

Suppose They Took the AM
Out of the AMT?

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Suppose They Took the AM Out of the AMT?

The individual alternative minimum tax (AMT) was originally intended to assure that high-income people paid at least some tax. But the AMT was poorly designed and affects more and more middle-income people every year. Unless the tax law changes, about 30 million taxpayers will fall prey to the complicated tax by the end of the decade.

Unfortunately, the AMT raises a lot of tax revenue: reforming or eliminating it could cost \$500 billion or more over the next decade.

These problems have led some to suggest that the best option would be to make the AMT the regular tax system, rather than an alternative. This option would have several advantages, according to its proponents. The AMT is nearly a flat-rate tax—there are only two statutory rates, 26 and 28 percent. It eliminates various special tax breaks in the regular tax system—that is, it applies to a broader base. And, over the long run, it is a more effective revenue generator than the regular income tax. Indeed, by 2009, it would cost less to eliminate the regular tax than to eliminate the AMT.

There are some problems with this analysis. First, the AMT is not really a flat tax: it has high phantom tax rates—32.5 and 35 percent—caused by the phaseout of the exempt threshold. Second, some of the base broadeners in the AMT have questionable validity as policy. For example, deductions for certain legal expenses are not allowed under the AMT, so some people who win civil damage awards with contingent legal fees can end up worse off after tax than they would have been if they had lost the lawsuit. Parents may not claim deductions for their children against the AMT. And the AMT can impose very large marriage penalties on certain households. Finally, the AMT's power as a revenue generator stems entirely from the fact that its parameters are not indexed for

inflation. In consequence, people whose incomes only just keep pace with inflation will face higher and higher average tax rates over time (a phenomenon sometimes referred to as bracket creep).

Nonetheless, the notion that taxpayers should not be subject to two tax systems has merit. This paper examines the implications of basing a reformed tax system on the AMT rules. The next section describes how the AMT works and compares the AMT's rules with those of the regular income tax system. Section II discusses various policy simulations aimed at illustrating how repealing the regular income tax, or splicing the AMT's rules onto the regular income tax structure, would affect households and revenues. Several options are designed to be approximately revenue-neutral, meaning they are admissible candidates for reform under the president's guidelines to the Tax Reform Panel.¹ Section III discusses policy implications.

I. The AMT Compared with the Regular Income Tax

How the AMT Works

The individual AMT operates parallel to the regular income tax, with a different income definition, rate structure, and allowable deductions, exemptions, and credits.² In short, after calculating their regular tax liability, taxpayers must calculate their "tentative AMT" under the alternative rules and rates and pay whichever amount is larger. To calculate tentative AMT, taxpayers determine the AMT tax base, apply the AMT tax rate and exemption phaseout schedules, and then subtract applicable credits. Technically, AMT

¹ See Executive Order 13369: President's Advisory Panel on Federal Tax Reform (Bush 2005).

² See General Accounting Office (2000), Joint Committee on Taxation (2001), and Rebelein and Tempalski (2000) for excellent summaries of AMT rules. A separate alternative minimum tax, similar in design to the individual AMT, applies to corporations. See Lyon (1997).

liability is the excess, if any, of tentative AMT above the amount of taxes due under the regular income tax alone.

AMT income: Alternative minimum taxable income (AMTI) is the sum of three components: regular taxable income for AMT purposes, AMT preferences, and AMT adjustments. Regular taxable income for AMT purposes is the same concept as taxable income used for regular tax purposes, except it is allowed to be negative if deductions exceed adjusted gross income.

An AMT preference is an item identified as a potential tax saving in the regular income tax that is not permitted in the AMT. An AMT adjustment is simply any other exclusion, exemption, deduction, credit, or other treatment (such as a method for computing depreciation) in the regular income tax that is either restricted or disallowed in the AMT. There is no interesting economic distinction between preferences and adjustments in general; we will generally refer to both as preferences. Interesting distinctions do emerge among the various preferences themselves, however.

Preferences are of two types: exemptions or deferrals. Exemption preferences broaden the AMT tax base, and include the disallowance of personal exemptions, the standard deduction, and itemized deductions for miscellaneous expenses and taxes.³ Deferral provisions change the timing of the recognition of income and deductions, typically to accelerate income and postpone deductions. Thus, they tend to raise the current-year tax base, but only at the expense of future tax bases. The most prominent

³ Other exemption items include disallowal of deductions for mortgage interest on debt not used to buy, build, or improve a home and for medical expenses between 7.5 and 10 percent of AGI. AMTI includes interest income from private activity bonds and adjusts the depletion allowances taxpayers can claim. The AMT also limits net operating loss deductions to 90 percent of AMTI (Harvey and Tempalski 1997).

among these relate to the treatment of incentive stock options, depreciation of personal property, and passive activity losses.⁴

Deferral and exemption provisions differ in use, distributional effects, revenue effects, complexity, and policy implications. A small number of exemption provisions involve widely used features of the tax code and account for the overwhelming share of the difference between regular taxable income and AMTI. In 2002, for example, state and local taxes accounted for over 50 percent of the difference, personal exemptions for 21 percent, and miscellaneous expenses above the 2 percent of AGI floor for 20 percent (table 1).

Exemption provisions are used heavily by middle-income AMT taxpayers, but are relatively simple to comply with, since they just involve adding figures to taxable income. The exemption measures might be interpreted as an effort to reduce tax incentives generally and move toward an alternative tax simpler than the regular system.

Deferral preferences differ considerably from exemption items. Relative to exemption preferences, there are more deferral items in the code, but they are used much less frequently, tend to be used by high-income taxpayers, and generate much less revenue. Deferral items tend to be complex as taxpayers generally need to recalculate income and costs using different schedules and keep separate books for regular tax and AMT. Also, taxpayers may use AMT liability created by deferral provisions, but not by exemption provisions, as a credit against future years' regular tax liability in excess of the tentative AMT. The deferral provisions, coupled with the credit they create, are

⁴ Other deferral items include some of the excluded capital gain on small business stock; farm shelter activity losses; retiming of income from long-term contracts; and costs associated with intangible drilling, research and experimentation, mining exploration, circulation expenses, and amortization of pollution control facilities (Harvey and Tempalski 1997).

consistent with a policy goal of having every high-income filer pay some positive tax in each year, even if his or her overall multiyear tax liability does not change.

AMT exemption: Exemptions in the AMT are neither indexed for inflation nor adjusted for family size. For tax years before 2001 and after 2005, the AMT exemption is \$45,000 for married couples filing jointly and for surviving spouses, \$33,750 for unmarried individuals other than surviving spouses, and \$22,500 for married individuals filing separately. Since 2001, temporary measures have increased the exemptions, which are set at \$58,000, \$40,275, and \$29,000, respectively, through 2005. AMT exemptions phase out for high-income taxpayers at a rate of 25 cents per dollar of AMTI over thresholds of \$150,000 for joint returns, \$112,500 for singles, and \$75,000 for married individuals filing separately. The thresholds are not indexed for inflation.⁵

AMT tax rates: Pre-credit tentative AMT liability is determined by imposing the AMT tax rate schedule and the exemption phaseout schedule on the AMT tax base. The statutory AMT tax rate is 26 percent on the first \$175,000 in AMT tax base for married couples or singles (\$87,500 for married taxpayers filing separately) and 28 percent on additional amounts. The phaseout of the exemption, noted above, makes the effective marginal tax rate one-fourth larger than the statutory rate through the phaseout range. AMT tax brackets are not indexed for inflation. The AMT generally preserves the lower tax rates on capital gains and dividends in the regular tax.

⁵ Besides the rules noted above, married taxpayers who file separately must also increase their AMTI by an amount equal to the phaseout rate of the AMT exemption (25 percent) times the amount that their AMTI exceeds the income level at which the exemption is completely phased out, up to a maximum equal to the married filing separately exemption amount. The purpose of this provision is to eliminate any AMT advantage of filing separately.

