

# SALT Deduction: Debunking the “Moocher State” and Cost-of-Living Justifications

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## KEY TAKEAWAYS

There is no inherent reason to allow taxpayers to deduct state and local taxes; so many rely on the myth of “moocher states” to justify the tax preference.

Lawmakers cannot simultaneously pursue a progressive tax code while denouncing the disparity in taxes paid by high-income states and low-income states.

The SALT deduction does not act as a cost-of-living adjustment to federal income taxes, and it would still not be justified if it did.

Since the 2017 tax reform bill capped state and local tax (SALT) deductions, legislators in high-tax states from New Jersey to Minnesota have ratcheted up rhetoric against supposed “moocher” states—states that critics claim do not carry their weight of the federal tax burden.<sup>1</sup> They argue that an increased or unlimited SALT deduction is necessary to reduce perceived imbalances between states.<sup>2</sup> Another common but dubious claim is that the SALT deduction improves the fairness of the tax code by mostly reducing the tax burden of individuals in high cost-of-living areas.<sup>3</sup>

Prior to the Tax Cuts and Jobs Act of 2017 (TCJA), individual taxpayers who itemized their tax returns could deduct an unlimited amount of state and local taxes from their federal taxable income.<sup>4</sup> TCJA placed a \$10,000 limitation on SALT deductions, though this

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provision is scheduled to expire in 2025, along with other reforms to the individual side of the tax code.<sup>5</sup> The Build Back Better Act, as passed by the House of Representatives, would raise the SALT deduction cap to \$80,000 through 2030,<sup>6</sup> a change that would benefit a small number of mostly high-income taxpayers.<sup>7</sup>

There was and continues to be a sound rationale for capping (or eliminating) the SALT deduction. The deduction is unwarranted because residents should benefit from the state and local government services their taxes fund.<sup>8</sup> Taxpayers cannot claim a deduction for private consumption, nor should they be able to deduct the cost of the services that they (or their elected representatives) choose to have provided by their state or local governments. Representative Dean Phillips (D–MN) inadvertently made this point while arguing for the SALT deduction: “Minnesota is a high-tax state and by investing in our communities we have made our state a national leader in health care provision, quality education, parks, safety, a strong economy, and so much more.”<sup>9</sup> The notion that the SALT deduction is then necessary to level the playing field between taxpayers in high-tax states and low-tax states implies that state governments are poor stewards of taxpayer dollars. The idea of making tax burdens fairer across states confuses the issue because it implicitly suggests that states pay federal taxes, when, in fact, only people pay taxes.

The federal government’s expansion into roles and powers that the Constitution leaves to the purview of the states naturally leads to disagreements about who should fund those activities. The solution to such disagreements is not to change the tax code to bring about regional equity. Instead, lawmakers should devolve federal programs back to the states so that a state’s taxpayers are responsible for funding their own programs.

Putting the notion of true federalism aside, advocates of a higher or unlimited SALT cap most often rely on two arguments for the tax preference, the “moocher state” argument and the cost-of-living argument. This *Backgrounders* describes these two arguments for an expanded SALT deduction and explains why they have no merit.

## The “Moocher State” Argument

The “moocher state” argument describes some states as net donors in the federal tax-and-spending system and others as net recipients—or, more bluntly, moochers. Proponents of this argument claim to want states’ balance of payments (outlays from the federal government to the state minus taxes and other payments to the federal government) to be more even. They claim that

TABLE 1

## 10 States with Highest SALT Deductions as a Percentage of Adjusted Gross Income (AGI)

SALT Rank	State	SALT Deduction, Percent of AGI	Top Income Tax Rate	Income Tax Rank	Property Tax Rank
1	New York	9.68%	8.82%	8	4
2	New Jersey	9.05%	8.97%	6	1
3	Connecticut	8.78%	6.99%	13	3
4	California	8.6%	13.3%	1	18
5	Maryland	7.95%	5.75%	24	17
6	Oregon	7.40%	9.9%	3	27
7	Minnesota	6.62%	9.85%	4	21
8	Massachusetts	6.6%	5.1%	28	6
9	Rhode Island	6.38%	5.99%	22	7
10	Wisconsin	5.88%	7.65%	9	19
<b>U.S. Average</b>		<b>5.63%</b>	<b>5.3%</b>		

**SOURCES:** Internal Revenue Service, “Tax Year 2017: Historic Table 2 (SOI Bulletin),” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022); Tax Foundation, “State Individual Income Tax Rates and Brackets for 2018,” March 5, 2018, <https://taxfoundation.org/state-individual-income-tax-rates-brackets-2018/> (accessed January 13, 2022); and Tax Foundation, “How Much Does Your State Collect in Property Taxes Per Capita?,” May 19, 2021, <https://taxfoundation.org/state-collect-property-taxes-per-capita-2021/> (accessed January 13, 2022).

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the states that have the most negative balance of payments (the donor states) are the high-tax states that benefit most from the SALT deduction.<sup>10</sup> Therefore, some see expansion of the SALT deduction as a fix for this perceived imbalance.<sup>11</sup>

This argument is correct in one regard. The SALT deduction does provide disproportionate benefit to taxpayers in a few high-tax states. New York, New Jersey, Connecticut, and California all rank among the top states in income tax rates and property taxes per capita. In 2017, the last year before the SALT deduction was capped:

- The average individual federal taxpayer claimed SALT deductions equal to 5.6 percent of adjusted gross income (AGI);
- New York taxpayers claimed SALT deductions equal to 9.7 percent of AGI (highest of 50 states);

CHART 1

## Total Federal State and Local Tax (SALT) Deductions Claimed

### Tax Year 2017

IN BILLIONS OF U.S. DOLLARS



### Tax Year 2018

IN BILLIONS OF U.S. DOLLARS



**NOTE:** SALT deductions as a percentage of adjusted gross income are based on author's calculations using IRS Statistics of Income data.

**SOURCES:** Internal Revenue Service, "Tax Year 2017: Historic Table 2 (SOI Bulletin)," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022), and Internal Revenue Service, "Tax Year 2018: Historic Table 2 (SOI Bulletin)," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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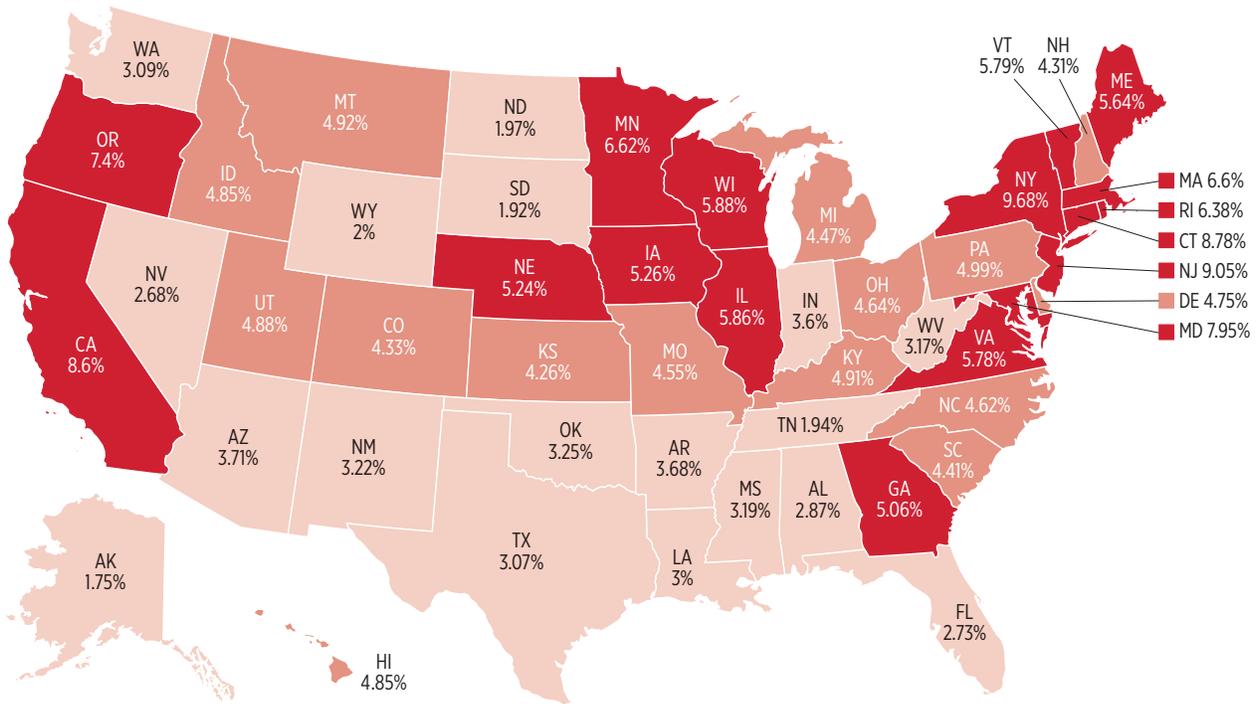
- New Jersey taxpayers claimed SALT deductions equal to 9.1 percent of AGI (second-highest);
- Connecticut taxpayers claimed SALT deductions equal to 8.8 percent of AGI (third-highest); and
- California taxpayers claimed SALT deductions equal to 8.6 percent (fourth-highest).<sup>12</sup>

