

SIGNIFICANCE OF A DECLINE IN CIGARETTE USE ON TAX REVENUES

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"WHERE there's smoke, there's fire" is a time-worn adage. To the tax official, "where there's smoke, there's revenue" is a time-tested fact; a great deal of revenue as we are all aware.

The federal government's tax on cigarettes, eight cents a pack, produced some 2 billion 63 million dollars in the fiscal year ended last June 30 (1965).

The states derived nearly one billion 200 million dollars from their taxes on tobacco products in their fiscal years ending in 1964. Local governments also tapped this source, among them New York City, whose four-cent tax on cigarettes yielded \$41 million in the city's fiscal year ended last June 30 (1965).

A sharp rise in the revenue of the states can be expected in next year's figures which will reflect the legislation of 1965. By August 1, 22 states had increased their cigarette tax rates, an all-time high for the number of states taking such action in any one year. In Hawaii and New York the rate was doubled, New York becoming one of three states with a rate of ten cents a pack.

Rates throughout the states range from 0 in North Carolina and Oregon to eleven cents in Texas and Washington. The most frequent rate, eight cents, is found in 21 states (Table 1); Oregon has enacted a four-cent tax to become effective July 1, 1966, if approved by popular referendum.

In New York, cigarettes are also subject to the state retail sales tax of 2 per cent, which became effective Au-

gust 1, and to the local sales taxes imposed in New York City and several of the larger upstate counties and cities at rates ranging from 1 per cent to 3 per cent.

The budget of New York State for the present fiscal year calls for 3 billion 251 million dollars in total current revenue. The cigarette tax is expected to produce 230 million dollars, 7 per cent of this total.

Why is it that the cigarette is called upon to support in its fragile column so great a weight of taxation? The answers lie in the rising demands upon the revenue sources of the states and their municipalities, in the field of tax theory, and in the patterns of human behavior.

The factors causing extreme pressure on the resources of state and local governments—the rapid rise in expenditures for public education, health, mental health, care of the aged, highway construction and maintenance, and conservation of our natural heritage—are so well known as to require no elaboration here.

Changes in Revenue Systems

To meet these needs, many changes have been made in the revenue systems of the states in recent years. The base of taxation has been broadened and rates increased.

Any tax structure—state, federal, or local—has got to contain elements of progressivity on one hand and stability

on the other. Now, income, sales taxes, and estate taxes are illustrative of the principle of productivity. I mean by this, when times are good, the returns from these taxes increase commensurate with the times, however, they likewise decline when times are not so good.

Excise taxes on commodities are prime examples of stability. Thus, the yield for motor fuel taxes, because of the importance of the motor vehicle to our personal and commercial transportation, continues an uninterrupted growth as population and vehicle use rise, without much regard to fluctuations in the economy as a whole. We say the de-

mand for such a commodity as motor fuel is "inelastic."

The cigarette taxes are attractive as revenue producers because the habit of smoking is so entrenched in our society that, in this case again, demand has proved relatively inelastic over a long period. The yield of the cigarette taxes has followed an upward pattern as population in the smoking ages has increased. It has been our experience in the past in New York State, and it has been true quite generally, that a rise in price has had little or no lasting effect on consumption of cigarettes.

From the standpoint of equity, ciga-

Table 1—State cigarette tax rates per 20 regular size cigarettes (New York and adjacent states underscored)

State	Rate (Cents)	State	Rate (Cents)	State	Rate (Cents)
Alabama	7	Louisiana	8	Pennsylvania	8
Alaska	8	Maine	8	Rhode Island	8
Arizona	6½	Maryland	6	South Carolina	5
Arkansas	8	Massachusetts	8	South Dakota	8
California	8	Michigan	7	Tennessee	7
Colorado	5	Minnesota	8	Texas	11
Connecticut	8	Mississippi	9	Utah	8
Delaware	7	Missouri	4	Vermont	10
District of Columbia	2	Montana	8	Virginia	3
Florida	8	Nebraska	8	Washington	11
Georgia	8	Nevada	7	West Virginia	6
Hawaii	40% of Wholesale Price	New Hampshire	21% of Retail Value	Wisconsin	10
Idaho	7	New Jersey	8	Wyoming	4
Illinois	7	New Mexico	8		
Indiana	6	New York	10		
Iowa	8	North Dakota	8	Oregon	4
Kansas	8	Ohio	5		
Kentucky	2½	Oklahoma	8	North Carolina	No Tax

Source: CCR State Tax Guide ("All States" volume), Research and Statistics Bureau.

