

# CAMPAIGN For TOBACCO-FREE Kids®

## RAISING STATE CIGARETTE TAXES ALWAYS INCREASES STATE REVENUES (AND ALWAYS REDUCES SMOKING)

Every single state that has significantly raised its cigarette tax rate has enjoyed substantial increases to state revenues, despite the fact that cigarette tax increases reduce state smoking levels and despite any related increases in cigarette smuggling or cigarette tax avoidance. Put simply, the increased tax per pack brings in far more new state revenue than is lost through the related reductions in the number of packs sold and taxed in the state.

As detailed in the table below, every state that increased its cigarette tax from 2000 to 2002 has enjoyed large revenue increases despite above-average consumption and pack-sale declines. Although there is not yet sufficient data to calculate the year-to-year revenue and pack-sale changes for the numerous state cigarette tax increases from late 2002 through 2004, preliminary data from the states that have recently raised their cigarette tax rates confirms that state cigarette tax increases always raise state revenues despite reducing pack sales. Previous versions of this factsheet showed that states that passed cigarette taxes prior to 2000 enjoyed similar large revenue increases, consumption declines, and reduced pack sales. In sharp contrast, those states that have failed to increase their cigarette taxes have experienced gradual tobacco tax revenue declines caused by ongoing reductions in state smoking levels.

### State Experiences With Cigarette Tax Increases 2000-2002

State	Date	Tax Increase Amount (per pack)	New State Tax (per pack)	State Pack Sales Decline	Nationwide Pack Sales Decline	Revenue Increase (percent)	New Revenues (millions)
Connecticut	4/02	61¢	\$1.11	-12.6%	-6.7%	+116.3%	+\$133.8
Hawaii	7/02	20¢	\$1.20	+0.2%	-5.4%	+12.7%	+\$8.0
Illinois	7/02	40¢	\$0.98	-27.6%	-5.4%	+38.5%	+\$178.6
Indiana	7/02	40¢	\$0.555	-16.7%	-5.4%	+206.5%	+\$227.9
Louisiana	7/02	12¢	\$0.36	-14.5%	-5.4%	+12.1%	+\$11.9
Maine	10/01	26¢	\$1.00	-7.3%	-6.7%	+26.9%	+\$20.0
Maryland	6/02	34¢	\$1.00	-13.5%	-6.7%	+32.2%	+\$63.7
New Jersey	7/02	70¢	\$1.50	-17.6%	-5.4%	+51.0%	+\$199.8
New York	3/00	55¢	\$1.11	-20.2%	-5.7%	+57.4%	+\$365.4
Ohio	7/02	31¢	\$0.55	-6.8%	-5.4%	+109.4%	+\$281.6
Rhode Island	7/01	29¢	\$1.00	-5.0%	-1.4%	+33.7%	+\$19.7
Rhode Island	7/02	32¢	\$1.32	-10.0%	-5.4%	+18.9%	+\$14.8
Utah	5/02	18¢	\$0.695	-4.1%	-6.7%	+15.4%	+\$6.6
Washington	1/02	60¢	\$1.425	-18.8%	-6.7%	+42.1%	+\$99.6
Wisconsin	10/01	18¢	\$0.77	-7.6%	-6.7%	+20.6%	+\$50.2

Sources: Orzechowski & Walker, *Tax Burden on Tobacco*, 2004. Consumption declines and revenue increases calculated from the last full fiscal year (7/1 to 6/30) before the tax increase to the first full year after it. Nationwide consumption declines are for the 50 states and DC. The power of state tax increases to reduce consumption would be even more apparent if each tax-increase state's pack sale declines were compared to the overall change in pack sales among all the other states that did not increase their cigarette taxes in the same time period. Utah's relatively small decline resulted from the state raising its cigarette tax only modestly and, even more, from Utah already having the lowest smoking rates in the country before its cigarette tax increase.

### False Cigarette Company Claims About Smuggling & Tax Avoidance

The cigarette companies and their allies falsely argue that cigarette tax increases will not produce substantial amounts of new state revenue because they will prompt enormous surges in cigarette smuggling and smoker efforts to evade the higher taxes through cross-border or internet cigarette purchases. It is amazing that the companies make this argument given the established fact that ***every single state that has significantly increased its cigarette taxes has significantly increased its revenues – despite the lost sales from related smoking declines and despite any increases in cigarette smuggling or other tax-avoidance.***

Research also shows that smuggling and tax avoidance are relatively minor problems, especially compared to the additional new revenues, public health benefits, and smoking-caused cost reductions from state cigarette tax increases. An economic research study published in 2003 study found that all state smuggling and tax avoidance revenue losses totaled less than eight percent of total state cigarette tax revenues (with those losses concentrated in the highest-tax states).<sup>1</sup> Similarly, a 2005 study found that all smuggling and tax evasion accounted for less than ten percent of all cigarette sales.<sup>2</sup> In California, a survey found that soon after the state's 50-cent cigarette-tax increase went into effect in 1999 no more than five percent of all continuing smokers were purchasing cigarettes in nearby states, from Indian reservations or military bases, or via the internet, or were otherwise avoiding the state's cigarette tax.<sup>3</sup> It is also clear that states can implement a range of measures to sharply curtail any tobacco tax evasion or cigarette smuggling that may be occurring.<sup>4</sup>

