TAX FORMS AND TAX EQUITY FOR OLDER AMERICANS

HEARING

BEFORE THE

SPECIAL COMMITTEE ON AGING
UNITED STATES SENATE

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TAX FORMS AND TAX EQUITY FOR OLDER AMERICANS

FRIDAY, FEBRUARY 24, 1978

U.S. SENATE,
SPECIAL COMMITTEE ON AGING,
Washington, D.C.

The committee met at 10:38 a.m., pursuant to notice, in room 6226, Dirksen Senate Office Building, Hon. Frank Church, chairman, presiding.

Present: Senator Church.

Also present: William E. Oriol, staff director; David A. Affeldt, chief counsel; Garry V. Wenske, assistant counsel for operations; Margaret S. Fayé, minority professional staff member; Theresa M. Forster, fiscal assistant; and Marjorie J. Finney, correspondence assistant.

OPENING STATEMENT BY SENATOR FRANK CHURCH, CHAIRMAN

Senator CHURCH. We are operating under a considerable time restraint since the Panama Canal debate has commenced in the Senate. One of the rules we are obliged to follow is that 2 hours after the Senate convenes, Senators may no longer sit in committee. This morning, the Senate convened at 8:45, which gives me 5 minutes. However, the staff is prepared to carry forward with the questioning and to develop the record we hope to make today.

Even though I will be obliged as the manager of the treaties to go to the floor, I want you to know the reasons why. I hope that the record we make will be very helpful for the subject we are pursuing which is "Tax forms and tax equity for older Americans."

I shall ask the witnesses this morning to stay within their allotted time in order that we can make a complete record and to permit the staff to ask the questions they wish.

Before we open the testimony, I would like to make a few key points.

First, Congress has enacted several measures to provide tax relief for older Americans, such as the tax credit for the elderly and allowing older Americans to exclude fully or partially the gain from a sale of a personal residence.

Unfortunately, some of these tax benefits require a maze of computations, statements, and schedule transfers to complete.

For the unsuspecting taxpayer, form 1040 with its accompanying schedules, can be like going through a minefield with numerous linguistic boobytraps.

My point is this: Tax relief provisions are not very helpful unless they are workable and understandable.

President Carter has made tax equity and tax simplification two of his top priority goals. The committee stands ready, willing, and able to work with the administration to achieve these goals. I hope that the hearing this morning can shed more light on possible improvements for the tax form.

Protection Against Overpayment of Income Tax

Second, the committee is concerned that many older Americans needlessly overpay their taxes each year because they are unaware of helpful deductions, credits, and exemptions.

The Internal Revenue Service has repeatedly emphasized that the Federal Government wants no individual to pay more taxes than legally due.

In recent years the committee has published a checklist of itemized deductions to alert older and younger taxpayers alike about tax benefits that can save them money.

We have been assisted by competent and dedicated staff of Internal Revenue Service who have reviewed the committee's publication for accuracy and clarity. I would like to extend again our sincere appreciation to Commissioner Kurtz and the IRS staff for this cooperation.

Additional steps, though, are needed to safeguard individuals from overpaying their taxes.

Tax preparation assistance, for example, can be made more readily available. We shall hear from Commisioner Kurtz later about IRS efforts to assist aged persons in preparing their tax returns.

The committee will also want to know what future actions are planned to extend tax preparation services.

Tax Credit for Elderly

Third, we are concerned about apparent anomalies in the tax law for older Americans.

A classic example may be the tax credit for the elderly. Some elderly taxpayers are discovering that they are being penalized upon reaching age 65.

Qualifying persons under 65 years of age may now claim a 15-percent credit on up to $2,500 of Government pensions, producing a $375 tax savings for persons with no social security benefits and little earnings.

But upon becoming 65, these same individuals may lose the credit entirely, even though their needs may be greater. This is because the $2,500 starting point is reduced by $1 for each $2 of adjusted gross income above $7,500. The effect is that the credit is phased out completely for persons 65 or older with income of $12,500 or more.

I've received many letters from elderly persons who object to one set of rules applied to persons under 65 and another set for those 65 or older.

Our witnesses, I am sure, will have more to say about this situation. We look forward to your comments and possible recommendations.

Administration's Tax Package

Finally, the committee wants to hear from administration officials and others about the impact of the President's tax package for older Americans.

How will the proposed rate reductions and the new $240 personal exemption credit affect elderly taxpayers?

Will older Americans be adversely affected by the recommended reduction or elimination of expenses which are now deductible? If so, to what extent?

The committee will seek answers to other important questions during the hearing on "tax forms and tax equity for older Americans."

So with these considerations in mind, we shall hear from our lead-off witness.

Mr. Commissioner, I understand that Emil Sunley, the Deputy Assistant Secretary for Tax Policy of the Department of the Treasury, is going to lead off the testimony this morning. I just want to express to both of you our appreciation for your aid.

STATEMENT OF EMIL M. SUNLEY, DEPUTY ASSISTANT SECRETARY FOR TAX POLICY, DEPARTMENT OF THE TREASURY

Mr. Sunley. Mr. Chairman, I appreciate the opportunity to appear. I have a prepared statement which I hope will be entered into the record.[1] I, however, would like to just summarize part of that statement. The first part of my statement treats the current tax treatment of the aged. The middle section of my statement includes some comments on the impacts of the President's program on the aged. Finally, I conclude with the administration position on a number of bills which have been submitted to Congress on providing changes in the tax treatment of the aged.

President's Tax Program for Aged

Let me begin first with the impact of the President's program on the aged. Now, under the President's tax program, older Americans will have a substantial tax cut, as will taxpayers generally. It is noteworthy, however, that as social security beneficiaries they generally will not have to offset their income tax cut with social security tax increases scheduled for the nonaged. As a consequence, the overall tax cut for the aged will be substantially greater than that of the nonaged. The tax liabilities of the aged will drop by $925 million under the President's program. The average net tax cut will be almost $250 per tax return. The tax savings will be spread fairly evenly among taxpayers in all income classes below $100,000.

Aged taxpayers with adjusted gross incomes of $100,000 or more will, on the average, experience a tax increase. There is a relatively small number of such high-income aged persons, filing about 66,000 tax returns.

The President's tax program will substantially increase the tax-free levels of income for the elderly and more than 1 million addi-

[1] See p. 5.

tional returns now filed by taxable persons aged 65 or over will be dropped from the income tax rolls. This arises from the fact that the tax program proposes to substitute a $240 per capita credit for the personal exemption and the general tax credit.

Tax-Free Levels

As a result, the tax-free levels of income for a single person aged 65 or over will increase by $850, from $6,400 to $7,250, and will increase by $1,200 for a couple, with both spouses aged 65 and over, from $10,450 under current law to $11,650 under the President's proposal.

The President has also proposed changes in the rules under which qualified retirement plans may integrate with social security. The proposed rules will assure that if a company provides a pension for an employee, it must make a substantial provision for every employee not represented by a collective bargaining unit. This proposal would insure that the low-income aged in the future will receive more adequate private pensions to supplement their social security benefits.

Under the President's tax program, to obtain fairness between the taxpayers at various income levels, the personal exemption and the general tax credit would be converted to a $240 per capita credit. A tax credit is directly subtracted from tax as opposed to an exemption which is subtracted from income. The aged would each receive two per capita credits for a total of $480, irrespective of income level and rate bracket.

Break-Even Income Levels

Although the per capita credit is being proposed in combination with the restructuring of the tax rates, it may be helpful for the committee to know the break-even income bracket level if the per capita credit were presented as an isolated change. For an elderly couple with less than $20,200 income, the new $240 credit will provide greater tax savings than the existing personal exemption and general tax credit. At that level of income, the elderly couple is neither better off nor worse off. The tax before the credit for the elderly would be $2,586 under either the $240 credit or under existing law. Most elderly couples with incomes above $20,200 would be better off because lower rate schedules have been proposed to offset the tax increases that would occur at high income levels if a $240 credit simply replaced the existing personal exemption and general tax credit.

The $240 credit and the new rate schedule would achieve first equity; the credit for the aged couple is worth the same regardless of the couple's level of income. Second, it would achieve simplification; one credit will replace the existing combination of a deduction and alternative credits.

Treasury Opposition to S. 2128

Now let me turn to S. 2128. Briefly, this bill would increase the maximum amounts of which the credit for the elderly is computed from $2,500 to $3,000 for an aged individual and from $3,750 to

$4,500 for an aged couple. The bill would also remove completely the adjusted gross income phaseout of the maximum amount. The current phaseout begins at $7,500 of adjusted gross income for an aged person and $10,000 of adjusted gross income for an aged couple.

The phaseout is a reduction of the maximum amount by one-half of the excess over the stipulated AGI levels. In addition, the bill would change the maximum amounts each year according to annual changes in the Consumer Price Index.

The Treasury opposes enactment of the bill. First, the elderly already receive substantial tax benefits and a group is already favorably treated as compared to taxpayers generally. The cost of the bill, if applicable to tax year 1978, would be $963 million and would increase about 10 percent a year. Just looking at the bill from a revenue cost standpoint, there is no room in the President's tax program and in the near term Federal budget for that type and amount of revenue loss.

On equity grounds, the bill is highly questionable. It would provide substantial tax benefits for the elderly who are relatively affluent and would do absolutely nothing for the 18 million older Americans who are not even on the tax rolls, but who may face the serious problem of lack of income. Even among the 6 million older Americans who do pay tax, the bill would distribute the $1 billion inequitably. Two-thirds of that benefit would go to taxpayers with over $15,000 and one-fourth of the benefit would go to those with incomes over $30,000.

In fact, the bill would distribute almost $100 million for taxpayers with $50,000 or more of income.

In addition, the Treasury is opposed to introducing indexing with respect to a specific item or tax allowance. The issue of indexing is one that must be faced on a universal basis. It is just not good tax policy to put one group in a better position than another with respect to inflation, as this bill would do.

That concludes my formal remarks.

[The prepared statement of Mr. Sunley follows:]

PREPARED STATEMENT OF EMIL M. SUNLEY

Mr. Chairman and members of the committee, I am pleased to be here this morning and to join with Commissioner Kurtz in testifying on the income tax treatment of older Americans. My remarks will address two important questions:

(1) How are older Americans affected by the Federal income tax?

(2) How will they be affected under the President's tax program?

I will also discuss briefly, the Treasury's position on several bills in which you, Mr. Chairman, and your committee have a particular interest and which have tax policy implications.

Let me answer the two questions first.

CURRENT TREATMENT OF THE AGED

Mr. Chairman, older Americans, age 65 or more, are treated favorably under the Federal income tax which is structured so that 18 million of the 24 million older Americans currently pay no income tax. The tax law keeps these 18 million off the tax rolls by providing tax-free levels of income that are approximately double the tax-free income levels provided for individuals under 65 years. For example:

—A single person under age 65 can now receive $3,200 before he is liable for tax, while a single person over 65 is not subject to tax until his income exceeds $6,400. The tax-free level may be higher if he receives social security benefits since these benefits are exempt from tax.

—A married couple with both spouses under age 65 is not subject to tax until the couple's income exceeds $5,200, while if both are 65 or over, the couple is not subject to tax until the couple's income exceeds $10,450.

These tax-free levels of income reflect the combined effect of a number of tax allowances, including special ones for the elderly. These allowances include: The regular personal exemption, the extra personal exemption for the aged, the general tax credit, the zero bracket amount or standard deduction, and the special credit for the elderly.

Let me turn to the 6 million who are taxpayers, about one out of four older Americans. They are the relatively more affluent who have incomes on average of nearly $20,000. They now pay $13.5 billion in income taxes. Under current income tax law, they also are granted favorable treatment in the following ways:

First, they are granted an extra personal exemption of $750.

Second, the aged are allowed an extra $35 credit, if the 2-percent rule is not elected under the general tax credit. The credit currently is equal to $35 per exemption or 2 percent of taxable income up to a credit of $180, whichever is greater.

Third, social security and railroad retirement income is not subject to tax.

Fourth, for the aged, with little or no social security or railroad retirement income, the credit for the elderly is allowed.

Fifth, taxpayers age 65 or over are allowed an exemption for all gains on sales of personal residences selling for $35,000 or less, and a portion of gains for residences selling for more than that amount.

These special tax preferences for the aged reduce Federal revenues by $6 billion annually. That is a substantial Government benefit for older Americans that does not appear on the outlay side of the budget.

I might mention, Mr. Chairman, that the credit for the elderly replaced the highly complex retirement income credit. Enacted as part of the Tax Reform Act of 1976, the current credit is much simpler to use than the former credit. In fact, a taxpayer may now ask the Internal Revenue Service to compute the credit. But the computation is actually quite straightforward. Let me illustrate by an example:

For a married couple filing a joint return, assume that both spouses are over age 65. The couple's adjusted gross income is $12,000 and they also receive $2,000 of social security benefits. The elderly credit would be computed as follows:

Initial amount of income for credit computation (This amount is specified in the Internal Revenue Code. For a single individual, the initial amount is $2,500)	$3, 750
Deduct social security pension ($2,000) and one-half of adjusted gross income that exceeds $10,000 ($1,000)	3, 000
Balance	750
Credit for the elderly (15 percent of $750)	112. 50

The couple therefore may reduce its tax liability (if any) by $112.50.

IMPACT OF PRESIDENT'S PROGRAM ON AGED

Under the President's tax program, older Americans will have a substantial tax cut, as will taxpayers generally. It is noteworthy however, as social security beneficiaries, they generally will not have to offset their tax cut with the social security tax increase scheduled for the nonaged. As a consequence, the overall tax cut of the aged will be substantially greater than that of the nonaged. The tax liabilities of the aged will drop by $925 million (see table 1). The average net tax cut will be almost $250. The tax savings will be spread fairly evenly among taxpayers in all income classes below $100,000. Aged taxpayers with adjusted gross incomes of $100,000 and over will, on average, experience tax increases. They are a relatively small number of aged persons filing about 66,000 returns.

TABLE 1.—COMPARISON OF TAX LIABILITIES FOR PERSONS AGE 65 OR OVER UNDER CURRENT LAW AND UNDER THE ADMINISTRATION PROPOSALS (1976 INCOME LEVELS)

Expanded income[1] class	Current law		Administration proposal		Difference	
	Number of taxable returns (thousands)	Amount of tax (millions)	Number of taxable returns (thousands)	Amount of tax (millions)	Number of taxable returns (thousands)	Amount of tax (millions)
Under $5,000	378	$10	(2)	$-13	-378	$-23
$5,000 to $10,000	1,651	589	985	291	-666	-298
$10,000 to $15,000	1,083	1,113	1,035	888	-48	-226
$15,000 to $20,000	541	1,039	538	910	-3	-129
$20,000 to $30,000	501	1,739	501	1,561		-179
$30,000 to $50,000	305	2,109	305	1,980		-129
$50,000 to $100,000	158	2,709	158	2,654		-56
$100,000 to $200,000	51	2,016	51	2,044		28
$200,000 and over	15	2,192	15	2,279		87
Total	4,682	13,518	3,588	12,593	-1,095	-925

1 Expanded income does not include social security and railroad retirement benefits.
2 Less than 500.

NOTE—All tax amounts include the full amount of the earned-income credit. Details may not add to totals because of rounding.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Feb. 24, 1978.

Mr. Chairman, the President's tax program will substantially increase the tax-free levels of income for the elderly. More than a million additional returns now filed by taxable persons age 65 or over would be dropped from the income tax rolls. This arises from the fact that the tax program proposes to substitute a $240 per capita credit for personal exemption and the general tax credit. As a result the tax-free levels of income for persons age 65 or over, will increase by $850 for a single person, from $6,400 to $7,250 of income, and will increase by $1,200 for a couple with both spouses 65 and over, from $10,450 to $11,650.

The President has proposed changes in the rules under which qualified retirement plans may integrate with social security. The proposed rules will assure that, if a company provides a pension for an employee, it must make a substantial provision for every employee not represented by a collective bargaining unit. This proposal will insure that the low-income aged in the future will receive more adequate private pensions to supplement their social security benefits.

THE PROPOSED $240 CREDIT

Under the President's tax program, to obtain fairness between taxpayers at various income levels, the personal exemption and the general tax credit would be converted to a $240 per capita credit. A tax credit is directly subtracted from tax as opposed to an exemption which is subtracted from income. The aged would each receive two per capita credits for a total of $480, irrespective of income level and rate bracket.

Although the per capita credit is being proposed in combination with a restructuring of tax rates, it may be helpful for the committee to know the credit's "break-even level" if presented as an isolated change. For an elderly couple with less than $20,200 of income, the new $240 credit will provide greater tax savings than the existing personal exemption and general tax credit, assuming no changes were made in the tax rate schedule. At that level of income, the elderly couple is neither better off nor worse off. The tax (before the credit for the elderly) would be $2,586 under either the $240 credit or under existing law.

EXAMPLE OF OPERATION OF THE PROPOSED $240 PER CAPITA CREDIT AND THE "BREAK-EVEN" LEVEL

	Current law	Proposed law (assuming current law rate schedule)
Adjusted gross income	$20,200	$20,200
Less two personal exemptions and two aged exemptions	3,000	
Taxable income[1]	17,200	20,200
Tax before credits	2,766	3,546
General tax credit	180	
Less four per capita credits		960
Tax after per capita credit but before credit for the elderly	2,586	2,586

1 The example assumes the taxpayer has no itemized deductions in excess of the zero bracket amount.

Most elderly couples with incomes above $20,200 would be better off because lower rate schedules have been proposed to offset the tax increases that would occur at high-income levels if a $240 credit simply replaced the existing personal exemption and general tax credit.

The $240 credit and the new rate schedule would achieve:

Equity—the credit for aged couple is worth the same regardless of the couple's level of income; and

Simplification—one credit will replace the existing combination of a deduction and alternative credits.

OTHER TAX PROPOSALS

Now let me turn to the proposed legislation of special interest to the committee. These are: S. 2128, a bill to expand the credit for the elderly; S. 1014, a bill to use tax allowances to expand housing opportunities for the elderly; S. 835, a bill to provide tax counseling for the elderly; and finally the Church-Domenici amendment to the energy tax bill, to provide a refundable tax credit to the elderly to meet the rising energy costs.

