United States General Accounting Office

GAO

Report to the Honorable
Orrin G. Hatch, U.S. Senate

September 1996

TAX ADMINISTRATION

Income Tax Treatment of Married and Single Individuals

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GAO/GGD-96-175

United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-272101

September 3, 1996

The Honorable Orrin G. Hatch
United States Senate

Dear Senator Hatch:

This report responds to your request for information on income tax provisions in the Internal Revenue Code (IRC) that potentially create "marriage penalties" or "marriage bonuses" with respect to the tax liability of married couples. As defined herein, a marriage penalty results when two married individuals have a greater tax liability than two similarly situated single individuals, i.e., individuals with the same total income. Conversely, a marriage bonus results when a married couple owes less taxes than two similarly situated single individuals. This report (1) summarizes the current income tax provisions in the IRC whose applicability depends upon whether a taxpayer is married or single, (2) identifies those provisions likely to result in marriage penalties or marriage bonuses or both, and (3) discusses the feasibility of quantifying the numbers of taxpayers affected by the marriage penalties and bonuses.

Background

Current federal income tax law divides individual taxpayers into two major groups—those who are married and those who are single. Married people can file jointly with their spouse or can elect to file separately ("married filing separately"). Single people file either as an unmarried taxpayer or as an unmarried taxpayer maintaining a household with dependents ("head of household"). A married person may file as a single person only under limited circumstances.[1] For the most part, married taxpayers file jointly with their spouse.[2]

Traditionally, the tax treatment of married and single taxpayers has involved trade-offs among three basic principles: (1) there should be progressive tax rates, with successively higher income brackets taxed at increasingly higher rates; (2) families with equal income should have equal tax burdens, notwithstanding how the income is divided between spouses;

[1]A married taxpayer can file as a single taxpayer or as a head of household if he or she is legally separated under a decree of divorce or separate maintenance, or if he or she qualifies as an "abandoned spouse" under IRC section 7703(b). To be considered an abandoned spouse, the taxpayer must have maintained a household for a dependent child, provided over 50 percent of the household expenses for the tax year, and lived apart from his or her spouse for the last 6 months of the tax year.

[2]In 1992, about 95 percent of all married taxpayers filed jointly. At present, the income tax rates are structured to discourage married taxpayers from electing to file separate returns. Under current law, such an election would lead to higher taxes in most cases.

and (3) individual tax liability should not change when people marry (the tax system should be "marriage neutral"). The trade-offs among these principles exist because, as public finance experts have long recognized, a tax system cannot satisfy all three principles simultaneously.

An example of the trade-offs is our current tax system, which has progressive tax rates and taxes married couples with the same income equally. However, this can result in the income of some married couples falling into different tax brackets than would be the case if they were to file as single individuals. Therefore, the present tax system is not "marriage neutral" and two married people may not have the same tax liability as two similarly situated single people. Generally, large income differences between spouses can lead to marriage bonuses while roughly equal incomes can lead to marriage penalties.

The equity of the comparative treatment of married and single people under the income tax laws has been the subject of debate for nearly the past 50 years. In 1948, Congress permitted married couples to split their income between spouses if they reported the income on a joint return. For most married couples at the time, this change led to lower tax liability.[3] Since that time, most married people have elected to file jointly, while most unmarried people file as single individuals.

In general, the debate over the most equitable way to deal with married and single taxpayers has focused on the tax rate structure. Beginning in 1948, the rate schedules were structured so that the tax liability for married taxpayers was never more than—and could be up to 42 percent less than—that of similarly situated single people. To correct the apparent inequity in the tax rate for single people, Congress enacted a separate rate schedule for single taxpayers in 1969, providing that the tax liability for a middle-income single person could be no more than 20 percent greater than that for a married couple with the same total income. This rate change, however, created a new "marriage penalty" for certain married couples if both spouses earned approximately the same income.[4]

[3]The change came about after inequities arose between married taxpayers in "community property" states and those in "common law" states. Because community property states required spouses to split income between one another, typically the tax liability for taxpayers in these states was less than that of taxpayers in common law states. By allowing all married couples to split their income when reporting jointly, the differences in federal tax liability were effectively eliminated.

[4]With the new rate schedule, married taxpayers were not allowed to file as single individuals. If, therefore, two married people with roughly equivalent incomes were bumped up into a higher tax bracket than either would be in had each filed individually, the new law provided no relief.

Notwithstanding the focus on the rate structure, many other provisions of the income tax code take into account the fact that one large group of people reports jointly as a household, while the other large group reports as single earners.[5] This adds complexity to the income tax code, and the continuing possibility of tax breaks for some, under certain circumstances, and tax penalties for others, under different circumstances. Over the years, various proposals have been made for dealing with these inequities. We summarize the major proposals in appendix VI of this report.

Results in Brief

We identified 59 provisions in the income tax code where tax liability depends, at least in part, on whether a taxpayer is married or single. These provisions include three IRC sections most commonly discussed in connection with marriage penalties and bonuses: the sections on the tax rate, the standard deduction, and the earned income credit. The remaining 56 provisions are less frequently discussed and include many different types of tax law provisions, such as those dealing with taxation of social security benefits, limitations on capital losses, and the home mortgage interest deduction.

When enacting these varied provisions, Congress has dealt with the equities between income reported jointly by most married couples and the single income reported by most single people in different ways, which we categorize into four groups. One of these groups encompasses nine provisions, such as those on the tax rate and social security taxation, for which Congress has created different sets of requirements for married and single people, making some adjustment for the differences between joint and single income. For a second group encompassing 15 other provisions, such as those limiting capital losses and the home mortgage interest deduction, the laws include only 1 limit for both married and single taxpayers. For a third group of nine provisions, like that allowing a personal exemption, Congress has treated married couples as if they were single individuals, or provided them with twice the benefit allowed a single person. A fourth group consists of 26 provisions under which married people are considered a unique unit for the purpose of the tax code section.

The different ways that married and single people are treated under the income tax code could lead to situations where the tax liability of married taxpayers is not the same as that of two similarly situated single taxpayers.

[5]In 1992, 42 percent of taxpayers filed jointly with their spouse, while 43 percent of taxpayers filed as single individuals.

As defined in this report, these situations may result in either a marriage penalty (married couple owes more tax) or a marriage bonus (married couple owes less tax).[6] All but 3 of the 59 income tax provisions we identified could result in a marriage penalty or a marriage bonus, depending on the individual circumstances of the taxpayer.

The marriage penalties and bonuses associated with the various provisions discussed in this report follow several patterns, but all hinge upon the individual circumstances of the married couple. The single most important factor in these situations is how income is divided between spouses. Generally, disparate income between spouses could lead to marriage bonuses, while equivalent income could result in marriage penalties. Thus, where one spouse has a high income and the other spouse has little or no income, tax rates for the married couple filing jointly would be lower than had each spouse filed individually—a marriage bonus. If, though, both spouses earn roughly the same income, their combined income may increase their tax rate beyond what either would have had as a single filer—a marriage penalty.

Marriage penalties and bonuses related to many provisions, though, are tied to other individual factors, such as which spouse owns property and which spouse is qualified for tax deductions and credits, in addition to the split of income between husband and wife. For example, current law limits deduction of capital losses from ordinary income to $3,000 for either a married couple or a single taxpayer. If husband and wife have capital losses of $3,000 each, the law leads to a marriage penalty—the couple would be able to deduct $6,000 as single taxpayers instead of $3,000 filing jointly. On the other hand, if one spouse has $8,000 in capital losses and the other has $8,000 in capital gains, the capital loss completely offsets the capital gain, leading to a marriage bonus.

The impact on taxpayers of marriage penalties and bonuses is widely varied, both in terms of the numbers of taxpayers potentially affected by the provisions and in terms of the dollar amounts involved in the tax liability. To assess the comparative importance of these many different provisions, we attempted to quantify the number of taxpayers potentially subject to the specific marriage penalties and bonuses. However, when we

[6]Public finance experts have long recognized alternative views in determining when tax schedules are "neutral" with respect to marriage. As one example, if two can live together cheaper than two people alone, then a couple living together may be viewed as having a greater ability to pay taxes than two people living alone with the same combined income. According to this view, therefore, imposing the same tax burden on a married couple as on two single individuals living apart results in a marriage subsidy or bonus.

examined the information available, we determined the current data insufficient to make such an assessment.

