Cornell Law Review

Volume 36
Issue 4 *Summer 1951*

Article 4

Cigarette Tax A Study in Discriminatory Legislation

Benjamin Werne

THE CIGARETTE TAX — A STUDY IN DISCRIMINATORY LEGISLATION

*Benjamin Werne**

I. Introduction

The cigarette tax becomes an increasingly difficult problem as we move towards a mobilized economy. Long a political football, the levies continue to mount from three flanks—federal, state and municipal. Legislators seize this means to raise funds for operational expenses, without regard for the impairment of a major industry, peril to the tobacco farmer and injustice to the smoking consumer.

A look at the record of price increases for the pack of cigarettes highlights the inequity of the tax burden. Over a period of 10 years, the price for a package of cigarettes has been raised *only 2¢* per pack *by the manufacturer.* The price line has been held despite increases in the cost of raw tobacco, upward spiralling of wages, increased freight tariffs and mounting cost of other supplies. Scientific and technological improvements have been made in every aspect of manufacturing cigarettes, from methods of curing and seasoning to packaging. Yet, although the cost of living (according to the Bureau of Labor Statistics) has risen 75% in 10 years, the manufacturer gets only one penny more for cigarettes.

During this same period, however, the Federal government has taken an added 1¢ in taxes, the states an average of 3¢ and municipalities an average of 2¢. Those added taxes explain the higher price you pay for cigarettes today!

In their widening search for new sources of revenue to bolster sagging budgets, federal, state and local legislators alike have come up with a slogan that seems to have magnetic appeal: *Your Best Bet is to Tax the Cigarette.*

The bandwagon rush to this unfair, inequitable, hidden type of excise tax has reached alarming proportions. Cigarette and tobacco taxes are mounting without regard to the needs and rights of those being taxed, without regard to the threat to a vital industry in our national economy—and, possibly most important, without regard to the dangers inherent in such a tax system. Once the consuming public has submitted to and "accepted" the excessive tax burden on one such commodity in regular daily use, other unreasonable levies will follow.[1] An expanding tax sys-

* See Contributors' Section, Masthead, page 688, for biographical data.

[1] *Cf.* the statement in the Annual Report of the Comptroller of the State of Texas, pt. I, 211 (1947). Consumer demand for goods and services, states the report,

tem follows the path of least resistance, not necessarily the wisest or soundest one.

II. Triple Pyramid of Taxes

Just how extensive is the tobacco tax pattern? Is it really excessive? Here are the facts: The federal government, 40 states[2] and more than 75[3] cities have cigarette taxes. In some cases, the consumer must contribute to all three governments every time he purchases a single pack.[4]

The first time taxes were imposed on cigarettes was by the federal government in 1865.[5] The annual per capita consumption was 11 cigarettes and the tax produced $11,495 that year.[6] This constituted only 5% of the total revenue produced from the federal tax on snuff.[7]

It was 24 years later—1889—before the annual revenue from the cigarette tax produced a million dollars.[8] In 1920 the annual per capita consumption had reached 419 cigarettes.[9] That year federal cigarette tax receipts reached $151,300,000 and exceeded 50% of total receipts from taxes on all tobacco products.[10] Today cigarette taxes exceed 93% of the total receipts from taxes on all tobacco products—and the annual per capita consumption is more than 2300 cigarettes.[11] From 1913 to 1942 the federal tax on cigarettes was gradually raised from $1.25 per thousand to $3.50 per thousand. Federal receipts in 1949 totalled $1,242,000,000.[12]

The federal tax on a package of cigarettes is 7¢.[13] The resident of a state which has not yet levied a tax on cigarettes, and who consumes a pack a day, pays an annual tax of $25.55.

Forty states and the District of Columbia tax cigarettes.[14] The range

"has driven state revenue skyward by producing additional taxes on the products for which the demand has been so great."

2 Address of W. P. Hedrick of the N. C. Tobacco Advisory Council, Raleigh, N. C., before 1950 convention of the National Association of Tobacco Distributors. Reported in 1950 Convention Diary of An N.A.T.D. Member 55 (1950).

3 *Ibid.*

4 *Compare* app. 5 *and* 7.

5 Address of W. P. Hedrick, *supra* note 2.

6 The Cigarette Tax 4 (The Nat. Tobacco Tax Research Council, Richmond, 1950).

7 *Ibid.*

8 *Ibid.*

9 *Id.* at 5.

10 *Ibid.*

11 Annual Report on Tobacco Statistics, 1950 (Production and Marketing Administration, Dept. of Agriculture, Washington, D. C.) Statistical Bull. No. 92, pp. 50, 55.

12 NATD Co-ordinator 62 (Nat. Ass'n of Tobacco Distributors, N. Y., March 1950).

13 *Id.* at 283.

14 Address of F. M. Parkinson, reported in 1950 Convention Diary of An N.A.T.D. Member 51 (1950).

is from 2¢ to 8¢. The average is 3¢. Six of the states take a nickel on every package; nine others collect 4¢.

In the seven states officially listed as without taxes, the situation is not what it seems. Among the states which do not exact such taxes are Maryland, Virginia and North Carolina—but note that Baltimore, Md., and Lynchburg, Va., have city cigarette taxes. And Baltimore usually means Maryland, since that city has 48% of the state's population and does 61% of the state's total retail sales.[15] Missouri has no state tax, but fifteen cities within Missouri have a 2-cent-per-package tax.[16] These cities contain over 43% of the state's population and account for 75% of the state's retail sales. Wyoming and Colorado have no state tax, although Denver and Pueblo, Colorado, have city cigarette taxes.[17] These two cities, by the way, contain over 37% of the entire state's population and account for 50% of the state's retail sales. Finally, in the Far West we find California and Oregon with no state cigarette tax, although California[18] has a formidable substitute in the form of a sales tax assessed by approximately 130 municipalities.

