



2023 Study Cards



SEE

Special Enrollment Exam
Part 1 - Individuals

2022 Filing Requirements

A taxpayer (T/P) must file a return if his or her gross income was at least the amount shown on the following chart:

Filing Status	Age*	Gross Income**
Single	Under 65	\$12,950
	65 or older	\$14,700
Married filing jointly	Both spouses are under 65	\$25,900
	One spouse is 65 or older	\$27,300
	Both spouses are 65 or older	\$28,700
Married filing separately	Any age	\$5
Head of household	Under 65	\$19,400
	65 or older	\$21,150
Qualifying surviving spouse	Under 65	\$25,900
	65 or older	\$27,300

*If T/P turns 65 on January 1, 2023, T/P is considered 65 at end of 2022. **Gross Income = standard deduction

2022 Filing Requirements Dependents

A dependent must file a tax return if any of the following apply:

Single Dependent

- ▶ Unearned income was more than \$1,150 (\$2,900 if age 65 or older **OR** blind; \$4,650 if age 65 or older **AND** blind).
- ▶ Earned income was more than \$12,950 (\$14,700 if age 65 or older **OR** blind; \$16,450 if age 65 or older **AND** blind).
- ▶ Gross income was more than the larger of:
 1. \$1,150 (\$2,900 if age 65 or older **OR** blind; \$4,650 if age 65 or older **AND** blind), or
 2. Earned income (up to \$12,550) plus \$400 (\$2,150 if age 65 or older **OR** blind; \$3,900 if age 65 or older **AND** blind).

Married Dependent

- ▶ Gross income was at least \$5 and spouse files separate return and itemizes deductions.
- ▶ Unearned income was \$1,150 (\$2,550 if age 65 or older **OR** blind; \$3,950 if age 65 or older **AND** blind).
- ▶ Earned income was more than \$12,950 (\$14,350 if age 65 or older **OR** blind; \$15,750 if age 65 or older **AND** blind).
- ▶ Gross income was more than the larger of:
 1. \$1,150 (\$2,550 if age 65 or older **OR** blind; \$3,950 if age 65 or older **AND** blind) or,
 2. Earned income (up to \$12,550) plus \$400 (\$1,800 if age 65 or older **OR** blind; \$3,200 if age 65 or older **AND** blind).

2022 Filing Requirements Self-Employed Taxpayers

Taxpayers must file a return if:

1. Their net earnings from self-employment (excluding church employee income) were \$400 or more, or
2. They had church employee income of \$108.28 or more.

Gross income from self-employment. Gross income from self-employment includes the amount of gross income on line 7 of Schedule C (Form 1040 or 1040-SR), Profit or Loss From Business and gross income on line 9 of Schedule F (Form 1040 or 1040-SR), Profit or Loss From Farming.

Types of Self-Employment Income:

- ▶ Income from sole proprietorship and non-employee compensation.
- ▶ Corporate director fees.
- ▶ Partnership income from partnership operating a business (unless limited partner).
- ▶ Guaranteed payment from a partnership (including limited partners).
- ▶ Bartering income.
- ▶ Real estate rent (if received as a real estate dealer).
- ▶ Income paid to retired insurance agents based on commissions received prior to retirement.
- ▶ Interest received in a trade or business.
- ▶ Net earnings of members of the clergy (unless taken a vow of poverty).
- ▶ Gains and losses by a dealer in options or commodities from dealing or trading in section 1256 contracts or property related to those contracts.
- ▶ A professional fiduciary who administers a deceased person's estate.

2022 Filing Requirements Resident Aliens

Resident Aliens, who reside in the U.S. for the entire year, must file their tax returns using the same rules that apply to U.S. Citizens. A resident alien's income is subject to the same manner as a U.S. Citizen and must report all income whether from sources within or outside the U.S.

Resident alien. A resident alien is an individual who is not a citizen or national of the United States and who meets either the green card test or the substantial presence test for the calendar year:

1. **Green card test.** T/P is a U.S. resident if T/P was a lawful permanent resident of the United States at any time during the calendar year. This is known as the green card test because resident aliens hold immigrant visas (also known as green cards).
2. **Substantial presence test.** A T/P is considered a U.S. resident if T/P meets the substantial presence test for the calendar year. To meet this test, T/P must be physically present in the United States on at least:
 - a) 31 days during the current calendar year, and
 - b) A total of 183 days during the current year and the 2 preceding years, counting all the days of physical presence in the current year, but only $\frac{1}{3}$ the number of days of presence in the first preceding year, and only $\frac{1}{6}$ the number of days in the second preceding year.

Dual-status aliens. If a person is a U.S. resident for the calendar year, but is not a U.S. resident at any time during the preceding calendar year, the person is a U.S. resident only for the part of the calendar year that begins on the residency starting date. The person is a nonresident alien for the part of the year before that date.

Filing Requirements Nonresident Alien

How income of nonresident aliens is taxed. A nonresident alien usually is subject to U.S. income tax only on U.S. source income. A nonresident alien's income that is subject to U.S. income tax must be divided into two categories:

1. Income that is effectively connected with a trade or business in the U.S., and
2. Income that is not effectively connected with a trade or business in the U.S.

The difference between these two categories is that effectively connected income, after allowable deductions, is taxed at graduated rates. These are the same rates that apply to U.S. citizens and residents. Income that is not effectively connected is taxed at a **flat 30%** (or lower treaty) rate.

Effectively connected income (ECI). If a T/P is engaged in a U.S. trade or business, all income, gain, or loss for the tax year that a taxpayer gets from sources within the U.S. (other than certain investment income) is treated as ECI. This applies whether or not there is any connection between the income and the trade or business being carried on in the U.S. during the tax year. Investment income will be considered to be ECI if:

- ▶ The income is associated with U.S. assets used in, or held for use in, the conduct of that trade or business; or
- ▶ The activities of that trade or business conducted in the U.S. are a material factor in the realization of the income.

Deductions are allowed against ECI, and net ECI is taxed at the same graduated rates used by U.S. citizens.

Filing Requirements

Nonresident Alien

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Fixed or determinable annual or periodical income (FDAP). FDAP income consists primarily of passive investment income — interest, dividends, rents, royalties, etc. In theory, FDAP income may consist of any kind of U.S. source income attributable to a foreign person. FDAP income may or may not be effectively connected with a U.S. business. For example, effectively connected income includes rents from real property if the nonresident alien chooses to treat that income as effectively connected with a U.S. business. Deductions are not allowed against FDAP income, and it is taxed at a flat 30% rate or lesser rate under a tax treaty.

30% Withholding Tax. U.S. payers of income other than wages, such as dividends and royalties are required to withhold tax at a flat **30%** on nonwage income paid to nonresident aliens.

Filing Requirements

Nonresident Alien

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Deductions. Nonresident aliens can claim similar deductions that resident aliens can claim. However, nonresident aliens can claim only deductions related to income that is effectively connected with their U.S. trade or business.

Standard deductions. Nonresident aliens cannot claim the standard deduction unless they are students and business apprentices from India who are eligible for the benefits of Article 21(2) of the US-India Income Tax Treaty.

Itemized Deductions. Nonresident aliens can deduct certain itemized deductions if they receive income effectively connected with a U.S. trade or business. These deductions include state and local income taxes, charitable contributions to U.S. organizations, and casualty and theft losses. Use Schedule A of Form 1040-NR to claim itemized deductions.

Filing Requirements Nonresident Alien

Filing requirements. Nonresident aliens are required to file an income tax return (Form 1040-NR) if they are any of the following:

1. A nonresident alien individual engaged or considered to be engaged in a trade or business in the United States during the year. A nonresident alien individual must file even if:
 - a) The nonresident alien had no income from a trade or business conducted in the U.S.,
 - b) The nonresident alien had no income from U.S. sources, or
 - c) The nonresident alien's income is exempt from income tax.
2. A nonresident alien individual not engaged in a trade or business in the United States with U.S. income on which the tax liability was not satisfied by the withholding of tax at the source.
3. A representative or agent responsible for filing of an individual in (1) or (2) above.
4. A fiduciary for a nonresident alien estate or trust.

Filing Requirements Nonresident Alien

Exceptions. Nonresident aliens do not need to file Form 1040-NR or Form 1040-NR-EZ if they meet either of the following conditions:

1. The alien was a nonresident alien student, teacher, or trainee who was temporarily present in the U.S. under an “F,” “J,” “M,” or “Q” visa and has no income that is subject to tax.
2. The alien was a student or business apprentice who was eligible for the benefits of Article 21 (2) of the United States–India Income Tax Treaty, was single or a qualifying surviving spouse, and gross income for 2022 was less than or equal to \$12,950 if single (\$25,900 if a qualifying surviving spouse).
3. The alien was a partner in a U.S. partnership that was not engaged in a trade or business in the U.S. during 2022 and his or her Schedule K-1 (Form 1065) includes only income from U.S. sources that is not effectively connected with a U.S. trade or business.