Analysis of the Income Tax Treatment of Married and Single Taxpayers

In the first 4 appendixes to this report, we discuss the 59 income tax provisions we have identified. The four appendixes group the provisions according to the general tax treatment of married and single taxpayers, and each appendix lists various provisions, describing how each provision operates, how it affects married taxpayers, and what potential marriage penalties and bonuses may arise through the operation of the provision.

Appendix I describes nine income tax provisions, including two—on the tax rates and the standard deduction—which potentially affect most taxpayers. These nine provisions adjust the income levels and deduction amounts to account for joint and single income. However, the adjustments for married couples filing jointly are less than twice those allowed to a single person. Thus, the tax rate for single people in tax year 1995 was 28 percent for taxable income over $23,350, while married people are taxed at a rate of 28 percent when taxable income exceeds $39,000—less than twice the income level of the single taxpayer.

Generally, all these provisions potentially could lead to either a marriage penalty or a marriage bonus, depending on the relative income of the two spouses. With the tax rates, for example, there would be a marriage penalty if each spouse earns $21,000—their joint taxable income of $42,000 would be taxed at a marginal rate of 28 percent, even though if each filed as single individuals their highest tax rate would be 15 percent. On the other hand, there would be a marriage bonus if one spouse earns $34,000 and the other spouse earns $2,000—the married couple would be taxed at a rate of 15 percent although the spouse with $34,000 in taxable income would have a marginal tax rate of 28 percent filing as an individual.

Appendix II shows 15 income tax provisions that provide the same income or deduction level, whether the taxpayer is filing jointly as a married couple or as a single individual. For instance, the home mortgage interest deduction is limited to the interest on a mortgage balance not exceeding $1 million; this limit is the same for a married couple as for a single person.

Overall, the tax treatment of married and single people in these provisions leads to a mixed impact on married taxpayers. These provisions produce both penalties and bonuses, depending on the individual circumstances.

With the home mortgage interest deduction, for example, two married taxpayers may both own houses with mortgages of $600,000 each, for a combined mortgage of $1.2 million—over the $1 million limit. As a married couple, the taxpayers would not be able to deduct interest attributable to the mortgage amount over $1 million. As single taxpayers, though, each could deduct the interest on the two individual mortgages. However, suppose that one of the married taxpayers owns a home with a mortgage balance but has little or no income; in this case, the mortgage interest could be used to offset the other spouse's income, a tax advantage unavailable to two unmarried taxpayers.

Appendix III examines nine provisions that provide full adjustment for joint and single income, either by treating married taxpayers as single taxpayers or allowing them twice the tax benefit allowed a single person. Thus, married taxpayers are each allowed to deduct the same personal exemption as a single person—$2,500 per spouse. For the most part, these provisions could only result in a tax bonus to the married couple. For example, even though one spouse has little or no income, a married couple would be eligible for two personal exemptions of $2,500, and both exemptions could be used to offset the income of the other spouse.

Appendix IV describes 26 income tax provisions that treat married couples as a unique unit in the case of certain special situations between husband and wife. In one such provision, the law provides that a husband (or wife) cannot deduct losses on a sale of property to a spouse because they are considered "related parties." Technically, many of these provisions could create tax penalties for married couples. For instance, where the loss on the sale of property between two spouses is nondeductible, such a loss would be deductible in a sale involving an unmarried couple. On the other hand, some provisions, such as IRC section 7872 on below-market loans, free married people of the tax consequences of financial dealings between spouses.

Insufficient Data Available to Measure the Comparative Significance of the Different Tax Penalties and Bonuses Cited in This Report

We found that tax data, as currently reported by taxpayers and compiled by the Internal Revenue Service (IRS), did not contain data elements that would permit the identification of the numbers of people potentially affected by all the marriage penalties and bonuses described in this report. Such data would be necessary, for example, to rank the comparative significance of the individual provisions. Assessment of the numbers of taxpayers potentially affected by these penalties and bonuses would require identification of the married taxpayers whose individual tax situations include a marriage penalty or bonus. Information on numerous individual factors, the most important of which is division of income between spouses, would be critical to attribution of a specific penalty or bonus to a married couple.

Current IRS tax data do not contain information on how income is split between spouses.[7] Even with information on how income is split between spouses, though, much other necessary information—for example, the amount of a couple's home mortgage balance or which spouse owns assets resulting in capital gains or losses[8]—is not available. Although some studies[9] have been done making assumptions as to how to allocate certain common tax items, such as itemized deductions, other types of tax items, such as those identified above, would be difficult, at best, to estimate and allocate without further information.

To add some perspective to the many different provisions we describe in this report, appendix V includes a list showing the numbers of married and single taxpayers filing under some of the provisions discussed herein; specifically, those provisions for which we could quantify the number of taxpayers filing using IRS' public tax files. However, these numbers do not in any way indicate the number of taxpayers actually affected by the marriage penalty or marriage bonus possible in application of the

[7]At the current time, taxpayers do not generally report information on how income is split between spouses. The last time taxpayers reported such information was in tax year 1986 on Schedule W, Deduction for a Married Couple When Both Work. IRS is adding information on earned income and other types of income to its compilation of Statistics of Income tax data for tax year 1993; however, this information will not be available until, at the earliest, the beginning of next year.

[8]A married couple may be penalized because the amount of mortgage interest deductible on a joint return is limited to that attributable to a mortgage balance of less than $1 million; although the tax return reports the total amount of interest deducted by the couple, it provides no information on the total amount of the mortgage held by the couple. Similarly, with capital gains and losses, the tax return does not provide information on which spouse owned the property sold for a capital gain or loss.

[9]See, for example, Daniel R. Feenberg and Harvey S. Rosen, "Recent Developments in the Marriage Tax," National Tax Journal 48 No. 1 (March 1995): 91-101. In this article, the authors look at the marriage tax for three IRC sections—on the tax rates, the standard deduction, and the earned income credit. To calculate the marriage tax, they assumed that itemized deductions would be reported by the spouse with the higher income.

provision; as we have indicated above, other factors must be considered before it can be determined that an individual married couple is subject to a marriage penalty or bonus.

Objectives, Scope, and Methodology

Our objectives were to (1) identify provisions in the income tax code that treat married and single taxpayers disparately, determining how each section operates, and how its treatment of taxpayers varies depending on marital status; (2) analyze each provision to determine whether the provision can create a marriage penalty or marriage bonus, or both; and (3) quantify, to the extent possible, the number of taxpayers potentially affected by marriage penalties or marriage bonuses.

To identify the income tax code provisions, we conducted a computer search of the IRC using certain key words such as "joint," "married," and "spouse," and we examined the available literature on the subject. Through this research we also determined how each section operated, and how it dealt with married and single taxpayers. From this analysis, we identified whether the specific treatment of married and single taxpayers could lead to marriage penalties or bonuses.

To determine the extent to which we could quantify the number of taxpayers potentially affected by marriage penalties and bonuses, we reviewed data available in IRS' public file on Statistics of Income, a compilation of tax data from a sample of individual tax returns. We also interviewed IRS staff responsible for research on individual returns. In addition, we researched the relevant literature to determine whether other theoretical models could provide sufficient information to estimate the numbers of taxpayers affected by IRC sections described in this report.

We did our work in Washington, D.C. between March 1996 and July 1996 in accordance with generally accepted government auditing standards.

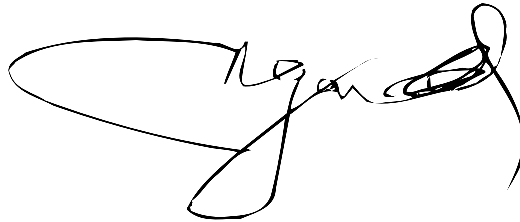
Agency Comments

We requested comments on a draft of this report from the Commissioner of Internal Revenue or her designated representative. At a meeting held August 2, 1996, representatives of the IRS Office of Chief Counsel suggested technical revisions to this report. We revised the report as suggested.

