

## **The Minnesota Income Tax Marriage Credit**

The marriage credit, enacted by the 1999 Legislature, is designed to reduce the “marriage tax penalty” paid by some married couples without increasing marriage bonuses. The credit equals the higher income tax paid by a married couple under the married joint income tax brackets, as compared with the tax they would pay if their earned income were taxed separately under the single tax brackets. The maximum credit in tax year 2006 is \$313; the credit amounts and other parameters are adjusted annually for inflation and for changes to Minnesota’s tax rates.

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## **The Marriage Penalty in Minnesota’s Income Tax Rates and Brackets**

**There are many marriage penalties and bonuses under the federal and Minnesota income taxes.** A marriage penalty occurs when a married couple pays higher tax than they would if each spouse could file as a single and pay tax on his or her own income. A bonus occurs when they pay lower tax as a married couple than they would if they filed as singles. Penalties and bonuses result from:

- the use of combined income for a married couple to calculate their tax
- the progressive rate structure
- the dollar limits on deductions and credits

**Minnesota’s income tax produces marriage penalties and bonuses because couples generally pay tax under a progressive rate structure on their joint incomes.** As has been widely recognized, when two individuals marry, their combined income tax frequently changes.

It may increase, resulting in a marriage “penalty,” or it may drop, yielding a marriage “bonus.” Penalties and bonuses result because both federal and state taxes effectively require the spouses to combine their incomes in calculating tax.<sup>1</sup> In the case of Minnesota’s income tax rates, joint filing and reporting of income interacts with the progressive tax rate schedule to produce marriage penalties or bonuses. Generally, couples with closely equal incomes will experience a penalty, while one-earner couples will receive a bonus. The examples in the boxes on this page and the next illustrate how the Minnesota tax, before determination of the marriage credit, can result in marriage penalties for some couples and bonuses for others.

### **Example of a Marriage Penalty**

H and W each earn \$30,000 and claim the standard deduction. If they can file as singles, each will have Minnesota tax liability of \$1,097 or a combined tax of \$2,194 for tax year 2006. If H and W marry and file a joint return, their combined tax increases to \$2,529, a marriage penalty of \$188.

The marriage penalty results because the married joint tax brackets are not twice the width of the single brackets. For a single filer, the first \$20,510 of income is taxed at 5.35 percent. Thus as single filers, H and W would have \$41,020 of their income taxed at the 5.35 percent rate as (i.e., twice the bracket for single filers). As a married joint filer, the first \$29,980 is taxed at 5.35 percent and additional income at 7.05 percent. As a result, H and W will have \$11,040 more ( $\$41,020 - \$29,980 = \$11,040$ ) of their income taxed at 7.05 percent, rather than 5.35 percent. This accounts for the \$188 of the marriage penalty. As described in the text, the marriage credit addresses this marriage penalty.<sup>2</sup>

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<sup>1</sup> A married couple may file separate federal returns with each spouse separately reporting his and her income and deductions. However, doing so nearly always results in a higher total tax liability. Minnesota law requires taxpayers to file using the same filing status that they do for federal purposes. [Minn. Stat. § 289A.08](#), subd. 6.

<sup>2</sup> Before tax year 2003 and in tax year 2005, H and W would have faced an additional marriage penalty under the Minnesota income tax as a result of the standard deduction for married joint filers being smaller than that allowed for single filers. As a result, marriage resulted in a combined reduction in the standard deduction compared with filing singly. The federal Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 put the marriage penalty in the standard deduction on a schedule to gradually phase out by tax year 2009. The federal Jobs Growth Tax Relief Reconciliation Act (JGTRRA) of 2003 temporarily accelerated the married joint standard deduction to equal twice the single deduction for tax years 2003 and 2004 only. Minnesota conformed to the EGTRRA 2001 and JGTRRA 2003 changes. The federal Working Families Tax Relief Act of 2004 (WFTRA) further accelerated the schedule so that the married joint standard deduction would equal twice the single deduction for tax years 2005 through 2010. Minnesota did not conform to WFTRA until tax year 2006, so that Minnesota’s income tax included a marriage penalty resulting from the standard deduction in tax years before 2003, and in tax year 2005.

