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Marriage Penalty Tax Relief: The Gramm Amendment

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Summary

On May 21, 1998, Senator Phil Gramm introduced an amendment to the Tobacco Settlement bill (S. 1415), which is intended to provide marriage penalty tax relief for low to middle income taxpayers. The amendment would create a new above-the-line deduction for taxpayers filing joint returns whose modified adjusted gross incomes fall below $50,000 in 1999.

This report, which will be updated if legislative action warrants, provides a brief description of the amendment and discusses some associated issues. For more detailed information on the federal income tax and marriage see: U.S. Library of Congress. Congressional Research Service. The Federal Income Tax and Marriage Neutrality. CRS Report 97-190E, by Gregg A. Esenwein. January 1997. For information on the tobacco settlement see: U.S. Library of Congress. Congressional Research Service. The Tobacco Settlement: Issues. CRS Issue Brief 98022, by C. Stephen Redhead. Updated periodically.

The Gramm Amendment

On May 21, 1998, Senator Phil Gramm introduced Amendment 2436 to the Tobacco Settlement bill (S. 1415). The amendment is intended to provide marriage penalty tax relief for low to moderate income households. The amendment is effective for tax years beginning in 1999. Specifically, the amendment creates a new above-the-line deduction for taxpayers filing joint returns whose modified adjusted gross incomes fall below $50,000 in 1999.

In any given tax year, the flat deduction would be equal to the amount by which the sum of the standard deduction for single returns and head of household returns exceeds the regular standard deduction for joint returns. For example, if the amendment were in effect in tax year 1998, then the above the line deduction would be $3,400 (the $4,250 standard deduction for single returns plus the $6,250 standard deduction for head of household returns, less the $7,100 standard deduction for joint returns). Since this new deduction is only available to taxpayers in the 15% tax bracket the maximum tax reduction (if the deduction went into effect in 1998) would be $510.

Because standard deductions are indexed for inflation the amount of the above-the-line marital deduction for 1999 is not known at this time. The amendment would index the $50,000 income level at which the marital deduction ends for inflation occurring after tax year 1999.

Furthermore, the amendment contains provisions which would adjust the earned income tax credit (EITC) phaseout threshold to reflect the new deduction. Basically, these provisions would reduce, by the amount of the marriage penalty deduction claimed, the taxpayer's income for purposes of the earned income tax credit phaseout. This has the effect of increasing the earned income tax credit for households in the phaseout range.

Analysis

Under the current income tax system, single individuals, heads of households, and married couples are subject to different standard deductions and tax rate schedules. The EITC amounts and phaseout ranges also vary according to filing status. These differences mean that some married couples pay more income tax filing joint returns than they would filing as two singles (a marriage tax penalty) while some married couples would pay less income tax (a marriage tax bonus).

In general, the division of income determines whether a married couple has a marriage tax bonus or penalty. The largest marriage tax bonuses occur when one spouse earns 100% of the income. The largest marriage tax penalties occur when each spouse earns half of the income.

While the amendment provides marriage-penalty tax relief, it does not achieve marriage neutrality because it reduces taxes for all married couples regardless of whether they actually incur a marriage tax penalty or bonus. Hence, while it reduces or eliminates marriage tax penalties for some couples, it also increases marriage tax bonuses for other couples. In addition, for low income families with children a significant factor in producing marriage tax penalties is the differences in EITC phaseout ranges and amounts. This issue is not addressed by the Gramm amendment. It should also be noted that by setting a specific income level at which the new deduction ends, the amendment creates a serious notch effect. For example, married couples with modified adjusted gross incomes of $49,999 could pay $510 dollars less in taxes than married couples with modified adjusted gross incomes of $50,001.

Some might argue that this amendment could also provide a means of reducing the regressivity of any tobacco tax increase. However, it provides only an imprecise means of offsetting the regressivity of a possible increase in tobacco taxes. The amendment would provide income tax reductions based on marital status, not on the use of tobacco products. Hence, non-smoking married couples would get the same tax relief as married couples who use tobacco products, while single individuals who use tobacco products would get no income tax reductions as an offset to a possible tobacco tax increase.