



State-Level Wage AGI Gap for Tax Years 2000-2002

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Abstract

The Bureau of Economic Analysis (BEA), under contract with the Internal Revenue Service (IRS) Office of Research, undertook an update of BEA's state-level wage reconciliation for 2000 between BEA wages and salaries and IRS wages and salaries in Adjusted Gross Income. The initial reconciliation for the year 2000 was documented in the BEA Working Paper, *The Feasibility of Producing Personal Income to Adjusted Gross Income (PI-AGI) Reconciliations by State*. This study updates state estimates of the reconciliation of BEA and IRS wages and salaries for 2001 and 2002.

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Introduction

The Bureau of Economic Analysis (BEA), under contract with the Internal Revenue Service (IRS) Office of Research, undertook an update of BEA's state-level wage reconciliation for 2000 between BEA wages and salaries and IRS wages and salaries in Adjusted Gross Income. The initial reconciliation for the year 2000 was documented in the BEA Working Paper, *The Feasibility of Producing Personal Income to Adjusted Gross Income (PI-AGI) Reconciliations by State*.¹ This study updates state estimates of the reconciliation of BEA and IRS wages and salaries for 2001 and 2002.

Except in the cases of two components of wages and salaries—deferred compensation and nontaxable military wages—the estimating procedures used for 2001 and 2002 are the same as that for 2000. For those two components, the methodology developed for the previous working paper was revised to address a problem of missing data in the later years.

This paper details items identified in BEA's national wage reconciliation that are adjusted for definitional differences and allocated to the states using updated data identified in the 2000 study. A summary of the definitional differences, the estimating procedures, and the sources of the estimates is provided below, followed by a table showing the national reconciliation of wages for 2000-2002 and a more detailed description of the adjustments to reconcile personal income wages and adjusted gross income wages and the state level methodology for producing those adjustments.

¹ See BEA Working Paper, *The Feasibility of Producing Personal Income to Adjusted Gross Income (PI-AGI) Reconciliations by State (WP2006-05)*, by Robert L. Brown, Ann E. Dunbar, and Adrienne T. Pilot | January 2006 http://www.bea.gov/papers/working_papers.htm

Summary Of The Methodology For State-Level Wages and Salaries (W&S)	
Items in PI W&S, not in AGI W&S	State Distributor Series
Imputed income in PI W&S	
Non UI-Covered Wages	BEA direct state estimates
UI Covered Wages	BEA W&S State Employment in Accommodations and Food Services
Employee nontaxable contributions to retirement plans	Unpublished IRS expanded sample state estimates from W-2 Informational Returns 2000, 2002. Data missing in 2001. Used 2000 state distribution extrapolated forward by the movement in BEA state wages by residence for 2001.
Tax exempt military pay	Unpublished IRS expanded sample state estimates from W-2 Informational Returns. For 2002 W-2 did not collect this information. Used 2001 state distribution moved by the growth in BEA state military employment estimates for 2002.
Tax exempt mass transit benefit	BEA state estimates of federal civilian employment. Special adjustment for DC
Items in AGI W&S, not in PI W&S	
Supplemental Unemployment Benefits	2-year average of BLS extended mass layoff estimates in the transportation industry
Disability retirement payments taxed as wages	
Federal Government	Census Bureau state estimates of federal pensions by state
S&L Government	Census Bureau state estimates of S&L pensions by state

To derive a BEA version of IRS AGI wages by state the BEA state wage data, which are estimated and published by place of work, were adjusted to a place-of-residence basis using Decennial Census journey-to-work data and annual IRS wages. In addition, estimates of untaxed imputed wages, elective deferred compensation, nontaxable military wages, and transit subsidies were subtracted from BEA wages, and estimates of supplemental unemployment compensation and disability pensions taxed as wages were added. No adjustment was made to BEA wages for those employees earning wages but not required to file income taxes. A downward adjustment to IRS AGI wages in New Mexico was made to account for tax year 2000 returns included in the IRS 2001 state data because of extensions granted to victims of the Cerro Grande fire. The IRS AGI wages were not adjusted for the impact of extensions granted because of terrorist attacks on September 11, 2001.

Details

BEA annually compares the components of BEA Personal Income and IRS Adjusted Gross Income (AGI) at the national level.² Table 1 details the primary differences among wages and salaries in national income and product accounts (NIPA) personal income, state personal income (titled Sum of States in table 1), and IRS AGI.

