

The President's Advisory Panel on
Federal Tax Reform

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**The Alternative Minimum Tax
Staff Presentation
July 20, 2005**

Alternative Minimum Tax

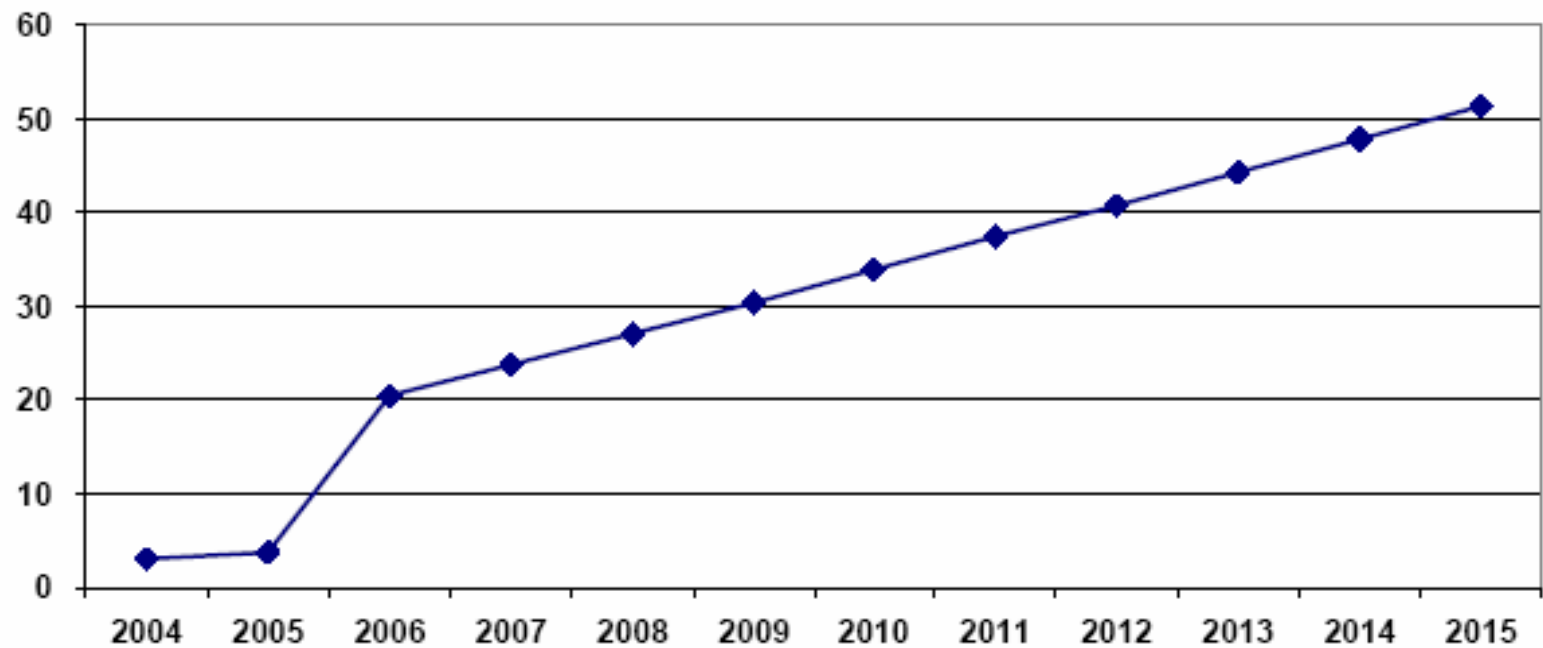
- History
 - First enacted in 1969 largely as an add-on tax. Intended to assure that a very small group of high-income individuals would pay at least some tax.
- AMT today
 - A second, parallel tax system that has its own exemptions, tax rates, tax credits and a definition of income that is broader than the regular income tax.
 - Calculated by adding back income and deductions that are excluded under the regular income tax.
 - Preferences include state and local tax deductions, interest on home equity loans, personal exemptions, the standard deduction, net operating losses, incentive stock options, and medical deductions
 - Taxpayers must pay tax on the amount of AMT income that exceeds the AMT exemption at rates of 26 percent and 28 percent. Taxpayers compare the amount of tax computed under the AMT with the tax due under the regular tax and pay whichever amount is higher.

Growth of Alternative Minimum Tax

- Growth of AMT
 - The AMT exemptions and tax rate brackets are not indexed for inflation, which causes more taxpayers to be subject to the AMT each year.
 - Lawmakers have enacted temporary fixes to the AMT to limit its reach but have not indexed the exemption and brackets for inflation.
- The AMT will affect **3.8 million** taxpayers this year.
- The AMT will affect **20.5 million** taxpayers in 2006.
 - These taxpayers will pay \$2,736 more in taxes because of the AMT.
- The AMT will affect **51.3 million** taxpayers in 2015
 - Roughly 45 percent of all taxpayers with income
- The AMT will increasingly affect middle-income taxpayers -- 13 percent of taxpayers with incomes between \$100,000 and \$200,000 will be subject to the AMT in 2005
 - By 2006, more than 75 percent of taxpayers in this income group will be subject to the AMT.
 - By 2015, 3/4 of taxpayers with income between \$50,000 and \$1 million will be subject to the AMT!

More and More Taxpayers Pay AMT

AMT Taxpayers (millions)



Note: Assumes EGTRRA and JGTRRA sunsets are repealed and the temporary AMT provisions are allowed to expire in 2005.

