



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

Every single state that has raised its cigarette tax rate has subsequently received more tax revenue than they would have received without a rate increase, despite the fact that cigarette tax increases reduce state smoking levels and despite any related increases in cigarette smuggling or tax evasion. Put simply, the increased tax per pack brings in more new state revenue than is lost from the related reductions in the number of packs sold and taxed in the state. Moreover, the substantially higher revenue levels enjoyed by those states that significantly increase their cigarette tax rates persist over time (while the cost savings from the related smoking declines grow rapidly).<sup>1</sup>

The table below shows states with cigarette tax increases greater than 50 cents from 2006 to 2008, with each state enjoying large revenue increases in the following 12 months (compared to the prior 12 months) despite related consumption and pack-sale declines. Tax increases of less than 25 cents per pack or 10% of the average state pack price do not produce significant benefits because cigarette companies can easily offset the small increases with coupons and other promotional discounting. Data from earlier state cigarette tax increases show the same kinds of positive results (as documented in previous versions of this factsheet), and subsequent state tax increases will show the same, as well, once the data is available. In sharp contrast, those states that fail to increase their cigarette taxes typically experience gradual cigarette tax revenue declines from year to year caused by ongoing reductions in state smoking levels.

### State Revenue Gains from Recent Cigarette Tax Rate Increases

State	Effective Date	Tax Increase Amount (per pack)	New State Tax Rate (per pack)	State Pack Sales Decline	Nationwide Pack Sales Trend	Revenue Increase	New Revenues (millions)
Arizona	12/8/06	82¢	\$2.00	- 32.5%	- 4.4%	+ 13.6%	\$44.5
Delaware	7/31/07	60¢	\$1.15	- 35.1%	- 4.9%	+ 35.1%	\$31.8
Washington, DC	10/1/08	\$1.00	\$2.00	- 25.9%	- 7.0%	+ 57.3%	\$13.2
Iowa	3/15/07	\$1.00	\$1.36	- 30.6%	- 4.7%	+ 140.2%	\$128.0
Maryland	1/1/08	\$1.00	\$2.00	- 27.1%	- 4.2%	+ 45.8%	\$126.9
Massachusetts	7/1/08	\$1.00	\$2.51	- 20.3%	- 5.3%	+ 32.2%	\$137.8
New York	6/3/08	\$1.25	\$2.75	- 15.2%	- 5.8%	+ 40.3%	\$377.4
South Dakota	1/1/07	\$1.00	\$1.53	- 25.8%	- 4.9%	+ 115.4%	\$31.8
Texas	1/1/07	\$1.00	\$1.41	- 21.0%	- 4.9%	+ 191.7%	\$1,003.7
Vermont	7/1/06	60¢	\$1.79	- 15.2%	- 3.0%	+ 27.9%	\$13.2
Wisconsin	1/1/08	\$1.00	\$1.77	- 15.0%	- 4.2%	+ 93.9%	\$283.0

Sources: Orzechowski & Walker, *Tax Burden on Tobacco*. U.S. Alcohol and Tobacco Tax and Trade Bureau. Consumption declines and revenue increases are for the 12 months before and after the tax increase. Nationwide consumption declines are for the 50 states and DC. Trends for rate increases after January 2008 include the impact of the 61.66-cent federal cigarette tax increase (effective April 1, 2009).

### False Cigarette Company Claims about Smuggling & Tax Evasion

The cigarette companies and their allies continue to make the clearly false argument that cigarette tax increases will not produce substantial amounts of new state revenue because the increases will prompt enormous new surges in cigarette smuggling and smoker tax evasion. *But every single state that has increased its cigarette taxes has received more revenue than it would have collected absent a rate increase – despite the lost sales from related smoking declines and despite any increases in cigarette smuggling or other tax-evasion.*<sup>\*</sup>

<sup>\*</sup> By increasing its cigarette tax by 17.5 cents in 2006, New Jersey increased its cigarette tax revenues for the following years, but not enough to offset all of the declines already underway because of various other factors that were reducing cigarette sales in the state, such as the new smoke-free law. Consequently, state revenues declined modestly from 2006 to 2007, but the revenue decline would have been much larger without the rate increase (and a larger cigarette tax increase would have brought in even more revenues). It is inaccurate for tobacco industry critics to say that the 2006 NJ cigarette tax increase caused state revenues to decline when the rate increase clearly brought the state more revenues than it would have received without any tax increase.