Subtract foreign tax credits: After determining pre-credit tentative AMT liability above, taxpayers subtract foreign tax credits (FTC) to calculate tentative AMT liability.

AMT liability: AMT liability is the excess, if any, of the tentative AMT liability over a tax liability measure based on the regular income tax. The latter measure is regular income tax liability before credits (that is, the tax due on adjusted gross income minus allowable exemptions and deductions) less any taxes due because of lump-sum distributions and less any applicable FTC in the regular tax. For simplicity, we refer to this measure as regular tax liability for AMT purposes.

AMT and the use of regular tax credits: After calculating regular tax liability for AMT purposes and AMT liability, taxpayers return to the 1040 to calculate applicable credits. The AMT does not restrict the use of personal refundable credits—the earned income tax credit and the child credit. Through 2005, all personal nonrefundable credits can be used to reduce personal income tax liabilities regardless of the AMT.⁶ After 2005, all these credits other than the adoption, child, and savers tax credits are allowed only to the extent that the individual’s regular tax liability exceeds the tentative AMT liability. The general business credit can reduce tax only to the level of tentative AMT liability, but unused portions may be carried backward or forward to other tax years. Taxpayers whose ability to use credits is limited by their tentative AMT liability are said to have “lost credits.” Finally, as noted above, payment of AMT creates a regular income tax credit for future years to the extent that the AMT liability is the result of timing-related preferences or adjustments.

⁶ The credits include the child and dependent care tax credit; the credit for the elderly and disabled; the adoption, child, HOPE, lifetime learning, savers, and D.C. homebuyers credits; and the credit for interest on certain home mortgages (Joint Committee on Taxation 2005).

Differences between the AMT and Regular Income Tax

As is evident from the previous discussion, the AMT creates significant complexities for affected taxpayers. But what would the AMT look like as a stand-alone tax? Table 2 compares the major features of the AMT with the regular tax rules. To start with, the AMT has similar top rates to the regular income tax. The top four rates under the regular income tax are 25, 28, 33, and 35 percent. Under the AMT, the four effective rates are 26, 28, 32.5, and 35 percent. A notable difference, however, is that the top AMT rates do not apply to the highest-income taxpayers, because they are created by the phaseout of the AMT exemption. Beyond that phaseout range (AMTI of \$150,000 to \$382,000 for married filing joint taxpayers), the marginal tax rate is 28 percent.⁷ Perhaps even more important, the rate brackets and the AMT exemption (the amount of income for which a tax rate of zero applies) are not indexed for inflation, meaning the relatively high AMT tax rates apply at lower and lower real incomes over time.

Figure 1 compares the rate schedules under the AMT and the regular tax in 2004 for a married couple filing a joint return with two children and all income from wages (that is, the simplest case for comparison). The family is eligible for a standard deduction of \$9,700 and personal exemptions of \$3,100 per person under the regular tax (for a total exemption of \$22,100 under the regular tax), but not under the AMT. Instead, the family may claim a flat \$58,000 exemption. Another difference is that the family may claim the standard deduction only if it chooses not to itemize deductions, whereas the AMT exemption applies regardless of itemization status. A further distinction is that all these

⁷ After 2005, the upper end of the range is scheduled to fall to \$330,000 when the exemption returns to pre-EGTRRA levels.

regular income tax parameters are indexed for inflation whereas none of the AMT parameters are indexed.

The AMT thus applies at substantially higher income for this couple in 2004—\$58,000 compared with \$22,100 under the regular income tax.⁸ However, the AMT immediately applies higher tax rates—26 percent compared with only 15 percent under the regular income tax. Tax rates are surprisingly similar for taxpayers with incomes between about \$80,000 and \$380,000. As noted, at very high incomes, the regular income tax assesses higher rates.

Over time, however, the AMT will be applying at lower real income levels under current law. First, the AMT exemption is set to return to its pre-2001 level starting in 2006. Second, the AMT exemption and other parameters are not indexed for inflation, whereas all the regular income tax parameters relevant to figure 1 are indexed. In consequence, the couple illustrated in figure 1 will become subject to the 26 percent AMT tax rate at an income of less than \$38,000 in 2004 dollars by 2010, assuming an inflation rate of 3 percent a year. That is, the AMT schedule will slide steadily to the left over time. It will also get more compressed because the thresholds for the 28 percent tax bracket and the exemption phaseout are not indexed. This explains why more middle-income households will be subject to the AMT over time, and also why the vast majority of AMT taxpayers will face higher marginal tax rates than they would under the regular income tax by 2010 (Burman et al. 2004).

⁸ In fact, this family would not have positive income tax liability until its income was significantly higher if it qualified for the child tax credit. Since that credit is allowed against both the AMT and the regular tax, it would not affect the qualitative comparison between the two tax bases.

Another difference between the AMT and the regular income tax concerns how they treat heads of household and married couples compared with singles. The regular income tax generally applies lower tax rates to a head of household than to a single with the same income; married filing joint returns qualify for the lowest tax rates. Married filing joint returns may also claim a standard deduction twice as large as that of a single filer; the standard deduction for a head of household lies between those two levels.

The AMT, in contrast, makes no distinction between heads of households and singles. Effectively, the benefits of head of household status are treated as an AMT preference item. The AMT exemption is higher for married filing joint returns than singles, but it is not twice as large. Moreover, the tax rates and exemption phaseout apply at exactly the same level of AMTI regardless of filing status. Thus, under the AMT, two single taxpayers who marry may face much higher tax rates simply because they marry. That is, they can face marriage penalties, which generally are larger than they would be under the regular income tax.⁹

The other differences between the AMT and regular income tax shown in table 2 have to do with preference items, which are added back into AMTI, as discussed above. Effectively, these items are allowed against the regular income tax, but disallowed or subject to further restrictions under the AMT. For example, state and local taxes and miscellaneous itemized deductions are disallowed against the AMT. Unreimbursed medical expenses are subject to a higher floor under the AMT than the regular income tax

⁹ Although the elimination of head of household status tends to reduce the size of marriage penalties (since single heads of household do not qualify for a special tax benefit under the AMT), the fact that rate schedules and exemption phaseouts are not adjusted for filing status and that the exemption is not twice as large for a married couple as for a single filer means that substantial marriage penalties can result if it qualified for the child tax credit or the earned income credit.

(10 percent versus 7.5 percent of AGI) and mortgage interest is only deductible to the extent that the mortgage is used to build, purchase, or improve a home.

In summary, the alternative minimum tax would have certain drawbacks as a stand-alone tax. First, it is not indexed for inflation, creating bracket creep. Second, most taxpayers with AMTI above the exemption threshold face higher marginal tax rates under the AMT than they would under the regular income tax, and those higher tax rates are applying at lower and lower real incomes over time. Third, the AMT can create significant marriage penalties. Fourth, although the AMT is more progressive than the regular income tax, it is becoming less so over time (Burman et al. 2004). Moreover, since the tax rate that applies to the highest-income households is significantly lower under the AMT than under the regular income tax, the AMT is significantly less progressive at the very top of the income distribution.

II. Policy Simulations

We now examine some policy alternatives that would eliminate either the AMT or the regular income tax.¹⁰ For comparison purposes, first consider the effect of simply repealing the AMT. In 2010, the peak year for AMT participation over the next ten years (assuming that the 2001–03 tax cuts are allowed to expire as scheduled after 2010), the AMT would affect almost 30 million tax units and raise about \$100 billion in that year.¹¹ Repealing the AMT would cut taxes on 18 percent of tax units, by an average of about

¹⁰ All estimates in this paper are based on CBO's microsimulation tax model. The estimates differ slightly from those reported in Burman (2005) because of differences in underlying datasets and modeling assumptions. The small differences are well within the range of statistical uncertainty.

¹¹ The estimates calculated here are changes in liability assuming no changes in behavior. The changes in revenue are estimated for 2010, but the cost of reform for a given proposal will tend to vary over time because, under current law, the AMT has a differential impact over time.

