Key Elements of the U.S. Tax System

Q. What is the AMT?

A. The individual alternative minimum tax (AMT) operates alongside the regular income tax. It requires some taxpayers to calculate their liability twice—once under the rules for the regular income tax and once under the AMT rules—and then pay the higher amount. Originally in-tended to prevent perceived abuses by a handful of the very rich, the AMT affected roughly 5 million filers in 2017. The Tax Cuts and Jobs Act dramatically reduced the reach of the AMT, albeit temporarily, so that the tax will hit only 200,000 filers in 2018.

In January 1969, Treasury Secretary Joseph W. Barr informed Congress that 155 taxpayers with incomes exceeding $200,000 had paid no federal income tax in 1966. The news created outrage. That year, members of Congress received more constituent letters about the 155 taxpayers than about the Vietnam War. Congress subsequently enacted an "add-on" minimum tax that house-holds paid in addition to regular income tax. It applied to certain income items ("preferences") taxed lightly or not at all under the regular income tax. The largest preference item was the por-tion of capital gains excluded from the regular income tax.

Congress enacted the modern alternative minimum tax (AMT) in 1979 to operate in tandem with the add-on minimum tax. The main preference items, including capital gains, moved from the add-on tax to the AMT. Congress finally repealed the add-on tax, effective in 1983.

The original minimum tax and the AMT affected fewer than 1 million taxpayers annually through the late 1990s. In 2001, Congress passed the Economic Growth and Tax Relief Reconciliation Act, which substantially reduced regular income taxes but provided only temporary relief from the AMT. Over the following decade, Congress repeatedly passed legislation—often at the last possible moment—to temporarily "patch" the AMT by increasing the AMT exemption amount.

Although the patches prevented an AMT explosion, the number of taxpayers affected by the AMT continued to grow throughout the decade (figure 1) because (1) the regular income tax was indexed for inflation, but the AMT was not; and (2) Congress enacted substantial cuts to the regular income tax.

The American Taxpayer Relief Act of 2012 enacted a permanent AMT fix by establishing a higher AMT exemption amount, indexing the AMT parameters for inflation, and allowing specified tax credits under the AMT. As a result, the number of AMT taxpayers fell from 4.5 million in 2012 to about 4.0 million in 2013. That number grew modestly to 5.0 million in 2017.

