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BENEFICIARIES OF PROPOSED SOCIAL SECURITY-RELATED TAX CUT HAVE SIGNIFICANT WEALTH

Their Average Net Worth Exceeds $1 Million, While Their Median Net Worth is $420,000

by Robert Greenstein and Diane Whitmore[1]

On July 27, the House of Representatives passed legislation by a 265 to 159 vote to repeal the provision of current law under which 85 percent of Social Security benefits are counted as part of adjusted gross income for the approximately one-fifth of beneficiaries with the highest incomes. It is not clear at this juncture whether the Senate will take up this measure in September, which it could do either as a separate bill or as a measure appended to other legislation moving through Congress in the final days of the session.

This provision of law was enacted in 1993. It is designed to ensure that Social Security benefits are counted as taxable income for high-income beneficiaries to the extent that the benefits these individuals receive exceed the Social Security payroll tax contributions they have made. This is the same approach as is used in determining the portion of private pension payments that is taxable. The provision enacted in 1993 makes 85 percent of Social Security benefits taxable because, on average, approximately 85 percent of the Social Security benefits that beneficiaries receive exceed the payroll tax contributions they have made.[2]

In assessing the proposal to repeal this provision of law, one important question is who would benefit from its repeal. Most discussions of this proposal have simply noted that the Social Security taxation provision that would be repealed begins to phase in at $34,000 of adjusted gross income for single filers and $44,000 for married filers. Some have concluded, as a result, that this proposal would reduce taxes for seniors of modest means. Simply citing these dollar figures, however, doesn't tell very much about who would be affected for two reasons. First, these are the income levels at which the 85-percent taxation provision begins to phase in, not the income levels at which it takes full effect. Second and more important, significant numbers of retirees possess very substantial assets but have current incomes that do not look especially high. Thus, to determine whether those who would be affected by repealing this provision are retirees struggling to make ends meet or are people with much more substantial means entails examining the assets, as well as the current income, of this group.

To secure data on the assets these individuals possess, we used the best source of information on this matter, the Survey of Consumer Finances, which is conducted by the Federal Reserve Board. The latest survey data are from the survey conducted in 1998, which provides data for 1997. These survey data include information on Social Security benefits and adjusted gross income, as well as on assets, so one can determine which families and individuals have a portion of their Social Security benefits subject to taxation and what their assets and incomes are. The results are as follows:

- The beneficiaries who would receive a tax cut if the 1993 provision is repealed (i.e., who would receive a tax-cut under the bill the House passed on July 27) had average net worth of nearly $1.1 million in 1997. Their median net worth was $420,200.

- If one looks at *financial* assets (which excludes housing and debt)[3] rather than total net worth, those who would benefit

Asset Holdings of Social Security Beneficiaries Who Would Receive a Tax Cut Under House Bill Related To Taxation of Social Security Benefits

	Net Worth		Financial Assets		Income	
	Average	**Median**	**Average**	**Median**	**Average**	**Median**
Beneficiary Households that Will Receive a Tax Cut Under House Bill	$1,066,300	$420,200	$607,100	$187,000	$96,300	$66,000
Beneficiary Households that Are Not Subject to Taxation of Any Portion of Their Benefits	$137,400	$74,000	$49,400	$11,000	$17,000	$15,000

Source: 1998 Survey of Consumer Finances. Figures in 1997 dollars.

from the tax cut had average financial assets of $607,100 in 1997 and median financial assets of $187,000.

- The average current income of those who would get the tax cut was $96,300. The median income was $66,000.

Figures Likely to be Higher Today

These figures reflect assets in 1997 and do not include the large gains in the stock market that have occurred since then. Given that those retirees who would benefit from the proposed tax cut had substantial financial assets in 1997 and that the value of stocks has risen sharply since 1997, it is a safe assumption that this group has significantly higher levels of assets today.

Other Beneficiaries Have Much Less Wealth

The wealth and income of those who would benefit from this tax cut stand in sharp contrast to the wealth and income of those beneficiaries whose Social Security benefits are not taxable. In 1997, the group whose benefits are not subject to taxation included roughly the bottom three-quarters of Social Security beneficiaries (the bottom 72 percent, to be precise).[4]

This large group of beneficiaries whose benefits are not subject to taxation had average net worth of $137,400 and median net worth of $74,000 in 1997. If one looks just at financial assets, this group had average financial assets of $49,400 and median financial assets of only $11,000.