We are sending copies of this report to the Chairmen and the Ranking Minority Members of the House Committee on Ways and Means, the Senate Committee on Finance, and various other congressional committees; the Secretary of the Treasury; the Commissioner of Internal Revenue; and other interested parties. Copies will be made available to others upon request.

The major contributors to this report are listed in appendix VII. If you have any questions, please contact me on (202) 512-9044.

Sincerely yours,



Natwar M. Gandhi
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and Administration Issues

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Abbreviations

AGI	adjusted gross income
IRA	individual retirement account
IRC	Internal Revenue Code
IRS	Internal Revenue Service

Marriage Penalties and Bonuses Associated With Income Tax Provisions Allowing Some Adjustment for Joint and Single Income

In this appendix, we describe nine income tax provisions that have some type of tax adjustment (generally, a higher income limit) for the combined income of married taxpayers filing jointly relative to single taxpayers. The adjustments in this category, though, are always less than twice the limit allowed to single taxpayers. These sections include provisions that affect large numbers of taxpayers. For example, section 1 sets the rate schedules for all taxpayers, section 63 determines the standard deduction, and section 86 defines when social security benefits are taxable.

Generally, all these sections have one pattern for a penalty and one for a bonus—both of which are derived from the relative incomes of the two spouses. A married couple may have a tax penalty if both spouses have relatively equal income—in that case, their combined income may put them into a higher rate bracket or give them a lower deduction, even though individually each taxpayer would have been eligible for a lower tax bracket or a larger deduction. However, where the husband and wife have larger disparities in individual income, the couple may get a marriage bonus—in this case, the spouse with the higher income may owe less in a joint return than if he or she were to file as a single taxpayer.

To illustrate these tax penalties and bonuses, table I.1 shows how the tax rate under IRC section 1 affects the tax liabilities of two hypothetical married couples with the same household taxable income. For couple A, the husband and wife have the same taxable income while for couple B, the wife earns all the household income. To indicate a tax penalty or bonus, we compare the tax liability of these couples as joint filers with that of unmarried individuals.

Table I.1: Comparison of How the 1995 Tax Rate Schedule Affects Two Married Couples Filing Jointly and as Singles

	Couple A		Couple B	
	Husband	**Wife**	**Husband**	**Wife**
Income	$30,000	$30,000	0	$60,000
Combined income	$60,000		$60,000	
Tax if filed jointly	$8,503		$8,503	
Tax if filed as single	$3,580	$3,580	0	$11,980
Combined tax as singles	$7,160		$11,980	
Amount joint tax differs from tax as singles	$1,343		–$3,477	
Marriage penalty or bonus	Penalty		Bonus	

Source: GAO analysis of IRC section 1, assuming use of the standard deduction.

As shown in table I.1, couple A are penalized $1,343 by filing a joint return because their combined income puts them in a higher tax bracket than if they were each taxed as single individuals. On the other hand, couple B receive a $3,477 tax bonus by being able to file a joint return because the wife's $60,000 income is taxed at a lower rate filing jointly than it would have been had she been allowed to file as a single individual.

Table I.2 describes nine income tax provisions that have some type of tax adjustment.

Table I.2: 1995 Income Tax Provisions With Some Adjustment for Joint and Single Income

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
1. Section 1: Tax Imposed on Individuals (tax rates)	Tax rates are set according to personal status: married or single. Income tax rates are progressively increased at various income levels, depending on personal status. The tax rates range from 15 percent at the lowest income levels to 39.6 percent at the highest income levels.	Except for the highest tax rate, the income level at which tax rates are increased is higher for married couples than single people. However, it is not twice the level of the single income level. Thus, the tax rate for married couples is increased from 15 to 28 percent when joint taxable income is over $39,000, while a single person pays 28 percent if taxable income is over $23,350. Married filing separately is taxed at 28 percent when taxable income is $19,500. At the highest income rate (39.6 percent), the income level of $256,500 is the same for both married couples filing jointly and single people.	Relatively equal income between two spouses—tax rate would be less if each filed as single than if filed jointly.	Relatively unequal income between two spouses—tax rate would be greater if filed as single than if filed jointly.

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
2. Section 22: Credit for the Elderly and the Permanently and Totally Disabled (elderly credit)	If over 65 or disabled, taxpayer is eligible for credit of up to $1,125 for married couples and $750 for singles. However, the amount of the credit is reduced (and potentially eliminated) by amounts one-half of tax-free social security and pensions received by the taxpayer, and by amounts the taxpayer's adjusted gross income (AGI) exceeds certain limits.	The income levels at which the credit is reduced or eliminated are higher for married couples than single people, but not double. The credit for married couples with both spouses eligible is eliminated when either tax-free social security or other nontaxable income is $7,500 or more or AGI is $25,000 or more; for single people, the figures are $5,000 and $17,500, respectively. A married couple must file jointly to get credit unless couple is legally separated or taxpayer qualifies as an "abandoned spouse."[a]	Relatively equal income between two spouses—credit would be greater if each filed as single than if filed jointly.	Relatively unequal income between two spouses—credit would be less if each filed as single than if filed jointly.
3. Section 38: General Business Credit	Total amount of tax credits from 11 various business credits cannot exceed either the tentative alternative minimum tax or 25 percent of regular tax liability over $25,000, whichever is greater.	The operation of this provision is dependent on two other provisions, section 55 on the alternative minimum tax and section 1 on tax rates. For both these latter provisions, the income levels for the tax rates are higher for married couples than single people, but not double. If married filing separately, level is one-half of married filing jointly unless one spouse has no credit or carryover or carryback of the credit.	Relatively equal income between two spouses—credit would be greater if each filed as single than if filed jointly.	Relatively unequal income between two spouses—credit would be less if each filed as single than if filed jointly.

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
4. Section 55: Alternative Minimum Tax Imposed (alternative minimum tax)	Taxpayer who gets certain special deductions and credits may be subject to an "alternative minimum tax" if income exceeds certain levels.	The income levels for the minimum tax are higher for a married couple than a single person, but not double: married people are taxed if income is over $45,000, while single people are taxed if income is over $33,750. If married filing separately, level is $22,500.	Relatively equal income between two spouses—tax rate would be less if each filed as single than if filed jointly.	Relatively unequal income between two spouses—tax rate would be greater if each filed as single than if filed jointly.
5. Section 63: Taxable Income Defined (standard deduction)	Rather than itemize individual deductions, taxpayer can take "standard deduction." The amount of the deduction depends on personal status.	The amount of the deduction for a married couple is higher than for a single person, but not twice as much: married, $6,550; single, $3,900. If married filing separately, deduction is $3,275 and the other spouse may not itemize.	Both spouses have income over $6,400 and would elect to file individually with the standard deduction.	One spouse's income is less than $6,400 and the spouse would not file individually.
6. Section 86: Social Security and Tier I Railroad Retirement Benefits (social security benefits)	Social security income may be taxed if taxpayer has other types of income. To be taxed, the sum of the other income plus one-half of social security benefits must exceed certain limits.	Threshold limits at which social security is taxed are higher for a married couple than a single person, but not double: if married, up to 50 percent of benefits will be taxed if threshold exceeds $32,000, while if single, $25,000. If married filing separately, any other income will result in taxable social security, unless legally separated, or an abandoned spouse, or live apart from spouse the entire year.	One spouse's taxable income may require other spouse's social security benefits to be taxed.	Relatively unequal income between two spouses—tax on individual benefits would be more than tax on combined income.

