HOUSE RESEARCH

000293

February 2000

Information Brief

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The Minnesota Income Tax Marriage Credit

The 1999 Legislature enacted a new income tax credit designed to reduce the "marriage tax penalty" paid by some married couples. The credit is designed to reduce marriage penalties without increasing marriage bonuses. The credit is shown in a table in the income tax instructions, with the amount equaling the additional income tax imposed on the earned income of a married couple compared to single filers because of the width of Minnesota's income tax brackets. The maximum credit in tax year 1999 is $261; the credit amounts and other parameters are adjusted annually for inflation.

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.[1] 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 $1,362 or a combined tax of $2,724 for tax year 1999. If H and W marry and file a joint return, their combined tax increases to $2,988, a marriage penalty of $264. The marriage penalty results from two factors.

- The married joint tax brackets are not twice the width of the single brackets. For a single filer, the first $17,250 of income is taxed at 5.5 percent. Thus as single filers, H and W would have $34,500 of their income taxed at the 5.5 percent rate as (i.e., twice the bracket for single filers). As a married joint filer, the first $25,220 is taxed at 5.5 percent and additional income at 7.25 percent. As a result, H and W will have $9,280 more ($34,500 - $25,220 = $9,280) of their income taxed at 7.25 percent, rather than 5.5 percent. This accounts for $162 of the marriage penalty.

- The standard deduction for married joint filers is $7,200, while it is $8,600 for two single filers. As a result, the married couple has $1,400 more in taxable income. Since this income is taxed at 7.25 percent, it accounts for $102 of the penalty. The standard deduction is set by federal law; Minnesota adopts it by using federal taxable income in calculating its tax.

[1] 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.

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 $3,537 for tax year 1999. Marriage to H will reduce the tax to $2,988, a marriage bonus of $549. Three factors account for the bonus:

- More income is taxed at the 5.5 percent rate. As a single filer, the first $17,250 of W's income is taxed at 5.5 percent. Marriage increases this to $25,220. As a result, W will have $7,970 more of her income ($25,220 - $17,250 = $7,970) taxed at 5.5 percent, rather than 7.25 percent. This accounts for $139 of the bonus.

- The standard deduction for married joint filers is $7,200, while as a single filer, W could claim only $4,300. Since H had no income, he received no tax benefit from the standard deduction. As a result, marriage reduced W's taxable income by $2,900 ($7,200 - $4,300 = $2,900). Since this income would have been taxed at 7.25 percent, it accounts for $210 of the bonus.

- An additional personal exemption of $2,750 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 7.25 percent, the personal exemption accounts for $199 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 gone to provide 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. Information about earned 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. Joint taxable income is already calculated as part of the tax return. As a result, taxpayers should find it relatively simple to look up their credit in the tax instructions. The table below shows the credit as it was enacted into law. The same table appears in the 1999 tax booklet. The legislation provides for the table to be indexed annually for inflation.

Marriage Credit Table, Minnesota 1999 M-1 Tax Form Instructions*

If the amount on line 39 is:		and the amount on line 36 is:		If the amount on line 39 is:		and the amount on line 36 is:	
at least	but less than	$25,000 to 99,999	$100,000 and over	at least	but less than	$25,000 to 99,999	$100,000 and over
		your credit is				*your credit is*	
$14,000	$15,000	$9	$0	39,000	40,000	162	91
15,000	16,000	27	0	40,000	41,000	162	99
16,000	17,000	44	0	41,000	42,000	162	106
17,000	18,000	62	0	42,000	43,000	162	114
18,000	19,000	79	0	43,000	44,000	162	121
19,000	20,000	97	0	44,000	45,000	162	129
20,000	21,000	114	0	45,000	46,000	162	136
21,000	22,000	132	0	46,000	47,000	162	144
22,000	23,000	149	0	47,000	48,000	162	151
23,000	24,000	162	0	48,000	49,000	162	159
24,000	25,000	162	0	49,000	50,000	162	166
25,000	26,000	162	0	50,000	51,000	162	174
26,000	27,000	162	0	51,000	52,000	162	181
27,000	28,000	162	0	52,000	53,000	162	189
28,000	29,000	162	9	53,000	54,000	162	196
29,000	30,000	162	16	54,000	55,000	162	204
30,000	31,000	162	24	55,000	56,000	162	211
31,000	32,000	162	31	56,000	57,000	162	219
32,000	33,000	162	39	57,000	58,000	162	226
33,000	34,000	162	46	58,000	59,000	162	234
34,000	35,000	162	54	59,000	60,000	162	241
35,000	36,000	162	61	60,000	61,000	162	249
36,000	37,000	162	69	61,000	62,000	162	256
37,000	38,000	162	76	62,000	and over	162	261
38,000	39,000	162	84				