First, S. 2128. Briefly, the bill would increase the maximum amounts on which the credit is computed, from $2,500 to $3,000 for an aged individual and from $3,750 to $4,500 for an aged couple. In addition, the bill would change the maximum amounts each year according to annual changes in the Consumer Price Index.

The Treasury opposes enactment of the bill. First, the elderly already receive substantial tax expenditures and the group is already favorably treated as compared to taxpayers generally. The cost of the bill, if applicable to tax year 1978, would be $963 million and would increase about 10 percent a year. Just looking at the bill from a revenue cost standpoint, there is no room in the President's tax program and in the near-term Federal budget for that type and amount of revenue loss.

On equity grounds, the bill is highly questionable. It would provide substantial tax benefits to the elderly who are relatively affluent and would do absolutely nothing for the 18 million older Americans who are not even on the tax rolls but who may face the serious problem of lack of income. Even among the 6 million who do pay tax, the bill would distribute the $1 billion inequitably. Two-thirds of that benefit would go to taxpayers with incomes over $15,000. One-fourth of the benefit would go to those with incomes over $30,000. In fact, the bill would distribute almost $100 million dollars to taxpayers with $50,000 or more of income.

In addition, the Treasury is opposed to introducing indexing with respect to a specific item of income or tax allowance. The issue of indexing is one that must be faced on a universal basis. It is just not good tax policy to put one group in a better position than another with respect to inflation, as this bill would do.

Next, S. 1014. The bill would provide a $250 tax credit or a $1,000 deduction to a taxpayer who maintains a dependent age 65 or more within his home. The purpose is to provide housing for older Americans.

The Treasury is opposed to the bill on several grounds. First, the $800 million revenue cost would be substantial. It would generate double allowances for aged dependents. One allowance is the existing $750 dependency exemption and the other would be $1,000 deduction or the $250 credit in the bill. It would tend to move older Americans from nondependency status to dependency status to take advantage of the double allowance. It is noteworthy that the Congress granted the dependency exemption to taxpayers who supported relatives outside the home. The purpose was to provide some independence for the dependent. S. 1014 would move in the opposite direction.

The extra allowance would be discriminatory among aged since the dependency test requires that the children provide more than half of the support for the parent. Low income families may provide a home for an aged parent but not meet the support test. Higher income families could more easily meet the support test and thus qualify for the additional allowance.

The double allowance would also provide a windfall to those taxpayers who already have aged dependents in their home. To the extent that the windfall does nothing to provide more housing opportunities, the large revenue cost of providing the windfall would be a deadweight loss.

In addition, it is hard to justify the double allowance that would be granted by the bill and not grant it to other dependents who are also in need of housing but are not age 65 or older. These include dependents who are incapacitated or who are unemployed or are students.

Perhaps most importantly, the S. 1014 double allowance would be regressive in its impact. The greatest portion of the benefit would go to those in the higher incomes who have the resources and facilities to provide housing for their aged dependents and can meet the support test. In many cases the regressive impact of the allowance would be compounded by the fact that the aged dependent already lives in the house and thus the allowance would be a windfall to the taxpayer.

Next, S. 835. A provision of the bill would authorize the tax-free reimbursement for certain expenses incurred by volunteers who provide tax assistance to the elderly. I want to focus only on the tax exemption aspect.

The Treasury is opposed to the tax exemption. The Department objects to introducing another statutory exclusion from the tax base. To the extent that the volunteer is a low income person, the reimbursement of certain expenses as provided in the bill would generally be nontaxable in any case.

Finally, let me turn to the Church-Dominici amendment (No. 1523) to the energy tax bill, H.R. 5263. As part of his national energy plan, the President proposed that the proceeds of the crude oil equalization tax be rebated to individuals on a per capita basis in order to assist them in meeting increased costs attributable to that tax. It is estimated that the per capita rebate would total approximately $45 per year when the tax is fully effective. In addition, the plan provides for a reduction in heating oil costs of consumers equal to the increase that would be caused by the imposition of the tax. When the crude oil tax is fully effective that reduction in price would total approximately $50 per year for a typical purchaser of heating oil.

These payments, of course, would be available to all individuals, whether young or old. In fact, in the case of the low income individuals, the amount to be paid to them under the plan would exceed the additional costs they would incur by reason of the crude oil tax.

The Church-Domenici amendment provides a refundable credit for the elderly in addition to these payments and adjustments. It would provide an additional $75 to heads of households age 65 or over with a phaseout for taxpayers with adjusted gross incomes between $7,500 and $12,500.

Treasury opposes the refundable credit for the elderly. Adequate adjustments for increased energy costs for the consumer are provided in the national energy plan and elsewhere. The credit would also deplete general revenues to the extent of $6.7 billion in the fiscal years 1978–85. In addition, the effect of such a widely distributed refundable credit would be to restore to the tax rolls millions of aged taxpayers who had been removed from the rolls in the last several years.

Thank you, Mr. Chairman.

Mr. AFFELDT [presiding]. Now we will hear from Commissioner Kurtz.

STATEMENT OF JEROME KURTZ, COMMISSIONER, INTERNAL REVENUE SERVICE

Mr. KURTZ. I appreciate this opportunity to be here to discuss several aspects of tax administration that are of concern to the elderly. I will begin with a summary of our programs of assistance to all taxpayers, including the elderly. I will then discuss several specific items of proposed legislation which are of immediate interest to this committee.

The Internal Revenue Service taxpayer assistance program provides the general public with comprehensive information about the Federal tax system. The IRS offers toll-free telephone assistance to all taxpayers. The IRS also provides walk-in service, including returns preparation assistance. Since December 1976, the IRS has provided tax assistance by TV–phone and teletypewriter services for the deaf on a nationwide, toll-free basis.

VITA—Volunteer Income Tax Assistance

In addition to its direct taxpayer assistance activities, the Service promotes the volunteer income tax assistance, or VITA, program to provide tax counseling and help in return preparation. Through VITA, IRS trains volunteers who, in turn, offer tax assistance to taxpayers at convenient locations throughout their communities. The VITA program focuses primarily on providing assistance to lower income, elderly, or non-English speaking taxpayers.

This year, as a result of a special congressional appropriation of additional funds for VITA, we have expanded the VITA program so that this free assistance can be provided to a greater number of taxpayers.

IRS Efforts To Help Elderly

In addition to our overall taxpayer service activities, the Service also has a number of programs which provide benefits especially to the elderly. For example, the Service makes every effort to locate its taxpayer service offices near public transportation and on the first floor of buildings, making them particularly convenient to the elderly and the handicapped.

We are also continuing to conduct retiree income seminars as a part of our overseas taxpayer assistance program. These seminars are designed to assist retirees and senior citizens residing abroad to determine their correct U.S. tax obligations.

We also distribute a number of free publications aimed especially at tax issues relevant to our older citizens. These include: Publication 524, "Tax Credit for the Elderly"; publication 554, "Tax Benefits for Older Americans"; publication 502, "Deductions for Medical and Dental Expenses"; publication 522, "Tax Information on Disability Payments"; publication 575, "Tax Information on Pension and Annuity Income"; and publication 567, "Tax Information on U.S. Civil Service Retirement and Disability Retirement."

Publication 554, a primary source of tax information for the elderly, is printed in large type for easy readability, and is distributed by both the Service and the Social Security Administration. For the 1979 edition, we plan to simplify certain portions of the text and add a comprehensive example with accompanying forms to illustrate many of the tax situations that face senior citizens.

Our public affairs organization conducts a number of programs targeted for the Nation's senior citizens and also works with numerous other organizations to provide specialized media coverage for the elderly. News releases, television and radio public service announcements, and other media material such as question and answer columns, are specifically directed toward promoting older Americans' awareness of the taxpayer assistance and VITA services I have just described.

Tax Benefits for Older Americans

In addition, these materials call attention to features of the tax law of particular interest to the elderly. These include such items as the increase from $20,000 to $35,000 of the nontaxable limit on the sale of a personal residence; the additional $750 personal exemption available to persons age 65 or older; the gross income levels under which persons age 65 or older are not required to file; the nontaxability of social security payments and railroad retirement benefits; the existence of Form W–4P, which authorizes the payor of retirees' pensions to withhold taxes at the source to avoid a large tax bill at the end of the tax year; and the necessity for part-time workers, many of whom are 65 or over, to file for a possible refund if there was any tax withheld from their pay during the year.

Simplify Tax Forms and Instructions

Another major Service activity which benefits all taxpayers, including the elderly, is our ongoing effort to simplify tax return forms and instructions. In addition to the areas of the Internal Revenue Code which are specifically directed at the elderly, the older taxpayer, of course, is subject to all of the general provisions of the code.

However, it has been our experience that the retired taxpayer frequently must deal with some of the complex individual income tax situations such as rental property, income from dividends, pension and annuity income, sales of securities, et cetera. Thus, any simplification achievements realized within the overall forms and publications area directly benefit the elderly.

The Tax Reduction and Simplification Act of 1977 allowed us to make considerable progress in the area of simplification. The computations previously required of most taxpayers for determining the total deduction for personal exemptions, the general tax credits, and the actual tax liability have been incorporated into the new tax tables, and generally do not have to be computed on the return.

Continuing efforts are being made to simplify the language used in the forms and instructions. In 1977, for example, the Form 1040 was pretested among a number of groups to identify potential problem areas. Included among the pretest group were a number of retirees representing the American Association of Retired Persons. We have also assisted the National Association of Retired Persons with their comprehensive tax publication.

There are presently several pending legislative proposals which are aimed at reducing either the economic or administrative burden of income taxation upon the Nation's older citizens. While we defer to the Treasury Department regarding commentary on the substantive features of such pending legislation, we do have some observations to make concerning some of their administrative features.

S. 2128—Tax Credit for Elderly

S. 2128 would increase the maximum credit for the elderly through an initial increase in the maximum amount on which the credit for the elderly is computed, effective with taxable years beginning after December 31, 1976. Beginning with the 1977 tax year, annual increases in the maximum amount would be tied to changes in the Consumer Price Index.

The effective year provision of this legislation, if left unchanged, could result in the filing of a large number of amended returns for 1977. This bill also provides for an elimination of the current phaseout of credit based on adjusted gross income. This could result in a large increase in the number of returns claiming the credit.

S. 835—Older Americans Tax Counseling Assistance Act

Another pending measure, S. 835, provides for reimbursement to volunteers for transportation, meals, and other expenses incurred by them in training or in providing tax counseling for the elderly. This would pose distinct administrative problems for the Service.

Though the reimbursements probably would be relatively small, the Service would have extensive budgeting, monitoring, and audit responsibilities related to the moneys spent by volunteers.

In addition, we are concerned that by providing these reimbursement rights solely for volunteers working with the elderly, this act would work to the detriment of our VITA program, to the extent that it would establish a double standard which would not apply to volunteers working with taxpayers other than the elderly.

S. 1014—Maintaining Older Dependent in Taxpayer's Home

S. 1014 would provide for either a $250 tax credit or a $1,000 deduction to individuals who maintain a dependent age 65 or over within their homes. We believe that this bill would further add to the complexity of the Form 1040 and instructions, since the choice of a credit or deduction would have to be presented on the form and in the instructions, and since the better alternative may not necessarily be clear to the taxpayer.

For example, it would not be advantageous to a taxpayer to use the deduction option unless this deduction, plus other itemizable deductions, exceeded the zero bracket amount and in addition the taxpayer's marginal rate exceeded 25 percent.

Refundable Tax Credit for Rising Energy Costs

Finally, section 1012 of H.R. 5263, the Senate-passed version of the energy bill, would make available a refundable tax credit, subject to an income phaseout, for all individuals age 65 or over who maintain a household. Because the tax credit would be refundable to taxpayers who would otherwise not have any tax liability and would not be required to file, the provision would expand substantially the number of individual returns filed.

Our experience with the refundable earned income credit demonstrates the difficulties of reaching individuals who are not otherwise required to file, to inform them of the credit. The Service does not know the identity of these persons, since they are not on the tax rolls; and they can only be reached through special publicity efforts which may not be wholly successful.

This concludes my prepared remarks, and I will be pleased to answer any questions.

Mr. Affeldt. Thank you very much.

Head of Household Versus Single Status Question

I would like to pose a question to you first, Commissioner Kurtz. From time to time, we receive calls from elderly taxpayers who have questions about tax problems. In this particular example, an elderly lady wondered whether she could claim head of household treatment under these circumstances: She was a single aged taxpayer; she, together with her brothers and sisters, contributed more than one-half of her elderly mother's support. Her mother was 84 years old. She claims her mother as a dependent under a multiple support agreement. She also furnishes more than one-half of the cost of maintaining a household for her mother, and her mother lived with her for more than one-half of the year.

The issue raised was: Can this elderly taxpayer claim head of household status when shé claims her mother as a dependent under a multiple support agreement or would she be required to file as a single person?

Page 14, I think, of "Your Federal Income Tax" publication provides some information. In addition, section 2(b) of the Internal Revenue Code and page 7 of your instructions for Form 1040 would be helpful.

I was asked the question. I thought I knew the answer. I know something about taxes, but I had to do some checking and I was not sure after I read it whether I was right or not.

All right. Let me tell you what the answer is.

Mr. KURTZ. Thank you. [Laughter.]

Mr. AFFELDT. We have an IRS agent who works in the new Senate office building and I raised the question with him and he said the answer is head of household. Section 2(b) of the Internal Revenue Code provides that when a relative must be claimed as a dependent the dependency status cannot be established through a multiple support agreement.

I read some of these instructions and I was not sure. So I asked some of the staff of our committee to make calls to IRS information offices and this is the result. They called nine offices. Five of them said head of household status, four of them said single status. So you know five of them were wrong in this particular case if my interpretation is correct.

ASSURING TAXPAYERS ACCURATE INFORMATION FROM IRS

So that leads to the question I want to raise here. What steps can be taken to provide greater asurances that taxpayers receive accurate information when they call IRS offices? I know the tax law is very complex. In fairness to the IRS, I should point out that we raised another question with regard to what to include in the basis of property when an elderly person would sell that property. In this particular case, there was unanimity with regard to the responses that we received. So, in one case there was agreement.

In this case, which I grant is more complex, there was disagreement. But, the point is that the taxpayer here could be mislead to his or her detriment. What was at stake was potentially hundreds of dollars.

Mr. KURTZ. It is unfortunate, but those things do occur. In every filing season we see reports of those kinds of occurrences.

Overall, the accuracy rate on the telephone assistance is quite high and that is due to the fact that most of the questions asked are simpler than the one you asked. The problem is that a great deal of tax advice, answers to questions during the filing season, are given by temporary employees who expand our services very substantially.

As I say, the accuracy rate overall is quite high. I suppose the answer to some extent might be more training, although our telephone assisters do receive approximately 5 weeks of training before they answer calls, and there are, in addition, the front line assisters, second and third line assisters, who handle more complex questions.

I suppose, ultimately, the answer is a simpler law, a simple law. I have been at it 20 years and I didn't know the answer to your question without doing a fair amount of research.

Now, as I say, I think overall the quality of the advice is good. That does not make it perfect and we keep working with it.

Mr. AFFELDT. Let me just point out something that was confusing to me and may perhaps be inaccurate. You can have your technicians check this item. This is the reason I had some people check on this information on page 7 of the instructions.

Mr. KURTZ. The 1040 instructions?

Mr. AFFELDT. Yes. If you will bear with me, it is the middle column. We have some forms over there that you can examine yourself. The middle column reads, and I quote:

> You may use the filing status—

Referred to as head of household—

> . . . only if, on December 31, 1977, you were unmarried (including certain married persons living apart), or legally separated, and met one of the following tests:
>
> 1. You paid more than half the cost of keeping up a home which was the main home of your father or mother whom you can claim as a dependent (you do not have to live with that parent).

All right. Skip down to (b) where it says:

> Any other person listed in 5(a) under lines 6 (c) and (d)—

And that is children and other dependents on page 8 of the instructions—

> . . . whom you can claim as a dependent provided he or she is not your dependent under a multiple support agreement.

What is 5(a)? When you look over the form, there is no block 5(a) on form 1040, unless there is a reference to something else that confuses me. Block 5, I believe, refers to surviving spouse status for a qualifying widow or widower.

Now 6(c) and 6(d) match up with regard to dependent children who live with you or other dependents who do not live with you but can be claimed as dependents provided certain tests are met. There are basically five tests for a dependent to be claimed.

So I don't know if you can respond at this point, but this appears to be confusing or inaccurate in terms of the line references.

Mr. KURTZ. Well, we will look at it and try to straighten it out.

Mr. AFFELDT. All right. Another question that I have is——

Mr. KURTZ. It is referring to paragraph 5(a) of the instructions but it is not clear.

Mr. AFFELDT. Oh, paragraph 5(a).

Mr. KURTZ. Paragraph 5(a) of the instructions, which is on the next page.

Mr. SUNLEY. The instructions for line 6(d) and 6(c).

Mr. AFFELDT. Paragraph 5(a)——

Mr. KURTZ. It lists the relationship.

Mr. AFFELDT. Where does paragraph 5(a) appear on the form?

Mr. KURTZ. It is not on the form.

Mr. AFFELDT. On the instructions.

Mr. KURTZ. Page 8, lower left-hand corner.

NOTCH PROBLEMS

Mr. AFFELDT. Fine. The tax tables, I think, will simplify tax preparation for many taxpayers because they are not required to make complex computations to determine their tax liability. However, the tax table is divided into increments of $50 which may pose certain notch problems.

For example, a taxpayer with more than $1 of taxable income may wind up paying $21 more in taxes for that additional dollar. I think there may be an incentive for some people to remember suddenly that perhaps they gave an extra dollar or two to the Salvation Army for their cash contributions, putting them in that lower $50 bracket. But, what can be done to lessen the impact of these notch problems and still make the tax computation simple, through the use of the tax table. Would it be possible to break it down into smaller increments?

Mr. KURTZ. The tables have the $50 increments because that was our understanding of the congressional mandate setting the tables forth. The problem is that to break them down into $25 segments will require twice as many tables and there is some trade-off there. We now have some 12 or so pages of tables and to go to $25 increments would give you perhaps 25 pages of tables.

