

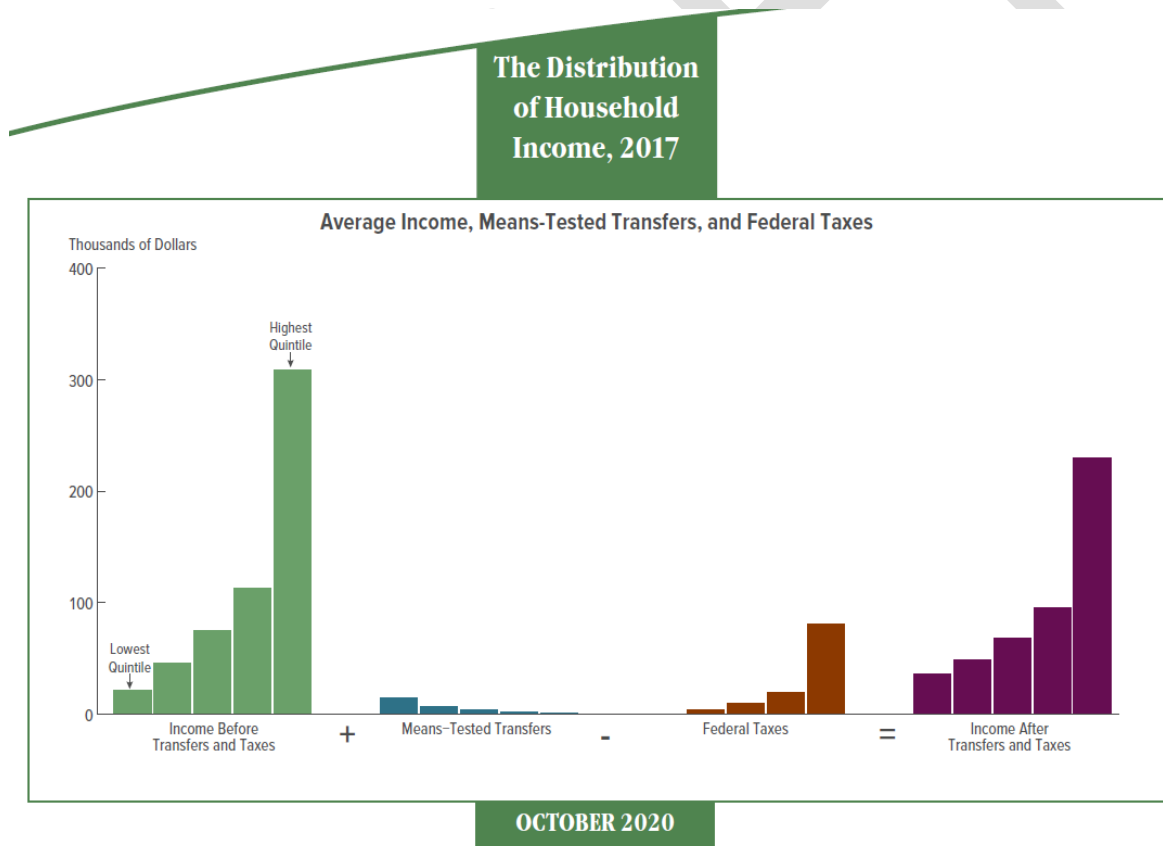
# Commissioner Brighton’s Draft on Incidence Study

Incidence Study--DRAFT

In order to understand the equity and progressivity of our tax structure, we recommend undertaking a comprehensive and ongoing study of income, taxes, and the various transfer payments and government benefit programs. This would help future legislatures look at changes over time, recommend adjustments, and measure progress.

The study would first divide households, adjusted by size, into deciles by market income. Next, it would compute transfer payments received by each of those deciles. Finally, it would compute taxes paid by each decile.

There are two approaches. The first would be based on state totals, similar in both methodology and assumptions to the national studies done by the Congressional Budget Office. The difference would be the addition of state taxes and state transfer programs.



A second approach may be considered in order to differentiate between types of households. This may be particularly important in shining a light on specific inconsistencies, such as different treatment for households with children or renters, or for determining if there are income levels at which there are

sudden increases in tax liabilities or decreases in transfer payments. In this approach, different family types are created with average or hypothetical characteristics, and the transfer payments and taxes paid are calculated based on those characteristics, showing the net resources available to the family type at different income levels.