On the other hand, taxpayers in eight of the nine states with no individual income tax claimed SALT deductions of less than 3.1 percent of AGI, ranking between 40th and 50th among the 50 states.<sup>13</sup>

MAP 1

## SALT Deduction as Percent of Adjusted Gross Income (AGI), by State

0%–3.99% 4%–4.99% 5%+



SOURCE: Internal Revenue Service, “Tax Year 2017: Historic Table 2 (SOI Bulletin),” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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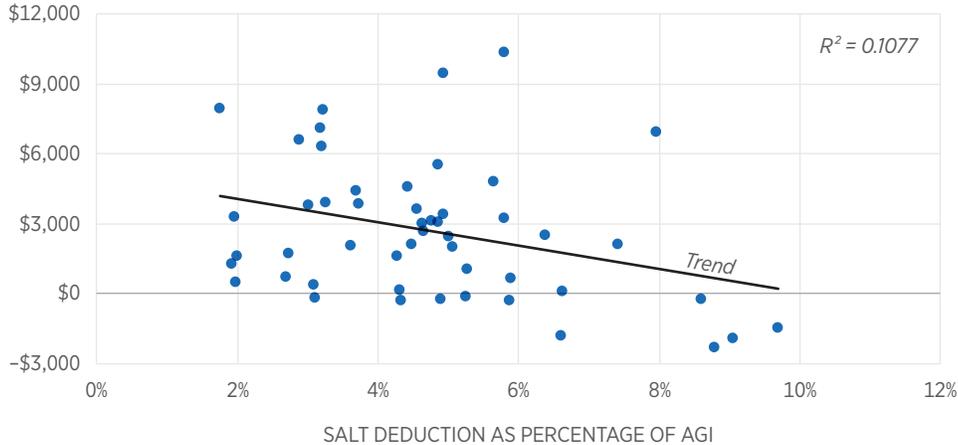
**The Basis for the “Moocher State” Argument.** Those making the “moocher state” argument often cite an annual report prepared by the Rockefeller Institute of Government.<sup>14</sup> This report uses broad definitions of both *revenues* and *expenditures* to estimate states’ balance of payments. It seeks to assign or allocate every dollar of federal budget expenditures in the following categories to a recipient state:<sup>15</sup>

- Wages to federal employees,
- Direct payments to individuals,
- Contracts for services and other procurement to the federal government, and

CHART 2

## SALT Deduction as Percentage of AGI Versus Per Capita Balance of Payments

PER CAPITA BALANCE OF PAYMENTS



**NOTE:** Each circle represents a state in the U.S.

**SOURCES:** Rockefeller Institute of Government, “Giving or Getting? New York’s Balance of Payments with the Federal Government,” <https://rockinst.org/issue-area/giving-getting-new-yorks-balance-payments-federal-government-2/> (accessed January 13, 2022), and Internal Revenue Service, “Tax Year 2017: Historic Table 2 (SOI Bulletin)” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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- Grants.<sup>16</sup>

The analysis—partially funded by New York taxpayers<sup>17</sup>—finds that “New York’s residents and businesses in 2019 sent \$22.8 billion more to the federal government than they got back in return—a shortfall larger than that of the second and third-ranked state combined.” The report shows some other high-tax states—such as Connecticut, New Jersey, and Massachusetts—among the states with the most negative balance of payments, but overall correlation between per-capita balance of payments and levels of state and local tax deductions claimed is relatively weak.<sup>18</sup>

Many of the factors that cause other states to receive a high, positive balance of payments from the federal government have nothing to do with the residents of those states freeloading off other states. The reality is far more nuanced than the notion that there are states that give and states that take.

**Federal Wages, Federal Contracts, and the Military.** The Rockefeller Institute report finds that from 2015 to 2019, Virginia was the largest net

recipient of federal dollars. The report's methodology records all wages and contracts paid by the federal government as adding to a state's balance of payments, so Virginia's huge federal workforce (due to its proximity to the nation's capital) causes the state to appear as a recipient of a disproportionate share of federal expenditures.<sup>19</sup> Although the report omits Washington, DC, from its analysis, based on the report's methodology, the District would undoubtedly rank as a bigger per-capita recipient of federal dollars than any U.S. state.<sup>20</sup>

The largest federal employer, by far, is the military. According to the Rockefeller Institute report, over 38 percent of federal government wages are for the military.<sup>21</sup> High levels of military wages contribute to some states with large military populations accumulating high, positive balances of payments, including Alaska (3rd), Hawaii (9th), and South Carolina (11th).<sup>22</sup> Of course, military personnel support the defense of the whole nation, not just the states where they are stationed. The concentration of military forces in Hawaii and Alaska, for example, is strategically motivated.<sup>23</sup> More servicemembers in a state certainly should not be construed as making it more of a moocher state.

**Social Security and Medicare Payments.** A larger factor determining states' balance of payments is the share of the state's residents that receive benefits from the federal government's two largest programs, Social Security and Medicare.<sup>24</sup> Based on the Rockefeller Institute report, of the \$2.56 trillion of federal direct payments to individuals in 2019, more than 70 percent were Social Security and Medicare outlays.<sup>25</sup> Since Social Security and Medicare comprise a large share of federal spending, states with more elderly residents tend to appear as net recipients of federal funds in the Rockefeller Institute report.