Source: U.S. Department of Treasury, Office of Tax Analysis

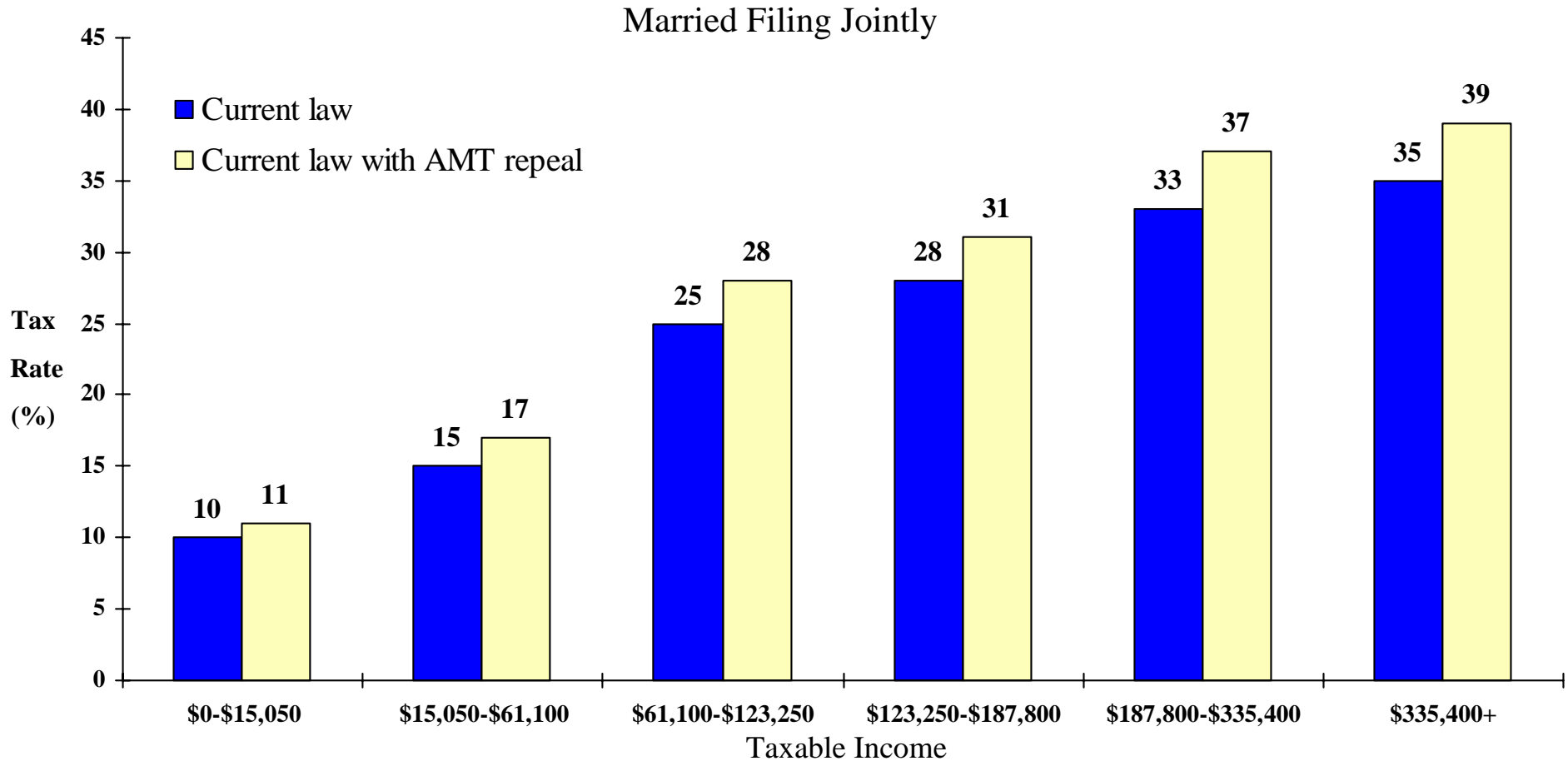
Who Pays the AMT

- Large families will be hit especially hard. Because the AMT does not allow personal exemptions, these families are more likely to be subject to the AMT.
- The AMT also has a marriage penalty – the exemption amount for married couples is only 37 percent larger than the amount for singles.
- In 2006, Treasury predicts that the percentage of married taxpayers in the \$100,000-\$200,000 range required to pay AMT will be:
 - Almost 100% of families with four children
 - More than 85% of families with three children
 - More than 2/3 of families with two children

AMT Tax Revenues

- Revenues raised by the AMT grow rapidly over the next ten years.
 - Revenues increase from \$15 billion in 2004 to \$210 billion by 2015 (11 percent of total individual income tax revenues!)
 - The Treasury Department estimates that repealing the AMT will cost \$1.2 trillion for FY 2006-2015
- The AMT collects this revenue by imposing a tax that is higher than the statutory regular income tax rates.

Tax Rate Schedule: Effect of AMT Repeal



Source: Department of the Treasury, Office of Tax Analysis

Note: Taxable income brackets are estimates for 2006.

The AMT: Complex, Unfair and Ineffective

- Complex
 - Having to comply with two parallel tax systems is complex and burdensome.
 - Taxpayers often are unaware that they are subject to the AMT and owe more tax until they sort through the complex interactions between the regular tax and the AMT.
- Unfair
 - Creates unpleasant surprises for families depending on family size, marital status, and deductions claimed.
- Ineffective
 - The AMT has failed to achieve its primary objective of ensuring that all taxpayers pay some amount of tax.
 - What began as a way to impart more equity into the system has developed into a burden for millions of middle-class Americans.