Unquestionably, the wider the bracket, the more questionable the notch. I don't doubt that.

Mr. SUNLEY. You also have taxpayers who benefit by being $1 under the top side; otherwise the amount of tax for every $50 bracket is computed at what the tax would be if they have the income right in the middle. So on average it gets the right answer. It is true that——

Mr. AFFELDT. There is a break-even point.

Mr. SUNLEY. Yes. There are many taxpayers who get a benefit as well under this provision.

Mr. AFFELDT. But the ones who complain are those who lose, of course. They are the people that we hear from, not the winners.

ITEMIZED DEDUCTIONS

I would like to direct another question to you concerning how the tax form deals with schedule A for itemized deductions. We have found that many elderly people overpay their taxes because they are unaware of certain itemized deductions. Do you think that schedule A could perhaps be improved if there would be more specific reference to allowable itemized deductions? In 1970, Commissioner Thrower testified before our committee and we suggested to him at the time that there could be some additional line references with regard to medical expenses, such as transportation. I think eyeglasses was another one.

Mr. KURTZ. They are on there—dentures, transportation. There is also a debate on forms every year as to how much instructions to put on the forms and there is a trade-off between the complexity of the form and the information contained on it. The more you put on it, the more complex it appears and in some respects misleading. If you itemize certain items as being on a line and not every one, which is frequently impossible to do because of the number, it may create an implication that the one not listed is not deductible, so there are considerations both ways, and generally we try to include summary information on the form and rely on the instructions for more details.

In any particular case it is a close question and it does change somewhat from year to year. Where we find that a particular item is overlooked or misunderstood, we tend to put more instructions on the form as to that to demonstrate it is a deficiency.

PAYROLL TAX REDUCTIONS?

Mr. AFFELDT. Let me pose some questions now to Assistant Secretary Sunley. Senator Church, I know, is very much interested in the administration's tax package. Your overall proposal would result in about a $23.5 billion reduction for individuals. This, of course, is designed to offset the social security tax increase that was enacted in December. But Senator Church was wondering whether a different approach may be more effective for individual taxpayers.

What he is thinking about is perhaps targeting more of that relief in the form of payroll tax reductions. This could be achieved perhaps through general revenue financing either partially or totally for the medicare part A hospital insurance program. What this would mean is there may be a smaller reduction for the individual income tax cut to stay within the administration's target of $23.5 billion in tax reductions. But the issue here is: How would the administration feel about having a different mix in terms of a $23.5 billion tax cut?

I know other Senators are giving considerations to this, such as Senator Nelson. Do you have any thoughts about this approach?

Mr. SUNLEY. As you may recall, last year the administration twice proposed some general financing of social security. First, there was the payroll tax credit for employers, proposed as part of the stimulus bill, and the Congress rejected the credit for employers and instead substituted an employment tax credit. Second, in the social security proposals that the administration submitted, provision was made for some general financing of social security, and again Congress rejected that proposal. It is true, that since the social security legislation was enacted, there has been considerable interest in the last few weeks in the possibility of, instead of only income tax cuts, having smaller income tax cuts and some social security tax cuts.

So, my judgment at this time, and it depends on how contentious the issue of financing social security will be, is that it would probably be better for Congress to come back and look at social security in 1979 and not even tangle with that in this year's tax bill. But it is possible, of course, that the Congress will want to cut taxes for individuals by providing both income tax cuts and social security tax cuts.

I would add, though, and this may be of particular interest to this committee, that if the tax program is restructured along the lines that you suggest, the aged social security beneficiaries would receive smaller income tax reductions and generally would not benefit from the social security tax reductions which would be substituted.

Mr. AFFELDT. Under your tax package, most workers will have an overall reduction for their combined social security taxes and income taxes in 1979.

Mr. SUNLEY. That is correct.

BREAK-EVEN POINT

Mr. AFFELDT. What is the break-even point? Do you happen to know off the top of your head?

Mr. SUNLEY. It varies a little bit. The breaking point is about $20,000 of earned income if all the income of a four-person, one-earner family is from earnings. For a four-person, two earner family, the break point is $30,000.

Mr. AFFELDT. What would be the effect in the 1980's when the social security tax rate increases much more sharply? The rate is now 6.05 percent, it rises to 6.13 percent next year. By 1982, it is up to 6.7. In 1985, it rises to 7.05 percent. So, within a period of 7 years, the social security tax rate will increase by 1 percent, and 1 percent for a wage earner earning $20,000 would be a $200 increase in social security taxes.

Mr. SUNLEY. I would anticipate that there would be additional income tax reductions in the years ahead.

Mr. AFFELDT. To offset the——

Mr. SUNLEY. To offset the higher social security taxes and in part to offset the impact inflation may have on pushing taxpayers into higher tax brackets and increasing effective tax rates. Over the last 20 years, it has been the practice for Congress to periodically cut taxes. In fact, the average tax rate of American taxpayers has fluctuated in a fairly narrow band. So, as inflation tends to push effective tax rates up, Congress provides new tax reductions. I would anticipate that this pattern would continue in the future and that it is very likely additional individual income tax reductions would be enacted in 1980.

HOW MUCH ECONOMIC STIMULUS?

Mr. AFFELDT. Senator Church was also wondering whether the tax cuts in recent years, or the one that is proposed now, will have that much economic stimulus. It was his feeling that the last tax reduction did not result in that much money being pumped into the economy. Many people, instead, chose to save the money or to meet some other larger expenses. How do you feel about that? This is one reason that he wonders whether it would be more desirable to target the relief toward social security payroll taxes in order that more lower and moderate-income persons would be the beneficiaries.

Mr. SUNLEY. Well, as you may know, in determining the size of a tax cut to propose, a number of factors are taken into consideration. But the key factor in arriving at the overall dollar magnitude of the program is the amount necessary to sustain economic recovery. We had a very good year in 1977, in terms of reducing the level of unemployment from 7.7 percent in December 1976 to 6.4 percent in December 1977. Also, 4.2 million additional jobs were created in the economy and 1.2 million people were removed from the unemployment rolls. So we are first trying to set a level of fiscal stimulus that will sustain that recovery.

Now this particular level, when it is split between business and individuals, leads to a net tax reduction in 1979 of about $16.8 billion dollars for individuals, and if compared to 1977, the overall effective tax rates in 1979—that is to say, individual tax rates plus social security tax rates—will be about the same as they were in 1977.

Mr. AFFELDT. Is the $16.8 billion a net reduction? You have $23.5 billion in tax relief through lower Federal income taxes. I gather there is going to be an offset here because of increased social scurity taxes. What else would offset this $23.5 billion reduction to get to your net.

Mr. SUNLEY. The social security is not a part of the net. The net is from a gross of $23.5 billion to a net of $16.8 billion. The difference is revenue raising reforms and structure reforms in the individual income tax.

$925 MILLION TAX REDUCTION PROPOSED FOR ELDERLY

Mr. AFFELDT. In this context, you indicated that elderly people would receive a $925-million reduction in their taxes under the administration's proposals. But there are also some items that would take away itemized deductions for the elderly, such as elimination of the deduction for the personal property tax, the sales tax, and the gasoline tax. These three items, in 1974, provided more than $700 million in relief for aged taxpayers. You are also constricting the deduction for medical expenses.

In 1974, the medical expense deduction was claimed by about 2 million tax returns with an aged taxpayer, producing $2.8 million in tax relief.

My question to you is, whether this $925 million in tax relief takes into account these losses in your tax relief provisions that had been available to the elderly? Is this a net figure or is it something else?

Mr. SUNLEY. No, the $925 million figure is a net figure. It is a component of the $16.8 million of net.

Let me, if I may, elaborate a little bit on the itemized deduction changes. First, it should be be kept in mind that out of 24 million Americans age 65 or over, 18 million pay no Federal income tax currently, so those who pay income tax currently are generally the better off of the aged.

Second, in proposing changes in itemized deductions such as the repeal of the deductions for gasoline taxes and sales taxes and the revisions in the medical deduction, we proposed at the same time rate reductions which will in most cases offset the tax increases that would come from the repeal of certain itemized deductions. Also, 96 percent of all American taxpayers who now pay taxes get a tax reduction under the program. There are something like, I think, 2½ million taxpayers who would have a tax increase under the program.

Mr. AFFELDT. That many taxpayers or returns on which taxpayers are claimed?

Mr. SUNLEY. Those are returns on which taxpayers are claiming itemized deductions.

I believe you know that our itemized deduction proposals are quite consistent with your line of questioning of Commissioner Kurtz expressing worry about the complexity of itemized deductions. The medical deduction now has some 10 to 12 lines on the form, requiring you first to segregate your insurance premiums, and then to compute 3 percent of income, so you may deduct in excess of 3 percent, and then to compute your drugs in excess of 1 percent, but to count toward that in the excess of the 3 percent computation. As you can see, this has been a source of considerable complexity.

Although it is true that the elder Americans probably have higher medical expenses than the nonaging, they tend also, of course, to be better protected by insurance. So, I believe that this program of revising the medical deduction when accompanied by significant rate reductions will not have an adverse impact on the aged.

I should add that even of the 6 million aged who currently pay income tax, most of them do not itemize their deductions. Most of them claim the standard deduction and would not be affected in any event.

Mr. AFFELDT. For the record, out-of-pocket per capita health care costs for the elderly are somewhere between $400 and $500 a year. This is even with medicare, medicaid, and other Federal reimbursement programs.

REIMBURSEMENT FOR EXPENSES IN PROVIDING TAX ASSISTANCE

You made some comments about the legislation that I find interesting. But first, I would like to raise a question with you concerning the treatment of reimbursement for meals and out-of-pocket expenses for people who would be doing tax counseling assistance. This may qualify as rendering service for a charitable organization. When you render services as an individual taxpayer for a charitable organization, you may claim mileage. You may claim either your actual expenses, or you make take a standard mileage rate of 7 cents a mile.

For my own edification, a taxpayer who performs services for a charitable organization and incurs meals expenses would not be able to claim out-of-pocket expense deduction for the meals unless he is away from home overnight. Would that be the same as for business purposes?

Mr. KURTZ. Yes, that is my understanding.

Mr. AFFELDT. The provision in S. 835 would exempt the reimbursement for travel and meals as being includable as income. If you were to include the reimbursement as income, it would probably not be that much. In addition, it may create more problems for the elderly taxpayer in terms of filling out his tax form.

With this in mind let me ask you this question. If this provision were changed, what would the Treasury's position be with regard to S. 835? Would the Treasury be inclined to support enactment of the bill if the reimbursement provision would be adjusted to your satisfaction?

Mr. SUNLEY. We are generally opposed to introducing another statutory exclusion from the tax base. Commissioner Kurtz also pointed out the inequity of having one set of rules applying to volunteers who counsel the aged, and then a different set of rules applying to volunteers who counsel the nonaged. I think that would give us some trouble.

Mr. AFFELDT. There is another way of dealing with that problem, and that, of course, is to treat the others the same way as the elderly are treated. One of the tax counselors under the tax aid program, Ira Funston, pointed out that some people are discouraged from participating in the program because they are incurring out-of-pocket expenses. Some elderly people living on limited budgets may be very competent tax preparers, but they may discover that it is a hardship to incur these expenses.

Mr. SUNLEY. Again, I think we should remember the very high tax-free levels of income that are currently provided the aged in the income tax law and what the administration is proposing. When you are talking about the elderly for whom taxing these reimbursements would be a hardship, you are probably also talking about an elderly individual or an elderly couple who is currently not subject to income tax. So there are no tax consequences of having the reimbursements included in the tax base.

Mr. AFFELDT. We are talking about tax-free levels of $6,400 for individuals and $10,450 for elderly couples.

Mr. SUNLEY. Other than social security.

Mr. AFFELDT. But even so, an individual having $10,000 in income is certainly not living lavishly, particularly in an area like Washington, D.C. It is very costly and it still may be expensive. I don't know if we are going to settle this at all, but we do feel there is a justification for having this provision.

If you feel that there is some middle ground on this measure, or some other way to improve it, we are open to your suggestions.

Let me get back to this point. Assuming that we could work out some of these problems concerning the Older American Tax Counseling Assistance Act, would the administration support the enactment of the overall bill?

Mr. SUNLEY. From a tax policy point of view, we have no problem if the special exclusion of the reimbursement was omitted from the bill. Jerry may have some problems with other aspects of the bill.

REHIRING OF FORMER IRS AGENTS

Mr. AFFELDT. I may also point out the IRS suggested, the last time we developed this bill, that there be a provision in there to permit the rehiring of former IRS agents. We put that provision in the bill at the suggestion of the IRS and we thought that it would be desirable. However, it did create problems with the Civil Service Commission. So, it was deleted this time when the bill was reintroduced. There is no objection to that provision from a substantive standpoint. It was deleted for strategy reasons.

We would like to sit down with officials from the Treasury or IRS to see if we can work out something.

Mr. SUNLEY. We have met with you and your staff before, and I look forward to meeting you again.

INCOME BENEFICIARIES UNDER S. 2128

Mr. AFFELDT. In this context, you have expressed opposition to Senator Inouye's proposal, S. 2128.

Mr. SUNLEY. Yes, sir.

Mr. AFFELDT. For the record, I would appreciate it if the Treasury could indicate to us how that relief would be targeted by adjusted gross income brackets. The reason I am making that request is because I obtained some different figures when I called Treasury. The assumptions may have been different. The additional cost was based on 1976 income levels under the 1978 law. The total figure I received was $767 million. Of that total, $365 million, or 46 percent, would be attributable to taxpayers with adjusted gross income exceeding $20,000.

So, if you could just provide this information for the record, we would appreciate it.

Mr. SUNLEY. It may be the difference between the 1976 levels of income and 1978.

Mr. AFFELDT. You were able to get the 1978 income levels.

Mr. SUNLEY. We will check and provide a table for the record.

Mr. AFFELDT. Thank you.

[Subsequent to the hearing, the Treasury Department provided the following distribution of the revenue loss under 1978 law and at calendar year 1976 income levels:]

Adjusted gross income class:	Revenue loss (millions)
0–5	$3
5–10	71
10–15	192
15–20	165
20–30	163
30–50	109
5–100	64
100 and over	29
Total	796

Mr. AFFELDT. One last question. We may submit some additional questions to you in writing.

Would the administration support any type of proposal to modernize the tax credit for the elderly, and if so, what would it be? If you are opposed to the so-called Inouye bill, S. 2128, is there something else that you would accept as an alternative, such as raising the maximum amounts for computing the credit to $3,000 for individuals and $4,500 for elderly couples filing jointly, or other changes as well?

Mr. SUNLEY. Of the three changes which are proposed in Senator Inouye's bill, the most serious problem is removing the adjusted gross income limit. I think that would be conclusively in contradiction to the basic purpose of the credit for the elderly as it was enacted. We also have trouble with the indexing. We would have less problem with increasing the $3,750 to $4,500. But it was not a proposal that the administration made.

Mr. AFFELDT. It is my understanding the costs of this provision would be around $50 million.

Mr. SUNLEY. Yes, the cost of that change would be smaller.

[Subsequent to the hearing, the Treasury Department provided the estimate of $79.5 million in taxable year 1978.]

Mr. AFFELDT. Mrs. Fayé.

Mrs. FAYÉ. No questions.

Mr. AFFELDT. As I said before, I would like to proceed further but we must hear from other witnesses.

One other thing for the Commissioner of IRS. We would like to discuss with you and your staff some alternative funding levels that Senator Church may seek with regard to the volunteer income assistance program and we shall contact you by phone.

Mr. KURTZ. We will be happy to do whatever we can to be helpful.

Mr. AFFELDT. Thank you very much. We appreciate your testimony.

Mr. SUNLEY. Thank you.

Mr. AFFELDT. We have three groups testifying after the administration. What I plan on doing now is to call them up individually. After all three have had an opportunity to present their testimony, we can pose questions to the three groups.

Our next witness is David Marlin, who is the director of Legal Research and Services for the Elderly.

STATEMENT OF DAVID H. MARLIN, WASHINGTON, D.C., DIRECTOR, LEGAL RESEARCH AND SERVICES FOR THE ELDERLY, NATIONAL COUNCIL OF SENIOR CITIZENS

Mr. MARLIN. Thank you, Mr. Affeldt.

My testimony this morning is based on two things. One is during the 10 years experience I have had with the membership of the National Council of Senior Citizens, 3.5 million persons, discussing their tax liabilities and their difficulties with Federal tax forms. The second is a survey with consumer emphasis that we made in response to the committee's invitation to testify today. We conducted a telephone survey[1] among 20 selected major State and local organizations of older persons, elderly law projects, area agencies on aging, and senior centers to assess: The expressed demand by older persons for assistance in completing Federal tax forms, the cooperation between IRS and these organizations in disseminating tax saving information and assistance for older persons; and the major problem areas in the language of the IRS tax instructions and tax forms.

In addition, we have reviewed the IRS publication 554, "Tax Benefits for Older Americans"; the "Volunteer Income Tax Assistance Course Book"; the 1977 instructions for Forms 1040 and 1040A as well as the 1040 forms and schedules A, B, D, E, R, and RP.

The findings of this brief, informal study are as follows:

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[1] See p. 25 for listing.

Low Demand for Tax Assistance

Older persons' expressed demand for tax assistance: Despite the fact that we are currently in the Federal income tax season, none of the organizations contacted have been flooded with requests from older persons for tax assistance. Two District of Columbia organizations, Legal Counsel for the Elderly and PEP—both of whom have widely publicized tax assistance clinics—reported only low to moderate utilization of their services.

The Older Philadelphians Legal Services Plan, which is a new, older-person controlled, low-cost telephone advice and reduced fee referral program which specifically includes assistance in tax matters as a covered service, has had a similar utilization rate during its first month of operation. With 1,000 enrolled members, OPLS has had only 10 inquiries regarding tax matters. Of these inquiries, four involved Federal tax matters.

Also, 14 other organizations and/or agencies representing primarily the urban elderly reported only limited demand by older persons for tax assistance, as did 3 organizations serving primarily rural areas.

