Report on the Taxation of Social Security and Railroad Retirement Benefits in Calendar Years 1997 through 2004

Report to the Congress,
the Secretary of Health and Human Services,
the Social Security Administration,
and the Railroad Retirement Board

Department of the Treasury

January 2009

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

JAN 16 2003

The Honorable Richard Cheney
President of the Senate
Washington, DC 20510

Dear Mr. President:

Section 121 of the Social Security Amendments of 1983 (P.L. 98-21), directs the Secretary of the Treasury to transfer from the general fund of the Treasury to the Social Security and Railroad Retirement trust funds amounts equivalent to the tax liabilities attributable to the taxation of Social Security and Railroad Retirement benefits. Section 121 further provides that the Secretary of the Treasury shall submit annual reports concerning (1) the transfers made that year, and the methodology used in determining the amount of such transfers and the funds of accounts to which made, and (2) the anticipated operation of the transfers during the next five years.

Pursuant to Section 121, I am pleased to submit the "Report on the Taxation of Social Security and Railroad Retirement Benefits in Calendar Years 1997 through 2004."

This report is also being transmitted to the Speaker of the House, the Secretary of the Department of Health and Human Services, the Commissioner of the Social Security Administration, and the Chairman of the Railroad Retirement Board.

Sincerely,

Kevin I. Fromer
Assistant Secretary for Legislative Affairs

cc: The Honorable Clifford C. Eby
Administrator (Acting), Federal Railroad Administration

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

JAN 16 2009

The Honorable Nancy Pelosi
Speaker of the House of Representatives
Washington, DC 20515

Dear Madam Speaker:

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INTRODUCTION AND SUMMARY

I. Introduction

Since January of 1984, the Treasury Department has been required to estimate the individual income tax liabilities attributable to the inclusion of Social Security (Federal Old Age and Survivors and Federal Disability Insurance) and Railroad Social Security Equivalent benefits in adjusted gross income (AGI) for each liability year. These estimated liabilities are transferred from the general fund to the Federal Old Age and Survivors Insurance (FOASI), Federal Disability Insurance (FDI), and Railroad Social Security Equivalent Benefit Account (SSEBA) trust funds on a quarterly basis. Since 1994, transfers have also been made to the Federal Hospital Insurance (Medicare) trust fund (FHI). The amounts transferred to these trust funds are calculated as the difference between forecasts of tax liabilities made with and without the inclusion of forecasted levels of benefits in AGI. Both the taxation of benefits and the transfers to the trust funds are required by the Social Security Amendments of 1983 (P.L. 98-21), as amended by the Railroad Retirement Solvency Act of 1983 (P.L. 98-76), the Consolidated Budget Reconciliation Act of 1985 (P.L. 99-272), and the Omnibus Budget and Reconciliation Act of 1993 (OBRA 93) (P.L. 103-66). P.L. 98-21 also requires that correcting adjustments be made to the amounts transferred to the trust funds if the estimates of the tax liability attributable to the benefits are subsequently shown to be incorrect.

In addition, P.L. 98-21 requires the Treasury Department to submit annual reports to the Congress, the Secretary of Health and Human Services, and the Railroad Retirement Board containing both a description of the methodology used to estimate the transfers to the trust funds and a forecast of transfers over the five subsequent years. The Treasury Department's Office of Tax Analysis (OTA) is responsible for preparing these annual reports, as well as for estimating transfers to the trust funds and calculating correcting adjustments to the transfers based on actual tax return data. This report covers an eight year period, and describes (1) the transfers to the trust funds for calendar years 1997 through 2004, (2) the necessary correcting adjustments to the transfers for calendar years 1997 through 2004, and (3) the forecast of liability and transfers for calendar years 2005 through 2009.[1]

To determine if any benefits were taxable in calendar years 1997 through 2004, taxpayers had to add both tax-exempt interest income and one-half of Social Security and Railroad Social Security Equivalent benefits to AGI. This augmented AGI is referred to as provisional income. If provisional income exceeded thresholds of $25,000 for single filers and $32,000 for joint filers, taxpayers were required to include in AGI the lesser of one-half of the benefits or one-half of the excess of provisional income over the thresholds. If provisional income exceeded $34,000 for single filers and $44,000 for joint filers, taxpayers were required to include in AGI the lesser of:

(1) 85 percent of the recipient's Social Security or Railroad Social Security Equivalent benefit

or

(2) the sum of

(a) the smaller of (i) the amount included under the lower thresholds or (ii) $4,500 (for single filers) or $6,000 (for joint filers)

plus

(b) 85 percent of the excess of the recipient's provisional income over the applicable second provisional income threshold.[2]

Certain married beneficiaries not filing joint returns had a provisional income threshold of zero. The adjusted gross income of these individuals included the lesser of 85 percent of the beneficiary's Social Security or Railroad Social Security Equivalent benefit or 85 percent of the recipient's provisional income. Therefore, for the highest income beneficiaries, a maximum of 85 percent of Social Security or Railroad Social Security Equivalent benefits was includable in AGI. None of the provisional income thresholds are indexed for inflation.

For beneficiaries whose provisional incomes are above the first threshold but below the second threshold, the tax liabilities attributable to the included benefits are transferred to the FOASI and FDI (Social Security) trust funds and the Railroad Social Security Equivalent benefit trust fund. For beneficiaries whose provisional incomes are above the second threshold, the tax liabilities attributable to the additional included benefits are transferred to the FHI (Medicare) trust fund.

To summarize, the Office of Tax Analysis estimates the income tax liability attributable to the partial inclusion of FOASI, FDI and SSEBA benefits in adjusted gross income and estimates the amounts to be transferred to the corresponding trust funds plus the FHI (Medicare) trust fund.[3] Subsequently, OTA makes adjustments to correct the amounts put into each fund. Throughout the report, some tables will show benefits and/or tax liability by income source (FOASI, FDI or SSEBA benefits) while others will show the amounts transferred to the various trust funds (FOASI, FDI, SSEBA or FHI).

II. Summary

The Summary Table shows OTA's original tax liability estimates by benefit source and the transfers made to the trust funds based on those estimates, the adjusting transfers subsequently made, and the resulting net amounts transferred to each trust fund for each calendar year. For example, for calendar year 1997, OTA initially estimated that the tax liability attributable to partial inclusion of Social Security and Railroad Social Security Equivalent benefits was $12,936 million. Based on this estimate, transfers of $7,561 million, $458 million, $4,856 million, and $61 million were made from the general fund to the FOASI, FDI, FHI, and SSEBA trust funds, respectively. OTA subsequently determined that

the amount of tax liability calculated from actual 1997 tax return data exceeded the amount transferred by $1,461 million. Transfers to the FOASI, FDI, FHI, and SSEBA trust funds were understated by $793 million, $37 million, $606 million, and $25 million, respectively. Correcting adjustments to the FOASI, FDI, and SSEBA trust funds were made in July 2000 and October 2001. Correcting adjustments to the FHI trust fund were made in September 2000 and September 2001.[4] The resulting net amount transferred for calendar year 1997 liability was $14,397 million. Of this amount, $8,354 was transferred to the FOASI trust fund, $495 million was transferred to the FDI trust fund, $5,462 was transferred to the FHI trust fund, and $86 million was transferred to the SSEBA trust fund.

This report provides the detail supporting the tax liability and transfer amounts. Chapter 1 presents OTA's methodology for estimating the tax liability attributable to the inclusion of benefits in AGI and presents a comparison of estimates to actual amounts of income tax liability calculated from tax return data for calendar years 1997 through 2004. Chapter 2 presents the methodologies for estimating the initial amounts to be transferred to the trust funds and the subsequent correcting adjustments. The chapter also presents those initial transfer amounts and the correcting adjustments for 1997 through 2004 liabilities. Chapter 3 presents the forecast of transfers of estimated amounts to the trust funds for calendar years 2005 through 2009. Chapter 4 describes the distribution of taxable benefits by income class for calendar years 1997 through 2004. It also contains an analysis of the sources of provisional income for taxpayers with taxable benefits for the 1995 through 2004 period.