III. First State Tax in 1921

It was not until the depression days of the early 20's that the states cut into this pie. Iowa enacted a tax in 1921. By 1925 seven others followed the lead. Another spurt came in the thirties. In most of the early cases, the legislatures were aware of the unsound features of the tax and professed to be enacting "emergency" measures—but the emergency never seemed to pass. In fact, more states passed the measures and the pioneers went about raising the rates. In 1949 alone, 11 states enacted a levy or raised their own taxes.

State	Effective Date of Rate Change	Rate Change
Florida	Nov. 1	from 4¢ to 5¢
Georgia	July 30	from 3¢ to 5¢
Massachusetts	Sept. 1	from 4¢ to 5¢
Minnesota	Apr. 26	from 3¢ to 4¢
Nevada	July 1	from 2¢ to 3¢
New Mexico	June 10	from 3¢ to 4¢
North Dakota	July 1	from 3¢ to 5¢
Vermont	June 1	from 2¢ to 4¢
Washington	Nov. 28	from 2¢ to 4¢
Wisconsin	July 21	from 2¢ to 3¢

15 *Ibid.*

16 *Ibid.*

17 *Ibid.*

18 *Ibid.*

Delaware and the District of Columbia enacted cigarette taxes which became effective on July 1 and August 1, 1949, respectively.[19]

Almost 400 million dollars went into state coffers from this tax in 1948. The revenue increased 145% from 1945 to 1949, rising from 3% to 4% of total state tax revenues.[20]

The tobacco industry today is the second largest producer of federal and state tax revenue in the nation![21]

To complete the picture, municipalities and other local units are turning to this lucrative source of revenue which never seems to dry up. Seventy-five cities collected more than $25,000,000 in 1949.[22] Twenty or more states have granted added taxing powers to city and other local governments in "home rule" moves since World War II. The executive director of the Tax Institute, Inc., has stated[23] that "the most important aspect of the new look in municipal finance is the turn to new local tax sources. The cities are demanding, and the legislatures are granting, ever-increasing tax privileges. The wisdom of some of these privileges is questionable. . . ."

Pennsylvania's Act 481,[24] effective in June, 1947, authorized 3600 municipalities and school districts to impose taxes on any subject not levied upon by the state. In California, a state tax enabling act led to a mushroom growth of sales taxes.[25] New York followed in the same path soon after the end of World War II.[26]

Birmingham, Alabama, collected annually over half a million dollars.[27] Denver took in a third of a million.[28] Kansas City's intake runs over $1,000,000 each year.[29] St. Louis nets 1¼ million dollars a year.[30]

Florida, in addition to raising the state levy in 1949, took steps to make cigarette taxes a source of municipal revenue.[31] Municipalities

---

19 COMPARATIVE STATE TOBACCO TAX COLLECTIONS: 1947 7 (Nat. Tobacco Tax Ass'n, Chicago, 1950).

20 Address of F. M. Parkinson, reported in 1950 CONVENTION DIARY OF AN N.A.T.D. MEMBER 51 (1950).

21 FEDERAL EXCISE TAXES ON TOBACCO (U. S. Treasury Dept., Division of Tax Research, Washington, D. C.) February, 1948. No. S-640, pp. 1-31.

22 THE CIGARETTE TAX 6 (The Nat. Tobacco Tax Research Council, Richmond, 1950).

23 Walker, *Municipal Revenue Trends,* MUNICIPAL FINANCE 37-42 (Nov. 1949). See also Walker, *Factors Affecting Municipal Revenues,* MUNICIPAL FINANCE 15-20 (Aug. 1947).

24 PA. STAT. ANN. tit. 53, § 2015.5 (1947).

25 See note 23 *supra.*

26 *Ibid.*

27 Address of W. P. Hedrick, reported in 1950 CONVENTION DIARY OF AN N.A.T.D. MEMBER 56 (1950).

28 *Ibid.*

29 *Ibid.*

30 *Ibid.*

31 Barker, *Florida Municipalities Receive Cigarette Tax Revenue,* THE MUNICIPALITY 72 (April 1950).

were granted the power to tax up to the full rate of the state tax, with 5¢ per pack as the maximum state-wide rate.

More than 175 cities of Florida's total of 240 have passed cigarette levies![32] To emphasize the character of this tax, it should be noted that it is designed to give direct relief to the property taxpayer. Cities adopting this tax must reduce annual ad valorem levies by 50% of their increase in their current cigarette tax yield and that of the preceding year. In most Florida cities, which had never taxed cigarettes in the past, property tax collections will be reduced by a full 50% of the first year's yield.[33] Levies will not be used for any specific purpose, but will apply to a broad range of activities, including streets, sanitation, health, hospitals and public safety. Why should a single commodity like the cigarette bear the burden of general welfare financing?[34]

IV. State Expenditures Jump

Adoption of new services, a huge backlog in capital improvements, expansion of programs already underway, and the decrease in purchasing price of the dollar have combined to boost state expenditures at a far higher rate than revenues in the post-war period. A superficial glance at the chart[35] of the movement of state revenue and expenditure from 1943-1948 discloses:

Fiscal Year	State General Revenue (in millions)	% Increase	State General Expenditure (in millions)	% Increase
1948	$10,025	18	$10,400	28
1947	8,481	18	8,099	27
1946	7,198	7	6,404	7
1945	6,729	2	5,997	1
1944	6,605	5	5,929	1
1943	6,277	3	5,882	1

If there is any doubt about what these statistics signify in terms of state debt, it should be noted that the gross debts of state and local governments reached new peaks in 1949. A few more figures will show the brief history of that debt. Note in the following table[36] the sharp

32 *Ibid.*

33 *Ibid.*

34 The enlightening article in the April 1950 issue of The Municipality, note 31 *supra*, details how the Florida League of Municipalities put over the tax which it describes as a "windfall." The article declares that the strategy by which the tax was imposed was "fostered by an alert legislative staff, but would have been impossible without strong friends in the ruling committees. . . ." In addition, the author states, "the new taxes have been accepted by the public with unexpected equanimity."

