

Who Pays State and Local Taxes? What Makes Tax Systems Unfair– And What You Can Do About It

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The ITEP Tax Model-What it Does

- Predicts the distributional effect of proposed tax changes on taxpayers at different income levels
- Predicts the overall revenue gain (or loss) from proposed changes
- Estimates the overall state and local tax burden in each of the 50 states and Washington, DC
- Measures the interaction between state and federal tax changes (how state tax changes affect federal taxes paid, and how federal “tax mandates” affect the states)

The ITEP Tax Model-How it Works

- Based on a sample of 750,000 federal tax returns, allows a statistically valid sample for all 50 states and D.C.
- Income data from these returns is “matched” with Consumer Expenditure Survey, Census Bureau, and other data to estimate property, sales and excise tax burdens for any year from 1988 to 2012.
- This “matching” process allows us to estimate the impact of proposed changes in sales, income, and property taxes in each state—and to estimate the impact of “tax swaps” involving more than one of these tax bases simultaneously.
- The use of federal tax data allows us to estimate the effect of state tax changes on federal taxes—and vice versa.

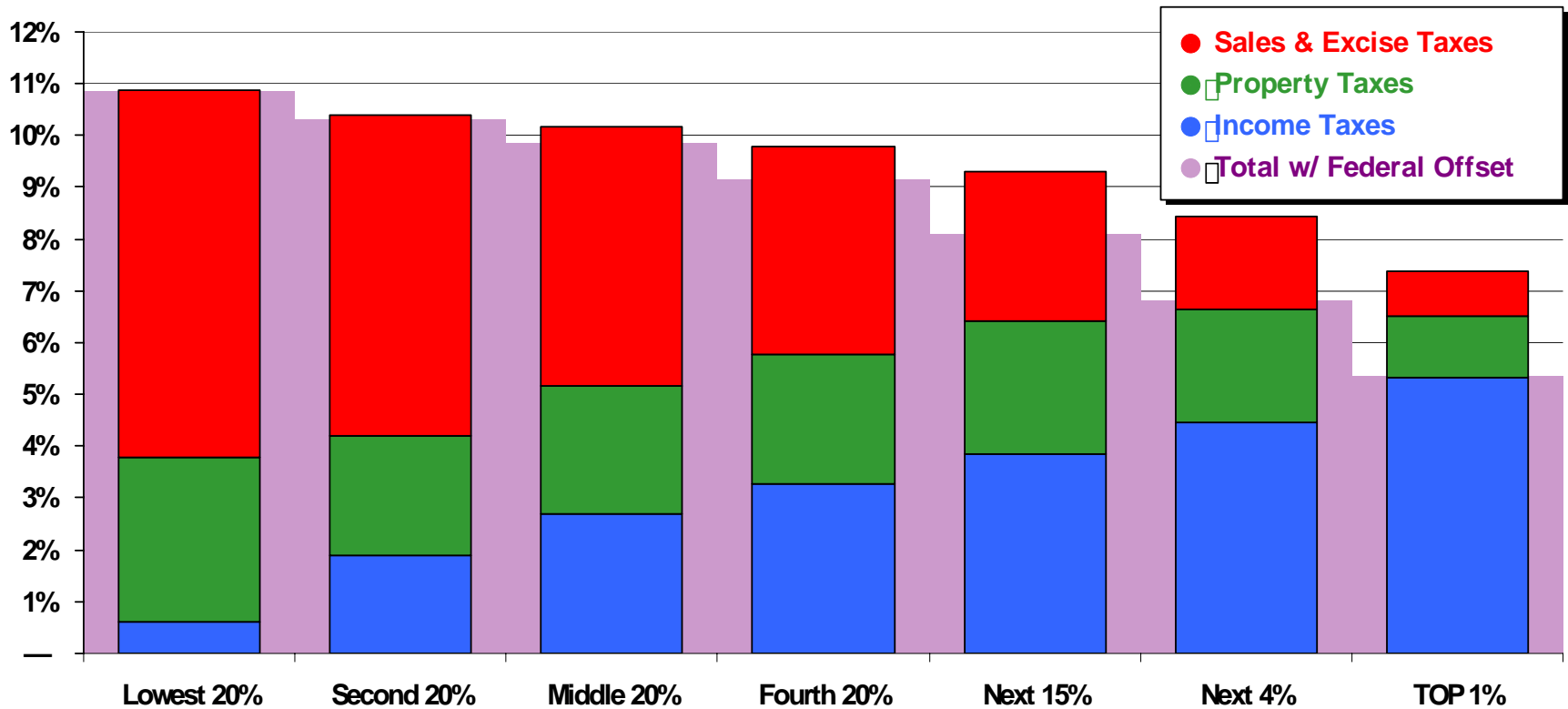
What “Who Pays” Measures:

- The fairness of each state’s state and local taxes in 2006;
- The impact of tax changes that have already been enacted but have not yet taken effect (for example, income tax rate cuts in Ohio).
- The study’s universe includes all non-elderly taxpayers.
- The study separates each state’s non-elderly population into income “quintiles” – groups of twenty percent of the population.

Who Pays? Prelim Results

State & Local Taxes in All 50 States, 2006

Shares of family income for non-elderly taxpayers

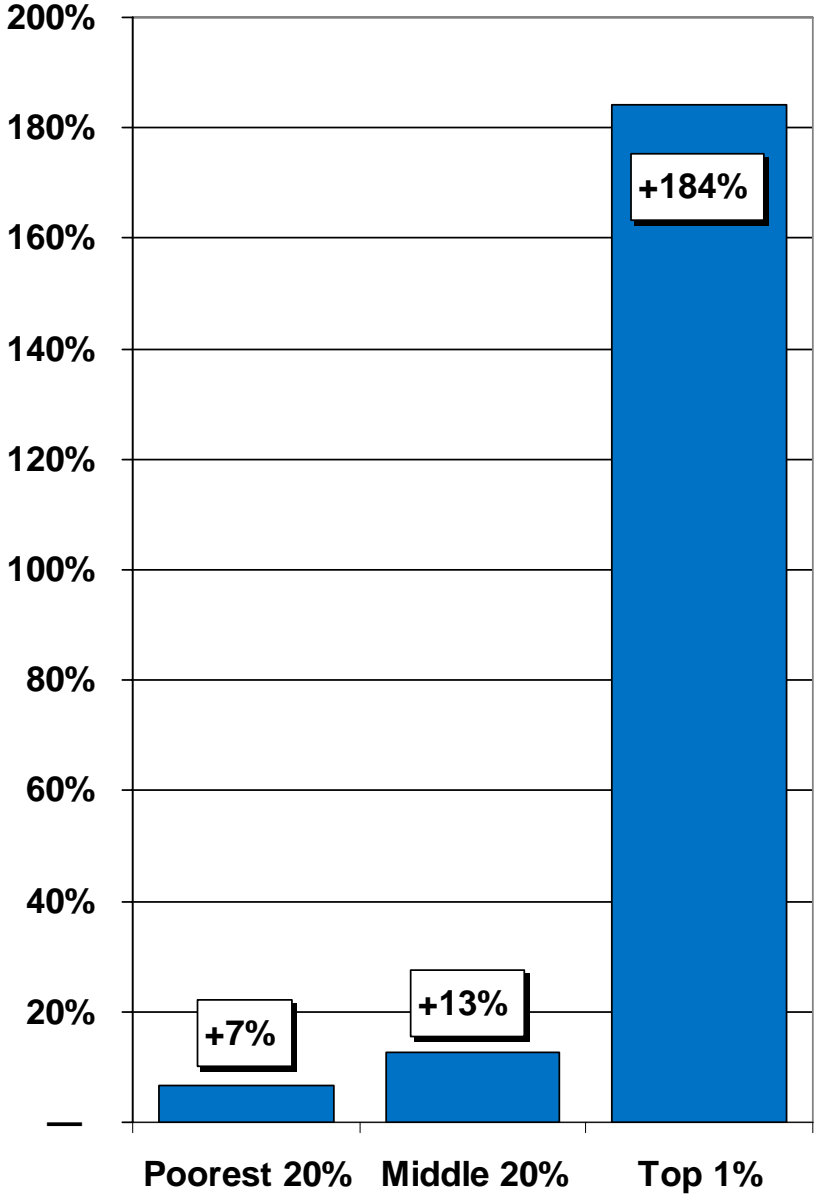


Major findings of the study:

