NATIONAL WOMEN'S LAW CENTER
EXPANDING THE POSSIBILITIES

Private Investment Managers Dodge Billions in Medicare Taxes

This analysis finds that hedge fund and private equity fund managers dodge about $900 million to $1.8 billion in Medicare payroll taxes per year: an amount sufficient to pay the Medicare hospital costs of 204,000 to 408,000 Americans and strengthen the financing of a program that is especially important to women. They avoid paying Medicare payroll taxes by means of the same tax loophole that enables them to pay a lower federal income tax rate on their compensation than ordinary working Americans.[1]

- **Low-wage workers pay more payroll taxes to support Medicare than private equity and hedge fund managers do on their carried interest income**.

All earnings, including those of the lowest earners, are subject to the 2.9% payroll tax to support Medicare, but capital gains income is not subject to payroll taxes.[2] So, when private equity and hedge fund managers make compensation for their services look like capital gains by taking it as a share of profits ("carried interest"), and lower their federal income tax rate from 35% to a maximum of 15%,[3] they also avoid paying Medicare payroll taxes on that income.

Medicare payroll taxes paid by:	
Child care provider earning $20,000.	**$580**
Small business owner earning $50,000	**$1,450**
Hedge fund manager earning $500,000,000 in carried interest. . .	**zero**

- **The failure of hedge fund and private equity managers to pay their fair share costs Medicare billions of dollars of much-needed revenue.**

Hedge fund and private equity managers exploiting the carried interest loophole are depriving Medicare of $900 million to $1.8 billion per year in payroll tax revenue, based on the methodology used by the Economic Policy Institute to estimate lost income tax revenue.[4]

- **The amount of payroll taxes avoided by hedge fund and private equity managers is enough to cover Medicare hospital expenses for hundreds of thousands of Americans and strengthen the Medicare Hospital Trust Fund.**

Medicare payroll taxes pay for inpatient hospital, skilled nursing facility, home health and hospice care through the Hospital Insurance Trust Fund (Medicare Part A).[5] These costs averaged $4,410 per beneficiary in 2006.[6]

> The $900 million to $1.8 billion in Medicare payroll taxes not paid by hedge fund and private equity managers is enough to cover Medicare hospital expenses for 204,000 to 408,000 Americans.[7]

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The Hospital Insurance Trust Fund is currently running a surplus, estimated at $15.4 billion for 2007.[8] However, income and reserves in the Trust Fund will only be sufficient to fully cover hospital benefits until 2019, according to the Trustees' latest estimate.[9]

$900 million to $1.8 billion in additional payroll taxes would increase the current $15.4 billion annual surplus by 6 to 12%, strengthening the Hospital Insurance Trust Fund.

- **Women will be especially hurt if a shortfall in Medicare revenues forces cuts in benefits and the shifting of more costs to beneficiaries.**

Medicare plays a vital role in protecting the well-being of 43 million elderly and disabled Americans, but is especially important to women. Women comprise well over half of all Medicare beneficiaries, and nearly three quarters of beneficiaries 85 and older. In addition, older women are more economically vulnerable than older men, with less income, fewer assets, and greater health care needs. Older women also spend more out-of-pocket on health care than older men, even with Medicare coverage, both in dollars and as a share of their incomes.[10]

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[1] *See* National Women's Law Center, *Private Investment Managers Should Pay Their Fair Share of Taxes* (August 2007), available at http://www.nwlc.org/pdf/TaxingPrivateInvestmentManagersFairly.pdf.

[2] Employees and employers each contribute 1.45% of wages for Medicare; self-employed persons pay 2.9%. There is no maximum on the amount of wages subject to Medicare tax as there is for the Social Security payroll tax, which applies only to the first $97,500 in 2007. Capital gains income is not subject to payroll taxes for Medicare or Social Security. *See generally*, Tax Policy Center, *Tax Topics: Payroll Taxes*, available at http://www.taxpolicycenter.org/taxtopics/Payroll-Taxes.cfm Private investment managers who receive at least $97,500 in other forms of compensation that are taxed as ordinary income (for example, a management fee calculated as a percentage of assets under management) would have paid the maximum Social Security tax; however, those who receive all their compensation in the form of carried interest would escape that tax as well.

[3] National Women's Law Center, *Private Investment Managers Should Pay Their Fair Share*, *supra* note 1.

[4] The Economic Policy Institute estimates that hedge fund managers alone earned about $31.5 billion in U.S.-taxable carried interest in 2006, and avoided $6.3 billion in income taxes by paying income tax at the lower capital gains tax rate; if private equity managers earned an equal amount, lost income tax revenue totaled $12.6 billion. Randall Dodd, EPI Policy Memorandum #120, *Tax Breaks for Billionaires* (July 2007). The National Women's Law Center calculated lost Medicare revenue by multiplying the estimated carried interest earnings of hedge fund and private equity managers by 2.9%.

[5] Medicare Part B covers physician, outpatient, home health, and preventive services; it is funded by beneficiary premiums and general revenues. Part D, the prescription drug benefit, is financed by beneficiary premiums, general revenues, and state payments. Part C, Medicare Advantage, is not separately financed. *See* Kaiser Family Foundation, *Medicare Spending and Financing* (June 2007), available at http://www.kff.org/medicare/upload/7305-02.pdf.

[6] 2007 Annual Report of the Board of Trustees of the Federal Hospital Insurance and Federal Supplementary Medicare Insurance Trust Funds [2007 Medicare Trustees' Report], Table II.B1, available at http://www.cms.hhs.gov/ReportsTrustFunds/downloads/tr2007.pdf.

[7] Calculations by National Women's Law Center.

[8] 2007 *Medicare Trustees' Report*, *supra* note 6, Table II.E1.

[9] *Id*. at 4.

[10] Juliette Cubanski, Kaiser Family Foundation, *The Impact of Health Expenses on Older Women's Financial Security*, presentation to AcademyHealth 2007 Annual Research Meeting, available at http://www.academyhealth.org/2007/sunday/southernhemisphere2/cubanskij.ppt