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
7. Section 135: Income from U.S. Savings Bonds Used to Pay Higher Education Tuition and Fees (savings bonds for education)	Taxpayer who redeems U.S. savings bonds to pay college expenses can exclude from income the amount of interest earned on the bonds. The exclusion is phased out when the taxpayer's modified AGI exceeds certain limits.	The limits at which the exclusion is phased out are higher for a married couple than a single person, but not double: for married couple, phased out if modified AGI is $63,450 and eliminated at $93,450; for single, the figures are $42,300 and $57,300, respectively. Married person (unless "abandoned spouse") cannot qualify unless files jointly or is legally separated.	Relatively equal income between spouses—exclusion would be greater if filed individually than if filed jointly.	Relatively unequal income between spouses—exclusion would be less if filed individually than if filed jointly.
8. Section 151(d)(3): Phaseout of Allowance of Deductions for Personal Exemptions (personal exemption phaseout)	Taxpayer can deduct $2,500 for each personal exemption—for taxpayer, spouse, dependents. The deduction is phased out if AGI is above certain limits.	The deduction begins to be phased out at higher AGI for married couple than single person, but not double: if married, over $172,050; if single, over $114,700. If married filing separately, deductions phased out over $86,025.	Relatively equal income between spouses—exemptions would not be phased out if each filed individually.	Relatively unequal income between spouses—exemption for higher-income spouse would be phased out if each filed as single rather than as married.
9. Section 219(g): Retirement Savings (individual retirement account with employer plan)	Taxpayer can deduct up to $2,000 per year in tax-free individual retirement account (IRA). However, if also in employer pension plan, deduction is reduced over certain modified AGI levels.	The deduction begins to be phased out at higher AGI if filing joint return than filing as single person, but not double the amount of the single taxpayer: if married, phased out beginning at modified AGI over $40,000; if single, beginning at modified AGI over $25,000. If married filing separately, will be phased out when AGI exceeds zero, unless the married couple lives apart for whole year.	Relatively equal income between spouses—deduction would not be phased out if each filed individually.	Relatively unequal income between spouses—deduction would be phased out if each filed as single rather than as married.

[a]See footnote 1 on page 1. A taxpayer who qualifies as an "abandoned spouse" is not considered married for the purposes of the IRC. Such a taxpayer may file as a single person or as a head of household. This option is applicable for all code sections discussed in this report.

Source: GAO's analysis of IRC provisions.

Marriage Penalties and Bonuses Associated With Income Tax Provisions That Make No Adjustment for Joint and Single Income

In this appendix, we describe 15 income tax provisions that each allow some type of tax benefit—a credit, a deduction or an exclusion—which is limited either in the amount of the benefit or by the amount of total taxpayer income. For all these provisions, the benefit and income limits are the same whether for two married taxpayers or for one single taxpayer.

Each of these provisions offers the possibility of tax penalties to married couples and, generally, there are two patterns of potential marriage penalties. First, there would be a penalty when the joint income exceeds the limit for the tax benefit, even though individually one or both of the spouses could qualify for the benefit. As an example, consider a husband and wife who each earn $14,000, for a combined adjusted gross income (AGI) of $28,000. Because IRC section 32 on the earned income credit limits the earned income credit for 1995 to those taxpayers—married or single—with an AGI less than $26,673, the couple would be ineligible for the credit. However, if each had filed as a single taxpayer, both may have qualified for the credit.

Another type of penalty is possible where the tax benefit is limited to one amount—for either a married or single taxpayer—and the married couple would have reported more than that amount if they had each filed as single taxpayers. For instance, if two taxpayers each have $3,000 in capital losses, for a total of $6,000 in losses, the deduction limit of $3,000 in IRC section 1211 imposes a tax penalty on a married couple.

However, nine of these provisions, including IRC section 1211 on capital losses, offer possible tax advantages to a married couple that are unavailable to two similarly situated single people. With joint returns, taxpayers could pool their income and deductions, using any available deductions to offset their combined income. Thus, where one spouse has a deduction (or a loss), that amount could be applied to reduce the income (or gains) of the other spouse.

Table II.1 shows the tax consequences of the marriage penalties and bonuses related to section 1211 on capital losses. Couple A is a hypothetical married couple where each spouse has sold property, each losing $8,000 in long-term capital losses. With couple B, though, the wife has incurred a long-term capital loss of $8,000 but the husband has sold property for a long-term capital gain of $8,000.

Table II.1: Comparison of 1995 Tax Liability Involving Capital Losses and Gains of Two Married Couples Filing Jointly and as Singles

	Couple A		Couple B	
	Husband	**Wife**	**Husband**	**Wife**
Taxable income (before capital gains or losses)	$30,000	$30,000	$30,000	$30,000
Capital gains (or losses)	($8,000)	($8,000)	$8,000	($8,000)
Capital loss deduction if filed jointly ($3,000 maximum)	($3,000)		0	
Tax if filed jointly	$10,897		$11,737	
Capital gains (or losses) if file as singles ($3,000 maximum loss deduction)	($3,000)	($3,000)	$8,000	($3,000)
Tax if filed as single	$4,532	$4,532	$7,612	$4,532
Combined tax as singles	$9,064		$12,144	
Amount joint tax differs from tax as singles	$1,833		–$407	
Marriage penalty or bonus	Penalty		Bonus	

Source: GAO analysis of IRC section 1211.

As can be seen in table II.1, couple A's tax liability as a married couple is $1,833 greater than their liability had they filed as singles. As single taxpayers, they could deduct $6,000 in capital losses, while they could deduct only $3,000 as a married couple. Couple B, though, received a tax bonus when they filed jointly. As married taxpayers filing jointly, they could use the wife's capital loss to offset the husband's gain. As single taxpayers, however, the husband would have had to report the full $8,000 as capital gain, and the wife could have deducted only $3,000 of her capital losses from ordinary income.

Table II.2 describes 15 income tax provisions that allow some type of tax benefit.

Table II.2: 1995 Income Tax Provisions With No Adjustment for Joint and Single Income

