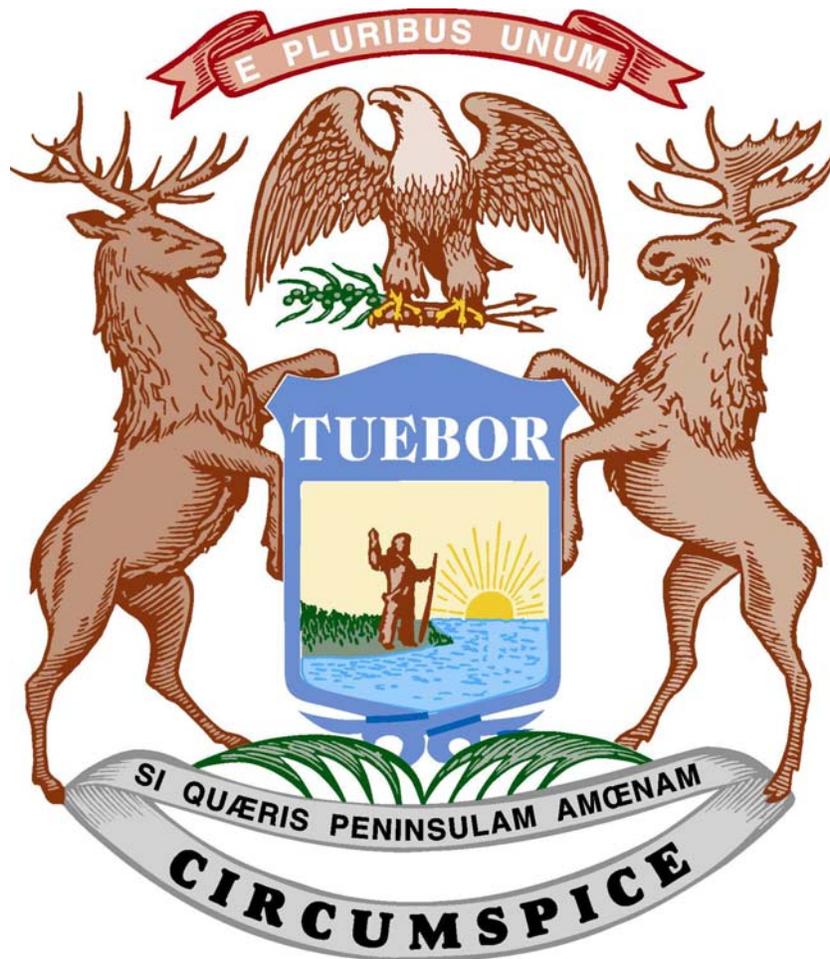
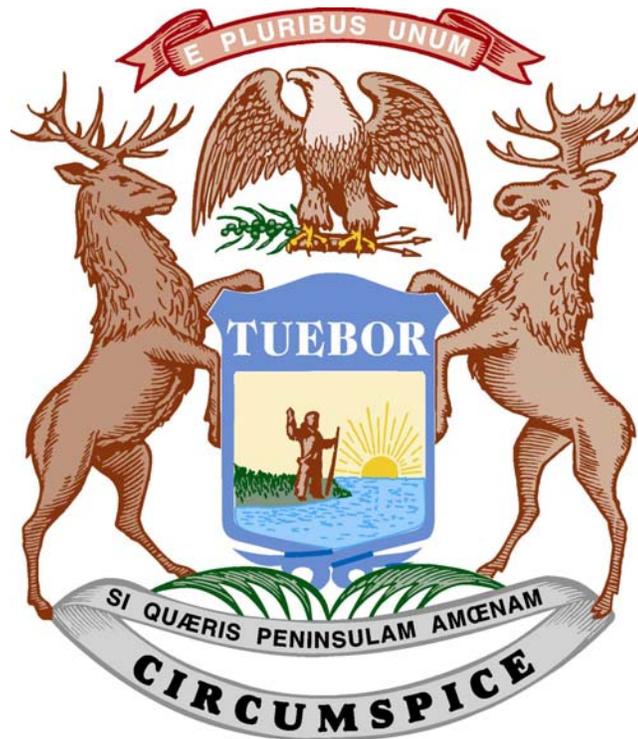


The Effects of an Aging Population on the Components of Michigan Income



Michigan Department of Treasury
Office of Revenue and Tax Analysis
August 2009

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This report was written and compiled by Andrew Lockwood and Eric Krupka under the direction of Howard Heideman, Director, Tax Analysis Division, Michigan Department of Treasury and Jeffrey Guilfoyle, Director of the Office of Revenue and Tax Analysis.

This report is available electronically at the Department of Treasury's Web site:
<http://www.michigan.gov/treasury>.

Key Finding

The dynamics between income characteristics and tax preferences that exclude senior income sources from taxation suggest that Michigan Income Tax revenue collections may be weakened as the population ages.

Summary

- Senior population (age 65 and older) is increasing.
 1. Senior population is projected to grow from 1.2 million in 2000 to 2.1 million in 2030 (+71%)
 2. Non-senior population is projected to decrease from 8.7 million in 2000 to 8.6 million in 2030 (-1%)
- Senior taxpayers earn lower wages.
 1. Seniors earned an average \$8,746 in wage income compared to \$41,619 for non-seniors in 2004
 2. Wages are a non-exempt income source and comprise the largest percentage of taxable income.
- Pensions, which are generally exempted from Michigan taxation, are an important source of income for seniors.
 1. Seniors received an average of \$12,530 in taxable pension income compared to \$1,772 non-seniors in 2004.
 2. Michigan exempts State, local, and federal pensions income from taxation.
 3. Michigan exempted most private pension income from taxation (Single-\$43,440, Joint-\$86,880) in tax year 2008.
- Senior citizens receive additional exclusions from taxation.
 1. Seniors received \$4,665 in federally taxable Social Security income on average compared to \$167 for non-seniors in 2004.
 2. Michigan exempts all federally taxable Social Security income from taxation.
 3. On average, seniors earned \$12,038 in capital gains, interest and dividends compared to \$2,137 for non-seniors.
 4. Michigan exempted a portion of senior capital gains, interest and dividend income (Single-\$9,690, Joint-\$19,380) in tax year 2008.

Introduction

Nationally, the number of people 65 and older is increasing each year due to the aging of the Baby Boom Generation and increased life expectancy. According to a U.S. Census report, the 65 plus population in 2030 is forecast to be over twice as large as in the 2000 Census, growing from 35 million to 72 million.

Michigan's population is also projected to get older over time. The median age of a Michigan resident was 35.5 years for the 2000 Census and is projected to rise to 37.8 years in 2015 and to 40.2 years in 2030. Michigan persons aged 65 years and older totaled 1.219 million during the 2000 Census and is projected to rise to 2.080 million in 2030, an increase of 70.7 percent. From 2000 to 2030, the total Michigan population is projected to rise 7.6 percent.

