



COMMISSIONER

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

November 13, 2012

The Honorable Orrin G. Hatch  
Ranking Member  
Committee on Finance  
United States Senate  
Washington, DC 20510

Dear Senator Hatch:

In response to recent requests, I am writing to update you on how the IRS is preparing for the 2013 tax filing season in light of the uncertainty related to several tax provisions that expired at the end of 2011 – principally the income thresholds for the Alternative Minimum Tax (AMT) – but also a number of temporary tax benefits generally known as “extenders.”

Each year, the IRS conducts in-depth planning during the summer to ensure that we are prepared for all aspects of the upcoming filing season – from training our customer service employees, to modifying forms and publications, to programming our technology systems to reflect changes in the tax law. This year has been particularly challenging due to several unresolved tax issues. When Congress takes action well after this planning process is underway, there is potential for substantial disruption to the filing season ahead.

As Congress returns this week, I wanted to provide you with a detailed description of the effects on IRS operational planning if the current uncertainty regarding the AMT and extenders continues.

***Alternative Minimum Tax (AMT)***

The AMT applies to individual taxpayers with incomes above specific thresholds set by law. For many years, Congress has been enacting “patches” to index these income thresholds for inflation in order to prevent millions of taxpayers from being subject to the AMT. The last such patch expired on December 31, 2011.

More specifically, for tax year 2011, the AMT exemption amount (as indexed for inflation) was \$48,450 for individuals and \$74,450 for married taxpayers filing jointly. Because of these thresholds, only about 4 million taxpayers paid AMT for tax year 2011. Under current law, however, the thresholds revert to much lower levels for 2012 – \$33,750 for individuals and \$45,000 for married taxpayers filing jointly. At these levels, approximately 33 million taxpayers would pay AMT for tax year 2012 (with returns filed in the spring of 2013). This is about 28 million more taxpayers who would pay the AMT than if the exemption amounts were increased as in the past.

In addition, the AMT patch has historically been accompanied by a special tax credit ordering rule that applies to all taxpayers claiming certain tax credits – whether they owe AMT or not. The ordering rules change the order in which a number of popular tax credits are applied against tax liability, and how they may be used to offset both regular and alternative minimum tax.

Taken together, the changes to the AMT exemption amount and the special tax credit ordering rules could affect more than 60 million taxpayers – nearly half of all individual income tax filers. In addition, the changes to the tax credit ordering rules that result from a lapse in the AMT patch are highly complex and cut deeply into the core tax processing logic of IRS's critical filing season technology systems.

In prior years – most recently 2007 and 2010 – Congress allowed the AMT patch to lapse for more than 11 months, but then retroactively reinstated it. In both 2007 and 2010, the IRS consulted with Congress and was provided with bipartisan, bicameral assurances that Congress was working expeditiously to enact a patch. The IRS, in turn, made a risk-based decision to leave its systems programmed assuming that Congress would continue its historical practice and again enact extensions of both the increased AMT exemption amount and the special tax credit ordering rules.

Consistent with past practice, I have instructed IRS staff again this year to leave our core systems “as-is” with respect to the AMT, and hold off on the substantial design and engineering work that would be required in order to revert the core tax systems back to 1998 law (which will otherwise apply for 2012 in the absence of any action by Congress). Therefore, if Congress enacts an AMT patch, including both increased exemption amounts and the special tax credit ordering rules, before the end of the 2012 calendar year, the IRS would likely be able to open the 2013 tax filing season with minimal delays for most taxpayers.

However, if there is no AMT patch enacted by the end of the year, the IRS would be forced to operate the 2013 tax filing season based on the expiration of the AMT patch. There would be serious repercussions for taxpayers.

Without an AMT patch, about 28 million taxpayers would be faced with a very large, unexpected tax liability for the current tax year (2012). In addition, in order to allow time for the IRS to make the programming changes necessary to conform our processing systems to reflect expiration of the AMT patch and the credit ordering rules, the IRS would, at minimum, need to instruct more than 60 million taxpayers that they may not file their tax returns or receive a refund until the IRS completes the necessary systems changes. Because of the magnitude and complexity of the changes, it is entirely possible that these taxpayers would not be able to file until late March 2013, if not even later. Tens of millions of these taxpayers would unexpectedly have to pay additional income tax for 2012, leaving them with a balance due return or a much smaller refund than expected. For millions of other taxpayers, refunds would be delayed.

Finally, because the AMT patch already expired at the end of 2011, there is no ability to consider partial year extensions of the AMT (since by the end of 2012 it would have already lapsed for an entire year).

### ***Tax "Extenders"***

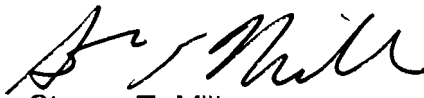
A number of other tax provisions affecting individuals also expired at the end of 2011. These include tax deductions for educators' out-of-pocket classroom expenses, tuition and related fees for higher education, and state and local sales taxes. The last provision is of particular importance to taxpayers in states with no income tax.

These tax law changes are generally not as complex and do not present anything near the operational risk associated with the AMT patch. Two years ago, Congress enacted legislation extending these provisions retroactively in mid-December 2010. As a result, the IRS made the necessary changes to its forms and systems, and delayed the opening of the 2011 filing season by four weeks for approximately 9 million affected taxpayers.

If the IRS were presented with a similar scenario of late enactment of tax extenders legislation this year, I would anticipate a similar outcome. There would be some inconvenience and delayed refunds for a substantial number of taxpayers, but the overall risk to the tax filing season would be manageable.

I hope this information is helpful, and I would be happy to discuss any of these issues in more detail. I am also writing to Chairman Baucus, Chairman Camp, and Ranking Member Levin. If you have questions, please contact me or have your staff contact Catherine Barrè, Director, Legislative Affairs, at (202) 622-3720.

Sincerely,

A handwritten signature in black ink, appearing to read "S. T. Miller", written in a cursive style.

Steven T. Miller  
Acting Commissioner