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Sebelius' Cigarette Tax Proposal Ignores Economic Realities

Once again, a politician has decided to take aim at "Big Tobacco" – this time, it's Kansas' own Kathleen Sebelius. During a recent press conference, Governor Sebelius said she plans to put a 50 cent per pack cigarette tax increase "right back on the table." Unfortunately for the governor, hiking taxes on smokers is one of the least effective ways to raise long-term revenue for the state.

Cigarette taxes always look attractive to lawmakers on paper, as revenue forecasters often show a windfall of projected receipts from the tax. However, in the real world, people respond to incentives and cigarette taxes have been shown to encourage smokers to avoid high-tax jurisdictions. As state after state has learned, the promise of substantial cigarette tax revenue often goes up in smoke.

Take the state of Maryland for example. Last year, state lawmakers doubled the state's cigarette tax to \$2.00 per pack to pay for additional health care and balance the budget. Of course they expected a revenue boom to help fix their state's unstable finances. However, they were sorely mistaken, as the *Wall Street Journal* reports that cigarette sales are down 25%. In fact, nearly 30 million fewer cigarettes have been sold in Maryland since the tax increase this year. Therefore, the cigarette tax, which was supposedly the panacea for the state's budget woes, has come up short, and lawmakers in Annapolis are back to the drawing board.

Retailers in Maryland have seen their cigarette sales plummet because of good old fashion competition – and in this case, specifically tax competition. Just across the Potomac River, Maryland residents can take full advantage of the lower taxes in Virginia. Maryland's neighbor to the south has one of the lowest cigarette taxes in the nation at 30 cents per pack. Such a cost difference with a bordering state has made it profitable for Maryland drivers to venture down Interstate 95 into the Old Dominion, saving \$1.70 a pack in cigarette taxes alone. Maryland has responded with hopeless attempts to control out of state cigarette purchases with investigations and searches of suspected "tax evaders" on the border.

Only a few states in the nation have lower cigarette taxes than Virginia. Unfortunately for Governor Sebelius and the other cigarette tax hikers in Kansas, neighboring Missouri is one of them. The Show-Me State levies a tax of only 17 cents per pack of cigarettes, which is the second lowest cigarette tax in America.

With competitors like these sitting just across Kansas' border, it should make every policymaker in Topeka very aware that changes to policy are not created in a vacuum. Every time a state changes tax policy, it directly and immediately influences the incentives of individuals and businesses – in this case, smokers.

If Governor Sebelius is successful and Kansas lawmakers adopt the proposed cigarette tax increase, the tax would increase to \$1.29 per pack. At that point, the tax cost per pack of cigarettes would be \$1.12 lower in Missouri – not to mention Kansas' tax would be the highest of any bordering state. Even House Minority

Leader, Dennis McKinney has publicly acknowledged the difficulty of Kansas competing with Missouri if the tax increase passed.

As lawmakers in Maryland have painfully learned, states cannot expect that cigarette taxes will raise enough revenue to solve budget problems, or expand health coverage. Furthermore, states cannot expect smokers to ignore the incentive to purchase their cigarettes in bordering states – especially when that incentive is high enough. Just think of the thousands of residents in Johnson County who would only be a short drive away from significant savings on tobacco products.

Unfortunately, with politically charged topics such as these, it is easy for some public policy leaders to lose sight of basic economic realities. However, it is clear that the proposed tobacco tax increase will fail to raise the revenue suggested. Not only will consumers have a greater incentive to purchase their cigarettes across state lines, today they can evade the increased taxes in the comfort of their own home, through the Internet.

Politically, cigarette taxes are an easy sell because they target a fraction of society and involve a socially unpopular activity. However, cigarette taxes are strikingly bad public policy. As Governor Sebelius is striving to put the cigarette tax hike “back on the table,” maybe she ought to think again.

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