



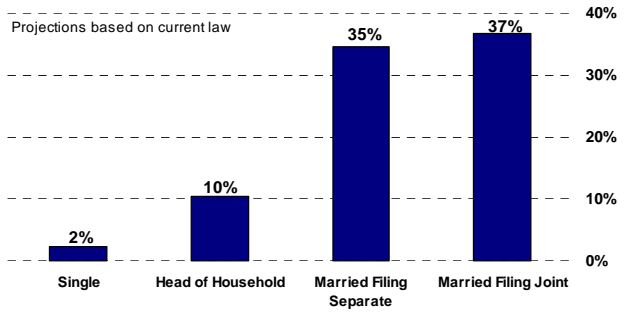
April 11, 2007

Has the Alternative Minimum Tax Become the Anti-Marriage Tax?

In 2006, married couples were five times more likely than singles to be subject to the Alternative Minimum Tax (AMT). If nothing is done to reform the AMT this year, married couples will be fifteen times more likely to pay AMT tax in 2007.¹ The AMT requires that taxpayers calculate the taxes they owe under both the normal tax system and the AMT, and pay the larger of the two taxes.

Originally enacted in 1969 to ensure that very high income households pay taxes, the AMT creates a separate tax system in which certain items, such as personal and dependent exemptions and state and local tax deductions (called “preference” items), are not allowed. Additionally, the AMT contains separate tax rates—26% and 28% (as well as phantom rates of 32.5% and 35%)²—that apply to AMT income³ above specified exemptions. Whereas the income exemption for married couples is twice that of singles under the regular income tax system, the AMT exemption for married couples is only 33% higher than for singles – creating another marriage penalty in tax law. Additionally, the regular tax system has higher tax bracket income limits for married couples, but the AMT applies the same brackets and rates regardless of marital status. Thus, as Figure 1 shows, 36% of married filers will pay the AMT in 2007 versus only 2% of singles and 10% of heads of households.

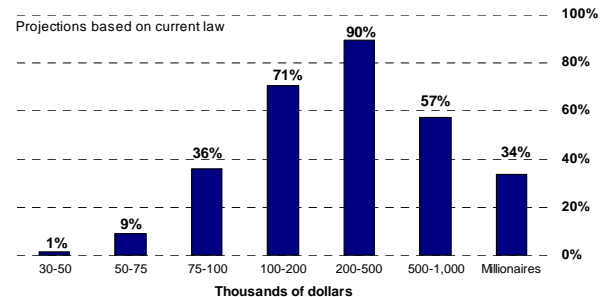
Figure 1:
Percent of Tax Filers Subject to the AMT by Filing Status, 2007



Source: Urban-Brookings Tax Policy Center

Although the AMT takes away personal and dependent exemptions, it does provide higher income exemptions than the regular tax system.⁴ Based on current AMT law, single taxpayers are allowed a \$33,750 exemption from AMT liability and married couples, a \$45,000 exemption.⁵ If these exemption levels seem low for a tax aimed at millionaires, it is because the AMT was never indexed for inflation. Consequentially, the AMT continues to creep down the income scale, affecting families making as little as \$30,000-\$50,000 in 2007 and families making under \$30,000 by 2017. Ironically, as lower-income taxpayers move into the AMT, higher-income taxpayers shift off of it because the AMT’s top statutory rate of 28% is lower than the 35% rate applicable under the regular income tax. As Figure 2 shows, taxpayers who make between \$75,000 and \$100,000 will be more likely than millionaires to pay the AMT in 2007.

Figure 2:
Percent of Tax Filers Subject to the AMT by Annual Income, 2007



Source: Urban-Brookings Tax Policy Center

¹ All projections herein based on Tax Policy Center calculations.

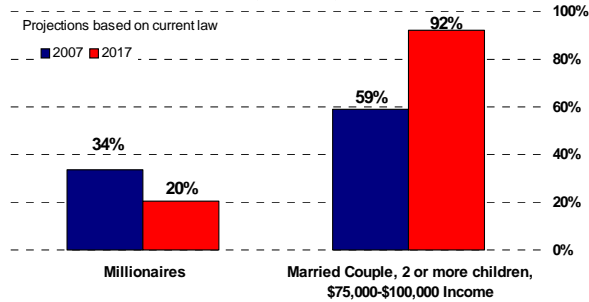
² The statutory tax rates are 26% and 28%, but a phase-out of exemptions adds effective rates of 32.5% and 35%.