- Most states have regressive tax systems.
- Virtually every state taxes its best-off citizens at a *lower* rate than the poor.
- Only 4 states tax their best-off citizens at the same effective rate as the middle 20% of the income distribution.
- “Low-tax” states are often those with the *highest* taxes on the poor.

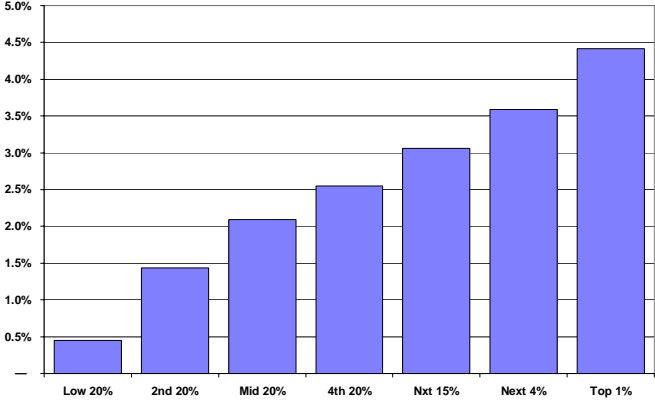
The Rich Get Richer:

Real Income Growth, 1979-2000

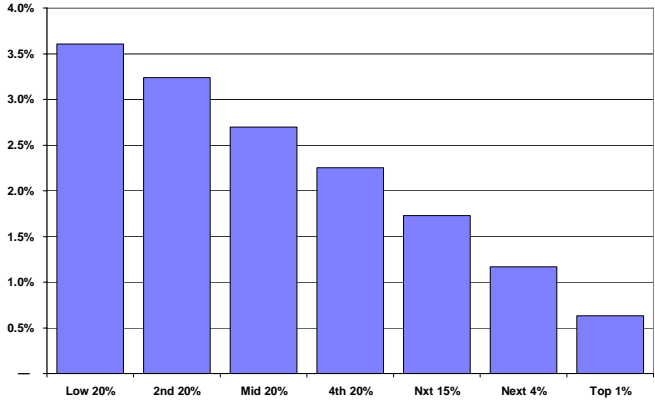


This “average” US state and local tax system is the result of the interaction between personal income taxes, sales and excise taxes, property taxes, and corporate income taxes.

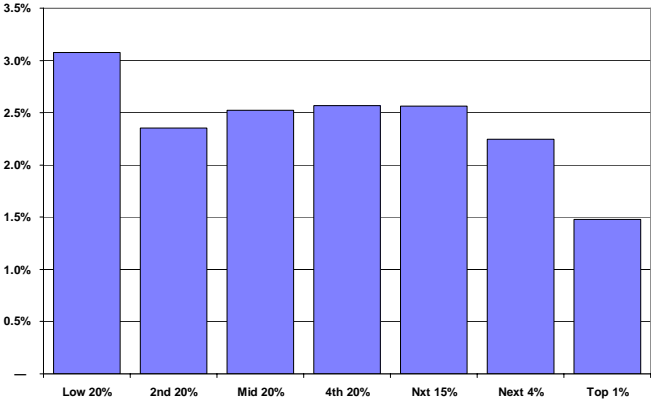
Personal Income Taxes



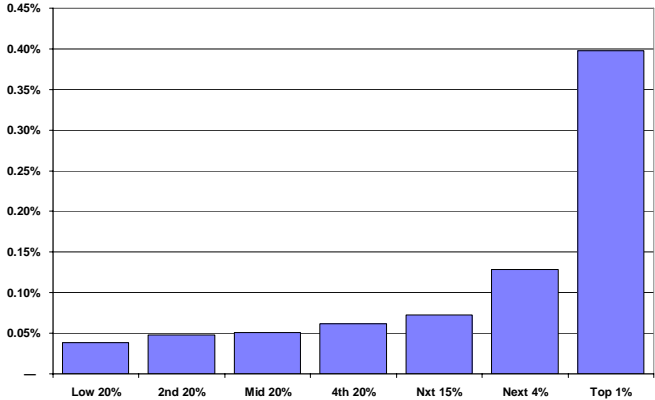
General Sales Taxes



Property Taxes



Corporate Income Taxes



The Ten Most Regressive State Tax Systems

Taxes as shares of income by income for non-elderly residents

Income Group	Taxes as a % of Income on			Poor/ Top 1%	Middle/ Top 1%
	Poorest 20%	Middle 60%	Top 1%		
Washington	17.5%	11.4%	2.1%	828%	540%
South Dakota	12.5%	10.2%	2.6%	477%	389%
Florida	12.4%	9.3%	3.1%	403%	300%
Arizona	14.6%	11.6%	6.0%	245%	194%
Texas	11.7%	8.7%	3.3%	353%	264%
Tennessee	10.7%	8.6%	3.3%	325%	262%
Wyoming	9.3%	7.9%	2.1%	436%	373%
Illinois	12.4%	10.2%	5.3%	233%	191%
Pennsylvania	11.9%	10.0%	5.0%	238%	200%
Hawaii	14.4%	11.5%	7.7%	188%	150%

Features of the Ten Most Regressive Tax Systems

	No Broad-Based Income Tax	Flat Income Tax	Heavy Use of Sales & Excise Taxes
Washington	✓		✓
South Dakota	✓		✓
Florida	✓		✓
Arizona			✓
Texas	✓		✓
Tennessee	✓		✓
Wyoming	✓		
Illinois		✓	
Pennsylvania		✓	✓
Hawaii			✓

Characteristics of the Least Regressive Tax Systems

	Personal Income Tax	
	Very Progressive	Other Details
		Low Use of Sales & Excise Taxes

