Abstract:

Taxes are a primary tool for influencing behavior. In traditional economic models, this influence is achieved through the price channel: holding all else equal, taxes increase prices and thus decrease demand. However, the nature of social and political discourse in the course of a tax law change can conceivably result in all else not being held equal. The process by which laws are changed may directly affect consumer preferences by providing information and directing attention to the behavior, introducing a “nudge” channel that can influence demand even in the absence of price changes. We decompose the relative importance of the price channel and the nudge channel as mechanisms for the decrease in cigarette consumption caused by state-level cigarette tax increases. To do so, we exploit institutional features of the legal process of both passed and failed state tax laws and distinguish between state tax increases resulting from a bill passed by state legislatures and those resulting from a direct vote by citizens via a referendum. We document a marked increase in related media coverage and lobbying efforts in the immediate lead-up to proposed tax law changes from a referendum. The intensity of the information campaigns is directly associated with decreases in cigarette consumption, even when controlling for price changes. Illustrating this effect, we find that cigarette consumption meaningfully decreases following referenda that fail, despite the consequence that taxes remain constant. Our results support a conception of the tax-change process not only as a price intervention, but also as a marketing intervention that directly shapes consumer preferences.