

# How Progressive is the U.S. (Federal) Tax System?

Data is for 1999 or 2002 depending on the series

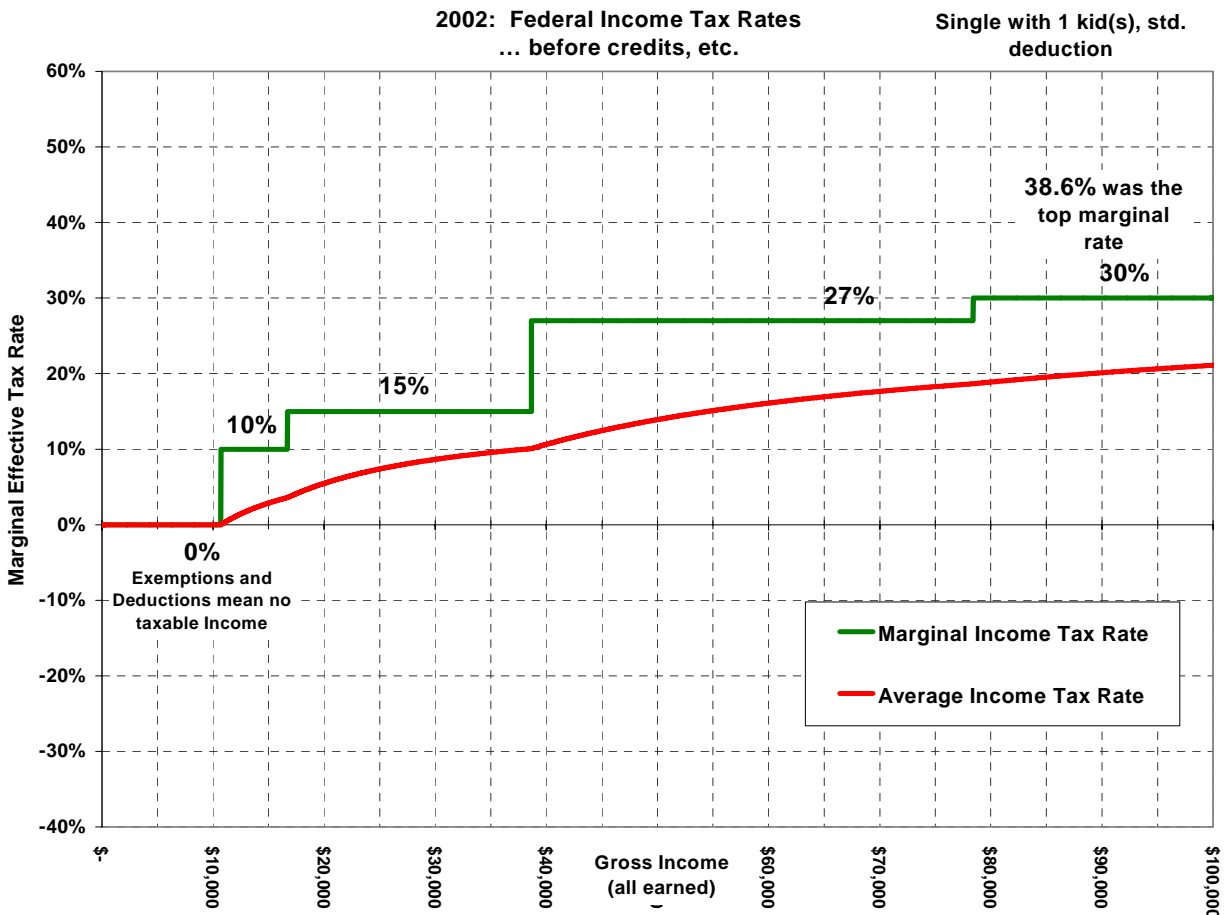