Delaware



Vermont



Ref. Credits*



California



Oregon



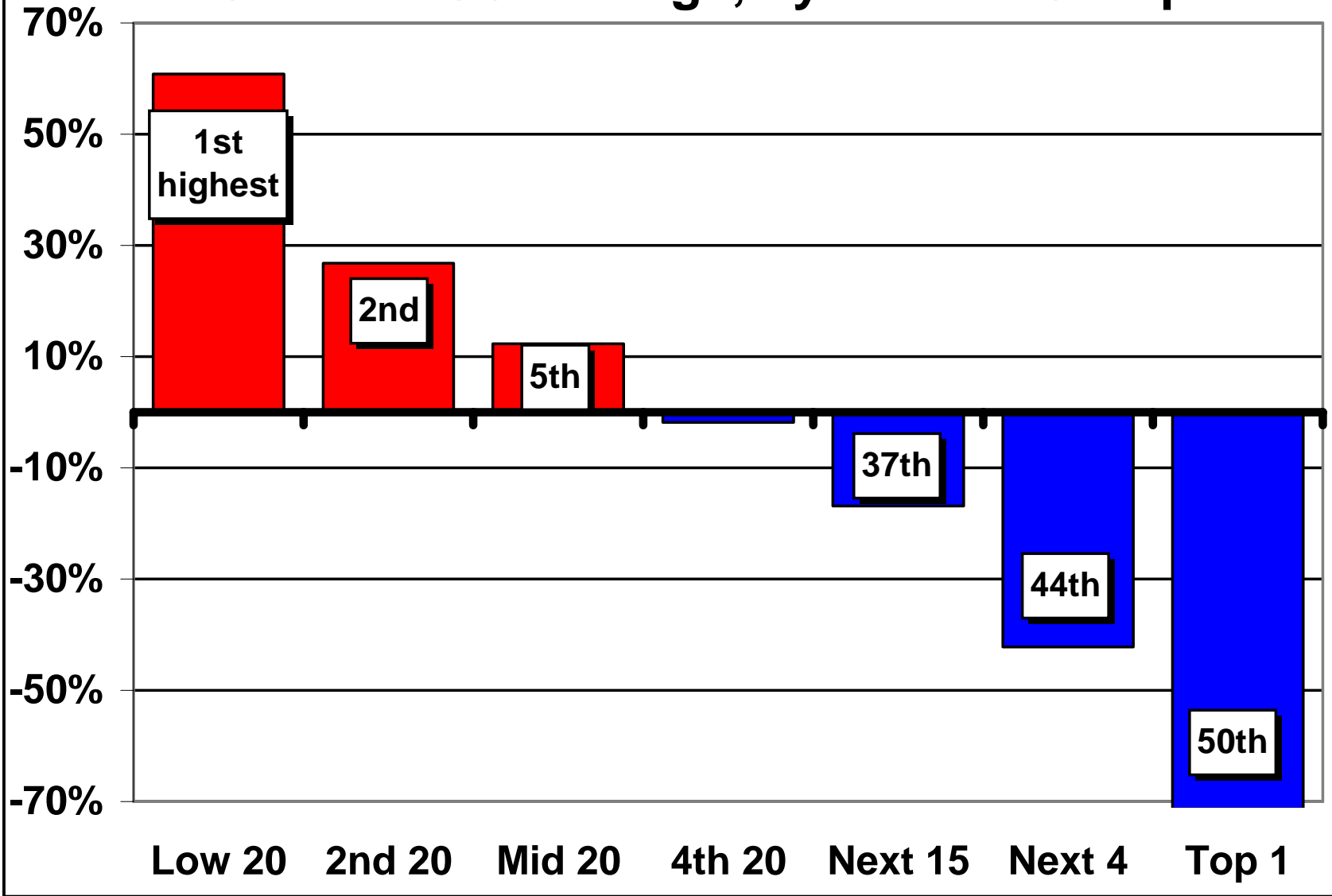
High reliance



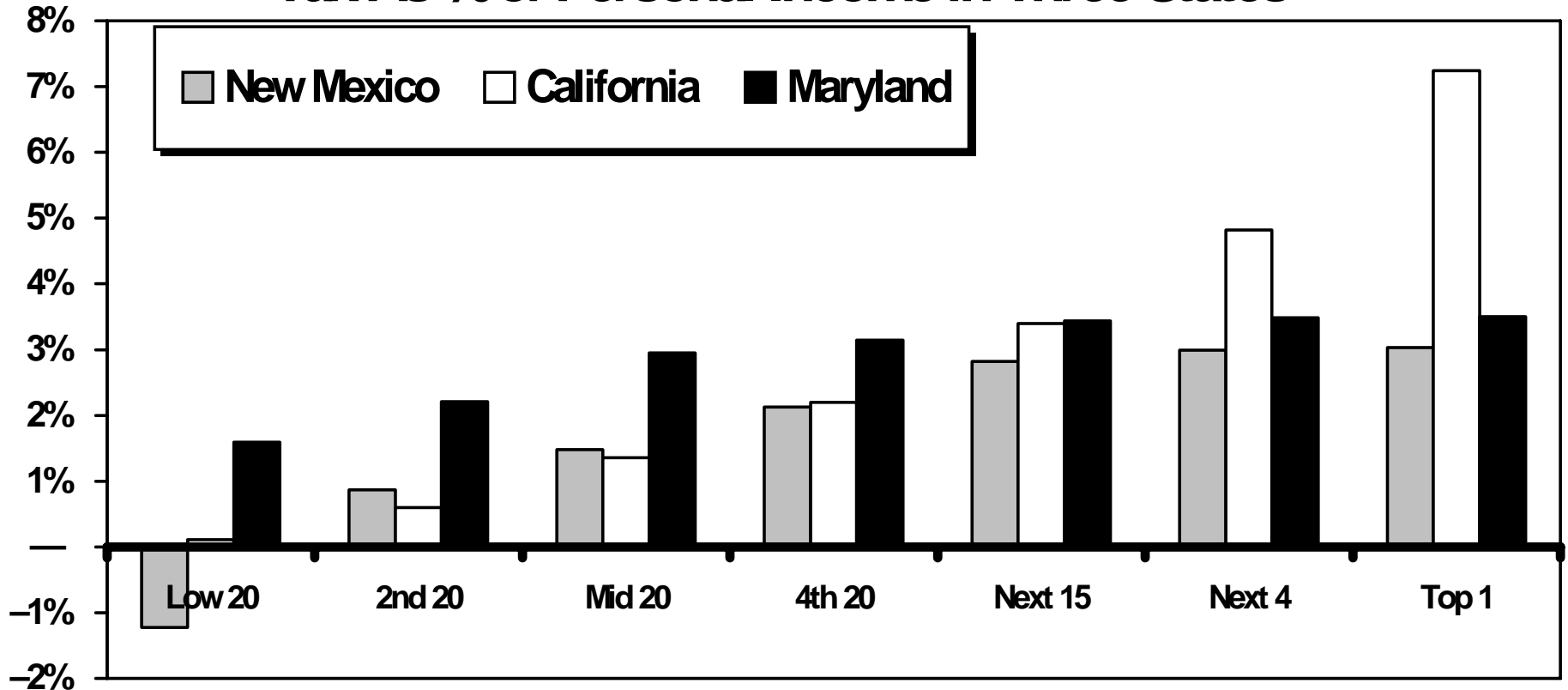
**Refundable credits are allowed even if they exceed a low-income family's income tax liability.*

The Ten States with the Highest Taxes on the Poor		Ten States with the Lowest Taxes on the Rich	
Washington	17.5%	Nevada	1.9%
Arizona	14.6%	Washington	2.1%
Hawaii	14.4%	Wyoming	2.1%
Arkansas	14.1%	New Hampshire	2.4%
Rhode Island	13.0%	South Dakota	2.6%
South Dakota	12.5%	Alaska	2.8%
Florida	12.4%	Florida	3.1%
Illinois	12.4%	Tennessee	3.3%
Pennsylvania	11.9%	Texas	3.3%
Oklahoma	11.7%	Pennsylvania	5.0%

A Low-Tax State? Washington Taxes As a Share of US Average, by Income Group



Not All Income Taxes Are Created Equal: State Income Tax As % of Personal Income in Three States



Some states have especially progressive income taxes.

