



Taking Stock of the Size and Burden of the Taxes Alabamians Pay

Before we close the book on April and the tax forms and filings that are part of this month, it is worth looking at the size of the taxes we pay to support government and who bears the burden of paying them.

HOW BIG IS THE TOTAL TAX BURDEN?

According to an annual roundup published by the Washington, D.C.-based Tax Foundation, about two-thirds of all taxes in the United States – currently \$2.76 trillion – are paid to the federal government, while one-third – \$1.45 trillion today – are paid to state and local governments.

Each year, the Tax Foundation calculates what it calls Tax Freedom Day by estimating all the taxes collected by all levels of government and measuring them as a percentage of total personal income for the nation.

The Foundation's report then applies that percentage to the calendar year and comes up with a number of days it takes to pay those taxes. It's not an accurate reflection of any particular individual's tax bill, but it is one way to talk about tax burdens.

Using the Tax Foundation's approach, close to 30 percent of the national income is needed to pay taxes at all levels of government. That puts Tax Freedom Day on April 18th this year, 108 days or 30 percent through the calendar year.

The biggest share of the tax burden goes to pay federal taxes. It would take all of us working 70 days out of 365 to generate enough income to pay all federal taxes. The biggest federal tax is the individual income tax, but the total also includes payroll taxes that support Social Security and Medicare, as well as corporate income taxes and excise taxes on such items as motor fuel. These tax collections don't cover all federal spending. The federal government runs deficits and borrows each year to support current spending levels.

According to the Tax Foundation, it would take another 21 days of work this year to generate the \$833 billion needed to balance the budget and eliminate the deficit.

The Tax Foundation also applies its estimates at the state level and computes Tax Freedom Days for individual states. Some states have higher taxes than others, and the period assigned for paying federal income taxes is somewhat longer in high-income states due to the progressivity of the federal tax system.

States with lower incomes and lower state and local taxes need less time to pay their tax bill.

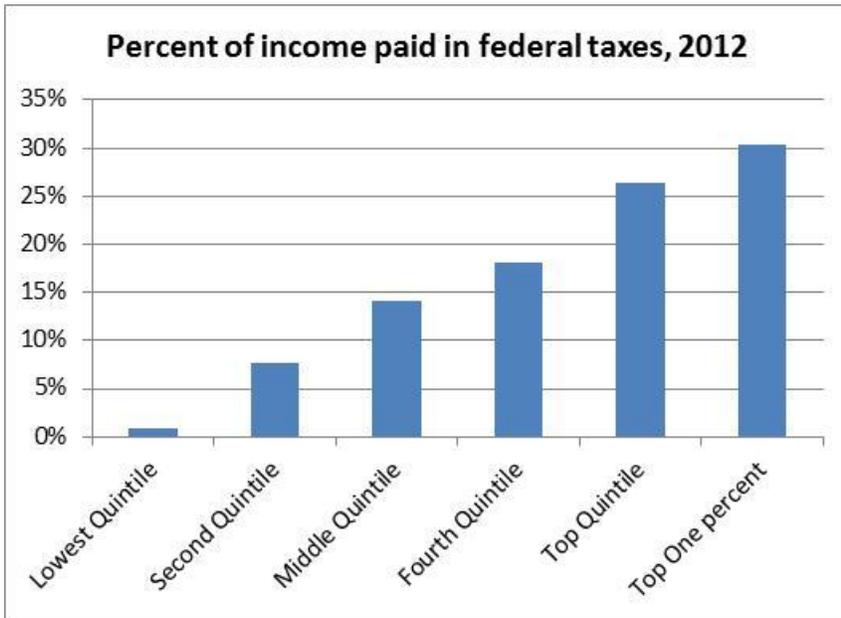
Both factors conspire to make Alabama's Tax Freedom Day arrive earlier than in most states. According to the Foundation's calculation, 26 percent of Alabama personal income goes to combined federal, state and local taxes in Alabama.

The Tax Foundation ranks Alabama's burden of state and local taxes the 8th lowest out of 50 states, capturing on average 8.18% percent of income. The national average is 9.9%. The Tax Foundation estimates that Alabama's taxpayers pay \$2,740 per capita in state and local taxes. April 5, the 94th day of the calendar year, is Tax Freedom Day in Alabama, well below the national average.



HOW IS THE TAX BURDEN DISTRIBUTED?

As the two charts below make plain, federal taxes are distributed in a very different way across the



income spectrum than are the taxes paid to state and local government. The federal tax system is “progressive,” meaning that it takes a greater percentage of income from affluent taxpayers than from those who earn less. State and local taxes, on the other hand, tend to be “regressive” because they require a higher percentage of income from those on the lower end of the earnings scale.

