

SPECIAL REPORT

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Tax Burden on American Families Rises Again

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In 1997, the tax burden on America's median income families increased again. This year federal, state and local taxes combined are projected to claim 38.2 percent of the income of a median income two-earner family, up from 37.3 percent in 1996. For a single-earner family, total taxes as a percentage of income are projected to increase to 35.6

percent, up from 35.5 percent last year.

For the dual-earner family, the tax burden is approaching its historic high. In 1981, before the federal income tax reduction and bracket indexation of the Economic Recovery Act of 1981 took effect, the dual-income family used 38.9 percent of its income to pay for its taxes.

Table 1 charts the historical evolution of the tax burden borne by median income single and dual-earner families. The tax burden is calculated on a decade by decade basis from 1955 through 1985 and yearly thereafter. Since 1955, the tax burden as a percentage of income has grown 10.3 percentage points for two-income families; for single income families, it has grown almost 9 percentage points.

As *Table 1* shows, after adjusting for inflation, total taxes on the median income dual-earner family today are \$22,521, nearly triple 1955's burden when they were \$8,089. In real (inflation-adjusted) dollars, the projected total tax burden of the median income two-earner family will be higher than in any previous year.

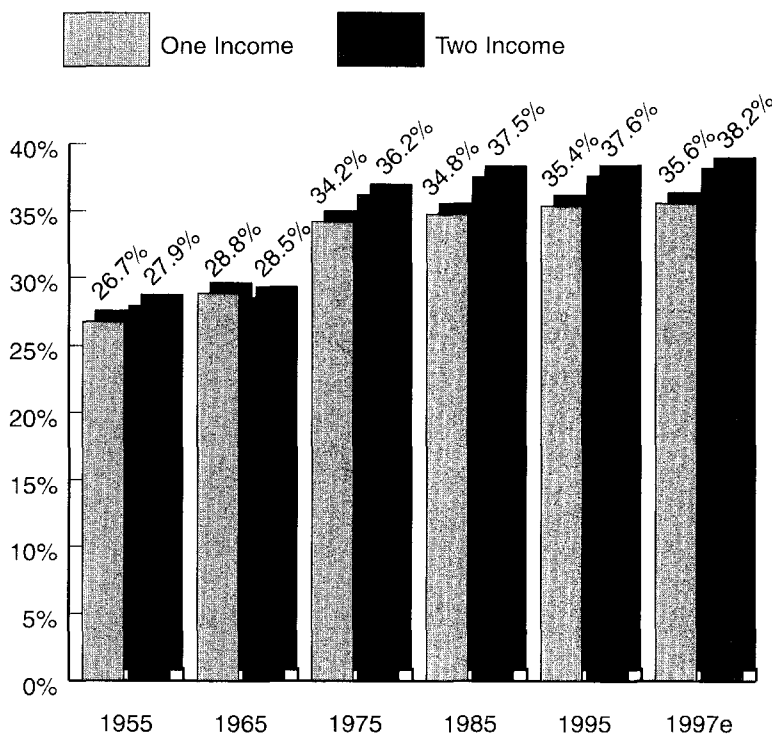
For the single-income family, total taxes (adjusted for inflation) have almost doubled from \$6,024 in 1955 to \$11,002 in 1997. However, the median income single-earner family will be paying less in real terms by the standards of the Eighties and Nineties due to the declining real income of families of this kind.

The Growth of Taxation

Two forces have driven the increasing burden of taxation on America's median-income families in recent years: the growth of the federal payroll tax and a general increase in state and local taxation.

Payroll taxes for social insurance have

Figure 1
 Taxes as a Percentage of Income for Median One- and Two-Income Families Selected Years, 1955-1997



*Table 1a
Taxes and the Median Single-Income Family, 1955-1997e*

	1955	1965	1975	1985	1986	1987	1988	1989
Median Family Income	4,069	6,060	11,568	21,190	22,310	23,111	23,872	25,226
Federal income tax	296	444	941	1,790	1,802	1,622	1,681	2,023
Payroll Tax:								
Employee Portion	79	174	656	1,449	1,547	1,603	1,739	1,838
Employer Portion	79	174	656	1,449	1,547	1,603	1,739	1,838
Other Federal Taxes	354	437	563	738	768	876	904	922
Total Federal Taxes	807	1,229	2,817	5,426	5,665	5,704	6,063	6,621
State and Local Taxes	302	567	1,359	2,444	2,637	2,736	2,772	2,941
Total Taxes	1,109	1,796	4,176	7,870	8,302	8,440	8,835	9,562
After Tax Income	3,039	4,438	8,048	14,769	15,555	16,274	16,776	17,502
Total Taxes as a Percentage of Income	26.7%	28.8%	34.2%	34.8%	34.8%	34.2%	34.5%	35.3%
Inflation Adjusted Total Taxes (1997\$)	6,024	8,105	11,176	11,288	11,605	11,445	11,559	12,004

Note: The burden of federal and state corporate income taxes are included. After-tax income does not deduct employer's share of payroll taxes because the burden of the payroll tax is assumed to reduce income before the "gross" seen on paychecks. "Total taxes as a percentage of income" is calculated by adding the employer's share of the payroll tax to the median-family income.

