

# IRET Congressional Advisory

INSTITUTE FOR RESEARCH ON THE ECONOMICS OF TAXATION

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## WHAT ARE THEY SMOKING?

Voters in Arizona, California, Missouri, and South Dakota are being asked to approve ballot measures on November 7 to raise their state cigarette taxes substantially. The expected revenue would supposedly be earmarked for various good works, such as health care for the uninsured, child care spending, recreation, environment, or property tax relief.

Is this proposed rise in the tobacco tax good public policy? No. The ballot questions are best seen as ploys to get a majority vote for a tax hike by imposing the tax on a minority and pretending that the money will be earmarked for good causes.

A tax on a minority is bad public policy. A good tax is borne by everyone, showing them that government is not a free good. Otherwise, what would stop the majority from making the minority pay for everything the majority consumes?

We are nearly there for the federal income tax. The top 5 percent of income earners now pay over 50% of the progressive income tax. People in the bottom half pay less than 4% of the tax and often get money back after wage and child credits. For them, government spending other than Social Security is a free good. The poor are soaking the rich.

Excise taxes are also bad taxes. They affect only a few selected products, hit hardest those people who most value them, and let others off lightly. The tobacco tax is a good example. Smokers are an unpopular minority being smacked

by the majority. Unlike the income tax, cigarette taxes are highly regressive, for two reasons. First, a pack-a-day habit takes a bigger chunk out of a low annual income than a high one. Second, upper income individuals tend to smoke less than lower income people. Richer non-smokers don't pay the tax, and can use it to shift some of the cost of state spending to poorer smokers.

The higher tax will induce some smokers to cut back, so the revenues will not rise in proportion to the tax rate. The states will also have higher costs of enforcement to counter additional smuggling and evasion, which they have mostly not considered. In California and Arizona, much of the remaining hoped-for revenue is pledged to child health or welfare programs. California, Missouri, and South Dakota would raise spending for hospitals and HMOs to help cover emergency room costs and other care for the poor and uninsured. California pledges a bit of the revenue to environmental protection, recreation, and general state spending. Most of the proposed spending is welfare. Most is already-mandated state spending. Only one measure, in South Dakota, would devote some of the tobacco money to tax relief (specifically, lower property taxes).

There is no good reason to stick smokers with the cost of either property tax relief or welfare programs. Why should low income smokers who rent pay for property tax relief for higher income non-smokers who own homes? Why should welfare support costs be borne by a lower-income minority of the taxpayers? To create a false connection to

smokers, the California, Missouri, and South Dakota initiatives promise to spend some small part of the money on anti-smoking campaigns (about 10% in the California initiative), as if that somehow justifies the sting. The tax does not benefit smokers. They would lose twice: they would have to pay more for cigarettes and would have to listen to more anti-smoking ads that call them idiots.

Can this earmarking to "good works" even be trusted? No, the money could be diverted to other uses at the whims of the legislatures, with no increases for the favored programs. Whatever the states are already spending on health or anti-smoking or other promised programs could be diverted to other uses and replaced by the new tax money, without violating the initiatives. That assumes the states would even bother to go through the motions. According to the Government Accountability Office, about 70% of the famous

1998 tobacco settlement, which awarded \$240 billion just in the first 25 years to 46 states, and which was widely pledged for anti-smoking and public health purposes, is being diverted to the states' general budgets for other uses.

Non-smokers win only if the tobacco revenue relieves them of some of the cost of existing state spending, and gives them a tax cut. If the legislatures simply spend the extra money on additional outlays, it would benefit only the direct recipients of the largesse. Before voting for a tax increase, voters should ask themselves, "Whom do I trust?" If their inner voices answer, "The legislature," then others should ask them, "What are you smoking?"

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