

# Minnesota's Taxation of Social Security Income

February 2020

## Part or all of a taxpayer's Social Security benefits are exempt from Minnesota's income tax

Only a portion of a taxpayer's Social Security income is subject to Minnesota's income tax. There are two separate tax policies that result in Social Security income being nontaxable—an exclusion in federal law that “flows through” to the taxpayer's Minnesota income tax, and an additional Minnesota-specific subtraction available for a portion of the income that is taxable federally. In tax year 2017, about 565,000 resident returns in Minnesota reported about \$12.8 billion in Social Security income. Of that amount, 48.9 percent was taxable federally, and about 41.3 percent was taxable in Minnesota.

### Social Security Benefits Taxable Federally and in Minnesota, Minnesota Residents Filing Returns Only, Tax Year 2017

Federal Adjusted Gross Income	Total Soc. Sec. Income (\$)	Federal Exclusion (\$)	Minnesota Subtract. (\$)	% Taxable Federally	% Taxable, Minnesota
Less than \$25,000	3,604,000,000	3,521,000,000	69,000,000	0.5%	0.4%
\$25,000 to \$50,000	2,408,000,000	1,638,000,000	362,000,000	32.0%	16.9%
\$50,000 to \$75,000	2,076,000,000	653,000,000	337,000,000	68.6%	52.3%
\$75,000 to \$100,000	1,679,000,000	283,000,000	178,000,000	83.2%	72.6%
\$100,000 to \$150,000	1,823,000,000	280,000,000	17,000,000	84.7%	83.7%
\$150,000 and Greater	1,234,000,000	185,000,000	0	85.0%	85.0%
<b>Total</b>	<b>12,824,000,000</b>	<b>6,560,000,000</b>	<b>963,000,000</b>	<b>48.9%</b>	<b>41.3%</b>

Tax Year 2017 Estimates using the House Income Tax Simulation model. Compiled by House Research.

In December 2017, the Social Security Administration reported about \$1.368 billion in monthly Old-Age, Survivors, and Disability Insurance (OASDI) benefits were paid to Minnesota residents, which implies Minnesota residents earned about \$16.4 billion in total benefits that year. This implies that about \$3.6 billion in benefits were paid to taxpayers who did not file a return, likely because they had no Minnesota income tax liability. Including residents who did not file a return, **about 32 percent of all benefits paid to Minnesota residents were subject to Minnesota income tax.**

## The federal Social Security exclusion

The starting point for calculating Minnesota's income tax is Federal Adjusted Gross Income (FAGI), which is a federally defined measure of income minus certain exclusions. Any income that is not included in FAGI is not subject to Minnesota's income tax. Federal law allows taxpayers to exclude a portion of their Social Security income when calculating FAGI. This exclusion consequently applies to Minnesota's income tax. The formula used to calculate the exclusion is complicated; the amount of a taxpayer's exclusion depends on the taxpayer's provisional income (provisional income is discussed in detail in the final section of this publication). Social Security benefits included in FAGI are subject to federal tax in the manner as other ordinary income (e.g., wage, salary, and interest income).

The federal Social Security exclusion has three tiers. Depending on the taxpayer's provisional income, the federal exclusion is either 100 percent, 50 percent, or 15 percent of Social Security income. The table below shows the income ranges for the different tiers.

Married Couple's Provisional Income	Single Filer's Provisional Income	Exclusion Percentage
\$32,000 or less	\$25,000 or less	100%
<b>Tier 1:</b> \$32,000 to \$44,000	<b>Tier 1:</b> \$25,000 to \$34,000	50%
<b>Tier 2:</b> \$44,000 or greater	<b>Tier 2:</b> \$34,000 or greater	15%

Taxpayers with provisional income **below the first tier threshold** are allowed to exclude 100 percent of their Social Security income. For taxpayers with provisional income **between the first and second tier thresholds**, the amount of benefits subject to federal tax equals the lesser of:

- 50 percent of provisional income over the first tier threshold; or
- 50 percent of Social Security benefits.

For taxpayers with provisional income **above the second tier threshold**, the amount of benefits subject to federal tax equals the lesser of:

- 85 percent of provisional income over the second tier threshold, plus 50 percent of the difference between the second and first tier thresholds; or
- 85 percent of benefits.

## Minnesota's Social Security subtraction

Minnesota allows a subtraction for a portion of a taxpayer's Social Security income that is subject to federal tax. A taxpayer may claim the subtraction in addition to the federal exclusion. Taxpayers may subtract a portion of their taxable benefits, up to a maximum established in law. In tax year 2020 the maximum subtraction is \$5,240 for married taxpayers filing joint returns and \$4,090 for single taxpayers. The subtraction is phased out based on a taxpayer's provisional income—in tax year 2020, the phaseout begins at \$79,480 for married couples filing joint returns and \$62,090 for single taxpayers. The maximums and thresholds are adjusted annually for inflation.

About 290,000 taxpayers benefited from the subtraction in tax year 2017, resulting in a revenue decrease of about \$58.3 million. The average tax savings from the subtraction was about \$201.

## What is provisional income?

Provisional income is a federal definition of income equal to FGI, excluding taxable Social Security benefits, plus certain "above-the-line" deductions, plus nontaxable interest, plus 50 percent of Social Security benefits. The deductions that are added back in calculating provisional income are: adoption expenses, student loan interest, tuition expenses, certain foreign income, and income from Puerto Rico and certain other U.S. territories. The formula for provisional income is as follows:

### *Provisional Income*

$$= \text{FGI} - \text{Taxable Social Security Benefits} + 50\% \text{ of Social Security Benefits} \\ + \text{Nontaxable Interest} + \text{Certain above the line deductions}$$



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