Filing Requirements Filing Due Dates

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Taxpayer (calendar year)	Form	Due Date*	Due Date with Extension
Most Taxpayers	Form 1040	April 15	October 15
Taxpayers Outside the U.S.	Form 1040	June 15	October 15
Decedent Taxpayer	Form 1040	April 15	October 15
Resident Aliens	Form 1040	April 15	October 15
Nonresident Aliens with wages subject to withholding	Form 1040-NR	April 15	October 15
Nonresident Aliens without wages subject to withholding	Form 1040-NR	June 15	October 15

* If the due dates above land on a holiday or weekend, the due date is the next business day.

Automatic extension. A T/P may obtain an automatic 6-month extension of time to file a U.S. individual income tax return in one of the following ways:

1. Electronically file Form 4868, Application For Automatic Extension of Time To File U.S. Individual Tax Return, using tax software with a personal computer.
2. Pay all or part of the estimated taxes due using a credit or debit card or by using the Electronic Federal Tax Payment System (EFTPS).
3. File a paper Form 4868 by mail.

Payment of tax. An extension of time to file is not an extension of time to pay. The T/P must make an accurate estimate of tax liability for that year and pay any amount due with the extension. If the T/P cannot pay the full amount of tax due, he or she can still get the extension. The T/P will owe interest on the unpaid amount.

Taxpayers outside the U.S. A T/P is allowed an automatic 2-month extension to file his or her the tax return and pay any federal tax due if the T/P is a U.S. citizen or resident and on the regular due date of the return:

1. Was living outside the U.S. and Puerto Rico, and his or her main place of business or post of duty is outside the U.S. and Puerto Rico, or
2. Is in the military or naval service on duty outside the U.S. and Puerto Rico.

Extension beyond 2 month. Taxpayers who cannot file their returns within the automatic 2-month extension, can get an additional 4-month extension by filing Form 4868 (check box on line 8).

Extension period for individuals serving in combat zone. For individuals serving in a combat zone, the deadline for filing a return, paying any tax due, and filing a claim for refund is extended for at least 180 days after the later of:

1. The last day T/P is in a combat zone or the last day the area qualifies as a combat zone, or
2. The last day of any continuous qualified hospitalization for injury from service in the combat zone.

Postponed tax deadlines affected by a federally declared disaster. The IRS may postpone for up to one year certain tax deadlines of T/Ps who are affected by a federally declared disaster. The tax deadlines the IRS may postpone include those for filing income, excise, and employment tax returns, paying income, excise, and employment taxes, and making contributions to a traditional IRA or Roth IRA.

Mandatory 60-day extension. Certain T/P's affected by a federally declared disaster that occurs after December 20, 2019, may be eligible for a mandatory 60-day extension for certain tax deadlines such as filing or paying income, excise, and employment taxes; and making contributions to a traditional IRA or Roth IRA.

Filing Status

Marital Status

Unmarried persons. A T/P is considered unmarried for the entire year if, on the last day of the tax year, the T/P is either:

- ▶ Unmarried, or
- ▶ Legally separated from a spouse under a divorce or separate maintenance decree. State law governs whether A T/P is married or legally separated under a divorce or separate maintenance decree.

Considered married. T/P is considered married for the entire year if on the last day of the year the T/P and spouse meet any one of the following tests:

1. Married and living together.
2. Living together in a common law marriage that is recognized in the state of residence or in the state where the common law marriage began.
3. Married and living apart, but not legally separated under a decree of divorce or separate maintenance.
4. Separated under an interlocutory (not final) decree of divorce. For purposes of filing a joint return, the T/P is not considered divorced.

Death of spouse. If a spouse died during the year, the T/P is considered married for the entire year. If surviving spouse remarried before the end of the year, he or she may file a joint return with the new spouse. A joint return cannot be filed with the deceased spouse. The deceased spouse's filing status is married filing separately for that year.

There are five (5) filing statuses:

1. Single (S).
2. Married Filing Jointly (MFJ).
3. Married Filing Separately (MFS).
4. Head of Household (H/H).
5. Qualifying Surviving Spouse (QSS).

Single

A T/P's filing status is single if he or she is unmarried or legally separated from his or her spouse under a divorce or separate maintenance decree and does not qualify for another filing status. A T/P is considered unmarried for the entire year if, on the last day of the year, the T/P is unmarried or legally separated from spouse under a signed divorce or separate maintenance decree.

Filing Status

Married Filing Jointly

In order to file jointly both spouses must:

1. Include all their income and deductions on the joint return, and
2. Use the same accounting period (spouses can use different accounting methods).

Nonresident alien and dual-status alien. A joint return generally cannot be filed if either spouse is a nonresident alien at any time during the year. However, if at the end of the year one spouse was a nonresident alien or dual-status alien married to a U.S. citizen or resident, both spouses may choose to file a joint return. Both spouses will be taxed as U.S. citizens or residents for the entire tax year.

Annulled marriages. If an individual obtains a court decree of annulment (which holds that no valid marriage ever existed), that individual must file amended returns claiming a filing status of single or head of household, whichever applies, for all prior tax years affected by the annulment that are not closed by the statute of limitations.

Joint responsibility. Both spouses may be held responsible, jointly and individually, for the tax and any interest or penalty due on a joint return. One spouse may be held responsible for all the tax due even if all the income was earned by the other spouse. A T/P may want to file separately if:

- ▶ T/P believes his or her spouse is not reporting all of his or her income, or
- ▶ T/P does not want to be responsible for any taxes due if the spouse does not have enough tax withheld or does not pay enough estimated tax.

Filing Status

Married Filing Jointly

Relief from joint responsibility. In some cases, one spouse may be relieved of joint liability for tax, interest, and penalties on a joint return for items of the other spouse that were incorrectly reported on the joint return. A T/P can ask for relief no matter how small the liability. There are three types of relief available:

1. **Innocent spouse relief.** T/P must meet all of the following conditions to qualify for innocent spouse relief:
 - a) Filed a joint return which has an understatement of tax due to erroneous items of T/P's spouse (or former spouse).
 - b) Establish that at the time T/P signed the joint return T/P did not know, and had no reason to know, that there was an understatement of tax.
 - c) Taking into account all the facts and circumstances, it would be unfair to hold T/P liable for the understatement of tax.
2. **Separation of liability.** Applies to joint filers who are divorced, widowed, legally separated, or have not lived together for the 12 months ending on the date election of this relief is filed.
3. ***Equitable relief.*** Applies to all joint filers who do not qualify for innocent spouse relief or separation of liability and to married couples filing separate returns in community property states.

Filing Status

Married Filing Jointly

Community property laws. A T/P must follow community property laws when filing a tax return if married and live in a community property state. Generally, community property laws provide that the T/P and spouse are both entitled to one-half of the total community income and expenses. If the T/P and spouse filed a joint return in a community property state, both spouses are jointly and severally liable for the total liability on the return. However, community property laws are not taken into account in determining whether an item belongs to the T/P or spouse (or former spouse) if requesting relief from joint and several liability.

Relief From Liability for Tax Attributable to an Item of Community Income. A T/P is not responsible for the tax relating to an item of community income if all the following conditions exist.

1. Did not file a joint return.
2. Did not include the item of community income in gross income.
3. The item of community income did not include (a) spouse's wages, salaries or other compensation; (b) spouse's business income; (c) spouse's share of partnership income; (d) spouse's income from separate property; and (e) any other income belonging to spouse under community property law.
4. T/P established that he or she did not know of, and had no reason to know of, that community income.
5. Under all facts and circumstances, it would not be fair to include the items of community property in the T/P's gross income.

Filing Status

Married Filing Jointly

Relief from Joint responsibility (cont.)

When to file Form 8857. A T/P should file Form 8857, Request for Innocent Spouse Relief, as soon as the T/P becomes aware of a tax liability for which he or she believes only the spouse or former spouse should be held responsible. However, the T/P generally must file Form 8857 no later than 2 years after the first IRS attempt to collect the tax from the T/P.

Exception for equitable relief. The amount of time to request equitable relief depends on whether the T/P is seeking relief from a balance due, seeking a credit or refund or both.

