

Inquiring Minds topic – 7 December 2012

Harold Gibson, Moderator

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More income should be taxed, a writer says. Readers react.

To the Editor:

In a nation that prides itself on fair play and equal opportunity, it seems incongruous that people with wealth-based income — interest, dividends, capital gains, rent — are excused from paying Social Security (traditionally 12.4 percent) and Medicare taxes (2.9 percent) on that income. Equally odd, they do not pay Social Security tax on wages above \$110,100. Shouldn't these taxes be paid on all income? Taxing the “earned” and not the “unearned” seems rather un-American, doesn't it?

The two preferences hark back to Social Security's 1930s groundbreaking origins. Without these exclusions, would there have been a political consensus to create Social Security? Maybe, maybe not, but no decision is fixed forever.

If these preferences were eliminated and the economy recovered to mirror a positive year like 2007, the Social Security Trust Fund would nearly double its annual revenue. We could expect to see an additional \$500 billion for Social Security and \$100 billion for Medicare. The additional Social Security inflow would almost cover the annual outflow, leaving most of the current revenue as a surplus to accommodate the baby boomers.

Virtually all income of the bottom 50 percent is “earned” and fully taxed for Social Security and Medicare. Many people are unaware that wealthy taxpayers are entitled to exempt much, if not most, of their wages, as well as investment income. Ending those exemptions would allow a major reduction in Social Security and Medicare tax rates.

Alternatively, if tax rates stayed at or near current levels, Congress could use half the new revenue to strengthen Social Security, Medicare, food stamps, unemployment and other support programs. The other half could be used to abolish the corporate income tax, which has averaged about \$224 billion in annual revenues over the last decade.

Such a “grand bargain” would make the funding of the safety net fairer and eliminate the double taxation of dividends. Abolishing the corporate income tax would also make American companies more competitive internationally.

- JAMES ABERT - Lancaster, Pa., June 4, 2012 - *The writer is a retired faculty member at the McDonough School of Business, Georgetown University.*

Readers React

Mr. Abert argues for imposing Social Security taxes on all income on the grounds that this nation prides itself on fair play. But the people of this nation also pride themselves on self-reliance.

Social Security gained its great popularity precisely because it is not a welfare program. People pay into it from the money they earn during their working years. The amount of benefits they receive is calculated based on lifetime earnings. No one feels guilty about getting Social Security because “it’s my own money I’m getting back.”

Mr. Abert’s proposal would change all that. While the amount of income taxed would no longer be capped at \$110,100, or at all, the maximum payments presumably would be limited. Thus, many Americans would pay taxes on income not included in the calculation of the benefits they will receive on retirement. In short, wealthier Americans will be subsidizing the retirement of the less wealthy. No one would any longer be able to say, “I’m just getting my own money back.”

Franklin D. Roosevelt believed that Social Security could never be repealed because all workers invested in it and all shared an interest in its continuation. Breaking the link between taxes and benefits would destroy that sense of self-reliance that has long sustained the program. Turning Social Security into a welfare program would be the first step on the way to its eventual demise.

- CHARLES W. SNYDER - Savannah, Ga., June 6, 2012 - *The writer is a lawyer.*

I agree with some things Mr. Abert says and disagree with others. The most upsetting is using the excess revenues for things other than Social Security.

Revenues from the payroll tax do not go into the general fund. Sure, the surplus is invested in Treasury bonds, with proceeds going toward financing general government spending until the bonds mature and get paid back, but no Social Security money is used for anything other than Social Security. That is one key factor that gives Social Security such widespread support.

Increasing or abolishing the ceiling on earned income subject to Federal Insurance Contributions Act, or F.I.C.A., contributions would alone finance Social Security in perpetuity, and the rate may even be lowered after the baby boom generation passes through the system.

The biggest problem Social Security has is that most Americans do not understand it. Participants (involuntarily, I’ll grant you) make contributions to the fund while they are working, then withdraw from it when they retire. If the money just sat there, there would be no accumulation for population bulges, like the baby boom, and no increase for inflation. Therefore, it is invested in Treasury bonds, where it collects interest and allows the government to borrow domestically from its own citizens instead of sending interest payments to foreigners. The money is completely accounted for, and the government is obliged to pay the promised benefits.

It is an ingenious system, and we must do everything we can to preserve it.

- SCOTT KOCHMAN - Brooklyn, June 6, 2012

Mr. Abert’s letter points out the enormous inequity in our tax system that is heavily skewed in favor of the wealthy. I also agree with him that a tax code that treats “unearned income” more favorably than “earned income” is toxic in a society that still professes to have at least a modicum of commitment to equal rights and equal opportunity.

What I don't understand is the rationale for his proposal to abolish corporate income taxes. Don't the laws of the United States already treat corporations more favorably than ordinary mortals?

