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If Health Surtax Is 3 Percent, Taxpayers in 24 States Would Pay a Top Tax Rate Over 50%

By TF Staff

New taxes to fund the federal government's plan for higher health insurance spending continue to be debated in Washington. According to a Washington Post report released late Friday, tax writers at the House Ways and Means Committee have agreed to propose a three-tiered surtax aimed at high-income tax returns. The top surtax rate would be 3 percent and may apply to married couples and single filers as follows:

- * 1 percent surtax on AGI between \$350,000 and \$500,000 (singles between \$280,000 and \$400,000)
- * 1.5 percent surtax on AGI between \$500,000 and \$1,000,000 (singles between \$400,000 and \$800,000)
- * 3 percent surtax on AGI beyond \$1,000,000 (singles beyond \$800,000)

States have been raising taxes on this same group, leading to concern over how high the combined tax rates would be in each state, especially in the growing number of states with double-digit tax rates. Some commentators merely sum the rates at the federal, state and local level to give a statutory total tax rate. A more accurate method is to calculate the effective marginal tax rate, which takes into consideration deductions and adjustments.

In Table 1 below we present calculations of the effective marginal tax rate on top earners, assuming that the current state income tax rates remain through 2011, the top federal taxable income rate rises as scheduled to 39.6 percent, and a new 3 percent surtax on AGI earned at very high-income levels is imposed.

Table 1
Top Effective Marginal Rates under Proposed Health Care Surtax by State, Sorted by Combined Tax Rate in 2011

State	Top State Rate	Top Federal Ordinary Rate	New Surtax	Medicare Tax	Combined Top Rate
Oregon	11.00%	39.60%	3.00%	2.90%	55.18%
Hawaii	11.00%	39.60%	3.00%	2.90%	54.85%
New Jersey	10.75%	39.60%	3.00%	2.90%	54.71%
New York^	8.97%	39.60%	3.00%	2.90%	54.55%
California	10.55%	39.60%	3.00%	2.90%	54.44%
Rhode Island	9.90%	39.60%	3.00%	2.90%	53.85%
Vermont	9.40%	39.60%	3.00%	2.90%	53.40%
Maryland	6.25%	39.60%	3.00%	2.90%	53.25%
Minnesota	7.85%	39.60%	3.00%	2.90%	52.00%
Idaho	7.80%	39.60%	3.00%	2.90%	51.95%
North Carolina	7.75%	39.60%	3.00%	2.90%	51.91%
Wisconsin	7.75%	39.60%	3.00%	2.90%	51.91%
Ohio	5.93%	39.60%	3.00%	2.90%	51.90%
Delaware	6.95%	39.60%	3.00%	2.90%	51.33%
Arkansas	7.00%	39.60%	3.00%	2.90%	51.28%
South Carolina	7.00%	39.60%	3.00%	2.90%	51.23%
Maine	6.85%	39.60%	3.00%	2.90%	51.09%
Nebraska	6.84%	39.60%	3.00%	2.90%	51.08%
Kentucky	6.00%	39.60%	3.00%	2.90%	51.01%
West Virginia	6.50%	39.60%	3.00%	2.90%	50.77%
Kansas	6.45%	39.60%	3.00%	2.90%	50.73%
Missouri	6.00%	39.60%	3.00%	2.90%	50.43%
Georgia	6.00%	39.60%	3.00%	2.90%	50.32%
Virginia	5.75%	39.60%	3.00%	2.90%	50.09%
Oklahoma	5.50%	39.60%	3.00%	2.90%	49.87%
Massachusetts	5.30%	39.60%	3.00%	2.90%	49.69%
Iowa	8.98%	39.60%	3.00%	2.90%	49.47%
Connecticut	5.00%	39.60%	3.00%	2.90%	49.41%
Mississippi	5.00%	39.60%	3.00%	2.90%	49.41%
Utah	5.00%	39.60%	3.00%	2.90%	49.41%
New Mexico	4.90%	39.60%	3.00%	2.90%	49.32%
North Dakota	4.86%	39.60%	3.00%	2.90%	49.29%
Michigan	4.35%	39.60%	3.00%	2.90%	49.22%
Colorado	4.63%	39.60%	3.00%	2.90%	49.08%
Indiana	3.40%	39.60%	3.00%	2.90%	49.02%
Arizona	4.54%	39.60%	3.00%	2.90%	49.00%
Pennsylvania	3.07%	39.60%	3.00%	2.90%	48.80%
Montana	6.90%	39.60%	3.00%	2.90%	48.28%
Louisiana	6.00%	39.60%	3.00%	2.90%	47.83%
Illinois	3.00%	39.60%	3.00%	2.90%	47.60%
Alabama	5.00%	39.60%	3.00%	2.90%	47.43%

Alaska	0.00%	39.60%	3.00%	2.90%	44.88%
Florida	0.00%	39.60%	3.00%	2.90%	44.88%
Nevada	0.00%	39.60%	3.00%	2.90%	44.88%
New Hampshire	0.00%	39.60%	3.00%	2.90%	44.88%
South Dakota	0.00%	39.60%	3.00%	2.90%	44.88%
Tennessee	0.00%	39.60%	3.00%	2.90%	44.88%
Texas	0.00%	39.60%	3.00%	2.90%	44.88%
Washington	0.00%	39.60%	3.00%	2.90%	44.88%
Wyoming	0.00%	39.60%	3.00%	2.90%	44.88%
District	8.50%	39.60%	3.00%	2.90%	52.59%
New York City^	8.51%	39.60%	3.00%	2.90%	52.59%
Source: Tax Foundation calculations, State Individual Income Tax Rates					

Note: The rightmost column, Combined Top Rate, is the top effective marginal rate, taking into account deductions and adjustments, and therefore does not equal the sum of the first four rates.

Technical Notes

To calculate marginal effective tax rate, we add the weighted average of local tax rates in the state based upon 2009 State Business Climate Index (not shown in table) to top state tax rate and to the top federal rate as scheduled to be in effect in 2011 under current law and under Obama's budget (39.6 percent), plus a 3 percent surtax and the top Medicare tax rate for the self-employed. We allowed for a deduction of the state and local tax rate (20 percent thereof assuming limitation on itemized deduction returns and taxpayer is outside the phase-out range) and the adjustment allowed against income from 1/2 self-employment tax (on both state/local and federal returns). For those few states that allow federal deductibility at high income levels, such a deduction was included in the calculation as well. New York City's rate merely includes the state rate plus the city rate. Maine's scheduled top tax rate for 2011 (6.85%) is higher than its current rate (8.5%). Oregon's current 11 percent tax rate is technically temporary, and under a 9.9 percent rate (assuming the temporary hike expires), the state's top combined marginal rate would be 54.18, placing it fifth instead of tied for first.

The Washington Post article explicitly said that for singles the first surtax rate of 1 percent would kick-in for AGI beyond \$280,000, and thereby the AGI levels that we assume the 1.5 percent and 3 percent surtax rates kick-in at are assumed to be 80 percent (28/35) of the married level.

These are not the highest possible marginal tax rates that a taxpayer can face. At some income levels for different types of taxpayers, due to the phase-outs of various tax credits, exemptions or deductions, effective marginal tax rates can be extremely high. Also, if one wanted to include the fact that many low-income transfer programs are means-tested and have phase-out ranges (or in some cases mere cliffs), the marginal disincentive to work can be very high. For more on this issue, see [Kotlikoff and Rapson](#).

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