

**OVERVIEW OF THE DEFINITION OF INCOME USED BY  
THE STAFF OF THE JOINT COMMITTEE ON TAXATION  
IN DISTRIBUTIONAL ANALYSES**

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of the  
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## INTRODUCTION

This document,<sup>1</sup> prepared by the staff of the Joint Committee on Taxation (“Joint Committee staff”), provides information on the definition of income used by Joint Committee staff in distributional analyses. The Joint Committee staff defines a concept, called “expanded income,” to sort taxpayers by income level. Expanded income is not the same as adjusted gross income (“AGI”), an income measure that taxpayers calculate as a step in determining their income tax liability. Part I of this document explains the similarities and differences between the two definitions and provides some justification for the use of expanded income by the Joint Committee staff. Part II presents data on the distribution of income under adjusted gross income and expanded income concepts. Part III provides additional detail on the definition of income using the expanded income concept.

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<sup>1</sup> This document may be cited as follows: Joint Committee on Taxation, *Overview of the Definition of Income Used by the Staff of the Joint Committee on Taxation in Distributional Analyses* (JCX-15-12), February 8, 2012. This document can also be found on our website at [www.jct.gov](http://www.jct.gov).

## I. ADJUSTED GROSS INCOME VERSUS EXPANDED INCOME

The largest and most reliable data source containing microdata information on the incomes of individuals in the United States is the Individual Income Tax Returns file prepared by the Statistics of Income (“SOI”) division of the Internal Revenue Service (“IRS”). The file is a stratified sample of individual income tax returns submitted to the IRS in a calendar year. The file contains amounts for the various income sources, deductions, credits and taxes reported on Forms 1040 (including 1040A, and 1040EZ) and the subsequent forms and schedules.

The SOI division prepares several distributional analyses tables. In most of SOI’s distribution tables, tax returns are distributed according to adjusted gross income (“AGI”). AGI includes all sources of taxable money income, reduced by adjustments such as contributions to certain retirement accounts and alimony paid. However, as discussed below, AGI, a tax return concept, does not lend itself to comprehensive distributional analyses, because it does not fully reflect the taxpayer’s command over economic resources, and, therefore, it creates an incomplete picture of economic well-being.

When preparing distributional analyses, the Joint Committee staff uses an income concept meant to measure economic income, not just taxable income, since economic income is the conceptually appropriate measure of economic well-being. Economic income includes the annual flow of all resources at the command of an individual and represents an individual’s total well-being. However, the measurement of economic income involves some difficult issues. In general, the approach taken by the Joint Committee staff is to resolve these issues so that people in similar economic situations are treated similarly.

As a practical matter, the income concept used in distributional analyses needs to balance the goal of a measure that accurately reflects economic well-being with a measure that can be accurately constructed using available data sources. When preparing distributional analyses, the Joint Committee staff uses an income concept that starts with AGI but includes several additional sources of income which are generally easy to measure. Although theoretical ambiguities and data constraints prevent the Joint Committee staff from constructing a perfect measure of economic income, the JCT income classifier represents an attempt to come as close as possible to matching this income concept. The concept developed by the Joint Committee staff is referred to as expanded income. Expanded income is defined as follows:

Expanded Income =  
Adjusted Gross Income  
+ tax-exempt interest  
+ workers’ compensation  
+ nontaxable Social Security benefits  
+ excluded income of U.S. citizens living abroad  
+ value of Medicare benefits in excess of premiums paid  
+ minimum tax preferences  
+ employer contributions for health plans and life insurance  
+ employer share of payroll taxes

Expanded income is a current-year, pre-tax and transfer income concept, expressed in nominal dollars. Economists generally agree that, in theory, a Haig-Simons<sup>2</sup> measure of income is the best measure of economic well-being. Broadly speaking, Haig-Simons income is defined as consumption plus changes in net worth. Increases in net worth are generally derived from savings and become a source of a family's consumption in a future year. Decreases in net worth are generally the result of drawing down a family's past savings. While conceptually easy to define, because of data limitations, a Haig-Simons measure of income is extremely difficult to implement. For example, a Haig-Simons measure includes changes in balances of a family's savings accounts. Such data, on a micro-level, is tenuous at best. Expanded income tries to capture the most practically measurable elements of Haig-Simons income.

