



*Procedures Were Not Always Followed When  
Resolving Alternative Minimum Tax  
Discrepancies*

**July 30, 2008**

**Reference Number: 2008-40-146**

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

**Redaction Legend:**

1 = Tax Return/Return Information

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TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

July 30, 2008

**MEMORANDUM FOR** COMMISSIONER, WAGE AND INVESTMENT DIVISION

**FROM:** *Michael R. Phillips*  
Michael R. Phillips  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – Procedures Were Not Always Followed When  
Resolving Alternative Minimum Tax Discrepancies  
(Audit # 200740037)

This report presents the results of our review of the Alternative Minimum Tax (AMT). The overall objective of this review was to determine whether the Internal Revenue Service (IRS) computer systems accurately identified and computed the AMT for taxpayers who might be liable, including both taxpayers who claimed the AMT and those who did not claim it but should have. This review was part of the Treasury Inspector General for Tax Administration Fiscal Year 2007 Annual Audit Plan and related to the Fiscal Year 2007 Major Management Challenge of addressing the complexity of the tax law.

*Impact on the Taxpayer*

The number of taxpayers affected by the AMT is expected to grow significantly in the next 10 years if Congress does not continue to increase exemption amounts. AMT revenue increased from \$16.7 billion for Tax Year 2005 to \$21.4 billion for Tax Year 2006. Determining whether the AMT is owed is complex and time consuming, and the complexity causes taxpayer errors. Computer checks calculate what the AMT should be based on the information reported on the tax return. Tax returns with an AMT discrepancy are sent to IRS tax examiners for review. Our review identified that tax examiners did not always follow established procedures when resolving these discrepancies, which in some instances caused taxpayers to be assessed incorrect amounts.



## *Procedures Were Not Always Followed When Resolving Alternative Minimum Tax Discrepancies*

### Synopsis

The AMT has its own definition of income subject to tax and its own tax rates. Taxpayers might not know they are subject to the AMT until they compute their tax under the regular tax system. The IRS recognizes the difficulty the AMT causes taxpayers both in determining whether the AMT applies to them and, if applicable, in computing their specific AMT liabilities. The IRS provides taxpayers with tools to determine whether they will have to prepare an Alternative Minimum Tax—Individuals (Form 6251)<sup>1</sup> to determine their AMT liabilities. These tools include the *Worksheet To See If You Should Fill In Form 6251* and the AMT Assistant on the IRS web site (IRS.gov). We reviewed a random sample of 80 tax returns filed with a Form 6251. In every case, the AMT Assistant correctly notified the taxpayer whether a Form 6251 should or should not be completed.

Despite the tools provided to assist taxpayers, the complexity of the AMT causes errors in determining and computing the tax. In Calendar Year 2006, computer checks identified about 226,000 discrepancies between the AMT figures reported, or not reported, by the taxpayers and the amounts computed by the IRS. When a discrepancy exists, the tax return is sent to an IRS tax examiner, who reviews the return and looks for obvious input errors or misplaced entries. The tax examiner determines where the difference occurred. If the examiner cannot resolve the issue, a notice is sent to the taxpayer asking for additional information or informing the taxpayer that the AMT calculation was incorrect.

***Computer checks have been developed to identify discrepancies in the reporting of the AMT. However, examiners did not always correctly resolve AMT discrepancies.***

We reviewed a random sample of 52 tax returns filed in Calendar Year 2006 on which IRS computers identified a discrepancy. For all 52 cases, computer checks correctly identified that there was a discrepancy, and the cases were correctly sent to tax examiners for further review. However, examiners did not follow procedures when resolving 11 (21 percent) of the 52 cases. Of these 11 cases, 3 resulted in the examiners incorrectly computing the amount of tax owed. Correct identification and resolution of discrepancies is essential to avoid further increasing the burden for taxpayers subject to the AMT.

### Recommendation

The Commissioner, Wage and Investment Division, should provide information to tax examiners reiterating the importance of correctly resolving AMT discrepancies and highlighting specific issues that could lead to incorrect resolution.

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<sup>1</sup> Appendix V provides an example of Form 6251.



## *Procedures Were Not Always Followed When Resolving Alternative Minimum Tax Discrepancies*

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### *Response*

IRS management agreed with our recommendation. In the Submission Processing Division employee annual training, the IRS Error Resolution function will emphasize the effect of the AMT on taxpayers and the correct processing of returns to which it applies. In addition, during the filing season,<sup>2</sup> a reminder will be issued on the Submission Processing Division “Hot Topics” web site referencing the complexity of resolving AMT discrepancies and highlighting specific issues as necessary. Management’s complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report recommendation. Please contact me at (202) 622-6510 if you have questions or Michael E. McKenney, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 622-5916.

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<sup>2</sup> The period from January through mid-April when most individual income tax returns are filed.



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*Abbreviations*

AMT	Alternative Minimum Tax
IRS	Internal Revenue Service
TY	Tax Year



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## *Background*

In 1969, the Secretary of the Treasury reported that 155 individuals, each with an Adjusted Gross Income<sup>1</sup> of \$200,000, paid no Federal income tax in 1966. Subsequently, Congress enacted the minimum tax to ensure that taxpayers pay at least a minimum amount of tax. This minimum tax was a precursor to the current Alternative Minimum Tax (AMT)<sup>2</sup> that was created in 1978. The AMT is a recalculated tax to reduce the ability of high-income individuals to avoid paying any tax on their income. The AMT eliminates many deductions and credits allowed under the regular tax system. In 1969, high-income taxpayers were defined as those who had income of at least \$200,000. If adjusted for inflation, this figure would be equal to more than \$1.1 million dollars today.

