R-133-1756

To: The Honorable Kristina D. Roegner
Ohio Senate

From: Philip A. Cummins, Senior Economist *PAC*

Date: August 22, 2019

Subject: Additional income tax paid by married couples because of Ohio's joint filing brackets

This memorandum is in response to an email from Joseph Baker asking for research on the additional income tax paid by married couples annually because of Ohio's joint filing brackets, the extent to which this additional tax is offset by the joint filer credit (JFC), the additional amount paid by a couple with the average household income, and the percent offset for this average couple by the JFC.

The revenue loss from the proposal of taxing separately the nonbusiness incomes of spouses who filed jointly for tax year (TY) 2016 is estimated to total $847 million on an all funds basis. The revenue loss from the JFC in current law is estimated at $194 million. If the JFC were to be repealed under the proposal, the net revenue loss would be $653 million. For a couple with the estimated median household income of Ohio married couples in 2017, $79,479, tax savings from the credit total $99, and tax savings if their nonbusiness income is taxed separately total $596, under assumptions listed below. If the JFC were repealed, the net tax savings would be about $497.

Concepts

For tax purposes, Ohio income of individuals is split into business and nonbusiness income. Tax before credits is calculated on the nonbusiness portion using the same tax table regardless of whether the taxpayer is married filing jointly; married filing separately; or single, head of household; or qualifying widow or widower. Ohio has no separate joint filing brackets. The table is progressive, with higher marginal tax rates in higher income brackets. Consequently, married taxpayers who can have their nonbusiness incomes taxed separately will tend to pay lower rates at the margin, hence have a lower tax liability. An exception is married taxpayers whose nonbusiness income is all or substantially all earned by one of the two spouses. Tax before credits for these latter taxpayers on their nonbusiness income could be higher if they file separately and in consequence are unable to use the full exemption amount of one of the spouses to reduce taxable income.

The JFC may be claimed by taxpayers who file a joint return, if each spouse has $500 or more of qualifying income, defined as any amount included in Ohio adjusted gross income (OAGI) other than interest, dividends and distributions, royalties, rent, and capital gains. Amounts deducted in computing OAGI, such as the business income deduction and Social Security benefits taxable at the federal level, are not qualifying income. For TY 2017, 59% of returns filed jointly claimed the JFC. The credit equals a percentage of the amount of tax owed after certain credits have been subtracted.[1] A provision of H.B. 166 of the 133rd General Assembly (the enacted budget) tied these percentages to modified adjusted gross income (MAGI) less exemptions, with MAGI defined as OAGI plus any business income deducted in computing OAGI. The percentages are shown in the following table.

MAGI Less Exemptions	Credit Percentage
$25,000 or less	20%
More than $25,000, not more than $50,000	15%
More than $50,000, not more than $75,000	10%
More than $75,000	5%

The JFC is capped at a maximum of $650 per return.

Tax before credits is calculated on the business portion of individuals' incomes in two different ways depending on filing status. Taxpayers who are married filing separately are allowed to deduct up to $125,000. All other taxpayers may deduct up to $250,000. On any business income over those amounts, tax before credits is figured at a 3% rate. Consequently, a married taxpayer with more than $125,000 in business income who can have his or her business income taxed jointly will tend to have a lower tax liability.

Please note that whether a married couple with both business and nonbusiness income will owe more or less tax by filing jointly or separately will depend on the specific amounts of that couple's business and nonbusiness income. Mr. Baker's questions appear to pertain only to taxation of nonbusiness income. In the analysis that follows, taxation of business income is held constant and only taxation of nonbusiness income is allowed to vary.

Some income of married taxpayers can readily be attributed to one or the other of the spouses, for example, income from employment. Other income is joint, such as receipts from financial instruments owned by both.

[1] The credits taken before the JFC are as specified in R.C. 5747.98 and include the retirement and senior citizen credits, the $20 per exemption credit, and other less commonly claimed credits.

Data

The analysis reported here was carried out on two samples, a sample of TY 2016 tax returns provided by the Department of Taxation[2] and a sample of Ohio households from the Census Bureau's American Community Survey (ACS).

The sample from the Department includes a limited number of line item entries from more than 140,000 returns, including nearly 90,000 filed jointly. The sample includes weights for converting sample values to population estimates. It does not show, for the joint returns, amounts of income earned by each of the two marriage partners, nor does it indicate how much of the business and nonbusiness income to attribute to each partner.

The ACS data used include incomes of Ohio married couples in the 12 months before the survey in 2017, the individual survey respondents' incomes, the incomes of their spouses, and weights with each set of sample values to use in estimating population values. Incomes of any other household members are excluded, as are data on households with an absent spouse. Values may be negative, indicating losses. Data generally are as reported by the survey respondents but are subject to maximums and minimums to prevent disclosure for high-income individuals in the sample or persons experiencing large losses.

The two samples are entirely separate, with no way to reliably link Department data on a specific taxpayer with ACS data on any specific household.

Analysis

The tax savings from the JFC in TY 2016 were about $195 million on an all funds basis. This is the calculated amount of additional tax liability if the JFC is set to zero for all 2016 joint filers, in a model built using the sample provided by the Department. This amount is somewhat less than the $199.4 million estimated for FY 2017 in the Tax Expenditure Report, which was on a GRF basis rather than all funds. Calculated tax savings from the JFC, using the tax rate table for 2019 in the recently enacted H.B. 166 and the 2016 sample data, totaled virtually the same amount, $194 million.

The 2017 ACS data indicate that the spouse with the higher income averaged about 75% of couples' combined incomes, and the spouse with the lower income averaged 25% of the total. These percentages, which relate to income from all sources, were used in combination with the taxpayer sample from the Department to generate a set of hypothetical nonbusiness income amounts for each spouse. As noted above, taxation of business income was held unchanged and not attributed to either spouse. The reduction in tax liabilities on the nonbusiness income, net of nonrefundable credits and calculated using the 2019 tax table, totals about $847 million on an all funds basis. The tax reduction due to the JFC totaled about 23% of this amount.

[2] Please note that the sample provided does not include identifying information about the taxpayers in the sample.

The finding regarding the tax savings from separate taxation of nonbusiness income of spouses is slightly larger than earlier results from this office and somewhat closer to estimates issued by the Department, both of which are cited in the fiscal note for H.B. 333 of the 132nd General Assembly, which also dealt with this subject.

Median income of the married couples in the 2017 ACS data is $79,479. If all of this income is assumed to be from nonbusiness sources, taxes due under current law as amended for TY 2019 by H.B. 166 total $1,888, assuming two exemptions at $2,100 each and no credits except the JFC. The JFC saves this couple $99; without the JFC, their tax bill would be $1,988. Alternatively, if one of the spouses earns 75% of the total amount and the other earns 25%, taxing the amounts separately implies a total tax bill of $1,391, a total savings of $596, or $497 in addition to the tax reduction resulting from the JFC. In this example, the full tax liability would fall on the higher-income spouse; the lower-income spouse would have zero tax liability. Also, under current law, neither spouse could claim the JFC if they filed separately.

Questions, additional information

If you have questions about this memorandum or want more information, please contact me at (614) 387-1687 or phil.cummins@lsc.ohio.gov.

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