Because of data limitations, the formulation of expanded income embodies significant departures from the Haig-Simons concept. For instance, it includes realized, not accrued, income from capital gains and pension benefits, and it ignores the rental value of owner-occupied housing and other durable goods. The most economically significant departure from the Haig-Simons concept is the inclusion of nominal, rather than real, capital income. Both interest income and capital gains are overstated in the presence of inflation. For example, if a taxpayer has a \$1,000 savings account that pays a five percent annual interest rate, the taxpayer has \$50 of nominal interest income. This nominal interest income is included in AGI and in expanded income. However, if the annual inflation rate is four percent, then the annual real interest rate is only one percent and the taxpayer's real interest income is only \$10. The real interest income is equal to the \$50 nominal interest income minus the \$40 decline in real value of the savings account balance due to the four percent inflation.<sup>3</sup> Similar mis-measurement occurs with respect to capital gains, because AGI and expanded income measure the difference between the nominal sales price of the asset and its nominal purchase price, with no adjustment for any inflation that occurs between the date of purchase and the date of sale. Similarly, depreciation allowances are based on original costs, with no adjustments for inflation occurring from the time of purchase, to the time the depreciation allowance is claimed.

These departures from the Haig-Simons concept mean that expanded income does not accurately reflect this broad measure of economic income. However, because expanded income starts with AGI as a base, and adds other income components not included in AGI, it is a closer approximation of economic income than AGI.

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<sup>2</sup> Robert M. Haig. "The Concept of Income- Economic and Legal Aspects;" *The Federal Income Tax*. New York: Columbia University Press, 1921, pp. 1–28; Henry Simons. *Personal Income Taxation: the Definition of Income as a Problem of Fiscal Policy*. Chicago: University of Chicago Press, 1938, p. 49.

<sup>3</sup> The computation of real interest may even be more complicated. If a bond sells at premium or discount compared to its face value, the coupon payment does not even measure nominal interest income correctly. Since the taxpayer's tax return does not report whether the bond was purchased at premium or discount (nor the value of the premium or discount), it is not possible to adjust reported interest for inflation in such a case.

## II. DISTRIBUTION OF INCOME UNDER ADJUSTED GROSS INCOME VERSUS EXPANDED INCOME CONCEPTS

Table 1 below shows the number of returns across income categories (for tax year 2011) using expanded income and using AGI as classifiers. According to the table, there are more taxpayers with less than \$20,000 of income as measured by AGI than there are using expanded income. There are fewer taxpayers with income between \$20,000 and \$500,000 using AGI versus expanded income; there is essentially no difference in the number of taxpayers with greater than \$500,000 of income using AGI versus expanded income.

**Table 1.—Estimated Distribution of Number of Returns  
by Expanded Income and AGI for Tax Year 2011**

INCOME CATEGORY	Returns by Expanded Income	Returns by Adjusted Gross Income
	(Millions)	(Millions)
Less than \$10,000 .....	20.4	37.6
\$10,000 to \$20,000.....	16.9	21.9
\$20,000 to \$30,000.....	18.4	17.4
\$30,000 to \$40,000.....	15.4	14.4
\$40,000 to \$50,000.....	13.6	11.6
\$50,000 to \$75,000.....	26.7	21.2
\$75,000 to \$100,000.....	17.0	12.5
\$100,000 to \$200,000.....	22.1	15.4
\$200,000 to \$500,000.....	4.9	3.5
\$500,000 to \$1,000,000 .....	0.6	0.6
\$1,000,000 and over.....	0.3	0.3
<b>Total, All Taxpayers.....</b>	<b>156.4</b>	<b>156.4</b>

Note: Return count totals exclude returns filed by dependents and returns with negative expanded income. However, the return counts include returns from potential non-filers.