The Adequate Eight: Progressive State Income Taxes

Income taxes as shares of income by non-elderly residents

Income group	Lowest 20%	Middle 60%	Top 1%	Notes
California	0.1%	1.4%	7.2%	<i>Highly graduated rates, low-income credit</i>
New Jersey	-0.6%	1.6%	6.5%	<i>High top rate, generous refundable credit*</i>
Vermont	-0.5%	1.6%	5.8%	<i>Highly graduated rates, refundable credits</i>
New York	-1.4%	2.8%	5.4%	<i>Highly graduated rates, refundable credits</i>
Maine	0.5%	2.7%	6.3%	<i>Graduated rates, low-income credit</i>
Minnesota	0.5%	3.4%	5.9%	<i>Graduated rates, refundable credits</i>
Idaho	0.2%	2.6%	5.3%	<i>Highly graduated rates, low-income credit</i>
Kansas	-0.7%	2.6%	4.8%	<i>Highly graduated rates, low-income credit</i>

**Refundable credits are allowed even if they exceed a low-income family's income tax liability*

But other state income taxes are virtually flat.

Seven States with Little or No Personal Income Tax Progressivity

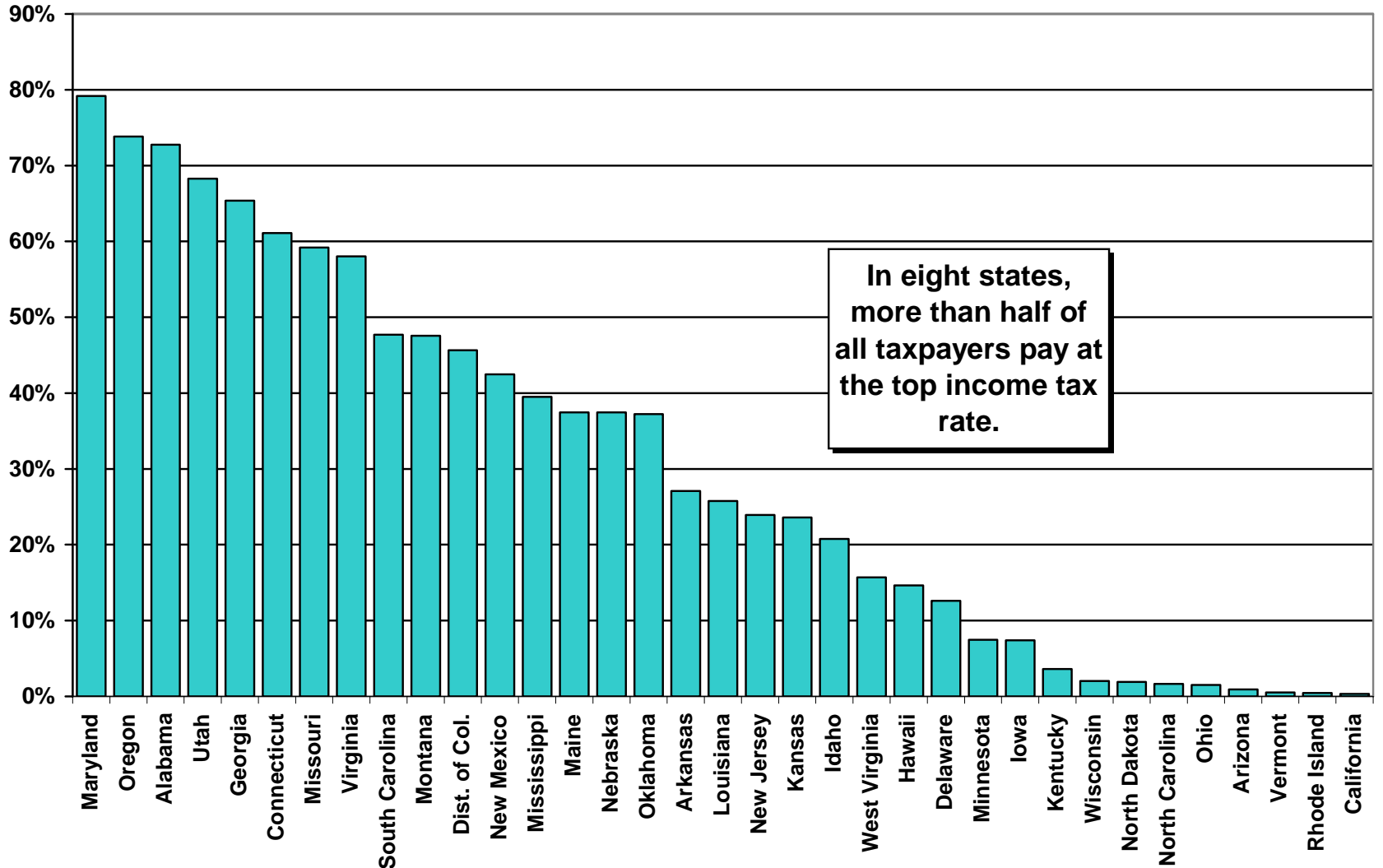
Income taxes as shares of income by non-elderly residents

Income group	Lowest 20%	Middle 60%	Top 1%	Notes
Pennsylvania	2.7%	2.9%	2.8%	<i>Flat rate</i>
Alabama	2.7%	3.0%	3.0%	<i>Effectively flat rate*</i>
Indiana	2.0%	2.5%	2.4%	<i>Flat rate</i>
Illinois	2.1%	2.3%	2.4%	<i>Flat rate</i>
Maryland	2.6%	3.1%	3.2%	<i>Effectively flat rate*</i>
Colorado	2.1%	3.2%	3.2%	<i>Flat rate</i>
Arizona	2.1%	3.0%	3.2%	<i>Low top rate, wide brackets</i>