- ▶ **Balance due.** Generally, must file a request within the time period the IRS has to collect the tax (10 years).
- ▶ **Credit or Refund.** Generally, must file a request within 3 years after the date the original return was filed or within 2 years after the date the tax was paid, whichever is later.

Exception for relief from liability for tax attributable to an item of community income. A T/P must file Form 8857 no later than 6 months before the expiration of the period of limitations on assessment (including extensions) against the T/P's spouse or former spouse for the tax year for which the T/P is requesting relief. However, if the IRS begins an examination of the T/P's return during that 6-month period, the latest time for requesting relief is 30 days after the date of the IRS' initial contact letter to the T/P. The period of limitations on assessment is the amount of time, generally 3 years, that the IRS has from the date the return is filed to assess taxes that are owed.

Filing Status

Married Filing Separately

Married filing separately. If spouses file separate returns, each spouse reports only his or her own income, deductions, and credits on his or her individual return. A taxpayer can file a separate return even if his or her spouse had no income.

Separate liability. When spouses file separately, each spouse is responsible only for the tax due on his or her own return.

Itemized deductions. If spouses file separate returns and one spouse itemizes deductions, the other spouse cannot use the standard deduction and should also itemize deductions.

Community property states. If a T/P lives in AZ, CA, ID, LA, NV, NM, TX, WA, or WS and files separately, the T/P's income may be considered separate income or community income for income tax purposes. If the spouses file separately, each spouse must report half of all community income and all of his or her separate income on his or her federal tax return.

Filing Status

Married Filing Separately

Community property. Generally, community property is property:

- ▶ That the T/P, his or her spouse (or registered domestic partner), or both acquire during the marriage (or registered domestic partnership) while the T/P and spouse (or registered domestic partner) are domiciled in a community property state.
- ▶ That the T/P and his or her spouse (or registered domestic partner) agreed to convert from separate to community property.
- ▶ That cannot be identified as separate property.

Community income. Generally, community income is income from:

- ▶ Community property.
- ▶ Salaries, wages, and other pay received for the services performed by the taxpayer, his or her spouse (or registered domestic partner), or both during the marriage (or registered domestic partnership) while domiciled in a community property state.
- ▶ Real estate that is treated as community property under the laws of the state where the property is located.

Identifying income, deductions, and credits (Form 8958). If spouses (or domestic partners) file separate returns, each spouse must attach Form 8958, Allocation of Tax Amounts Between Certain Individuals in Community Property States, to his or her Form 1040 or 1040-SR to identify the community and separate income, deductions, credits, and other return amounts according to the laws of the state of domicile.

Filing Status

Married Filing Separately

Special rules which apply to married filing separately status:

1. If one spouse itemizes deductions, the other spouse must also itemize deductions.
2. T/P cannot take the credit for child and dependent care expenses in most cases, and the amount that can exclude from income under an employer's dependent care assistance program is limited to \$2,500 (instead of \$5,000).
3. T/P cannot take the education credits (the American opportunity and lifetime learning credits), or the deduction for student loan interest.
4. T/P cannot take the earned income credit unless separated from spouse at the end of the year and meet certain requirements.
5. If T/P lived with spouse at any time during the tax year:
 - a) T/P cannot take the credit for the elderly or the disabled, and
 - b) T/P may have to include more (up to 85%) Social Security benefits received.
6. T/P cannot exclude any interest income from qualified U.S. Savings Bonds that was used for higher education expenses.
7. T/P cannot take the credit for adoption expenses in most cases.
8. T/P may have a smaller child tax and retirement savings contribution credit than if filing jointly.
9. T/P's capital loss deduction limit is \$1,500 instead of \$3,000 if filing a joint return.

Joint return after separate returns. If T/P and spouse file separate returns, they may change to a joint return any time within 3 years from the due date of the separate returns. Once a joint return is filed, the spouses cannot choose to file separate returns for that year after the due date of the return.

Filing Status Head of Household

To file as head of household, a T/P must meet all of the following requirements:

1. Be unmarried or considered unmarried on the last day of the year.
2. Have paid more than half the cost of keeping up a home that was the main home for more than half the year for the T/P and any of the following:
 - a) A qualifying child.
 - b) A qualifying relative.

Note: A dependent can qualify only one T/P to use the head of household filing status for any year.

Special rule for parent. The T/P may file as head of household even if a parent whom the T/P claims as a dependent does not live with T/P. The T/P must pay more than half the cost of keeping up a home that was the main home for the entire year for a parent or pay more than half the cost of keeping a parent in a rest home or home for the elderly.

Temporary absences. T/P and his or her qualifying child or relative are considered to live together even if one or both are temporarily absent from the home due to special circumstances such as:

- | | |
|-------------|------------------------------------|
| ▶ Education | ▶ Vacation |
| ▶ Illness | ▶ Military service |
| ▶ Business | ▶ Detention in a juvenile facility |

Filing Status Head of Household

Considered unmarried. A T/P is considered unmarried on the last day of the tax year if he or she meets all the following tests:

1. Filed a separate tax return. A separate return includes a return claiming married filing separate, single, or head of household filing status.
2. Paid more than half the cost of keeping up a home for the tax year.
3. Not have lived with spouse during the last 6 months of the tax year.
4. T/P's home was the main home for T/P's child, stepchild, or eligible foster child for more than half the year.
5. Must be able to claim the child as a dependent. T/P can still meet this test if child was not claimed because noncustodial parent is allowed to claim the child as a dependent.

Filing Status

Qualifying Surviving Spouse

A T/P may use married filing jointly in the year spouse dies and qualifying surviving spouse, if eligible, in the following two years. To be eligible, T/P must meet all of the following tests:

1. Be entitled to file a joint return with spouse for year spouse dies.
2. Did not remarry before the end of the tax year.
3. Have a child, stepchild, or adopted child, (not a foster child) who qualifies as a dependent except that:
 - ▶ The child had gross income of \$4,400 or more
 - ▶ The child filed a joint return, or
 - ▶ The T/P can be claimed as a dependent on someone else's return.
4. The child lived in the T/P's home all year, except for temporary absences.
5. Paid more than half the cost of keeping up a home for the year.

Death or birth. A T/P may be eligible to file as a qualifying surviving spouse if the child who qualifies the T/P for this filing status is born or dies during the year. The T/P must have provided more than half of the cost of keeping up a home that was the child's main home during the entire part of the year he or she was alive.

Dependency Tests

T/P must list either the social security number or taxpayer identification number (TIN) or adoption taxpayer identification number (ATIN) of every person for whom T/P claims as a dependent. A person can be claimed as a dependent if he or she is a qualifying child or qualifying relative and meets the following three tests:

1. **Dependent taxpayer test.** The T/P cannot claim any dependents if the T/P can be claimed as a dependent by another person.
2. **Joint return test.** A T/P cannot claim a married person who files a joint return as a dependent.
Exception: The dependent filed a joint return merely as a claim for refund and no tax liability would exist for either spouse on separate returns.
3. **Citizenship or resident test.** To meet this test, the person must be a U.S. citizen or resident alien, or a resident of Canada or Mexico.

Qualifying child tests. The following are the five tests that must be met for a child to be a qualifying child:

1. **Relationship test.** To meet this test, a child must be:
 - a) A son, daughter, stepchild, adopted child, eligible foster child, or a descendant (e.g., grandchild) of any of them, or
 - b) A brother, sister, half brother, half sister, stepbrother, stepsister, or a descendant (e.g., niece or nephew) of any of them.
2. **Age test.** To meet this test, a child must be:
 - a) Under age 19 at the end of the year and younger than T/P (or spouse if filing jointly),
 - b) A full-time student under age 24 at the end of the year and younger than T/P, or
 - c) Permanently and totally disabled at any time during the year, regardless of age.
3. **Residency test.** To meet this test, a child must have lived with the T/P for more than half of the year. A child is considered to have lived with the T/P during periods of time when either the T/P or child or both, are temporarily absent due to special circumstances such as illness, education, business, vacation, military service or detention in a juvenile facility. A child who died during the year is treated as having lived with T/P all year if T/P's home was the child's home the entire time he or she was alive during the year. T/P can claim a child as a dependent who was born alive during the year, even if the child lived only for a moment. There must be proof of a live birth shown by an official document (e.g., birth certificate).

Qualifying Child Tests (cont.)

4. **Support test.** To meet this test, the child cannot have provided more than half of his or her own support for the year.

5. **Joint return test.** To meet this test, the child cannot file a joint return for the year.

