Saying ‘I Do’ after the 2001 Tax Cuts

Adam Carasso and C. Eugene Steuerle

Since 1948, when the nation moved from a system of individual taxation to one dependent on marital status, the effect of “marriage penalties” implicit in the tax code has sparked debate. Several recent trends have rekindled the debate: the increase in two-earner couples, the greater number of cohabitating couples paying less tax than similarly situated married couples, and the large marriage penalties faced by low-income individuals who lose tax and welfare benefits. This renewed interest aided passage of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), which contained a suite of relief provisions aimed directly at reducing marriage penalties.

Various provisions of the tax code can penalize—or subsidize—marriage, depending on each spouse’s income and number of children. Individuals pay a marriage “penalty” when their tax liability as a couple exceeds the sum of their liabilities as single individuals or single heads of household. A couple receives a marriage “subsidy” when its liability as a joint filer is less than if each partner had filed as a single.

While the 2001 legislation contained straightforward provisions reducing penalties (or increasing subsidies) for married couples without children, the law also effectively eased marriage penalties for heads of household with children. Unlike single tax filers, heads of household are often eligible for significant tax benefits that can be penalized away by marriage. In fact, the very design of tax programs targeting single-headed families—such as the earned income tax credit (EITC), and the child tax credit—is often what gives rise to such penalties, because additional household income or the event of marriage often excludes the family from participation. For low-income households, marriage can also significantly cut welfare benefits.

To examine marriage penalty relief for heads of household, this brief simulates the 2001 legislation’s effect on a range of hypothetical families with two children. The analysis primarily focuses on families earning less than $35,000—a group that tends to have the highest tax penalties (as well as penalties from other welfare programs)—though we also examine families with incomes as high as $80,000. Notably, the simulations reflect tax law in 2010, the year all EGTRRA provisions fully phase in. The analysis does not address whether legislators will extend the law beyond 2010, the year EGTRRA’s provisions sunset.

Lower-income households face some of the highest effective marginal tax rates, because additional income can both cause them to forfeit tax credits and incur tax liability. Take the EITC, a tax program that benefits low- to moderate-income working families with children. The EITC phases out at 21.06 cents for every dollar of income a household earns above $13,090. Now suppose a head of household with two children earning $10,000 marries someone earning $15,000. The household now has an income of $25,000, but the couple loses 21.06 percent of any income over the EITC’s beginning phaseout point of $13,090. Here, the marriage penalty arising from this one tax provision is a loss of $2,508 of credit. A couple’s total penalty or
The enhanced child credit—though not among EGTRRA’s stated marriage penalty relief provisions—helps couples the most.

subsidy reflects the combined impact of all provisions that force some of the couple’s income—whether from earnings or tax benefits—to be taxed at a different rate once they marry.

Figure 1 summarizes how marriage penalties and subsidies changed under the 2001 legislation. The figure plots the marriage penalty or subsidy at six different income levels under old law (dashed line) and under new law (solid line), depending on the secondary earner’s share of household income. In these hypothetical examples, the secondary earner is a head of household who had two children prior to the marriage. We calculate the couple’s marriage penalty or subsidy based on the earnings brought by the head of household to the marriage, ranging from 0 percent to 50 percent of total household earnings, in 10 percent increments. The difference between the two lines is the change in penalty or subsidy caused by the 2001 legislation.6

EGTRRA significantly reduces marriage penalties or increases marriage subsidies for most households. The new partially refundable, doubled child tax credit, the expanded EITC, and the new 10 percent tax bracket provide the most tax relief to low- and middle-income families. In fact, the revamped child credit alone does more for moderate-income couples with children than the combined provisions of the law’s advertised marriage penalty suite—that is, the expanded standard deduction, the EITC, and the 15 percent tax bracket.7 However, some families do less well, because by reducing individual tax rates, EGTRRA boosts the incentive to remaining single.

Overall, the new law creates less of a penalty or more of a subsidy at most household incomes and at most income shares for the secondary earner. But where increases in penalties or decreases in subsidies do occur, they are fairly small. In other words, the winners win a lot, while the losers lose a little.

The analysis also reveals the following:

• Among middle- and lower-income families, tax outcomes from marriage can range from about $7,000 in subsidies to $4,000 in penalties.
• The biggest reductions in penalties (or increases in subsidies), to the nearest $5,000 of income, are for households earning between $10,000 and $45,000.
• In general, households earning between $70,000 and $80,000 also benefit. In most cases, these households enjoy some reduction in penalties regardless of the share of earnings contributed by the secondary earner.
• Slight increases in penalties affect some households earning in the $45,000 to $75,000 range, when earnings are more evenly split between spouses.
• Families earning around $10,000 with income that is less evenly split confront slight reductions in subsidies.

