Q. What is the child tax credit?

A. The child tax credit provides a credit of up to $2,000 per child under age 17. If the credit exceeds taxes owed, families may receive up to $1,400 per child as a refund. Other dependents—including children ages 17–18 and full-time college students ages 19–24—can receive a nonrefundable credit of up to $500 each.

HOW THE CHILD TAX CREDIT WORKS TODAY

Taxpayers can claim a child tax credit (CTC) of up to $2,000 for each child under age 17 who is a citizen. The credit is reduced by 5 percent of adjusted gross income over $200,000 for single parents ($400,000 for married couples). If the credit exceeds taxes owed, taxpayers can receive up to $1,400 of the balance as a refund, known as the additional child tax credit (ACTC) or refundable CTC. The ACTC is limited to 15 percent of earnings above $2,500 (figure 1).

For the most part, the CTC is not indexed for inflation. The exception to this is the amount of the credit families with children under 17 can receive as a refund. This amount (currently $1,400) will increase with inflation after 2018 until it becomes equal to the full value of the credit ($2,000).

Starting in 2018, a $500 credit is available to dependents who are not eligible for the $2,000 CTC for children under 17 (figure 1). Before 2018, these individuals would not have qualified for a tax credit but would have qualified for a dependent exemption, which was eliminated by the 2017 Tax Cuts and Jobs Act (TCJA). These include children ages 17–18 or those 19–24 and in school full time in at least five months of the year. Also included are older dependents—representing about 6 percent of dependents eligible for the CTC.

After 2025, the CTC is scheduled to revert to its pre-TCJA form. At that point, taxpayers will be able to claim a credit of up to $1,000 for each child under age 17 and the credit will be reduced by 5 percent of adjusted gross income over $75,000 ($110,000 for married couples). If the credit exceeds taxes owed, taxpayers will be able to receive the balance as a refund. The refundable portion of the credit will be limited to 15 percent of earnings above $3,000.

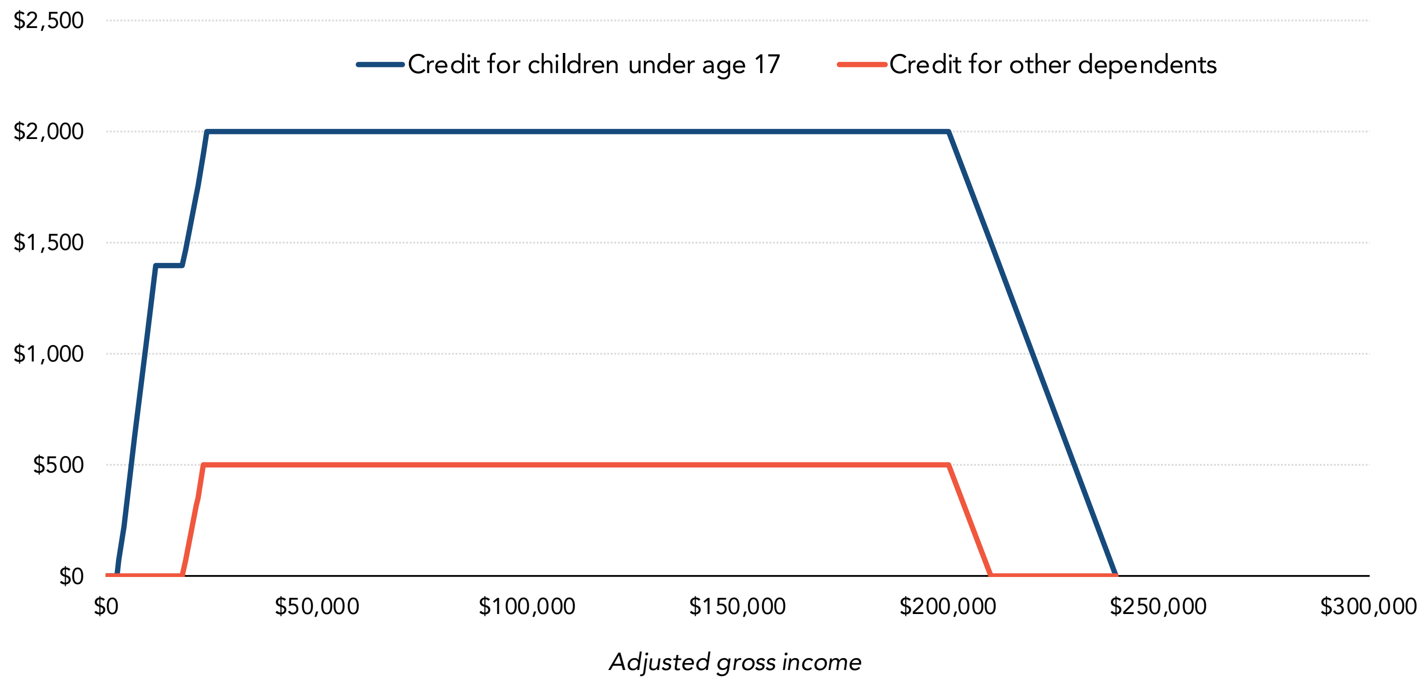
IMPACT OF THE CTC

The Tax Policy Center estimates that 91 percent of families with children will receive an average CTC of $2,420 in 2018 (the average credit can exceed the maximum per child credit because families can have more than one child). Families with children in all income groups will benefit from the CTC, but families in the lowest income quintile are least likely to benefit from the credit because more of them will not have sufficient earnings to qualify for the credit. Just over three-quarters of families in the lowest income quintile

Key Elements of the U.S. Tax System

What is the child tax credit?

FIGURE 1
Child Tax Credit, Single Parent
For one child, tax year 2018



Source: Urban-Brookings Tax Policy Center calculations.
Notes: Assumes all income comes from earnings, and child meets all tests to be a CTC-qualifying dependent. Credit for married parents begins to phase out at $400,000 of income. Only citizen children qualify for the $2,000 CTC for children under 17. Noncitizens under age 17 who meet the dependency tests of eligibility can qualify for the credit for dependents over age 17.

(the bottom one-fifth of the income distribution, ranked by household income) will be eligible for a CTC, receiving an average benefit of $1,340. The average credit is the smallest for this group because low-income families are most likely to be limited to the refundable portion of the credit, which is capped at $1,400 rather than the full $2,000 limit for the nonrefundable credit (figure 2).

The percentage of families with children receiving the credit and the average credit received are higher among moderate- and middle-income families. Almost 94 percent of families with children in the second income quintile will receive a CTC as will almost all families in the third and fourth income quintiles (98 and 99 percent, respectively). The proportion of families with children receiving a credit drops to 87 percent in the highest income group because of the income limits (figure 2).