Much of the disparity in the number of returns within a given income range between expanded income and AGI shown in Table 1 above is explained by three additions to AGI in calculation of expanded income. These three additions are nontaxable Social Security benefits, employer contributions for health plans and life insurance, and the employer share of payroll taxes. Table 2 shows that of these three, nontaxable Social Security benefits accounts for the largest portion of the disparity for taxpayers with less than \$20,000 of income. For example, nontaxable Social Security benefits for taxpayers with AGI less than \$10,000 total about \$205.3 billion. In comparison, for taxpayers with expanded income less than \$10,000, these benefits total \$6.9 billion. Similarly, nontaxable Social Security benefits are \$108.9 billion for taxpayers with \$10,000 to \$20,000 AGI, but are only \$30.8 billion using expanded income. Essentially, by including nontaxable Social Security benefits in the definition of income, many taxpayers that otherwise would have been observed having income of less than \$20,000 are pushed up into

higher income categories. The pattern is reversed for taxpayers with greater than \$20,000 of income; there are fewer dollars of nontaxable Social Security benefits by AGI than by expanded income. For taxpayers with \$20,000 to \$30,000 of expanded income, nontaxable Social Security benefits are \$79.0 billion compared to \$59.1 billion using AGI. For taxpayers with \$30,000 to \$40,000 of expanded income, nontaxable Social Security benefits are \$66.7 billion using expanded income compared to \$35.5 billion using AGI. A similar pattern holds for income categories above this range as well. Simply using AGI, instead of using a broader measure of income that includes nontaxable Social Security benefits and other similar sources of income, systematically biases upward the number of returns in the lower portion of the income distribution and biases downward the number of returns in the upper portion of the income distribution.

There are also differences in the distribution of amounts of employer contributions for health plans and life insurance when using AGI as opposed to expanded income. These amounts are larger using AGI versus expanded income for income levels below \$75,000 and smaller for income levels greater than \$75,000. In other words, using AGI to measure income masks the fact that for some taxpayers, nominal wage earnings understate the compensation they receive for their labor because they also receive significant forms of other income, such as employer contributions for health plans and life insurance. There is a similar pattern of differences in the employer share of payroll taxes depending on whether income is measured using AGI or expanded income. Together, these discrepancies indicate that including nontaxable Social Security benefits, employer contributions for health plans and life insurance, and the employer share of payroll taxes in measures of income can significantly alter the measurement of the income distribution.

**Table 2.—Estimated Distributions of Nontaxable Social Security Income, Employer Contributions for Health Plans and Life Insurance, and Employer Share of Payroll Taxes by Expanded Income and AGI for Tax Year 2011**

INCOME CATEGORY	BY EXPANDED INCOME			BY AGI		
	Excluded SS Inc	Employer Health	Employer FICA	Excluded SS Inc	Employer Health	Employer FICA
	(Millions of Dollars)			(Millions of Dollars)		
Less than \$10,000.....	6,928	7,210	3,577	205,273	38,548	6,196
\$10,000 to \$20,000.....	30,751	22,535	9,830	108,910	58,715	15,583
\$20,000 to \$30,000.....	78,992	38,860	16,614	59,122	66,192	24,258
\$30,000 to \$40,000.....	66,742	51,781	21,652	35,543	71,852	29,450
\$40,000 to \$50,000.....	66,805	60,715	24,721	19,237	67,910	31,257
\$50,000 to \$75,000.....	130,730	154,945	69,022	21,092	155,842	78,590
\$75,000 to \$100,000.....	63,424	136,167	64,552	7,664	112,818	68,117
\$100,000 to \$200,000.....	19,009	244,151	151,740	7,666	166,364	123,791
\$200,000 to \$500,000.....	2,818	59,805	51,229	1,782	39,262	36,902
\$500,000 to \$1,000,000.....	406	7,030	7,538	343	5,953	6,638
\$1,000,000 and over.....	253	3,404	5,218	226	3,145	4,909
<b>Total, All Taxpayers.....</b>	<b>466,859</b>	<b>786,603</b>	<b>425,691</b>	<b>466,859</b>	<b>786,603</b>	<b>425,691</b>

### III. DETAILED ISSUES IN DEFINING INCOME

To arrive at a measure of income which more closely approximates economic well-being, the Joint Committee staff adds some items to AGI and subtracts others. This section provides a detailed discussion of these additions and subtractions.