Exception: The joint return test does not apply if the child and his or her spouse file a joint return merely as a claim for refund.

Special test for qualifying child of more than one person. If a T/P and another person have the same qualifying child, use the following tie-breaker rules:

- ▶ If only one of the persons is the child's parent, the child is the qualifying child of the parent.
- ▶ If the parents do not file a joint return together, the child is the qualifying child of the parent with whom the child lived for the longer period of time during the year.
- ▶ If no parent can claim the child as a qualifying child, the child is treated as the qualifying child of the person who had the highest AGI for the year.
- ▶ If a parent can claim the child as a qualifying child but no parent claims the child, the child is treated as the qualifying child of the person who had the highest AGI for the year, but only if that person's AGI is higher than the highest AGI of any of the child's parents who can claim the child.

Qualifying Relative Tests

There are four tests that must be met for a person to be a qualifying relative:

1. **Not a qualifying child test.** A child is not a qualifying relative if the child is the taxpayer's qualifying child or the qualifying child of any other taxpayer.
2. **Member of household or relationship test.** To meet this test, a person must either:
 - a) Live with the taxpayer all year as a member of household, or
 - b) Be the taxpayer's child, stepchild, eligible foster child or a descendant of any of them, sibling, step-sibling, half-sibling, parent, step parent, foster parent, any of these relationships established through marriage (in-laws), uncle, aunt, niece, and nephew. Any of these relationships that were established by marriage are not ended by death or divorce.
3. **Gross income test.** To meet this test, a person's gross income for the year must be less than \$4,400. Gross income is all income (in the form of money, property, and services) that is not exempt from tax. Gross receipts from rental property are gross income. Do not deduct taxes, repairs, etc., to determine the gross income from rental property. Gross income includes a partner's share of the gross, not a share of the net partnership income.
4. **Support test.** To meet this test, a taxpayer must provide more than half of a person's total support during the calendar year.

Support Test (To be a qualifying relative)

T/P must provide more than half of a person's total support. Items included in support:

- ▶ Food
- ▶ Clothing
- ▶ Education
- ▶ Transportation
- ▶ Recreation
- ▶ Medical and Dental Care
- ▶ Medical Insurance
- ▶ Lodging (FMV of the room, apartment, or house in which person lives)
- ▶ Other similar necessities

Items not included in total support:

1. Federal, state, and local income taxes paid by persons from their own income.
2. Social security and Medicare taxes paid by persons from their own income.
3. Life insurance premiums.
4. Funeral expenses.
5. Scholarships received by a child if the child is a student.
6. Survivors' and dependents' educational assistance payments used for support of the child who received them.

Support Test (To be a qualifying child or relative)

Figuring support. Compare the amount contributed by T/P to the person's support with the total amount of support the person received from all sources. This includes the person's own funds used for support. A person's own funds are not support unless they are actually spent for support.

Tax-exempt income. In figuring a person's total support, include tax-exempt income, savings, and borrowed amounts used to support that person.

Child support. All child support payments actually received from the noncustodial parent are considered used for the support of the child. If the support payments are more than the amount required for this year, any payment for an earlier year is not support provided by the noncustodial parent for either the earlier year or for this year.

Support Test for Children of Divorced or Separated Parents

Custodial parent. The custodial parent is the parent with whom the child lived for the greater number of nights during the year. The other parent is the noncustodial parent.

Noncustodial parent. A child will be treated as a qualifying relative of the noncustodial parent if all four of the following apply:

1. The parents are either divorced or legally separated under a decree, separated under a written separation agreement, or have lived apart during the last 6 months of the year.
2. The child received over half of his or her support for the year from both parents.
3. The child is in the custody of one or both parents for more than half the year.
4. Either of the following statements is true.
 - a) The custodial parent signs a written declaration (Form 8332) that he or she will not claim the child as a dependent for the year and the noncustodial parent attaches this written declaration to his or her return.
 - b) A pre-1985 decree of divorce or separate maintenance or written separation agreement that applies to the tax year states that the noncustodial parent can claim the child as a dependent and the noncustodial parent provides at least \$600 for the support of the child during the year.

Gross Income Employee Compensation

An employee must include in income the following compensation and fringe benefits:

- ▶ Advance commissions
- ▶ Back pay awards
- ▶ Bonuses and awards
- ▶ Employer provided child care assistance
- ▶ Christmas gifts (that can be exchanged for cash)
- ▶ Employer's allowances or reimbursements from a nonaccountable plan
- ▶ Property purchased from employer (if purchased below market value)
- ▶ Property received for services (FMV)
- ▶ Severance pay
- ▶ Accrued leave payment
- ▶ Sick pay
- ▶ Stock appreciation rights (if exercised)
- ▶ Stock options (if exercised)
- ▶ Unemployment compensation
- ▶ Supplement unemployment benefits
- ▶ Union benefits
- ▶ Strike and lockout benefits
- ▶ Employer-provided commuter highway vehicle and transit passes exceeding \$280 a month
- ▶ Employer-provided qualified parking exceeding \$280 a month
- ▶ Employer-provided financial counseling program
- ▶ Off-premises athletic facilities
- ▶ Employer-provided car for personal use
- ▶ Group-Term Life Insurance over \$50,000 of coverage

Gross Income Employee Compensation

Fringe Benefits

Type of Fringe Benefit	Tax Treatment
Accident or health plan	Value of plan is nontaxable. Benefits received taxable if paid by employer.
Achievement awards	Nontaxable up to \$1,600 for qualified plan awards (\$400 for nonqualified awards).
Adoption assistance	Nontaxable up to \$14,890.
Athletic facilities	Nontaxable if used by employees, their spouses, and their dependent children and the facility is operated by the employer on premises owned or leased by the employer.
De minimis (minimal) benefits	Nontaxable for property or services provided by employer that have little value such as holiday gifts or tickets to theater or sporting events. Cannot be cash or cash equivalent benefit.
Dependent care assistance	Nontaxable up to \$5,000 (\$2,500 if married filing separate).
Educational assistance	Nontaxable up to \$5,250.
Employee discounts	Nontaxable up to 20% of the price charged nonemployee customers for the service.

Gross Income Employee Compensation

Fringe Benefits (cont.)

Type of Fringe Benefit	Tax Treatment
Group-term life insurance coverage	Nontaxable up to cost of \$50,000 of coverage.
Health savings accounts (HSAs)	Nontaxable for qualified individuals up to the HSA contribution limits.
Holiday gifts	Nontaxable if items like turkey, ham, or other items of nominal value. Taxable if cash, gift certificate, or similar items exchanged for cash.
Lodging on employer's business premises	Nontaxable if furnished for employer's convenience as a condition of employment.
Meals	Nontaxable if furnished on employer business premises for employer convenience.
Moving expense reimbursements	Exclusion from income for members of the U.S. Armed Forces on active duty only.
No-additional-cost services	Nontaxable.
Retirement planning services	Nontaxable if employer maintains a qualified retirement plan.
Transportation (commuting) benefits	Nontaxable up to \$280/month for qualified parking, \$280/month for transit passes.

Gross Income Employee Compensation

Clergy

A member of the clergy must include in income offerings and fees received for marriages, baptisms, funerals, etc., in addition to salary. If the offering is made to the religious institution, it is not taxable. If a member of a religious organization gives outside earnings to the organization, the earnings are still included in gross income and a charitable deduction is allowed.

The rental value of a home (or utility expenses) provided to an ordained, licensed or commissioned minister as part of pay is not income.

Housing allowance is not taxable if used to pay household expenses in the year received. Any housing allowance not used to pay household expenses is considered income. A member of the clergy can deduct qualified mortgage interest and real estate taxes paid even if nontaxable housing allowance funds are used to make the payments.

Self-employment tax. Include rental value of home and housing allowances as earnings from self-employment for figuring self-employment tax if the T/P is subject to the self-employment tax. Members of a religious order who have taken a vow of poverty are not subject to self-employment tax on earnings for performing duties required by the order.

Gross Income Tips

When to Report Tips to Employer

Less than \$20 in one month. If T/P receives less than \$20 in tips while working for one employer during a month, tips are not reportable to that employer. T/P must include the tips in gross income but does not have to pay social security and Medicare tax on tips.

\$20 or more in one month. If T/P receives tips of \$20 or more in a month while working for one employer, the total amount of tips must be reported to that employer by the tenth day of the next month.

Reporting social security and Medicare taxes on tips not reported to employer. If T/P received \$20 or more in cash and charge tips in a month from any one job and did not report all of those tips to his or her employer, T/P must report the social security and Medicare taxes on the unreported tips as additional tax on his or her return. To report these taxes, T/P must file a return even if he or she would not otherwise have to file. T/P must use Form 4137 (Form 1040 or 1040-SR) to figure these taxes.