For Tax Year (TY) 2005, the AMT generated \$16.7 billion in additional revenue. That figure grew to \$21.4 billion (28 percent) for TY 2006 and will continue to grow as the number of taxpayers subject to the AMT increases.

### **The AMT continues to affect more taxpayers**

In 1970, only 20,000 taxpayers were subject to the AMT. The number of taxpayers who paid the AMT remained fairly steady from 1987 through 1992 and increased only slightly through 1997. However, the number began to grow considerably in 2002 and is expected to continue to grow significantly in the next 10 years. In recent years, Congress has temporarily increased the AMT exemption amount to help reduce the number of taxpayers subject to the AMT. For example, in 2006, the temporary exemption increase prevented more than 18 million taxpayers from paying the AMT. Similar legislation was again passed in December 2007 for TY 2007. Congress estimated that the temporary exemption increase would reduce the number of taxpayers who would pay the AMT in TY 2007 from 23 million to 4 million.

***Congress has temporarily increased AMT exemption amounts to reduce the number of taxpayers subject to the AMT.***

Although the AMT was originally intended for taxpayers with high income, a growing number of middle-income taxpayers are subject to the AMT. As shown in Figure 1, almost 46 percent of those who paid the AMT for TY 2005 had Adjusted Gross Income of \$200,000 or less.

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<sup>1</sup> Adjusted Gross Income is income less certain deductions, such as the Health Savings Account, Individual Retirement Account, and Education deductions, and/or expenses, such as Educator Expenses and Moving Expenses.

<sup>2</sup> Appendix IV provides the legislative history of the Alternative Minimum Tax.



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**Figure 1: Number of Taxpayers Reporting AMT Liabilities for TY 2005**

Adjusted Gross Income	Number of Taxpayers	Percentage of Taxpayers
Less than \$0	5,416	0.1%
\$0 to \$100,000	352,243	8.9%
\$100,001 to \$200,000	1,443,404	36.5%
\$200,001 to \$300,000	1,204,896	30.5%
\$300,001 to \$400,000	468,924	11.9%
\$400,001 to \$500,000	214,022	5.4%
\$500,001 to \$1,000,000	193,782	4.9%
More than \$1,000,000	69,809	1.8%
<b>Total</b>	<b>3,952,496</b>	<b>100.0%</b>

Source: Analysis of the Internal Revenue Service (IRS) Individual Return Transaction File<sup>3</sup> for TY 2005.

Figure 2 shows the exemption amounts for single taxpayers and married taxpayers filing joint returns for TYs 1993 through 2007. The exemption amounts are based on the taxpayers' filing status and are subtracted from the taxpayers' Alternative Minimum Taxable Income. They reduce the amount of income that is used to determine the AMT.

**Figure 2: Congressional Increases to the AMT Exemption Amounts**

Tax Year	Exemption Amount for Single Taxpayers	Exemption Amount for Married Taxpayers Filing Jointly
<b>1993-2000</b>	\$33,750	\$45,000
<b>2001-2002</b>	\$35,750	\$49,000
<b>2003-2005</b>	\$40,250	\$58,000
<b>2006</b>	\$42,500	\$62,550
<b>2007</b>	\$44,350	\$66,250

Source: Alternative Minimum Tax—Individuals (Form 6251) for TYs 1993 through 2007.

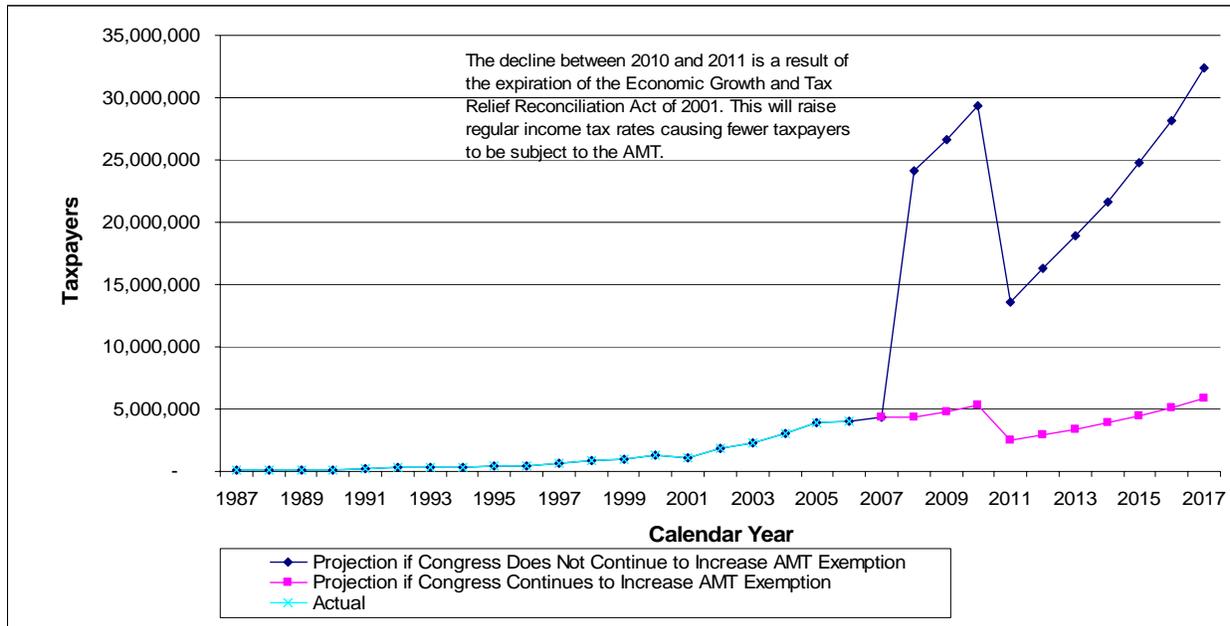
<sup>3</sup> The Individual Return Transaction File contains data from the Individual Master File. The Individual Master File is the IRS database that maintains transactions or records of individual tax accounts.



