

Cato Blog Post – July 2015
Obamacare’s Not-So-Hidden Tax: Thank You for Smoking
Aaron Yelowitz

Without government interference, insurance markets will naturally charge higher premiums for riskier individuals. For example, [life insurance](#) premiums vary considerably based on factors that increase the likelihood of death, such as age, gender, smoking status, and health.

Under Obamacare, many factors that influence healthcare expenditures are excluded from premiums. For example, premiums make no distinction for obesity, likelihood of having a baby, alcoholism or pre-existing conditions. One notable exception is for smokers, where premiums may be up to 50 percent higher than that for non-smokers. I have collected data on premiums for smokers and non-smokers in 35 states, and the data shows large variation in the extent to which smokers are charged more for their choice.

Smokers are certainly a riskier group than non-smokers. Thus, one would expect some actuarial adjustment to premiums. Given the variation across states, it is clear that premiums vary not only due to a smoker’s greater risk, but other factors as well. At least part of the markup for smokers should be viewed as a “smoker’s tax” rather than an actuarial adjustment.

One expects that the detrimental effects of smoking would build over time. You wouldn’t expect to see large risk adjustments for young individuals. Let’s consider a 27-year-old who doesn’t receive subsidies but is mandated to purchase health insurance. If a non-smoker lived in Cheyenne, WY, he or she could purchase [Blue Cross Blue Shield of Wyoming - BlueSelect Silver ValueTwo Plus Dental](#) plan for \$334 per month. This plan has a \$3,000 deductible and an out-of-pocket maximum of \$6,600. If the 27-year-old smoked, [same plan](#) would be \$417 per month, or 24.9% higher. For a pack-a-day smoker, this represents a \$2.72 per-pack increase in expenditure due to Obamacare.

Smoker's Premium in Wyoming - \$2.72 per pack for a pack-a-day 27-year-old smoker

Smoker

HealthCare.gov | Individuals & Families | Small Businesses | Log In | Español

Plan Details

BACK TO RESULTS

OPTIONS

- Print
- Link: <http://go.hc.gov/10c0348>
- Email

Important: E-mailing or sharing plan details can expose information about your income, household members, smoking status, and other sensitive matters. Share this information only with people you trust.

LIKE THIS PLAN? TAKE THE NEXT STEP

Blue Cross Blue Shield of Wyoming - BlueSelect Silver ValueTwo Plus Dental

Silver | PPO
National Provider Network
Plan ID: 11269WY0070018

ESTIMATED MONTHLY PREMIUM	ESTIMATED DEDUCTIBLE	ESTIMATED OUT-OF-POCKET MAXIMUM
\$417 Number of people covered: 1	\$3,000 Estimated individual total	\$6,600 Estimated individual total

PEOPLE COVERED: 1 (Age 27): Covered

MORE INFORMATION

- Summary of Benefits
- Plan brochure
- Provider directory
- List of covered drugs

Costs for Medical Care

Primary Care Visit to Treat an Injury or Illness	\$40
QL limits and exclusions apply	
Specialist Visit	20% Coinsurance after deductible
Hearing Aids	Benefit not covered
Routine Eye Exam for Children	20% Coinsurance after deductible
QL limits and exclusions apply	
Eye Glasses for Children	20% Coinsurance after deductible
QL limits and exclusions apply	

Non-Smoker

HealthCare.gov | Individuals & Families | Small Businesses | Log In | Español

Plan Details

BACK TO RESULTS

OPTIONS

- Print
- Link: <http://go.hc.gov/11qz2V>
- Email

Important: E-mailing or sharing plan details can expose information about your income, household members, smoking status, and other sensitive matters. Share this information only with people you trust.