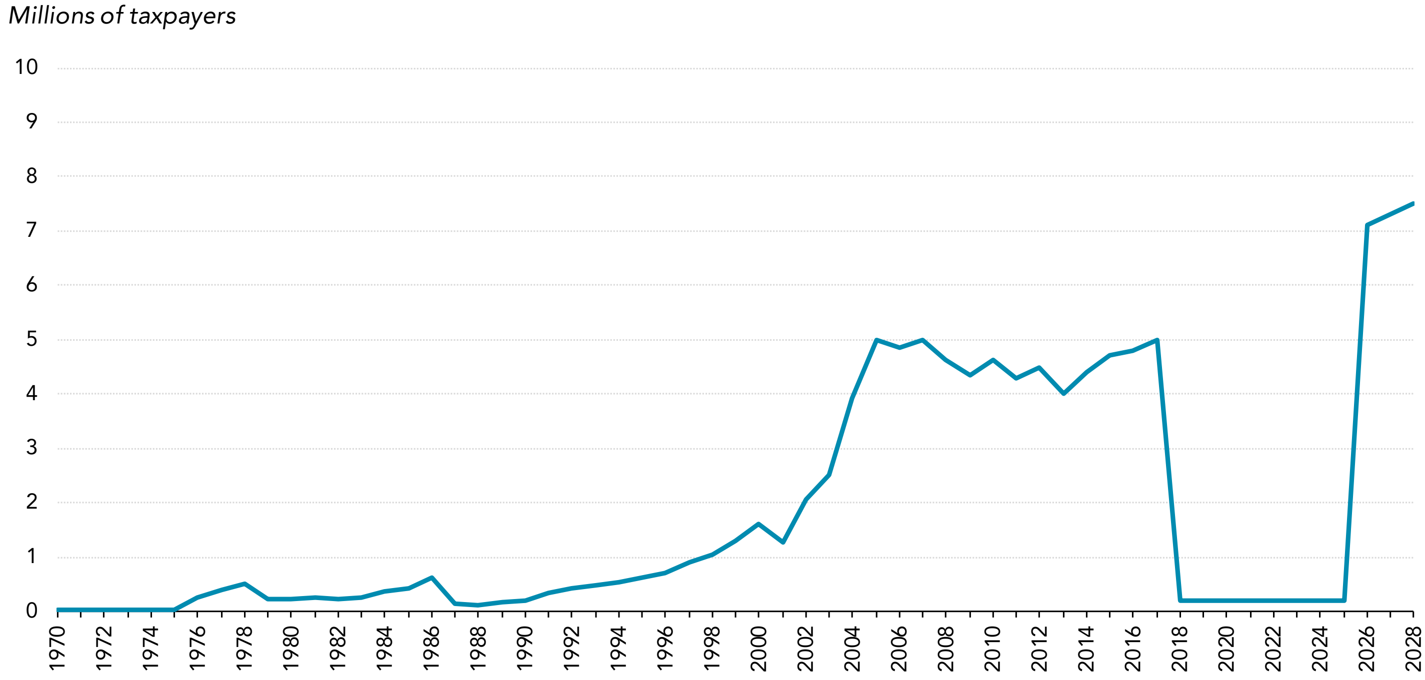
Key Elements of the U.S. Tax System

What is the AMT?

FIGURE 1

Alternative Minimum Tax

Number of taxpayers affected, 1970–2028



Source: Urban-Brookings Tax Policy Center Microsimulation Model (versions 0304-3, 0308-4, 1006-1, 0613-1, 0718-1); Harvey and Tempalski (1997); private communication from Jerry Tempalski; and SOI Division of Internal Revenue Service.
Note: Data includes those with direct AMT liability on Form 6251, those with lost credits, and (for years 2001-2028) those with a reduced deduction. Tax units that are dependents of other taxpayers are excluded from the analysis.

The 2017 Tax Cuts and Jobs Act (TCJA), included provisions that significantly reduced the im-pact of the AMT. TCJA enacted a higher AMT exemption and a large increase in the income at which the exemption begins to phase out. It also repealed or scaled back some of the largest AMT preference items—personal exemptions, the state and local tax deduction, and miscellane-ous deductions subject to the 2 percent of adjusted gross income floor—further limiting the AMT's scope. As a result, TPC projects that the number of AMT taxpayers will fall to just 200,000 in 2018 and remain roughly constant through 2025.

The AMT provisions, along with almost all other individual income tax measures in TCJA, are set to expire at the end of 2025. Thus, barring legislation from Congress, the AMT will return in force in 2026, affecting 7.1 million taxpayers. That number will rise to 7.5 million by 2028.

Key Elements of the U.S. Tax System

What is the AMT?

STRUCTURE

After calculating their regular income tax, some middle- and upper-income taxpayers must add AMT "preference items" to their taxable income, subtract an AMT exemption amount, and recal-culate their tax using the AMT tax rate structure. AMT liability is the excess, if any, of this amount over the amount of tax owed under the regular income tax rules.

Before the enactment of TCJA, some of the larger AMT preference items included the deduction for state and local taxes (62 percent of all preferences in 2012 according to data from the US Department of the Treasury), personal exemptions (21 percent), and the deduction for miscella-neous business expenses (9.5 percent). Because TCJA temporarily repealed the latter two provi-sions and capped the deduction for state and local taxes at $10,000, other preferences, such as the standard deduction and the special AMT rules for the treatment of net operating losses, de-preciation, and passive losses, will become more important through 2025.

The AMT exemption for 2018 is $109,400 for married couples filing jointly, up from $84,500 in 2017 (table 1). For singles and heads of household, the exemption rises from $54,300 in 2017 to $70,300 in 2018.

The AMT has two tax rates. In 2018, the first $191,100 of income above the exemption is taxed at a 26 percent rate, and income above that amount is taxed at 28 percent. The AMT exemption begins to phase out at $1 million for married couples filing jointly and $500,000 for singles, heads of household, and married couples filing separate returns. TCJA dramatically increased the exemption phaseout threshold, which was $160,900 for married couples ($120,700 for singles and heads of households) in 2017. Because the exemption phases out at a 25 percent rate, it cre-ates a top effective AMT tax rate of 35 percent (125 percent of 28 percent). All values are in cur-rent dollars, and the 2018 values are indexed annually for inflation using the chain-weighted con-sumer price index.