Table 1: Wage and Salary Disbursements
(Billions of dollars)

	National			Sum of States		
	2000	2001	2002	2000	2001	2002
Wage and Salary Disbursements, BEA*	4,829.2	4,942.8	4980.9	4,824.8	4,938.9	4975.4
Less: items in PI W&S, not in AGI W&S	124.9	130.8	142.8	121.5	125.9	131.1
Imputed income in PI W&S	11.5	11.7	12.1	11.5	11.7	12.1
Other PI W&S not in AGI W&S	113.4	119.1	142.8	110.0	114.2	119.0
Employee nontaxable contributions to retirement plans	97.4	99.6	102.8	97.4	99.6	102.8
Tax exempt military pay (SPI Overseas Adjustment)	16.0	19.3	27.8	12.6	14.5	16.1
Tax exempt mass transit benefit	0.0	0.1	0.1	0.0	0.1	0.1
Plus: items in AGI W&S, not in PI W&S	32.6	35.1	36.2	10.6	11.1	13.4
Other types of AGI W&S						
Supplemental unemployment	1.8	1.8	1.9	1.8	1.8	1.9
AGI wages from abroad	22.0	23.9	22.8	n.a.	n.a.	n.a.
Disability retirement payments taxed as wages	8.8	9.3	11.5	8.8	9.3	11.5
Equals: BEA-derived AGI W&S	4,736.9	4,847.1	4,874.2	4,713.9	4,824.0	4,857.6
IRS AGI W&S	4,456.2	4,565.2	4,559.7	4,396.3	4,503.3	4,512.4
Wage Gap	280.8	281.8	314.5	317.6	320.7	345.2

*The Sum of States for this item are BEA place of residence wages. These figures differ from BEA place of work wages by \$1.2 billion in 2000-2002 to account for commuting with residents of Canada and Mexico.

n.a. Not applicable

The different source data used in BEA and IRS makes this reconciliation useful to analysts. The BEA state estimates of wages and salaries are primarily based on place-of-work wages reported by the Quarterly Census of Employment and Wages (QCEW), which is collected by the Bureau of Labor Statistics for unemployment insurance purposes.³ BEA adjusts these

² See Mark A. Ledbetter, "Comparison of BEA Estimates of Personal Income and IRS Estimates of Adjusted Gross Income: New Estimates for 2002 Revised Estimates for 2001" *Survey of Current Business*, November 2004 9-14.

³ Although the QCEW includes most of what would be considered wages, each individual state defines what income to report as wages for unemployment insurance (UI) purposes. For example, Alaska does not include employee contributions to 401K plans. States also differ on the inclusion of various section 125 cafeteria plans. Washington state excludes the compensation of corporate officers in its UI, but BEA is able to get estimates of corporate officer

estimates to a place of residence using Census 2000 journey-to-work data and annual place of residence wage data from the IRS. The IRS wage data are from tax returns filed by individuals for the purpose of paying federal income tax. They are reported by place of return address on the Form 1040 income tax return.

While the definitions of wages and salaries for BEA and IRS include many items that overlap, the definitions are different. BEA's NIPA wage and salary disbursements consist of: the monetary remuneration of employees, including the compensation of corporate officers; commissions, tips, and bonuses; employee contributions to certain deferred compensation plans, such as 401(k) plans; employee gains from exercising nonqualified stock options; and receipts in kind that represent income.

BEA's state wages and salaries differ from NIPA wages and salaries because of the treatment of the income of U.S. residents who are working abroad and the treatment of the income of foreign residents who are working in the United States. The total of the state estimates of wages and salaries consists of the income earned by persons who live in the United States and of foreign residents who work in the United States.

The national measure of wage and salary disbursements in the NIPAs is broader than the state measure. It includes the earnings of Federal civilian and military personnel stationed abroad and of U.S. residents on foreign assignment for less than a year. Earnings of foreign residents are included only if they live and work in the United States for a year or more.