EGTRRA and Marriage

The 2001 legislation affected marriage penalties primarily through six tax provisions: (1) the partially refundable, doubled child tax credit, (2) the higher EITC phase-out point for married couples only, (3) the new 10 percent tax bracket, (4) the expanded standard deduction applying only to married couples, (5) the expanded 15 percent tax bracket applying only to married couples, and (6) the new 25 percent tax bracket (lowered from 28 percent). Provisions 2, 4, and 5 comprise the legislation’s marriage penalty suite—that is, provisions advertised by Congress as reducing marriage penalties. Table 1 summarizes all six provisions and describes their general effects on marriage penalties.9

Overall, the reforms improved the incentives to marry among most couples with children in the moderate-income range of $10,000 to $45,000 as well as in many other income ranges. Households without children (i.e., marriages between two single filers), up to very high incomes, are even more likely to avoid any marriage penalty. This outcome occurs because the new law doubles the size of the standard deduction, the width of the 10 percent bracket, and the width of the 15 percent
FIGURE 1. Marriage Penalties Subsidies under Prior 2001 Tax Law and EGTRRA for a Married Couple with Two Children

Source: Authors' calculations.

Note: The “secondary earner” was a head of household with two children, prior to marriage. Her earnings are 0%, 10%, 20%, 30%, 40%, and 50% of household income in each example. The Primary Earner earns the balance, and was a single filer without children, prior to marriage.
bracket for married filers versus single filers. A few individuals may experience less of a marriage subsidy for a simple reason: because individual tax rates are lower, less tax rate reduction can be achieved by moving some income from a higher individual rate into a lower joint rate.

We examine the new law’s effect on marriage penalties among five hypothetical couples. Table 2 summarizes our results.

**Table 2. Summary of Results**

<table>
<thead>
<tr>
<th>Tax provision</th>
<th>AGI or taxable income</th>
<th>Prior 2001 law applied in 2010</th>
<th>New law applied in 2010</th>
<th>Marriage penalty effects: joint vs. single + HOH filers</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Child tax credit</strong></td>
<td>AGI</td>
<td>Nonrefundable credit of $403 per child (not indexed for inflation).&lt;sup&gt;1&lt;/sup&gt; Phaseout begins: HOH: $60,480 J joint: $88,704</td>
<td>Doubled to $806 per child (not indexed for inflation), refundable at a 15% rate on income above $10,000. Phaseouts unchanged.</td>
<td>Does the most to reduce marriage penalties. Provides an additional $403 per child in many cases; refundability adds up to another $403 per child for those who formerly could not take the credit. Penalties increased for some higher-earning couples.</td>
</tr>
<tr>
<td><strong>10% bracket</strong></td>
<td>Taxable income</td>
<td>Nonexistent</td>
<td><strong>Single:</strong> $0-$5,931 HOH: $0-$8,472, or 1.43 × single J joint: $0-$11,861, or 2.00 × single</td>
<td>Lowers penalties for many couples but increases penalties or lowers subsidies for others. Usually the most at stake is $297.</td>
</tr>
<tr>
<td><strong>Standard deduction</strong></td>
<td>Deduct from AGI</td>
<td>Single: $4,550 HOH: $6,650 J joint: $7,600, or 1.67 × single</td>
<td>Single: Unchanged HOH: Unchanged J joint: $9,100, or 2.00 × single</td>
<td>Generally reduces penalties on couples (except itemizers) that owe tax. Typically, the amount of relief is $225.</td>
</tr>
<tr>
<td><strong>15% bracket</strong></td>
<td>Taxable income</td>
<td>Single: $0-$27,050 HOH: $0-$36,250 J joint: $0-$45,200, or 1.67 × single</td>
<td>Single: $5,931-$27,050 HOH: $8,472-$36,250 J joint: $11,861-$54,100, or 2.00 × single</td>
<td>Additional marriage penalty relief of $513 for all couples earning near $75,000; $1,040 for couples earning $80,000.</td>
</tr>
<tr>
<td><strong>28% bracket</strong></td>
<td>Taxable income</td>
<td>28% tax rate Single: $27,050-$65,550 HOH: $36,250-$93,650 J joint: $45,200-$109,250, or 1.67 × single</td>
<td>25% tax rate Single: Unchanged HOH: Unchanged J joint: $54,100-$109,250, or 1.43 × single</td>
<td>Raises marriage penalties for middle- and higher-income couples, especially those with less even income splits.</td>
</tr>
</tbody>
</table>