During the 1950s, corporations paid about 49 percent of their profits in taxes, yet the economy grew and the middle class expanded and prospered. By 2011, corporations paid taxes at about half that rate, as they outsourced American jobs, destroyed unions, deindustrialized the economy and hollowed out the middle class. Corporations should not be rewarded for their irresponsible behavior.

More important, Mr. Abert's proposed "grand bargain" needs to be viewed in the context of current political realities. The enormous concentration of wealth in a minuscule income group has spawned an incredibly influential elite who have gamed this country's dysfunctional political system and are able to shape it to serve their needs. Until this problem is addressed, no proposals that compel the wealthy to pay higher taxes, however meritorious, have a chance of ever being enacted into law.

- PAUL L. NEVINS - Boston, June 6, 2012 - *The writer is a lawyer.*

There are several points I take issue with in Mr. Abert's letter.

There is a limit on Social Security payments in retirement. So if we raise the current cap on F.I.C.A. taxes from \$110,100 to infinity, should we also raise the maximum Social Security retirement benefit? If not, then where is the "fairness" in that?

Mr. Abert's references to a "positive year like 2007" would be more accurately translated as "bubble year." The economy in 2012 is most likely the new normal, so the additional revenue Mr. Abert cites is highly suspect.

There are many retirees who, after working 30 to 40 years, have amassed a "golden years" nest egg. As the Federal Reserve maintains record low interest rates, many retirees have found their income decimated. To add an F.I.C.A. tax on the earned interest, even at a reduced level, would add insult to injury.

While I agree with Mr. Abert that abolishing the corporate income tax would make American companies more competitive internationally, the current political reality will keep that a distant fantasy. Until our multitrillion-dollar national debt is pared down, corporations should not be let off the hook.

- JOHN LAIDO - Brooklyn, June 7, 2012

Eight decades ago it was a new notion, but Social Security has been the most popular government program for many decades. Mr. Ebert's suggestions regarding caps and unearned income are ripe for pursuing. We should go beyond "saving Social Security" to both strengthening the Trust Fund *and* increasing benefits.

We could include in the proposal to increase the Trust Fund's income some increases in benefits. This is particularly attractive nowadays as people are conscious of two new threats to their old-age security: employer-provided pensions have been eliminated or reduced, and individual savings have been crippled by the recession.

It would not be as expensive as might, at first, appear. Our Social Security income is taxable, and the proceeds circulate back to the Trust Fund. Raise our benefits and we pay a bit more taxes — to the benefit of the Trust Fund.

It is politically possible. Recall that eliminating the cap on Medicare “taxes” occurred during Bill Clinton’s presidency with barely a whimper. Few even know that it occurred.

- RAMELLE MaCOY & MARTIN MORAND - Mifflintown, Pa., June 7, 2012 - *The writers are retired professors of industrial and labor relations at Indiana University of PA.*

Social Security was designed as a payroll tax, not a second income tax, so it is not appropriate to include unearned income in the tax base. The system is intended to partly replace earnings after retirement, not investment income.

While the income level on which taxes are levied is capped at \$110,100, so too are benefits. Moreover, the benefits formula is redistributive, heavily favoring low-income earners.

In 2012, benefit recipients receive 90 percent of their first \$767 of monthly earnings, 32 percent of their next \$3,857 of monthly earnings, and only 15 percent of their monthly earnings in excess of \$4,624 (up to the cap). It is hard to see why this is so unfair to the poor.

- MICHAEL SESNOWITZ - Henrico, Va., June 7, 2012 - *The writer is a professor of economics at Virginia Commonwealth University.*

The Writer Responds

Responding to Mr. Kochman, I envision that all revenues from the expanded “safety net tax” would be designated for specific safety-net-related programs. Social Security and disability insurance would grow somewhat. Other safety net programs, such as food stamps, would be swept out of the regular budget to new trust funds supported by the safety net tax. This swap allows for the corporate tax relief part of the bargain.

Mr. Nevins is right. Any legislation that raises taxes paid by the rich faces stiff opposition. But there would be considerable compensation. Elimination of the corporate tax should increase corporate profits, repatriate overseas income, increase dividends and drive up stock prices.

Mr. Laido asks if the maximum Social Security payout should increase since the amount of taxed income — earned plus unearned — would increase. No. These payments are intended to provide a safety net. They are more insurance than investment. The Social Security payout should provide a reasonable standard of living to those who have little, not a supplementary payment to those who have much.

I agree with Mr. Snyder that most Americans favor self-reliance and feel guilty if forced to seek welfare. I only wish that those who have turned “entitlement” into a code word for freeloaders would agree as well.

- JAMES ABERT - Lancaster, Pa., June 8, 2012