IRS wages are what the relevant tax laws dictate. For example, in tax year 2000, wages and salaries on line 7 of the Form 1040 consists of taxable wages from employee's W-2 forms (box 1), allocated tip income (box 8), all or a portion of certain dependent care benefits (box 10), all or a portion of employer provided adoption benefits (box 13 code T), non-reported tip income, non-reported scholarships and fellowship grants, wages less than \$1,200 received as a household employee, and excess salary deferrals.⁴ Filers are instructed to reclassify disability income shown on a Form 1099R Retirement Distributions if they have not met pension age requirement. If box 15 of the W-2 is checked indicating the W-2 recipient is a statutory employee and the recipient has related expenses to deduct, the taxpayer is instructed to report the

pay directly from the state.

⁴ See Appendix B for a list of the items in the W-2 box 1 for 2005 from the IRS website.

amount in box 1 on Schedule C, rather than report it as wages.⁵

The state estimate of wages and salaries for 2000 is \$4,824.8 billion, \$4.4 billion lower than the NIPA national total. Reconciling wages and salaries to IRS AGI wages begins with the removal of \$11.5 billion of **imputed income**. Food furnished for employees (including military and domestic service) comprises over 92 percent of the imputation for wage items. Other imputed income items include standard clothing issued to military and employees' lodging. In the production of state personal income, BEA produces state estimates for about 42 percent of the total imputation (farm pay-in-kind, military pay-in-kind, and lodging and food for non UI-covered industries). The remaining balance was allocated to states using BEA's estimate of the number of employees by state in eating and drinking establishments and hotels and motels.

An additional \$110.0 billion is removed from the 2000 SPI wage estimates in the category of **other personal income not in AGI**. This category can be further split, for the production of state estimates, into \$97.4 billion for employee nontaxable contributions to retirement plans, \$12.6 billion for tax exempt military pay, and \$0.0 billion for mass transit benefit nontaxable wages.⁶ For nontaxable employee contributions to private pension plans, the national estimate is based primarily on information from Form 5500 Annual Return/Report of Employee Benefit Plan. State-level data do not exist from this form. However, BEA has received unpublished state-level estimates of deferred compensation and total wages reported on the Form W-2 from the IRS Statistics of Income (SOI) expanded sample for 2000 and 2002.⁷ A state ratio of deferred compensation to total wages is applied to the IRS individual master file (IMF) wages to get state estimates, which are then used to distribute the national estimate of deferred compensation. The 2001 estimates were distributed to states using the 2000 distribution extrapolated by the growth in state wages by place of residence and controlled to the national

⁵ Statutory employees include full-time life insurance salespeople, certain agent or commission drivers and traveling salespeople, and certain homeworkers. In the NIPAs, the wages and salaries of statutory employees remain in wages and salaries.

⁶ The military pay estimate differs from the NIPA wage estimate because of a \$3.4 billion adjustment to remove those employees stationed overseas. The national estimate was adjusted by data from the IRS SOI state sample to account for those nontaxed military benefits received by out-of-state filers. The mass transit benefit estimate is \$10 million in 2000 but increases to \$0.1 billion in 2001 and 2002, as the federal program of mass transit benefits became fully implemented.

⁷ The SOI expanded sample is a sample of about 170,000 information returns. It includes filers and nonfilers. BEA contracted with SOI to process this large sample and the smaller 120,000 sample for 2000-2002, but the 2001 data for deferred compensation were not available.

estimate.

For exempt military pay, the national estimate is derived from details presented in the *Budget of the United States*. No state estimates independent of IRS data exist. State-level estimates are available on the Form W-2 from the IRS SOI expanded sample for 2000 and 2001.⁸

A state ratio of Form W-2 nontaxed military benefits to W-2 total wages is applied to the IRS IMF wages to get state results that are then used to distribute the national estimate of nontaxed military benefits for 2000 and 2001. The 2001 distribution was then moved forward to 2002 using military employment. The national control for 2002 was increased by 11 percent from 2001 based on information from the Congressional Research Service.⁹ The difference between the published national estimate of nontaxable military wages and the sum of the states is considered to be income overseas.

Regarding mass transit benefit nontaxable wages, BEA does not have state-level estimates. The U.S. Department of Transportation provides national estimates of the Federal government transit subsidy. Federal civilian employment by state was used to distribute the transit benefit.