* *Effectively flat because top bracket is so low, most taxpayers fall into it*

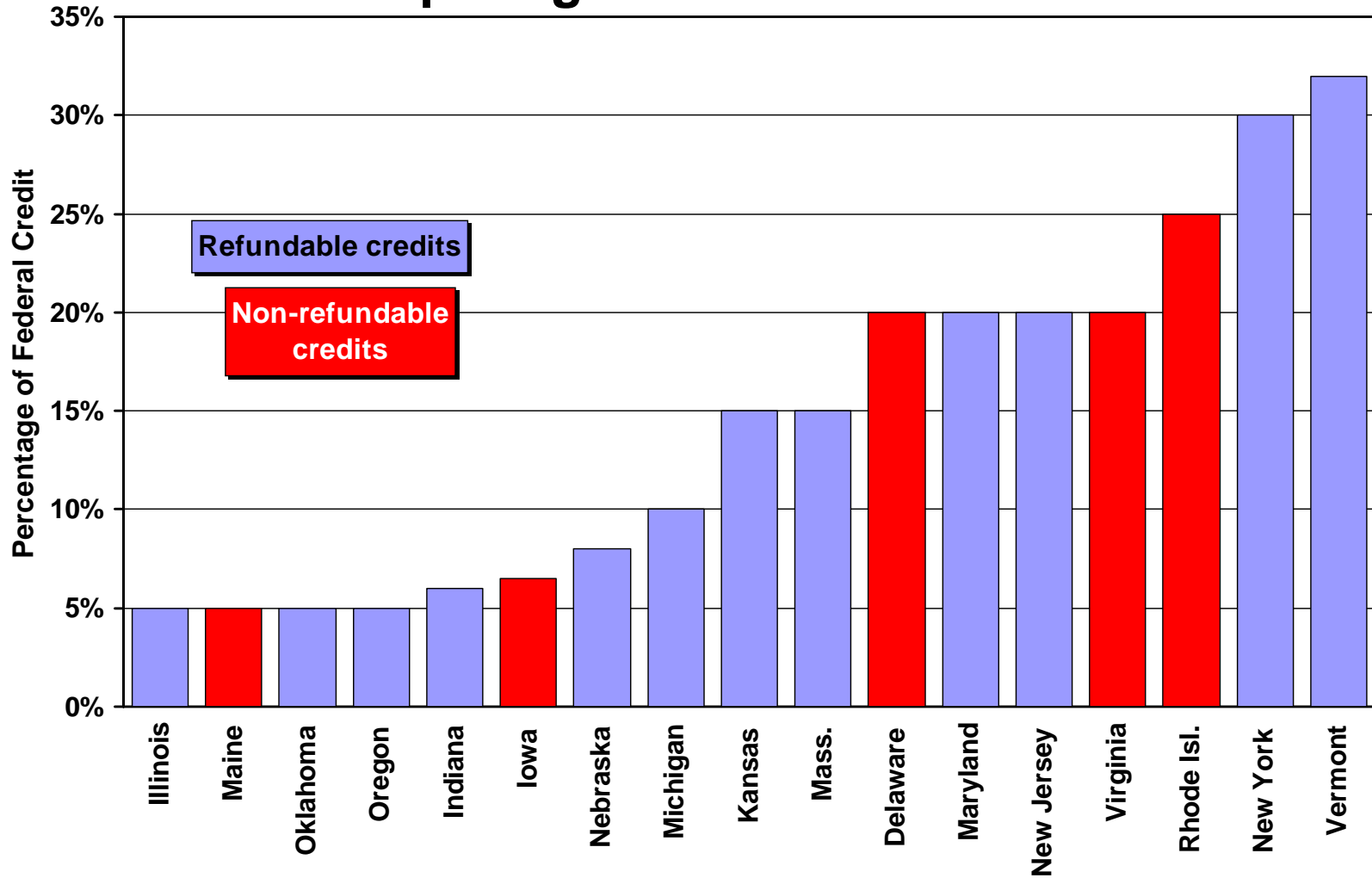
Not all graduated income taxes are created equal.

% of Taxpayers Paying at Top Income Tax Rate, 2005



Not all EITC's are created equal either: some are refundable, and some are redundant.

Comparing State EITCs in 2006

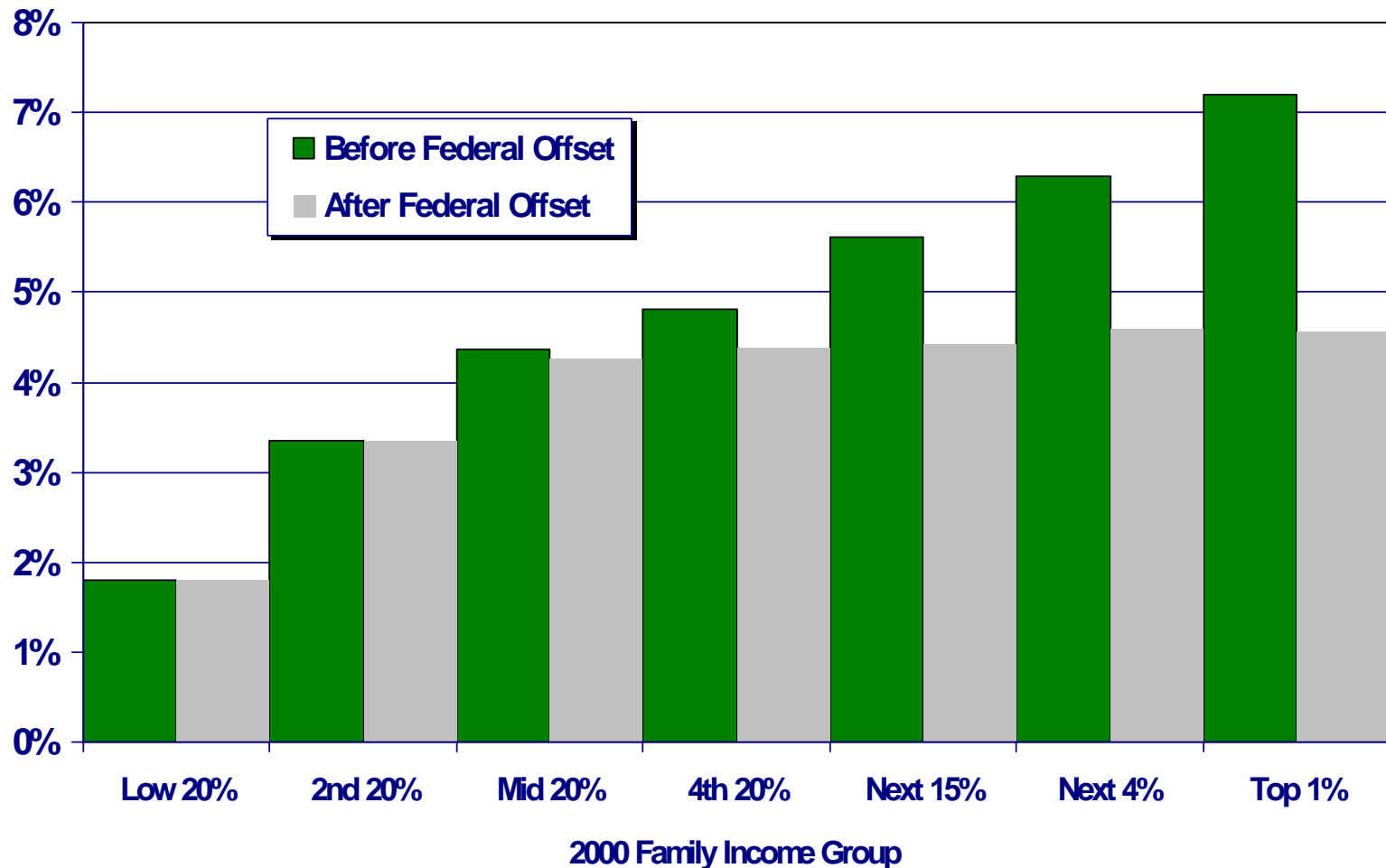


Notable Income Tax “Reforms,” 2003-2006

- **New Mexico** eliminated 3 of 7 tax brackets. Top bracket used to start at \$100K for couples— now at \$24K. Top rate drops from 8.2% to 4.9%. New capital gains break.
- Fairness ranking drops from 3rd to 23rd !!!
- **Kentucky** moved in the opposite direction, creating a new top tax bracket over \$75,000 (up from \$8,000). % paying at top rate drops from 60% to < 10%
- **California, New Jersey** imposed “millionaire’s tax” affecting only a small percentage of wealthy families.
- **Earned Income Tax Credits** galore.

The “federal offset” makes state tax systems even more regressive—but allows states to export taxes out of state.