TABLE 1

Alternative Minimum Tax (AMT) Parameters

Dollars, 2017 and 2018

AMT Parameter	Single	Married Filing Jointly	Head of Household	Married Filing Separately
			2018	
Exemption	$70,300	$109,400	$70,300	$54,700
28 Percent Bracket Threshold	$191,100	$191,100	$191,000	$95,500
Exemption Phaseout Threshold	$500,000	$1,000,000	$500,000	$500,000
			2017	
Exemption	$54,300	$84,500	$54,300	$42,250
28 Percent Bracket Threshold	$187,800	$187,800	$187,800	$93,900
Exemption Phaseout Threshold	$120,700	$160,900	$120,700	$80,450

Source: Internal Revenue Code.
Note: All parameters are indexed annually for inflation.

Key Elements of the U.S. Tax System

What is the AMT?

Data Sources

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Q. Who pays the AMT?

A. Before the 2017 Tax Cuts and Jobs Act (TCJA), the individual alternative minimum tax (AMT) primarily affected well-off households, but not those with the very highest incomes. It was also more likely to hit taxpayers with large families, those who were married, and those who lived in high-tax states. TCJA shields almost all upper-middle and high-income taxpayers from the reach of the AMT. The AMT is now most likely to hit those at the top of the income scale who are engaged in certain sheltering activities.

Taxpayers pay the higher of their tax calculated under regular income tax rules or under the rules for the alternative minimum tax (AMT). In 2017—before enactment of the Tax Cuts and Jobs Act (TCJA)— the 39.6 percent top rate under the regular income tax was much higher than the 28 percent top statutory AMT rate. Thus, households with very high incomes who did not at-tempt to shelter much income typically paid the regular income tax. Households not at the very top of the income scale but still with high income faced somewhat lower statutory tax rates under the regular tax and were therefore more likely to pay the AMT.

Only about 3 percent of households overall were on the AMT in 2017 but the percentage was much higher among high-income groups. The AMT increased taxes for 27.2 percent of house-holds with "expanded cash income" (a broad measure of income) between $200,000 and $500,000, 61.9 percent of those with incomes between $500,000 and $1 million, and 20.6 per-cent of households with incomes greater than $1 million.

THE AMT AFTER TCJA

TCJA enacted a higher AMT exemption and a large increase in the income at which the exemp-tion begins to phase out. The act also repealed or scaled back some of the largest AMT "prefer-ence items"—items allowable under the regular tax but not the AMT—such as personal exemp-tions, job-related and other miscellaneous expenses, and the deduction for state and local taxes. As a result, TCJA shielded almost all upper-middle and high-income taxpayers from the AMT. The tax is now most likely to affect those at the top of the income scale who take advantage of certain tax shelters allowed under the regular tax but not the AMT.

In 2018, the AMT will impact just 0.1 percent of households overall. This includes 0.4 percent of households with income between $200,000 and $500,000, 2.2 percent of those with incomes be-tween $500,000 and $1 million, and 11.5 percent of households with incomes greater than $1 million (table 1).

Key Elements of the U.S. Tax System

Who pays the AMT?

TABLE 1

Share of Tax Units Affected by the AMT

Expanded cash income (2018$)[a]	2017	2018	2025	2026
Less than $50,000	*	*	*	*
$50,000 – $75,000	*	*	*	0.1%
$75,000 – $100,000	0.3%	*	*	0.3%
$100,000 – $200,000	1.9%	*	*	2.6%
$200,000 – $500,000	27.2%	0.4%	0.3%	29.5%
$500,000 – $1,000,000	61.9%	2.2%	1.9%	61.9%
More than $1,000,000	20.6%	11.5%	8.7%	16.8%

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0718-1).
Notes: Includes AMT liability on Form 6251, lost credits, and the value of reduced deductions. Tax units that are dependents of other tax units are excluded fom the analysis.
(a) Tax units with negative adjusted gross income are excluded from their respective income classes but are included in the totals.
* Less than 0.05%

The AMT provisions in TCJA, along with almost all of its other individual income tax measures, are set to expire at the end of 2025. Thus, barring congressional legislation, the AMT will return in force in 2026. It will increase taxes for almost 30 percent of taxpayers in the $200,000 to $500,000 income range and more than 60 percent of those with incomes between $500,000 and $1 million. It will again be less likely to affect those at the top of the income scale, hitting only about 17 percent of taxpayers with incomes greater than $1 million.