**Notes:**
- **Marriage Penalty-related Provisions: New Law versus Old Law**
- **Source:** Joint Committee on Taxation (2001) and authors’ calculations.
- **Notes:** Amounts are in real 2001 dollars. Thus, $500 in 2010 is worth $403 in 2001 dollars. AGI = Adjusted Gross Income. HOH = Head of Household.
- a. Denotes whether parameters apply to AGI or taxable income. Tax brackets apply to taxable income. To determine where the brackets fall in terms of AGI, if the taxpayer takes the standard deduction and all personal exemptions, then add $7,450 for singles, $15,350 for heads of household, and $20,700 ($19,200 under old law) for joint filers to taxable income to arrive at AGI numbers.
- b. Under prior 2001 law, the child credit was refundable by the amount that a family’s social security taxes exceeded its EITC. This provision—known as “full refundability for excess dependents,” or FRED—is also applicable for families under new law if it provides them with higher benefits. Hence, some families need to calculate the child tax credit both ways and take the higher of the two.

**Couple 1:** A head of household with income of $9,000 marries a single filer with income of $21,000 (combined income of $30,000). Couple 1 benefits from the doubling of the child credit, the EITC expansion, the larger standard deduction, and the creation of the new 10 percent tax bracket. But the two spouses do not earn enough to benefit from the 15 percent bracket expansion or the new 25 percent tax rate.
Couple 2: A head of household with income of $15,000 marries a single filer earning $15,000 (combined income of $30,000). Couple 2 earns the same amount as couple 1, but its income is more evenly split. This couple benefits less from the child credit as a result of marriage. The mother, as head of household, already enjoyed a substantial fraction of the full child credit before she married, so that the additional income from marriage does not notably increase her child credit. This couple’s biggest gain is from less reduction in the EITC—relative to old law—once they marry.

Couple 3: A head of household with income of $6,000 marries a single filer with $14,000 of income (combined income of $20,000). This couple benefits greatly from the child credit, receiving an additional $1,500 relative to old law. While this couple also benefits from the EITC change, the two spouses do not earn enough to owe tax beyond the old standard deduction. Therefore, they do not benefit from the expanded standard deduction and the new 10 percent tax bracket.

Couple 4: A head of household with income of $24,000 marries a single filer with $36,000 of income (combined income of $60,000). Couple 4 pays slightly more marriage penalty as a result of the new law. The head of household already enjoyed the full child credit but had lost most of the EITC before marrying. Because the couple itemizes, the standard deduction offers no benefit. The new 10 percent and 25 percent tax brackets lower their taxes, but the new brackets reduce their gain from marriage relative to old law.

Couple 5: A head of household with income of $8,000 marries a single filer with $72,000 (combined income of $80,000). Couple 5 has one worker bringing in most of the earnings to the marriage. The couple receives an additional $806 of child credit under the new law. Even with the expanded EITC bracket, the head of household must give up a sizable EITC benefit. The proportionally wider 10 percent bracket for married couples nets another $297. The doubling of the 15 percent bracket for couples in proportion to singles is the largest source of additional marriage penalty relief, providing $1,040. As with couple 4, couple 5 itemizes, so the standard deduction does not apply, and the new 25 percent rate reduces the single worker’s gain from marriage.

**Directions for Future Policy Work**

Several EGTRRA provisions reduce marriage penalties, some by design and others indirectly. For households with children, the refundable, doubled child tax credit provides more marriage penalty relief than the suite of provisions officially targeted to

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**TABLE 2. Impact of Different Provisions on Marriage Penalties for Five Stylized Households**

<table>
<thead>
<tr>
<th>Provision</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Child credit</td>
<td>$(806)</td>
<td>$(56)</td>
<td>$(1,500)</td>
<td>$0</td>
<td>$(806)</td>
</tr>
<tr>
<td>EITC expansion</td>
<td>$(577)</td>
<td>$(577)</td>
<td>$(577)</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>Std. deduct.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>expansion</td>
<td>$(225)</td>
<td>$(225)</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>10% bracket</td>
<td>$(168)</td>
<td>$(168)</td>
<td>$297</td>
<td>$127</td>
<td>$(297)</td>
</tr>
<tr>
<td>15% bracket</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$(1,040)</td>
</tr>
<tr>
<td>28%-to-25% bracket</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$851</td>
</tr>
<tr>
<td>Total change in</td>
<td>$(1,776)</td>
<td>$(1,026)</td>
<td>$(1,780)</td>
<td>$127</td>
<td>$(1,292)</td>
</tr>
<tr>
<td>marriage penalty</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: Authors’ calculations. See Carasso and Steuerle (2002) for results for a range of other hypothetical households.*
that purpose. Moreover, this provision helps most households potentially subject to large marriage penalties resulting from other transfer programs. Even when the credit reduces tax incentives to marry (e.g., for some single heads of household earning more than $16,000 a year), the effect is slight. At $16,000 of income or higher, heads of household are also more likely to receive marriage subsidies from other tax provisions and are less likely to pay the penalties associated with means-tested or welfare programs.