## First, some Definitions

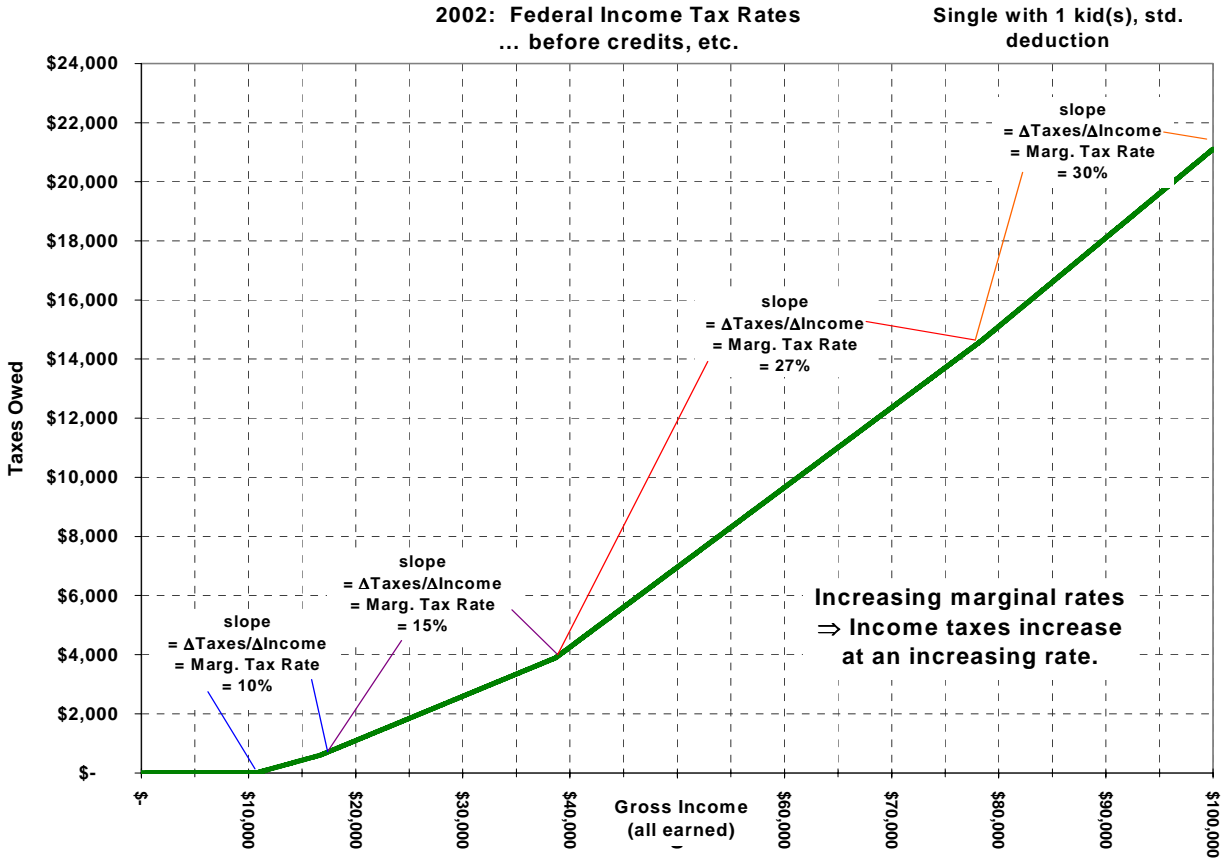
Regressive Tax System: \_\_\_\_\_

Proportional Tax System: \_\_\_\_\_