\$3,400 (see table 3). Overall, the tax cut would average \$628, or a little over 1 percent of gross income.

The biggest beneficiaries in dollar terms would be those with incomes over \$1 million, but the largest gains as a percentage of income would apply to those with incomes between \$200,000 and \$500,000. Over 97 percent of tax units in that income category would experience tax cuts, averaging 3.3 percent of income. Those with incomes between \$100,000 and \$200,000 would also gain a great deal. More than 82 percent would get a tax cut, averaging \$2,622. Overall, the tax cut would average about 1.6 percent of income in that income group. In addition, families with children would be the largest winners from this policy (Burman et al. 2004). Without an AMT in place, more than twice as many households would receive a marriage bonus (that is, pay lower taxes by virtue of being married) as a marriage penalty. Compared with current law, more than 7 percent of couples would switch from suffering a marriage penalty to receiving a marriage bonus.

If the regular income tax were instead eliminated along with all tax credits other than the foreign tax credit, income tax revenues would decline by \$66 billion in calendar year 2010 (before accounting for any behavioral response).¹² It is interesting to note that this is less than the revenue raised by the alternative minimum tax that year (\$101 billion). This policy would change the distribution of tax burdens significantly. Tax units with incomes below \$20,000 would lose because of the elimination of refundable tax credits (see table 4). The biggest winners would be those with incomes between \$30,000

¹² The estimates in this paper are static changes in tax liabilities. Unlike revenue estimates produced by the Joint Committee on Taxation or the Treasury Department, they do not account for behavioral responses. Thus, the actual effect on tax revenues could be larger or smaller than the static estimates.

and \$50,000, who would receive an income tax cut worth 3.5 percent or more of income, and people with incomes over \$1 million, who would now face a much lower marginal tax rate (28 percent versus 35 percent under current law). Nearly 25 percent of tax units would pay higher taxes, averaging \$2,041 in 2010, while about 45 percent would pay lower taxes by almost the same amount (\$2,013).¹³

Eliminating the regular income tax would increase slightly the percentage of couples suffering marriage penalties—from 36 to 38 percent—but it would slash the number with bonuses—from 56 to 31 percent. It would also increase average marginal tax rates (weighted by earnings) of middle-class households. Those with incomes between \$40,000 and \$50,000 would face an average tax rate of 19.9 percent under the option, compared with 19.1 percent under current law. Tax units with incomes between \$50,000 and \$75,000 would see their average marginal tax rate increase from 20.3 percent to 24.8 percent. On the other hand, people with very high and very low incomes would see lower marginal rates. Tax units with incomes over \$1 million would see their effective rate drop from 34.4 percent to 27.9 percent; those with incomes under \$30,000 would see their average rate drop to 0.5 percent or less. Overall, average marginal tax rates would decline by 1.3 percentage points.

The tax increases in table 4 could be eliminated by retaining the current law tax credits while repealing the regular tax. Table 5 shows that under such a scenario, static tax liability would decline by \$165 billion in 2010, but there would be no tax increases. More than half of tax units would get a tax cut, averaging \$1,903. People with incomes below \$30,000 would be largely exempt from tax. The tax cut would average 5.7 percent

¹³ Loss of refundable tax credits is included in the tax increase estimate.

of income for those with incomes between \$30,000 and \$40,000 and over 4 percent for those with incomes between \$20,000 and \$50,000. Again, taxpayers with incomes over \$1 million would gain most, receiving an average tax cut of \$77,425 or 2.6 percent of income. Interestingly, restoring the tax credits would increase both marriage penalties and bonuses, by close to 7 percentage points. Again, more households would suffer penalties than receive bonuses.

Indexing the AMT exemption and rate brackets would eliminate one of its primary flaws but would be very expensive. If in addition to eliminating the regular tax the parameters of the AMT were indexed for inflation beginning in 2006, revenues would lower by over \$410 billion in 2010 alone (see table 6). This simulation illustrates that the AMT's power as a revenue generator largely stems from inflation-induced bracket creep. In this simulation, tax units with incomes under \$40,000 in 2010 are totally exempt. The option would convey a tax cut worth about 7 percent of income for households with incomes between \$30,000 and \$75,000. Interestingly, a tiny fraction of households actually face a tax increase under this proposal. These households are married filing separate returns, which can end up paying more tax because of the odd formula used for phasing out the AMT exemption.¹⁴

Table 7 takes on another major defect of the AMT—its large marriage penalties. In this simulation, in addition to indexing the AMT exemption level, the exemption for couples is twice the level for singles, and a single flat 28 percent tax rate applies with no exemption phaseout. This option would reduce income tax liabilities by \$578 billion in 2010, reducing taxes by \$3,600 on average. People with incomes between \$75,000 and

¹⁴ See footnote 6.

\$100,000 would receive the largest tax cut as a share of income (8.2 percent), but income classes between \$30,000 and \$200,000 would all get tax cuts worth over 6 percent of income. Marriage bonuses would outnumber penalties by almost three to one.

What would it take to make the option in table 7 revenue-neutral (before accounting for behavioral response)? One answer is a very high flat tax rate—49 percent (table 8). This option would shift the tax burden dramatically away from low- and middle-income tax units onto those with high incomes. Almost all tax units with incomes under \$75,000, and most with incomes below \$200,000, would pay lower taxes under the revenue-neutral option, but almost all tax units with higher incomes would pay more taxes. The average tax increase would be \$363,000 for those with incomes over \$1 million. This option would, like the previous one, eliminate most marriage penalties and increase bonuses. Not surprisingly, it would also substantially increase average marginal tax rates, which would take a toll on economic efficiency.

The AMT exemption for couples was set at twice the single level in tables 7 and 8. If instead the single exemption is reduced to eliminate marriage penalties, the revenue neutral flat rate falls to 37 percent. In this scenario, more tax units face higher taxes, but the average tax increase for those who pay higher taxes is less than one-third as much (see table 9). Similarly, fewer households experience tax cuts. There is a slight increase in households with both marriage penalties and bonuses, probably because the income tax changes are smaller relative to credits, which can create both bonuses and penalties.

The final option in this set would eliminate the special preferential rate for capital gains in 2010.¹⁵ This option would simplify tax compliance and remove a major element behind some tax shelter schemes. For that reason, preferential capital gains tax rates were considered an AMT preference item until 1987, when the Tax Reform Act of 1986 (temporarily) eliminated the capital gains tax preference under the regular tax. If capital gains are taxed at the same 37 percent rate as other income, the option could raise \$67 billion that could be applied to deficit reduction. Alternatively, the additional revenues could be used to lower the tax rate to achieve revenue neutrality.

This option would significantly increase tax burdens on those with incomes over \$100,000, and especially on those with incomes over \$1 million, who would see an average tax increase of almost 7 percent of income (table 10). More than 99 percent of those with incomes over \$200,000 would pay higher taxes. Low- and middle-income households would pay lower taxes, and this option would have virtually the same effect on marriage penalties as the previous one.

Of course, the regular income tax already has many of the desirable properties that the previous options would splice onto the AMT base: its parameters are indexed for inflation and its marriage penalties are relatively small and uncommon. In addition, most people pay relatively low marginal tax rates (fewer than 1 percent pay statutory rates in excess of 25 percent) and the regular income tax rate schedule is more consistently progressive than the AMT rate schedule (see figure 1).

¹⁵ Note that the lower capital gains tax rates also apply to dividends until 2008, but that tax break, enacted in 2003, is currently set to expire before 2010. As with the previous estimate, this estimate assumes no change in realization behavior.

Table 11 examines the effects of repealing the AMT but maintaining the base broadeners that may be related to tax shelter activity—the timing preferences and adjustments.¹⁶ This option would reduce slightly the revenue cost of repeal, from \$101 billion in table 3 to \$96 billion. The change is small because timing preferences do not raise much revenue directly. It is possible, however, that they stem revenue losses due to tax avoidance that could make the actual revenue comparisons more significant. About 3.5 percent of households would pay higher taxes under this option based on our static estimates.

