

## COMMENT

# THE INDIVIDUAL ALTERNATIVE MINIMUM TAX: IS IT TOUCHING PEOPLE THAT IT SHOULDN'T BE?\*

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Over the next ten years, many taxpayers from the middle income brackets will become very aware that their accountant or accounting software, many times, will be filing two separate tax returns for their customers. Already, there is chatter among

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\* 2004 J.D. Candidate from the University of Houston Law Center. This Paper was selected as the recipient of the Chamberlain, Hrdlicka, White, Williams & Martin Writing Award for Distinguished Paper in Taxation.

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them of what is to come.<sup>1</sup> Taxpayers are familiar with the Form 1040, but they will also become very aware of the Form 6251: the Individual Alternative Minimum Tax Return. In 2000, only 1.3% of the 100 million U.S. taxpayers had to send payment to the IRS for their Alternative Minimum Tax (“AMT”) liability.<sup>2</sup> In 2010, times will have changed: 35.6 million taxpayers will have to write checks for their AMT liability.<sup>3</sup> Additionally, this shadow tax system will surreptitiously recollect in excess of the savings earned from the 2001 Bush tax cuts, rendering them mostly ineffective.<sup>4</sup>

The chief problem behind the effects of the AMT over the coming ten years, though, is that it will seep into the middle class, forcing the class to bear the main burden of this complicated shadow tax, even though Congress designed the AMT to focus on the rich who were able to avoid income tax liability through various deductions and credits.<sup>5</sup> Complicating the matter, the Treasury has come to depend upon the bankroll that the AMT contributes to its coffers.<sup>6</sup> In a time in which budget surpluses are now a distant memory, this dependence upon the AMT shoves Congress into a corner when it comes to major reform of AMT.<sup>7</sup>

The real effect of the AMT’s infiltration into the middle class is that the American income tax system will become less of a progressive tax, placing more of a burden upon the middle class.<sup>8</sup> Rather, the income tax rates will look more like a slanted bell curve, causing the tax rates to peak at the income range of \$200,000 to \$500,000 and then drop drastically thereafter.<sup>9</sup> This effect leaves the “super-rich’s”<sup>10</sup> pocketbooks unscathed by the

1. See, e.g., Karen Hube, *Silent Killer: The Alternative Minimum Tax is Slaying Taxpayers. Will You be Next?*, BARRON’S, Feb. 11, 2002, at 1–3.

2. See ROBERT REBELEIN & JERRY TEMPALSKI, WHO PAYS THE INDIVIDUAL AMT?, tbl. 1 (U.S. Treasury Dep’t, OTA Paper 87, 2000).

3. LEONARD E. BURMAN ET AL., THE INDIVIDUAL AMT: PROBLEMS AND POTENTIAL SOLUTIONS, tbl. 3 (Urban-Brookings Tax Policy Ctr., Discussion Paper No. 5, 2002).

4. See *id.* at fig. 7.

5. See Martin A. Sullivan, *Economic Analysis: AMT Changes Everything*, 2002 TAX NOTES TODAY 186–7 (Sept. 23, 2002).

6. See *id.*

7. See *id.*

8. See BURMAN ET AL., *supra* note 3, at 41–42.

9. See *id.*

10. That is, as termed by Martin Sullivan, those with an annual income greater than \$500,000. See generally Sullivan, *supra* note 5 (“The upper-middle class will be subject to higher effective tax rates than the super rich.”); see also Martin A. Sullivan, *Economic Analysis—AMT, Estate Tax Time Bombs Set Stage for Some High-Class Warfare*, 2002 TAX NOTES TODAY 176–6 (Sept. 9, 2002) (“In addition to the usual controversy about the relative tax burdens on the rich and poor, there is a second type of class warfare lurking on the horizon: the rich vs. the super-rich.”).

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growing tax burden and produces much unfairness between taxpayers, much like what was perceived when the AMT was created.<sup>11</sup> Congress created the AMT in 1969 to alleviate the public's perception that the rich escaped paying their taxes.<sup>12</sup> Most likely, once taxpayers become aware of the disparity and unfairness of the present tax system, we will come to a similar crossroads in which there will be a public outcry forcing Congress to act.

This comment will first explain the origins and intent of the AMT because this tax system was primarily created upon the principle of equity and not upon the creation of a needed revenue source.<sup>13</sup> Secondly, this comment will discuss how the AMT mechanically works alongside the regular tax system. Thirdly, it will discuss the problem with the AMT that is on the horizon by analyzing the statistical projections and pinning down the reasons for the AMT's infiltration into the middle class. Fourthly, it will discuss the existing criticisms and how the problem with the AMT emboldens these criticisms. Lastly, it will explain the potential solutions to the AMT dilemma and the problems with each solution because none of them come without costs.<sup>14</sup>

## I. OVERVIEW OF THE AMT

### A. *Origins, Intent & Evolution*

In 1969, Secretary of Treasury Joseph Barr gave testimony to the Joint Economic Committee that in 1967, 155 individual taxpayers with adjusted gross incomes over \$200,000 paid no federal income tax.<sup>15</sup> Additionally, the Joint Economic Committee Report cited that in 1964, over 1,100 individual returns reporting AGI in excess of \$200,000 reported average tax liability that equaled only 22% of economic income.<sup>16</sup> This tax burden was much lower than that of most working Americans,

11. See Sullivan, *supra* note 5.

12. See Stewart S. Karlinsky, *A Report on Reforming the Alternative Minimum Tax System*, 12 AM. J. TAX POL'Y 139, 140-141 (1995).

13. See BURMAN ET AL., *supra* note 3, at 7. This particular fact is important in this author's opinion when it comes to the analysis of the AMT's current situation because the chief reason to keep the AMT and the complications that it brings are for equitable reasons only.

14. See *id.* at 37-45 (examining the costs and benefits of various solutions to the AMT tax dilemma).

15. Hearings on the 1969 Econ. Report of the President Before The Joint Econ. Comm., 91<sup>st</sup> Cong. 8-44 (1969) (statement of Secretary of Treasury Joseph W. Barr).

16. H.R. REP. NO. 91-413 (1969), *reprinted in* 1969 U.S.C.A.N. 1645, 1725.

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and therefore, caught the attention of the Congress and public.<sup>17</sup> Legislators received more letters that same year expressing disgust over this unfairness than they did in protest of the Vietnam War, which was a fairly large amount in itself.<sup>18</sup> Congress believed this fact posed an immediate problem because these perceived abuses eroded taxpayer compliance, which is the nightmare of a self-assessment tax system.<sup>19</sup> Scholars determined if high-income taxpayers excessively exploited these special incentives offered by tax deductions and credits, a mechanism should be devised to curb their availability.<sup>20</sup> In 1970, Congress reasoned that:

[t]he prior treatment imposed no limits on the amount of income which an individual . . . could exclude from tax as a result of various tax preferences. As a result, there were large variations in the tax burdens placed on individuals . . . with similar economic incomes . . . . [I]ndividuals . . . [who] received the bulk of their income from such sources as capital gains or were in a position to benefit from . . . tax-preferred activities tended to pay relatively low rates of tax. In fact many individuals with high incomes who could benefit from these provisions paid lower effective rates of tax than many individuals with modest incomes. In extreme cases, individuals enjoyed large economic incomes without paying any tax at all.<sup>21</sup>

Based upon this reasoning, Congress ultimately enacted an "add-on" tax of ten percent, which was levied on tax preferences after the first \$30,000 in income and a deduction for regular tax payments.<sup>22</sup>

Since then, the alternative minimum tax regime has been wrought with constant changes due to dissatisfaction with its effects.<sup>23</sup> In 1974, the Treasury determined that 244 high-income

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17. See Karlinsky, *supra* note 12, at 141.

18. See BURMAN ET AL., *supra* note 3, at 6.

19. See Karlinsky, *supra* note 12, at 141.

20. See *id.*

21. JOINT COMM. ON TAXATION, 91ST CONG. GEN. EXPLANATION OF THE TAX REFORM ACT OF 1969 (Comm. Print 1970).

22. Tax Reform Act of 1969, Pub. L. No. 91-172, § 56, 83 Stat. 487, 580 (Codified as amended in scattered sections of 26 U.S.C.).

23. See, e.g., Tax Reform Act of 1976, Pub. L. No. 94-455, sec. 301, § 56, 90 Stat.

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taxpayers still had no tax liability.<sup>24</sup> Increasingly, Congress had become concerned with excessive tax benefits derived from the use of accelerated depreciation on real estate and leased personal property, percentage depletion, qualified stock options (now called ISOs), and the reduced rate for capital gains.<sup>25</sup> In response, the Tax Reform Act of 1976 amended the exemption of the add-on tax to only the first \$10,000 or half of regular tax liabilities.<sup>26</sup> Furthermore, Congress raised the tax rate to 15%, added certain itemized deductions with preference to their abovementioned concerns, and required the Treasury to annually report on high-income taxpayers without a federal income tax liability.<sup>27</sup>

A few years later, Congress enacted the Revenue Act of 1978<sup>28</sup> to respond to a concern that the add-on tax discouraged capital formation.<sup>29</sup> This Act created the modern Alternative Minimum Tax.<sup>30</sup> The AMT operated like a parallel tax, and not as a separate tax like the prior add-on tax.<sup>31</sup> The AMT allowed an exemption of the first \$20,000 and had graduated rates of 10%, 20%, and 25%.<sup>32</sup> Taxpayers potentially could become susceptible to all three taxes: the income tax, the add-on tax, and the alternative minimum tax,<sup>33</sup> but the Revenue Act of 1978 greatly reduced the add-on tax's revenues.<sup>34</sup>

In 1982, Congress enacted the Tax Equity and Fiscal Responsibility Act (TEFRA).<sup>35</sup> This act completely removed the add-on tax created in 1969 and moved all of its preferences under the AMT scheme.<sup>36</sup> Additionally, it made research and

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1520, 1549-54 (codified as amended in scattered sections of 26 U.S.C.); Revenue Act of 1978, Pub. L. No. 95-600, sec. 421, § 55, 92 Stat. 2763, 2871 (codified as amended in scattered sections of 26 U.S.C.); Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, sec. 201, § 55, 96 Stat. 324, 411 (codified as amended in scattered sections of 26 U.S.C.).

