Center on Budget and Policy Priorities

POLICY BASICS

Where Do Federal Tax Revenues Come From?

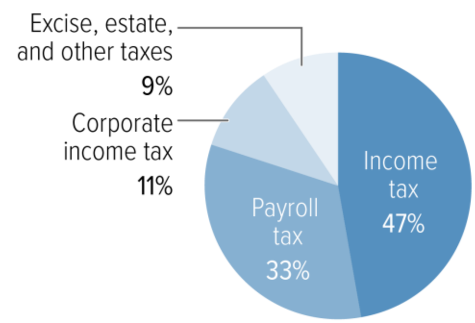
> "The three main sources of federal tax revenue are individual income taxes, payroll taxes, and corporate income taxes."

Updated March 4, 2016

In fiscal year 2015, the federal government spent $3.7 trillion on the services it provides, such as national defense, health care programs like Medicare and Medicaid, Social Security benefits for the elderly and disabled, and investments in infrastructure and education, in addition to interest on the debt (see our related *Policy Basics: Where Do Our Federal Tax Dollars Go?*). Federal revenues financed over $3.2 trillion of that $3.7 trillion. Borrowing financed the remaining amount ($438 billion); future taxpayers will ultimately pay this deficit.

The three main sources of federal tax revenue are individual income taxes, payroll taxes, and corporate income taxes; other sources of tax revenue include excise taxes, the estate tax, and other taxes and fees.

Sources of Federal Tax Revenue, 2015



Note: "Other Taxes" category includes profits on assets held by the Federal Reserve.

Source: Office of Management and Budget

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Almost half of all federal revenue (47 percent) comes from **individual income taxes.** The income tax is generally progressive: higher-income households pay a larger share of their income in income taxes than lower-income households do.

Another 33 percent of revenue comes from **payroll taxes**, which are assessed on the wage or salary paychecks of almost all workers and used to fund Social Security, Medicare Hospital Insurance, and unemployment insurance. By law, employers and employees split the cost of payroll taxes, but research has shown that employers pass their portion of the cost on to workers in the form of lower wages.

Payroll taxes as a whole are regressive: they collect a higher percentage of total earnings from lower-income workers than higher-income ones. However, if one looks at the overall impact of Social Security, Medicare, and unemployment insurance — the benefits they provide as well as the taxes they collect — these programs are progressive. (See our related *Policy Basics: Top Ten Facts About Social Security* and *Policy Basics: Federal Payroll Taxes*).

Corporate income taxes make up about 11 percent of federal revenue, with the remaining 9 percent coming from **excise taxes, estate taxes, and other taxes.** Excise taxes are collected on the sale of certain goods (e.g., fuel, alcohol, and tobacco); they are intended to raise revenue and,

Policy Basics is a series of brief background reports on issues related to budgets, taxes, and government assistance programs.

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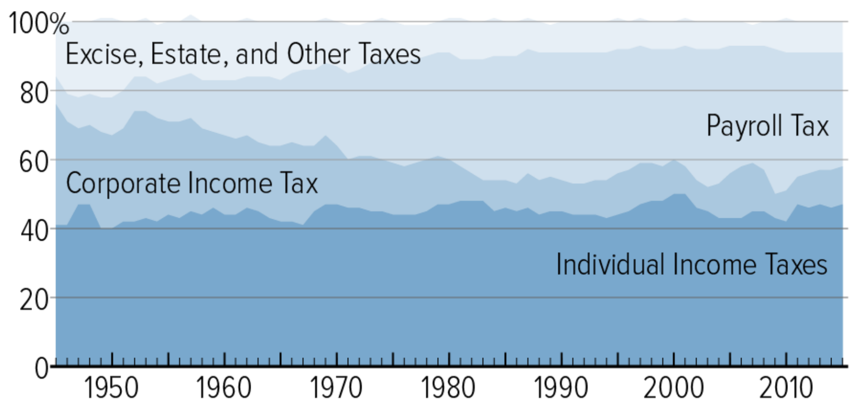
in some cases, discourage consumption of the taxed product. These made up about 3 percent of federal receipts in 2015.

The estate tax is a tax on assets such as cash, real estate, or stock that are transferred from deceased persons to their heirs. Because the first $10.86 million of a married couple's estate was exempt from the estate tax in 2015, and because of other special exemptions from the estate tax, fewer than the wealthiest two of every 1,000 e states nationwide owed any estate tax in 2015. Estate tax revenues made up 0.6 percent of total federal receipts in 2015.

Sources of Federal Tax Revenue, 1945-2015



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Another source of federal revenue is profits on assets held by the Federal Reserve System. These have grown from 0.9 percent of total revenue in 2005 to about 3 percent in 2015. The increase in these receipts is due to extraordinary actions taken by the Federal Reserve to combat the financial crisis and is projected to decline in the coming years.

The small remainder of federal revenues comes from various sources such as regulatory fees and custom duties.

Over recent decades, the share of federal revenues coming from individual income plus payroll taxes has grown, while the share coming from corporate taxes and other revenues has fallen. The Great Recession — one of the worst economic downturns since the Great Depression — and the policies enacted to combat it, including temporary tax cuts, depressed federal revenues below the typical levels of recent decades. Revenues fell from 17.9 percent of gross domestic product in 2007 (the last fiscal year before the recession) to 14.6 percent in 2009 and 2010. Revenues have recovered with the economy and were 18.3 percent of gross domestic product in 2015.

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