



# FISCAL FACT

February 17, 2010  
No. 211

---

## Georgia Tobacco Tax Favors High-Income Counties

By Patrick Fleenor

### Introduction

The flood of new, detailed data on public finance in usable formats continues to change what's possible when analyzing public policy. Data on personal consumption of products can be combined with tax and spending data to reveal enlightening patterns. Tobacco is often at the forefront of this type of analysis because health-related studies track its consumption carefully and because taxes on it are generally high and well documented.

Consider Georgia's cigarette excise. The Georgia Department of Human Resources divides the state into 18 public health districts and publishes data on the rate of smoking in each. Since cigarette tax revenue goes into the general fund, providing benefits to residents in the same proportions as other general fund money, we can safely conclude that the cigarette tax transfers funds from areas with high smoking rates to those with low smoking rates.

The biggest winners in this fiscal transfer were the Cobb-Douglas and Fulton health districts. Cobb-Douglas received \$1.29 in state services for every \$1.00 its residents paid in cigarette taxes for a total gain of \$4.2 million. Similarly, the Fulton health district, comprised entirely of Fulton County, receives \$1.27 in spending for every \$1.00 in cigarette taxes paid, for a total transfer of \$4.7 million.

Most analysts would consider this exchange inequitable because the residents of Cobb, Douglas and Fulton counties have higher-than-average incomes: 20 percent higher in Cobb-Douglas and 60 percent higher in Fulton, as compared to incomes in the rest of the state.

On the most extreme paying end of this transfer is the Northwest health district, comprised of Bartow, Catoosa, Chattooga, Dade, Floyd, Gordon, Haralson, Paulding, Polk and Walker counties. On net, the state's fiscal system provided 78 cents in benefits to this region for every \$1.00 it extracted in cigarette tax revenue for a total loss of \$3.8 million. The next biggest "loser" was the North Georgia health district which is comprised of Cherokee, Fannin, Gilmer, Murray, Pickens, and Whitfield counties.

*Patrick Fleenor is chief economist at the Tax Foundation.*

## Background

Georgia has levied a tax on cigarettes since 1923. Currently the rate is 37 cents per pack. A tax is also levied on other tobacco products such as snuff and chewing tobacco. Revenues from tobacco taxes are deposited in the state's general fund.<sup>1</sup>

Tobacco taxes are popular with the public. According to a 2002 poll in Georgia, 71 percent of respondents favored hiking the tax on tobacco.<sup>2</sup> Numbers like that, which roughly correspond with the percentage of residents who do not smoke, have persuaded politicians to embrace tobacco taxes. During the last two recessions, tobacco taxes were the tax of choice for politicians needing to make-up revenue shortfalls.

In contrast to the public and politicians, many economists are less enamored with product-specific excises like tobacco taxes. Instead, they favor tax policies that treat all products and services equally, allowing the market system to allocate resources efficiently. By contrast, product-specific excises distort prices and reduce general economic welfare over time.

## Tobacco Taxes and Tax Fairness

Tax fairness is always one of the first concerns in evaluating any tax or tax system, and many people have grave reservations about the fairness of product-specific excises like the tobacco tax. Two ways of thinking about tax fairness dominate the debate, concepts that economists call horizontal equity and vertical equity.

### *Horizontal Equity*

Horizontal equity is a standard of fairness that is satisfied when all the people in the same income group are burdened equally by a tax. This standard of fairness is especially important when the tax revenue is deposited in the general fund. Since public services financed by the general fund provide general benefits, their costs should be spread evenly within each income class. For example, if 100 people in a county earn \$50,000 each, they should all be paying close to the same amount of tax. Do tobacco taxes or other product-specific taxes spread the burden fairly by this standard? No, just the opposite. People who don't buy the highly taxed product pay nothing while regular purchasers pay a great deal. If the revenue were spent only on the people paying, that would be fair, but tobacco revenue goes right into the general fund for the benefit of all.

### *Vertical Equity*

Vertical equity is a fairness standard satisfied when people who earn more pay more, not just more dollars but more as a percentage of their earnings. This is often called progressivity. Some people disagree, believing taxes should be proportional, not progressive. Fans of proportionality believe the rich should pay more dollars of tax but the same percentage of income. For example, take two next-door neighbors. If one earns \$50,000 and pays \$1,000 in a particular tax (2%), and the other earns \$100,000 and pays \$2,000 (also 2%), they are paying proportional tax burdens: the same percentage of their income goes to pay the tax. On the other hand, if the high earner pays more than \$2,000 (more than 2% of income), then the tax is progressive and would be called vertically equitable.

Aside from progressively or proportionally, the only other way the burden of a tax can be spread is regressively. The burden of a regressive tax is heavier on the poor as a percentage of income, satisfying no one's idea of fairness. Yet existing cigarette taxes are exactly that way, and to an extreme degree, extracting a much higher percentage of poor people's incomes than rich people's.

Under current law, the 20 percent of Georgia residents who earn the least shoulder a tobacco tax burden 18 times greater as a percentage of their income than do the 20 percent of residents who earn the most.

### *Intrastate Equity*

Tax fairness can be related to both geography and income. Let's consider Georgia's cigarette tax in more detail. The first column of Table 1 lists the various rates of smoking in Georgia's 18 public health districts, ranging from a high of 29.0 percent in the Northwest district to a low of 17.6 percent in the Cobb-Douglas District.