Labor force participation, increased consumption of medical services and services in general, and types of income earned by an older population will affect the United States and Michigan economically and fiscally for many years to come.

This report will show how income is earned by age, income tax preferences for certain types of income and how Michigan income tax revenue may be affected by an aging population. Because of income tax exemptions and income exclusions, the aging of Michigan's population will affect how much income tax is collected. Exhibit 1 provides a brief summary of the main features for the 2008 Michigan individual income tax.

Exhibit 1 Michigan 2008 Individual Income Tax Features

<u>Feature</u>	<u>Description</u>
Starting Point	Federal AGI
Income Tax Rate	4.35%
Personal Exemption	\$3,500
Senior Exemption	\$2,200
Child Exemption	\$600
Private Pension Exclusion	\$43,440 single/\$86,800 joint
Public Pension Exclusion	Exempt
Interest, Dividends, Cap. Gain Exclusion	\$9,690 single/\$19,380 joint
Homestead Property Tax Credit	\$1,200 maximum
Earned Income Tax Credit	10% of Federal Credit

For the Michigan individual income tax, the beginning point is federal adjusted gross income (AGI). The tax rate is currently a flat rate of 4.35 percent, and the tax rate is scheduled to decrease by 0.1 percent every fiscal year starting in FY 2012 until the rate reaches 3.95 percent. In FY 2016, the rate is lowered to 3.9 percent. Senior citizens qualify for the personal exemption of \$3,500 in 2008 and a special senior exemption of \$2,200.

For 2008, private pension income is exempted up to \$43,440 on a single return and up to \$86,800 on a joint return. All pension income earned from the State of Michigan, Michigan local governmental units, federal civil service and military retirement pay is exempted from the

income tax. Out-of-state government pensions are not fully exempt but qualify for the private pension exclusion. The private pension exclusion is indexed to inflation.

Michigan also exempts a portion of interest, dividend and capital gains income for persons age 65 and older. For 2008, this exclusion is for up to \$9,690 for a single filer and up to \$19,380 for a joint filer and must be reduced by any private pension income claimed for exclusion by the taxpayer. The interest, dividend, and capital gains exclusion is indexed to inflation. Michigan also exempts Social Security benefits taxable at the federal level from the state income tax.

The Michigan income tax has many refundable and non-refundable credits available to taxpayers. The homestead property tax credit and newly enacted Michigan earned income tax credit are two of the largest and will be discussed later. A brief discussion of sales tax revenue and spending patterns of seniors will also be mentioned.

The data used for this report are from tax year 2004. These data are the latest federal comprehensive data set available to analyze. The income statistics are reported by age of taxpayer. The age of the head of household was used to compile the totals.

Income by Age

Exhibit 2 provides a summary of the components of federal total income by age for tax year 2004. As discussed above, the starting point for the Michigan Individual Income Tax is federal AGI which is federal total income less adjustments. AGI will be discussed later. Wage income comprises the majority of Michigan federal total income at 74.2 percent in 2004. Federally taxable pensions are next at 7.1 percent of total federal total income. Other sources of income such as interest and dividends, capital gains and Social Security each account for under 5 percent of total federal income.

However, the income shares vary greatly for the 65 and older population (see Exhibit 3) compared to the state average. Taxable pensions comprise 28.1 percent of total income for Michigan persons age 65 and above. Average taxable pension income for the age group 65 years and above is \$12,530 compared to non-seniors at \$1,772 and the all taxpayer average of \$3,472.

Wages are 19.6 percent of total income for people 65 and above, far below the Michigan average of 74.2 percent. Michigan average wage income was \$36,398 compared to \$8,746 for those 65 years and above. As people retire, wages will make up a lower percentage of income. People between 65 and 74 have wages that make up 29.6 percent of income which goes to near zero (2.5 percent) for persons aged 85 years and above.

Other types of income become more important as a person ages. Interest and dividends for persons 65 years and above become a much larger piece of income compared to other age groups. Interest and dividends make up 15.1 percent of total federal total income for seniors while the Michigan average is 3.7 percent. For younger age brackets (25 years to 44 years), interest and dividends combined make up less than 1 percent of total federal total income.

Capital gains income also rises as a percentage of federal total income as Michigan taxpayers turn older. Capital gains comprise 11.9 percent of total federal total income for seniors compared to the average of 3.7 percent for all taxpayers.

Exhibit 2
Income Sources for Michigan Taxpayers by Age, 2004 Federal Income Tax

Age Group	Number of Returns	Income Sources by Age						Income Sources by Age					Total Income
		Wages	Taxable Interest	Dividends	(Schedule C) Business Income	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E) Passive Income	Taxable Social Security	Miscellaneous Income		
Under 25 Yrs	746,089	\$7,455,165,649	\$49,621,394	\$53,903,310	\$124,077,775	\$22,337,506	\$4,646,187	\$18,176,263	\$82,200,328	\$730,069	\$147,335,815	\$7,958,194,296	
25 to 34 Yrs	690,118	\$23,779,218,546	\$60,061,008	\$50,293,853	\$510,305,020	\$98,830,198	\$40,599,384	\$143,903,321	\$209,116,586	\$5,746,776	\$451,199,513	\$25,349,274,205	
35 to 44 Yrs	818,813	\$42,617,415,672	\$213,671,645	\$228,372,606	\$1,354,842,873	\$623,206,885	\$159,975,262	\$392,279,051	\$1,542,064,113	\$35,424,086	\$683,889,567	\$47,851,141,760	
45 to 54 Yrs	845,476	\$50,089,091,079	\$543,806,747	\$672,445,408	\$1,851,960,666	\$1,864,981,577	\$312,804,559	\$1,064,185,575	\$2,781,556,292	\$119,280,629	\$812,927,103	\$60,113,039,635	
55 to 64 Yrs	615,334	\$30,708,071,215	\$750,131,799	\$769,244,127	\$1,414,505,832	\$1,942,016,929	\$822,837,398	\$4,964,754,379	\$2,104,023,615	\$460,682,827	\$597,000,516	\$44,533,268,637	
65 to 74 Yrs	347,923	\$5,286,919,659	\$764,751,833	\$751,141,533	\$423,032,750	\$1,618,269,542	\$1,232,323,230	\$4,710,296,725	\$983,704,765	\$1,898,830,071	\$213,657,207	\$17,882,927,315	
75 to 84 Yrs	251,230	\$771,411,942	\$867,620,208	\$1,409,633,193	\$82,075,992	\$1,578,984,827	\$922,680,560	\$3,137,202,792	\$526,296,693	\$1,058,167,558	(\$34,787,173)	\$10,319,286,592	
85 and Over	102,180	\$75,193,585	\$465,298,549	\$472,482,398	\$10,425,330	\$514,068,451	\$107,444,936	\$940,152,692	\$114,964,041	\$307,401,911	\$8,975,463	\$3,016,407,356	
Missing Age	14,310	\$512,579,686	\$22,230,378	\$4,102,387	\$13,584,968	(\$282,297,499)	\$3,804,051	\$16,454,900	\$14,704,165	\$3,925,153	\$3,860,546	\$312,948,735	
Totals	4,431,473	\$161,295,067,033	\$3,737,193,561	\$4,411,618,815	\$5,784,811,206	\$7,980,398,416	\$3,607,115,567	\$15,387,405,698	\$8,358,630,598	\$3,890,189,080	\$2,884,058,557	\$217,336,488,531	

