

## **THE MARRIAGE PENALTY: HOW INCOME STACKING AFFECTS THE SECONDARY EARNER'S DECISION TO WORK**

*Kevin M. Walsh\**

I.	OVERVIEW.....	84
II.	THE MARRIAGE PENALTY AND INCOME STACKING'S EFFECT ON SECONDARY EARNERS ...	85
III.	INEFFICIENCY, ELASTICITY AND CRITIQUED PROPOSALS .....	89
IV.	CHANGING THE FILING SYSTEM.....	95
V.	AMENDMENTS TO CURRENT POLICIES .....	98
VI.	CONCLUSION .....	100

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\* Experienced Associate, PricewaterhouseCoopers International Tax Services; LL.M. in Taxation, New York University School of Law, 2014; Law Clerk for the Superior Court of Connecticut, 2012-2013 term; J.D., Suffolk University Law School, 2012, *magna cum laude*; B.A., University of Michigan, 2008. Kevin wishes to thank his family, friends and professors for their support and encouragement.

## I. OVERVIEW

The progressive tax rate structure of the United States aims to tax citizens fairly and based on their ability to pay.<sup>1</sup> The rate structure, however, strays from this aim when applied to the income taxation of married individuals.<sup>2</sup> The federal government (“government”) may tax a married couple deciding to file jointly at a higher rate than the rate at which it taxes similarly situated individuals.<sup>3</sup> This has created what we know today as the “marriage penalty,” which can serve as a deterrent to the secondary earner from working.<sup>4</sup> There is no simple solution to address how the marriage penalty, in combination with necessary and cost of living expenses, affects the secondary earner’s decision to work. This is why legislators and scholars have introduced a variety of policies to help remedy the issue.<sup>5</sup> The policies currently in place, however, are not sufficient to resolve the issues surrounding the secondary earner’s decision to work.

This article will first describe the mechanics of how the marriage penalty and income stacking affect the secondary earner’s decision to work. It will then address some of the solutions that have been proposed to help remedy the issue and why these proposals are not viable solutions. Next, this article will introduce and describe a new solution to this issue. Furthermore, although many proposals attempt to resolve the issue of how the marriage penalty may negatively affect the secondary earner’s decision to work, they do not address childcare expenses, which are a major factor that a secondary earner takes into consideration when deciding whether to work or to stay at home and take advantage of imputed benefits. Lastly, this article will briefly discuss two options that are available to help offset childcare expenses and how these options can be improved to further eliminate the disincentive for the secondary earner to work.

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<sup>1</sup> I.R.C. § 1 (2012).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> Jim Wang, *How Much the Marriage Tax Penalty Will Cost You*, MY MONEY BLOG (Mar. 12, 2014, 9:00 AM), <http://money.usnews.com/money/blogs/my-money/2014/03/11/how-much-the-marriage-tax-penalty-will-cost-you>.

<sup>5</sup> Kiplinger’s Personal Finance Editors, *Tax Planning for Newlyweds*, KIPLINGER (Feb. 2014), <http://www.kiplinger.com/article/taxes/T055-C000-S001-marriage-and-taxes.html>.

## II. THE MARRIAGE PENALTY AND INCOME STACKING'S EFFECT ON SECONDARY EARNERS

To begin, it is important for the reader to understand the United States' system of taxing wage income. First, an individual earns wage income. This income is not the amount that the government taxes, however, because deductions, which are nominal amounts that reduce the dollar amount of income subject to taxation, are first applied.<sup>6</sup> These deductions include the standard deduction and personal exemption, which are available to everyone.<sup>7</sup> Taxpayers have the choice to use either the standard deduction or itemized deductions.<sup>8</sup> Itemized deductions are those that reduce income because of certain expenses, such as charitable giving.<sup>9</sup> The final product, after applying these deductions, is called the taxable income.<sup>10</sup> Taxable income is the amount of income to which tax rates are applied in determining taxes.<sup>11</sup>

The United States has a progressive tax rate structure. This means that different portions of one's taxable income are taxed at different rates. For example, if an unmarried individual has \$100,000 of taxable income, the government does not tax the entire \$100,000 at 31%.<sup>12</sup> Instead, the government taxes the first \$22,100 at 15%; the difference between \$22,100 and \$53,500 at 28%; the difference between \$53,500 and \$100,000 at 31%; and so on if the taxpayer earns more than \$100,000.<sup>13</sup> Congress adjusts these ranges as needed.<sup>14</sup> This is our progressive rate system. Next, this article will discuss the injustice regarding the taxation of a secondary earner's income and how that taxation affects his or her decision to work.

When a couple marries and decides to jointly file their tax returns

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<sup>6</sup> U.S. Dep't of Treas., I.R.S., Form 1040 (Washington, D.C. 2013), [www.irs.gov/pub/irs-pdf/f1040.pdf](http://www.irs.gov/pub/irs-pdf/f1040.pdf).