Summary Table

	Calendar Years; Millions of Dollars							
	1997	1998	1999	2000	2001	2002	2003	2004
Original Liability Estimate Attributable To								
FOASI Benefits	12,169	14,645	15,145	17,579	19,443	19,633	18,841	20,754
FDI Benefits	674	853	881	1,070	1,219	1,300	1,265	1,505
SSEBA Benefits	93	121	124	157	151	150	152	163
Total Original Liability Estimates	12,936	15,619	16,150	18,806	20,813	21,083	20,258	22,422
Original Transfers Made To								
FOASI Trust Fund	7,561	9,003	9,219	10,445	11,982	12,574	11,466	12,831
FDI Trust Fund	458	552	572	662	822	902	851	1,017
FHI Trust Fund	4,856	5,990	6,280	7,597	7,915	7,510	7,844	8,465
SSEBA Trust Fund	61	74	79	102	94	97	97	109
Total Original Transfers	12,936	15,619	16,150	18,806	20,813	21,083	20,258	22,422
Subsequent Correcting Adjustments Made To								
FOASI Trust Fund Transfers	793	189	885	1,614	48	-1,135	-842	-1,167
FDI Trust Fund Transfers	37	22	88	88	-27	-92	-95	-102
FHI Trust Fund Transfers	606	181	655	807	357	143	-796	-515
SSEBA Trust Fund Transfers	25	14	15	3	6	-4	-12	-18
Total Trust Fund Transfers	1,461	406	1,643	2,512	384	-1,088	-1,745	-1,802
Net Amounts Transferred To								
FOASI Trust Fund	8,354	9,192	10,104	12,059	12,030	11,439	10,624	11,664
FDI Trust Fund	495	574	660	750	795	810	756	915
FHI Trust Fund	5,462	6,171	6,935	8,404	8,272	7,653	7,048	7,950
SSEBA Trust Fund	86	88	94	105	100	93	85	91
Total Net Amounts	14,397	16,025	17,793	21,318	21,197	19,995	18,513	20,620

Department of the Treasury
Office of Tax Analysis

CHAPTER 1: METHODOLOGY AND ESTIMATES OF THE TAX LIABILITY ATTRIBUTABLE TO THE TAXATION OF BENEFITS FOR CALENDAR YEARS 1997 THROUGH 2004

I. Methodology for Estimating Tax Liability

The Office of Tax Analysis (OTA) is responsible for estimating the annual tax liability attributable to the partial inclusion of Social Security and Railroad Social Security Equivalent benefits received in AGI, making quarterly transfers from the general fund to the trust funds based on these estimates, and calculating correcting adjustments to amounts initially transferred. OTA provides this information to the Treasury Department's Financial Management Services, which has the authority to transfer funds between the general revenue fund and the trust funds as necessary.

OTA estimated the amount of tax liability for each of the years 1997 through 2004 attributable to the inclusion of Social Security benefits in AGI using results from OTA's Individual Income Tax Model (ITM).[5, 6] The ITM is OTA's primary tool for preparing revenue estimates and analyzing taxpayer behavior. For this application, the ITM was used to account for changes in other tax provisions resulting from the inclusion of benefits in AGI. That is, the use of deductions and credits, as well as the calculations of alternative minimum tax liabilities, can be affected by the inclusion of benefits in AGI.[7]

The ITM is built on a stratified random sample of individual income tax returns contained in the Internal Revenue Service's Statistics of Income (SOI) file. ITM computations are weighted to produce results that are representative of the entire population of taxpayers. Tax returns alone, however, do not provide sufficient data to estimate the tax liability effects of the partial inclusion of Social Security and Railroad Social Security Equivalent benefits in AGI. Therefore, imputations are added to the ITM to compensate for the missing data. The Social Security Administration and the Railroad Retirement Board provide information on the total amounts of benefits paid to recipients. These amounts are distributed among appropriate taxpayers on the ITM using, as a guide, two important data sources: (1) a file of Form SSA-1099 and Form RRB-1099 information returns that are matched to the SOI file; and (2) Current Population Survey data from the Census Bureau to aid in matching benefits to recipients who were not required to file a tax return. Records on the ITM are extrapolated to future years in accordance with the President's macroeconomic forecast in use at the time of the extrapolation. As part of the extrapolation, total Social Security and Railroad Social Security Equivalent benefits are projected to grow at the rate indicated in the benefits forecast provided by the Social Security Administration and the Railroad Retirement Board.

The base year for the ITM extrapolation is updated approximately every three years. Estimates for tax years 1997 through 2000 were made using a 1995-based ITM. That is, OTA extrapolated sample tax returns, SSA-1099 forms, RRB-1099 forms, and CPS data for 1995. Estimates for tax years 2001 through 2003 were made using a 1998-based ITM. OTA extrapolated sample tax returns, SSA-1099 forms, RRB-1099 forms and CPS data for 1998.

Estimates for 2004 were made using a 2001-based ITM. OTA extrapolated sample tax returns, SSA-1099 forms, RRB-1099 forms and CPS data for 2001.

The ITM uses the tax return information, the imputations, and extrapolations to estimate the level of Social Security and Railroad Social Security Equivalent benefits included in AGI and the Federal income tax liability attributable to the inclusion of those benefits for all of the filing units on the model. To do this, each tax unit's liability is estimated with and without the inclusion of benefits. The difference between those two levels of tax liability equals the tax liability attributable to the inclusion of benefits. The ITM results are used to calculate both the percentage of total benefits included in AGI and the average effective marginal tax rates applicable to the taxable benefits. Final estimates of tax liability attributable to the partial inclusion of benefits are produced using a spreadsheet-based model. This model blends the estimates of the percent of benefits in AGI and the average effective marginal tax rates with more recent tax return information (not available when the ITM is extrapolated) and the most current tax collection information.

The Social Security Amendments of 1983 require adjustments to the trust funds if actual tax return data subsequently reveal that the initial transfers were incorrect. To calculate the actual tax liability for each of the calendar years 1997 through 2004, the IRS created data files for each year based on Form 1040 records. All filers who reported taxable Social Security or Railroad Social Security Equivalent benefits on their Form 1040 were included in these data files (as opposed to the data used to determine the original transfer estimates, which are sample data). The methodology for determining the adjustments is discussed in Chapter 2, Section II.

II. Estimates of Tax Liability Attributable to the Taxation of Benefits in Calendar Years 1997 to 2004

Tables 1.A through 1.H compare the assumptions and parameters used to determine the estimates of tax liability with the parameters calculated from actual tax return and benefit data for each calendar year from 1997 to 2004. As noted above, the former are determined from a base year of SOI sample data, other data sources, and an extrapolation algorithm while the latter are based on IRS population data. The patterns of benefit inclusion and tax liability are generally constant for each calendar year.

For example, the top section of Table 1.A shows that OTA estimated that $54,856 million of $366,793 million in total benefits (14.96 percent) would be included in AGI for calendar year 1997. The estimated tax liability attributable to those benefits was $12,936 million, for an average effective marginal tax rate of 23.58 percent. The bottom section of the table shows that, based on calendar year 1997 tax return and benefits data, $60,897 million of $366,201 million in total benefits (16.63 percent) were included in AGI. The actual tax liability attributable to those benefits was $14,397 million, for an average effective marginal tax rate of 23.64 percent.

Continuing the example, the total liability estimate for calendar year 1997 was the sum of the estimates of the tax liability attributable to the partial inclusion of FOASI, FDI,

and SSEBA benefits. The top section of Table 1.A shows that OTA estimated that $51,045 million of $314,703 million of FOASI benefits (16.22 percent) would be included in AGI. The estimated tax liability attributable to those benefits was $12,169 million, for an average effective marginal tax rate of 23.84 percent. The bottom section of the table shows that, based on calendar year 1997 tax return and benefits data, $56,630 million of $315,477 million in FOASI benefits (17.95 percent) were included in AGI. The actual tax liability attributable to those benefits was $13,503 million, for an average effective marginal tax rate of 23.84 percent.

Recipients of FDI benefits have, on average, lower incomes than FOASI beneficiaries. Therefore, the estimated inclusion rates for benefits in AGI and average effective marginal tax rates for FDI beneficiaries are lower than those for FOASI recipients. The top section of Table 1.A shows that OTA estimated that $3,348 million of $47,050 million in FDI benefits (7.12 percent) would be included in AGI. The estimated tax liability attributable to those benefits was $674 million, for an average effective marginal tax rate of 20.13 percent. The bottom section of the table shows that, based on calendar year 1997 tax return and benefits data, $3,705 million of $45,660 million in FDI benefits (8.11 percent) were included in AGI. The actual tax liability attributable to those benefits was $767 million, for an average effective marginal tax rate of 20.70 percent.

Railroad SSEBA beneficiaries have, on average, incomes that are slightly lower than FOASI beneficiaries but higher than FDI recipients. The top section of Table 1.A shows that OTA estimated that $463 million of $5,040 million in SSEBA benefits (9.19 percent) would be included in AGI. The estimated tax liability attributable to those included benefits was $93 million, for an average effective marginal tax rate of 20.08 percent. The bottom section of the table shows that, based on calendar year 1997 tax return and benefits data, $562 million of $5,064 million in SSEBA benefits (11.10 percent) were included in AGI. The actual tax liability attributable to included SSEBA benefits was $127 million, for an average effective marginal tax rate of 22.60 percent.

