BACKGROUNDER

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Iowa Fiscal Partnership

Iowa's Taxes Remain Lower than Average

Iowans continue to pay less than the national average for state and local public services, according to the most recent information from the Census of Governments.

The best way to compare tax levels between states is to measure total taxes collected as a percent of personal income – the total income earned by the state's residents. On that measure, total state and local taxes in Iowa represented 10.4 percent of income. This is below the national average of 10.9 percent. Iowa ranked 26th among the 50 states (see Figure 1). Even when considering just state taxes (income and sales taxes are the major ones) or just local taxes (property taxes and local sales taxes) the conclusions are the same: Iowa tax levels are below average. If Iowa taxed at the same rate as the average state (10.9 percent of personal income) an additional $532 million would have been generated in FY2008.

Figure 1. Iowa Below Average on State and Local Taxes as a Percent of State Personal Income, FY2008

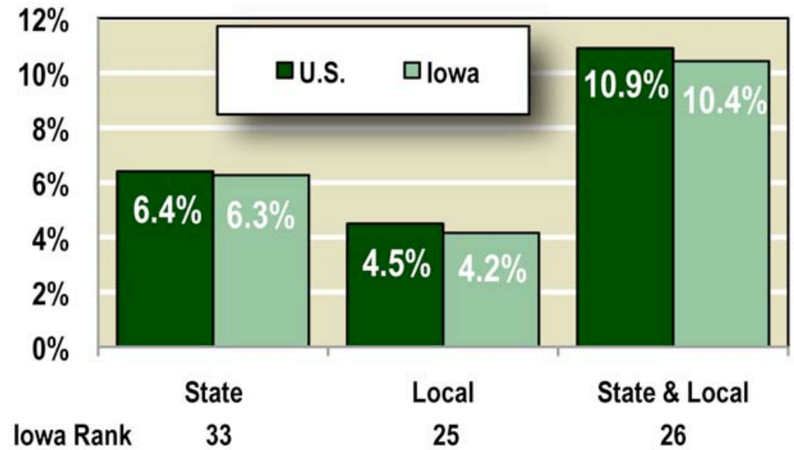
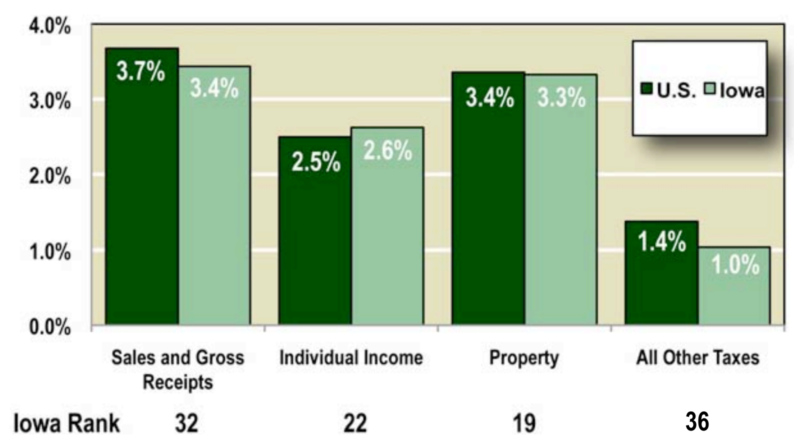


Figure 2. By Tax, Iowa in Middle on State and Local Taxes as a Percent of State Personal Income, FY2008



The largest revenue generators in Iowa are sales and gross receipts taxes, followed by property taxes and individual income taxes. In all three cases Iowa ranks in the middle third of the states, with tax levels either a little above or a little below the national average (Figure 2). It should be noted that "All Other Taxes" includes the Corporate Income Tax, where Iowa ranks very low (see *Iowa's Businesses Already are Taxed Lightly* at http://www.iowapolicyproject.org/2011docs/110209-IFP-biztaxes-bgd.pdf.)

It is common practice to compare Iowa with neighboring states, since those are most likely to compete

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with Iowa for residents and businesses. Table 1 shows overall tax levels in six of the neighboring states are higher, while in only two are they lower.

