

# State & Local Taxes Hit Poor & Middle Class Far Harder than the Wealthy

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By an overwhelming margin, most states tax their middle- and low-income families far more heavily than the wealthy, according to a new study by the Institute on Taxation & Economic Policy.

“In the coming months, lawmakers across the nation will be forced to make difficult decisions about budget-balancing tax changes—which makes it vital to understand who is hit hardest by state and local taxes right now,” said Matthew Gardner, lead author of the study, *Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. “The harsh reality is that most states require their poor and middle-income taxpayers to pay the most taxes as a share of income.”

Nationwide, the study found that middle- and low-income non-elderly families pay much higher shares of their income in state and local taxes than do the very well-off:

- The average state and local tax rate on the best-off one percent of families is 6.4 percent before accounting for the tax savings from federal itemized deductions. After the federal offset, the effective tax rate on the best off one percent is a mere 5.2 percent.
- The average tax rate on families in the middle 20 percent of the income spectrum is 9.7 percent before the federal offset and 9.4 percent after—almost twice the effective rate that the richest people pay.
- The average tax rate on the poorest 20 percent of families is the highest of all. At 10.9 percent, it is more than double the effective rate on the very wealthy.

“Fairness is in the eye of the beholder.” noted Gardner. “But virtually anyone would agree that this upside-down approach to state and local taxes is astonishingly inequitable.”

## The “Terrible Ten” Most Regressive Tax Systems

Ten states—Washington, Florida, South Dakota, Tennessee, Texas, Illinois, Arizona, Nevada, Pennsylvania, and Alabama—are particularly regressive. These “Terrible Ten” states ask poor families—those in the bottom 20% of the income scale—to pay almost six times as much of their earnings in taxes as do the wealthy. Middle-income families in these states pay up to three-and-a-half times as high a share of their income as the wealthiest families. “Virtually every state has a regressive tax system,” noted Gardner. “But these ten states stand out for the extraordinary degree to which they have shifted the cost of funding public investments to their very poorest residents.”

The report identifies several factors that make these states more regressive than others:

- The most regressive states generally either do not levy an income tax, or levy the tax at a flat rate;
- These states typically have an especially high reliance on regressive sales and excise taxes;
- These states usually do not allow targeted low-income tax credits such as the Earned Income Tax Credit; these tax credits are especially effective in reducing state tax unfairness.

“For lawmakers seeking to make their tax systems less unfair, there is an obvious strategy available,” noted Gardner. “Shifting state and local revenues away from sales and excise taxes, and towards the progressive personal income tax, will make tax systems fairer for low- and middle-income families. Conversely, states that choose to balance their budgets by further increasing the general sales tax or cigarette taxes will make their tax systems even more unbalanced and unfair.”

## **Implications for State Budget Battles in 2010**

“In the coming months, many states’ lawmakers will convene to deal with fiscal shortfalls even worse than those they faced last year,” Gardner said. “Lawmakers may choose to close these budget gaps in the same way that they have done all too often in the past—through regressive tax hikes. Or they may decide instead to ask wealthier families to pay tax rates more commensurate with their incomes. In either case, the path that states choose in the upcoming year will have a major impact on the well-being of their citizens—and on the fairness of state and local taxes.”

### **A one-page chart summarizing U.S. average state & local taxes by income group follows**

The Institute on Taxation and Economic Policy is a nonpartisan Washington-based research group. The full *Who Pays?* report is available in PDF format at [www.whopays.org](http://www.whopays.org). Printed copies can be ordered by calling ITEP at 202-299-1066.

