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HOW TO MINIMIZE ALTERNATIVE MINIMUM TAX (AMT)
(PART 2 - MEDICAL, INTEREST, EXEMPTIONS, DEPRECIATION & OTHER DEDUCTIONS)

By Victor Sy, CPA

We discussed strategies to minimize the dreaded AMT for standard deduction, mortgage interest and taxes in Part 1. Let's now plan to combat AMT for medical, investment interest, exemptions, depreciation and miscellaneous deductions in Part 2.

Medical Deductions:

Strategy 1 - Accelerate or Defer Expenses - Defer or accelerate medical expenses from one year to another, such as paying the orthodontist in installments or all at once.

Strategy 2 - Child of Divorced or Separated Parents - If either parent can claim a child as a dependent under the rules of divorced or separated parents, each parent can include medical expenses that he/she she pays for the child. This is true even if an exemption for the child is claimed by the other parent. If one parent is hit with AMT, consider having that parent pay medical expenses for the child.

Investment Interest Expense:

Strategy 1 - Omit Investment Expenses - For both the regular tax and the AMT, the deductible investment interest expense is limited to net investment income. It is taxable investment income reduced by investment expenses. Investment expenses are reported on Schedule A as investment taxes or as miscellaneous investment expenses. Both of these categories are not deductible for AMT purposes. Therefore, if the taxpayer is taxed by the AMT method, omit investment taxes and expenses from Schedule A. You may wish to double check your software's computation to see if it makes this adjustment automatically. To be on the safe side, simply don't deduct it. Caution: This may have an adverse effect on the state and overall tax liability.

Strategy 2 - Utilize the Capital Gains Election - Income that is subject to the long-term capital gains rates is not investment income for purposes of computing the net investment income limitation. However, the election to tax LTCG at ordinary rates and include that LTCG income as investment income applies to both the regular tax and the AMT. This will allow a larger deduction for investment interest for both the regular tax and the AMT. This adjustment is generally automatic in most tax preparation software. Therefore, if there is a planning reason not to utilize this election, the software will need to be overridden.

Regular Tax Exemptions:

Strategy 1 - Release of Claim to Exemption for Child of Divorced or Separated Parents - If a dependent's parents are utilizing Form 8332 (Release to Claim to Exemption for Child of Divorced or Separated Parents), care should be taken to evaluate who claims the child in light of the AMT implications. It would not be tax smart to release the claim to a parent who would not get any benefit from a reduction in income tax because of an increase in AMT.

Strategy 2 - Multiple Support Agreement - When several people together provide over 50% of a potential dependent's support, all who provide more than 10% of the support can agree which of them will claim the dependent. Care should be taken that the dependency is not assigned to an individual who is being taxed by AMT.

Depreciation:

Strategy 1 - Use AMT Depreciation Rates - Taxpayers who are regularly subject to the AMT should consider using the 150% declining balance method to avoid the AMT adjustment between the 150% and 200% methods.

Strategy 2 - Use the Section 179 Deduction - The Section 179 expense deduction is NOT a preference adjustment for AMT. Therefore, the 179 deduction can be used in place of the MACRS depreciation to avoid an AMT adjustment. If there is a limit on the 179 deduction of the taxpayer's circumstances, a partial 179 deduction can be combined with the 150% declining balance method to avoid AMT.

Miscellaneous Deductions:

Strategy 1 - Have IRA/Pension Fees Deducted from the Pension Accounts - Some taxpayers who wish to maximize their IRA and other pension accounts pay expenses to maintain those accounts directly (not have them deducted from the pension account). These individuals can then include those expenses in their miscellaneous Tier II itemized deductions. However, if they are subject to the AMT, they gain no benefit from those deductions and should consider having the fees deducted from the retirement accounts. This strategy also applies to taxpayers who lose the benefit of the deduction because of the AGI limitation and those who take the standard deduction.

Strategy 2 - Negotiate Accountable Reimbursement Plans with Employer - Taxpayers who have sufficient employee business expenses should attempt to negotiate an "accountable" reimbursement plan with their employer which would eliminate the need to claim the expenses as a miscellaneous deduction and essentially allow the expenses to be deducted from gross income.

Strategy 3 - Allocate Tax Fee to Other Schedules - Where possible, allocate tax preparation fees to other schedules such as C, E and F.

Strategy 4 - Accelerate or Defer Expenses to Non-AMT Tax Years - Where possible, accelerate or defer the Tier II deduction to a tax year where the taxpayer is not subject to the AMT.