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Social Security: Raising or Eliminating the Taxable Earnings Base

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Social Security: Raising or Eliminating the Taxable Earnings Base

Summary

Social Security taxes are levied on earnings up to a maximum level set each year. In 2006, this maximum — or what is referred to as the taxable earnings base — is $94,200. The taxable earnings base serves as both a cap on contributions and a cap on benefits. As a contribution base, it establishes the maximum amount of earnings for each worker that is subject to the payroll tax. As a benefit base, it establishes the maximum amount of earnings used to calculate benefits.

Since 1982, the Social Security base has risen at the same rate as average wages in the economy. However, the percent of covered earnings that are taxable have decreased from 90% in 1982 to 85% in 2004. The percentage of covered earnings that is taxable is projected to decline to about 83% for 2014 and later. Since the cap was indexed to the average growth in wages, the share of the population below the cap has remained relatively stable at roughly 94%. Of the 8.5 million Americans with earnings above the base, roughly 80% are men and only 9% had any earnings from self-employment income. New Jersey has the highest share of the population above the maximum (10%) and South Dakota has the lowest share (2%).

Raising or eliminating the cap on wages that are subject to taxes would reduce the long-range deficit in the Social Security Trust Funds. For example, raising the maximum taxable earnings from $94,200 to $150,000 — roughly the level needed to cover 90% of all earnings — would eliminate roughly 40% of the long-range shortfall in Social Security. This change would generate $182 billion over the five-year budget window of 2006-2010 and $433 billion in additional revenue between 2006-2015. If all earnings were subject to the payroll tax but the base was retained for benefit calculations, the Social Security Trust Funds would remain solvent for the next 75 years. However, the link between contributions and benefits would be broken.

There is no similar earnings base for the Medicare Hospital Insurance (HI) portion of the payroll tax; all earnings are taxable for HI purposes. Elimination of the HI base was proposed by President Clinton as a way to raise revenue and enacted in 1993, effectively beginning in 1994.

This report will be updated as legislative activity warrants.

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Social Security: Raising or Eliminating the Taxable Earnings Base

Background

Social Security was enacted in 1935, and the Social Security tax was first levied in 1937. From 1937 through 1949 the tax rate was 1% (on employee and employer, each) on earnings up to $3,000 a year. Since that time the rate has risen to 6.2% and the taxable maximum has been increased to help meet the financing needs of the program, and to keep up to date with changing earnings levels. Since 1982, the Social Security earnings base has risen at the same rate as wages in the economy. By law the Commissioner of Social Security is required to raise the base whenever an automatic benefit increase — cost of living adjustment (COLA) — is granted to Social Security recipients, assuming wages have risen. The increase in the base from $90,000 in 2005 to $94,200 in 2006 is based on the increase in average wages from 2003 to 2004.[1]

Origin and History of the Taxable Earnings Base

In 1935, the designers of Social Security — President Franklin Roosevelt's Committee on Economic Security — did not recommend a maximum level of taxable earnings in its plan, and the draft bill that President Roosevelt sent to the Hill did not include one. The bill emphasized who was to be covered by the system, not how much wages should be taxed. Being in the midst of the Depression, the Administration's attention was on the large number of aged people living in poverty. Its goal in proposing a Social Security program was to complement public assistance measures (Old-Age Assistance) in its plan. The plan offered immediate cash aid to the aged poor and created an earnings-replacement system intended to lessen the need for welfare benefits in the long run. It was recognized that the new system would not be sufficient to provide full income in retirement, but would provide a "core" benefit as a floor of protection against poverty. Not concerned about high-income retirees, the Administration's proposal exempted non-manual workers earning $250 or more a month from coverage (i.e., $3,000 on an annual basis). Manual workers were to be covered regardless of their earnings, but few had earnings above this level.

It was the Social Security bill reported by the House Ways and Means Committee that clearly established a maximum taxable amount, which it set at

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[1] The reason for the two-year lag in reflecting increases in average wages in the taxable earnings base is that average wages for the year immediately prior to the year of the increase simply are not know in time.

$3,000 per year.[2] In addition, the committee dropped the exemption for non-manual workers with high earnings. The committee's report and floor statements made at the time give no clear record as to the reasoning for the taxable limit, but concerns about tax equity and attaining as much program coverage of the workforce as possible were suggested as factors for rejecting the high-earner exemption. Not covering them meant that they would not pay the tax where lower wage earners would, and coverage would be erratic for workers whose earnings fluctuated above and below the $250 monthly threshold.