## Procedures Were Not Always Followed When Resolving Alternative Minimum Tax Discrepancies

Figure 3 shows the trends in the number of taxpayers subject to the AMT as well as the number of taxpayers who could be affected if Congress does not continue to increase exemption amounts.

**Figure 3: Growth in the AMT**



Source: United States Joint Committee on Taxation and our analysis of IRS data.<sup>4</sup>

If Congress does not continue to pass legislation to increase AMT exemption amounts, the rates will revert to levels established by the Omnibus Reconciliation Act of 1993.<sup>5</sup> These amounts are \$33,750 for single taxpayers and \$45,000 for married taxpayers. For TY 2007, legislation was not passed until December 2007. Because of the late passage of this legislation, 13.5 million taxpayers who used 5 AMT-related tax forms or schedules had to wait until February 11, 2008, to file their returns. Delaying the processing of these returns allowed the IRS enough time to update and test its systems to accommodate the changes to the forms without major disruptions to other return processing operations. We are evaluating the effectiveness of the IRS' implementation of the AMT legislation in our review of the 2008 individual filing season.<sup>6</sup>

<sup>4</sup> Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107-16, 115 Stat. 38.

<sup>5</sup> Pub. L. No. 103-66, Title XII, Sec. 12001, 107 Stat. 413.

<sup>6</sup> The period from January through mid-April when most individual income tax returns are filed.



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**Determining whether the AMT is owed is complex and time consuming**

The AMT has its own definition of income subject to tax and its own tax rates. Taxpayers might not know they are subject to the AMT until they compute their tax under the regular tax system. Instructions for the U.S. Individual Income Tax Return (Form 1040) direct taxpayers to fill out the *Worksheet To See If You Should Fill In Form 6251*<sup>7</sup> or to use the AMT Assistant (the Assistant) on the IRS web site (IRS.gov) to determine whether they will have to prepare Form 6251 to determine their AMT liabilities. Form 6251 is composed of three parts:

- Part I – contains 28 lines and is used to compute a taxpayer's Alternative Minimum Taxable Income. This Part requires a taxpayer to add certain income-related items back to his or her Adjusted Gross Income to arrive at Alternative Minimum Taxable Income.
- Part II – contains seven lines and is used to compute the AMT.
- Part III – contains 20 lines and is used to compute the AMT using the maximum capital gains rates.

After completing Form 6251, the taxpayer transfers the AMT amount back to his or her Form 1040 and completes the remainder of the tax return. Approximately 8 million taxpayers filed a Form 6251 for TY 2005. Approximately 6.7 million (84 percent) of these taxpayers had their returns prepared by paid preparers.

The complexity of the AMT causes errors in determining and computing the AMT. The IRS developed computer checks to identify taxpayer discrepancies when reporting the AMT. These checks are performed during the processing of the tax return and calculate what the AMT should be based on the information reported on the tax return. The checks identify the following types of tax returns:

- A tax return for which an AMT liability appears to exist but the taxpayer has not claimed the AMT.
- A tax return for which the amount of the AMT claimed by the taxpayer differs from the amount computed by the IRS.

When a discrepancy exists, the tax return is identified for further review by an IRS tax examiner, who reviews the return and looks for obvious input errors or misplaced entries. If there are not obvious errors, the tax examiner determines where the difference occurred. If the examiner cannot resolve the issue, a notice is sent to the taxpayer asking for additional information or informing the taxpayer that the AMT calculation was incorrect.

This review was performed at the IRS Wage and Investment Division Headquarters in Atlanta, Georgia, in the Office of Customer Account Services, Submission Processing Division,

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<sup>7</sup> Appendix V provides an example of Form 6251.



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during the period February through November 2007. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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*Results of Review*

***Computer Checks Identify Alternative Minimum Tax Discrepancies;  
However, Examiners Did Not Always Follow Established Procedures  
When Resolving the Discrepancies***

The IRS recognizes the difficulty the AMT causes taxpayers both in determining whether the AMT applies to them and, if applicable, in computing their specific AMT liabilities. The IRS has taken steps to help taxpayers better understand their responsibility for paying the AMT. IRS instructions for the U.S. Individual Income Tax Return (Form 1040) direct taxpayers to fill out a *Worksheet To See If You Should Fill In Form 6251* to determine if they will have to prepare a Form 6251 to calculate their AMT liabilities.

***The IRS provides tools to assist taxpayers in determining if the AMT applies to them and, if applicable, in computing their specific AMT liabilities.***

The IRS also provides the Assistant, which is an electronic version of the AMT worksheet. Taxpayers enter information from their returns, and the Assistant will inform them as to whether they need to complete Form 6251 to determine their tax liabilities. We reviewed a random sample of 80 tax returns filed with a Form 6251. In every case, the Assistant correctly notified the taxpayer whether a Form 6251 should or should not be completed.

***Computer checks identify AMT discrepancies***

The complexity of the AMT causes taxpayer errors in determining and computing tax liabilities. IRS computer programs calculate what the AMT should be based on the information reported on the tax return. The calculated amount is then compared to the AMT reported by the taxpayer. During Calendar Year 2006, the IRS identified 1) approximately 61,000 tax returns on which taxpayers appeared to owe the AMT but did not claim it on their tax returns and 2) approximately 165,000 tax returns that had discrepancies between the amount of AMT shown by the taxpayer and what was computed by the IRS.