24. BURMAN ET AL., *supra* note 3, at 16.

25. See Karlinsky, *supra* note 12, at 142-43.

26. See Tax Reform Act of 1976, sec. 301 § 56(a).

27. See *id.*

28. Pub. L. No. 95-600, 92 Stat. 2763 (codified as amended in scattered sections of 26 U.S.C.).

29. See BURMAN ET AL., *supra* note 3, at 16.

30. See Revenue Act of 1978, sec. 421, § 55.

31. BURMAN ET AL., *supra* note 3, at 16.

32. See Revenue Act of 1978, sec. 421, § 55(a)(1).

33. See *id.*, sec. 421, § 55(a)(2).

34. BURMAN ET AL., *supra* note 3, at 16.

35. Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, sec. 201, § 55, 96 Stat. 324 (codified as amended in scattered sections of 26 U.S.C.).

36. See Tax Equity and Fiscal Responsibility Act, sec. 201, § 55; see also BURMAN ET AL., *supra* note 3, at 17.

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development expenses a preference under the revised AMT.<sup>37</sup> The Act did allow certain itemized deductions such as qualified home mortgage interest, casualty losses, charitable gifts, and limited medical deductions.<sup>38</sup> The standard exemption rose to the first \$40,000, and the tax rate for all incomes was 20%.<sup>39</sup> Scholars have said that even though the 1983 AMT system was the “harbinger of the current system,” it did not incorporate the parallel world concept, and, thus, did not require different basis adjustments for assets or a minimum credit.<sup>40</sup> Therefore, its application was “far simpler and more administrable than the current system.”<sup>41</sup>

Then Congress enacted the Tax Reform Act (TRA) of 1986,<sup>42</sup> which substantially changed the entire tax system.<sup>43</sup> This time, Congress incorporated the parallel world concept, which increased the differences between the calculations of taxable income for the AMT and the regular tax system.<sup>44</sup> Each system allows different deductions from the other as well as different limitations on various deductions such as charitable contributions and requiring the computation of a different adjusted basis in assets.<sup>45</sup> Furthermore, this bill introduced the creation of an exemption phase-out, limitations on the extent to which net operating losses and foreign tax credits could reduce AMT, and an AMT credit in the regular income tax for AMT liability caused by deferral items.<sup>46</sup> Subsequent to the 1986 Act,

37. See Tax Equity and Fiscal Responsibility Act, sec. 201(?), § 57(a).

38. See *id.*, sec. 201(a), § 55.

39. See *id.*, sec. 201(a), § 55(a)(1),(f).

40. Karlinksy, *supra* note 12, at 144.

41. *Id.*

42. Pub. L. No. 99-514, 100 Stat. 2085 (codified as amended in scattered sections of 26 U.S.C.).

43. See BURMAN ET AL., *supra* note 3, at 17.

44. See *id.*

45. See Karlinksy, *supra* note 12, at 147–48. For an example of the confusion that the parallel world concept creates for taxpayers, see *Allen v. Comm’r*, 118 T.C. 1 (2002). In this case, the court held that even though the taxpayer ultimately did not owe any income tax under the AMT, the taxpayer’s AMT income affected the extent to which the taxpayer could take advantage of the Targeted Jobs Credit under the regular income tax scheme. *Id.* at 2. I.R.C. § 38(c)(1) controls this limitation:

(c) Limitation based on amount of tax

(1) In general.— The [Targeted Jobs] credit allowed under subsection (a) for any taxable year shall not exceed the excess (if any) of the taxpayer’s net income tax over the greater of—

(A) the tentative minimum tax for the taxable year, or

(B) 25 percent of so much of the taxpayer’s net regular tax liability as exceeds \$25,000.

I.R.C. § 38(c)(1) (2001).

46. See BURMAN ET AL., *supra* note 3, at 17.

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participation and revenues in the AMT system fell to pre-1982 levels.<sup>47</sup>

Unlike the regular tax system, one thing that the 1986 Act did not do to the AMT was index it for inflation.<sup>48</sup> During the nineties, the lack of indexing was not a concern, and, consequently, under various pieces of legislation in the nineties, Congress actually increased the AMT tax rates along with the regular income tax rates.<sup>49</sup> In 1999, the AMT accounted only for 1% of returns and revenues.<sup>50</sup>

Then, Congress passed the Bush Administration's Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001.<sup>51</sup> This Act lowered the tax rates in the regular income tax scheme until the law expires in 2010, but did not make corresponding reductions in the AMT rates.<sup>52</sup> However, the EGTRRA did temporarily increase the AMT exemptions and allow adoption, child, earned income and IRA credits to be used despite the limitations made by the AMT.<sup>53</sup>

*B. The Technicalities: How the AMT Works Alongside the Regular Income Tax*

I.R.C. §§ 55–59 set out the rules of the AMT.<sup>54</sup> A taxpayer can be subject to the AMT either directly by having an AMT liability or indirectly by the AMT placing limitations on credits available under the regular income tax scheme under the parallel tax concept.<sup>55</sup> Section 55(a) imposes a tax on the excess of the tentative minimum tax greater than the regular tax of that year.<sup>56</sup>

47. *Id.*

48. Currently, the Code still does not allow for indexing of the AMT for inflation. Compare I.R.C. § 55(b) (2000) (no indexing created for AMT tax brackets), and I.R.C. § 55(d) (2000) (no indexing created for the AMT exemptions), with I.R.C. § 1(f) (2000) (creating an adjustment in the regular income tax scheme based upon the cost-of-living), and I.R.C. § 63(c)(4) (2000) (creating an adjustment of the regular income tax's standard deduction).

49. See BURMAN ET AL., *supra* note 3, at 17–18; Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, 104 Stat. 1388; Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, 107 Stat. 312; Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788.

50. See BURMAN ET AL., *supra* note 3, at 18.

51. Pub. L. No. 107-16, 115 Stat. 38 (codified as amended in scattered sections of 26 U.S.C.).

52. Compare *id.*, sec. 101, § 1, with *id.*, sec. 701, §55.

53. See *id.*, sec. 701, §55.

54. I.R.C. §§ 55–59 (2000).

55. See REBELEIN & TEMPALSKI, *supra* note 2, at 6. For an example of the indirect effects the AMT can cause for a taxpayer, see *Allen*, 118 T.C. at 1.

56. I.R.C. § 55(a) (2000).

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The tentative minimum tax is the tax liability calculated using AMT income, the AMT exemption, the AMT tax rates, and allowable AMT credits.<sup>57</sup> Section 55(d) allows an exemption amount of \$45,000 for joint returns and \$33,750 for single individuals and heads-of-household to be subtracted from the AMT income before the tax rates are applied.<sup>58</sup> However, phase-outs of the exemptions begin for each of these groups at the alternative minimum taxable income of \$150,000 and \$112,500, respectively, at a rate of \$0.25 per \$1 of AMT income.<sup>59</sup> Whatever AMT income, that does not exceed \$175,000, is taxed at 26% and, above \$175,000, at 28%.<sup>60</sup>

Income under the AMT is the taxable income under the regular income tax in addition to the various preferences and adjustments unique to the AMT.<sup>61</sup> AMT income can never be lesser than regular taxable income.<sup>62</sup> The preferences and adjustments can be categorized into two groups: deferral and exemption provisions.<sup>63</sup> To comply with exemption provisions is not too complicated since they involve simply adding back the exemptions that were subtracted for the regular income tax.<sup>64</sup> Exemption provisions have the most pervasive effect on the majority of taxpayers.<sup>65</sup> As of 2000, there were twenty-eight AMT preferences and adjustments, which causes AMT income to be greater than regular taxable income.<sup>66</sup> Three exemption provisions accounted for approximately 97% of total AMT preferences: (1) state and local tax deductions<sup>67</sup> at 54%, (2) personal exemptions<sup>68</sup> at 23%, and (3) miscellaneous deductions above the 2-percent floor<sup>69</sup> at 20%.<sup>70</sup> To comply with deferral

57. REBELEIN & TEMPALSKI, *supra* note 2, at 5–6.

58. See I.R.C. § 55(d)(1) (2000).

59. See *id.* § 55(d)(3). Taxpayers in the phase-out range of the AMT exemption will effectively pay a 32.5% rate if in the 26% bracket and a 35% rate if in the 28% bracket. REBELEIN & TEMPALSKI, *supra* note 2, at 6 n.11.

60. See I.R.C. § 55(b)(1)(A).

61. See REBELEIN & TEMPALSKI, *supra* note 2, at 6.

62. See I.R.C. § 56.

63. See *id.* §§ 57–58; BURMAN ET AL., *supra* note 3, at 11.

64. See I.R.C. § 57.

65. See BURMAN ET AL., *supra* note 3, at 11 (“Exemption preferences broaden the AMT tax base, and include disallowances of personal exemptions, the standard deduction, and itemized deductions for miscellaneous expenses and taxes.”).

66. See REBELEIN & TEMPALSKI, *supra* note 2, at 6.

67. See generally I.R.C. § 56(b)(1)(A)(ii) (disallowing deductions for various state and local taxes).

68. See generally I.R.C. § 56(b)(1)(E) (disallowing deduction for the standard exemption and personal exemption).

69. See generally I.R.C. § 56(b)(1)(A)(i) (disallowing any miscellaneous itemized deductions). Among miscellaneous deductions are attorney’s fees, about which much noise has been made in courts recently. See generally *Alexander v. IRS*, 72 F.3d 938 (1st

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provisions is much more difficult because there are more of them, and they are more complex because they involve recalculating income and costs using different schedules from the regular income tax and keeping separate sets of books for regular tax and AMT.<sup>71</sup> Deferral provisions change the timing of income recognition and deductions, accelerating income and postponing deductions.<sup>72</sup> The most common deferral provisions that arise are those that relate to incentive stock options (ISOs),<sup>73</sup> depreciation of personal property,<sup>74</sup> and passive activity losses.<sup>75</sup> However, taxpayers do not fall susceptible to deferral provisions as frequently as exemption provisions, and if they do, the taxpayer tends to have a high income.<sup>76</sup>

An example is most likely necessary in order to understand the complications and the differences in the calculation of the AMT from the regular income tax. Assume:

in 2002 a married couple filing a joint return had taxable income of \$71,000, based on \$205,000 of gross income and the following deductions allowable in computing regular tax liability: (1) ACRS deductions of \$50,000 under § 168 on property placed in service in 1994, which is reduced to \$30,000 when computed under § 56(a)(1); (2) \$40,000 of mine exploration expenses

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Cir. 1995) (treating taxpayer's legal fee as a miscellaneous itemized deduction subject to the application of the AMT). *But see* *Srivastava v. Comm'r*, 220 F.3d 353 (5th Cir. 2000) (holding that attorney's fees were not includable in gross income and, therefore, not susceptible to the AMT). Attorney's fees are deductible under the regular tax system, but are not allowed under the AMT. *Id.*

70. See REBELEIN & TEMPALSKI, *supra* note 2, at 6.

71. See BURMAN ET AL., *supra* note 3, at 12.

72. See I.R.C. § 58.

73. See I.R.C. § 56(b)(3) (modifying the rules otherwise governing the treatment of stock options for purposes determining the amount of income subject to the AMT). Under the regular income tax, exercising an ISO generates no tax liability, but under the AMT, exercising an ISO generates taxable income equal to the difference between the sale price and the option price if the stock is not sold within the same year. See 26 I.R.C. §§ 421-422. The effect that the AMT has had upon ISO participants, particularly out of the technology sector, has caused quite a stir of debate recently. See generally Warren Rojas, *Outdated AMT Claims First Victims of the 21<sup>st</sup> Century*, 2001 TAX NOTES TODAY 83-1 (Apr. 30, 2001); see also Francine J. Lipman, *Incentive Stock Options and the Alternative Minimum Tax: The Worst of Times*, 39 HARV. J. ON LEGIS. 337, 340 (2002).