Oregon Personal Income Tax as Share of Income in 2000



What Makes a Sales Tax Regressive: Taxing Food

The 7 Most Regressive General Sales Taxes

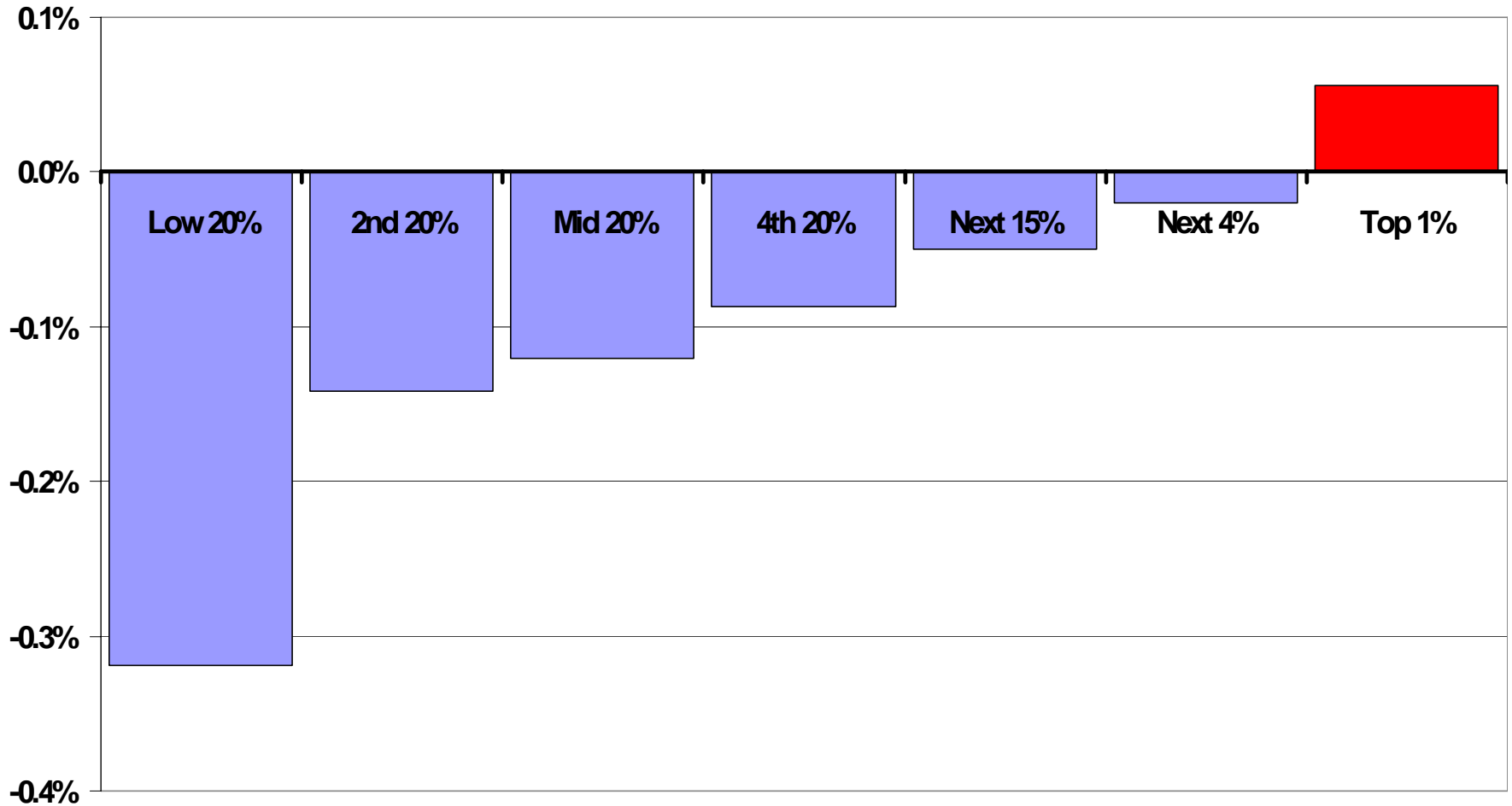
Sales taxes as shares of income by family income group

Income Group	Total State Sales Tax			Sales Tax on Groceries?
	Lowest 20%	Middle 20%	Top 1%	
Arkansas	7.7%	4.1%	1.0%	
Mississippi	7.6%	5.4%	1.3%	
Arizona	5.3%	3.5%	0.8%	
New Mexico	4.7%	3.0%	0.7%	
South Dakota	7.3%	4.9%	1.4%	
Tennessee	4.2%	2.7%	0.7%	
Texas	4.6%	3.1%	0.8%	

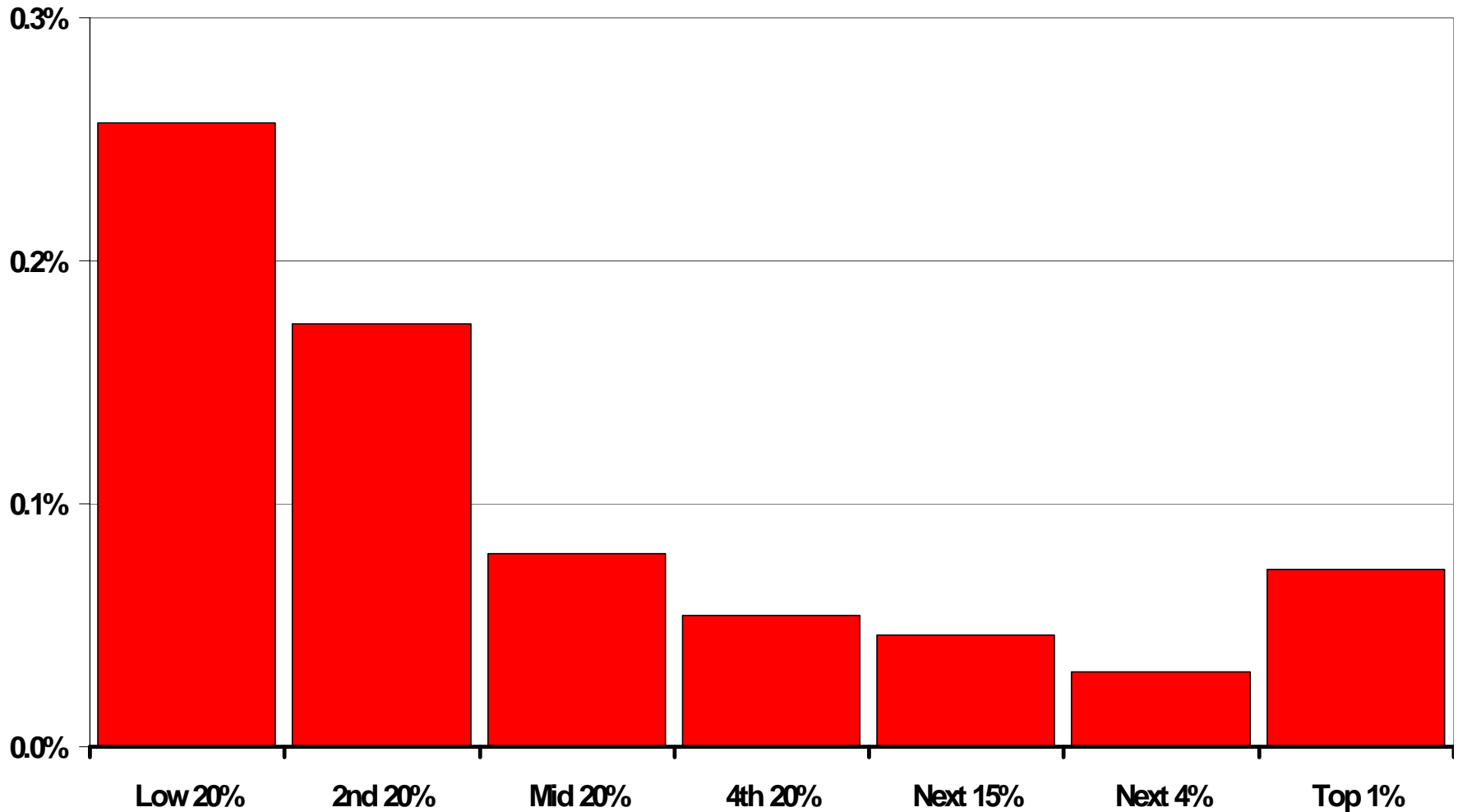
Does Exempting Food Make the Tax System Less Regressive? Maybe.