The CTC has a significant impact on the economic well-being of low-income families with children. If the official estimate of poverty counted the CTC as income (including the refundable portion), 2.7 million fewer people would have fallen below the federal poverty line in 2016, including about 1.5 million children. Counting the credit would have also reduced the severity of poverty for an additional 12.3 million people, including 6.1 million children (Center on Budget and Policy Priorities 2018).

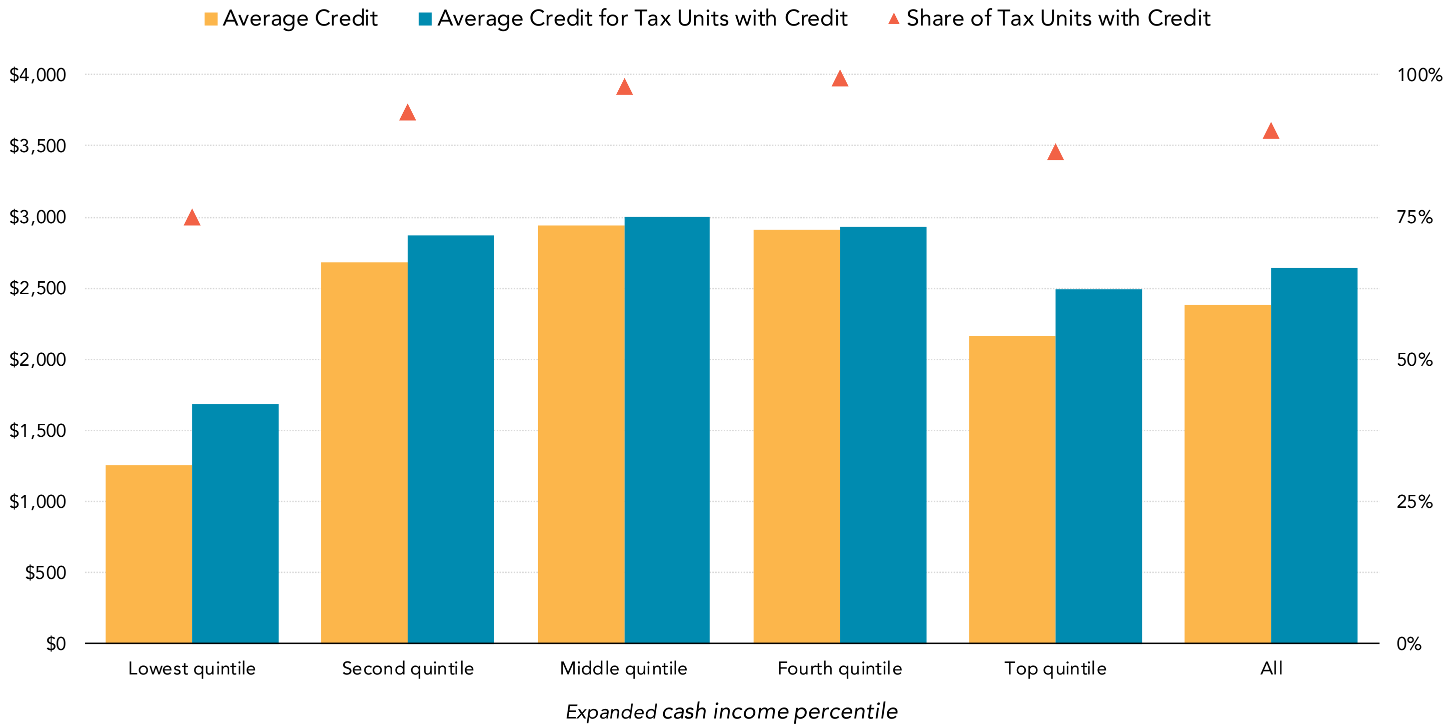
Key Elements of the U.S. Tax System

What is the child tax credit?

FIGURE 2

Distribution and Share of Child Tax Credit for Tax Units with Children

2018



Source: Urban-Brookings Tax Policy Center. "TPC Microsimulation Model, version 0718-1."
Note: Includes the $500 nonrefundable portion of the child tax credit, also referred to as the credit for other dependents.

RECENT HISTORY OF THE CTC

In 2018, the Tax Cuts and Jobs Act doubled the CTC for children under 17 from $1,000 per child to $2,000 per child, up to $1,400 of which families can receive as a refundable credit. Only children who are US citizens may receive this credit. The legislation also allows dependents who do not qualify for the $2,000 credit to qualify for a nonrefundable credit worth up to $500. The legislation is temporary and expires after 2025. At that point, the credit for children under 17 will revert to $1,000 per child, and other dependents will no longer be eligible for a CTC.

Before these changes, the American Taxpayer Relief Act of 2012 had increased the CTC from $500 per child, its pre-2001 level, to $1,000 per child. It also temporarily extended the provisions of the American Recovery and Reinvestment Act of 2009 (the anti-recession stimulus package) that reduced the earnings threshold for the refundable CTC from $10,000 (adjusted for inflation starting after 2002) to $3,000 (not adjusted for inflation). The Bipartisan Budget Act of 2015 made the $3,000 refundability threshold permanent. The TCJA further reduced the refundability threshold to $2,500 starting in 2018, but that lower threshold will expire after 2025 when the $3,000 refundability threshold will return.

Key Elements of the U.S. Tax System

What is the child tax credit?

The refundable CTC was originally designed in 2001 to coordinate with the earned income tax credit (EITC). Once earnings reached $10,020 for families with two children in 2001, there was no further increase in the EITC. The earnings threshold for the refundable CTC was set at $10,000 so families could now receive a subsidy for earnings in excess of that amount. Like the earned income amount for the EITC, the $10,000 earnings threshold was indexed for inflation. When the earnings threshold for the refundable CTC was reduced—first to $8,500 in 2008 and then to $3,000 in 2009—that link between the phase-in of the refundable CTC and the EITC was broken.

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Q. What is the adoption tax credit?

A. The tax code provides an adoption credit of up to $13,810 of qualified expenses (in 2018) for each child adopted, whether via public foster care, domestic private adoption, or international adoption. The total amount of adoption credits for 2018 is estimated to reach approximately $400 million.

CREDIT AMOUNT

Taxpayers can receive a tax credit for all qualifying adoption expenses up to $13,810 in 2018. The maximum credit is indexed for inflation. Taxpayers may also exclude from income qualified adoption expenses paid or reimbursed by an employer, up to the same limit as the credit. Taxpayers can use the tax credit and the income exclusion but cannot claim the same expenses for both.

