The Bush Tax Cuts, State by State

What the analysis entails

Our analysis looks at the impact of President George W. Bush's proposed tax cuts by income level on taxpayers in each of the 50 states and the District of Columbia. We included the effects of (1) the Bush income tax rate reductions as approved by the House of Representatives in March (H.R. 3); (2) the House's versions of the President's proposed "marriage penalty" relief and doubling of the $500 per-child tax credit, also passed by the House in March (H.R. 6); and (3) the President's proposed repeal of the federal estate tax on the largest two percent of estates[1] and his relatively small proposed corporate tax breaks, which are still pending in the House.

The proposed Bush tax cuts are shown as if they were fully effective in 2001, at 2001 income levels and in 2001 dollars. Note, however that the tax reductions would not actually be fully in place until ten years from now, in 2011.[2]

In our presentation, taxpayers (or, more precisely, "taxpaying units") include both individuals and couples.[3] We group taxpayers by income based on income reported (or reportable) on federal tax returns, plus income that is not taxable (e.g., tax-exempt interest, non-taxable transfer payments, etc.)

We offer two sets of state-by-state distributional tables by income groups:

One set of tables is based on the *national* break points for each income quintile (and subquintiles of the top fifth). Since both average incomes and income distributions differ substantially by state, some states are over-represented in the nation's higher-income groups, while others are over-represented in the nation's lower-income groups.[4]

We also report our results by income groupings *specific to each state*. These tables show how, for example, how middle-income (median) taxpayers in each state fare, how much of the total Bush tax cut for a specific state goes to that

[1] Our figures may substantially understate the effects of estate tax repeal, since the Joint Committee on Taxation has recently increased its estimate of the cost of repeal by more than 80 percent, due to expected income tax avoidance that estate tax repeal would engender.

[2] The proposed income tax rate reductions and the child credit increase would be phased in between 2001 and 2006. Most of the "marriage penalty" relief would be phased in between 2004 and 2009. About two-thirds of the repeal of the estate tax would be put off until 2011, although the estate tax would be gradually reduced somewhat starting in 2002. One income tax change, a small increase in the Alternative Minimum Tax exemption for couples, is not slated to be fully effective until 2048.

[3] Separate tables for couples and singles would be a plausible alternative, but would lead to a proliferation of tables in the report, and could impede rather than enhance intelligibility.

[4] For example, 1.5 percent of New Jersey taxpayers are in the best-off one percent nationally, while only 0.4 percent of West Virginia taxpayers earn enough (more than $373,000) to make the national top one percent. At the other end of the income scale, 28 percent of Louisiana taxpayers are in the lowest fifth of the income scale nationally, while only 12.9 percent of Connecticut taxpayers fall into the nation's bottom 20 percent.

particular state's best-off one percent, and so forth.

Each set of tables offers different and interesting insights into the effects of the Bush tax cuts on taxpayers at various income levels and in the states.

Because of the extreme concentration of the Bush tax cuts in the upper income groups—45 percent of the total Bush tax cut dollars are targeted to the best-off one percent of all taxpayers—there is a very large difference between what typical taxpayers would get under the Bush plan, i.e., the *median* tax cuts, and the *average* tax cuts. In fact, nationally, the average tax cut is considerably more than double the median cut.

Brief overview of findings

As is well known, the Bush tax cuts are targeted to the wealthiest Americans. When (and if) the tax cuts are finally fully in place, the best-off one percent of all taxpayers would get an average annual tax reduction (in 2001 dollars) of $54,400 a year, compared to a tax cut of $552 a year for the typical taxpayer. There are also dramatic differences in the effects of the Bush tax cuts among the states.

We can start with the wide disparities by state in the average size of the tax cuts that the President has proposed. These range from a high of $1,855 a year per taxpayer in Connecticut down to a low of $708 a year per taxpayer in West Virginia. The average tax reductions in Connecticut, Washington, DC and Nevada are each more than 25 percent higher than the national average tax cut, while the average tax cuts in West Virginia, Montana, Mississippi, New Mexico, Arkansas, South Carolina and Kentucky are all more than 25 percent below the national average.

The median annual tax cuts also differ substantially by state, ranging from a high of $785 a year per taxpayer in Alaska to a low of $404 a year in Mississippi.