We reviewed a random sample of 52 tax returns filed in Calendar Year 2006 with a difference between the AMT figure provided by the taxpayer and that computed by the IRS. Computer checks correctly identified that there was a discrepancy for all 52 cases, and the cases were sent to IRS tax examiners for further review.

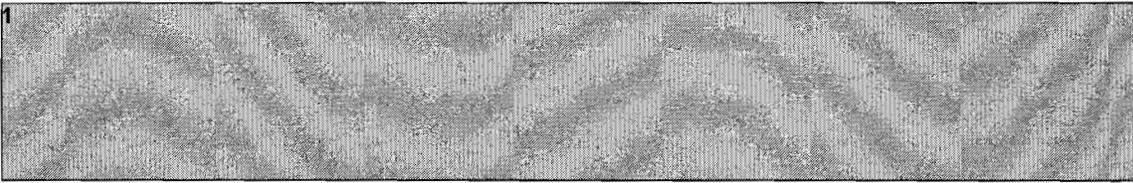


## ***Procedures Were Not Always Followed When Resolving Alternative Minimum Tax Discrepancies***

### **Examiners did not always follow procedures when resolving AMT discrepancies**

In resolving the identified discrepancies, examiners did not follow procedures for 11 (21 percent) of the 52 cases sampled. For 8 of those 11 cases, the discrepancy resulted from IRS employees incorrectly transcribing information from paper tax returns to IRS computers when the tax returns were processed. The transcription errors resulted in the taxpayers' AMT figures being incorrectly computed when the IRS performed its verification. Examiners working these cases identified that the discrepancies were the result of transcription errors but did not correct the transcription errors in IRS computers as required. There was no effect on the amount of tax that the taxpayer owed, and contact with the taxpayer was not necessary because the IRS resolved the errors internally.

For the remaining three cases, the incorrect resolution resulted in an incorrect amount of tax being assessed:

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Computer checks accurately identified AMT discrepancies for further review. However, incorrect tax examiner resolution of AMT discrepancies can result in the incorrect calculation of the tax owed. Resolving these discrepancies correctly will help to ensure that taxpayers are correctly paying their tax liabilities. In addition, correct identification and resolution of discrepancies is essential to avoid further increasing the burden for taxpayers subject to the AMT.



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**Recommendation**

**Recommendation 1:** The Commissioner, Wage and Investment Division, should provide information to tax examiners reiterating the importance of correctly resolving AMT discrepancies and highlighting specific issues that could lead to incorrect resolution.

**Management's Response:** IRS management agreed with this recommendation. In the Submission Processing Division employee annual training, the IRS Error Resolution function will emphasize the effect of the AMT on taxpayers and the correct processing of returns to which it applies. In addition, during the filing season, a reminder will be issued on the Submission Processing Division "Hot Topics" web site referencing the complexity of resolving AMT discrepancies and highlighting specific issues as necessary.



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## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

Our overall objective was to determine whether the IRS computer systems accurately identified and computed the AMT for taxpayers who might be liable, including both taxpayers who claimed the AMT and those who did not claim it but should have. Our review included an analysis of the demographics of those taxpayers affected by the AMT. To accomplish this objective, we:

- I. Evaluated the information that taxpayers can use to determine their need to consider whether they might owe the AMT.
  - A. Reviewed the U.S. Individual Income Tax Return (Form 1040) and related instructions and *Your Federal Income Tax For Individuals* (Publication 17) for references to AMT issues. We also reviewed the Alternative Minimum Tax—Individuals (Form 6251) and related instructions for clarity and reviewed draft publications covering the AMT. In addition, we reviewed the AMT Assistant on IRS.gov for clarity and ease of use.
- II. Identified the IRS processing controls in place to identify and correct returns that are claiming the AMT or should be claiming the AMT.
  - A. Reviewed the Internal Revenue Manual to determine the information from the Form 6251 that was transcribed for paper returns and was available in the computer system for both paper and electronic returns. We reviewed the Internal Revenue Manual processing procedures related to the AMT for the IRS Code and Edit and Error Resolution functions.
  - B. Reviewed any Examination function referral procedures to determine how a return gets to the Examination function.
  - C. Reviewed the computer programming to determine how the IRS calculated potential AMT.
- III. Evaluated the processing controls by reviewing a sample of tax returns that had the AMT assessed.
  - A. Extracted all TY 2005 Forms 6251 filed in Calendar Year 2006 from the IRS Return Transaction File<sup>1</sup> in the Treasury Inspector General for Tax Administration Data

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<sup>1</sup> The Individual Return Transaction File contains data from the Individual Master File. The Individual Master File is the IRS database that maintains transactions or records of individual tax accounts.



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- Center Warehouse<sup>2</sup> and separated the records into 2 files: cases for which the AMT was more than \$0 and cases for which the AMT equaled \$0. Data were validated to the Integrated Data Retrieval System.
- B. Randomly sampled 52 of the 7,583 tax returns processed at all Submission Processing sites for which the AMT was more than \$0 and there was a significant<sup>3</sup> difference between the AMT calculated by the IRS and the AMT calculated by the taxpayer. A random number generator was used to ensure that tax returns had an equal chance of being selected. We reviewed the sample cases to determine whether IRS processing procedures were correctly followed. We determined that a statistically valid sample was not needed based on our review of these 52 returns.
- IV. Determined the number of taxpayers who filed Form 6251 but were not required to pay the AMT (AMT = \$0).
- A. Randomly sampled 28 of the 4,016,823 returns that had AMT = \$0 from the data extract in Step III.A. A random number generator was used to ensure that tax returns had an equal chance of being selected. We reviewed the sampled cases to determine whether the AMT Assistant on IRS.gov would mislead the taxpayer into thinking the AMT could be owed. We determined a statistically valid sample was not needed based on the results of our review of these 28 returns.

