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Income Taxes: Who Pays and How Much?

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With the tax filing season in full swing, these summary figures may provide some perspective on the issue of who is paying federal individual income taxes and, more importantly, the relative shares paid by different groups of taxpayers. (Note that, because I do not include the impact of other taxes, such as payroll taxes, my discussion does not address the overall tax system.)

Federal tax receipts for 2003 totaled \$1.7 trillion, with the largest share (43 percent) coming from individual income taxes (IIT). As shown in the table, receipts from IIT totaled \$747.9 billion for 2003, the result of 128.6 million filed returns that reported total adjusted gross income (AGI) of \$6.3 trillion. Thus, the ratio of taxes to income, known as the total average tax rate, was 11.9 percent. Undertaking the same calculation for earlier years, one finds that the average tax rate for 2003 is the lowest rate for 1985–2003.

The table also provides data on the income tax burdens of specific groups. By ordering the returns based on AGI from highest to lowest, one can calculate useful income and tax information. Let's start with the top 50 percent and the bottom 50 percent: The former group accounted for 86 percent of AGI and paid more than 96.5 percent of IIT, while the latter group accounted for 14 percent of AGI and 3.5 percent of IIT. The average tax rate for the top 50 percent was 13.4 percent, while the rate for the bottom 50 percent was 3 percent. Both of these rates for 2003 are at their lowest levels for 1985–2003.

Next, let's look at groups in the top 50 percent. The top 25 percent accounted for 64.9 percent of AGI and paid 83.9 percent of IIT. Their tax rate was 15.4 percent. Meanwhile, the top 10 percent accounted for 42.4 percent of AGI and paid 65.8 percent of IIT. Their tax rate

was 18.5 percent. Comparing the top 25 percent with the top 10 percent, one sees that those with higher incomes pay higher average tax rates. This fact continues to hold as we examine those with even higher income, which is a characteristic of a progressive income tax system (i.e., the income tax rate increases as income increases). The top 5 percent accounted for 31.2 percent of AGI and paid 54.4 percent of IIT. Their tax rate was 20.7 percent. Finally, the top 1 percent accounted for 16.8 percent of AGI and paid 34.3 percent of IIT. Their tax rate was 24.3 percent, roughly eight times the average rate of the bottom 50 percent. The rate of 24.3 percent is approximately twice the average rate for all taxpayers, which is roughly the midpoint of the range of 1.8 to 2.3 based on annual calculations for 1985–2003.

Reaching political consensus on a tax system that simultaneously (i) provides desirable incentives to work, save, and invest; (ii) is viewed as fair; (iii) is easy to understand; and (iv) generates sufficient revenues to fund spending decisions has proven to be a major challenge in the United States.¹ One place to start the discussion is with some basic facts about the existing income tax system. ■

¹ For a discussion of reform options, see *Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System*, Report of the President's Advisory Panel on Federal Tax Reform, November 2005.

Federal Income Tax Burden by Income Group, 2003

Income group	Number of returns	AGI (\$ millions)	Income taxes paid (\$ millions)	Group's share of total AGI (%)	Group's share of income taxes (%)	Average tax rate (%)
All taxpayers	128,609,786	6,287,586	747,939	100.00	100.00	11.90
Top 1%	1,286,098	1,054,567	256,340	16.77	34.27	24.31
Top 5%	6,430,489	1,960,676	406,597	31.18	54.36	20.74
Top 10%	12,860,979	2,663,470	492,452	42.36	65.84	18.49
Top 25%	32,152,447	4,078,277	627,380	64.86	83.88	15.38
Top 50%	64,304,893	5,407,851	722,027	86.01	96.54	13.35
Bottom 50%	64,304,893	879,735	25,912	13.99	3.46	2.95

SOURCE: Internal Revenue Service, Individual Income Tax Returns with Positive Adjusted Gross Income (AGI), Tables 5 and 6; www.irs.gov/taxstats/indtaxstats/article/0,,id=133521,00.html.