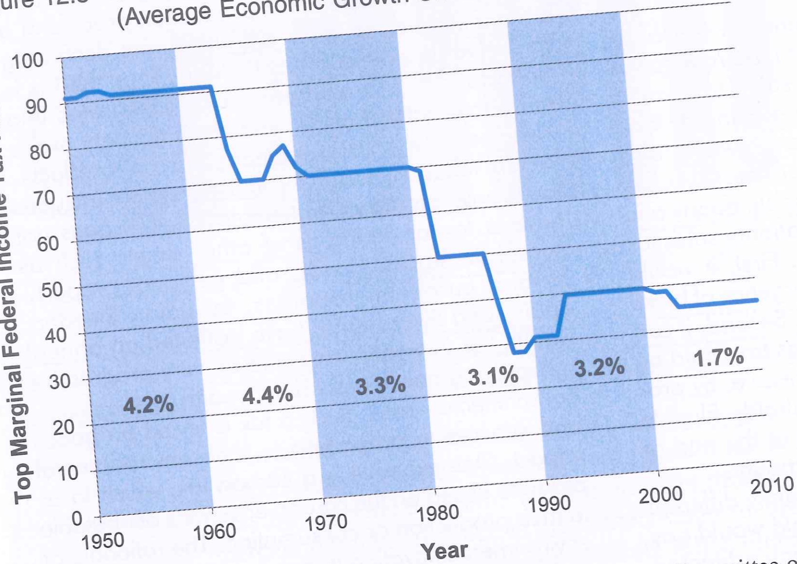
that the periods with the highest average growth rates, the 1950s and 1960s, were associated with the highest marginal tax rates. When the top marginal rate fell significantly in the 1980s, growth rates stayed about the same as they were in the 1970s. The top rate increased in the early 1990s, without a noticeable effect on average growth rates. It fell in the early 2000s, but that decade experienced the lowest overall growth rates.

Figure 12.8 **The Top Marginal Federal Tax Rate and Average Economic Growth, 1950–2010** (Average Economic Growth Shown by Decade as a Percentage)



The graph indicates that lowering the top marginal federal income tax rate does not seem to be correlated with higher economic growth.

Source: Sarah Anderson, "Full Testimony to the Senate Budget Committee on Inequality, Mobility, and Opportunity," Institute for Policy Studies, February 8, 2012.

The Distribution of Taxes

An often-quoted fact is that nearly half of Americans do not pay any federal income tax. Some people conclude that this implies that nearly half of Americans are not paying *any* taxes and thus are a drain on government resources who are not paying their fair share. But this represents an incomplete picture of who pays taxes. Of course, we have learned that the federal income tax is just one of the many taxes paid by Americans. In order to analyze the distribution of the tax burden accurately, we need to consider all taxes, not just focus on one specific tax.

Another important point is that we need to understand the difference between who actually pays a tax and who feels the burden of the tax. Let's take the Social Security tax as an example. On paper, both an employee and an employer pay half the tax. But are employers able to essentially pass on the burden of their share of the tax to employees by offering them lower wages? Another example is property taxes paid by landlords. Do landlords bear the burden of these taxes or are they able to pass them on to renters by charging higher rents than they would otherwise?

Economists rely upon **tax incidence analysis** to determine who bears the ultimate burden of a tax. Tax incidence analysis is:

tax incidence analysis: the study of who bears the ultimate burden of a tax

> the study of who bears the economic burden of a tax. More generally, it is the positive analysis of the impact of taxes on the distribution of welfare within a society. It begins with the very basic insight that the person who has the legal obligation to make a tax payment may not be the person whose welfare is reduced by the existence of the tax.[5]

Tax incidence analysis has produced some generally accepted conclusions regarding the burden of different taxes.

- Social insurance taxes, even though they are split evenly on paper, are borne almost entirely by employees. The reason is that an employer will pay a worker only the value of his or her marginal contribution to profits (recall our discussion from Chapter 10). As an employer's share of social insurance taxes reduces their profits, employers will accordingly reduce the amount of pay offered to employees.
- The burden of corporate taxes ultimately falls on real people. The general consensus is that the burden of corporate taxes falls primarily on owners of capital investments such as stocks and mutual funds.
- Excise taxes, though paid by manufacturers and retailers, are actually mostly paid by consumers based on their consumption patterns. In other words, businesses are generally able to pass on excise taxes to consumers. The reason is that most excises taxes are placed on goods with relatively inelastic demand curves.
- Property taxes paid by landlords are passed on to renters.

Based on research using tax incidence analysis, we can gain a complete picture of how taxes are distributed within a society. Table 12.4 provides an estimate of the U.S. tax burden in 2013 at different income levels.

We see that the overall U.S. tax system is progressive—meaning that tax rates tend to increase with increases in income. But, far from paying nothing in taxes, even those in the lowest income group pay nearly 20 percent of their income in taxes (even if they do not pay federal income tax) when we consider all taxes. Those in the middle-income group pay about 27 percent of their total income in taxes. After the middle-income group, average tax rates continue to rise, though rather modestly, especially for the top 20 percent.

Table 12.4 **The Distribution of Taxes in the United States, 2013**

Income group	Average income	Average total tax rate	Share of all taxes	Share of all income
Lowest 20%	$13,500	18.8%	2.1%	3.3%
Second 20%	$27,200	22.5%	5.1%	6.9%
Middle 20%	$43,600	26.6%	9.9%	11.2%
Fourth 20%	$71,600	29.8%	18.2%	18.4%
Next 10%	$109,000	31.4%	14.6%	14.0%
Next 5%	$154,000	32.0%	10.7%	10.1%
Next 4%	$268,000	32.2%	15.3%	14.3%
Top 1%	$1,462,000	33.0%	24.0%	21.9%

Source: Citizens for Tax Justice, "New Tax Laws in Effect in 2013 Have Modest Progressive Impact," April 2, 2013.

It is true that high-income earners bear a large share of the tax burden, but this must be assessed relative to their income. For example, those in the top 1 percent pay 24 percent of all taxes, but they also receive about 22 percent of all income. Combined, the top 20 percent pay 65 percent of all taxes and receive about 60 percent of all income. These figures indicate that the overall tax system is slightly, but not heavily, progressive.

Whether the current progressivity of the overall tax system in the United States is appropriate is, of course, a normative issue. According to a 2012 survey, 58 percent of Americans think that the "rich" pay too little in taxes, 26 percent say that the rich pay their fair share, and only 8 percent say that the rich pay too much.[6] Changes in tax policies can be used to change the overall progressivity of the tax system. Most tax policy debates emphasize the federal income tax. But considering that nearly half of Americans do not pay federal income taxes, reducing