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THE ALTERNATIVE MINIMUM TAX ADDITIONAL NOTES

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These notes are based on the United States Internal Revenue Code and are for a presentation to the Northern Chapter of the Virginia Society of Certified Public Accountants on November 15, 2011. They are meant for educational purposes only. They are not meant as, nor should they be used as tax advice.

I) AMT Adjustment Items:

These may be additions or subtractions.

A) Adjustments Applicable To All Taxpayers:

Depreciation on Property Placed In Service After December 31, 1986:

AMT depreciation is calculated using the alternative MACRS method Code Section 168(g) and the 150% declining balance switching to straight line method. For real property (property subject to Code Section 1250) use a 40 year, straight line, mid-month convention. The requirement to use ADS class lives was repealed for property placed in service after December 31, 1998. The AMT adjustment is the difference between AMT depreciation and regular tax depreciation.

Mining Exploration and Development Costs Paid or Incurred After December 31, 1986:

The amount deductible for AMT for each mine or other natural deposit (other than an oil, gas, or geothermal well) is calculated by capitalizing these expenditures and amortizing them over a 10 year period beginning with the tax year in which they were incurred. The AMT adjustment is the difference between the regular tax deduction and the AMT deduction.

Treatment of Certain Long-term Contracts Entered Into On or After March 1, 1986:

The AMT taxable income from any long-term contract entered into by the taxpayer on or after March 1, 1986 shall be determined under the percentage of completion method of accounting (as modified by Code Section 460(b)). However, for small construction contracts the percentage of the contract completed shall be determined by using the simplified procedures for allocation of costs prescribed under Code Section 460(b)(3). A small construction contract is any home construction contract, or any other construction contract entered into by a taxpayer who estimates (at the time the contract is entered into) that such contract will be completed within the 2 year period beginning on the contract commencement date of such contract, and whose average annual gross receipts for the 3 taxable years preceding the taxable year in which such contract is entered into do not exceed \$10,000,000.

The requirement that the percentage of completion be used to calculate AMT will not apply to any contract entered into after June 21, 1988 that is: a home construction contract; is estimated that it will be completed within 2 years beginning on the contract commencement date; and the taxpayer's average annual gross receipts do not exceed \$10,000,000 for the 3 taxable years preceding the taxable year in which such contract is entered into.

Alternative Tax Net Operating Loss Deduction:

The AMT net operating loss deduction shall be allowed in lieu of the regular tax net operating loss deduction. The AMT net operating loss is computed as it is for regular tax except that the adjustments to taxable income are made and the loss is reduced by items of tax preference.

The NOL that can be deducted from AMT income may not exceed 90% of AMT income as determined before the NOL deduction.

Pollution Control Facilities Placed In Service After December 31, 1986:

The AMT allowable for amortization of any certified pollution control facility placed in service after December 31, 1986 shall be determined under the alternative system of Code Section 168(g). In the case of such a facility placed in service after December 31, 1998, such deduction shall be determined under Code Section 168 using the straight line method.

Adjusted Basis:

For AMT purposes taxpayers must recalculate the gain or loss on property sold during the taxable year using their AMT basis. The AMT basis is the regular tax basis adjusted for the following AMT adjustments:

For all taxpayers: Depreciation on property placed in service after December 31, 1986; mining exploration and development costs; and pollution control facilities.

For taxpayers other than corporations: Circulation expenditures; and research and development expenditures.

The AMT adjustment is the difference in gain or loss calculated using the regular tax basis vs. the AMT basis. This adjustment may be positive or negative.

Code Section 87 Not Applicable:

AMT taxable income does not include the alcohol and biodiesel fuels credit required by Code Section 87 for regular tax purposes.

B) Adjustments Applicable To Taxpayers Other Than Corporations:

Standard Deduction and Personal Exemptions: Individuals are not allowed deductions for the standard deduction or for personal exemptions.

Estates and trusts are not allowed the deduction in lieu of personal exemptions under IRC Section 642(b).

Phase-Out of Itemized Deductions: There is no phase of itemized deductions in 2011 or 2012 for regular tax or for AMT.

Medical Expenses: Only medical expenses in excess of 10% of AGI are deductible for AMT.

Miscellaneous Itemized Deductions:

For estates and trusts this means miscellaneous deductions subject to the 2% floor (Line 15b on the 2010 Form 1041).