The critical issue, of course, is what does low demand for tax assistance mean? It may mean that the annual filing of Federal income tax forms—although not a pleasant task—is at least a familiar one. It is not a new burden thrust upon older persons when they reach retirement age.

Or perhaps, H. & R. Block, and similar private entrepreneurs, have simply cornered the market and currently satisfy the demand by older persons desiring assistance in completing income tax returns.

In addition, this is only February and there will be an increased demand as the filing date draws closer.

However, lack of demand for assistance may also be reflective of older persons' lack of awareness of the tax savings they might realize through careful preparation of their income tax returns.

Effectiveness of IRS information and assistance efforts: In assessing the validity of this last explanation, we asked the organizations we contacted three questions:

One: Are you aware of any IRS efforts in your area to educate older persons regarding changes in the tax laws and to provide assistance in filing the tax returns?

Two: Has your organization been contacted by the IRS to disseminate Federal income tax information to your clients and/or members?

Three: What recommendations would you make for improving IRS tax assistance to the elderly?

The majority of the 20 organizations contacted were aware that IRS provided tax assistance to the general population through district and local IRS centers.

However, they pointed out that such services were confined to larger population centers and generally not well publicized. Older persons in rural areas, particularly, may be unaware of the free tax service available from IRS.

Although IRS does have toll-free lines, these lines are not listed in the telephone directories of towns or counties lacking an IRS office.

The second major IRS effort to educate older persons regarding tax benefits, IRS publication 554, "Tax Benefits for Older Americans," has not been received by the majority of the organizations contacted. The few who had read it described it as too complex for the ordinary older taxpayer.

In addition, 18 of the 20 organizations responded that they have never been contacted by IRS to serve as conduits of tax information to older persons. The two contacted were invited and did participate in an IRS sponsored volunteer income tax assistance program. They found the training generally useful, but questioned whether it was sufficient to prepare non-tax-trained persons to effectively assist older persons in tax return preparation. They also questioned the adequacy of the VITA program in terms of its priority within IRS with respect to space and staffing as well as its realistic capacity to serve large numbers of persons.

For example, the Philadelphia-based VITA program was able to assist 800 to 900 persons—both old and young—to prepare tax returns during the past year. As there are over 327,000 persons in Philadelphia 60 years of age and over, the resources of the VITA program are insignificant should a significant portion of older Philadelphians desire tax assistance.

Suggestions to Improve IRS Services

As for methods of improving IRS services aimed at older taxpayers, the following suggestions were offered by the contacted aging organizations:

IRS might publish and disseminate through the State and area agencies on aging, as well as through the major national and State organizations of older persons, reproducible drop ads which simply and clearly summarize tax provisions favorable to older persons. These organizations could publish these ads in their own publications or in local newspapers.

IRS might publish and disseminate simple 1- or 2-page descriptions of the major tax provisions important to older persons which could be used as handouts in community education programs currently being offered by elderly law projects and community colleges.

In rural areas, IRS might circuit-ride during tax season through towns and counties not having a permanent IRS office. In many rural areas, social security has already established this practice and found it useful in meeting the needs of older persons.

The WATTS-line number of IRS should be publicized in local newspapers, on television and radio stations.

The basic IRS informational piece directed toward older persons is "Tax Benefits For Older Americans." Rather than critique it in detail, I suggest that the committee simply compare it to the Commerce Clearinghouse, Inc., January 21, 1977, publication entitled "Special Tax Benefits for the Senior Citizen." Both publications cover substantially the same material; however, CCH's treatment is far simpler and more logical. It is written from the point of view of the taxpayer. Using questions many older persons might have as a guide, the CCH publication clearly sets out the basic provisions in the tax law affecting older persons and explains tax saving techniques. Perhaps IRS should simply distribute CCH's publication rather than writing or revising its own. I believe the Commissioner said they were going to revise it.

Regarding the tax forms themselves, we offer two basic suggestions:

One: The various schedules should be screened in color like forms 1040 and 1040A and set in large type to enable older persons to read them more easily. The typeface for the instructions for form 1040, particularly, should be substantially enlarged.

Two: Form 1040A might include a line for pension income to enable older persons living solely on pensions and social security to fill out form 1040A rather than the 1040 long form.

Beyond these cosmetic changes, it appears to us that IRS has translated the complex provisions of the tax laws into fairly understandable forms. The remedy for the complexity of schedules and forms does not appear to us to lie with the IRS but with Congress.

Congress, of course, must continue to balance the need for simplicity in tax laws with the public policy of shielding vulnerable population groups from an undue tax burden through a system of credits and deductions. As older persons presently benefit from many of the tax preferences which contribute to the complexity of the tax forms, we would resist the push for simplicity of forms if the net result would be to increase rather than decrease the Federal tax burden on the elderly.

[The listing of organizations to which Mr. Marlin referred to follows:]

ORGANIZATIONS CONTACTED REGARDING TAX ASSISTANCE FOR OLDER PERSONS

(1) Action Alliance, Philadelphia, Pa.
(2) Archdiocesan Council of Senior Citizens, Philadelphia, Pa.
(3) Barney Senior Citizens Center, Washington, D.C.
(4) Bay Area Senior Citizens Legal Services, Tampa, Fla.
(5) Betterment for United Seniors, Prince Georges County, Md.
(6) Georgia State Office on Aging, Atlanta, Ga.
(7) Greater Boston Legal Services Elderly Law Program, Boston, Mass.
(8) Legal Council for the Elderly, Washington, D.C.
(9) Legal Services for Maine's Elderly, Augusta, Maine.
(10) Massachusetts Association of Older Persons, Boston, Mass.
(11) Mississippi Council on Aging, Jackson, Miss.
(12) Model Cities Senior Citizens Center, Washington, D.C.
(13) National Council of Senior Citizens, Washington, D.C.
(14) Northwestern Legal Services, Erie, Pa.
(15) Older Philadelphians Legal Services Plan, Philadelphia, Pa.
(16) Operation PEP, Washington, D.C.
(17) Pennsylvania Association of Older Persons, Harrisburg, Pa.
(18) Philadelphia Corporation for Aging, Philadelphia, Pa.
(19) Southern Mississippi Area Agency on Aging, Biloxi, Miss.
(20) Southwestern Mississippi Area Agency on Aging, Natchez, Miss.

Mr. AFFELDT. Thank you, Mr. Marlin.

We shall hear from our next witnesses and then we shall call you up to respond to questions later.

Now we shall hear from the National Retired Teachers Association and the American Association of Retired Persons. Mr. Hacking is the assistant legislative counsel and Arthur Stanat is a tax-aide counselor in Washington, D.C.

STATEMENT OF JAMES HACKING, WASHINGTON, D.C., ASSISTANT LEGISLATIVE COUNSEL, NATIONAL RETIRED TEACHERS ASSOCIATION/AMERICAN ASSOCIATION OF RETIRED PERSONS, ACCOMPANIED BY WILLIAM C. McMORRAN, NATIONAL COORDINATOR, TAX-AIDE PROGRAM

Mr. HACKING. Thank you, Mr. Affeldt.

My name is James Hacking. I am assistant legislative counsel for the 11-million member National Retired Teachers Association/American Association of Retired Persons.

On my far right is William C. McMorran. He is national coordinator of the association's tax-aide program. On my immediate right is Arthur Stanat, who is a tax aide counselor.

I would like to submit my full statement for the record of the hearing, and with your permission, I would like to summarize some parts of it.

Mr. AFFELDT. Your statement will be incorporated in the record.[1]

Mr. HACKING. As I proceed I would like to focus on a wide number of topics. First, I shall make some comments about the background in the context of which the tax reductions have been offered this year. Second, I shall comment on some of the specific items contained in the package. Third, I shall comment on some items and issues of concern to older persons that are not included in the package, but which we would like to see included. Finally, I shall address the need on the part of the elderly for tax assistance and the Older Americans Tax Counseling Assistance Act. Mr. Stanat will then supplement my remarks with some comments about his experience as a tax-aide counselor in the District of Columbia.

With your permission I will proceed.

This administration has offered its tax cut package this year for a number of reasons. The first, of course, is the need to strengthen and maintain the economic expansion and further lower the unemployment rate. Second, there is a need to offset the increasing income tax burden that results from the combination of inflation-induced income increases and the progressive income tax rate structure. Third, business investment is in need of stimulus. Business activity has lagged ever since the economic recovery began in 1975. Finally, and I think for us most importantly, the tax cut package has been offered in part to offset the social security payroll tax increase that took effect this year and the one scheduled for next year.

CONCERN ABOUT INCREASED PAYROLL TAXES

We are seriously concerned over what may be developing here—namely, a public policy of increasing payroll tax burdens on the one hand and cutting income taxes on the other. Here is why. First, such a policy will increase the share of Federal Government revenue derived from regressive payroll taxes relative to that derived from progressive income taxes.

Second, at a time when continued reduction in unemployment is a primary economic goal, it makes no sense to discriminate against

[1] See p. 30.

labor by enacting legislation that schedules enormous increases in payroll taxes. Higher payroll taxes increase the cost of labor and make reducing employment that much more difficult. This is especially so when you look at other increases in cost that have been legislated and will be legislated, for example, increases in unemployment insurance taxes and the energy bill.

Third, many households will lose more from payroll tax increases than they will gain from income tax cuts. That is not, of course, true in the case of households of workers who are not affected by payroll tax increases; these households will have a very substantial windfall via the income tax cuts.

Rather than scheduling enormous increases in payroll taxes to shore up the social security system and then cutting income taxes to offset the adverse economic consequences of the initial policy choice, it would have made better sense and created fewer problems to have introduced some limited use of "general revenues" into the cash benefit programs to deal with the short-term financial imbalance problem.

Limited Use of General Revenues for Social Security

Since 1975, our associations have advocated a limited, and hopefully temporary, use of general revenues to fund a portion of the cost of automatic benefit increases to the extent that those increases exceed a specified level, say, for example, 4 percent a year. The administration last year came out with a proposal that would have replaced from general revenues income lost to the social security system as a result of unemployment rates in excess of 6 percent. We thought that too made a great deal of sense.

We have very good reasons for continuing to espouse these two limited uses of general funds directly in the cash benefit programs. First, these two general revenue devices—one on the outgo side and one on the income side of the social security ledger—will insulate the system from the extraordinarily adverse consequences of high rates of inflation and unemployment over time.

Second, they will assist sound financial planning for future payroll tax needs by assuring a minimum amount of income to the system each year and also by assuring that the payroll tax mechanism will only be called upon to fund the cost of automatic benefit increases up to a specified maximum level; the annual cost of automatic increases excess of that level would come from the general fund. It is almost impossible for an actuary to sit down today and tell you over the 75-year projection period what inflation is going to be. They try to make reasonable projections, and today those projections may indeed be reasonable when made, but that does not mean that they will turn out to be correct.

Third, by desensitizing the social security system to adverse economic dvelopments, not only would the system be better protected but beneficiaries and workers would have greater assurance of its ongoing financial viability.

Fourth, by introducing general revenues into the cash benefit programs, some of the inflationary pressures that payroll tax increases cause could be avoided. In many sectors of the economy, businesses simply mark up prices as a percentage over cost, and in that respect, as the costs go up, so do the prices. That means more inflation.

At this juncture we would strongly urge that the Congress set about developing legislation to introduce general revenue uses into the cash benefit programs and repeal at least part of these payroll tax increases that are scheduled for future years.

Now, I would like to comment on specific items contained in the administration's tax cut package, indicating those we specifically support, those we specifically oppose, and one we would like modified.

Administration Tax Proposals Supported

First, we support the administration's proposal to reduce the marginal tax rates for individual income taxpayers. This, of course, will help to counteract the tendency of inflation to push people into higher tax brackets.

Second, we support the proposals to reduce corporate tax rates and strengthen the investment credit. Business investment has lagged all through the recovery and certainly is in need of some stimulation.

Finally, we endorse the repeal of what remains of the communications tax and the proposed reduction in unemployment tax rates.

Administration Tax Proposals Opposed

Certain items in the package we specifically oppose.

We oppose the administration's proposal to eliminate the existing deduction for medical care expenses and substitute a single hardship loss deduction—with a high threshold amount—for such medical care expenses and casualty and theft losses. I would point out that in taxable year 1974, 27 percent of all returns filed by persons age 65 and over claimed the medical expenses deduction. I would also point out that the rising cost of health care is imposing an increasing expenditure burden upon the elderly. I believe, Mr. Affeldt, you have already stated for the record the present level of out-of-pocket medical expenses on the part of the elderly.

We oppose the administration's proposal to eliminate the deductibility of nonbusiness sales and personal property taxes. The administration, in justification for this particular proposal, indicates that the elimination of the deductibility of these taxes would relieve the taxpayer of a great recordkeeping burden. Well, we are certain that the elderly taxpayers who in 1974 filed 1.9 million returns claiming deductions for sales taxes and the 800,000 returns claiming deductions for personal property taxes would prefer to endure the administrative burden and spare themselves the increased taxes. It is interesting that almost every time some tax simplification proposal surfaces, it usually entails an increase in taxes for the taxpayer and some revenue gain for the Treasury.

We believe that some degree of tax simplification can be achieved that lowers the taxpayer's burden. For example, if one wanted to simplify the medical expense deduction, one might eliminate the 1-percent floor for drugs and the 3-percent floor for medical expenses. That would certainly be advantageous to the elderly.

Finally, our associations are opposed to the administration's proposal to tax interest earned on premium payments for deferred life annuities as that interest accrues during the accumulation period prior to the annuity starting date. The administration claims this has become a "tax shelter." We believe that this proposed change is going to discourage persons from saving for their retirement and this matter is of increasing concern to us.

If you review the statistics, you will find that the elderly are increasingly dependent for income on Government programs and have not been providing on their own for their later years of life. It has been a long-standing policy of the association to support incentives, in addition to those available under current laws, as for example, tax breaks to encourage the establishment of private pension plans and IRA accounts, to reverse this trend among the elderly toward increasing income dependency. Also, we think more incentives are going to be needed to offset the antisaving bias that long term and high level rates of inflation may very well cause.

Credit for Personal Exemption Deduction

The final item on which our associations wish to comment with respect to the administration's package, is the $240 credit per exemption as a replacement for the present $750 deduction per exemption and the general tax credit. The associations would modify this proposal to give the taxpayer the choice between the combination that is available to them under the present law or the $240 credit per exemption that the administration has proposed.

We believe it is enough that inflation-induced income increases have been pushing people into higher tax brackets and increasing their tax burden and, in effect, shifting the burden of the income tax upwards. There is, consequently, a modest amount of tax reform going on automatically. We don't think it is necessary to take away certain tax advantages that are available to persons and take the increased revenues gained thereby and redistribute it to persons in th lowest tax brackets—as has been the practice in recent years when the Congress has designed tax cut legislation—in order to achieve some measure of tax reform. We think it is enough that some reform is being achieved automatically now. We would give the taxpayer the choice on this item in the administration's package.

I would like to comment briefly on some items that are not included in the package. First, it is the elderly tax credit. The second is the sick pay exclusion. The third is the 3-year rule on annuity income

Tax Credit for Elderly

With respect to the tax credit for the elderly, we would like to see as a part of this tax cut package an increase in the amount that can be taken into account for the purpose of computing the credit and hopefully some increase in the $7,500 trigger figure for the phaseout figure.

We have indicated our support for Senator Inouye's bill, which is sponsored on the House side by Congressman Bafalis. However, in view of the administration's strenuous opposition, as expressed this morning, we would accept some modest liberalizations in the credit that would remedy some of the inequities in the current treatment of persons under 65 and persons over 65 under schedules R and RP. That should certainly be possible, considering the number of cosponsors that are interested in the Inouye and Bafalis bills.

Sick Pay Exclusion

As far as the sick pay exclusion is concerned, we would at least like to see the trigger figure for the phaseout increased in the case of married couples filing joint returns. At the present time, it is $15,000 for both single persons and married couples. We also would like to see a one-for-two phaseout for AGI in excess of $15,000, rather than the present one-for-one. I would add that the phaseout I have just described for sick pay should also be adopted for the elderly credit since both provisions are supposed to work in harmony.

Finally, you know that in the tax treatment of annuities under the Internal Revenue Code, section 72, persons who are not able to recover their contribution costs within 3 years must set up what is called an "exclusion ratio." In other words, they can only exclude from a gross income a portion of their cost from the payments they receive each year. The remainder of the payments have to be included in gross income. If the annuity is for life, the taxpayer has to use IRS life tables to set up the exclusion ratio. It seems to us that the Treasury could very well afford to suffer a modest revenue loss and allow the taxpayer to recoup his cost contributions before he is required to include any payments in gross income.

Tax Preparataion Problems of Elderly

Now I would like to deal briefly with the subject of tax preparation problems of the elderly. It has already been said here today that when a person retires the tax rules with which he is confronted change because their income sources are different. We have found that the elderly certainly are in need of tax preparation assistance. That is why our tax-aide program was begun. I think that, in view of the fact that last year our tax-aide program helped in the preparation 475,000 returns, you should have some idea of the need for this type of service.

I would like now to ask Arthur Stanat, one of our tax-aide counselors, to comment on his experiences helping individual senior citizens prepare their tax returns.

Mr. Affeldt. Thank you very much, Mr. Hacking, your prepared statement will be entered into the record at this time.

[The prepared statement of Mr. Hacking follows:]

Prepared Statement of James Hacking

I. The Administration's Tax Reduction and Reform Proposal: In General

Four factors have motivated the administration to develop a tax cut package that will reduce Federal income tax liability for individuals and business by about $25 billion in 1979. First, there is need to strengthen and maintain the ongoing economic expansion and thus perpetuate the downward trend in unemployment. Second, there is a need to offset the increasing income tax burden that results from the combination of inflation-induced income increases and the progressive tax rate structure. Third, business investment is in need of stimulus; it has lagged appreciably since the economy began to recover from the bottom of the recession in 1975. Finally, increases in payroll taxes for social security and unemployment insurance need to be offset.

