What to Know About Social Security Benefits and Your Taxes

Plan ahead to keep Social Security income from raising your marginal tax rate.

Key Insights

- People in the 10%, 12%, and 22% federal tax brackets could be affected by high marginal tax rates caused by taxation of Social Security benefits.
- Planning ahead for required minimum distributions can help you minimize or avoid high tax rates.
- High marginal tax rates tend to affect people with relatively large annual Social Security benefits. But it’s not a good reason to lower your payments by claiming Social Security early.

Federal income taxes are fairly straightforward for most people during their working years because their income is primarily derived from a paycheck. “Income taxes in retirement may get more complicated, however,” says Roger Young, CFP®, a thought leadership director with T. Rowe Price. “This is because retirees are often receiving income from multiple sources with different tax characteristics, including Social Security.”

A calculation of your overall income dictates how much of your Social Security benefit is taxable. This calculated income (sometimes called “provisional” or “combined” income) is essentially half of your Social Security benefit plus other income, such as retirement plan distributions and any interest earned on municipal bonds.

Your Social Security benefits aren’t taxable up to a certain threshold of provisional income. Once above that threshold, however, there’s a graded scale of taxation:

- If your provisional income is $25,000 to $34,000 for single filers ($32,000 to $44,000 for joint filers), then up to 50% of your benefits are taxable.
- If your provisional income is more than $34,000 ($44,000 for joint filers), then up to 85% of your benefits are taxable.

In some cases, those in the 22% federal tax bracket could end up paying a marginal tax rate as high as 40.7% because additional retirement income causes more of their Social Security income to become taxable. (See the chart, “Social Security Income Can Raise Your Marginal Tax Rate.”)

Social Security Income Can Raise Your Marginal Tax Rate

Taxes on Social Security benefits can result in marginal rates of up to 40.7%.

Ordinary Marginal Tax Rate (A)	Additional Social Security Benefits Taxed (B)	Potential Total Marginal Rate (A x (1+B))
10%	50%	15%
10%	85%	18.5%
12%	50%	18%
12%	85%	22.2%
22%	85%	40.7%

Note: Not all people in these brackets will have the higher marginal rate.

Who Could Be Affected

People in the 10%, 12%, and 22% federal tax brackets could be affected by the high marginal rate, especially those with above-average Social Security benefits. If you're part of this group, consider working with a tax professional to fine-tune your retirement expenses, income, and tax projections. Doing so could help you determine whether additional planning or adjustments may be necessary.

Suppose you and your spouse collect $70,000 a year in combined annual Social Security benefits and your only other income is $65,000 of distributions from individual retirement accounts (IRAs). This makes your provisional income $100,000. At that level, you haven't quite reached the 85% cap on taxability of Social Security.* Now suppose you take an additional $1,000 from your IRA. You might expect to pay $220 more in taxes since you'll be in the 22% bracket. However, since that $1,000 results in $850 more of your Social Security benefits being subject to tax, your tax bill increases by $407 (22% of $1,850). Your marginal tax rate is really 40.7% at this point, but at higher income levels, it eventually goes back down to 22%. If there are steps you can take to minimize the income taxed at this level, they are worth considering.

Actions You Can Take

Since required minimum distributions (RMDs) may put you into this high marginal rate situation, it's important to plan before reaching age 73.** One strategy to consider is converting Traditional IRA assets to a Roth IRA. Converting at a relatively low tax rate early in retirement could reduce future RMDs that would push you into a higher bracket and trigger the 40.7% marginal rate described above.

Having some financial flexibility can also help you limit your highly taxed income. If you think you could be subject to high marginal rates, you may want to fund additional spending needs with income sources that generate little or no taxable income. This could include drawing on your cash reserve or a Roth account or selling off investments with small gains.

If you're approaching the point where the maximum 85% of your Social Security benefits are taxable, you could take more taxable distributions once you pass the 85% cap. That would free up cash to use next year so that you can avoid the high marginal rate in that year.

Considering Taxes

For many people, it's best to delay claiming Social Security until full retirement age or later. Waiting as long as possible to claim benefits reduces the chances of outliving your money while also maximizing survivor benefits (if you're the higher earner). While Social Security is part of a broader retirement income plan, taxes should be a secondary consideration. Remember that at least 15% of your Social Security income is exempt from federal income taxes no matter what. "Don't be tempted to claim Social Security early just because you may be affected by higher marginal rates," Young says.

Like many financial aspects of retirement, taxes on Social Security benefits can be confusing. "Fortunately," Young says, "a little planning can prevent it from being a major problem."

*The taxable portion of Social Security benefits is calculated as follows: 50% of combined income between $32,000 and $44,000 = $6,000. 85% of combined income over $44,000 = 85% x ($100,000 - $44,000) = $47,600. $6,000 + $47,600 = $53,600 of Social Security benefits included in taxable income. That is less than 85% of $70,000 ($59,500), so additional income would increase the taxable portion (until the point where $59,500 is taxed).
**The SECURE 2.0 Act of 2022 changes the required minimum distribution (RMD) age to 73 for individuals who turn age 72 on or after January 1, 2023. The new law also provides that the RMD age will change again to 75 in 2033.

Source: TRowePrice

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