Progressive Tax System: \_\_\_\_\_

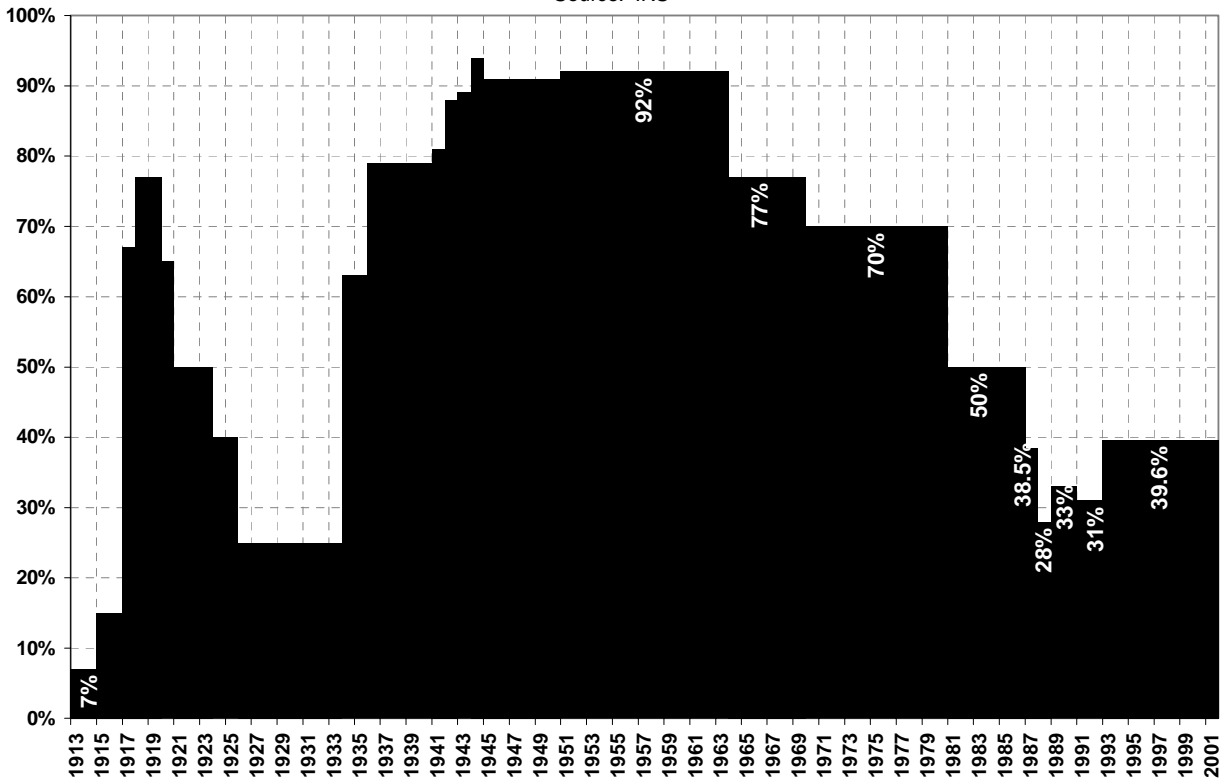
## A 1<sup>st</sup> Look: Increasing Marginal Rates ⇒ Progressivity