The last option would also disallow the middle-class tax preferences under the regular income tax, so the regular income tax base would include virtually all items in the AMT tax base. The one exception is that the standard deduction and exemptions for taxpayers (but not dependents) would be retained. This option would still reduce static revenues by \$41 billion in 2010. Compared with current law, it would increase taxes on households in high-tax states, those with children, and those with large miscellaneous deductions, such as legal fees for tort damage awards. However, these additions were also in the previous options to eliminate the regular income tax. Under this scenario, most people with incomes over \$100,000 get a tax cut, but few people with incomes under \$75,000 would. On average, those with incomes under \$75,000 pay higher taxes, averaging less than 1 percent of income. Although those with incomes over \$1 million pay lower taxes on average, they get a much smaller average tax cut than they would under the options that repealed the regular income tax.

¹⁶ The estimates in the table assume that only tax units on the AMT would have timing preferences if they were disallowed under the regular income tax. This is almost surely not true, but we have no way of measuring these items for those not on the AMT.

III. Discussion

Some have suggested that making the AMT the only tax could be an easy way to reform our tax system. Our analysis suggests this is not so. Simply eliminating the regular income tax would sacrifice substantial revenues, especially if the income tax credits are retained, and could produce significant marriage penalties and higher marginal tax rates (exacerbated by bracket creep) that could discourage working and saving and encourage inefficient tax avoidance behavior. It would also substantially reduce tax burdens for those most able to pay tax.

Some of those problems could be mitigated by indexing the AMT parameters for inflation and moving toward a flat rate tax, but the required tax rate to raise the same amount of revenue in 2010 would be significant. A lower tax rate would be possible if long-term capital gains were taxed at the same rate as other income, but that proposal would raise a host of other political and policy issues (see Burman 1999). The bottom line is that there is no simple solution.

Would removing the “AM” from the AMT make the tax system much simpler? The main benefit comes from reducing two tax calculations to one, but one could achieve that gain just as well from eliminating the AMT. There is some simplification from eliminating the preference items, but most of those do not apply to most taxpayers (and the ones that do apply widely have constituencies that would make it hard to eliminate them). Even if the regular tax rate schedule and significant AMT preferences were eliminated, much of the complexity of the tax code would remain. The tax code would still retain, for example, the rules for reporting business income and deductions along with the particular eligibility rules for each tax credit.

One could simplify further by eliminating some of the complexity in the regular tax, for example, by replacing the alternate capital gains tax rates with a flat percentage exclusion. But those simplifications could be done just as well to the regular tax without scrapping it, so again the case is far from clear.

Some argue that the AMT is more efficient because it applies low, relatively flat rates to a broad tax base. In fact, the high exemption means that the AMT base is often smaller than the regular income tax base. And the phaseout of the AMT exemption creates effective tax rates as high as the highest statutory rate under the regular income tax.

The taxation of preference items under the AMT could make it more neutral among different activities (and allow rates to be lower than they would be, given the high exemption), but many preference items are missing from the list—most notably, capital gains. Moreover, some preference items may be unwarranted. For example, depreciation is slower under the AMT than under the regular income tax, but the U.S. Department of the Treasury (2000) concluded that depreciation for most assets was probably about right on average. Thus, the AMT depreciation schedule may move AMTI farther away from economic income.

Is the AMT tax base fairer? The AMT is more progressive than the regular tax, but it is becoming less so over time. And eliminating the regular tax would provide the largest tax cuts to tax units earning over \$1 million.

The AMT does improve horizontal equity on several dimensions—for example, between families with children and those without, and between residents of high-tax and

low-tax states. However, both those equity gains might be viewed as losses if the tax preferences for children or state and local taxes are deemed to have merit.

The AMT reduces equity on other dimensions. For example, those with certain damage awards can be taxed at rates of 100 percent or more on their net income, while those with other kinds of awards are taxed at only their statutory rate (Johnston 2003). Individuals who exercised stock options at the peak of the stock market and who do not have substantial other assets can be much worse off than those who exercised at a more propitious time and sold their stock before the market crashed. And the AMT can produce significant marriage penalties, although those can be eliminated through design changes.

In sum, the AMT could be the basis for a better tax system, but not without significant structural changes. Absent those changes, it would make more sense to reform the income tax minus the AMT than to eliminate the regular income tax and repair the AMT.

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Table 1. Reconciling AMTI and Taxable Income for AMT Taxpayers in 2002

	Number of taxpayers with AMT preference (millions)	Amount (\$ millions)	Percentage of all preferences
Taxable income from Form 1040 (including negative amounts)		317,144	
+ AMT adjustments and preferences			
1 State and local tax deductions	2.0	42,103	51.1
2 Personal exemptions	1.9	17,801	21.6
3 Miscellaneous deductions above the 2-percent floor	1.0	16,741	20.3
4 Regular tax NOLs	0.0	9,811	11.9
5 Incentive stock options	0.0	1,987	2.4
6 Passive activity loss	0.3	1,197	1.5
7 Standard deduction	0.2	1,026	1.2
8 Post-1986 depreciation	0.3	965	1.2
9 Beneficiaries of estates	0.1	478	0.6
10 Private activity bond interest	0.1	437	0.5
11 Medical deductions	0.2	414	0.5
12 Long-term contracts	0.0	397	0.5
13 Other and related	0.0	351	0.4
14 Capital gains exclusion (section 1202)	0.0	224	0.3
15 Depletion	0.0	193	0.2
16 Loss limitations	0.0	179	0.2
17 Certain home-mortgage interest	0.0	163	0.2
18 Intangible drilling costs	0.0	68	0.1
19 Circulation expenses	0.0	5	0.0
20 R&E expenditures	0.0	5	0.0
21 Mining costs	0.0	2	0.0
22 Large partnerships	0.0	0	0.0
23 Installment sales	0.0	-3	0.0
24 Investment interest	0.0	-67	-0.1
25 Disposition of property	0.2	-1,257	-1.5
26 State and local tax refunds	1.0	-2,409	-2.9
27 AMT NOLs	0.0	-3,383	-4.1
28 Limit on itemized deduction under regular tax	1.1	-5,313	-6.5
29 Undetermined		211	0.3
Total preferences and adjustments	2.2	82,326	100.0
= AMTI		400,496	

Source: Office of Tax Analysis, Department of the Treasury (unpublished tabulation).

Note: AMT taxpayers are those affected by the AMT, including those who lose tax credits.