Age Group	Number of Returns	Income Source Shares by Age						Income Source Shares by Age					Total Income
		Wages	Taxable Interest	Dividends	(Schedule C) Business Income	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E) Passive Income	Taxable Social Security	Miscellaneous Income		
Under 25 Yrs	16.8%	93.7%	0.6%	0.7%	1.6%	0.3%	0.1%	0.2%	1.0%	0.0%	1.9%	100.0%	
25 to 34 Yrs	15.6%	93.8%	0.2%	0.2%	2.0%	0.4%	0.2%	0.6%	0.8%	0.0%	1.8%	100.0%	
35 to 44 Yrs	18.5%	89.1%	0.4%	0.5%	2.8%	1.3%	0.3%	0.8%	3.2%	0.1%	1.4%	100.0%	
45 to 54 Yrs	19.1%	83.3%	0.9%	1.1%	3.1%	3.1%	0.5%	1.8%	4.6%	0.2%	1.4%	100.0%	
55 to 64 Yrs	13.9%	69.0%	1.7%	1.7%	3.2%	4.4%	1.8%	11.1%	4.7%	1.0%	1.3%	100.0%	
65 to 74 Yrs	7.9%	29.6%	4.3%	4.2%	2.4%	9.0%	6.9%	26.3%	5.5%	10.6%	1.2%	100.0%	
75 to 84 Yrs	5.7%	7.5%	8.4%	13.7%	0.8%	15.3%	8.9%	30.4%	5.1%	10.3%	-0.3%	100.0%	
85 and Over	2.3%	2.5%	15.4%	15.7%	0.3%	17.0%	3.6%	31.2%	3.8%	10.2%	0.3%	100.0%	
Missing Age	0.3%	163.8%	7.1%	1.3%	4.3%	-90.2%	1.2%	5.3%	4.7%	1.3%	1.2%	100.0%	
Totals	100.0%	74.2%	1.7%	2.0%	2.7%	3.7%	1.7%	7.1%	3.8%	1.8%	1.3%	100.0%	

Age Group	Number of Returns	Average Income by Source and Age						Average Income by Source and Age					Total Income
		Wages	Taxable Interest	Dividends	(Schedule C) Business Income	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E) Passive Income	Taxable Social Security	Miscellaneous Income		
Under 25 Yrs	746,089	\$9,992	\$67	\$72	\$166	\$30	\$6	\$24	\$110	\$1	\$197	\$10,667	
25 to 34 Yrs	690,118	\$34,457	\$87	\$73	\$739	\$143	\$59	\$209	\$303	\$8	\$654	\$36,732	
35 to 44 Yrs	818,813	\$52,048	\$261	\$279	\$1,655	\$761	\$195	\$479	\$1,883	\$43	\$835	\$58,440	
45 to 54 Yrs	845,476	\$59,244	\$643	\$795	\$2,190	\$2,206	\$370	\$1,259	\$3,290	\$141	\$962	\$71,100	
55 to 64 Yrs	615,334	\$49,905	\$1,219	\$1,250	\$2,299	\$3,156	\$1,337	\$8,068	\$3,419	\$749	\$970	\$72,373	
65 to 74 Yrs	347,923	\$15,196	\$2,198	\$2,159	\$1,216	\$4,651	\$3,542	\$13,538	\$2,827	\$5,458	\$614	\$51,399	
75 to 84 Yrs	251,230	\$3,071	\$3,453	\$5,611	\$327	\$6,285	\$3,673	\$12,487	\$2,095	\$4,212	(\$138)	\$41,075	
85 and Over	102,180	\$736	\$4,554	\$4,624	\$102	\$5,031	\$1,052	\$9,201	\$1,125	\$3,008	\$88	\$29,521	
Missing Age	14,310	\$35,820	\$1,553	\$287	\$949	(\$19,727)	\$266	\$1,150	\$1,028	\$274	\$270	\$21,869	
Totals	4,431,473	\$36,398	\$843	\$996	\$1,305	\$1,801	\$814	\$3,472	\$1,886	\$878	\$651	\$49,044	

Note: Miscellaneous Income includes state and local tax refunds, alimony, other income and farm income

Exhibit 3
Income Sources for Michigan Taxpayers 65 and Older, 2004 Federal Income Tax

Income Sources by Age

Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E)	Taxable Social Security	Miscellaneous Income	Total Income
					Business Income				Passive Income			
65 to 74 Yrs	347,923	\$5,286,919,659	\$764,751,833	\$751,141,533	\$423,032,750	\$1,618,269,542	\$1,232,323,230	\$4,710,296,725	\$983,704,765	\$1,898,830,071	\$213,657,207	\$17,882,927,315
75 to 84 Yrs	251,230	\$771,411,942	\$867,620,208	\$1,409,633,193	\$82,075,992	\$1,578,984,827	\$922,680,560	\$3,137,202,792	\$526,296,693	\$1,058,167,558	(\$34,787,173)	\$10,319,286,592
85 and Over	102,180	\$75,193,585	\$465,298,549	\$472,482,398	\$10,425,330	\$514,068,451	\$107,444,936	\$940,152,692	\$114,964,041	\$307,401,911	\$8,975,463	\$3,016,407,356
Totals	701,333	\$6,133,525,186	\$2,097,670,590	\$2,633,257,124	\$515,534,072	\$3,711,322,820	\$2,262,448,726	\$8,787,652,209	\$1,624,965,499	\$3,264,399,540	\$187,845,497	\$31,218,621,263

Income Source Shares by Age

Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E)	Taxable Social Security	Miscellaneous Income	Total Income
					Business Income				Passive Income			
65 to 74 Yrs	49.6%	29.6%	4.3%	4.2%	2.4%	9.0%	6.9%	26.3%	5.5%	10.6%	1.2%	100.0%
75 to 84 Yrs	35.8%	7.5%	8.4%	13.7%	0.8%	15.3%	8.9%	30.4%	5.1%	10.3%	-0.3%	100.0%
85 and Over	14.6%	2.5%	15.4%	15.7%	0.3%	17.0%	3.6%	31.2%	3.8%	10.2%	0.3%	100.0%
Totals	100.0%	19.6%	6.7%	8.4%	1.7%	11.9%	7.2%	28.1%	5.2%	10.5%	0.6%	100.0%