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> U.S. Dep't of Treas., I.R.S., Schedule A (Form 1040) (Washington, D.C. 2013), [http://www.irs.gov/file\\_source/pub/irs-pdf/f1040sa.pdf](http://www.irs.gov/file_source/pub/irs-pdf/f1040sa.pdf).

<sup>10</sup> U.S. Dep't of Treas., I.R.S., Form 1040, *supra* note 6.

<sup>11</sup> U.S. Dep't of Treas., I.R.S., Form 1040, *supra* note 6.

<sup>12</sup> I.R.C. § 1 (2012).

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*; see *National Taxpayer Advocate Delivers Annual Report to Congress; Focuses on Tax Reform, Collection Issues, and Implementation of Health Care Reform*, IRS (Jan. 5, 2011), <http://www.irs.gov/uac/National-Taxpayer-Advocate-Delivers-Annual-Report-to-Congress%3B-Focuses-on-Tax-Reform,-Collection-Issues,-and-Implementation-of-Health-Care-Reform>.

their incomes are essentially “pooled” together.<sup>15</sup> This “pooling” of income has multiple effects. For some couples, there is a marriage penalty because instead of each person taking advantage of the low-rate progressive structure, the government taxes the couple’s jointly filed income at higher rates sooner than it taxes single taxpayers for the same level of income.<sup>16</sup> For example, consider a situation in which a husband and wife each earn \$100,000 and file jointly. Together, their taxable income is \$200,000, and their tax liability is \$57,528.50 on their 2014 joint tax return.<sup>17</sup> However, if they could file as unmarried individuals, they each would have a tax liability of \$26,522.<sup>18</sup> The difference between these tax liabilities means that the couple faces a marriage penalty of \$4,484.50 when jointly filing as married individuals instead of filing as unmarried individuals. Said differently, the marriage penalty in this example is the difference between the total taxes applied to two similarly situated unmarried individuals of \$53,044 and the taxes applied to the married couple of \$57,528.50.

There is a strong bias in favor of single-earner families as a result of pooling spousal income, stacking the secondary earner’s income on top of the primary earner’s income, and applying the accompanying tax rate structure.<sup>19</sup> The majority of this article will describe how stacking the secondary earner’s income on top of the primary earner’s income may affect the secondary earner’s decision to work. The solutions described in detail below are proposed to address this issue.

When a couple pools their incomes together, the “secondary earner,” or the spouse that earns less income, is deemed to have his or her income “stacked” on top of the income of the spouse that earns more income, termed the “primary earner.”<sup>20</sup> This secondary earner is deemed to be the “marginal earner” because as a result of the income stacking previously

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<sup>15</sup> I.R.C. § 1.

<sup>16</sup> Edward J. McCaffery, *Taxation and the Family: A Fresh Look at Behavioral Gender Biases in the Code*, 40 UCLA L. REV. 983, 1025–26 (1993).

<sup>17</sup> See I.R.C. § 1; Robertson Williams, *Taxation and the Family: What are Marriage Penalties and Bonuses?*, TAX POLICY CNTR., <http://www.taxpolicycenter.org/briefing-book/key-elements/family/marriage-penalties.cfm> (last updated Apr. 4, 2008) (noting that the IRS makes it easy for users to compute tax liability by providing base amounts of tax that incorporate all previous rates).

<sup>18</sup> I.R.C. § 1.

<sup>19</sup> McCaffery, *supra* note 16, at 989, 1025–26.

<sup>20</sup> Lawrence Zelenak, *Marriage and the Income Tax*, 67 S. CAL. L. REV. 339, 365–66 (1994); Lawrence Zelenak, Book Note, *Tax and the Married Woman*, 70 S. CAL. L. REV. 1021, 1021–22 (1997) (reviewing EDWARD J. MCCAFFERY, *TAXING WOMEN* (1997)).

described, the government taxes each dollar of the secondary earner's income at the primary earner's marginal rate—which is the highest tax rate applied to taxable income for a particular individual.<sup>21</sup> Consider the following example to demonstrate this point further. If the primary earner is making \$460,000, the primary earner has reached the tax rate of 39.6%, which happens to be the highest tax rate in our current tax structure and in this instance, the marginal rate for the taxpayer. This means that if the primary earner makes \$50,000 more, the government taxes each dollar above \$460,000 at 39.6%. Similarly, if a secondary earner chooses to work in this scenario, each dollar the secondary earner makes is deemed to be taxed at 39.6% because the secondary earner's income is deemed to be stacked on top of the primary earner's \$460,000. The issue that arises is whether the secondary earner will choose to work upon consideration of what the net income will be following taxes and expenses.<sup>22</sup>

Assuming that the primary earner earns enough income to put the couple in the highest tax bracket, the government will tax all of the secondary earner's income at a 39.6% rate.<sup>23</sup> Adding in other payroll taxes, such as Social Security, Medicare, and state and local taxes, the government can subject the secondary earner to taxes on more than fifty percent of his or her gross income.<sup>24</sup> When deciding whether to work, an individual must also consider relevant expenses associated with working. These expenses include clothing, travel, training, and, most importantly, childcare.<sup>25</sup> Using New York as a benchmark, “[i]n Brooklyn, day care costs can cost \$1,700 per month, while it can run as much as \$2,300 a month in Manhattan.”<sup>26</sup> The secondary earner may not ultimately bring in much income to the household after taxes from earned wage income and the aforementioned necessary costs of working are taken into account. In fact, it may actually cost the secondary earner money to work considering the very high childcare expenses in locations such as New York City.

