

# Vermont Legislative Joint Fiscal Office

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## ISSUE BRIEF

October 2016

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### Taxation of Social Security Benefits

Vermont follows the federal rules for the income tax treatment of Social Security benefits.<sup>1</sup> At least 15 percent of benefits are always exempt and up to 100 percent may be exempt depending on the taxpayer's "combined income" and filing status.

#### How much is exempt?

A taxpayer must include other income (wages, self-employment, interest, and dividends), nontaxable interest and 1/2 of their Social Security benefits in the calculation of combined income to determine the percentage of their total Social Security benefits that are taxable. The percentage of benefits that are subject to the federal income tax is shown in the table below. Because Vermont uses federal taxable income as its starting point for state income tax calculations, Social Security benefits that are taxed at the federal level are included in the state taxable income base.

**Federal Taxation of Social Security Benefits**

Combined Income		% of Social Security Benefits exempt
Single	Married Filing Joint	
< \$25,000	< \$32,000	All 100% Exempt
\$25,001 - \$34,000	\$32,001 - \$44,000	Up to 50% Exempt
\$34,001 and over	\$44,001 and over	At least 15% exempt and up to 50% exempt

Source: Social Security Administration (<https://www.ssa.gov/planners/taxes.html>)

The income thresholds are not indexed at the federal level and have been unchanged since they were established in 1984. Because wages and other income have increased, the proportion of beneficiaries who must pay income tax on their benefits has risen over time. For example, if the \$32,000 exemption level for married taxpayers had been indexed by the CPI, it would be just over \$74,000 in 2016. According to Congressional Budget Office estimates, nationally about half of Social Security recipients paid some tax on their benefits in 2014 (<https://www.cbo.gov/publication/49948>).

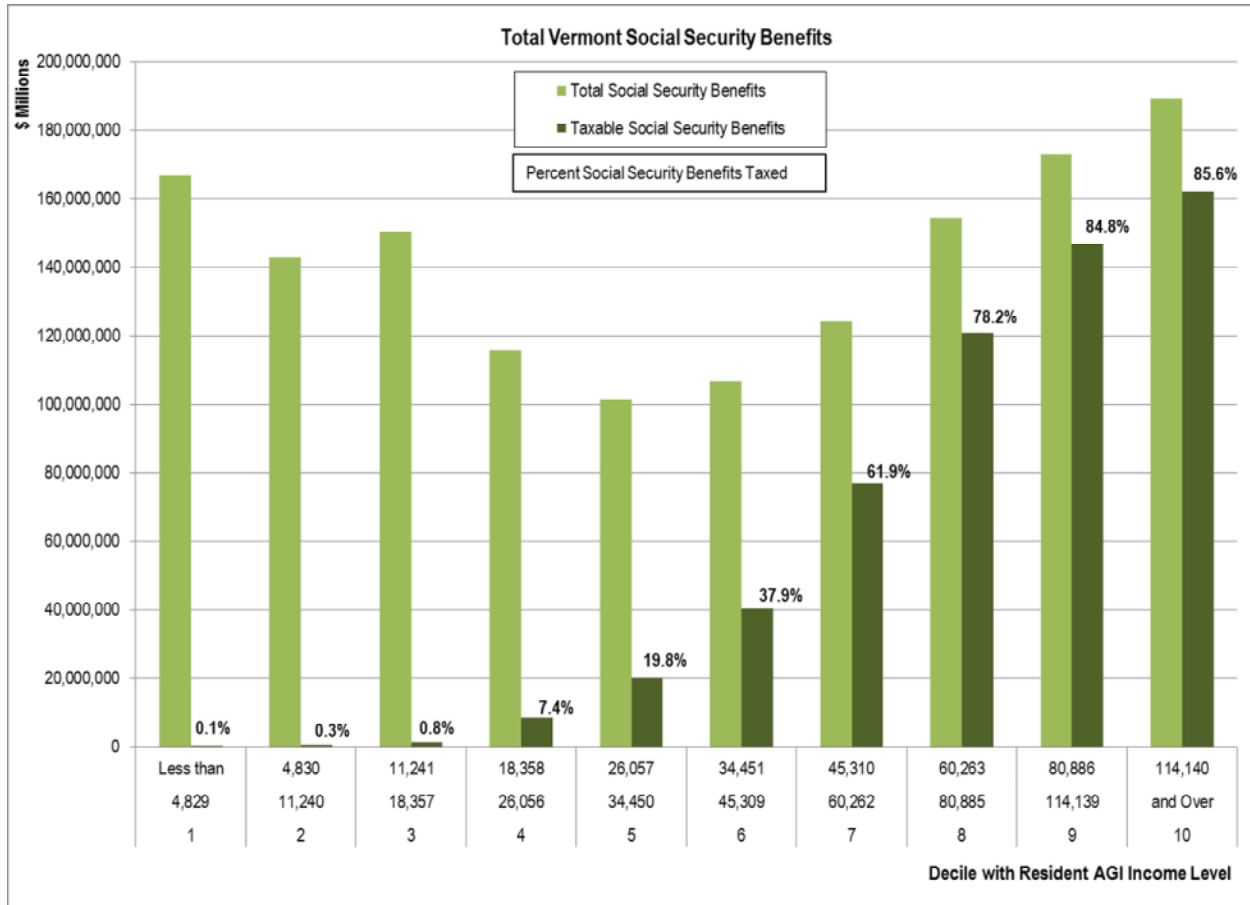
The 15 percent exemption was established by Congress to ensure that nearly all post tax contributions to the Social Security system would be treated similarly to pensions. This amount was determined by the Social Security Administration's Office of the Actuary to avoid "double taxation." Workers pay income taxes on the employee share of FICA (Social Security) contributions at the time they earn wages; and the untaxed share of benefits paid out in later years is subject to income tax in later years for higher-income taxpayers.<sup>2</sup>