West Virginia (26.9 percent), Maine (26.3 percent), Vermont (25.0 percent), and Alabama (23.7 percent) rank as having the most Social Security beneficiaries per capita.<sup>26</sup> The Rockefeller Institute report ranks these states as having the 5th-, 10th-, 19th-, and 7th-highest per capita balance of payments, respectively.<sup>27</sup>

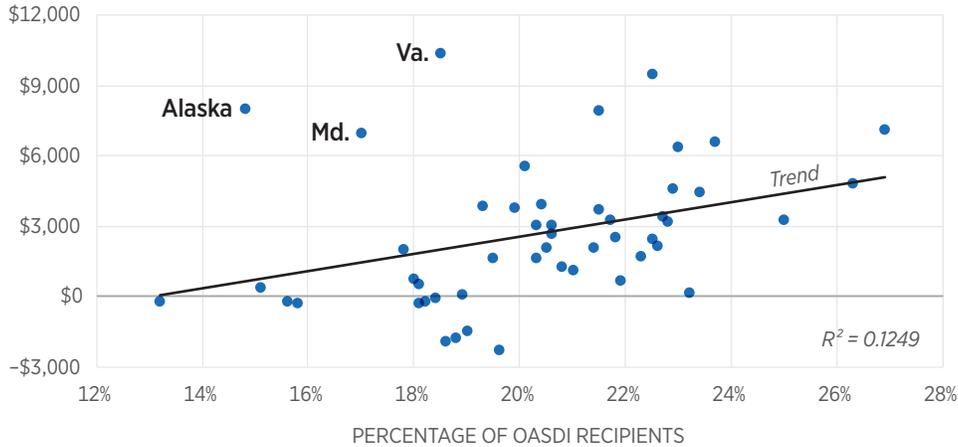
Meanwhile, Utah (13.2 percent), Alaska (14.8 percent), Texas (15.1 percent), and California (15.6 percent) have the smallest relative shares of Social Security beneficiaries.<sup>28</sup> The report ranks these younger states as having the 43rd-, 3rd-, 38th-, and 44th-highest balance of payments per capita.<sup>29</sup> (Alaska's large share of the armed services and federal research installations partially explains it being an outlier.)

The federal government does not pay Social Security and Medicare benefits to states; it pays these benefits to individuals based on their age and previous work history. If a California resident retires and moves to Maine, he receives the same benefits there that he would have in California.

CHART 3

## Per Capita Balance of Payments and Percentage of Social Security (OASDI) Beneficiaries

BALANCE OF PAYMENTS



**NOTE:** Each circle represents a state in the U.S.

**SOURCES:** Rockefeller Institute of Government, "Giving or Getting? New York's Balance of Payments with the Federal Government," <https://rockinst.org/issue-area/giving-getting-new-yorks-balance-payments-federal-government-2/> (accessed January 13, 2022), and Social Security Administration, "Beneficiaries as a Percentage of the Total Resident Population and of the Population Aged 65 or Older, by State, December 2020," [https://www.ssa.gov/policy/docs/statcomps/oasdi\\_sc/2020/table01.pdf](https://www.ssa.gov/policy/docs/statcomps/oasdi_sc/2020/table01.pdf) (accessed January 13, 2022).

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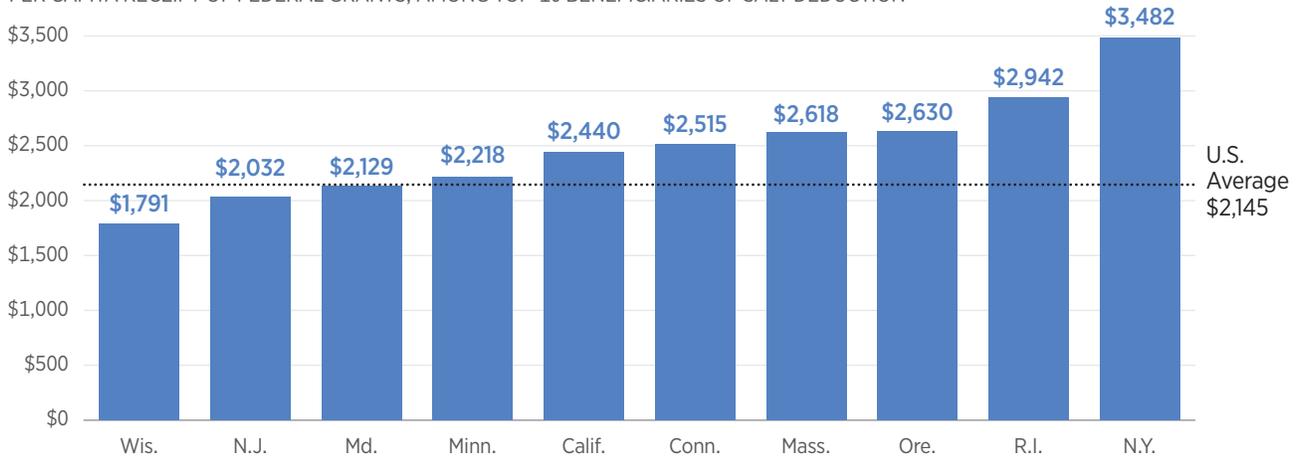
The fact that states such as Maine and West Virginia house a large share of retirees who are on Social Security makes those states appear as bigger net recipients, regardless of how much those retirees might have previously contributed to Social Security and federal income taxes.

**Grants.** The category of federal expenditures where benefits are most often state-specific is grants.<sup>30</sup> Federal grants include Medicaid services, transportation services, child nutrition programs, public housing and rental assistance, income security programs such as Temporary Assistance for Needy Families, and educational grants.<sup>31</sup> The Rockefeller Institute estimates that in 2019, New York received the fourth-highest level of grants per capita, at \$3,482 compared to a U.S. average of \$2,145. This hardly suggests that federal outlays shortchange New York.<sup>32</sup> Other high-tax states that benefit most from the SALT deduction receive federal grants at near the same rate or higher than the U.S. average, as shown in Chart 4.

CHART 4

## Per Capita Federal Grant Expenditures Received by High-Tax States

PER CAPITA RECEIPT OF FEDERAL GRANTS, AMONG TOP-10 BENEFICIARIES OF SALT DEDUCTION



**SOURCES:** Rockefeller Institute of Government, “Giving or Getting? New York’s Balance of Payments with the Federal Government,” <https://rockinst.org/issue-area/giving-getting-new-yorks-balance-payments-federal-government-2/> (accessed January 13, 2022), and Internal Revenue Service, “Tax Year 2017: Historic Table 2 (SOI Bulletin),” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

### The Inescapable Reality of a Highly Progressive Federal Tax Code.

People in states that pay more federal taxes per capita do claim SALT deductions at a somewhat higher rate, though the amount of SALT deductions does not cause such states to pay more federal taxes (technically the opposite is true). The key factor is the composition of the state, namely its concentration of high-income taxpayers. Because the SALT deduction disproportionately benefits the wealthy, states with more high-income residents also claim more SALT deductions. At the same time, states with more high-income residents also pay more federal taxes per capita.<sup>33</sup>

New York and other high-income states in the Northeast do tend to pay more federal taxes per capita—but not because they have high state and local taxes. They pay more federal taxes because they have a larger share of high-income individuals. This, of course, is the nature of a progressive tax system. Individuals and groups with higher incomes pay more in taxes not by accident but by design. The U.S. federal tax system is highly progressive. According to Congressional Budget Office data, the top 1 percent of taxpayers pay an average federal tax rate of 30 percent, while the poorest 20 percent of taxpayers pay an average federal tax rate of less than 0.1 percent.<sup>34</sup>