35 See note 21 *supra*.

36 National Municipal Review, Feb. 1951, p. 104.

rise through 1932, moderate change until 1940, the wartime decline and the sharp post-war rise.

STATE AND LOCAL DEBT
(in millions)

Year	State	Local	Total
1922	$1,163	$ 9,093	$10,256
1930	2,444	16,015	18,459
1932	2,896	16,680	19,576
1940	3,526	16,720	20,246
1946	2,358	13,564	15,922
1947	2,978	13,847	16,825
1948	3,722	14,980	18,702
1949	4,024	16,851	20,875

Where do the states go for this revenue? To the commodities for which demand has been greatest. Says a Federation of Tax Administrators report:[37]

"Tobacco taxes were among those most frequently turned to by state legislatures for additional revenues."

What elements make for a structurally sound tax measure?

Local revenue structure says one expert,[38] should be "adequate, stable and equitable." Business is attracted to a city "with a balancd budget and tax system which would remove the constant fear of new types of taxes that *might be* imposed."[39] The cost of government should be borne on a broad tax base. A sound tax is one "based on benefits and tied very closely to ability to pay."

An earlier analytical report[40] sets up three standards to test a sound revenue system:

"A satisfactory tax system will as far as possible require those who receive special direct, measurable benefits from government to contribute enough to cover the costs involved.

". . . will be made up of taxes which are as unobjectionable as possible from the standpoint of the taxpayer. . . .

"The system as a whole . . . should be distinctly progressive. Progressive taxes are in the interest of preserving the community, of improving consumption and of maintaining the ability of the factors of production. These may be added principles of sound justice."

37 TRENDS IN STATE FINANCES 1949, RESEARCH REPORT No. 26 (Federation of Tax Administrators, Chicago, 1949).

38 Culver, *How Shall Business Be Taxed?* MUNICIPAL FINANCE 21-23 (Aug. 1950).

39 *Ibid.*

40 SCHMIDT, AN APPRAISAL OF THE NEBRASKA TAX SYSTEM 27 *et seq.* (U. of Neb., Lincoln, 1946).

Delegates to a recent national conference[41] on taxation heard these criteria for state legislatures outlined:

1) adequacy
2) economic and political stability
3) "sources of revenue should respect the familiar concept of ability to pay"
4) taxes should entail "minimum collection and compliance costs"

Later on, the same convention heard R. G. Burke, a speaker noted in the field, say: "The zeal for additional revenue, born perhaps out of despair, has frequently dulled the minds of responsible officials. . . . The important thing seems to be—tax and collect."[42]

How does the cigarette tax measure up against the above-mentioned criteria?

V. Tax Affects Poor and Rich Alike

The tax is a regressive one. There is no relationship between one's economic status or what he earns or what he can afford and the amount of the tax he pays. The bank president and the bank teller stopping at the tobacco stand on the way to work pay the same tax for their cigarettes.

Because of the nature of the tax, it falls most heavily on those least able to pay. Low income groups are hit hardest because they spend relatively more on the items that are taxed. To take a not-too-extreme example, if two members of a Louisiana family average three packs a day between them, their annual cigarette tax would be over $164.00. That is more than three times the amount the average worker has to pay in federal income taxes in one year.[43] Roughly 60% of the cost per pack of cigarettes paid by the consumer represents taxes of one sort or another—this on an item that represents 3.8% of total expenditures for consumer goods.[44] Table 1 in the Appendix shows how excise taxes bear most heavily on those least able to pay.

VI. Tax Leads to Loss of Business

The tax often cuts the local businessman two ways. First, the housewife may have to cross an item off her shopping list to compensate for the high price of tobacco with its excessive tax burden. Rather than forego the carton of her favorite brand, the shopper will overlook the purchase of an equally necessary commodity. But if it were not for that extra tax bite, there would be more cash to spend on other items.

---

41 Proceedings of the Forty-first Annual Conference of Taxation 14-15, 25-26 (Nat. Tax Ass'n, Denver, Colo., Oct. 4-7, 1948) (N.T.A., Sacramento, 1948).

42 *Ibid.*

43 The Cigarette Tax 5 (The Nat. Tobacco Tax Research Council, Richmond, 1950).

44 Tobacco Tax Facts 6 (The Nat. Tobacco Tax Research Council, Richmond, 1950).

The city, or even the state, that taxes cigarettes loses to the neighboring non-taxing area. A city or state that has a higher tax than an adjoining city or state likewise forfeits business to its lower taxing neighbor. Until New Jersey resolved the problem by imposing a tax of its own, New York City residents were purchasing a sizable portion of their cigarette supply across the river. Nor did the purchases end with just the pack or carton of cigarettes. There are always other commodities at hand. These represent purchases that would have been made in the home-town stores. This diversion of business from the taxing city is a permanent loss, running as high as 1 million dollars annually in some areas. (See Appendix 2.)

In 1949, the State of New Hampshire collected $2,300,000 from cigarette taxes. During that same period, the federal government collected an additional $3,700,000. That is a total of $6,000,000 paid annually by New Hampshire citizens for the privilege of smoking. Inasmuch as only about 45% of the population smoke, is it not fair to say that they are paying more than their share of the tax burden? In the face of these facts, how can an increase in the present tax on cigarettes be justified?

Figures for 1949 and other years show that the State of New Hampshire collects annually a half million dollars more than it is entitled to collect for cigarette taxes. It is an easy matter to explain this condition. States bordering New Hampshire all impose a higher cigarette tax. People, naturally, resent an excessive cigarette tax and will go to the extreme to evade it. It matters not how much gasoline they burn or how much time it takes. They make up for their inconvenience by making other purchases while on their mission to procure cigarettes where the tax is lower. Cities in New Hampshire which border the states of Maine, Vermont and Massachusetts, all do a thriving business with residents of those states; as a direct result, cigarette tax revenue in New Hamphire exceeds the amount due according to the per capita consumption.