Our associations have supported the individual and corporate income tax reductions that have been enacted during the past few years to facilitate economic recovery. But we would also point out that recent tax cut legislation, as shaped by the Congress, has not returned the same amount of real income to each household that it has lost as a result of inflation-induced increases in tax liability. Instead, tax reductions have been concentrated on lower and middle income households. The combined impact of inflation-induced increases in tax burdens and tax relief concentrated among lower and moderate income taxpayers has resulted in a redistribution of the income tax burden among income groups. If one of the objectives of tax reform is a shifting of the Federal income tax burden toward higher income households on the grounds that they have greater ability to pay, then this combination has already achieved some modest degree of tax reform.

Unfortunately, the context in which the present tax cut package is proposed is more complicated than in past years. We are seriously concerned about the consequences of a policy of increasing social insurance payroll taxes on the one hand and cutting income taxes on the other. First, such policy will increase the share of Federal Government revenue derived from regressive payroll taxes relative to that derived from progressive income taxes. Second, at a time when continued reduction in unemployment is a primary economic goal, it makes no sense to discriminate against labor by enacting legislation that schedules enormous increases in payroll taxes. Higher payroll taxes increase the cost of labor (relative to the cost of capital) and make reducing employment that much more difficult. Third, many households will lose more from payroll tax increases than they will gain from income tax cuts; households not subject to the payroll tax increases will gain a windfall via the income tax cuts.

Rather than scheduling enormous increases in payroll taxes to shore up the social security system and then cutting income taxes to offset the adverse economic consequences of the initial policy choice, it would have made better sense and created fewer problems to have introduced some limited use of "general revenues" into the cash benefit programs to deal with the short-term financial imbalance problem. The excess of outgo over income—a situation that has existed since 1975—is primarily attributable to the impact that elevated rates of inflation and unemployment have had upon the social security programs. Since benefits move up automatically with inflation, the higher the inflation level, the higher the outgo from the system. As consumer purchasing power declines (as a result of inflation, higher taxes, etc.) unemployment increases and payroll tax contributions to the system fall below anticipated levels. The public policy answer to the social security short-term financial imbalance should have responded, but did not, to the economic causes of the problem.

Beginning in 1975, our associations have advocated a limited (and hopefully temporary) use of general revenues to fund a portion of the cost of automatic benefit increases to the extent that those increases exceed a specified level (for example, 4 percent). As the rates of inflation and unemployment decline and the difference between the rate of inflation and the rate of increase in average covered wages in social security covered employment increases, the annual general revenue contribution should gradually phase out automatically. In addition to our own proposal, last year we endorsed the administration's proposal that would have used general revenues to replace income lost to the social security system as a result of unemployment rates in excess of 6 percent. As unemployment declines below that figure the annual general revenue contribution for this purpose would also phase out automatically.

Our associations continue to espouse these two specific uses of general revenues for the cash benefit programs. First, these two general revenue devices—one on the outgo and one on the income side of the social security ledger—will serve to protect the system from the two-fold threat posed by high rates of inflation and unemployment. Second, they will assist sound financial planning for future payroll tax needs by assuring a minimum amount of income to the system each year. They will also assure that the payroll tax mechanism will only be called upon to fund the cost of automatic benefit increases up to a specified maximum level; the annual cost of automatic increases in excess of that level would come from the general fund. Third, by desensitizing the social security system to adverse economic developments, not only would the system be better protected, but beneficiaries and workers would have greater assurance of its ongoing viability. Fourth, by introducing general revenues into the cash benefit programs, some of the inflationary pressures that payroll tax increases cause could be avoided.

We would not wish to leave this topic without some comment on the source of the "general revenues" which we propose to use for social security purposes. In our view, these "general revenues" can come from: (1) Increased and non-earmarked revenue derived existing or new tax mechanisms; (2) deficit financing through the sale of Federal securities; and (3) the shifting of expenditure priorities within the context of the Federal budget. To the extent that general revenues are needed for social security purposes in any year, the choice of the source for those general funds should be made in the light of the needs of the economy at the time. We hasten to add that since our associations believe the Federal budget ought to be balanced over the business cycle, no single source for those general revenues should be relied upon year after year.

In view of the foregoing, it should be clear that our associations believe the Congress, by choosing to rely almost exclusively on payroll tax increases to deal with the short-term financial imbalance in the social security system, made a serious mistake. We felt compelled to acquiesce in what the legislative process produced in order to avoid the interruption of benefit payments (the D.I. trust fund was projected to run out of assets next year). Nevertheless, we urge new legislation to introduce some general revenues into the system as a substitute for at least some of the payroll tax increases now scheduled under current law. We would add a note of urgency to our entreaty. We fear that, if our recommendation is ignored, a crisis between the generations will be precipitated as scheduled payroll tax increases become effective and FICA payments become larger and more visible on pay stubs of current workers.

II. COMMENTS ON SPECIFIC ITEMS CONTAINED IN THE ADMINISTRATION'S TAX CUT PACKAGE

Before advancing certain proposals of our own, we would like to address certain items contained in the administration's 1978 tax reduction and reform package. Some, we specifically endorse. First, we support the administration's proposal to reduce the marginal tax rates for individual income taxpayers. This proposal will help to counteract the tendency of inflation to increase the share of personal income that taxpayers pay in Federal income taxes, thus diminishing the fiscal drag that, automatically, rising tax collections have on the economy. Second, we support the proposal to reduce corporate tax rates and strengthen the investment credit. Reducing the effective rates of tax on income from capital and providing business with additional incentives to invest should help to promote long-term capital formation, improve productivity and strengthen and maintain the current economic recovery. Finally, we endorse the repeal of what remains of the communications tax and the reduction in unemployment tax rates. These proposals should help to reduce both business and individual living costs.

Certain items in the package, we specifically oppose.

First, we oppose the administration's proposal to eliminate the existing deduction for medical care expenses and substitute a single hardship loss deduction (with a high threshold amount) for such medical care expenses and casualty and theft losses. We would point out that in taxable year 1974, 27 percent (2 million) of all returns filed by persons age 65 and over (7.4 million) claimed the medical expense deduction. The rising cost of health care is imposing an increasing expenditure burden upon the elderly, among whom the incidence of chronic illness is high. That same cost trend is diminishing any real prospects for a significant expansion of health care protection through the existing medicare program or through a new national health program.

We recognize that the administration's proposal to curtail the medical expenses deduction was advanced, in part, in the name of tax simplification. We propose that the medical expense deduction be retained but, in order to achieve some degree of simplification, the 1 percent floor for medicine and drugs (IRC section 213(b)) and the 3 percent floor (IRC section 213(a)) for other medical expenses should be eliminated at least with respect to elderly taxpayers.

Our associations also oppose the administration's proposal to eliminate the deductibility of non-business sales and personal property taxes. While it is true that these deductions entail a substantial recordkeeping burden and that eliminating them would make tax reporting simpler for the taxpayer, that simplification would come at a price of higher tax burdens on the taxpayers affected. We are certain that the elderly taxpayers who, in 1974, filed 1.9 million returns claiming deductions for sales taxes and 800,000 returns claiming deductions for personal property taxes would prefer to endure the administrative burden and spare themselves the increased taxes.

Finally, our associations are opposed to the administration's proposal to tax interest earned on premium payments for deferred annuities as that interest accrues during the accumulation period prior to the annuity starting date. We believe this proposed change would discourage persons from saving for their retirement. Indeed, not only do we think that current tax treatment of deferred annuities should remain unchanged, but we also believe that interest on long term savings bank and savings and loan association certificates (that are specifically designated as sources of retirement income) should be treated the same way. Incentives (in addition to those available under current law) that encourage persons to accumulate assets to provide themselves with additional sources of income during their later years are needed to reverse the trend among the elderly toward increasing income dependency on public programs and to offset any antisaving bias that long-term high rate inflation may cause.

The final item on which our associations wish to comment specifically is the administration's proposal to substitute a $240 credit per exemption for the present deduction of $750 per exemption and the general tax credit. Our associations would modify this proposal to give the taxpayer a choice between the combination of the deduction for personal exemptions and the general tax credit and the proposed new $240 credit per exemption. We agree that credits are more in accord with ability-to-pay principles than deductions in that they grant equal tax relief at all levels of income (whereas the value in terms of tax savings for exclusions from gross income and deductions depends upon the marginal rate of tax which would otherwise apply to the income that is excluded or deducted), but the administration's proposal will help lower income taxpayers at the expense of higher income taxpayers. Since (middle) and higher income workers are being penalized more heavily by scheduled payroll tax increases and since all taxpayers are being penalized by the combination of inflation-induced income increases and the progressive rate schedule, we see no reason to penalize higher income taxpayers even further in the name of tax reform at this time.

III. ADDITIONAL ITEMS NOT INCLUDED IN THE ADMINISTRATION'S TAX CUT PACKAGE

There are certain issues which the administration's package fails to address but which are of importance to the elderly. We hope that the legislation will address these issues by the time it reaches the end of the legislative process.

A. Tax credit for the elderly

Under the 1976 Tax Reform Act, Congress attempted to update and restructure the old retirement income credit. This credit was originally enacted in 1954 to provide non-social security retirees with roughly the same tax relief provided social security recipients. Although the original credit did achieve this objective, the non-social security retiree, with the passage of years, began falling behind his social security counterpart as a result of periodic increases in tax-free social security benefits. In addition, many elderly taxpayers found the credit extremely difficult to compute and some were not even aware it existed.

Finally in 1976, Congress tried to simplify the credit and increased the maximum amounts used in computing it from $1,524 to $2,500 in the case of individuals and from $2,284 to $3,750 in the case of couples. Unfortunately, the new provisions also introduced a phaseout of the credit in the case of taxpayers age 65 and older who have adjusted gross income in excess of $7,500 ($10,000 in the case of married couples.) This new AGI phaseout feature has the effect of denying many retirees all or a substantial portion of the tax credit they used to receive under the old retirement income credit.

Furthermore, the AGI phaseout penalizes taxpayers when they reach age 65 (and when their income tend to be greater) compared to retirees under age 65 who are not subject to the same phaseout when computing their credit. Because these changes in the credit were enacted in October 1976, but were effective beginning January 1976, the taxpayers adversely affected by the changeover to the new law experienced retroactive tax increases. An amendment attached to the 1977 Tax Reduction and Simplification Act by Senator Church temporarily corrected this problem by permitting these taxpayers to file amended returns using the provisions of the old retirement income credit.

Our associations are still dissatisfied with the maximum amounts used to compute the credit. These amounts should be increased to at least $3,000 and $4,500 for single persons and married couples, respectively. These amounts would be more in accord with average social security benefit levels. In addition, the amounts as so increased should be automatically cost-indexed to eliminate the need for constant updating. The $7,500 AGI feature should be eliminated from the law or at least increased so that it meshes more closely with the phaseout feature of the sick pay exclusion (taking into account our recommendations on this item herein below).

Our associations support legislation introduced by Senator Daniel Inouye (S. 2128), which would increase the maximum amounts to $3,000 for individuals and $4,500 for couples, cost-indexing the base amounts and eliminate the AGI phaseout feature. An identical bill sponsored by Representative Bafalis (H.R. 8818) is pending in the House and has a large number of cosponsors. Pending reform of the tax credit for the elderly and, in anticipation of extended debate on the issue, our associations would urge Congress to renew the "Church amendment" so that taxpayers hurt by the 1976 changeover to the new credit will continue to receive some measure of tax relief.

B. Sick pay exclusion

The 1976 Tax Reform Act revised the rules governing the use of sick pay exclusion. These changes had the effect of restricting the exclusion's availability to persons retired on disability. Now the $5,200 maximum exclusion is available only to persons under age 65 who are permanently and totally disabled; moreover the amount otherwise excludable must be reduced dollar-for-dollar for all adjusted gross income in excess of $15,000 (in the case of both single persons and married couples).

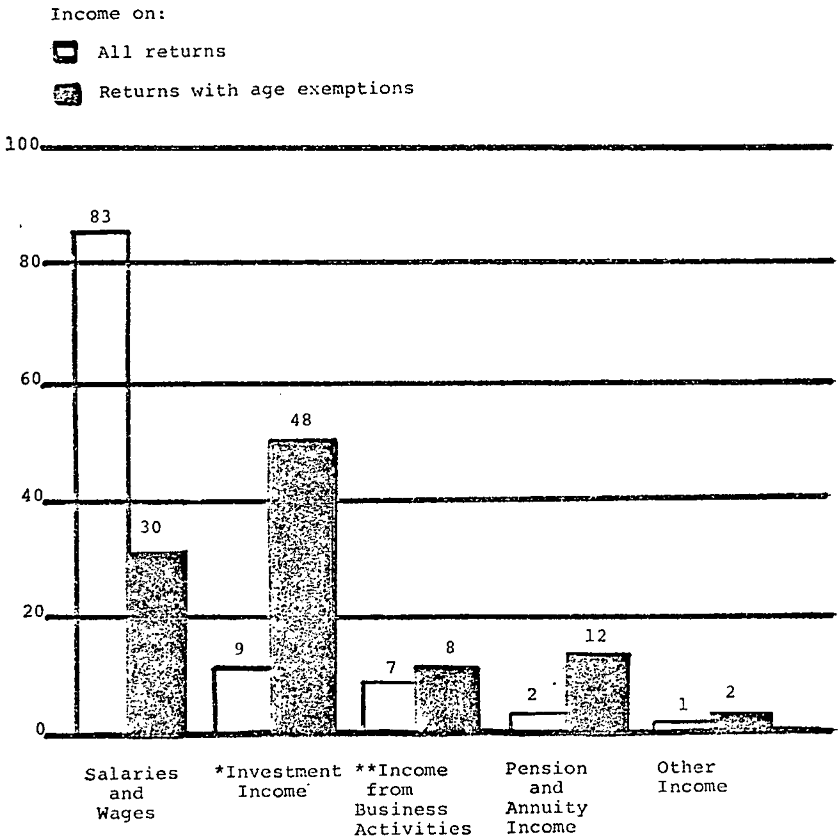
Although our associations understand what prompted Congress to impose these restrictions, we feel that some of the new provisions result in overly harsh tax treatment of certain disabled persons. We suggest the following liberalizations. First, if the current $15,000 trigger figure for the income phaseout feature is retained for single persons, it ought to be increased to at least $20,000 in the case of married couples filing jointly. Second, the reduction of the $5,200 maximum exclusion on a dollar-for-dollar basis should be liberalized to a $1 for $2 reduction.

IV. TAX PREPARATION PROBLEMS OF THE ELDERLY

As you are aware, for over 9 years our associations have been providing free, counseling assistance to older adults in preparing their tax returns through sponsorship of the NRTA/AARP tax-aide program. Our extensive experience with this program provides us with a special insight into this subject.

When a taxpayer reaches the age of 65 or retires, he is suddenly confronted with an entirely new set of Federal income tax provisions which make reporting his income and computing his tax liability an extremely difficult and frustrating task. The increased difficulty which the retired taxpayer has in filing a return is caused by a dramatic change in the source of his income. As illustrated in the following chart, IRS data on the elderly's sources of income indicate that, in 1973, salary and wages—the easiest type of income to report—constituted only 30 percent of the elderly's total adjusted gross income (AGI), as compared to 83 percent of the total AGI for taxpayers under age 65. Other forms of income, from investments, business activities, pensions and annuities, become dominant when the taxpayer reaches age 65. The provisions governing these forms of income are some of the most complex contained in the tax code, and require use of multiple supporting schedules in addition to the 1040 (long) form. Statistics for 1973 indicate that only 5 percent of elderly taxpayers could use the 1040a short form, while 27 percent of all taxpayers were able to use it.

PERCENTAGE DISTRIBUTION OF ADJUSTED GROSS INCOME: ALL RETURNS AND RETURNS WITH AGE EXEMPTIONS



* Includes dividends, interest, and net income from sales of capital assets, rents and royalties.

** Includes net income from a business, profession, farm, partnership, and small business corporation

(Reproduced from Department of Treasury, 1973 Statistics of Income, Page. 121)

The long form must also be used in order for the elderly to benefit from special tax preferences, such as the tax credit for the elderly, and sick pay exclusion. The tax credit for the elderly (formerly the retirement income credit) is an excellent example of a special tax provision specifically designed by Congress to provide tax equity for certain retired persons. Yet, any benefit from the credit depends on the taxpayer's knowledge of it and ability to calculate it. In 1974, IRS Commissioner Donald Alexander offered the following statistic: "Almost four out of ten taxpayers eligible for the credit either don't claim the credit or make errors in computing the amount allowed."[1]

Congress recognized the severe burdens placed on large numbers of elderly persons by the format and rules of the old credit and consequently attempted to simplify them under the 1976 Tax Reform Act. Many complicated calcula-

[1] Hearings before the Senate Appropriations Subcommittee on the Department of Treasury concerning taxpayer assistance and compliance programs, April 1974, page 689.

tions were eliminated (which allows the use of a more simplified schedule R), however, complexities in the credit still exist. Furthermore, it has been estimated that the 1976 liberalization of the credit increased the number of returns claiming it from 400,000 to 2.4 million.[2]

In 1977, due to Senator Church's efforts and those of other members of the Aging Committee, Congress corrected the retroactive tax increases it had imposed by the 1976 revision of the tax credit and sick pay exclusion. This action required thousands of elderly taxpayers to file amended returns so that they could recoup the extra taxes they had been forced to pay.

Filing and making payments of estimated tax is another requirement that can be particularly burdensome to retirees. Upon reaching retirement age, the taxpayer—who is previously accustomed to having his tax withheld by his employer—now receives income in the form of pensions, interest, dividends, etc., not subject to withholding. Many retired taxpayers must file a declaration of expected AGI and estimated their tax for the year. Quarterly declaration vouchers must be submitted along with tax payments. If the taxpayer fails to comply with these estimated tax requirements, IRS may impose interest and penalty charges. Older persons in the first few years of retirement experience the most difficulty with these requirements since the rules are new to them.

Expenditures for health care represent a substantial portion of an older person's budget. Therefore, they are frequent users of the medical expenses deduction (27 percent of elderly returns claimed the medical deduction in 1974). Computation of this deduction is very complicated, often involving five separate calculations to arrive at the net amount of medical expenses to be deducted.

