

Alternative minimum tax credit relief for individuals; returns required for certain options (secs. 402 and 403 of the bill and secs. 53 and 6039 of the Code)

Present Law

In general

Present law imposes an alternative minimum tax (“AMT”) on an individual taxpayer to the extent the taxpayer’s tentative minimum tax liability exceeds his or her regular income tax liability. An individual’s tentative minimum tax is the sum of (1) 26 percent of so much of the taxable excess as does not exceed \$175,000 (\$87,500 in the case of a married individual filing a separate return) and (2) 28 percent of the remaining taxable excess. The taxable excess is the amount by which the alternative minimum taxable income (“AMTI”) exceeds an exemption amount.

An individual’s AMTI is the taxpayer’s taxable income increased by certain preference items and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items.

The individual AMT attributable to deferral adjustments generates a minimum tax credit that is allowable to the extent the regular tax (reduced by other nonrefundable credits) exceeds the tentative minimum tax in a future taxable year. Unused minimum tax credits are carried forward indefinitely.

AMT treatment of incentive stock options

One of the adjustments in computing AMTI is the tax treatment of the exercise of an incentive stock option. An incentive stock option is an option granted by a corporation in connection with an individual’s employment, so long as the option meets certain specified requirements.⁸⁴ Under the regular tax, the exercise of an incentive stock option is tax-free if the stock is not disposed of within one year of exercise of the option or within two years of the grant of the option.⁸⁵ The individual then computes the long-term capital gain or loss on the sale of the stock using the amount paid for the stock as the cost basis. If the holding period requirements are not satisfied, the individual generally takes into account at the exercise of the option an amount of ordinary income equal to the excess of the fair market value of the stock on the date of exercise over the amount paid for the stock. The cost basis of the stock is increased by the amount taken into account.⁸⁶

⁸⁴ Sec. 422.

⁸⁵ Sec. 421.

⁸⁶ If the stock is sold at a loss before the required holding periods are met, the amount taken into account may not exceed the amount realized on the sale over the adjusted basis of the stock. If the stock is sold after the taxable year in which the option was exercised but before the required holding periods are met, the required inclusion is made in the year the stock is sold.

Under the individual alternative minimum tax, the exercise of an incentive stock option is treated as the exercise of an option other than an incentive stock option. Under this treatment, generally the individual takes into account as ordinary income for purposes of computing AMTI the excess of the fair market value of the stock at the date of exercise over the amount paid for the stock.⁸⁷ When the stock is later sold, for purposes of computing capital gain or loss for purposes of AMTI, the adjusted basis of the stock includes the amount taken into account as AMTI.

The adjustment relating to incentive stock options is a deferral adjustment and therefore generates an AMT credit in the year the stock is sold.⁸⁸

Furnishing of information

Under present law,⁸⁹ employers are required to provide to employees information regarding the transfer of stock pursuant to the exercise of an incentive stock option and to transfers of stock under an employee stock purchase plan where the option price is between 85 percent and 100 percent of the value of the stock.⁹⁰

Explanation of Provision

Allowance of credit

Under the provision, an individual's minimum tax credit allowable for any taxable year beginning before January 1, 2013, is not less than the "AMT refundable credit amount". The "AMT refundable credit amount" is the greater of (1) the lesser of \$5,000 or the long-term unused minimum tax credit, or (2) 20 percent of the long-term unused minimum tax credit. The long-term unused minimum tax credit for any taxable year means the portion of the minimum tax credit attributable to the adjusted net minimum tax for taxable years before the 3rd taxable year immediately preceding the taxable year (assuming the credits are used on a first-in, first-out basis). In the case of an individual whose adjusted gross income for a taxable year exceeds the threshold amount (within the meaning of section 151(d)(3)(C)), the AMT refundable credit amount is reduced by the applicable percentage (within the meaning of section 151(d)(3)(B)). The additional credit allowable by reason of this provision is refundable.

⁸⁷ If the stock is sold in the same taxable year the option is exercised, no adjustment in computing AMTI is required.

⁸⁸ If the stock is sold for less than the amount paid for the stock, the loss may not be allowed in full in computing AMTI by reason of the \$3,000 limit on the deductibility of net capital losses. Thus, the excess of the regular tax over the tentative minimum tax may not reflect the full amount of the loss.

⁸⁹ Sec. 6039.

⁹⁰ Sec. 423(c).

Example.—Assume in 2010 an individual has an adjusted gross income that results in an applicable percentage of 50 percent under section 151(d)(3)(B), a regular tax of \$45,000, a tentative minimum tax of \$40,000, no other credits allowable, and a minimum tax credit for the taxable year (before limitation under section 53(c)) of \$1.1 million of which \$1 million is a long-term unused minimum tax credit.

The AMT refundable credit amount for the taxable year is \$100,000 (20 percent of the \$1 million long-term unused minimum tax credit reduced by an applicable percentage of 50 percent). The minimum tax credit allowable for the taxable year is \$100,000 (the greater of the AMT refundable credit amount or the amount of the credit otherwise allowable). The \$5,000 credit allowable without regard to this provision is nonrefundable and the additional \$95,000 of credit allowable by reason of this provision is treated as a refundable credit. Thus, the taxpayer has an overpayment of \$55,000 (\$45,000 regular tax less \$5,000 nonrefundable AMT credit less \$95,000 refundable AMT credit). The \$55,000 overpayment is allowed as a refund or credit to the taxpayer. The remaining \$1 million minimum tax credit is carried forward to future taxable years.

If, in the above example, the adjusted gross income did not exceed the threshold amount under section 151(d)(3)(C), the AMT refundable credit amount for the taxable year would be \$200,000, and the overpayment would be \$155,000.

Information returns

The provision requires an employer to make an information return with the IRS, in addition to providing information to the employee, regarding the transfer of stock pursuant to exercise of an incentive stock option, and to certain stock transfers regarding employee stock purchase plans.

Effective Date

The provision relating to the minimum tax credit applies to taxable years beginning after the date of enactment.

The provision relating to returns applies to calendar years beginning after the date of enactment.