Although tax policy concerns were raised in later years, with a higher base preferred by those seeking a more proportional tax system, there was little if any serious attention given to eliminating the base entirely. In the late 1940s and early 1950s and to a lesser extent later on, the major arguments were over the base's size and how it affected the development of Social Security. A larger base meant that more earnings would be credited to a person's Social Security record and would lead to higher benefits (since benefits are based on a worker's earnings). Proponents argued that the base needed to be raised to reflect wage or price growth so that the benefits of moderate and well-to-do recipients would not erode over time (thereby preserving their support for the system). Critics argued that this would increase benefits for people who could save on their own while making saving by private means more difficult. In 1972, as a means of financing cost-of-living adjustments for Social Security recipients, procedures were enacted that increased the base automatically to reflect the growth in average wages. In 1977, the base was raised beyond what resulted from the automatic increase provision (by $7,500 over three years) as a means of raising revenue to help shore up the program's ailing financial condition. These ad hoc adjustments were intended to achieve a base under which 90% of all covered payroll would be subject to tax.

Medicare was enacted in 1965 with the hospital insurance (HI) portion of the program financed with payroll taxes. The HI tax was first levied in 1966 at a rate of 0.35% (on employee and employer, each) and the maximum taxable amount was set at same level as Social Security's.[3] The HI rate was subsequently raised periodically (reaching its current level of 1.45% in 1986) to meet the financing needs of the program, but its base continued to be the same as Social Security's through 1990. Then, to reduce federal budget deficits, the Omnibus Budget Reconciliation Act of 1990 (P.L. 101-518) raised the HI base to $125,000. The HI base then rose automatically to $135,000 over the next two years. In 1993, as part of his plan to reduce budget deficits, President Clinton proposed that the HI base be eliminated entirely. As part of the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) the HI base was removed, raising an estimated $29 billion in revenues over the FY1994-FY1998 period.

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[2] The maximum for a worker was to be $3,000 per year per employer, so that, under the original legislation enacted in 1935, someone could have paid tax on more than $3,000 in earnings per year (and received benefits from all such wages) if they worked for more than one employer.

[3] The same maximum taxable amount was set for the self-employed when they were covered in 1951 and for the Disability Insurance (DI) portion of the tax when it was first levied in 1957.

The Taxable Earnings Base Today

In 2004 an estimated 157 million workers paid Federal Insurance Contributions Act (FICA) taxes and Self-Employment Contributions Act (SECA) taxes on their wages and net self-employment income.[4,5] Both employers and employees contribute earnings at the FICA rate and SECA taxes are paid by the self-employed. Both taxes have three components: Old Age and Survivors Insurance (OASI), Disability Insurance (DI), and the Hospital Insurance part of Medicare. The OASDI tax is levied on earnings up to $94,200 in 2006. The HI tax is levied on all earnings.

2006 Social Security and Medicare Tax Rates and Maximum Taxable Earnings

FICA and SECA Tax Rates:	**FICA**	**SECA***
Old-Age and Survivors Insurance	5.3%	10.6%
+Disability Insurance	0.90%	1.8%
=Subtotal Social Security (OASDI)tax rate	6.20%	12.4%
+ Hospital Insurance tax rate	1.45%	2.9%
Total FICA and SECA rate	*7.65%*	*15.3%*

Combined Employee and Employer FICA Tax Rates:

Employee	7.65%
+Employer	7.65%
Combined FICA rate	*15.3%*

Maximum Taxable Earnings:

Social Security	$94,200
Hospital Insurance	no maximum

Maximum FICA/SECA Taxes:	**OASDI**	**HI**
Employee/Employer (each):	$5,840.40	No limit
Self-Employed:	$11,680.80	No limit

Percent of Aggregate Earnings Above the Base (not taxed) 2004:

Social Security	15.4%
Hospital Insurance	(all earnings are taxed)

Social Security Benefit for 2006 Retiree With Earnings at or Above the Maximum for Entire Career :	**Monthly**	**Annual**
Retired at age 62:	$1,530	$18,360
Retired at full retirement age (65+6 months):	$2,053	$24,636