Average Income by Source and Age

Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)	Capital Gains	Taxable IRA Distributions	Taxable Pensions	(Schedule E)	Taxable Social Security	Miscellaneous Income	Total Income
					Business Income				Passive Income			
65 to 74 Yrs	347,923	\$15,196	\$2,198	\$2,159	\$1,216	\$4,651	\$3,542	\$13,538	\$2,827	\$5,458	\$614	\$51,399
75 to 84 Yrs	251,230	\$3,071	\$3,453	\$5,611	\$327	\$6,285	\$3,673	\$12,487	\$2,095	\$4,212	(\$138)	\$41,075
85 and Over	102,180	\$736	\$4,554	\$4,624	\$102	\$5,031	\$1,052	\$9,201	\$1,125	\$3,008	\$88	\$29,521
Totals	701,333	\$8,746	\$2,991	\$3,755	\$735	\$5,292	\$3,226	\$12,530	\$2,317	\$4,655	\$268	\$44,513

Note: Miscellaneous Income includes state and local tax refunds, alimony, other income and farm income

Exhibit 4
Income Sources for Michigan Taxpayers Under 65 Years Old, 2004 Federal Income Tax

Income Sources by Age													
Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)			Taxable IRA Distributions	Taxable Pensions	(Schedule E)		Miscellaneous Income	Total Income
					Business Income	Capital Gains	Taxable Social Security			Passive Income			
Under 25 Yrs	746,089	\$7,455,165,649	\$49,621,394	\$53,903,310	\$124,077,775	\$22,337,506	\$4,646,187	\$18,176,263	\$82,200,328	\$730,069	\$147,335,815	\$7,958,194,296	
25 to 34 Yrs	690,118	\$23,779,218,546	\$60,061,008	\$50,293,853	\$510,305,020	\$98,830,198	\$40,599,384	\$143,903,321	\$209,116,586	\$5,746,776	\$451,199,513	\$25,349,274,205	
35 to 44 Yrs	818,813	\$42,617,415,672	\$213,671,645	\$228,372,606	\$1,354,842,873	\$623,206,885	\$159,975,262	\$392,279,051	\$1,542,064,113	\$35,424,086	\$683,889,567	\$47,851,141,760	
45 to 54 Yrs	845,476	\$50,089,091,079	\$543,806,747	\$672,445,408	\$1,851,960,666	\$1,864,981,577	\$312,804,559	\$1,064,185,575	\$2,781,556,292	\$119,280,629	\$812,927,103	\$60,113,039,635	
55 to 64 Yrs	615,334	\$30,708,071,215	\$750,131,799	\$769,244,127	\$1,414,505,832	\$1,942,016,929	\$822,837,398	\$4,964,754,379	\$2,104,023,615	\$460,682,827	\$597,000,516	\$44,533,268,637	
Totals	3,715,830	\$154,648,962,161	\$1,617,292,593	\$1,774,259,304	\$5,255,692,166	\$4,551,373,095	\$1,340,862,790	\$6,583,298,589	\$6,718,960,934	\$621,864,387	\$2,692,352,514	\$185,804,918,533	

Income Source Shares by Age													
Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)			Taxable IRA Distributions	Taxable Pensions	(Schedule E)		Miscellaneous Income	Total Income
					Business Income	Capital Gains	Taxable Social Security			Passive Income			
Under 25 Yrs	20.1%	93.7%	0.6%	0.7%	1.6%	0.3%	0.1%	0.2%	1.0%	0.0%	1.9%	100.0%	
25 to 34 Yrs	18.6%	93.8%	0.2%	0.2%	2.0%	0.4%	0.2%	0.6%	0.8%	0.0%	1.8%	100.0%	
35 to 44 Yrs	22.0%	89.1%	0.4%	0.5%	2.8%	1.3%	0.3%	0.8%	3.2%	0.1%	1.4%	100.0%	
45 to 54 Yrs	22.8%	83.3%	0.9%	1.1%	3.1%	3.1%	0.5%	1.8%	4.6%	0.2%	1.4%	100.0%	
55 to 64 Yrs	16.6%	69.0%	1.7%	1.7%	3.2%	4.4%	1.8%	11.1%	4.7%	1.0%	1.3%	100.0%	
Totals	100.0%	83.2%	0.9%	1.0%	2.8%	2.4%	0.7%	3.5%	3.6%	0.3%	1.4%	100.0%	

Average Income by Source and Age													
Age Group	Number of Returns	Wages	Taxable Interest	Dividends	(Schedule C)			Taxable IRA Distributions	Taxable Pensions	(Schedule E)		Miscellaneous Income	Total Income
					Business Income	Capital Gains	Taxable Social Security			Passive Income			
Under 25 Yrs	746,089	\$9,992	\$67	\$72	\$166	\$30	\$6	\$24	\$110	\$1	\$197	\$10,667	
25 to 34 Yrs	690,118	\$34,457	\$87	\$73	\$739	\$143	\$59	\$209	\$303	\$8	\$654	\$36,732	
35 to 44 Yrs	818,813	\$52,048	\$261	\$279	\$1,655	\$761	\$195	\$479	\$1,883	\$43	\$835	\$58,440	
45 to 54 Yrs	845,476	\$59,244	\$643	\$795	\$2,190	\$2,206	\$370	\$1,259	\$3,290	\$141	\$962	\$71,100	
55 to 64 Yrs	615,334	\$49,905	\$1,219	\$1,250	\$2,299	\$3,156	\$1,337	\$8,068	\$3,419	\$749	\$970	\$72,373	
Totals	3,715,830	\$41,619	\$435	\$477	\$1,414	\$1,225	\$361	\$1,772	\$1,808	\$167	\$725	\$50,004	

Note: Miscellaneous Income includes state and local tax refunds, alimony, other income and farm income

As expected, taxable Social Security benefits make up a greater percentage of income as age increases. For persons aged 65 years and older, taxable Social Security income comprises 10.5 percent of total federal income. For person under 54 years of age, taxable Social Security benefits as a percentage of income is near zero.

Federal total income declines as taxpayers age. The overall Michigan average is \$49,044, while the average for ages 65 years and above is \$44,513. As shown by Exhibit 3, total income decreases significantly for ages 85 years and above to \$29,521.

The age groups with the highest total income are the age groups 45 years to 54 years and 55 years to 64 years. Exhibit 4 provides a breakout of income for age groups under 65 years old. The cohort ages 55 years to 64 years has the highest average total of income of \$72,373 followed closely by the 45 years to 54 years cohort with an average of \$71,100.

The composition of income for age groups 45 years to 54 years and 55 years to 64 years is also important. Wage income as a percentage of total income decreases and other forms of retirement income begin to increase. For the age group 45 years to 54 years, wages comprise 83.3 percent of total income but that percentage falls to 69.0 percent for the age group 55 years to 64 years. As people near retirement contributions to 401(k) plans, which are tax-deferred and reduce wage income, tend to increase for those still working. Taxable pensions as a percent of total income rises significantly from 1.8 percent for the 45 year to 54 year group to 11.1 percent for the 55 year to 64 year group.

