

# Tax cuts from full Social Security exemption skewed to higher-income Minnesotans

The path to a stronger, more equitable recovery is through strengthening public services so that all Minnesotans, their families, and communities can thrive. But some policymakers want instead to enact billions of dollars in poorly targeted tax cuts that leave out the most struggling Minnesotans while giving the largest tax cuts to higher-income Minnesotans.

The Minnesota Senate Republican caucus has laid out two major tax cut priorities – expanding Minnesota’s tax exemption for Social Security benefits and cutting the income tax rate in the first bracket – with a total cost of \$8.5 billion over three years.<sup>1</sup> These tax cuts are tilted toward those with the most resources and would prevent making strong investments in schools, health care, child care, housing, and other public services that would create a brighter future for us all.

This issue brief looks at how and why higher-income Minnesotans get the most benefit from expanding state income tax exemptions to include all Social Security benefits.<sup>2</sup>

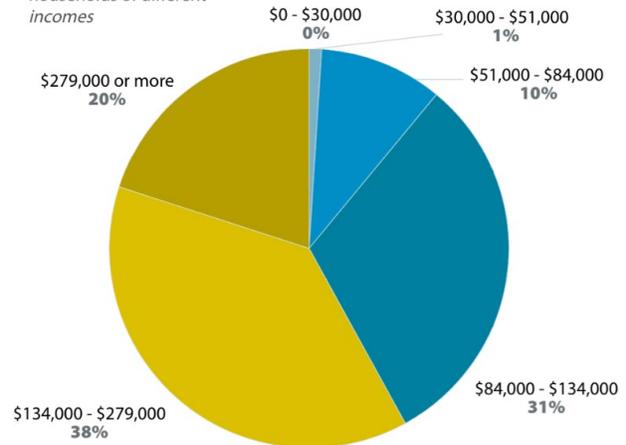
## Exempting all Social Security benefits gives the biggest tax cuts to higher-income households

If this proposal is intended to help seniors struggling to get by on fixed incomes, it fails to meet that goal. More than half of the Social Security tax cuts would go to households with incomes above \$134,000 – that’s the top 20 percent of the income distribution in Minnesota.<sup>3</sup> High-income seniors would receive annual tax cuts of \$1,000, \$2,000, or more simply because Social Security benefits are one of their sources of income.

Modest-income Minnesotans are less likely to get any tax cut from expanding the Social Security exemption, and any tax cut they receive would be smaller. Households with incomes \$279,000 and higher would get an average tax cut more than 20 times larger than what households with incomes \$30,000 to \$51,000 would receive, and more than five times than what households with incomes \$51,000 to \$84,000 would receive.

### More than half of Social Security tax cuts go to highest-income Minnesotans

Share of tax cuts going to households of different incomes



Source: Institute on Taxation and Economic Policy  
Minnesota Budget Project | [mnbudgetproject.org](http://mnbudgetproject.org)

Income	Average tax cut (for those with a cut)
<b>Less than \$30,000 (Lowest 20%)</b>	\$0
<b>\$30,000 - \$51,000 (Second 20%)</b>	\$102
<b>\$51,000 - \$84,000 (Middle 20%)</b>	\$398
<b>\$84,000 - \$134,000 (Fourth 20%)</b>	\$859
<b>\$134,000 - \$279,000 (Next 15%)</b>	\$1,432
<b>\$279,000 or more (Top 5%)</b>	\$2,130

## Federal and state tax laws already provide targeted Social Security tax exemptions

This proposal is so tilted towards higher-income households because both federal and state tax laws already provide tax exemptions for Social Security benefits that prioritize lower- and modest-income seniors.

Under federal tax laws, the lowest-income folks don't pay any federal income taxes on their Social Security benefits, and everyone has some of their Social Security benefits exempt. Minnesota follows this practice and adds additional exemptions targeted by income. The cumulative result is that about two-thirds of Social Security benefits going to Minnesota residents is already exempt from state income taxes.<sup>4</sup>

Understanding which Social Security benefits are exempt and which are taxable is complicated.<sup>5</sup> How much is exempt depends on a household's *provisional income*, which is their Federal Adjusted Gross Income minus taxable Social Security benefits plus some other kinds of income, including nontaxable interest and 50 percent of Social Security benefits.<sup>6</sup>

### Federal income tax treatment of Social Security benefits

	Single filers	Married filers
100% of Social Security benefits are exempt if provisional income is...	\$25,000 or less	\$32,000 or less
50% of Social Security benefits are exempt if provisional income is...	\$25,000 to \$34,000	\$32,000 to \$44,000
15% of Social Security benefits are exempt if provisional income is...	\$34,000 or more	\$44,000 or more