Wages in AGI but not in state personal income have to be added. An adjustment in 2000 of \$1.8 billion—titled **other types of income** in BEA's table—consists of supplemental unemployment benefits, which are taxable wages for IRS but are not reported as wages in the NIPAs. In the NIPAs, employer contributions to the supplemental unemployment benefit programs are recorded in supplements to wages; benefits paid are not recorded in personal income. There are no state estimates of this item available from IRS. A two-year average of state-level mass layoff data for the transportation sector from the Bureau of Labor Statistics was used to distribute the national total of this item. The transportation sector was used under the assumption that the supplemental unemployment benefits were paid primarily by the automobile industry.

⁸ Basic housing allowances, allowances for subsistence, overseas housing allowances and hostile fire pay/imminent danger pay (combat pay) are excluded from military wages for the federal income tax. Also, enlisted personnel pay received while in a designated area and receiving combat pay is excluded from taxable income. For officers, the amount is capped at the highest enlisted pay plus combat pay. In 2002 this monthly limit was \$5,532.90. See <http://www.irs.gov/newsroom/article/0,,id=101262,00.html>. In 2000 and 2001, such nontaxable military wages were reported in Box 12 Code Q on the W-2 form. For 2002, the Form W-2 did not require that nontaxable military wages be reported.

⁹ *Military Compensation Background Papers*, sixth edition, <http://www.loc.gov/rr/frd/mil-comp.html>

The national reconciliation adds \$22.0 billion in 2000 for the wages of U.S. citizens living abroad. These individuals are nonresidents for purposes of the national accounts, so their wages are added to personal income wages to get to the national IRS wages in the published reconciliation. However, the state-level IRS wage data from the individual master file (IMF) do not include this income because these citizens are not residing in a state. Therefore this adjustment is not needed in the state-level regional reconciliation.

Taxable disability income payments of \$8.8 billion, which are treated as wages in IRS data but are treated as pensions by BEA, must be reallocated from pensions and annuities to wages for the purposes of this reconciliation. IRS instructs taxpayers who are not eligible for retirement and who receive a Form 1099R pension statement to report this disability pension income on the wage and salary line, not the pension line. For the PI/AGI reconciliation this means that an estimate of the disability pension must be added to the BEA wage estimate. The national methodology applies this tax provision to government pensions. The Federal government disability payments were distributed to states by pension data reported by the Census Bureau. The state and local government disability payments were distributed to states by pension benefits reported by the Census Bureau.¹⁰

The state-level IRS wage estimates that are compared with BEA wages are the 2000-2002 IRS Individual Master File (IMF) data published in the IRS publication, *Statistics of Income*. The IMF file is a tabulation of all income tax returns filed by individuals, for example, in 2001 for tax year 2000. As was indicated earlier, an adjustment to IRS IMF wages was made to account for tax returns reported in the 2001 IRS state data and not included in the 2000 IRS state data because of filing extensions that were granted to victims of the Cerro Grande fire in New Mexico. Many of those tax returns were not filed until 2002, and were therefore included in the published data for 2001 and not for 2000. No adjustment was made for extensions that were granted to victims of the terrorist attacks of September 11, 2001.

State-by-State Reconciliation—A summary of the state level results of reconciling personal

¹⁰ The Census state and local government retirement benefits are reported in the state of the retirement plan, not in the state where the beneficiaries live.

income and adjusted gross income are shown in the table below.