Source: *SSA*
**Certain adjustments and income tax deductions apply.*

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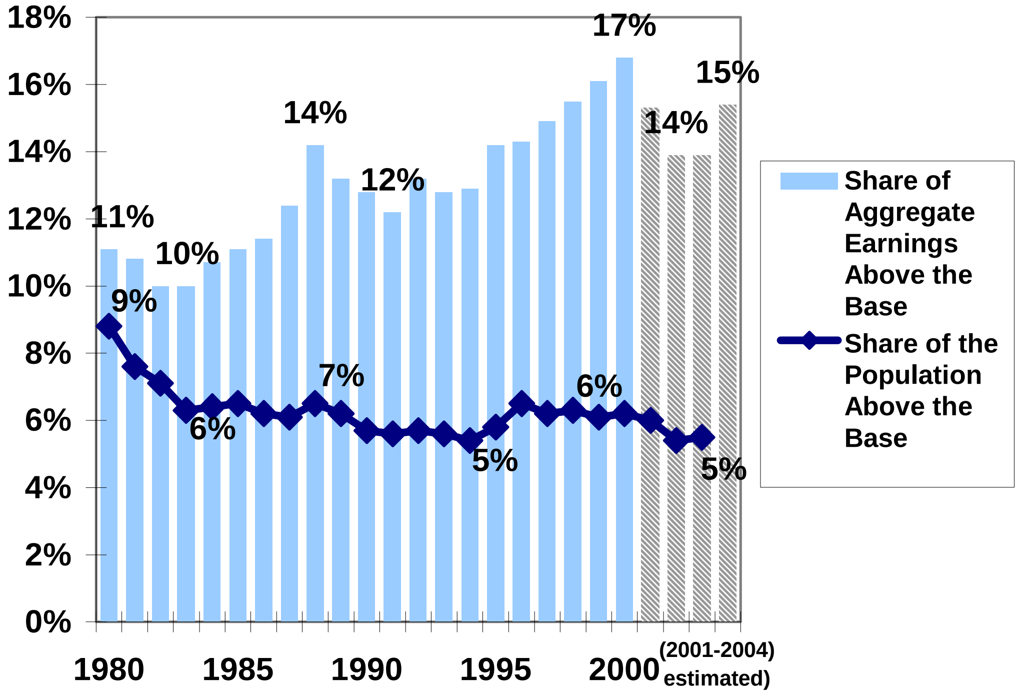
[4] Social Security Administration, Annual Statistical Supplement, 2005.

[5] Some workers are exempt from payroll taxes. For a listing of workers who are exempt from FICA and SECA taxes see CRS Report 94-28, *Social Security and Medicare Taxes and Premiums: Fact Sheet*, by Dawn Nuschler.

The Taxable Earnings Base Over Time. As shown in **Table 1** and **Figure 1**, the share of covered workers below the taxable earnings base has remained relatively stable since the 1980s at roughly 94%. However, during the same period the share of covered payroll that is taxed has fallen from 90% of all earnings in 1982 to 85% in 2004. The large declines in the late 1990s were mainly due to the fact that salaries for top earners grew faster than the pay of workers below the cap.[6]

Figure 1. Share of Earnings and Population Above the Taxable Earnings Base 1980-2004



Source: Figure prepared by Congressional Research Service (CRS), based on data from the Social Security Administration, Social Security Bulletin, Annual Supplement, 2005.

The Taxable Earnings Base by State. In 2002, slightly more than 5% of workers with wage and salary income had earnings above the taxable base of $84,900.[7] However, focusing on the nationwide average hides the diversity between the states. As shown in **Table 2**, the share of the population above the base in 2002 ranges from a high in New Jersey where 10.2% of covered workers earn above the base to a low in South Dakota where less than 2% of workers earn this amount. The states with the lowest share of workers over the base are: South Dakota, North Dakota, Montana, West Virginia, and Arkansas. Those with the highest share of

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[6] At least some of this decline and subsequent increase in the ratio is believed to be due to stock option activity surrounding the stock market bubble in 2000 and is not likely to recur. (SSA, *2005 OASDI Trustees Report*)

[7] These figures do not include individuals with only self-employment income. Note that the calculations in **Tables 1**, **2** and **3** differ slightly due to differences in data.

workers over the base are: New Jersey, the District of Columbia, Connecticut, Massachusetts, California and New York.

The Taxable Earnings Base by Employment Status and Gender. In 2003, the latest year for which data is available, 8.5 million individuals had earnings above the taxable maximum.[8] As shown in **Table 3**, these individuals represent 6% of all workers covered by Social Security. Roughly 80% of these individuals were men and 93% were wage and salary workers. Only 765,000 or 9% of these individuals received any self-employment income. In total, 8% of all male workers and 3% of all female workers in 2003 had earnings above the maximum. Of the self-employed, roughly 7% of men and 2% of women earned more than the taxable earnings base.

The Future of the Taxable Earnings Base. The taxable wage base is increased annually by the average growth in wages, so the share of the population below the cap is expected to remain relatively stable over time. However, the share of payroll that is taxed is expected to decline even further. Under the intermediate assumptions of the 2005 Trustees Report, the percentage of covered earnings that is taxable is projected to decline to about 83% for 2014 and remain stable thereafter.

Impact of Raising or Eliminating the Taxable Earnings Base

Raising or removing the taxable earnings base could reduce or eliminate the long-term Social Security deficit. The full impact of the policy change would depend on whether or not the wages above the maximum would be counted toward benefits. The taxable earnings base serves as both a cap on contributions into the system and a cap on benefits. As a contribution base, it establishes the maximum amount of covered earnings for each worker that is subject to the payroll tax. As a benefit base, it establishes the maximum amount of earnings that are used to calculate benefits. The current benefit for an individual who, during his or her working life, earned the maximum amount or higher for at least 35 years (the number of years on which benefits are calculated) and retired at the full retirement age (65 and six months in 2006) is $2,053 a month or $24,636 per year. The benefit replaces about 26% of the worker's taxable earnings. Maintaining the current structure, where benefits are calculated on the full contribution base, while raising or eliminating the taxable earnings base would lead to higher monthly Social Security checks for wealthy individuals who would pay the additional taxes.