It should be of interest to note that Massachusetts, because of its cigarette tax of 5¢ per package, lost over $3,000,000 in the amount of revenue due, and that the $3,000,000 sum showed up in excess revenue in New Hampshire, Maine, Connecticut and Rhode Island.

Eleven states show an excess in the amount of revenue due from a cigarette tax predicated upon the per capita consumption. Arizona has a 2¢ state tax. The excess collected amounts to more than $150,000 annually.

At least one state, Arkansas, tried to meet the diversion problem by providing for a different tax rate in border-line cities where the tax in an adjoining out-of-state city was different. But revenue continued to drop off at an alarming rate.[45] Merchants experienced a severe loss of business to neighboring Missouri where there was no tax. In 1949, the Arkansas Legislature *cut* its cigarette tax rate from 6¢ to 4¢.[46]

St. Louis realizes that its tax is driving cigarette business out of the city. On the theory, evidently, that two wrongs make a right, the Missouri State Legislature has been asked for an enabling act to provide *the county* with the right to tax cigarettes.[47] Thus taxes breed more taxes.

Atlantic City, N. J., suffered a diversion of business because of the tax. Figures on this city may be examined in Table 3 of the Appendix.[48]

The case of Alexandria, Va., illustrates the extent of business diversion accompanying the tax. When Washington, D. C., enacted its 1¢ tax per pack, from 35-50% of its cigarette business plus other business moved to outlying cities. Much of the capital's working force is concentrated in these fringe areas. An Alexandria drug store chain reported increased cigarette sales amounting to $2,000 per month—and a general business spurt of 10%. Another chain increased cigarette business $35,000 in five months. A hardware company reported a 50% boost in cigarette sales. Then, Alexandria got the idea and adopted her own tax. During the first 21 days of the effective period of the tax, one of these stores reported the loss of the $2,000 cigarette business they had gained earlier, a loss of $4,000 of their own normal cigarette business and an overall drop of 14%.[49] Merchants kept accurate sales records covering a 3-months period before the tax and for the entire tax period. In December, 1950, enough city councilmen had seen the error of their ways to record a *unanimous vote to repeal the tax.* Alexandria decided it wished residents to do their Christmas shopping at home!

Earlier experiments with cigarette taxation have met with similar results. The date is different; the effect of the tax is the same. For example, Kansas City's council adopted an ordinance requiring the use of tax stamps early in 1927. It had been predicted that about $300,000 would be reaped from this tobacco harvest. Despite the fact that hundreds of dealers were hailed into court on bootlegging charges, gross receipts amounted to about $4,000 monthly. The public was aroused this time, the dealers were outraged—and there was little or no revenue.

45 TAX BARRIERS TO TRADE 120 (Tax Institute Symposium, Dec. 2, 1940) (Tax Institute, Phila., 1941).

46 TAX ADMINISTRATORS NEWS 18 (Feb. 1949).

47 U. S. TOBACCO J. 25 (Jan. 21, 1950).

48 See app., Table 3.

49 Communication from Tobacco Tax Research Council, Dec. 1950.

The law was finally repealed by the unanimous vote of the same council that passed the measure.[50]

It took lawmakers of Sedalia, Mo., only 11 weeks to realize what a big mistake they had made in the summer of 1933. During that short period, the tax was passed and repealed.[51]

VII. Tobacco Grower Affected

Maximum production is discouraged by the fact that the farmer's return is far less than the tax collected on tobacco products. Every time a grower gets $1 gross for his tobacco, the federal government alone gets $2.00. In 1948, for example, the farmer received $900 million for cigarette tobacco; federal and state governments took in more than twice that amount, over $1.8 billion.[52]

Unmistakable evidence of the harmful effect on the farmer was found by a Congressional committee headed by Representative Vinson of Georgia. Digging into the problem of double taxation (state and federal), the committee came up with these remarks:

> . . . the increased price for the product undoubtedly means decreased consumption thereof. All those connected with tobacco industries, the grower and manufacturer, will suffer by such decreased consumption.
>
> The tobacco tax is the only war tax and prohibition tax that remained unchanged during the prosperous years that followed its levy. It is the only excise tax levied upon agricultural products, with the exception of the tax on oleomargarine, which is placed thereon to benefit other farm products. In addition to the excise tax, tobacco bears the processing tax. Tobacco is the only commodity now paying a processing tax that likewise bears the burden of any excise tax.
>
> It is the thought of the tobacco grower expressed during the hearings that if the heavy hand of Federal taxation is lifted in part from his back, the consumption of his product will increase materially, and the general economic law of supply and demand will give him a living price for his tobacco without the necessity of having any artificial stimuli.[53]

VIII. Industry Investments Are Jeopardized

Taxes may well reach the dangerous point where consumption is threatened. It is well therefore to consider the tobacco industry's place in our over-all industrial and agricultural economy. A stable tobacco industry provides stability of employment; it fortifies an efficient and economic system of distribution to more than two-thirds of all the retail outlets of the United States; it provides a steady flow of income to more

---

50 The Truth About Tobacco Taxation by the States 21-24 (Tobacco Merchants Ass'n, N. Y., 1934). Kansas City had reenacted a cigarette tax in 1938.

