



## Giving Retirees a Break

The Tax Modernization Committee recently released a list of potential tax reform options, including a proposal to either reduce or eliminate taxes on Social Security income.[\[i\]](#)

Nebraska is one of only six states to tax Social Security income to the same extent as the federal government, taxing up to 85 percent of benefits for individuals with income of at least \$32,000 per year, or \$40,000 per year for married couples.[\[ii\]](#) Seven other states also tax Social Security benefits but provide exemptions for incomes under a certain amount. Of our neighboring states, Missouri phased out its income tax of Social Security benefits last year, while Iowa will finish phasing out its taxation of Social Security next year, leaving Kansas as our only neighbor taxing Social Security benefits.[\[iii\]](#)

According to a 2010 study by the Congressional Research Service, approximately 16.9 million Social Security beneficiaries were affected by the federal income tax on Social Security in 2005, roughly 39 percent of all beneficiaries at that time. Because income thresholds determine tax liability and are not indexed for inflation, the number of seniors required to pay taxes on their Social Security benefits continues to grow. For example, the number of impacted beneficiaries increased from 26 to 32 percent in the two short years between 1998 and 2000.[\[iv\]](#) Despite its wide reach, taxing Social Security beneficiaries does not raise a significant amount of revenue, only generating roughly 2.1 percent of the Social Security Trust Fund's total

income in 2008.[\[v\]](#)

Because Social Security taxes are based on income thresholds, seniors with outside retirement incomes or pensions may exceed the threshold and be subjected to the tax.[\[vi\]](#) In essence, seniors who invested in their own retirement accounts or earned pensions from their employers, all while paying into the system, are penalized for not relying exclusively on Social Security benefits for retirement.

Taxing Social Security benefits also constitutes as double taxation; seniors were forced to pay into the system throughout their working life and then are taxed again when they became eligible to receive Social Security.

Although only Congress can provide seniors relief at the federal level, Nebraska can exempt Social Security income at the state level to allow seniors to keep more of their benefits and encourage retirees to remain in the state. Despite the homestead exemption for seniors with income under \$39,000, the taxation of Social Security benefits-coupled with the inheritance tax and some of the nation's highest property taxes-have made Nebraska one of the "least tax-friendly states for retirees," along with California, Connecticut, Maine, and Iowa.[\[vii\]](#) This puts Nebraska at a competitive disadvantage for keeping and attracting retirees, particularly when Wyoming, our neighbor to the northwest, has been ranked as the second most tax-friendly state for retirees, with no income tax, no estate or inheritance tax, a very low sales tax, and low property taxes.[\[viii\]](#) Research conducted by David Drozd of the University of Nebraska at Omaha also appears to show a correlation between retirees leaving the state due to high taxes.[\[ix\]](#) Apart from simply losing population, the loss of retirees is detrimental to Nebraska's economy because retirees are no longer spending their money in the state at local businesses, resulting in a loss of revenue for businesses who might otherwise sell to retirees and state and

local governments that lose out on the sales tax revenue that would otherwise come from those transactions. Research from the Tax Foundation shows that between 2000 and 2010, Nebraska lost approximately \$1.7 billion in personal income due to out-migration.<sup>[x]</sup> When Nebraska's net migration is compared with each state specifically over that same time period, it was found that emigrating Nebraskans tended to settle in the low-tax states of Texas, Florida, Arizona, South Dakota, and Colorado.<sup>[xi]</sup>

If Nebraska wants its residents to stay when they retire, and perhaps attract retirees from other states who could contribute to the economy, it should end the double taxation of Social Security benefits and eliminate the inheritance tax.

<sup>[i]</sup> Fred Knapp, "Nebraska tax change "options" headed for public hearings," *KVNO News*, September 9, 2013. Accessed September 16, 2013, <http://www.kvnonews.com/2013/09/nebraska-tax-change-options-headed-for-public-hearings/>.

<sup>[ii]</sup> Jennifer Habersham, "What States Tax Social Security Income?" March 17, 2013. Accessed September 16, 2013, [http://www.ehow.com/list\\_7290681\\_states-tax-social-security-income\\_.html](http://www.ehow.com/list_7290681_states-tax-social-security-income_.html); Christine Scott and Janemarie Mulvey, "Social Security: Calculation and History of Taxing Benefits," Congressional Research Service, January 15, 2010. Accessed September 16, 2013, <http://www.aging.senate.gov/crs/ss24.pdf>.

<sup>[iii]</sup> Jennifer Habersham, "What States Tax Social Security Income?" March 17, 2013. Accessed September 16, 2013, [http://www.ehow.com/list\\_7290681\\_states-tax-social-security-income\\_.html](http://www.ehow.com/list_7290681_states-tax-social-security-income_.html).

[iv] Christine Scott and Janemarie Mulvey, "Social Security: Calculation and History of Taxing Benefits," Congressional Research Service, January 15, 2010. Accessed September 16, 2013, <http://www.aging.senate.gov/crs/ss24.pdf>.

[v] Christine Scott and Janemarie Mulvey, "Social Security: Calculation and History of Taxing Benefits," Congressional Research Service, January 15, 2010. Accessed September 16, 2013, <http://www.aging.senate.gov/crs/ss24.pdf>.

[vi] Rachel L. Sheedy, "Strategies to Reduce Taxes on Social Security," *Kiplinger* September 1, 2010. Accessed September 16, 2013, <http://www.kiplinger.com/article/taxes/T051-C000-S001-strategies-to-reduce-taxes-on-social-security.html>.

[vii] Shelly Gigante, "The least tax-friendly states for retirees," *CNBC* August 22, 2013. Accessed September 16, 2013, <http://finance.yahoo.com/news/the-least-tax-friendly-state-for-retirees-174649409.html>.

[viii] Sandra Block, "10 Most Tax-Friendly States for Retirees: Wyoming," *Kiplinger* August 2013. Accessed September 16, 2013, <http://www.kiplinger.com/slideshow/retirement/T006-S001-10-most-tax-friendly-states-for-retirees/index.html>.

[ix] Joseph Moore, "Bills would exempt Social Security benefits from tax," *Nebraska News Service*, 2013. Accessed September 16, 2013, <http://kneb.com/news/index.php?more=3yjyws5j>.

[x] Richard Borean, "Monday Map: Migration of Personal Income," Tax Foundation, August 19, 2013. Accessed September 20, 2013, <http://taxfoundation.org/blog/monday-map-migration-personal-income>.

[xi] Tax Foundation, "State to State Migration Data." Accessed September 20, 2013, <http://interactive.taxfoundation.org/migration/>. That link is to the

overall table comparing Nebraska to all fifty states, specific state by state comparisons can be found by clicking individual states on that link, such as the example here:

<http://interactive.taxfoundation.org/migration/graph.php>.