For individuals this does not include legal fees and court costs incurred in connection with a claim of unlawful discrimination. But it does include Form 2106 employee business expenses, hobby loss deductions, and legal fees related to taxable settlements.

Taxes: For individuals and for estates and trusts no deduction is allowed for: state, local, and foreign, real property taxes; state and local personal property taxes; state, local, and foreign, income, war profits, and excess profits taxes; state and local general sales taxes.

While refunds of the above listed taxes may be included in regular taxable income the refunds are not taxable for AMT purposes.

Interest Expense:

There are two major differences for AMT purposes:

Residential Housing Interest: The portion of home equity loan interest that is not connected with the purchase, construction or substantial improvement of a qualified residence may not be deducted for AMT purposes. A houseboat (by which is meant a boat containing full living facilities) may not be claimed as a qualified residence for AMT purposes.

Keep in mind that the regular tax restrictions on mortgage interest apply. Also if you refinanced, the proceeds from refinancing have to be traced to their use.

Investment Interest Expense: Investment interest expense is calculated separately for AMT purposes. A separate Form 4952 is used for the calculation. For AMT – tax exempt private activity bond interest included as an AMT preference is included in investment income and interest expense incurred in acquiring these bonds is included in investment expenses. Investment income and expenses are calculated by including these items and the other adjustments in Code Sections 56, 57 and 58. However investment expenses which are classified as miscellaneous itemized deductions are not allowed for AMT purposes.

Circulation Expenditures After December 31, 1986: Expenditures to establish, maintain or increase the circulation of a newspaper, magazine or other periodical which are deducted in full. For AMT purposes these must be amortized ratably over the 3 year period beginning in the year they are incurred. This applies to individuals, estates, trusts and personal holding companies.

Research And Experimental Expenditures: Expenditures, which are allowed as a current year deduction pursuant to Code Section 174 for regular tax purposes, shall be amortized ratably over the 10 year period beginning with the taxable year in which they were made. This will not apply to expenditures in connection with an activity in which the taxpayer materially participates within the meaning of Code Section 469(h).

Incentive Stock Options:

For AMT purposes the excess of the fair market value of the stock over the option price on the date the option is exercised is a positive adjustment. This will not apply if the stock is subject to restrictions on transferability and to a substantial risk of forfeiture.

C) Adjustments Applicable To Corporations:

Adjusted Current Earnings (ACE) Adjustment:

This does not apply to any: S Corporation; Regulated Investment Company; Real Estate Investment Trust; or REMIC.

For AMT purposes: The AMT income of any corporation for any taxable year shall be increased by 75% of the excess (if any) of – (A) the adjusted current earnings of the corporation over (B) the AMT income (determined without regard to adjustments based on adjusted current earnings and the AMT net operating loss).

A negative adjustment is allowed: In general the AMT income of any corporation for any taxable year shall be reduced by 75% of the excess (if any) of – the amount referred to in (B) above over the amount referred to in (A) above. But this reduction shall not exceed the aggregate increases in AMT income above for prior taxable years over the aggregate reductions for prior taxable years.

For purposes of this subsection the term “adjusted current earnings” means the AMT income for the taxable year determined with the following adjustments (but determined without regard to this subsection and the AMT net operating loss): (A) depreciation; (B) inclusion of items included for purposes of computing earnings and profits (The term “earnings and profits” means earnings and profits computed for purposes of Subchapter C of the Internal Revenue Code.) such as the buildup in life insurance contracts; (C) disallowance of items not deductible in computing earnings and profits (with some exceptions); (D) certain other earnings and profits adjustments; (E) disallowance of loss on exchange of debt pools; (F) depletion; (G) treatment of certain ownership changes; (H) adjusted basis; (I) treatment of charitable contributions (notwithstanding (B) and (C) in this paragraph, no adjustment related to the earnings and profits effects of any charitable contribution shall be made in computing adjusted current earnings).

Merchant Marine Capital Construction Funds:

Amounts deposited in these funds are not deductible for AMT purposes. Earnings on these funds must be included in AMT gross income.

Special Deduction Under Code Section 833(b):

This deduction (which relates to Blue Cross and Blue Shield organizations, etc.) is not allowed for AMT purposes.

II) Items Of Tax Preference:

Tax-Exempt Interest on Specified Private Activity Bonds:

AMT income includes interest on specified private activity bonds reduced by any deduction not allowed for regular tax purposes which would have been allowable if the interest income were includible in regular tax gross income. The interest income includes exempt-interest dividends (as defined in Code Section 852(b)(5)(A)).