What tips to report. Report to employer only cash, check, and debit and credit card tips received. Do not report the value of any noncash tips, such as tickets or passes, to employer. The value of these tips is not subject to social security and Medicare taxes or railroad retirement tax.

Gross Income Tips

Penalty for not reporting tips. If a T/P does not report tips to employer as required, T/P may be subject to a penalty equal to 50% of the social security and Medicare taxes or railroad retirement tax owed on the unreported tips.

Reporting tips on tax return. Report tips with wages on Form 1040 or 1040-SR, line 1. Report all tips received, including both cash tips and noncash tips. Any tips reported to an employer are included in the wages shown in box 1 of Form W-2. Add to the amount in box 1 only the tips that were not reported to the employer.

Allocated tips. These are tips that an employer assigned to the T/P in addition to the tips the T/P reported to his or her employer for the year. The employer will have done this only if:

1. T/P worked in an establishment (restaurant, cocktail lounge, or similar business) that must allocate tips to employees, and
2. The tips reported to employer were less than the T/P's share of 8% of food and drink sales.

Note: No income, social security, or Medicare taxes are withheld on allocated tips.

Reporting allocated tips. Report the amount in box 1 and the allocated tips in box 8 of Form W-2 as wages on Form 1040 or 1040-SR, line 1. Because social security and Medicare taxes were not withheld from the allocated tips, report those taxes as additional tax on the tax return by completing Form 4137.

Gross Income Interest Income

Taxable interest income. The following are taxable interest income:

1. Interest from bank, savings and loans, credit unions, cooperative banks, and domestic building and loan associations.
2. U.S. obligations. (e.g., Treasury bills, notes, and bonds). Interest from U.S. obligations is subject to federal income tax but is exempt from all state and local income taxes.
3. Gift for opening account. For deposits of less than \$5,000, gifts or services valued at more than \$10 must be reported interest. For deposits of \$5,000 or more, gifts or services valued at more than \$20 must be reported as interest.
4. Distributive share of interest from partnerships or S corporations. This interest is reported on Schedule K-1 (Form 1065 or Form 1120S).
5. Any interest income reported on Form 1099-INT.

Nontaxable interest income. The following interest income is exempt from federal taxes:

1. State and local government obligations. Tax-exempt interest is still required to be reported on an individual's tax return.
2. Interest received on the redemption of qualified U.S. saving bonds if used to pay for higher educational expenses during the same year.
3. Interest on a private activity bond that is a qualified bond.

Gross Income Interest Income

How to Report Interest Income

Schedule B. Use Schedule B (Form 1040 or 1040-SR) if any of the following apply:

1. Interest income is more than \$1,500.
2. Claiming the interest exclusion under the Education Savings Bond Program.
3. Received interest from seller-financed mortgage and the buyer used the property as a home.
4. Received a Form 1099-INT for U.S. savings bond interest that includes amounts that were reported in previous years.
5. Received, as a nominee, interest that actually belongs to someone else.
6. Received a Form 1099-INT for interest on frozen deposits.
7. Received a Form 1099-INT for interest on a bond that was bought between interest payment dates.
8. Reporting OID in an amount less than the amount shown on Form 1099-OID.
9. Had a financial interest in, or signature authority over, a financial account in a foreign country or received a distribution from, or were a grantor of, or transferor to, a foreign trust.

Nominee distributions. If T/P receives a Form 1099-INT that includes an amount as a nominee for the real owner, report the full amount shown as interest on Schedule B, then subtract the nominee distribution from the subtotal.

File Form 1099-INT with the IRS. If T/P received interest as a nominee, T/P must file a Form 1099-INT for that interest with the IRS.

Reporting tax-exempt interest. Report tax-exempt interest on line 2a of Form 1040 or 1040-SR.

Gross Income Dividend Income

Ordinary dividends. Ordinary dividends are the most common type of distribution from a corporation or a mutual fund. They are paid out of earnings and profits and are ordinary income. This means they are not capital gains.

Qualified dividends. The dividends must have been paid by a U.S. corporation or a qualified foreign corporation. The stock must have been held for more than 60 days during the 121-day period that begins 60 days before the ex-dividend date. The ex-dividend date is the first date following the declaration of a dividend on which the buyer of a stock will not receive the next dividend payment.

Qualified dividends taxed at capital gains rates. The maximum tax rate for qualified dividends is:

- ▶ 0% on any amount that would be taxed at a 10% or 12% rate.
- ▶ 15% on any amount that would be taxed at rates greater than 12% but less than 37%.
- ▶ 20% on any amount that would be taxed at a 37% rate.

Dividend reinvestment plan. Some corporations allow shareholders to use dividends to buy more shares of stock. A shareholder who chooses to use dividends to purchase additional shares of stock instead of receiving the dividends in cash must report the dividends as income. If the plan allows the shareholder to purchase more stock at a price less than FMV, the shareholder must report as income the FMV of the additional stock on the dividend payment date. If the plan allows the shareholder to invest more cash to buy shares of stock at a price less than FMV, the shareholder must report as dividend income the difference between the cash invested and the FMV of the stock purchased.

Gross Income Dividend Income

Money market funds. Report amounts received from money market funds as dividend income. Money market funds are a type of mutual fund and should not be confused with bank money market accounts that pay interest.

Nondividend distribution. A nondividend distribution is a distribution that is not paid out of the earnings and profits of a corporation or a mutual fund. It is a return of capital and is not taxed until the taxpayer's basis in the stock is fully recovered.

Liquidating distributions. Liquidating distributions, sometimes called liquidating dividends, are distributions received during a partial or complete liquidation of a corporation. These distributions are, at least in part, one form of a return of capital.

Distributions of stock and stock rights. Distributions by a corporation of its own stock are commonly known as stock dividends. Stock rights are distributions by a corporation of rights to acquire the corporation's stock. Generally, stock dividends and stock rights are not taxable and not reported on the tax return.

Dividends on insurance policies. Insurance policy dividends the insurer keeps and uses to pay premiums are not taxable. However, report as taxable interest income the interest that is paid or credited on dividends left with the insurance company.

Dividends on veterans' insurance. Dividends received on veterans' insurance policies are not taxable. In addition, interest on dividends left with the Department of Veterans Affairs is not taxable.

Gross Income Rental Income

Rental income. The following are considered rental income in the year received:

1. Advance rent (rent received before the period it covers, regardless of the method of accounting used).
2. Payment by tenant for canceling a lease.
3. Landlord expenses paid by tenant.
4. FMV of property or services received in exchange for rent.

Security deposits are not included in income if they are to be returned to the tenant at the end of the lease. If tenant forfeits security deposit due to breach of lease, include in rental income.

Repairs. A repair keeps the property in good working condition and does not materially add to the value of the property. The costs of repairs are deductible. Repainting the property inside or out, fixing gutters or floors, fixing leaks, plastering, and replacing broken windows are examples of repairs. If repairs are made as part of an extensive remodeling or restoration of the property, the whole job is an improvement.

Improvements. An improvement adds to the value of the property, prolongs its useful life, or adapts it to new uses. The costs of improvements increase the basis of the property and are not deductible. Improvements must be depreciated. Examples of improvements are remodeling a room, putting up a fence, paving a driveway, putting on a new roof, and putting in new plumbing, wiring, or cabinets.

Gross Income Rental Income

Depreciation of Rental property

Depreciating a property. Three factors determine how much depreciation to deduct each year: (1) the basis in the property, (2) the recovery period for the property, and (3) the depreciation method used. Deduct depreciation only on the part of the property used for rental purposes. Depreciation reduces the basis in the property for figuring gain or loss on a later sale or exchange.

When does depreciation begin and end. Begin depreciating rental property when it is place in service for the production of income. Stop depreciating the property either when the property has been fully depreciated or when the property is retired from service, whichever happens first.

Idle Property. Continue to claim a deduction for depreciation on property used in a rental activity even if it is temporarily idle (not in use). For example, if repairs are done after a tenant moves out, still depreciate the rental property during the time it is not available for rent.

Section 179 deduction. The section 179 deduction is not allowed for property used in connection with residential rental property.

Alternative minimum tax. If a T/P uses accelerated depreciation, the taxpayer may be subject to the AMT. Accelerated depreciation allows a T/P to deduct more depreciation earlier in the recovery period than could be deducted using a straight line method (same deduction each year).

