The Anniston Star

New tax law may hold a surprise for working poor

by Tim Lockette
Assistant Metro Editor
01.20.11 - 03:00 am

When President Barack Obama and congressional Republicans cut a deal on the extension of Bush-era tax cuts last month, the move was billed as a tax reduction for all.

But the working poor may find an unpleasant surprise in their paychecks this month, says one tax expert.

“If you’re a low-wage earner, you’ll be worse off, as will about 50 million households,” said Roberton Williams, a scholar at the nonprofit Tax Policy Center, which is run jointly by the Urban Institute and the Brookings Institution. “You’ll probably see the effects of the change in your next paycheck.”

The Star contacted Williams after a reader pointed out that her first January paycheck was actually smaller than her paycheck from last year — despite a recent compromise tax bill that was widely interpreted as a tax cut.

Republicans and Democrats sparred throughout December over extension of Bush-era cuts to income taxes, which were set to expire Dec. 31 of last year.

Democrats wanted to extend the cuts, but only for people making less than $250,000 per year. GOP legislators pushed to extend the tax cuts for everyone — a move that, Republicans said, would stimulate the economy.

Both sides reached a compromise that kept the tax cuts in place, even for the top wage-earners. The deal also included a one-year cut in federal withholding for Social Security — the tax that appears on your paycheck as “FICA.”

Less publicized was the Dec. 31 expiration of an earlier tax incentive. The Making Work Pay tax credit, which was approved by Congress in 2009, expired at the end of 2010. The one-year measure reduced the amount of non-FICA income tax withheld from everyone’s paycheck.

Back in December, Williams warned that the expiration of Making Work Pay would be costly for people on the low end of the wage scale. That’s because non-FICA withholding is going up to pre-2010 levels, he said, and that money will not be coming back in your refund.

And the cut to FICA withholding, he said, won’t make up for it — at least not for people making less than $20,000 per year.

Williams said the changes will more or less cancel each other out, for most people, resulting in only a slight decrease or increase in take-home pay.

But Williams' figures show that workers who make less than $10,000 per year will pay an average of $140 more in taxes this year.

Earners between $200,000 and $500,000 per year will save an average of almost $1,900 on their taxes, according to Williams' numbers.

Williams said the change doesn't really accomplish what the tax cut package set out to do — namely, stimulate the economy.

"If stimulus is your goal, you need to put more money in the hands of people at the low end of the wage scale," he said. "For those people, every dollar that goes in goes right back out, because people have to eat."

Denise Hunt, disbursements manager at Jacksonville State University — which employs a number of part-time and student workers — said she was aware of the potential effect of the expiration of Making Work Pay. But she was reluctant to declare Williams' prediction correct.

"I'm always cautious about interpreting tax policy," she said. "Everyone's situation is complicated, and there are a number of factors that come into play."

She said Wednesday that paychecks for student workers are being processed now, and it wasn't clear "whether there is an across-the-board effect."

She said no one complained after JSU paid out another payroll, for both full- and part-time workers, earlier this month.

One reason many workers may not notice is that the cut is spread out over a year's worth of paychecks, said Chris Sanders, a policy analyst for the Arise Citizens' Project, a Montgomery-based nonprofit that advocates for the needs of people in poverty.

"It's possible that many people didn't notice the increase they got when Making Work Pay was in effect," Sanders said. "At the time, the thinking was that if you give people a tax refund in one lump sum, they may sock it away, but if you give them a few dollars in every paycheck, they're more likely to go out and spend it."

Sanders said his organization knew the new tax legislation would amount to a tax increase for many working people in poverty. He said he saw it as "a design flaw, and not something intentional in the bill."

He said that despite the flaw, he was encouraged to see some of the concessions Obama obtained in the deal-making over the bill. Among other things, he said, the deal included extensions to unemployment benefits and the Earned Income Tax Credit.

"There were some good things that were extended," he said. "Given the deadline, and the fact that it came down to this bill or nothing, the result isn't as bad as it could have been."

Williams said there was little relief in sight for low-wage earners disgruntled about their lower take-home pay. But he noted that even more people are likely to feel the pain this time next year, when the Social Security withholding reduction expires.

"At that point," he said, "everybody's taxes will go up."

Star assistant metro editor Tim Lockette: 256-235-3560.