<sup>1</sup> Social Security benefits that are paid to retirees, individuals with disabilities, and qualifying spouses and dependents. These are referred to as OASDI (Old Age Survivor and Disability Insurance) benefits.

<sup>2</sup> For a full explanation see Minnesota House Research Paper <http://www.house.leg.state.mn.us/hrd/issinfo/SSincometaxBP.pdf>

## Vermont Social Security Benefits Data

This information is from tax year 2013 federal and Vermont tax returns. The data are organized by population decile which means that the returns are divided into 10ths and each contains an equal number of taxpayers. Approximately 23% of resident taxpayers (about 72,000) receive Social Security benefits and about 40% of those benefits are taxed by the state in aggregate.



This chart and the detailed data that follow show that while benefits are distributed across all deciles, taxable benefits are concentrated in the top four deciles. The bars represent the aggregate amount of Social Security benefits and the taxable portion of those benefits. Also included in the chart is the percentage of the Social Security benefit that is taxable.

Almost all of the Social Security benefits for people in the first four deciles with the lowest income are exempt. Taxpayers in the middle (5th) decile pay tax on about 20% of their benefits; in the 6th decile approximately 38% of the benefits are taxed; in the 7th decile about 62% of the benefits are taxed, and in the 8th 78% are taxed. The top two deciles reach the maximum, and 85% of the benefits are taxed – or 15% are exempt.

## Vermont Income Tax on Social Security Benefits

Resident Details by Decile			Total Social Security Benefits (SSB)			Taxable Social Security Benefits							
Decile	AGI Range Resident Taxpayers		Total # Returns	# with SSB	Total SSB	Average Total SSB per return	# Pay Tax on SSB	Taxable SSB	Average Taxable SSB	Total Tax Paid on SSB	Average Tax Paid	% SSB Taxable	% Returns with SSB that Pay Tax
1	Less than	4,829	31,933	10,390	166,731,376	16,047	62	211,901	3,414	14	0	0.1%	0.6%
2	4,830	11,240	31,933	8,536	143,053,204	16,758	114	494,170	4,331	769	7	0.3%	1.3%
3	11,241	18,357	31,933	8,354	150,370,886	17,999	1,127	1,268,031	1,125	20,001	18	0.8%	13.5%
4	18,358	26,056	31,933	6,149	115,677,246	18,812	4,489	8,502,672	1,894	183,168	41	7.4%	73.0%
5	26,057	34,450	31,933	5,222	101,544,187	19,445	5,080	20,063,481	3,949	586,261	115	19.8%	97.3%
6	34,451	45,309	31,933	5,507	106,766,267	19,386	5,488	40,467,536	7,373	1,344,068	245	37.9%	99.7%
7	45,310	60,262	31,933	6,398	124,364,580	19,437	6,390	76,991,644	12,048	2,939,642	460	61.9%	99.9%
8	60,263	80,885	31,933	7,495	154,464,794	20,608	7,493	120,849,129	16,127	5,009,616	669	78.2%	100.0%
9	80,886	114,139	31,933	7,240	173,068,040	23,904	7,240	146,740,720	20,268	7,302,046	1,009	84.8%	100.0%
10	114,140 and Over		31,933	7,017	189,435,071	26,997	7,009	162,250,573	23,149	11,244,716	1,604	85.6%	99.9%
<b>Resident Totals</b>			<b>319,330</b>	<b>72,311</b>	<b>1,425,475,650</b>	<b>19,713</b>	<b>44,494</b>	<b>577,839,854</b>	<b>12,987</b>	<b>28,630,301</b>	<b>643</b>	<b>40.5%</b>	<b>61.5%</b>
Non Resident Totals			53,576	6,741	154,322,763	22,894	5,511	99,937,884	18,133	1,129,204	205	64.8%	81.8%
<b>Total all Tax Returns</b>			<b>372,906</b>	<b>79,051</b>	<b>1,579,798,413</b>	<b>19,984</b>	<b>50,005</b>	<b>677,777,738</b>	<b>13,554</b>	<b>29,759,505</b>	<b>595</b>	<b>42.9%</b>	<b>63.3%</b>