Other annual childcare costs, by state, include: Minnesota \$13,579 with a single mother median income set at \$26,123; Oregon \$11,079 with

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<sup>21</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 365–66.

<sup>22</sup> *Id.*

<sup>23</sup> I.R.C. § 1(a)(2).

<sup>24</sup> McCaffery, *supra* note 16, at 989.

<sup>25</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 351.

<sup>26</sup> McCaffery, *supra* note 16, at 1008–09; Aaron Smith, *Loans for Day Care Issued to New York City Parents*, CNN MONEY (Aug. 5, 2013), <http://money.cnn.com/2013/08/05/news/economy/day-care-loans/>.

a single mother median income set at \$22,250; and Colorado \$12,621 with a single mother median income set at \$26,366.<sup>27</sup> Although these childcare costs are less than those cited in New York, the costs can prevent the secondary earner's decision to work because after taxes there is not much net income leftover.

In deciding whether to work, the secondary earner will balance the potentially small gain from working against leisure time, the imputed income of working as a homemaker and taking care of children, and spending more time with family.<sup>28</sup> Thus, the secondary earner may choose not to work, and the primary earner may work more to make up the difference in income.<sup>29</sup> Financially, this may make the most sense. This scenario demonstrates that the Internal Revenue Code ("the Code") works inefficiently because it changes individuals' behavior by causing secondary earners to decide not to work as a result, at least partly, of tax implications.<sup>30</sup>

A main purpose of the Code is to raise revenue through income taxation.<sup>31</sup> The income taxes imposed, however, are not intended to change an individual's behavior.<sup>32</sup> The Code's influence over individual behavior speaks to its efficiency—the Code is operating efficiently if a tax does not change behavior.<sup>33</sup> The Code operates inefficiently if a tax changes behavior in a manner that was not intended by Congress.<sup>34</sup> For example, the Code operates inefficiently if Congress decides to tax water products so much that people no longer buy such products (a result that Congress would not likely intend). This article contends that when the Code operates inefficiently, Congress should amend it with respect to that particular policy to ensure that the Code does not affect behavior. In a similar sense, if the Code taxes wage income at a level that discourages individuals from working, such as through marginal rates imposed on secondary earners, then the Code operates inefficiently and Congress

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<sup>27</sup> Nat'l Ass'n of Child Care Resource & Referral Agencies, *Parents and the High Cost of Child Care*, CHILDCARE AWARE OF AM. (2012), <https://archive.org/details/625968-child-care-cost-report-2012-final-081012-0>.

<sup>28</sup> McCaffery, *supra* note 16, at 1026–28.

<sup>29</sup> *Id.*

<sup>30</sup> JOEL SLEMROD & JON BAKIJA, *TAXING OURSELVES: A CITIZEN'S GUIDE TO THE DEBATE OVER TAXES* 119–27 (4th ed. 2008).

<sup>31</sup> *Id.* at 13.

<sup>32</sup> *Id.* at 119–27.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

should amend it accordingly.

### III. INEFFICIENCY, ELASTICITY AND CRITIQUED PROPOSALS

The Code does not operate efficiently with respect to secondary earners because secondary earners are changing their behavior as a result of the tax consequences. Also, the Code does not operate fairly because secondary earners are taxed at the primary earner's marginal rate for the first dollar earned.<sup>35</sup> This is unfair to secondary earners because they do not have the opportunity to take advantage of the initial low tax rates in the Code's progressive rate structure (such as a 15% tax on the first \$22,100 of taxable income for unmarried individuals).<sup>36</sup> Instead, the government taxes the secondary earner's wage income as if the primary earner was simply making more money. As mentioned above, this means that if the primary earner were already making enough money for the government to tax this money at a marginal rate of 39.6%, the government would tax every additional dollar earned at 39.6%. Similarly, if the primary earner were already making enough money for the government to tax this money at a marginal rate of 39.6%, the government would also tax all income brought in by the secondary earner at 39.6% due to the income stacking effect.

Thus, regardless of whether the primary earner makes more income by himself or herself, or the secondary earner chooses to work to earn some income, the government taxes the income at the primary earner's marginal rate. This is not fair because the government taxes the secondary earner, who may earn significantly less than the primary earner, according to the highest level of the primary earner's tax rates, that is, the marginal rate. The effect of these high-level tax rates, in combination with childcare expenses and work-related expenses, may inhibit the secondary earner's decision to work and thereby, render the Code inefficient.

