Common Good **Iowa**
Bold Policy for Families & Communities

January 2024

Use the Taxpayer Relief Fund to promote shared prosperity

The one-time dollars should support one-time tax initiatives for broad-based prosperity, not permanent tax breaks going overwhelmingly to the rich

Governor Kim Reynolds' 2025 budget proposal to the Iowa General Assembly includes another increase in the so-called "Taxpayer Relief Fund," the repository of one-time dollars accumulated by lawmakers to pay for tax cuts.

Some see this pool approaching $4 billion in one-time funds as a resource to pay for big income-tax cuts — even, as outlined in Senate File 552, to permanently eliminate personal income-tax rates.

Instead of instituting another permanent tax giveaway skewed to the rich that locks us in to devastating budget cuts, lawmakers should use the TRF for short-term tax credit expansions that promote broad-based prosperity.

The TRF contains one-time dollars; income tax cuts are permanent

It is unsustainable to use the one-time Taxpayer Relief Fund dollars to pay for the ongoing expense of general income tax cuts. (See sidebar, above right.) Once the TRF funds are used up, there would be no means to pay for the ongoing cost of permanent tax cuts — other than cutting services. It is basic math.

The personal income tax generates nearly half the state General Fund. Temporarily paying for big tax cuts with the TRF only postpones the pain and a transparent look

What is the Taxpayer Relief Fund?

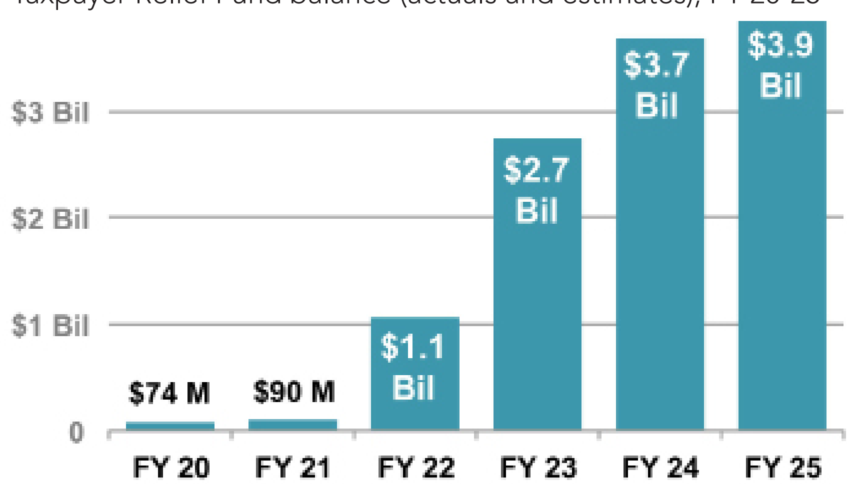
When the state has budget surpluses, some of the unspent revenues spill into the Taxpayer Relief Fund (TRF). Created in 2011, the TRF, with a few exceptions, may only be tapped for "tax relief," including tax credits or reducing rates.

For most of its history, the TRF was modest in size. But in last few years, the uncapped fund has grown to nearly $3.7 billion, bolstered by General Fund surpluses. Surpluses have grown for two main reasons. First, a strong economy, supported by temporary federal pandemic aid, has boosted revenues. Second, lawmakers have restricted state investments in schools, health and other priorities below what's needed to meet needs and keep up with rising costs.

As recently approved tax cuts phase in, state revenue is projected to decline, and so will surpluses. As surpluses decline, so will growth of the TRF. Using one-time TRF funds to pay for permanent tax cuts is a recipe for a budget cuts.

Driven by pandemic-aid boosted economy and suppressed state budgets, TRF has grown fast

Taxpayer Relief Fund balance (actuals and estimates), FY 20-25



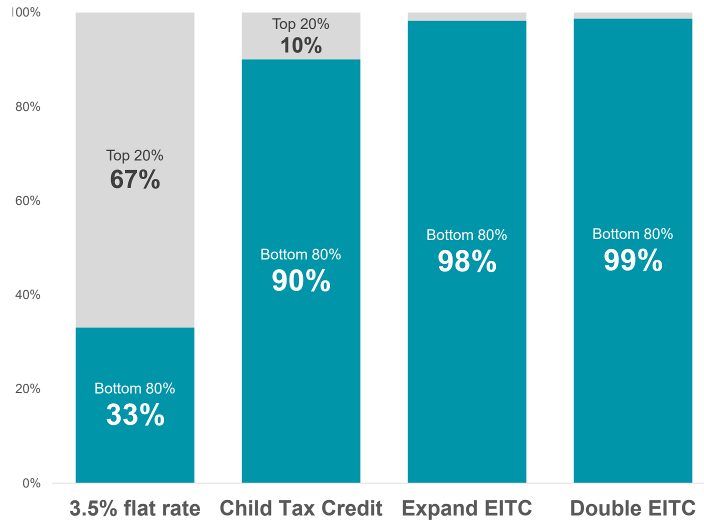
Source: Iowa Legislative Services Agency at the impact of the cuts. Without replacement funding, the revenue losses will force service cuts that degrade our state's quality of life and make Iowa a less attractive place for families and businesses: school closings, crowded classrooms, cuts to public health and safety, fewer workplace safeguards and fewer outdoor recreation options.

Income tax cuts make our overall tax system more unfair

Using the TRF to slash the income tax would also significantly worsen our already "upside down" tax system in which low- and middle-income earners pay higher shares of their incomes in total state and local taxes (income, sales and property) than higher-income earners. Analysis by the Institute on Taxation and Economic Policy shows that two-thirds of the benefit from implementing a 3.5% flat rate would go to the top 20% of residents by income.

Targeted tax credits would help Iowans who will see little benefit from recent and proposed income tax rate cuts

Share of tax benefit going to Iowa residents in the bottom 80% of incomes by use



Source: Institute on Taxation and Economic Policy

A better agenda for the TRF

Passing more tax cuts mostly benefiting the wealthy could wipe out the TRF in as little as a year or two. **Lawmakers should instead use TRF dollars for temporary tax credit improvements targeting Iowans who will see no or modest benefit from recent or proposed cuts in income tax rates.**

Moving to a 3.5% flat tax would cost the state about $1.8 billion annually, according to ITEP. Targeted tax credit improvements would cost significantly less.

Their track record of promoting tax equity and prosperity offers a strong case for making these improvements permanent. But because they would be funded by the one-time TRF funds, they could be structured as pilots to run as long as the funds are available. That period would add to the evidence and lay the groundwork for making them permanent.

1. Establish a State Child Tax Credit

Annual cost: ~$200 million

Similar to the federal CTC that was temporarily expanded in 2021 and boosted opportunities for hardworking families, reduced child poverty and strengthened local economies, it would help families pay for essentials like food, utilities and diapers. A credit providing $100 to $600 per child could reach 93% of Iowa children. Twelve states have some form of a CTC, including Minnesota.

2. Double the State EITC

Annual cost: ~$80 million

Iowa's Earned Income Tax Credit is now 15% of the federal EITC. Doubling it would better support low-wage working families who can't make ends meet on earnings alone. The well-documented benefits of the EITC include reducing child poverty and improving health.

3. Expand State EITC to childless adults

Annual cost: ~$2 million-$4 million

Many low-wage childless adults — filling needed jobs in our communities — are now ineligible for the EITC due to age requirements under current law. Making them eligible for the credit would relieve financial hardship, put dollars into local economies, and lessen inequities in Iowa's tax system.

Visit **www.commongoodiowa.org** or contact deputy director Mike Owen at mowen@commongoodiowa.org to learn more about tax policy that promotes prosperity.