The appropriate treatment of the family unit is a major issue in the design of an individual income tax system. Gravelle's paper begins by discussing the current state of family taxation, and how it has evolved over time. She argues persuasively that many of the important changes in the tax treatment of the family were not consequences of policy decisions focusing on families per se. Rather, they were incidental consequences of decisions that were made without much thought about the effects on the family. Gravelle then goes on to provide a useful discussion of alternative major approaches to family taxation, and to draw out the implications of each for such issues as whether credits or exemptions are more suitable measures for correcting for differences in family size.

One of the points that arises in the course of Gravelle's discussion is that it is difficult to deal with people who are part of the same consuming group but have no legal relationship with each other. In this context, Gravelle notes that "Taxation involves the application of laws which can recognize legal relationships but has difficulty in recognizing relationships which are not legal in nature." This assertion, with which I agree, implies that certain theoretically appealing solutions to the tax treatment of the family may be administratively impossible. However, I would be inclined to carry this line of reasoning farther than Gravelle--even in the presence of well-defined legal relationships, apparently quite simple changes in the tax treatment of the family may create difficult administrative problems. In this comment, I would like to discuss some examples of administrative problems that arise in taxing the family.

Let us begin with an issue that receives a lot of attention in Gravelle's paper and that is currently the subject of a lot of debate in Washington--the size of the dependency exemption. From an administrative viewpoint, hardly anything seems simpler than adjusting the size of the exemption. If every family were like the Cleaver's of "Leave It to Beaver," this would be so. But, in a world in which many households are headed by divorced or never married parents, complications can arise. Consider the following possible issues:

1. A parent who is not living with the child is providing some support for the child. Who gets to claim the exemption?
2. Suppose the child being taken care of is not a son or a daughter, but some other relationship is involved. Can the exemption be claimed nonetheless?
3. Just how old can a person be and still be considered a child? Should exceptions be made for full-time students who are above the cutoff? How many months a year is "full-time"?

All of these questions (and others) have to be answered in order to administer the exemption. The flow chart in Figure 6a.1 shows how these questions are answered under current law.

There may be a tendency, especially for economists, to dismiss all of these issues as a lot of irrelevant nit-picking. That tendency is dangerous. In the absence of precise definitions, it may be impossible to target relief at the families for whom it is desired. A closely related concern is abuse of the exemption. Any increase in the exemption, no matter how desirable from some policy perspective or another, will put increased pressure on the dependency rules. To the extent that increasing the exemption leads to abuse, the ultimate attractiveness of the increase is reduced. Unfortunately, we do not have good information about how much abuse of the exemptions takes place under current law, let alone under some hypothetical regime under which the payoff to abuse would be higher. However, there is some indirect evidence that in the past taxpayers were cognizant of the opportunities to exploit the dependency rules. After the Internal Revenue Service imposed a rule that each dependent be identified on the tax return by his or her social security number, the number of dependent exemptions fell by about seven million. Such episodes suggest that, if there are weaknesses in the system, they will be exploited.

The second issue to illustrate the importance of administrative issues is the Earned Income Tax Credit (EITC). In terms of Gravelle's taxonomy, the EITC is a type of "family assistance" because it uses credits rather than exemptions to distinguish among families of different sizes. About 13.8 million households are estimated to be eligible for the credit. Under 1991 law, eligible low-income workers may claim a refundable credit of up to 16.7 percent of the first $7,140 of earned income. (The rate is 17.3 percent for taxpayers with more than one qualifying child.) The EITC is phased out at a rate of 11.93 percent of earnings in excess of $11,250 (12.36 percent for taxpayers who have more than one qualifying child). As a consequence of changes enacted in 1990, there are two additional credits. First, a supplemental credit of 5 percent is available for qualifying children under the age of one year. Second, a supplemental credit of 6 percent is available to taxpayers who buy health insurance policies that include coverage for their qualifying children. (The credit cannot exceed the actual amount paid for health insurance coverage.)

As pointed out by Gravelle, under some conditions, a credit like the EITC is sensible tax policy for the family. Let us put aside the issue of whether the EITC is desirable in theory, and discuss its administrative aspects. How complicated is it for individuals to determine whether they are entitled to the credit, and, if so, how large a credit? The first step is to determine whether a child is "qualifying." Under current law, a child has to pass three tests to qualify: First is a relationship test—the child must be a son, daughter, adopted child, grandchild, step child, or foster child. Second is an age test—the child must be under age 19, or under age 24 and a full-time student, or any age and permanently and totally disabled. Third is a residency