TABLE 2

## Per Capita Balance of Payments Calculations: U.S., New York, and New York with Shared Non-Grant Federal Spending

<b>Expenditures</b>	<b>U.S.</b> Billions of Dollars	<b>New York</b> Billions of Dollars	<b>New York, Assuming Shared Non-Grant Federal Spending</b> Billions of Dollars
Grants	\$2,145	\$3,482	\$3,482
Direct payments for individuals	\$7,672	\$7,419	\$7,672
Contracts and procurement	\$1,706	\$905	\$1,706
Wages	\$833	\$365	\$833
<b>Total Expenditures</b>	<b>\$12,356</b>	<b>\$12,171</b>	<b>\$13,693</b>
<b>Revenue</b>			
Individual income taxes	\$5,161	\$8,037	\$8,037
Employment taxes	\$3,739	\$4,012	\$4,012
Corporate income taxes	\$694	\$949	\$949
Excise taxes	\$300	\$250	\$250
Estate and gift taxes	\$50	\$95	\$95
<b>Total Revenue</b>	<b>\$9,944</b>	<b>\$13,343</b>	<b>\$13,343</b>
BALANCE OF PAYMENTS	\$2,412	-\$1,172	\$350
DIFFERENCE BETWEEN U.S. AND NEW YORK	\$3,584		\$2,062

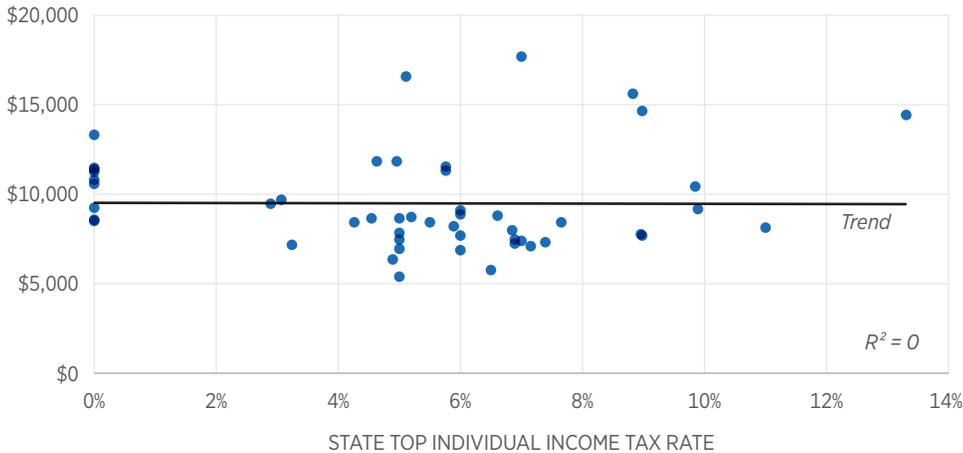
**SOURCE:** Rockefeller Institute of Government, “Giving or Getting? New York’s Balance of Payments with the Federal Government,” <https://rockinst.org/issue-area/giving-getting-new-yorks-balance-payments-federal-government-2/> (accessed January 13, 2022)

The amount of federal income taxes paid by states (per filing) does not increase with the state’s top statutory income tax rate. For example, the nine states with no income tax (on wages) would benefit least from a higher SALT deduction, yet they rank toward the top in federal income taxes per tax filing. Six of the no-income-tax states rank in the top 15 of federal income taxes per filing, and all nine rank in the top 30.<sup>35</sup> Since high-tax states do not generally pay more in federal taxes than low-tax states do, the case for the federal SALT deduction as a fix for “moocher states” is demonstrably false.

CHART 5

## Federal Income Tax Per Filing Versus Top State Income Tax Rate

2018 FEDERAL INCOME TAX LIABILITY PER INDIVIDUAL INCOME TAX FILING



**NOTES:** Federal income taxes per filing are based on author’s calculations using IRS Statistics of Income data. Each circle represents a state in the U.S.

**SOURCES:** Internal Revenue Service, “Tax Year 2018: Historic Table 2 (SOI Bulletin),” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022), and Tax Foundation, “State Individual Income Tax Rates and Brackets for 2018,” March 5, 2018, <https://taxfoundation.org/state-individual-income-tax-rates-brackets-2018/> (accessed January 13, 2022).

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If one aims to equalize the average federal taxes paid by residents of different states, changing the SALT deduction would not be a particularly good way to do so. Any other features of the tax code that disproportionately affect the wealthy could be changed instead. For example, the alternative minimum tax (AMT) mostly hits individual taxpayers with incomes greater than \$200,000. A state’s AMT paid as a percentage of AGI is more strongly correlated with federal taxes paid per filing (or balance of payments) than the SALT deduction is.<sup>36</sup> Eliminating the AMT would reduce disparities in the total taxes per filer across states, and it would simplify the tax code without giving special advantages to states adopting particular tax policies.

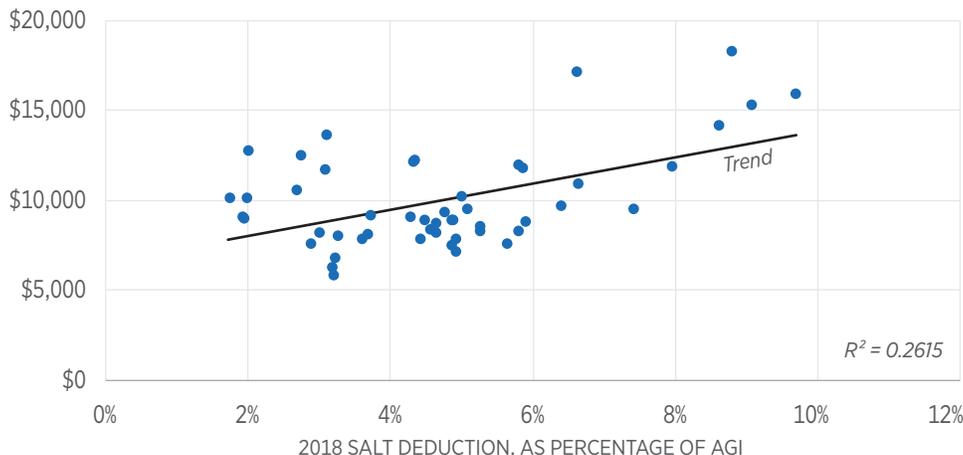
## The Flawed Cost-of-Living Argument

The other common indirect argument used to justify the SALT deduction is that the deduction accounts for differences in cost of living. One’s

CHART 6

## Federal Income Taxes Per Filing and SALT Deduction as Percent of AGI

2018 FEDERAL TAXES PER CAPITA



**NOTES:** SALT deductions as a percentage of adjusted gross income and federal income taxes per tax filing are based on author's calculations using IRS Statistics of Income data. Each circle represents a state in the U.S.

**SOURCE:** Internal Revenue Service, "Tax Year 2018: Historic Table 2 (SOI Bulletin)," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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paycheck does not go as far in New York City or the California coast as in the rest of the country, so some argue that taxpayers there end up paying more taxes than their cost-adjusted income warrants. The SALT deduction, they argue, acts like a cost-of-living-adjustment, because taxpayers in California and New York disproportionately benefit from the SALT deduction.<sup>37</sup>

**State and Local Taxes, Public Amenities, and Cost-of-Living Differences.** It is, of course, true that the cost of living is significantly higher in certain parts of the country. Cost-of-living differences in some cases reflect differences in tax rates, so, unsurprisingly, there is some correlation between an area's price levels and the amount of SALT deductions. Higher state taxes, of course, indicate higher levels of state government services. To the extent state taxes cause cost-of-living differences, the taxpayers in more expensive states already receive the benefits of those services (assuming a well-run state government). A federal SALT deduction in that case simply rewards consumption of state-government-provided services over the consumption of

CHART 7

## Federal Taxes Paid Per Filing and Individual Alternative Minimum Tax (AMT) as Percent of AGI

2018 FEDERAL TAXES PER FILING



**NOTES:** SALT deductions as a percentage of adjusted gross income and federal income taxes per tax filing are based on author's calculations using IRS Statistics of Income data. Each circle represents a state in the U.S.