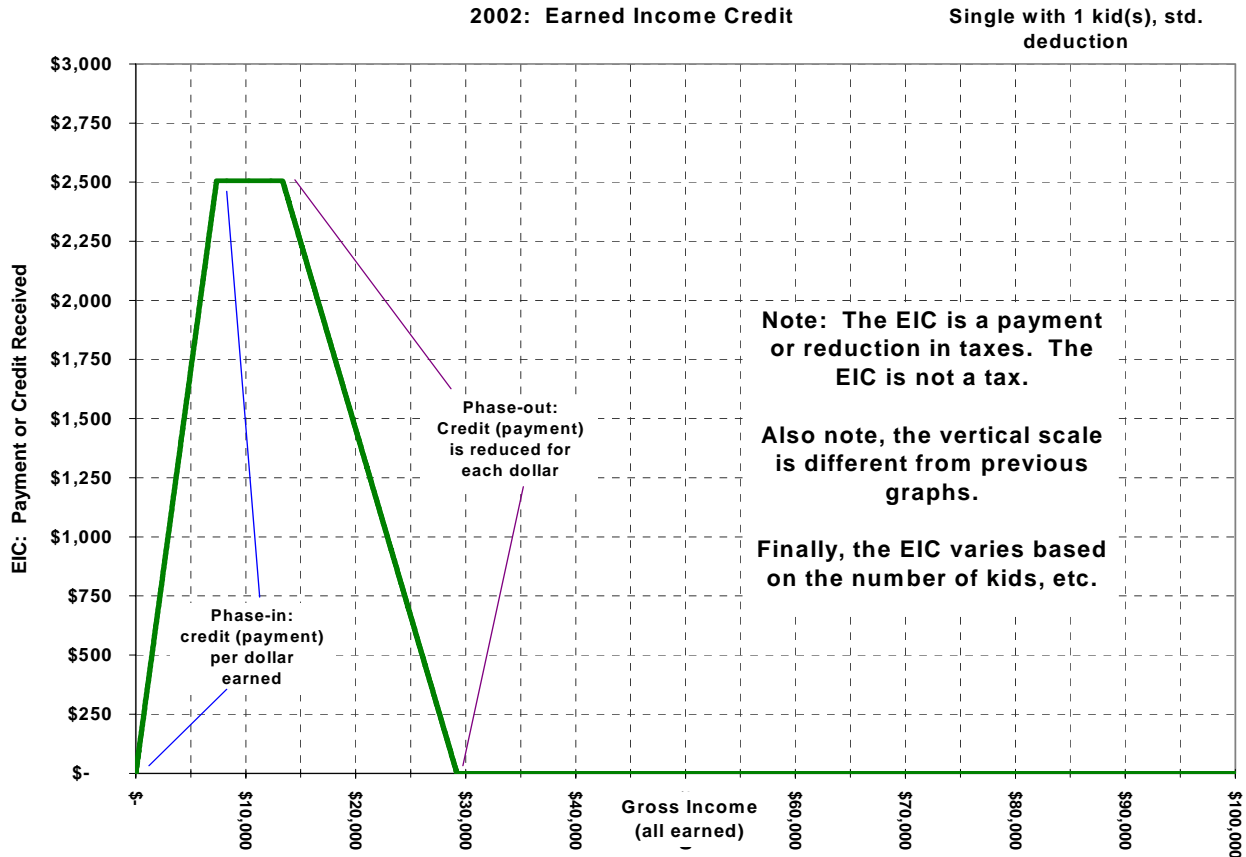
**Top Marginal