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## **How Will the Elimination of the SALT Deduction Affect Delaware Valley Households?**

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The recent passage of tax reform bills by the U.S. Senate and House of Representatives aim to eliminate—or at least significantly reduce—the deductible amount of state and local taxes (hereafter, SALT) from federal income taxes. Although members of both chambers still need to meet in conference to reconcile the two bills into a single final one, it seems highly likely that the resulting bill will retain this objective. As such, it is worth examining how this will affect households across the region.

To do this, data from the IRS's 2015 Statistics of Income, which aggregates data to the Zip Code-level from all tax returns filed for the 2015 tax year, was downloaded and analyzed. This data was obtained for the eleven counties in the Philadelphia Metropolitan Statistical Area (MSA). For each Zip Code, the average SALT deduction was computed as the average sum of deductions taken for income, sales and property taxes levied at the state and local levels. This was computed only for households that itemized their returns. Since both versions of the bills that were passed capped the property tax deduction at \$10,000, this same cap was imposed on the data where the average property tax deduction in any of the Zip Codes exceeded \$10,000. The following histogram shows the distribution of average SALT deductions across all Zip Codes in the region:

### **Distribution of Average SALT Deduction Across Delaware Valley Zip Codes**

**% of Zip Codes**  
% of Zip Codes

**\$ Deduction**

\$ Deduction

The horizontal axis shows the variation in average dollar deduction taken in SALT taxes, while the vertical axis shows the percentage of Zip Codes in that category. There are some Zip Codes where there are zero SALT deductions taken, which are overwhelmingly located in very low-income neighborhoods and townships. The median deduction is \$12,268 and the average deduction is nearly \$14,000. The bottom twenty-five percent of the region's Zip Codes deduct less than \$9,706, while the top twenty-five percent deduct nearly \$16,500 or more. The Zip Code with the highest average SALT deduction deducts an average of slightly over \$67,200.

To examine where the high v. low deducting areas are, the following map was generated by vertically extruding each Zip code by the average size of its SALT deduction. Additionally, each Zip is color-coded by the size of its average deduction using a temperature color ramp: warm colors denote relatively high levels of deductions while cool colors denote relatively low levels.

**Delaware Valley Zip Codes Extruded and Color-Coded by Average SALT Deduction**

The categories of the color ramp were set so that each category contains exactly twenty percent of all Zip codes in the region. So, the bottom twenty percent of Zip Codes in the region (colored blue) have a SALT deduction of \$9,000 or less. Conversely, the top twenty percent of Zip Codes (colored red) have SALT deductions of \$18,000 or more. As can be casually observed in the map, the size of average SALT deductions is heavily correlated with both house prices and household incomes. The relatively low-income neighborhoods of North and West Philadelphia, the city of Chester, Pennsylvania and Zip Codes in southern New Castle County in Delaware have the lowest levels of SALT deductions. At the other extreme, the relatively affluent neighborhoods of Center City and Chestnut Hill in Philadelphia, the prosperous communities in and around Princeton NJ, parts of southern NJ, and in northern Bucks County as well as the Main Line suburbs west of Philadelphia have the highest average SALT deductions. Lastly, we examine those Zip Codes that compose the top ten neighborhoods and townships with the highest SALT deductions. They are given in the following table:

### **Top Ten Zip Codes with Highest SALT Deductions**

The Zip codes are ranked in descending order of average SALT deduction. “Avg. AGI” is the average Adjusted Gross Income in each Zip, as computed by the IRS. The Total SALT deduction is the sum of deductions taken on income, sales and real estate taxes, and is given in the final column. As can be readily observed in the table, areas with large SALT deductions are areas where incomes are also very high. Every single Zip Code in the top ten has an average adjusted gross income well into the six figures. Moreover, since high-income households are more likely to itemize on their returns—which is necessary in order to take advantage of the SALT deduction—this is likely another important factor in explaining the correlation of the size of SALT deductions with household incomes.

The community of Gladwyne, located in Lower Merion Township in Pennsylvania, has both the highest average AGI and SALT deduction, at \$957,162 and \$67,204, respectively. There are also three communities in the Princeton, New Jersey area, which also has among the highest house prices in the region. The remaining communities are scattered on the Main Line, in South Jersey and in Northern Delaware. Only one Zip Code is located in Philadelphia proper: Zip 19103, which is the tony neighborhood of Rittenhouse Square.

While the fact that households with the largest SALT deductions are among the most affluent is unsurprising, there are a few notable results beyond this.

- First, despite having among the highest property taxes in both the region and the U.S., communities in New Jersey do not dominate the list of highest-SALT areas. In fact, they are a minority: composing only four out of the top ten.
- Second, despite having no sales tax, the city of Wilmington, Delaware made the list. This is primarily because both the city and state levy fairly high income taxes.
- Thirdly, despite having a relatively high income (wage) tax in addition to sales and property taxes, only one Philadelphia neighborhood made the top ten list. In fact, only four Zip Codes in Philadelphia made the top twenty percent of highest SALT-deducting Zip Codes in the entire region. Of course, if other city taxes were included in this analysis, the results might differ.

Finally, it should be remembered that the elimination of the SALT deduction does not represent a simple one-sided loss to all household that itemize to claim this deduction. Rather, these losses should be netted against the potential gains in income, profits and capital gains that reduced tax rates in other parts of the bill are designed to achieve. However, whether the net difference will

be positive or negative will vary not only by household, but also by one's own political and economic opinions.

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