Despite the improvements in the new law, the analysis reveals some missed opportunities to reduce penalties. For example, the gradual erosion of the child tax credit owing to inflation lessens its potential to ease EITC-related penalties over time. Indexing the child tax credit to inflation would readily solve this problem.

The law also did not achieve much in the way of simplification, and it complicated some provisions, such as the child tax credit. Making the child credit partially refundable helped reduce marriage penalties and increased net after-tax income for many heads of household. Effectively, the child credit now phases in as the EITC phases out. But a far simpler approach would have been to phase out the EITC more slowly.

Looking ahead, a more ambitious simplification measure would be to fully integrate the two child-related credits (the child tax credit and the EITC) into a single credit. Folding the dependent exemption into the new combined credit would further simplify the system. These options would also neatly tackle marriage penalty issues. Letting tax benefits go with the child—regardless of the household’s tax filing status and income level—will eliminate a whole category of marriage penalties. However, the proposed, integrated credit could phase out at a very slow rate, so that additional household income (including that gained through marriage) and filing status would generate smaller marriage penalties, and have a slighter effect on child-related benefits, than under EGTRRA. Several government organizations have also recommended that all programs adopt a uniform definition of “qualifying child” to ease administrative complexity and taxpayer confusion.

Another area worth reviewing is the head of household status. Lawmakers introduced the head of household tax brackets and standard deduction, in part, to help low-income households. Today, refundable credits make that goal less urgent. Our system of tax exemptions and deductions already shelters a good deal of income from any tax, making the filing status irrelevant for most lower-income households. Indeed, the tax-advantaged head-of-household rate schedule only benefits households with two children reporting income above $31,000, while the head of household’s added standard deduction amount only aids those earning more than $24,000. Families with income below $24,000 do not owe taxes and thus receive no benefit. In addition, the head of household status is the only filing status adjusted for the costs of raising children—joint filers do not similarly benefit.

Eliminating the head of household schedule would remove a major source of marriage penalties, as these filers would no longer lose so much by marrying. To maintain the spirit of the deduction, this measure could be achieved in a way that progressively allocates potential revenue savings back to households with children (e.g., by expanding other child-related benefits that are independent of filing status).

A final goal of reform should be to better integrate the EITC phaseout rate with the phaseout rates of key welfare programs such as food stamps, federal housing assistance, and Medicaid. The refundable portion of the child tax credit, which was designed with this concern in mind, is a good first step.

Despite the 2001 reforms, many low- to moderate-income households face significant marriage penalties, because of the interaction of programs on both the tax and expenditure side of the budget. Policymakers wishing to improve the plight of the working poor, and to bolster
marriage incentives, should view EGTRRA’s marriage penalty relief as a foundation on which to build.

Notes

1. See Carasso and Steuerle (2002) and Steuerle (1999) for more in-depth discussions of marriage penalties and the different ways they arise under the U.S. tax code.

2. Marriage penalties arising from welfare and income-conditioned programs, such as food stamps, housing subsidies, and health benefits, often fall heaviest upon heads of household. See Steuerle and Giannarelli (1996) for a detailed analysis.

3. An actual distributional analysis of marriage penalties and subsidies is complicated because, in addition to the difficulty of observing marriages that dissolve or do not occur as the result of marriage penalties, a relevant question is how large these penalties are for potential marriages.

4. The analysis does assume that lawmakers will adjust the alternative minimum tax prior to 2010.

5. These figures are for prior-2001 tax law extended out to 2010, with the amounts expressed in real 2001 dollars.

6. See appendix table 1 in Carasso and Steuerle (2002) for the underlying data points.

7. This point is especially significant since the child credit, though it doubles in nominal terms, is not indexed for inflation, so its real value in 2010 is about $800 rather than $1,000.

8. Generally, the more similar two persons’ incomes are, the more tax liability they will face if they marry.

9. For a provision-by-provision description of how EGTRRA changes marriage penalties and subsidies, see Carasso and Steuerle (2002).


11. This income is the head of household’s first point of tax entry, after one takes into account her standard deduction, personal exemptions for herself and her two children, the child credit, and the EITC.

References


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