It also appears that many smokers who initially try to avoid large state cigarette tax increases soon use up their stockpile of cigarettes purchased right before the increase or tire of driving across state border or going to the internet to buy cheaper cigarettes and return to the convenience of normal full-tax purchases in their own state.<sup>5</sup> Indeed, the vast majority of smokers prefer to buy cigarettes by the pack, but cross-border and internet purchases involve multiple cartons.<sup>6</sup> For example, New York state's taxable pack sales decreased sharply in the year after the state's 55-cent tax increase in March 2000, beyond what consumption declines might explain, but then increased in the following year (despite new consumption-reducing price increases by the cigarette companies) -- most likely because of smokers' depleted pre-increase stockpiles of cigarettes, tax-avoidance fatigue, and the strong appeal of convenient single-pack purchases from nearby sales outlets.

It is also worth noting that any real or imagined problems with smuggling and tax avoidance after New York State's cigarette tax increase in 2000 were not significant enough to stop the state from increasing its cigarette tax again, by 39 cents, in 2002, to \$1.50 per pack. Nor did it stop the state from permitting New York City to increase its supplementary local cigarette tax from 8 cents to \$1.50 per pack a few months later. Because of these State and City increases, the combined cigarette tax rate in New York City of \$3.00 per pack is much higher than the current or proposed rate in any other state or city. The levels of cigarette smuggling and tax avoidance in New York City are also supposedly the highest in the country. But in the first year there was a nine-fold increase to the City's cigarette tax revenues, to \$250 million (significantly more than the City had expected).<sup>7</sup>

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***For more on the benefits from state tobacco tax increases, see the Campaign website at:***

***<http://tobaccofreekids.org/reports/prices> & <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=18>.***

***For information on cigarette company involvement in cigarette smuggling, see***

- <http://www.tobaccofreekids.org/research/factsheets/pdf/0044.pdf>

***For steps states can take to prevent and reduce cigarette smuggling and cigarette tax evasion, see***

- <http://tobaccofreekids.org/research/factsheets/pdf/0274.pdf>.

<sup>1</sup> Farelly, M. et al., *State Cigarette Excise Taxes: Implications for Revenue and Tax Evasion*, RTI International, May, 2003, [http://www.rti.org/pubs/8742\\_Excise\\_Taxes\\_FR\\_5-03.pdf](http://www.rti.org/pubs/8742_Excise_Taxes_FR_5-03.pdf). See, also, Yurekli, A. & P. Zhang, "The Impact of Clean Indoor-Air Laws and Cigarette Smuggling on Demand for Cigarettes: An Empirical Model," *Health Economics* 9:159-170, 2000. Farelly, M. et al., *Impact of Cigarette Excise Tax Increases in Low-Tax Southern States on Cigarette Sales, Cigarette Excise Tax Revenue, Tax Evasion, and Economic Activity*, RTI Int'l, September, 2003, [http://www.rti.org/pubs/8742\\_Southern\\_Neighbors\\_FR\\_9-18-03.pdf](http://www.rti.org/pubs/8742_Southern_Neighbors_FR_9-18-03.pdf) [low-tax states gain substantial revenue from cigarette tax increases, despite losing sales to smugglers, internet sellers, and customers from higher-tax states].

<sup>2</sup> Stehr, M., "Cigarette Tax Avoidance and Evasion," *Journal of Health Economics*, 24(2): 277-297, March, 2005, [http://www.ncbi.nlm.nih.gov/entrez/query.fcgi?cmd=Retrieve&db=pubmed&dopt=Abstract&list\\_uids=15721046](http://www.ncbi.nlm.nih.gov/entrez/query.fcgi?cmd=Retrieve&db=pubmed&dopt=Abstract&list_uids=15721046).

<sup>3</sup> Emery, S et al., "Was There Significant Tax Evasion After the 1999 50 Cent Per Pack Cigarette Tax Increase in California?," *Tobacco Control* 11: 130-34, June 2002, <http://tc.bmjournals.com/cgi/reprint/11/2/130.pdf>.

<sup>4</sup> See, e.g., Campaign factsheet, *State Options to Prevent and Reduce Cigarette Smuggling and Block Other Illegal Efforts to Evade State Tobacco Taxes*, <http://tobaccofreekids.org/research/factsheets/pdf/0274.pdf>.

<sup>5</sup> See, e.g., Spencer, M., "Incensed Smokers Stock Up Before Tax Rises," *Hartford Courant*, April 3, 2002.

<sup>6</sup> Quinn, C., "Tobacco Ad Fight Headed to Court: 3 Companies Want to Keep Philip Morris From Grabbing Retail-Counter Display Space," *Winston-Salem Journal*, June 7, 1999 [65% of cigarette sales are individual packs according to papers filed in federal lawsuit against Philip Morris by the three other largest U.S. cigarette companies].

<sup>7</sup> New York City Department of Finance.