Specified private activity bond means any private activity (as defined by Code Section 141) which is issued after August 7, 1986 and the interest on which is not includible in gross income under Code Section 103.

Specified private activity bonds do not include:

- (1) Any qualified Code Section 501(c)(3) bond as defined in Code Section 145.
- (2) Any bond issued after the date of enactment of this clause if such bond is – (I) an exempt facility bond issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide qualified residential rental projects as defined in IRC Section 142(d); (II) a qualified mortgage bond as defined in Code Section 143(a); or a qualified veterans’ mortgage bond as defined in Code Section 143(b).
- (3) Any bond issued after December 31, 2008 and before January 1, 2011.

Gain On The Sale of Certain Small Business Stock:

AMT income includes 7% of the amount excluded from gross income for the taxable year under IRC Section 1202. Section 1202 provides for an exclusion of a part of the gain from the sale or exchange of qualified small business stock (as defined in IRC Section 1202) held for more than 5 years.

Intangible Drilling Costs:

Excess intangible drilling costs are a tax preference to the extent that they exceed 65% of the net income from the oil, gas, and geothermal properties.

Excess intangible drilling costs is the excess of the intangible drilling and development costs paid for the taxable year (other than costs incurred in drilling a nonproductive well) over the amount which would have been allowable for the taxable year if such costs had been capitalized and straight line recovery had been amortized over 120 months.

Percentage Depletion:

The AMT tax preference is the excess of the allowable depletion deduction over the adjusted basis of the property at the end of the taxable year (determined without regard to the depletion deduction for the taxable year).

Accelerated Depreciation Or Depletion Of Property Placed In Service Before January 1, 1987:

The AMT preference is the excess of accelerated depreciation or depletion over straight line deduction for certain property placed in service before January 1, 1987.

III) Denial Of Certain Losses:

Denial of Farm Losses:

For AMT purposes: For purposes of computing the AMT income for any taxable year of a taxpayer other than a corporation: No loss of the taxpayer for any taxable year from any tax shelter farm activity shall be allowed. Any such disallowed loss shall be treated as a deduction allocable to such activity in the 1st succeeding taxable year.

The term tax shelter farm activity means any farming syndicate as defined in Code Section 464(c); and any other activity consisting of farming which is a passive activity within the meaning of Code Section 469(c).

For purposes of the denial of farm losses, a personal service corporation (within the meaning of Code Section 469(j)(2)) shall be treated as a taxpayer other than a corporation.

In the year of a complete disposition of a farm shelter activity, any loss attributable to such activity (determined after carryovers) shall be allowed in computing AMT income.

Passive Activity Losses:

In computing AMT income for any taxable year Code Section 469 shall apply, except that in applying said section 469 the adjustments for AMT adjustments and AMT preferences shall apply; and the passive activity loss shall be computed without regard to qualified housing interest (as defined in Code Section 56(e)). This applies to individuals, estates, trusts, and corporations which are personal service corporations or closely held corporations.

Special Rules For Tax Shelter Farm Losses and Passive Losses:

For AMT purposes the amount of disallowed losses shall be reduced by the amount by which the taxpayer is insolvent as of the end of the taxable year.

IV) Miscellaneous Definitions And Special Rules:

Loss Limits:

Re Code Section 291 Special rules relating to corporate preference items:

For AMT purposes: Except as otherwise provided Section 291 (relating to cutback of corporate preferences) shall apply before the application of the AMT.

Patron's Adjustment:

Distributions received from a cooperative may be includible in income. Unless the distributions are nontaxable, include the AMT patronage dividend adjustment reported by the cooperative (on Form 1099-PATR, etc.).

Income Eligible For Credits Under Code Sections 30A Or 936:

In the case of any corporation for which a Puerto Rico or Puerto Rico and possessions credit is allowable for the taxable year under IRC Sections 30A or 936, AMT income shall not include any income with respect to which a credit is determined under either Section 30A or 936.

Net AMT Adjustment From an Electing Large Partnership:

The adjustment (if any) is passed through as a net amount from the partnership.

Partnerships:

Regular partnerships pass through the separate items of AMT adjustments and preferences to partners as separate items.

S Corporations:

S corporations pass through the separate items of AMT adjustments and preferences to shareholders as separate items.

