TECHNICAL EXPLANATION
OF H.R. 7005, THE
"ALTERNATIVE MINIMUM TAX RELIEF ACT OF 2008"

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of the
JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a technical explanation of H.R. 7005, the "Alternative Minimum Tax Relief Act of 2008."

[1] This document may be cited as follows: Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions of H.R. 7005, the "Alternative Minimum Tax Relief Act of 2008"* (JCX-71-08), September 24, 2008. This document can also be found on our website at www.jct.gov.

A. Extend Alternative Minimum Tax Relief for Individuals (secs. 2 and 3 of the bill and secs. 26 and 55 of the Code)

Present Law

Present law imposes an alternative minimum tax ("AMT") on individuals. The AMT is the amount by which the tentative minimum tax exceeds the regular income tax. An individual's tentative minimum tax is the sum of (1) 26 percent of so much of the taxable excess as does not exceed $175,000 ($87,500 in the case of a married individual filing a separate return) and (2) 28 percent of the remaining taxable excess. The taxable excess is so much of the alternative minimum taxable income ("AMTI") as exceeds the exemption amount. The maximum tax rates on net capital gain and dividends used in computing the regular tax are used in computing the tentative minimum tax. AMTI is the individual's taxable income adjusted to take account of specified preferences and adjustments.

The present exemption amount is: (1) $66,250 ($45,000 in taxable years beginning after 2007) in the case of married individuals filing a joint return and surviving spouses; (2) $44,350 ($33,750 in taxable years beginning after 2007) in the case of other unmarried individuals; (3) $33,125 ($22,500 in taxable years beginning after 2007) in the case of married individuals filing separate returns; and (4) $22,500 in the case of an estate or trust. The exemption amount is phased out by an amount equal to 25 percent of the amount by which the individual's AMTI exceeds (1) $150,000 in the case of married individuals filing a joint return and surviving spouses, (2) $112,500 in the case of other unmarried individuals, and (3) $75,000 in the case of married individuals filing separate returns or an estate or a trust. These amounts are not indexed for inflation.

Present law provides for certain nonrefundable personal tax credits (i.e., the dependent care credit, the credit for the elderly and disabled, the adoption credit, the child credit[2], the credit for interest on certain home mortgages, the HOPE Scholarship and Lifetime Learning credits, the credit for savers, the credit for certain nonbusiness energy property, the credit for residential energy efficient property, and the D.C. first-time homebuyer credit).

For taxable years beginning before 2008, the nonrefundable personal credits are allowed to the extent of the full amount of the individual's regular tax and alternative minimum tax.

For taxable years beginning after 2007, the nonrefundable personal credits (other than the adoption credit, child credit and saver's credit) are allowed only to the extent that the individual's regular income tax liability exceeds the individual's tentative minimum tax, determined without regard to the minimum tax foreign tax credit. The adoption credit, child credit, and saver's credit are allowed to the full extent of the individual's regular tax and alternative minimum tax.[3]

[2] The child credit may be refundable in whole or in part to a taxpayer.

[3] The rule applicable to the adoption credit and child credit is subject to the EGTRRA sunset.

Explanation of Provision

The provision provides that the individual AMT exemption amount for taxable years beginning in 2008 is (1) $69,950, in the case of married individuals filing a joint return and surviving spouses; (2) $46,200 in the case of other unmarried individuals; and (3) $34,975 in the case of married individuals filing separate returns.

For taxable years beginning in 2008, the bill allows individuals to offset their entire regular tax liability and alternative minimum tax liability by the nonrefundable personal credits.

Effective Date

The provision is effective for taxable years beginning in 2008.

B. Increase in AMT Refundable Credit Amount for Individuals With Long-Term Unused Credits for Prior Year Minimum Tax Liability, Etc. (sec. 4 of the bill and sec. 53 of the Code)

Present Law

In general

Present law imposes an alternative minimum tax on an individual taxpayer to the extent the taxpayer's tentative minimum tax liability exceeds his or her regular income tax liability. An individual's tentative minimum tax is the sum of (1) 26 percent of so much of the taxable excess as does not exceed $175,000 ($87,500 in the case of a married individual filing a separate return) and (2) 28 percent of the remaining taxable excess. The taxable excess is the amount by which the alternative minimum taxable income exceeds an exemption amount.