THE AMT AND MARRIAGE PENALTIES

Under the regular income tax, many married couples receive a "marriage bonus" because they pay less tax than they would if they were single. This is not true under the AMT, which imposes sig-nificant marriage penalties. AMT tax brackets are identical for married and single taxpayers, and the AMT exemption for married couples is only about one and a half times as large as the exemp-tion for singles.

In contrast, the standard deduction for married couples under the regular income tax is twice that for singles, and all but the highest tax brackets for married couples are twice as wide as those for singles. TCJA reduced AMT marriage penalties somewhat by increasing and adjusting the in-come at which the exemption begins to phase out so that it is twice as large for married couples as for singles. AMT marriage penalties, combined with married couples tending to have higher incomes than single individuals, make married couples more likely to pay the AMT than singles (table 2).

Key Elements of the U.S. Tax System

Who pays the AMT?

TABLE 2

Share of Tax Units Affected by the AMT

Filing status	2017	2018	2025	2026
Single	1.0%	*	*	1.3%
Married filing jointly	5.6%	0.2%	0.2%	7.5%
Head of household	2.1%	*	*	2.8%
Married filing separately	7.1%	0.4%	0.3%	8.1%

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0718-1).
(a) Includes AMT liability on Form 6251, lost credits, and the value of reduced deductions. Tax units that are dependents of other tax units are excluded fom the analysis.
* Less than 0.05%

Data Sources

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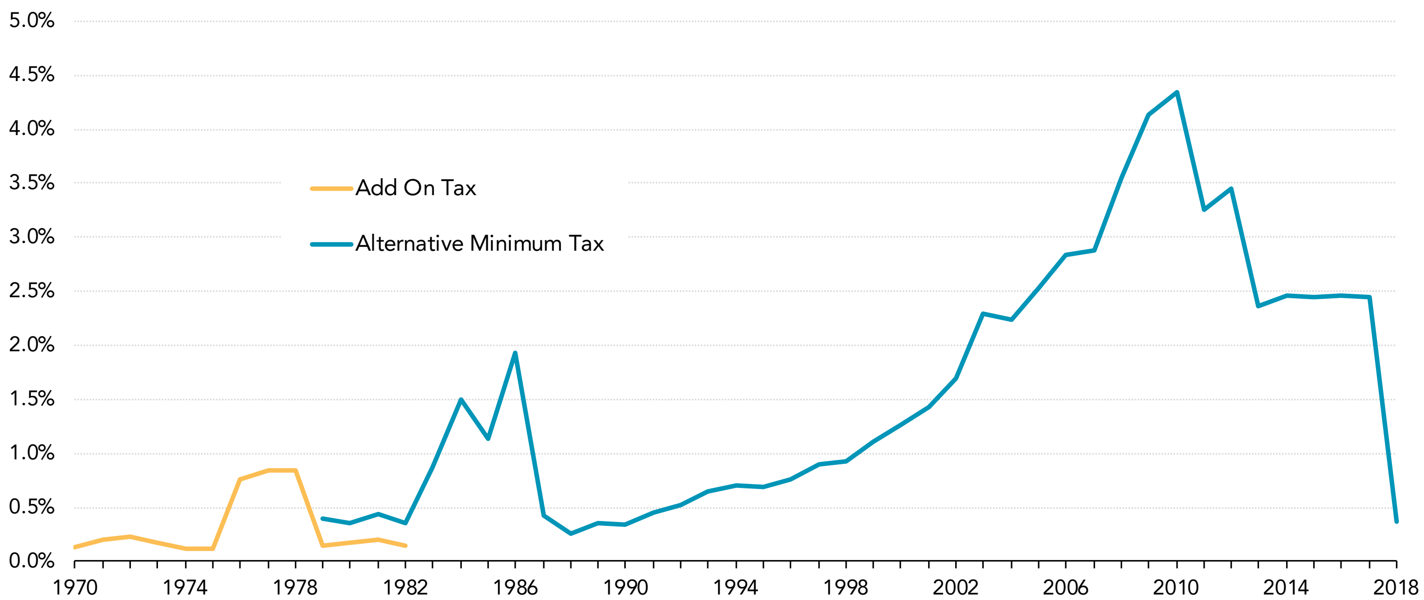
Q. How much revenue does the AMT raise?