SUMMARY RESULTS

	Initial Wage Gap: BEA POR Wages Less IRS Wages						Adjusted Wage Gap: BEA-derived IRS Wages Less IRS Wages					
	2000	2001	2002	Pct	Pct	Pct	2000	2001	2002	Pct	Pct	Pct
				2000	2001	2002				2000	2001	2002
UNITED STATES	428,503,292	435,572,234	462,961,950	8.9	8.8	9.3	317,632,292	320,732,234	345,205,950	6.7	6.6	7.1
(Sum of States)												
ALABAMA	5,123,490	5,495,087	6,175,546	8.7	9.1	10.0	3,834,334	4,058,541	4,917,670	6.7	6.9	8.1
ALASKA	160,362	265,405	263,628	1.6	2.5	2.4	-240,733	-175,510	-177,667	-2.6	-1.7	-1.7
ARIZONA	7,892,842	7,276,154	7,964,057	10.3	9.2	9.9	6,047,188	5,351,068	5,577,664	8.1	6.9	7.1
ARKANSAS	2,645,190	2,815,767	2,945,218	8.5	8.7	8.9	2,001,132	2,161,614	2,428,988	6.6	6.8	7.5
CALIFORNIA	52,364,061	61,988,746	64,633,672	8.2	9.6	10.1	39,106,066	48,060,341	50,082,911	6.3	7.6	8.0
COLORADO	8,922,102	9,924,898	10,107,171	10.3	11.2	11.6	6,668,140	7,672,674	7,683,990	7.9	8.9	9.1
CONNECTICUT	3,933,736	4,794,822	4,621,616	4.7	5.5	5.5	2,331,524	3,138,066	2,752,232	2.8	3.7	3.3
DELAWARE	678,156	1,437,063	1,067,266	4.8	9.4	7.1	408,352	1,225,941	814,305	3.0	8.1	5.5
DISTRICT OF COLUMBIA	1,908,231	2,442,622	1,832,592	15.5	18.2	14.3	1,484,468	2,077,973	1,454,983	12.4	15.9	11.7
FLORIDA	15,210,388	15,998,902	16,924,277	6.6	6.6	6.8	10,335,885	10,786,919	11,630,601	4.6	4.6	4.8
GEORGIA	14,762,479	14,903,237	15,391,358	10.6	10.4	10.7	11,460,350	11,491,075	11,736,720	8.4	8.2	8.4
HAWAII	2,494,539	2,546,768	2,868,887	12.9	12.8	13.7	1,547,808	1,532,438	1,892,759	8.4	8.1	9.5
IDAHO	1,191,675	1,442,712	1,582,345	7.0	8.3	8.9	742,101	946,205	1,132,370	4.5	5.6	6.5
ILLINOIS	22,183,059	22,517,726	22,906,339	9.5	9.4	9.6	17,488,147	17,761,021	18,437,700	7.6	7.6	7.9
INDIANA	8,529,278	7,451,208	8,383,210	8.7	7.6	8.4	6,212,792	5,494,174	6,615,216	6.5	5.7	6.8
IOWA	4,520,033	4,567,948	4,906,701	10.5	10.4	11.0	3,428,499	3,421,042	3,904,508	8.2	8.0	8.9
KANSAS	4,000,006	4,351,824	4,441,613	9.5	10.0	10.1	2,804,152	3,160,571	3,552,847	6.8	7.5	8.2
KENTUCKY	4,420,094	4,756,878	4,994,158	8.2	8.6	8.9	3,077,765	3,451,373	3,822,002	5.9	6.4	6.9
LOUISIANA	5,156,910	5,516,550	5,860,558	9.3	9.5	9.9	3,630,503	3,816,846	4,459,496	6.7	6.8	7.7
MAINE	1,267,807	1,343,893	1,432,466	7.1	7.2	7.4	724,435	755,723	934,809	4.2	4.2	5.0
MARYLAND	10,897,418	10,070,078	13,639,367	9.8	8.7	11.2	8,043,078	6,929,778	10,410,836	7.4	6.2	8.8
MASSACHUSETTS	12,038,527	15,225,264	15,836,273	8.2	10.2	10.9	9,072,396	12,211,453	12,604,624	6.3	8.4	8.9
MICHIGAN	15,534,475	13,882,815	15,264,308	8.8	8.0	8.7	10,880,891	9,233,257	11,566,474	6.3	5.5	6.8
MINNESOTA	9,784,394	10,580,636	11,440,870	10.3	10.7	11.4	7,378,066	8,097,267	8,998,295	7.9	8.4	9.2
MISSISSIPPI	3,060,975	2,652,881	3,133,526	9.5	8.2	9.3	2,459,378	1,978,143	2,407,710	7.8	6.2	7.3
MISSOURI	7,007,653	7,306,234	7,529,799	8.2	8.4	8.5	4,873,297	5,171,018	5,623,315	5.9	6.1	6.5
MONTANA	643,775	687,314	887,246	6.4	6.6	8.1	360,390	406,222	639,174	3.7	4.0	6.0
NEBRASKA	2,461,451	2,720,822	2,735,148	9.6	10.2	10.0	1,761,895	1,977,929	2,030,335	7.0	7.6	7.6