Similarly, secondary earners have an elastic labor supply curve because taxes play a large role in the secondary earner's decision to work.<sup>37</sup> Elasticity is an economic term that represents an individual's response to a change in price or in this case, a change in tax rates.<sup>38</sup> For

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<sup>35</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 365–66.

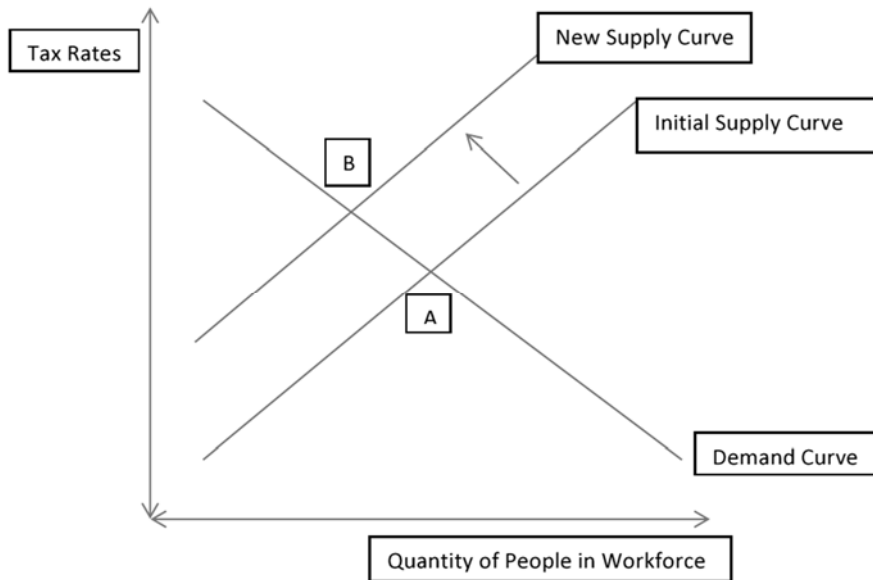
<sup>36</sup> I.R.C. § 1(c) (2012).

<sup>37</sup> McCaffery, *supra* note 16, at 1037–39.

<sup>38</sup> N. GREGORY MANKIW, *ESSENTIALS OF ECONOMICS (EXCERPTS) APPLICATION: THE COSTS OF TAXATION* 159–61 (Cengage Learning, 6th ed. 2011).

example, if an individual's purchasing behavior does not respond to a change in price, such as the price of medicine required for that person, that individual has an inelastic demand curve with respect to the price of medicine.<sup>39</sup> This means that no matter how much the medicine's price changes, the individual will buy the medicine.

In contrast, if an individual's behavior changes as a result of a change in price, that individual has an elastic demand curve.<sup>40</sup> For example, most individuals would stop buying a pack of Wrigley's gum if the price goes up by ten dollars. These individuals would have an elastic demand curve with respect to gum. Similarly, if tax rates increase, secondary earners are less likely to enter or remain in the workforce. These individuals would have an elastic labor supply curve with less people willing to enter or remain in the workforce. See the graph below for an illustration of this example:



The y-axis, or vertical axis, represents the income tax rates, and the x-axis, or horizontal axis, represents the quantity of people in the workforce. From an economic perspective, this graph illustrates that an

