

# M&Y INTERNATIONAL FINANCIAL SERVICES NEWSLETTER



## M&Y International Financial Services

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## What's the average American's tax rate?

According to the IRS's preliminary data from the 2015 tax year (the returns you filed during 2016), there was a total of \$1.454 trillion in income tax owed, which translates to an average effective federal income tax rate of about 13.5% per return. However, that doesn't tell the entire story, as there are several other taxes that most Americans pay. Here's a clearer picture of how much Americans pay in taxes as a percentage of their income.

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*“The average American pays almost 30% of their income to taxes”.*

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### The average American's federal income tax

For the 2015 tax year, the IRS assessed income tax of \$1.454 trillion on Americans, out of the 150.6 million tax returns received by the agency. A quick calculation shows that the average taxpayer owed \$9,655 in income tax. Since the average taxpayer's gross income was \$71,258 for 2015, this translates to an effective federal income tax rate of 13.5%.

Just to add a little color, know that this rate is a bit misleading because it includes the more than 50 million tax returns that had no federal income tax liability. Only 99.2 million tax returns owed any income tax whatsoever after adjustments, deductions, exemptions, and tax credits were taken into account, so the average taxpayer who paid income tax had a tab of \$14,654.

The other taxes Americans pay

In addition to federal income tax, there are several other taxes Americans may have to pay. Some are income-based, like state income tax, and other are consumption-based, like sales taxes.

**State and local income taxes:** It's tough to say what the average state income tax rate is, because this varies tremendously based on where you live, and several states don't have an income tax at all. For example, the average state income tax in Florida is zero. With that in mind, the U.S. Census Bureau has estimated that Americans pay an average rate of 9.9% in state and local income taxes annually.

**Social Security tax:** Social Security tax is assessed at a 6.2% rate on employees and employers, but only applies to the first \$127,200 of earned income for 2017. For most Americans, this is the Social Security tax rate they actually pay.

However, Social Security tax is a bit more complicated. Self-employed individuals are considered to be the employee and the employer, and therefore have to pay both sides of the tax. For a quick (but imperfect) calculation, Social Security took in \$679.5 billion in payroll tax during 2015, and Americans generated \$7.3 trillion in wage income, so the overall average Social Security tax rate is 9.3%. However, since only half is paid by employees, the average rate paid by taxpayers is actually about 4.7% (remember, higher-income individuals only pay the tax on part of their income). Bear in mind that this doesn't consider the roughly 20 million Americans who paid at least some self-employment tax in 2015, but it's pretty close to the actual average rate.

**Medicare tax:** Medicare tax is assessed at a 1.45% rate for both employees and employers, on all earned income, and high earners pay an additional Medicare tax. Self-employed individuals pay both sides of the tax, and using a similar calculation method as I used to find the average Social Security tax rate, we find that the average Medicare tax rate is 3.3% overall, or 1.66% per person. This makes sense, since it accounts for the high earners' additional Medicare tax payments.

**Property taxes:** These are taxes you pay for the privilege of owning something, and the most common forms are real estate taxes and vehicle taxes. These vary from state to state, and obviously, people who don't own homes or cars don't have to pay them, so it's difficult to say how much the average person pays.

Sales tax: This is another one where it's somewhat misleading to talk about the "average" sales tax, since it varies significantly from state to state, and some states don't have a sales tax. Having said that, the overall average sales tax rate in the U.S. was 8.45% in mid-2015, according to a report from Thomson Reuters.

Of course, there are other taxes you could be paying as well. If you stay in a hotel in most places, for example, you'll pay some type of tourism or hospitality tax. Part of the price of a pack of cigarettes is tax, and this amount can vary tremendously by location. The same applies when you buy a gallon of gasoline.

So, what is the average American's overall tax rate?

If you add up the four income-based categories of taxation (Federal, state/local, Social Security, and Medicare), the average American's effective tax rate is 29.8%. This is in addition to any consumption-based taxes paid, such as sales tax, property tax, or other taxes on specific items.