U.S. Income Tax Rate**

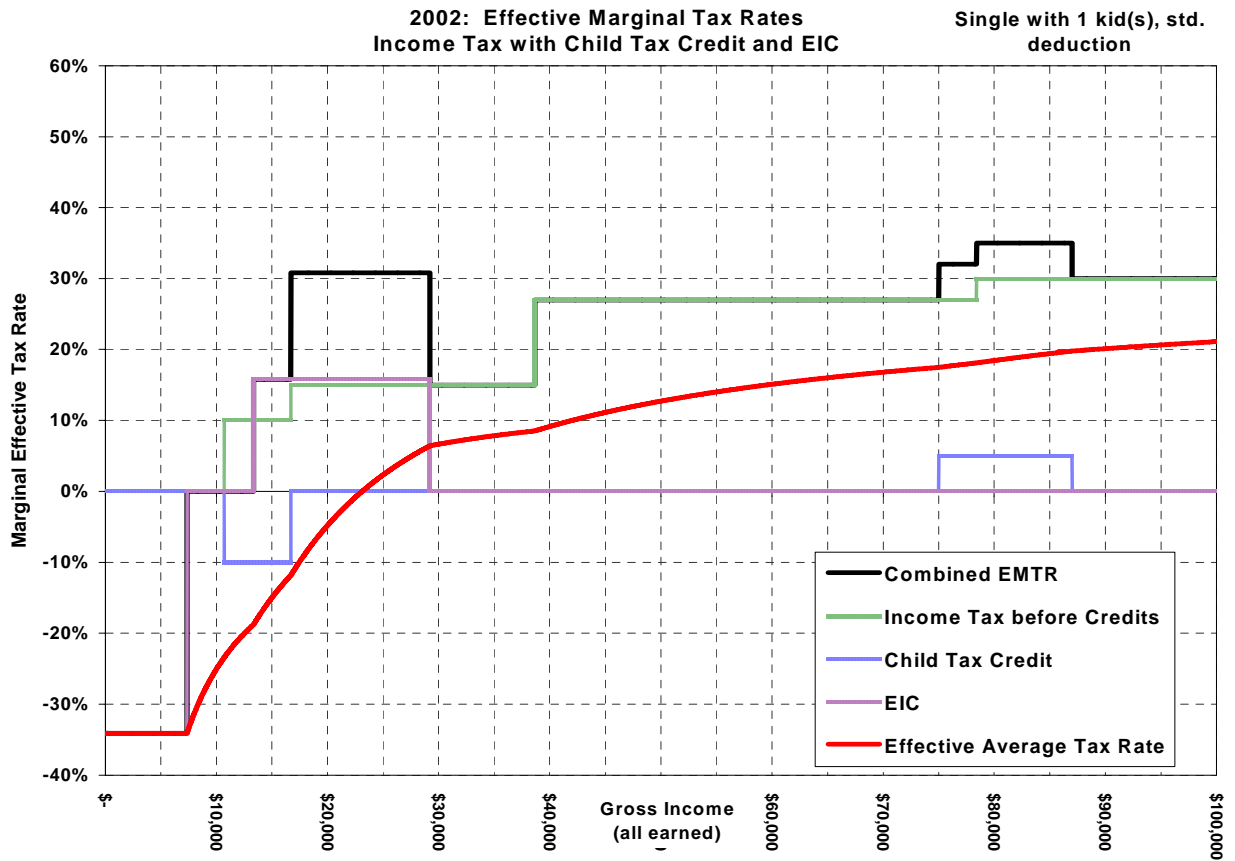
