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The Honorable Phil Barnhart
House Revenue Committee
901 Court Street
Salem, OR 97301

Chair Barnhart:

On behalf of AARP Oregon, thank you for the opportunity to comment on what is commonly referred to as the Senior Medical Deduction. AARP appreciates the concerns associated with the growing cost of Oregon's elderly medical expense deduction.

AARP Public Policy

Five broad principles guide AARP's evaluation of tax options, including tax expenditures: equity, economic neutrality, administrative efficiency, revenue, and social and economic goals.

The principle of equity is pertinent to the senior medical deduction. Equity means revenue sources should distribute the tax burden according to people's ability to pay and, to the extent possible, achieve vertical and horizontal equity. Vertical equity means the tax burdens – the percentage of income in taxes – should increase with a person's ability to pay. Horizontal equity holds that those with equal resources should be taxed equally. In general, taxation should be progressive, and people of comparable incomes should be taxed at comparable rates.

In addition, when evaluating tax expenditures, AARP considers (1) whether there is a need for a subsidy, (2) whether a tax subsidy is preferable to a direct spending program, and (3) whether the tax subsidy is well designed.

Oregon's Senior Medical Deduction

Under current federal law, taxpayers may claim an itemized deduction for medical expenses that exceed 7.5 percent of adjusted gross income. The spending threshold recognizes that while taxpayers can be expected to pay some of their own medical expenses, expenses in excess of 7.5 percent of income may be particularly onerous. Moreover, while the benefit of a tax deduction is generally regressive, the medical deduction is less regressive because higher-income taxpayers must have higher expenses to qualify.

All Oregon taxpayers who itemize medical and dental expenses on their federal return can also itemize those same expenses on their state tax return. In addition, taxpayers age 62 and older can itemize those expenses that they could not claim on their federal return (those expenses under the 7.5 percent threshold). Therefore, taxpayers age 62 and older can claim all unreimbursed medical and dental expenses as itemized deductions on their state return. Taxpayers age 62 and older who do not itemize on their federal return can still claim their medical and dental expenses on their state return through the senior medical deduction but they must itemized all expenses for the purposes of the Oregon return (rather than claiming the standard deduction).

In its current form, Oregon's senior medical deduction is in conflict with AARP's equity principle – both horizontal and vertical equity. The deduction fails to help people who claim the standard deduction or people who do not file a tax return or people who do not have sufficient tax liability. These are likely to be lower-income people who may need the most assistance with their medical expenses. In addition, those taxpayers age 62 and older will pay less tax than taxpayers under the age of 62 with comparable income.

Changes under Consideration

Bills this session – and in the past - maintain the age threshold and gradually increase that threshold from the current age 62 to either 66 or 67 years of age. There is little rationale for the age threshold associated with the current deduction, nor for the increased age threshold. AARP sees no reason why two taxpayers with the same incomes and same medical expenses should receive different tax benefits solely due their ages. However, the primary concern related to the current senior medical deduction is the growing cost associated with it. AARP recognizes that eliminating the age threshold would be contrary to the intent to reduce or cap the costs of the deduction.

While bills under consideration gradually phase out the tax benefit for taxpayers of higher income, some maintain the current deduction while others converts the itemized deduction to a subtraction from federal taxable income and caps the subtraction. A tax deduction is a poor mechanism for targeting benefits to the neediest families because the benefit of a tax deduction increases with the marginal tax rate, and therefore with income. And, as previously noted, taxpayers must itemize expenses to receive a deduction. A subtraction would provide the same benefit for a dollar of medical expense to all taxpayers, provided that they file a return and have a tax liability.

Compared to the current tax policy and the senior medical deduction, most of the bills under consideration can be considered "better" public policy, primarily due the to the phase-out of the tax benefit for higher-income taxpayers. However, since many low- and moderate-income Oregon residents do not itemize their deductions and receive no benefit from the current senior medical deduction, the conversion to a subtraction would be the preferred tax policy to consider.

Budget Concerns

The 2013-2015 Co-Chairs Budget (CCB) calls for targeted reductions of $135 million from human services. The targeted reduction in the Division of Aging and People with Disabilities (APD) in general fund dollars is $22.4 million – with federal matching funds considered the reduction to APD could be $65-75 million. These reductions will have a devastating impact on Oregon's long-term care system. While AARP does not generally support earmarking funds for a specific service, we do believe that any revenue generated by changes in the senior medical deduction be utilized to lessen the impact of budget reductions on – and if possible enhance – services and supports to seniors and people with disabilities.

With that in mind, AARP does not intend to take a position on any bill associated with the senior medical deduction until there is a better understanding of the final 2013-2015 budget and its funding of services for seniors and people with disabilities.

Thank your for your consideration.

Sincerely,

Rick Bennett

Rick Bennett
Director of Government Relations
AARP Oregon