



Issue Brief: AMT AND TAX-EXEMPT BONDS

Updated April 2010

Background

The corporate alternative minimum tax (AMT) has an enormous impact on the investment decisions of corporations. It negatively affects their ability to invest in bonds issued by state and local governments used to finance infrastructure, including ports, water and sewer systems, public buildings and airports. Corporations are unable to deduct the interest from private activity tax-exempt bonds on their taxes, making these bonds less attractive as an investment.

The AMT applies to otherwise tax-exempt interest in two ways. First, all of the interest on tax-exempt private-activity bonds is subject to both individual and corporate AMT. As a result, interest rates paid by states and localities on these AMT bonds have historically been between 25 and 30 basis points (0.25 to 0.30 percentage points) higher than yields on other similar bonds – and in today's market, that basis point increase is even greater. In addition to subjecting the interest on private-activity bonds to the AMT, the Internal Revenue Code also subjects a portion of interest on public purpose tax-exempt bonds to the corporate AMT. Thus, the AMT blunts investor demand for both governmental and private-activity bonds.

Finally, more individuals are being impacted by the AMT under the current tax law. This has led to a growing concern that demand for tax-exempt bonds may be further diminished by individuals caught in the AMT scenario in addition to the marked reduction in corporate demand.

Congress, in the *2009 American Recovery and Reinvestment Act*, eliminated the application of AMT on private activity bonds issued in 2009 and 2010. The *Act* allows refundings done in 2009 and 2010 on bonds that were initially issued after Dec. 31, 2003 to also be exempt from the AMT.

Outlook: 2010

In addition to the two year reprieve of AMT application on private activity bonds included in the *The American Recovery and Reinvestment Act*, legislation to permanently exempt the application of the AMT on private activity bonds also has been introduced in both chambers (S. 138 and H.R. 425). Also, in March 2010, The House of Representatives acted to extend the AMT exclusion on private activity bonds through Dec. 31, 2011.

Related GFOA Public Policy Statements (see www.gfoa.org)

- Federal Tax Policy and Preserving the Tax-Exempt Status of Municipal Bonds (2005)
- Application of a Minimum Income Tax to Municipal Securities (1982)