“Special needs” adoptions automatically qualify for the maximum credit regardless of actual out-of-pocket expenses. For purposes of the credit, a child has special needs if a state’s welfare agency determines that the child cannot or should not be returned to his or her parents’ home and that the child probably will not be adoptable without assistance provided to the adoptive family. This provision is designed to encourage parents to adopt children who would otherwise be hard to place, even if most of the adoption expenses are covered by someone else (such as a public foster care program).

ELIGIBILITY

The adoption credit is available to most adoptive parents, with some exceptions. The credit is not available to taxpayers whose income exceeds certain thresholds. The thresholds are indexed for inflation. In 2018 the credit begins to phase out at $207,140 of modified adjusted gross income and phases out entirely at income of $247,140. The credit also is not available for adoptions of stepchildren.

REFUNDABILITY

The adoption tax credit is nonrefundable but can be carried forward for up to five years. The credit is thus of little or no value to low-income families who pay little or no income tax over a period of years. The Patient Protection and Affordable Care Act of 2010 made the adoption tax credit refundable for 2010 and 2011. Concerned about the potential for fraud, the Internal Revenue Service (IRS) stepped up compliance efforts. The result, according to the National Taxpayer Advocate Service, was substantial delays for taxpayers, with 69 percent of all adoption credit claims filed in 2012 selected for audit. The IRS ultimately disallowed only 1.5 percent of claims, and 20 percent of the savings from the disallowed credits was spent on interest owed to taxpayers with delayed refunds. The credit reverted to nonrefundability in 2012.

Key Elements of the U.S. Tax System

What is the adoption tax credit?

COST OF THE CREDIT

The credit has been repeatedly expanded, from an initial maximum value of $5,000 in 1997 to $13,810 in 2018. In 2016, taxpayers claimed total adoption credit of $290 million (figure 1). The temporary availability of a refundable credit pushed the cost of the credit up to the dramatically higher figures of $1.2 billion in 2010 and $610 million in 2011 (including the refundable portion).

WHO GETS IT

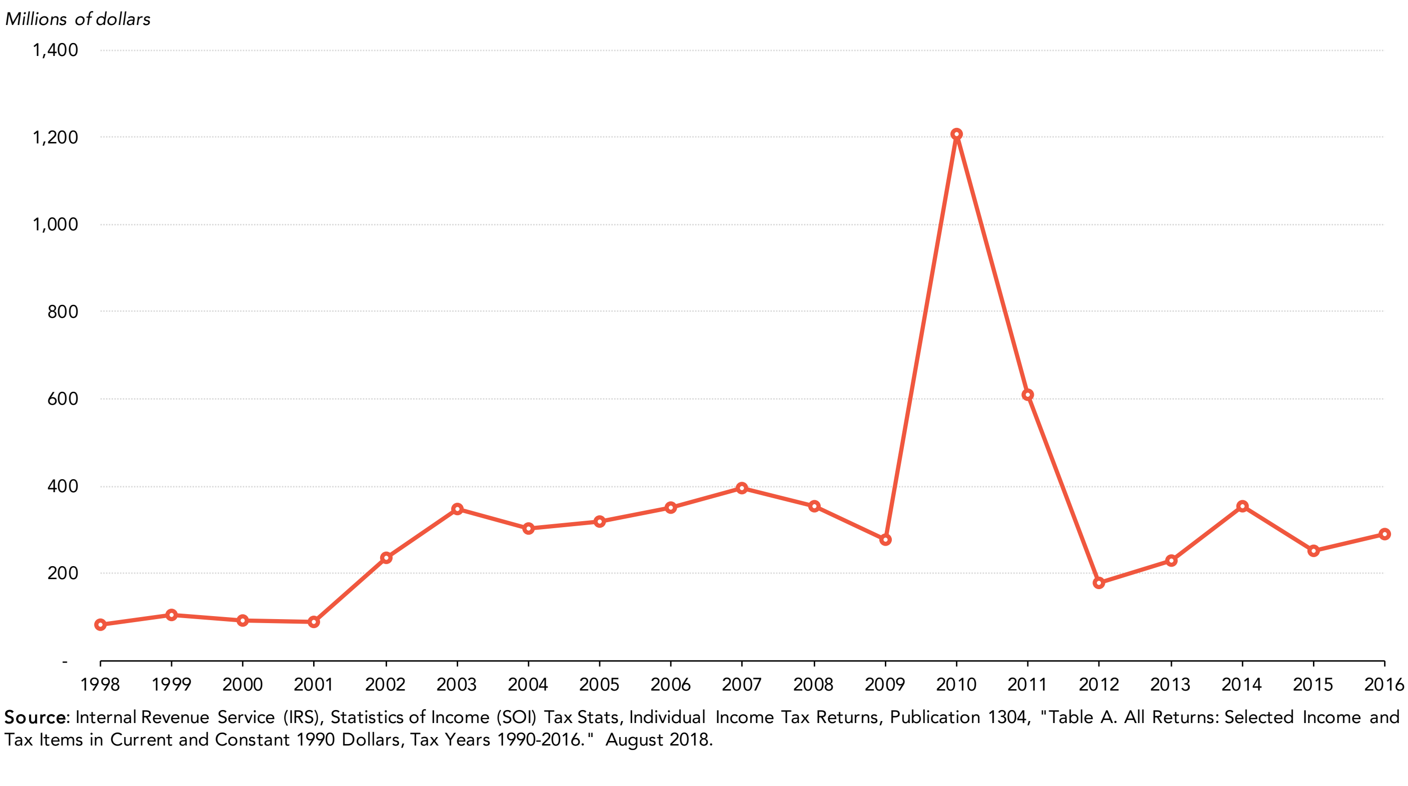
The distribution of the credit across income groups ranges from small amounts for low- and moderate-income households (because of their minimal tax liability and the credit's nonrefundability) and the highest-income households (because of the income cap) to substantial amounts to those with upper-middle incomes. For example, in tax year 2016, the credit for those with incomes between $50,000 and $75,000 (almost one-third of claimants) averaged $2,388 per adoption, while the average credit for households with incomes between $100,000 and $200,000 (about 30 percent of claimants) was $7,233 per adoption (table 1).

The most recent year with data available by adoption type (2004) indicates that nearly half of adoptions for which the credit was claimed were for domestic children without special needs, with only 18 percent classified as special needs, and the remainder reflecting international adoptions.