- **Georgia** exempted food from the state sales tax in 1998— and has since expanded local sales tax authority more than almost any other state.
- **Louisiana** has periodically exempted food and utilities from the state sales tax—and has continually allowed local rates to climb.
- **North Carolina** exempted food in 1998, and has since raised both state and local sales tax rates.
- **New Mexico** exempted food in 2003— and hiked the sales tax rate almost immediately to pay for it.
- Discussions of food tax repeal in **Mississippi** have focused on immediately replacing (most of) the revenue loss with a cigarette tax hike.

New Mexico's "sales tax swap" had a progressive short-term impact...



But it didn't last long: hikes in excise taxes drowned out the benefits to low-income families.



Even “Across-the-Board” Property Tax Cuts are Regressive– Or Are They?

Impact of Property Tax- Sales Tax Swap

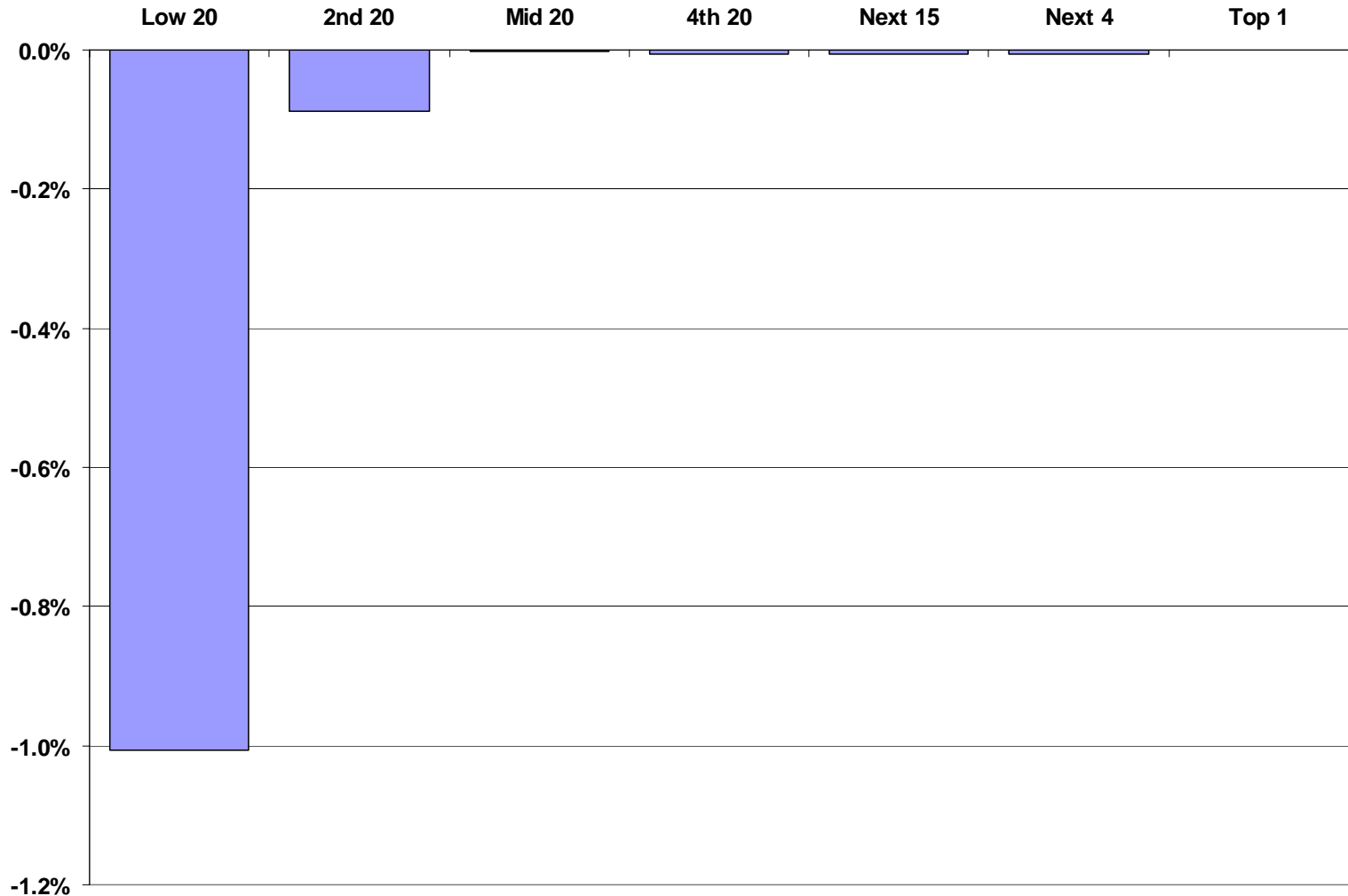
All Idaho Taxpayers, 2006 levels

2006 Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%	Next 4%	Top 1%	
Income Range	Less Than \$16,000	\$16,000 – \$28,000	\$28,000 – \$48,000	\$48,000 – \$74,000	\$74,000 – \$134,000	\$134,000 – \$298,000	\$298,000 – Or More	State Revenue Change, 2006
Average Income in Group	\$10,000	\$22,000	\$36,000	\$59,000	\$95,000	\$179,000	\$863,000	
Tax Change as % of Income								
Property Tax Cut	-0.4%	-0.3%	-0.2%	-0.2%	-0.2%	-0.2%	-0.2%	\$ -125,000
Sales Tax Increase	+0.5%	+0.5%	+0.4%	+0.3%	+0.2%	+0.1%	+0.1%	\$ +105,000
Both Changes	+0.1%	+0.2%	+0.2%	+0.1%	+0.0%	-0.1%	-0.1%	\$ -20,000