Table 1. Iowa State and Local Taxes Lower Than Most Neighboring States, Taxes as a Percent of State Personal Income, FY2008

	All Taxes	Sales and Gross Receipts	Individual Income	Property	All Other Taxes
Wisconsin	11.6%	3.2%	3.2%	4.2%	1.1%
Minnesota	11.1%	3.5%	3.5%	3.0%	1.2%
Kansas	10.9%	3.8%	2.7%	3.4%	1.1%
Nebraska	10.7%	3.5%	2.5%	3.5%	1.2%
Illinois	10.6%	3.5%	1.9%	3.9%	1.3%
Indiana	10.5%	3.9%	2.5%	3.2%	1.0%
Iowa	**10.4%**	**3.4%**	**2.6%**	**3.3%**	**1.0%**
Missouri	9.3%	3.4%	2.6%	2.6%	0.8%
South Dakota	8.1%	4.4%	0.0%	2.8%	0.9%

While the average state collected the same share of personal income in taxes in 2008 as it did in the early 1990s, Iowa's tax share has fallen since that time (Figure 3). From 1991 to 1995 state and local taxes represented 11.5 percent of Iowa state income; by 2008 the share had fallen to 10.4 percent. Over that period Iowa went from the 12th highest to the 26th highest tax level among the 50 states.

More recent data are available for state taxes alone. In fiscal year 2009, state taxes nationally and in Iowa were a smaller share of income than in the previous year, though the decline was less pronounced in Iowa, with the result that Iowa taxes were closer to the national average (Figure 4).[1] Iowa still ranked in the bottom half of the states, however.

Figure 3. Iowa State and Local Taxes Have Fallen, Share of Personal Income, FY1991-95 to FY2008

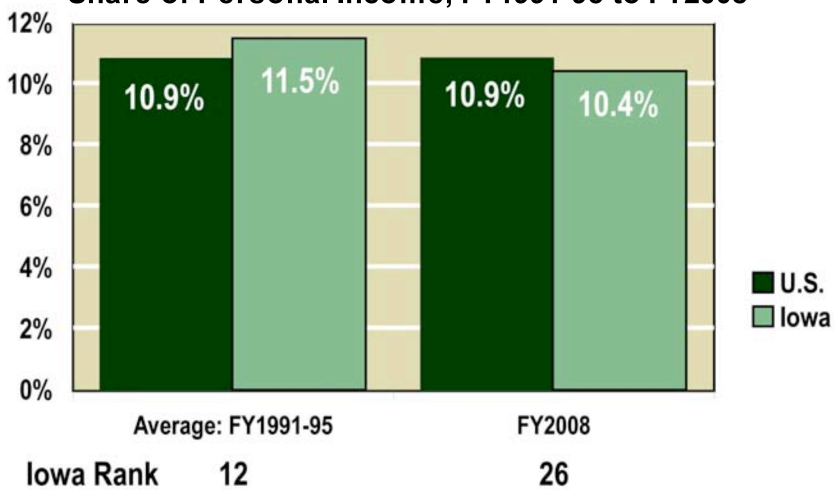
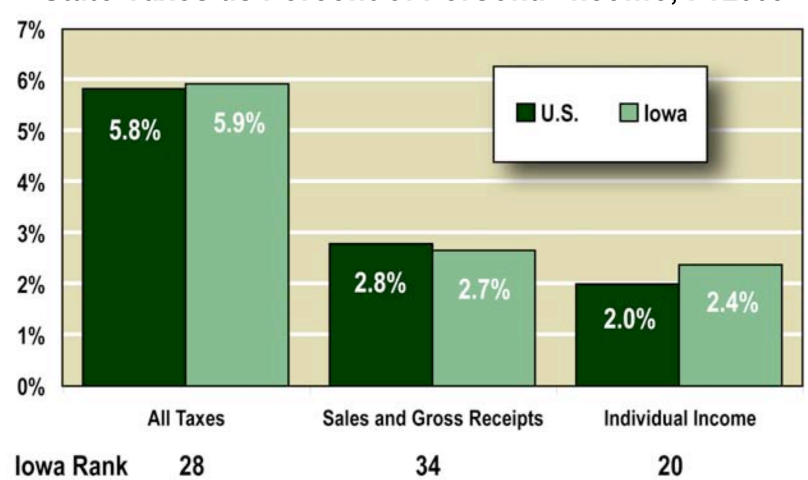


