

318 2nd Ave. N • Mount Vernon, IA 52314

www.iowapolicyproject.org

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CONTACT: Mike Owen (319) 643-3628  
ipp@Lcom.net

## Iowa Taxes: Who Pays?

### Study Shows Iowa Taxes Hit Poor, Middle-Income Iowans Hardest

IOWA CITY, Iowa (January 7, 2003) – Low- and moderate-income Iowans pay a much larger share of their income in taxes than those at the top of the income scale, according to a report released today.

A new report from the Institute on Taxation and Economic Policy in Washington, D.C., examines the burden of sales taxes, property taxes and income taxes on non-elderly taxpayers' family incomes in all 50 states. For Iowa, the study found, the total burden for the lowest three-fifths of income earners was over 10 percent of their income after federal deductions, with that level dropping sharply at the higher end of the income scale.

“Some politicians like to focus only on the income-tax burden, ignoring the fact that sales and property taxes combine to make the Iowa tax burden proportionately highest for lower- and middle-income taxpayers,” said David Osterberg, executive director of the Iowa Policy Project.

Osterberg said the ITEP report is especially timely, coming the week before the Iowa General Assembly convenes amid new discussion of both continued budget problems for the state, and ideas to change Iowa's tax system.

“This new report demonstrates that any changes in Iowa's tax structure need to keep from further harming working Iowans,” Osterberg said.

An IPP report last year demonstrated how the combination of changes in Iowa sales and income taxes in the 1990s made Iowa's state tax structure more regressive – meaning the structure is more burdensome on lower-income earners. That report did not take property taxes into account.

“State and local governments are being called upon to take on more and more responsibilities,” said Robert S. McIntyre, ITEP's tax policy director and lead author of the study, titled *Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. “Unfortunately, when it comes to paying for services, Iowa has an unfair tax system.”

For Iowa's top 1 percent of taxpayers in 2002, the total burden after federal deductions was 5.8 percent of income, and for the next 4 percent of taxpayers, the burden was 7.2 percent of income. That compares with 10.6 percent for the lowest one-fifth of income earners, 10.5 percent for the next one-fifth, and 10.4 percent for the middle one-fifth.

“The only progressive tax in Iowa is the state income tax,” said IPP Research Director Peter Fisher. “That is deductible on a person's federal income tax return, and so is the property tax. The sales tax is not deductible. Only higher income taxpayers itemize deductions, so this deductibility has the effect of substantially reducing the tax burden on the richest taxpayers.”

For the richest 1 percent of Iowans in 2002, that reduced the combined state and local tax burden from 7.9 percent of income to 5.8 percent, the ITEP study found. That compares with a 10.6 percent rate for the lowest 20 percent – those making less than \$14,000 a year.

Fisher noted that Iowa is one of the few states that allow federal taxes to be deducted on state income tax returns.

“This is the major factor making the Iowa income tax only modestly progressive and preventing it from offsetting the regressivity of sales and property taxes,” Fisher said. “The ITEP study shows that, despite a top rate of 8.98 percent, actual income taxes paid by the richest Iowans average just 5.2 percent of income. And this is before the effects of deducting state taxes on federal returns, which further lowers the effective rate on the rich.”

“The regressivity of the state-local tax system, particularly at the high end, needs to be kept in mind when considering proposals for reform of Iowa taxes,” Fisher added.

Some legislators, for example, have discussed a flat-rate income tax.

“Any proposal to move to a flat-rate income tax would necessarily be most beneficial to those at the top,” Fisher said. “They already constitute the major beneficiaries of tax policy in the 1990s. It would make the income tax less progressive, and the overall tax system more regressive.”

The ITEP study also shows that the sales tax remains quite regressive even with the exemption of residential utilities. (The ITEP study estimates tax burdens with the exemption fully phased in.) Thus any increase in the sales tax would make the system more regressive, unless accompanied by offsetting tax relief for low and middle income Iowans, Fisher said.

The Iowa Policy Project is a non-profit, non-partisan research organization headquartered in Mount Vernon, Iowa. The IPP engages scholars at Iowa’s public and private colleges and universities to perform research on issues of importance to the citizens of Iowa. IPP reports are available to the public, free of charge, on the web at [www.iowapolicyproject.org](http://www.iowapolicyproject.org).

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For more information, see <http://www.itep.org>, or <http://www.iowapolicyproject.org>.

For interviews with Peter Fisher or David Osterberg, contact Mike Owen at (319) 643-3628 or [ipp@Lcom.net](mailto:ipp@Lcom.net)