
Iowa Fiscal Partnership

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Contact: Mike Owen, (319) 338-0773 office, (319) 331-1287 cell

Report: Iowa Tax Breaks Pose New Challenges

DES MOINES, Iowa (April 19, 2005) – Iowa’s personal income tax system offers generous treatment to retirees, according to a new analysis that points to a looming loss of resources to serve the state’s growing elderly population and other essential needs.

As the state’s income-tax filing deadline is approaching and Iowa legislators are working on the state’s budget, the Iowa Fiscal Partnership – a nonpartisan budget watchdog initiative – is renewing a call for fairness and attention to accepted principles in the adoption of any tax policy.

“The political dialogue this year, as in years past, has been too focused on purported benefits of tax exemptions without a demonstration of their effectiveness, and without attention to what is lost when revenues aren’t adequate,” said Charles Bruner, executive director of the Child & Family Policy Center (CFPC) in Des Moines. “Our review demonstrates that we already face big challenges in serving our elderly population, and that we simply can’t afford new tax breaks for the wealthiest retirees.”

In a new report for the Iowa Fiscal Partnership (IFP), Bruner and CFPC colleague Mike Crawford examine how Iowa’s current personal income tax system affects six different types of tax filers, from retired and working families, with and without children.

“What we see is that Iowa already gives substantial tax preferences to Social Security and pension income, and that it doesn’t perform well in assuring that taxpayers with similar ability to pay are treated equitably,” Crawford said. “Iowa’s system also doesn’t offer much recognition of the cost of raising a family. We should have a tax system that more resembles the federal system in this respect and provides better benefits to working families with children.”

As an example, the authors noted that Iowa does not tax Social Security income for couples whose “provisional” income is at or below \$32,000. This “provisional” level of income is an adjustment reflecting the state’s exemption of half of all Social Security benefits from taxation. In other words, a couple making \$39,000, with \$14,000 of it from Social Security, is considered to have \$32,000 in income because half of the Social Security benefits aren’t counted. At that income level or below, the couple has the further benefit of having none of the benefits taxed.

“Given some of the political debate surrounding that issue, it might surprise many Iowans to learn they would not face any tax on their Social Security benefits. Eliminating the tax for those who do actually would benefit only higher-income retirees,” Bruner said. “As it is, those highest-income retirees still are exempt from paying tax on half the Social Security benefits they receive.”

Iowa also has a \$6,000 individual exemption (\$12,000 for couples) on pension income.

“These preferences come with a price tag,” Bruner said. “As those tax breaks stood in 1999, they cost the treasury about \$110 million, and are going to increase in cost as society ages and retirees have more retirement income.”

Likewise, the preferences mean Iowans with similar incomes don't necessarily pay the same in taxes. As examples:

■ A working couple who made \$35,000 in 2004 would pay \$1,485 in Iowa state income tax; a retired couple at that income, nothing.

■ A working individual who made \$35,000 in 2004 would pay \$1,503; a retired individual at that income, \$356.

■ A working couple who made \$55,000 in 2004 would pay \$2,870; a retired couple at that income, \$640.

■ A working individual who made \$55,000 in 2004 would pay \$2,622; a retired individual at that income, \$1,572.

Further calculations in the report show the treatment of families. State income tax liability for a working couple making \$55,000 and raising two children, for example, is 3 1/2 times that of a retired couple with the same income, and higher than it is for a retired couple making \$80,000.

Bruner said it was important to recognize – as demonstrated by a poll commissioned by the IFP in 2004 and supported by separate polls for the Des Moines Register and AARP – that Iowans believed recent tax breaks have benefited wealthy individuals and multi-state corporations, and that they would favor specified tax increases to raise revenue for services. A report about that poll, and other reports on budget issues, is available at the IFP website, www.iowafiscal.org <<http://www.iowafiscal.org>>.

“The Iowa income tax system needs to be reformed, but not through additional cuts and exemptions. It needs to be made fairer and simpler, and it needs to be capable of continuing to provide needed revenue, over time,” the authors stated.

The Iowa Fiscal Partnership is a joint effort of two nonprofit, nonpartisan organizations, the CFPC and the Iowa Policy Project in Mount Vernon.

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