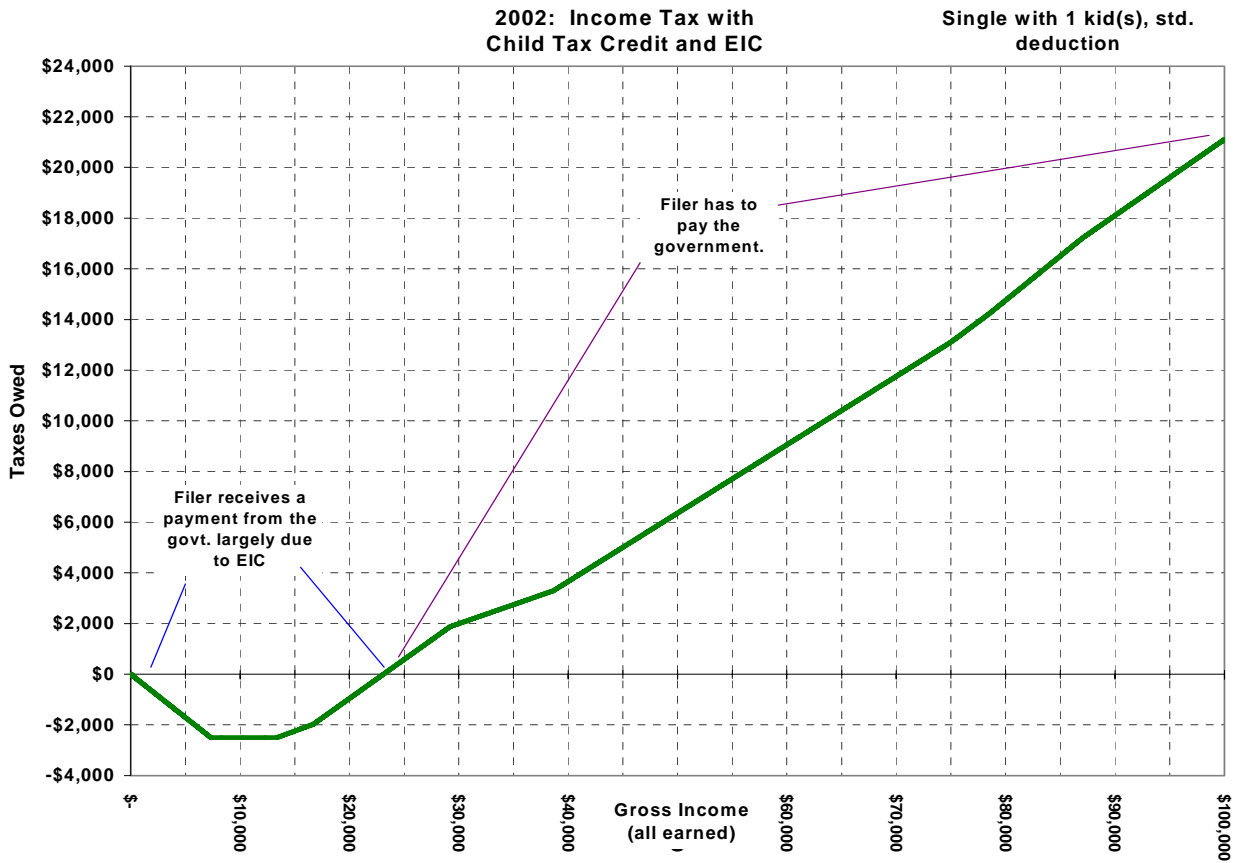
Source: IRS