Source: Tax Foundation.

*Table 1b
Taxes and the Median Two-Income Family, 1955-1997e*

	1955	1965	1975	1985	1986	1987	1988	1989
Median Family Income	5,250	7,983	16,058	33,411	35,108	36,799	38,702	40,658
Federal income tax	475	655	1,792	3,853	3,906	3,367	3,519	4,216
Payroll Tax:								
Employee Portion	84	174	825	2,261	2,410	2,526	2,790	2,931
Employer Portion	84	174	825	2,261	2,410	2,526	2,790	2,931
Other Federal Taxes	457	576	781	1,164	1,209	1,395	1,466	1,487
Total Federal Taxes	1,100	1,579	4,223	9,540	9,935	9,814	10,565	11,565
State and Local Taxes	389	747	1,887	3,853	4,150	4,357	4,493	4,740
Total Taxes	1,489	2,326	6,110	13,393	14,085	14,170	15,059	16,305
After Tax Income	3,845	5,831	10,773	22,279	23,433	25,154	26,434	27,285
Total Taxes as a Percentage of Income	27.9%	28.5%	36.2%	37.5%	37.5%	36.0%	36.3%	37.4%
Inflation Adjusted Total Taxes (1997\$)	8,089	10,495	16,349	19,210	19,688	19,217	19,703	20,468

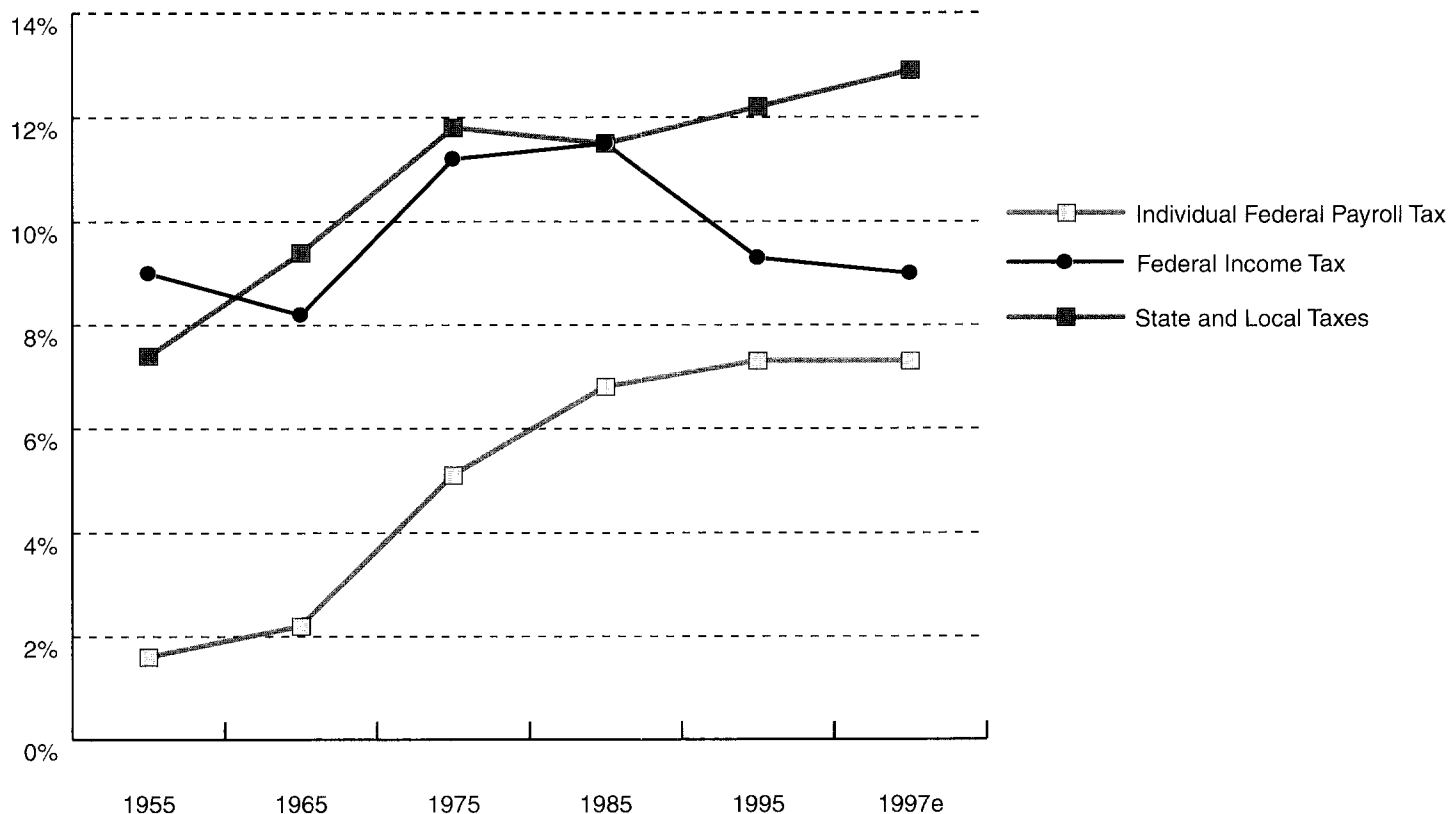
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Source: Tax Foundation.