Impact on the Social Security Trust Funds. Under the assumptions of the 2004 Trustees Report, the actuaries at the Social Security Administration calculate that it would take an immediate increase in combined payroll taxes of 1.89% of taxable payroll (from 12.4% to 14.29%) to achieve solvency over the next

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[8] *Social Security Administration, Annual Statistical Supplement, 2005.* See [http://www.ssa.gov/policy/docs/statcomps/supplement/2005/4b.html#table4.b1].

75 years.[9] Without this increase or other changes to the system, the OASDI Trust Funds are projected to be exhausted in 2042.

An alternative to raising the payroll tax rate to improve solvency is to rase or remove the taxable earnings base. Workers with earnings below the base would not contribute additional taxes, but those above the base would make higher FICA and SECA contributions. This policy option could be implemented in a variety of ways. The base could be removed completely or the base could be set to cover a given share of total earnings in the economy. The wage base could also be set at different levels for employers and employees rather than at an equal level as under current law. Further, the current base could be maintained for the calculation of benefits or high earners' benefits could be based on the new taxable earnings base. The impact on the Social Security Trust Funds of three of these options is detailed below.

Option1: Cover 90% of earnings and pay higher benefits. One proposal would be to slowly raise the taxable wage base for both employers and employees to cover 90% of all earnings — roughly the level in 1983 when Congress last addressed Social Security's finances — and credit these taxes to allow individuals to receive correspondingly higher benefits. In 2005, it was estimated that a cap of $150,000 would roughly cover 90% of wages. If the wage base was $150,000, contributions by employers and employees would be at most $3,459 higher than under current law. Under this option, benefits at retirement for high earners would also rise. These changes would have a net positive impact on the Social Security Trust Funds. Raising the wage base to 90% would eliminate 40% of the long-range financial shortfall — extending the Trust Funds' exhaustion date to 2053.[10] To achieve solvency for the next 75 years under this option, the payroll tax rate would also have to be raised by 1.14% of taxable payroll (from 12.4% to 13.54%).[11]

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[9] The projections in this section were done using the assumptions of the 2004 Trustees Report. Under the intermediate assumptions of the 2005 Trustees Report, the actuarial deficit is 1.92% of taxable payroll for the 75-year projection period and the trust fund is projected to be exhausted in 2041. (Social Security Administration, *2005 OASDI Trustees Report*.)

[10] Reno and Lavery, *Options to Balance Social Security Funds*, Feb. 2005.

[11] Social Security Administration, *Estimated OASDI Long-Range Financial Effects of Several Provisions Requested by the Social Security Advisory Board*, Memorandum, dated Feb. 2, 2005, [http://www.ssab.gov/financing/2004_update.pdf].

Impact on the Social Security Trust Funds of Raising or Eliminating the Social Security Taxable Earnings Base*

	Year the Trust Funds are exhausted	75-year Actuarial Balance (as a % of taxable payroll)	Percent of 75-year shortfall met
No change to current law	2042	-1.89	
Option 1: Make 90% of the earnings subject to the payroll tax and credit them for benefit purposes (phased in 2005-2014)	2053	-1.14	40%
Option 2: Make all earnings subject to the payroll tax and credit them for benefit purposes (beginning in 2005)	2079	-0.14	93%
Option 3: Make all earnings subject to the payroll tax but retain the cap for benefit calculations (Beginning in 2005)	n.a.**	0.32	116%

Sources: *Social Security Administration, Memorandum, dated Feb. 2, 2005.* Reno and Lavery, *Options to Balance Social Security Funds*, Feb. 2005.

** All calculations use the intermediate assumptions of the 2004 Trustees Report.*
***Solvent beyond 75-year estimate*.

Option2: Cover all earnings and pay higher benefits. If the earnings base was completely eliminated for both employers and employees so that all earnings were taxed, 93% of the projected financial shortfall in the Social Security program would be eliminated. Under this scenario high earners would pay higher taxes but also receive higher benefits. However, the net benefit to the Trust Funds is positive as $5 in revenue would provide only $1 in additional benefits (on average over their 75-year valuation period).[12] Annual Social Security benefit payments would be much higher than today's maximum of $24,636. A worker who paid taxes on earnings of $400,000 each year would get a benefit of about $6,000 a month or $72,000 a year — a replacement rate of 18% — while someone with lifetime earnings of $1 million a year would get a monthly Social Security benefit of about $13,500 a month or $162,000 a year — a replacement rate of 16.2%.[13,14]

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[12] Eliminating the base would generate revenue equal to 2.21% of payroll on average, while benefit costs would rise by 0.46%. (1.75% total).