* Note: Line 36 is Minnesota taxable income; line 39 is the earned income of the lesser-earning spouse.

The credit table is a function of the difference between Minnesota's three marginal rates. For tax year 1999, the rates are 5.5 percent, 7.25 percent, and 8.0 percent; there is 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. If future legislation were to change the current relationship between the rates, the credit table would have to be updated, or else it would subsequently provide either bonuses or penalties of its own, depending on how the rates had changed.

The marriage credit enacted in 1999 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 that are "passed through" to the Minnesota income tax because of the federal standard deduction or other 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 pension or unearned income between spouses. There is currently no reporting required as to the amount of pension income or 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. Because it was not the intent of legislators to either provide a complicated solution or one that resulted in the tax system influencing behavior, the credit was limited to earned income.

Other Marriage Penalties in Minnesota's Income Tax System

Eight 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 marriage penalty and bonus for each of the provisions.[2] 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.

[2] 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. For a more detailed discussion of each of these provisions, see the research report **Marriage Penalties and Bonuses and the Minnesota Income Tax**, January 1999.

Provisions of the Minnesota Income Tax Creating Marriage Penalties and Bonuses, Tax Year 2000[3]

Provision	Maximum Penalty	Maximum Bonus
Calculation of taxable income		
Elderly exclusion	$469	$508
Education deduction per dependent K-6	None	130
Education deduction per dependent 7-12	None	200
Tax rates		
Couples with dependents	556	184
Tax credits		
Dependent care credit	1,440	None
Education credit	4,000	None
Long-term care credit	None	100
Working family credit	2,487	1,243
Alternative minimum tax exemption	1,300	650
Alternative minimum tax exemption phase-out	1,219	609

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 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

[3] All calculations of total penalties under current law were made using the 1997 sample of individual income tax returns prepared by the Department of Revenue in conjunction with the House Income Tax Simulation (HITS) model and the growth assumptions of the November 1999 economic forecast prepared by the Department of Finance.

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.

Options to Reduce Marriage Penalties

The table in this section provides tax year 2000 estimates of the cost of reducing the remaining marriage penalties in Minnesota's income tax. For a more thorough discussion of these options, please see **Options for Reducing Marriage Penalties Under the Minnesota Income Tax**, a policy brief, February 1999.

Tax Year 2000
Cost of Options to Reduce Marriage Penalties
(amounts in millions)

Description of Option	Cost
Increase width of married joint brackets to twice the single brackets	$ 63.1
Increase widths of married joint brackets to equal the single bracket amounts plus the head of household bracket amounts	113.8
Increase the base amount and phase-out threshold of the elderly exclusion to be twice that for single individuals	18.4
Increase the exemption amount and phase-out threshold of the alternative minimum tax to be twice that for single filers	14.9
Restructure working family credit	
Double the income qualifying for credit for married couples	35.7
Double phase-out threshold for married couples	24.4
Double disqualified income for married couples	2.4
Double income qualifying for credit, phase-out threshold, and disqualified income	51.0
Double the income phase-out threshold for married couples under the dependent care credit	7.4
Restructure the education credit	NA
Double the phase-out threshold for married couples	NA
Double the maximum credit amount for married couples	NA
NA = no estimate is available for these options	