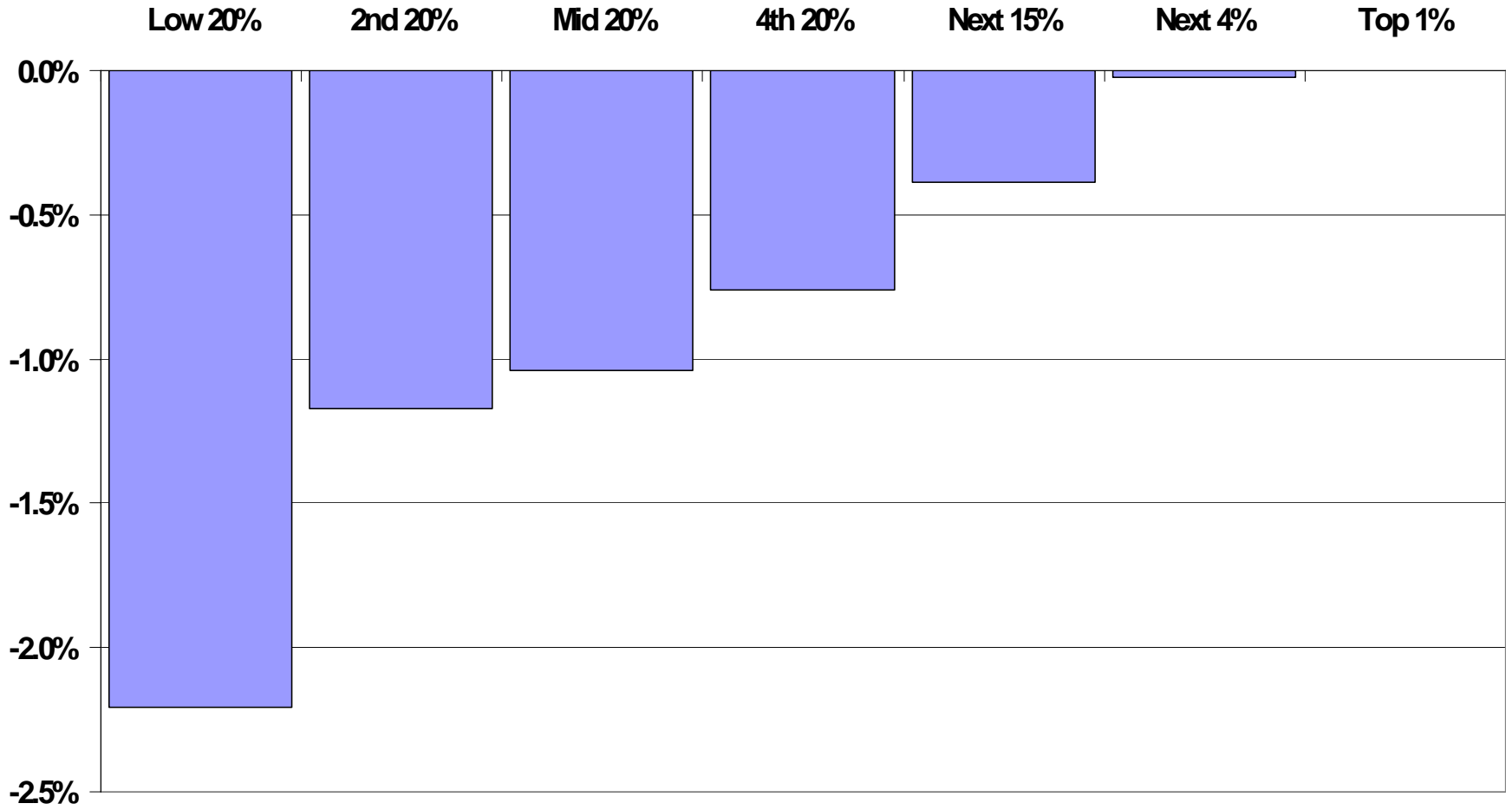
SOURCE: Institute on Taxation and Economic Policy, February 2006

“Circuit-breaker” property tax credits are usually targeted to the very poorest taxpayers.

The Wisconsin Low-Income "Circuit Breaker"

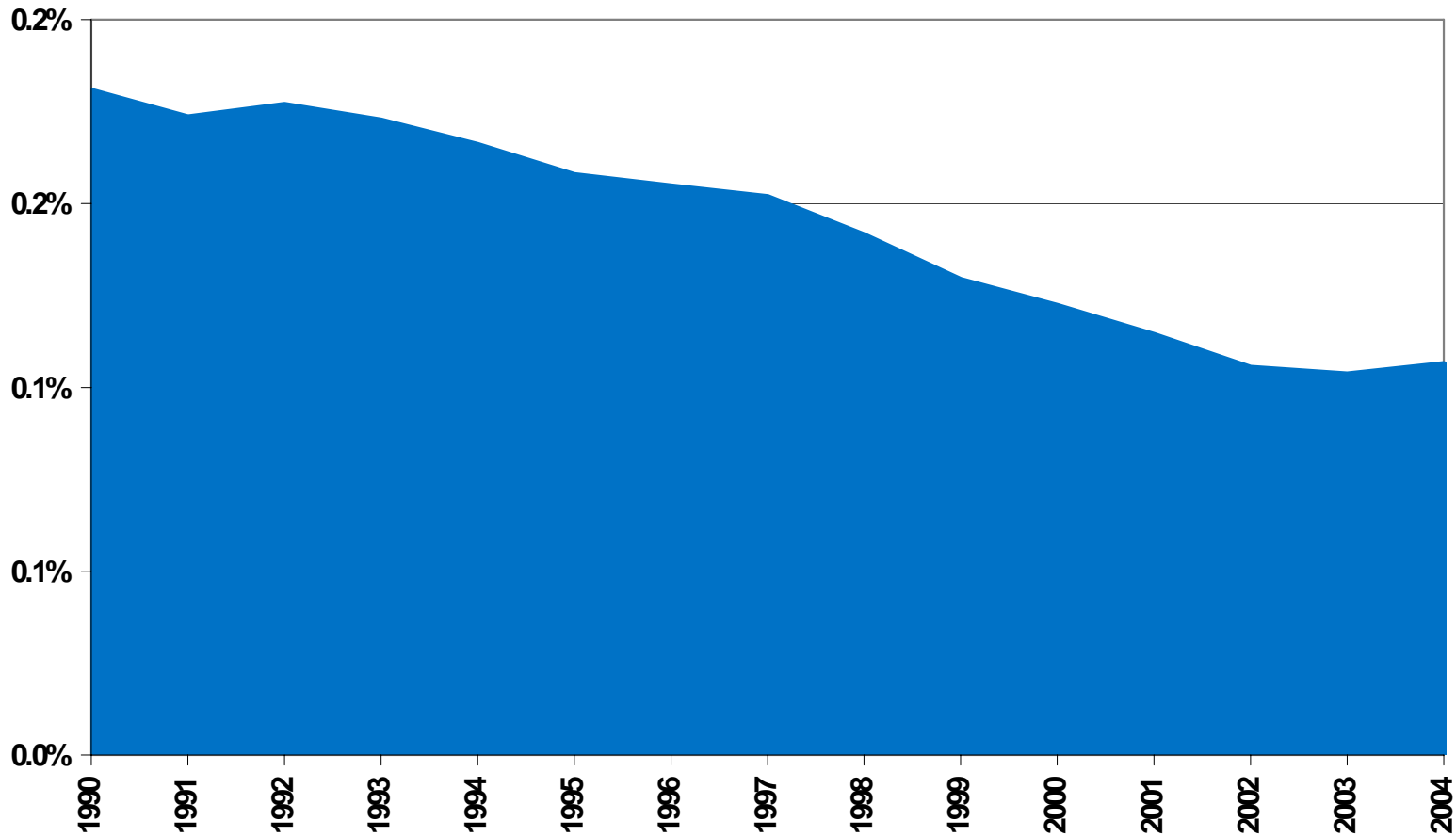


New Jersey's "circuit breaker" credit is aimed at a wider swath of the income distribution.



Smoke 'Em If You've Got 'Em: The Decline of State and Local Cigarette Taxes

Minnesota Cigarette Tax Revenues as a Share of Personal Income, 1990-2004



Want to Know More?

- **Tentative release date: January 2007**
- ITEP staff will provide technical support to state-based groups organizing releases around Who Pays.
- Embargoed final results will be distributed ahead of the final release.
- To find out more about ongoing efforts for (or against) tax fairness, subscribe to ITEP's weekly **Tax Justice Digest** by sending an email to ctj@ctj.org.