



The Alternative Minimum TAX

It's Coming For You!

By Eileen Cohen, CPA, Partner

The Alternative Minimum Tax (AMT) was originally designed to ensure that wealthy taxpayers were not able to escape taxation by exploiting deductions. However, the AMT has not been appropriately indexed for inflation, which means that it affects a growing number of taxpayers every year.

If government forecasts are correct, **30 million taxpayers will be paying AMT by 2010.**

Just weeks before the start of the 2008 filing season, Congress finally passed a temporary "AMT patch", which is expected to keep millions of middle income taxpayers out of the reach of the AMT – but **only for the 2007 tax year**. The 2007 AMT exemption amounts, which are higher than the 2006 exemption amounts, are: \$44,350 for single taxpayers and heads of household; \$66,250 for married couples filing jointly; and \$33,125 for married couples filing separately. However, the computation of the alternative minimum tax is complex and requires a careful evaluation of your tax situation.

Unfortunately, it is not a good strategy to engage in planning that necessarily focuses solely on eliminating AMT liability. Due to the complex manner in which the regular tax system and the alternative minimum tax system intertwine, **a concentration on lowering minimum tax liability alone can easily result in an unwanted increase in your regular income tax liability.**

To reduce the possibility of being affected by the AMT, **you may want to consider timing your income and deductions, deferring certain items to a future year and accel-**



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erating others into the current year. As a general rule, it is best to accelerate items of income into AMT years and postpone deductions into non-AMT years. For example, you may consider:

- Delaying payment of certain items, such as state and local income taxes, property taxes, medical expenses, and miscellaneous expenses (provided this does not impair your credit status or business standing, or cause you to incur late charges);
 - Avoiding the exercise of incentive stock options;
 - If large long-term capital gains will affect your AMT, delaying the asset sale until after year-end or spreading the gain over a number of years by using an installment sale;
 - Making use of any AMT credit, if applicable.
- In addition, several states, including California, also have an AMT. Fortunately, very few

people are required to pay California AMT. Also keep in mind that the AMT rules for corporate returns are completely different; this article discusses **individual** AMT.

How does AMT work?

To understand how the AMT works, in a nutshell, you begin with taxable income as computed for purposes of the regular federal income tax. Then you add back to taxable income many of the important deductions you claimed to arrive at regular taxable income. For example, state and local income and property taxes, miscellaneous itemized deductions, and personal exemptions all may need to be added back. Depending on the types of businesses and investments you're involved in, there could be other adjustments as well. For example, certain tax breaks for incentive stock options aren't allowed for AMT purposes. After all adjustments and so-called preferences have been made, you subtract an exemption amount that varies with your income level. Then what remains is taxed at 26% or 28% to arrive at a figure called the tentative minimum tax. If this tentative minimum tax is higher than your regular income tax, you must pay the excess as AMT tax. For example, if your regular tax bill is \$25,000, and the tentative minimum tax is \$32,000, you will pay the regular tax bill plus an AMT tax bill of \$7,000 (\$32,000 less \$25,000).

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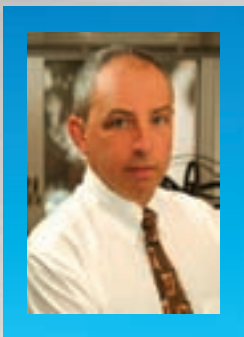
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