Washington Research Council

POLICY brief

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Understanding the Tax Rankings

BRIEFLY

The Washington Research Council cites data showing Washington's tax burden as 11th in the nation measured per capita and 13th when measured as a share of the economy. Other data sources report slightly different rankings. This brief explains the variation and the Council's decision to use Census data.

Washington has the nation's sixth highest tax burden.

No, wait, it's the eleventh.

Actually, that's not right either. It ranks thirteenth.

More confusing, contradictory government data manipulation?

Not really, it's just a demonstration of the different approaches people take to comparing tax burdens across the nation.

The Washington Research Council report, *How Washington Compares,* presents information from the standard data source, the U.S. Department of Commerce, Bureau of the Census. The data available from the bureau suffer from a lag time of several years – 1996 is the most recent fiscal year, for example – as the process of collecting, categorizing, and publishing data on local government revenue and expenditure is labor intensive. At that, the bureau relies on statistical samples to estimate local government activity.

Using those data, we report that Washington ranks 11th in per capita total state and local taxes, $2,795 per person. Nationally, state and local taxes claim $2,597.

When taxes are computed as a share of statewide personal income, Washington ranks 13th, with a tax burden of about $120 per $1,000 of personal income. Nationwide, state and local taxes claim $113 per $1,000 of personal income (i.e., 12%).

When the District of Columbia is excluded, Washington's ranking rises from 11th per capita to 10th and from 13th as a share of personal income to 12th.

The Washington Research Council generally looks only at the combined state and local data, because variation in state-local fiscal systems limits the usefulness of comparisons looking at only state activity. Washington, for example, is more centralized in its tax collections than most states. Funding for the public schools is heavily skewed toward state financing, which is the major reason for the state property tax.

Often people want more current data and are willing to sacrifice some precision in order to get it.

Nationally, Tax Foundation analysts prepare an estimate of state and local collections based on their own statistical model. Unlike the Census Bureau, which estimates collections from surveys of local governments, the Tax Foundation, an independent tax research group, calculates taxes based on economic activity, adjusted for past performance by state and local governments and tax policy changes. The Foundation's estimate for Washington places us eighth in 1999 in state and local tax collections as a share of personal income, again at about 12%.

Only when Federal tax collections are added does Washington rise to sixth place. As the Tax Foundation reports, "Federal income taxes place such a proportionately greater burden on America's affluent that when these taxes are

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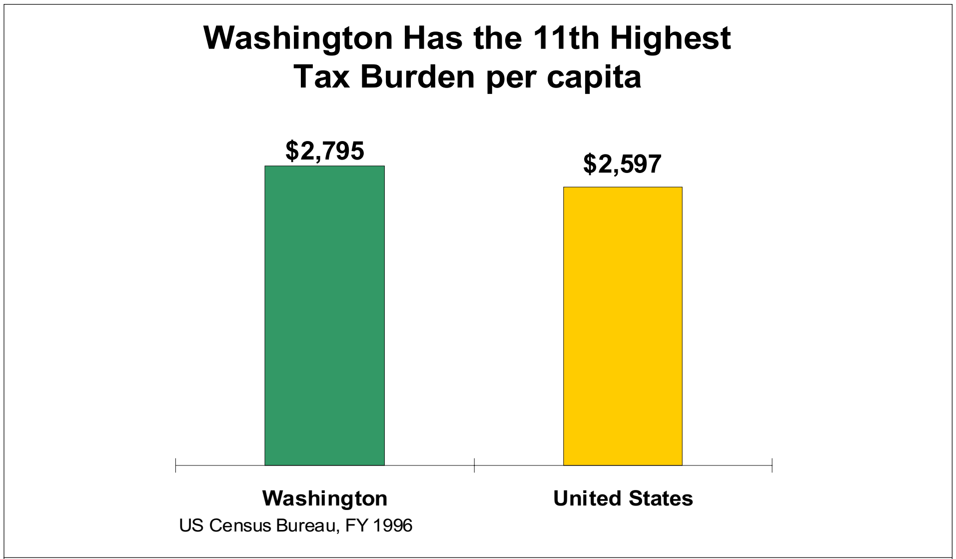
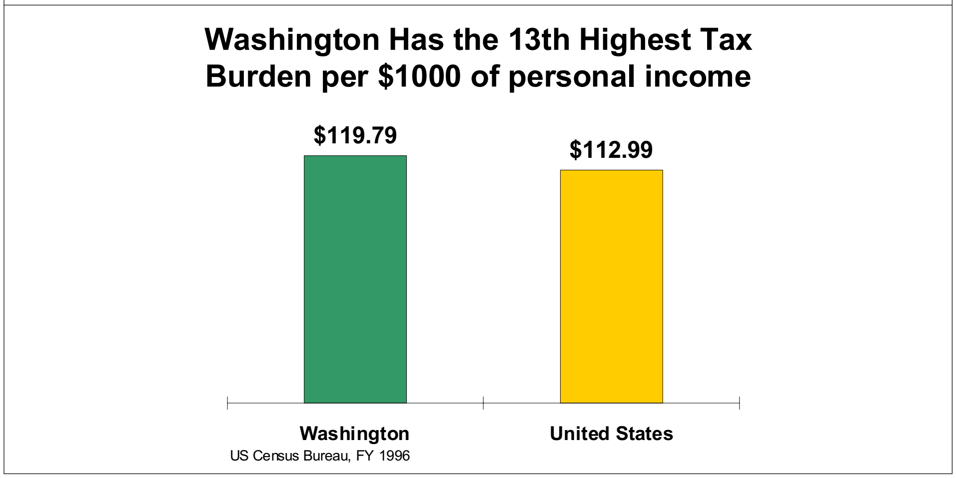
removed from the calculation, less affluent states…" will rise in the rankings.

The Tax Foundation makes another unusual adjustment. Their five highest taxed states (combined state and local taxes) are these: Hawaii, New York, Maine, Wisconsin, and Minnesota.

From *How Washington Compares*, these five emerge as the most heavily taxed states: Alaska, New York, Wisconsin, Minnesota, and Hawaii.

The rankings move around some. Most of the change reflects the Tax Foundation's attempt to adjust for state and local corporate profits taxes and major severance taxes. Most dramatic, Alaska tops the Census Bureau rankings and comes in 49th on the Tax Foundation's list. Wyoming similarly drops, from 17th using Census Bureau Data to 50th on the Tax Foundation list.





The Tax Foundation method has the merit of attempting to address the legitimate problems involved in accounting for taxes that are exported, that is, paid by people outside the state. Economists differentiate between "economic incidence" and "initial incidence." The economic incidence allocates the tax burden to the actual payer of taxes, recognizing that business taxes, for example, are passed on to consumers, shareholders, and employees. Initial incidence looks at who remits the tax to the tax collector, disregarding how the burden may be reallocated down the line.

The Tax Foundation methodology takes care of the biggest share of the problem as it affects those small population states with high tax collections paid by oil producers and others drawing on natural reserves. By making the adjustment, however, the Tax Foundation introduces another layer of complexity into the equation. Hawaii, for example, now topping their list, relies on tourism revenues for which no adjustment is made. And so on. While useful, the attempt does not, in our opinion, fully succeed.

The inclusion of federal taxes, on the other hand, adds nothing much to an understanding of state and local fiscal policy. There's not much state and local governments can do to influence the federal tax burden of their residents.

In conclusion, the best measure of state and local tax burden is that produced by the US Census Bureau and reported in *How Washington Compares.*

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