**But Wait, There's More!**

- **Earned Income Credit:** Subsidy (payment) to taxpayers for working. The government gives a taxpayer a payment (\$0.07 to \$0.40) for every dollar they earn up to a certain level of income. This credit is phased-out (taken away) at high income levels.
- **Child Tax Credit:** Up to \$600 (raised to \$1,000 in 2003) reduction in taxes for each child. In 2002, this could not result in a payment to families, only a reduction in taxes. Ex., if one otherwise owed \$0 in income taxes, one got \$0 child credit. If one otherwise owed \$400 in taxes, one got a \$400 credit. If one otherwise owed \$600 or more one got the \$600 maximum credit. Phased out at high income levels.

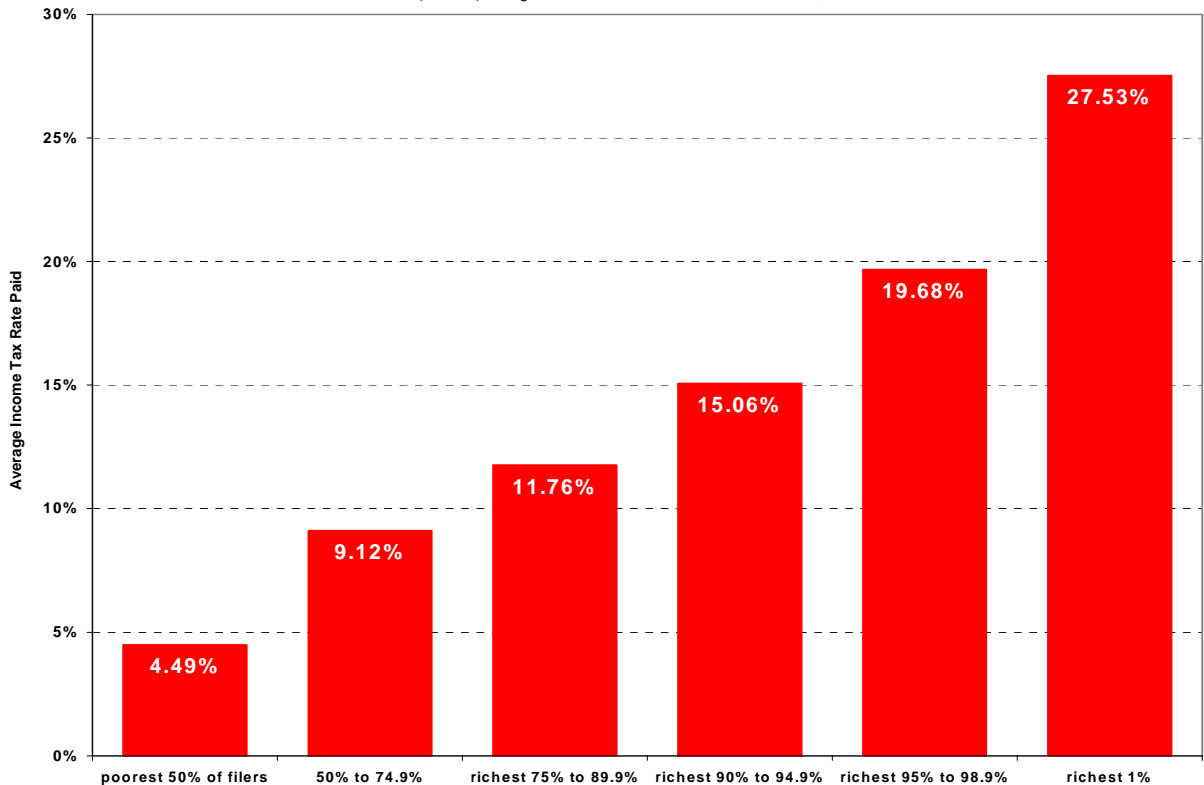




### What’s the point(s) ... so far?

- **Increasing Marginal Tax Rates:** The basis of our federal income tax system is a series of increasing marginal tax rates.
- **Progressive System:** The system is basically progressive. Higher income earners typically pay a higher average tax rate. Progressive, like elastic, is not just black and white, however. It is also a question of degree. The basis of our tax system is progressive. This still leaves us with the question of; “Should we make it more progressive, less progressive, or keep it the same?”.
- **“Across the board” cuts in income tax rates result in most of the \$ value of the cuts going to the rich:** Why? The rich are paying most of the income tax. Check out the charts and table below and on the next page. Half of all income tax payers could have their income tax reduced to zero and it would only be a 4% tax cut overall!

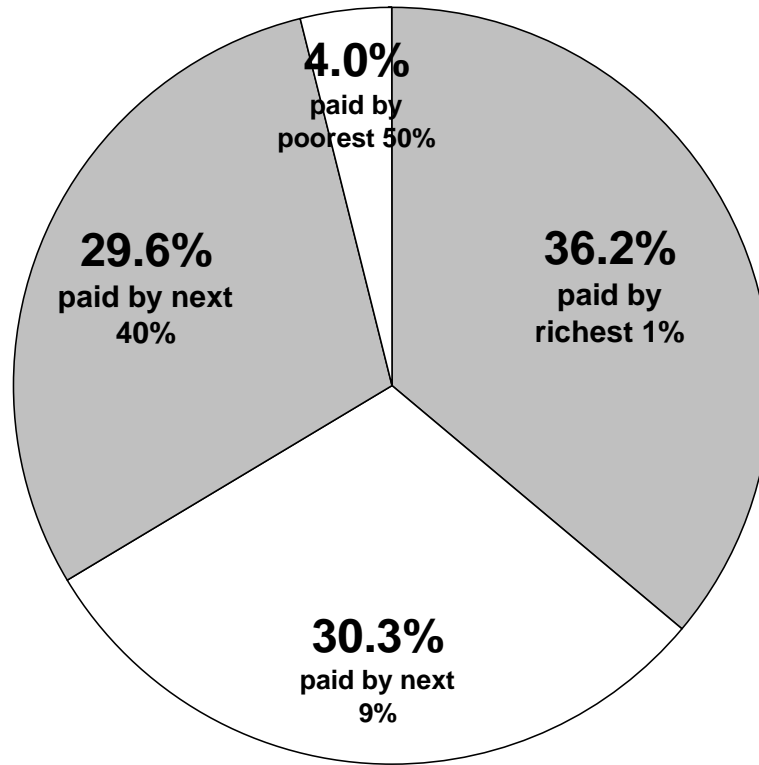
**Average Income Tax Rate Actually Paid: 1999**  
 Source: (House) Congressional Joint Economic Committee, 2002