74. Compare I.R.C. § 56(a)(1) (application of 150 percent declining balance depreciation method for most personal property put into commission after 1986 under the AMT), and I.R.C. § 168(g) (application of the straight line depreciation method for most personal property put into commission after 1998 under the AMT), with I.R.C. § 168(b) (application of the faster 200 percent declining balance depreciation method for most personal property other than 15-year or 20-year property under the regular income tax).

75. See I.R.C. § 58(b) (disallowing passive activity losses).

76. See BURMAN ET AL., *supra* note 3, at 12.

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under § 616; (3) \$20,000 of home mortgage interest deductible under § 163(h)(3), only \$5,000 of which was attributable to a purchase-money loan; (4) \$20,000 of investment expenses deductible under § 212 (after taking into account the § 67 limitation); and (5) two \$2,000 personal exemptions allowed under § 151. In addition, the taxpayers (1) received \$15,000 of interest on a qualified mortgage bond described under § 141 that is exempt from tax under § 103; (2) exercised an incentive stock option at a price \$75,000 below the fair market value of the stock purchased pursuant to the option; and (3) deducted mine development expenses of \$60,000 in the previous year. Their regular tax liability for 2002 is \$14,142. Their AMT income is computed as follows:

1. Taxable income	\$71,000
2. Adjustments	
a. Excess of regular tax depreciation over AMT depreciation (\$50,000 -\$30,000)	\$20,000
b. 2002 mine development expenses (90% X \$40,000)	\$36,000
c. 2001 mine development expenses (10% X \$60,000)	(\$6,000)
d. Home mortgage interest	\$15,000
e. Miscellaneous deductions (\$ 212 expenses)	\$20,000
f. Incentive Stock Option	\$75,000
g. Personal exemptions (2)	<u>\$ 4,000</u>
h. TOTAL	\$164,000
3. Tax preference items	
a. Private activity bond tax exempt interest	\$5,000
b. TOTAL	\$5,000
4. AMTI	
(sum of lines 1, 2h, and 3b)	\$240,000

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5. Less: Exemption amount (reflects \$22,500 reduction under § 55(d)(3))	<u>(\$26,500)</u>
6. Excess of AMTI over exemption amount (line 4 minus line 5)	\$213,500
7. Tentative AMT (26% of \$175,000 and 28% of \$38,500)	\$56,540
8. Regular tax	<u>\$14,142</u>
9. AMT (line 7 minus line 8)	\$42,398 <sup>77</sup>

Thus, these taxpayers would not only be responsible for the \$14,142 in taxes under the regular income tax, but they would be responsible for the AMT tax of \$42,398.<sup>78</sup> Their total liability to the IRS for the year would be \$56,540. Regardless of the fact that AMT tax rates are considerably lower than regular income tax rates,<sup>79</sup> a taxpayer can expect to pay the IRS quite a greater sum with the AMT in its present state because of all the preferences and adjustments added to the tax base.

## II. ATTACK OF THE AMT

### A. *My, How You've Grown*

In 2001, AMT, **either** by form 6251 liability or lost credits under the regular income tax, affected only 1.8 million taxpayers, which was less than 2% of all taxpayers with a positive tax liability and less than 1.5% of all returns.<sup>80</sup> Notwithstanding EGTRRA's increase in the AMT exemption, economic simulations

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77. BORIS I. BITTKER & MARTIN J. MCMAHON, JR., *FEDERAL INCOME TAXATION OF INDIVIDUALS* ¶ 45.3[4] (2d ed. 2002). This example obviously is not representative of the majority of taxpayers—especially the middle class, but is intended more so to demonstrate the striking differences in which the AMT deals with certain events. While it may not be representative of the middle class, it is likely that middle class taxpayers share at least one or more items with the couple in this example.

78. *See* I.R.C. § 56.

79. *Compare* I.R.C. § 55(b)(1)(A) (imposing tax rates of 26% on amounts up to \$175,000 and 28% as exceeds \$175,000), *with* I.R.C. § 1(a) (setting forth tax rate structure for married couples filing jointly under which, if the taxpayers make over \$140,000 but less than \$250,000 in income, their marginal rate is already 35%, and 38.6% if over \$250,000 in 2002).

80. BURMAN ET AL., *supra* note 3, at 19.

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project that AMT participation will triple between 2001 and 2004 to 5.5 million.<sup>81</sup> The expiration of the higher exemption in 2004 will cause AMT participation to rise to 20 million by 2006, and then to more than 35 million by 2010.<sup>82</sup> Additionally, if inflation occurs at a rate of 3.5% rather than 2.5% (which is what all of these calculations are based), AMT participation in 2010 would increase by 20% to 42 million while AMT revenues would rise over 40% to \$199 billion.<sup>83</sup>

AMT revenue correspondingly follows a similar pattern.<sup>84</sup> In 2001, AMT only offered the Treasury \$11 billion in revenues, which is 1.2% of all income tax receipts.<sup>85</sup> By 2004, AMT revenue will rise to \$21 billion, \$61 billion in 2006, and \$141 billion in 2010.<sup>86</sup> By 2010, the AMT will account for 10% of all income tax revenue.<sup>87</sup> This increase in the AMT revenues in proportion to other income tax revenues demonstrates the dependency that the Treasury will begin to develop upon the AMT.<sup>88</sup> Therefore, this reliance demonstrates the increasing difficulty for Congress to reform or repeal the AMT.<sup>89</sup> By 2008, it actually would cost less to repeal the regular income tax by setting all rates to zero and abolishing all credits than to repeal the AMT,<sup>90</sup> giving fervor to some scholars' premonitions that the AMT would replace the regular income tax.<sup>91</sup>

The Bush administration's EGTRRA has tremendously exacerbated the AMT problem.<sup>92</sup> If Congress had indexed the AMT when the regular income tax was indexed, the AMT would have only affected 300,000 taxpayers in 2002.<sup>93</sup> Roughly only the same number of taxpayers would face the AMT in 2010 if

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81. *Id.*

82. *Id.*

83. *Id.* at 20. Of course, for the coming years, economists fear deflation rather than inflation. *Of Debt, Deflation and Denial*, ECONOMIST, Oct. 12, 2002, at 69–70. This, of course, would lessen the AMT's rise to predominance.

84. BURMAN ET AL., *supra* note 3, at 19.

85. *Id.*

86. *Id.*

87. *Id.*

88. *See id.* at 19–20.

89. *See id.* (arguing that the actual costs of AMT repeal would actually be greater to the extent that repeal or reform induces additional tax sheltering).

90. *Id.* at 20.

91. *See* Michael J. Graetz, *The 1982 Minimum Tax Amendments as a First Step in the Transition to a 'Flat-Rate' Tax*, 56 S. CAL. L. REV. 527 (1983).

92. *See* Sullivan, *supra* note 5; *see also* Al Davis, *Candidate Bush's Tax Cut Plan*, 2000 TAX NOTES TODAY 6–72, (Jan. 10, 2000); Alan J. Auerbach et al., *The Budget Outlook and Options for Fiscal Policy*, 2002 TAX NOTES TODAY 112–44 (June 10, 2002).

93. BURMAN ET AL., *supra* note 3, at 21.

Congress did not enact EGTRRA.<sup>94</sup> Despite the non-existence of AMT indexing, if Congress had not made EGTRRA law, 18 million taxpayers would have an AMT liability by 2010. Therefore, EGTRRA nearly doubles the number of AMT taxpayers in 2010 from 17.9 million to 35.6 million.<sup>95</sup> Similarly, AMT revenue triples under EGTRRA from \$47 billion to \$141 billion.<sup>96</sup> After 2010, AMT trends rely upon whether EGTRRA sunsets as the law presently requires<sup>97</sup> or gets extended as the President and Republican-controlled Congress continuously advocate.<sup>98</sup> If Congress extends EGTRRA, AMT will affect 37% of all taxpayers in 2012<sup>99</sup>—a far cry from the “less than 1.5%” of all returns in 2001.<sup>100</sup>

### B. *What is to Come*

While the AMT is gaining its predominance over the regular income tax, new trends of its tax burden's distribution are emerging, demonstrating that the AMT no longer is a tax system to prevent rich taxpayers from escaping the regular income tax.<sup>101</sup> The most prominent trend is the sharp rise in AMT participation in the middle class.<sup>102</sup> In 2002, AMT will affect 1.4% of taxpayers with income between \$50,000 and \$75,000 and 3% with income between \$75,000 and \$100,000.<sup>103</sup> By 2010, these percentages jump to 43% and 79%, respectively.<sup>104</sup> In addition, approximately 95% of taxpayers with income between \$100,000 and \$500,000 will face AMT. The amount of taxpayers with income above \$500,000 that are susceptible to AMT will be substantially lower than the amount of those with income between \$100,000 and \$500,000 by 2010: only 45%.<sup>105</sup>

Another new trend is that AMT also places a greater tax

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94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.* at 19.

101. *See id.* at 19–21.

