



Income Tax Measure Costly, Increases Inequities

A “Simpsons” cartoon by Nick Anderson is applicable to a marquee piece of tax legislation moving in the Iowa House. Homer Simpson is holding two bills, exclaiming, “Woo, hoo!” about his tax cut. His boss, Mr. Burns, is observing from his place among sacks of money: “Sucker ...”

House File 194 provides a 20 percent cut in Iowa’s individual income tax rates. The issue is not just that the state of Iowa, recovering from a recession and major cuts to education and other public services, cannot afford such a tax cut and sustain essential public services — though that issue is very real. The Fiscal Note for HF194 puts the cost at \$330 million for FY2012, \$704.1 million for FY2013, \$711.5 million for FY2014, and \$750.6 million in FY2015. This comes when Iowans are told revenues are low.



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the Washington Post Writers Group and the Cartoonist Group.*

The problem also is that such a tax cut is very much misdirected, taking Iowa tax policy further down the path of helping the wealthiest the most — a trend building since the mid-1990s, starting with a 10 percent cut in income tax rates in 1997. Since then, Iowa lawmakers have passed more income-tax cuts, avoided equitable income-tax reform, and raised and encouraged local governments to raise sales and property taxes, which take a greater share of income of low-income and middle-income taxpayers than of high-income taxpayers.

HF194 provides yet another windfall primarily for the wealthiest. According to an analysis by the Institute on Taxation and Economic Policy, the effect of the tax cut will average \$18 for taxpayers in the lowest quintile of Iowa taxpayers (with incomes below \$21,000) and \$6,822 for taxpayers in the top 1 percent of Iowa taxpayers (with incomes of 358,000 or more (See Table 1).

The Iowa Policy Project

20 E. Market Street
Iowa City, IA 52245
(319) 338-0773 • www.iowapolicyproject.org

CHILD & FAMILY POLICY CENTER

505 5th Avenue • Suite 404
Des Moines, IA 50309
(515) 280-9027 • www.cfpciowa.org

While the bottom one-fifth of Iowa taxpayers see their overall taxes (sales, property and income combined) reduced by about 1.6 percent, the top 1 percent see their overall tax burden reduced by about 9.3 percent. Further, a disproportionate share of those in the top 1 percent of income are out-of-state tax filers who made profits in Iowa and they (or their home states) would be big beneficiaries of such cuts.

Moreover, such a cut does nothing to reduce any of the current inequities in Iowa's tax code as they relate to working families with children, who are the most heavily taxed of all Iowans relative to their discretionary income. While a family of four making \$40,000 owes no federal income tax, that family owes more than \$1,200 in Iowa income taxes. At the same time, a retired couple with no children and \$40,000 in Social Security and pension income owes no state income tax.

Table 1. Wealthy Benefit Most From 20 Percent Income Tax Rate Cut
Effects of HF194 By Income Quintile — 2010 Income

Income Group	Income Range	Avg Tax Change
Top 1%	Over \$358,000	- \$ 6,822
Next 4%	\$147,000 to \$358,000	- \$ 1,247
Next 15%	\$86,000 to \$147,000	- \$ 690
Fourth 20%	\$57,000 to \$86,000	- \$ 410
Middle 20%	\$38,000 to \$57,000	- \$ 239
Second 20%	\$21,000 to \$38,000	- \$ 123
Lowest 20%	Under \$21,000	- \$ 18

Source: Institute on Taxation and Economic Policy

In fact, as noted by the official Fiscal Note on HF194, a reduction in income tax would mean a reduction for many school districts, which count on income surtaxes for portions of their budgets. This could force another tax shift to property taxes, because school districts fund their Physical Plant and Equipment and Instructional Support programs through a combination of property tax and local income surtax. Districts would be able to make up for lost income surtax with a greater share of those programs being funded through property tax. The surtax is used by 85 percent of Iowa's 359 school districts.

Alternatives

Doubling the state Earned Income Tax Credit (from 7 percent to 14 percent of the federal EITC) would provide much greater benefit to 70,000 working low- and moderate-income families with children than the cuts in rates proposed in HF194 and would be a step to addressing a significant problem in Iowa's income tax law. It would cost the state less than one-twentieth the cost of the tax cut in HF194. It also could be coupled with more appropriate tax treatment of select capital gains and other tax exemptions to high-income families and cover its cost. Such alternatives are much more appropriate ways to provide for tax fairness to hard-working Iowa families.

Iowa Fiscal Partnership

The Iowa Fiscal Partnership is a joint budget and tax policy initiative of two nonpartisan, Iowa-based organizations, the Iowa Policy Project in Iowa City and the Child & Family Policy Center in Des Moines. Find IFP on the web at www.iowafiscal.org.