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Latest IRS Data Reveal Fundamental Mismatches in the States *Most Unequal States Either Don't Have a Personal Income Tax* *or Have One in Need of Improvement*

Data released late last week by the Internal Revenue Service (IRS) indicate that 10 states have greater concentrations of reported income among their very wealthiest residents than the country as a whole. Unfortunately, the tax systems in those ten states generally ignore that very important reality. Of those ten states:

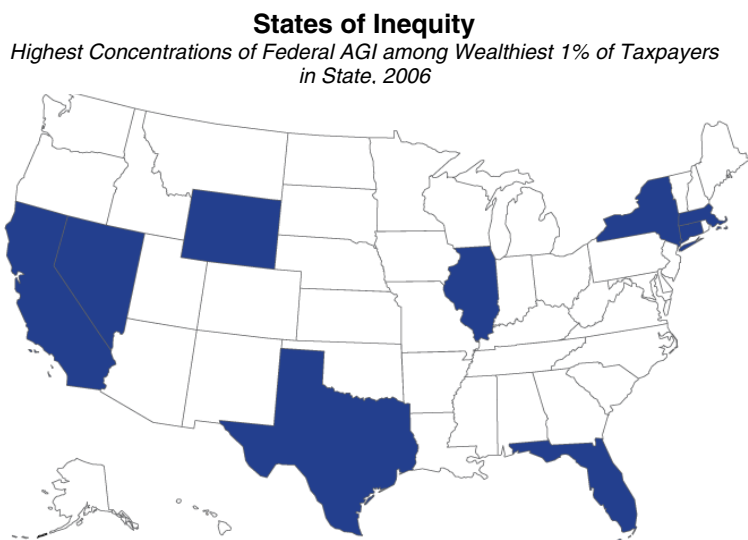
- four lack a broad-based personal income tax;
- three either impose a single, flat rate personal income tax or have a rate structure that all but functions in that manner; and
- three use a graduated rate structure, but two have cut income taxes for their most affluent residents substantially over the past two decades and are now struggling to close multi-billion dollar budget gaps.

The failure to use sufficiently progressive personal income taxes — or to levy any personal income tax at all — results in an overall tax system that is unsustainable, inadequate, and unfair over the long-run. Indeed, of these ten states, over half face severe or chronic budget shortfalls. Reforms to improve the personal income tax — or simply to institute one — should be on the agenda in each of these states.

What the IRS Data Show

On July 31, the IRS released data for 2006 (the most recent year for which such information is available) on the distribution of reported income for federal income tax filers on a state by state basis. These data indicate that, for the country as a whole, the richest 1 percent of taxpayers reported over one-fifth — 21.1 percent — of total adjusted gross income (AGI). Ten states, as shown in the figure at right, exceeded that mark, meaning that they have income distributions that particularly favor the wealthy few. In those states, the richest

1 percent of federal taxpayers received as much as 25 percent of AGI — or even 30 percent in the case of Wyoming.



Source: IRS Statistics of Income, 2006

Distribution of Federal AGI Within the States, 2006

	Share of Federal AGI Reported by State Residents, 2006		
	Top 1%	Bottom 50%	Ratio
Wyoming	30.7%	11.6%	2.64
New York	28.7%	10.7%	2.68
Nevada	28.6%	13.2%	2.16
Connecticut	28.1%	10.6%	2.66
Florida	27.3%	11.7%	2.33
District of Columbia	25.5%	11.9%	2.13
California	23.1%	12.2%	1.89
Massachusetts	22.9%	12.0%	1.92
Texas	22.7%	12.1%	1.88
Illinois	21.4%	12.3%	1.74
United States	21.1%	12.7%	1.66
Arizona	20.5%	14.1%	1.46
Colorado	20.5%	13.2%	1.55
Oklahoma	20.4%	13.6%	1.50
New Jersey	19.9%	11.9%	1.67
Louisiana	19.5%	12.9%	1.51
Washington	19.1%	13.9%	1.38
Georgia	19.1%	12.8%	1.49
Idaho	19.0%	14.2%	1.34
Tennessee	19.0%	13.7%	1.39
South Dakota	18.9%	13.9%	1.36
Utah	18.6%	14.1%	1.32
New Hampshire	18.3%	13.5%	1.35
Alabama	18.2%	13.7%	1.32
Delaware	18.1%	14.0%	1.30
Pennsylvania	18.1%	13.1%	1.38
Maryland	18.1%	13.5%	1.33
Nebraska	17.7%	14.3%	1.24
Virginia	17.5%	13.3%	1.31
Minnesota	17.4%	13.7%	1.27
Kansas	17.2%	13.6%	1.26
Rhode Island	17.2%	13.6%	1.26
North Carolina	17.0%	14.0%	1.22
Missouri	16.9%	13.9%	1.22
Vermont	16.9%	13.8%	1.22
South Carolina	16.8%	14.1%	1.19
Wisconsin	16.5%	14.3%	1.15
Oregon	16.3%	14.2%	1.15
Montana	16.3%	13.6%	1.19
Hawaii	16.1%	14.7%	1.09
Mississippi	15.9%	14.7%	1.09
New Mexico	15.6%	13.8%	1.12
Ohio	15.5%	14.9%	1.04
Arkansas	15.4%	14.7%	1.05
Indiana	15.2%	14.2%	1.07
Kentucky	15.0%	14.5%	1.04
Michigan	15.0%	13.4%	1.12
North Dakota	14.9%	14.8%	1.01
Maine	14.9%	15.0%	0.99
Iowa	14.0%	15.5%	0.91
Alaska	14.0%	13.2%	1.06
West Virginia	12.1%	15.2%	0.79

Source: IRS Statistics of Income, 2006

To be sure, the distribution of reported income in any state could hardly be characterized as equal. According to the IRS data, the poorest half of the income distribution had as large a share of total AGI as the richest 1 percent in only three states in 2006. Yet, in the 10 least equal states, such inequities were especially pronounced. In six of the ten, the top 1 percent accumulated *twice* as large a share of total AGI as the bottom half of taxpayers; in the other four, they received at least one and a half times as much.

“In light of these realities, it is essential for states to levy a personal income tax that employs a graduated rate structure,” said Jeff McLynch, ITEP’s Northeast Regional Director. “Such an approach not only promotes the long-term sustainability of states’ tax systems, since they would better reflect the distribution of economic gains, but also provides states with opportunities to mitigate unfair economic outcomes.”

Nearly all of the 10 most unequal states come up short in this regard, however. Wyoming, Nevada, Florida, and Texas completely lack a personal income tax. Massachusetts and Illinois have personal income taxes but impose a single, flat rate, while Connecticut nearly does. (It has two rates — 3 percent and 5 percent — but roughly three out of five taxpayers face the higher 5 percent rate.) Both New York and California have weakened the progressivity of their income taxes since the 1990s, providing enormous tax cuts to the very wealthy and leaving a lasting legacy of structural budget deficits. In this context, then, these states should strive to create an income tax or to build a more progressive one.