102. *Id.*

103. *Id.*

104. *Id.*

105. *See BURMAN ET AL., supra* note 3, at tbl.4. The reason for this disparity is the top tax rate in the AMT is below that in the regular income tax. *Id.* at 22. The highest AMT tax bracket is 28%, while the highest regular tax bracket in 2010 is 35%. *Compare* I.R.C. § 55(b)(1)(A)(i)(II) (2000), *with* I.R.C. § 1(i)(2) (2000). Most high-income taxpayers will usually face a higher regular income tax than their tentative alternative minimum tax, making them less likely to face AMT. REBELEIN & TEMPALSKI, *supra* note 2, at 10.

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burden on large families compared to small ones since AMT disallows exemptions.<sup>106</sup> More than 50% of taxpayers with three or more children will face the AMT in 2010 relative to 46% of those with two children and 16% of those with no children.<sup>107</sup> However, many filers with children do not pay income tax.<sup>108</sup> Therefore, among those with three or more children that do have a tax liability, 94% will face AMT.<sup>109</sup> Eighty percent of those who have two children and do have tax liability will face AMT.<sup>110</sup>

Additionally, taxpayers in states with high income and property taxes currently are more likely to face the AMT than those from states with low taxes because the AMT does not allow a deduction for state and local taxes, causing horizontal inequity in between the states.<sup>111</sup> In 2000, taxpayers in low-tax states accounted for 18% of all AMT taxpayers, whereas taxpayers in middle-tax states accounted for 24%, and those in high-tax states accounted for 58%.<sup>112</sup> In 2010, it is predicted that taxpayers in high-tax states will bear 45% of the AMT burden.<sup>113</sup> The importance of this trend will decline over the years, though, because the lack of indexation and EGTRRA will cause more taxpayers to face AMT notwithstanding the lack of a deduction for state and local taxes.<sup>114</sup> Therefore, should Congress reform the AMT, perhaps this inequity between the states will remain a significant problem.<sup>115</sup> State and local tax deductions do account for 54% of the exemption provisions that make taxpayers susceptible to AMT.<sup>116</sup>

Because the AMT does not allow taxpayers to take advantage of standard deductions or the various exemptions that are allowed under the regular income tax, many taxpayers who use these deductions or exemptions will be more likely to face AMT.<sup>117</sup> In 2010, taxpayers who file under the head of household

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106. BURMAN ET AL., *supra* note 3, at 22.

107. *Id.*

108. *Id.*

109. *Id.*

110. *Id.*

111. *Id.* at 23. *See also* I.R.C. § 56(b)(1)(A)(ii) (2000) (disallowing a deduction for state and local taxes for purposes of AMT).

112. REBELEIN & TEMPALSKI, *supra* note 2, at 15. To determine which category a state belonged, Rebelein and Tempalski divided the fifty states into three tiers (low, middle, and high) based upon the average state and local taxes assessed. *See id.* at 14.

113. *Id.* at 15.

114. BURMAN ET AL., *supra* note 3, at 23; *see also* REBELEIN & TEMPALSKI, *supra* note 2, at 15–16.

115. *See* REBELEIN & TEMPALSKI, *supra* note 2, at 15.

116. *Id.* at 6.

117. *See* BURMAN ET AL., *supra* note 3, at 23.

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status will be have a 10% chance of incurring AMT liability, as compared to 3% for singles.<sup>118</sup> A greater problem, though, is that many taxpayers use more than one exemption or standard deduction.<sup>119</sup> Claiming multiple combinations of exemptions and standard deductions can cause even greater susceptibility to AMT.<sup>120</sup> For example, many heads of household claim one or more dependent exemptions as well.<sup>121</sup> “[I]n 2010, among couples who file jointly and have two children, 71% of those with AGI between \$50,000 and \$75,000 and fully 97% of those with AGI between \$75,000 and \$100,000 will be on the AMT.”<sup>122</sup> Furthermore, approximately “99% of couples with two children and with income between \$100,000 and \$500,000 will face the AMT.”<sup>123</sup>

All of these trends culminate to create a less progressive AMT.<sup>124</sup> Currently, the AMT is more progressive than the regular income tax.<sup>125</sup> In 2002, the Treasury expects to collect roughly an equal proportion of revenue from the AMT as from the regular income tax for taxpayers with an income above \$1 million and from taxpayers with incomes between \$100,000 and \$200,000: approximately 21%.<sup>126</sup> From taxpayers with incomes between \$200,000 and \$1 million, the AMT collects 51% of its revenues and the regular income tax collects 25%; from taxpayers with incomes between \$15,000 and \$100,000, the AMT collects 6% of its revenues whereas the regular income tax collects 33%.<sup>127</sup> This greater progressivity makes sense because the AMT’s intention is to reduce vertical inequities that occur when higher-income taxpayers are able to escape a greater proportion of their tax burden than those with lower incomes.<sup>128</sup> As the AMT expands over the next ten years, the progressivity will wane.<sup>129</sup> In 2010, from taxpayers with income over \$1 million, the AMT will receive 5% of its revenues while the regular income tax will

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118. *Id.*

119. *See id.*

120. *See id.*

121. *Id.*

122. *Id.*

123. *Id.*

124. *See id.* at tbl. 5 (compare the percent of tax liability in 2010 of the AMT to the total income tax).

125. *See id.* (compare the percent of tax liability in 2002 of the AMT to the total income tax).

126. *See id.*

127. *See id.*

128. *See supra* text accompanying note 21.

129. *See BURMAN ET AL., supra* note 3, at tbl. 5 (compare the percent of tax liability in 2010 of the AMT and the total income tax to the same in 2002).

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collect 18.5%.<sup>130</sup> From taxpayers with incomes between \$200,000 and \$1 million, AMT will collect 32% while the regular income tax will collect 27%.<sup>131</sup> From taxpayers with incomes between \$100,000 and \$200,000, it will collect 38% while the regular income tax collects 27%.<sup>132</sup> From taxpayers with incomes between \$15,000 and \$100,000, it will collect 24% whereas the regular income tax will collect 30%.<sup>133</sup>

These statistics show that 54% of AMT taxpayers will have incomes of \$100,000 or below.<sup>134</sup> Additionally, 25% of AMT's revenues will come from the same economic group.<sup>135</sup> These taxpayers will be subject to the AMT, obviously, not because of tax sheltering, but for reasons related to filing status, number of children, and state and local taxes paid.<sup>136</sup> Moreover, once the AMT is in full bloom by 2010, its progressivity will peak at the income bracket of \$100,000 to \$200,000.<sup>137</sup> Thirty-six percent of this economic group will pay 38% of the AMT.<sup>138</sup>

Then, the AMT returns of taxpayers with incomes above \$200,000 and the revenues from those groups will drop dramatically.<sup>139</sup> Only 8.6% of taxpayers with incomes between

130. See *id.*(table partly provided below).

Y2010 (thousands of 2001 \$)	Less than \$0	\$0-\$15	\$15- \$30	\$30- \$50	\$50- \$75	\$75- \$100	\$100- \$200	\$200- \$500	\$500- \$1,000	More than \$1,000
% of AMT Returns	0.0	0.0	0.4	6.2	22.0	25.1	36.7	8.6	0.8	0.2
% of All Returns	0.7	28.3	21.6	17.3	12.3	7.7	9.4	2.1	0.4	0.2
% of AMT Liability	0.2	0.0	0.1	1.4	8.1	14.7	**38.2	28.5	3.9	5.0
% of All Income Tax	0.0	-1.9	1.0	7.0	10.5	11.1	**27.1	18.6	8.0	18.5

\*\* Indicates the apex of progressivity.

131. See *id.*

132. See *id.*

133. See *id.*

134. See *id.*

135. See *id.*

136. See REBELEIN & TEMPALSKI, *supra* note 2, at 6.

137. See BURMAN ET AL., *supra* note 3, at tbl. 5.

138. See *id.*

139. See *id.*

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\$200,000 and \$500,000 will fall susceptible to AMT while still financing 28.5% of AMT revenue.<sup>140</sup> Less than 1% (0.8%) of taxpayers with incomes between \$500,000 and \$1,000,000 will pay AMT while the AMT will receive 3.9% of its revenues from this group.<sup>141</sup> Finally, only 0.4% of taxpayers with incomes above \$1,000,000 will face AMT, and AMT will receive 5% of its revenues from this group.<sup>142</sup>

An additional point to make here is that in 2010, when the AMT has fully shifted onto the middle class, the burden of the tax system, as a whole, will shift to taxpayers with incomes between \$100,000 and \$500,000.<sup>143</sup> The Urban-Brookings Tax Policy Center considered the effects of repealing the AMT, but adjusting the regular income tax to compensate for the lost AMT revenues and to maintain the same distribution among income brackets.<sup>144</sup> This study provides a clear view of the burden of the tax system as a whole despite the AMT's indirect manner.<sup>145</sup> Currently, as it stands, the regular income tax brackets in 2010 are 10%, 15%, 25%, 28%, 33%, and 35%.<sup>146</sup> After repeal of the AMT, the regular income tax rates would have to adjust to 10.7%, 16.3%, 29.2%, 33.8%, 43%, and 33.2%.<sup>147</sup> Thus, the progressivity of the tax system will appear more like a bell curve slanted to the right.<sup>148</sup> This progressiveness-cut-short will leave taxpayers with incomes above \$500,000 with less of the burden in relation to their income, while taxpayers with incomes between \$100,000 and \$500,000 would bear the brunt of the nation's tax burden.<sup>149</sup> Although this tax structure is not fully progressive, there is tax literature that justifies similar structures in which the tax system is not completely progressive for the sake of revenue maximization.<sup>150</sup> These arguments rely upon the fact that taxable income is much more elastic for higher income earners than for lower income earners.<sup>151</sup> Therefore, they argue

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140. *See id.*

141. *See id.*

142. *See id.*

143. *See Sullivan, supra* note 5.

144. *See BURMAN ET AL., supra* note 3, at 41–42.

145. *See Sullivan, supra* note 5.

146. BURMAN ET AL., *supra* note 3, at fig.7.

147. *Id.*

148. *See id.*

149. *See Sullivan, supra* note 5.

150. *See BURMAN ET AL., supra* note 3, at 42.