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<sup>2</sup> A Treasury Inspector General for Tax Administration repository of IRS critical historical data. The mission of the Warehouse is to provide data and data access services; centralize storage, security, and administration of files; and develop uniform and user-friendly interfaces for users to access data.

<sup>3</sup> For the purpose of our review, we considered a difference of \$100 between the AMT calculated by the IRS and the AMT calculated by the taxpayer to be significant.



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**Appendix II**

*Major Contributors to This Report*

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Kathleen A. Hughes, Senior Auditor  
Glory Jampetero, Senior Auditor  
Ryan C. Powderly, Intern



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**Appendix III**

*Report Distribution List*

Commissioner C  
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Commissioner, Small Business/Self-Employed Division SE:S  
Deputy Commissioner, Small Business/Self-Employed Division SE:S  
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**Appendix IV**

*Legislative History of the Alternative Minimum Tax*

Congress enacted the minimum tax in 1969 after the Secretary of the Treasury reported that 155 individuals, each with an Adjusted Gross Income<sup>1</sup> of \$200,000, paid no Federal income tax in 1966. In 1978, Congress enacted a minimum tax that resembles the current AMT. The 1978 tax was payable in addition to all other tax liabilities to the extent that it exceeded the individual’s regular tax liability. It was imposed at a flat rate of 20 percent on Alternative Minimum Taxable Income in excess of an exemption amount.<sup>2</sup>

Congress repealed the minimum tax in 1982 and expanded the AMT to include the tax preferences from the minimum tax. The provisions enacted in 1982 are the foundation for today’s AMT. The AMT has been amended a number of times. The following table describes the legislative action for the original minimum tax and the current AMT.

Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Tax Reform Act of 1969 (P.L. 91-172)	\$30,000 plus regular tax	\$30,000 plus regular tax	10%	<b>Introduced the “add-on” minimum income tax</b> of 10 percent of the amount of preferences <sup>3</sup> in excess of an exemption of \$30,000 for both joint and single filers. The main preference item was capital gains, but preferences also included stock options, depreciation, and depletion allowances.

<sup>1</sup> Adjusted Gross Income is income less certain deductions, such as Health Savings Account, Individual Retirement Account, and Education deductions, and/or expenses, such as Educator Expenses and Moving Expenses.

<sup>2</sup> Present Law and Issues Relating to the Individual AMT, Joint Committee on Taxation (JCX-3-98, dated February 2, 2008).

<sup>3</sup> Certain income-related items that must be added back to Adjusted Gross Income to arrive at an Alternative Minimum Taxable Income.



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Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Excise, Estate, and Gift Tax Adjustment Act of 1970 (P.L. 91-614)	No change	No change	No change	Allowed deduction of the “unused regular tax carryover” from the base for the minimum tax.
Tax Reform Act of 1976 (P.L. 94-455)	Greater of \$10,000 or ½ of regular tax	Greater of \$10,000 or ½ of regular tax	15%	Raised the rate of minimum income tax to 15 percent and lowered the exemption to the greater of \$10,000 or one-half of regular taxes. This Act also added certain itemized deductions as preferences.
Tax Reduction and Simplification Act of 1977 (P.L. 95-30)	No change	No change	No change	Reduced the minimum tax preference for intangible costs of drilling oil and gas wells.
Revenue Act of 1978 (P.L. 95-600)	\$20,000	\$20,000	10% on \$0 - \$40,000 20% on \$40,001 - \$80,000 25% on more than \$80,000	<b>Introduced the AMT</b> alongside the minimum income tax and moved certain itemized deductions and capital gains to the AMT. The AMT had graduated rates of 10 percent, 20 percent, and 25 percent and an exemption of \$20,000.
Economic Recovery Tax Act of 1981 (P.L. 97-34)	No change	No change	10% on \$0 - \$40,000 20% on more than \$40,000	Eliminated the 25 percent AMT rate to correspond with reductions in rates of regular income tax.



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Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97-248)	\$40,000	\$30,000	20%	<b>Repealed the “add-on” minimum tax</b> and made the AMT rate a flat 20 percent of AMT income after exemptions of \$30,000 for single filers and \$40,000 for jointly filed returns. The preferences from the add-on tax were moved to the AMT.
Deficit Reduction Act of 1984 (P.L. 98-369)	No change	No change	No change	Made minor changes concerning the Investment Tax Credit, intangible drilling costs, and other items.
Tax Reform Act of 1986 (P.L. 99-514)	No change	No change	21%	Raised the AMT rate to 21 percent, made high-income taxpayers subject to phaseout of exemptions, increased the number of tax preferences by adding preferences for interest on private activity bonds and for appreciation on charitable contributions. The AMT base was expanded to include deferral items, <sup>4</sup> and an AMT credit for a prior year AMT liability due to deferral items was introduced. Net operating losses were allowed to offset only 90 percent of Alternative Minimum Taxable Income, and the Foreign Tax Credit was not allowed to be used to reduce the tentative minimum tax by more than 90 percent.
Revenue Act of 1986 (P.L. 100-203)	No change	No change	No change	Made technical corrections related to the Tax Reform Act of 1986.

<sup>4</sup> A deferral item is an amount for which the asset or liability is not realized until a future date.