### Example of a Marriage Bonus

W earns \$60,000 and claims the standard deduction. H has no income and no tax. W's tax as a single filer would be \$3,286 for tax year 2006. Marriage to H will reduce the tax to \$2,529, a marriage bonus of \$756. Three factors account for the bonus:

- More income is taxed at the 5.35 percent rate. As a single filer, the first \$20,510 of W's income is taxed at 5.35 percent. Marriage increases this to \$29,980. As a result, W will have \$9,470 more of her income ( $\$29,980 - \$20,510 = \$9,470$ ) taxed at 5.35 percent, rather than 7.05 percent. This accounts for \$161 of the bonus.
- The standard deduction for married joint filers is \$10,300, while as a single filer, W could claim only \$5,150. Since H had no income, he received no tax benefit from the standard deduction. As a result, marriage reduced W's taxable income by \$5,150 ( $\$10,300 - \$5,150 = \$5,150$ ). Since this income would have been taxed at 7.05 percent, it accounts for \$363 of the bonus.
- An additional personal exemption of \$3,300 is available. H had no income and derived no benefit from the exemption; marriage allows H's personal exemption to reduce W's taxable income. Since this income would have been taxed at 7.05 percent, the personal exemption accounts for \$234 of the bonus.

## The Marriage Credit

**Legislators sought to address the marriage penalty issue as part of a package of income tax rate reductions proposed in the 1999 legislative session.** Initial legislation proposed increasing the brackets for married joint filers to be twice the width of the brackets for single filers. This approach had been proposed in several bills introduced in both the 1997 and 1998 legislative sessions. While increasing the married joint brackets would have eliminated penalties for the 350,000 Minnesota couples who faced them, it also would have increased marriage bonuses for other filers. The cost depended on the magnitude of the rate reductions proposed; setting the married joint brackets at twice the width of the single brackets at the 5.5 percent, 7.25 percent, and 8.0 percent rates ultimately enacted would have cost an estimated \$106 million in tax year 1999. Over half this cost—\$58 million—would have provided bonuses, with the remaining \$48 million removing penalties.

**Budget constraints led lawmakers to seek a less costly way to address the issue, and the discussion focused on a credit that would remove the penalties without increasing bonuses.** The marriage penalty credit that developed consisted of a table that provided a credit roughly equal to the penalty faced by couples at different income levels. The credit offsets penalties under the rate and bracket system, but does not provide bonuses. The estimated cost for the credit was \$48 million in tax year 1999, \$58 million less than the estimate for doubling the brackets.

**The credit is based on the earned income of the lesser-earning spouse, and the taxable income of the couple.** The credit as enacted in 1999 defined "earned income" as wages and self-employment income. Information about these forms of income is readily available to both taxpayers and the Department of Revenue through W-2 forms filed by employers and through

reporting of self-employment income for Social Security tax purposes. Legislation enacted in 2000 expanded the definition of “earned income” to include taxable pension and Social Security income, which are reported separately to each spouse and generally reflect an individual’s earning history.<sup>3</sup> Joint taxable income is already calculated as part of the tax return. As a result, it is relatively simple for taxpayers to look up their credit in the tax instructions. The table below shows the credit as it will appear in the 2006 tax booklets.

### Marriage Credit Table Tax Year 2006

Earned Income of Lesser-Earning Spouse at least                  but less than		Joint Taxable Income					
		\$31,000 to \$50,000	\$50,000 to \$70,000	\$70,000 to \$90,000	\$90,000 to \$110,000	\$110,000 to \$130,000	\$130,000 to \$150,000
		<i>your credit is</i>					
\$18,000	\$20,000	\$18	\$18	\$2	\$0	\$0	\$0
20,000	22,000	52	52	52	0	0	0
22,000	24,000	86	86	86	0	0	0
24,000	26,000	120	120	120	0	0	0
26,000	28,000	154	154	154	42	0	0
28,000	30,000	178	188	188	91	0	0
30,000	32,000	144	188	188	107	0	0
32,000	34,000	110	188	188	123	0	0
34,000	36,000	76	188	188	139	0	0
36,000	38,000	42	188	188	155	2	2
38,000	40,000	8	188	188	171	18	18
40,000	42,000	0	188	188	187	34	34
42,000	44,000	0	188	188	188	50	50
44,000	46,000	0	188	188	188	66	66
46,000	48,000	0	188	188	188	82	82
48,000	50,000	0	170	188	188	98	98
50,000	52,000	0	136	188	188	114	114
52,000	54,000	0	102	188	188	130	130
54,000	56,000	0	68	188	188	146	146
56,000	58,000	0	34	188	188	162	162
58,000	60,000	0	0	188	188	178	178
60,000	62,000	0	0	188	188	194	194
62,000	64,000	0	0	188	188	195	210
64,000	66,000	0	0	188	188	195	226
66,000	68,000	0	0	188	188	195	242
68,000	70,000	0	0	170	188	195	258
70,000	72,000	0	0	136	188	195	274
72,000	74,000	0	0	102	188	195	290
74,000	76,000	0	0	68	188	195	306
76,000	78,000	0	0	24	178	185	313