A. About $5.2 billion in 2018, or 0.4 percent of all individual income tax revenue. That is down significantly from $36.2 billion—2.4 percent of income tax revenue—in 2017, primarily be-cause of the 2017 Tax Cuts and Jobs Act (TCJA). Since most TCJA individual income tax provisions expire at the end of 2025, AMT revenue will soar to $68.9 billion by 2028, or 2.6 percent of all individual income tax revenue.

Congress enacted the original minimum tax in 1969. It was an "add-on" tax households paid in addition to any regular income tax they owed. It applied to certain income items ("preferences") taxed lightly or not at all under the regular income tax. The largest preference item was the por-tion of capital gains excluded from the regular income tax. Revenue from the add-on tax grew from $122 million (0.14 percent of aggregate individual income tax revenue) in 1970 to $1.5 billion (0.84 percent) by 1978 (figure 1).

FIGURE 1
Individual Alternative Minimum Tax Revenue as a Share of All Individual Income Tax Revenue
1970–2018



Source: Urban-Brookings Tax Policy Center Microsimulation Model (versions 0304-3, 1006-1, 0308-7, 0309-1, 0509-2, 0411-1, 0718-1); Harvey and Tempalski (1997); private communication from Jerry Tempalski; IRS.

Key Elements of the U.S. Tax System

How much revenue does the AMT raise?

Congress enacted the modern individual alternative minimum tax (AMT) in 1979 to operate alongside the add-on minimum tax. The main preference items, including capital gains, moved from the add-on tax to the new AMT. As a result, revenue from the add-on tax plummeted to $300 million in 1979. Congress subsequently repealed the add-on tax, effective in 1983. Revenue from the new AMT climbed rapidly from $870 million (about 0.4 percent of all individual income tax revenue) in its inaugural year of 1979 to $6.7 billion (2.0 percent) in 1986.

The Tax Reform Act of 1986 (TRA86) changed both the regular income tax and the AMT. The TRA eliminated much tax-sheltering activity and thus shifted much of the AMT base to the regu-lar income tax system. In particular, TRA86 eliminated the partial exclusion of capital gains, which had accounted for 85 percent of total AMT preferences in 1985. As a result, AMT revenue fell to $1.7 billion in 1987, back to the same 0.4 percent of aggregate individual income tax reve-nue that it had raised in 1979.

Unlike the regular income tax system, Congress did not index the AMT for inflation. Each year, the standard deduction, personal exemptions, and tax bracket thresholds in the regular income tax would rise to keep pace with inflation. In contrast, the AMT exemption and brackets stayed fixed. Thus, over time, as a taxpayer's income rose with inflation, AMT liability rose relative to regular income tax liability. Because taxpayers paid the larger of the two taxes, inflation pushed more people onto the AMT, and AMT revenue increased steadily after 1987.

In 2001, Congress passed the Economic Growth and Tax Relief Reconciliation Act, which sub-stantially reduced regular income taxes but provided only temporary relief from the AMT. Over the following decade, Congress repeatedly passed legislation—known as the AMT "patch"—to prevent an explosion in the number of AMT payers. Despite the annual patches, AMT revenue continued to grow, reaching $37.6 billion—or 3.5 percent of individual income tax revenue—in 2012.

The American Taxpayer Relief Act of 2012 (ATRA) enacted an AMT "fix" by establishing a higher AMT exemption, indexing the AMT parameters for inflation, and allowing certain tax credits under the AMT. Combined with the fact that ATRA raised regular income taxes on high-income taxpayers, the permanent AMT fix reduced AMT revenue to $27 billion, or 2.4 percent of income tax revenue, in 2013.