FIGURE 1

Cost of the Adoption Credit

Tax years 1998–2016



Source: Internal Revenue Service (IRS), Statistics of Income (SOI) Tax Stats, Individual Income Tax Returns, Publication 1304, "Table A. All Returns: Selected Income and Tax Items in Current and Constant 1990 Dollars, Tax Years 1990-2016." August 2018.

Key Elements of the U.S. Tax System

What is the adoption tax credit?

TABLE 1

Distribution of Adoption Credit

By adjusted gross income, tax year 2016

Size of Adjusted Gross Income (dollars)	Total Number of Returns with Eligible Expenses	Total Amount of Benefits	Average Amount of Credit
Less than $40,000	7,113	$5,392,000	$758
$40,000 – under $50,000	6,337	$10,795,000	$1,703
$50,000 – under $75,000	21,421	$51,154,000	$2,388
$75,000 – under $100,000	10,639	$48,944,000	$4,600
$100,000 – under $200,000	20,074	$169,067,000	$8,422
$200,000 and over	666	$4,817,000	$7,233
All returns	66,250	$290,168,000	$4,380

Source: Internal Revenue Service (IRS), Statistics of Income (SOI) Tax Stats, Individual Income Tax Returns, Publication 1304, "Table 3.3 All Returns: Tax Liability, Tax Credits, and Tax Payments, by Size of Adjusted Gross Income, Tax Year 2016 (Filing Year 2017)." August 2018.

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Q. What is the earned income tax credit?

A. The earned income tax credit subsidizes low-income working families. The credit equals a fixed percentage of earnings from the first dollar of earnings until the credit reaches its maximum. The maximum credit is paid until earnings reach a specified level, after which it declines with each additional dollar of income until no credit is available.

HOW THE EARNED INCOME TAX CREDIT WORKS

The earned income tax credit (EITC) provides substantial support to low- and moderate-income working parents, but very little support to workers without qualifying children (often called childless workers). Workers receive a credit equal to a percentage of their earnings up to a maximum credit. Both the credit rate and the maximum credit vary by family size, with larger credits available to families with more children. After the credit reaches its maximum, it remains flat until earnings reach the phaseout point. Thereafter, it declines with each additional dollar of income until no credit is available (figure 1).

By design, the EITC only benefits working families. Families with children receive a much larger credit than workers without qualifying children. (A qualifying child must meet requirements based on relationship, age, residency, and tax filing status.) In 2018, the maximum credit for families with one child is $3,461, while the maximum credit for families with three or more children is $6,431.

In contrast to the substantial credit for workers with children, childless workers can receive a maximum credit of only $519. Moreover, the credit for childless workers phases out at much lower incomes. Also, childless workers must be at least 25 and not older than 64 to qualify for a subsidy—restrictions that do not apply to workers with children. As a result of these tighter rules, 97 percent of benefits from the credit go to families with children.

IMPACT OF THE EITC

Research shows that the EITC encourages single people and primary earners in married couples to work (Dickert, Houser, and Sholz 1995; Eissa and Liebman 1996; Meyer and Rosenbaum 2000, 2001). The credit, however, appears to have little effect on the number of hours they work once employed. Although the EITC phaseout could cause people to reduce their hours (because credits are lost for each additional dollar of eanings, which is effectively a surtax on earnings in the phaseout range), there is little empirical evidence of this happening (Meyer 2002).

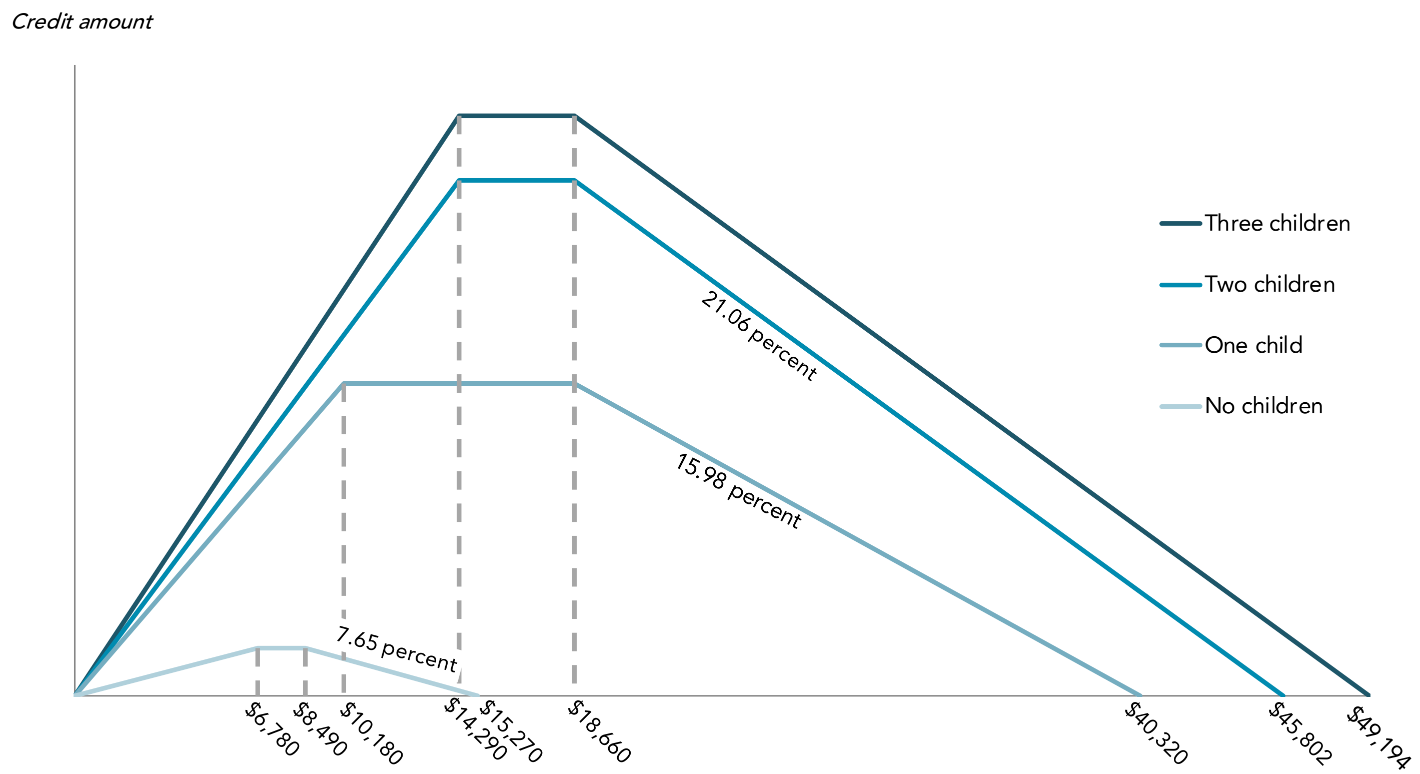
Key Elements of the U.S. Tax System

What is the earned income tax credit?