Table 2. Regular Tax and Alternative Minimum Tax Provisions

Provisions	Treatment under regular tax	Treatment under AMT
Marginal tax rates	10%, 15%, 25%, 28%, 33%, and 35%. Brackets are indexed for inflation.	26% and 28% (32.5% and 35% for taxpayers in the phaseout range of exemptions). Not indexed for inflation.
Standard deduction/exemption	Deduction of \$9,700 for married taxpayers filing jointly, \$4,850 for single taxpayers, and \$7,150 for heads of households allowed in 2004 for those who do not itemize deductions. Indexed for inflation.	AMT exemption (equivalent to a deduction) of \$58,000 for married taxpayers filing jointly and \$40,275 for single taxpayers and heads of household in 2005; \$45,000 and \$33,750 thereafter (not indexed for inflation). Exemption phases out at 25% rate for high-income taxpayers.
Personal exemptions	Deduction of \$3,100 per family member and dependent allowed against regular tax in 2004. Indexed for inflation. Phased out for high-income taxpayers.	Not allowed.
Head of household status	Single heads of household qualify for lower tax rates and larger standard deductions than singles.	Heads of household face the same tax rates and AMT exemption as singles.
Itemized deductions	Allowed under regular tax if standard deduction is not taken. Itemized deductions phase out at 3% rate for taxpayers with higher incomes (certain items do not phase out).	If deductions are itemized under regular tax, tax preference items are subtracted from the deductions for AMT purposes. No phaseout for higher-income taxpayers.
State and local tax deductions	Income and property taxes are allowed as itemized deductions. Sales taxes are allowed for 2004 and 2005.	Not allowed.
Miscellaneous deductions	Miscellaneous expenses including tax preparation fees, unreimbursed employment expenses, and certain legal fees in excess of 2% of AGI are allowed as itemized deductions.	Not deductible.
Home mortgage interest	Mortgage interest for the first or second home and second mortgages and home equity lines are deductible subject to certain limits.	Only deductible if the proceeds are used to improve, buy, or build the taxpayer's home.
Unreimbursed medical expenses	Expenses in excess of 7.5% of AGI are allowed as itemized deductions.	Expenses in excess of 10% of AGI are allowed as itemized deductions.
Treatment of capital gains and dividends	Dividends and capital gains taxed at 5% and 15% from 2005 to 2008; 0% and 15% in 2008. Capital gains taxed at 10% and 20% from 2009 onwards while dividends are taxed as regular income.	Same.
Net operating loss	Deducted from taxable income.	Not deductible, but may be carried forward to offset future income.
Incentive stock options	Exercising an ISO generates no tax liability. Selling the stock generates capital gains taxes on the difference of the sale price and the option price.	Exercising a stock option generates taxable income equal to the difference between the exercise price and the option price if the stock is not sold within the same year. Selling the stock generates capital gains taxes on the difference between the sale price and the exercise price.
Other timing preferences	Depreciation of equipment, oil depletion allowances, allowances for intangible drilling costs, or mining exploration and development costs are allowed under regular tax.	Deductions for timing preferences are allowed at a slower rate under the AMT. These preferences generate the AMT credit, which can be taken against regular tax liability in the future years. However, these credits cannot be used to lower regular tax liability below the tentative liability for that year.
Child, adoption, and savers credits	Allowed against regular tax.	Allowed against AMT until 2010. (Savers credit expires after 2006.)
Refundable credits	Allowed against regular tax.	Same.
Foreign tax credit	Allowed against regular tax.	Same.
Nonrefundable personal credits other than above	Allowed against regular tax.	Allowed against AMT through 2005. Not allowed thereafter.
Business tax credits	Allowed against regular tax.	Only certain ones allowed.

Table 3. Effects of Repealing the AMT, by AGI, 2010

AGI (\$ thousands)	% of tax units	% of income tax	Change in Tax						Marriage Penalty		Marginal Tax Rate on Earnings	
			Average (\$)	As % of income	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law	Under option
					% of tax units	Average (\$)	% of tax units	Average (\$)				
Less than 0	1.1	0.0	-27	0.0	0.0	0	0.1	-46,000	9.3	40.2	-0.5	-0.7
0-10	21.4	-0.6	-1	0.0	0.0	0	0.0	-39,000	7.2	15.4	-3.2	-3.2
10-20	12.8	-1.5	0	0.0	0.0	0	0.0	0	9.1	83.4	5.9	5.9
20-30	11.5	0.2	0	0.0	0.0	0	0.0	-571	10.7	87.8	16.9	16.9
30-40	9.3	2.1	-5	0.0	0.0	0	1.1	-461	13.3	85.8	18.2	18.0
40-50	7.6	3.2	-26	-0.1	0.0	0	3.6	-709	23.6	75.3	19.1	18.8
50-75	13.8	10.1	-122	-0.2	0.0	0	14.3	-852	39.7	58.8	20.3	18.9
75-100	8.5	9.9	-668	-0.8	0.0	0	51.7	-1,292	30.6	69.2	24.2	20.5
100-200	10.8	25.5	-2,154	-1.6	0.0	0	82.1	-2,622	39.9	60.0	28.7	26.4
200-500	2.6	17.9	-9,310	-3.3	0.0	0	97.4	-9,563	43.9	56.0	32.8	31.4
500-1,000	0.4	9.3	-8,728	-1.3	0.0	0	61.5	-14,195	44.9	55.1	31.3	35.1
More than 1,000	0.2	24.1	-18,235	-0.6	0.0	0	23.0	-79,437	56.5	43.5	34.4	35.0
All	100.0	100.0	-628	-1.1	0.0	0	18.4	-3,406	28.4	63.1	24.7	23.4

Addendum: Static change in liability = -\$101 billion

Notes: Simulations show distribution of tax changes for nondependent tax units age 18 or over in calendar year 2010. Tax changes are on a liability basis and do not account for behavioral responses. They are not revenue estimates. Marriage penalty and bonus calculations apply only to married filing joint tax units. They assume that the alternative to marriage is a divorce in which the lesser-earning spouse claims all children as dependents and nonlabor income is split equally. See Weiner and Williams (1997) for discussion and alternative models. The marginal tax rates on earnings are weighted by earnings.

Table 4. Effects of Repealing the Regular Tax and Credits (except Foreign Tax Credit), by AGI, 2010

AGI (\$ thousands)	Change in Tax						Marriage Penalty		Marginal Tax Rate on Earnings			
	% of tax units	% of income tax	Tax Increase			Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)	
			Average (\$)	As % of income	% of tax units	Average (\$)	% of tax units					Average (\$)
Less than 0	1.1	0.0	347	-0.4	24.2	1,430	0.0	0	0.0	17.8	-0.5	0.1
0-10	21.4	0.0	209	8.1	20.2	1,094	7.6	-156	0.0	0.8	-3.2	0.0
10-20	12.8	0.0	902	6.0	35.3	3,400	49.7	-596	0.0	0.9	5.9	0.0
20-30	11.5	0.0	-84	-0.3	30.2	2,939	66.5	-1,461	0.0	2.5	16.9	0.5
30-40	9.3	0.4	-1,332	-3.8	19.6	1,992	78.4	-2,197	0.0	30.9	18.2	11.5
40-50	7.6	1.6	-1,580	-3.5	15.6	1,343	81.8	-2,189	12.7	58.5	19.1	19.9
50-75	13.8	8.2	-1,050	-1.7	21.5	1,567	72.5	-1,913	45.1	50.6	20.3	24.8
75-100	8.5	10.3	-48	-0.1	33.8	1,703	40.5	-1,537	61.7	37.9	24.2	26.1
100-200	10.8	28.0	150	0.1	24.8	1,490	19.2	-1,144	67.7	32.2	28.7	28.0
200-500	2.6	20.5	-5	0.0	7.1	877	7.0	-965	63.3	36.6	32.8	32.7
500-1,000	0.4	9.4	-3,919	-0.6	3.1	955	41.4	-9,545	68.9	30.9	31.3	28.1
More than 1,000	0.2	21.7	-74,077	-2.5	0.5	1,000	78.1	-94,855	76.2	23.8	34.4	27.9
All	100.0	100.0	-414	-0.7	24.3	2,041	45.2	-2,013	37.9	30.7	24.7	23.4

Addendum: Static change in liability = -\$66 billion

Note: This option would repeal the regular income tax and all tax credits except for the foreign tax credit, leaving the AMT as the default tax system. See notes to table 3 for assumptions underlying simulations.