A. Recommendations for form improvements

In recent years, the IRS has taken several administrative actions with respect to form improvement that have been beneficial to all taxpayers as well as the elderly. First, the standard form 1040 and certain support schedules were improved to take account of special needs and limitations of the aged. For example, additional deductible items, such as hearing aids, dentures, and eyeglasses in the case of the medical expense deduction, are now listed on schedule A to help assure full tax advantage. Form 1040 also allows for a simplified method of reporting income from fully taxable pensions and annuities; consequently, many pension and annuity recipients are not required to file a separate schedule E.

Second, the IRS has continued to publish and distribute informational materials designed to assist elderly taxpayers. These include "Tax Credit for the Elderly," "Tax Benefits for Older Americans," and "Tax Information on Pension and Annuity Income." All of these publications are available free of charge at IRS offices as well as through some local social security offices and are used extensively in taxpayer education programs. We might suggest the further development of pamphlets which provide tax return preparation information using a line-by-line format. This simplified approach would be more useful to the aged taxpayer. I am attaching a copy of an NRTA/AARP publication, entitled "Your Retirement Income Tax Guide" which utilizes this format.

Third, the IRS has continued and expanded its various programs of direct taxpayer assistance. A toll-free telephone service is available to assist taxpayers with specific questions. Taxpayer representative service personnel are also available at local IRS offices. Furthermore, according to a report submitted to Commissioner Alexander to the Senate Aging Committee,[3] the IRS plans to institute computer preparation of form 1040 on a trial basis during 1977. This will permit IRS to provide a complete return preparation service rather than limited self-help presently available to the older taxpayers and other individuals less able to prepare their own returns. Our associations endorse this effort and hope in the future IRS will take on more responsibility for preparing tax returns and computing tax liability for elderly taxpayers.

Fourth, in 1977, IRS—for the first time in its history—tested out the new long 1040 on a pilot group of taxpayers before releasing it for the public's use this year.

The IRS contacted our tax-aide program and arranged for approximately 20 older adults to work out sample tax returns on the new form. This pretesting revealed that certain problems and errors kept reoccurring with use of the

[2] S. Rept. No. 94–938, 94th Congress, 2d session (1976), page 131.
[3] S. Rept. No. 95–98, 95th Congress, 1st session, (1977), page 199.

new form. This prompted the IRS to make two major changes in the final 1040 form. Our associations encourage IRS to continue this practice of trying out new forms on test groups of taxpayers.

In the interim, however, several tax areas which create special problems for elderly taxpayers demand IRS attention. In the area of pensions and annuities, an administrative effort should be made to encourage the development of methods by which payers of pensions and annuities can more readily inform payees of the taxable portion of the gross annual payment. Since the computation of the taxable portion of income from a pension or annuity under IRC section 72 often requires the use of materials such as annuity life-expectancy tables not readily available or understandable to the average retiree, IRS should therefore increase its technical assistance to pension and annuity plans so that these plans may in turn assist the aged taxpayer. An increased number of IRS technical staff personnel and increased budgetary allocation should be devoted specifically to the achievement of this recommendation. The Civil Service Commission, the largest payer of retirement annuities, has undertaken to supply annual statements to annuitants showing the taxable portion of their annuities. Certainly this constitutes significant progress and we hope IRS would encourage and assist other retirement systems in doing the same.

Insuring the availability and use of Form W–4P so that retirees may have income tax automatically withheld from their pensions and annuities should be another IRS objective. This form eliminates the need to file estimated tax forms and make quarterly tax payments on pension and annuity income. IRS should require the distribution of the form to retired annuitants by payers.

Changes made by the 1976 Tax Reform Act and 1977 Reduction and Simplification Act should also be widely publicized by IRS. Efforts to reach the additional elderly taxpayers who can qualify for the revised tax credit for the elderly should be made through the electronic and printed media and through taxpayer assistance programs.

V. THE NEED FOR TAX PREPARATION ASSISTANCE FOR THE ELDERLY

This testimony has covered only a few of the complex tax provisions the elderly are forced to use. It must be remembered, however, that many elderly taxpayers must not only contend with these intricate rules, but must often do so under substantial physical and mental limitations. Impairments, such as declining visual or hearing accuity, decreasing physical mobility and mental alertness, are often part of the process of aging. In the special case of the aged widow taxpayer, all of these problems are aggravated by an additional factor—lack of experience. Not only is she confronted by all of the problems which confront the aged taxpayer in general, but she usually lacks even the advantage of having had experience working with the Federal income tax return prior to becoming a widow since the deceased husband probably prepared the tax return for the family.

Considering all of these problems combined with a maze of forms and calculations, it is no wonder that some informed individuals have concluded that the older taxpayer tends to overpay his taxes. In 1970, the Senate Aging Committee undertook an extensive investigation of this situation and concluded that the elderly often over-report their income and do not claim special tax benefits intended for them.

A 1971 IRS survey of taxpayer experience with the standard form 1040, revealed that approximately 80 percent of aged taxpayers sought outside assistance in preparing their Federal tax returns—a substantially greater percentage than in the case of the nonaged. While certainly this 80 percent includes many who were assisted without charge by friends and relatives, it must include many who had to purchase their assistance. This type of commercial assistance can be a financial burden to lower-income elderly persons since it is likely to be expensive due to its complexity.

A. The VITA/tax-aide programs

The alternative to expensive commercial assistance is free tax counseling offered by the IRS and cooperating organizations through the volunteer income tax assistance (VITA) program. Our associations' tax-aide program is the only nationwide program working with IRS in assisting older persons and contains two-thirds of the total number of elderly volunteer counselors participating in VITA. During 1977, 6,300 volunteer counselors were trained under our program and approximately 475,000 tax returns were assisted.

Based on our experience with this program, we are convinced that this volunteer approach is the most effective and efficient method for counseling older adults. Tax-aide services are free to the taxpayer and available at local sites which are easily accessible to the elderly. Furthermore, since the program is run almost entirely by volunteers, the costs to IRS are low relative to the costs of other types of taxpayer services. It is our informal understanding that it costs approximately 67¢ to 85¢ to handle one telephone call to an IRS service center (depending on the complexity of the telephone equipment and number of personnel). In comparison, tax-aide's cost in 1975 was 43¢ per return assisted and was reduced to 36¢ per return in 1977. We expect this cost per return to continue dropping as our volunteer counselors become more experienced with their work and tax aide receives more widespread publicity.

When seeking advice at a local IRS district office (usually located in downtown, heavily developed areas), the older taxpayer must compete against other taxpayers and is often required to stand in line for hours after traveling a long distance to get assistance. The pace at tax-aide sites is much slower and volunteers generally have more time and patience to provide thorough assistance. In contrast, to tax-aide counselors, IRS taxpayer service representatives are oriented toward responding to specific questions rather than providing comprehensive assistance in preparing the taxpayer's entire return, making sure taxpayers take advantage of their full legal tax benefits.

Another factor contributing to tax-aide's success and effectiveness as a part of the VITA is its centralized administration. For the 1977 tax year, our national tax-aide coordinator directed 110 overall coordinators (who operate on a statewide or county basis) and 915 local coordinators who were responsible for utilizing our 6,300 volunteer counselors.

This organization or "chain of command" has proved to be the key to our effectiveness. Once IRS trains volunteers to provide assistance, followup organizational structure must exist to ensure that tax assistance sites are set up, publicized, and the trained volunteers are scheduled to provide counseling. To the best of our ability, we have encouraged our counselors to volunteer a minimum of three hours per week during the Federal filing season. We also attempt to ensure that older taxpayers use the program to its capacity by stressing the need for conducting advertising campaigns at the local level.

This high level of coordination and centralized administration proves its value when one examines the average number of returns assisted by each of our volunteers. In 1976 volunteers in the entire VITA elderly program assisted with an average of 18 Federal returns, while our tax-aide volunteers assisted with an average of 35 Federal returns. During 1977, tax-aide counselors improved and assisted with an average of 42 Federal returns, far above the national IRS average.

B. Problems with the current VITA program

Despite the rapid growth of our program and its improved effectiveness and efficiency, our potential has been continually hampered by insufficient funding. Our associations would like to see a larger portion of the total taxpayer education funds allocated to elderly VITA programs so that they can be expanded and improved. We note that the IRS plans to increase fiscal year 1979 funding for elderly VITA assistance by only $4,000 (or 2 percent) over what was budgeted for fiscal year 1978. In addition, IRS should devote increased effort and resources to its taxpayer education program in the context of its provision of taxpayer services.

IRS personnel have certainly been as supportive of our program as possible, but it has been handicapped by serious lack of funds. For instance, during 1976, we repeatedly faced the situation where no funds were available at the district level to teach VITA courses. Recognizing the IRS's budgetary limitations in many regions, we piloted a program of volunteer instruction where carefully selected volunteers would participate in district instruction training workshops. In this manner our own volunteers took responsibility for training other volunteers in tax counseling. This method of operation allowed us to provide instruction and counseling in many areas of the country where IRS training assistance was unavailable or extremely limited.

Related to the problem of insufficient funding, VITA has experienced administrative problems in overseeing volunteers and ensuring they are fully utilized. At the district office level, the taxpayer education coordinator (TPEC) is responsible for setting up VITA programs in that area. All too often this coordinator has other responsibilities of a higher priority and cannot allocate the necessary time to VITA pojects. The coordinator can usually only devote a part of his time to VITA and is likely to be transferred to another assignment within the district office after one year. This lack of priority and constant turnover do not promote the stability and administrative oversight needed to effectively coordinate a volunteer program. A national organization such as ours, in cooperation with IRS, seems better equipped to provide the effective administration, followup, and oversight that the program's local operation needs.

Due to the efforts of Senator Frank Church and several other Senators, an additional $300,000 (or 60 percent increase in funds over last year's budget) was secured for VITA's fiscal year 1978 operations. Already, this additional funding is permitting VITA to overcome some of the administrative problems and limitations it has faced in the past years, but there is still a need to increase the program's priority within IRS.

C. Older Americans Tax Counseling Assistance Act

Legislation (S. 835) that would overcome both the administrative and funding problems faced by the VITA/tax-aide program has been introduced in this Congress by Senator Frank Church. This bill would build upon the VITA program by authorizing IRS to enter into training and technical assistance agreements with nonprofit agencies to prepare volunteer counselors. The measure would also permit these counselors to be reimbursed for their out-of-pocket expenses incurred in providing assistance.

Our associations strongly endorse this bill because we believe it will permit IRS to place the emphasis on elderly taxpayer problems which is necessary and long overdue. Despite the many budgetary and administrative constraints of the past, VITA/tax-aide has managed to expand remarkably in the past several years—training more and more volunteer counselors each year who are able to assist increasing numbers of elderly taxpayers. Since 1973, our tax-aide program has experienced a 244-percent increase in the total number of tax returns assisted (from 138,000 returns in 1973 to 475,000 returns in 1977) and a 117-percent increase in the number of volunteer counselors trained (from 2,900 counselors in 1973 to 6,300 in 1976). This extremely rapid growth in our program is evidence that elderly taxpayers do have a significant need for tax return preparation assistance and that there is a high demand for this type of special assistance which accommodates the aged's particular needs.

Demographic trends indicate that the size of the target population for this program will substantially increase throughout this century from 23 million today to 31 million by the year 2,000. And, as Congress continues to move toward providing improved tax equity and special benefits for the elderly, the number and complexity of the tax rules and provisions they must use will grow as well.

Mr. Affeldt. We shall now hear from Arthur Stanat.

STATEMENT OF ARTHUR STANAT, WASHINGTON, D.C., TAX-AIDE COUNSELOR, NATIONAL RETIRED TEACHERS ASSOCIATION/AMERICAN ASSOCIATION OF RETIRED PERSONS

Mr. Stanat. My name is Arthur Stanat. I have been with the NRTA/AARP tax-aide program for 4 years and have been trained by the IRS during those years. In fact, I have had about 100 hours of instruction. I am not a tax expert, and do not hold myself as being so. Nevertheless, when I go to assist people, they immediately categorize me as an IRS person and I have to explain this.

I have prepared some comments which I would like to submit for the record. I shall make additional comments on them.

Mr. Affeldt. Your statement will be incorporated in the record.[1]

Mr. Stanat. As I listened this morning, certain thoughts came to mind relative to my own experience. I think we should be cognizant of the persons we are trying to serve; namely, the elderly. The tax instructions in the IRS forms may be quite clear to a tax expert and

[1] See p. 41.

to a person who studies their publication and understands them, but I would like to describe the comprehension problems that elderly persons often have with these publications.

One of my services to the community was to assist high school students in mathematics for a short while. One morning a high school sophomore came to me with her problems with algebra. I said: "Well, what are your problems?" She said: "I dont' understand one of the assigned problems." She opened the book and showed me a problem about a rectangle. The problem was to define the width, length, and area where given. I said: "What is so hard about that?" "Well," she said, "I don't know what a rectangle is."

This is part of the problem that older people have with IRS publications. They don't understand some of the words; they don't understand some of the phrases; they don't understand some of the sentences. Consequently, they need the kind of assistance we are giving. They need somebody alongside them to explain and answer their questions and help them understand what is required or described.

Even if the IRS continued to improve its publications and forms, it would never achieve the level that is necessary for some old people to understand. So, I think it is a futile avenue for improvement.

I think what we need are neighborhood helpers for older persons, and I don't think there is any other recourse, because they won't read and they won't study. They do not have the attitude that they must make themselves tax experts to fill out their tax forms. They do this once a year, and they don't spend any time getting prepared for it.

It is very easy to do something if you repeat it every day but these people don't repeat tax forms every day and they have problems in January, February, and March. They just don't understand.

TAX-AIDE COUNSELORS RENDER ESSENTIAL SERVICES

I think tax-aide counselors like myself do render a very essential service to older people near their homes, where they don't have to get on a bus, spend all day at the IRS, and fight the crowds on the way home. I would also add that they can't even get service over the telephone during the critical period of the year. I have tried it myself. You try all day, and all you get is a busy signal. Regardless of the phones the IRS has, and the trained people it has to answer the phones, you just can't get through.

Getting on a bus and coming down to the IRS office often requires that you get there before it opens; otherwise there are 100 people ahead of you, and you spend all day sitting in a chair waiting. Older people just can't put up with that.

I think for that reason the neighborhood service that a program affords is essential for the limited type of taxpayer that we are talking about. I am sure, as I stated in my prepared statement, that every taxpayer I have assisted was thoroughly appreciative of the service we rendered. I think we can continue to help them out.

That is all I have to say.

Mr. AFFELDT. Thank you very much, Mr. Stanat. I am sure you do a very effective job in assisting older people with their taxes.

Mr. STANAT. Thank you.

[The prepared statement of Mr. Stanat follows:]

Prepared Statement of Arthur Stanat

Senator Church, fellow Senators, and members of the committee, it is a privilege to appear before your committee in behalf of the older citizens of this country who have earned their stripes. I am Arthur Stanat, currently a counselor with NRTA/AARP tax-aide program and assigned to the Guy Mason Recreation Center of this city. I have assisted the tax-aide program for 4 years. In prior years, I have worked at the U.S. Soldiers and Airmens Home in Northeast Washington, Cleveland Park Library, and the Presbyterian Center in Northwest Washington.

NRTA/AARP TAX-AIDE PROGRAM

The tax-aide program is a volunteer counseling program that is conducted by older citizens for senior taxpayers. I was trained along with 45 other tax-aide volunteers through the Internal Revenue Service volunteer income tax assistance program. Currently, we are working at various libraries and other public facilities within the District. There are currently 17 regularly scheduled counseling locations. My site is under the supervision of a volunteer coordinator, Mr. Burt Werner. Mr. Werner is responsible for the administration of five specific locations. He, along with three other local coordinators work in conjunction with the overall coordinator for the District, Miss Margaret Packer, and with the national tax-aide office. This "chain of command" has proven to be effective and reflects the program's success. In the 4 years that I have served, the program has improved its administrative procedures, as well as in its outreach. For example, in 1973, 25 counselors helped persons in filing 895 returns. This past year, 48 counselors assisted in the filing of 2,268 returns. (It is too early to project the final results for this current season, as our busiest time of assistance is in the final 6 weeks of the Federal filing season.) In addition to providing assistance with Federal returns, I was trained by the District of Columbia Revenue Office to assist individuals in filing District returns, as well as assisting low-income older adults in claiming the special property tax rebate benefit allowed this year by the District of Columbia.

In addition to better organization, the reason for the program's growth has been the improved training that we have received from the IRS and better publicity in the local media. Each year the training class provided is more comprehensive and helpful. The IRS instructors are better prepared, and more knowledgeable of the senior taxpayers' problems each year. It has helped me and the other counselors provide more capable assistance to the persons we serve. This is critical, for there are many complex problems that older taxpayers face. In addition, due to their own circumstances, many of them are ill-equipped to deal with the tax laws. For example, 2 years ago a man's wife died; she had always prepared the family tax return, and he was at a loss to file his own return that year. As a tax-aide, I was able to assist him that year and the next year when his filing status was again different. He called me on the telephone this week and asked when I could help him this year again.

As a tax-aide counselor serving the U.S. Soldier's and Airmen's Home, I found that many men did not realize the benefits available to them, and if they were aware of them, were often unable to properly claim them, due to the changes in the tax law. This is particularly true in regard to the credit for the elderly. Many of the men there did not know that they could benefit from it, and a great deal of my time was given to the correct filing of schedules R and RP. The men also did not realize that they could claim the credit for past years by filing an amended return. I was able to help them obtain refunds for previous years when possible.

The Tax Reform Act of 1976 changed the status of individuals qualifying for disability payments. This has never been an easy area for an individual to properly claim his benefits, due to the changing natures of the laws affecting disability benefits. I helped them apply the law to their own situation, and where possible, obtained the current benefits.

As I served there, I discovered that certain residents in the home would assist other residents with their tax returns for a fee, usually $5 or so, whereas our volunteer program provides it free. Knowing the incomes that these men and other senior citizens have, I realize that they are hard-pressed to pay for preparing their returns. Most of the older taxpayers we assist must survive on limited incomes and cannot afford to pay a professional preparer to correctly file the necessary tax return. Through our work, we can help them save precious dollars.

I understand that one of the long established income tax services in this city charges a minimum of $13 for the simplest return. Additional charges are made for filing additional schedules such as A, B, R, and RP, and when other problems are involved.

