Federal Income Tax Thresholds for Selected Years: 1996 Through 2009

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Summary

One principle of tax fairness or equity accepted by many is that households at the low end of the income spectrum, especially those near the poverty threshold, should not be subject to the federal income tax. This report estimates income tax thresholds—the point at which taxpayers have an actual out-of-pocket income tax payment. In addition, the report compares these income tax thresholds to the latest available poverty thresholds for families of different sizes.

The major structural components of the income tax code which influence the income tax threshold levels include the standard deduction, the personal exemption, the child tax credit, and the earned income tax credit (EITC). Each of these items increases the income level at which an individual or family incurs an out-of-pocket federal income tax liability. In 2009, single taxpayers eligible for EITC with income below $11,124 do not face the income tax liability. Married couples with two kids do not have to pay income tax until their income reaches $44,900. The threshold for head of household filers with one child is $31,026 in 2009.

Federal income tax thresholds are high enough so that, with the exception of single taxpayers, the equity principle of exempting poverty level households from income taxation has been achieved over time. The introduction and subsequent increase in the child tax credit along with the measures reducing the marriage tax penalty, however, have significantly increased income tax thresholds for households with children, especially married filers.

For households with children, the income tax thresholds are now substantially higher than the comparable poverty thresholds. In fact, the child tax credit represents a departure from past policy practices because it is not designed primarily as a means of differentiating between families of different size at or near the poverty threshold, but rather is designed to provide general tax reductions to middle and upper income taxpayers with dependent children under the age of 17.

The increases in the child tax credit and marriage tax penalty relief measures are scheduled to sunset (expire) in 2011. The provisions may be extended or modified, however. As a result, it is likely that Congress will revisit the issue soon.

This report, originally written by Gregg A. Esenwein, now retired, will be updated as new data become available or as events warrant.

The major structural components of the income tax code which influence the income levels at which households become subject to federal income tax include the standard deduction, the personal exemption, the child tax credit, and the earned income tax credit (EITC). Each of these items increases the income level at which an individual or family incurs an out-of-pocket federal income tax liability.[1]

For instance, consider the case of a married couple with one dependent child under the age of 17. In 2009, the standard deduction for a married couple filing a joint return is $11,400, each personal exemption is worth $3,650, and the child tax credit is $1,000. This family would reach the basic income tax threshold (the point at which they have an actual out-of-pocket tax payment) for their filing status and family size at an income level of $22,350 (standard deduction of $11,400 plus three personal exemptions of $3,650 each).

Income over $22,350 would be subject to tax, but the child tax credit would offset the first $1,000 of this couple's income tax liability. At this taxable income level the marginal tax rate is 10%. That means that the child tax credit shields an additional $10,000 of income ($1,000 divided by 10%).

At this point, the EITC would come into play. The maximum EITC for 2009 for families with one child is $3,043. The credit phases out for families filing joint returns with incomes above $19,540, until it reaches zero for families whose incomes exceed $38,583. The income tax threshold for the family in this example will be the point at which the EITC is just enough to offset any pre-EITC income tax liability, so that the net tax liability of the family is zero. In the case of a couple with one dependent child filing a joint return the income level, in 2009, will be $36,184. At this income level, the family's income tax liability before EITC would be $383 and the family's EITC would also be $383. The two would offset each other, and the family would not have any net income tax liability.

The federal income tax thresholds for singles, joint returns, and head of households for select years between 1996 and 2009 are shown in **Table 1**. The table does not incorporate the effects of one-time tax rebates authorized by Economic Stimulus Act of 2008 (P.L. 110-185). Such rebates would have increased the thresholds further.

The data in **Table 1** show that the biggest increases in income tax thresholds, in both dollar and percentage terms, over the 1996 to 2009 period occurred for households who had dependent children under the age of 17. For example, married couples with children experienced increases in their income tax thresholds ranging from 82% for married couples with one child to 154% for married couples with four children. The increase in the income tax thresholds for head of households between 1996 and 2009 ranged from 70% for households with one child to 135% for households with four children.

The increases in income tax thresholds for single individuals and married couples without children were more moderate than those experienced by households with children. Tax thresholds

[1] The child and dependent care tax credit might also influence a household's federal income tax threshold, but it is not addressed in this report because it is not widely used by households at the lowest end of the income spectrum.

for single individuals only increased by 47% between 1996 and 2009, while tax thresholds for married couples with no children increased by 59%.

Table 1. Federal Income Tax Thresholds: Select Years, 1996 to 2009

	1996	2000	2004	2006	2007	2008	2009
Single Individuals							
Eligible for EITC	$7,547	$8,276	$9,484	$10,045	$10,416	$10,656	$11,124
Not eligible for EITC	$6,550	$7,200	$7,950	$8,450	$8,750	$8,950	$9,350
Married Couples							
No Children	$11,800	$12,950	$15,900	$16,900	$17,500	$17,900	$18,700
One Child	$19,883	$23,380	$30,435	$32,537	$33,572	$34,841	$36,184
Two Children	$23,672	$28,683	$40,200	$41,867	$42,850	$43,583	$44,900
Three Children	$24,732	$31,350	$49,967	$51,833	$52,917	$53,750	$55,217
Four Children	$25,793	$37,483	$59,733	$61,800	$62,983	$63,917	$65,533
Head of Households							
One Child	$18,260	$21,589	$26,988	$28,321	$29,276	$29,873	$31,026
Two Children	$22,277	$27,143	$33,939	$35,524	$36,674	$37,400	$38,765
Three Children	$23,336	$29,695	$42,953	$44,333	$45,183	$45,817	$46,933
Four Children	$24,400	$33,783	$52,713	$54,300	$55,250	$55,983	$57,250

Source: Calculations by CRS.

