

lion annually, but by 1965 they had more than doubled to 12.5 billion annually (5, p. 14; 6, p. 6). The Internal Revenue Service in its "Statistics of Income" has analyzed the returns of taxpayers over 65, but OAI benefits are not reported by taxpayers and so it is uncertain which taxpayers are benefiting from this tax exemption or how large the revenue loss is. However, two-thirds of the 3 million taxable returns reported no wage income, and so there was no barrier from this source to receiving benefits. In fact, almost 50 percent of each group of returns showing over \$15,000 adjusted gross income showed no wage or salary income (11, p. 89). These persons who reported no wages could have received their full OAI benefits and enjoyed significant tax savings.

The exemption of these benefits from tax does not conform to the accepted standards of either vertical or horizontal equity, and several writers have proposed that the benefits be included in taxable income. There is a departure from the standards of vertical equity as expressed by the tax rates because OAI benefits received by wealthy persons will be subject to the same zero tax rate as those received by low-income beneficiaries. The concept of horizontal equity is violated by having two persons whose incomes are equal, one receiving OAI benefits and the other receiving an equal amount of wage income, but subject to different tax rates.

These benefits are tax preferred in the sense that the general definition of income as given in the Internal Revenue Code specifically includes retirement benefits. "Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items: "* * * (9) Annuities; (10) Income from life insurance and endowment contracts; (11) Pensions: * * * (9, sec. 61)." Accordingly, retirement benefits are normally included in adjusted gross income to the extent that they exceed the amount contributed by and previously taxed to the recipient, but OAI benefits are tax exempt in their entirety.

The proper tax treatment of amounts paid as workers' contributions is not so widely agreed on as the tax treatment of benefits. Some argue for the exemption of contributions from taxable income because, as they propose, benefits will be taxed later (3). Others point out that with a retirement income credit still operative, benefits, though includible in adjusted gross income, could still escape taxation, and so contributions should be taxed to compensate for this exemption (1). In view of the variety of forms of income covered by the retirement income credit and not previously taxed, this latter policy would seem to single out OAI for prepayment of taxes in anticipation of future possible exemption.

A stronger case can be built if one combines the generally accepted definition of income supported by most economists, that income is the algebraic sum of changes in net worth plus consumption, with the treatment of insurance as proposed by Vickrey (14, pp. 58-85). His point is that insurance against a future loss of income is analogous to a business expense and should be deductible under a personal income tax. Thus, the contribution made under OAI could be viewed as a legitimate expense of guaranteeing future income under given contingencies and should not be a part of adjusted gross income. The later payments of benefits would then be taxable. For the individual the