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Better Understanding ‘The 47 Percent’

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The current political environment has set off a firestorm of confusion about who does and who does not pay taxes in America — and unfair criticism of many working families and others.

It's true that 47 percent of Americans pay no *federal income taxes*, but they do pay taxes.

In fact, almost two-thirds of the 47 percent are low-income, working households who are paying payroll taxes to help finance Social Security and Medicare, and many pay federal excise taxes on things like gasoline, alcohol and cigarettes.¹ These households are also paying a large percentage of their income in state and local sales and property taxes.

Many working Americans are exempt from the income tax because of features Congress added to the tax code — with overwhelming bipartisan support, in an effort to enable people to care for themselves and their children while encouraging them to work.

Some of these features include the Earned Income Tax Credit (EITC), a Ronald Reagan era anti-poverty program that enables low-wage working families with children to meet their basic needs while promoting employment. (See the Iowa Fiscal Partnership website for resources about the impact of the EITC in Iowa.²) In addition, the child tax credit gives families a tax credit through the form of a refund check even when they don't owe federal income taxes.³

The other one-third of the 47 percent — those households that aren't paying either major federal tax — includes those who are unemployed, low-income senior citizens who paid taxes during their working years and aren't currently taxed on Social Security benefits, students, those who have disabilities or can't work due to serious injury and people who don't meet the income tax obligation because their wages aren't high enough.

A household paying no federal personal income tax still pays about the same percentage of income to taxes as those who pay income taxes.⁴ In fact, 82 percent of working households pay more in payroll taxes than in income taxes, and low- and moderate-income earners pay a much larger share of their incomes in payroll taxes than high-income earners do. In 2007, the bottom 20 percent paid more than five times the percentage in payroll taxes than the top 1 percent of the income distribution. Higher-income earners generate much larger shares of their incomes from capital gains and dividends, which are not subject to Social Security payroll taxes and have earnings far above the \$110,000 per year subject to the Social Security portion of the payroll tax.⁵

Often missed in the focus on those who are not currently paying income taxes is the errant assumption that all those people have never paid taxes and never will. Just because a household

doesn't owe income tax one year, doesn't mean they won't pay income taxes over their lifetime. For many, a career change, the loss of a job, a disability or injury, or low wages can lead to incomes too low to pay taxes. A study by the U.S. Census Bureau⁶ found that almost 20 percent of households experienced a bout of poverty over a two-year period, but only 4.8 percent of households were in poverty the entire time. Of the households in poverty, 75 percent were in poverty for one year or less.

Iowa households not paying federal income tax still pay a large percentage of their incomes in state and local taxes. As the Iowa Policy Project reported in 2009, using information from the Institute on Taxation and Economic Policy (ITEP)⁷, moderate- and low-income Iowans pay more of their income in state and local taxes than the rich do — with the poorest households paying 11 percent, middle-income households paying over 9 percent, and the top 1 percent only paying 6 percent of their income.⁸ Iowa's regressive tax system takes a larger share of the incomes of those who have the least, and a smaller share from those who have the ability to pay a larger percentage of their income. Make no mistake: Working Iowans are paying taxes.

The ITEP report, "Who Pays? A Distributional Analysis of the Tax Systems in All 50 States"⁹, shows the problem with a regressive tax system.

Iowa families earning less than \$20,000

- Sales & Excise Taxes – 6.5%
 - Property Taxes – 3.7%
 - Income Taxes – 0.7%
- Total after federal deduction offset – 11.0%

Middle-income households earning between \$37,000 and \$56,000

- Sales & Excise Taxes – 4.5%
 - Property Taxes – 3.7%
 - Income Taxes – 3.1%
- Total after federal deduction offset – 9.6%

Those in the top 1 percent – who earn an average income of \$989,200

- Sales & Excise Taxes – 0.9%
 - Property Taxes – 1.7%
 - Income Taxes – 4.8%
- Total after federal deduction offset – 6.0%

¹ <http://www.taxpolicycenter.org/publications/url.cfm?ID=901527>

² <http://www.iowafiscal.org/EITC.html>

³ <http://www.iowapolicyproject.org/2012docs/120329-IFP-EITC4.pdf>

⁴ <http://www.itepnet.org/whopays3.pdf>

⁵ <http://www.cbpp.org/cms/index.cfm?fa=view&id=3505>

⁶ <http://www.census.gov/sipp/p70-55.pdf>

⁷ <http://www.iowapolicyproject.org/2009docs/091118-WhoPays-release.pdf>

⁸ <http://www.itepnet.org/whopays3.pdf>

⁹ <http://www.itepnet.org/whopays3.pdf>