[13] Calculations are for 2005 from Reno and Lavery, *Options to Balance Social Security Funds*, Feb. 2005.

[14] Benefits this high would be extremely rare as very few individuals earn above the taxable wage base for their entire career.

Option3: Cover all earnings and pay no additional benefits. Finally if the base was completely eliminated for both employers and employees so that all earnings were taxed, but those earnings did not count toward benefits, solvency would be restored to Social Security. The increased revenue would eliminate 116% of the projected shortfall and the program would have surplus of 0.32% of wages. Under this scenario, the payroll tax rate could be immediately *lowered* by 2.6% of taxable payroll (from 12.4% to 12.08%), and the system would remain solvent for the next 75 years. However, the traditional link between the level of wages that are taxed and the level of wages that count toward benefits would be broken.

Impact on Federal Revenue. Raising the taxable earnings base would lead to an increase in total federal revenues. The Joint Committee on Taxation has estimated that rasing the wage base to 90% of earnings, roughly $150,000 in 2005, would generate $182 billion in additional revenue over the five-year budget window of 2006-2010.[15,16] Over 10 years the policy would generate more than $430 billion. Rasing the payroll tax to cover an additional 1%-2% of income (above the 90% level) would generate $30-$64 billion more over five years and $65-$148 billion more over 10 years.

Revenue Impact of Raising the Social Security Taxable Earnings Base

	Taxable wage base (dollars)	Total change in revenues (billions of dollars)	
Year	**2005**	**2006-2010**	**2006-2015**
Tax 92% of earnings	$190,000	+246.6	+581.1
Tax 91% of earnings	$170,000	+216.0	+515.6
Tax 90% of earnings	$150,000	+182.3	+433.4

Source: *Joint Committee on Taxation, 2005.*

Impact on Workers and Employers. The reaction of high-earning workers and their employers to raising or removing the taxable earnings base is unknown. There would be a reduction in the incentive to work for individuals who earn more than the cap (currently $94,200) as their after-tax earnings will fall.[17] However,

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[15] Congressional Budget Office, Budget Options, *Revenue Option 39: Increase the Upper Limit for Earnings Subject to the Social Security Payroll Tax,* Feb. 2005 [http://www.cbo.gov].

[16] Note that the estimates by the actuaries at the Social Security Administration (SSA) and the Joint Committee on Taxation (JCT) differ slightly due to different assumptions. SSA assumes the maximum wage base will be adjusted each year to keep taxable wages at a constant percent of wages while the JCT assumes it will be a one-time increase with adjustments only for inflation thereafter. JTC estimates also account for the effects on all sources of revenue including changes income taxes and Medicare taxes.

[17] The response by high earners may depend on whether the wage base is raised slightly or

(continued...)

whether these individuals will significantly reduce the amount they work is a matter of debate. Each worker will face a decision between the reduced earnings and the additional leisure time, based on the worker's individual preferences. Increasing the wage base may also have an impact on wages reported by employers. Workers who have earnings above the base would have an incentive to change the form of their compensation to avoid paying the payroll taxes.[18] The impact of raising the base on employers of high-income earners is also unknown. Employers contribute 6.2% of workers' wages up to the taxable wage base toward Social Security. If employers are unable to pass along the higher tax costs to workers in the form of reduced earnings, their overall labor costs will increase. Employers may react by raising prices to consumers, reducing other non-wage forms of compensation such as health benefits or pensions, or reducing the number of workers.

Legislation

Legislation in Prior Congresses. A number of proposals to raise or eliminate the base have been made in recent sessions of Congress. In the 105th Congress, Senator Moynihan proposed raising the base to $97,500 by 2003 ($15,600 more than it was projected to be under current law) as part of a package of changes to restore Social Security's long-range solvency (S. 1792). He again included an increase in the base in a solvency package he introduced in the 106th Congress (S. 21). Similar base hikes were contained in other solvency bills in the 106th introduced by Senators Gregg and Breaux, et al. (S. 1383 and S. 2774) and by Representative Nadler (H.R. 1043). In the 107th Congress, H.R. 2771, introduced by Representatives Kolbe and Stenholm, would have held the base at 86% of total payroll. In the 108th Congress two bills would have raised the wage base. A bill by Kolbe and Stenholm (H.R. 3821) would have gradually raised the base to $133,200, in 2008 and then held the base equal to 87% of total payroll thereafter. H.R. 5179, sponsored by Representative Obey, would have brought the percent of covered earnings subject to the Social Security payroll tax up to 90% by increasing the rate of growth in the Social Security taxable wage base by 2 percentage points above average wage growth for years 2006 through 2036.