1990	1991	1992	1993	1994	1995	1996	1997e
25,878	25,960	26,059	26,193	27,145	28,423	28,383	28,808
2,027	1,952	1,874	1,801	1,829	1,916	1,987	2,017
1,920	1,926	1,934	1,944	2,014	2,109	2,106	2,138
1,920	1,926	1,934	1,944	2,014	2,109	2,106	2,138
922	908	913	985	1,108	1,205	1,199	1,252
6,790	6,713	6,654	6,673	6,966	7,339	7,398	7,544
3,019	3,118	3,160	3,173	3,296	3,456	3,440	3,458
9,808	9,831	9,815	9,847	10,262	10,795	10,838	11,002
17,990	18,056	18,178	18,290	18,898	19,737	19,651	19,944
35.3%	35.3%	35.1%	35.0%	35.2%	35.4%	35.5%	35.6%
11,803	11,378	11,055	10,805	10,999	11,283	11,076	11,002

1990	1991	1992	1993	1994	1995	1996	1997e
42,146	43,623	45,563	47,424	48,970	50,989	53,361	54,910
4,261	4,280	4,313	4,451	4,568	4,757	4,802	4,942
3,095	3,204	3,346	3,483	3,596	3,745	3,919	4,033
3,095	3,204	3,346	3,483	3,596	3,745	3,919	4,033
1,502	1,526	1,596	1,783	1,999	2,162	2,254	2,386
11,953	12,214	12,601	13,200	13,760	14,408	14,894	15,393
4,917	5,239	5,526	5,745	5,945	6,199	6,468	7,127
16,870	17,453	18,127	18,945	19,705	20,607	21,362	22,521
28,372	29,374	30,782	31,961	32,861	34,127	35,918	36,423
37.3%	37.3%	37.1%	37.2%	37.5%	37.6%	37.3%	38.2%
20,300	20,200	20,418	20,790	21,120	21,540	21,831	22,521

Figure 2
Taxes as a Percentage of Median Family's Income, 1955-1997
(Two-Income Family)



Source: Tax Foundation.

been increasing rapidly since the mid-1960s when they were about 2 percent of median family income. Today, they account for about 7 percent of median family income. (See *Figure 2*.) Payroll taxes fund three federal social insurance programs: Old Age and Survivors Insurance (OASI—more commonly known as Social Security), which provides income support for retired workers; Disability Insurance (DI); and Hospital Insurance (HI—the primary component of Medicare), which provides health benefits to retirees and the elderly.

Currently, an employee and employer each pay a tax of 7.65 percent of the worker's income to the federal government as payroll taxes. Economists generally agree that employers pass their share of payroll taxes on to workers by paying wages that are proportionately less than they would be in the absence of the tax. At the current level of the

payroll tax, then, the median income family's gross wages are more than 7 percent less than they would be without the payroll tax.

While federal taxes as a percentage of income have fallen since the mid-1980s when the Economic Recovery Act of 1981 took effect, state and local taxes have been increasing rapidly since the 1950s. They have grown about 5 percent since 1955 and since 1985 have been a larger fraction of median family income, surpassing federal income taxes as a percentage of family income in 1985.