Table 1.A
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 1997 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	314,703	51,045	16.22%	12,169	23.84%
Federal Disability Insurance	47,050	3,348	7.12%	674	20.13%
Railroad Social Security Equivalent Benefits	5,040	463	9.19%	93	20.08%
Total	366,793	54,856	14.96%	12,936	23.58%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	315,477	56,630	17.95%	13,503	23.84%
Federal Disability Insurance	45,660	3,705	8.11%	767	20.70%
Railroad Social Security Equivalent Benefits	5,064	562	11.10%	127	22.60%
Total	366,201	60,897	16.63%	14,397	23.64%

Department of the Treasury
Office of Tax Analysis

1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

Table 1.B
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 1998 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	326,347	61,720	18.91%	14,645	23.73%
Federal Disability Insurance	48,393	4,103	8.48%	853	20.79%
Railroad Social Security Equivalent Benefits	5,082	551	10.84%	121	21.97%
Total	379,822	66,374	17.48%	15,619	23.53%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	326,189	62,811	19.26%	14,999	23.88%
Federal Disability Insurance	48,182	4,328	8.98%	895	20.68%
Railroad Social Security Equivalent Benefits	5,089	608	11.95%	131	21.55%
Total	379,460	67,747	17.85%	16,025	23.65%

Department of the Treasury
Office of Tax Analysis

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Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

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Table 1.C
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 1999 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	334,466	64,304	19.23%	15,145	23.55%
Federal Disability Insurance	51,068	4,270	8.36%	881	20.63%
Railroad Social Security Equivalent Benefits	5,078	569	11.20%	124	21.81%
Total	390,612	69,142	17.70%	16,150	23.36%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	333,847	68,532	20.53%	16,611	24.24%
Federal Disability Insurance	51,359	4,951	9.64%	1,038	20.97%
Railroad Social Security Equivalent Benefits	5,076	664	13.08%	144	21.69%
Total	390,282	74,147	19.00%	17,793	24.00%

Department of the Treasury
Office of Tax Analysis

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The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

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Table 1.D
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 2000 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	352,195	75,815	21.53%	17,579	23.19%
Federal Disability Insurance	54,922	4,960	9.03%	1,070	21.57%
Railroad Social Security Equivalent Benefits	5,100	702	13.76%	157	22.38%
Total	412,216	81,476	19.77%	18,806	23.08%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	352,109	81,649	23.19%	19,974	24.46%
Federal Disability Insurance	54,961	5,691	10.35%	1,182	20.77%
Railroad Social Security Equivalent Benefits	5,125	751	14.66%	162	21.57%
Total	412,195	88,091	21.37%	21,318	24.20%

Department of the Treasury
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1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

Table 1.E
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 2001 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	372,385	84,466	22.68%	19,443	23.02%
Federal Disability Insurance	59,714	5,949	9.96%	1,219	20.49%
Railroad Social Security Equivalent Benefits	5,207	755	14.51%	151	19.99%
Total	437,306	91,171	20.85%	20,813	22.83%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	371,770	84,315	22.68%	19,797	23.48%
Federal Disability Insurance	59,596	6,239	10.47%	1,248	20.00%
Railroad Social Security Equivalent Benefits	5,225	733	14.04%	152	20.72%
Total	436,591	91,287	20.91%	21,197	23.22%

Department of the Treasury
Office of Tax Analysis

1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

Table 1.F
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 2002 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	387,349	92,109	23.78%	19,633	21.32%
Federal Disability Insurance	68,856	6,704	9.74%	1,300	19.39%
Railroad Social Security Equivalent Benefits	5,283	775	14.67%	150	19.35%
Total	461,488	99,587	21.58%	21,083	21.17%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	387,546	84,406	21.78%	18,647	22.09%
Federal Disability Insurance	65,680	6,344	9.66%	1,207	19.03%
Railroad Social Security Equivalent Benefits	5,269	719	13.65%	141	19.61%
Total	458,495	91,469	19.95%	19,995	21.86%

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1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

Table 1.G
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 2003 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	398,920	88,188	22.11%	18,841	21.36%
Federal Disability Insurance	70,575	6,717	9.52%	1,265	18.83%
Railroad Social Security Equivalent Benefits	5,308	802	15.11%	152	18.95%
Total	474,803	95,707	20.16%	20,258	21.17%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	399,272	84,315	21.12%	17,202	20.40%
Federal Disability Insurance	70,913	6,239	8.80%	1,184	18.98%
Railroad Social Security Equivalent Benefits	5,285	733	13.88%	127	17.31%
Total	475,470	91,287	19.20%	18,513	20.28%

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1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

Table 1.H
Comparison of Parameters Used to Estimate Tax Liability Attributable to the Partial Inclusion of Benefits in AGI with Parameters Calculated from Actual Amounts
Calendar Year 2004 /1

Benefit Source	Total Benefits Paid /2	Benefits Includable in AGI /2	Percent of Total Benefits Includable in AGI	Tax Liabilities on Benefits Includable In AGI /2	Average Effective Marginal Tax Rate on Benefits Includable In AGI
			Estimate Parameters /3		
Federal Old-Age and Survivors Insurance	426,997	104,810	24.55%	20,754	19.80%
Federal Disability Insurance	83,224	8,446	10.15%	1,505	17.82%
Railroad Social Security Equivalent Benefits	5,340	935	17.51%	163	17.43%
Total	515,562	114,191	22.15%	22,422	19.64%
			Actual Parameters /4		
Federal Old-Age and Survivors Insurance	414,456	97,468	23.52%	19,030	19.52%
Federal Disability Insurance	78,208	8,712	11.14%	1,452	16.67%
Railroad Social Security Equivalent Benefits	5,359	800	14.93%	138	17.24%
Total	498,023	106,981	21.48%	20,620	19.27%

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1/ Estimated tax liabilities were updated on a semi-annual basis to conform with updates to the President's macroeconomic assumptions.
The table compares the parameters used in the final estimates of tax liability with the parameters derived from actual tax return and benefits data.
Rounding of results may prevent exact matching of total. Benefits paid to non-resident aliens are not included in the FOASI or FDI benefits paid figures.

2/ Benefits amounts and tax liabilities in millions of dollars, excluding benefits paid to non-resident aliens.

3/ The total benefits paid data are estimates provided by the Social Security Administration and the Railroad Retirement Board; the other data are estimated from the Office of Tax Analysis Individual Income Tax Model.

4/ The total benefits paid data are derived from the 2007 Annual Statistical Supplement to the Social Security Bulletin (Tables 4.A1 and 4.A2), the Social Security Administration and the Railroad Retirement Board; the Benefits in AGI and tax liability data come from the Internal Revenue Service's Individual Master File.

CHAPTER 2: METHODOLOGY FOR ESTIMATING TRANSFERS AND CALCULATING ADJUSTMENTS TO TRANSFERS OF LIABLITY IN CALENDAR YEARS 1997 THROUGH 2004

I. Methodology for Estimating Quarterly Transfer Amounts

Based on the estimates of annual liability given in Chapter 1, the Department of the Treasury's Office of Tax Analysis constructed estimates of the quarterly transfers from the general fund to the FOASI, FDI, FHI, and SSEBA trust funds. Since OBRA 93 created the second thresholds for inclusion of benefits in AGI, and directed that the additional tax liability be directed to the FHI trust fund, OTA estimated the annual liability attributable to the inclusion of FOASI, FDI, and SSEBA benefits in AGI on both a pre-OBRA 93 and a post-OBRA 93 basis. The amounts of liability transferable to the FOASI, FDI, and SSEBA trust funds were the pre-OBRA 93 liability estimates. The amount of liability transferable to the FHI trust fund was taken as the difference between the post-OBRA 93 total liability estimate and the pre-OBRA 93 total liability estimate. OTA then estimated the quarterly transfer amounts associated with the current and subsequent calendar years. Separate methodologies were used to transfer the pre-OBRA 93 and post-OBRA 93 quarterly amounts due to differences in statutory requirements.

With respect to pre-OBRA 93 transfers, statutory requirements dictate that liability should be transferred quarterly as it accrues. Therefore, the quarterly transfers are made on the first day of the calendar quarters beginning with the months of January, April, July, and October. For a given liability year, the total amounts transferable to the FOASI, FDI, or SSEBA trust funds are the amounts of liability estimated from the most recent forecast of estimated annual liability, less any amounts of liability already transferred for that year. This net difference is divided over the remaining quarters still available for transfers.