Depreciation methods. Use the Modified Accelerated Cost Recovery System (MACRS) to depreciate residential rental property placed in service after 1986.

Gross Income Rental Income

Depreciation of Rental property (cont.)

Depreciation systems. MACRS consists of two systems that determine how to depreciate a property: the General Depreciation System (GDS) and the Alternative Depreciation System (ADS). A T/P must use GDS unless he or she is specifically required by law to use ADS or the T/P elects to use ADS.

Recovery periods for property used in rental activities under regular MACRS (GDS):

5-year property. Includes light trucks, computers, office machinery, automobiles, appliances such as stoves and refrigerators, carpets and furniture used in rental property.

7-year property. Includes office furniture and fixtures and any property that does not have a class life and that has not been designated by law as being in any other class.

15-year property. Includes certain depreciable improvements made directly to land or added to it, such as shrubbery, fences, roads, and bridges.

20-year property. Includes municipal sewers and farm buildings.

Residential rental property. Includes buildings or structures and structural components such as furnaces, water pipes, venting, etc. Depreciated over **27.5 years**.

Nonresidential real property. This is section 1250 property, such as an office building, store, or warehouse, which is neither residential rental property nor property with a class life of less than 27.5 years. Depreciated over **39 years**.

Gross Income Rental Income

Figuring Income & Deductions

If the property rented was used for personal purposes more than the greater of 14 days or 10% of the total days rented at fair rental price, determine income and deductions as follows.

Rented less than 15 days. Do not report any income if rented for less than 15 days during the year. Do not deduct any rental expenses.

Rented 15 days or more. Report all rental income and divide expenses between personal and rental use based on the number of days used for each purpose.

Figuring rental loss. Deduct expenses only to the amount equal to gross rental income. Rental expenses exceeding gross rental income must be carried forward to the next year.

Figuring Income & Deductions (cont.)

If the property rented was used for personal purposes more than the greater of 14 days or 10% of the total days rented at fair market value, figure rental loss in the following order:

1. Deduct the rental use portion of mortgage interest and taxes.
2. Deduct rental expenses not directly related to rental property (e.g., agent fees, office supplies and advertising fees).
3. Deduct rental expenses directly related to rental property (e.g., repairs, insurance and utilities).
4. Deduct rental use portion of depreciation.

Note: Rental expenses exceeding gross rental income must be carried forward to the next year and treated as rental expense for the same property, subject to same limitations.

Rental property not used for personal purposes more than the greater of 14 days or 10% of the total days rented: Deductible rental expenses can be more than gross rental income.

Gross Income Rental Income

Figuring Income & Deductions (cont.)

Limits on rental losses: T/P is allowed to deduct up to \$25,000 (\$12,500 if MFS and living apart from spouse for entire year; \$0 if MFS and not living apart from spouse) of losses from passive rental real estate activities (in which T/P actively participated) from nonpassive income. A T/P actively participated in a real estate activity if he or she (and spouse) owned at least 10% of the rental property and made management decisions in a significant bona fide sense. Management decisions include approving new tenants, deciding on rental terms, approving expenditures, and similar decisions. The \$25,000 (\$12,500) offset phases out at the rate of \$0.50 for each dollar by which AGI, computed with certain modifications, exceeds \$100,000 (\$50,000 if MFS).

At-Risk Rules

Any loss from an activity subject to the at-risk rules is allowed only to the extent of the amount a T/P has at risk in the activity at the end of the year. A T/P is considered at risk to the extent of cash and the adjusted basis of other property he or she contributed to the activity and certain amount borrowed for use in the activity. Losses from passive activities are first subject to the at-risk rules.

Passive Activity Limits

Passive activity losses can only be deducted from passive activity income. A rental activity is a passive activity even if a T/P materially participated unless the T/P materially participated as a real estate professional. If T/P actively participated in a passive real estate activity T/P can deduct losses up to \$25,000. If T/P materially participated as a real estate professional it is not a passive activity and there is no limit on the rental losses.

Real estate professional. T/P is a real estate professional if the time spent performing services in real property trades or businesses in which T/P materially participated was:

1. More than half of the time spent performing all personal services during the year, and
2. More than 750 hours.

Material participation. Generally, a T/P materially participates in an activity for the tax year if T/P were involved in its operations on a regular, continuous, and substantial basis during the year.

Reporting Rental Income and Expenses

Schedule E (Form 1040 or 1040-SR). Use Schedule E for reporting residential rental income and expenses. However, do not use that schedule to report a not-for-profit activity.

Schedule C (Form 1040 or 1040-SR). If providing substantial services that are primarily for the tenant's convenience, such as regular cleaning, changing linen, or maid service, report rental income and expenses on Schedule C, Profit or Loss From Business. Substantial services do not include the furnishing of heat and light, cleaning of public areas, trash collection, etc.

Gross Income Rental Income

Qualified business income (QBI) deduction (Section 199A). A safe harbor is available to individuals and owners of passthrough entities who seek to claim the deduction under section 199A with respect to a rental real estate enterprise. Under the safe harbor a rental real estate enterprise will be treated as a trade or business for purposes of the QBI deduction if a T/P meets all the following conditions.

1. Separate books and records are maintained to reflect income and expenses for each rental property.
2. For rental real estate enterprises that have been in existence less than four years, 250 or more hours of rental services are performed per year. For other rental real estate enterprises, 250 or more hours of rental services are performed in at least three of the past five years.
3. Maintains contemporaneous records, including time reports, logs, or similar documents, regarding the following: hours of all services performed; description of all services performed; dates on which such services were performed; and who performed the services.
4. Attach a statement to the return filed for the tax year(s) the safe harbor is relied upon.

Section 199A rental real estate safe harbor statement. The T/P must attach a signed statement to the return that confirms that all requirements above for the safe harbor per IRS Notice 2019-07 have been satisfied to claim this rental real estate for the QBI deduction.

Gross Income

Traditional IRAs - Withdrawals & Distributions

Distributions fully taxable. If only deductible contributions were made there is no basis in the IRA. Because there is no basis in the IRA, any distributions are fully taxable when received.

Exceptions. Exceptions to distributions from traditional IRAs being taxable in the year received are one of the following:

1. Rollovers (Must be reinvest within 60 days).
2. Qualified charitable distributions (QCD). A QCD is generally a nontaxable distribution made directly by the trustee of the IRA (other than a SEP or SIMPLE IRA) to an organization eligible to receive tax deductible contributions. T/P must be 70½ when the distribution was made. The maximum annual exclusion for QCDs is \$100,000. If filing jointly, spouse can also have a QCD and exclude up to \$100,000. A QCD counts towards the required minimum distribution.
3. Tax-free withdrawals of contributions.
4. The return of nondeductible contributions.

Ordinary income. The distributions are taxed as ordinary income.

No special treatment. In figuring the tax, a T/P cannot use the 10-year tax option or capital gain treatment that applies to lump-sum distributions from qualified retirement plans.

Distributions partly taxable. If nondeductible contributions were made or any after-tax amounts were rolled over to a traditional IRA, the IRA has a cost basis (investment in the contract) equal to the amount of those contributions. These nondeductible contributions are not taxed when they are distributed. They are a return of investment in the IRA.

Gross Income

Traditional IRAs - Withdrawals & Distributions

Figuring the Nontaxable and Taxable Amounts. The following worksheet is used to determine the taxable and nontaxable portion of a distribution:

1. Enter the basis (nondeductible contribution) in IRA(s) as of 12/31/2021. \$ _____
2. Enter all IRA contributions made for 2022, whether or not deductible
(including contributions made during 2023 that were for 2022) \$ _____
3. Add lines 1 and 2. \$ _____
4. Enter the value of ALL traditional IRA(s) as of 12/31/2022 (include
any outstanding rollovers from traditional IRAs to other traditional IRAs). \$ _____
5. Enter the total IRA distributions from traditional IRAs (including amounts
converted to Roth IRA) received in 2022. \$ _____
6. Add lines 4 and 5. \$ _____
7. Divide line 3 by line 6. Enter the results as a decimal. (Do not enter more than 1.00) . \$ _____
8. Nontaxable portion of the distribution (multiply line 5 by line 7). \$ _____
9. Taxable portion of the distribution (Subtract line 8 from line 5) If there is
no amounts converted to Roth IRAs, STOP HERE. \$ _____
10. Enter the amount included on line 9 that was converted to Roth IRA by 12/31/2022. . \$ _____
11. Taxable portion of the distribution (after adjustment for conversions)
Subtract line 10 from line 9. \$ _____

Gross Income

Traditional IRAs - Withdrawals & Distributions

Age 59½ rule. A T/P cannot withdraw assets from an IRA without having to pay a 10% additional tax until age 59½.

