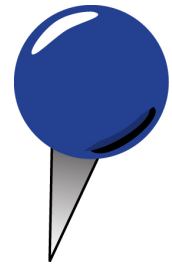




Iowa Policy Project

A Roadmap for Opportunity



What real Iowa tax reform would look like

Iowa is an average-tax state. Even before expensive tax cuts passed in 2018 to benefit the wealthiest, Iowans paid about 2.5 percent of their income toward income taxes, 2.3 percent for sales taxes, which earns us a rank of 20th and 25th, respectively, among the 50 states.¹ Business taxes are right in the middle as well, according to recent studies by two accounting firms.²

Destination:

A tax system that raises revenue fairly and adequately to meet critical public service needs that benefit all Iowans.

But our tax system already failed the fairness test before those new tax cuts. The highest income Iowans pay a smaller share of their income to state and local taxes than lower and middle-income Iowans — our tax system is regressive.³ And hundreds of millions in tax revenue are lost every year to corporate loopholes and to business tax credits that produce little or no benefit to the state. At the same time, the state struggles every year to adequately fund education, public safety, health care and other priorities.

Real tax reform, given that context, would mean three things: (1) ensuring adequate revenue, (2) reducing the regressivity of our tax system, and (3) reining in corporate tax credits and loopholes.

Recent tax bill fails the test

The legislation signed into law in May of this year does none of these things. It cuts revenue, makes the tax system more regressive by concentrating tax cuts on the rich, and fails to reform credits or loopholes.⁴ The package had one true benefit: modernizing the sales tax to include online purchases and level the playing field for local and state-based businesses.

Little for the middle class: Tax bill benefits the wealthiest

Average tax cuts, percent of total cuts, by income, Iowa residents, 2021

Adjusted Gross Income	Percent of Taxpayers	Average Tax Cut	Percent Reduction	Percent of Total Tax Cut	Tax Cut: Percent of Income
Under \$30,000	39.6%	\$ (21)	-17.2%	2.8%	-0.23%
\$30,000 to \$60,000	25.5%	\$ (121)	-8.4%	10.3%	-0.28%
\$60,000 to \$100,000	17.1%	\$ (232)	-7.5%	13.2%	-0.30%
\$100,000 to \$250,000	15.4%	\$ (534)	-8.2%	27.3%	-0.38%
\$250,000 to \$1 million	2.3%	\$ (4,014)	-17.5%	30.4%	-1.00%
\$1 million or more	0.2%	\$ (24,636)	-19.4%	16.1%	-1.01%
Total	100%	\$ (300)	-11.1%	100.0%	-0.48%

Source: Iowa Department of Revenue, Memo to Legislative Services Agency, May 2, 2018, Table 9A

Under this legislation, however, the income tax savings to a middle-class family by 2021 amount to just \$5 to \$10 a week and much of that will be taken back by the sales-tax increase. Millionaires, on the other hand, will see on average a \$24,636 cut for the year. Almost half of the tax cuts will go to the richest 2.5 percent of Iowa taxpayers, those making \$250,000 or more.

The 2018 tax bill also piles \$40 million in corporate tax cuts on top of commercial property tax cuts enacted several years ago that have cost local governments millions of dollars. A new special tax break for business owners who receive “pass-through” income will cost in excess of \$65 million a year, with 60 percent of the benefit going to the top 2 percent of taxpayers.

Overall, the bill will take \$300 to \$400 million a year out of the budget that could have gone to adequately fund education or public safety or mental health care. Those revenue cuts will happen regardless of the state of the Iowa economy or the budget; no safeguards will prevent it, despite the bill’s much touted “triggers.”⁵

To add insult to injury, the tax bill is far more likely to hurt the Iowa economy than to help it. The tax cutting experiment in Kansas was a failure, harming the state economy rather than helping it.⁶ And Iowa’s own experience with massive tax cutting, in the late 1990s, not only failed to stimulate growth, but likely contributed to the subsequent slowing of the state’s economy.⁷

Policy Alternatives: Real reform is needed more than ever

True reform would **ensure adequate funding for our schools**, which have been underfunded for years, revenue failing to keep pace with costs. It would end the cuts to state funding of Iowa’s public universities and community colleges, which have been forced to raise tuition, leaving students and families with rising debt.

True reform would **plug corporate tax loopholes** that cost Iowa a conservatively estimated \$100 million a year. It would rein in business tax credits that have grown from \$200 million to \$423 million over the past six years.⁸

And true reform would **make our tax system fairer**, and better based on ability to pay. This should be done by providing enhanced recognition of the cost of raising a family by expanding the child tax credit and the child and dependent care credit. It should include eliminating federal deductibility while reducing selected income-tax rates, but not reducing revenues, a key reform abandoned in the final version of the 2018 bill.⁹ This rebalancing of elements of the tax code would reduce its current regressive nature, which imposes higher taxes as a share of income on lower- and middle-income Iowans than on the wealthy.

¹ Taxes as a percent of state personal income for the most recent five years available, 2011-2015, from the U.S. Census, Census of Government Finances.

² “Myth-Buster: Competitiveness no problem for Iowa taxes.” Iowa Fiscal Partnership, March 15, 2018. <http://www.iowafiscal.org/wp/wp-content/uploads/2018/03/180319-IFP-myth1-bgd.pdf>

³ “Cementing Inequity: Richest Iowans Pay Lower Tax Rate.” Iowa Fiscal Partnership, January 14, 2015. <http://www.iowafiscal.org/cementing-inequity-richest-iowans-pay-lower-tax-rate/>

⁴ See Charles Bruner and Peter Fisher, “Tax plan facts vs. spin.” Iowa Fiscal Partnership, May 5, 2018. <http://www.iowafiscal.org/tax-plan-facts-vs-spin/>

⁵ All the triggers would do is save us from an even larger budget disaster in 2023 and beyond. The triggers are revenue targets; if the targets are not achieved, the last round of cuts will not take place as scheduled for tax year 2023.

⁶ Michael Mazerov. “Kansas Provides Compelling Evidence of Failure of ‘Supply-Side’ Tax Cuts.” Center on Budget and Policy Priorities, January 22, 2018. <https://www.cbpp.org/research/state-budget-and-tax/kansas-provides-compelling-evidence-of-failure-of-supply-side-tax-cuts>

⁷ Peter Fisher. “Tax cuts: Already tried, failed.” Iowa Policy Points, April 23, 2018. <https://iowapolicypoints.org/2018/04/23/tax-cuts-already-tried-failed/>

⁸ “Growing cost, lax oversight of Iowa business tax credits.” Iowa Fiscal Partnership, March 16, 2018. <http://www.iowafiscal.org/wp/wp-content/uploads/2018/03/180319-IFP-taxcredit-bgd.pdf>

⁹ The bill eliminates federal deductibility, and adopts the federal child tax credit, only in 2023 and then only if revenue targets are met, targets that are unlikely to be achieved.