

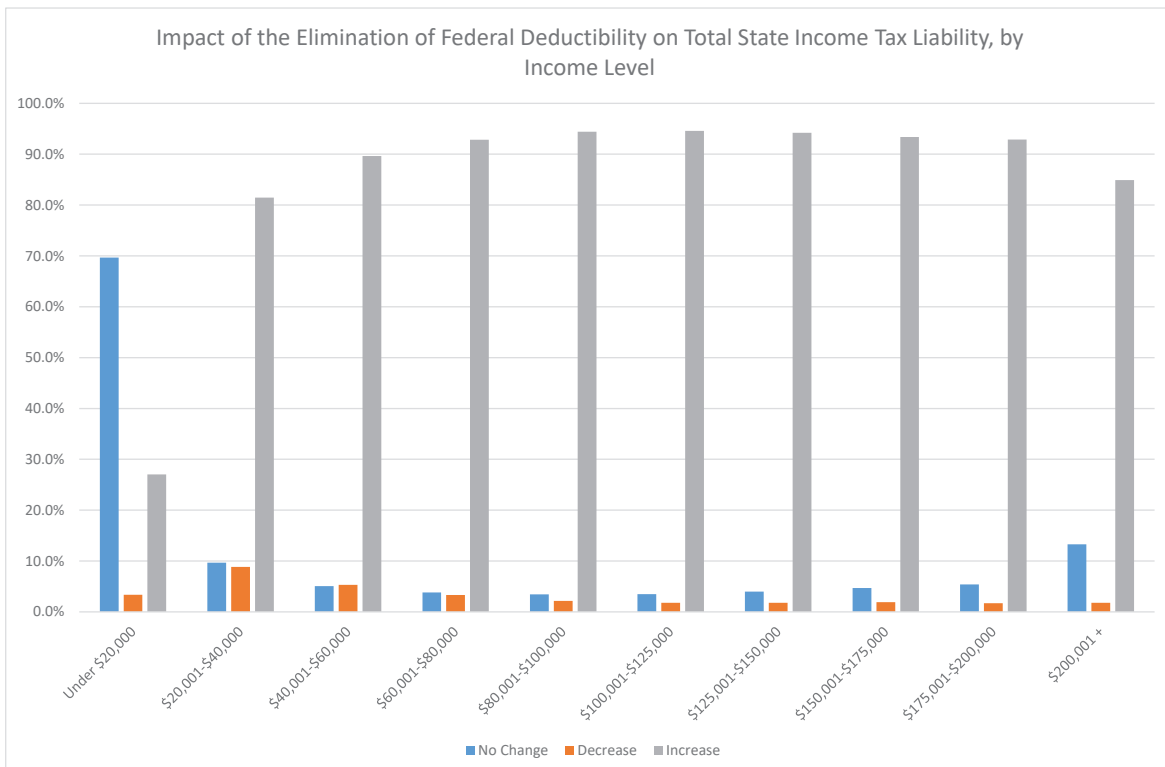
Federal Deductibility Benefits Low and Middle-Income Iowans

Discussions are underway to simplify Iowa’s income tax system, which is a worthy goal. However, decision-makers should keep in mind that the ability to deduct federal income taxes paid from Iowa income when filing state taxes benefits many low and middle income level workers in Iowa.

Federal deductibility is one of the largest tax deductions for many low to middle income Iowans, and if not the largest it is often the second-largest deduction for those who own a home and take the home mortgage deduction. However, unlike the home mortgage deduction, taxpayers do not have to itemize to take advantage of federal deductibility.

According to Iowa Department of Revenue data, Iowans saved \$845,046,557 they would have otherwise paid in state income taxes if federal deductibility were not an option for taxpayers in 2014, the latest data available.¹ Nearly 30 percent of the total change in tax liability that would occur with the elimination of federal deductibility would go to those Iowa families with an adjusted gross income (AGI) from \$1 to \$100,000, according to Public Interest Institute calculations. In other words, those taxpayers would be paying \$242,663,467 more in state income taxes if federal deductibility were eliminated, with no other tax code changes.

The Iowa Department of Revenue data shows the difference in tax liability of Iowa taxpayers if federal deductibility had been eliminated, using the 2014 tax data.² Overall, among all taxpayers, 68.7 percent would have seen tax liability increase, 4.5 percent would have seen a decrease, and 26.8 percent would have seen no change in tax liability. However, if you look at this data across income levels, 90 percent or more of taxpayers with AGI from \$40,001 to \$200,000 would see an increase in tax liability.



Looking further at the 68.7 percent of taxpayers with an increase in state income tax liability with the elimination of federal deductibility, the Iowa Department of Revenue has calculated the average increase in tax liability by income level.³

AGI	Average increase in tax liability
\$10,000 or less	\$18
\$10,001 to \$20,000	\$57
\$20,001 to \$30,000	\$125
\$30,001 to \$40,000	\$204
\$40,001 to \$50,000	\$287
\$50,001 to \$60,000	\$381
\$60,001 to \$70,000	\$460
\$70,001 to \$80,000	\$536
\$80,001 to \$90,000	\$634
\$90,001 to \$100,000	\$741

Eliminating federal deductibility, with no other tax code changes, would increase tax liability and take away one of the largest tax deductions now available for many low and middle-income taxpayers in Iowa.

Endnotes:

¹“Information Regarding the Impact of Federal Deductibility on Iowa Individual Income Taxpayers,” Iowa Department of Revenue, June 23, 2016, revised July 21, 2016.

² Ibid.

³ Ibid.