FIGURE 1

Earned Income Tax Credit

2018



Source: Urban-Brookings Tax Policy Center (2018). Internal Revenue Procedure 2018-18, Internal Revenue Service.
Notes: Assumes all income comes from earnings. Amounts are for taxpayers filing a single or head-of-household tax return. For married couples filing a joint tax return, the credit begins to phase out at income $5,690 higher than shown.

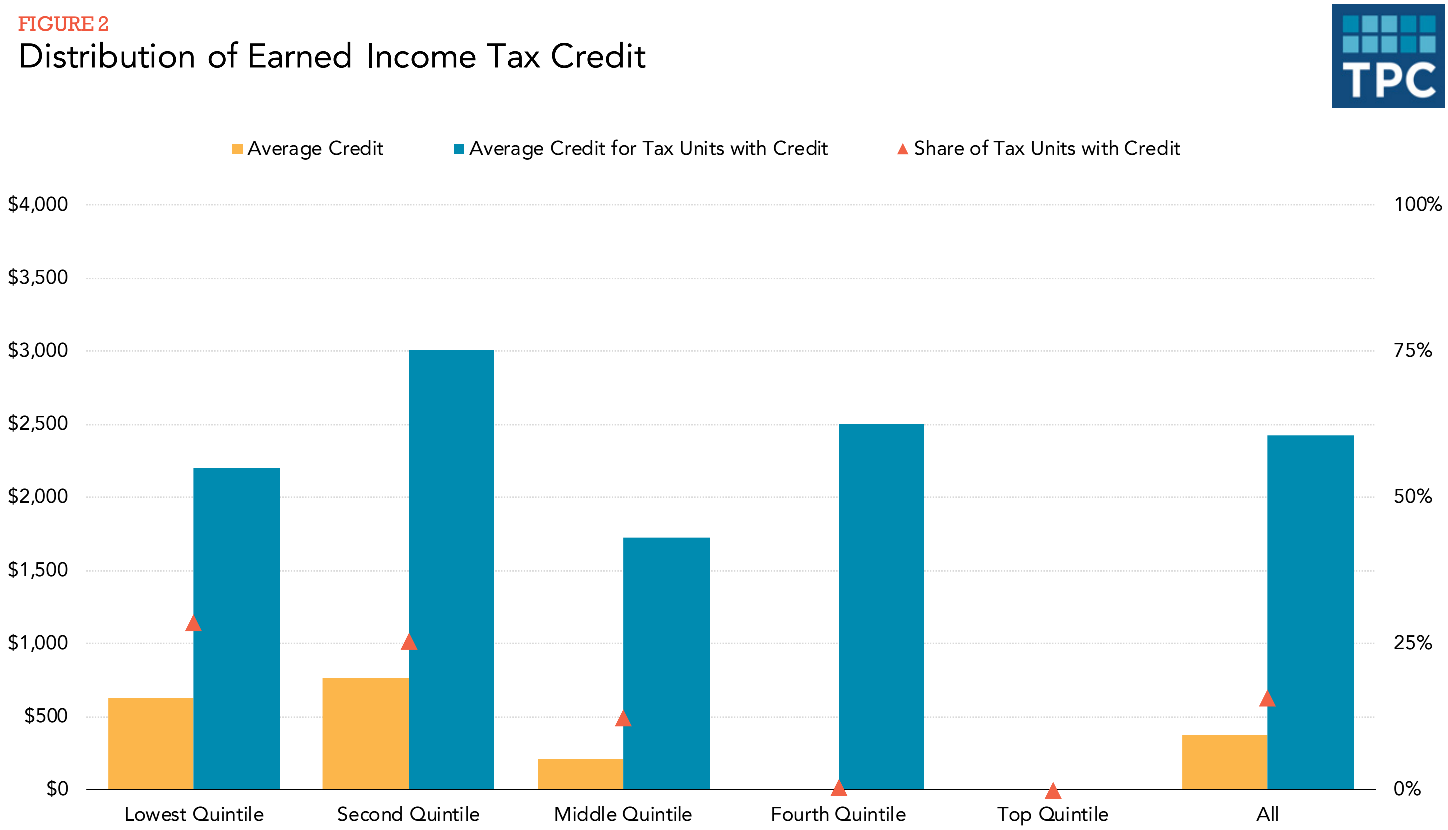
The one group of people that may reduce hours of work in response to the EITC incentives is lower-earning spouses in a married couple (Eissa and Hoynes 2006). On balance, though, the increase in work resulting from the EITC dwarfs the decline in participation among second earners in married couples.

If the EITC were treated like earnings, it would have been the single most effective antipoverty program for working-age people, lifting about 5.8 million people out of poverty, including 3 million children (CBPP 2018). The EITC is concentrated among the lowest earners, with almost all of the credit going to households in the bottom three quintiles of the income distribution (figure 2). (Each quinitle contains 20 percent of the population, ranked by household income.) Very few households in the fourth quinitle receive an EITC (fewer than 0.5 percent).

Key Elements of the U.S. Tax System

What is the earned income tax credit?

FIGURE 2
Distribution of Earned Income Tax Credit



Source: Urban-Brookings Tax Policy Center. "TPC Microsimulation Model, version 0718-1."

RECENT CHANGES

As a result of legislation enacted in 2001, the EITC phases out at higher income levels for married couples than for single individuals. That threshold was increased as part of the American Recovery and Reinvestment Act of 2009 (ARRA). The same act increased the maximum EITC for workers with at least three children. The American Taxpayer Relief Act of 2012 made the 2001 EITC changes permanent (a $3,000 higher threshold for married couple phaseout, indexed) but extended the ARRA changes (a $5,000 higher threshold for married couple phaseout, indexed, and higher credit maximum for workers with at least three children) through the end of 2017. The Protecting Americans from Tax Hikes Act of 2015 made these changes permanent. The Tax Cuts and Jobs Act, enacted in 2017, adopted a more conservative measure of inflation to be used in the federal income tax system beginning in 2018. As a result, the EITC will grow more slowly over time.