On top of the federal exemption, Minnesota provides an additional income tax subtraction. For the 2021 tax year, married couples with provisional incomes up to \$80,270 can exempt an additional \$5,290 of Social Security benefits from state income taxes, and single and head of household filers with incomes up to \$62,710 can exempt an additional \$4,130. Seniors with incomes above these thresholds can subtract smaller amounts of Social Security benefits until their provisional incomes reach \$106,720 for married couples or \$83,360 for single or head of household filers.<sup>7</sup> Both the income thresholds and amount of Social Security benefits that can be exempted are increased each year with inflation.

These special income tax exemptions and subtractions on Social Security benefits are in addition to the standard or itemized deductions that all Minnesotans can take that further reduce their taxable income.

The bottom line: the lowest-income Minnesotans don't pay any state income taxes on their Social Security benefits, and everyone has at least some of their income taxes exempt.

## Large tax cuts threaten essential public services

Fiscal estimates from the Minnesota Department of Revenue demonstrate how the cost of the proposed Social Security exemption would grow over time from \$510 million in FY 2023 to \$547 million in FY 2024 to \$579 million in FY 2025.<sup>8</sup> The cost will continue to grow as the number of Minnesota seniors grows. It would cut state revenues at the same time that the number of seniors is growing, and threaten the services they count on, whether those be community-based services to enable them to stay in their homes, transit services to get to the doctor or shopping, or high quality nursing home care. And as noted above, the majority of the tax cuts would go to high-income seniors, not those seniors struggling the most to pay the bills.

Proponents of this tax cut point out that there are other states that don't tax Social Security income. But those other states are facing severe financial challenges down the road that will make it more difficult to provide the

services seniors count on, or to invest in families and communities. The Center on Budget and Policy Priorities estimates that the cost of senior tax breaks provided by states will more than double from 2017 to 2030 with the growth of the senior population.<sup>9</sup>

While some middle-income Minnesotans would receive some benefit from this tax cut, so much more could be achieved by investing in public services that seniors and other Minnesotans count on to thrive.

The Senate Republican caucus reports their full tax cut package would total \$8.5 billion over three years. Enacting tax cuts of this magnitude would mean failing to invest in things from schools to child care to housing to infrastructure that Minnesotans, their families, and communities need to recover from the pandemic and its economic disruption.

Large tax cuts would also undermine the state's ability to fund public services in the future. Permanent tax cuts of this size are irresponsible when we know that some of the current large projected budget surpluses are being driven by short-term factors, including the positive effects that federal legislation have had on the economy, household incomes, and state budgets. For example, the additional federal aid to states is coming to an end, and families across the country have already seen their buying power drop because Congress allowed the federal Child Tax Credit expansion to expire.

Rather than this expensive proposal that gives the largest tax cuts to high-income seniors, Minnesota should continue to take a targeted approach to Social Security taxation that also protects sustainable funding for the public services that Minnesota seniors – and their children, grandchildren, friends, and neighbors – count on.

*By Nan Madden*

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<sup>1</sup> Minnesota Senate Republican Caucus, [Senate Republicans Propose Biggest Tax Cut Ever](#), February 24, 2022. Legislation to exempt all Social Security benefits from taxation have also been introduced by Independent and Democratic legislators.

<sup>2</sup> See also Minnesota Budget Project, [Costly first bracket income tax cut leaves out everyday Minnesotans](#).

<sup>3</sup> The data in this brief on the distribution of tax cuts by income group and average tax cut amounts are from Institute on Taxation and Economic Policy, March 2022, and model the impact on Minnesota residents.

<sup>4</sup> Minnesota House Research Department, [Taxation of Social Security Benefits in Minnesota](#), August 2020.

<sup>5</sup> Minnesota House Research Department has an online calculator that estimates state income taxes under current law and under a full exemption for households with various income levels. Visit <https://www.house.leg.state.mn.us/hrd/issinfo/sstaxes.aspx>.

<sup>6</sup> “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.” Minnesota House Research Department.

<sup>7</sup> Minnesota Department of Revenue, [Social Security Benefit Subtraction](#), accessed March 26, 2022.

<sup>8</sup> Minnesota Department of Revenue, [Revenue analysis of Senate File 2838](#), March 2022.

<sup>9</sup> Center on Budget and Policy Priorities, [States Should Target Senior Tax Breaks Only to Those Who Need Them, Free up Funds for Investments](#), June 2019.