51 *Ibid.*

52 Tobacco Tax Facts 2 (The Nat. Tobacco Tax Research Council, Richmond, 1950).

53 H. R. Rep. No. 1882, 73d Cong., 2d Sess. 9776 (1934).

than two million tobacco growers. It insures an uninterrupted need for the transportation services of the nation's rail and motor carriers; it affords credit accommodation to hundreds of thousands of aspiring, hard-working independent merchants, and is instrumental in nurturing and sustaining small business enterprises by providing a basic foundation of constant sales which, in their total effect, support the entire business and the sale of other merchandise. Credit Norman S. Rabb, vice-president in charge of merchandising of Stop & Shop, Inc.,[54] major New England super-market chain, with this estimate of the importance of cigarette sales:

> It seems to be generally agreed that the sales per square foot of space obtained from cigarettes exceed those of any other category of merchandise. Although the mark-up is usually far below the average for other lines sold in super-markets, the rapidity of turnover and the small space required for their sale are compensating factors.
>
> Super-market operators pay their bills and earn their profits in dollars, not percentages, and cigarettes can produce substantial gross profit dollars.

IX. Proposed Tax Boost Threatens Wholesalers

An acute refinancing problem would face wholesalers of cigarettes, and also retailers, if the proposed Treasury Department plan for a new 40% increase (an added 3¢ per pack) is approved.[55] The impact of such an increase would be reflected in three ways:

(1) the wholesaler would have to invest large amounts of new capital to do the same amount of business,
(2) greater credit risks, to the extent of the new tax, would have to be assumed, and
(3) there would be a substantial increase in operating costs.

Since the wholesaler pays the federal tax to the manufacturer as part of the invoice cost of cigarettes, additional capital will be needed to finance his business on the same scale as before. Thousands of small merchants, many already insecure, will be faced with the task of raising additional capital. The large chains and other giant enterprises will take up much of the business of these firms, contrary to persistent government efforts to bolster the small man.

Wholesale business will be jeopardized by the increased credit risk. Tobacco wholesalers extend credit to retailers on cigarette sales for as long as 30 days. The new tax would mean an increase in the credit extended for the same amount of merchandise. The only other alterna-

54 U. S. Tobacco J. 10 (Jan. 21, 1950).

55 Based on testimony before House Ways and Means Committee by Claude Harrison, president of NATD, March 8, 1951.

tive is to sell less, and cut revenue. This threat comes at a time when credit restrictions are being tightened and little cash is available.

If the wholesaler has to resort to a commercial loan, the interest rate alone may be enough to take away as much as 50% of his normal profit. Overall, tobacco distributors will have to find more than $40 million in additional capital to finance inventory cost increases and the cost of carrying accounts receivable.

Other operating costs will inevitably go up. Insurance rates will be boosted to take care of the higher inventory value. State inventory taxes and other similar expenses will rise. The impact on retailers will be just as severe under the circumstances.

X. Will Consumption Falter?

The idea that consumption might well be affected by too-high taxes is not just a figment of the imagination. A Federation of Tax Administrators report[56] on 1949 consumption has this to point out:

> Of the states in which cigarette consumption was 1,720 per capita or less, Oklahoma taxes at 5 cents a pack; Arkansas now levies a 4-cent rate, but taxed at 6 cents up to June, 1949. These figures do not reflect a true picture of actual consumption based as they are on tax assessed cigarettes, not those consumed by tax evaders.
>
> Utah's rate is only 2 cents a pack, but it borders two non-tax states, Colorado and Wyoming. Similarly, Kansas with a 3-cent rate has the non-tax states of Colorado and Missouri on its borders. Kentucky, with a 2-cent rate, also falls into this low consumption group.
>
> Five southern states which tax other tobacco products along with cigarettes also are among those in which tax collections indicate consumption of less than 1,720 cigarettes per capita. The high-tax states of Georgia (5 cents), Louisiana (8 cents) and Mississippi (4 cents) are in this group.
>
> Tax collections of Alabama and Tennessee, which levy a 3-cent rate, indicate higher per capita consumption than the former three states, although under the 1,720 mark.

For a long period of years, the annual increase in the federal revenue from taxes averaged 8%. Last year, it dropped to 1½% in the face of a tremendous population increase.

XI. Tax Stimulates Inflationary Wage Demands

It is common knowledge that the steady rise in wages, generated by the rising cost of basic necessities, is fast approaching dangerous heights. We have heard much of the old claim that, left to the ordinary play of competitive forces and the sound economic law of supply and demand, prices, however, far out of line, would eventually right themselves. By and large this has been true. Not, however, with cigarettes, because the

56 *Federation of Tax Administrators Report,* U. S. Tobacco J. 1, 6 (Aug. 12, 1950).

tax maintains price at a high level, without regard to any other factors.

Much of the history of labor-management bargaining reflects the struggle of workers to raise their earnings sufficiently to effect the increased cost of living, created not alone by price rises, but also by the imposition of millions in excise taxes on products of daily purchase and consumption. The consumer can expect, and in fact has received from time to time, some measure of relief, from record high prices of a great many basic commodities. The law of competition eventually takes care of that. But from the oppressive cigarette tax there is no relief—it stands inexorable, moving higher and higher.

How real is the wage increase, upon which managements and unions agree, when it is insidiously dissipated by the vicious force of an excise tax? If a price rise occurs, competition may check it. The occurrence of the slightest increase in price is exploited by vigilant competitors and an alert buying public. A cigarette tax rise is fixed by an arbitrary authority. There is no review of its necessity and no appeal from its finality.

XII. Enforcement Problems Are Severe

Enforcement chaos exists where the cigarette tax is concerned. No less an economist than Adam Smith warned in his classic, *The Wealth of Nations,* against taxes that "may require a great number of officers, whose salaries may eat up the greater part of the produce of the tax, and whose perquisites may impose another additional tax upon the people."[57]

Counterfeiting of tax stamps and meter machine dies, bootlegging and litigation are accompaniments of such an unevenly levied excise. Action had to be taken by the federal government in 1949 to assist the states in collecting cigarette taxes.[58] The Jenkins Act, Public Law #363,[59] was signed in October, 1949, to prevent evasion of the tax through mail order purchase. Shippers of cigarettes in interstate commerce to other than licensed distributors must report such shipments by the 10th day of the following month. If the Act is fully effective, mail order callers of cigarettes will go out of business. The law has been upheld in two out of three major suits and is now the subject of a criminal prosecution brought by the U. S. District Attorney in New Orleans.