Table 5. Effects of Repealing Regular Tax, but Retaining Tax Credits, by AGI, 2010

AGI (\$ thousands)	Change in Tax								Marriage Penalty		Marginal Tax Rate on Earnings	
	% of tax units	% of income tax	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)		
			Average (\$)	As % of income	% of tax units	Average (\$)						
Less than 0	1.1	0.0	-2	0.0	0.0	0	0.0	0	11.5	32.4	-0.5	-0.5
0-10	21.4	-0.7	-12	-0.5	0.0	0	8.5	-139	7.5	14.1	-3.2	-5.7
10-20	12.8	-2.2	-310	-2.1	0.0	0	54.2	-571	14.7	45.3	5.9	-1.1
20-30	11.5	-1.6	-1,121	-4.5	0.0	0	86.3	-1,299	15.8	33.6	16.9	5.2
30-40	9.3	-0.4	-1,993	-5.7	0.0	0	94.7	-2,104	18.3	49.5	18.2	14.6
40-50	7.6	1.2	-2,062	-4.6	0.0	0	95.3	-2,165	24.3	60.2	19.1	20.1
50-75	13.8	7.7	-1,625	-2.6	0.0	0	86.5	-1,879	50.0	47.1	20.3	24.7
75-100	8.5	10.4	-715	-0.8	0.0	0	52.4	-1,365	64.8	34.8	24.2	26.7
100-200	10.8	29.8	-233	-0.2	0.0	0	21.9	-1,065	70.0	30.0	28.7	28.9
200-500	2.6	22.2	-164	-0.1	0.0	0	9.8	-1,675	64.2	35.7	32.8	32.7
500-1,000	0.4	10.1	-4,485	-0.7	0.0	0	45.4	-9,887	69.1	30.8	31.3	28.1
More than 1,000	0.2	23.5	-77,425	-2.6	0.0	0	81.0	-95,583	75.9	23.8	34.4	27.9
All	100.0	100.0	-1,030	-1.8	0.0	0	54.1	-1,903	44.8	37.2	24.7	24.0

Addendum: Static change in liability = -\$165 billion

Note: This option would repeal the regular income tax, but allow current law tax credits against the AMT, which would be the default tax system. See notes to table 3 for assumptions underlying simulations.

Table 6. Effects of Option in Table 5 Plus Indexing Brackets after 2005, by AGI, 2010

AGI (\$ thousands)	Change in Tax								Marriage Penalty		Marginal Tax Rate on Earnings	
	% of tax units	% of income tax	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)		
			Average (\$)	As % of income	% of tax units	Average (\$)						
Less than 0	1.1	-0.1	-5	0.0	0.0	0	0.1	-8,000	12.1	30.4	-0.5	-0.6
0-10	21.4	-0.8	-12	-0.5	0.0	0	8.5	-140	7.5	13.9	-3.2	-5.7
10-20	12.8	-2.8	-310	-2.1	0.0	0	54.2	-571	14.7	45.1	5.9	-1.1
20-30	11.5	-2.1	-1,136	-4.6	0.0	0	86.3	-1,315	15.9	32.8	16.9	4.7
30-40	9.3	-1.0	-2,293	-6.6	0.0	0	95.7	-2,395	20.3	33.8	18.2	4.4
40-50	7.6	-0.3	-3,456	-7.7	0.0	0	98.4	-3,510	24.9	36.8	19.1	7.3
50-75	13.8	2.9	-4,426	-7.2	0.0	0	99.3	-4,458	31.8	48.8	20.3	15.0
75-100	8.5	6.8	-4,936	-5.7	0.0	0	99.8	-4,945	45.8	51.8	24.2	24.5
100-200	10.8	28.8	-5,030	-3.8	0.0	0	99.9	-5,037	59.5	40.3	28.7	27.9
200-500	2.6	25.8	-5,619	-2.0	0.2	2,000	99.2	-5,669	56.5	43.4	32.8	33.4
500-1,000	0.4	12.9	-4,912	-0.7	0.6	2,250	95.1	-5,175	69.1	30.8	31.3	28.2
More than 1,000	0.2	29.9	-77,747	-2.6	0.5	2,500	94.7	-82,092	76.2	23.5	34.4	27.9
All	100.0	100.0	-2,571	-4.4	0.0	2,067	71.2	-3,611	36.1	40.2	24.7	20.7

Addendum: Static change in liability = -\$412 billion

Notes: This option would repeal the regular income tax, index the AMT exemption and tax brackets after 2005, and allow current law tax credits against the AMT. See notes to table 3 for assumptions underlying simulations.

Table 7. Effects of Option in Table 6 Plus Eliminating Exemption Phaseout, Flat 28 Percent Rate, and Eliminating Marriage Penalties, by AGI, 2010

AGI (\$ thousands)	% of tax units		% of income tax		Change in Tax				Marriage Penalty		Marginal Tax Rate on Earnings	
					Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)
					Average (\$)	As % of income	% of tax units	Average (\$)				
Less than 0	1.1	-0.1	-8	0.0	0.0	0	0.1	-13,000	12.0	30.5	-0.5	-0.6
0-10	21.4	-1.0	-12	-0.5	0.0	0	8.5	-140	7.5	13.9	-3.2	-5.7
10-20	12.8	-3.4	-310	-2.1	0.0	0	54.2	-571	14.7	45.1	5.9	-1.1
20-30	11.5	-2.6	-1,136	-4.6	0.0	0	86.3	-1,316	15.9	32.8	16.9	4.7
30-40	9.3	-1.2	-2,292	-6.6	0.0	0	95.7	-2,394	20.3	33.8	18.2	4.5
40-50	7.6	-0.4	-3,441	-7.7	0.0	0	98.4	-3,495	24.8	36.9	19.1	7.8
50-75	13.8	3.6	-4,446	-7.2	0.0	0	99.3	-4,478	24.2	51.4	20.3	12.6
75-100	8.5	4.3	-7,047	-8.2	0.0	0	99.8	-7,061	4.4	85.7	24.2	10.8
100-200	10.8	24.7	-9,535	-7.1	0.0	0	99.9	-9,547	18.8	80.3	28.7	27.1
200-500	2.6	26.5	-14,834	-5.2	0.0	0	99.9	-14,852	36.4	62.9	32.8	28.1
500-1,000	0.4	14.0	-24,074	-3.6	0.0	0	100.0	-24,074	41.7	58.0	31.3	28.0
More than 1,000	0.2	35.7	-96,760	-3.2	0.0	0	99.7	-97,016	57.5	42.2	34.4	27.9
All	100.0	100.0	-3,602	-6.1	0.0	0	71.3	-5,055	17.8	56.3	24.7	17.7

Addendum: Static change in liability = -\$578 billion

Notes: This option would repeal the regular income tax, set the AMT exemption for married filing joint returns equal to twice the exemption level for singles, eliminate the AMT exemption phaseout, apply a single 28-percent tax rate, index the AMT exemption amounts after 2005, and allow current law tax credits against the AMT. See notes to table 3 for assumptions underlying simulations.

Table 8. Effects of Option in Table 7 with 49 Percent Flat Rate, by AGI, 2010

AGI (\$ thousands)	Change in Tax						Marriage Penalty		Marginal Tax Rate on Earnings			
	% of tax units	% of income tax	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)		
			Average (\$)	As % of income	% of tax units	Average (\$)						
Less than 0	1.1	0.0	4	0.0	0.0	0	0.1	-4,000	12.0	30.5	-0.5	-0.5
0-10	21.4	-0.6	-11	-0.4	0.0	22,000	8.5	-139	7.5	13.9	-3.2	-5.7
10-20	12.8	-1.9	-310	-2.1	0.0	0	54.2	-571	14.7	45.1	5.9	-1.1
20-30	11.5	-1.5	-1,136	-4.6	0.0	0	86.3	-1,315	15.9	32.8	16.9	4.7
30-40	9.3	-0.7	-2,276	-6.5	0.0	0	95.7	-2,378	20.3	33.8	18.2	4.9
40-50	7.6	-0.1	-3,279	-7.3	1.1	621	97.3	-3,375	24.7	37.0	19.1	13.7
50-75	13.8	4.1	-3,210	-5.2	11.4	1,491	87.9	-3,845	22.0	53.6	20.3	22.0
75-100	8.5	4.7	-4,934	-5.7	26.0	4,119	73.8	-8,132	3.0	87.1	24.2	18.9
100-200	10.8	24.3	-1,677	-1.3	35.1	7,962	64.8	-6,904	18.0	81.2	28.7	46.8
200-500	2.6	25.5	18,976	6.7	93.5	21,003	6.4	-10,117	35.2	64.1	32.8	49.3
500-1,000	0.4	13.4	78,324	11.6	94.7	83,547	5.1	-15,833	41.2	58.5	31.3	49.4
More than 1,000	0.2	32.8	340,430	11.4	94.2	363,207	5.5	-30,571	56.8	42.9	34.4	49.1
All	100.0	100.0	-46	-0.1	10.7	19,412	60.6	-3,497	17.0	57.2	24.7	30.6

Addendum: Static change in liability = -\$8 billion

Notes: This option is approximately revenue neutral in 2010: it would repeal the regular income tax, set the AMT exemption for married filing joint returns to twice the exemption level for singles, eliminate the AMT exemption phaseout, apply a single 49-percent tax rate, index the AMT exemption amounts after 2005, and allow current law tax credits against the AMT. See notes to Table 3 for assumptions underlying simulations.

