



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

July 31, 2007

Number: **INFO 2007-0032**
Release Date: 9/28/2007

CONEX-131245-07
CC:ITA:04

UIL No.: 55.01-01

The Honorable David Scott
Member, U.S. House of Representatives
173 North Main Street
Jonesboro, GA 30236

Attention:

Dear Congressman Scott:

I am responding to your inquiry, dated June 26, 2007, on behalf of your constituents, . They asked about an amendment to section 55(b)(3) of the Internal Revenue Code (the Code) that the Congress included as part of the Working Families Tax Relief Act of 2004 (2004 Act). On July 27, 2007, and I discussed this issue, and the legal principles involved, with . The amendment changed the way the law taxes capital gains for purposes of calculating the alternative minimum tax (AMT).

To determine whether a taxpayer is liable for the AMT, the taxpayer must first calculate his or her regular tax liability. The taxpayer then makes a separate calculation to determine an alternative amount of taxable income, the AMTI. A taxpayer calculates the AMTI by taking into account a number of adjustments and preferences, which generally are income and deduction items treated less favorably in computing AMTI than when calculating regular taxable income. After the taxpayer has computed AMTI, he or she determines tentative minimum tax, or TMT, which is the excess of AMTI over an AMT exemption amount, multiplied by the applicable AMT tax rate. If TMT is greater than the regular tax liability, the taxpayer has an AMT liability to the extent of the excess.

asked how the law taxes capital gains for the AMT. In general, if the sale of a capital asset (almost everything an individual owns and uses for personal purposes or investment is a capital asset) held for more than one year results in a gain, the law taxes the gain at a lower tax rate than ordinary income. Similarly, for the AMT, if a taxpayer's AMTI includes a capital gain, the law taxes the AMT capital gain at the reduced capital gain rate.

The 2004 Act increased the amount of AMT capital gain permitted to be taxed at the lowest capital gain rate (presently 5 percent). Prior to the change, section 55(b)(3) of the Code limited the amount of AMT capital gain taxed at the lowest rate to the amount of capital gain actually taxed at the lowest capital gain rate for regular tax purposes. This amendment to the law did not change the AMT capital gain rate. Rather, the law change increased the amount of AMT capital gain allowed to be taxed at the lowest capital gain rate for certain taxpayers.

The 2004 change to section 55(b)(3) of the Code was effective for tax years ending after May 6, 1997. Taxpayers entitled to a refund as a result of the law change can file an amended tax return, Form 1040X, for the tax years for which they are entitled to a refund. However, not all taxpayers who paid AMT and had capital gains in the years affected by the law change are entitled to a refund. In general, a taxpayer would be entitled to a refund as a result of the amendment to section 55(b)(3) only if, for a taxable year, all of the taxpayer's taxable income for regular tax purposes was taxed at a rate below 25 percent and, in that same year, the taxpayer had capital gains in excess of taxable income.

Finally, even if a taxpayer is eligible to receive a refund, the taxpayer must generally file a Form 1040X by the later of 3 years from the due date of the return he or she is amending or 2 years from the date the taxpayer paid the tax. This office cannot accept claims for refund. Taxpayers must file refund claims with the office where they filed their original return.

I hope this information is helpful. If we can assist you further, please contact
or me at () .

Sincerely,

Michael J. Montemurro
Branch Chief
Office of Associate Chief Counsel
(Income Tax & Accounting)