Source: Minnesota Department of Revenue  
 (Filers with higher incomes are referred to a worksheet.)

<sup>3</sup> Laws 2000, ch. 490, art. 4, § 22.

**The credit table is a function of the difference between Minnesota’s three marginal rates, and the relationship between the brackets for single and married joint filers.** The credit table enacted in 1999 was tied to the marginal tax rates in effect for 1999—5.5 percent, 7.25 percent, and 8.0 percent, with a 1.75 percentage point difference between the first and second rates, and a 0.75 percentage point difference between the second and third rates. The 1999 law directed the Commissioner of Revenue to index the credit annually for inflation, just as the brackets are indexed annually. The 2000 omnibus tax law reduced the marginal tax rates to their current level (5.35 percent, 7.05 percent, and 7.85 percent) and adjusted the table to reflect a changed relationship between the rates. There is now a 1.7 percentage point difference between the first and second rates, and a 0.8 percentage point difference between the second and third rates. The 2000 law also directed the commissioner to adjust the table as needed to reflect the relationship between the tax rates.<sup>4</sup> This provision allows the marriage credit to automatically follow along with any future changes to the marginal rates. In 2001, the legislature enacted language proposed by the Department of Revenue replacing the credit table enacted in 1999 with the formula used in calculating the table.<sup>5</sup>

**The marriage credit only addresses penalties imposed under Minnesota’s rate structure.** It does not remove bonuses currently paid under that rate structure, nor does it alleviate penalties or bonuses that are “passed through” to the Minnesota income tax because of features of federal law. Instead, it simply provides a credit roughly equal to the penalty couples face because of Minnesota’s progressive rate structure and combined filing requirement.

**The marriage credit does not address penalties that exist as a result of the distribution of unearned income between spouses.** There is currently no reporting required as to the amount of unearned income on a return that pertains to each spouse. Applying a credit to unearned income would require greater reporting and could also encourage couples to reallocate the ownership of assets to maximize the credit. The types of income used in calculating the marriage credit—wages, self-employment income, taxable pensions, and taxable Social Security benefits—cannot be easily reallocated from one spouse to another. Because it was not the intent of legislators to either provide a complicated solution or one that resulted in the tax system encouraging asset shifting, the credit was limited to earned income.

## **Other Marriage Penalties in Minnesota’s Income Tax System**

**Nine other features of the Minnesota individual income tax create marriage penalties or bonuses.**

The following table lists provisions of the Minnesota income tax that may cause individuals who marry to pay a higher Minnesota income tax. The table also shows the theoretically maximum

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<sup>4</sup> [Laws 2000, ch. 490](#), art. 4, §§ 23-24.

<sup>5</sup> [Laws 2001, 1<sup>st</sup> spec. sess., ch. 5](#), art. 7, § 41.

marriage penalty and bonus for each of the provisions.<sup>6</sup> The provisions are listed in the order in which they occur in computation of the income tax—i.e., deduction from federal tax income first, application of the rates, and finally tax credits.