Table 9. Effects of Option in Table 8 but with Smaller Exemptions and 37-Percent Flat Rate, by AGI, 2010

AGI (\$ thousands)	Change in Tax								Marriage Penalty		Marginal Tax Rate on Earnings	
	% of tax units	% of income tax	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)		
			Average (\$)	As % of income	% of tax units	Average (\$)						
Less than 0	1.1	0.0	1	0.0	0.0	0	0.1	-4,000	11.2	33.5	-0.5	-0.5
0-10	21.4	-0.6	-11	-0.4	0.0	12,000	8.5	-139	7.4	14.1	-3.2	-5.7
10-20	12.8	-1.9	-310	-2.1	0.0	0	54.2	-571	14.6	45.4	5.9	-1.1
20-30	11.5	-1.5	-1,135	-4.6	0.0	0	86.3	-1,315	15.8	34.1	16.9	4.7
30-40	9.3	-0.1	-1,746	-5.0	1.3	312	94.5	-1,853	17.3	54.5	18.2	22.8
40-50	7.6	1.8	-1,261	-2.8	12.7	918	85.8	-1,606	15.2	65.8	19.1	24.4
50-75	13.8	6.8	-1,613	-2.6	39.5	1,696	59.8	-3,819	11.0	82.2	20.3	23.0
75-100	8.5	8.2	-1,523	-1.8	28.8	4,011	71.0	-3,775	12.1	86.2	24.2	34.8
100-200	10.8	28.9	1,885	1.4	61.9	4,141	38.0	-1,787	32.7	65.9	28.7	38.1
200-500	2.6	22.0	8,053	2.8	93.6	9,048	6.3	-6,485	41.9	57.1	32.8	37.3
500-1,000	0.4	10.6	28,140	4.2	93.9	30,740	6.1	-11,651	45.2	54.6	31.3	37.3
More than 1,000	0.2	25.7	98,404	3.3	93.4	107,511	6.6	-30,560	59.7	40.0	34.4	37.0
All	100.0	100.0	-19	0.0	18.7	5,650	52.6	-2,046	19.3	61.6	24.7	29.5

Addendum: Static change in liability = -\$3 billion

Notes: This option is approximately revenue neutral in 2010: it would repeal the regular income tax, set the AMT exemption for single returns at half the current law exemption level for married filing joint returns, eliminate the AMT exemption phaseout, apply a single 37 percent tax rate, index the AMT exemption amounts after 2005, and allow current law tax credits against the AMT. See notes to table 3 for assumptions underlying simulations.

Table 10. Effects of Options in Table 9 but with no Preferential Capital Gains Tax Rate, by AGI, 2010

AGI (\$ thousands)	Change in Tax								Marriage Penalty		Marginal Tax Rate on Earnings	
	% of tax units	% of income tax	Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)		
			Average (\$)	As % of income	% of tax units	Average (\$)						
Less than 0	1.1	0.0	6	0.0	0.1	14,000	0.1	-3,000	11.2	33.5	-0.5	-0.5
0-10	21.4	-0.5	-11	-0.4	0.0	12,000	8.5	-139	7.4	14.1	-3.2	-5.7
10-20	12.8	-1.8	-310	-2.1	0.0	0	54.2	-571	14.6	45.4	5.9	-1.1
20-30	11.5	-1.4	-1,135	-4.6	0.0	0	86.3	-1,315	15.8	34.1	16.9	4.7
30-40	9.3	-0.1	-1,740	-5.0	1.4	307	94.4	-1,847	17.3	54.6	18.2	22.8
40-50	7.6	1.8	-1,236	-2.8	13.3	904	85.1	-1,593	15.2	65.8	19.1	24.4
50-75	13.8	6.5	-1,568	-2.5	40.2	1,732	59.1	-3,831	11.0	82.2	20.3	23.1
75-100	8.5	8.0	-1,384	-1.6	29.6	4,102	70.2	-3,705	12.3	86.0	24.2	34.8
100-200	10.8	28.0	2,333	1.7	65.2	4,429	34.6	-1,604	33.0	65.7	28.7	38.1
200-500	2.6	21.7	10,716	3.8	99.4	10,811	0.5	-7,421	43.1	55.8	32.8	37.3
500-1,000	0.4	10.6	38,447	5.7	99.6	38,702	0.3	-31,500	47.7	51.9	31.3	37.4
More than 1,000	0.2	27.3	205,897	6.9	99.5	207,464	0.5	-89,500	64.1	35.9	34.4	37.2
All	100.0	100.0	417	0.7	19.5	7,460	51.8	-1,997	19.5	61.4	24.7	29.6

Addendum: Static change in liability = \$67 billion.

Notes: This option would repeal the regular income tax, set the AMT exemption for single returns at half the current law exemption level for married filing joint returns, eliminate the AMT exemption phaseout, apply a single 37 percent tax rate, index the AMT exemption amounts after 2005, tax long-term capital gains as ordinary income, and allow current law tax credits against the AMT.

See notes to table 3 for assumptions underlying simulations.

Table 11. Effects of Repealing AMT and Adding Back AMT Timing Preferences and Adjustments to Regular Taxable Income, by AGI, 2010

AGI (\$ thousands)	% of tax units	% of income tax	Change in Tax						Marriage Penalty		Marginal Tax Rate on Earnings	
			Tax Increase			Tax Cut			% with penalty	% with bonus	Current law (%)	Under option (%)
			Average (\$)	As % of income	% of tax units	Average (\$)	% of tax units	Average (\$)				
Less than 0	1.1	0.0	-1	0.0	0.1	5,000	0.1	-7,000	9.5	40.0	-0.5	-0.5
0-10	21.4	-0.6	0	0.0	0.0	0	0.0	0	7.2	15.4	-3.2	-3.2
10-20	12.8	-1.5	1	0.0	1.2	48	0.0	0	9.1	83.5	5.9	6.0
20-30	11.5	0.2	3	0.0	3.8	72	0.0	-286	10.7	87.8	16.9	16.9
30-40	9.3	2.1	2	0.0	6.0	108	1.1	-367	13.5	85.7	18.2	18.0
40-50	7.6	3.2	-14	0.0	7.6	148	3.6	-699	23.7	75.3	19.1	18.8
50-75	13.8	10.1	-101	-0.2	7.7	224	14.2	-832	39.8	58.7	20.3	18.9
75-100	8.5	9.9	-637	-0.7	6.1	304	51.0	-1,286	30.6	69.2	24.2	20.6
100-200	10.8	25.4	-2,100	-1.6	1.7	495	81.6	-2,584	40.1	59.9	28.7	26.4
200-500	2.6	17.9	-9,048	-3.2	0.3	5,231	97.2	-9,326	44.2	55.8	32.8	31.4
500-1,000	0.4	9.4	-7,789	-1.1	0.9	15,500	60.8	-13,035	45.5	54.5	31.3	35.1
More than 1,000	0.2	24.1	-15,689	-0.5	0.8	86,333	22.2	-73,869	57.1	42.9	34.4	35.0
All	100.0	100.0	-597	-1.0	3.5	267	18.3	-3,317	28.5	63.0	24.7	23.4

Addendum: Static change in liability = -\$96 billion

Notes: This option would repeal the AMT but apply AMT rules with respect to timing preferences (e.g., AMT depreciation schedules) under the regular income tax. See notes to table 3 for assumptions underlying simulations.

