Day v. Commissioner, 108 T. C. 11 (1997)

The tax benefit rule under section 59(g) does not permit adjustments to increase the availability of section 29 nonconventional fuel source credits against regular income tax.

Summary

In Day v. Commissioner, the taxpayers sought to use the tax benefit rule under section 59(g) to exclude certain tax preference items from their alternative minimum taxable income (AMTI), thereby increasing their ability to apply section 29 credits against their regular income tax (RIT). The U. S. Tax Court held that such adjustments were not permissible, emphasizing the statutory limitations on section 29 credits and the discretionary nature of section 59(g). The decision underscored the distinct differences between the alternative minimum tax (AMT) and the previous add-on minimum tax regime, and clarified that the section 29 credits not used due to the AMT could be carried forward indefinitely.

Facts

Roy E. and Linda Day invested in oil and gas properties, generating section 29 nonconventional fuel source credits. For the tax years 1988 through 1990, they had depletion, intangible drilling costs, and other tax preference items. These preferences reduced their taxable income, but also limited their ability to use section 29 credits against their RIT due to the AMT. The Days argued that they should be allowed to exclude these preferences from their AMTI under section 59(g) to increase their section 29 credit usage.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the Days’ federal income taxes for 1988, 1989, and 1990. The Days petitioned the U. S. Tax Court, seeking to apply the tax benefit rule to adjust their AMTI. The case was reassigned to Judge Arthur L. Nims, III, who issued the final decision.

Issue(s)

1. Whether the Days can utilize section 59(g) to exclude tax preference items from their AMTI, thereby increasing the extent to which they can apply section 29 credits against their RIT.

Holding

1. No, because the tax benefit rule under section 59(g) is discretionary and does not apply to increase the section 29 credit limitation, as the credits not used due to the AMT can be carried forward indefinitely under section 53.

Court’s Reasoning

The court emphasized that the AMT system was designed to ensure a minimum tax liability regardless of tax breaks available under the RIT. The Days’ argument to exclude preferences from AMTI would effectively circumvent the statutory limitation on section 29 credits, allowing them to apply these credits against the AMT itself, which is not permitted. The court distinguished this case from First Chicago Corp. v. Commissioner, noting that the add-on minimum tax at issue in that case was fundamentally different from the AMT. The discretionary nature of section 59(g) and the availability of indefinite carryovers for unused section 29 credits under section 53 further justified the court’s decision. The court also noted that the Days did receive a current tax benefit from their preferences, as these reduced their RIT beyond what their section 29 credits could offset.

Practical Implications

This decision clarifies that taxpayers cannot use the tax benefit rule to manipulate their AMTI in order to increase the use of section 29 credits against RIT. Practitioners should be aware that the AMT system’s design to ensure a minimum tax liability remains intact, and that the carryover provisions of section 53 provide an alternative relief mechanism for unused credits. This ruling affects how similar cases involving the interaction of AMT and nonconventional fuel source credits should be analyzed, reinforcing the importance of statutory limitations and the distinct nature of the AMT from previous minimum tax regimes. Subsequent cases have adhered to this interpretation, ensuring that taxpayers with similar credits understand the limitations and available carryover options.