Notes: Assumes all children qualify for the child tax credit. Does not incorporate the effects of one-time tax rebates authorized by Economic Stimulus Act of 2008.

Income tax thresholds change over time because of two factors. First, they change because of the annual inflation adjustments to personal exemptions, standard deductions, tax rate brackets, and the EITC. Second, they change because of legislative changes to the tax system.

The relatively large changes in the tax thresholds for households with children can be traced to three main legislative changes that occurred over the 1996 to 2009 time period. These changes included establishment and subsequent increases in the child tax credit, an increase in the size of the standard deduction for joint returns, and an increase in the width of the 15% tax bracket for joint returns.[2]

The Taxpayer Relief Act of 1997 established the child tax credit. Initially, the credit was set at $500 for each qualifying child under the age of 17. Additional legislative changes under the Economic Tax Relief and Reconciliation Act of 2001 increased the child tax credit to $1,000. The

[2] For more information on the child tax credit and changes to the tax parameters for joint returns, see CRS Report RL34715, *The Child Tax Credit*, by (name redacted), and CRS Report RL34425, *Expiration and Extension of the Individual Income Tax Cuts Enacted in 2001 Through 2008*, by (name redacted).

2001 Act also increased the width of the 15% tax bracket and increased the standard deduction for joint returns. Although these changes were originally scheduled to be phased in over a number of years, subsequent legislation in 2003 and 2004 accelerated implementation and made these provisions effective in full through 2010.

The end result of these legislative actions has been a significant increase in the income tax thresholds for households with children. Economic theory does not provide an answer to the question of how the costs of child rearing should be accounted for under an income tax. However, one principle of tax fairness or equity accepted by many is that households at the low end of the income spectrum, especially those near the poverty threshold, should not be subject to the federal income tax. It has been argued that given the precarious financial position of these households, they should not be compelled to pay federal income tax, an action that would further reduce their level of subsistence.

The Tax Reform Act of 1986 explicitly cited this principle of eliminating income tax burdens for families with incomes near the poverty level as the reason for increasing the dollar amounts of standard deductions and personal exemptions. This act increased the value of personal exemptions and raised the standard deductions for joint returns and head of households such that, in combination with the EITC, the income tax thresholds for these taxpayers would be above their respective poverty thresholds.

Given this principle, one can compare income tax thresholds to poverty thresholds to see if this equity goal has been achieved over time. **Table 2** shows the poverty thresholds for singles and households with children for 1996 and 2007, the latest year poverty threshold data are available.[3]

Comparison of the data in these two tables reveals several trends. First, the income tax threshold for single individuals was below their respective poverty threshold in both 1996 and 2007. The difference became smaller for singles eligible for EITC, but it remained significant for those not eligible. There are many qualifications for EITC. As an example, childless adults 65 years and older are not eligible.[4]

On the other hand, the tax threshold for married couples without children exceeded their respective poverty thresholds in both 1996 and 2007. In addition, the amount by which their tax threshold exceeded their poverty threshold increased over the period. In 1996, the tax threshold for married couples without children exceeded their poverty threshold by about 12%, but by 2007 the difference had increased to 26%.

A more significant trend, however, occurred for families with children. In 1996, the federal income tax thresholds for families with children exceeded their respective poverty thresholds by relatively comfortable margins. By 2007, these margins had increased substantially, especially for

[3] 2007 represents the most recent poverty threshold data available. The 2008 poverty guidelines—the other version of the federal poverty measure, issued by the Department of Health and Human Services for administrative purposes—are approximately equal to the Census Bureau poverty thresholds for calendar year 2007.

[4] For more information on the earned income tax credit, see CRS Report RL31768, *The Earned Income Tax Credit (EITC): An Overview*, by (name redacted)

larger families. For example, in 1996, the income tax threshold for a married couple with four children was $25,793, while the poverty threshold for this same size/type family was $20,965. So the tax threshold was about 23% higher than the poverty threshold. By 2007, the income tax threshold for this family had increased to $62,983, while the 2007 poverty threshold had only increased to $27,705. In this instance, the income tax threshold increased to 227% of the poverty threshold. The income tax thresholds for head of households show similarly large increases relative to their corresponding poverty levels.

Table 2. Poverty Thresholds: 1996 and 2007

	1996	2007
Single Individual	$8,163	$10,787
Two Adults		
-No children	$10,507	$13,884
-One child	$12,629	$16,689
-Two children	$15,911	$21,027
-Three children	$18,725	$24,744
-Four children	$20,965	$27,705
One Adult		
-One child	$10,815	$14,291
-Two children	$12,641	$16,705
-Three children	$15,967	$21,100
-Four children	$18,438	$24,366

Source: U.S. Census Bureau.

As these tables demonstrate, with the exception of single taxpayers, the equity principle of exempting poverty level households from income taxation has been achieved over time. In addition, however, there have been significant increases in the tax thresholds for families, especially the ones with children.

These changes in the relationship between income tax and poverty thresholds for households with children can be attributed primarily to the introduction and subsequent increases in the child tax credit and to the measures addressing marriage tax penalty. In fact, the child tax credit represents a departure from past policy practices because it is not designed primarily as a means of differentiating between families of different size at or near the poverty threshold, but rather is designed to provide general tax reductions to middle and upper income taxpayers with dependent children under the age of 17.

The recent increases in the child tax credit and marriage tax penalty relief are scheduled to sunset (expire) in 2011. As a result, it is likely that Congress will revisit these issues soon.

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