



Tax Incidence Analysis: Shedding Light on Mississippi's Tax System

Tax Incidence or Distributional Analysis is an important tool that could enhance the current types of information available to evaluate tax policy decisions. Through Tax Incidence Analysis, policy makers receive annual or bi-annual updates on who incurs the burden of paying state and local taxes in relation to household income. Incidence analysis also allows states to estimate and report who will pay more or less by income as a result of a specific proposed tax change.

At least three states, Texas, Maine, and Minnesota require regular reviews of their tax systems that involve distributional analysis. In addition to the regular reviews, some states incorporate the analysis into evaluations of proposed revenue legislation. For example, in Texas, the legislative committees charged with making tax policy can request tax incidence analysis from the department of revenue on specific revenue bills to get an estimate on who will pay more or less by income as a result of the tax policy change prior to voting on a bill.

Benefits of Tax Incidence Analysis

- Provides members of the legislature with information to make more informed decisions about tax proposals.
- Provides a regular review of Mississippi's tax policies which will eventually allow the state to evaluate how tax burdens change over time.
- Allows citizens greater access to information about the implications of our tax system and tax proposals.

An Example of Tax Incidence Analysis

The following provides two examples of how tax incidence analysis provides valuable information on tax proposals. It shows how taxpayers at different income levels would be affected by two tax proposals: enactment of a state Earned Income Tax Credit and replacement of the current individual income tax with a flat income tax.

Tax Incidence Analysis of Selected Tax Reform Options in Mississippi

2007 Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%	Next 4%	Top 1%
Income	Less Than	\$13,400 –	\$24,100 –	\$39,700 –	\$68,100 –	\$130,000 –	\$312,100 –
Range	\$13,400	\$24,100	\$39,700	\$68,100	\$130,000	\$312,100	Or More
Average Income in Group	\$ 8,400	\$ 18,600	\$ 30,900	\$ 51,900	\$ 90,100	\$ 175,500	\$ 800,400

Create a refundable earned income tax credit equal to 10% of the federal credit

2007 Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%	Next 4%	Top 1%
Tax Change as % of Income	-1.0%	-0.7%	-0.2%	-0.1%	—	—	—
Average Tax Change	-84	-138	-68	-43	—	—	—
Share of Total Tax Change	25%	41%	21%	13%	—	—	—

Details

Average Tax Cut for Affected Taxpayers	-221	-306	-190	-293	—	—	—
% of Mississippians Affected	38%	45%	36%	15%	0%	0%	0%
% Mississippians with tax cut, total--27%							
Total State Tax Change--(\$84,000,000)							

Replace current rate structure with a single rate of 5% on income in excess of \$10,000

2007 Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%	Next 4%	Top 1%
Tax Change as % of Income	-0.1%	-0.7%	-0.8%	-0.7%	-0.6%	-0.3%	-0.1%
Average Tax Change	-7	-130	-259	-350	-523	-570	-548
Share of Total Tax Change	1%	10%	20%	27%	30%	9%	2%

Details

Average Tax Cut for Affected Taxpayers	-58	-214	-329	-476	-578	-661	-614
% of Mississippians Affected	12%	61%	79%	74%	90%	86%	89%
% Mississippians with tax cut, total--62%							
Total State Tax Change--(\$326,000,000)							

SOURCE: Institute on Taxation and Economic Policy, May 2008

Tax Incidence Analysis Example Interpretation – Earned Income Tax Credit

The following provides guidance on how to interpret the Tax Incidence Analysis Table for the Refundable Earned Income Tax Credit equal to 10% of the Federal Credit.

- Tax Change as a % of Income – this is the change in the tax burden for the group of taxpayers represented in the income bracket. For taxpayers earning between \$13,400 and \$24,100, the overall decrease in the tax burden for the entire group of taxpayers is 0.7%
- Average Tax Change – this is the average change for all taxpayers in that income group, regardless of eligibility for the tax change. For all taxpayers earning between \$13,400 and \$24,100, the average tax change is a reduction of \$138, even though some would not receive any tax change because they are not eligible and others would receive a tax change greater than \$138.
- Share of Total Tax Change –this provides a measure of the distribution of the total tax change. For example, 41% of the total tax change will be realized by people earning \$13,400 to \$24,100
- Average Tax Cut for Affected Taxpayers – this measure shows the average tax change for all tax payers who are eligible for the tax change and are earning a certain income. In the example above, the average tax reduction for taxpayers who are eligible for the EITC and earn between \$13,400 and \$24,100 is \$306. Some in that income group will receive a lower tax reduction, and some will receive a greater tax reduction.
- % of Mississippians affected –this the % of Mississippians in a given income group that would be affected by the tax change. For example, 45% of Mississippians earning between \$13,400 and \$24,100 will be affected by the tax change.