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
1. Section 21: Expenses for Household and Dependent Care Services Necessary for Gainful Employment (child-care credit)	Taxpayer who maintains more than 50 percent of household expenses is allowed a credit for child-care expenses of up to $720 for one child, $1,440 for two or more. Credit is for 20-30 percent of expenses, depending on AGI, but cannot exceed taxpayer's earned income. The reduction of the percentage begins at AGI in excess of $10,000 and ends at AGI over $28,000.	Income limits are the same for a married couple as for a single person. A married couple must file jointly to get credit, unless taxpayer is legally separated or qualifies as an abandoned spouse. Unless one spouse is a full-time student, both spouses must work, and credit cannot exceed either spouse's earned income. If spouse is a full-time student, the spouse is considered to earn $200 per month.	The combined income of both spouses may reduce credit, even though individually one or both spouses may be eligible for larger credit.	Full-time student without earned income but otherwise eligible for the credit, will be able to take credit if married.
2. Section 32: Earned Income Credit	Low-income taxpayer with earned income allowed credit. With two children, credit up to $3,110, but eliminated if AGI greater than $26,673. With no children, allowed up to $314, but eliminated at AGI of $9,230.	Income limits are the same for a married couple as for a single person. A married couple generally must file jointly to get credit, unless taxpayer qualifies as an abandoned spouse.	The combined income of both spouses may reduce or eliminate credit, even though individually one or both spouses may be eligible for larger credit.	Person with no children but with income less than limit marries person with children and little or no earned income.
3. Section 62(b)(2): Certain Trade and Business Expenses of Qualified Performing Artist (performing artist expense)	Performing artists whose AGI without regard to this deduction is $16,000 or less may deduct certain business expenses to determine AGI, rather than as a miscellaneous itemized business deduction.	Income limits are the same for a married couple as for a single person. A married couple must file a joint return, unless taxpayer lived apart from spouse for entire year or qualifies as an abandoned spouse.	The combined income of both spouses may eliminate deduction, even though individually one or both spouses may be eligible.	Married couples can pool income and deductions—spouse eligible for deduction has little or no income.
4. Section 68: Overall Limitation on Itemized Deductions (itemized deduction limit)	If AGI exceeds $114,700, certain itemized deductions (not medical, investment interest, casualty loss, or gambling loss) are reduced.	Income limits are the same for a married couple as for a single person. If married couple elect to file separately, limit is $57,350.	The combined income of both spouses may require reduction in deductions, even though individually one or both spouses would not be required to reduce deductions.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
5. Section 121: One-Time Exclusion of Gain from Sale of Principal Residence by Individual Who Has Attained Age 55 (one-time residential sale exclusion)	Taxpayer over 55 who sells principal residence may exclude up to $125,000 in gain from the sale. Taxpayer may elect to exclude gain only once during lifetime.	Exclusion amount is the same for married couple as for single person. Married couples must jointly elect to exclude the gain whether filing jointly or separately. Once having elected to exclude gain, must jointly revoke to revise. Married filing separately may exclude up to $62,500.	Two unmarried taxpayers would be eligible for twice the amount of the total exclusion.	None
6. Section 129: Dependent Care Assistance Programs (employer child-care benefits)	Taxpayer can exclude employer benefits for child-care, up to either $5,000 or the amount of earned income, whichever is smaller.	Limit on exclusion is the same for married couple or single person. Married couple is limited to the smaller amount of earned income by either spouse, and if filed separately, total exclusion cannot exceed $2,500.	Two unmarried taxpayers would be eligible for twice the amount of the total exclusion.	None
7. Section 163(h)(3): Qualified Residence Interest (mortgage interest deduction)	Taxpayer can deduct interest costs on mortgages from one or two residences and on home equity debt. The mortgage balance cannot exceed $1 million, and the amount of the home equity loan cannot exceed $100,000.	Limit on mortgage principal is same for married couple or single person. If married couple files separately, loan limits are reduced to $500,000 for mortgage and $50,000 for home equity, and each spouse can only deduct interest from one residence unless other spouse consents in writing.	Two unmarried taxpayers would be eligible for twice the amount of the total deduction.	Married couple can pool income and deductions—spouse with deduction has less income than deduction amount.
8. Section 165(l): Losses in Insolvent Financial Institutions (uninsured financial deposit loss)	Taxpayer can deduct losses of uninsured financial deposits as a miscellaneous itemized deduction, to the extent that losses are over 2 percent of AGI, up to $20,000, with respect to each financial institution.	Limit on loss deduction is same for married couple as for single person. If married filing separately, the limit is reduced to $10,000, with respect to each financial institution.	Two unmarried taxpayers would be eligible for twice the amount of the total deduction.	Married couple can split deductions—spouse with lower income can file separately to meet AGI percentage.
9. Section 179: Election to Expense Certain Business Assets (section 179 assets)	The cost of certain tangible personal property used over 50 percent for business can be treated as expense and immediately deducted. The deduction is limited to $17,500.	Limit on deduction is same for married couple or single person. If married filing separately, the limit would be automatically divided between the spouses, unless otherwise agreed.	Two unmarried taxpayers would be eligible for twice the amount of the total deduction.	Married couple can pool income and deductions—spouse with deduction has less income than deduction amount.

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
10. Section 194: Amortization of Reforestation Expenses (reforestation deduction)	Certain costs of maintaining timber property can be amortized over 7-year period. However, taxpayer is limited to $10,000 per year.	Limit on deduction is same for married couple or single person. If married couple files separately, limit is reduced to $5,000.	Two unmarried taxpayers would be eligible for twice the amount of the total deduction.	Married couple can pool income and deductions—spouse with deduction has less income than deduction amount.
11. Section 469: Passive Activity Losses and Credits Limited (passive activity loss)	Taxpayer can deduct losses from rental real estate against ordinary income only if taxpayer is "active participant." Deduction is limited to $25,000 per year, and is reduced if AGI exceeds $100,000 and eliminated if AGI is over $150,000. Excess losses can be deferred to future years.	Deduction amounts and AGI limits are the same for married couple as for single person. However, married filing separately cannot take deduction if the spouses lived together any time during the tax year. If lived apart the entire year, deduction limited to $12,500, reduced if AGI is over $50,000, and eliminated if AGI is over $75,000.	Two unmarried taxpayers would be eligible for twice the amount of the total loss; also, combined income, but not individual income, reduces or eliminates amount of loss deduction.	Married couple can pool passive gains and losses—loss from one spouse will offset gain from other spouse; also, generally can pool income and deductions—spouse with deduction has less income than deduction amount.
12. Section 1044. Rollover of Publicly Traded Securities Gain into Specialized Small Business Investment Companies (small business rollover)	Taxpayer can elect to roll over gain from sale of public stock if gain is reinvested in a small business licensed by the Small Business Administration. The tax basis of the small business stock (which is used to calculate gain or loss on a later sale of that stock) is reduced by the rolled over gain. Limit on rollover is $50,000 a year, or $500,000 reduced by amount previously rolled over, whichever is smaller.	Limits are same for married couple as for single person. If married couple files separately, rollover amount is limited to $25,000, or $250,000 reduced by amount previously rolled over, whichever is smaller.	Two unmarried taxpayers would be eligible for twice the amount of the rollover gain.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
13. Section 1202: 50 Percent Exclusion for Gain from Certain Small Business Stock (small business stock exclusion)	Beginning in 1998, a taxpayer can exclude 50 percent of the gain from sale of stock in qualified small business if purchased at its original issue and held for 5 years. Gain is limited to $10 million reduced by amounts previously excluded or 10 times the taxpayer's basis in the business, whichever is greater.	Exclusion limit is same whether for married couple or single person. If married couple files separately, taxpayer is limited to $5 million reduced by amounts previously excluded or 10 times the taxpayer's basis in the business, whichever is greater.	Two unmarried taxpayers would be eligible for twice the amount of the total exclusion.	None
14. Section 1211: Limitations on Capital Losses (capital loss)	Taxpayer can deduct a net capital loss of $3,000 against ordinary income. Excess over $3,000 can be carried forward into future years.	Deduction limit is same for married couple or single person. If married couple filing separately, annual deduction is limited to $1,500.	Two unmarried taxpayers would be eligible for twice the amount of the total loss.	Married couple can pool capital gains and losses—loss from one spouse can offset gain from other spouse.
15. Section 6654: Failure by Individual to Pay Estimated Income Tax (estimated income tax)	If estimated quarterly payments are based on last year's tax, taxpayer with AGI under $150,000 must pay quarterly 25 percent of 100 percent of last year's tax. If AGI is over $150,000, taxpayer must pay quarterly 25 percent of 110 percent of last year's tax.	AGI limit is same for married couple as for single person. If married couple files separately, must pay quarterly 25 percent of last year's tax if AGI is $75,000 or less. If AGI is over $75,000, taxpayer must pay quarterly 25 percent of 110 percent of last year's tax.	Combined spousal income, but not individual income, increases amount of estimated tax to be paid quarterly.	None

Source: GAO's analysis of IRC provisions.

Marriage Penalties and Bonuses Associated With Income Tax Provisions That Fully Adjust for Joint and Single Income

The nine IRC provisions described below fully adjust for joint and single income. The operations of these tax provisions are widely different. Some of these provisions effectively treat married taxpayers the same as if they were single people. IRC section 6017, for example, requires that self-employment tax be calculated separately on each spouse's individual self-employment income. Section 213 allows a married taxpayer filing separately to report medical deductions with the same limitations allowed a single taxpayer. Other sections allow a married couple twice the benefit allowed a single person. Thus, section 1244 permits married couples to deduct $100,000 in losses, while a single person is limited to $50,000.

For the most part, these sections can only result in the same, or less, tax liability for married taxpayers than for single people. Thus, the self-employment tax assessed on two married people should always be the same as that assessed for a similarly situated unmarried couple. Three sections—section 213 on medical deductions, section 165 on nonbusiness losses, and section 172 on net operating losses—require that married taxpayers file separately to take full advantage of the tax bonuses possible for a married couple. When married taxpayers file separately, many tax provisions reduce or eliminate the tax benefits available to the taxpayer. To take full advantage of these three sections, therefore, a married taxpayer may have to forgo other possible tax benefits, leading to a possible tax penalty.