An individual's AMTI is the taxpayer's taxable income increased by certain preference items and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items.

The individual AMT attributable to deferral adjustments generates a minimum tax credit that is allowable to the extent the regular tax (reduced by other nonrefundable credits) exceeds the tentative minimum tax in a future taxable year. Unused minimum tax credits are carried forward indefinitely.

AMT treatment of incentive stock options

One of the adjustments in computing AMTI is the tax treatment of the exercise of an incentive stock option. An incentive stock option is an option granted by a corporation in connection with an individual's employment, so long as the option meets certain specified requirements.[4]

Under the regular tax, the exercise of an incentive stock option is tax-free if the stock is not disposed of within one year of exercise of the option or within two years of the grant of the option.[5] When the stock is sold, the individual's long-term capital gain or loss is determined using the amount paid for the stock as the cost basis. If the holding period requirements are not satisfied, the individual generally takes into account at the exercise of the option an amount of ordinary income equal to the excess of the fair market value of the stock on the date of exercise over the amount paid for the stock. The cost basis of the stock is increased by the amount taken into account.[6]

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[4] Sec. 422.

[5] Sec. 421.

[6] If the stock is sold at a loss before the required holding periods are met, the amount taken into account may not exceed the amount realized on the sale over the adjusted basis of the stock. If the stock

Under the individual alternative minimum tax, the exercise of an incentive stock option is treated as the exercise of an option other than an incentive stock option. Under this treatment, generally the individual takes into account as ordinary income for purposes of computing AMTI the excess of the fair market value of the stock at the date of exercise over the amount paid for the stock.[7] When the stock is later sold, for purposes of computing capital gain or loss for purposes of AMTI, the adjusted basis of the stock includes the amount taken into account as AMTI.

The adjustment relating to incentive stock options is a deferral adjustment and therefore generates an AMT credit in the year the stock is sold.[8]

Allowance of long-term unused credits

Under present law, an individual's minimum tax credit allowable for any taxable year beginning after December 31, 2006, and beginning before January 1, 2013, is not less than the "AMT refundable credit amount." The "AMT refundable credit amount" is the amount (not in excess of the long-term unused minimum tax credit) equal to the greatest of (1) $5,000, (2) 20 percent of the long-term unused minimum tax credit for the taxable year, or (3) the amount (if any) of the AMT refundable credit amount for the preceding taxable year before any reduction by reason of the reduction for adjusted gross income described below. The long-term unused minimum tax credit for any taxable year means the portion of the minimum tax credit attributable to the adjusted net minimum tax for taxable years before the 3rd taxable year immediately preceding the taxable year (assuming the credits are used on a first-in, first-out basis).

In the case of an individual whose adjusted gross income for a taxable year exceeds the threshold amount (within the meaning of section 151(d)(3)(C)), the AMT refundable credit amount is reduced by the applicable percentage (within the meaning of section 151(d)(3)(B)). The additional credit allowable by reason of this provision is refundable.

Explanation of Provision

The provision generally allows the long-term unused minimum tax credit to be claimed over a two-year period (rather than five years) and eliminates the AGI phase-out.

The provision provides that any underpayment of tax outstanding on the date of enactment which is attributable to the application of the minimum tax adjustment for incentive

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is sold after the taxable year in which the option was exercised but before the required holding periods are met, the required inclusion is made in the year the stock is sold.

[7] If the stock is sold in the same taxable year the option is exercised, no adjustment in computing AMTI is required.

[8] If the stock is sold for less than the amount paid for the stock, the loss may not be allowed in full in computing AMTI by reason of the $3,000 limit on the deductibility of net capital losses. Thus, the excess of the regular tax over the tentative minimum tax may not reflect the full amount of the loss.

stock options (including any interest or penalty relating thereto) is abated. No tax which is abated is taken into account in determining the minimum tax credit.

The provision provides that the AMT refundable credit amount and the AMT credit for each of the first two taxable years beginning after December 31, 2007, are increased by one-half of the amount of any interest and penalty paid before the date of enactment on account of the application of the minimum adjustment for incentive stock options.

Effective Date

The provision generally applies to taxable years beginning after December 31, 2007.

The provision relating to the abatement of tax, interest, and penalties takes effect on date of enactment.