**SOURCE:** Internal Revenue Service, "Tax Year 2017: Historic Table 2 (SOI Bulletin)," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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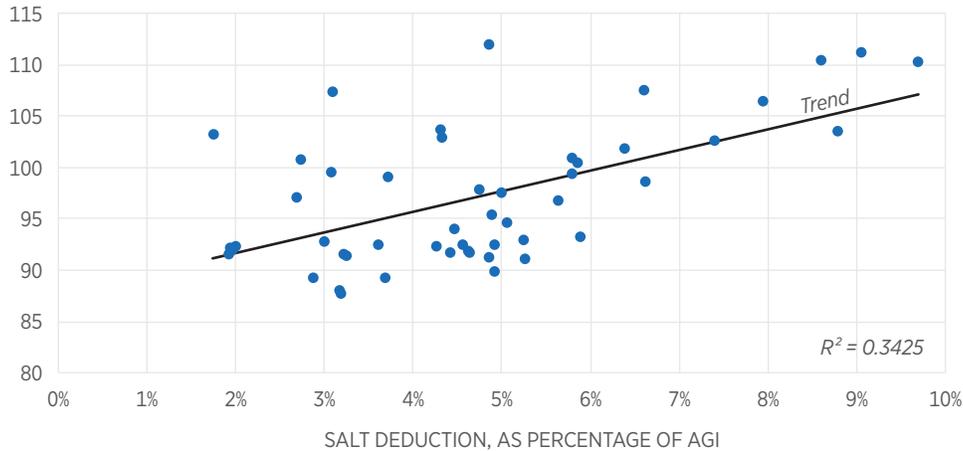
private-sector goods and services. Here, the SALT deduction does not fix a disparity in the tax code; it creates one.

**Natural Amenities and Cost-of-Living Differences.** Even though taxes can directly cause higher prices in an area, the connection between high taxes and high cost of living goes only so far. For example, housing—by far the most important factor in cost of living—is generally more expensive in the Mountain West region than in states bordering the Great Lakes, even though SALT-deductible taxes tend to be lower in the Mountain West.<sup>38</sup> The median housing value averaged about \$192,000 between 2015 and 2019 in the eight states bordering the Great Lakes—Illinois, Indiana, Michigan, Minnesota, New York, Ohio, Pennsylvania, and Wisconsin<sup>39</sup> (about \$175,000 if New York is excluded). The eight states in the Mountain West region—Arizona, Colorado, Idaho, Montana, Nevada, New Mexico, Utah, and Wyoming—averaged a \$244,000 median home value between 2015 and 2019.<sup>40</sup> While the Mountain West states averaged more than 30 percent higher housing values, in 2017

CHART 8

## State Price Level and SALT Deduction as Percent of AGI

STATE PRICE LEVEL



**NOTE:** Each circle represents a state in the U.S.

**SOURCES:** Bureau of Economic Analysis, “Regional Price Parities by State and Metropolitan Area,”

[https://apps.bea.gov/iTable/drilldown.cfm?reqid=70&stepnum=40&Major\\_Area=3&State=0&Area=XX&TableId=101&Statistic=1&Year=2020&YearBegin=-1&Year\\_End=-1&Unit\\_Of\\_Measure=Levels&Rank=1&Drill=1&nRange=5](https://apps.bea.gov/iTable/drilldown.cfm?reqid=70&stepnum=40&Major_Area=3&State=0&Area=XX&TableId=101&Statistic=1&Year=2020&YearBegin=-1&Year_End=-1&Unit_Of_Measure=Levels&Rank=1&Drill=1&nRange=5) (accessed January 13, 2022), and Internal Revenue Service, “Tax Year 2017: Historic Table 2 (SOI Bulletin),” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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they averaged more than 30 percent less in SALT deductions (3.82 percent versus 5.72 percent).<sup>41</sup>

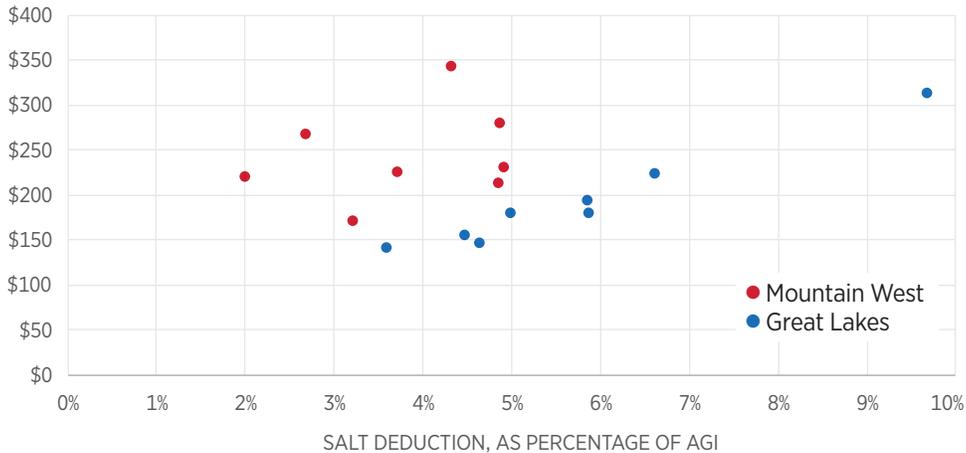
Differences in natural amenities—and perhaps to a lesser extent differences in weather—are likely part of the reason for the higher cost of living in the Mountain West than in states bordering the Great Lakes.<sup>42</sup> On the one hand, homebuyers, on average, are willing to pay more to have scenic natural views and access to outdoor activities that the Mountain West states offer. This tends to drive up housing demand relative to supply, resulting in higher housing prices. At the same time, there are constraints on housing supply in the Mountain West, including difficulties of building in mountainous terrain and the vast swaths of land owned by the federal government.<sup>43</sup>

**The SALT Deduction: A Bad Proxy for Cost of Living.** If the SALT deduction were expanded as a quasi-cost-of-living adjustment, the federal tax code would exacerbate such differences between Mountain West states and states bordering the Great Lakes. Residents of the Great Lakes

CHART 9

## Housing Value and SALT Deduction: Mountain West vs. Great Lakes

HOUSING VALUE, IN THOUSANDS OF U.S. DOLLARS



**NOTE:** The eight mountain west states are Arizona, Colorado, Idaho, Montana, Nevada, New Mexico, Utah, and Wyoming. The eight states bordering the Great Lakes are Illinois, Indiana, Michigan, Minnesota, New York, Ohio, Pennsylvania, and Wisconsin.

**SOURCES:** U.S. Census Bureau, "American Community Survey 2015-2019, Selected Housing Characteristics," [https://data.census.gov/cedsci/table?q=housing%20value%20by%20state&g=0100000US,%240400000\\_0400000US01,02,04,05,06,08,09,10,11,12,13,15,16,17,18,19,20,21,22,23,24,25,26,27,28,29,30,31,32,33,34,35,36,37,38,39,40,41,42,44,45,46,47,48,49,50,51,53,54,55,56&tid=ACSDT5YAIAN2010.B25080](https://data.census.gov/cedsci/table?q=housing%20value%20by%20state&g=0100000US,%240400000_0400000US01,02,04,05,06,08,09,10,11,12,13,15,16,17,18,19,20,21,22,23,24,25,26,27,28,29,30,31,32,33,34,35,36,37,38,39,40,41,42,44,45,46,47,48,49,50,51,53,54,55,56&tid=ACSDT5YAIAN2010.B25080) (accessed January 13, 2021), and Internal Revenue Service, "Tax Year 2017: Historic Table 2 (SOI Bulletin)," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed January 13, 2022).