151. *See, e.g., JON GRUBER & EMMANUEL SAEZ, THE ELASTICITY OF TAXABLE INCOME: EVIDENCE AND IMPLICATIONS*, at 5 (Nat'l Bureau of Econ. Research, Working Paper No. 7512, 2000). According to the authors:

We estimate small income effects of tax changes on reported income,

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that there is an optimum tax rate for higher income earners that maximizes tax revenues while minimizing the incentive to seek tax shelters that high tax rates encourage.<sup>152</sup>

Nonetheless, these arguments do not discount the fact that when the number of taxpayers with incomes below \$100,000 is more likely to face AMT than those with incomes above \$500,000,<sup>153</sup> the AMT legitimately earns the classification of “middle-class” tax, as it has been called.<sup>154</sup> If the AMT becomes a middle-class tax, no longer will the AMT serve its intended purpose of removing vertical inequities that exist in the Tax Code, benefiting the “individuals . . . [who] received the bulk of their income from such sources as capital gains or were in a position to benefit from . . . tax-preferred activities tended to pay relatively low rates of tax.”<sup>155</sup>

### III. WHY WE SHOULD NOT LET THE AMT NEAR THE MIDDLE CLASS

There are issues with allowing the AMT to become a middle-class tax. There were already many criticisms of the role of the AMT in the U.S. tax system even during the years that it arguably has served its intended purpose.<sup>156</sup> These criticisms become more heightened, though, once the AMT has become a middle-class tax.<sup>157</sup>

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implying that the compensated and uncompensated elasticity of taxable income are very similar. We also find that this response is driven largely by the behavior of high income taxpayers; the elasticity of taxable income for those with incomes above \$100,000 is 0.57, while it is less than one-third for lower income groups. High income taxpayers who itemize appear to be particularly responsive on tax changes. Finally, our estimates suggest that the optimal system for most redistributive preferences consists of a large demogrant that is rapidly taxed away for low income taxpayers, with lower marginal rates at higher income levels.

*Id.*

152. *See id.*

153. *See* BURMAN ET AL., *supra* note 3, at tbl. 5.

154. Sullivan, *supra* note 5; *see also* BURMAN ET AL., *supra* note 3, at 28.

155. JOINT COMM. ON TAXATION, 107<sup>TH</sup> CONG., STUDY OF THE OVERALL STATE OF THE FEDERAL TAX SYSTEM AND RECOMMENDATIONS FOR SIMPLIFICATION, PURSUANT TO SECTION 8022(3)(B) OF THE INTERNAL REVENUE CODE OF 1986, vol. II, at 2 (Comm. Print 2001).

156. *See, e.g.*, Daniel Shaviro, *Perception, Reality and Strategy: The New Alternative Minimum Tax*, 66 TAXES 91 (1988).

157. *See* BURMAN ET AL., *supra* note 3, at 24–37.

2004] *THE INDIVIDUAL ALTERNATIVE MINIMUM TAX* 277A. *Complexity*

Complexity is a major issue to a voluntary tax system.<sup>158</sup> Too much complexity causes such effects as (1) “decreased levels of voluntary compliance,” (2) “increased costs for taxpayers,” (3) “reduced perceptions of fairness in the Federal tax system,” and (4) “increased difficulties in the administration of tax laws.”<sup>159</sup> Decreased levels of voluntary compliance derive from “inadvertent errors or intentional behavior by taxpayers.”<sup>160</sup> In regards to the increased costs for taxpayers, taxpayers have “increased their use of tax return preparers, computer software for tax return preparation, and IRS taxpayer assistance over the last ten years.”<sup>161</sup> The reduced perceptions of fairness of the tax system derives from “disparate treatment of similarly situated taxpayers,” “opportunities for manipulation of the tax laws by taxpayers who are willing and able to obtain professional advice,” and “disillusion[ment of] taxpayers to Federal tax policy because of the uncertainty created by complex laws.”<sup>162</sup> In regards to administration of tax laws, complex laws increase the difficulty “for the IRS to explain the law to taxpayers in a concise and understandable manner in forms, instructions, publications, and other guidance.”<sup>163</sup> Moreover, “the IRS is more likely to make mistakes in the assistance of taxpayers and in the application of the law.”<sup>164</sup>

The AMT is probably one of the most complex aspects of the Code.<sup>165</sup> The National Association of Enrolled Agents took a

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158. See JOINT COMM. ON TAXATION, 107<sup>TH</sup> CONG., *supra* note 155, at 6 (considering the effects of complexity on voluntary compliance).

159. *Id.*

160. *Id.*

161. *Id.*

162. *Id.* The perfect example is the taxpayer who is placed on the AMT by denial of the state and local income tax deduction. See Daniel Shaviro, *Tax Simplification and the Alternative Minimum Tax*, 2001 TAX NOTES TODAY 103–108, ¶ 17 (May 28, 2001). The taxpayer will perceive this particular deduction as not really a deduction after all; they will perceive it as a deduction “only to the extent needed to reduce one’s regular tax liability from what it would be without the deduction to the amount of AMT liability.” *Id.*

163. JOINT COMM. ON TAXATION, 107<sup>TH</sup> CONG., *supra* note 155, at 6.

164. *Id.*; see also Gene Steuerle, *Moving Beyond The Fight Over The Alternative Minimum Tax*, 2001 TAX NOTES TODAY 118–31, ¶ 4 (June 18, 2001) (“IRS compliance efforts on many items of the AMT are minimal. The Service essentially enforces items that are reported elsewhere on a normal tax return, such as state and local tax deductions and personal exemptions.”).

165. See Shaviro, *supra* note 162, at ¶ 12. “The AMT may also generate a significant quantum of what [David] Bradford calls ‘transactional complexity’ (referring to the problems faced by the taxpayer in keeping records, choosing forms, making necessary calculations, and so on).” *Id.* at ¶ 18 (quoting DAVID F. BRADFORD, *UNTANGLING THE INCOME TAX* 266–67 (Cambridge, Harvard University Press, 1986)). Obfuscation has its own value through the creation of optimal social policies without political suicide. *Id.* at ¶

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survey of its 10,000 members, who proclaimed that the AMT “is the biggest headache for practitioners and their clients.”<sup>166</sup>

Additionally, the late W. Val Overson, from the National Taxpayer Advocate, has declared the AMT as “absolutely, asininely stupid.”<sup>167</sup> The IRS approximates that in 1997 more than five million taxpayers completed the AMT’s Form 6251, spending 29 million hours in the process.<sup>168</sup> Basically, this means that each AMT taxpayer spent almost 6 hours and 2 minutes on preparation of Form 6251 or the monetary equivalent (paying a professional tax preparer).<sup>169</sup> As AMT grows over the next few years, the total number of hours spent on the preparation of Form 6251 obviously will grow alongside it.<sup>170</sup> Already in 1999, the IRS received more than 6,400 calls for help in regards to the AMT despite the fact that near 93% of returns with AMT liability were completed by paid preparers.<sup>171</sup> Moreover, the IRS found that more than 10% of tax returns with AMT liability were filed with errors in the AMT calculations.<sup>172</sup> Additionally, the AMT proves difficult even for tax software especially because of its multi-year calculations, e.g., the AMT credit.<sup>173</sup>

By allowing the AMT to affect the middle class, the complexities of the AMT will compound. Notwithstanding the simple fact that taxpayers with incomes between \$30,000 and \$100,000 filing AMT returns will increase from 23% in 2002 to 53.7% in 2010,<sup>174</sup> the compliance costs paid by this economic group will increase by a similar rate.<sup>175</sup> Moreover, economists estimate that taxpayers with income below \$100,000 will have an

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[T]ransparency need not be a supreme value if—always a big if—obfuscation permits well-meaning policymakers to choose better policies. [For example], the chief ‘rationale for muddying the relationship between social security taxes and benefits was to increase the potential to engage in hidden but it was thought desirable, progressive redistribution.’

*Id.* (quoting from DANIEL N. SHAVIRO, *MAKING SENSE OF SOCIAL SECURITY REFORM* 20 (Chicago, University of Chicago Press, 2000)).

166. Ryan J. Donmoyer, *NAEA Says AMT Is Biggest Tax Headache Of All*, 2000 TAX NOTES TODAY 61–6 (Mar. 28, 2000).

167. Sheryl Stratton, *Overson Speaks Out On Tax Code Complexity*, 2000 TAX NOTES TODAY 168–1 (Sept. 4, 2000).

168. 2000 TAX NOTES TODAY 128–40, ¶¶ 94, 106 (June 5, 2000).

169. *Id.* at 26.

170. See BURMAN ET AL., *supra* note 3.

171. Daniel Shaviro, *Tax Simplification and the Alternative Minimum Tax*, 2001 TAX NOTES TODAY 103–108 ¶ 14 (May 28, 2001).

172. *Id.*

173. *Id.*

174. See BURMAN ET AL., *supra* note 3.

175. See BURMAN ET AL., *supra* note 3, at 35.

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average AMT liability of less than \$2,000 in 2010.<sup>176</sup> Thus, the amount of compliance costs in relation to revenue will be high.<sup>177</sup> Additionally, taxpayers whose regular income tax credits the AMT diminishes or is disallowed may be forced to fill out the complicated AMT worksheets only to determine to what extent the AMT diminishes their personal credits—even though they owe no tax under AMT.<sup>178</sup> Finally, a majority of those taxpayers who fill out the AMT forms ultimately do not owe AMT. In 1998, “more than 6.4 million returns required AMT computation, and more than 4 million filers submitted the form, of which 3.4 million did not owe any AMT.”<sup>179</sup> Filers with incomes below \$100,000 submit most of these completed forms that do not have AMT liability.<sup>180</sup> This burden is further compounded because the bulk of middle class tax returns are done by software like Turbo Tax if not manually.<sup>181</sup> Thus, the inference can be made that as the AMT encroaches upon the middle class, either the IRS must expect a greater error rate on AMT forms (because more of the middle class might not begin to hire professional help) and spend more on taxpayer guidance, or more of the middle class will have to begin paying for professional tax preparation.<sup>182</sup> Both outcomes add to the regressive effects of the AMT because, no matter what, the middle class bears the bulk of AMT costs: not only its liability but, arguably, its negative externalities.<sup>183</sup>

### B. *AMT's Pro-Cyclical Effect*

For the most part, tax and transfer rules are “automatically countercyclical.”<sup>184</sup> When the economy expands, tax revenues increase because taxpayers have more income, and when there is recession, tax revenues decrease because taxpayers have less income.<sup>185</sup> To the contrary, the AMT tends to be pro-cyclical by taking in greater revenues during recessions and lesser revenues during economic expansions.<sup>186</sup> This effect only exacerbates the

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176. BURMAN ET AL., *supra* note 3, at 35.