The 2017 Tax Cuts and Jobs Act (TCJA), included provisions that greatly reduce the revenue the AMT will generate. For 2018, TCJA enacted a higher AMT exemption and a large increase in the income level at which the exemption begins to phase out. It also repealed or scaled back some of the largest AMT preference items, further limiting the tax's scope. As a result, AMT revenue will fall from $36.2 billion in 2017 to just $5.2 billion in 2018—a drop from 2.4 percent to 0.4 percent of all individual income tax revenue.

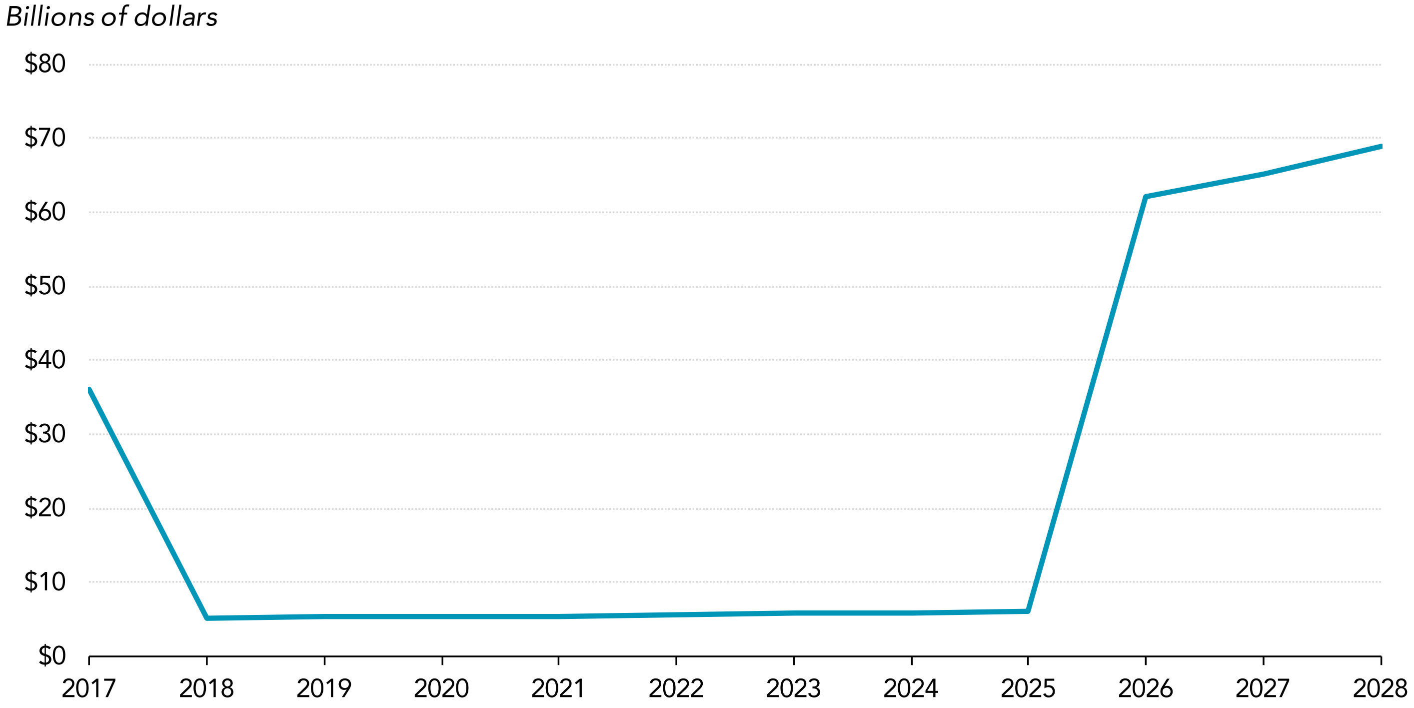
PROJECTIONS

The AMT provisions in TCJA, along with almost all its other individual income tax measures, are set to expire at the end of 2025. Thus, barring new legislation, AMT revenue will explode from $6.2 billion in 2025 to $62.1 billion in 2026. It will continue to rise to $68.9 billion—2.6 percent of all individual income tax revenue—by 2028 (figure 2).

Key Elements of the U.S. Tax System

How much revenue does the AMT raise?

FIGURE 2
Projected Individual Alternative Minimum Tax Revenue
2017–28



Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0718-1).

Data Sources

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