Because of differences in income distributions and family demographics, some states stand to get relatively high *average* tax cuts along with relatively low *median* tax cuts under the Bush plan, while the opposite occurs in other states. For example, New York ranks ninth in terms of its average Bush tax cut, but 44th in median tax cut. Conversely, North Dakota ranks 43rd in average tax cut, but is well above average (7th) in its median Bush tax cut.[5]

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[5]New York's high *average* tax cut reflects its high incomes, particularly at the upper end of the income scale where the bulk of the Bush tax reductions are targeted. The average income of New York's top one percent in 2001 is $1.7 million, compared to $1.1 million nationally. North Dakota's low average tax cut reflects its relatively low incomes, particularly at the upper end of the income scale—the average income of North Dakota's top one percent in 2001 is $598,000, barely more than half the national average for the top one percent.

New York's relatively low *median* tax cut reflects, among other things, the fact that only 28 percent of the taxpaying units in New York's middle income group are married couples, compared to 35 percent nationally. North Dakota's relatively high median tax cut reflects, among other things, the fact that three-fifths of the taxpaying units in North Dakota's middle income group are married couples. As it turns out, New York's $33,800 median income for all taxpaying units is almost identical to North Dakota's $33,400 median income. Since the Bush income tax cuts are much larger for married couples than for unmarried taxpayers, North Dakota's *median* tax cut of $664 is 34

The percentage of taxpayers getting no tax cut at all under the Bush program also varies substantially by state. For example, one out of every three Mississippi taxpayers would get no tax reduction under the Bush plan, compared to one in six taxpayers who would get no tax cut in New Hampshire.

Of course, the Bush tax cuts are only one option out of several possible uses of the projected budget surpluses. Alternatives could include debt reduction, continued or enhanced federal services, tax reductions that are distributed differently, or some combination of these. Many residents of states that get less than the national average tax cut under the Bush tax program might logically prefer something different than what the President has proposed—although 20 of the 31 states that get noticeably less than average from the Bush tax program gave their electoral votes to Bush in the last election.

Many citizens of states that get above-average tax cuts under the Bush program also might favor other options—perhaps because they find the concentration of the Bush tax cuts on the best-off Americans (even within their own states) to be unwise or unfair, or perhaps because they value public services or fiscal prudence more highly than tax reductions. After all, eight of the 14 states that are targeted for above-average tax cuts voted for Al Gore in the last election.[6]

MORE TO COME

Sidebar: AMT issues

The differences among the states in the size of the average Bush tax cuts reflect, more than anything, else differences in average incomes in the various states, in particular differences in incomes for the richest people in particular states. But other factors are at work as well.

For example, a substantial portion of the Bush income tax reductions that would otherwise go to taxpayers in the top income quintile—excluding the top one percent—would be offset by increases in the Alternative Minimum Tax.[7] A key part of the AMT calculation involves disallowing itemized deductions for state and local taxes, with state income taxes being the primary state tax paid by upper-income taxpayers in most states. In effect, the Bush tax cut wipes out federal tax deductions

percent bigger than New York's $495—even though New York's *average* tax cut is 47 percent above North Dakota's.

[6]Of the six states whose average tax cuts under the Bush plan are very close to the national average, four voted for Bush and two voted for Gore.

[7]The Bush tax plan lowers the current 28 percent and 31 percent regular tax rates to 25 percent, but does not reduce the current 26 percent and 28 percent Alternative Minimum Tax rates. As a result, a very large portion of taxpayers whose regular top marginal tax rate is cut from 28 or 31 percent will find themselves in the AMT. The AMT effect dissipates at the highest income levels, because the top Bush regular tax rate is 33 percent (replacing the current 36 percent and 39.6 percent rates).

for state and local taxes for a large portion of itemizers in most states.[8]

Better-off taxpayers in the handful of states that have no state income tax are much less likely to be affected by the AMT than taxpayers in "normal" states. As a result, these no-income-tax-state taxpayers get larger federal tax cuts under the Bush plan than do taxpayers with similar incomes in other states. To illustrate the magnitude of this AMT issue, the ten states with the largest average tax cuts under the Bush plan include five of the eight states with no broad-based state income tax: Nevada, Wyoming, Florida, Washington and Texas. The states ranking 11th and 13th in average tax cuts under the Bush plan—New Hampshire and Alaska—also have no state income tax.

[8]For most affected taxpayers, the AMT calculation involves replacing regular tax deductions for personal exemptions and either the standard deduction, if taken, or certain itemized deductions, primarily state and local taxes, with a flat exemption of $45,000 for couples and $33,750 for unmarried taxpayers. These exemptions are not indexed for inflation, so by 2008 they will decline to about $37,600 and $28,200 in 2001 dollars.

Based on this "Alternative Taxable Income, a "tentative AMT" is calculated, at tax rates of 26 percent on the first $175,000 and 28 percent on amounts above that. The tentative AMT replaces the regular tax if the AMT is bigger.