With respect to post-OBRA 93 transfers, statutory requirements dictate that liability should be transferred quarterly as it is collected. Therefore, that calendar year liability is transferred in five installments, representing four quarterly estimated payments and one final payment of liability. Transfers to the FHI trust fund are made on the fifteenth day of the quarter beginning with the months April, June, September, and January. The total April 15 transfer to the FHI trust fund always contains two installments – one estimated payment for the current year's liability and one final payment for the prior year's liability. For a given liability year, the total amount transferable to the FHI trust fund is the amount of liability estimated from the most recent forecast of estimated annual liability, less any amounts of liability already transferred for that year. This net difference is divided over the remaining installment periods still available for transfers.

II. Methodology for Adjustments to Transfers of Estimated Amounts

The Social Security Amendments of 1983 require adjustments to the trust funds if actual tax return data subsequently reveal that the initial transfers were incorrect. To calculate the actual tax liability for each of the calendar years 1997 through 2004 resulting from the partial taxation of Social Security and Railroad Social Security Equivalent benefits, the IRS creates data files for each year based on Form 1040 records. All filers who report taxable Social Security or Railroad Social Security Equivalent benefits on their Form 1040 are included in these data files. Although the Form 1040 provides information on the total amount of benefits includable in taxable income, it does not indicate whether the filer received FOASI, FDI, or SSEBA benefits. Such information is needed to allocate revenues accurately to the trust funds. To obtain this information, the Form 1040 records belonging to those beneficiaries who reported taxable benefits are matched to Form SSA-1099 records provided by the Social Security Administration and Form RRB-1099 records provided by the Railroad Retirement Board.[8]

Using this matched file of Form 1040 and Form SSA-1099 and RRB-1099 records, the IRS calculates the tax liability attributable to the taxation of Social Security and Railroad Social Security Equivalent benefits, for both pre-OBRA 93 and post-OBRA 93 liability. For each taxpayer, the total tax liability attributable to the taxation of benefits is calculated as the difference between tax liability with and without benefits included in AGI. The pre-OBRA 93 tax liability is calculated as the difference between tax liability with benefits includable under pre-OBRA 93 law and with no included benefits. The post-OBRA 93 tax liability is the difference between the total tax liability and the pre-OBRA 93 tax liability. The total difference taken over all taxpayers equals the tax liability attributable to the taxation of benefits.

After comparing the IRS liability calculations with the OTA liability estimates, OTA calculates adjustments to the original transfers. These adjustment amounts are equal to the difference between the IRS liability calculations and OTA's original liability estimates. The adjustment amounts are included in the transfer amounts in the first quarter following their determination. Thus, the net transfer for that quarter reflects the transfer for the current period liability and the adjustment to the estimate of prior period liability.

III. Transfers of Estimated Amounts and Adjustments to Transfers for Liability in Calendar Years 1997 through 2004

Table 2 shows the estimated liability amounts transferred to the FOASI, FDI, FHI and SSEBA trust funds in each calendar year from 1997 to 2004. For example, in calendar year 1997, total transfers of $7,561 million, $458 million, and $61 million were made to the FOASI, FDI, and SSEBA trust funds, respectively, and total transfers of $4,856 million were made to the FHI trust fund. As noted in section I, amounts were transferred quarterly to the FOASI, FDI and SSEBA trust funds between January 1 and October 1 of the relevant year. Amounts were transferred quarterly to the FHI trust fund between April 15th of the relevant year and April 15th of the succeeding year.

Table 2 also shows the IRS calculations of final trust fund amounts, and the resulting adjustments to the FOASI, FDI, FHI, and SSEBA trust funds due to the reconciliation of OTA estimates and IRS calculations. For example, as a result of the reconciliation of estimated and actual 1997 tax liability, adjustments of $793 million, $37 million, $606 million, and $25 million were made, for the FOASI, FDI, FHI, and SSEBA trust funds, respectively. The final column of Table 2 shows the quarter in which each adjustment was made.

Table 2
Comparison of OTA Estimated Transfers, IRS Calculated Transfers, and Corresponding Adjustments for Calendar Years 1997 to 2004 /1

Year and Trust Fund	OTA Estimated Transfers	IRS Calculated Transfers	Adjustment Amount	Adjustment Quarter
CY 1997 Liability				
FOASI	7,561	8,354	793	/2
FDI	458	495	37	/2
FHI	4,856	5,462	606	/2
SSEBA	61	86	25	/2
Total	12,936	14,397	1,461	
CY 1998 Liability				
FOASI	9,003	9,192	189	October 1, 2002
FDI	552	574	22	October 1, 2002
FHI	5,990	6,171	181	September 15, 2002
SSEBA	74	88	14	October 1, 2002
Total	15,619	16,025	406	
CY 1999 Liability				
FOASI	9,219	10,104	885	October 1, 2003
FDI	572	660	88	October 1, 2003
FHI	6,280	6,935	655	September 15, 2003
SSEBA	79	94	15	October 1, 2003
Total	16,150	17,793	1,643	
CY 2000 Liability				
FOASI	10,445	12,059	1,614	October 1, 2004
FDI	662	750	88	October 1, 2004
FHI	7,597	8,404	807	September 15, 2004
SSEBA	102	105	3	October 1, 2004
Total	18,806	21,318	2,512	
CY 2001 Liability				
FOASI	11,982	12,030	48	April 1, 2006
FDI	822	795	-27	April 1, 2006
FHI	7,915	8,272	357	June 15, 2006
SSEBA	94	100	6	April 1, 2006
Total	20,813	21,197	384	
CY 2002 Liability				
FOASI	12,574	11,439	-1,135	April 1, 2008
FDI	902	810	-92	April 1, 2008
FHI	7,510	7,653	143	January 15, 2008
SSEBA	97	93	-4	April 1, 2008
Total	21,083	19,995	-1,088	
CY 2003 Liability				
FOASI	11,466	10,624	-842	July 1, 2008
FDI	851	756	-95	July 1, 2008
FHI	7,844	7,048	-796	September 15, 2008
SSEBA	97	85	-12	July 1, 2008
Total	20,258	18,513	-1,745	
CY 2004 Liability				
FOASI	12,831	11,664	-1,167	October 1, 2008
FDI	1,017	915	-102	October 1, 2008
FHI	8,465	7,950	-515	January 15, 2009
SSEBA	109	91	-18	October 1, 2008
Total	22,422	20,620	-1,802	

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1/ Amounts in millions of dollars.

2/ This adjustment was made in two steps. Preliminary adjustments of $1,010 million, $53 million, and $26 million to the FOASI, FDI, and SSEBA trust funds, respectively, were included with the July 1, 2000 transfer. A preliminary adjustment of $813 million to the FHI trust fund was included with the September 15, 2000 transfer. Subsequent to these adjustments, IRS issued new totals for calendar year 1997 tax liability. Second adjustments of -$217 million, -$16 million, and -$1 million to the FOASI, FDI, and SSEBA trust funds, respectively, were included with the October 1, 2001 transfer. A second adjustment of -$207 million to the FHI trust fund was included with the September 15, 2001 transfer. The total net adjustments were adjustments of $793 million, $37 million, $606 million, and $25 million, for the FOASI, FDI, FHI, and SSEBA trust funds, respectively.

CHAPTER 3: FORECAST OF TRANSFERS TO TRUST FUNDS FOR CALENDAR YEARS 2005 TO 2009

I. Forecasting Methodology

The Social Security Amendments of 1983 require that the annual report include a forecast of transfers to the trust funds for the next five years. The forecast years are currently calendar years 2005 to 2009, since no correcting adjustments have been made to those years' liability transfers. This forecast was produced using the same methods that were used to produce the initial estimates of calendar year 1997 through 2004 liability, described in Chapter 1. The calendar year forecasts for 2005 and 2006 were produced using results from the 2001-based ITM described in that chapter while the 2007 through 2009 forecasts were produced using results from a comparable ITM based on 2004 SOI data and imputations.

As noted in Chapter 2, tax returns alone do not provide sufficient data to estimate the revenue effects of the partial inclusion of Social Security and Railroad Social Security Equivalent benefits in AGI. Therefore, imputations of total Social Security and Railroad Social Security Equivalent benefits are added to both the 2001-based and 2004-based versions of the ITM to compensate for the missing data. In both cases, the total benefit amounts are distributed among appropriate recipients on the ITM using Form SSA-1099 and Form RRB-1099 information returns that are matched to the tax returns in the SOI files. In both versions, the most recent Current Population Survey data from the Census Bureau is used as a guide to the non-filing population.