We illustrate the impact of a tax provision that allows married taxpayers twice the benefit provided to single people in table III.1 below. In this table, we show how income tax section 1244, which allows married taxpayers to deduct up to $100,000 on the sale of certain small business stocks, would affect two married couples filing jointly and as singles. Each spouse in couple A holds $50,000 in small business stock losses, while for couple B, the husband has incurred $100,000 in losses by himself.

Table III.1: Comparison of How Section 1244 Loss Deductions Affect Two Married Couples Filing Jointly and as Singles in 1995

	Couple A		Couple B	
	Husband	**Wife**	**Husband**	**Wife**
Taxable income (before 1244 losses)	$60,000	$60,000	$60,000	$60,000
1244 losses	$50,000	$50,000	$100,000	0
1244 loss deduction if filed jointly ($100,000 is maximum loss)	$100,000		$100,000	
Tax if filed jointly	$3,004		$3,004	
1244 loss deduction if filed as single ($50,000 is maximum loss)	$50,000	$50,000	$50,000	0
Tax if filed as single	$1,504	$1,504	$1,054	$13,876
Combined tax as singles	$3,008		$14,930	
Amount joint tax differs from tax as singles	–$4		–$11,926	
Marriage penalty or bonus	Bonus		Bonus	

Source: GAO analysis of IRC section 1244.

As shown in table III.1, couple A's tax liability is nearly the same whether the couple files jointly or single individuals. In each case, both spouses could deduct the full amount of their individual section 1244 losses. Couple B, on the other hand, received an $11,926 tax bonus by filing jointly because the husband's entire loss (which is twice that allowed a single person) can be applied to offset his wife's income.

Table III.2 describes nine tax provisions that fully adjust for joint and single income.

Table III.2: 1995 Income Tax Provisions With Full Adjustment for Joint and Single Income

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
1. Section 151: Allowance of Deduction for Personal Exemptions (personal exemptions)	Taxpayer is allowed to deduct $2,500 as "personal exemption." Personal exemption also allowed for spouse and all dependents.	Each married taxpayer is allowed same exemption amount as a single taxpayer; each spouse is allowed to deduct $2,500.	None	Exemption amount for one spouse with little or no income can be used to offset larger income of other spouse.
2. Section 165: Losses (casualty and gambling losses)	Taxpayer can deduct certain nonbusiness losses: casualty losses, to the extent that each loss is over $100 and the net casualty loss exceeds 10 percent of AGI; and gambling losses, up to amount of gambling wins.	Married taxpayers and single taxpayers are treated the same—married taxpayers can file separately to reduce AGI levels. Married taxpayers are subject to same limits whether filing jointly or separately.	To take full advantage of possible marriage bonus related to casualty loss, spouses must file separate returns. Separate returns would, in many instances, reduce or eliminate other tax benefits available to the taxpayer.	Married taxpayers can file separately to reduce AGI levels; can also pool gains and losses.
3. Section 172: Net Operating Loss	In cases where casualty or theft losses exceed total income, the taxpayer may have a "net operating loss." In this case, the taxpayer can deduct amount against taxes in either prior or future years.	Married taxpayers and single taxpayers are treated the same—married taxpayers can file separately to reduce income level. Married taxpayers are subject to same limits whether filing jointly or separately.	To take full advantage of possible marriage bonus, spouses must file separate returns. Separate returns would, in many instances, reduce or eliminate other tax benefits available to the taxpayer.	Married taxpayers can file separately to reduce AGI levels; can also pool gains and losses.
4. Section 213: Medical, Dental, Etc., Expenses (medical expenses)	Taxpayer can deduct medical expenses to the extent that the expenses exceed 7.5 percent of AGI. Taxpayer can also deduct medical expenses for spouse and dependents.	Married taxpayers and single taxpayers are treated the same—married taxpayers can file separately to reduce income level. Married taxpayers are subject to same limits whether filing jointly or separately.	To take full advantage of possible marriage bonus, spouses must file separate returns. Separate returns would, in many instances, reduce or eliminate other tax benefits available to the taxpayer.	Married taxpayers can file separately to reduce AGI levels; one spouse can also deduct expenses paid for medical costs of other spouse.
5. Section 219: Retirement Savings (IRA with no employer plan and special IRA)	If taxpayer is not covered by an employer pension plan, taxpayer can deduct up to $2,000 per year, limited to amount of earned income.	IRA deduction for two married taxpayers calculated exactly same as single taxpayers. However, if one spouse's income is less than $250, other spouse can deduct up to $2,250 for both.	None	"Special IRA" allows a larger IRA deduction to married taxpayer whose spouse has very little or no income.

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
6. Section 1034: Rollover of Gain on Sale of Principal Residence (residence rollover)	Taxpayer who sells old home and buys new home costing at least as much as the old home must roll over gain on sale by applying the amount of the gain to reduce the basis of the new home. The tax basis of the new home is reduced by the gain. Can only be used once every 2 years.	Married taxpayers allocate the rollover of gain on sale of a residence, without regard to who owned the old home or who bought the new home, if both meet certain requirements.	None	None
7. Section 1244: Losses in Small Business Stock	Taxpayer can deduct loss from sale or exchange of certain small business stocks against ordinary income, limited to $50,000 per year.	For married couples, the deduction limit is twice that allowed single taxpayers—$100,000 if married filing jointly.	None	One married taxpayer can deduct up to twice as much as single taxpayer.
8. Section 6017: Self-Employment Tax Returns (self-employment tax)	Every taxpayer with self-employment income over $400 must file a return and report on self-employment tax.	Married taxpayers calculate self-employment tax exactly as if they were two single taxpayers—tax is computed on separate earnings of each spouse. The amount reported on the joint return is the sum of the two taxes.	None	None
9. Section 6096: Designation by Individuals (presidential campaign)	Every taxpayer may designate that $3 be paid to the Presidential Election Campaign Fund.	Married taxpayers treated as if they are two single taxpayers—each spouse may designate $3 to campaign fund.	None	None

Source: GAO's analysis of IRC provisions.

Marriage Penalties and Bonuses Associated With Income Tax Provisions That Treat Married Taxpayers as Special Unit

Table IV.1 describes the operations of 26 IRC sections that treat married taxpayers as unique units. For the most part, these sections relate to special situations between spouses—for example, loans or sales between husband and wife.

The purpose of many of these provisions was to regulate sham transactions in commercial ventures. For example, IRC section 1092 taxes "straddles"—business investments in which the taxpayer buys two interests in property, each of which offsets the other. Under the current tax law, the investor cannot recognize the loss in one interest without realizing the gain in the offsetting investment. To identify a straddle position, any property purchased by a wife that offsets property previously purchased by her husband is considered to be owned by the husband. Under certain circumstances, this provision could create a tax penalty, where, for instance, both husband and wife are independent investors. In that case, the married couple might incur a greater tax liability than a similarly situated unmarried couple.