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

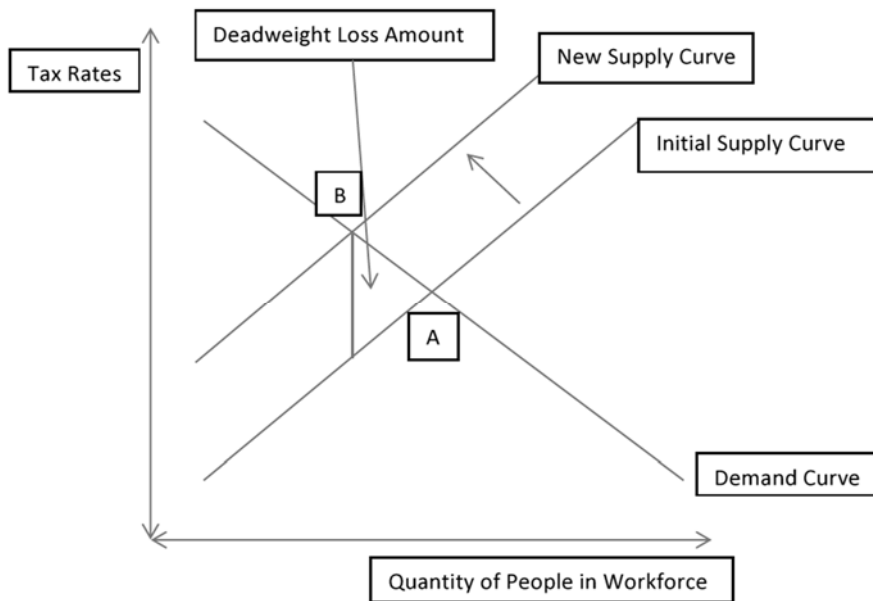


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## THE MARRIAGE PENALTY

91

increase in taxes will reduce the quantity of people in the workforce. The optimal scenario is where the “demand curve” and “initial supply curve” meet. This means that in this context, the demand for jobs equals the supply of jobs available. This is at point “A” on the graph. The Code operates efficiently at point “A.” However, with an increase in taxes, fewer individuals will be willing to enter or remain in the workforce or obtain second or third jobs. To show this increase in supply of jobs, meaning more jobs available and less people in the workforce as a result of the high tax rates, the supply curve shifts up or to the left. Now there is a new point, “B,” where the “new supply curve” meets the “demand curve.” Point “B” represents higher taxes and less people in the workforce than does point “A.” Point “B” is inefficient because it means that the supply of jobs now exceeds the demand for jobs or in other words, there is an excess supply of jobs. The Code operates inefficiently at point “B.” This excess of supply is called deadweight loss. Deadweight loss is an economic term that represents, in our context, the amount of workers that are lost in the workforce, meaning that workers are choosing not to work as a result of taxes.<sup>41</sup> The graph below is the same as above with the added “deadweight loss” concept:



<sup>41</sup> *Id.* at 156–62.

We want to limit this deadweight loss amount as much as possible because the loss amount means that secondary earners that would normally go to work are choosing not to, simply because of tax rates. In other words, the Code should be amended accordingly back to point “A” by reducing the applicable tax rates to secondary earners because the Code currently operates in an inefficient manner. If tax rates for secondary earners decrease, the amount of individuals entering the workforce would increase, that is, the excess supply of jobs would decrease because more people would be working, and depending on the chosen tax rate, it is possible that the excess supply of jobs is extinguished. This optimal scenario is point “A” on the first graph above.

Putting this all-together, secondary earners have an elastic labor supply curve because the supply curve shifted when tax rates increased to show the decrease of the quantity of people in the workforce. This means that as tax rates applied to the secondary earner’s wage income increase, less individuals enter or remain in the workforce or obtain additional jobs, which creates an excess supply of jobs, as described above. With higher tax rates, secondary earners are less likely to work at all or work more, whichever the case may be.<sup>42</sup> Said differently, for the group of secondary earners that choose to stay home as a result of tax rates, the substitution effect is greater than the income effect.<sup>43</sup> The substitution effect, in this context, means that as a result of the high taxes, the secondary earner will “substitute” working for staying at home, which shifts the supply curve to the left.<sup>44</sup> Thus, a labor supply deadweight loss, that is excess jobs, exists when the substitution effect results in the secondary earner choosing to stay at home in favor of working.<sup>45</sup>

In contrast, the income effect means that because of taxes imposed, the individual will need to work harder to make up for the difference in taxes imposed.<sup>46</sup> The primary earner’s income, on the other hand, is more inelastic than that of the secondary earner because the tax rate plays less of a role in the primary earner’s decision to work.<sup>47</sup> In other words,

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<sup>42</sup> McCaffery, *supra* note 16, at 1037–40.

<sup>43</sup> McCaffery, *supra* note 16, at 1037–40.

<sup>44</sup> McCaffery, *supra* note 16, at 1028, 1037–40.

<sup>45</sup> Lora Cicconi, Comment, *Competing Goals Amidst the “Opt-Out” Revolution: An Examination of Gender-Based Tax Reform in Light of New Data on Female Labor Supply*, 42 GONZ. L. REV. 257, 276–78 (2007).

<sup>46</sup> McCaffery, *supra* note 16, at 1028, 1037–40.

<sup>47</sup> McCaffery, *supra* note 16, at 1037–39.

regardless of the tax rate, the primary earner is going to work. In contrast to the secondary earner, the primary earner may be motivated to work harder to make up the difference as a result of a higher tax rate.<sup>48</sup> This exhibits the income effect on the primary earner.

Some scholars have proposed an optimal tax to address the elasticity discrepancy between the primary and secondary earner and the corresponding substitution/income effects.<sup>49</sup> Proponents of the optimal tax propose that secondary earners should be taxed less and primary earners taxed more.<sup>50</sup> Scholars reason primary earners are more inelastic to changes in wage tax rates because the increase in taxes will not affect their decision to work.<sup>51</sup> Additionally, optimal tax proponents argue that wage rates for secondary earners should be lowered because secondary earners are elastic to wage rates.<sup>52</sup> A justification for the optimal tax is that tampering with the tax system in this way can provide neutrality amongst spousal income earners.<sup>53</sup>

This proposal, however, treats primary earners and single filers unfairly. Under this proposal regime, primary earners would be treated unfairly because they would be intentionally taxed more, and secondary earners would be taxed less in an attempt to encourage secondary earners to work. This article takes up two issues with respect to potential consequences in the execution of the optimal tax for the married couple. First, even though the secondary earner's tax rates would be lowered, the secondary earner could still be subject to relatively high tax rates depending on the primary earner's marginal rate. If the secondary earner is still subject to relatively high tax rates and decides to stay home, the optimal tax would only have the effect of treating the primary earner of the household worse than before the additional taxes were imposed. As an overall effect, taxing the primary earner more, regardless of whether the secondary earner chooses to work or not, would negatively impact the

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<sup>48</sup> McCaffery, *supra* note 16, at 1037–39.