**Provisions of the Minnesota Income Tax  
 Creating Marriage Penalties and Bonuses, Tax Year 2006**

Provision	Maximum Penalty	Maximum Bonus
<b>Calculation of taxable income</b>		
Elderly exclusion	\$450	\$448
Education deduction per dependent K-6	None	128
Education deduction per dependent 7-12	None	196
Charitable contribution deduction for nonitemizers	None	20
<b>Tax rates</b>		
Couples with dependents	666	222
<b>Tax credits</b>		
Dependent care credit	1,440	None
Education credit	1,000 times number of children	None
Long-term care credit	None	100
Working family credit	3,174	1,587
<b>Alternative minimum tax exemption</b>	1,280	1,280
<b>Alternative minimum tax exemption phaseout</b>	1,200	600

For a more thorough discussion of marriage penalties in Minnesota’s income tax, please see the House Research information brief [Marriage Penalties and Bonuses and the Minnesota Income Tax](#).

**A number of features of the federal income tax create marriage penalties or bonuses that carry over to the Minnesota individual income tax.**

Marriage penalties and bonuses under the Minnesota income tax also result from the close links between the state tax and the federal income tax. Calculation of Minnesota taxable income

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<sup>6</sup> The amounts are theoretical maximums, since it is not clear if any couple has the specific circumstances necessary to realize the maximum penalty or bonus. In some instances, fairly unusual or atypical circumstances may be required to reach the maximum penalty or bonus. Nevertheless, the maximums may be useful to point out the outer limits or parameters for the penalties and bonuses of each provision.

begins with federal taxable income. Taxpayers take the amount of federal taxable income from their federal return and then make a few modifications to determine Minnesota taxable income to which the tax rates apply. As a result, many deductions and exclusions under federal law determine the amount of state taxable income. For example, itemized and standard deductions, deduction of capital losses, and retirement savings deductions (e.g., 401(k) plans, IRAs, and so forth) are determined by federal law for state purposes.

The legislature has opted to conform to federal income tax provisions for a number of reasons. Perhaps the most important of these is simplicity and ease of compliance and administration for both taxpayers and the Revenue Department. Since most individuals must comply with the federal tax, adopting its provisions greatly simplifies compliance with the Minnesota tax. Adopting an approach that deviates from federal law on these basic tax base calculations could have a high cost in additional resources for individuals to comply with the law. This was one of the major complaints about the pre-1985 Minnesota tax which differed substantially from federal law, including using individual filing rather than joint filing by married couples, the major source of penalties and bonuses.

The federal government enacted several marriage penalty relief provisions in the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001. The act does the following:

- Increases the standard deduction for married joint filers to be twice as large as the deduction allowed single filers. Subsequent federal legislation (the Jobs Growth and Tax Relief Reconciliation Act (JGTRRA) of 2003 and the Working Families Tax Relief Act (WFTRA) of 2004) accelerated this increase to take effect in 2003.
- Increases the size of the 15-percent bracket for married joint filers to be twice the size of the bracket for single filers. (Scheduled to take full effect for tax year 2008.)
- Increases the income level at which the earned income credit begins to phase out for married joint filers. (Scheduled to take full effect for tax year 2008.)

Minnesota conformed to the acceleration of the increased standard deduction in JGTRRA 2003 (effective for tax years 2003 and 2004), but delayed one year, to tax year 2006, before conforming to the continued acceleration of the deduction in WFTRA 2004. As a result, the standard deduction allowed married joint filers at the state level in 2005 was smaller than that allowed at the federal level. For 2006 through 2010,<sup>7</sup> the increased standard deduction will flow through to Minnesota income tax returns and decrease penalties at the state level. The other two federal changes do not directly affect penalties in Minnesota's income tax. However, in 2001 Minnesota followed the federal earned income tax credit changes by increasing the income level at which the working family credit begins to phase out to match the increases provided at the federal level under EGTRRA: by \$1,000 in tax years 2002 to 2004, \$2,000 in 2005 to 2007, and \$3,000 in 2008, with the amount adjusted for inflation in following years.<sup>8</sup>

*For more information about income taxes, visit the income tax area of our web site, [www.house.leg.state.mn.us/hrd/issinfo/tx\\_inc.htm](http://www.house.leg.state.mn.us/hrd/issinfo/tx_inc.htm).*

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<sup>7</sup> Like many other EGTRRA 2001 provisions, the increased standard deduction, sunsets after 2010.

<sup>8</sup> Laws 2001, 1<sup>st</sup> spec. sess., ch. 5, art. 10, § 7.