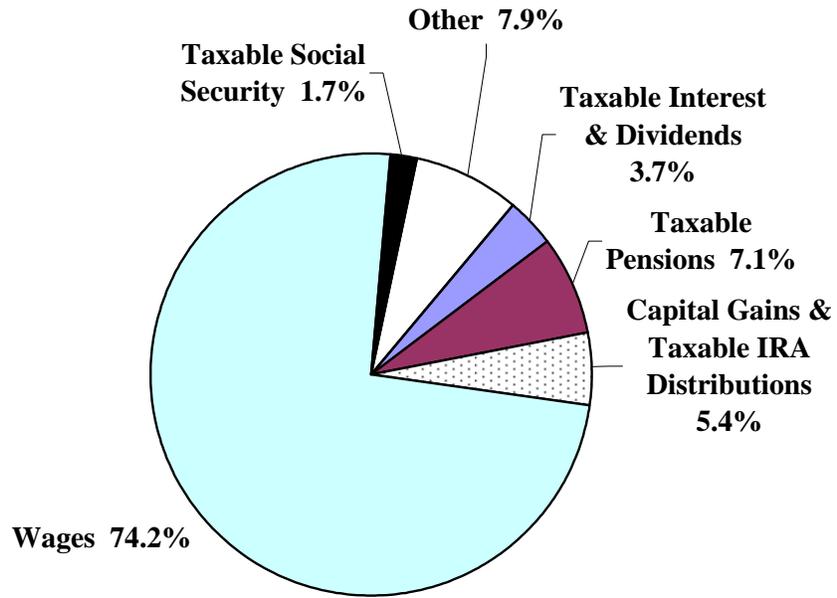
Exhibit 5 shows the percentage of federal total income by category for Michigan. Exhibit 6 shows the percentage of federal total income by category for taxpayers ages 45 years to 54 years. Exhibit 7 shows the percentage of federal total income by category for taxpayers ages 55 years to 64 years. Exhibit 8 provides data on the percentage of total federal income for persons 65 years old and above. Exhibit 6 through Exhibit 8 shows the changing of income composition as the Michigan taxpayers age.

Exhibit 9 shows the share of federal total income for Michigan taxpayers 65 years and older. People 65 years and older comprise 15.8 percent of all tax returns and make up 14.4 percent of total income. As we would expect, older residents have a higher percentage of income that is associated with retirement income.

Persons aged 65 years and older receive 83.9 percent of total taxable Social Security income in Michigan. This age group has 62.7 percent of taxable IRA distribution income, 57.1 percent of total taxable pensions, 59.7 percent of dividends and 56.1 percent of taxable interest. Wages are a much smaller percentage at 3.8 percent of the statewide total.

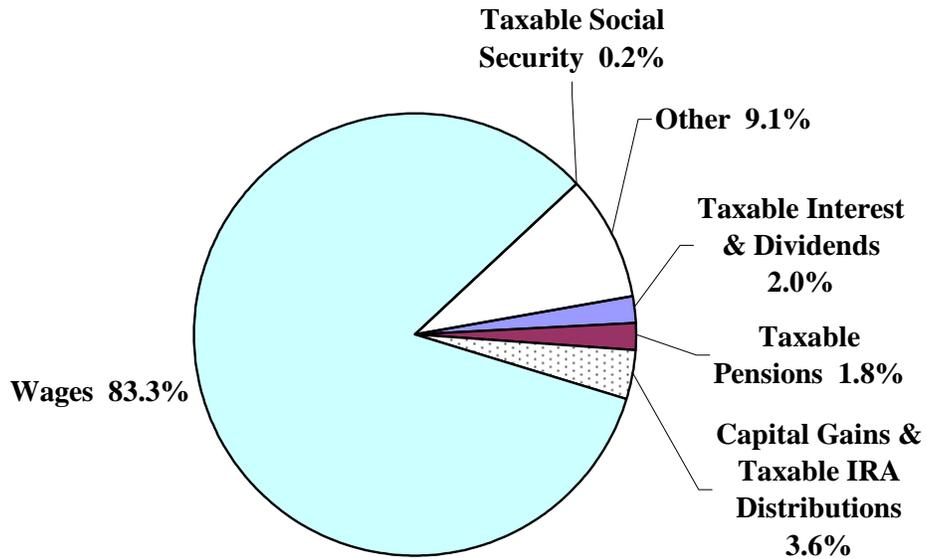
Persons 65 years and older have \$31.2 billion of federal total income compared to the statewide total of \$217.3 billion, or 14.4 percent. People 65 and over comprised approximately 12.3 percent of population. Taxpayers 65 years and older received \$8.8 billion in taxable pension income while the Michigan total was \$15.4 billion, or 57.1 percent of the total.

Exhibit 5
Wages Comprise Highest Percentage of Federal Total Income for All Taxpayers



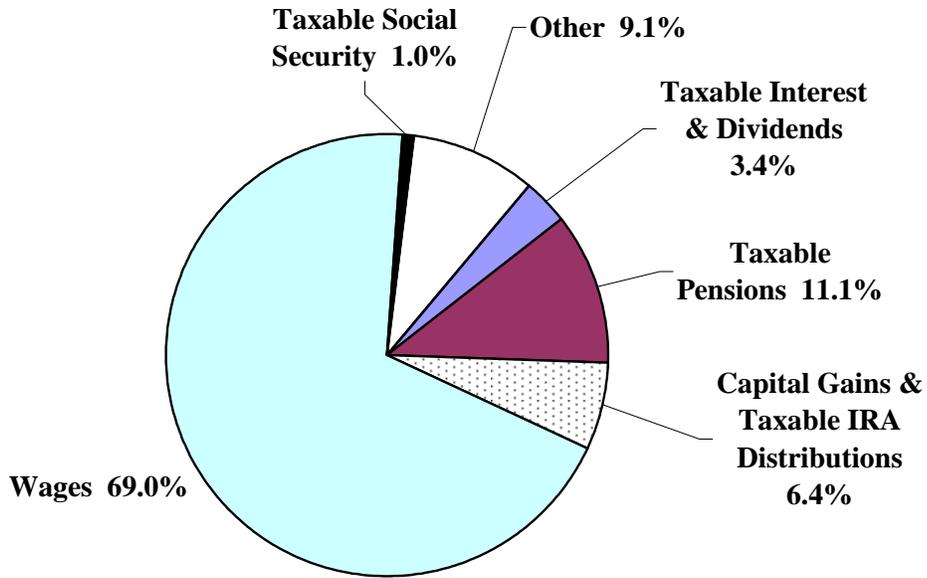
Source: Michigan Department of Treasury.