The cross-sectional records on both versions of the ITM are extrapolated to future years in accordance with the President's macroeconomic forecast in use at the time of the extrapolation. As part of the extrapolation, total benefits are projected to grow at the rates indicated in the forecasts provided by the Social Security Administration and the Railroad Retirement Board.

II. Forecast of Transfers to the Trust Funds

The estimates of liability incurred in calendar years 2005 through 2009 and the amounts transferred to the trust funds are presented in Table 3. The transfers of estimated liability for 2005 through 2007 have been completed and include adjustments attributable to prior years' liabilities. The FOASI, FDI, FHI, and SSEBA transfers for calendar year 2006 liability include adjustments due to the reconciliation of calendar year 2001 estimated and actual liabilities. The FHI transfer for calendar year 2007 liability includes an adjustment due to the reconciliation of calendar year 2002 estimated and actual liability. The FOASI, FDI and SSEBA transfers for calendar year 2008 liability include adjustments due to the reconciliation of calendar year 2002 estimated and actual liability. The FOASI, FDI, FHI and SSEBA transfers for calendar year 2008 liability also include adjustments due the reconciliation of calendar year 2003 and calendar year 2004 estimated and actual liability. For the liability attributable to the partial inclusion of Social Security and Railroad Retirement benefits in AGI incurred in calendar years 2005 through 2009, OTA forecasts

that $87,390 million, $7,302 million, $60,650 million, and $696 million will be transferred from general revenues to the FOASI, FDI, FHI, and SSEBA trust funds. These transfers will be adjusted for prior periods' liabilities. The adjustments will total -$3,096 for FOASI, -$316 for FDI, -$811 for FHI, and -$28 for SSEBA. The net transfer to the trust funds is estimated to be $151,787 million.

Table 3
Forecast of Transfers, Net of Adjustments,
to the FOASI, FDI, FHI, and SSEBA Trust Funds
for Calendar Year Liability in 2005 to 2009

Calendar Year Liability in Millions of Dollars

	Completed Transfers			Estimated Transfers		Totals
Trust Fund	2005	2006	2007	2008	2009	2005-2009
FOASI						
Estimated Transfer /1	13,698	15,437	17,047	18,564	22,644	87,390
Prior Year Adjustment /2	0	48	0	-3,144	0	-3,096
Net Transfer	13,698	15,485	17,047	15,420	22,644	84,294
FDI						
Estimated Transfer /1	1,068	1,253	1,389	1,598	1,994	7,302
Prior Year Adjustment /2	0	-27	0	-289	0	-316
Net Transfer	1,068	1,226	1,389	1,309	1,994	6,986
FHI						
Estimated Transfer /1	9,354	10,108	11,774	12,996	16,418	60,650
Prior Year Adjustment /2	0	357	143	-1,311	0	-811
Net Transfer	9,354	10,465	11,917	11,685	16,418	59,839
SSEBA						
Estimated Transfer /1	117	125	135	144	175	696
Prior Year Adjustment /2	0	6	0	-34	0	-28
Net Transfer	117	131	135	110	175	668
Totals						
Estimated Transfer /1	24,237	26,923	30,345	33,302	41,231	156,038
Prior Year Adjustment /2	0	384	143	-4,778	0	-4,251
Net Transfer	24,237	27,307	30,488	28,524	41,231	151,787

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Notes:

1/ Estimated Transfers are amounts transfered to the trust funds for liability incurred in the year indicated. Note that the final two estimated liabilty transfers to the FHI trust fund for a given year actually occur in January and April of the following year.

2/ Prior Year Adjustments are amount transferred to or from the trust funds that correct the original estimated liabilities transferred for prior years. Because the final two estimated liability transfers to the FHI trust fund for a given year occur in January and April of the following year, a Prior Year Adjustment to a given year's FHI estimated transfer may actually occur in the next year:

Adjustments made to CY 2006 liability were for liability incurred in CY 2001. Adjustments to the FOASI, FDI and SSEBA trust funds were made in July. Adjustments to the FHI trust fund were made in June.

Adjustments made to CY 2007 liability were for liability incurred in CY 2002. The adjustment to the FHI trust fund was made in January 2008.

Adjustments made to CY 2008 liability were for liability incurred in CY 2002, CY 2003 and CY 2004. Adjustments to the FOASI, FDI and SSEBA trust funds were made in April (for CY 2002 liability), July (for CY 2003 liability) and October (for CY 2004 liability). Adjustments to the FHI trust fund were made in September 2008 (for CY 2003 liability) and January 2009 (for CY 2004 liability).

CHAPTER 4: DISTRIBUTION OF TAXABLE BENEFITS AND ANALYSIS OF PROVISIONAL INCOME SOURCES

I. Distribution of Taxable Benefits by Provisional Income Class for Calendar Years 1997 Through 2004

This section presents a distributional analysis of taxable Social Security and Railroad Social Security Equivalent benefits. The tabulations were made using the 1997 through 2004 SOI samples and the tax calculators attached to each. Note that since the tables in this chapter are based on sample data, the statistics shown are subject to sampling error. In particular, the tax liabilities presented in 4.A through 4.H do not exactly match the population totals provided by the IRS and presented in the bottom sections of Tables 1.A through 1.H. (See the discussion in Chapter 3, Section II.)

Tables 4.A through 4.H summarize the benefit inclusion rates and average marginal tax rates on benefits for families with taxable benefits by provisional income class for calendar years 1997 through 2004. Provisional income is AGI (excluding Social Security and Railroad Social Security Equivalent benefits included in AGI) plus tax exempt interest income plus one-half Social Security and Railroad Social Security Equivalent benefits.

The tables show that, on average, families with taxable benefits included 58 percent of their benefits in AGI from 1997 through 2004. The tables also show how the benefit inclusion rates rise as provisional income rises. In each year, returns with provisional income of $30,000 or less include only about 14 percent of benefits in AGI while returns with provisional income of $75,000 or more include 85 percent of benefits in AGI. Since provisional income is somewhat correlated with the business cycle, benefit inclusion rates rise and fall over the period. Overall, the benefit inclusion rate peaked at 59 percent in 1999 and 2000 and troughed at 56 percent in 2003.

Tables 4.A through 4.H also show that the average marginal tax rate rises with provisional income. Returns with provisional income of $30,000 or less faced a tax rate on included benefits of 14 percent in 1997 while returns with provisional income over $200,000 faced a tax rate of 35 percent. This pattern is apparent in all years.

The tables also show that for each group, the average marginal tax rate fell over the period. The overall average effective marginal tax rate on taxable benefits hovered between 22 percent and 24 for calendar years 1997 through 2002. In 2003, the overall average effective marginal tax rate dropped to 19 percent.

II. Comparison of Provisional Income Sources for Calendar Years 1995 to 2004

Table 5 provides some information about the levels and distributions of provisional income sources for taxpayers with taxable benefits in calendar years 1995 through 2004.[9] The table first shows the number of tax returns with Social Security and Railroad Social Security Equivalent benefits included in AGI, approximately 6.6 million in 1995. By 2004, about 11.7 million returns included benefits in AGI, an increase of about 77 percent. Recall from Chapter 1 that taxpayers are required to calculate provisional income and include a certain percentage of benefits in AGI if provisional income meets or exceeds certain thresholds. For all the tax returns in Table 5, provisional income was greater than or equal to the first threshold ($25,000 for single filers or $32,000 for joint filers).[10] These thresholds are not indexed for inflation, thus the 77 percent rise in the number of returns with benefits included in AGI is due to both the increase in the size of the beneficiary population and increases in nominal income.

The next column shows the total provisional income for all taxpayers with benefits included in AGI (in millions of dollars), as well as the mean and median provisional income (in dollars). In 1995, total provisional income for all taxpayers with taxable benefits was $449,992 million. Mean provisional income was $68,201, while the median was somewhat lower: $46,221. The relative levels of the mean and the median suggest that the lower half of the provisional income distribution is more closely bunched than the top half. That is, a relatively small number of taxpayers have extremely high levels of provisional income. By 2004, total provisional income had risen 117 percent to $978,007 million while the mean had risen 23 percent to $83,649. The median rose 8 percent to $49,948. The growth in provisional income is not monotonic, but rather reflects the business cycle. Provisional income reached a peak of $886,695 million in 2000 before declining to $806,145 million in 2002. Thereafter, provisional income rose to $978,007 in 2004. (In fact, the number of returns required to include benefits in AGI fell slightly from 2001 to 2002.)