Table IV.1: 1995 Income Tax Provisions Treating Married Taxpayers as Special Unit

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
1. Section 1(g): Certain Unearned Income of Minor Children Taxed as if Parent's Income (kiddies tax)	Child under 14 will be taxed at parent's highest marginal rate.	If married parents file separately, child is taxed at the rate of the parent with the highest income.	Even if child's custodial parent files separately, the child's unearned income is taxed based on the rate of the parent with the highest income.	None
2. Section 42: Low-Income Housing Credit	Tax credit for investment in low-income housing project. Credit must be recaptured if project fails to meet program requirements.	Certain partnerships with 35 or more partners are treated as one taxpayer for the purpose of recapture unless partnership elects not to be so treated; a husband and wife are considered one partner of such a partnership.	If husband and wife are in a partnership dealing with low-income housing unit, they will not be considered independent investors for purpose of determining whether partnership is to be treated as one unit for purpose of recapture.	None
3. Section 63(c)(6): Certain Individuals Not Eligible for Standard Deduction (election to itemize)	A married individual filing a separate return is not eligible for a standard deduction if spouse itemizes deductions.	Where married taxpayers file separately, both spouses must either itemize their deductions or elect to take the standard deduction.	If unmarried, two taxpayers could determine individually whether to itemize or use the standard deduction.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
4. Section 125: Cafeteria Plans	A taxpayer need not include any amount in income solely because, as an employee, the taxpayer may choose among different compensation benefits, unless the taxpayer can be considered a “highly compensated” employee.	The spouse of a “highly compensated” employee may have to include income attributable to a choice of benefits if he or she is also a participant in the compensation plan.	Two taxpayers, who are neither married to each other nor is one a dependent of the other, would not be affected by this provision.	None
5. Section 147(a): Substantial User Requirement of Certain Private Activity Bonds (private activity user)	Where a holder of a private activity bond is a “substantial user” of the local facilities financed by the bond, the bond is not eligible for tax-exempt status. Any interest earned from the bond must be included in income.	If the bond holder’s spouse is a “substantial user” of the facilities financed by the bond, the bond is not qualified for tax-exempt status.	Two unrelated taxpayers who are not married to each other would each be able to use private activity facility without affecting the tax status of the other.	None
6. Section 147(c)(2): Limitation of Use of Certain Private Activity Bonds for Land Acquisition (private activity first-time farmer)	Private activity bond is not qualified for tax-exempt status if 25 percent of the proceeds are to be used to buy land except if land purchase is for the use of a “first-time farmer.” First-time farmer must have never previously owned a farm and must not have received over $250,000 in financing.	Any prior ownership of a farm, or receipt of financing, by the first-time farmer’s spouse will be imputed to the farmer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision and neither would be bound by the prior history of the other.	None
7. Section 162(l)(1): Special Rules for Health Insurance Cost of Self-Employed Individuals (self-employed health insurance)	Self-employed taxpayer can deduct up to 30 percent of health insurance costs.	Taxpayer can deduct costs of health insurance for spouse and dependents.	None	If unmarried, taxpayer cannot deduct costs of medical insurance of another person who is not a dependent.
8. Section 263A(e)(2): Exception to Capitalization Requirements for Farming Businesses (farm deduction)	Taxpayer can elect to deduct costs of certain plants used on farm.	Taxpayer bound by deduction elected by spouse.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and neither would be bound by the prior deductions elected by the other.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
9. Section 267: Losses, Expenses and Interest with Respect to Transactions between Related Parties (related party losses)	No deduction is allowed for loss from sale or exchange of property between "related parties." Related parties includes spouse.	Married taxpayers cannot deduct losses from transactions between spouses.	Two unrelated taxpayers who are not married to each other can deduct losses from a sale of property between them.	None
10. Section 318: Constructive Ownership of Stock (corporate ownership in distributions); also sections 302, 304	For purposes of certain corporate distributions and adjustments, the taxpayer will be considered to own stock owned by members of the taxpayer's family.	Ownership of stock by the taxpayer's spouse will be imputed to the taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and ownership of stock by one would not be attributed to the other.	None
11. Section 341: Collapsible Corporations	Gain from the sale, exchange, or distribution of a collapsible corporation is ordinary income.	Ownership of stock by the taxpayer's spouse will be imputed to the taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and ownership of stock by one would not be attributed to the other.	None
12. Section 424(d): Attribution of Stock Ownership (employee stock options); also sections 422, 423	Stock options or employee stock purchase plans provided to employee are not immediately taxable to the employee unless the employee owns certain amount of the company's stock.	For the purpose of the limitation on the tax-free provision, ownership of stock by the taxpayer's spouse will be imputed to the taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and ownership of stock by one would not be attributed to the other.	None
13. Section 544: Stock Ownership in Personal Holding Companies (personal holding companies); also sections 542, 543	An additional tax will be imposed on certain undistributed income in a personal holding company. To be a "personal holding company" there must be five or fewer shareholders and 60 percent of the company's income must be specified types of income.	For the purposes of the number of shareholders, ownership of stock by the taxpayer's spouse will be imputed to the taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and ownership of stock by one would not be attributed to the other.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
14. Section 613(A)(c): Exemption of Percentage Depletion Limitation for Independent Producers and Royalty Owners of Oil and Gas Wells (percentage depletion)	Independent producers and royalty owners are allowed to use the percentage depletion method to account for dwindling oil and gas reserves. However, percentage depletion is limited to a production of 1,000 barrels per day.	The oil and gas holdings of the taxpayer, the taxpayer's spouse, and other members of the taxpayer's family are treated as if held by one taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and holdings of one would not be attributed to the other.	None
15. Section 672: Related or Subordinate Party to Grantor of Trust (trust income); also sections 674, 675, 677	Trust income will be income to the grantor to the extent that the grantor has power to control the use of the trust assets. If power over the trust is exercised by an independent trustee, the grantor will not be treated as the owner.	A grantor/taxpayer's spouse is presumed to be a "subordinate party" to the grantor, and not an independent trustee for control of the trust assets. The grantor is also treated as holding any power or interest of the grantor's spouse.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and one taxpayer could act as independent trustee for the other.	None
16. Section 704(e): Partner's Distributive Share of Family Partnership (family partnership)	An interest in partnership purchased by one member of a family from another is treated as a gift from the seller and the fair market value of the purchased interest will be considered donated capital.	Taxpayer/seller's family includes spouse, ancestors, and lineal descendants.	Sale of partnership interest between two unrelated taxpayers not married to each other would not be considered a gift.	None
17. Section 911: Citizens or Residents of the U.S. Living Abroad (foreign housing allowance)	A taxpayer living abroad can elect to exclude from gross income a certain amount related to the costs of foreign housing.	The housing expenses excluded from gross income include those paid or incurred for the taxpayer's spouse and dependents.	None	If unmarried, taxpayer could not include housing expenses of another person into housing cost exclusion.
18. Section 1092: Straddles	A taxpayer with offsetting investment positions ("straddles") cannot recognize loss on these investments until the gain is realized.	To the extent that the taxpayer's spouse holds an investment position that offsets that of the taxpayer, the spouse's investment position will be attributed to the taxpayer.	Between an unmarried couple, the assets of one taxpayer would not be attributed to the other.	None
19. Section 1233: Gains and Losses from Short Sales (short sales)	Tax treatment of gain or loss from short sale of property depends upon whether the property used to close the sale was a capital asset.	For purposes of gain and loss on short sales, investments of either spouse are attributed to the other spouse.	If a couple is not married to each other, the assets of one taxpayer will not be attributed to the other.	None

(continued)

Code section	Description	Treatment of married taxpayers	Basis for penalty	Basis for bonus
20. Section 1235: Sale or Exchange of Patents (patents)	Sale or exchange of a patent is considered sale of a long-term capital asset, unless transfer is between related parties.	Any transfer of a patent between husband and wife will not be considered sale of a long-term capital asset.	If taxpayers unmarried to each other engage in sale of patent, the sale will be considered that of a long-term capital asset.	None
21. Section 1239: Gain from Sale of Depreciable Property between Certain Related Taxpayers (related party gains)	Gain from sale of depreciable property between related parties is considered ordinary income.	Gains on sale between husband and wife of depreciable property is treated as ordinary income.	Two unrelated taxpayers who are not married to each other can treat gains on sale of property between them as capital gains.	None
22. Section 1256(e): Mark to Market Not to Apply to Hedging Transactions (hedging transactions)	Gain or loss from contracts deemed section 1256 contracts shall be treated as 40 percent short-term gain or loss and 60 percent long-term gain or loss.	The interest of a spouse who actively participates in management will not be treated as held by a limited partner or limited entrepreneur.	Two taxpayers who are not married to each other would not be affected by this provision.	None
23.. Section 1272: Current Inclusion in Income of Original Issue Discount (original income discount)	Discount on issuance of certain bond or other debt instrument must be included in income as it accrues (it is considered a form of interest). However, this will not apply if it is a loan between two people, neither in business to make loans, and the loan is less than $10,000.	In considering the personal loan exception, husband and wife are treated as one person.	None	Married persons can make loans between one another without tax consequences.
24. Section 1361: S Corporation Defined	To qualify as an “S” corporation, a business cannot have more than 35 shareholders.	For the purposes of counting shareholders, husband and wife are treated as one person.	None	If both spouses own S corporation, only one will count toward limit on number of S corporation owners.
25. Section 1563: Controlled Group Corporation	Taxpayer has certain limits on multiple tax benefits if associated with certain controlled corporations.	For the purpose of determining whether entity is controlled group corporation, spouse’s stock holdings are attributed to the taxpayer.	Two unrelated taxpayers who are not married to each other would not be affected by this provision, and assets of one would not be attributed to the other.	None
26. Section 7872: Treatment of Loans with Below-Market Interest Rates (below-market loans)	If below-market interest rate on loan, IRS can impute interest income to the lender and interest expense to the borrower.	Husband and wife are treated as one person.	None	Married persons can make loans between one another without tax consequences.