Tax-aide program is a peer counseling program. Just as many of the older taxpayers that we assist have to deal with a limited income, we as counselors do also. After 2 years of serving in the home, I asked to be transferred to a site that was closer to my own home. The expense and hazards of driving across the city in adverse weather and road conditions was more than I wanted to bear on my own as a counselor. I am pleased that you, Mr. Chairman, have introduced a bill, S. 835, that will allow for the reimbursement of volunteer counselors in providing peer group tax assistance. Such funding will help to further our program's outreach to those in need.

In conclusion, Mr. Chairman, I appreciate the opportunity to speak to you about the needs of older taxpayers. It is a source of satisfaction to me that I can help to meet these needs through my volunteer work as a counselor in the tax-aide program. This committee's hearings on the older taxpayers' situation should highlight the need to expand present programs and reinforce our efforts to secure passage of S. 835. I am confident that every taxpayer that we have assisted was thoroughly appreciative of the service we rendered. It no doubt helped alleviate the feeling that he was a forgotten citizen and once again could reflect on the thought that the U.S. Government was concerned with his welfare.

Mr. AFFELDT. Now we shall hear from the National Association of Retired Federal Employees. Stephen Skardon, who is a legislative assistant, will testify. He will be accompanied by Judy Park who is also a legislative assistant.

STATEMENT OF STEPHEN SKARDON, WASHINGTON, D.C., LEGISLATIVE ASSISTANT, NATIONAL ASSOCIATION OF RETIRED FEDERAL EMPLOYEES, ACCOMPANIED BY JUDY PARK, LEGISLATIVE ASSISTANT

Mr. SKARDON. Our president, John McClelland, asked us to send his regrets and asked that his statement be inserted into the record. He is out of town today and wanted very much to be here.

Mr. AFFELDT. The statement of Mr. McClelland will be entered into the record.[1]

Mr. SKARDON. In summary, Mr. McClelland's statement touches on two major legislative goals of our organization. The first is the 1976 tax credit for the elderly which has been discussed to some extent today, the other is the recent changes in the sick pay exclusion. We have some specific recommendations on both. All of that is included in the statement, so I will very briefly run over some of the highlights.

TAX CREDIT FOR ELDERLY

The purpose of the tax credit for the elderly, as was its predecessor, is to provide some form of tax relief to elderly persons with little or no social security income on the level roughly comparable to that received by persons with substantial social security income. The problem, of course, is that social security income is tax exempt.

The reason for this very lucrative tax break is that the Federal Government considers the ability of elderly taxpayers to meet basic financial needs of such social significance as to warrant this special tax consideration. We agree with this and we have no problem with it.

[1] See p. 45.

as far as it goes. However, we believe very strongly that the ability of elderly persons not substantially covered by social security to meet these same financial needs is of no less social significance.

It is our belief that tax treatment of elderly persons should apply equally, across the board. Just because a person is entitled to social security income does not make him any less elderly or any more capable or meeting the financial demands of old age. It is our position that every elderly American should be entitled to either a tax exemption under social security or a tax credit under an amended tax credit for the elderly.

As noted in President McClelland's statement, the current highly restrictive nature of the provisions of the tax credit have rendered it inadequate and prevented it from even coming close to achieving its original purpose.

The "Means Test"

Our major objection to the current law is the "means test" or phaseout provisions which require a phaseout of the taxpayer's credit for every dollar of adjusted gross income above $7,500 for single persons, and in case of married taxpayers, $10,000. Our association finds this particularly inequitable in light of the fact that social security income is tax free at all income levels. It is ludicrous to think that under current law, former Vice President Nelson Rockefeller would receive full tax-free social security benefits while a 70-year-old public pensioner is considered too affluent for the tax credit with an income of $12,500.

Our association believes very strongly that the Inouye proposal speaks specifically to this problem and goes a long way in correcting this inequity. Specifically the Inouye bill would raise the amount of the maximum credit from $375 to $450, it would also insure.that that amount would increase annually with the cost of living as do social security payments and, third, it would eliminate the phaseout all together.

Presently, the Inouye bill has seven cosponsors, including two members of this committee, and on the House side we have 119 cosponsors, 11 of whom are members of the House Ways and Means Committee.

On behalf of our association I would like to ask this committee to join us in a vigorous effort to secure passage of this bill. We feel it is particularly important to the financial livelihood of the people that we represent and we hope that the Senators on this committee can make a sustained effort as has happened on the House side.

Medical Deductions

I would like to simply add on the related question of medical deductions, which has been mentioned briefly here, that we do oppose the President's proposals in this area specifically in terms of the administration's concept of tax simplification. Mr. Hacking pointed out that every time the administration talks about tax simplification it inevitably results in greater taxes for the taxpayer and increased revenue for the Treasury Department.

In the case of medical deductions, this seems to be the case. I am still not sure what they mean by this statement in the analysis of the President's program. I would like to——

Mr. AFFELDT. You are reading from what page?

Mr. SKARDON. Page 47. They are talking about the impact that the President's proposals on medical deductions would have on the taxpayers. I think that I would just like to read directly from it.

Adoption of the new hardship deduction will reduce by 11.1 million or 83 percent the number of taxpayers who itemize their medical expenses and nonbusiness casualty and theft losses under the current laws.

Skipping to page 49:

Over 35 percent of amounts currently deductible on account of medical expenses and casualty and theft losses will continue to be deductible by these individuals. All other taxpayers will be spared the administrative burden involved in claiming and substantiating the medical, and casualty and theft loss, deductions.

Most significantly, these changes will cause 2.3 million taxpayers to switch to the standard deduction. For these taxpayers the burden or compliance will be vastly reduced since they will be relieved of the numerous difficulties encountered in itemizing deductions.

That might be simpler but I can assure you I speak for those 2.3 million people who would much rather fill out a form than be "relieved" of a substantial tax savings.

I was a bit alarmed after I saw this. I got a letter from IRS asking if we had any suggestions for simplification of schedule R and schedule RP. I don't know if they are trying to tell us something about future tax proposals, but I hesitate to complain about the complexity of any forms now.

TAX CREDIT FOR ELDERLY

As a final note, I would just like to respond a little bit to what Mr. Sunley said about the tax credit to the elderly. As you know, the main problem that has precipitated the Inouye proposal is the fact that social security is tax free and that there are lots of elderly people who are not on social security and not receiving a comparable tax break. That is the question, that is the problem.

Mr. Sunley didn't even deal with that for some reason. Frankly, I was surprised, because the administration had been very concerned about this in the past, and made a determined effort to come up with some kind of corrective legislation.

It is interesting at the beginning of his statement, Mr. Sunley said how wonderful the President's tax program would be for elderly people. He pointed out, I think, that some $925 million in tax relief would go to elderly people and how terrific this was; and yet on page 7 he dismisses the tax credit for the elderly by saying the elderly already have too many tax benefits and, therefore, it is unreasonable to go ahead and try to consider anything further. That seems rather peculiar logic to me.

I was interested also in the cost figures for S. 2128, which in previous months he has been unable to come up with. These cost figures differ significantly from the figures that have been furnished us by the Joint Committee on Taxation. I would be very interested in seeing the anlysis and how they came up with this proposal. I also would point out that we do have the joint committee's analysis and would be glad to furnish them for the record.

Mr. AFFELDT. We would appreciate it if you would furnish the Joint Committee on Taxation analysis in reaching that $578 million figure.

Mr. SKARDON. Fine, no problem.

Finally I simply would like to say that Mr. Sunley's statement on the equity problems involved with the Inouye proposal totally escapes me. As I said before, the administration willingly admits there is a problem here. When you have two retired individuals both earning $15,000, both living in the same situation, yet one has $5,000 in social security income, you find that there is a difference of $1,400 in the taxes that the two are paying. We feel it is simply not right that people similarly situated have to pay different tax bills and such a substantial difference.

For that reason we feel strongly that some action has to be taken by this conference on this equity question.

We have commitments from nearly half of the Members of the House to support some form of the Inouye bill. As I said, there are 109 cosponsors of H.R. 8818 on the House side, 11 of whom are on the Ways and Means Committee. That indicates there is substantial interest in Congress that something be done and I am very disappointed that the administration has not tried to come up with some alternative proposal that would enable us to at least begin to deal with the problem.

Mr. AFFELDT. Thank you very much for your presentation. The statement of Mr. McClelland will be entered into the record now.

[The statement of John F. McClelland follows:]

PREPARED STATEMENT OF JOHN F. MCCLELLAND

Mr. Chairman, I am John F. McClelland, president of the National Association of Retired Federal Employees (NARFE). The association is 57 years old and composed entirely of retired Federal employees, their spouses and survivors. We have a dues-paying membership of nearly 300,000, representing the interests of 1.5 million retired Federal workers, their spouses and survivors.

Mr. Chairman, we very much appreciate the efforts of this committee to raise various issues of tax reform as they affect the Nation's elderly, particularly since Congress plans to pass major tax reform legislation this year. Since our organization has been deeply involved in the development of some of these issues, we welcome the opportunity to comment publicly.

Let me say initially that our organization does not argue that Federal tax policy is not reasonable in its treatment of the elderly relative to the rest of the population. Indeed, the tax code contains numerous helpful tax relief mechanisms for seniors which effectively place them on par with their younger counterparts.

However, it is the position of NARFE that the recent enactment of certain tax laws has created inequities and difficulties for older Americans which we hope will be addressed in the anticipated tax reform bill. Again I stress that our argument before you is one of simple equity and fundamental fairness.

TAX CREDIT FOR THE ELDERLY

As I am sure you are aware, a primary legislative concern of our organization has been the tax treatment of elderly persons with little or no social security income.

Under current law, social security income is tax exempt. The rationale behind this lucrative tax break is that Congress considers the ability of elderly persons to meet basic medical and economic needs of such social significance as to warrant this special consideration. This exemption is not something that is earned nor is it a benefit for which one must otherwise qualify. It is automatic and given to everyone on social security.

We have no problem with this. However, we do feel that the ability of nonrecipients of social security to meet basic medical and economic needs is no less important than that of persons receiving social security. Ever since 1954 Congress has agreed with this concept, and evolved the current tax mechanism known as the tax credit for the elderly (TCE). It is the purpose of the TCE to provide roughly comparable tax treatment to those elderly without substantial social security income. However, it is our position that the TCE, enacted as part of the Tax Reform Act of 1976, is inadequate and fails to even come close to accomplishing its purpose.

CURRENT LAW

Perhaps it would be well to briefly summarize the current law:

Under the TCE, an individual is allowed to subtract 15 percent of a maximum base figure (otherwise known as the "section 37 amount") from taxes owed for a given tax year. However, the maximum base figure is reduced by the amounts and sources of income.

An individual's base figure is determined in the following manner:

a. Individuals 65 and over (IRS schedule R) are allowed to take into account for purposes of computing the maximum base figure up to $2,500 of adjusted gross income ($3,750 for couples filing jointly) to be reduced by:

(1) the amount of social security and/or railroad retirement income the individual has received during the tax year, and

(2) $1 for every $2 in adjusted gross income over $7,500 ($10,000 for couples filing jointly).

b. Public retirees under 65 (IRS schedule RP) are allowed to take into account for purposes of determining the maximum base figure up to $2,500 of retirement income ($3,750 for couples filing joint returns) to be reduced by:

(1) the amount of social security and/or railroad retirement income the individual received during the tax year, and

(2) $1 for every $2 of earnings over $1,200 and below $1,700, and dollar-for-dollar over $1,700.

(3) for persons under 62, dollar-for-dollar for earnings over $900.

In other words, for persons 65 and older only those with adjusted gross incomes under $7,500 and no social security income are eligible for full $375 credit (15 percent of $2,500). Those persons with modest incomes ($7,500–$12,500) receive little or no credit, while those with incomes above $12,500 receive nothing. Of course, the maximum base figure is reduced by any social security income (or railroad retirement income) up to $2,500, at which point the individual's credit is completely eliminated. ($3,750 for couples filing jointly.)

For persons under 65, there is an earnings test instead of the phaseout rule, although the social security offset still applies.

An important innovation of the TCE is the inclusion of all persons 65 and older among those eligible for the credit. Under the pre-1976 rules, only those receiving public retirement income were eligible. The primary beneficiaries of this policy shift were elderly persons whose social security income was below the $2,500/$3,750 maximum base figure, and whose adjusted gross income fell below the $7,500/$10,000 phaseout level.

CURRENT LEGISLATIVE PROPOSALS

In the first session of this Congress Senator Inouye of Hawaii introduced S. 2128 which is designed to upgrade the TCE and narrow the gap between those receiving social security and those with little or no social security income. This bill has the full support of our organization along with that of many other groups.

The Inouye bill is premised on three main points:

(1) The maximum base figure ("section 37 amount") used in computing the TCE be raised to $3,000 for individuals and $4,500 for couples filing jointly.

(2) The maximum base figure be cost-indexed to reflect changes in the cost of living each year, and

(3) The phaseout figures on the adjusted gross income of persons 65 and older be eliminated (schedule R only).

Currently, there are seven Senate cosponsors on this legislation, including Senator Domenici and Senator Chiles of this committee. On the House side there are 108 cosponsors of an identical bill (H.R. 8818) including 11 Members of the Committee on Ways and Means and House Aging Committee Chairman, Claude Pepper of Florida. The Inouye proposal, if enacted, will rectify the major deficiencies of the current law:

First, it would increase the amount of maximum credit available to qualified persons from $375 to $450. This is a result of increasing the maximum base amounts. Historically this amount has been arbitrarily fixed at a level roughly equivalent to the average annual primary social security benefit.

Second, the Inouye bill would insure that the maximum credit amount will be increased each year to keep pace with the cost of living. This has been a major problem in previous years in that Congress' agenda has often squeezed out consideration of relatively insignificant updating legislation.

Third, the Inouye bill insures that all persons 65 and older will be eligible for either the tax exemption under social security or a tax credit under the TCE. Due to the $7,500/$10,000 phaseout figures on adjusted gross income, the TCE excludes all but low-income elderly. Since social security income is tax free at all income levels, our membership feels that TCE should also be available to all other taxpayers who would otherwise qualify. (The attached chart demonstrates the profound inequity created by this double tax structure.)

Fourth, the elimination of the phaseout rule would remove what is, in essence, a penalty against savings and investment income, and active employment earnings by persons 65 and older. Since the phaseout rule is based on an individual adjusted gross income, limiting income from these other sources often pushes an otherwise qualified taxpayer above the phaseout level causing him to lose all or part of his credit.

Currently, the TCE results in a revenue loss of $303 million each year. Official estimates of the additional loss effected by enactment of the Inouye proposal range from $300 million to $578 million.

TAX TREATMENT OF DISABILITY ("SICK PAY") INCOME

Mr. Chairman, Congress has a long-standing policy of granting special tax treatment to a portion of an individual's income received as a result of sickness or disability. Qualifying individuals are allowed to exclude up to $100 a week in income received as a result of sickness or disability. The maximum exclusion is $5,200.

While the $100-a-week exclusion was continued, the Tax Reform Act of 1976 severely restricted eligibility for the exclusion. Specifically, the new law requires that persons seeking to qualify for the exclusion must (1) be "permanently and totally" disabled, (2) submit a doctor's certificate to that effect each year, and (3) file a joint return if married. In addition, Congress imposed a dollar-for-dollar phaseout of the exclusion at $15,000, while lowering the maximum allowable age for eligibility from 70 to 65.

PROBLEMS

Obviously, as a result of the new eligibility restrictions, many persons who had been using the exclusion suddenly found themselves with enormous increases in their tax bills. This prompted criticism of nearly every aspect of the new law.

(1) The focus of much of the public dissatisfaction with the new law was that it affected persons who were already retired on disability. These people had gone on disability with the expectation that "the rules of the game" would not be changed on them, and became embittered at the prospect of a substantial change in their tax liability.

(2) While requiring eligible taxpayers to be "permanently and totally" disabled, the Tax Reform Act of 1976 failed to define the term—particularly as it relates to "substantial gainful employment." To date, IRS has refused to issue any guidelines on the subject, preferring instead to wait for a court challenge. This has caused endless complications for many disabled persons who simply do not know if they qualify.

(3) Critics have also argued that the requirement of an annual doctor's statement certifying "permanent and total" disability is a needless hardship.

(4) Criticism of the new law has also centered on the requirement that married persons can only file for the exclusion on a joint return. Since the exclusion phases out when the couple's adjusted gross income reaches $15,000, this has caused a significant hardship. (This same phaseout is also used for a single taxpayer.) Disability income seldom is enough to meet necessary medical and social needs and, thus, often forces the employable spouse to go to work. In many cases, it is the additional income generated by the spouse that pushes the couple's adjusted gross income above the $15,000 phaseout figure. Mr. Chairman, at the very least, I would suggest on this question that Congress establish a second phaseout figure for couples filing jointly, and eliminate the requirement of a joint return.

The major "sick pay" tax legislation in the current session focuses on the following:

H.R. 1826 (Fisher) would "grandfather" all those on the disability rolls prior to enactment of the Tax Reform Act of 1976. Essentially, this would mean that such persons would continue to be governed by the eligibility rules in effect prior to enactment.

H.R. 3927 (Mikulski) and H.R. 9529 (Risenhover) would simply repeal the new sick-pay rules enacted as part of the Tax Reform Act of 1976.

COSTS

According to the Joint Committee on Taxation, the increase in tax receipts obtained by enactment of the 1976 law amounts to $380 million in fiscal 1977; $357 million in 1978; and $450 million by 1981.

Income	Current law			Proposed law	
	Taxes paid by single person [1] with no social security income		Taxes paid by single person [1] whose income includes $5,000 social security	Taxes paid by single person [1] with no social security income	
$5,000	$520	[2] ($375)	0	$445	[2] ($450)
7,500	1,089	(375)	$403	1,014	(450)
10,000	1,896	(188)	895	1,634	(450)
12,500	2,768	0	1,464	2,318	(450)
15,000	3,512	0	2,084	3,062	(450)
17,500	4,332	0	2,768	3,899	(450)
20,000	5,221	0	3,512	4,771	(450)

[1] Person 65 or older/does not include other exemptions or credits.
[2] Amount of credit used in computing taxes owed.