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states would benefit more from the SALT deduction despite living in a more affordable region.

Average cost of living also varies wildly within states, so many residents of high cost-of-living states face low prices in the cities or towns where they live.<sup>44</sup> Likewise, some residents of low cost-of-living states may face high local prices. Housing in Miami, Florida, for example, is almost twice as expensive as in Buffalo, New York.<sup>45</sup> However, a Buffalonian could deduct more state and local taxes than a Miamian with the same income.<sup>46</sup>

The point here is not that there is a negative relationship between state taxes and cost of living. The point is that the SALT deduction is a very blunt tool to adjust for cost-of-living differences. Furthermore, to the extent the causation is reversed (a higher SALT deduction leading to higher cost of living), it indicates that the high-tax-state residents already receive the

corresponding benefit of higher state government spending and should not require an additional federal tax deduction.

**Would a Cost-of-Living Adjustment Be a Good Thing?** As alluded to above, a portion of cost-of-living differences between areas reflects differences in amenities, whether those are government-provided or natural amenities. Part of the reason that it is more expensive to buy or rent a home in Hawaii or California is that many Americans prefer warm weather and sandy beaches, and only a small portion of the United States (by area) offers those amenities. Some will pay a premium to live near the beach, while others might opt for a lower cost of living with fewer amenities.<sup>47</sup> The tax code should not give a special preference to taxpayers that pay more to live in an area with abundant natural amenities.

Differences in cost of living are a valuable market signal, so even if the SALT deduction were a perfect cost-of-living adjustment, it would still be undesirable. A high cost of living in an area indicates that the supply of housing (or some other product) is struggling to meet demand.<sup>48</sup> When potential homebuyers or renters see the high cost of living of an area, some will be dissuaded from moving there and further straining the area's limited resources. If the tax code provides a tax break for living in high cost-of-living areas, this pushes more people into those areas and puts more strain on stretched housing markets, only further driving up prices.

## Recommendations to Reduce Regional Bias in the Federal Budget

Instead of raising the SALT deduction cap, Congress should consider the following solutions, which would reduce any regional bias in the federal budget:

- **Eliminate the SALT deduction and other unwarranted tax preferences.** The SALT deduction is a subsidy for high-tax states and states that rely more heavily on the income tax.<sup>49</sup> Ending the SALT deduction would put pressure on states to reduce spending and taxes. This would help ensure that state governments only spend on programs and projects when the benefits to their residents outweigh the true costs. The SALT deduction should be eliminated altogether, along with the wide range of energy tax credits, housing credits, and place-based credits such as opportunity zones.<sup>50</sup> Most tax preferences in the tax code are economically unwarranted.<sup>51</sup>

- **Reject future state bailouts.** The 2021 American Rescue Plan included over \$300 billion of funding for state and local governments, ostensibly to allow them to respond to the COVID-19 pandemic, despite little actual drop in state tax revenue during the pandemic.<sup>52</sup> The formula used to determine each state's allocation was based on its unemployment rate during the fourth quarter of 2020.<sup>53</sup> This had the effect of rewarding states for choosing to prolong economic lockdowns and extend generous unemployment benefits. The federal government should not protect state and local governments from their own fiscal and economic decisions.<sup>54</sup>
- **Reduce non-defense federal spending and devolve more governance to the states.** The federal government should have little power to redistribute resources in the first place, but as the federal government has encroached more and more on states' rights, federal government redistribution has become commonplace.<sup>55</sup> Prior to World War II, state and local governments accounted for most government spending in the United States.<sup>56</sup> Until the expansion of the welfare state that took place under President Lyndon Johnson's Great Society, most federal spending was defense related.<sup>57</sup> Moving back toward a limited scope for the federal government would reduce redistribution among individuals in different states, which would in turn reduce disagreements among states about the distributive impacts of federal taxation and spending.

## Conclusion

The fact that certain high-tax states stand to benefit disproportionately from a SALT deduction expansion has led to region-based justifications for the deduction. Region-based justifications for the SALT deduction fall apart on closer inspection. The United States does not break down neatly into donor states and recipient states. Americans in high-tax states do not carry the federal fiscal burdens of other Americans. High-income *individuals* do pay a disproportionate share of the federal tax burden and claim more SALT deductions—but this is true regardless of whether they live in high- or low-tax states, and it is an intended result of a highly progressive federal tax code.

High state taxes (and regulations) can directly lead to higher cost of living, though this does not justify a SALT deduction, because state taxes fund public amenities that are meant to benefit a state's residents. If certain states want to provide tax relief to high-income residents, they should do so by making their own tax codes less progressive instead of pushing those burdens onto other federal taxpayers.

In other cases, differences in natural amenities drive cost-of-living differences. However, supply-and-demand forces dictate such cost-of-living differences, so it is unclear why the tax code should be used to alleviate these differences. With no valid justification for its existence, the SALT deduction is a solution in search of a problem.