In one major decision,[60] a special three-judge Federal Court unani-

57 2 Smith, Wealth of Nations 311 (4th ed. Cannan, 1925).

58 Tax Administrators News 112 (Oct. 1949).

59 63 Stat. ch. 699 (1949), 15 U. S. C. § 375 *et seq.* (1950 Supp.).

60 Consumer Mail Order Ass'n v. McGrath, 94 F. Supp. 705 (D. C. 1950), *aff'd, per curiam,* 71 Sup. Ct. 500 (1951).

mously upheld the Act's constitutionality. Circuit Judge Fahy's opinion stated that Congress exercised a valid authority over the regulation of interstate commerce in passing the law. (An appeal to the Supreme Court is expected.) The Act was challenged by the Consumer Mail Order Association of America, Joplin, Mo., and associated mail order firms. They charged violations of the commerce clause, and of the Fifth and Tenth Amendments, since the law involved taking property without due process. An improper mingling of federal and state functions was also charged. The case went directly to the special court.

Briefly, the other two suits are:

(1) One case was filed in U. S. District Court in Chicago by Edward Sales Co. of Hammond, Indiana. A declaratory judgment of unconstitutionality has been denied by the court.[61] Illinois was chosen because the state supreme court had earlier declared that individuals purchasing cigarettes outside the state were not liable to a tax because no use tax was in effect. A clause presuming that anyone who bought more than a specified number in a year was a retailer was declared unconstitutional.

(2) An individual, doing business as the Cooperative Buying Service, of Murphy, No. Carolina, is being prosecuted[62] for violation of the Act. The defense rests on the claim that the purchaser of cigarettes in a taxing state has asked a resident of a non-taxing state to act as his agent. Hence, the buyer is technically the shipper of cigarettes.

With buying services, purchasers' cooperatives and the like regaining a good portion of the business of the mail-order houses, a clearcut court victory will be necessary to end this phase of the cigarette tax dispute. Full enforcement will still require constant surveillance over post office box and truck deliveries, express packages and freight houses.

While waiting for official action and strict enforcement of this Act, states are losing revenue at an annual rate estimated at $40,000,000. If the states are losing that much in taxes, it can be argued that wholesalers and retailers in the states affected are losing something like $250,000,000 in diverted sales of tobacco products.

Actually, decreased revenues from the tax have been reported in the case of Birmingham, Ala. According to a statement[63] by W. L. Marshall, the Jefferson County Junior Auditor:

> . . . we find tobacco tax receipts decreasing while there is an increase in other lines. Whereas January, 1950, tobacco tax receipts show an

[61] Kaufman, *The Jenkins Act—Law to Ban Interstate Cigarette Bootlegging is a Product of Industry and Government Teamwork* (Nat. Assn. Tobacco Distributors, N. Y. 1951) pp. 45ff.

[62] *Ibid.*

[63] Reported in U. S. Tobacco J. 24 (April 22, 1950).

increase over 1949—$81,444 as compared with $79,665—in both February and March there was a decrease. Tobacco tax revenue for February, 1950, was $69,983 as compared with $73,626 for February, 1949; and $80,419 for March, 1950, as compared with $81,830 for March, 1949.

Administrative costs of such excises have not been too carefully studied. However, two reports[64] indicate cost of collection figures for tobacco taxes ranging between 1.4% and 8% of collections.

XIII. Cigarettes Are Not a Luxury

The burden of taxes on cigarettes and other tobacco products is explained away by some who claim they are a luxury. Are they? One could ask the GI's who were at posts all over the world during 1941-1945. They will relate that the exchange value of their little packs of "butts" far exceeded that of money or even food. Much of the globe was indeed on a cigarette standard. Or one may check the results of a nationwide survey[65] of super-market and service food stores conducted by the *Progressive Grocer*. It found that "a high percentage of shoppers now think of a carton of cigarettes like meat, soaps, or cereals, as a regular part of their weekly or semi-weekly grocery purchase." More than 5¢ in every dollar spent in food stores goes for cigarettes—it is the largest selling packaged product in the retail food business.

A little probing into American history uncovers the fact that tobacco was currency in colonial times. Metallic money was scarce; commodity monies had to be used. Tobacco was by far the most important, especially in the South. Up to the 18th century, it was recognized in Virginia and Maryland. Houses, cattle, furniture and food were bought and sold for what they would bring in tobacco. At its highest development, colonial Virginia provided for a form of warehouse receipt or "tobacco note" that was as good (maybe better) as your dollar bill is today.

To most consumers, the cigarette is far from an added comfort which they could and should do without. Most people find in them a constant and needed source of solace as important as bread itself. For the pleasure tobacco affords, they may well forego other needs. Is it reasonable to assume that the consuming public, including low income groups, spends nearly 4 billion dollars a year for a luxury? Does the use of 363 billion

---

64 Derrick, *Consumption Excise Taxes as a Relief for the Tax Burden on Farm Property*, Proceedings of the . . . Nat. Tax Ass'n 274 (1929). Shoup, Sales Taxes on Selected Commodities, Report of the Ky. State Comm'n for the Revision of the Tax Laws, Memo #6, Leg. Doc. No. 77, pp. 6-7, Table 1 (1932).

65 Mueller, *Cigarettes Now Lead Food Store Sales*, Tobacco World 104-105 (July 1950) (Mr. Mueller is Managing Editor of the Progressive Grocer.)

cigarettes in 1950 indicate they are a luxury? Cigarettes are a utility product that serve a needed and useful purpose.

XIV. Advertising Cost Is Minor

Because advertisements of cigarette, cigar and tobacco companies are constantly in the eye—and the ear—of the consumer, it is thought they constitute a major portion of the cost. Actually, they are so small that the consumer would save practically nothing if advertising were entirely eliminated. According to a recent Treasury Department survey, the advertising expenditure per package is "substantially smaller than the price differential that appears to be necessary to stimulate the sale of an unadvertised brand."