Effective
7/1/66 sub-
ject to voter
approval.

Table 2—Per capita consumption of cigarettes by persons 18 years of age and over (calendar years)

Year	United States	New York State
1950	3,522	
1951	3,744	
1952	3,886	
1953	3,778	} Cancer } State
1954	3,546	
1955	3,597	3,640
1956	3,660	3,792
1957	3,755	4,003
1958	3,953	4,209
1959	4,073	4,256
1960	4,172	4,273
1961	4,266	4,373 ← High
1962	4,265	4,356
1963	4,345 ← High Surgeon General's Report	4,319
1964	4,196 ← High Surgeon General's Report Prelim. Estimate	4,190 ← Surgeon General's Report
1965	4,318	—

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1964 figure shows decline of 1.6% from 1961 and 3.4% from 1963.	1964 figure shows decline of 4.2% from 1961.
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1965 estimate indicates rise of 2.9% from 1964.

Source: National Tobacco Tax Association. (Data derived from revenue figures.)
New York State Department of Taxation and Finance, Research and Statistics Bureau.

rette taxes have the advantage of being imposed on a commodity which is not a basic necessity. No matter how much we may enjoy smoking, we must concede that we have a clear choice whether to smoke or not to smoke. In this sense, the tax is self-assessed.

Drop in Consumption

The Surgeon General's Report of January 11, 1964, like the publicity given to the suspected health hazards of cigarette smoking in the early 1950's caused a temporary, rather sharp fall-

ing-off in consumption. The figures in Table 2 show the trend of per capita consumption both nationally and in New York State for persons 18 years of age and over.

Nationally, per capita consumption by persons in the smoking ages has risen from 3,522 cigarettes in 1950 to 4,345 in 1963, with an interruption of the upward trend in 1953 and 1954, and a temporary leveling off in 1962. In 1964 per capita consumption declined 3.4 per cent from the previous year, reacting to the Surgeon General's Report. The estimate for 1965, however, indicates a

reversal of the decline, for a 2.9 per cent rise from 1964.

The New York State figures available since 1955 show much the same pattern as the national data. In New York, however, the highest per capita figure, 4,373 cigarettes, was reached in 1961, followed by a tapering off in 1962 and 1963, and a sharper decline in 1964 after the release of the Surgeon General's Report. New York's decline from 1961 to 1964 was 4.2 per cent, considerably greater than the nation-wide decline of 3.4 per cent in the same period.

The figures for New York State cigarette tax revenue in Table 3, when expressed as the amount of tax collections per one cent of the tax rate, show a gradually rising trend over the past 15

years. The figures for the state's fiscal years ending March 31, 1954 and 1955, show declines due to the onset of the cancer scare, followed by a quick resumption of the upward trend. Again, the Surgeon General's Report broke the upward trend temporarily with a decline of 2 per cent in the 1964 fiscal year from the level of 1963.

In this table, it is interesting to note the effect of the increases in the rate of tax on April 1, 1959, when New York's rate was raised from three cents to five cents, and in 1965 immediately prior to the change from five cents to ten cents. In both cases smokers, stocking up in advance of the rate increase, pushed revenues up sharply.