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Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Technical and Miscellaneous Revenue Act of 1988 (P.L. 100-647)	No change	No change	No change	Made technical corrections related to the Tax Reform Act of 1986.
Omnibus Budget Reconciliation Act of 1989 (P.L. 101-239)	No change	No change	No change	Made further technical amendments.
Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508)	No change	No change	24%	Raised the AMT rate to 24 percent.
Energy Policy Act of 1992 (P.L. 102-486)	No change	No change	No change	Made changes regarding intangible costs of drilling oil and gas wells.
Omnibus Reconciliation Act of 1993 (P.L. 103-66)	\$45,000	\$33,750	26% on \$0 - \$175,000 28% on more than \$175,000	Introduced graduated AMT rates of 26 percent and 28 percent. This Act also increased the exemption to \$33,750 for single filers and \$45,000 for jointly filed returns, changed rules about gains on stock of small businesses, and eliminated the appreciated charitable property deduction preference.



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Alternative Minimum Tax Discrepancies*

Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Taxpayer Relief Act of 1997 (P.L. 105-34)	No change	No change	No change	Made changes regarding depreciation and farmers' installment sales, and repealed the requirement that alternative depreciation periods be used in computing the deduction for Accelerated Cost Recovery System depreciation.
Tax Technical Corrections Act of 1998 (P.L. 105-206)	No change	No change	No change	Adjusted the AMT for new capital gains rates.
Tax Relief Extension Act of 1999 (P.L. 106-170)	No change	No change	No change	Allowed use of all personal nonrefundable credits against the AMT through 2001.
Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16)	\$49,000 for years 2001-2004 \$45,000 for 2005 and beyond	\$35,750 for years 2001-2004 \$33,750 for 2005 and beyond	No change	Temporarily increased the exemption amount to \$35,750 for single filers and \$49,000 for jointly filed returns. This Act allowed use of the child, adoption, and Individual Retirement Account credits against the AMT liability through 2010.
Job Creation and Worker Assistance Act of 2002 (P.L.107-147)	No change	No change	No change	Allowed all personal nonrefundable credits to be used against the AMT liability through 2003.



*Procedures Were Not Always Followed When Resolving  
Alternative Minimum Tax Discrepancies*

Legislation	Married Filing Jointly Exemption	Single Exemption	Tax Rates	Comments
Jobs and Growth Tax Relief Reconciliation Act of 2003 (P.L. 108-27)	\$58,000 for years 2003-2004 \$45,000 for 2005 and beyond	\$40,250 for years 2003-2004 \$33,750 for 2005 and beyond	No change	Temporarily increased the exemption amount to \$40,250 for single filers and \$58,000 for jointly filed returns. This Act conformed the AMT rates for dividends to the lower rates adopted for the regular tax.
Working Families Tax Relief Act of 2004 (P.L. 108-311)	No change	No change	No change	Extended the temporary increase in the exemption amounts made by the Jobs and Growth Tax Relief Reconciliation Act of 2003.
American Jobs Creation Act of 2004 (P.L. 108-357)	No change	No change	No change	Allowed the Foreign Tax Credit to offset the entire tentative minimum tax (repealed the 90 percent limitation on use of Foreign Tax Credits).
Tax Relief Extension Reconciliation Act of 2005 (P.L. 109-222)	\$62,550 for 2006 \$45,000 for 2007 and beyond	\$42,500 for 2006 \$33,750 for 2007 and beyond	No change	Increased the exemption amount to \$42,500 for single filers and \$62,550 for jointly filed returns.
Tax Increase Prevention Act of 2007 (P.L. 110-166)	\$66,250 for 2007 \$45,000 for 2007 and beyond	\$44,350 for 2007 \$33,750 for 2007 and beyond	No change	Increased the exemption amount to \$44,350 for single filers and \$66,250 for jointly filed returns.



Procedures Were Not Always Followed When Resolving Alternative Minimum Tax Discrepancies

Appendix V

Alternative Minimum Tax-Individuals (Form 6251)

Form **6251** **Alternative Minimum Tax—Individuals** OMB No. 1545-0074  
 Department of the Treasury Internal Revenue Service (99) **2007** Attachment Sequence No. **32**  
 Name(s) shown on Form 1040 or Form 1040NR Your social security number  
 ▶ See separate instructions. ▶ Attach to Form 1040 or Form 1040NR.

**Part I Alternative Minimum Taxable Income** (See instructions for how to complete each line.)

1	If filing Schedule A (Form 1040), enter the amount from Form 1040, line 41, and go to line 2. Otherwise, enter the amount from Form 1040, line 38, and go to line 7. (If less than zero, enter as a negative amount.)	1	
2	Medical and dental. Enter the <b>smaller</b> of Schedule A (Form 1040), line 4, or 2.5% (.025) of Form 1040, line 38. If zero or less, enter -0-	2	
3	Taxes from Schedule A (Form 1040), line 9	3	
4	Enter the home mortgage interest adjustment, if any, from line 6 of the worksheet on page 2 of the instructions	4	
5	Miscellaneous deductions from Schedule A (Form 1040), line 27	5	
6	If Form 1040, line 38, is over \$156,400 (over \$78,200 if married filing separately), enter the amount from line 11 of the <b>Itemized Deductions Worksheet</b> on page A-10 of the instructions for Schedule A (Form 1040)	6	( )
7	Tax refund from Form 1040, line 10 or line 21	7	( )
8	Investment interest expense (difference between regular tax and AMT)	8	
9	Depletion (difference between regular tax and AMT)	9	
10	Net operating loss deduction from Form 1040, line 21. Enter as a positive amount	10	
11	Interest from specified private activity bonds exempt from the regular tax	11	
12	Qualified small business stock (7% of gain excluded under section 1202)	12	
13	Exercise of incentive stock options (excess of AMT income over regular tax income)	13	
14	Estates and trusts (amount from Schedule K-1 (Form 1041), box 12, code A)	14	
15	Electing large partnerships (amount from Schedule K-1 (Form 1065-B), box 6)	15	
16	Disposition of property (difference between AMT and regular tax gain or loss)	16	
17	Depreciation on assets placed in service after 1986 (difference between regular tax and AMT)	17	
18	Passive activities (difference between AMT and regular tax income or loss)	18	
19	Loss limitations (difference between AMT and regular tax income or loss)	19	
20	Circulation costs (difference between regular tax and AMT)	20	
21	Long-term contracts (difference between AMT and regular tax income)	21	
22	Mining costs (difference between regular tax and AMT)	22	
23	Research and experimental costs (difference between regular tax and AMT)	23	
24	Income from certain installment sales before January 1, 1987	24	( )
25	Intangible drilling costs preference	25	
26	Other adjustments, including income-based related adjustments	26	
27	Alternative tax net operating loss deduction	27	( )
28	<b>Alternative minimum taxable income.</b> Combine lines 1 through 27. (If married filing separately and line 28 is more than \$207,500, see page 7 of the instructions.)	28	