LIKE THIS PLAN? TAKE THE NEXT STEP

Blue Cross Blue Shield of Wyoming - BlueSelect Silver ValueTwo Plus Dental

Silver | PPO
National Provider Network
Plan ID: 11269WY0070018

ESTIMATED MONTHLY PREMIUM	ESTIMATED DEDUCTIBLE	ESTIMATED OUT-OF-POCKET MAXIMUM
\$334 Number of people covered: 1	\$3,000 Estimated individual total	\$6,600 Estimated individual total

PEOPLE COVERED: 1 (Age 27): Covered

MORE INFORMATION

- Summary of Benefits
- Plan brochure
- Provider directory
- List of covered drugs

Costs for Medical Care

Primary Care Visit to Treat an Injury or Illness	\$40
QL limits and exclusions apply	
Specialist Visit	20% Coinsurance after deductible
Hearing Aids	Benefit not covered
Routine Eye Exam for Children	20% Coinsurance after deductible
QL limits and exclusions apply	
Eye Glasses for Children	20% Coinsurance after deductible
QL limits and exclusions apply	

However, not all of the \$2.72 per-pack is a tax. Smokers are more expensive. Consider a non-smoker in Marquette, MI, who selects [Blue Cross Blue Shield of Michigan - Blue Cross Silver Extra with Dental and Vision, a Multi-State Plan](#). That person pays \$335 per month, nearly identical to the premium

for the non-smoker in Wyoming. The plan has a \$2,000 deductible and an out-of-pocket maximum of \$5,500. If the 27-year smoked, the [same plan](#) costs \$351 per month (4.8 percent higher), or \$0.53 per-pack of cigarettes. If 53 cents per pack approximates the actuarial adjustment for young smoker, then much of the mark-up in Wyoming – \$2.19 of the \$2.72 – doesn't represent risk, and can be viewed as a smoking tax.

Smoker's Premium in Michigan - \$0.53 per pack for a pack-a-day 27-year-old smoker

Smoker

HealthCare.gov | Individuals & Families | Small Businesses | Log In | Español

Plan Details

BACK TO RESULTS

OPTIONS

- Print
- Link
- Email

Important: E-mailing or sharing plan details can expose information about your income, household members, smoking status, and other sensitive matters. Share this information only with people you trust.

LIKE THIS PLAN? TAKE THE NEXT STEP

Blue Cross Blue Shield of Michigan - Blue Cross® Silver Extra with Dental and Vision, a Multi-State Plan

Silver | PPO
National Provider Network
Plan ID: 1356M0880001

ESTIMATED MONTHLY PREMIUM	ESTIMATED DEDUCTIBLE	ESTIMATED OUT-OF-POCKET MAXIMUM
\$351 Number of people covered: 1	\$2,000 Estimated individual total	\$5,500 Estimated individual total

PEOPLE COVERED

1 (Age 27): Covered

MORE INFORMATION

- Summary of Benefits
- Plan brochure
- Provider directory
- List of covered drugs

Costs for Medical Care

Primary Care Visit to Treat an Injury or Illness QLimits and exclusions apply	\$20 Copay before deductible
Specialist Visit QLimits and exclusions apply	\$50 Copay before deductible
Hearing Aids	Benefit not covered
Routine Eye Exam for Children QLimits and exclusions apply	No charge
Eye Glasses for Children QLimits and exclusions apply	No charge

Non-Smoker

HealthCare.gov | Individuals & Families | Small Businesses | Log In | Español

Plan Details

BACK TO RESULTS

OPTIONS

- Print
- Link
- Email

Important: E-mailing or sharing plan details can expose information about your income, household members, smoking status, and other sensitive matters. Share this information only with people you trust.

LIKE THIS PLAN? TAKE THE NEXT STEP

Blue Cross Blue Shield of Michigan - Blue Cross® Silver Extra with Dental and Vision, a Multi-State Plan

Silver | PPO
National Provider Network
Plan ID: 1356M0880001

ESTIMATED MONTHLY PREMIUM	ESTIMATED DEDUCTIBLE	ESTIMATED OUT-OF-POCKET MAXIMUM
\$335 Number of people covered: 1	\$2,000 Estimated individual total	\$5,500 Estimated individual total

PEOPLE COVERED

1 (Age 27): Covered

MORE INFORMATION

- Summary of Benefits
- Plan brochure
- Provider directory
- List of covered drugs

Costs for Medical Care

Primary Care Visit to Treat an Injury or Illness QLimits and exclusions apply	\$20 Copay before deductible
Specialist Visit QLimits and exclusions apply	\$50 Copay before deductible
Hearing Aids	Benefit not covered
Routine Eye Exam for Children QLimits and exclusions apply	No charge
Eye Glasses for Children QLimits and exclusions apply	No charge

It might be the case that the numbers above are the exception, not the rule. Yet, in a more comprehensive analysis of premiums, it is clear that the smoker's premium varies considerably by state. Wyoming has some of the highest mark-ups, while Michigan has some of the lowest mark-ups. The plans

presented above are quite similar with respect to premiums and cost sharing for non-smokers, yet the smoker’s mark-up varies greatly. The table below shows average mark-ups for young smokers, restricting the set of plans to Obamacare “Silver” plans for 27-year-olds.