#### **Items added to AGI**

##### Cash receipts not included in AGI

Tax-exempt interest.—Tax-exempt interest is added to AGI to more fully reflect economic resources from capital. Holders of tax-exempt investments accept a lower rate of return in exchange for the exemption from income tax on interest received. The difference between the taxable and the tax-exempt rates may be viewed as an implicit tax which is “paid” to State and local government issuers. A pre-tax definition of income would include both the tax-exempt earnings and the implicit tax, and the distribution analysis would credit the tax as paid by holders of tax-exempt issues. The implicit tax, however, is paid to State and local governments, and would not be included in the calculation of Federal taxes paid. Consequently, the Joint Committee staff includes only the tax-exempt earnings as income. The omission of the implicit tax in these calculations leads to underestimation of the economic income of the taxpayer. However, the addition of tax-exempt interest moves us closer to calculation of economic income than AGI.

Workers’ compensation.—Workers’ compensation is an insurance program that provides income replacement and medical benefits when employees are injured in the course of employment. Employers contribute to this program on behalf of their workers, and these contributions represent a portion of total compensation. The insurance value of this program is difficult to assess and the dollar value of the benefit approximately reflects the value of the program to the worker, so the Joint Committee staff includes program payments in expanded income. These payments represent the taxpayer’s potential to command economic resources and the inclusion of these payments in these calculations allows for a closer approximation of economic income.

Social Security benefits.—Social Security exhibits characteristics of both a tax-based retirement plan and a system of social welfare transfers: Social Security benefits are based on lifetime earnings in covered employment, but the relationship between payroll taxes paid on covered earnings and the benefits ultimately received varies greatly among taxpayers depending on their income and marital status. Because of the loose association between payroll taxes paid in and benefits received, and the mandatory nature of payroll taxes, Social Security contributions more closely resemble a tax than a payment to a retirement system. As a tax, it should not be treated as basis in a retirement benefit. Thus, the Joint Committee staff treats the entire Social Security benefit as part of expanded income.”

Excluded income of U.S. citizens living abroad.—For tax year 2011, U.S. citizens living abroad are entitled to exclude from gross income up to \$92,900 of earned income from foreign sources, as well as a housing allowance. The amount of the housing allowance is based on

employer-provided foreign housing costs. This compensation is clearly economic income, and the excluded income is incorporated in the Joint Committee staff income classifier.

#### Value of non-means-tested Federal program

Insurance value of Medicare.—Medicare (parts A, B, and D) is a Federal program designed to provide health care benefits to elderly and disabled persons who are insured under the Social Security program. The insurance value of this benefit represents a contribution-based insurance plan. It is equivalent to Social Security benefits in this context, and should be treated in a consistent manner. Thus, the expanded income measure includes the insurance value of all Medicare benefits net of premiums paid for part B and D coverage.

#### Special or enhanced deductions allowed in computing AGI

Alternative minimum tax preferences.—Tax preference items generate considerable tax savings by reducing AGI. It is generally believed that the value of such preferences represent economic income. Therefore, they are added back into AGI in the computation of Expanded Income. Alternative minimum tax preference items included in Expanded Income are obtained only from taxpayers who include Form 6251 (The Alternative Minimum Tax) when filing their income taxes. Among the minimum tax preference items are the following:

- (a) Excess depreciation on assets;
- (b) Excess depletion allowances;
- (c) Exercise of incentive stock options;
- (d) Certain mining costs;
- (e) Certain loss limitations;
- (f) Passive activity gains and losses.