The Legislature directs the Joint Fiscal Office to estimate the income needed to meet the basic needs of Vermont families.<sup>1</sup> The basic needs study, completed every other year, looks at six hypothetical family types:

- Single Person
- Single Person, Shared Housing
- Single Parent with One Child
- Single Parent with Two Children
- Two Adults with No Children – both wage earners
- Two Adults with Two Children – one wage earner
- Two Adults with Two Children – both wage earners

For each family type, the study estimates the cost of meeting its basic needs which include food, housing, transportation, child care, clothing and household expenses, telecommunications charges, health and dental care, renter's insurance, life insurance, and savings.<sup>2</sup>

A concurrent tax and transfer study could look at the ability of these same hypothetical family types, starting with a very low market income and moving up until they could meet their basic needs. It would illustrate points at which the families net worth decreases (aka benefit cliffs), and disclose exactly which taxes and transfers contribute to the problem.

As an example, the chart below is based on one of the families in the JFO Basic Needs Budget Report: one working parent with two children, aged four and six. The gross wages are on the horizontal axis. The net wages, after subtracting taxes, plus all state and federal benefits (including tax credits) make up the total net resources available to the family. It illustrates that there are points at which a family may earn more income and lose ground. The net wage increases steadily, but the combined decreases in tax credits and various benefits result in the family having fewer resources to make ends meet.

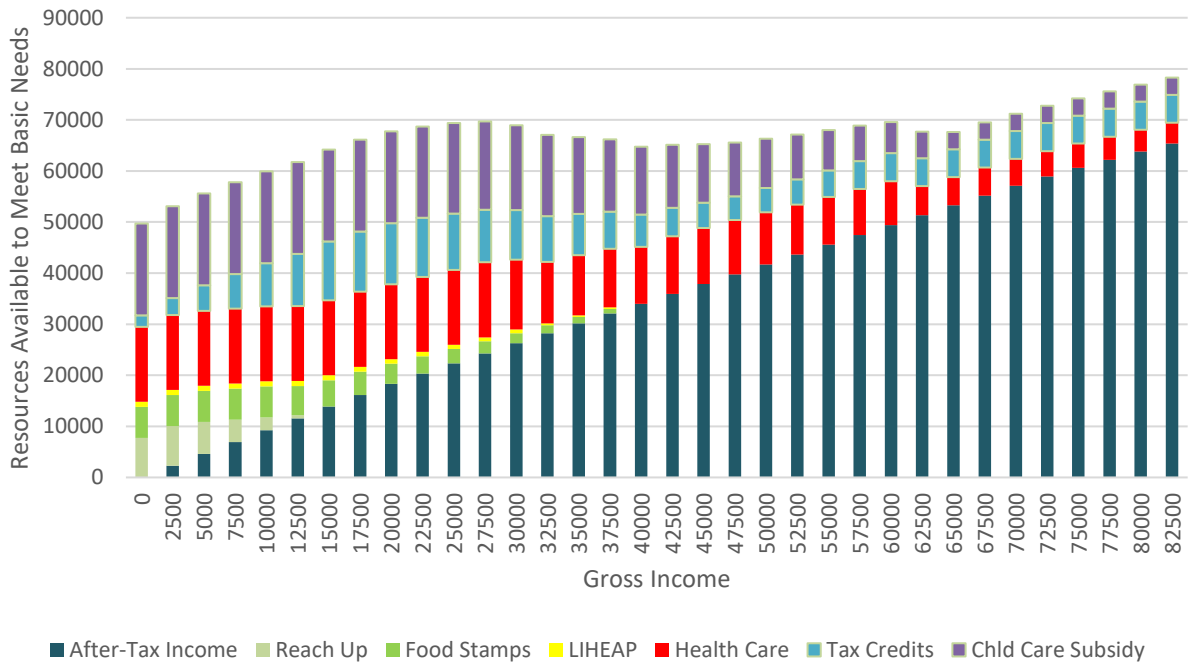
This dismays unsuspecting families, and discourages work for those in the know. It is the unintentional result of good intentions, but it needs a redesign. In addition to looking at each tax provision or transfer program in isolation, we need to look at the combined effect. In addition to looking at averages by income category, we need to look at different family types. In addition to looking at smoothly phasing out each benefit, we need to look at smoothly phasing in a family's ability to pay. We worry that a federal top-bracket income tax rate of 50% would be too high, with the assumption that it would discourage work. However, we effectively have created a marginal rate that is greater than 100% for some families who do not have enough income to meet their basic needs.

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<sup>1</sup> 2 V.S.A Section 505

<sup>2</sup> <https://ljfo.vermont.gov/assets/Subjects/Basic-Needs-Budgets/2c974b591b/2019-Basic-Needs-Budget-and-Livable-Wage-report-FINAL-1-15-2019-v2.pdf>

## Resources Available to Meet Basic Needs: Single Parent, 2 Children. 2019



Note: Child Care Subsidy includes the Pre-K voucher