177. *Id.*

178. *Id.*

179. *Id.* (citing NAT'L TAXPAYER ADVOC., FY 2001 ANN. REP. TO CONGRESS, I.R.S. Pub. 2104, 175 (Dec. 2001) at <http://www.irs.gov/pub/irs-pdf/p2104.pdf>).

180. *Id.* (citing 2000 TAX NOTES TODAY, 128–40, ¶ 88 (June 5, 2000)).

181. Sharviro, *supra* note 162, at 1457.

182. *See id.*

183. *See* BURMAN ET AL., *supra* note 3, at 35.

184. Shaviro, *supra* note 162, at 1458 (including not only the income tax, but the various welfare, social insurance, and other transfer systems as well).

185. *Id.*

186. *Id.*

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bumpiness of a business cycle.<sup>187</sup> This effect occurs because taxpayers will determine the investments they will make over a number of years, taking into consideration their AMT liability.<sup>188</sup> Should a downturn in the economy come about during one of those years that causes a decrease in income, the AMT will increase above its expected level in the event of a recession.<sup>189</sup>

This argument is not as significant as others against the AMT.<sup>190</sup> Although it is true that AMT revenues increase during recessions, the regular income tax counterbalances this effect somewhat by taking in less revenues.<sup>191</sup> In addition, gross AMT taxable income tends to be less in recessions than during expansion periods because taxpayers simply have less regular taxable income to adjust for AMT purposes.<sup>192</sup> These facts still do not stop opponents of the AMT like Jack Faris, the president of the National Federation of Independent Business, from using AMT's pro-cyclical nature as ammunition for its repeal.<sup>193</sup>

### C. *Perceived Inequity: A Faulty Rationale?*

The purpose of the AMT is solely philosophical; it is not the creation of a revenue stream for the Treasury.<sup>194</sup> In 1969, when Congressmen received more letters about the "gross unfairness" of the tax system, which was allowing several hundred taxpayers

187. Shaviro, *supra* note 162, at 1458.

188. *See id.*

189. Shaviro, *supra* note 162, at 1458.

190. *Id.*

191. *Id.*

192. *Id.*

193. *See* National Federation of Independent Business, *NFIB Small-Business Agenda: Tax Relief*, (Jan. 9, 2003) at [http://www.nfib.com/cgi-bin/NFIB.dll/jsp/issues/newsReleaseDisplay.jsp?BV\\_SessionID+@@@0121257681.1069006143@@@&BV\\_EngineID=ccceadcjllhdiifcngcfkmdffgdhfi.0&contentId=3639736](http://www.nfib.com/cgi-bin/NFIB.dll/jsp/issues/newsReleaseDisplay.jsp?BV_SessionID+@@@0121257681.1069006143@@@&BV_EngineID=ccceadcjllhdiifcngcfkmdffgdhfi.0&contentId=3639736) (referring to Faris's statement that: "The AMT literally kicks taxpayers 'when they are down' and should be eliminated.").

194. *See* STAFF OF HOUSE JOINT COMM. ON TAXATION, 99TH CONG., GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1986, 432-33 (Comm. Print 1986):

[T]he minimum tax should serve one overriding objective: to ensure that no taxpayer with substantial economic income can avoid significant tax liability by using exclusions, deductions, and credits. Although these provisions may provide incentives for worthy goals, they become counterproductive when taxpayers are allowed to use them to avoid virtually all tax liability. The ability of high-income taxpayers to pay little or no tax undermines respect for the entire tax system and, thus, for the incentive provisions themselves. In addition, even aside from public perceptions, Congress decided that it is inherently unfair for high-income taxpayers to pay little or no tax due to their ability to utilize tax preferences.

*Id.*

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with annual incomes above \$500,000 to get away with no tax liability—and again in 1986, when Congress implemented the current version of the AMT, these Congressmen obviously believed that the public's perception of the tax system was significant.<sup>195</sup> Thus, they believed that if nothing was done about this inequity, it would destroy their constituents' faith and honesty towards the tax system.<sup>196</sup> The AMT was supposed to allay this anger and restore this faith.<sup>197</sup>

However, the AMT, itself, did not solve the inequities of the tax system.<sup>198</sup> In reality, the AMT never has achieved the goal of requiring all high-income taxpayers pay some federal income tax.<sup>199</sup> With the AMT in place, in 1974, 246 taxpayers with incomes over \$200,000 did not pay any federal income tax.<sup>200</sup> In 1988, two years after the massive overhaul of the AMT, 822 taxpayers of the same income bracket still did not pay any federal income tax.<sup>201</sup> Ten years later, in 1998, 1,467 taxpayers of the same bracket did not pay any federal income tax.<sup>202</sup> Percentage-wise, this number has not changed significantly—if not improved.<sup>203</sup> However, the IRS estimates that without the AMT, 14,000 individuals would have no income tax liability.<sup>204</sup>

Therefore, the AMT's role within the broad scope of the U.S. tax system can stand the firmest upon the economic theory of second-best.<sup>205</sup> When implementing large national policies, like a tax system, it is near impossible to eradicate all the existing inequities—no matter how careful its design.<sup>206</sup> The eradication of inequities becomes especially difficult if Congress wants to

195. *See id.*; *see also* BURMAN ET AL., *supra* note 3, at 6.

196. *See id.*

197. *See id.*

198. Rep. Jim Saxton, *AMT is Growing Burden, Says JEC Report*, 2001 TAX NOTES TODAY 105–36, ¶ 20 (May 30, 2001).

199. *Id.*

200. *See id.* at tbl. 3.

201. *See id.*

202. *See id.*

203. *See id.* (compare 0.79% of taxpayers with incomes above \$200,000 that paid no federal income tax in 1974 to 0.07% in 1998).

204. TAX NOTES TODAY, *supra* note 168, at 27.

205. Shaviro, *supra* note 162, at 1463 (“Absolutely, asininely stupid’ . . . though the AMT may be, the theory of the second-best applies to asininity and stupidity, just as much as to anything else. Two asinine and stupid tax systems that interact in asinine and stupid ways might nonetheless conceivably produce less overall asininity and stupidity than just one.”); *see also* Daniel Shaviro, *Selective Limitation on Tax Benefits*, 56 U. CHI. L. REV. 1189, 1204 (1989) (“The theory of second-best . . . holds that if one or more constraints prevents the attainment of optimal conditions, one cannot predict in the abstract whether removing any other constraints will improve or worsen conditions.”).

206. *See* BURMAN ET AL., *supra* note 3, at 26.

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incentivize certain activities that create inequity.<sup>207</sup> That the AMT is necessary to maintain respect for or improve the tax system is debatable.<sup>208</sup> There is no empirical evidence supporting that AMT actually allays these concerns.<sup>209</sup> A second-best justification for the AMT also assumes that “policy in the regular [income] tax contains flaws,” but the “policy in the AMT, made by the same political agents who are subject to the same budget and political constraints as when they make changes in the regular tax, effectively counteract those flaws.”<sup>210</sup>

In addition to the lack of empirical evidence that the AMT improves the tax system as a whole, there is difficulty even to the logic that AMT improves the tax system.<sup>211</sup> The question must be asked “why a decline in the nominal rate from 20% to 0% should raise a greater concern than a decline from 40% to 20% when, ‘in simple arithmetical terms, each equal percentage step in the reduction of one’s tax liabilities has the same effect on revenues, no matter what the starting or stopping point.’”<sup>212</sup> Additionally, the public’s perception of inequity in the tax system focuses on taxes paid, rather than actual tax incidence.<sup>213</sup> This focus risks a misunderstanding of the distributional effects of the income tax system.<sup>214</sup> Tax benefits may be fully capitalized into market prices, leaving those who enjoy them no better off than those who are paying actual taxes in lieu of implicit taxes, and thereby converting any possible unfairness into inefficiency.<sup>215</sup> The fact that one taxpayer did not have an income tax to pay in a given year does not indicate what taxes that taxpayer has paid in the

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207. Take, for example, the Texas independent oil entrepreneur, who is one type of taxpayer that is more likely to escape tax liability because of the likelihood that his company’s tax structure allows pass-through income and allows him to use all the depletion and deductions available to him. Compare this type of taxpayer with a taxpayer in the upper-management of a large public company who receives much of his income through salary. Even though the two taxpayers may generate the same amount of income, it is likely that the latter’s adjusted gross income will be much higher than the former. Therefore, the latter will have more difficulty escaping the income tax. The reason the oil entrepreneur can escape the higher tax burden of the corporate manager is the allowance of deductions, such as depletion in the regular income tax, which Congress designed to incentivize the exploration and production of natural resources. *See generally* I.R.C. § 611 (2000).

208. *See* Shaviro, *supra* note 162, at ¶ 32.

209. *Id.*; *see also* BURMAN ET AL., *supra* note 3, at 26.

210. Burman et al., *supra* note 3, ¶ 26.

211. Shaviro, *supra* note 162, at ¶ 32.

212. *Id.* at ¶ 34 (quoting Daniel Shaviro, *Perception, Reality and Strategy: The New Alternative Minimum Tax*, 66 TAXES 91, 96 (1988)).

213. *Id.* at ¶ 35.

214. *Id.*

215. *See* Boris I. Bittker, *Equity, Efficiency, and Income Tax Theory: Do Misallocations Drive Out Inequities?*, 16 SAN DIEGO L. REV. 735 (1979).

