

Class Warfare Fact and Fiction

Myth 1: The rich deserve most of the tax cuts because they pay most of the taxes



By Bernard Wasow

Nothing written here is to be construed as necessarily reflecting the views of The Century Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

The class-warfare pitch: "About 19.5 million tax-return filers in 2000 had adjusted gross incomes of \$75,000 or more and earned 63% of total U.S. taxable personal income. Even though these taxpayers accounted for just 15% of all tax returns, they paid 75% of total federal income taxes... The class-warfare warriors further fail to mention that fewer than 240,000 households making \$1 million or more pay almost one-quarter of all federal income tax."

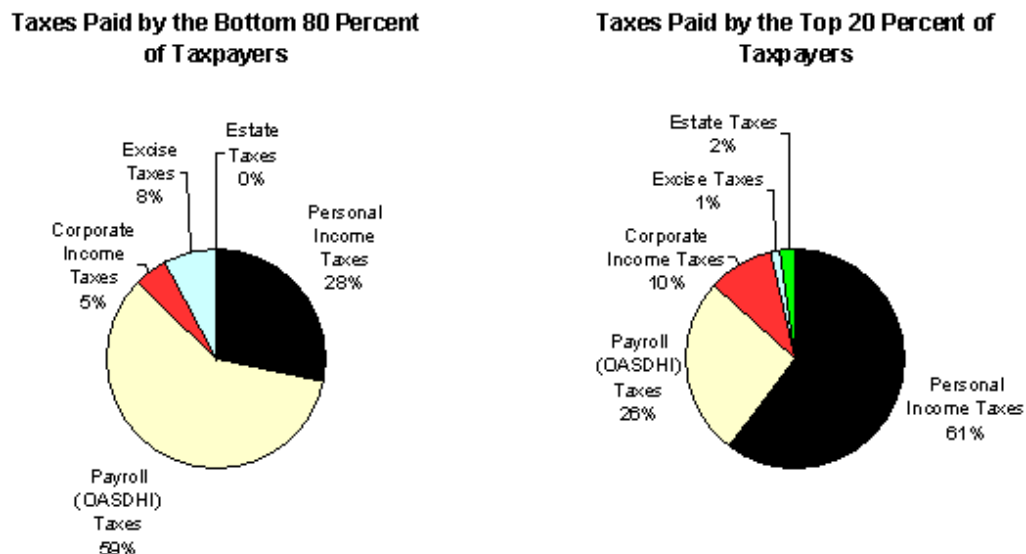
---William P. Kucewitz, National Review Online, January 10, 2003

Comparing how much different households pay in taxes by focusing only on the federal income tax is like contrasting how much food people consume by counting only their breakfasts. To see who pays what in federal taxes, we need to look at the entire tax system—not one component in isolation.

In our federal system, households pay taxes to the federal government, state governments, and local governments. As we broaden the consideration of the taxes a family must pay from the federal income tax to include the rest of the federal tax system plus state and local taxes, the burden is shifted more and more to families in the middle and bottom of the income distribution.

The federal tax system is composed of several main elements: the personal income tax, the payroll tax (which finances Social Security and Medicare coverage), the corporate income tax, various excise taxes—notably on gasoline, alcohol, and tobacco—and the estate tax. For most households, the payroll tax takes a bigger bite out of their income than any other federal tax.

Figure 1. The Income Tax and Other Federal Taxes for the Top 20 Percent and Bottom 80 Percent of Taxpayers



Source: Data provided by Citizens for Tax Justice, Washington, D.C.

As the figures makes clear:

- For the bottom 80 percent of taxpayers, excise taxes and especially Social Security and Medicare taxes and are quite important, with income taxes taking up much less of the federal tax burden.
- For the top 20 percent, in contrast, income taxes constitute the great bulk of their federal tax burden, both as personal taxes and as taxes on corporate income that they own through shares.