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## Endnotes

1. Representative Josh Gottheimer (D-NJ) celebrated the House of Representatives' November 2021 passage of an increase in the SALT deduction cap (as part of the Build Back Better Act still under consideration in the Senate) by stating, "Thanks to this bill, we scored a big round against the Moocher States and we will cut taxes for families across New Jersey's Fifth District." News release, "Statement: After Years-Long Fight, Gottheimer Passes Legislation to Reinstate SALT," November 19, 2021, <https://gottheimer.house.gov/news/documentsingle.aspx?DocumentID=2816> (accessed December 15, 2021). In 2017, Representatives Gottheimer and Leonard Lance (D-NJ) introduced H.R. 4161, which they referred to as the Anti-Moocher Bill. The bill would have entitled federal taxpayers to a tax credit if they lived in states whose federal taxes exceeded the federal outlays received by the state. See news release, "Gottheimer, Lance Announce 'Anti-Moocher Bill' to Claw Back Tax Dollars," October 26, 2017, <https://gottheimer.house.gov/news/documentsingle.aspx?DocumentID=384/> (accessed December 15, 2021).
2. See, for example, Representative Dean Phillips's (D-MN) news release in which he "reiterated his strong opposition to the \$10,000 cap on the SALT deduction, which disproportionately impacts states like Minnesota that contribute more than they receive in federal aid." News release, "Phillips Decries Moocher States, Calls for More Investment in Minnesota," April 16, 2021, <https://phillips.house.gov/media/press-releases/phillips-decries-moocher-states-calls-more-investment-minnesota/> (accessed December 15, 2021).
3. See, for example, news release, "Bipartisan Legislation to Fully Restore the SALT Deduction Introduced in House of Representatives," Representative Thomas Suozzi (D-NY), January 29, 2021, <https://suozzi.house.gov/media/press-releases/bipartisan-legislation-fully-restore-salt-deduction-introduced-house/> (accessed December 15, 2021).
4. By far the two largest taxes deducted under the SALT deduction are state and local income taxes and property taxes. Taxpayers can also elect to deduct sales taxes in lieu of income taxes.
5. Adam N. Michel, "The Tax Cuts and Jobs Act: 12 Myths Debunked," Heritage Foundation *Backgrounders* No. 3600, March 23, 2021, <https://www.heritage.org/taxes/report/the-tax-cuts-and-jobs-act-12-myths-debunked/>.
6. The Build Back Better Act only temporarily raises the SALT deduction cap to \$80,000. In 2031, the cap would revert to \$10,000, whereas under current law the SALT deduction cap would expire after 2025 (reverting to no SALT deduction whatsoever). The back-end revenues that the Build Back Better Act gains from lowering the SALT cap in 2031 offset some of the deficits the act creates in the initial four-year period. There is no plausible economic rationale to justify why the SALT deduction should be lowered, then raised, then lowered again.
7. The TCJA also doubled the standard deduction, which now stands at \$25,100 in 2021 for a married tax filer. With the higher standard deduction, typically only high-income earners have SALT and other deductions that exceed \$25,100, so the SALT deduction limitation is non-binding for most taxpayers, except high-income earners. See Preston Brashers, "4 Problems with Left's Hypocritical Plan to Give Wealthy Constituents a Bigger SALT Deduction," *The Daily Signal*, December 3, 2021, <https://www.dailysignal.com/2021/12/03/four-problems-with-the-lefts-hypocritical-plan-to-give-wealthy-constituents-a-bigger-salt-deduction/>.
8. Rachel Greszler, Kevin Dayaratna, and Michael Sargent, "Why Tax Reform Should Eliminate State and Local Tax Deductions," Heritage Foundation *Backgrounders* No. 3256, October 16, 2017, <https://www.heritage.org/taxes/report/why-tax-reform-should-eliminate-state-and-local-tax-deductions/>.
9. Phillips, "Phillips Decries Moocher States."
10. See, for example, Stephen Ohlemacher, "AP Fact Check: Blue High-Tax States Fund Red Low-Tax States," Associated Press, December 9, 2017, <https://apnews.com/article/north-america-business-local-taxes-ap-top-news-politics-2f83c72de1bd440d92cdbc0d3b6bc08c> (accessed December 21, 2021).
11. There are two ways to change the tax system to reduce such imbalances between states. First, one could make the federal tax code less progressive. At the extreme, one could impose a head tax, requiring all individuals to pay the same amount in tax, regardless of their means. The only imbalances left would relate to differences in the distribution of federal expenditures. A second way to reduce imbalances between the states is to reduce the role of the federal government and devolve more powers to the states. If the federal government only collected taxes to support its necessary, constitutional functions, states would be more autonomous.
12. Author's calculations based on IRS Statistics of Income Table 2, "Individual Income and Tax Data, by State and Adjusted Gross Income, Tax Year 2017," <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed December 15, 2021).
13. *Ibid.*
14. Laura Schultz, "Giving or Getting? New York's Balance of Payments with the Federal Government: 2021 Report," Rockefeller Institute of Government, January 2021, <https://rockinst.org/wp-content/uploads/2021/01/2021-Balance-of-Payments-Report-web.pdf> (accessed December 16, 2021).
15. "Subcategory totals are allocated to states and US territories based on agency data documenting geographic distributions or appropriate proxies. Data identifying the geographic source of receipts and location of spending were collected from relevant agencies wherever possible. Where complete data on the distribution of receipts and expenditures were not available, proxies were developed based on all available data." Schultz, "Giving or Getting?," p. 8.
16. Schultz, "Giving or Getting?," p. 18.

17. The report begins with a letter from the New York State director of the budget that states, “[T]he current [COVID-19] crisis requires informed evidence-based analysis on how federal tax dollars have been distributed. The Division of the Budget collaborated with the Rockefeller Institute of Government on the research and publication of this report to inform how policies in Washington are impacting the state revenues and New Yorkers.” After describing the size of New York’s balance of payments deficit, the letter goes on to state, “We continue to hold out hope that new leadership in Washington will deliver the funding New York State desperately needs.”
18. The correlation between states’ 2015–2019 per capita balance of payments and their 2017 SALT deduction as a percentage of AGI (based on Table 2, IRS Statistics of Income) is –32.8 percent. Most of this correlation (60 percent) comes from just three high-tax states around the New York City metropolitan area: New York, New Jersey, and Connecticut. (These calculations are based on the balance of payments reported in Table 8B of the Rockefeller Institute report.) However, as this *Backgrounder* will describe, the reported balance of payments for New York overstates the extent to which New York is a net donor state.
19. Maryland, which also boasts a large federal workforce, had the sixth-highest per capita balance of payments from 2015 to 2019, according to the report.
20. Notably, Washington, DC, is also a high-tax jurisdiction whose residents disproportionately benefit from the SALT deduction.
21. Table 18 of the Rockefeller Institute report concludes that \$105.9 billion of federal wages are military and \$170.5 billion of federal wages are non-military.
22. Balance of payment statistics are based on Table 8B of the Rockefeller Institute report. Although already mentioned for its large federal workforce, Virginia (highest balance of payments) is also home to many military servicemembers.
23. See, for example, the Honorable Mark Begich, “Alaska’s Strategic Role in the Defense of the United States and the Vital Role of Missile Defense,” Heritage Foundation *Lecture* No. 1133, September 10, 2009, <https://www.heritage.org/defense/report/alaskas-strategic-role-the-defense-the-united-states-and-the-vital-role-missile>.
24. In fiscal year (FY) 2019, Social Security and Medicare made up a total of 41.3 percent of all non-interest federal outlays. Congressional Budget Office, “An Update to the Budget Outlook: 2020 to 2030,” September 2, 2020, <https://www.cbo.gov/publication/56517> (accessed December 21, 2021).
25. According to Table 13 of the Rockefeller Institute report, in 2019, \$1.04 trillion of direct payments to individuals were Social Security payments, and \$762.7 billion were Medicare payments. The Social Security payments included \$892.9 billion for old age and survivors’ insurance and \$145.1 billion for disability insurance.
26. Social Security Administration, “Table 1: Social Security Beneficiaries as a Percentage of the Total Resident Population,” [https://www.ssa.gov/policy/docs/statcomps/oasdi\\_sc/2020/table01.pdf/](https://www.ssa.gov/policy/docs/statcomps/oasdi_sc/2020/table01.pdf/) (accessed December 21, 2021).
27. Schultz, “Giving or Getting?,” Table 8B.
28. Social Security Administration, “Table 1: Social Security Beneficiaries as a Percentage of the Total Resident Population.”
29. Schultz, “Giving or Getting?,” Table 8B.
30. According to the National Association of State Budget Officers, federal grants-in-aid comprised 32.4 percent of total state spending in FY 2020. See Diane Katz, “Federalism in Crisis: Urgent Action Required to Preserve Self-Government,” Heritage Foundation *Special Report* No. 248, November 30, 2021, <https://www.heritage.org/conservatism/report/federalism-crisis-urgent-action-required-preserve-self-government>.
31. See Schultz, “Giving or Getting?,” Table 16.
32. See Schultz, “Giving or Getting?,” Table 2.
33. On the other hand, the amount of federal taxes per capita bears little to no relationship with the top statutory income tax rate of a state.
34. See Congressional Budget Office, “The Distribution of Household Income, 2018,” Exhibit 10, August 2021, <https://www.cbo.gov/system/files/2021-08/57061-Distribution-Household-Income.pdf> (accessed December 28, 2021).
35. As of 2018, the nine states that have no income tax (including New Hampshire and Tennessee, which taxed investment income only) were Washington, Wyoming, New Hampshire, Florida, Nevada, Texas, Alaska, Tennessee, and South Dakota. They ranked 6th, 10th, 11th, 13th, 14th, 15th, 19th, 27th, and 28th, respectively, in federal taxes paid per income tax filing. Author’s calculations using IRS Statistics of Income data, Table 2, “Individual Income and Tax Data, by State and Adjusted Gross Income, Tax Year 2018,” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed December 15, 2021).
36. The correlation between states’ AMT per filing in 2018 and federal income taxes paid per filing in 2018 was 69.5 percent. The correlation between states’ SALT deductions per filing in 2017 (the last year before it was capped) and federal income taxes paid per filing in 2017 was 51.1 percent. Author’s calculations based on IRS Statistics of Income data, Table 2, “Individual Income and Tax Data, by State and Adjusted Gross Income, Tax Year 2017 and Tax Year 2018,” <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2/> (accessed December 15, 2021).
37. See, for example, George Skelton, “Trump’s Cap on Tax Deductions Hurt Californians. It’s Time to Stop the Bleeding.” *Los Angeles Times*, November 15, 2021, <https://www.latimes.com/california/story/2021-11-15/skelton-salt-cap-congress-california> (accessed December 28, 2021).