Source: Chainbridge Vermont Income Tax Model

This table includes detailed information on the number of returns, AGI income level, total amount of Social Security benefits, the taxable portion of Social Security benefits and the amount of tax paid on those benefits. The amount of benefits that are taxed increases as income increases so it is the highest income taxpayers that pay taxes on a higher portion of their benefits.

Vermont collected \$29.8 million from the taxation of Social Security benefits in TY 2013. Of the total tax revenue collected on Social Security benefits, 65% comes from the top two deciles, with \$7.3 million (26%) paid by those between \$80,000 and \$114,000 adjusted gross income and \$11.2 million (39%) paid by those with total incomes greater than \$114,000. Social Security benefits are distributed across all of the deciles; the tax on these benefits is paid by the highest income taxpayers.

The average Social Security benefit per return was \$19,713 for residents. The last two columns show the percentage of the total benefits that are taxable and the percentage of returns that pay tax on their benefits by decile.

Lastly, because of national demographics, the core of the baby boom has only just begun receiving benefits; both the number of beneficiaries and the amount of taxes on benefits paid will increase substantially in the near future.

## Taxation of Social Security Benefits Across the States

Of the 50 states and Washington, D.C., 37 and Washington D.C. have no income tax on any Social Security benefits; 13 states, including Vermont, tax a portion of the benefits based on income level or age. Of those 13, five follow the federal treatment while eight have a partial benefit exemption based on either income level or age. Often the tax treatment of Social Security benefits mirrors the treatment of other retirement income sources. State-specific tax treatment may be more or less beneficial than federal tax treatment. More details are included below.

Tax Treatment of Social Security Benefits	State
No State Income Tax (9)	Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington and Wyoming (Note NH and TN tax interest and dividend income)
Social Security Benefits Exempt (28 and DC)	Alabama, Arizona, Arkansas, California, Delaware, DC, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Mississippi, New Jersey, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Virginia, and Wisconsin
Same as Federal (5) based on income level	Minnesota, New Mexico, North Dakota, Vermont and West Virginia
Partial Exemption (8) based on income level or age	Colorado, Connecticut, Kansas, Missouri, Montana, Nebraska, Rhode Island, and Utah

### Partial Exemption State Details

State	Social Security Benefits Tax Treatment
Colorado	Age 55-64 up to \$20,000 pension income – including SS benefits -- are exempt. Age 65+ up to \$25,000 pension income – including SS benefits -- are exempt.
Connecticut	AGI < \$60K MFJ and \$50K single no tax on Social Security benefits AGI > than those thresholds exempt the difference between the amount included for federal income tax purposes and the lesser of 25% of the excess of the taxpayer's MAGI
Kansas	AGI < \$75K all Social Security benefits exempt
Missouri	AGI < \$100K MFJ and \$85K Single all Social Security benefits exempt
Montana	AGI < \$25K Single; \$32K HOH and MFJ all SS benefits exempt
Nebraska	AGI < \$43K Single; \$58K MFJ all Social Security benefits exempt
Rhode Island	AGI < \$80K Single; HOH or Separate; \$100K MFJ all SS benefits exempt
Utah	Utah taxpayers may be able to claim a retirement tax credit of up to \$450 under age 65 and \$900 over age 65. Previously, an income exclusion was allowed taxpayers age 65 or over, and a deduction of retirement income received was allowed taxpayers under the age of 65. The credit will be phased out by a percentage of the excess modified gross income, over a certain amount based on filing status.

Source: State Tax Treatment of Social Security, Pension Income [https://c342180.ssl.cf1.rackcdn.com/wp-content/uploads/2011/12/state\\_tax\\_treat\\_ss\\_pi\\_2015.pdf](https://c342180.ssl.cf1.rackcdn.com/wp-content/uploads/2011/12/state_tax_treat_ss_pi_2015.pdf)