V) We Now Have Arrived at Alternative Minimum Taxable Income Before Exemption:

Exception: A corporation that holds a residual interest in a REMIC may have to allow for another difference.

Exemptions:

For Taxpayers Other Than Corporations:

	<u>Exemption</u>	<u>AMT Income Range Over Which It Is Phased Out</u>
Married, filing jointly or a qualifying Surviving spouse	74,450	\$150,000 to \$447,800
Single, not a surviving spouse	48,450	112,500 to 306,300
Married, filing separately	37,225	75,000 to 223,900
Estate or trust	22,500	75,000 to 160,000

For a child subject to the kiddie tax: The exemption is the lesser of 48,450 or
The child's earned income plus 6,800. This will be adjusted each year for inflation.

For Corporations:

Regular Corporations:

The exemption amount is 40,000 and the phase-out range is \$150,000 to \$310,000.

For Small Corporations:

The tentative minimum tax shall be \$0 for any corporation if its average gross receipts are \$7,500,000 for the 3 taxable years (beginning after December 31, 1993) before the current taxable year. Substitute \$5,000,000 for \$7,500,000 for the first 3 taxable year period (or portion thereof). If the corporation ceases to be a small corporation, the AMT provisions shall apply prospectively from the change date.

Subtracting The Exemption Gives The AMT Income On Which To Compute The AMT (called the Taxable Excess in the Internal Revenue Code).

Tentative Minimum Tax:

For Taxpayers Other Than Corporations:

The tax rate is 26% of the first 175,000 of the taxable excess and 28% of the taxable excess above 175,000. From this subtract the AMT foreign tax credit for the taxable year. The result is the Tentative Minimum Tax. (Note: If the taxpayer is filing as married filing separately, substitute 87,500 for 175,000 above)

For Corporations:

The tax rate is 20% of the taxable excess. From this subtract the AMT foreign tax credit for the taxable year to arrive at the Tentative Minimum Tax.

In computing the tentative minimum tax:

For non-corporate taxpayers the maximum rate of tax on net capital gain applies.

For corporate taxpayers the maximum rate of tax on qualified timber gain applies.

Alternative Minimum Tax:

The alternative minimum tax is the excess of the tentative minimum tax over the regular tax.

The regular tax is the regular tax liability for the tax year (as defined in Code Section 26(b) reduced by: the foreign tax credit and the credits allowed under Code Sections 936 and 30A. The regular tax shall not include any increase in tax under Code Sections 45(e)(11)(C) [Decrease in the amount of credit allocated to a patron of a cooperative for electricity produced from certain renewable resources]; 49(b) [Due to a net increase with

respect to the taxpayer in the amount of nonqualified non-recourse financing]; 50(a) [Recapture of investment credit]; 42(j) [Repayment of low income housing credit] or 42(k) [Application of at risk rules to the low income housing credit].

Income Averaging for Farmers and Fisherman:

Solely for purposes of calculating the AMT, Code Section 1301 (relating to averaging of farm and fishing income) shall not apply in computing the regular tax liability.

Alternative Minimum Tax Foreign Tax Credit:

The AMT foreign tax credit for any taxable year shall be the credit which would be determined for such taxable year if the pre-credit tentative minimum tax were the tax against which the credit was taken; the Code Section 904 limitation were applied on the basis of AMT income instead of regular taxable income; the determination of whether any income is high-taxed income for purposes of Section 904(d)(2) were made on the basis of AMT rates.

Credit For Prior Year Minimum Tax Liability:

A credit is allowed for the minimum tax attributable to deferral preferences (that is the excess of the AMT over the AMT attributable to non-deferral preferences) from prior years which have not been used in prior years. The amount of the carry-forward credit which may be used in a taxable year is limited to the excess of the regular tax (reduced for certain credits) over the tentative minimum tax for the taxable year. However, the credit is allowable for exclusion items of a corporation.

Special Rule For Individuals With Long-term Unused Credits:

Applies to unused credits in any taxable year which are attributable to tax years before the third tax year immediately preceding the current tax year. It applies to tax years beginning after December 20, 2006 but before January 1, 2013. It is a refundable credit. For years beginning after December 31, 2007, the refundable credit is equal to the greater of 50% of the long-term unused minimum tax credit for the tax year or the amount of the AMT refundable tax credit for the taxpayer's preceding tax year.

Exempt Organizations:

Organizations liable for tax on unrelated business taxable income may be liable for AMT. If the organization files Form 990T, take a look at the AMT possibility.