Mr. AFFELDT. Now I would like to call back to the witness table the representatives from NRTA/AARP to pose some questions for both of you.

I will direct my first question to the National Association of Retired Federal Employees. The AARP representatives may also respond.

ALTERNATIVES TO S. 2128 (INOUYE BILL)

If it would not be possible to enact S. 2128 because of administration opposition, would you accept other alternatives to improve the tax credit for the elderly and, if so, what would they be? I realize your association is very strongly committed to S. 2128.

Ms. PARK. Certainly we feel there should be an increase in the computation base; and, second, if phaseouts could not be eliminated totally, we feel they should be substantially increased. I agree with the comment Mr. Hacking made earlier that they should be more in line with the phaseout figures on the sick pay exclusion. It was assumed at one time that the sick pay exclusion would be phased out at age 65 because people would then be able to take advantage of the tax credit for the elderly.

There is no correlation between those two, now.

We feel very strongly about the phaseouts. We think they should be eliminated because of the lack of a "means test" in the tax treatment of social security. We look at that as the point of equity. If they are not eliminated, we definitely feel they should be increased considerably.

Mr. AFFELDT. Mr. Hacking.

Mr. HACKING. I have already said pretty much the same thing—a substantial increase in the base and liberalization and correlation of the phaseout features of the tax for the elderly and the current sick pay exclusion.

Mr. AFFELDT. This is also directed at the National Association of Retired Federal Employees.

Mr. Sunley, in his testimony, indicated that most of the relief in the Inouye proposal would be directed at upper income persons. For example, of the $963 million in tax relief, he said approximately one-half would go to persons with incomes of $15,000 or more and one-fourth would go to taxpayers with incomes of $30,000 or more. How do you respond to that point?

Mr. SKARDON. Not knowing how he arrived——

Mr. AFFELDT. Let's assume for purposes of responding to the question the accuracy of the statement.

Mr. SKARDON. The tax relief mechanism that we are talking about is a tax credit. Credits inherently favor lower income people because of an across-the-board credit means that a person can subtract a greater percentage of his tax liability at the lower end of the income scale rather than at the higher levels.

So while benefits will be distributed evenly throughout all income levels, the persons who will be helped the greatest are the people who are at the lower end of the scale rather than at $20,000 and above.

SIMPLIFYING TAX CREDIT FOR ELDERLY SCHEDULE

Mr. AFFELDT. I know you are a little apprehensive about responding to the administration's request for simplifying the schedule for the tax credit for the elderly. But let's assume that it would not produce something detrimental to the members of your association. Would you have any thoughts about simplifying the schedule R or schedule RP?

Mr. SKARDON. The Inouye proposal would go a long way toward simplifying both schedules. We could condense it to about four steps.

Mr. STANAT. I have a comment about lower income elderly taxpayers and the fact that their credits give them a higher percentage of relief. The comment is that the price of bread and groceries for old people is the same as for higher income younger people. The elderly need that higher percentage of relief based on their income.

Mr. AFFELDT. Mr. Stanat, you assist quite a few elderly tax preparers with their returns. Do you find that some of the new concepts incorporated in the tax forms this year create confusion or doubt among elderly persons or would you say that the tax forms represent an improvement?

Mr. STANAT. Well, it is pretty early in the tax filing season, but my impression is that the tax forms have never been too complicated if one spends enough time trying to understand them. Also, I think there is a limit as what can be done by way of simplifying the forms.

I do believe that older persons don't take the time to study these forms and don't want to study them and the instructions when tax filing season comes along. Consequently, they need some assistance. That's why I think that programs that VITA makes possible ought to be deemed essential and expanded. Our own tax-aide counselors are located at points in neighborhoods where the elderly live so that they don't have to commute and spend all day in town or try to get somebody on the telephone.

Advantages of Volunteer Service

Mr. Affeldt. I gathered that you feel that there are some advantages that a volunteer, nonprofit, private organization would have in delivering this service compared with a governmental agency such as the Internal Revenue Service.

If so, would you care to elaborate?

Mr. Stanat. Well, I think the Government is getting a good return on its investment in VITA. If the IRS had to hire people to go out into the neighborhoods either on a part-time or some other basis it would cost much more. Also, certain types of older persons, like myself, are interested in volunteering their services for purposes needed by the community.

Mr. Affeldt. Mr. McMorran.

Mr. McMorran. We find that it is better not to advertise the fact that the training is provided by the IRS, because people tend to distrust, at times, some of the service that the IRS provides. Consequently, we just claim that we are trained to assist individuals with their tax returns. This approach is more effective.

Mr. Affeldt. It is my understanding that the IRS provides about 2 days of training for counselors who have worked in the program and 3 for new counselors. First, is that correct?

Second, if it is correct, do you think that this is an adequate amount of time devoted for training? If it is not correct, do you think that the time that the IRS does provide for training counselors is sufficient?

Mr. McMorran. The average last year for our tax aid program, which is generally more extensive, was 3 days. There is an experienced training class for capable volunteers of 2 days and a basic training course of 3 days. In some cases, this training goes on for 4 or 5 days. If you add to that training in State taxes, some of our volunteers end up being trained for 6 full days.

Mr. Affeldt. Mrs. Fayé, do you have any questions?

Mrs. Fayé. No.

Funding Level Needed for VITA

Mr. Affeldt. Mr. Hacking, Mr. McMorran may want to assist you on this question. The administration budget request is $800,000 for the volunteer assistance program and it is estimated that $324,000 of this amount will be allocated for elderly tax counseling assistance. This will enable about 12,000 elderly volunteers to be trained. What level of funding do you think is needed by the volunteer income tax assistance program, taking into account budgetary constraints and the overall need for the program?

Mr. Hacking. Let me defer to Mr. McMorran on that.

Mr. McMorran. We presented testimony last summer before the House Ways and Means Committee's Subcommittee on Oversight, to the effect that there was a need for increased appropriations simply because the IRS wanted to do a good job, but didn't have the funding. We were very pleased that Senator Church obtained an additional appropriation last year. That added funding has already had a viable effect. However, there are still some areas that we need to address, like increased outreach, so we seek additional funding. Additional funding would allow us greater training and extended growth for the program.

Mr. Affeldt. The question I have is: What amount is reasonable? The administration is requesting $800,000. Would $1 million be reasonable? How about $1.2 million or $1,250,000? Do you have any idea at this juncture?

Mr. McMorran. It is difficult to give you an exact figure. One of the problems is that the program is not a priority. The national IRS staff has done their best, but they do need increased staff positions. Certainly, $1.2 million or $1.3 million would give it a higher rating in the district office and thus give us a greater priority in terms of IRS staff commitment to the program locally at the grass roots.

Social Security Tax Relief

Mr. Affeldt. Mr. Hacking, if Senator Church were to work for the enactment of a substitute to President Carter's tax proposal, using general revenues to finance all or a part of medicare or perhaps some other approach, do you have any thoughts concerning how this should be targeted? From your statement I gather that you would be very supportive of efforts to ease the payroll tax burden for workers in view of the 1977 social security financing amendments. Do you have any thoughts on this?

Mr. Hacking. Well, first of all my statement indicates quite clearly we are very supportive of efforts to introduce general revenues into the social security program. We have also made it quite clear over the last 3 years that we believe that the manner in which those general revenues are introduced should take account of the economic circumstances that have caused the short-term imbalance in the first place and, in effect, insulate social security from those economic causes.

If this were done, we could deal with economic problems on the one hand without having all kinds of adverse ramifications in terms of the OASDI programs.

Now I am quite aware that there is growing support for the use of general revenues to fund at least a portion of the cost of the hospital insurance program of medicare and to transfer over some of the scheduled increases in the HI portion of the payroll tax to the cash benefit area to offset some of the future increases scheduled under last year's financing legislation.

This proposal is not new. I believe it was first advanced by the Social Security Advisory Council in 1975. That was the same council that first identified the short-term problem, as I recall. Now if it were to appear, after having had a full and fair discussion through the hearing process of the issues and options available, that a proposal to fund part of the cost of medicare out of general revenues would indeed clear the legislative process, but other options, even though preferable on the merits, would not, then our association would support the option that was possible. Certainly that would be better than what we presently have in place.

We are very much afraid that as those scheduled payroll tax increases become effective we are going to encounter a very serious and substantial reaction against the elderly and against the program that served the elderly. Our aim is to avoid a crisis between generations.

We are quite aware, of course, of the demographics. We are simply going to have many more older people in this country. Sole reliance on the payroll tax mechanism to generate all the revenues for the income transfer programs of social security is just not going to work.

At some point we would be confronted with the choice between practically confiscatory levels of taxes on workers or substantial cuts in benefits with a concomitant increase in the incidence of poverty among the elderly.

General Revenues for Medicare or Entire Social Security System

Mrs. Fayé. Are you restricting your use of general revenues to the medicare program or are you suggesting that general revenues be used for the entire social security system?

Mr. Hacking. Let me make that clear. We support introducing general revenue financing to fund a portion of the cost of automatic cost-of-living benefit increases in excess of a specified amount. As I said earlier, if that specified level were 4 percent, then general revenues would only fund the cost of automatic increases in excess of that level.

We also support using general revenues to replace payroll taxes that social security loses as a result of unemployment in excess of 6 percent.

Now we like those devices, one on the outgo side and one on the income side of the social security ledger, because they tend to insulate the system from inflation and unemployment—the very factors which have caused the short-term problem in the first place. The higher the level of inflation, the higher the benefits. The higher the benefits, the higher the outgo. The higher the level of unemployment the greater the shortfall in expected revenue from payroll taxes.

The scheduling of large payroll tax increases does not guarantee that the cash benefit programs will be adequately funded. The reason why is that you cannot know from any point in time what the trend in inflation is going to be over the 75-year projection period and you don't know whether we are going to have another series of international commodity shortages and petroleum price increases by other cartels that are going to aggravate our current problems of inflation and unemployment. That is our concern.

Mrs. Fayé. It just becomes a transfer of funds.

Mr. Hacking. That's right. If we were to find that our proposals were not legislatively possible for HI. We would certainly go along with that because that is better than what we have.

Mrs. Fayé. Senator Domenici would agree with you, of course, in regard to the tax burden on the employees of today and the future. There is also a problem of where the general revenues are to come from.

Mr. Hacking. My statement deals with this matter of the source of the "general revenues." As a matter of fact, every time we advanced our proposal in the last 3 years before the members of the House Subcommittee on Social Security, the question has always been asked: "Where do the general revenues come from?"

Well, general revenues can come from one of three sources:

First of all, income from increased revenue derived from existing nonearmarked tax sources like the income tax or from new tax sources.

Second, they can come from deficit financing through the sale of Government securities in the marketplace. That is how we make ends meet in the context of the Federal budget when Government outgo exceeds income.

Third, they can come from a shift in expenditure priorities within the context of the Federal budget.

Now the choice of sources for any general revenue contribution to social security in any given year should depend upon what the economy needs at the time. Our association supports a balanced budget over the business cycle. We still have a business cycle. Despite the efforts of the Federal Government to "fine tune" the economy, the business cycle still exists. We have economic upswings and downswings. If we are on the upswing of the business cycle, it may be appropriate to introduce a temporary tax mechanism—like a surtax on the income tax, perhaps to raise the needed general revenues.

On the other hand, if we are on a downswing and it is appropriate to resort to deficit financing, then that should be the source for the general revenues. But if neither is possible then by all means shift around the expenditure priorities in the context of the budget.

We have a budget process in the Congress now and that is where the decision with respect to the source should be made and it should be made on the basis of what the economy needs at the time.

I would also add that we are not talking about permanent infusions of general funds into the cash benefit programs. We would hope that these two devices would phase out. If unemployment declines below the specified level, the general revenue contribution on the income side is eliminated. If inflation declines below the specified level and the revenue coming into the system form the automatic increases in the taxable wage base—which, by the way, is supposed to fund automatic benefit increases in the first place—is suffiient to offset the aggregate cost of the automatic benefit increases, then any need for general revenues on the outgo side is also automatically eliminated.

These devices would be there to safeguard the system and prevent the kind of roller coaster economic experience we have had—where unemployment shoots way up and cuts way down the payroll taxes going into the system—from causing a problem. People get upset and tend to lose faith in the financial viability of the system. Workers say, "Why should I put money into this system, and even more in the future, when there is a very strong likelihood that there is going to be nothing for me when I reach age 65."

We strongly urge that what was done last December be in part undone and corrected.

Mrs. FAYÉ. Thank you.

GREATER PAYROLL TAX RELIEF VERSUS SMALLER INCOME TAX DEDUCTION

Mr. AFFELDT. One more question. Mr. Sunley indicated that if greater payroll tax relief were granted and we operated within the administration's ceiling with regard to a total tax reduction, this would mean a smaller amount of the tax reduction would go to elderly taxpayers. What are your thoughts about that? Would it be worth the tradeoff?

Mr. HACKING. In the first place there is nothing in the law that requires the administration to come up with a tax cut. The administration has done so for some very good reasons, most of which are economic. You know, I should think that introducing some general revenues into the social security system would make more economic sense, since we still have this problem with unemployment and are facing a downturn in the business cycle. If the administration came in now with a proposal for some general revenues for social security and payroll tax cuts, but reduced the magnitude of its proposed income tax cuts, then the elderly taxpayers would have to accept that.

I think that is the situation. Besides, if we ever had to choose between a pragmatic approach to the funding needs of the social security system over some immediate short-term tax cuts, that would probably be quickly offset by the combination of inflation and the progressive rate structure of the income tax, I would have to say that we would have to come down on the side of a more sane, rational and pragmatic approach to the financial needs of social security. Social security, not income tax cuts, is the cornerstone of the elderly's income.

Mr. AFFELDT. We are nearing 1 o'clock. I would like to continue, but I am sure many of you would like to eat.

I thank all of you for participating. The hearing will be concluded until the call of the Chair.

Thank you again.

[Whereupon at 12:50 p.m., the hearing adjourned.]

APPENDIX

LETTER AND ENCLOSURE FROM C. O. YOUNGSTROM, CHAIRMAN, LEGISLATIVE COMMITTEE, IDAHO FEDERATION OF NATIONAL ASSOCIATION OF RETIRED FEDERAL EMPLOYEES, TO SENATOR FRANK CHURCH, DATED MARCH 6, 1978

DEAR SENATOR CHURCH: I am pleased to transmit to you a statement relative to tax reform and the tax credit for the elderly.

This is presented on behalf of our NARFE members in Idaho and is submitted to be a part of the record of the hearing convened by your committee on February 28.

We appreciate being advised by your office of this hearing and that the record is still open permitting this testimony to become a part of that record.

Sincerely yours,

C. O. YOUNGSTROM, *Chairman.*

[Enclosure.]

STATEMENT OF THE IDAHO NARFE FEDERATION LEGISLATIVE COMMITTEE ON TAX REFORM AND THE ELDERLY

The Idaho NARFE Federation Legislative Committee wishes to express its sincere appreciation for the opportunity to present this statement to the Senate Special Committee on Aging and to its chairman, Senator Frank Church.

Tax reform and particularly modification of the tax credit for the elderly are matters of substantial concern to Federal retirees and we are pleased the hearing record is still open to permit this statement to be entered on behalf of the Idaho NARFE Federation, its eight chapters, and their members.

The Idaho NARFE organization has had a continuing concern in securing the updating of retirement income credit and preserving it as a matter of fairness and justice for civil service annuitants as an equitable offset to the tax-free benefits available to social security recipients. This has been the subject of repeated expressions to the chairman of the Special Committee on Aging as well as to other members of Idaho's congressional delegation.

As an accepted goal of our Idaho NARFE organization, updating and modernization of retirement income credit was the principal thrust of the testimony offered by the Idaho NARFE Legislative Committee to the hearing of the Special Committee on Aging held in Twin Falls, Idaho, May 16, 1974.

We are particularly grateful to the chairman and to those members of this committee who helped restore for 1976 returns the optional use of retirement income credit on the same basis as available to taxpayers prior to the tax credit for the elderly.

When the tax credit for the elderly became a part of our income tax code in 1976, the changes made in the statutes provided for a substantially broader income definition on which to base the credit for those over 65. At the same time, it greatly limited its availability for those with modest incomes of $7,500 for single persons and $10,000 for couples making joint returns. This results from the credit phaseout applied at those income levels.

There was differential and favored treatment for those public retirees under age 65 who did not have the credit reduced by the phaseout, in effect retaining for them the principal features of the pre-1976 retirement income credit while denying it to those over 65.

We place our emphasis on three principal points as we have sought to improve retirement income credit and since 1976 to modify and make more useful the tax credit for the elderly:

(1) We urge updating the dollar amounts used in determining the credit base. From 1962 until 1976, when a small upward adjustment was made, no change had been made in this figure despite repeated increases in social security benefits which this credit was originally intended to offset. The current amounts do not provide for equity or comparability with the justified improvements made in social security benefits.

(2) We recommend an automatic adjustment or indexing of this credit base to provide for a continuing level of comparability with changes in social security benefits resulting from increases in cost-of-living. This would avoid a long period of inattention to such needed adjustments as occurred from 1962 to 1976, when the credit base amount remained unchanged despite the sharp inflation which took place particularly during the later years of that time frame.

(3) We recommend elimination of the phaseout currently applied to the credit when the adjusted gross income of persons over 65 reaches even the moderate levels established under the provisions of the tax credit for the elderly. Our argument here is simply that no such phaseout applies to social security beneficiaries at any level of their adjusted gross incomes. Fairness and equity justifies similar treatment for Federal annuitants.

We urge adoption of legislation which would accomplish these three objectives.

A measure was introduced in the first Session of this Congress by Senator Inouye as S. 2128 which would produce those results. It embodies the three general objectives we have outlined and in our judgment would correct the major shortcomings in the Tax Credit for the Elderly.

We are hopeful that this or a similar measure will receive favorable attention by this committee and subsequently by the Senate. We do wish to point out an identical bill was introduced in the House last year as H.R. 8818.

We wish to acknowledge with appreciation this opportunity to present the views of Idaho NARFE members to the Senate Special Committee on Aging.

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