THE FEDERAL

NEARLY a month after the federal fiscal year began, Congress and the President screened the final episode of the 1990 sequel to the Perils of Pauline. They snatched the fair maiden of federal programs from in front of the onrushing locomotive of the Gramm-Rudman-Hollings Line for the last time in 1990.

For most individual taxpayers, the 1990 tax bill made only small changes in the proportion of their incomes that will go to federal taxes. Changes average 0.6 percent of income or less for everybody with an income less than $200,000. The major change is for taxpayers in the $200,000-plus income brackets. Changing the famous "bubble" means that taxes for this group will rise by 1.6 percent of income. No longer will the rich pay a smaller percentage of their incomes than the near-rich.

The "bubble" wasn't eliminated, but it will be different. The exact provisions depend on some inflation calculations that haven't been made yet, but the outlines are clear. A new 31 percent marginal rate applies to income over $82,500 (for married taxpayers). Then taxpayers will lose three dollars of their itemized deductions for every $100 of income above $100 thousand, raising their rate to nearly 32 percent. Personal exemptions will begin to be phased out at $150 thousand for married taxpayers. The effect will be to raise the marginal rate by about half a percent for each personal exemption, so the size of the increase will vary with the size of the family. Payroll taxes for social security have raised effective rates in the lower brackets for many years, but one change in the 1990 Act will affect higher income taxpayers. The 1.45 percent tax for Medicare will now apply up to $125 thousand of wages (and at 2.9 percent to self-employment income). The graph of effective rates also reflects changes in taxes on beer, wine, liquor, tobacco and gasoline, as well as a number of other tax changes.

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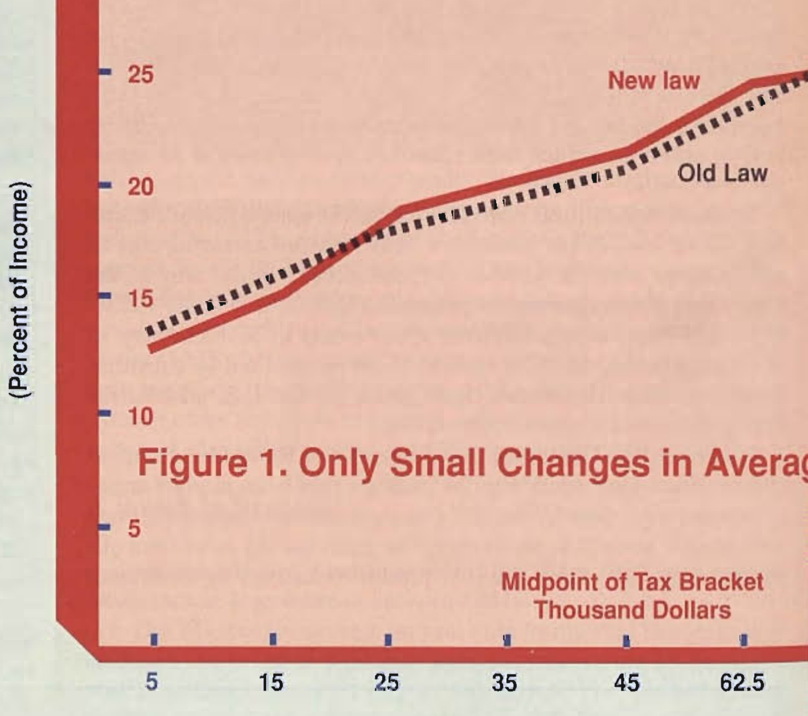

Figure 1. Only Small Changes in Averag

One fact that emerges from the discussion is startling. Roughly 45 percent of the increase in Federal tax revenues is estimated to come from the $200-thousand-and-over income group. Students of public finance have known for years that while rates on the poorest and richest taxpayers made most of the headlines, it was the middle-income taxpayers who produced most of the revenue. Not this time, apparently.