Comparing who gets income and who pays federal taxes:¹

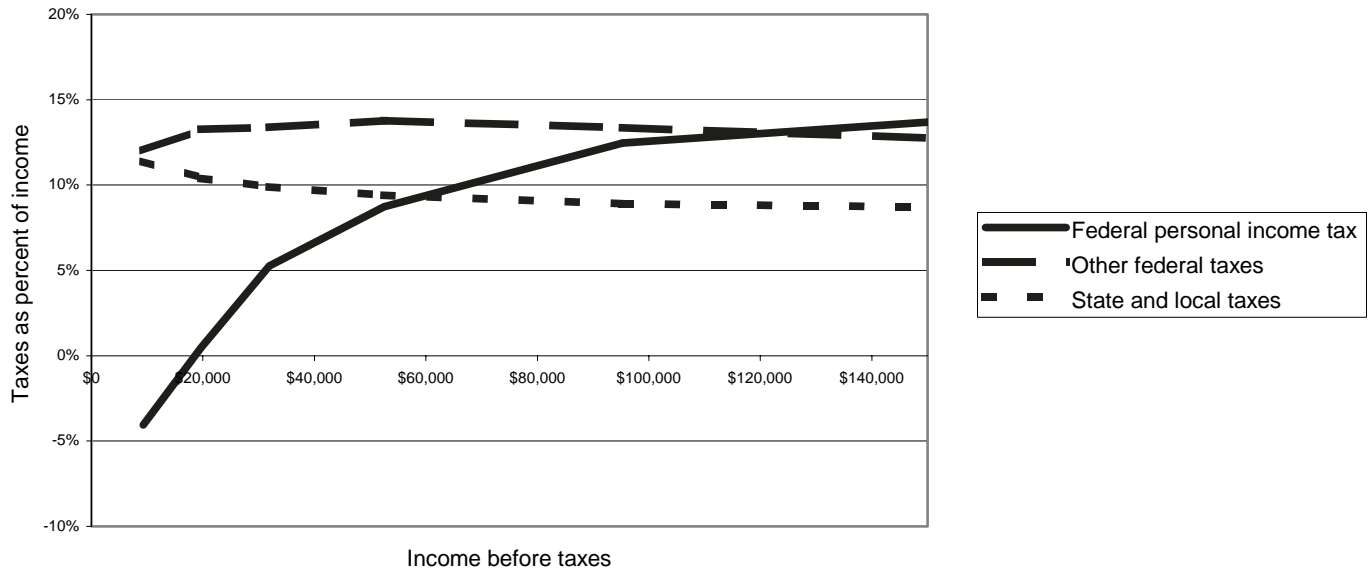
- Those who earn less than \$50,000 receive 25 percent of all income and pay 17 percent of federal taxes.
- Those who earn \$50,000 to \$150,000 receive 45 percent of income and pay 44 percent of federal taxes.
- Those who earn more than \$150,000 receive 30 percent of income and pay 39 percent of taxes.

If the federal tax system is only modestly progressive, the state and local tax system, which depends much less on income taxes and more on sales and excise taxes, is substantially regressive. The property tax, too, is regressive, especially at the very top of the income distribution, where the family home is a much smaller part of total wealth than for the middle

¹ *Effective Federal Tax Rates 1979-1997*, Congressional Budget Office, Washington, D.C., 2001, available at <http://www.cbo.gov/showdoc.cfm?index=3089&sequence=0>. Data reported in the bullet points are for 1997, last year available in the study.

class. Figure 2 shows tax rates for the federal personal income tax, other federal taxes, and state and local taxes.²

Figure 2. Tax Rates at Various Income Levels



Sources: Federal tax data provided by Citizens for Tax Justice, Washington, D.C. State and local tax data from Who Pays? A Distributional Analysis of the Tax Systems in All 50 States, Institute on Taxation and Economic Policy, Washington, D.C., January 2003, available at <http://www.ctj.org/itep/whopays.htm>. The federal and state and local numbers are nearly, but not entirely, comparable because the state and local numbers are for the nonelderly only and apply to taxes levied by a jurisdiction on its own residents. The grand total tax burden should include taxes paid in one state by residents of another state, for example sales taxes paid by domestic tourists.

Figure 2 shows that

- The federal income tax is quite progressive, collecting a smaller share of the income of the middle class than of the rich. For the working poor, the income tax even delivers net refunds, through the Earned Income Tax Credit.
- The remainder of the federal tax system is not progressive, becoming regressive for incomes above about \$20,000 per year.
- Average state and local taxes are steadily regressive, with the tax burden declining uniformly with income.

Overall, our tax system is far less progressive than the federal income tax viewed in isolation. The share of the total tax burden carried by high-income families is much smaller than their share of income taxes alone. By focusing on income tax cuts, and on cuts at the top, at that, advocates of the proposed tax cuts conveniently ignore the taxes that actually burden the majority of taxpayers.

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² State and local taxes obviously differ from place to place. Figure 2 shows the national average.