

**DESCRIPTION OF THE
“ENCOURAGING WORK AND
SUPPORTING MARRIAGE ACT OF 2002”**

Scheduled for a Markup
By the
HOUSE COMMITTEE ON WAYS AND MEANS
on May 2, 2002

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION



April 30, 2002
JCX-32-02

CONTENTS

| | <u>Page</u> |
|--|-------------|
| INTRODUCTION | 1 |
| A. Acceleration of the Basic Standard Deduction Marriage Penalty Relief..... | 2 |
| B. Modification of the Work Opportunity Tax Credit and Welfare-To-Work Tax Credit..... | 4 |

INTRODUCTION

The House Committee on Ways and Means has scheduled a markup of the (“Encouraging Work and Supporting Marriage Act of 2002”). This document¹, prepared by the staff of the Joint Committee on Taxation, provides a description of the (“Encouraging Work and Supporting Marriage Act of 2002”).

¹ This document may be cited as follows: Joint Committee on Taxation, *Description of the “Encouraging Work and Supporting Marriage Act of 2002”* (JCX-32-02), April 30, 2002.

A. Acceleration of the Basic Standard Deduction Marriage Penalty Relief

Present Law

Marriage penalty

A married couple generally is treated as one tax unit that must pay tax on the couple's total taxable income. Although married couples may elect to file separate returns, the rate schedules and other provisions are structured so that filing separate returns usually results in a higher tax than filing a joint return.

A "marriage penalty" exists when the combined tax liability of a married couple filing a joint return is greater than the sum of the tax liabilities of each individual computed as if they were not married. A "marriage bonus" exists when the combined tax liability of a married couple filing a joint return is less than the sum of the tax liabilities of each individual computed as if they were not married.

Basic standard deduction

Taxpayers who do not itemize deductions may choose the basic standard deduction (and additional standard deductions, if applicable),² which is subtracted from adjusted gross income ("AGI") in arriving at taxable income. The size of the basic standard deduction varies according to filing status and is adjusted annually for inflation. For 2002, the basic standard deduction amount for single filers is 60 percent of the basic standard deduction amount for married couples filing joint returns. Thus, two unmarried individuals have standard deductions the sum of which exceeds the standard deduction for a married couple filing a joint return.

Present law provides that the basic standard deduction for a married couple filing a joint return will be increased to twice the basic standard deduction for an unmarried individual filing a single return. This increase in the basic standard deduction is phased-in over five years beginning in 2005 and will be fully phased-in for 2009 and thereafter. Table 1, below, shows the standard deduction for married couples filing a joint return as a percentage of the standard deduction for single individuals.

² Additional standard deductions are allowed with respect to any individual who is elderly (age 65 or over) or blind.

**Table 1 – Phase-In of the Increase of the Basic Standard Deduction
for Married Couples Filing Joint Returns**

| Calendar Year | Standard Deduction for Joint Returns as Percentage of Standard Deduction for Single Returns |
|----------------------|--|
| 2002 - 2004 | 167% |
| 2005 | 174% |
| 2006 | 184% |
| 2007 | 187% |
| 2008 | 190% |
| 2009 and later | 200% |

Description of Proposal

The proposal would accelerate the increase of the basic standard deduction for married couples filing joint returns. Table 2, below, shows the standard deduction for married couples filing a joint return as a percentage of the standard deduction for single individuals during the phase-in period as modified by the proposal.

**Table 2 – Phase-In of the Increase of the Basic Standard Deduction
for Married Couples Filing Joint Returns**

| Calendar Year | Standard Deduction for Joint Returns as Percentage of Standard Deduction for Single Returns |
|----------------------|--|
| 2002 | 167% |
| 2003-2004 | 170% |
| 2005 | 174% |
| 2006 | 184% |
| 2007 | 187% |
| 2008 | 190% |
| 2009 and later | 200% |

Effective Date

The provision would be effective for taxable years beginning after December 31, 2002.

B. Modification of the Work Opportunity Tax Credit and Welfare-To-Work Tax Credit

Present Law

Work opportunity tax credit

Targeted groups eligible for the credit

The work opportunity tax credit is available on an elective basis for employers hiring individuals from one or more of eight targeted groups. The eight targeted groups are: (1) certain families eligible to receive benefits under the Temporary Assistance for Needy Families Program; (2) high-risk youth; (3) qualified ex-felons; (4) vocational rehabilitation referrals; (5) qualified summer youth employees; (6) qualified veterans; (7) families receiving food stamps; and (8) persons receiving certain Supplemental Security Income (SSI) benefits.

A qualified ex-felon is an individual certified as: (1) having been convicted of a felony under State or Federal law; (2) being a member of an economically disadvantaged family; and (3) having a hiring date within one year of release from prison or conviction.

Food stamp recipients are individuals who have attained age 18 but have not attained age 25 that are certified as being a member of a family either currently or recently receiving assistance under an eligible food stamp program.

Qualified wages

Generally, qualified wages are defined as cash wages paid by the employer to a member of a targeted group. The employer's deduction for wages is reduced by the amount of the credit.

Calculation of the credit

The credit equals 40 percent (25 percent for employment of less than 400 hours) of qualified first-year wages. Generally, qualified first-year wages are qualified wages (not in excess of \$6,000) attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer. Therefore, the maximum credit per employee is \$2,400 (40 percent of the first \$6,000 of qualified first-year wages). With respect to qualified summer youth employees, the maximum credit is \$1,200 (40 percent of the first \$3,000 of qualified first-year wages).

Minimum employment period

No credit is allowed for qualified wages paid to employees who work less than 120 hours in the first year of employment.