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years before or in the years to come.<sup>216</sup> Nor does it indicate what tax benefits this taxpayer receives or does without.<sup>217</sup>

## IV. POSSIBLE SOLUTIONS AND THEIR ANALYSIS:

Since Congress created the AMT to solve the perceived unfairness of the tax system,<sup>218</sup> that intent will probably remain a primary consideration. Therefore, the fact that the AMT ultimately will become a middle-class tax must be dealt with. Nonetheless, because AMT's revenues will become a great proportion of the tax revenues received by the Treasury over the coming years, any decision will not be solely political, but also financial.<sup>219</sup> It will be costly to alter the AMT, and, therefore, perhaps these costs will limit the options.<sup>220</sup>

The government deficits forecasted for the coming years compound this problem significantly.<sup>221</sup> Of course, the underlying question remains: what is the value of remediating the perceived inequities of the tax system?<sup>222</sup> Congress has a few major options to consider.<sup>223</sup> Obviously, it could do nothing.<sup>224</sup> We already have seen, though, that this approach would leave the budget intact, but would expose 35.6 million taxpayers to AMT by 2010 — a far cry from the 2.6 million expected in 2002.<sup>225</sup> So, if Congress were to act, it could do the following. *First*, Congress could index the AMT.<sup>226</sup> This solution will cut the number of taxpayers exposed to AMT in 2010 to 13.6 million if the indexing begins in 2004.<sup>227</sup> But it will cost the Congressional budget \$470 billion if Congress

216. See Shaviro, *supra* note 162, at ¶ 35–36.

217. *Id.*

218. See *supra* notes 195–197 and accompanying text.

219. See Sullivan, *supra* note 5 (“But it was only two years ago that Congress could have solved the entire problem at a cost of ‘only’ \$200 billion over 10 years . . . . And with each passing year, another far more expensive year crept into the back-end of the 10-year revenue window.”).

220. See BURMAN ET AL., *supra* note 3, at 19–20 (AMT will account for 10% of all tax revenues).

221. See Joseph Guinto, *Bush Seeks \$2.23 Tril For ‘04 Budget, Sees Record \$307 Bil Deficit*, INVESTOR’S BUSINESS DAILY, Feb. 4, 2003, available at [http://web.lexis-nexis.com/universe/document?\\_m=cc01496630f0811364c58f10d0609a16&wchp=dGLbVlb-zSkVA&\\_md5=708d915ad619a8d48b7106ad37228c84](http://web.lexis-nexis.com/universe/document?_m=cc01496630f0811364c58f10d0609a16&wchp=dGLbVlb-zSkVA&_md5=708d915ad619a8d48b7106ad37228c84).

222. Some suggest that the public’s perceived inequity is not worth much. See generally JOINT COMM. ON TAXATION, 107th CONG. *supra* note 155, at 10.

223. See, e.g., BURMAN ET AL., *supra* note 3, at 37–51 and Shaviro, *supra* note 162, at ¶ 53–102.

224. See Sullivan, *supra* note 5.

225. See BURMAN ET AL., *supra* note 3, at tbl. 5 (compare the percent of tax liability in 2010 of the AMT and the total income tax to the same in 2002).

226. See *id.* at 37.

227. *Id.* at tbl. 8.

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extends EGTRRA.<sup>228</sup> *Second*, Congress could index the AMT and include the regular income tax exemptions and credits in the AMT.<sup>229</sup> This solution will reduce the number of taxpayers who pay AMT in 2010 to 6 million, but at a cost of \$624 billion, again assuming Congress extends EGTRRA.<sup>230</sup> *Third*, Congress could index the AMT, include the exemptions and credits, and, additionally, allow state and local tax deductions and a repeal of the exemption phase-outs.<sup>231</sup> Basically, this would repeal the brunt of the AMT, reducing the number of AMT taxpayers to 300,000.<sup>232</sup> The amount of high-income taxpayers that have no tax liability would drastically increase.<sup>233</sup> *Fourth*, Congress could repeal the AMT.<sup>234</sup> This action will cost the budget \$951 billion and, again, increase the amount of high-income taxpayers with no tax burden.<sup>235</sup> *Lastly*, Congress could repeal the AMT and adjust the regular income tax code to account for the lost AMT revenues and maintain an identical distribution.<sup>236</sup> The Urban-Brookings Tax Policy Center (“UBTPC”) ran economic simulations to determine the outcomes of each of these scenarios. Obviously, each of these comes with their own benefits, costs and assumptions that must be analyzed in order to strike the right balance.

A. *Indexing the AMT: Option One*

The UBTPC considered indexing the AMT exemptions, tax brackets and threshold for the exemption phase-outs for inflation after 2002 just as the regular income tax.<sup>237</sup> These economists concluded that this option would reduce the number of AMT taxpayers in 2010 from 35.6 million to 10.4 million, which is a 71% reduction overall.<sup>238</sup> This option would highly benefit the middle class and leave the main burden of the AMT upon the upper-middle class and beyond.<sup>239</sup> If you break up this reduction amount by income bracket, nearly 94% of taxpayers with incomes between \$15,000 and \$75,000 would be relieved of their AMT

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228. *Id.*

229. *See id.* at 38.

230. *Id.* at tbl. 8.

231. *See id.* at 38–39.

232. *Id.* at tbl. 8.

233. *Id.* at tbl. 8.

234. *Id.* at 40.

235. *Id.* at tbl. 8.

236. *See id.* at 41–42.

237. *See id.* at 37–38.

238. *Id.* at tbl. 8.

239. *See id.* at tbl. 9.

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burden.<sup>240</sup> Greater than 84% of taxpayers with incomes between \$75,000 and \$100,000 no longer would pay AMT.<sup>241</sup> Almost 62% of taxpayers with incomes between \$100,000 and \$200,000 would be relieved as well.<sup>242</sup> At the same time, approximately 6% of taxpayers with incomes between \$200,000 and \$500,000 no longer would pay AMT, while 2.8% of taxpayers with incomes between \$500,000 and \$1,000,000 would no longer pay, and 1.4% of taxpayers with incomes above \$1,000,000 would no longer pay.<sup>243</sup> This option would make the overall tax system more progressive than it was because taxpayers with incomes below \$200,000 would benefit from 83% of the tax cut.<sup>244</sup> This option would cause the amount of zero-tax returns in 2010 for taxpayers with incomes greater than \$200,000 to increase slightly from 2,900 to 3,300, but the number would remain the same for taxpayers with incomes above \$1,100,000.<sup>245</sup> Unfortunately, during the years of 2003 and 2012, if this option were implemented, it would affect tax revenues by \$368 billion, should EGTRRA sunset in 2010, and by \$468 billion if Congress extended EGTRRA.<sup>246</sup> When figuring these costs into the federal budget and taking account for the interest payments on the added federal debt, the overall cost would be \$438 billion as long as EGTRRA sunsets and \$542 billion if EGTRRA does not.<sup>247</sup> This option may expire because so far, the repeal of the dividend tax and job creation have taken the front seat as the priorities of any tax changes that occur in 2003.<sup>248</sup>

Should Congress not index the AMT after 2002, for whatever reason, the UBTPC also ran a simulation that calculated the effects of indexing after 2004.<sup>249</sup> This two-year delay would make indexing slightly less expensive.<sup>250</sup> Tax revenues would only dip by \$319 billion, should EGTRRA sunset, which is 13% less than indexing after 2002.<sup>251</sup> If EGTRRA did not sunset, tax revenues would only dip \$408 billion, which is, again, 13% less than the

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240. *Id.*

241. *Id.*

242. *Id.*

243. *Id.*

244. *Id.* at 37.

245. *Id.* at tbl. 8.

246. *Id.*

247. *Id.*

248. See David Espo, *Bush Seeks \$1.3 Trillion in New Tax Relief*, Associated Press (Feb. 3, 2003), at [http://story.news.yahoo.com/news?tmpl=story&u=/ap/20030203/ap\\_on\\_go\\_pr\\_wh/budget\\_taxes\\_2](http://story.news.yahoo.com/news?tmpl=story&u=/ap/20030203/ap_on_go_pr_wh/budget_taxes_2).

249. BURMAN ET AL., *supra* note 3, at 38.

250. See *id.* at tbl. 8.

251. *Id.*

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2002 numbers.<sup>252</sup> The budget savings would be roughly equal to the tax revenue savings.<sup>253</sup> Of course, delaying the implementation of indexing would leave a greater burden on the middle class, but it would still receive the bulk of the AMT relief as opposed to those with incomes over \$200,000.<sup>254</sup>

B. *Indexing and Including Regular Income Tax Exemptions and Credits in the AMT: Option Two*

The UBTPC also simulated the option of indexing the AMT exemptions, tax brackets and threshold for the exemption phase-outs for inflation after 2002, as in the option above, but also allowing dependent exemptions and personal nonrefundable credits in the AMT since these items “focus on middle-class taxpayers and . . . are unrelated to egregious tax sheltering.”<sup>255</sup> This option would further reduce the amount of taxpayers subjected to AMT to only six million in 2010.<sup>256</sup> This would be an 83% reduction as opposed to a 71% reduction by only indexing.<sup>257</sup> Obviously, by removing more taxpayers from AMT susceptibility, the costs of this option would be greater.<sup>258</sup> Between the years of 2003 and 2012, and if EGTRRA sunsets, tax revenues would suffer a \$423 billion loss, and if Congress extends EGTRRA, a \$535 billion loss.<sup>259</sup> Moreover, the budget will suffer a \$507 billion loss if EGTRRA sunsets, and a \$624 billion dollar loss if EGTRRA is extended.<sup>260</sup> This option would cost approximately 13% more than solely indexing in 2002.<sup>261</sup> However, the amount of zero-tax returns in 2010 would roughly remain the same as the indexing option.<sup>262</sup> The benefit of these greater costs would be that the middle class, overall, would be relieved from the AMT, while the burden would remain on the upper-middle and upper

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252. *Id.*

253. *Id.*

254. *See id.* at tbl. 9. Over 90% of taxpayers with incomes between \$15,000 and \$75,000 would still avoid AMT as opposed to nearly 94% if indexing began after 2002. *See id.* Seventy-two percent of taxpayers with incomes between \$75,000 and \$100,000 would avoid AMT as opposed to 84.1%. *Id.* Forty-nine percent of taxpayers with income between \$100,000 and \$200,000 would be relieved from AMT. *Id.* Finally, below 4% of all taxpayers with incomes above \$200,000 would no longer pay AMT. *See id.*

255. *See id.* at 38.

256. *Id.* at tbl. 8.

257. *Id.* at 38.

258. *Id.*

259. *See id.* at tbl. 8.

