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Proposed "Children of Fallen Warriors AMT Relief Act"

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Rep. John R. Carter of Texas has introduced H. R. 5529, the proposed "Children of Fallen Warriors AMT Relief Act." Sen. Richard Burr of North Carolina has introduced an identical bill (S. 3334) in the Senate. The purpose of the bills is to amend Section 59(j)(1) of the Internal Revenue Code so that annuity payments received under the Uniformed Services Survivor Benefit Plan (SBP) would be taxed as "earned income" (income derived from sources of employment).

The SBP was created by Congress in 1972 to prevent surviving military family members from becoming destitute. The SBP is the only means by which a deceased service member's survivors can receive a portion of his or her military retired pay.

Under current U.S. tax law, an annuity paid to a surviving child of a fallen U.S. military service member under the SBP is classified as "unearned Income." As a result of this tax classification, the SBP annuity payments are subject to the Alternative Minimum Tax ("AMT") and a twenty-six (26%) percent tax rate (much higher than they would be if classified as "earned income").

The Alternative Minimum Tax (AMT) was introduced by the Tax Reform Act of 1969 and went into effect in 1970. Its initial target was high-income families that were eligible for so many tax benefits (under the U.S. tax code of the time) they paid little or no federal income tax despite enormous incomes. In 1986, the Internal Revenue Code was amended and the AMT provisions were redirected at a different set of income tax deductions (personal exemption, state and local taxes, standard deduction, investment expenses, employee business expenses, medical expenses, etc.). In addition, while "regular" income tax brackets, exemptions and standard deductions are adjusted annually for inflation, the AMT brackets and exemptions are not. This results in more individuals becoming subject to the AMT annually as their incomes grow.

The AMT is best described as a separate income tax system that requires a second income tax calculation without the inclusion of many personal deductions. Taxpayers must calculate their federal income tax and then their AMT. If the AMT is higher, the taxpayer is responsible to pay that amount. The tax differential is a result of the AMT distinction between "earned income" (salary, wages, etc.) and "unearned Income." The AMT places a substantially higher tax rate on a taxpayer's unearned income.

Presently, payments received by a child of a deceased service member under the SBP are treated as "unearned income" for AMT purposes. This classification is contrary to the fact that if the service member had continued living he or she would have paid the "earned income" rate on the income that the SBP is intended to replace. The legislation introduced by Rep. Carter and Sen. Burr would amend the Internal Revenue Code to treat SBP payments as "earned income" and exempt the payments from the AMT. The Military Coalition (which includes ROA) has endorsed this legislation.