

80th Annual FTA Tobacco Tax Conference Industry Forum

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Evaluating the Effectiveness of Tax increases

■ Goals & Objectives

Governments levy excise taxes on cigarettes & tobacco products for two reasons:

- to raise tax revenue
- to discourage smoking



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- Excise tax revenues have become an integral part of budgeting tools to offset deficits and balance budgets for most states.



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■ Effects of Excise Tax on Cigarette Prices

- Cigarette price goes up with each cigarette tax increase

■ Price Elasticity of Cigarette Demand

- The basic law of economics—that of the downward sloping demand curve:
 - Cigarette price \uparrow -- Cigarette Consumption \downarrow
 - Cigarette price \downarrow -- Cigarette Consumption \uparrow



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■ Effects on Price and Smoking Prevalence

- The changes in smoking resulting from the price changes are dependent upon:
 - changes in the number of smokers
 - the amount of cigarettes consumed by smokers.
- The changes in the number of smokers are caused by:
 - smoking cessation, initiation, and re-initiation.

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■ Effects on Price and Smoking Prevalence

- Because of the addictive nature of cigarette smoking, the long-term response to a permanent price change will be larger than the initial, short-term response, as some smokers gradually adjust to the new prices and these gradual adjustments add to the initial impact of price on some smokers.
- Conventional wisdom argues that people who are addicted to nicotine are less sensitive to price than others.
- Measuring Long-term vs. Short-term impacts



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■ Impact of cigarette prices on youth smoking

- Economic theory suggests several factors that would make youth smokers more sensitive to price increases than adult smoking:
 - Youth smokers have been smoking for a shorter time are likely to be less addicted than older smokers, and as a result will quickly adjust to the price changes.
 - Youth have lower incomes, making them relatively more responsive to changes in cigarette prices.
 - Peer Pressure is very important among youth.



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■ Effects on the health care system

- Smoking causes lung cancer, mouth diseases, heart diseases & other health problems
- Strains on the health care system
- Studies indicated that 8 out of 10 smokers who developed cancer would die within 5 years



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- Responses to Tax Increases by Manufacturers
 - Philip Morris developed a “defense plan” in 1989 in response to CA’s Proposition 99 to offset the short run impact. The defense plan included discount coupons, multipack discounts, value packs, etc.
 - RJR’s plan included postage paid reply cards in cartons that would allow smokers to let their Congressperson know of their opposition to the tax hike.



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■ Does Tax Increase Reduce Smoking?

- Research studies by various Health Organizations
- Statistics reported by surveys & studies
- Measuring long-run results against short-run results
- What about the missing pieces (outside of the statistics)?

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■ The Missing Pieces

- Consumers are crossing state lines to purchase cigarettes from lower-taxed jurisdictions
- Consumers are buying untaxed cigarettes over the Internet & Mail orders
- Consumers are buying untaxed Native cigarettes



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■ The Negative Impacts of Tax Increases

- Encourages Illegal Cigarette Smuggling Activities
- Thefts and Robberies are on the rise
- Counterfeit/Contraband Products & Cigarette Tax Stamps
- Black Market & Underground Market
- Internet Sales & Mail Orders
- Links to Organized Crimes
- Links to Terrorism

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- Are Tax Increases Effective?

You be the judge!!!