XV. Summary and Recommendations

For all the reasons cited

—because the taxes are discriminatory
—because they bear excessively on the industry
—because they threaten the farmer, the wholesaler and the retailer
—because the pyramided levies amount to more than the basic value of the product
—because cigarettes are a necessity, not a take-it-or-leave-it luxury

for these commanding reasons early action must be taken. Millions of consumers—and voters—are demanding that the burden be eased. What, then, can be done?

First, the dangerous tendency to slap another cent or two tax on cigarettes, and on cigarettes almost exclusively, whenever the time seems ripe, must be halted. The tax burden must be equalized.

Second, where possible, a reduction of taxes is advisable. Certainly the excise tax passed in haste as a stop gap measure should be rescinded. Various states and cities, after a calm reexamination of tax policies, will find it is vital to reduce the cigarette impost.

Third, to be equitable, more careful enforcement of tax measures is desirable.

Fourth, to enable states to avail themselves of the Jenkins Act provisions, "use" taxes should be provided in those states without such taxes.

APPENDIX I

The following table will illustrate the gross inequity of the cigarette tax because of its oppressive burden upon those least able to pay. Excise tax is shown as percentage of consumer income for 1938-1939.

Income	Excise Tax Federal	Excise Tax State
Under $500	3.0%	4.3%
500- 1,000	2.9%	3.5%
1,000- 1,500	2.8%	3.6%
1,500- 2,000	2.8%	3.9%
2,000- 3,000	2.7%	4.0%
3,000- 5,000	2.4%	3.7%
5,000-10,000	1.9%	3.1%
10,000-15,000	1.5%	2.7%
15,000-20,000	1.3%	2.3%
20,000 and over	0.8%	1.6%

Table from WHO PAYS THE TAXES, 12 (TNEC Monograph 3, 1940).

APPENDIX II

Gain or Loss in Revenue by Cigarette Taxing States†

	State	Population 1950	1949 Cigarette Tax Revenue	1949 per Capita Revenue	Gain or Loss in Revenue
1¢	West Virginia	1,998,536	$ 2,084,000	$ 2,198,389	$ 114,389—
2¢	Arizona*	742,364	1,795,000	1,633,200	161,800+
	Iowa	2,609,748	4,951,000	5,741,445	790,445—
	Kentucky	2,931,588	4,969,000	6,449,493	1,480,493—
	Montana*	587,196	1,329,000	1,291,831	37,169+
	Ohio	7,901,791	17,870,000	17,383,940	486,060+
	Utah	686,842	872,000	1,511,052	639,052—
3¢	Alabama	3,052,395	7,559,000	10,072,903	2,513,813—
	Connecticut	1,994,818	7,389,000	6,582,899	806,101+
	Idaho	586,037	1,633,000	1,933,922	300,922—
	Illinois	8,696,490	28,407,000	28,698,417	391,417—
	Indiana	3,917,904	12,297,000	12,929,083	632,083—
	Kansas	1,898,519	4,843,000	6,266,112	1,423,112—
	Michigan	6,334,172	22,643,000	20,902,767	1,740,233+
	Nebraska	1,317,566	3,840,000	4,347,967	507,967—
	Nevada*	158,378	635,000	632,647	2,353+
	New Hampshire	529,881	2,312,000	1,748,607	563,393+
	New Jersey	4,821,880	17,493,000	15,912,204	1,580,796+
	New York*	14,743,210	55,622,000	48,652,593	6,969,407+
	Rhode Island	786,324	3,012,000	2,594,869	417,131+
	South Dakota	650,025	1,779,000	2,145,082	366,082—
	South Carolina	2,107,813	5,694,000	6,955,782	1,261,782—

† Chart indicates what should have been collected based on per capita consumption, compared with actual revenue figures.

* Arizona, Montana and New York gain from tourists, as does Nevada. The others all gain from high impositions in neighboring states that bring in out-state business.

Appendix II (*continued*)

	State	Population 1950	1949 Cigarette Tax Revenue	1949 per Capita Revenue	Gain or Loss in Revenue
	Tennessee	3,280,575	8,365,000	10,825,897	1,460,897—
	Texas	7,677,060	23,692,000	25,334,298	1,642,298—
	Wisconsin	3,417,372	8,288,000	11,277,327	2,989,327—
4¢	Arkansas	1,900,246	5,181,000	8,361,082	3,180,082—
	Maine	907,205	5,165,000	3,991,702	1,173,298+
	Minnesota	2,967,210	10,223,000	13,055,724	1,832,724—
	Mississippi	2,171,806	6,718,000	9,555,946	2,837,946—
	New Mexico	677,099	1,964,000	2,979,235	1,015,235—
	Pennsylvania	10,435,965	41,748,000	45,918,246	4,170,246—
	Vermont	375,786	1,592,000	1,653,458	61,458—
	Washington	2,361,261	5,815,000	9,445,044	3,630,044—
5¢	Florida	2,734,086	13,063,000	15,037,473	1,974,473—
	Georgia	3,418,120	10,186,000	18,799,660	8,613,660—
	Massachusetts	4,711,753	22,730,000	25,914,641	3,184,641—
	North Dakota	616,185	2,348,000	3,389,017	1,041,017—
	Oklahoma	2,230,253	9,778,000	12,266,391	2,488,391—
8¢	Louisiana	2,669,043	17,559,000	23,487,578	5,928,578—

Appendix III

The revenue received to date by Atlantic City from the imposition of the tax is as follows:

Month	1947	1948	1949
January		$ 16,193.50	$ 15,086.00
February		12,819.60	10,550.00
March		21,446.40	14,781.20
April		13,706.70	17,680.00
May		20,628.00	17,260.00
June	$ 44,119.46*	24,995.00*	31,400.00*
July	39,137.76*	43,758.00*	43,846.00*
August	37,782.42*	35,882.80*	34,600.00*
September	24,232.96	19,970.00	15,380.00
October	13,672.20	18,960.00	11,710.00
November	18,042.60	9,550.00	16,200.00
December	14,656.46	19,250.00	14,000.00†
Total	$191,643.86	$257,140.08	$228,493.20

* Indicates summer season.