260. *Id.*

261. *Id.*

262. *Id.*

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classes.<sup>263</sup> Over 97% of taxpayers with incomes between \$15,000 and \$100,000 would no longer face AMT.<sup>264</sup> Over 81% of taxpayers with incomes between \$100,000 and \$200,000 would no longer pay AMT.<sup>265</sup> Concurrently, only 8.6% of taxpayers with incomes between \$200,000 and \$1,000,000 would not be susceptible to AMT, and 3.1% of those with incomes above \$1,000,000 would no longer pay.<sup>266</sup>

*C. Indexing; Including Exemptions, Credits, State and Local Tax Deductions; and Repealing Phase-outs: Option Three*

The UBTPC additionally simulated a model that included all the changes of the two options above, but also included a repeal of the AMT exemption phase-outs, in order to match the phase-outs in the regular income tax, and an allowance of the deductions for state and local taxes and miscellaneous expenses above the 2% AGI floor.<sup>267</sup> Again, these added items are not egregious tax shelters.<sup>268</sup> The main item left in the AMT for this simulation is the deferral provisions.<sup>269</sup> Unlike the items in the last option, these items tend to focus more upon high-income taxpayers since phase-outs do not apply until the thresholds of \$150,000 (for married individuals) and \$112,500 (for single filers), and since high-income taxpayers do pay more state and local taxes than lower-income taxpayers.<sup>270</sup> This option would reduce the number of taxpayers subjected to AMT from 35.6 million to 300,000 in 2010: a 99% reduction.<sup>271</sup> It virtually would repeal AMT for everyone except taxpayers with incomes below \$15,000 and those with incomes above \$1,000,000.<sup>272</sup> Still, 72.4% of taxpayers with incomes above \$1,000,000 would no longer face AMT.<sup>273</sup> Thus, this option would increase the number of zero-tax returns in 2010 by 88% for taxpayers with incomes above \$200,000 and 67% for those with incomes above \$1,000,000.<sup>274</sup> Since this option is a near-repeal, the effect on revenue would be

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263. *See id.* at tbl. 9.

264. *See id.* at 38.

265. *See id.* at tbl. 9.

266. *See id.*

267. *Id.* at 38–39.

268. *Id.* at 39.

269. *Id.* at 40.

270. *Id.* at 39.

271. *Id.* at tbl. 8.

272. 97.6% of them, at least. *See id.* at tbl. 9.

273. *Id.*

274. *See id.*

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great when compared to the aforementioned alternatives.<sup>275</sup> Between 2003 and 2012, tax revenues would shrink by \$597 billion if EGTRRA sunsets and \$749 billion if EGTRRA does not.<sup>276</sup> Consequently, the budget would suffer a \$725 billion shortfall if EGTRRA sunsets and \$883 billion if EGTRRA does not.<sup>277</sup>

#### D. *Repeal: Option Four*

The UBTPC ran a simulation of a complete repeal of the AMT, as well.<sup>278</sup> With the AMT no longer in place, the number of zero-tax returns would jump greatly to 17,200 by 2010 for taxpayers with incomes greater than \$200,000 and 1,300 for taxpayers with incomes over \$1,000,000.<sup>279</sup> This jump would increase these numbers 177% and 160%, respectively, over the last option mentioned.<sup>280</sup> However, on a percentage basis, taxpayers with incomes between \$100,000 and \$200,000 would receive the most benefit from this tax cut: 38.2% while taxpayers with incomes over \$1,000,000 would only receive a 4.9% tax cut.<sup>281</sup> Additionally, this option would be the most expensive for the federal government when compared to the other options.<sup>282</sup> Tax revenues would decrease in the years of 2003 to 2012 by \$647 billion if EGTRRA sunsets and \$802 billion if EGTRRA does not.<sup>283</sup> Furthermore, this option would shrink the budget by \$788 billion if EGTRRA sunsets and \$951 billion if EGTRRA does not.<sup>284</sup> This option would be approximately 8% more expensive than the last option and over 50% more expensive than the second option.<sup>285</sup>

#### E. *A Distribution-Neutral, Constant-Revenue, Repeal of AMT: Option Five*

All of these options discussed above involve altering the distribution and revenues of the tax system. A few scholars have

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275. *See id.* This option would be 29% more expensive than just indexing, allowing dependent exemptions and personal nonrefundable credits. *See id.*

276. *Id.*

277. *Id.*

278. *Id.* at 40–41.

279. *Id.* at tbl. 8.

280. *See id.*

281. *See id.* at tbl. 9.

282. *Id.* at tbl. 8.

283. *Id.*

284. *Id.*

285. *See id.*

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advocated that the fairest reform of the AMT would be its repeal with counterbalances in the regular income tax to maintain the current distribution and expected revenues that the AMT would have generated.<sup>286</sup> This solution also might be the most politically costly.<sup>287</sup> Taxpayers notice changes made to the basic structure of the regular income tax, more so than changes in the subtleties, e.g., deductions, exemptions.<sup>288</sup> The UBTPC determined in a simulation, using 2010 data, that the Congress would have to raise the statutory regular income tax rates from 10%, 15%, 25%, 28%, 33%, and 35% to 10.7%, 16.3%, 29.2%, 33.8%, 43%, and 33.2%, respectively.<sup>289</sup> Effectively, the rate of every bracket would be raised with the exception of the highest income bracket, which would be reduced.<sup>290</sup> Despite the policy-neutrality of this option, the amount of zero-tax returns in the high-income brackets would increase 400%.<sup>291</sup> Therefore, perhaps, this option is not fully policy-neutral because if there is any value to abating perceived inequity, it is left out of this option.<sup>292</sup> This option “would raise tax liabilities for 62[%] of all taxpayers, including more than 80[%] of those with AGI between \$15,000 and \$75,000.”<sup>293</sup> Thus, the burden of this reform would be shared with taxpayers who were not susceptible to AMT before its repeal.<sup>294</sup>

## V. CONCLUSION

If a cure for perceived inequity has more than a *de minimis*

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286. See, e.g., Shaviro, *supra* note 162, at ¶¶ 60–61. Some even say this option is the only possible option because of political tensions on Capitol Hill. See Gene Steuerle, *The Crazy Politics Of The Alternative Minimum Tax*, 1999 TAX NOTES TODAY 54–95 (March 22, 1999). According to Steuerle:

Some liberal advocates seem to be saying that any tax on the rich and upper-middle class, no matter how badly designed, is a good tax. Some conservative advocates seem to be saying that any tax on the rich is bad, but an explicit tax is worse than a badly designed, implicit, one. The compromise: keep the AMT more or less as it is . . . . Simply eliminate or cut the AMT and then replace it with more direct taxes on the income classes that benefit from the AMT tax cut.

*Id.*

287. See Sullivan, *supra* note 5 (“Even though overall revenue is unaffected and the distribution of the tax burden among income classes is unchanged, such a clearly visible tax rate increase would receive a lot more attention than the simplification achieved through eliminating the hard-to-comprehend AMT.”).

288. GRUBER & SAEZ, *supra* note 151, at 5.

289. BURMAN ET AL., *supra* note 3, at 42.

290. See *id.* at tbl. 7.

291. See *id.* at 42.

292. See *id.*

293. See *id.*

294. See *id.*

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value, the AMT still has a purpose within the U.S. tax system. Out of these options, Option One and Option Two seem to remain closest to the original intent of the AMT because they both mostly relieve the middle class from the AMT, for reasons mostly related to bracket-creep and personal exemptions, while ensuring that only a small number of zero-tax returns by individuals with high incomes exist. Option Three may repeal too much of the AMT, if this value exists, since it removes items that mostly affect the upper-middle and upper classes—even though these items are not used as egregious tax shelters. More of a reason, though, may be that this option allows for dramatically more zero-tax returns from high-income earners than the first two options.<sup>295</sup> Of course, if Congress had a choice between these three options only, and based that decision upon finance and maintaining AMT's intent, this option likely would lose because it is 29% more expensive than Option Two and 39% more expensive than Option One, while not staying as much within the lines of the AMT's intent as the other two.<sup>296</sup> Again, if there is value to cure for perceived inequity, then total repeal (Option Four) should not even be considered because it is the most expensive of options with the worst possible outcome of all of the options.<sup>297</sup> Even a “policy-neutral” repeal (with its counterbalances in the regular income tax) is not an answer if there is substantial value to the AMT, since the number of zero-tax returns of high-income earners increases fourfold under this option, and, therefore, is not neutral to all policies—even though it is the friendliest of options to the Treasury's pocketbook.<sup>298</sup> Additionally, policy-neutral repeal would be the most dangerous options for politicians and their careers at this time because the middle class has yet to feel the full wrath of the AMT upon them—whether there is substantial value to the AMT or not. Therefore, these taxpayers most likely would not understand that the regular income tax hikes implemented (except for the highest income bracket) by the Congress were to replace what was to come, that is, the AMT. Perhaps perceived inequity would not matter as much once the AMT *has* become a middle class tax? To wait to repair the situation and look like saviors would only become more costly, though.

If there is no substantial value to the cure for perceived inequity, then, obviously, there is no need for the AMT. But, again, would politicians be willing to enact the policy-neutral

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295. An 88% increase in zero-tax returns for income-earners of \$200,000 or more and a 67% increase for those within incomes of \$1,000,000 or more. *See id.* at tbl. 8.

296. *See id.*

297. *See id.*

298. *See id.*

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repeal with the regular income tax counterbalances—especially in the present business cycle slump? And if Congress repealed the AMT without the regular income tax counterbalances, does the Treasury want to stomach the debt necessary to do so when odds are that AMT repeal would take a backseat to the President's dividend tax repeal, which is itself being called into question as an excessive burden on the budget by some of the President's usual proponents, such as Chairman of the Federal Reserve Allan Greenspan?<sup>299</sup>

In regards to moving towards a solution over this matter, Gene Steurle writes:

With or without a broader agenda on which to hang the AMT reform, it's . . . going to require the two political parties to move beyond their current positions. For Democrats, it will require accepting a system that might even be less progressive than otherwise obtainable, while for the Republicans it will require accepting higher statutory rates than otherwise are attainable.<sup>300</sup>

Perhaps the AMT problem is just not ripe yet. Perhaps it is going to take a similar public outcry, as the catalytic one in 1969 that inspired the creation of the AMT, before the two political parties do move towards a solution.

*R. Jason Griffin*

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299. See Glenn Somerville, *Greenspan Questions Need for Economic Stimulus*, Reuters (Feb. 11, 2003), at [http://story.news.yahoo.com/news?tmpl=story&ncid=580&e=1&cid=580&u=/nm/20030212/bs\\_nm/economy\\_greenspan\\_dc](http://story.news.yahoo.com/news?tmpl=story&ncid=580&e=1&cid=580&u=/nm/20030212/bs_nm/economy_greenspan_dc).

300. Steurle, *supra* note 164, at ¶ 10.