<sup>49</sup> Zelenak, *Tax and the Married Woman*, *supra* note 20 at 1023–25.

<sup>50</sup> Zelenak, *Tax and the Married Woman*, *supra* note 20 at 1023–25.

<sup>51</sup> Cicconi, *supra* note 45, at 276; Zelenak, *Tax and the Married Woman*, *supra* note 20, at 1023–25.

<sup>52</sup> Cicconi, *supra* note 45, at 276; Zelenak, *Tax and the Married Woman*, *supra* note 20, at 1023–25.

<sup>53</sup> Nancy E. Shurtz, *Taxing Women: Thoughts on a Gendered Economy: Symposium: A Socio-Theoretic Overview: Gender Equity and Tax Policy: The Theory of "Taxing Men,"* 6 S. CAL. REV. L. & WOMEN'S STUD. 485, 497 (1997).

financial status of the family unit. Second, even if the secondary earner decides to work, the married couple may have less income overall depending on what the primary and secondary earner's incomes are and their corresponding tax rates.

The optimal tax proposal would also be unfair to single filers. If imposed, the Code would favor secondary earners over other individuals because only secondary earner tax rates would be arbitrarily reduced. Moreover, single filers are their own primary earners. If Congress is allowed to tax primary earners in a family unit more, members of Congress may subsequently interpret the language to arbitrarily tax all primary earners at higher rates with no corresponding benefit to a secondary earner. Therefore, this policy is unfair and should not be enacted.

Scholars have also proposed a mandatory individual filing or election to file individually.<sup>54</sup> This proposal has some merit because under this proposal, the secondary earner is no longer making decisions based upon the primary earner's marginal rate and is encouraged to work through the use of deductions, credits, and low tax rates.<sup>55</sup> There are many problems, however, associated with separate filing for married individuals. For example, determining how income, deductions, and credits are allocated between the spouses may be problematic.<sup>56</sup> A determination of how to tax property income would be especially difficult to administer because the Internal Revenue Service ("IRS") would need to determine whether: (1) to tax the owner of the property; (2) to allocate property income equally; (3) to allocate property income in proportion to the spouses' earned incomes; (4) to allocate property income to the primary earner; or (5) to tax property income according to ownership and not give any tax effect to inter-spousal property transfers.<sup>57</sup> The allocation of deductions and credits would also be difficult for the IRS to administer because it would have to keep track of the deductions and expenses that each spouse is incurring.<sup>58</sup> The shortfalls of both the optimal tax and

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<sup>54</sup> Amy C. Christian, *The Joint Return Rate Structure: Identifying and Addressing the Gendered Nature of the Tax Law*, 13 J. L. & POL. 241, 357–59 (1997); Zelenak, *Tax and the Married Woman*, *supra* note 20, at 1034.

<sup>55</sup> Christian, *supra* note 54, 357–59; Zelenak, *Tax and the Married Woman*, *supra* note 22, at 1034.

<sup>56</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 381.

<sup>57</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 384.

<sup>58</sup> Zelenak, *Marriage and the Income Tax*, *supra* note 20, at 391–92.

separate filing proposals make it necessary to explore other options. Therefore, this article next addresses a novel proposal to resolve the marriage penalty and income stacking effect, both of which influence the secondary earner's decision to work.

#### **IV. CHANGING THE FILING SYSTEM**

In lieu of the optimal tax and individual filing proposals, this article proposes that the IRS should provide an election on the joint return for the secondary earner to exclusively file wage income as a single filer. To take advantage of this opportunity the married couple would have to file as married filing jointly. It would not make sense for spouses to file as married filing separately and then elect to have the secondary earner's wage income taxed at the single filer rates because the couple may have jointly owned assets that prevent them from filing separately. Instead, on the joint return, the IRS could provide an election that would allow the secondary earner to file his or her wage income (and only wage income) separately as a single filer. This would resolve the elasticity issue that income stacking has on secondary earners because the secondary earner would not make the determination of whether to work primarily based upon income taxed at the primary earner's marginal rate. Instead, the secondary earner could take advantage of the lower rate structure offered to single filers. Therefore, the single-filer tax consequences to the secondary earner would not have as much of an impact on the decision to work. Since the Code operates inefficiently when taxes impact an individual's behavior in a manner unintended by Congress, this would promote greater efficiency of the Code because taxes would not be the driving factor in the secondary earner's decision-making. In a similar fashion, this policy would help to alleviate the substitution effect that the primary earner's marginal tax rates have on secondary earners.