<sup>1</sup> Adjusted Gross Income; basically one’s income before taxes.

Share of U.S. Federal Income Tax by Group: 1999

share of all income tax filers



Group	max AGI <sup>(1)</sup>	Avg. AGI	Avg. Tax	Avg. Rate	% of all income taxes
richest 1%	lots!	\$ 914,871	\$ 251,901	27.53%	36.18%
richest 95% to 98.9%	\$ 293,416	\$ 170,413	\$ 33,538	19.68%	19.27%
richest 90% to 94.9%	\$ 120,847	\$ 101,750	\$ 15,322	15.06%	11.00%
richest 75% to 89.9%	\$ 87,683	\$ 67,428	\$ 7,930	11.76%	17.09%
50% to 74.9%	\$ 52,966	\$ 38,056	\$ 3,469	9.12%	12.46%
poorest 50% of filers	\$ 26,416	\$ 12,430	\$ 558	4.49%	4.00%

- **It's more than the commonly reported marginal tax rates:** Anyone trying to judge the tax system based solely on the 10%, 15%, rates and their cutoffs is leaving out some very important details.
- **Complex System:** Hey! It's actually a lot more complex than all this. Individually, however, each of the additions to the base system, the EIC for example, makes sense to most people. When added together, they result in a very complex system.

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## But Wait, There's Even More!

- **There's lot more to the federal income tax system.** Examples include; Itemized deductions (ex. mortgage interest, health care spending), different taxation of capital gains, etc. Some make the system less progressive. Some make it more progressive.<sup>2</sup>
- **Income Taxes are not the only federal taxes.** FICA taxes, levied on payroll income (ex. wages and salaries) are collected to pay for Social Security and Medicare.<sup>3</sup> These taxes are pretty significant. Employers pay 7.65% of (most earnings) and employees pay the same. That's 15.3% total (remember, the statutory incidence has nothing to do with the economic incidence). Further, FICA taxes are not progressive. They are proportional up to about \$87,000, and then regressive thereafter. Further, "non-payroll" income, dividend income for example, is not subject to the FICA tax. The rich are more likely to earn non-payroll income. Corporate profit taxes, albeit only accounting for about 11% of federal revenues, are likely progressive.
- **State and local taxes further cloud the picture.** When will it end? Sales taxes tend to be regressive (the poor spend a higher percent of their income). Property taxes tend to be roughly proportional, and state and local income taxes tend to be mildly progressive.
- **Taxes are only one side of the picture.** Please make it stop! There are also benefit programs. Transfer programs such as Food Stamps, TANF (Temporary Assistance to Needy Families), WIC (Women with Infant Children), etc., if considered part of "the system", make it more progressive. Social Security and Medicaid payments, financed by FICA taxes, also make "the system" more progressive.

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<sup>2</sup> Please note that the diagrams do not represent every taxpayer. They are drawn for someone with one dependent and "single" as their filing status. Why, by the way, did I not choose "head of household"? 1) "single" allowed me to assume away a few more things. Further, the difference between single and "head of household" rates do not change the basic picture presented by the graphs.

<sup>3</sup> FICA stands for "Federal Insurance Contribution Act". Social Security and Medicare are considered "social insurance".