#### Non-taxable, non-cash compensation

Employer contributions for health plans, life insurance, and health flexible spending accounts (“FSA”).—The value of employer contributions to health and life insurance plans and health FSA’s are included in expanded income. These benefits represent a significant proportion of total compensation.

Employer expenditures for health and life insurance plans and health FSA’s increase the economic well-being of workers, and should therefore be included in income. However, it is not clear how the value of these expenditures should be computed for purposes of inclusion in income. If the expenditures are on commodities that the workers would otherwise have purchased themselves, they should be valued at cost divided by  $(1.0 - \text{tax rate})$ , since they are not taxed. For instance, a one dollar expenditure on health insurance would have the same value as \$1.54 in wages for a worker with a 35-percent marginal tax rate who would have purchased the insurance if his or her employer did not provide health coverage. However, because these benefits are non-taxable, compensation packages will oversupply benefits relative to what workers would choose in the absence of a tax advantage. At the margin, the value of one dollar of benefits is one dollar in wages, since workers will choose to be compensated in benefits until the value of the last dollar spent on benefits is just equal to one dollar of wage income. Thus, on

average, the value of benefits exceeds its cost to the worker. However, because it is not possible to know the magnitude of the excess of value over cost, and because the implicit tax paid on these benefits is not actually paid (see discussion in (1) above), these benefits are valued at cost in the income classifier.

Employer share of payroll taxes.—The employer share of payroll taxes (contributions to FICA) are included in expanded income, as is the above-the-line deduction for 50 percent of SECA taxes. The employers’ share of the FICA tax includes Old Age, Survivors, and Disability Insurance (commonly thought of as Social Security) and Hospital Insurance (Medicare, part A). This represents a significant portion of total compensation.

### **Items not included in expanded income**

#### Annual accruals of capital gain

Conceptually, an income classifier measuring economic income would include wealth as it accrues. Appreciation of an individual’s assets represents economic income to the taxpayer, and a true Haig-Simons approach would incorporate all accruing capital gains and losses in income.

Because income is taxed only upon realization, unrealized capital gains on financial assets and on tangible assets (housing, real estate, etc.) are not reported on the tax return. Consequently, data on gain and loss accruals are not available for the individual taxpayer, and estimates of accrued wealth are imprecise. Realizations of capital income reported on the tax return, however, are included in the income classifier. As a result, the Joint Committee staff expanded income measure only partially reflects accrued wealth in each year.

The most significant of untaxed increments to wealth includes accrued capital gains and tax-deferred contributions to savings and retirement plans. Although annual changes in wealth constitute a significant part of Haig-Simons income, it is not clear that estimated valuations of accrued wealth should be incorporated in an income classifier. Estimations of the nominal value of assets are often uncertain. Moreover, the conversion of these assets into income can involve large transactions costs reducing the realized value of the asset. Additionally, the convertibility of assets at the current market value is never guaranteed.

In theory, the Joint Committee staff could impute capital gains and losses on corporate equity with corporate income information in an effort to create an accrued wealth concept. Allocating corporate profits and retained earnings to stockholders can only be done by making many assumptions about the distribution of stock ownership and then imputing corporate income based on these assumptions. Among the assumptions would be those that reflect “who” holds “what.” These rules would then be applied to allocate corporate earnings among taxpayers on the tax model. For non corporate assets, imputing accrued gains and losses is even more uncertain.

It is important to note that capital gains realizations included in expanded income, a nominal income concept, mis-measures real income from capital. Gains are calculated by subtracting the nominal sales price of the asset from the nominal basis. Resource constraints

prevent the Joint Committee staff from routinely obtaining acquisition information to express the basis and the sales price in constant dollars,<sup>4</sup> so the resulting gain is greater than the increase in the real value of the asset. Increases in the price level are also reflected in the “capital gain.”