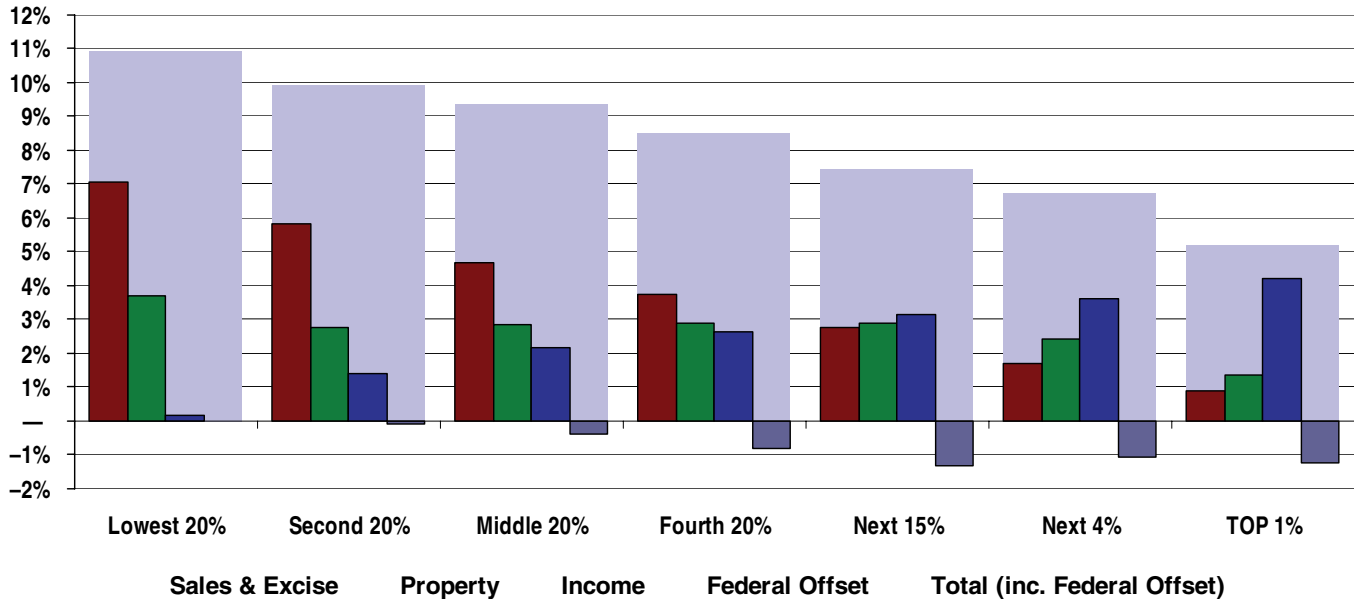
*Who Pays?* examines the tax systems of all 50 states and the District of Columbia, using the Institute on Taxation & Economic Policy Microsimulation Tax Model. The ITEP Model is similar in methodology and data sources to the elaborate computer models used by the U.S. Treasury and the congressional Joint Committee on Taxation, except that the ITEP Model adds state-by-state estimating capabilities.

The findings published in the study detail state and local taxes paid by non-elderly couples and individuals. The study includes all major state and local taxes: personal and corporate income taxes, property taxes, and sales and excise taxes.

# Averages for All States

## State & Local Taxes in 2007

Shares of family income for non-elderly taxpayers



Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
<b>Income Range</b>	Less than \$18,000	\$18,000 – \$33,000	\$33,000 – \$54,000	\$54,000 – \$90,000	\$90,000 – \$185,000	\$185,000 – \$476,000	\$476,000 or more
<b>Average Income in Group</b>	\$10,700	\$25,500	\$42,900	\$69,900	\$122,400	\$277,900	\$1,768,000
<b>Sales &amp; Excise Taxes</b>	<b>7.1%</b>	<b>5.9%</b>	<b>4.7%</b>	<b>3.7%</b>	<b>2.8%</b>	<b>1.7%</b>	<b>0.9%</b>
General Sales—Individuals	3.3%	3.0%	2.5%	2.1%	1.6%	1.0%	0.5%
Other Sales & Excise—Ind.	1.6%	1.1%	0.8%	0.6%	0.4%	0.2%	0.1%
Sales & Excise on Business	2.1%	1.8%	1.4%	1.1%	0.8%	0.5%	0.3%
<b>Property Taxes</b>	<b>3.7%</b>	<b>2.8%</b>	<b>2.9%</b>	<b>2.9%</b>	<b>2.9%</b>	<b>2.4%</b>	<b>1.4%</b>
Property Taxes on Families	3.6%	2.7%	2.7%	2.8%	2.7%	2.1%	0.7%
Other Property Taxes	0.1%	0.1%	0.1%	0.1%	0.2%	0.3%	0.7%
<b>Income Taxes</b>	<b>0.2%</b>	<b>1.4%</b>	<b>2.2%</b>	<b>2.6%</b>	<b>3.1%</b>	<b>3.6%</b>	<b>4.2%</b>
Personal Income Tax	0.2%	1.4%	2.2%	2.6%	3.1%	3.5%	3.93%
Corporate Income Tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.27%
<b>TOTAL TAXES</b>	<b>10.9%</b>	<b>10.0%</b>	<b>9.7%</b>	<b>9.3%</b>	<b>8.8%</b>	<b>7.8%</b>	<b>6.4%</b>
<b>Federal Deduction Offset</b>	<b>-0.0%</b>	<b>-0.1%</b>	<b>-0.4%</b>	<b>-0.8%</b>	<b>-1.3%</b>	<b>-1.1%</b>	<b>-1.25%</b>
<b>TOTAL AFTER OFFSET</b>	<b>10.9%</b>	<b>9.9%</b>	<b>9.4%</b>	<b>8.5%</b>	<b>7.4%</b>	<b>6.7%</b>	<b>5.2%</b>

Note: Table shows 2007 tax law updated to reflect permanent changes in law enacted through October 2009.