Silver Plans for a 27-year-old smoker, unsubsidized premium											
Rank	State	Average mark-up	Plans Examined	Rank	State	Average mark-up	Plans Examined	Rank	State	Average mark-up	Plans Examined
1	WY	31%	48	13	AR	13%	77	25	MS	7%	46
2	IA	29%	68	14	IN	12%	303	26	IL	7%	214
3	NE	20%	28	15	VA	12%	82	27	KS	7%	81
4	SC	20%	1,320	16	FL	12%	886	28	DE	7%	7
5	GA	17%	317	17	NV	11%	55	29	AL	7%	78
6	ND	17%	30	18	TX	10%	379	30	MO	6%	91
7	TN	17%	272	19	OR	9%	160	31	MI	6%	360
8	LA	17%	111	20	OK	8%	54	32	AK	5%	33
9	NC	16%	168	21	PA	8%	182	33	ME	4%	47
10	SD	16%	76	22	UT	8%	199	34	WV	2%	55
11	NH	16%	14	23	AZ	8%	161	35	NM	2%	83
12	MT	13%	56	24	OH	7%	333				

Notes: Each plan is evaluated for each rating area (unique health care market) within a state. For example, South Carolina has a separate rating area for each county.

If a “pack-a-day” smoker is [an overstatement](#) for actual consumption, then Obamacare cigarette taxes are extremely high in some states – in fact, far higher than the explicit excise tax. The median excise tax on cigarettes is [\\$1.36](#) per pack, and is \$0.60 per pack in Wyoming (ranking 40th out of the states) and \$2.00 per pack in Michigan (ranking 12th).

Based on this analysis, it is clear that the Obamacare smoker’s tax doesn’t represent risk adjustment in many states. But why are cigarette taxes in Obamacare – above and beyond the actuarial adjustment – a problem? Aren’t smokers are doing something terrible to themselves (and others, through secondhand smoke)? In economics, one of the core assumptions is individual rationality. People weight the costs and benefits of their actions and do what’s best for them. Everyday behavior – from smoking cigarettes, to eating pizza instead of broccoli ([or sometimes both](#)), to jaywalking in order to

save a few seconds of time, to getting in the car to drive to work – involves risk and rewards. If people understand the inherent risks and rewards, then we respect consumer autonomy even if we wouldn't make the same choice. The economic argument for taxing behavior like smoking (through excise taxes or Obamacare taxes) is that it creates negative externalities. For smoking, there are in fact [negative externalities](#). These are costs produced but not borne by the smoker, the most obvious of which is secondhand smoke. When such externalities exist, corrective taxation is one of several ways that a more efficient allocation of resources can be achieved. Nonetheless, evidence suggests that cigarette taxes at their current levels more than pay for such negative externalities. As importantly, there's no reason to think these externalities are much different in Wyoming and Michigan.

With that said, should we be concerned with Obamacare cigarette taxes versus, say, excise taxes? One disadvantage of differing excise taxes across state or city borders is that it encourages smuggling or purchases from low-tax areas. Thus, the tax doesn't correct the negative externality. That differs, of course, from Obamacare taxes where a person would need to move from Wyoming to Michigan to reduce the tax. Yet, Obamacare cigarette taxes present a host of problems. The vast majority of people do not receive health insurance from Obamacare, so its cigarette taxes do not correct the externalities smoking produces. In addition, the cigarette taxes in Obamacare lack transparency. They are buried in the weeds of Obamacare premiums as hefty smoking taxes, meant to influence or punish the choices of [18%](#) of American adults. Perhaps if smoking rates were as high as [obesity](#), they'd have enough political power that bureaucrats wouldn't punish them.

[Aaron Yelowitz](#) is an associate professor in economics at University of Kentucky and a Visiting Scholar at Cato Institute.