In fact, research shows that smuggling and tax evasion not only fails to eliminate revenue gains from cigarette tax increases but is also a much smaller problem than the cigarette companies and their allies claim (especially when compared to the additional new revenues, public health benefits, and smoking-caused cost reductions from state cigarette tax increases). For example, a 2003 economic research study found that state smuggling and tax evasion revenue losses totaled less than eight percent of total state cigarette tax revenues (with those losses concentrated in the highest-tax states).<sup>2</sup> Similarly, a 2005 study found that all smuggling and tax evasion accounted for less than ten percent of all cigarette sales.<sup>3</sup> In California, a survey found that soon after the state's 50-cent cigarette-tax increase went into effect, less than five percent of all continuing smokers were trying to evade the state's cigarette tax.<sup>4</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>5</sup>

After a cigarette tax increase, many smokers who initially try to avoid the higher rate 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. 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 – most likely because of smokers' depleted pre-increase stockpiles of cigarettes, smoker tax-evasion 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 evasion after New York state's cigarette tax increase in 2000 were not significant enough to stop the state from increasing its cigarette tax to \$1.50 per pack in 2002, and, more recently, to \$2.75 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 in 2002. The levels of cigarette smuggling and tax evasion in New York City are supposedly among the highest in the country; but in the first year after its 2002 rate increase revenues increased nine-fold, to \$250 million, significantly more than the city had expected.<sup>7</sup>

When the tobacco industry's false argument that states will not get additional revenues from raising cigarette tax rates is rejected, the cigarette companies and their allies often fall back to arguing that states have not received as much new revenue "as expected" from their cigarette tax increases. But such "less than expected" results are just a matter of some states making overly optimistic revenue projections that fail to account for ongoing smoking declines and all the smoking reductions and other pack sales declines prompted by cigarette tax increases.<sup>8</sup> As shown above, no matter what the cigarette companies say, they cannot get around the key fact that cigarette tax increases are a powerful tool for reducing smoking and increasing state or local revenues.

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**More information on the benefits from state tobacco tax increases are available at**

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

<sup>1</sup> See, e.g., Campaign for Tobacco-Free Kids (TFK) Factsheet, *Tobacco Tax Increases are a Reliable Source of Substantial New State Revenue*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0303.pdf>.

<sup>2</sup> Farrelly, 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 & Zhang, P, "The Impact of Clean Indoor-Air Laws and Cigarette Smuggling on Demand for Cigarettes: An Empirical Model," *Health Economics* 9:159-170, 2000.

<sup>3</sup> Stehr, M, "Cigarette Tax Avoidance and Evasion," *Journal of Health Economics*, 24(2):277-297, March 2005.

<sup>4</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>5</sup> See, e.g., TFK 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>. See, also, the TFK factsheet, *The Many Ways States Can Raise Revenue While Also Reducing Tobacco Use and Its Many Harms & Costs*, <http://tobaccofreekids.org/research/factsheets/pdf/0357.pdf>.

<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].

<sup>7</sup> TFK Factsheet, *The New York City Experience: New Revenues from a \$1.42 Per Pack Cigarette Tax Increase*, <http://tobaccofreekids.org/research/factsheets/pdf/0307.pdf>.

<sup>8</sup> For more on this additional false argument against state cigarette tax increases, see the TFK Factsheet, *Responses to Misleading and Inaccurate Cigarette Company Arguments Against State Tobacco Tax Increases* [at point II], <http://www.tobaccofreekids.org/research/factsheets/pdf/0227.pdf>.