Coordination of the work opportunity tax credit and the welfare-to-work tax credit

An employer cannot claim the work opportunity tax credit with respect to wages of any employee on which the employer claims the welfare-to-work tax credit.

Other rules

The work opportunity tax credit is not allowed for wages paid to a relative or dependent of the taxpayer. Similarly, wages paid to replacement workers during a strike or lockout are not eligible for the work opportunity tax credit. Wages paid to any employee during any period for which the employer received on-the-job training program payments with respect to that employee are not eligible for the work opportunity tax credit. The work opportunity tax credit generally is not allowed for wages paid to individuals who had previously been employed by the employer. In addition, many other technical rules apply.

Welfare-to-work tax credit

Targeted group eligible for the credit

The welfare-to-work tax credit is available on an elective basis to employers of qualified long-term family assistance recipients. Qualified long-term family assistance recipients are: (1) members of a family that has received TANF benefits for at least 18 consecutive months ending on the hiring date; (2) members of a family that has received such TANF benefits for a total of at least 18 months (whether or not consecutive) after August 5, 1997 (the date of enactment of the welfare-to-work tax credit) if the individual is hired within 2 years after the date that the 18-month total is reached; and (3) members of a family who are no longer eligible for TANF benefits because of either Federal or State time limits, if the individual is hired within 2 years after the Federal or State time limits made the family ineligible for TANF benefits.

Qualified wages

Qualified wages for purposes of the welfare-to-work tax credit are defined more broadly than the work opportunity tax credit. In contrast to the definition of wages for the work opportunity tax credit which includes only cash wages, the definition of wages for the welfare-to-work tax credit includes cash wages paid to an employee plus amounts paid by the employer for: (1) educational assistance excludable under a section 127 program; (2) certain health plan coverage for the employee that is excludable from income under sections 105 and 106 for income tax purposes, but not more than the applicable premium defined under section 4980B(f)(4); and (3) dependent care assistance excludable under section 129. The employer's deduction for wages is reduced by the amount of the credit.

Calculation of the credit

The welfare-to-work tax credit is available on an elective basis to employers of qualified long-term family assistance recipients during the first two years of employment. The maximum credit is 35 percent of the first \$10,000 of qualified first-year wages and 50 percent of the first \$10,000 of qualified second-year wages. Qualified first-year wages are defined as qualified wages (not in excess of \$10,000) attributable to service rendered by a member of the targeted group during the one-year period beginning with the day the individual began work for the employer. Qualified second-year wages are defined as qualified wages (not in excess of \$10,000) attributable to service rendered by a member of the targeted group during the one-year period beginning immediately after the first year of that individual's employment for the employer. The maximum credit is \$8,500 per qualified employee.

Minimum employment period

No credit is allowed for qualified wages paid to a member of the targeted group unless the member works at least 400 hours or 180 days in the first year of employment.

Coordination of the work opportunity tax credit and the welfare-to-work tax credit

An employer cannot claim the work opportunity tax credit with respect to wages of any employee on which the employer claims the welfare-to-work tax credit.

Other rules

The welfare-to-work tax credit incorporates directly or by reference many of the other rules contained on the work opportunity tax credit.

Description of Proposal

Combined credit

Targeted groups eligible for the combined credit

The proposal would combine the work opportunity and welfare to work tax credits. The combined credit would be available on an elective basis for employers hiring individuals from one or more of all nine targeted groups.

The proposal would also repeal the requirement that a qualified ex-felon be a member of an economically disadvantaged family for purposes of eligibility for the tax credit. Therefore a qualified ex-felon would be an individual certified as: (1) having been convicted of a felony under State or Federal law; and (2) having a hiring date within one year of release from prison or conviction.

The proposal would increase the age limit for qualified food stamp recipients by five years. Therefore a food stamp recipient would be an individual who has attained age 18 but has not attained age 30 who is certified as being a member of a family either currently or recently receiving assistance under an eligible food stamp program.

Qualified wages

Generally, qualified wages would be defined as cash wages paid by the employer to a member of a targeted group. Qualified first-year wages for the eight work opportunity tax credit categories, as modified by this proposal, would remain capped at \$6,000. No credit would be allowed for second-year wages. In the case of long-term family assistance recipients the cap of \$6,000 would be increased to \$10,000 for both qualified first-year wages and qualified second-year wages. The employer's deduction for wages would be reduced by the amount of the credit.

Calculation of the credit

First-year wages

The present-law work opportunity tax credit rules would be retained for the eight categories currently eligible for the work opportunity tax credit. Specifically, the credit would equal 40 percent (25 percent for employment of less than 400 hours) of qualified first-year wages. Generally, qualified first-year wages would be qualified wages (not in excess of \$6,000) attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer. Therefore, the maximum credit per employee for members of the eight work opportunity tax credit targeted groups would remain \$2,400 (40 percent of the first \$6,000 of qualified first-year wages). With respect to qualified summer youth employees, the maximum credit would remain \$1,200 (40 percent of the first \$3,000 of qualified first-year wages).

In the case of long-term family assistance recipients, the credit would equal 40 percent (25 percent for employment of less than 400 hours) of qualified first-year wages. Therefore the maximum credit would be \$4,000 (40 percent of the first \$10,000 of qualified first-year wages) with respect to long-term family assistance recipients.

Second year wages

In the case of long-term family assistance recipients the maximum credit would be 40 percent of the first \$10,000 of qualified second-year wages.

Minimum employment period

No credit would be allowed for qualified wages paid to employees who work less than 120 hours in the first year of employment.

Coordination of the work opportunity tax credit and the welfare-to-work tax credit

Coordination would no longer be necessary because the two credits would be combined.

Effective Date

The provision would be effective for wages paid or incurred with respect to qualified individuals who begin work for an employer after December 31, 2002.