NEVADA	3,683,836	3,397,392	3,610,990	10.6	9.4	9.6	2,806,337	2,408,203	2,699,419	8.2	6.8	7.4
NEW HAMPSHIRE	1,410,863	1,423,360	1,943,505	5.5	5.5	7.4	868,139	839,242	1,311,847	3.5	3.3	5.1
NEW JERSEY	19,176,511	17,319,128	18,581,374	9.5	8.4	9.1	15,664,003	13,793,201	14,663,549	7.9	6.8	7.3
NEW MEXICO	2,572,554	1,916,404	2,515,359	11.7	8.2	10.4	1,946,120	1,256,165	1,880,590	9.1	5.6	8.0
NEW YORK	40,367,860	28,219,937	31,617,117	11.0	7.6	8.6	33,873,514	21,528,284	19,489,260	9.4	5.9	5.5
NORTH CAROLINA	12,453,706	12,235,553	13,288,795	9.8	9.5	10.2	9,224,784	8,701,146	9,720,015	7.5	6.9	7.7
NORTH DAKOTA	662,856	765,999	758,065	8.3	9.1	8.7	308,540	417,309	435,220	4.0	5.2	5.2
OHIO	14,217,301	14,043,852	14,665,378	7.7	7.5	7.8	9,997,519	10,014,048	11,059,624	5.5	5.5	6.0
OKLAHOMA	3,506,338	3,544,267	3,849,128	8.2	7.9	8.5	2,378,141	2,448,437	2,876,873	5.7	5.6	6.5
OREGON	4,869,061	5,287,758	5,164,120	9.2	9.8	9.6	3,960,005	4,356,669	4,113,097	7.6	8.3	7.8
PENNSYLVANIA	14,853,475	15,475,997	17,398,254	7.4	7.5	8.3	10,791,159	11,215,847	13,389,766	5.5	5.6	6.5
RHODE ISLAND	1,339,207	1,042,911	1,179,289	7.7	5.8	6.4	860,151	500,878	729,911	5.1	2.9	4.1
SOUTH CAROLINA	5,235,412	5,032,426	5,664,785	9.3	8.8	9.7	3,909,058	3,640,653	4,186,812	7.1	6.5	7.4
SOUTH DAKOTA	782,956	928,386	902,607	8.3	9.4	8.9	485,155	629,598	638,080	5.3	6.6	6.4
TENNESSEE	7,007,212	6,967,778	7,410,484	8.4	8.2	8.5	5,406,236	5,251,241	5,693,416	6.6	6.3	6.7
TEXAS	35,667,305	37,632,037	37,752,600	10.5	10.6	10.7	26,747,676	28,425,901	29,382,376	8.1	8.3	8.5
UTAH	3,040,196	3,251,938	3,476,078	9.3	9.6	10.1	2,231,923	2,373,413	2,681,302	7.0	7.2	8.0
VERMONT	726,245	695,969	832,506	7.9	7.2	8.4	536,830	497,715	572,892	6.0	5.3	6.0
VIRGINIA	11,189,460	13,588,304	12,711,794	8.2	9.4	8.7	6,885,969	8,727,794	7,659,857	5.2	6.3	5.4
WASHINGTON	8,523,923	9,880,447	10,762,849	7.6	8.8	9.5	5,476,104	6,693,433	7,854,792	5.0	6.1	7.1
WEST VIRGINIA	1,075,915	950,566	1,140,037	5.4	4.6	5.4	652,940	484,059	762,281	3.3	2.4	3.7
WISCONSIN	7,115,398	6,690,923	7,562,230	7.9	7.3	8.0	4,673,022	4,245,277	5,268,773	5.3	4.7	5.7
WYOMING	232,596	316,648	405,391	3.4	4.4	5.4	26,668	90,559	208,670	0.4	1.3	2.8

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11 Adjusted wage gap percents in yellow are outside a one standard deviation interval.

In addition, the attached worksheet has state-level estimates of all of the adjustments to get from BEA wages to IRS wages. A state-by-state difference and percent difference between BEA place-of-residence wages are provided for reference purposes. The gap between BEA adjusted place of residence wages is also calculated, along with the percent gap relative to BEA adjusted wages.