**Part II Alternative Minimum Tax**

29	Exemption. (If this form is for a child under age 18, see page 7 of the instructions.) <b>IF your filing status is . . . AND line 28 is not over . . . THEN enter on line 29 . . .</b> Single or head of household . . . \$112,500 . . . \$44,350 Married filing jointly or qualifying widow(er) . . . 150,000 . . . 66,250 Married filing separately . . . 75,000 . . . 33,125 If line 28 is <b>over</b> the amount shown above for your filing status, see page 7 of the instructions.	29	
30	Subtract line 29 from line 28. If more than zero, go to line 31. If zero or less, enter -0- here and on lines 33 and 35 and skip the rest of Part II	30	
31	• If you are filing Form 2555 or 2555-EZ, see page 8 of the instructions for the amount to enter. • If you reported capital gain distributions directly on Form 1040, line 13; you reported qualified dividends on Form 1040, line 9b; or you had a gain on both lines 15 and 16 of Schedule D (Form 1040) (as refigured for the AMT, if necessary), complete Part III on the back and enter the amount from line 55 here. • <b>All others:</b> If line 30 is \$175,000 or less (\$87,500 or less if married filing separately), multiply line 30 by 26% (.26). Otherwise, multiply line 30 by 28% (.28) and subtract \$3,500 (\$1,750 if married filing separately) from the result.	31	
32	Alternative minimum tax foreign tax credit (see page 8 of the instructions)	32	
33	Tentative minimum tax. Subtract line 32 from line 31	33	
34	Tax from Form 1040, line 44 (minus any tax from Form 4972 and any foreign tax credit from Form 1040, line 51). If you used Schedule J to figure your tax, the amount from line 44 of Form 1040 must be refigured without using Schedule J (see page 9 of the instructions).	34	
35	<b>Alternative minimum tax.</b> Subtract line 34 from line 33. If zero or less, enter -0-. Enter here and on Form 1040, line 45	35	

For Paperwork Reduction Act Notice, see page 10 of the instructions. Cat. No. 13000G Form **6251** (2007)



*Procedures Were Not Always Followed When Resolving  
Alternative Minimum Tax Discrepancies*