Legislation in the 109th Congress. Two bills in the 109th Congress would change the taxable wage base. H.R. 440, introduced by Representative Kolbe and Representative Boyd, would gradually raise the base to $142,500 in 2010 and then index it to 87% of total payroll thereafter. A bill by Representative Wexler (H.R. 2472) would require workers and employers to each contribute 3% of earnings above the taxable wage base. Self-employed individuals would contribute 6% of earnings above the taxable wage base. Earnings above the taxable wage base taxed at the 3% rate would not be credited for benefit computation purposes.

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[17] (...continued)
completely eliminated.

[18] See Martin Sullivan, "Budget Magic and the Social Security Tax Cap," *Tax Notes*. Mar. 14, 2005.

Arguments for and Against Raising or Eliminating the Base

Some of the general arguments for and against changing the Social Security taxable earnings base follow.

Arguments For. The major complaint about the Social Security base is that it creates a regressive tax structure. Workers earning less than the base have a greater proportion of earnings taxed than workers whose earnings exceed it. In 2006, someone with annual earnings of $30,000 pays $1,860 in Social Security taxes, or 6.2% of his or her earnings (ignoring the HI portion and the employer share of the tax). However, because the tax is levied on only the first $94,200 in earnings, someone earning $200,000 a year pays $5,840, or 2.9% of his or her earnings.

Supporters of changing the wage base point out that only 5% of workers have earnings above the base. However due to rising income inequality, since 1991, the amount of their earnings that escape taxation has risen from 12% to 15%, and is projected to continue to rise through 2014. They therefore contend that the current tax structure favors a small group of the more well-off workers in society.

They also point out that the overall employee tax rate rose from 6.13% in 1980 to 7.65% in 1990 (counting the Medicare portion) — or by 25% — and complain that this increase is one of the main reasons for a disproportionate rise in the aggregate federal tax burden on lower and middle-income people over that decade.[19] They further maintain that for most workers, Social Security and Medicare taxes (counting the employer share, which they view as foregone wages) are now greater than their income taxes.

Supporters also argue that subjecting a larger percentage of earnings to the payroll tax would also adjust for the higher life expectancies of high earners.[20] On average, people with more education and higher earnings live longer than those with lower earnings and less education and this difference has been growing over time. The impact on the Social Security program is that these individuals receive benefits for more years over their lifetime making the system less progressive.[21] They claim that rasing the taxable wage base would make a reasonable adjustment for the faster-than-average life expectancy gains among high earners.

Thus, supporters of changing the base argue that raising or eliminating the base not only would be more fair, but also that the payroll tax rate could be reduced without causing a loss of revenue to the system, or, alternatively, that Social Security's projected long-range financing problems could be substantially alleviated.

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[19] See CRS Report RL32693, *Distribution of the Tax Burden Across Individuals: An Overview*, by Jane G. Gravelle and Maxim Shvedov.

[20] See Peter A. Diamond and Peter R. Orzag, *Saving Social Security: A Balanced Approach*, Brookings Institution, 2004.

[21] The Social Security is thought to be progressive in that the benefit formula favors low-wage earners by replacing a greater proportion of their earnings than it does for high-wage earners.

It is estimated that almost $100 billion in revenue to the Social Security program would be generated annually by taxing all earnings, and if such revenues were not used to lower the tax rate, they would reduce the government's outstanding debt and eliminate about 93% of Social Security's long-range deficit.

Arguments Against. Those who support keeping the base as it is point out that while the structure of the payroll tax may be regressive, it is offset by the progressive calculation of benefits.

They further maintain that its critics fail to take into account the effect of other tax and transfer programs targeted to low-earners. They point out that mitigating the Social Security tax bite was part of the motivation for creating the earned income tax credit (EITC), which provides an income tax credit on earnings up to $38,348 in 2006 for married workers with two or more children (up to $14,120 for married workers without children). They also point out that low-income families receive a greater share of government transfer payments that are not subject to Social Security taxes. They argue that the combination of these factors mitigates the flat-rate nature of the tax at lower earnings levels, and that for most other workers the tax is proportional (because it is flat-rate). It is only at the upper end of the income spectrum that it takes on a regressive appearance.

Critics also argue that raising the cap will serve as a disincentive to work and could serve as a drain on the economy.[22] Because additional work effort would generate less after-tax income, supporters claim that workers faced with this higher marginal rate would either reduce their hours or avoid the tax by changing the form of their compensation.

From another perspective, some — who might otherwise espouse progressive taxation — support raising the base but not eliminating it. Having a cap makes Social Security seem less like general purpose taxation. They argue that the system needs support from people of all earnings levels, and that the larger benefits that high earners would receive would represent a poor return for the higher taxes they would pay. Moreover, regardless of the money's worth issue, some question the wisdom of paying large benefits to well-to-do people. They argue that the purpose of the program is to provide a floor of protection for retirement, not large benefits for those who can save on their own. They contend that eliminating the base would raise public cynicism about a publicly financed system that pays enormous benefits to people who already are well off.