The next section of Table 5 provides information about the levels and distributions of certain sources of provisional income. These sources include Social Security and Railroad Social Security Equivalent benefits, pension income, taxable and tax exempt interest income, wages and salaries, net positive capital gains, dividends, and taxable IRA distributions. In addition to the total, mean and median amounts, the table shows the percent of returns reporting having the source, and the share the total amount of the source comprises of total provisional income. For example, in 1995, total pension income of $94,615 million comprised 21 percent of total provisional income and 71 percent of returns reported having pension income. The mean pension income was $14,340 while the median was $9,484.

The table shows that pension income rose considerably during the 1995 to 2004 period reaching $208,617 million, an increase of 120 percent. However, as a share of total provisional income, pensions remained constant. In 2004, pension income comprised 21 percent of provisional income and 72 percent of returns reported having that source. The mean pension income had risen 25 percent, to $17,843, while the median had risen 34 percent, to $12,564. Pension income is also less sensitive to the business cycle. In no year

did total or mean pension income show a decline, while the median dropped only 2 percent from 1995 to 1996.

By definition, all these returns reported positive Social Security and Railroad Social Security Equivalent benefits. Recipients must include one-half of their benefits when determining provisional income and those "one-half" amounts are shown in Table 5. Like pension income, Social Security and Railroad Social Security Equivalent benefits remained constant as a share of provisional income. In 1995, total benefits included in provisional income were $40,544 million and comprised 9 percent of provisional income. The mean included amount was $6,145 while the median was $5,785. By 2004, one-half of Social Security and Railroad Equivalent Social Security benefits totaled $95,586 million (an increase of 136 percent), and comprised 10 percent of provisional income. The mean and median included amounts rose 33 percent and 35 percent to $8,175 and $7,816, respectively.

In 1995, interest was comparable to pensions as a source of income for these taxpayers. Nearly all returns (96 percent) reported positive interest income, and the mean and aggregate total interest income (taxable plus tax exempt) were comparable to mean and aggregate pension income. In 1995, interest income totaled $85,494 million ($56,721 million taxable and $28,773 million tax exempt), or 19 percent of provisional income. The mean interest income was $12,957, about 90 percent of the mean pension income in that year. Median interest income ($4,071) was significantly lower than the median pension income ($9,484), however.

Over the next nine years, the importance of interest as an income source declined somewhat, at least in part due to declining interest rates.[11] The mean and median levels of interest income fell to $7,186 and $571, respectively. The median, in particular, fell 86 percent from its 1995 level. Moreover, interest income comprised only 9 percent of total provisional income in 2004. It should be noted however, that 87 percent of returns continued to report interest income, 15 percentage points more than those reporting pension income, and the most for any income source other than Social Security and its Railroad equivalent.[12]

Wages are also an important source of income, but, compared to pension, benefit, and interest income, for relatively few taxpayers. Table 5 shows that in 1995, the mean level of wage income for taxpayers with taxable benefits was $12,855, almost $1,500 less than mean pension income and nearly equal to mean interest income. In total, these taxpayers had $84,818 million in wage income, comprising 19 percent of total provisional income. However, unlike pension and interest income, only 44 percent of taxpayers reported having wage income. The mean wage income remained essentially flat over the next four years and total wages as a share of provisional income actually declined to 16 percent by 1999. However, from 2000 to 2004, wages grew in importance. By 2004, the mean wage had grown to $18,123, wages comprised 22 percent of provisional income, and 48 percent of returns reported having wage income.

Capital gains income was the most variable source of provisional income over the 1995 to 2004 period. In 1995, mean capital gains income was $6,935 while the median capital gains income was zero. Total capital gains income was $45,759 million, or 10

percent of total provisional income. About 14 percent of returns offset positive ordinary income with negative capital gains income, and 53 percent of tax returns reported zero capital gains. The remaining 33 percent of returns reported positive capital gains income. The next five years saw an increase in total and mean capital gains income. By 2000, mean capital gains income had more than doubled to $14,927, and by that measure, was the third largest source of provisional income, behind pensions and wages. Total capital gains were $158,351 million, about 18 percent of total provisional income. Median capital gains were still zero however. About 36 percent of tax returns reported positive capital gains, about 12 percent reported negative capital gains, and 52 percent of tax returns reported no capital gains. Interestingly, the percent of returns reporting positive capital gains reached a peak of 48 percent three years earlier in 1997. After 2000, capital gains declined in total, mean, and share of total provisional income, hitting a trough in 2002. Total and mean capital gains fell 52 percent over that span. The percent of taxpayers reporting positive capital gains hit a trough of 22 percent in 2003. From 2002 to 2004 total capital gains grew 98 percent to $150,563 million. However the median capital gain was still zero and only 26 percent of taxpayers reported having positive capital gains in AGI.

Almost two-thirds of all taxpayers reported positive dividend income in each year from 1995 to 2000, although most reported relatively modest levels.[13] In 1995, dividend income totaled $41,644 million, or 9 percent of provisional income. The median dividend income was $631. The mean dividend income was ten times that level ($6,312) indicating a small number of taxpayers with relatively high levels of dividend income. By 2000, aggregate dividend income had risen 57 percent, to $65,247 million, while the mean dividend income remained essentially constant. As a percent of provisional income, dividend income actually declined slightly to 7 percent. Like capital gains income, dividend income declined from 2000 to 2002, reaching a trough of $49,065 million. The mean dividend income had fallen to $4,584 and the median had fallen to $91. After 2002, dividend income began to rise. By 2004 total dividend income reached $64,815 million while mean dividend income reached $5,544.

Finally, taxable IRA distributions form a small but increasing source of income for taxpayers with taxable Social Security and Railroad Equivalent Social Security benefits. In 1995, taxable IRA distributions comprised only 4 percent of provisional income ($17,612 million). The mean distribution was $2,669 and only 29 percent of taxpayers received such a distribution. Total and mean distributions increased steadily through 2000, reaching $56,673 million and $5,342, respectively. Thirty-six percent of returns reported taxable IRA distributions. The total and mean distributions then declined through 2003, although the percent reporting a distribution remained constant. By 2004, however, total taxable IRA distributions rebounded to $61,235 million and the mean was $5,237. This provisional income source accounted for 6 percent of total provisional income, and 37 percent of taxpayers reported having the source.