**Part III Tax Computation Using Maximum Capital Gains Rates**

<p><b>36</b> Enter the amount from Form 6251, line 30. If you are filing Form 2555 or 2555-EZ, enter the amount from line 3 of the worksheet on page 8 of the instructions . . . . .</p>	<b>36</b>		
<p><b>37</b> Enter the amount from line 6 of the Qualified Dividends and Capital Gain Tax Worksheet in the instructions for Form 1040, line 44, or the amount from line 13 of the Schedule D Tax Worksheet on page D-10 of the instructions for Schedule D (Form 1040), whichever applies (as figured for the AMT, if necessary) (see page 9 of the instructions). If you are filing Form 2555 or 2555-EZ, see page 10 of the instructions for the amount to enter . . . . .</p>	<b>37</b>		
<p><b>38</b> Enter the amount from Schedule D (Form 1040), line 19 (as figured for the AMT, if necessary) (see page 9 of the instructions). If you are filing Form 2555 or 2555-EZ, see page 10 of the instructions for the amount to enter . . . . .</p>	<b>38</b>		
<p><b>39</b> If you did not complete a Schedule D Tax Worksheet for the regular tax or the AMT, enter the amount from line 37. Otherwise, add lines 37 and 38, and enter the <b>smaller</b> of that result or the amount from line 10 of the Schedule D Tax Worksheet (as figured for the AMT, if necessary). If you are filing Form 2555 or 2555-EZ, see page 10 of the instructions for the amount to enter . . . . .</p>	<b>39</b>		
<p><b>40</b> Enter the <b>smaller</b> of line 36 or line 39 . . . . .</p>	<b>40</b>		
<p><b>41</b> Subtract line 40 from line 36 . . . . .</p>	<b>41</b>		
<p><b>42</b> If line 41 is \$175,000 or less (\$87,500 or less if married filing separately), multiply line 41 by 26% (.26). Otherwise, multiply line 41 by 28% (.28) and subtract \$3,500 (\$1,750 if married filing separately) from the result . . . . . ▶</p>	<b>42</b>		
<p><b>43</b> Enter:</p> <ul style="list-style-type: none"> <li>• \$63,700 if married filing jointly or qualifying widow(er),</li> <li>• \$31,850 if single or married filing separately, or</li> <li>• \$42,650 if head of household.</li> </ul>	<b>43</b>		
<p><b>44</b> Enter the amount from line 7 of the Qualified Dividends and Capital Gain Tax Worksheet in the instructions for Form 1040, line 44, or the amount from line 14 of the Schedule D Tax Worksheet on page D-10 of the instructions for Schedule D (Form 1040), whichever applies (as figured for the regular tax). If you did not complete either worksheet for the regular tax, enter -0- . . . . .</p>	<b>44</b>		
<p><b>45</b> Subtract line 44 from line 43. If zero or less, enter -0- . . . . .</p>	<b>45</b>		
<p><b>46</b> Enter the <b>smaller</b> of line 36 or line 37 . . . . .</p>	<b>46</b>		
<p><b>47</b> Enter the <b>smaller</b> of line 45 or line 46 . . . . .</p>	<b>47</b>		
<p><b>48</b> Multiply line 47 by 5% (.05) . . . . . ▶</p>	<b>48</b>		
<p><b>49</b> Subtract line 47 from line 46 . . . . .</p>	<b>49</b>		
<p><b>50</b> Multiply line 49 by 15% (.15) . . . . . ▶</p>	<b>50</b>		
<b>If line 38 is zero or blank, skip lines 51 and 52 and go to line 53. Otherwise, go to line 51.</b>			
<p><b>51</b> Subtract line 46 from line 40 . . . . .</p>	<b>51</b>		
<p><b>52</b> Multiply line 51 by 25% (.25) . . . . . ▶</p>	<b>52</b>		
<p><b>53</b> Add lines 42, 48, 50, and 52 . . . . .</p>	<b>53</b>		
<p><b>54</b> If line 36 is \$175,000 or less (\$87,500 or less if married filing separately), multiply line 36 by 26% (.26). Otherwise, multiply line 36 by 28% (.28) and subtract \$3,500 (\$1,750 if married filing separately) from the result . . . . .</p>	<b>54</b>		
<p><b>55</b> Enter the <b>smaller</b> of line 53 or line 54 here and on line 31. If you are filing Form 2555 or 2555-EZ, do not enter this amount on line 31. Instead, enter it on line 4 of the worksheet on page 8 of the instructions . . . . .</p>	<b>55</b>		



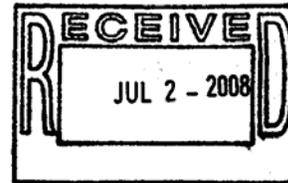
*Procedures Were Not Always Followed When Resolving  
Alternative Minimum Tax Discrepancies*

**Appendix VI**

*Management's Response to the Draft Report*



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
ATLANTA, GA 30308



JUL 02 2008

MEMORANDUM FOR MICHAEL R. PHILLIPS  
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: *for* Richard Byrd, Jr. *Paul G. Watson*  
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Procedures Were Not Always Followed  
When Resolving Alternative Minimum Tax Discrepancies  
(Audit # 200740037)

I reviewed the subject draft report and appreciate your review of our procedures to resolve Alternative Minimum Tax (AMT) discrepancies. As the AMT increasingly affects more taxpayers, it is important that the IRS calculates the additional tax correctly to ensure taxpayers pay the correct amount of taxes and decrease further taxpayer burden.

Determining whether taxpayers owe the AMT is a complex and time consuming task. To make it less complicated for the taxpayer, the IRS has included an AMT Assistant on IRS.gov that allows the taxpayer to answer a few simple questions about entries on Form 1040 (U.S. Individuals Income Tax Return). Based on the entries, the results will show that either the taxpayer does not owe the AMT or they must go further and complete Form 6251 (Alternative Minimum Tax – Individuals) to find out if they owe the AMT. In addition, the Form 1040 instructions have a non-electronic version of the worksheet, captioned "Worksheet to See if You Should Fill in Form 6251 – Line 45". For taxpayers that need additional information, Tax Topic 556 – Alternative Minimum Tax, included on IRS.gov, provides additional information and can also be accessed by calling (800) 829-4477.

Our annual training for Submission Processing employees will emphasize the effect of the AMT on taxpayers and the correct processing of returns containing the AMT. In addition, Submission Processing will include the AMT information on "Hot Topics", referencing the complexity of resolving AMT discrepancies and highlighting specific issues as necessary. Hot Topics is a Submission Processing intranet web page where employees access Internal Revenue Manual changes, alerts, and procedural clarifications.



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*Procedures Were Not Always Followed When Resolving  
Alternative Minimum Tax Discrepancies*

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Our comments to your recommendations are attached. If you have any questions regarding this response, please call me at (404) 338-7060, or members of your staff may contact Peter J. Stipek, Director, Customer Account Services, at (404) 338-8910.

Attachment



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*Procedures Were Not Always Followed When Resolving  
Alternative Minimum Tax Discrepancies*

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Attachment

**RECOMMENDATION 1**

The Commissioner, Wage and Investment Division, should provide information to tax examiners reiterating the importance of correctly resolving AMT discrepancies and highlighting specific issues that could lead to incorrect resolution.

**CORRECTIVE ACTION**

We agree with this recommendation. In the Submission Processing employee annual training, our Error Resolution function will emphasize the effect of the AMT on taxpayers and the correct processing of returns to which it applies. In addition, during the filing season, a reminder will be issued on the Submission Processing "Hot Topics" website referencing the complexity of resolving AMT discrepancies and highlighting specific issues as necessary.

**IMPLEMENTATION DATE**

December 15, 2008

**RESPONSIBLE OFFICIAL**

Director, Submission Processing, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

IRS will monitor this corrective action as part of our internal management control system.