State tax collection data compiled by the Tobacco Tax Council for the period

Table 3—New York State cigarette tax revenue

Fiscal Year Ended March 31	Net Collections	Rate of Tax per Pack	Collections per One Cent of Tax	% Change from Preceding Year
1950	\$ 56,684,179	3¢	\$18,894,726	—
1951	58,485,330	3¢	19,495,443	+3.2%
1952	59,768,830	3¢	19,922,943	+2.2
1953	61,608,862	3¢	20,536,287	+3.1
1954	60,011,398	3¢	20,003,799	-2.6 ← Cancer
1955	58,141,385	3¢	19,380,462	-3.1 ← Scare
1956	59,716,478	3¢	19,905,493	+2.7
1957	61,532,421	3¢	20,510,807	+3.0
1958	63,947,670	3¢	21,315,890	+3.9
1959	68,893,225	3¢	22,964,408	+7.7 ← Smokers stock up before rate increase
1960	114,767,193	5¢	22,953,438	-.05 ← Lag due to higher rate and unusually high previous year
1961	120,227,074	5¢	24,045,414	+4.8
1962	123,541,454	5¢	24,708,290	+2.8
1963	125,483,548*	5¢	25,096,709*	+1.6
1964	122,982,433	5¢	24,596,486	-2.0 ← Surgeon General's Report
1965	127,036,024	5¢	25,407,204	+3.3 ← Smokers stock up before rate is doubled

* Figure adjusted to eliminate effect of a change in deposit procedure which inflated 1963 actual collections to \$131,983,343.

New York State Department of Taxation and Finance, Research and Statistics Bureau.

Table 4—Monthly cigarette tax collections in New York State (calendar years 1963 to 1965)

(In Thousands)

	1963	1964	1965
January	\$ 10,191	\$ 9,710	\$ 9,275
February	9,560	7,827	9,177
March	8,595	8,549	12,243
April	11,350	10,510	17,835
May	11,688	9,799	16,748
June	10,058	11,128	19,658
July	11,148	11,576	20,105
August	11,044	10,499	19,491
September	10,302	10,777	19,054
October	11,047	10,533	
November	9,453	10,277	
December	10,806	11,241	
	\$125,242	\$122,426	

← Surgeon General's Report, Jan. 11
 ← Smokers stock up in advance of rate increase in April
 ← Smokers stock up in advance of sales tax
 ← Cigarettes subject to 2% state sales tax and local taxes ranging from 0 to 3% effective August

New York State Department of Taxation and Finance, Research and Statistics Bureau.

January through April, 1965, give evidence of the resurgence in cigarette sales as the effect of the Surgeon General's Report wore off. In the first four months of 1965, seven and a half billion packages of cigarettes were taxed by the states, an increase of 10 per cent over the number taxed in the January through April period a year earlier.

The upturn in cigarette sales in 1965 is the more striking because the decline in the earlier months of 1964 had been very widespread. Out of 45 states reporting, all but five showed declines in per capita consumption from 1963 to 1964. These ranged from one-tenth of one per cent in South Carolina to 12.5 per cent in South Dakota. The decline

in per capita consumption in New York was 3.8 per cent for this period. These particular per capita comparisons are related to the entire population, not just the population of smoking age. The trend is clear, whatever series is used.

It is too early to tell whether the doubling of the New York State cigarette tax rate six months ago, or the increases which other states have effected, will have any lasting effect in reducing the amount of cigarette smoking (Table 4). In March, 1965, the month immediately prior to the effective date of the New York tax increase, there was a great increase in sales because cigarette smokers stocked up in advance. The revenues for the next two months declined, but June,

July, August, and September have shown considerable recovery.

We shall have to look to the 1966 figures to see whether the increases in cigarette taxes will produce any depressing effect upon consumption.

In spite of the revenue needs of the states, it is difficult to see how such drastic rate increases as we have had in the past two years could be accepted by the smoking public, if society as a whole were beginning to have some concern about the effect of smoking on health. Governor Rockefeller, in recommending the increase from five cents to ten cents per pack in his Budget Message to the 1965 Legislature, recognized this concern. He said: "In view of the pressing revenue needs of the

state, and the potential health hazard associated with cigarette smoking, an increase in this tax is warranted."

It remains to be seen whether the increased cost of cigarettes, reflecting the recent sharp tax increases coupled with the public health factor, will overcome the pattern of the past. If the past repeats itself, we shall see a sharp recovery in consumption after the initial impact of the rate increases wears off. In the meantime, the United States Department of Agriculture, in its publication "The Tobacco Situation" for September, 1965, makes the following forecast: "Due mainly to continuing growth of the number of persons of smoking age, cigarette consumption in 1966 is likely to increase to a new high."

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