Exhibit 6
Wage Income Largest Source of Federal Total Income for Age Group 45 years to 54 years



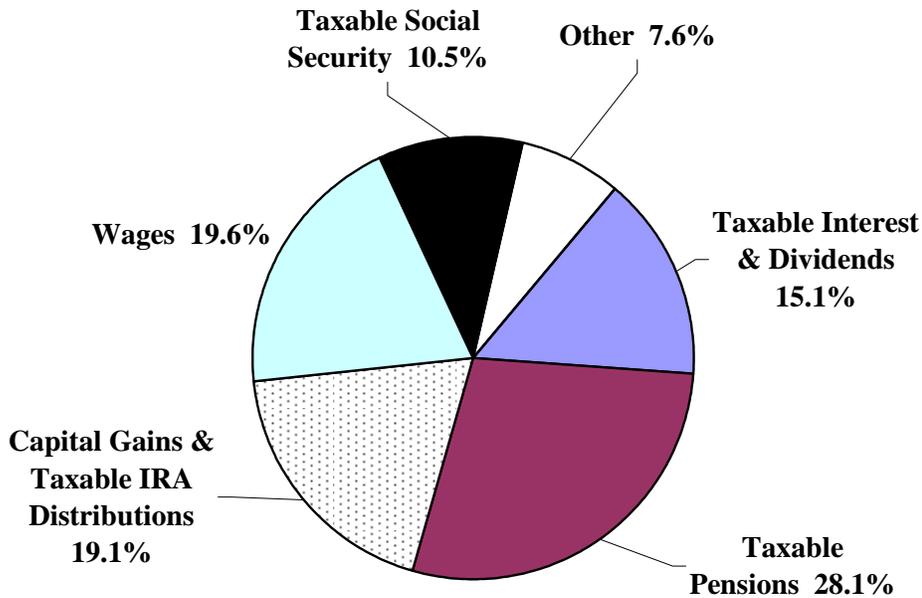
Source: Michigan Department of Treasury.

Exhibit 7
Other Types of Income Increase for Age Group 55 years to 64 years



Source: Michigan Department of Treasury.

Exhibit 8
Michigan Senior Taxpayers Sources of Federal Total Income Vary Widely
Taxable Pension Income Highest for People 65 Years Old and Above



Source: Michigan Department of Treasury.

Exhibit 9
Older Taxpayers Have a Greater Share of Non-Wage Income
Components of Federal Total Income, Tax Year 2004

<u>Item</u>	<u>Amount of Income</u>		<u>Percent of</u>
	<u>65 and Older</u>	<u>All Ages</u>	<u>Total</u>
Wages	\$6,133,525,186	\$161,295,067,033	3.8%
Taxable Interest	\$2,097,670,590	\$3,737,193,561	56.1%
Dividends	\$2,633,257,124	\$4,411,618,815	59.7%
Business Income (Schedule C)	\$515,534,072	\$5,784,811,206	8.9%
Capital Gains	\$3,711,322,820	\$7,980,398,416	46.5%
Taxable IRA Distributions	\$2,262,448,726	\$3,607,115,567	62.7%
Taxable Pensions	\$8,787,652,209	\$15,387,405,698	57.1%
Passive Income (Schedule E)	\$1,624,965,499	\$8,358,630,598	19.4%
Taxable Social Security	\$3,264,399,540	\$3,890,189,080	83.9%
Miscellaneous Income	<u>\$187,845,497</u>	<u>\$2,884,058,557</u>	<u>6.5%</u>
Total Income	\$31,218,621,263	\$217,336,488,531	14.4%

65 plus residents make up 15.8% of all returns

All Ages includes missing returns

Exhibit 10
Federal Adjusted Gross Income for All Taxpayers by Age

<u>Age Group</u>	<u>Returns</u>	<u>Total Income</u>	<u>Adjustments to Income</u>	<u>Adjusted Gross Income</u>
Under 25 Yrs	746,089	\$7,958,194,296	(\$51,657,617)	\$7,906,536,679
25 to 34 Yrs	690,118	\$25,349,274,205	(\$221,238,095)	\$25,128,036,110
35 to 44 Yrs	818,813	\$47,851,141,760	(\$414,199,410)	\$47,436,942,350
45 to 54 Yrs	845,476	\$60,113,039,635	(\$800,377,782)	\$59,312,661,853
55 to 64 Yrs	615,334	\$44,533,268,637	(\$681,395,597)	\$43,851,873,040
65 to 74 Yrs	347,923	\$17,882,927,315	(\$193,082,254)	\$17,689,845,061
75 to 84 Yrs	251,230	\$10,319,286,592	(\$338,351,682)	\$9,980,934,910
85 and Over	102,180	\$3,016,407,356	(\$106,639,979)	\$2,909,767,377
Missing Age	14,310	\$312,948,735	\$482,830,657	\$795,779,392
Totals	4,431,473	\$217,336,488,531	(\$2,324,111,759)	\$215,012,376,772

As noted earlier, the starting point for the Michigan individual income tax is federal AGI, which is federal total income less adjustments. Adjustments include deductions for moving expenses, health savings account deduction, self employed retirement plans among others for determining federal AGI. Exhibit 10 provides federal AGI by age for tax year 2004.

State Taxation of Retirement Income

Forty-three states and the District of Columbia levy an income tax. Of those forty-three states, forty-one levy a broad based income tax. The following information is taken from the Wisconsin Legislative Fiscal Bureau’s report, *Individual Income Tax Provisions in the States*, published in January 2009.

Many states provide exemptions for private pension income with four states (Mississippi, New Hampshire, Pennsylvania, Tennessee) totally exempting private pension income. Of states that do not fully exempt private pension income, Michigan has the largest exclusion in tax year 2007 (see Exhibit 11).

**Exhibit 11
Tax Year 2007 Private Pension Income Exclusion by State
States with Largest Exclusion Per Person**

<u>State</u>	<u>Private Pension Exclusion</u>
Michigan	\$42,240
Kentucky	\$41,110
Georgia	\$30,000
Colorado	\$24,000
Maryland	\$23,600
New York	\$20,000

There are a total of sixteen states that do not exempt private pension income at all. Four states exempt all pension income. Exhibit 12 provides information on how states tax different type of retirement income. While Michigan exempts public pension income, eight states (California, Connecticut, Minnesota, Nebraska, New Mexico, Rhode Island, Vermont, Virginia) do tax this type of income. Also, the same eight states tax federal retirement income. While Michigan exempts military retirement income, seven states tax this type of retirement income.

Michigan is one of twenty-six states that levy a broad based income tax that does not tax Social Security benefits. According to AARP, fifteen states do tax Social Security benefits at the state level. Some states that tax Social Security benefits have taken measures to lessen the tax by phasing out taxation of these benefits and allowing Social Security benefits to be included as part of their state retirement income exemption.