The initial differences between BEA place-of-residence wages and IRS wages for the U.S. in the tax years 2000-2002—that is, the differences between BEA place of residence wages and IRS published wages from the Individual Master File—were 8.9 percent, 8.8 percent, and 9.3 percent, respectively. In 2000, the state percentage differences ranged from 1.6 percent in Alaska to 15.5 percent in the District of Columbia. In 2001 the state differences ranged from 2.5 percent of BEA wages in Alaska to 18.2 percent in DC, with BEA estimates being higher in all states. For 2002, the initial difference between BEA place-of-residence wages and IRS wages ranged from 2.4 percent of BEA wages in Alaska to 14.3 percent in DC. BEA wages were always higher than IRS wages.

After the adjustments have been made to BEA wages, the gap between BEA and IRS narrows such that BEA-derived AGI wages for the nation was 6.7 percent in 2000, 6.6 percent in 2001, and 7.1 percent in 2002. In 2000, the state percentage differences between BEA-derived AGI wages and IRS wages ranged from -2.6 percent in Alaska to 12.4 percent in the District of Columbia. In 2001 the adjusted wage gap ranged from -1.7 percent in Alaska to 15.9 percent in the District of Columbia. In 2002 the adjusted wage gap ranged from -1.7 percent in Alaska to 11.7 percent in the District of Columbia. Alaska was the only state for which IRS wages were greater than BEA derived AGI wages.

A review of the adjusted wage gap by state shows that the percentage difference between the BEA-derived IRS wages and the published IRS wages is similar over the time period of 2000-2002 for most states. The most significant exceptions are Delaware, New Mexico, and New York. In Delaware, the difference among years is concentrated in the adjustment of the BEA wages to a place of residence. In New Mexico, the difference is concentrated in the IRS published wage estimate. Although we adjusted the 2000 IRS published wage to account for deferred income tax returns due to the Cerro Grande fire, the adjustments may not have been enough. In New York, the difference is concentrated in the estimates of employee nontaxable

contributions to retirement plans.

The 2001 results are similar to the 2000 findings except for New York where the difference between BEA's wages adjusted to IRS wages (i.e. the wage gap) and the reported IRS wages is only 5.9 percent in 2001 compared to 9.4 percent in 2000 and the District of Columbia where the wage gap increases from 12.4 in 2000 to 15.9 in 2001. For 2002, the wage gap for both New York and the District of Columbia falls to 5.5 percent and 11.7 percent respectively.

The outliers for all three years were Alaska and the District of Columbia. The adjusted wage gap remains negative for Alaska (IRS wages are greater than BEA's wages adjusted to IRS) for 2000-2002. This can be due to several factors. Since a large number of seasonal workers in Alaska also work at other times of the year in California—a state with a state income tax—those workers may report for Federal income tax purposes as residing in Alaska—a state with no state income tax—thus increasing the amount of wages reported in IRS. In addition, more military personnel may report to IRS from Alaska than are actually working in Alaska. Furthermore, in producing state personal income on a place-of-residence basis, BEA adjusts a large portion of seasonal/temporary wages out of Alaska and into other states because of the type of temporary work in the state (oil industry workers and construction workers on large projects, both of whom have specialized skills). This is the only state where BEA makes such adjustments for seasonal or temporary workers. Finally, the payment of an annual dividend from the Alaska Permanent Trust Fund might increase the level of IRS wages relative to BEA-derived IRS wages. This program provides an incentive for individuals to file their federal income tax return—and, thus, all of their wages earned during the year, including wages earned while residing in other states—with their Alaska address. In 2001, this payment was \$1,850.28 for each permanent resident of Alaska.

The District of Columbia is the only area with an adjusted wage gap percent in the double digits. In the District of Columbia, there may be a significant number of taxpayers who live and work in the city, but who file to IRS as nonresidents of the District of Columbia for Federal income tax purposes. Unlike Alaska, the state and local tax incentive is for taxpayers who actually live and work in DC to file as nonresidents of DC for Federal income tax purposes. These individuals would be included in Washington, D.C. in the BEA adjusted wage estimates.

For example, as stated before, military personnel may declare their permanent state of residence on their tax return to be something other than where they are actually located. There is an incentive for military to report their income to IRS from states with no state income tax.¹⁴ That same incentive also may affect wealthy families with two houses (e.g. one house in the District of Columbia and one in Florida, which they travel to on weekends. These families have the potential to report for income tax purposes from another area.) Finally, members of congress and their staffs may file income tax returns from their home states.

¹⁴ The states that do not tax wages are Alaska, Florida, Nevada, New Hampshire, South Dakota, Texas, Washington, and Wyoming.