The second figure relates federal and state/local revenues (as shown in the national income accounts) to personal income. The data through 1989 are history; those for 1990 and beyond are estimates by the author, based on Administration projections used
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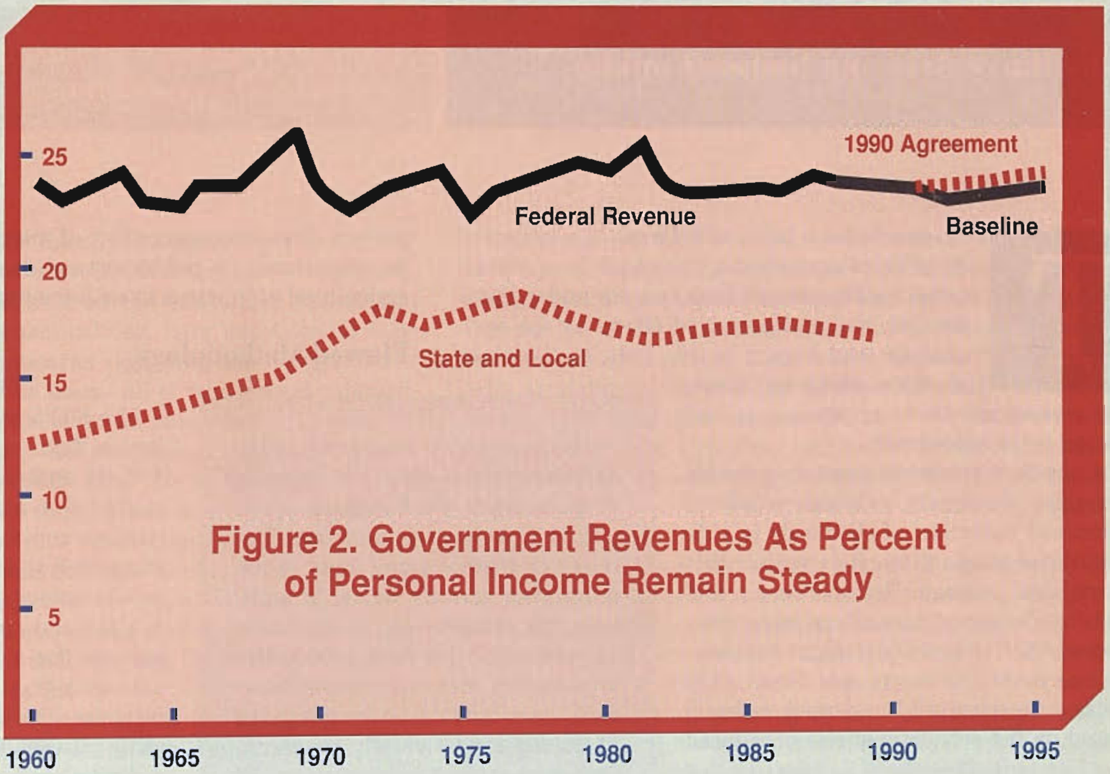

Figure 2. Government Revenues As Percent of Personal Income Remain Steady

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The $137 billion of new federal revenue expected over the 1991-95 period will add only about 0.5 percentage points to the total. The federal treasury will be richer, but even if the growth assumptions are too high (and many think they are), its impact on taxpayers, measured as a percent of personal income, is not likely to be much different from what it has been for years.

Pauline is alive, if not well, and the cost of her rescue does not seem to have been so much. Many, in fact, will hail the tax changes as improving vertical equity. Despite all the attention it attracted on television, this year's episode of Perils of Pauline is not likely to set new records when it is released to the corner video store.

Lest someone read more into Figure 1 than is there, remember that $87,500 is merely the midpoint of the $75,000 to $100,000 class. It is doubtful that average rates peaked exactly at $87,500 under the old law. Taxes include individual income taxes, payroll (social security) taxes, excise taxes and estate and gift taxes. Incomes are 1990, and include tax-exempt interest, nontaxable social security benefits and a variety of other adjustments to adjusted gross income. Source is Joint Committee on Taxation's JCX-46-90, October 26, 1990. Note that the horizontal scale of Figure 1 is not proportional.