PROPOSALS FOR REFORM

Both Democrats and Republicans have proposed EITC amendments to provide a substantial credit for childless workers. These proposals typically involve expanding the eligible age limits for the childless EITC—lowering the age of eligibility from 25 to 21 and increasing the age of eligibility from 64 to 67—increasing the maximum credit, and expanding the income range over which the credit is available. A more far-reaching approach to reform that would still expand benefits to childless workers would be to separate the credit into two pieces—one focused on work and one focused on children. Examples of this type of reform have been proposed by many, including the President's Advisory Panel on Federal Tax Reform (2005), the Bipartisan Policy Center (2013), and Maag (2015b).

ERROR RATES AND THE EITC

The EITC likely delivers more than a quarter (28.5 percent) of all payments in error, according to a recent Internal Revenue Service (IRS) compliance study. The largest source of error was determining whether a child claimed for the EITC actually qualified (IRS 2014). The child must live with the parent (or other relative) claiming the EITC for more than half of the year in order to qualify. The IRS receives no administrative data that can verify where a child resided for the majority of the year, making it difficult for the agency to monitor compliance. Attempts to use administrative data from other programs to verify child residence have not proven successful (Pergamit et al. 2014).

To reduce fraud, the Protecting Americans from Tax Hikes Act of 2015 requires the IRS to delay tax refunds for taxpayers who claim an EITC or additional child tax credit on their returns until at least February 15. Delaying refunds was paired with a requirement that third-party income documents related to wages and income be provided to the IRS by January 31 (in prior years, this information was due the last day of February for paper filing and March 31 for electronic filing, and employers were automatically granted a 30-day extension, if requested). As a result, information needed to verify wages often got to the IRS well after the first returns had been processed. Together, these measures allowed earlier systemic verification of EITC claims, which protected more revenue than in prior years (Treasury Inspector General for Tax Administration 2018).

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Key Elements of the U.S. Tax System

What is the earned income tax credit?

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Q. How does the tax system subsidize child care expenses?

A. Working parents are eligible for two tax benefits to offset child care costs: the child and dependent care tax credit and the exclusion for employer-provided child care.

THE CHILD AND DEPENDENT CARE TAX CREDIT

The child and dependent care tax credit (CDCTC) provides a credit worth between 20 and 35 percent of child care costs for a child under age 13 or any dependent physically or mentally incapable of self-care. Eligible child care expenses are limited to $3,000 per dependent (up to $6,000 for two or more dependents). Higher credit rates apply to families with lower adjusted gross income. Families with incomes below $15,000 qualify for the full 35 percent credit. That rate falls by 1 percentage point for each additional $2,000 of income (or part thereof) until it reaches 20 percent for families with incomes of $43,000 or more. The credit is nonrefundable so it can only be used to offset income taxes owed—in other words, any excess credit beyond taxes owed is forfeited. As a result, low-income families who owe little or no income tax get little benefit from the credit (table 1).

To qualify for the CDCTC, a single parent must be working or in school. For married couples, both adults must be working or attending school. In general, allowable expenses are capped at the earnings of the lower-earning spouse. Special rules allow individuals who were students or disabled to have their earned income assumed to be $250 per month ($500 if there is more than one qualifying child).

The Urban-Brookings Tax Policy Center estimates that, in 2018, 11.8 percent of families with children benefited from the CDCTC. Some families with children will not benefit because they do not have child care expenses or, in the case of married couples, only one partner works or goes to school. Among families with children who benefit from the CDCTC, taxes will be reduced by an average of $593. The only income quintile in which families average substantially different benefits is the lowest. (Each quintile contains 20 percent of the population ranked by household income.) Not only are their child care expenses likely to be lower than those of families in higher-income quintiles, they are typically unable to benefit from the credit because the CDCTC is nonrefundable (figure 1).

How does the tax system subsidize child care expenses?

TABLE 1

Child and Dependent Care Credit

2018

Adjusted gross income (dollars)	Credit rate (percent)	Maximum Credit (dollars)	
		One child	Two or more children
15,000 or less	35	1,050	2,100
15,001–17,000	34	1,020	2,040
17,001–19,000	33	990	1,980
19,001–21,000	32	960	1,920
21,001–23,000	31	930	1,860
23,001–25,000	30	900	1,800
25,001–27,000	29	870	1,740
27,001–29,000	28	840	1,680
29,001–31,000	27	810	1,620
31,001–33,000	26	780	1,560
33,001–35,000	25	750	1,500
35,001–37,000	24	720	1,440
37,001–39,000	23	690	1,380
39,001–41,000	22	660	1,320
41,001–43,000	21	630	1,260
43,000 and over	20	600	1,200

Sources: Internal Revenue Service. "Publication 503—Main Content." Accessed November 23, 2015; Urban-Brookings Tax Policy Center. "TPC Microsimulation Model, version 0718-1."

EMPLOYER EXCLUSION: FLEXIBLE SPENDING ACCOUNTS

Employer-provided child and dependent care benefits include amounts paid directly for care, the value of care in a day care facility provided or sponsored by an employer, and, more commonly, contributions made to a dependent care flexible spending account (FSA).

Employees can set aside up to $5,000 per year of their salary (regardless of the number of children) in an FSA to pay child care expenses. (FSAs are also available for health care expenses.) The money set aside in an FSA is not subject to income or payroll taxes. Unlike the CDCTC, though, which requires both partners in a married couple to work to claim benefits, only one parent must work to claim a benefit from an FSA. In 2014, 39 percent of civilian workers had access to a dependent care FSA (Bureau of Labor Statistics 2014). Lower earners are less likely to have access to an FSA than higher earners (Stoltzfus 2015).