Michigan provides greater relief for pension income from in-state government plans than out of state government plans. In-state government plans are fully exempt while out-of-state government plans receive the private pension exclusion. Michigan does not tax public pensions from other states if those states do not tax residents that receive a Michigan government pension.

Exhibit 12
State Tax Exclusions for Pension/Retirement Income
Tax Year 2007

<u>State</u>	<u>Private</u>	<u>State & Local</u>	<u>Federal Civilian</u>	<u>Military</u>
Alabama	State Calculation	Most exempt	Exempt	Exempt
Arizona	None	\$2,500	\$2,500	\$2,500
Arkansas	\$6,000	\$6,000	\$6,000	\$6,000
California	None	None	None	None
Colorado	\$20,000/\$24,000	\$20,000/\$24,000	\$20,000/\$24,000	\$20,000/\$24,000
Connecticut	None	None	None	None
Delaware	\$2,000/\$12,500	\$2,000/\$12,500	\$2,000/\$12,500	\$2,000/\$12,500
District of Columbia	None	\$3,000	\$3,000	\$3,000
Georgia	\$30,000	\$30,000	\$30,000	\$30,000
Hawaii	State Calculation	Exempt	Exempt	Exempt
Idaho	None	\$25,392/\$38,088 ^a	\$25,392/\$38,088	\$25,392/\$38,088
Illinois	State Calculation	Exempt	Exempt	Exempt
Indiana	None/\$5,200	None/\$5,200	\$2,000/\$7,200	\$2,000/\$5,200
Iowa	\$6,000	\$6,000	\$6,000	\$6,000
Kansas	None	Some exempt	Exempt	Exempt
Kentucky	\$41,110	State Calculation	State Calculation	State Calculation
Louisiana	\$6,000	\$6,000/Exempt	Exempt	Exempt
Maine	\$6,000	\$6,000	\$6,000	\$6,000
Maryland	\$23,600	\$23,600	\$23,600	\$23,600
Massachusetts	None	Exempt ^b	Exempt ^b	Exempt
Michigan	\$42,240	Exempt	Exempt	Exempt
Minnesota	None	None	None	None
Mississippi	Exempt	Exempt	Exempt	Exempt
Missouri	\$6,000	\$6,000	\$6,000	\$6,000
Montana	\$3,600	\$3,600	\$3,600	\$3,600
Nebraska	None	None	None	None
New Hampshire	Exempt	Exempt	Exempt	Exempt
New Jersey	\$15,000	\$15,000	\$15,000	Exempt
New Mexico	None	None	None	None
New York	\$20,000	Exempt	Exempt	Exempt
North Carolina	\$2,000	\$4,000/Exempt	\$4,000/Exempt	\$4,000/Exempt
North Dakota	None	None/\$5,000	None/\$5,000	None/\$5,000
Ohio	\$200 credit	\$200 credit	\$200 credit	\$200 credit
Oklahoma	\$10,000	\$10,000	\$10,000	\$10,000
Oregon	9% credit	9% credit	9% credit/pre-1991 exempt	9% credit pre-1991 exempt
Pennsylvania	Exempt	Exempt	Exempt	Exempt
Rhode Island	None	None	None	None
South Carolina	\$3,000/ \$10,000	\$3,000/ \$10,000	\$3,000/ \$10,000	\$3,000/ \$10,000
Tennessee	Exempt	Exempt	Exempt	Exempt
Utah	\$4,800/ \$7,500	\$4,800/ \$7,500	\$4,800/ \$7,500	\$4,800/ \$7,500
Vermont	None	None	None	None
Virginia	None	None	None	Most taxable
West Virginia	None	\$2,000	\$2,000	\$22,000
Wisconsin	None	Pre-1964 Exempt	Pre-1964 Exempt	Exempt

Notes:

(1) Exclusions per person

(2) Two figures indicate different exclusions based on age

^aApplies only in the case of certain public safety officials.

^bOnly contributory pension income is exempt.

Source: Wisconsin Legislative Fiscal Bureau, *Individual Income Tax Provisions in the States*, January 2009

Michigan Population

The Michigan population is projected to become older as the Baby Boom Generation ages and life expectancy increases. Exhibit 13 provides data on how the Michigan population is projected to change over time by age groups.

The median age is projected to increase from 35.51 years old from the 2000 Census to 37.81 years old in 2015 and to increase to 40.16 years old by 2030. From 2000 to 2030, the number of Michigan persons 65 years and older is projected to increase from 1,219,018 to 2,080,725, an increase of 70.7 percent. Conversely, the number of Michigan residents 19 years old and younger is projected to decline from 2,884,065 in the 2000 Census to an estimated 2,699,891 in 2030, a decline of 6.4 percent.

Over time, the Michigan population under 50 is projected to decline for all age groups by 2030. The total under 50 population is projected to decrease from 7,223,353 people from the 2000 Census to an estimated 6,761,953 people in 2030. The over 50 population increases from 2,715,091 people in 2000 to an estimated 3,932,219 people in 2030.

Exhibit 13
Michigan Population Projections
Elderly Population Increases

<u>Age Group</u>	<u>2000 Census</u>	<u>Projected</u>		<u>Percent Change 2000-2015</u>	<u>Percent Change 2000-2030</u>
		<u>2015</u>	<u>2030</u>		
0-19	2,884,065	2,747,985	2,699,891	-4.7%	-6.4%
20-29	1,298,468	1,420,524	1,252,057	9.4%	-3.6%
30-39	1,494,909	1,421,473	1,370,320	-4.9%	-8.3%
40-49	1,545,911	1,404,201	1,439,685	-9.2%	-6.9%
50-59	1,118,929	1,478,271	1,263,866	32.1%	13.0%
60-64	377,144	619,812	587,628	64.3%	55.8%
65 plus	<u>1,219,018</u>	<u>1,506,856</u>	<u>2,080,725</u>	<u>23.6%</u>	<u>70.7%</u>
Total	9,938,444	10,599,122	10,694,172	6.6%	7.6%
Median Age	35.51	37.81	40.16		

Source: Census Bureau, Interim Population Projections for Five-Year Age Groups and Selected Age Groups by Sex for States, released April 21, 2005

As shown by Exhibit 14, as a percentage of total population, the 65 years and above group is estimated to increase from 12.3 percent in 2000 to 19.5 percent in 2030. The 19 years old and under group is projected to fall from 29.0 percent of total population in 2000 to 25.2 percent in 2030. The under 50 population is projected to decrease from 72.7 percent of total population in 2000 to 63.2 percent in 2030. The over 50 population is estimated to increase from 27.3 percent of total population in 2000 to 36.8 percent in 2030.