### Pensions

An inclusive specification of Haig-Simons income would incorporate contributions to pensions when they occur, as well as the earnings on these funds when they accrue.

Funds contributed to an employer-sponsored pension plan, whether by an employer or employee, are not included in the income classifier for a number of reasons. First, it is difficult to determine the value of defined-benefit pension plans, since it depends on wage growth, employee turnover, and current and future rates of interest and inflation. Second, not all employees covered by pension plans are vested; this also makes it difficult to value the economic income associated with employer-sponsored pension plans. The Joint Committee staff does not include pension contributions as income when contributed, but rather includes distributions of principal and earnings when withdrawn.<sup>5</sup>

Although it is generally agreed that pension contributions represent a decision to save income, such contributions are tax-deductible at the employer level and excludible at the employee level, and this tax-sheltered income is not included in reported income from wages and salaries. Information on these contributions, therefore, would have to be estimated. Employer contributions to pensions and savings plans are another element of income that must be estimated, because this information is not reported on tax returns. Further, accrued earnings on these funds represent additions to wealth that would be considered a component of Haig-Simons income. Again, this income would have to be approximated, because earnings on such funds are not reported. Further, because plans and associated earnings vary greatly, estimates of these income components are too inexact to warrant imputation.

Pension income that escapes taxation when earned is reported on the tax return of the recipient when it is distributed. Including these funds in expanded income allows the Joint Committee staff to rely on tax data. This method also ensures that company-matched funds are included in income when they are withdrawn. This information is accurate and includes accrued interest as well as employer contributions. Expanded income, therefore, captures income from pensions by ignoring contributions and including distributions.

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<sup>4</sup> This is also done to maintain consistency with other income such as interest. All distributional measures use nominal dollars.

<sup>5</sup> Lump-sum pension distributions are not included in the Joint Committee staff income classifier, however, because they represent one-time realizations that distort the distribution of income. Generally taxpayers receiving a lump-sum distribution roll over the distribution into an IRA. The income from lump-sum distributions is included in AGI according to distribution rules applicable to IRAs and, therefore, in expanded income.

### Savings plans

Contributions to an individual retirement account (“IRA”) do not reduce a taxpayer’s economic income. However, because contributions to pension plans by employers on workers’ behalf are not included in employees’ income, and because current law restricts deductible IRA’s to people below a certain income level and people without pension plans, comparability between people with and without pension plans suggests that deductible contributions not be added to AGI to arrive at the Joint Committee staff’s measure of expanded income.

### Non-taxable government payments

The Joint Committee staff does not include some government payments in the income classifier, because the classifier reflects pre-tax income. Government payment programs that do not require the taxpayer to contribute are generally means-tested and can thus be viewed as negative tax programs, that do not belong in a pre-tax income concept. The transfers that the Joint Committee staff does not incorporate in its income classifier include both cash and non-cash benefits: the insurance value of Medicaid benefits, TANF (Temporary Assistance for Needy Families), SSI (Supplemental Security Income), SNAP (Supplemental Nutrition Assistance Program, i.e. food stamps), housing benefits, and educational assistance. The government programs that are included--Social Security, worker’s compensation, and Medicare--represent programs for which eligibility is not determined on a means-tested basis, and the income is more appropriately considered pre-tax income, and included in the expanded income measure.

### Rental value of housing (and other durable goods)

The rental value of a homeowner’s home represents economic income, similar to income received on any other investment. Consider a taxpayer who buys and occupies a \$100,000 house that could be rented for \$5,000 a year. This taxpayer would be equally well off (ignoring tax considerations) if he or she spent \$100,000 on a financial asset that pays \$5,000 per year and uses the cash to rent a similar house. It would be incorrect conceptually to say that the taxpayer had no income in the first case but had \$5,000 of income in the second case. Hence, the rental value of the house should be included in expanded income.