38. The average state income tax rate of the eight states bordering the Great Lakes, according to the Tax Foundation, was 5.85 percent as of 2018. The average for the eight Mountain West states was 4.17 percent. Similarly, the average state bordering the Great Lakes ranked 22nd in per capita property taxes, while the eight Mountain West states on average ranked 30th. Janelle Cammenga, “How Much Does Your State Collect in Property Taxes Per Capita?” Tax Foundation, May 19, 2021, <https://taxfoundation.org/state-collect-property-taxes-per-capita-2021/> (accessed February 1, 2022).
39. The median housing value of the seven Great Lakes states excluding New York is just \$175,000. Notably, the median housing value of most New York counties in the vicinity of the Great Lakes are at least as low as the broader Great Lakes region. Only Ontario County, NY, has a median housing value above \$200,000 (\$216,000 as of 2020). See New York State Department of Taxation and Finance, “Residential Median Sale Price Information by County,” <https://www.tax.ny.gov/research/property/assess/sales/resmedian.htm> (accessed February 1, 2022).
40. Statistics are based on the median values of owner-occupied housing by state, as reported in the Census Bureau’s 2015–2019 American Community Survey.
41. Author’s calculations based on 2017 Statistics of Income data.
42. The U.S. Department of Agriculture produces a county-level natural amenities scale based on “environmental qualities most people prefer.” These include warm winters, winter sun, temperate summer, low summer humidity, topographic variation, and water area. Counties in the Mountain West rank among the highest in natural amenities. The Natural Amenities Scale is available at <https://www.ers.usda.gov/data-products/natural-amenities-scale/> (accessed December 17, 2021).
43. “Federal Land Ownership: Overview and Data,” Congressional Research Service *Report for Congress*, updated February 21, 2020, <https://crsreports.congress.gov/product/pdf/R/R42346> (accessed December 28, 2021).
44. For example, the median home sale price in Rockland County, NY, was \$495,000 in 2021, while the median home price in Allegheny County, NY, was only \$76,000. See New York State Department of Taxation and Finance, “Residential Median Sale Price Information by County,” <https://www.tax.ny.gov/research/property/assess/sales/resmedian.htm> (accessed January 4, 2022).
45. The median listing price in the Buffalo–Cheektowaga–Niagara Falls metropolitan area is \$145.32 per square foot as of November 2021. In the Miami–Fort Lauderdale–West Palm Beach metropolitan area, it is \$345.78 per square foot. Federal Reserve Bank of St. Louis, “Housing Inventory Core Metrics,” <https://fred.stlouisfed.org/release/tables?rid=462&eid=1138280/> (accessed December 27, 2021).
46. New York City residents simultaneously face higher state and local taxes and a higher cost of living than do residents of Miami. However, since cost of living varies considerably within the state of New York, residents outside the New York City metro would benefit from the SALT deduction despite lower cost of living.
47. Michael Croley, “The Price of Living in ‘Paradise’ Is Higher Than Ever,” *New York Times*, November 4, 2021, <https://www.nytimes.com/2021/11/04/realestate/hawaii-housing-prices-pandemic.html/> (accessed December 27, 2021).
48. Like state taxes, state and local regulatory policies such as occupational licensure, regulated monopolies, environmental restrictions, and zoning laws can also restrict supply and drive cost-of-living increases. As with state and local taxes, such policies are set at the state and local level by voters and their elected officials. Such regulations are intended—at least in theory—to provide benefits to residents, such as enhanced safety, consumer protection, and environmental improvements. There is no justification, then, for providing a tax preference that offsets state and local regulatory costs. See Salim Furth, “Costly Mistakes: How Bad Policies Raise the Cost of Living,” Heritage Foundation *Background* No. 3081, November 23, 2015, <https://www.heritage.org/government-regulation/report/costly-mistakes-how-bad-policies-raise-the-cost-living>.
49. Preston Brashers, “4 Problems With Left’s Hypocritical Plan to Give Wealthy Constituents a Bigger SALT Deduction,” *The Daily Signal*, December 3, 2021, <https://www.heritage.org/taxes/commentary/4-problems-lefts-hypocritical-plan-give-wealthy-constituents-bigger-salt-deduction/>.
50. Nicolas Loris and Katie Tubb, “Allow Energy Tax Credits to Expire,” Heritage Foundation *Background* No. 3164, November 16, 2016, <https://www.heritage.org/environment/report/allow-energy-tax-credits-expire>, and Joel Griffith and Adam N. Michel, “Opportunity Zones: Understanding Them in the Context of Past Place-Based Incentives,” Heritage Foundation *Background* No. 3420, July 10, 2019, <https://www.heritage.org/taxes/report/opportunity-zones-understanding-them-the-context-past-place-based-incentives>.
51. Some features of the tax code that are referred to as tax expenditures are not actually tax preferences. For example, a lower tax rate on capital gains income is not a tax preference but instead mitigates the harm of double taxation inherent in the current federal tax system. Adam N. Michel, “A New Measure of Tax Expenditures to Support Pro-Growth Tax Policy,” Heritage Foundation *Issue Brief* No. 4951, April 9, 2019, <https://www.heritage.org/budget-and-spending/report/new-measure-tax-expenditures-support-pro-growth-tax-policy>.
52. Kate Davidson, “Covid-19’s Hit to State and Local Revenues Is Smaller Than Many Feared,” *Wall Street Journal*, February 7, 2021, <https://www.wsj.com/articles/covid-19s-hit-to-state-and-local-revenues-is-smaller-than-many-feared-11612706030/> (accessed December 20, 2021).
53. U.S. Department of the Treasury, “Allocation Methodology for States,” May 10, 2021, <https://home.treasury.gov/policy-issues/coronavirus/assistance-for-state-local-and-tribal-governments/state-and-local-fiscal-recovery-funds/> (accessed December 20, 2021).
54. Adam Michel, “State Bailouts Create Poor Incentives, Do Not Fix Underlying Problems,” Heritage Foundation *Background* No. 3488, April 17, 2020, <https://www.heritage.org/budget-and-spending/report/state-bailouts-create-poor-incentives-do-not-fix-underlying-problems>. Greszler, Dayaratna, and Sargent, “Why Tax Reform Should Eliminate State and Local Tax Deductions.”
55. Katz, “Federalism in Crisis,” and David Ditch, “Improving Surface Transportation Through Federalism,” Heritage Foundation *Background* No. 3450, November 12, 2019, <https://www.heritage.org/budget-and-spending/report/improving-surface-transportation-through-federalism>.

56. Michael Schuyler, "A Short History of Government Taxing and Spending in the United States," Tax Foundation, February 19, 2014, <https://taxfoundation.org/short-history-government-taxing-and-spending-united-states/> (accessed December 20, 2021).
57. David Ditch, "6 Charts Highlight Troubling Trends Driven by Growing Nondefense Spending," The Daily Signal, May 13, 2021, <https://www.heritage.org/debt/commentary/6-charts-highlight-troubling-trends-driven-growing-nondefense-spending/>.