† Indicates estimated revenue for December 1949.

The above figures clearly indicate that revenue returns are diminishing.

APPENDIX IV

Federal Revenue for 1949 from 7¢ Cigarette Tax by States

State	Amount	State	Amount
Alabama	$23,503,441	Nebraska	$10,145,258
Arizona	5,716,202	Nevada	1,108,646
Arkansas	14,631,894	New Hampshire	3,709,167
California	80,637,079	New Jersey	37,158,476
Colorado	10,127,086	New Mexico	5,213,662
Connecticut	15,360,098	New York	113,522,717
Delaware	2,438,659	North Carolina	31,068,406
Florida	21,052,462	North Dakota	4,750,014
Georgia	26,319,524	Ohio	60,843,790
Idaho	4,512,484	Oklahoma	17,177,948
Illinois	66,962,973	Oregon	11,628,139
Indiana	30,167,860	Pennsylvania	80,356,930
Iowa	20,095,059	Rhode Island	6,054,694
Kansas	14,518,596	South Carolina	16,230,160
Kentucky	22,573,227	South Dakota	5,005,042
Louisiana	18,893,301	Tennessee	25,260,424
Maine	6,985,478	Texas	37,333,362
Maryland	17,884,458	Utah	5,288,683
Massachusetts	36,280,498	Vermont	2,891,472
Michigan	48,773,124	Virginia	25,007,913
Minnesota	22,847,517	Washington	18,181,709
Mississippi	16,722,906	West Virginia	15,388,727
Missouri	30,216,494	Wisconsin	26,313,764
Montana	4,521,409	Wyoming	2,219,193

APPENDIX V

State Cigarette Taxes

State	(As of August, 1950) Tax Rate Per Package of 20 Cigarettes	State	(As of August, 1950) Tax Rate Per Package of 20 Cigarettes
Alabama	3¢	Montana	4¢
Arizona	2	Nebraska	3
Arkansas	4	Nevada	3
Connecticut	3	New Hampshire	2½
Delaware	2	New Jersey	3
District of Columbia	1	New Mexico	4
Florida	5	New York	3
Georgia	3	North Dakota	5
Idaho	3	Ohio	2
Illinois	3	Oklahoma	5
Indiana	3	Pennsylvania	4
Iowa	2	Rhode Island	3
Kansas	3	South Carolina	3
Kentucky	2	South Dakota	3
Louisiana	8	Tennessee	3
Maine	4	Texas	4
Massachusetts	5	Utah	2
Michigan	3	Vermont	4
Minnesota	4	Washington	4
Mississippi	4	West Virginia	1
		Wisconsin	3

APPENDIX VI
Cigarette Tax Receipts*

State	Tobacco Tax Revenue 1945	1949	% Total State Revenue (Fiscal '49)
Alabama	$ 5,000,000	$ 7,700,000	7.1
Arizona	———	———	—
Arkansas	2,700,000	6,100,000	7.5
Connecticut	3,100,000	7,300,000	7.8
Delaware	———	———	—
District of Col.	———	———	—
Florida	5,400,000	12,600,000	9.1
Georgia	5,100,000	8,300,000	7.6
Idaho	100,000	1,600,000	5.4
Illinois	10,800,000	30,200,000	8.0
Indiana	———	12,500,000	—
Iowa	2,200,000	4,900,000	3.5
Kansas	1,700,000	4,800,000	4.8
Kentucky	2,700,000	5,000,000	4.9
Louisiana	7,400,000	15,800,000	7.1
Maine	1,400,000	5,200,000	12.9
Massachusetts	7,500,000	21,200,000	9.5
Michigan	———	22,600,000	6.0
Minnesota	———	8,900,000	5.4
Mississippi	3,600,000	6,700,000	7.7
Montana	———	1,300,000	—
Nebraska	———	3,800,000	8.7
Nevada	———	500,000	5.5
New Hampshire	1,000,000	2,200,000	10.8
New Jersey	———	18,000,000	12.5
New Mexico	———	———	—
New York	23,200,000	52,200,000	7.0
North Dakota	700,000	1,700,000	4.6

* Survey by Tobacco Associates, Inc., reported in U. S. TOBACCO J. 16 (April 29, 1950).

APPENDIX VII

Partial List of City Cigarette Taxes

Alabama	
Abbeville	1¢
Anniston	2¢
Atmore	2¢
Attalla	2¢
Bessemer	1¢
Birmingham	2¢
Decatur	1¢
Gadsen	2¢
Mobile County	1¢
Montgomery	2¢
Opelika	2¢
Northport	1¢
Ragland	1¢
Tarrant City	2¢
Tuscaloosa	1¢
Wetumpka	2¢
Colorado	
Denver	2¢
Pueblo	1¢
Englewood	2¢
Aurora	1¢
Florida	
Chipley	1½¢
DeFuniak Springs	2¢
Lakeland	2¢
Marianna	1½¢
Miami	2¢
Panama City	1½¢
Pensacola	2¢
St. Petersburg	2¢
W. Palm Beach	2¢
Wewahitchka	1¢
Maryland	
Baltimore	1¢
Missouri	
Columbia	2¢
Excelsior Springs	2¢
Jefferson City	2¢
Kansas City	2¢
Moberly	2¢
Richmond	2¢
Springfield	2¢
St. Louis	3¢
New Jersey	
Atlantic City	2¢
Nebraska	
Omaha	2¢
Wyoming	
Cheyenne	2¢
Larimie	2¢
Casper	2¢
Rawlins	2¢