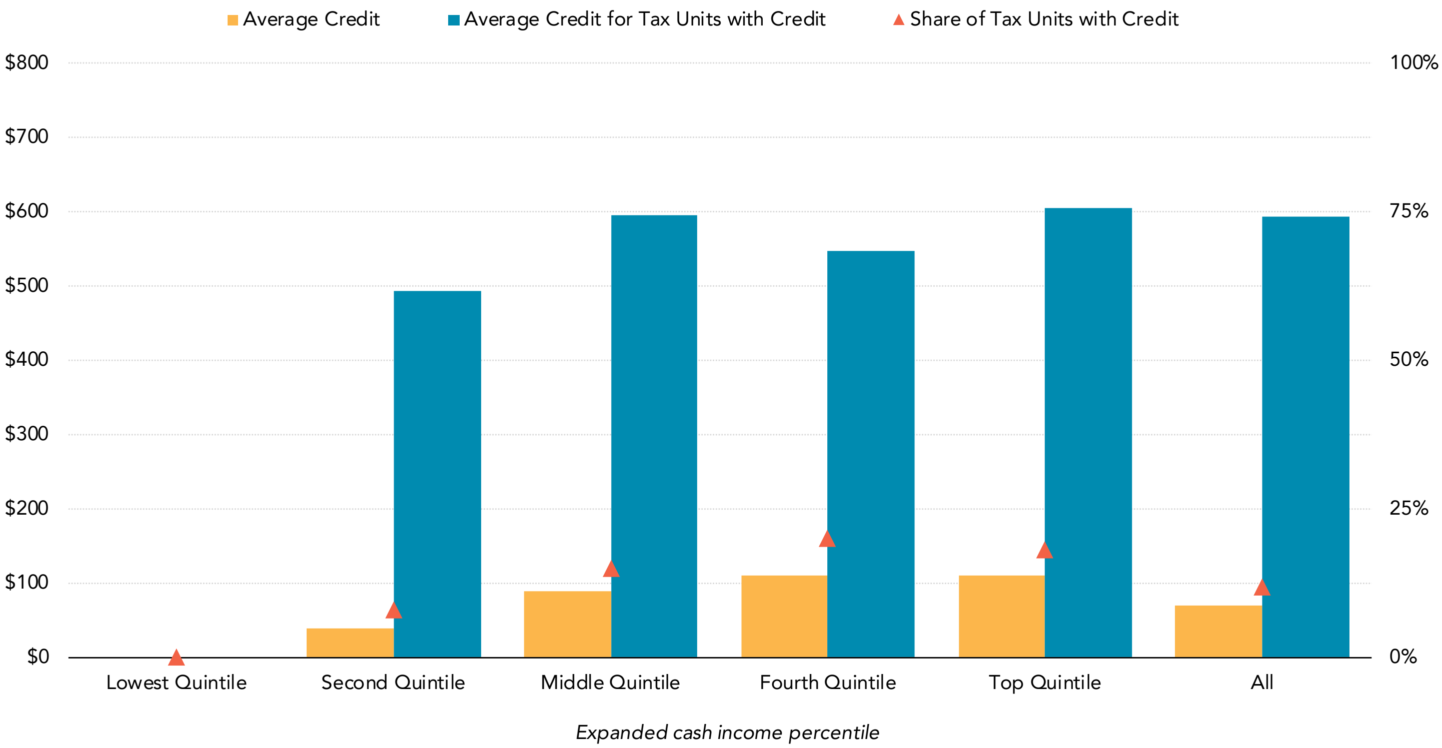
Key Elements of the U.S. Tax System

How does the tax system subsidize child care expenses?

FIGURE 1

Distribution of the Child and Dependent Care Tax Credit for Tax Units with Children

2018



Source: Urban-Brookings Tax Policy Center. "TPC Microsimulation Model, version 0718-1."

INTERACTION OF CDCTC AND FSAS

If a family has child care expenses that exceed the amount set aside in a flexible spending account, the family may qualify for a CDCTC. Families first calculate their allowable CDCTC expenses ($3,000 per child under age 13, up to $6,000 per family). If this calculation exceeds the amount of salary set aside in an FSA, a parent may claim a CDCTC based on the difference. For example, a family with two or more children can qualify for up to $6,000 of expenses to apply toward a CDCTC. If that family excluded $5,000 from salaries to pay for child care expenses in an FSA, it may claim the difference between the two ($1,000) as child care expenses for a CDCTC.

Higher-income families generally benefit more from the exclusion than from the credit because the excluded income is free from both income and payroll taxes. Most higher-income families with child care expenses qualify for a credit of 20 percent of their eligible expenses. Because the combined tax saving from each dollar of child care expenses excluded from income exceeds $0.20, the exclusion is worth more than the credit. The exclusion, however, is only available to taxpayers whose employers offer FSAs.
Neither the CDCTC nor the FSA are indexed for inflation. Thus, each year, the real (inflation-adjusted) value of benefits from the two provisions erodes.

Key Elements of the U.S. Tax System

How does the tax system subsidize child care expenses?

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Q. What are marriage penalties and bonuses?

A. A couple incurs a marriage penalty if the two pay more income tax filing as a married couple than they would pay if they were single and filed as individuals. Conversely, a couple receives a marriage bonus if they pay less tax filing as a couple than they would if they were single.

CAUSES OF MARRIAGE BONUSES AND PENALTIES

Marriage penalties and bonuses occur because income taxes apply to a couple, not to individual spouses. Under a progressive income tax, a couple's income can be taxed more or less than that of single individuals. A couple is not obliged to file a joint tax return, but their alternative—filing separate returns as a married couple—almost always results in higher tax liability. Married couples with children are more likely to incur marriage penalties than couples without children because one or both spouses could use the head of household filing status if they were able to file as singles. And tax provisions that phase in or out with income also produce marriage penalties or bonuses.

Marriage penalties are more common when spouses have similar incomes. Marriage bonuses are more common when spouses have disparate incomes. Overall, couples receiving bonuses greatly outnumber those incurring penalties.

MARRIAGE PENALTIES

Couples in which spouses have similar incomes are more likely to incur marriage penalties than couples in which one spouse earns most of the income, because combining incomes in joint filing can push both spouses into higher tax brackets.

A couple with two incomes and no children, for example, could pay more taxes as a married couple if tax brackets for joint filers were less than twice as wide as for single filers. Today, that happens only for couples with income above $600,000, but it was more common before the 2017 Tax Cuts and Jobs Act.
A couple with children can still face a marriage penalty because single parents can use the head of household filing status. Consider parents of two children, each parent earning $100,000 (table 1). Filing jointly and taking a $24,000 standard deduction, their taxable income is $176,000, for which their 2018 income tax liability is $26,819. If they could file separately, one as single and the other as the head of a household, the single filer would owe a tax of $15,410 and the head-of-household filer would owe $8,588, yielding a total tax of $23,998. Their joint tax bill is thus $2,821 higher than the sum of their hypothetical individual tax bills, imposing on them a marriage penalty equal to 1.4 percent of their adjusted gross income.

Key Elements of the U.S. Tax System

What are marriage penalties and bonuses?

TABLE 1

Calculation of the Marriage Penalty for a Hypothetical Couple with Two Children

2018

Item	Couple filing separately[a]		Couple filing jointly
	Spouse one	Spouse two	
Adjusted gross income	$100,000	$100,000	$200,000
Standard deduction	$12,000	$18,000	$24,000
Equals taxable income	$88,000	$82,000	$176,000
Of which:			
Taxable at 10 percent	$9,525	$13,600	$19,050
Taxable at 12 percent	$29,175	$38,200	$58,350
Taxable at 22 percent	$43,800	$30,200	$87,600
Taxable at 24 percent	$5,500	$0	$11,000
Regular tax liability	$15,410	$12,588	$30,819
Alternative minimum tax	$0	$0	$0
Child tax credit	$0	$4,000	$4,000
Tax liability after credits	$15,410	$8,588	$26,819
Final tax liability	**$23,998**		**$26,819**
Marriage penalty (difference in tax liabilities)		**$2,821**	
As share of adjusted gross income		**1.4%**	

Source: Urban-Brookings Tax Policy Center calculations.
Note: Detail may not sum to totals because of rounding.
(a) When the couple files separately, spouse one files as single and spouse two as head of household with two children.