Source: GAO’s analysis of IRC provisions.

Number of Taxpayers Filing Under Certain Provisions Cited in This Report

We compiled, from data in IRS' 1992 Individual Public Use Tax File for Statistics of Income, table V.1 showing the number of taxpayers who filed under various provisions described elsewhere in this report. The provisions included in this table are only those provisions for which such information is available in IRS' public tax file.[10] In addition to the number of taxpayers filing under each provision, by filing status, we have also included (in the last column) a cross-reference to the table where the provision has been described in this report.

Table V.1: Numbers of Taxpayers Filing in 1992 Under Specific Provisions Cited in This Report (Millions)

Income tax provision	All taxpayers	Married taxpayers filing jointly	Married taxpayers filing separately	Single taxpayers filing individually	Single taxpayers filing as head of household	Cross-reference to table where provision described
Section 1: filing status of taxpayers	113.60	48.02	2.46	48.58	14.45	Table I.2 (1)
Section 151:personal exemption	104.31	48.02	2.44	39.30	14.54	Table III.2 (1)
Section 63: standard deduction	80.07	25.15	1.53	40.92	12.47	Table I.2 (5)
Section 163(h)(3): home mortgage interest deduction	26.98	20.00	0.62	4.65	1.71	Table II.2 (7)
Section 6096: presidential campaign	23.31	10.02	0.40	9.40	3.50	Table III.2 (9)
Section 32: earned income credit	14.10	4.93	not applicable	0.36	8.81	Table II.2 (2)
Section 6654: estimated tax payments	12.78	7.47	0.15	4.80	0.35	Table II.2 (15)
Section 6017: self-employment tax	12.24	8.42	0.22	2.94	0.66	Table III.2 (8)
Section 86: social security benefits	10.78	6.35	0.12	3.98	0.34	Table I.2 (6)
Section 21: child-care credit (plus section 129 dependent care)	6.40	4.32	0.06	0.06	1.96	Table II.2 (1 and 6)

(continued)

[10]For many provisions listed in this report, information on how many taxpayers filed under the provision was not available in IRS' public file. For some provisions, such as section 135 on interest on U.S. savings bonds used for education, information is reported by the taxpayer but not available in IRS' public file. For other provisions, such as section 267 on related party losses, the taxpayer does not report any information on the application of the provision.

Income tax provision	All taxpayers	Married taxpayers filing jointly	Married taxpayers filing separately	Single taxpayers filing individually	Single taxpayers filing as head of household	Cross-reference to table where provision described
Section 213: medical expenses	5.51	3.50	0.11	1.5	0.39	Table III.2 (4)
Section 1211: net capital loss (a) total (b) with losses >$3,000	(a) 4.44 (b) 2.08	(a) 2.80 (b) 1.39	(a) 0.06 (b) none	(a) 1.41 (b) 0.62	(a) 0.17 (b) 0.07	Table II.2 (14)
Section 469: passive loss limits	3.66	2.59	0.05	0.87	0.14	Table II.2 (11)
Section 68: limitation on itemized deduction	3.34	2.92	0.04	0.31	0.07	Table II.2 (4)
Section 151(d)(3): reduction of personal exemption	1.68	1.26	0.06	0.31	0.04	Table I.2 (8)
Section 55: alternative minimum tax	0.29	0.19	0.02	0.07	0.01	Table I.2 (4)
Section 38: general business credit	0.25	0.21	<0.01	0.04	<0.01	Table I.2 (3)
Section 22: elderly tax credit	0.24	0.06	none	0.16	0.02	Table I.2 (2)
Section 42: low-income housing credit	0.14	0.11	<0.01	0.02	<0.01	Table IV.1 (2)
Section 165: net casualty loss	0.12	0.08	<0.01	0.02	0.01	Table III.2 (2)
Section 172: personal net operating loss	0.01	0.01	<0.01	<0.01	<0.01	Table III.2 (3)

Source: GAO analysis of IRS data.

Summary of Major Proposals to Change Current Treatment of Married and Single Taxpayers

Over the years there have been various proposals to change the tax treatment of married couples and single people. These proposals include: (1) mandatory separate filing by married couples using the same rate schedule as single taxpayers; (2) optional separate filing by married couples using the same rate schedule as single taxpayers; (3) tax deduction or credit for two-earner couples; (4) allowing single people to use the joint rate schedule; and (5) flattening the rate structure. These proposals all adjust, to some extent, the current balance among the principles of progressive tax rates, equal taxation of families with equal incomes, and marriage neutrality. We describe each of these proposals below.

(1) Mandatory separate filing by married couples using the same rate schedule as single taxpayers. This proposal would require all married taxpayers to file as single individuals, with one rate schedule for all taxpayers. In effect, this change would reinstate the tax system in place before 1948, and would impose different tax burdens on families with the same income. To address the problems of the different tax burdens in community property and common law states, rules would have to be set up to allocate income and deductions. Mandatory separate filing would eliminate the marriage penalties and bonuses in the current rate schedule. However, if the allocation rules for income and deductions were different for married and single people, new penalties and bonuses could be created.

(2) Optional separate filing by married couples using the same rate schedule as single taxpayers. As an alternative to mandatory separate filing, married couples could be allowed the option to file either under the joint rate schedule or the single rate schedule. (Currently, married couples can file separately, but the amount of taxable income at which the tax rates increase is much lower for such couples than for single individuals.) As with the first proposal, this would result in different tax burdens for families with the same income and there would need to be rules for allocation of income and deductions between spouses. Unlike the first proposal, though, there would be a certain revenue loss because only those married couples with tax decreases would be likely to file as single individuals.

(3) Tax deduction or credit for two-earner couples. Another proposal would continue the existing system of joint returns, but would provide some relief to two-earner married couples through a deduction (or credit) equal to a percentage of the earned income of the spouse with the lesser

amount of earnings. While this proposal would not make the system "marriage neutral," it would reduce the amount of the marriage penalty to two-earner couples. A tax deduction was allowed for two-earner couples between 1982 and 1986; this deduction was repealed by the Tax Reform Act of 1986. As enacted, this deduction provided lower taxes to all two-earner couples, not just those previously subject to a marriage penalty. Thus, although this reduced the marriage penalty for many couples, it also created marriage bonuses for other couples.

(4) Single taxpayers file under the joint rate schedule. A fourth proposal would allow single people to use the joint rate schedule. In effect, this would lower the tax rates for single people. This proposal would not lead to a system that would be "marriage neutral" and would, in fact, tend to increase the marriage penalty for two-earner couples. To be feasible, this proposal would need to be supplemented by other relief for two-earner couples, such as the tax deduction or credit described above.

(5) Flattening the rate structure. The final proposal would flatten the rate structure for all categories of taxpayers. By itself, this proposal would reduce the progressivity of the tax code. However, in doing so, it would decrease the number of tax brackets, thereby minimizing the effects of combining income on joint returns. When the Tax Reform Act of 1986 repealed the two-earner deduction, it also flattened the rate structure to reduce the marriage penalty to two-earner couples.

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