Exceptions: The following are exceptions to the age 59½ rule:

1. T/P becomes totally and permanently disabled.
2. Distributions are to beneficiaries of a deceased IRA owner.
3. Distributions are in the form of an annuity.
4. Amounts used to pay unreimbursed medical expenses more than 7.5% of T/P's AGI.
5. The distribution is used to pay medical insurance for T/P, spouse, and dependents and all four of the following conditions apply:
 - a) T/P lost his or her job.
 - b) T/P received unemployment compensation paid under any federal or state law for 12 consecutive weeks.
 - c) T/P made withdrawals during either the year he or she received unemployment compensation or the following year.
 - d) T/P made the withdrawals no later than 60 days after being reemployed.
6. Distributions used to pay for higher education expenses for T/P, spouse, children, and grandchildren.
7. Distributions up to \$10,000 to buy, build, or rebuild a first home.
8. The distribution is due to an IRS levy to the qualified plan.
9. The distribution is a qualified reservist distribution (called to active duty for more than 179 days).

Gross Income

Traditional IRAs - Withdrawals & Distributions

Required distributions. A T/P must start receiving distributions by April 1 of the year following the year in which he or she reaches age 72. If the required minimum distribution is not made, or if the distributions are less than the required minimum distribution, the T/P may have to pay a 50% excise tax for the year on the amount not distributed as required. If the excess accumulation is due to reasonable error and the T/P has taken steps to remedy the insufficient distribution, the T/P can request that the excise tax be excused.

Figuring the required minimum distribution. Figure the required minimum distribution for each year by dividing the IRA account balance as of the close of business on December 31 of the preceding year by the applicable distribution period or life expectancy

Form 8606. Nondeductible IRA contributions must be reported on Form 8606, Nondeductible IRAs, to establish a basis in the IRA. If Form 8606 is not filed, the contribution will be treated as deductible and no basis will be recognized in the IRA. All distributions from the IRA will be taxed unless the T/P can show that nondeductible contributions were made.

Gross Income

Traditional IRAs - Inherited IRAs

Inherited from spouse. If a T/P inherits a traditional IRA from his or her spouse, the T/P generally have the following three choices.

1. Treat it as his or her own IRA by designating himself or herself as the account owner.
2. Treat it as his or her own by rolling it over into his or her IRA, or to the extent it is taxable, into a:
 - ▶ Qualified employer plan,
 - ▶ Qualified employee annuity plan (section 403(a) plan),
 - ▶ Tax-sheltered annuity plan (section 403(b) plan),
 - ▶ Deferred compensation plan of a state or local government (section 457 plan), or
3. Treat himself or herself as the beneficiary rather than treating the IRA as his or her own.

Inherited from someone other than spouse. If a T/P inherits a traditional IRA from anyone other than his or her deceased spouse, the T/P cannot treat the inherited IRA as his or her own. This means that the T/P cannot make any contributions to the IRA or roll over any amounts into or out of the inherited IRA. However, the T/P can make a trustee-to-trustee transfer as long as the IRA into which amounts are being moved is set up and maintained in the name of the deceased IRA owner for the benefit of the T/P as beneficiary.

IRA with basis. If a T/P inherits a traditional IRA from a person who had a basis in the IRA because of nondeductible contributions, that basis remains with the IRA.

Gross Income Roth IRAs

Roth IRA. A Roth IRA is an individual retirement plan that is subject to the same rules that apply to traditional IRAs except for the following features:

- ▶ Contributions are never deductible.
- ▶ No minimum distributions are required.
- ▶ Qualified distributions are generally not included in income.

Qualified distributions. A qualified distribution is any payment or distribution from a Roth IRA that meets the following requirements:

1. It is made after the 5-year period beginning with the first taxable year for which a contribution was made to a Roth IRA set up for T/P's benefit, and
2. The payment or distribution is:
 - a) Made on or after the date T/P reaches age 59½,
 - b) Made because T/P is disabled,
 - c) Made to a beneficiary or to the T/P's estate after death, or
 - d) Made to buy, build, or rebuild a first home (up to a \$10,000 lifetime limit).

Tax on early distributions. Nonqualifying distributions are subject to a 10% additional tax on the taxable part of the distribution unless an exception applies.

Gross Income Roth IRAs

Contribution limits (Roth IRA only). If T/P contributes only to a Roth IRA, the maximum contribution is the lesser of:

1. \$6,000 (\$7,000 if T/P is age 50 or older), or
2. T/P's compensation.

Contributions to both Roth IRAs and traditional IRAs. If T/P contributes to both a Roth IRA and a traditional IRA, the contribution limit for the Roth IRA is the lesser of:

1. The maximum contribution limit reduced by all contributions (other than employer contributions under a SEP or SIMPLE IRA plan) for the year to all IRAs other than Roth IRAs, or
2. The maximum contribution reduced because modified AGI is above the amounts below.

Contribution limits reduced. A T/P's maximum contribution is gradually reduced (phased out) if his or her modified AGI is above the following amounts:

<u>Filing status</u>	<u>Phaseout range</u>
Married filing jointly or qualifying surviving spouse	\$204,000 - \$214,000
Married filing separate and lived with spouse	\$0 - \$10,000
All other filing statuses	\$129,000 - \$144,000

Tax on excess contributions. A 6% excise tax applies to excess contributions.

Roth IRAs - Withdrawals & Distributions

Conversions. T/P can convert amounts from either a traditional IRA, SEP, or SIMPLE IRA into a Roth IRA. The conversion is taxable.

Periodic distributions. If a T/P started taking equal periodic distributions from a traditional IRA, the T/P can convert the amounts in the traditional IRA to a Roth IRA and then continue the periodic payments. The 10% additional tax on early distributions will not apply.

Required distributions from a traditional IRA. Amounts that must be distributed from a traditional IRA for a particular year (including the calendar year in which a T/P reaches age 72) cannot be converted to a Roth IRA.

Distributions after owner's death. If a Roth IRA owner dies, the minimum distribution rules that apply to traditional IRAs apply to Roth IRAs as though the Roth IRA owner died before his or her required beginning date. Generally, the entire interest in the Roth IRA must be distributed by the end of the 5th calendar year after the year of the owner's death unless the interest is payable to a designated beneficiary over the life or life expectancy of the designated beneficiary. If the sole beneficiary is the spouse, he or she can either delay distributions until the decedent would have reached age 72 or treat the Roth IRA as his or her own. A beneficiary can combine an inherited Roth IRA with another Roth IRA maintained by the beneficiary only if the beneficiary either inherited the other Roth IRA from the same decedent or was the spouse of the decedent and the sole beneficiary of the Roth IRA and elects to treat it as his or her own IRA.

Roth IRAs - Withdrawals & Distributions

Recharacterizations. A T/P may be able to treat a contribution made to one type of IRA as having been made to a different type of IRA. This is called recharacterizing the contribution. To recharacterize a contribution, the T/P must have the contribution transferred from the first IRA (the one to which it was made) to the second IRA in a trustee-to-trustee transfer. If the transfer is made by the due date (including extensions) for the tax return for the year during which the contribution was made, then T/P can elect to treat the contribution as having been originally made to the second IRA instead of to the first IRA. To recharacterize the contribution, the T/P must do all three of the following:

- ▶ Include in the transfer any net income allocable to the contribution. If there was a loss, the net income that must be transfer may be a negative amount.
- ▶ Report the recharacterization on the tax return for the year during which the contribution was made.
- ▶ Treat the contribution as having been made to the second IRA on the date that it was actually made to the first IRA.

No recharacterizations of conversions made in 2018 or later. A conversion of a traditional IRA to a Roth IRA, and a rollover from any other eligible retirement plan to a Roth IRA, made in tax years beginning after 2017, cannot be recharacterized as having been made to a traditional IRA.

Reporting a recharacterization. If electing to recharacterize a contribution to one IRA as a contribution to another IRA, report the recharacterization on the tax return using Form 8606. Treat the contribution as having been made to the second IRA.

Gross Income

Qualified Plans - Withdrawals & Distributions

Tax Treatment of Distributions

Tax treatment of periodic payments. Distributions from a qualified plan minus a prorated part of the cost basis are subject to income tax in the year they are distributed. Since most recipients have no cost basis, a distribution is generally fully taxable. An exception is a distribution that is properly rolled over.