³ AMT income equals AGI from the normal tax system, plus AMT preference items such as personal exemptions and state and local taxes.

⁴ Under the regular tax system, the single exemption is \$5,350 and the married exemption is \$10,700.

⁵ Exemption levels are based on current law. Previous “fixes” have temporarily increased the exemption levels. Most recently, the 2006 levels were increased to \$42,500 for singles and \$62,550 for married couples.

Figure 3: Millionaires Less Likely to Pay AMT than Married Couples with 2 or More Children and \$75,000-\$100,000 Income



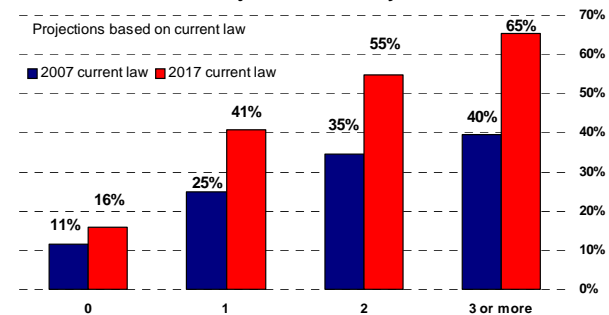
Source: Urban-Brookings Tax Policy Center

The percent of millionaires who are on the AMT will decline to only 20% by 2017.

In addition to affecting married couples and taxpayers with incomes increasingly further down the income scale, the AMT also affects taxpayers with children. Because the AMT does not allow for dependent exemptions, the more children a family has, the more likely the family is to be pulled into the AMT. Figure 4 shows that 40% of taxpayers with three or more children will be subject to the AMT in 2007 versus only 11% of taxpayers with no children. By 2017, taxpayers with three or more children will be four times more likely to be subject to the AMT than taxpayers without children.

If the AMT is not repealed or permanently fixed, it will become the primary tax system for the middle class—particularly those who are married and have children. Meanwhile, the wealthiest Americans, who were its original intended target, will become increasingly less affected. As Figure 3 shows, 59% of married couple families with 2 or more children and income between \$75,000 and \$100,000 will be on the AMT in 2007. By 2017, almost all of these families will be on the AMT. In contrast, only 34% of taxpayers making \$1 million or more will be on the AMT in 2007.

Figure 4: Percent of Tax Filers Subject to the AMT by Number of Children



Source: Urban-Brookings Tax Policy Center

While policymakers on both sides of the aisle recognize the need to repeal or significantly reform the AMT, the AMT generates substantial revenue that will continue to grow in magnitude. Eliminating the AMT would reduce projected revenues by \$750 billion over the next ten years if other tax relief is allowed to expire as scheduled. If the tax cuts are extended, the ten-year projected revenue loss would rise to \$1.3 trillion. Rather than eliminate the AMT altogether, some have suggested simply extending the increased 2006 exemption levels and indexing them to inflation. Even this modest reform would reduce projected revenues by \$500 billion over the next ten years if the tax cuts expire and by \$900 billion if they are extended.

Due to the high level of revenue generated by the AMT and its seeming simplicity, some have suggested allowing the AMT to become the primary tax system in the U.S. However, the AMT is a failure with respect to simplicity, fairness, and efficiency. Few people understand the complexity of the AMT and its impact on their economic situation. While some think the AMT is more efficient because it imposes lower rates on a broader base, most people affected by the AMT face higher marginal rates on a smaller base (due to the higher exemption levels). Furthermore, the general public and policymakers on both sides of the aisle agree that the AMT is an unfair tax.

Having two separate tax systems—one that contains benefits to help typical American families and another that takes those benefits away—only adds to the complexity, inequity and inefficiency of our tax system. Rather than serve as a minimum tax for the ultra-rich, the AMT is becoming a mass tax for average American families. The revenue it is projected to collect—by taxing married, middle to upper income class American families—was never intended. The AMT should be repealed on the basis of fundamental fairness, regardless of what projected revenue losses might be.