0%.