PA State-Local Taxes Moderately Regressive **IFO**

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As part of its statutory duties to "(p)rovide an analysis, including economic impact, of all tax and revenue proposals submitted by the Governor or the Office of the Budget," the Independent Fiscal Office (IFO) constructed a statewide tax incidence model that computes effective tax rates (ETRs) across six income groups. An ETR is the ratio of taxes paid to total income. The ETR metric can be used to assess the regressivity or progressivity of specific taxes and the overall state-local tax system. In a progressive (regressive) tax system, an ETR increases (decreases) with income level. See the methodology for technical explanations and a list of data sources used.

The table below displays results for taxes across six income groups for tax or calendar year 2022. Taxes included represent more than 95% of total state and local tax. Notable results include:

- The state and local income tax (30% of total tax) ETR increases significantly after the lowest income group, then largely flatlines. Despite the flat state statutory tax rate (3.07%), some progressivity occurs at the low end due to the exemption of retirement income and government benefits (e.g., SNAP, housing vouchers, refundable tax credits) and tax forgiveness for low-income filers.
- The property tax (28%) is regressive at the top end, a common result for tax incidence studies. The PTRR Program provides relief to the lowest-income group. The ETR only reflects homeowners and property tax passed through to renters. Property tax effectively paid by Pennsylvania landlords, consumers and owners/shareholders is included in All Other.
- The sales tax (19%) is regressive because high-income consumers save more of their income or use it to pay other local, state and federal taxes, which reduces after-tax income that can be spent.
- Miscellaneous consumption taxes (7%) are regressive due to tobacco taxes, and to a lesser extent, gasoline excise tax. Gaming taxes and net Lottery purchases (5%) are also regressive.
- While a small portion of total taxes, the inheritance tax (2%) adds significant progressivity to the system.
- All Other includes corporate net income, insurance premiums, and business property tax, which is passed through to consumers (prices), landlords (rent) or shareholders (returns). For those taxes, a significant portion is exported to other states and is not included in the analysis.
- The Total ETR is within 1 percentage point for the first three income groups, then declines for the next three groups.

Pennsylvania Effective Tax Rates by Income Level (2022)

| Income (000s) | | | | | Misc | Gaming | | All | |
Lower	Upper	Income	Property	Sales	Consum	Lottery	Inherit	Other	Total
$0	$50	2.1%	2.8%	3.1%	1.0%	0.7%	0.0%	0.9%	**10.7%**
$50	$100	3.1	2.5	2.1	0.8	0.8	0.0	0.7	**9.9**
$100	$200	3.3	2.8	1.8	0.8	0.6	0.0	0.8	**10.1**
$200	$500	3.6	2.7	1.4	0.5	0.4	0.2	0.8	**9.5**
$500	$1,000	3.6	1.7	1.0	0.5	0.2	0.4	1.0	**8.4**
$1,000	or more	3.3	0.6	0.7	0.1	0.1	1.0	1.1	**6.9**
All Income Groups		**3.1**	**2.3**	**1.8**	**0.7**	**0.5**	**0.2**	**0.8**	**9.5**

Notes: Income includes local income tax. Misc Consumption includes tobacco, alcohol, gasoline and gross receipts. All Other includes property tax passed through to landlords, consumers or shareholders, insurance premiums, corporate net income, vehicle registration fees and diesel fuel. Financial institution, realty transfer and local sales taxes excluded.

The second table displays the composition of income across the six groups, and provides insights into the ETR patterns from the first table. Notable results include:

- The lowest income group received a significant amount of exempt retirement income (pensions, Social Security) and government benefits income. Conversely, this group received little business (self-employment, partnership, S corporations), capital (dividends, interest, rent and royalties) and capital gains income.
- The exemption of retirement income from income tax increases the progressivity of the overall system. Retirement income is a much higher share of total income for lower-income residents.
- Wages comprised roughly two-thirds of total income for the next three income groups. The share of retirement income falls, and is replaced by business and capital income. The ETRs for these three groups are similar because most income is taxable, and property tax burdens largely reflect income levels (i.e., home values generally increase with income).
- For the two highest income groups, the share of business and capital income increases dramatically. For the top group above $1 million, capital gains comprised more than one-quarter of total realized income, while retirement income was modest (2%).
- Overall, wages and salaries comprised 58% of total Pennsylvania Cash Income. Retirement income was the next largest category at 17%, followed by business income (9%). See the methodology for a detailed description of Pennsylvania Cash Income components and data sources.

Income Composition by Income Level (2022)

Income (000s)		Wage-Salary	All Retire	Business Income	Capital Income	Capital Gains	Govt Benefit	Total
Lower	Upper							
$0	$50	50%	27%	3%	3%	1%	16%	**100%**
$50	$100	66	23	5	3	1	3	**100**
$100	$200	68	20	5	4	2	0	**100**
$200	$500	65	11	11	8	5	0	**100**
$500	$1,000	59	5	15	12	8	0	**100**
$1,000	or more	29	2	25	17	27	0	**100**
All Income Groups		**58**	**17**	**9**	**7**	**6**	**3**	**100**

Notes: All Retirement includes DB and DC pensions, Social Security and IRA withdrawals. Govt Benefit includes Supplemental Security Income, Social Security Disability, Veteran Benefits, SNAP, housing vouchers, unemployment compensation and refundable tax credits. Business Income includes self-employment, partnerships and S corporations. Capital Income includes dividends, interest, rents, royalties and estates.