MARRIAGE BONUSES

Couples in which one spouse earns all or most of a couple's income rarely incur a marriage penalty and almost always receive a marriage bonus because joint filing shifts the higher earner's income into a lower tax bracket.

Consider a couple with two children and $200,000 in total earnings, all earned by spouse two (table 2). Under 2018 tax law, filing a joint return rather than having spouse two file as head of household, will yield the couple a marriage bonus of more than $7,000 as a result of two factors. First, because tax brackets for joint returns (other than the 35 percent bracket) are wider than those for head-of-household returns, much of the couple's income is taxed at lower rates under joint filing than the 32 percent marginal rate that spouse two would pay filing separately. Second, the couple would benefit from an increased standard deduction. Couples filing jointly receive a $24,000 deduction in 2018, while heads of household receive $18,000. The combination of these two factors yields a marriage bonus of $7,719, or 3.9 percent of their adjusted gross income.

Key Elements of the U.S. Tax System

What are marriage penalties and bonuses?

TABLE 2

Calculation of the Marriage Bonus for a Hypothetical Couple with Two Children
2018

Item	Couple filing separately[a]		Couple filing jointly
	Spouse one	Spouse two	
Adjusted gross income	$0	$200,000	$200,000
Standard deduction	$0	$18,000	$24,000
Equals taxable income	$0	$182,000	$176,000
Of which:			
Taxable at 10 percent	$0	$13,600	$19,050
Taxable at 12 percent	$0	$38,200	$58,350
Taxable at 22 percent	$0	$30,700	$87,600
Taxable at 24 percent	$0	$75,000	$11,000
Taxable at 32 percent	$0	$24,500	$0
Regular tax liability	$0	$38,538	$30,819
Alternative minimum tax	$0	$4,000	$4,000
Child tax credit	$0	$0	$0
Tax liability after credits	$0	$34,538	$26,819
Final tax liability	**$34,538**		**$26,819**
Marriage bonus (difference in tax liabilities)		**$7,719**	
As share of adjusted gross income		**3.9%**	

Source: Urban-Brookings Tax Policy Center calculations.
Note: Detail may not sum to totals because of rounding.
(a) When the couple files separately, spouse one files as single and spouse two as head of household with two children.

EFFECTS OF THE TCJA ON MARRIAGE PENALTIES AND BONUSES

The 2017 Tax Cuts and Jobs Act (TCJA) limited many of the marriage penalties higher-income earners face, though penalties certainly still exist. Except for the 35 percent bracket, all tax brackets for married couples filing a joint return are now exactly double the single brackets. This limits a main cause of previous marriage penalties. It also expands the potential for marriage bonuses, as more couples find that filing together moves some income into lower tax brackets.

Additionally, the child tax credit phaseout now begins at $400,000 for couples, again double the $200,000 starting point of the phaseout for singles. Prior law began phasing out the credit at $75,000 for singles and $110,000 for couples, which could have introduced another marriage penalty for couples with children. The phaseout of the alternative minimum tax exemption is another source of marriage penalties for high-income taxpayers, because the income at which the exemption phaseout starts for couples is less than twice the starting point for singles. While this is still true under current law, TCJA increased both the alternative minimum tax exemption and the income at which it phases out, so the alternative tax will affect many fewer high-income taxpayers, singles and couples alike.

Key Elements of the U.S. Tax System

What are marriage penalties and bonuses?

MARRIAGE PENALTIES AND THE EARNED INCOME TAX CREDIT

Taxpayers who might qualify for the earned income tax credit (EITC) can suffer particularly large marriage penalties if one spouse's income disqualifies the couple. However, marriage can increase the EITC (a bonus) if a nonworking parent files jointly with a low-earning worker.

Consider a couple with two children and $40,000 in total earnings, split evenly between spouses (table 3). Two factors will cause them to incur a marriage penalty of $2,439 under 2018 tax law.

First, if the couple were not married, one spouse could file as head of household with two children and the other would file as single. Filing in that way, their combined standard deductions would be $30,000, $6,000 more than the $24,000 standard deduction available on a joint return.

Second—and more significant—filing separate returns, the head of household could claim an EITC of $5,434 and a $2,825 child tax credit; the other spouse would get neither tax credit. On net, the head of household would receive a payment of $8,059 and the other spouse would pay $800, yielding a joint tax refund of $7,259. Filing jointly, the couple would get a smaller EITC of $2,420, somewhat offset by a larger child tax credit of $4,000. Thus, filing jointly, the couple will receive a payment of $4,820, $2,439 less than the $7,259 they would have if they could have filed separately; the $2,439 difference equals 6.1 percent of their adjusted gross income.

TABLE 3

Calculation of the Marriage Penalty for a Hypothetical Low-Income Couple with Two Children

2018

Item	Couple filing separately[a]		Couple filing jointly
	Spouse one	Spouse two	
Adjusted gross income	$20,000	$20,000	$40,000
Less standard deduction	$12,000	$18,000	$24,000
Equals taxable income	$8,000	$2,000	$16,000
Of which:			
Taxable at 10 percent	$8,000	$2,000	$16,000
Regular tax liability	$800	$200	$1,600
Alternative minimum tax	$0	$0	$0
Child tax credit	$0	$2,825	$4,000
Earned income tax credit	$0	$5,434	$2,420
Tax liability after credits	$800	-$8,059	-$4,820
Couple's final tax liability	**-$7,259**		**-$4,820**
Marriage penalty (difference in tax liabilities)		**$2,439**	
As share of adjusted gross income		**6.1%**	

Source: Urban-Brookings Tax Policy Center calculations.

Note: Detail may not sum to totals because of rounding.

(a) When the couple files separately, spouse one files as single and spouse two as head of household with two children.

Key Elements of the U.S. Tax System

What are marriage penalties and bonuses?

Marriage penalties are not confined to the tax system. Married couples often receive lower benefits from government programs than they would if they had not married. Moreover, the interaction of a tax penalty and a program-eligibility penalty can create effective marginal tax rates that approach 100 percent.

Data Source

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