Figure 4. On State Taxes, Iowa is Competitive, State Taxes as Percent of Personal Income, FY2009



Data Sources and Methodology

For all figures and tables in this report except Figure 4, the source is an IPP analysis of data from the U.S. Census, Federal State and Local Governments, Annual State and Local Government Finances Statistics, at http://www.census.gov/govs/estimate/. Figure 4 is based on data from the U.S. Census, 2009 Annual Survey of State Government Tax Collections, released March 23, 2010, at http://www.census.gov/govs/statetax/ . Personal income is from the Regional Economic Information System, Bureau of Economic Analysis, U.S. Department of Commerce, at: http://www.bea.gov/regional/sqpi/default.cfm?selTable=SQ1 . Fiscal year personal income is the average of the four quarters of personal income that comprise the fiscal year.

For both 2008 and 2009, the census figures on state sales tax collections for Iowa have been adjusted to correct for the underreporting of sales tax revenues, as identified by Jeff Robinson of the Iowa Legislative Service Agency. An additional adjustment was made to state sales tax collections for Figure 4. When Iowa converted the SILO tax to a statewide tax, this had the effect of raising the state sales tax revenue by 20% because the census of governments categorized the new tax as a state tax, but the old SILO tax as a local tax. The change had no effect on total state-local tax revenue comparisons. The above figures adjust census of governments state sales tax receipts to remove the penny remitted to school districts so that state taxes reflect only taxes financing state government, and so that tax levels and rankings are comparable to previous years.

Our rankings differ from those produced by the Tax Foundation (TF), whose recent report shows Iowa ranked 34th in FY08 and 28th in FY09 in total state and local taxes paid by residents. There are several reasons for the different results. The TF attempts to estimate how much of the taxes collected in each state are actually paid by residents of other states, whereas our measure simply follows the more conventional approach used by many others, including the Federation of Tax Administrators, by dividing total Iowa tax collections by Iowa personal income. The TF, for example, estimates that in FY2008 Iowans paid $2,502 per capita to Iowa state and local governments, and another $1,117 in state and local taxes to other states. Thus fully 30 percent of the total state and local taxes per capita paid by Iowans according to the TF ($3,619) are actually taxes collected by other states. We are not comfortable with a measure that includes such a substantial component that is subject to error due to the very imperfect science of estimating tax shifting.

The TF also produces projections of local tax revenues well before the Census Bureau has released the data. The latest data currently available for local tax revenues are for fiscal year 2008, while the TF attempts to project local tax revenues for FY 2009 based on historical trends. In addition, serious questions have been raised about the TF methodology, which has changed substantially from year to year, producing drastic shifts in some state rankings from one report to the next. (See Nicholas Johnson, "Caution: The Tax Foundation's State and Local Tax Rankings are Unreliable." Center on Budget and Policy Priorities, August 13, 2008, available at http://www.cbpp.org/cms/?fa=view&id=574 .) Finally, the TF is presumably unaware of the systematic under-reporting of Iowa state tax revenues from FY1996 through at least FY2005 due to an error in the state's reporting system (see Issue Review, Sept. 2005, by the Iowa Legislative Services Agency at http://www.legis.state.ia.us/lsadocs/IssReview/2006/IRJWR000.PDF). Because of this under-reporting we have included historical data only for the period 1991-95. Furthermore, there seem to be some continuing problems with the reporting of state sales tax collections, and we have made appropriate adjustments to the figures.

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[1] The reasons for the decline in the effective state tax rate in Iowa and elsewhere no doubt have to do with the recession, the stock market plunge, and the collapse of the housing market. All these factors contributed to a large reduction in consumer spending (and hence sales tax revenues) and the capital losses in the stock market cut into income tax revenues. Apparently, these revenue losses were larger than the declines in measured personal income (which does not take capital gains and losses into account, or the loss in housing wealth).