

How Much Of My Social Security Do I Pay Tax On?



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It seems about once a week we get a phone call from someone considering retirement asking that question. The answer is simple, 0 to 85% or somewhere in between.

Several factors are involved when determining how much

Social Security income is taxable; the primary one being how much other income you have.

The rule states: Social Security benefits are 50% taxable to the extent income (as defined for this purpose) exceeds the base amount up to the additional amount and 85% taxable to the extent income exceeds the base plus additional amount, not to exceed 85% of total benefits. **That's quite a mouthful isn't it?**

I'm going to give two short examples to illustrate the importance of tax planning for Social Security and retirement. In both cases we are assuming one is retired (age 65) and the spouse is still working (age 64).

A- John & Jane Doe have \$15,600 S.S. benefits, \$16,000 pension income and a \$20,000 W2 for the spouse.

B-Bill & Mary Smith have \$15,600 S.S. benefits, \$16,000 pension income, a \$20,000 W2 for the spouse and a second W2 for \$5,000 from the retiree's part time job.

Using the rule above the Doe's taxable Social Security will be \$5,900 and the Smith's taxable Social Security will be \$10,080.

The Smiths will pay tax on an additional \$9,180 (\$5,000 Wages and \$4,180 increased taxable Social Security) when only \$5,000 additional income was received.

Using the 2005 tax rates and standard deduction (MFJ) with no additional dependents the Doe's total combined Federal and Missouri tax will be \$3,804 while the combined tax for the Smith's will be \$5,764

The difference is \$1,960 additional income tax (on \$5,000 additional W2 income).

When we add the Social Security and Medicare taxes (7.65% total) taken out of your paycheck you are only going to put \$2,657.50 of that extra \$5,000 in your pocket. That's about 53 cents on your dollar.

Kind of makes you think twice before taking that part time job doesn't it?

Keep in mind, this example only deals with taxes and Social Security. These rules don't change when you turn 65 or reach full retirement age. Many people confuse tax rules with the rules for reduction of Social Security benefits which do change upon reaching full retirement age.

As always, feel free to give us a call and we'll be happy to sit down with you and answer any questions you may have.

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