The Taxpayer Relief Act of 1997

The Taxpayer Relief Act of 1997 contains many provisions that will have an effect on the tax burden of the median income American family. Almost all of the tax reduction provisions of the law including the provisions that

Revised Estimates for Typical Family's Tax Burden, 1997

Since the release of the Tax Foundation's Special Report No. 74, the November 1997 median-income family study titled "Tax Burden on the American Family Rises Again," updated data has become available. The following table and pie chart represent the Tax Foundation's latest estimate for the median-income family in 1997. Using the new data, the average tax rate for a median single-earner family is slightly higher than was reported in the original report, while the rate for the dual-earner family is slightly lower than initially reported.

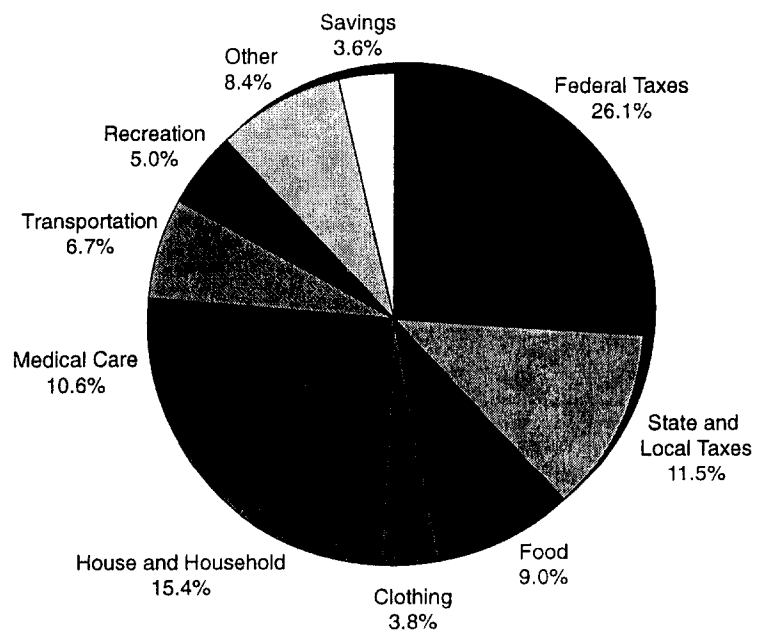
Taxes and the Median One- and Two-Income Family, 1997

	Single- Income	Dual- Income
Median Family Income	\$28,808	\$54,910
Federal Income Tax	2,017	4,942
Payroll Tax:		
Employee Portion	2,138	4,033
Employer Portion	2,138	4,033
Other Federal Taxes	1,260	2,401
Total Federal Taxes	7,551	15,408
State and Local Taxes	3,547	6,761
Total Taxes	11,099	22,169
After-Tax Income	19,847	36,774
Total Taxes as Percentage of Income	35.9%	37.6%

Note: The burden of federal and state corporate taxes are included. After-tax income does not deduct employer's share of payroll taxes because the burden of the payroll tax is assumed to reduce income before the "gross" seen on paychecks. "Total taxes as a percentage of income" is calculated by adding the employer's share of the payroll tax to the median-family income.

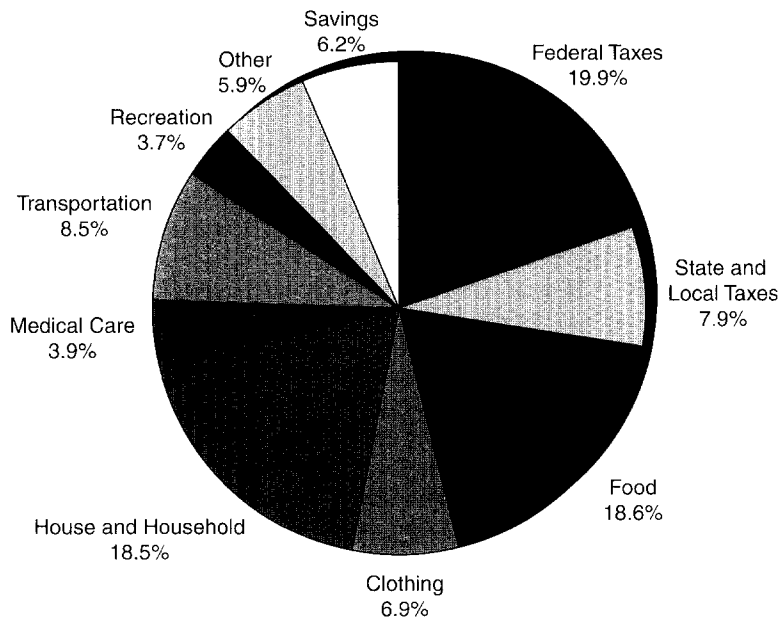
Source: Tax Foundation.