The federal tax system is dominated by the individual income and payroll taxes, which account for 82 percent of federal revenue.

Source: Urban Institute-Brookings Tax Policy Center

Federal income taxes take a greater share of income the more an individual earns. At the lowest end of the income spectrum, refundable credits actually pay the filer rather than the other way around.

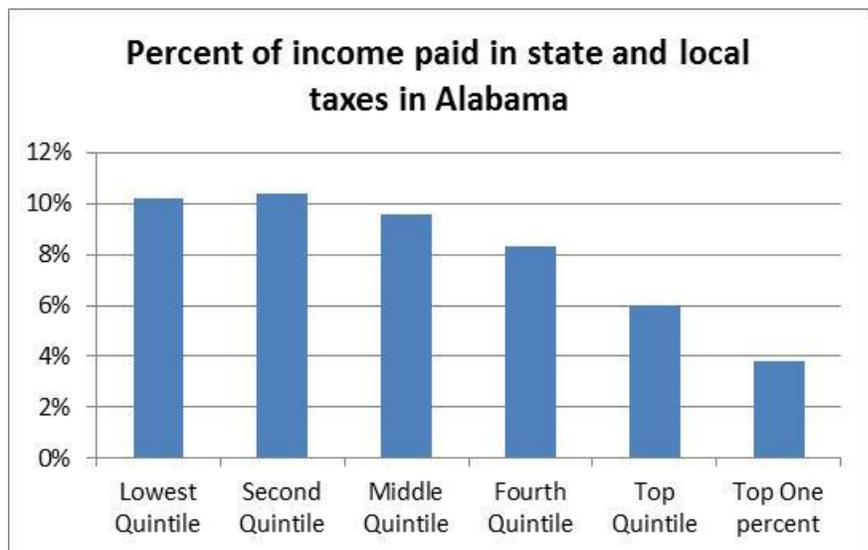
Federal payroll taxes support Social Security and Medicare. They apply uniformly to wages and salaries up to \$113,700, and at a reduced rate above that.

STATE AND LOCAL TAXES

At the state and local level, the sources of tax revenue are more diverse. In general, states tend to apply these taxes in a way that balances the tax burden across the income spectrum.

Three primary taxes fuel state and local government: property, sales, and income taxes. On average, states get 35 percent of their revenue from property taxes, 34 percent from sales taxes and 21 percent from individual income taxes.

In Alabama, the mix is different. Alabama’s property taxes, the lowest in the nation, produce



Source: Institute on Taxation & Economic Policy



just 19 percent of state and local tax revenue. The state's individual income tax brings in 20 percent of taxes. That leaves state and local governments in Alabama more dependent on sales taxes, which produce 47 percent of state and local tax revenue.

The heavy reliance on sales taxes leads to lower income residents in Alabama paying a greater percentage of their income in taxes than those who are better off. Most states take steps to lighten the sales tax burden on the poor in an attempt to create more balance in their tax structure. Some states don't apply the sales tax to groceries. Others offer a credit on income taxes to those at the lower end of the income scale, a credit designed to offset the burden of sales taxes. Alabama and Mississippi are the only two states that tax groceries at the full rate.

Another way states try to balance their tax burdens is through progressive state income taxes. Alabama's income tax was originally designed to be progressive, with increased rates applying to higher levels of income. However, because the brackets have not kept up with the growth of wages, the tax is now, for all intents and purposes, flat. The top rate of 5 percent kicks in at just \$6,000 of taxable income.

Also, many states provide more generous personal exemptions and standard deductions in their income tax systems, measures that can provide tax relief to those at the lower end of the income scale. Alabama begins taxing income at one of the lowest thresholds in the U.S.

According to calculations by the Center on Budget and Policy Priorities, in 2011, Alabama was one of only five states to require families of four in extreme poverty to pay income tax. In some scenarios, the [CBPP study](#) estimates Alabama's income tax burden on poverty families is the highest in the nation.

At the other end of the income spectrum, high-earning tax payers get a valuable deduction: Alabama is one of three states that allows a full deduction for federal income taxes (three other states allow a partial deduction).

As a result, the higher your taxes under the progressive federal income tax, the bigger your tax break in Alabama.

The combined effect of those policies earns Alabama's tax system a spot among the top 10 most regressive in the U.S., according to a 2013 report by the [Institute on Taxation & Economic Policy](#) (ITEP).

According to [ITEP's estimates](#), the lowest 20 percent of income earners in Alabama pay more than 10 percent of their incomes in state and local taxes. In contrast, the top 1 percent of earners in Alabama pay just 3.8 percent of their income in state and local taxes.