The rental income implicit in home ownership represents considerable economic resources. Because imputed rent is not taxed, its value may exceed the dollar amount of rent on an equivalent house. In the past several years, falling real estate prices have resulted in negative estimates of the aggregate value of imputed rental income. Tax returns do not include any information about house values. As a result, it is only possible to know if a taxpayer owns a home if the taxpayer claims an itemized deduction for mortgage interest expenses or a deduction for state and local real property tax expenses, or receives a Form 1098 Information return with the amount of home mortgage interest expense paid by the taxpayer. Therefore, the Joint Committee staff has decided that too little information exists to accurately impute rental values to owner-occupants.

### Fringe benefits other than health and life insurance

Certain fringe benefits provided by employers, in addition to health and life insurance, are not taxable. These include employer-provided parking, contributions of club dues, and child-care costs up to \$5,000. Because little data exist on these expenditures, and because the aggregate value of the non-taxable benefits is believed to be small, they are omitted from the income classifier.

### Disallowed losses

Certain losses such as capital losses greater than a given amount or passive losses are not permitted in determining AGI but reduce Haig-Simons income. No adjustment is made. As a result, AGI could overstate economic income.

### Unreported income

Unreported income refers to all sources of income that are not reported, or are under-reported, on the tax return. Some transactions for which there is no information reporting requirement fall into this category. This includes some cash transactions, such as tips, or some self-employment income that is not full-time. In addition, income from foreign sources is believed to be under-reported. Unreported income also includes the income of persons below the filing threshold (i.e., persons whose income is so low that they do not owe income taxes).

Adding under-reported income to the income classifier would enable the Joint Committee staff to more accurately estimate the distribution of taxes. Data limitations, however, make the imputation of this income very imprecise. Therefore, unreported income is not currently included in expanded income.

## **Special problem areas**

### Non-filers

The Joint Committee staff's distribution analyses include non-filers. Because there are no income tax returns for non-filers, measuring income for such persons is difficult. The starting point for the Joint Committee staff's individual tax model is a stratified random sample of individual tax returns filed with the IRS. Individuals included in this sample are exactly linked to a series of information returns, also filed with the IRS. In particular, the Joint Committee staff links individuals' Forms W-2 which contain information on wages, retirement plan participation, FICA taxes paid, and certain other information. Other information returns linked to the individual tax model include forms 1099-DIV, 1099-G, 1099-INT, and 1099-R. The Joint Committee staff augments the individual tax model with a sample of non-filers. The non-filer sample is derived from a random sample of information returns, Form W-2, 1099-DIV, 1099-INT, etc., associated with people who do not file a tax return. The distributional effect of including non-filers is to increase the number of low-income persons relative to those represented by filed tax returns. Excluding these persons from the income classifier would understate the distributional effects of proposals that would increase the number of taxpayers filing returns.

### Taxpayers with losses

The Joint Committee staff's expanded income measure includes losses that are subtracted from income when computing AGI. These include capital losses, partnership losses, S corporation losses, sole proprietor losses, rental losses, and farm losses as reported on the respective tax schedules. Unlike the reporting of wage and salary income, the reporting of income and losses from these sources can involve a substantial amount of discretionary tax planning. Some analyses, such as those published by the SOI, separate income from these sources into negative and positive income components to reflect these tax planning choices. To the extent that losses reflect tax planning strategies, an income classifier that includes negative incomes will tend to misrepresent some middle- and high-income taxpayers as low-income taxpayers. For this reason, the Joint Committee staff eliminates observations with negative net expanded income from distributional analyses.<sup>6</sup>

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<sup>6</sup> The Joint Committee staff generally does not modify the IRS sample in distributional analyses. There are no differences in the number of returns in the sample or any return's base-year sample weight. However, taxpayers with negative AGI are classified as non-itemizers in the Statistics of Income (SOI) data. The Joint Committee staff restores the deductions and returns these taxpayers to a more accurate classification as itemizers. As a result, the total itemized deductions, by type, conducted by the Joint Committee staff will differ from the IRS published totals.