Representative Budget of Median Two-Income Family, 1997



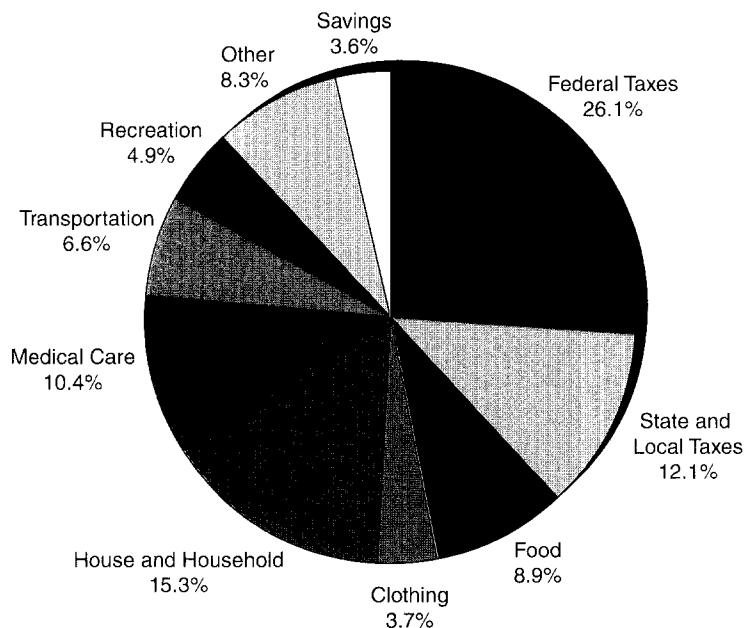
Source: Tax Foundation.

Figure 3
Representative Budget of Two-Income Family, 1957



Source: Tax Foundation.

Figure 4
Representative Budget of Two-Income Family, 1997



Source: Tax Foundation.

will most affect the median income family, such as the \$500-per-child tax credit and education tax incentives (primarily the HOPE Tax Credit), will take effect in the 1998 tax year.

Taxes and the Family Budget

Comparing *Figures 3* and *4*, one can see the growth of the tax burden as a percentage of the median family's budget. Both federal (primarily due to the increase in payroll taxes) and state taxes have grown as a share of the family budget since 1957.

Today, federal taxes dominate the budget of the American family. For a median two-income family, federal taxes alone will take the largest share of family income. Together, federal, state and local taxes (38.2 percent of family income) are approximately equivalent to what a family will spend on food, clothing, housing, household operations, and medical care combined (38.3 percent of family income).

Definitions, Assumptions and Methodology

The families represented in this study adhere to the Census Bureau's definition of a family: two or more people related by birth, marriage or adoption sharing a residence. The composition of families has change substantially since 1955. In 1955, 87 percent of families were married couples. In 1996, only 76 percent of families were married couples and fewer than half of these had children. The other families consist of male and female householders with no spouse present. In 1996, about 60 percent of these families had children.

Federal income taxes and payroll taxes are computed directly from family income. Families represented here are a weighted average of standard deduction filers and itemizers based on reported family income. Tax credits are accounted for in the analysis. In the computation of payroll taxes, it is assumed that wage income for a two-earner family represents 96 percent of its total income. For a single-earner family, wages are assumed to represent 97 percent of income.

The burden of other federal taxes (federal excise taxes, customs duties, the federal estate and gift taxes, federal corporate taxes) and state and local taxes (income, sales, excise, property and an array of miscellaneous fees and local levies) are calculated indirectly with formulas employing national averages. Average tax rates are derived by dividing the

revenue in question by net national product (gross domestic product less the depreciation of physical plant and equipment). These average tax rates are then applied to median family income to derive a dollar figure. Net national product is used to assure that all explicit and implicit forms of income are included in the derivation of average tax rates.

The Tax Foundation imputes the ultimate burden of all taxes paid by businesses to individuals. Economists generally agree that the burden of business taxation is ultimately passed along fully to individuals in one of three ways. First, businesses may attempt to pass the costs of taxation on to consumers by raising prices. Second, businesses may pass these costs to employees by paying them less than they would in the absence of the tax. Third, corporate shareholders may bear the burden through the realization of lower profits than they would realize in the absence of the tax.

The Tax Foundation employs its average-tax-rate method because it involves an equal weighting of the three alternatives. In addition, this method provides consistency across time.

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