

June 2010

Updating Excise Taxes

Holley Hewitt Ulbrich
Senior Scholar
Strom Thurmond Institute

After many unsuccessful efforts, the General Assembly finally passed an increase in the excise tax on cigarettes from seven cents a pack to 57 cents—over the governor’s veto. The seven-cent tax, set in 1972, would be 36 cents today if adjusted for inflation. The other 21 cents represents a tax increase. The state now ranks 42nd among the 50 states, with a national average of \$1.42 per pack.

South Carolina, like most other states, has a group of taxes that are imposed on particular commodities and services. The admissions/amusements tax, the accommodations tax, local hospitality taxes, the lottery, taxes on bingo, and most important, taxes on alcohol, tobacco and gasoline all fall into the general category of excise taxes. The first three—admissions, accommodations, and hospitality—all follow the same model as the general sales tax. Tax due is computed as a percent of the amount of sale. Admissions and amusements were taxed at the same rate as the general sales tax until that rate was raised from 5% to 6% in 2006. They not only pay the lower 5% rate but also are not subject to local option sales taxes. Taxes on accommodations and restaurant meals (hospitality) are levied for the benefit of local governments and are in addition to the general retail sales tax. The rationale for these latter two taxes is that both business and tourist visitors use public facilities and impose costs on local government than can be recouped by taxing these two services that are more likely to be used by visitors.

The other major excise taxes—on alcohol, tobacco, and gasoline—have been around much longer and follow a different pattern. Alcoholic beverages and tobacco products are subject to both general sales taxes and specific excise taxes. Gasoline is only subject to an excise tax. In all three cases, the tax is stated, not as a percentage of the price, but as an amount per unit. Fifty-seven cents per pack of cigarettes. Sixteen plus cents per gallon of gasoline; \$2.72 per gallon of distilled spirits (plus some other taxes), 77 cents per gallon of beer, 90 cents per gallon of wine. These taxes have a different justification from tourism taxes. The tax on gasoline is dedicated to the maintenance and repair of roads, so it is more or less a user tax. Those who pay the tax benefit from the services it supports. Taxes on alcohol and tobacco are intended to discourage their use because these products are considered harmful.

South Carolina's taxes on alcohol of all kinds are above the national average, but when it comes to cigarettes and gasoline, South Carolina is still on the low end for cigarettes and 47th among the 50 states for gasoline at 16.8 cents per gallon. The U.S. average is 29.3 cents per gallon. Since gasoline tax revenue from interstate truckers is shared among states based on miles driven in the state and the state's gasoline tax rate, South Carolina is losing revenue from that source without getting any particular benefit in return.

Because these taxes are computed on a basis of physical units rather than price, the revenue doesn't increase with inflation, unlike the general sales and income taxes. Between 1995 and 2009, overall general state revenue grew 71%, but revenue in the category of "other taxes" (mostly excise taxes) grew only 11%. Sales volume tends to keep pace with population, but if the tax is not linked to the price, revenue from these per-unit excise taxes grows more slowly than revenue from other sources. The seven cents per pack tax on cigarettes, set in the early 1970s, would have to be about 37 cents today to represent the same purchasing power. In other words, if the tax rates for alcohol, tobacco and gasoline are not adjusted regularly for inflation, consumers are actually getting a tax cut—and no one in the General Assembly gets to take the credit! So one possible way to keep pace with the price of everything else is to index these excise taxes for inflation.

It's true that these excise taxes are not major revenue sources. Taxes on alcohol, including beer and wine, only provided about \$109 million out of more than \$5 billion in South Carolina general revenue in 2008-09. Taxes on tobacco generated only \$28 million a year prior to the 50 cents per pack increase, which is expected to increase revenue by about \$100 million a year. But in times of economic downturn, every revenue source matters. When we as a state and nation are trying to discourage consumption of alcohol and tobacco, the rate itself matters. When South Carolina's roads and bridges are in poor repair because of inadequate funding for the highway trust fund, the gasoline tax rates matters. Whether the goal of an excise tax is to raise revenue or to discourage consumption (or both), low rates that are rarely adjusted don't accomplish either of those goals.



Jim Self Center on the Future
Strom Thurmond Institute of Government and Public Affairs
Pearman Boulevard
Clemson University
Clemson SC 29634-0125
864.656.4700
www.strom.clemson.edu

The views presented here are not necessarily those of the Strom Thurmond Institute of Government and Public Affairs or of Clemson University. The Institute sponsors research and public service programs to enhance civic awareness of public policy issues and improve the quality of national, state, and local government. The Institute, a public service activity of Clemson University, is a nonprofit, nonpartisan, tax-exempt public policy research organization.