Table 4.A
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 1997
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	822	7,841	1,201	15%	166	14%
$30,000 to $40,000	2,154	26,213	6,194	24%	1,057	17%
$40,000 to $50,000	1,589	20,102	10,394	52%	1,842	18%
$50,000 to $60,000	1,020	13,206	10,288	78%	1,966	19%
$60,000 to $75,000	1,000	13,613	11,399	84%	2,744	24%
$75,000 to $100,000	712	9,643	8,199	85%	2,186	27%
$100,000 to $200,000	713	11,048	9,392	85%	2,666	28%
Over $200,000	300	5,285	4,493	85%	1,562	35%
Total	8,308	106,951	61,558	58%	14,189	23%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 1997.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 105,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 45,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.B
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 1998
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	851	8,358	1,195	14%	169	14%
$30,000 to $40,000	2,354	29,674	7,034	24%	1,200	17%
$40,000 to $50,000	1,694	22,902	11,587	51%	2,110	18%
$50,000 to $60,000	1,043	13,637	10,749	79%	2,080	19%
$60,000 to $75,000	1,056	14,695	12,469	85%	3,106	25%
$75,000 to $100,000	803	11,538	9,908	86%	2,699	27%
$100,000 to $200,000	795	12,316	10,575	86%	3,070	29%
Over $200,000	345	6,038	5,185	86%	1,804	35%
Total	8,941	119,159	68,703	58%	16,238	24%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 1998.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 113,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 39,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.C
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 1999
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	844	8,515	1,193	14%	167	14%
$30,000 to $40,000	2,386	30,446	7,338	24%	1,228	17%
$40,000 to $50,000	1,766	24,254	12,304	51%	2,257	18%
$50,000 to $60,000	1,137	15,010	11,804	79%	2,188	19%
$60,000 to $75,000	1,116	15,612	13,202	85%	3,206	24%
$75,000 to $100,000	933	13,483	11,460	85%	3,115	27%
$100,000 to $200,000	887	13,941	11,850	85%	3,401	29%
Over $200,000	392	6,974	5,928	85%	2,045	34%
Total	9,459	128,235	75,079	59%	17,607	23%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 1999.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 114,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 37,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.D
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 2000
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	883	9,254	1,263	14%	163	13%
$30,000 to $40,000	2,566	33,963	8,121	24%	1,343	17%
$40,000 to $50,000	1,952	27,181	13,814	51%	2,529	18%
$50,000 to $60,000	1,318	19,162	14,464	75%	2,703	19%
$60,000 to $75,000	1,291	19,071	16,063	84%	3,875	24%
$75,000 to $100,000	1,040	15,876	13,494	85%	3,633	27%
$100,000 to $200,000	1,088	17,861	15,182	85%	4,406	29%
Over $200,000	472	8,898	7,563	85%	2,635	35%
Total	10,609	151,267	89,964	59%	21,287	24%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 2000.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 150,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 45,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.E
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 2001
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	943	9,944	1,412	14%	188	13%
$30,000 to $40,000	2,641	36,613	8,575	23%	1,359	16%
$40,000 to $50,000	2,083	30,350	15,284	50%	2,770	18%
$50,000 to $60,000	1,437	21,664	16,399	76%	2,940	18%
$60,000 to $75,000	1,231	18,574	15,567	84%	3,560	23%
$75,000 to $100,000	1,082	17,475	14,754	84%	3,901	26%
$100,000 to $200,000	953	17,217	14,579	85%	4,178	29%
Over $200,000	409	8,258	6,989	85%	2,427	35%
Total	10,779	160,097	93,559	58%	21,323	23%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 2001.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 137,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 46,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.F
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 2002
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	944	10,523	1,456	14%	172	12%
$30,000 to $40,000	2,764	40,262	8,664	22%	1,239	14%
$40,000 to $50,000	1,996	30,453	14,764	48%	2,557	17%
$50,000 to $60,000	1,341	21,028	15,378	73%	2,614	17%
$60,000 to $75,000	1,247	19,797	16,698	84%	3,523	21%
$75,000 to $100,000	1,057	16,982	14,444	85%	3,656	25%
$100,000 to $200,000	977	18,145	15,444	85%	4,263	28%
Over $200,000	377	7,769	6,612	85%	2,236	34%
Total	10,703	164,961	93,459	57%	20,261	22%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 2002.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 144,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 54,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.G
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 2003
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	942	10,865	1,585	15%	177	11%
$30,000 to $40,000	2,659	40,034	8,431	21%	1,136	13%
$40,000 to $50,000	2,210	34,300	15,872	46%	2,562	16%
$50,000 to $60,000	1,375	21,699	15,820	73%	2,595	16%
$60,000 to $75,000	1,214	19,785	16,560	84%	2,773	17%
$75,000 to $100,000	1,174	19,460	16,475	85%	3,512	21%
$100,000 to $200,000	1,013	18,854	15,992	85%	4,035	25%
Over $200,000	389	8,316	7,032	85%	2,201	31%
Total	10,975	173,314	97,768	56%	18,992	19%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 2003.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 165,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 70,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 4.H
Distribution of Taxable Social Security and Railroad Social Security Equivalent Benefits and Tax Liability Due to the Taxation of Benefits in Calendar Year 2004
By Provisional Income

Provisional Income /1	Returns /2	Total Benefits /3	Benefits in AGI /3	Benefit Inclusion Rate	Tax Liability Due to Inclusion of Benefits /3	Average Effective Marginal Tax Rate on Benefits in AGI
Under $30,000	990	11,630	1,955	17%	221	11%
$30,000 to $40,000	2,783	42,732	9,064	21%	1,219	13%
$40,000 to $50,000	2,149	35,070	16,244	46%	2,614	16%
$50,000 to $60,000	1,525	24,581	17,824	73%	2,998	17%
$60,000 to $75,000	1,411	24,286	20,249	83%	3,333	16%
$75,000 to $100,000	1,178	20,679	17,608	85%	3,757	21%
$100,000 to $200,000	1,166	21,742	18,585	85%	4,773	26%
Over $200,000	490	10,452	8,934	85%	2,817	32%
Total	11,692	191,172	110,462	58%	21,733	20%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for 2004.

1/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest.

2/ Returns in thousands. Includes about 168,000 returns with married beneficiaries who do not file jointly. These taxpayers have provisional income thresholds of zero. Approximately 68,000 have provisional income below the minimum threshold applicable to other types of filers.

3/ Benefit amounts and tax liability in millions of dollars.

Table 5
Distributional Analysis of Income Sources of Returns with
Taxable Social Security and Railroad Social Security Equivalent Benefits - 1995 to 2004

				Provisional Income Source				
				Social		Interest Income		
Year	Returns /1	Statistic /2	Provisional Income /3	Security /4	Pensions	Taxable	Tax Exempt	Total
1995	6,598	Total	449,992	40,544	94,615	56,721	28,773	85,494
		Mean	68,201	6,145	14,340	8,597	4,361	12,957
		Median	46,221	5,785	9,484	2,779	0	4,071
		Percent Positive		100%	71%	96%	29%	96%
		Share of Provisional Income		9%	21%	13%	6%	19%
1996	7,366	Total	527,261	46,357	107,386	64,799	28,915	93,714
		Mean	71,581	6,293	14,579	8,797	3,925	12,723
		Median	46,433	5,930	9,298	2,886	0	3,948
		Percent Positive		100%	71%	95%	28%	95%
		Share of Provisional Income		9%	20%	12%	5%	18%
1997	8,308	Total	612,968	53,475	123,259	69,768	29,707	99,475
		Mean	73,781	6,437	14,836	8,398	3,576	11,973
		Median	46,999	6,047	9,551	2,636	0	3,478
		Percent with Source		100%	72%	95%	25%	95%
		Share of Provisional Income		9%	20%	11%	5%	16%
1998	8,941	Total	686,482	59,579	135,909	74,335	30,004	104,338
		Mean	76,778	6,663	15,200	8,314	3,356	11,669
		Median	47,392	6,275	10,081	2,427	0	3,352
		Percent with Source		100%	72%	95%	23%	95%
		Share of Provisional Income		9%	20%	11%	4%	15%
1999	9,459	Total	744,295	64,118	148,761	73,245	30,184	103,429
		Mean	78,685	6,778	15,727	7,743	3,191	10,934
		Median	48,178	6,429	10,640	2,038	0	2,851
		Percent with Source		100%	73%	94%	22%	94%
		Share of Provisional Income		9%	20%	10%	4%	14%
2000	10,609	Total	886,695	75,633	169,105	87,076	31,007	118,082
		Mean	83,583	7,129	15,940	8,208	2,923	11,131
		Median	49,328	6,783	10,854	2,032	0	2,622
		Percent with Source		100%	72%	94%	20%	94%
		Share of Provisional Income		9%	19%	10%	3%	13%
2001	10,779	Total	838,846	80,048	176,129	87,673	32,646	120,319
		Mean	77,820	7,426	16,340	8,133	3,029	11,162
		Median	48,739	7,116	11,179	1,864	0	2,418
		Percent with Source		100%	72%	93%	19%	93%
		Share of Provisional Income		10%	21%	10%	4%	14%
2002	10,703	Total	806,145	82,480	184,503	66,047	32,111	98,158
		Mean	75,323	7,707	17,239	6,171	3,000	9,171
		Median	48,025	7,362	12,207	954	0	1,227
		Percent with Source		100%	72%	90%	19%	91%
		Share of Provisional Income		10%	23%	8%	4%	12%
2003	10,975	Total	844,190	86,657	193,725	54,013	31,478	85,491
		Mean	76,919	7,896	17,651	4,921	2,868	7,790
		Median	48,010	7,606	12,649	602	0	769
		Percent with Source		100%	72%	88%	18%	88%
		Share of Provisional Income		10%	23%	6%	4%	10%
2004	11,692	Total	978,007	95,586	208,617	53,697	30,318	84,015
		Mean	83,649	8,175	17,843	4,593	2,593	7,186
		Median	49,948	7,816	12,564	454	0	571
		Percent with Source		100%	72%	86%	17%	87%
		Share of Provisional Income		10%	21%	5%	3%	9%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for tax years 1997 to 2004.

1/ Returns with Social Security and Railroad Social Security Equivalent benefits included in AGI, in thousands.

2/ Totals are in millions of dollars. Means and medians are in dollars. Percent positive is the percent of returns with a positive value for the income source indicated. Net capital gains may be negative. All other income sources must be zero or positive. Share of Provisional Income is the percent of total provisional income attributable to the income source in the given year.

3/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest. Provisional income totals may not equal the sums over the provisional income components due to other sources of income and adjustments made in calculating AGI. (Equivalently, shares of provisional income may not add to 100). Other sources of income include (but are not limited to) partnership and other Schedule E income, while adjustments include (but are not limited to) the deduction for Self-Employment tax paid.

4/ Column shows one-half Social Security and Railroad Social Security Equivalent benefits since that amount is included in provisional income.