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[22] See D. Mark Wilson, *Removing the Social Security's Tax Cap on Wages Would Do More Harm Than Good*, The Heritage Foundation, Oct. 18, 2001.

Table 1. Social Security and Medicare Tax Rates and Taxable Earnings Bases 1937-2006

Year	Tax Rates: Social Security[a]	Tax Rates: HI[a]	Tax Rates: Self-employed (Social Security and HI combined)	Maximum taxable earnings for Social Security and HI	Percent of workers with earnings below Social Security base	Percent of covered earnings below Social Security base
1937	1.000	—	—	$3,000	96.9	92.0
1950	1.500	—	—	3,000	71.1	79.7
1951	1.500	—	2.25	3,600	75.5	81.1
1952	1.500	—	2.25	3,600	72.1	80.5
1953	1.500	—	2.25	3,600	68.8	78.5
1954	2.000	—	3.0	3,600	68.4	77.7
1955	2.000	—	3.0	4,200	74.4	80.3
1956	2.000	—	3.0	4,200	71.6	78.8
1957	2.250	—	3.375	4,200	70.1	77.5
1958	2.250	—	3.375	4,200	69.4	76.4
1959	2.500	—	3.75	4,800	73.3	79.3
1960	3.000	—	4.5	4,800	72.0	78.1
1961	3.000	—	4.5	4,800	70.8	77.4
1962	3.125	—	4.7	4,800	68.8	75.8
1963	3.625	—	5.4	4,800	67.5	74.6
1964	3.625	—	5.4	4,800	65.5	72.8
1965	3.625	—	5.4	4,800	63.9	71.3
1966	3.850	0.35	6.15	6,600	75.8	80.0
1967	3.900	.5	6.4	6,600	73.6	78.1
1968	3.800	.6	6.4	7,800	78.6	81.7
1969	4.200	.6	6.9	7,800	75.5	80.1
1970	4.200	.6	6.9	7,800	74.0	78.2
1971	4.600	.6	7.5	7,800	71.7	76.3
1972	4.600	.6	7.5	9,000	75.0	78.3
1973	4.850	1.0	8.0	10,800	79.7	81.8
1974	4.950	.9	7.9	13,200	84.9	85.3
1975	4.950	.9	7.9	14,100	84.9	84.4
1976	4.950	.9	7.9	15,300	85.1	84.3
1977	4.950	.9	7.9	16,500	85.2	85.0
1978	5.050	1.0	8.1	17,700	84.6	83.8
1979	5.080	1.05	8.1	22,900	90.0	87.3
1980	5.080	1.05	8.1	25,900	91.2	88.9
1981	5.350	1.3	9.3	29,700	92.4	89.2
1982	5.400	1.3	9.35	32,400	92.9	90.0
1983	5.400	1.3	9.35	35,700	93.7	90.0
1984	5.700	1.3	14.0	37,800	93.6	89.3
1985	5.700	1.35	14.1	39,600	93.5	88.9

Year	Tax Rates: Social Security[a]	Tax Rates: HI[a]	Tax Rates: Self-employed (Social Security and HI combined)	Maximum taxable earnings for Social Security and HI	Percent of workers with earnings below Social Security base	Percent of covered earnings below Social Security base
1986	5.700	1.45	14.3	42,000	93.8	88.6
1987	5.700	1.45	14.3	43,800	93.9	87.6
1988	6.060	1.45	15.02	45,000	93.5	85.8
1989	6.060	1.45	15.02	48,000	93.8	86.8
1990	6.200	1.45	15.3	51,300	94.3	87.2
1991	6.200	1.45	15.3	53,400 (HI-125,000)	94.4	87.8
1992	6.200	1.45	15.3	55,500 (HI-130,200)	94.3	86.8
1993	6.200	1.45	15.3	57,600 (HI-135,000)	94.4	87.2
1994	6.200	1.45	15.3	60,600 (HI-no limit)	94.6	87.1
1995	6.200	1.45	15.3	61,200 (HI-no limit)	94.2	85.8
1996	6.200	1.45	15.3	62,700 (HI-no limit)	93.9	85.7
1997	6.200	1.45	15.3	65,400 (HI-no limit)	93.8	85.1
1998	6.200	1.45	15.3	68,400 (HI-no limit)	93.7	84.5
1999	6.200	1.45	15.3	72,600 (HI-no limit)	93.9	83.9
2000	6.200	1.45	15.3	76,200 (HI-no limit)	93.8	83.2
2001	6.200	1.45	15.3	80,400 (HI-no limit)	94.0**	84.7**
2002	6.200	1.45	15.3	84,900 (HI-no limit)	94.6**	86.1**
2003	6.200	1.45	15.3	87,000 (HI-no limit)	94.5**	86.1**
2004	6.200	1.45	15.3	87,900 (HI-no limit)	Not yet known	84.6**
2005	6.200	1.45	15.3	90,000 (HI-no limit)	Not yet known	Not yet known
2006	6.200	1.45	15.3	90,000 (HI-no limit)	Not yet known	Not yet known

Source: Social Security Bulletin, *Annual Statistical Supplement, 2005* at [http://www.ssa.gov/policy/docs/statcomps/supplement/2005].

a. Same for employer except 1984 — employees received 0.3% credit (not reflected above). Various credits also applied to self-employed (not reflected above) for 1984-1989 period.