Health District	Smoking Rate	Cigarettes Legally Sold and Taxed (Millions of Packs)	Cigarette Tax Revenue in \$Millions	Spending Share in \$Millions	Gain (+) or Loss (-)	Spending Per Dollar of Tax	Average Personal Income
Cobb-Douglas	17.6%	39.1	\$ 14.5	\$ 18.6	+ \$ 4,153,057	\$ 1.29	\$ 40,614
Fulton (Atlanta*)	17.9%	48.7	\$ 18.0	\$ 22.8	+ \$ 4,784,020	\$ 1.27	\$ 54,215
DeKalb	19.2%	38.3	\$ 14.2	\$ 16.7	+ \$ 2,551,040	\$ 1.18	\$ 37,884
LaGrange	21.6%	45.4	\$ 16.8	\$ 17.6	+ \$ 819,403	\$ 1.05	\$ 29,693
South Central (Dublin)	21.5%	8.4	\$ 3.1	\$ 3.3	+ \$ 167,204	\$ 1.05	\$ 23,205
West Central (Columbus)	22.2%	21.4	\$ 7.9	\$ 8.1	+ \$ 162,072	\$ 1.02	\$ 31,690
State of Georgia	22.6%	589.6	\$ 218.1	\$ 218.1	\$ 0	\$ 1.00	\$ 33,499
North (Gainesville)	23.0%	37.2	\$ 13.8	\$ 13.6	- \$ 207,319	\$ 0.98	\$ 31,057
East Metro (Lawrenceville)	23.2%	60.4	\$ 22.3	\$ 21.8	- \$ 525,534	\$ 0.98	\$ 32,032
East Central (Augusta)	23.5%	28.3	\$ 10.5	\$ 10.1	- \$ 376,733	\$ 0.96	\$ 28,912
Southwest (Albany)	23.6%	23.4	\$ 8.7	\$ 8.3	- \$ 347,002	\$ 0.96	\$ 25,326
Clayton (Jonesboro)	23.9%	17.6	\$ 6.5	\$ 6.2	- \$ 340,327	\$ 0.95	\$ 24,221
Northeast (Athens)	23.9%	29.5	\$ 10.9	\$ 10.3	- \$ 568,985	\$ 0.95	\$ 28,260
North Central (Macon)	24.7%	34.1	\$ 12.6	\$ 11.6	- \$ 1,045,968	\$ 0.92	\$ 29,606
Coastal (Savannah)	24.9%	36.2	\$ 13.4	\$ 12.2	- \$ 1,208,665	\$ 0.91	\$ 33,913
South (Valdosta)	25.2%	16.7	\$ 6.2	\$ 5.5	- \$ 623,405	\$ 0.90	\$ 25,257
Southeast (Waycross)	26.8%	25.2	\$ 9.3	\$ 7.9	- \$ 1,441,864	\$ 0.85	\$ 23,001
North Georgia (Dalton)	27.5%	31.5	\$ 11.7	\$ 9.6	- \$ 2,053,000	\$ 0.82	\$ 31,867
Northwest (Rome)	29.0%	48.1	\$ 17.8	\$ 13.9	- \$ 3,897,992	\$ 0.78	\$ 27,299

\*Small parts of Atlanta fall outside Fulton County.

Since cigarette tax revenue flows into the general fund and back out for general expenditures that benefit the entire population, we can conclude that the cigarette tax effectively transfers funds from areas with high smoking rates to those with low smoking rates. The amount of spending received in each health district per dollar of tax paid is shown in the fifth column.

The biggest winner from this fiscal redistribution is Cobb-Douglas where the state spent \$1.29 on general services for every \$1.00 the residents paid in cigarette taxes; the total amount transferred was \$4.2 million in 2007. If Cobb and Douglas counties were relatively poor, many analysts would justify the transfer on grounds of vertical equity; that is, they would claim that the relatively poor residents deserve the extra spending. However, incomes in Cobb and Douglas counties are comparatively high, not low. In fact, on average, the residents earn 20 percent more than the rest of the state.

In the even higher-income Fulton health district, comprised entirely of Fulton County which includes most of Atlanta, the story is similar. On net, the state's fiscal system transferred \$1.27 to this area for every \$1.00 it received in cigarette taxes from Fulton residents, for a total transfer of \$4.7 million. The average income of Fulton residents is more than 60 percent higher than in the rest of Georgia.

Any system which bestows net benefits to some will impose net costs on others. The biggest loser in the fiscal redistribution caused by the cigarette tax is the Northwest health district of Bartow, Catoosa, Chattooga, Dade, Floyd, Gordon, Haralson, Paulding, Polk and Walker counties. On net, the state's fiscal system provided 78 cents in benefits to this region for every \$1.00 it extracted in cigarette tax revenue. The total amount transferred out of these counties to finance spending in the rest of the state was \$3.8 million. Similarly, in the North Georgia health district, comprised of Cherokee, Fannin, Gilmer, Murray, Pickens, and Whitfield counties, the state spent 82 cents in general services for every \$1.00 taken from district residents in cigarette taxes for a total loss of \$2.1 million.

In some counties, spending is roughly equal to tax revenue. For example, in the North, West Central and East Metro health districts, spending differs from tax revenue by only two cents per dollar.

## Conclusion

Cigarette taxes are one of those areas of tax policy where there is a great divide between what the public favors and what tax economists generally see as sound tax policy. Cigarette taxes tend to reduce economic welfare and harm tax equity across several dimensions. They are horizontally inequitable because within income groups only some – i.e. smokers – are required to pay a tax that funds general government services. They are vertically inequitable – or regressive - because they place a much higher burden on low-income smokers than they do on high-income smokers. Moreover, in Georgia, they tend to shift income from low- to relatively high-income areas.

---

<sup>1</sup> "Georgia Tobacco Tax Jumps," *Convenience Store News*, July 2, 2003.

<sup>2</sup> "71 Percent Support Georgia Cigarette Tax Hike, Poll Says," *Atlanta Journal-Constitution*, June 6, 2002.