This policy is more desirable than the optimal tax and individual filing proposals for several reasons. First, under the proposed policy, filing jointly would be necessary because the couple would avoid the problems associated with filing separately as described above, such as having many assets in the same name. From an administrative perspective, the policy promotes administrative ease because the IRS would not need to worry about issues related to income shifting, property income allocation, or passive income allocation, such as interest and dividends for joint filers. This is because everything other than the secondary earner's wage income is filed with the joint return. Moreover,

the secondary earner's final tax owed would be simple to determine under this proposal because the tax rate would only be applied against wage income.

To make this work, the government must always tax the primary earner at the married filing jointly rates. This is an important point to take note of because the IRS would be unwilling to give up the taxes it receives as a result of married filing jointly rates. The IRS would only lose the taxes it would normally receive from secondary earners at the married filing jointly rates. The IRS needs to realize, however, that although the government will "lose" revenue on secondary earners that choose to work regardless of the tax rates, the government still currently loses revenue because the income stacking effect discourages secondary earners from working. The government would collect less from the secondary earners it is already collecting from, but will make up the difference with secondary earners that choose to work as a result of this proposed policy. Therefore, the proposed policy has a zero-sum effect for the government.

Further, the proposed policy would not result in unfair treatment to the IRS because under the proposed policy, the IRS would likely get at least the same amount of taxes it would have received if the secondary earner chose not to work due to the presence of income stacking. In fact, the IRS will receive additional taxes from wage income by secondary earners that choose to work in lieu of staying home.

The policy will have a profoundly positive impact on the financial status of married couples because secondary earners that were already working will pay less in taxes or secondary earners that choose to work will bring in all of that extra income to the family unit. This article contends there is a widespread positive effect for bringing more income into the family unit. For example, with these lower tax rates, higher quality child care will be more attainable because the family unit will be able to afford some increased costs. Better education, starting at the earliest levels, is fundamental to a child's learning development.<sup>59</sup>

There are, of course, a few wrinkles associated with this policy.<sup>60</sup> First, the IRS will need to determine guidelines for when the married couple can file the election. The IRS could allow the election when the

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<sup>59</sup> CHRISTOPHER BALL, *START RIGHT: THE IMPORTANCE OF EARLY LEARNING 6-10* (1994).

<sup>60</sup> There are many issues with the secondary earner bias and the marriage penalty. This election does not address the merits of other concerns/issues and how they would affect the viability to this proposal other than to the extent of the concerns discussed.

2015]

*THE MARRIAGE PENALTY*

97

primary earner's marginal tax rate reaches a certain level. This policy, however, is not fair because it would only benefit a specific group of individuals that fit within the determined applicable income levels. Instead, the IRS could allow the election based on the relation between the primary and secondary earner's wage income with a certain cutoff point (reasoning that the very rich would not be able to take advantage of this proposed policy). For example, the IRS could allow the election if the primary earner's wage income is at least double that of the secondary earner, but disallow it if the combined income is above a certain level.

The fairest proposition is the one that allows everyone, regardless of income, to take advantage of the proposed policy for the election on the joint return. Income stacking affects all married couples. The issue is not a wealth gap where taxation attempts to bridge and close the gap. Instead, the issue is that low, middle, and high-income secondary earners sometimes choose to stay at home as opposed to working because they are taxed at the primary earner's marginal rate, and it may not be worth it to work when taking work and child-related expenses into consideration. This injustice applies to all secondary earners, and the proposed policy should be applicable to everyone.

Another issue that arises is determining which deductions and credits can be used for the joint return and which for the election that taxes the secondary earner's wage income. A fair result would be to allow the couple to itemize and take credits on the joint return as they normally would have and only allow the secondary earner to take a standard deduction and personal exemption on the single filing return. This is a fair result for several reasons. First, as stated earlier, the government will still tax the primary earner at joint return rates. It would not be fair to the government to additionally allow the primary earner reduced rates. Second, the government should not allow the couple to double dip their itemized deductions on both returns because otherwise, the couple would be deducting for the same expenses twice. An allowance of such "double dipping" would cause horizontal inequity amongst similarly situated married couples that only deduct for expenses as originally intended.

Third, a main purpose of allowing the secondary earner to take advantage of single-filer tax rates is to permit the secondary earner to take advantage of the deductions that are applicable to everyone, that is the standard deduction and the personal exemption, so that the low tax rates are utilized to their greatest extent. As of 2014, the standard deduction

for unmarried individuals reduces income to be taxed by \$6,200, and the personal exemption reduces income to be taxed by \$3,950 multiplied by the total number of exemptions claimed.<sup>61</sup> Lastly, marriage benefits should not be affected. There are sure to be other problems associated with the proposed policy, but it is a great start in the right direction and is certainly an option worth exploring and possibly implementing.