Exhibit 14
Michigan Population Percentage by Age Group

<u>Age Group</u>	<u>2000</u>	<u>Projected</u>	
	<u>Census</u>	<u>2015</u>	<u>2030</u>
0-19	29.0%	25.9%	25.2%
20-29	13.1%	13.4%	11.7%
30-39	15.0%	13.4%	12.8%
40-49	15.6%	13.2%	13.5%
50-59	11.3%	13.9%	11.8%
60-64	3.8%	5.8%	5.5%
65 plus	<u>12.3%</u>	<u>14.2%</u>	<u>19.5%</u>
Total	100.0%	100.0%	100.0%

Other Effects

In FY 2008, the Michigan individual income tax raised approximately \$7.2 billion. The largest credit amount claimed is the homestead property tax credit totaling nearly \$1 billion. This credit has enhanced features for taxpayers age 65 and above.

Property taxes paid above 3.5 percent of a taxpayer's household income are eligible for a credit with a \$1,200 maximum. Renters assume 20 percent of total rent as the amount of property taxes paid. For all taxpayers, the credit is phased-out at \$73,650 of household income with the credit totally phased-out at \$82,650.

Taxpayers under age 65 multiply the amount of property taxes in excess 3.5 percent of household income by 60 percent. Senior taxpayers receive a credit of 100 percent of taxes paid over 3.5 percent of household income. The credit has a \$1,200 maximum for all taxpayers.

Exhibit 15
Michigan Senior Homestead Property Tax Credit

<u>Senior HPTC</u>	<u>Tax Year</u> <u>2000</u>	<u>Tax Year</u> <u>2006</u>	<u>Percent</u> <u>Change</u>
Number Claimed	364,200	415,300	14.0%
Amount of Credit	\$220,132,000	\$308,300,200	40.1%

Over the past few years, the number and amount claimed on the senior homestead property tax credit has increased significantly. From tax year 2000 to tax year 2006, the number claimed increased by 14.0 percent from 364,200 to 415,300 and the credit amount increased 40.1 percent, from \$220.1 million to \$308.3 million (see Exhibit 15). However, the general homestead

property tax has increased more in number claimed and total amount of credit than the senior homestead property tax credit. The general credit has increased by 37.6 percent in the number claimed (743,100 to 1,022,800) from 2000 to 2006 and increased 93.1 percent in amount claimed from \$256.1 million to \$495.1 million.

Over time, the senior homestead property tax credit may rise faster than the general credit with an increasing senior population. The general homestead property tax credit recent increase may be due to the overall weakening economy over this time period.

A recently enacted Michigan income tax credit is the Earned Income Tax Credit (EITC). In 2008, the Michigan EITC is 10 percent of the federal EITC and increases to 20 percent of the federal EITC for tax year 2009 and beyond. The EITC is for low wage workers to help supplement income and encourage work. Exhibit 16 shows the distribution of the federal EITC by age for tax year 2004.

**Exhibit 16
Federal Earned Income Tax Credit by Age
Tax Year 2004**

<u>Age Group</u>	<u>Earned Income Credit</u>		
	<u>Number</u>	<u>Total Amount</u>	<u>Average</u>
Under 25 Yrs	68,106	\$152,401,547	\$2,238
25 to 34 Yrs	201,829	\$368,900,685	\$1,828
35 to 44 Yrs	188,169	\$359,217,679	\$1,909
45 to 54 Yrs	119,761	\$188,100,121	\$1,571
55 to 64 Yrs	45,557	\$48,068,195	\$1,055
65 to 74 Yrs	11,110	\$10,095,728	\$909
75 to 84 Yrs	1,528	\$1,581,522	\$1,035
85 and Over	136	\$112,623	\$828
Missing Age	<u>1,557</u>	<u>\$3,081,840</u>	<u>\$1,979</u>
Totals	637,753	\$1,131,559,940	\$1,774

Most of the recipients of the federal EITC in tax year 2004 are under 55 years old. Because the EITC credit is based on wages to encourage work and since seniors rely less on wage income, it is expected that fewer seniors would qualify for this credit. As more seniors remain in the workforce due to economic reasons, the cost of this credit from older persons may increase.

Future sales tax collections may be affected as the population ages over time. According to the 2006 Consumer Expenditure Survey, persons 65 and older have less overall income than any age group except for the under 25 group. Therefore, the 65 and older population has less money to spend on taxable items. Additionally, as the economy becomes more service-oriented, sales taxes based on a goods and manufacturing economy is subject to a shrinking taxable base.

Exhibit 17 shows national data by age group from the 2007 Consumer Expenditure Survey. Income peaks for the age 45 years to 54 years age group at \$80,560 and declines to \$40,305 for person aged 65 years and older. Likewise, average annual expenditures are nearly the largest in

the 45 year to 54 year old age group at \$58,331 and decline to \$36,530 for person 65 years and older.

Types of expenditures also change as the population ages. Healthcare spending is a prime example. As Exhibit 17 shows, healthcare spending as a percent of total expenditures increases steadily as the population ages. Persons 65 and older spend 12.7 percent of total expenditures on health care spending, while persons 55 years to 64 years spend 6.5 percent of total expenditures on healthcare. The age groups under 55 years old spend under 5.0 percent of total expenditures on healthcare.

The area of healthcare also magnifies the potential shrinking sales tax base. Since most healthcare spending is service related or exempted (prescription drugs) from the sales tax, more spending in this area reduces potential sales tax collections. As the population ages, less money is available for spending and greater percentages of spending go towards non-taxable items.

Exhibit 17
Seniors Spend Less in Total Than Most Other Age Groups
Healthcare Spending Much Higher for Persons 65 Years Old and Above

<u>Item</u>	<u>Age of Consumer Unit</u>					
	<u>Under 25</u>	<u>25-34</u>	<u>35-44</u>	<u>45-54</u>	<u>55-64</u>	<u>65+</u>
Income Before Taxes	\$31,443	\$57,256	\$76,540	\$80,560	\$71,048	\$40,305
Average Annual Expenditures	\$29,457	\$47,510	\$58,934	\$58,331	\$53,786	\$36,530
Healthcare Spending	\$800	\$1,740	\$2,315	\$2,792	\$3,476	\$4,631
Healthcare as a % of Total Spending	2.7%	3.7%	3.9%	4.8%	6.5%	12.7%

Source: 2007 Consumer Expenditure Survey, U.S. Bureau of Labor Statistics

Income Tax Revenue

Michigan's population is projected to get older over the next two decades. As shown by the distribution of income by age, the yield of the Michigan individual income tax as a percent of overall income may decline as the population ages and with tax preferences for retirement income.

In FY 2008, the Michigan individual income tax raised over \$7.2 billion. As shown by previous statistics, wage income is the primary driver of income tax revenue. The 65 years old and under population that primarily earns wages is projected to decrease over the next twenty years. As noted the 65 years old and above population is projected to increase significantly. This development alone in an expected reduced workforce will weaken Michigan income tax revenue collections.

The tax expenditure of exempting pension income (public & private) reduces income tax revenue in the range of \$600 million to \$700 million annually. As the population becomes older and receives pension income, this tax expenditure is expected to increase over time.