**Estimates

Table 2. The Number and Percentage of Wage and Salary Workers with Social Security Taxable Earnings Over the Taxable Earnings Base of $84,900, by State, 2002

State	Total Number of wage and salary workers with Social Security taxable earnings[a]	Number and share of wage and salary workers with Social Security taxable earnings above the taxable earnings base	
		Number of workers	Percent of workers
U.S. Total	144,897,000	7,653,277	5.3%
Alabama	2,130,628	65,223	3.1%
Alaska	346,020	15,719	4.5%
Arizona	2,531,563	115,340	4.6%
Arkansas	1,298,648	29,294	2.3%
California	15,195,908	1,163,710	7.7%
Colorado	2,230,556	136,979	6.1%
Connecticut	1,808,594	165,559	9.2%
DC	339,182	33,581	9.9%
Delaware	465,239	22,149	4.8%
Florida	8,013,995	330,301	4.1%
Georgia	4,211,139	214,961	5.1%
Hawaii	635,391	20,516	3.2%
Idaho	658,970	16,638	2.5%
Illinois	6,167,226	386,032	6.3%
Indiana	3,316,386	118,198	3.6%
Iowa	1,583,528	39,808	2.5%
Kansas	1,470,229	54,302	3.7%
Kentucky	2,010,899	55,322	2.8%
Louisiana	1,976,501	59,303	3.0%
Maine	661,419	18,781	2.8%
Maryland	2,920,249	205,571	7.0%
Massachusetts	3,190,226	269,978	8.5%
Michigan	5,259,305	291,208	5.5%
Minnesota	2,842,981	149,126	5.2%
Missouri	2,897,079	97,886	3.4%
Montana	466,362	8,676	1.9%
Nebraska	957,935	27,253	2.8%
Nevada	1,046,737	36,643	3.5%
New Hampshire	716,538	50,117	7.0%
New Jersey	4,489,895	460,136	10.2%
New Mexico	854,231	25,416	3.0%
New York	9,252,013	700,921	7.6%
North Carolina	4,213,589	160,762	3.8%
North Dakota	339,590	5,206	1.5%
Ohio	5,629,108	234,865	4.2%
Oklahoma	1,698,358	42,870	2.5%
Oregon	1,763,683	73,593	4.2%
Pennsylvania	6,366,571	303,457	4.8%
Puerto Rico	1,099,202	12,146	1.1%
Rhode Island	578,334	27,151	4.7%
South Carolina	2,041,520	64,509	3.2%
South Dakota	416,041	6,328	1.5%
Tennessee	2,921,371	101,663	3.5%
Texas	9,794,622	528,625	5.4%
Utah	1,166,977	35,725	3.1%
Vermont	351,736	10,615	3.0%

State	Total Number of wage and salary workers with Social Security taxable earnings[a]	Number and share of wage and salary workers with Social Security taxable earnings above the taxable earnings base	
		Number of workers	Percent of workers
Virgin Islands	42,666	1,225	2.9%
Virginia	3,905,437	254,871	6.5%
Washington	3,100,506	169,846	5.5%
West Virginia	820,854	16,025	2.0%
Wisconsin	3,061,719	104,419	3.4%
Wyoming	277,327	6,839	2.5%
Other	1,998,242	82,371	4.1%

Source: SSA, custom tabulation based on the 1% sample file, estimated for 2002.

a. Does not include workers with only self-employment income.

Table 3. Number and Percentage of Workers Above the Taxable Earnings Base of $87,000, by Type of Earnings and Sex, 2003

	Number[a] (in thousands)	Percent of group in total	Percent of group above the taxable maximum
All workers	8,491	100%	6%
Men	6,656	78%	8%
Women	1,832	22%	3%
All wage and salary workers	7,923	93%	5%
Men	6,220	73%	8%
Women	1,703	20%	2%
All self-employed	765	9%	5%
Men	624	7%	7%
Women	140	2%	2%

Source: Social Security Bulletin, *Annual Statistical Supplement, 2005* at [http://www.ssa.gov/policy/docs/statcomps/supplement/2005]. (CRS calculations based on 2003 estimates from tables, 4.B1,4.B4, 4.B7, and 4B.9).

a. Workers with earnings in both wage and salary employment and self-employment are counted in each type of employment but only once in the total.