Even if enacted, this policy would only help to resolve the income stacking effect that the primary earner's marginal tax rate has on the secondary earner's decision to work. There are other factors that affect the secondary earner's decision to work—most notably among them are childcare expenses. With childcare expenses reaching an average of \$2,300 per month in Manhattan, the government needs to offer deductions and credits to reduce the burden of such expenses.<sup>62</sup> There are several policies currently in place to help offset childcare expenses. These policies include the § 21 Dependent Care Tax Credit (“DCTC”) and the § 129 Dependent Childcare Assistance Program (“DCAP”).<sup>63</sup> These policies, however, do not adequately offset the expenses of child care.<sup>64</sup> Therefore, in addition to this article's proposal to tax secondary earner's wage income at single filer rates, this article also proposes that Congress should modify the DCTC and the DCAP to further encourage secondary earners with children to work.

## V. AMENDMENTS TO CURRENT POLICIES

The DCAP allows employees to take \$5,000 of their pay, tax-free, including social security taxes, in the form of childcare services.<sup>65</sup> The DCAP functions as a deduction, and therefore, a taxpayer may elect only the DCAP or the DCTC.<sup>66</sup> The problem with the DCAP is that the program requires an employer to establish the plan.<sup>67</sup> Since many employers do not, only a small amount of employees have access to this provision.<sup>68</sup>

The DCTC allows for a credit equal to 35% of the taxpayer's

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<sup>61</sup> U.S. Dep't of Treas., I.R.S., Form 1040, *supra* note 6.

<sup>62</sup> Smith, *supra* note 26.

<sup>63</sup> I.R.C. §§ 21, 129 (2012).

<sup>64</sup> McCaffery, *supra* note 16, at 1007–09.

<sup>65</sup> I.R.C. § 129(a); McCaffery, *supra* note 16, at 1007–09.

<sup>66</sup> McCaffery, *supra* note 16, at 1007–09.

<sup>67</sup> I.R.C. § 129.

<sup>68</sup> McCaffery, *supra* note 16, at 1007–09; Shurtz, *supra* note 53, at 521–23.



adjusted gross income for household and childcare expenses (reduced by 1% for every \$2,000 by which the taxpayer's adjusted gross income for the taxable year exceeds \$15,000, but the credit percentage is not to be reduced below 20%) up to \$3,000 for one child and \$6,000 for two or more children.<sup>69</sup> This provision, however, is "inadequate even to offset the tax costs of working to pay for child care" because childcare costs are extremely high and the total credit may hardly reach the amount of childcare expenses a family may incur.<sup>70</sup> For example, the DCTC may not offset a family's childcare expenses for a single month.

Congress can improve the DCTC in two ways. First, Congress should increase the applicable childcare expense amount to a flat \$3,000 for every child born.<sup>71</sup> As the law currently stands, the government caps the amount of support a family receives at \$6,000, which is the amount for two or more children. The DCTC amount should increase linearly by the amount of children in the family to fully account for childcare expenses the family incurs. Specifically, the DCTC amount should increase as the number of children increases because higher numbers of children naturally lead to higher childcare expenses. There should not be any administrative problems with this proposal because implementation only requires a change of the wording on the DCTC form.

Moreover, Congress should strike the adjusted gross income phase-out from the provision because the phase-out perpetuates the issue that the credits are not accounting for childcare expenses appropriately.<sup>72</sup> The phase-out distinguishes and hurts a specific group of individuals according to income, and this is unfair because as stated earlier, the secondary earner issue is one that applies to couples at all income levels. Putting these two modifications together, if a family has four children, the applicable DCTC amount should be \$12,000. This is the fairest construction of the statute because Congress should make an economic distinction between a family that has two children or four.

Broadly applying the proposed election on the joint return is just one piece of the puzzle. If this issue is going to be completely resolved, it needs to be addressed on all fronts without distinguishing individuals based on their incomes. As the laws currently stand, improvement of the

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<sup>69</sup> I.R.C. § 21(a)(c).

<sup>70</sup> McCaffery, *supra* note 16, at 1007–09.

<sup>71</sup> Cicconi, *supra* note 45, at 293–94 (author's proposal expanded upon).

<sup>72</sup> Cicconi, *supra* note 45, at 293–94.

DCTC is far more important than improvement of the DCAP because unlike the DCTC, the DCAP only applies to employees of a company that offers the program.<sup>73</sup>

## VI. CONCLUSION

The Code currently operates inefficiently with respect to married individuals. For some married taxpayers, the Code imposes a marriage penalty because the government taxes the married couple at higher rates sooner than it taxes single taxpayers for the same level of income. The secondary earner's income is deemed to be "stacked" on top of the primary earner's income, and the secondary earner's income is taxed at the primary earner's marginal rate, which can be very high. This taxation at the primary earner's marginal rate, in combination with other taxes imposed and associated working and childcare expenses, can cause the secondary earner to choose to stay at home instead of working.

Taxing the secondary earner's wage income at single filer rates and improving the DCTC may encourage secondary earners to work rather than choosing to stay at home because of taxes and expenses. This would result in the Code operating efficiently. Although these proposals may not completely resolve the issue, even if adopted together, such changes would be a step in the right direction.

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<sup>73</sup> I.R.C. § 129 (2012).