**Table 12. Effects of Option in Table 11 Plus Repealing Deductions for State and Local Taxes,
Miscellaneous Itemized Deductions, and Dependent Exemptions, by AGI, 2010**

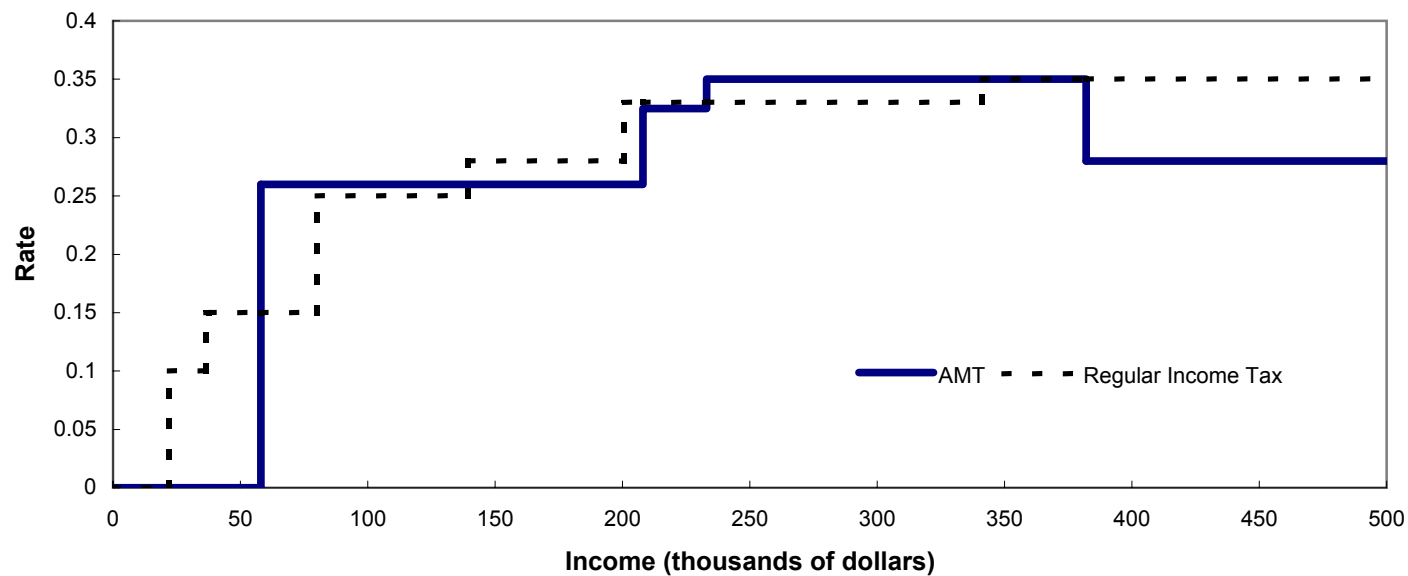
AGI (\$ thousands)	Change in Tax						Marriage Penalty		Marginal Tax Rate on Earnings			
	% of tax units		% of income tax		Tax Increase		Tax Cut		% with penalty	% with bonus	Current law (%)	Under option (%)
					Average (\$)	As % of income	Average (\$)	% of tax units				
Less than 0	1.1	0.0	0	0.0	0.1	3,500	0.1	-7,000	9.5	40.0	-0.5	-0.5
0-10	21.4	-0.6	0	0.0	0.0	0	0.0	-71	7.2	15.4	-3.2	-3.2
10-20	12.8	-1.4	29	0.2	10.1	286	0.8	-39	9.2	83.5	5.9	7.1
20-30	11.5	0.4	187	0.8	34.8	541	2.0	-75	11.3	87.2	16.9	18.9
30-40	9.3	2.3	294	0.8	39.6	755	4.6	-105	16.8	82.4	18.2	18.9
40-50	7.6	3.4	335	0.8	41.1	859	8.4	-211	28.0	71.0	19.1	19.4
50-75	13.8	10.5	368	0.6	46.5	853	11.4	-255	44.4	54.3	20.3	19.4
75-100	8.5	10.1	-19	0.0	37.7	764	45.2	-679	41.3	58.5	24.2	21.6
100-200	10.8	25.7	-1,136	-0.9	14.5	611	76.4	-1,603	49.4	50.6	28.7	26.7
200-500	2.6	17.6	-7,753	-2.7	1.1	2,565	97.4	-7,989	48.0	52.0	32.8	31.5
500-1,000	0.4	9.0	-6,415	-0.9	22.3	3,186	66.0	-10,786	46.7	53.3	31.3	35.1
More than 1,000	0.2	23.0	-15,132	-0.5	32.2	8,164	50.1	-35,426	55.2	44.8	34.4	34.9
All	100.0	100.0	-257	-0.4	23.5	761	17.9	-2,429	33.8	57.7	24.7	23.9

Addendum: Static change in liability = -\$41 billion

Notes: This option would repeal the AMT but apply AMT rules with respect to timing preferences (e.g., AMT depreciation schedules) under the regular income tax, and repeal the deductions for state and local taxes, miscellaneous itemized deductions, and dependent personal exemptions.

See notes to table 3 for assumptions underlying simulations.

**Figure 1. AMT Rate Schedule for Couples
Compared with Regular Tax Schedule, 2004**



Notes: Figure assumes married couple filing jointly with two children claiming standard deduction against regular income tax and no other deductions or credits. All income is from wages. Figure does not show the effect of the personal exemption and itemized deduction phaseouts under the regular tax.

Appendix Table 1. Statistics for Households under Current Law, by AGI, 2010

AGI (\$ thousands)	All				Married Filing Jointly						
	Returns (thous.)	Taxpayers (thous.)	Income (\$ mill.)	Income tax paid (\$ mill.)	Returns (thous.)	Marriage Penalty			Marriage Bonus		
						Returns (thous.)	% with penalty	Tax paid (\$ mill.)	Returns (thous.)	% with bonus	Tax paid (\$ mill.)
Less than 0	1,699	1	-132,075	-543	642	60	9.3	21	258	40.2	-2,760
0-10	34,376	2,620	88,754	-7,141	5,650	408	7.2	99	872	15.4	-1,629
10-20	20,525	10,207	308,779	-18,516	4,552	416	9.1	129	3,797	83.4	-7,599
20-30	18,448	12,289	458,791	1,826	4,644	499	10.7	138	4,076	87.8	-9,588
30-40	14,847	11,970	517,909	24,934	4,074	543	13.3	436	3,498	85.9	-8,605
40-50	12,137	11,030	543,371	39,084	4,061	961	23.7	1,257	3,059	75.3	-7,818
50-75	22,185	21,457	1,365,851	124,597	11,093	4,465	40.3	6,000	6,468	58.3	-21,057
75-100	13,694	13,616	1,181,783	128,290	9,606	4,251	44.3	5,629	5,349	55.7	-19,633
100-200	17,259	17,234	2,309,671	344,730	14,060	8,267	58.8	22,431	5,789	41.2	-29,593
200-500	4,095	4,090	1,161,921	254,467	3,458	2,170	62.8	15,143	1,288	37.2	-13,155
500-1,000	701	701	474,727	118,901	595	266	44.7	1,823	329	55.3	-7,071
More than 1,000	379	378	1,128,653	297,717	315	146	46.3	1,982	169	53.7	-11,740
All	160,345	105,595	9,408,134	1,308,345	62,750	22,451	35.8	55,089	34,951	55.7	-140,245

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