The average income of this group was $17,000. Its median income was $15,000.

Other Potential Uses of the Funds

The proposed tax cut would cost $17 billion a year by 2010. For such an amount, Congress could provide significant assistance to most of the four-fifths of Social Security beneficiaries who would receive nothing from the proposed tax cut related to the taxation of Social Security benefits.

- These resources could be used for such purposes as helping to finance a Medicare prescription drug benefit or a benefit relating to long-term care.

- Alternatively, a portion of these resources could be used to reduce income taxes for middle-income seniors, such as by doubling the additional standard deduction in the federal income tax for individuals who are 65 and over or blind. Doubling the deduction from the current $1,100 to $2,200 for singles, and from $1,700 to $3,400 for couples, would cost about $4 billion in 2010 — about one-fourth the cost of repealing the 1993 provision related to the taxation of Social Security benefits.

Yet it would benefit more than 15 million elderly taxpayers, a larger number than would benefit from repeal of the 1993 provision, with most of the benefits going to middle-income elderly people who would receive no benefit from the repeal legislation. Moreover, substantial funds would be left over for various other measures that could assist elderly and disabled individuals.

- For example, some of these resources could be used to reduce the high rate of poverty that persists among some groups of seniors such as elderly women living alone, a group that has a poverty rate nearly as high as the child poverty rate. One way to do that would be to make some overdue benefit adjustments in the Supplemental Security Income program, the program created under President Nixon that provides cash assistance to elderly and disabled individuals and couples who remain poor despite Social Security. Steps could be taken to recapture the ground lost to inflation in the past quarter century by the lack of an inflation adjustment in a key aspect of SSI that is used to help determine benefits for low-income retired workers (disproportionally women) who receive modest Social Security checks that leave them well below the poverty line. Restoring this aspect of the benefit structure to the same level of purchasing power it provided under President Nixon (a step that also would extend Medicaid coverage to some elderly and disabled people whose incomes are too high to qualify for it even though they are below the poverty line) would cost about $6 billion a year in 2010.

- The two steps just described — a broad tax cut for middle-income elderly people and a significant poverty-reduction initiative for poor retirees — would together cost about $4 billion less per year than the proposed tax cut, which, as noted would benefit only the top fifth of seniors.

Notes:

1. Diane Whitmore is a doctoral student in economics at Princeton and a former member of the staff of the President's Council of Economic Advisers.

2. In addition to the provision enacted in 1993, a provision enacted a decade earlier, in 1983, counts *50 percent* of Social Security benefits in adjusted gross income for single filers with incomes exceeding $25,000 and married filers with incomes exceeding $32,000. As a result, there are three groups of beneficiaries — those whose benefits are entirely exempt from taxation, those for whom 50 percent of benefits are subject to taxation, and those for whom 85 percent of benefits are subject to taxation. If the provision enacted in 1993 is repealed, there will be two categories of beneficiaries rather than three; for the one-fifth of beneficiaries with the highest incomes, 50 percent rather than 85 percent of benefits will be included in AGI.

3. Financial assets include liquid assets (checking, savings, money market accounts and call accounts), CDs, other mutual funds, stocks, bonds, savings bonds, quasi-liquid retirement accounts (including IRA, pension and thrift plans), the cash value of life insurance, other managed accounts, and other financial assets such as cash, royalties, non-public stock and deferred compensation. For more information, see the Federal Reserve Board home page.

4. A third group of beneficiaries has up to 50 percent of its Social Security benefits included in adjusted gross income. This group, which falls between the other two groups on the income scale, is the smallest of the three groups. Only 8.5 percent of beneficiaries were in this group in 1997. This group would not be affected by the proposed tax cut; these beneficiaries would continue to have up to half of their benefits counted in adjusted gross income. As noted earlier, the proposed tax cut would cut the percentage of benefits counted in AGI from 85 percent to 50 percent for the highest-income group of beneficiaries.