Table 5 (continued)
Distributional Analysis of Income Sources of Returns with
Taxable Social Security and Railroad Social Security Equivalent Benefits - 1995 to 2004

				Provisional Income Source			
Year	Returns /1	Statistic /2	Provisional Income /3	Wages and Salaries	Net Capital Gains	Dividends	Taxable IRA Distributions
1995	6,598	Total	449,992	84,818	45,759	41,644	17,612
		Mean	68,201	12,855	6,935	6,312	2,669
		Median	46,221	0	0	631	0
		Percent Positive		44%	33%	64%	29%
		Share of Provisional Income		19%	10%	9%	4%
1996	7,366	Total	527,261	96,615	67,366	46,624	23,042
		Mean	71,581	13,116	9,146	6,330	3,128
		Median	46,433	0	0	627	0
		Percent Positive		43%	37%	64%	31%
		Share of Provisional Income		18%	13%	9%	4%
1997	8,308	Total	612,968	107,020	96,822	53,851	30,525
		Mean	73,781	12,882	11,654	6,482	3,674
		Median	46,999	0	0	704	0
		Percent Positive		43%	48%	65%	33%
		Share of Provisional Income		17%	16%	9%	5%
1998	8,941	Total	686,482	114,706	124,321	55,172	37,997
		Mean	76,778	12,829	13,904	6,171	4,250
		Median	47,392	0	0	559	0
		Percent Positive		42%	47%	65%	33%
		Share of Provisional Income		17%	18%	8%	6%
1999	9,459	Total	744,295	122,676	134,640	59,821	47,640
		Mean	78,685	12,969	14,234	6,324	5,036
		Median	48,178	0	0	578	0
		Percent Positive		43%	39%	64%	35%
		Share of Provisional Income		16%	18%	8%	6%
2000	10,609	Total	886,695	162,724	158,351	65,247	56,673
		Mean	83,583	15,339	14,927	6,150	5,342
		Median	49,328	0	0	449	0
		Percent Positive		44%	36%	64%	36%
		Share of Provisional Income		18%	18%	7%	6%
2001	10,779	Total	838,846	176,910	94,489	55,257	54,378
		Mean	77,820	16,412	8,766	5,126	5,045
		Median	48,739	0	0	181	0
		Percent Positive		46%	29%	62%	36%
		Share of Provisional Income		21%	11%	7%	6%
2002	10,703	Total	806,145	181,343	76,155	49,065	51,636
		Mean	75,323	16,944	7,116	4,584	4,825
		Median	48,025	0	0	91	0
		Percent Positive		47%	24%	61%	36%
		Share of Provisional Income		22%	9%	6%	6%
2003	10,975	Total	844,190	195,705	91,441	52,956	50,555
		Mean	76,919	17,832	8,332	4,825	4,606
		Median	48,010	0	0	60	0
		Percent Positive		48%	22%	59%	36%
		Share of Provisional Income		23%	11%	6%	6%
2004	11,692	Total	978,007	211,892	150,563	64,815	61,235
		Mean	83,649	18,123	12,878	5,544	5,237
		Median	49,948	0	0	73	0
		Percent Positive		48%	26%	59%	37%
		Share of Provisional Income		22%	15%	7%	6%

Department of the Treasury
Office of Tax Analysis

Source: SOI Individual Tax Return Sample Data for tax years 1997 to 2004.

1/ Returns with Social Security and Railroad Social Security Equivalent benefits included in AGI, in thousands.

2/ Totals are in millions of dollars. Means and medians are in dollars. Percent positive is the percent of returns with a positive value for the income source indicated. Net capital gains may be negative. All other income sources must be zero or positive. Share of Provisional Income is the percent of total provisional income attributable to the income source in the given year.

3/ Provisional income is calculated as AGI (excluding Social Security and Railroad Social Security Equivalent benefits in AGI) plus one-half of Social Security and Railroad Social Security Equivalent benefits plus tax exempt interest. Provisional income totals may not equal the sums over the provisional income components due to other sources of income and adjustments made in calculating AGI. (Equivalently, shares of provisional income may not add to 100). Other sources of income include (but are not limited to) partnership and other Schedule E income, while adjustments include (but are not limited to) the deduction for Self-Employment tax paid.

4/ Column shows one-half Social Security and Railroad Social Security Equivalent benefits since that amount is included in provisional income.

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ENDNOTES

1. This report covers an eight year period due to various delays in determining final tax liability and in the production of the report. These delays prevented the timely publication of reports covering tax years 1997 through 2001. Shortly after the completion of the 2001 report, final tax liability information for tax years 2002 through 2004 became available and final correcting adjustments were made. Therefore, rather than issue one report for 1997 through 2001, and separate reports for 2002, 2003 and 2004, the analyses for 2002, 2003 and 2004 were added to the 1997 to 2001 report.

2. For single filers, $4,500 represents one-half of the difference between the first and second provisional income thresholds ($25,000 and $34,000). For joint filers, $6,000 represents one-half of the difference between the first and second provisional income thresholds ($32,000 and $44,000). The second provisional thresholds and the associated benefits-in-AGI inclusion rule were enacted as part of OBRA 93 and apply to all tax years beginning on or after January 1, 1994. OBRA 93 also stipulated that the additional tax liability arising from those provisions be directed to the FHI trust fund.

3. Liability estimates and the associated transfers are updated semi-annually (in December and May) to conform with updates to the President's macroeconomic forecast. All transfers are made using the most recently created forecast.

4. In May 2000, the IRS provided OTA with preliminary totals of tax liability with and without the inclusion of Social Security benefits for calendar year 1997. The July and September 2000 correcting adjustments were made based on these totals. In February 2001, the IRS provided OTA with revised totals for calendar year 1997. The second correcting adjustments made in September and October 2001 were based on these totals.

5. A detailed description of the Individual Income Tax Model can be found in Cilke (1994).

6. OTA does not estimate the liability attributable to the receipt of FOASI and FDI benefits by non-resident aliens. Prior to tax year 1995, one-half of any Social Security benefit received by a non-resident alien was subject to a 30 percent tax rate, and this amount was automatically withheld by the Social Security Administration. For tax years 1995 and after, the percent of benefits subject to withholding is raised to 85 percent (P.L. 103-465).

   Each month, the Social Security Administration sends a certification of the amount withheld to the Treasury Department's Financial Management Service. The withheld amount is transferred to general revenues and then back to the FOASI and FDI trust funds. Since the Social Security Administration has information on the actual amounts withheld, OTA does not estimate these withheld amounts.

   Similarly, the Railroad Retirement Board automatically withholds taxes on Railroad Social Security Equivalent benefits received by non-resident aliens. However, a different procedure is used to transfer these amounts to the SSEBA. OTA includes an estimate of the withheld amounts in its initial estimates of transfers to the trust funds and subsequently verifies these estimates with the Railroad Retirement Board.

The tables in this report do not include FOASI or FDI benefits received by non-resident aliens or the taxes attributable to these benefits. However, the tables do show the Railroad Social Security Equivalent benefits received by non-resident aliens.

7. For example, as AGI increases, a lesser amount of medical, casualty and certain miscellaneous expenses may be deducted. On the other hand, the increased tax liability resulting from the inclusion of benefits in AGI enables some taxpayers to use tax credits that otherwise might not be usable in that year.

8. The Form SSA-1099 records provided to the IRS distinguish between retirement and disability benefits, even though the Form SSA-1099s sent to taxpayers do not include this information.

9. The statistics shown in Table 5 are calculated from the 1995 through 2004 SOI files.

10. A small percentage of taxpayers file as "married, filing separately." These taxpayers have no thresholds and are always required to include Social Security and Railroad Social Security Equivalent benefits in AGI. They are included in Table 5.

11. The yield on a 10-year Treasury note declined from 6.58 percent in 1995 to 5.26 percent in 1998, before rising to 6.03 percent in 2000. The rate declined thereafter, to 4.02 percent in 2003 and 4.27 in 2004. Similarly, Moody's Aaa Corporate Bond yield declined from 7.59 percent in 1995 to 6.53 percent in 1998, before rising to 7.62 percent in 2000. It then declined to 5.63 in 2004.

12. While taxable and tax exempt interest are both important sources of provisional income, taxable interest comprises the major share of this income source. Only 29 percent of taxpayers reported positive tax exempt interest in 1995, and only 17 percent in 2004. In 1995, taxable interest income comprised 66 percent of total interest income. By 2000, its share had risen to 74 percent. By 2004, its share had declined to 64 percent.

13. Dividend income includes dividends paid by taxable corporations, distributions from mutual funds and bond funds, and other sources.