Iowa Fiscal Partnership policy points
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UNDERSTANDING IOWA TAXES

A Supplement to *The ITEP Guide to Fair State and Local Taxes*

The Iowa Fiscal Partnership is pleased to distribute a new report by the Institute on Taxation and Economic Policy: *The ITEP Guide to Fair State and Local Taxes*. We hope you will find this useful in understanding and evaluating state and local tax policy. Many of the general tax principles and issues presented in the ITEP report have been addressed in the context of Iowa tax policy over the past two years by the Iowa Fiscal Partnership.

Below we summarize several key points from our reports, all of which are available on our website, www.iowafiscal.org <http://www.iowafiscal.org>.

See the ITEP Guide

The ITEP Guide to Fair State and Local Taxes, released in February of 2005, offers a detailed primer on state and local tax policy.

The guide explains the differences between progressive, flat and regressive taxes — and why you should care. It covers the full range of taxes that states and localities can impose, including personal and corporate income taxes, property taxes, and sales and excise taxes.

The full text of the study is available in PDF format at <http://www.itepnet.org/guide.htm>

ARE IOWA'S TAXES COMPETITIVE WITH OTHER STATES?

Iowa's state and local governments ask $576 less in taxes per individual than the 50-state average ($2,837 vs. $3,143). This ranks Iowa 26th in the nation. As a percent of personal income, Iowa's taxes are 10.3 percent, which is equal to the 50-state average. Thus, Iowa is in line with other states. Where Iowa differs most is in corporate income, ranking 45th in corporate income taxes collected per individual ($30 vs. $98 for the 50-state average) and 44th as a percent of personal income (0.11 percent vs. 0.32 percent).

See "Average by Any Measure: State and Local Taxes in Iowa." [1]

DO STATE TAX CUTS SPUR GROWTH?

Tax cuts have little impact on economic growth and may hurt growth if they are paid for by cutting state and local public services. This is because government acts as an "angel investor," supporting a strong economy through investment in infrastructure, education, health care, public safety and more. The impact of state and local taxes on individual business decisions is dwarfed by far more powerful economic forces, such as workforce quality, proximity to markets, interest rates and quality of infrastructure.

See "Taxes and State Economic Growth: The Myths and the Reality." [2]

HOW IS IOWA'S FISCAL HEALTH?

Over the last five years, Iowa has borrowed $2 billion from trust funds in order to maintain spending priorities. Iowa's fiscal health is now in critical condition. Revenues have edged up, but only from the depressed levels they reached during the fiscal crisis. With an aging population and a tax code full of special preferences, Iowa will continue to be hobbled by budget deficits until a tax system is implemented that reflects actual demands on state and local governments.

See "Our Vanishing Budgets: Iowa's Response to the Fiscal Crisis in the States." [3]

WHAT IS FAIR?

The wealthiest Iowans work only three weeks to pay off their state and local taxes (5.8 percent of income), while the poorest Iowans have to work almost twice as long to do the same (10.6 percent of income). In order to align Iowa's overall tax system more closely with ability to pay, Iowa needs to make the income tax more progressive. While the federal government does not tax a four-person family with income of $35,000, the same family in Iowa would typically owe about $1,200 or more.

See "Iowa's Personal Income Tax: Reform for Iowans at Any Age."[4]

DO CORPORATIONS CONTRIBUTE THEIR FAIR SHARE TO IOWA SERVICES?

As the ITEP report shows, state and local corporate income taxes nationally have declined in importance for the past 25 years.[5] Iowa is no exception. Iowa's corporate income tax revenue was 0.4 percent of state personal income in 1992; it is now just 0.1 percent, only a third of the national average. We now rank 44th among the states on this measure, down from 21 in 1992. Many factors contribute to declining revenues from the corporate income tax. First, Iowa has long had two features that reduce revenue from the tax despite a relatively high top tax rate of 12 percent: single-factor apportionment, and the ability to deduct 50 percent of federal taxes. Second, Iowa has not acted to stem the loss of revenue from major loopholes that have increasingly been exploited by multi-state corporations in the last decade. To correct this, Iowa could adopt combined reporting and a "throwback" rule for apportionment. Generally, the state needs to re-evaluate a whole range of "tax expenditures," such as the research activities credit, to see if they serve a public purpose.

See the ITEP report, p. 42, and "Everything You Wanted to Know About Closing Tax Loopholes and Balancing Iowa's Budget ... But Were Afraid to Ask."[6]

Notes:

1 Fisher, Peter S., "Average by Any Measure: State and Local Taxes in Iowa." September 2004, Iowa Fiscal Partnership.

2 Fisher, Peter S., and Elaine Ditsler, "Taxes and State Economic Growth: The Myths and the Reality." May 2003, Iowa Fiscal Partnership. Page 3, table.

3 Bruner, Charles, Peter S. Fisher, Mike Crawford, Elaine Ditsler, Victor Elias, David Osterberg and Jeremy Varner, "Our Vanishing Budgets: Iowa's Response to the Fiscal Crisis in the States." February 2005, Iowa Fiscal Partnership. Also Ditsler, Bruner and Fisher. "A Chronic Budget Crisis: Can Iowa Keep Its Promises?" January 2005, Iowa Fiscal Partnership.

4 Bruner, Charles, and Mike Crawford. "Iowa's Personal Income Tax: Reform for Iowans at Any Age." April 2005, Iowa Fiscal Partnership. Page 7, Appendix 1 table.

5 Institute on Taxation and Economic Policy. "The ITEP Guide to Fair State and Local Taxes." February 2005. Page 36.

6 Iowa Fiscal Partnership. "Everything You Wanted to Know About Closing Tax Loopholes and Balancing Iowa's Budget ... But Were Afraid to Ask." January 2004.

Iowa Fiscal Partnership

The Iowa Fiscal Partnership is a joint initiative of the Iowa Policy Project and the Child & Family Policy Center, two nonprofit, nonpartisan Iowa-based organizations that cooperate in analysis of tax policy and budget issues facing Iowans. IFP reports are available on the web at http://www.iowafiscal.org.

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