Tax a threat to Arizona's fiscal health

By Kevin McCarthy
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Proposition 303, which would increase cigarette taxes by 60 cents a pack, is being promoted as a shot in the arm to the state treasury, but it is more likely another hazard to the state's fiscal health.

Proposition 303 continues what is becoming a disturbing and familiar practice in Arizona: ballot-box budgeting. Determining state budget priorities at the ballot box, as opposed to the Legislature's appropriation process, has become so accepted that now even the Legislature and governor participate.

The passage of the Voter Protection Act in 1998 placed strict limits on the Legislature's ability to make changes to voter-approved measures. As a result, statutory initiatives, for all practical purposes, rise to the level of constitutional amendments.

Ironically, at the same time the Legislature offers voters the opportunity to earmark more revenue outside the appropriations process, resolving the current budget crisis is complicated by the lack of budget flexibility caused by previous initiatives.

Ballot-box budgeting overrides the Legislature's primary responsibility and handcuffs its ability to respond to changing demands on the state. Furthermore, by circumventing the annual appropriations process, the earmarked revenues and the programs they fund escape periodic legislative scrutiny so important to maintain accountability for the spending of taxpayer dollars.

The Legislature cooperated in referring a tobacco tax increase to the ballot because many viewed it as providing much-needed relief to a state budget hemorrhaging red ink. However, in their desire for short-term budget relief, the Legislature gave little consideration to the long-term effect of the huge tax increase on future tobacco tax collections.

Dramatic increases in tobacco taxes are sold to voters as necessary to fund numerous government programs and simultaneously to discourage people from consuming tobacco products. It is a fact that as tax rates increase on tobacco products, tax collections decrease. But that does not necessarily mean a reduction in tobacco consumption.

Since the first full year of implementation of the voter approved 40-cent cigarette increase in 1994, annual tobacco collections have declined $13.2 million, a 7.7 percent decrease. Over and above the current rate of decline in revenue, the Joint Legislative Budget Committee, or JLBC, estimates that Proposition 303 drives down existing revenues an additional $19.9 million from fiscal 2003 to 2005.

The JLBC fiscal estimate of the impact of 303 on the price elasticity of demand for cigarettes was based on previous consumer behavior; however, their analysis probably underestimates the impact of such a large increase in price on taxable sales. The savings now provided on the Internet are dramatic and a switch to online purchases would not only avoid the new 60-cent increase but the existing 58 cents in state taxes as well.

In a recent article in *Governing Magazine*, Alan Ehrenhalt questioned both the sincerity and fiscal wisdom of states increasing their addiction to tobacco taxes:

"There are times when so-called 'sin taxes' are treated mostly as a fiscal proposition, others when they are portrayed largely in moral terms. . . . If government's main goal is to make money off of tobacco and alcohol, it needs to have people drink and smoke more, not less."

Until this state's citizens and political leadership recognize the long-term fiscal hazards associated with ballot-box budgeting, Arizona's fiscal health will continue to have a very poor prognosis.

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