

Bill would increase cost of cigarettes, raise state revenue

By Adam H. Covici

Smoke 'em if you got 'em.

Texans may soon see higher cigarette prices as part of generating revenue to fund reforms of the public school finance system. The increase would bring the total tax to \$1.41 and give Texas the 10th-highest cigarette tax in the nation, up from the 41st-highest. The sales tax will also be expanded to include bottled water, car washes and automotive repair services.

The House Ways and Means Committee passed its amended version of House Bill 3 on Wednesday. The bill, authored by chair Rep. Jim Keffer, R-Eastland, focuses on cutting property taxes by a third. Currently, the vast majority of school funding comes from a property tax that takes \$1.50 for every \$100 dollars of property value. Under the new legislation, property owners would be taxed \$1 for every \$100 of property value, with an enrichment provision that would allow districts to collect up to 10 cents more as needed. The provision represents the "meaningful discretion" District Judge John Dietz called for in his decision last November when he declared the state's reliance on property taxes to fund schools unconstitutional, as the Texas Constitution prohibits a state-wide property tax.

To fund the ambitious proposal, HB 3 calls for a sales tax hike from 6.25 percent to 7.2 percent, which will help make up part of the \$5.4 billion yearly loss in property tax revenue.

Dick Lavine, senior fiscal analyst for the Center for Public Policy Priorities, said Texas already depends on a regressive sales tax for 55 percent of its revenue and, in doing so, creates a lopsided system.

"Eighty percent of Texas families will be worse off because the drop in their property taxes won't make up what they will lose from the increased sales tax," said Lavine.

The plan also calls for the removal of the franchise tax to be replaced with a payroll tax that would take 1.1 percent of salaries up to \$80,000 per employee. Before making it to committee, the legislation changed to include a 1.25 percent payroll tax up to \$40,000. The current franchise tax has been criticized by some lawmakers because of the loopholes found in the tax that allow five out of every six businesses to avoid paying.

Byron Schlomach, chief economist for the Texas Public Policy Foundation, said he could not support HB 3 because of the payroll tax.

"We are pretending the tax is on businesses, but it is really on the employee," said Schlomach. "This is a tax on work, and when you tax something you tend to get less of it."

Schlomach said any business with a payroll will be hurt by the tax, and employers will have to take it into account when considering whether to hire new employees or give raises.

"As an economist, I favor a low, broad-based tax, but history shows they don't stay low," said Schlomach. "The state sees that it is a good source of revenue, and little by little the percentage goes up."

Schlomach said the proposal to lower property taxes by a third is "too big of a drop," and if the state would instead lower it 25 cents, or 17 percent, they could meet the needs of the education system without the creation of a payroll tax or a drastic hike in the sales tax.

Schlomach's concerns echo those of Gov. Rick Perry, who argued last session that a payroll tax would discourage job creation in Texas.

Another revenue component of the bill has tobacco taxes up 244 percent, which translates into \$1 more per pack for cigarettes and a comparable amount on cigars. Other tobacco products' price will increase almost 5 percent based on the manufacturer's price.

Lavine said the tobacco tax increase is fine because it discourages smoking, which leads to health risks that end up costing the state money in terms of health care and human services.

But John Singleton, spokesman for R.J. Reynolds Tobacco Co., maker of Camel and Winston cigarettes, said the problem with the tax is that it would further burden a minority of Texans who already earn less than the majority of residents. According to R.J. Reynolds, 23 percent of Texans are smokers, and they tend to have low to moderate incomes. For the fiscal year 2002, the median household income for a smoker was \$30,000, versus \$38,000 for a non-smoker.

"This is the most regressive tax you could dream up," Singleton said. "The golden rule of taxation is to tax as broadly as possible. This is simply picking on an unpopular minority."

HB 3 is scheduled for debate on the House floor next week.