Lump-sum distributions. A lump-sum distribution is the distribution or payment in 1 tax year of a plan participant's entire balance from all of the employer's qualified plans of one kind (for example, pension, profit-sharing, or stock bonus plans). A distribution from a nonqualified plan (such as a privately purchased commercial annuity or a section 457 deferred compensation plan of a state or local government or tax-exempt organization) cannot qualify as a lump-sum distribution.

Tax treatment for lump-sum distributions. A T/P has the following options for how to treat the taxable part of the lump-sum distributions:

- ▶ Report the part of the distribution from participation before 1974 as a capital gain (if T/P qualifies) and the part from participation after 1973 as ordinary income.
- ▶ Report the part of the distribution from participation before 1974 as a capital gain (if T/P qualifies) and use the 10-year tax option to figure the tax on the part from participation after 1973 (if T/P qualifies).
- ▶ Use the 10-year tax option to figure the tax on the total taxable amount (if T/P qualifies).
- ▶ Roll over all or part of the distribution. No tax is currently due on the part rolled over. Report any part not rolled over as ordinary income.
- ▶ Report the entire taxable part of the distribution as ordinary income on the tax return.

Gross Income Qualified Plans - Withdrawals & Distributions

Tax Treatment of Distributions (cont.)

10-year tax option. The 10-year tax option is a special formula used to figure a separate tax on the ordinary income part of a lump-sum distribution. The tax is paid only once, for the year in which the distribution is received, not over the next 10 years. A T/P can elect this treatment only once for any plan participant, and only if the plan participant was born before January 2, 1936.

Rollover. A T/P can defer the tax on an eligible rollover distribution by rolling it over into an IRA or another eligible retirement plan. If a T/P receives a distribution other than cash from an employer retirement plan, the T/P must roll over the same property into an IRA or sell all or part of the property and roll over the proceeds of the sale into an IRA.

Required distribution. A participant must begin to receive distributions from his or her qualified retirement plan by April 1 of the year that follows the later of:

1. Calendar year in which he or she reaches age 72, or
2. Calendar year in which he or she retires from employment with the employer maintaining the plan.

Gross Income

Qualified Plans - Withdrawals & Distributions

Tax Treatment of Distributions (cont.)

Withholding requirements. If a T/P takes an eligible rollover distribution that is \$200 or more, the payer is required to withhold (for Federal income tax) 20% of the taxable part of the distribution. If the T/P chooses to have the plan pay the distribution directly to an IRA or another eligible retirement plan (i.e. direct rollover), no withholding is required. If the distribution is not eligible for rollover treatment, the 20% withholding requirement does not apply.

Tax on early distribution. A distribution from a retirement plan to a T/P before he or she reaches age 59½ is a premature distribution subject to a 10% tax on the part of the distribution that is included in gross income.

Exceptions: The 10% tax will not apply if distributions before age 59½ are:

1. Made to a beneficiary (or to the estate of the employee) after the death of the employee.
2. Made due to the employee having a qualifying disability.
3. Rolled over to another retirement plan or an IRA within 60 days of the distribution.
4. Made because of an IRS levy on the plan.
5. Made as a qualified reservist distribution.
6. Made as a qualified birth or adoption distribution.
7. Made as a qualified disaster distribution.

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Gross Income Qualified Plans - Withdrawals & Distributions

Tax Treatment of Distributions (cont.)

Exceptions (cont.): The 10% tax will not apply if distributions before age 59½ are:

8. Part of a series of substantially equal periodic payments, beginning after separation from service, made at least annually for the life or life expectancy of the employee or the joint lives or joint life expectancies of the employee and his or her designated beneficiary. (The payments under this exception, except in the case of death or disability, must continue for at least 5 years or until the employee reaches age 59½, whichever is the longer period).
9. Made to an employee after separation from service, if the separation occurred during or after the calendar year in which the employee reached age 55.
10. Made to an alternate payee under a qualified domestic relations order (QDRO).
11. Made to an employee for medical care to the extent that the distribution does not exceed the amount allowable as a medical expense deduction (determined without regard to whether the employee itemizes deductions).
12. Timely made to reduce excess contributions under a 401(k) plan.
13. Timely made to reduce excess employee or matching employer contributions (excess aggregate contributions).
14. Timely made to reduce excess elective deferrals.

Gross Income Qualified Plans - Withdrawals & Distributions

Tax Treatment of Distributions (cont.)

Loans treated as distributions. If a T/P borrows money from a retirement plan, the T/P must treat the loan as a nonperiodic distribution from the plan unless it qualifies for the exception to this loan-as-distribution rule. This exception to the loan-as-distribution rule applies only to a loan that either:

- ▶ Is used to acquire a main home, or
- ▶ Must be repaid within 5 years.

If a loan qualifies for this exception, the loan will be treated as a nonperiodic distribution only to the extent that the loan, when added to the outstanding balances of all loans from all plans exceeds the lesser of:

- ▶ \$50,000, or
- ▶ Half the present value (but not less than \$10,000) of the T/P's nonforfeitable accrued benefit under the plan, determined without regard to any accumulated deductible employee contributions.

Gross Income

SIMPLE IRAs - Withdrawals & Distributions

Tax Treatment of Distributions

Distributions from a SIMPLE IRA are subject to IRA rules and generally are includible in income for the year received. Tax-free rollovers can be made from one SIMPLE IRA into another SIMPLE IRA. However, a rollover from a SIMPLE IRA to a non-SIMPLE IRA can be made tax free only after a 2-year participation in the SIMPLE IRA plan.

Tax on early distribution. Early withdrawals generally are subject to a 10% additional tax. However, the additional tax is increased to 25% if funds are withdrawn within 2 years of beginning participation.

Gross Income Social Security Benefits

Are benefits taxable? To determine whether any of the benefits are taxable, compare the base amount for the T/P's filing status (see below) with the total of:

1. One-half of benefits received, plus
2. All other income, including tax-exempt interest.

Base Amount	Filing Status
\$25,000	S, H of H, or QSS
\$25,000	MFS and did not live with spouse during the year
\$32,000	MFJ
\$ - 0 -	MFS and lived with spouse at any time during the year

If all other income, including tax-exempt interest, plus one-half social security benefits are more than the base amounts but less than \$34,000 (44,000 if MFJ), taxable social security benefits is the smaller of the following:

1. One-half of net benefits received, or
2. One-half of excess of (all other income + tax-exempt income + $\frac{1}{2}$ net benefits) over the base amount.

Gross Income Social Security Benefits

Maximum taxable part. Generally, up to 50% of social security benefits will be taxable. However, up to 85% of social security benefits can be taxable if either of the following situations applies:

- ▶ The total of one-half of social security benefits and all other income is more than \$34,000 (\$44,000 if married filing jointly).
- ▶ Married filing separately and lived with spouse at any time during the year.

If the sum of modified AGI and one-half social security benefits are more than \$34,000 (\$44,000 if married filing jointly), taxable social security benefits are the smaller of the following:

1. 85% of the net benefits received, or
2. 85% of the amount by which the sum of other income plus tax-exempt interest and one-half social security benefits exceed the adjusted base amount, plus the smaller of:
 - a. 50% of social security benefits,
 - b. 50% of the amount by which the sum of other income, nontaxable income and one-half the social security benefits exceed \$34,000 (\$44,000 if married filing jointly), or
 - c. \$34,000 (\$44,000 if married filing jointly).

Gross Income

Foreign Source Income

If a T/P is a U.S. citizen with income from sources outside the U. S. (foreign income), the T/P must report all such income on his or her tax return unless it is exempt by U.S. law. This is true whether residing inside or outside the U. S. and whether or not the T/P received a Form W-2 or Form 1099 from the foreign payer. This applies to earned income (such as wages and tips) as well as unearned income (such as interest, dividends, capital gains, pensions, rents and royalties). If the T/P resides outside the U. S., the T/P may be able to exclude all or part of the foreign source earned income.

FinCEN Report 114, Report of Foreign Bank and Financial Accounts. If a taxpayer has a financial interest in or signature authority over a foreign financial account, including a bank account, brokerage account, mutual fund, trust, or other type of foreign financial account, exceeding certain thresholds listed below, the Bank Secrecy Act requires the taxpayer to report the account yearly to the Department of Treasury by electronically filing a Financial Crimes Enforcement Network (FinCEN) 114, Report of Foreign Bank and Financial Accounts (FBAR).

Reporting Threshold. Aggregate value of financial accounts exceeds \$10,000 at any time during the calendar year. This is a cumulative balance, meaning if the T/P has 2 accounts with a combined account balance greater than \$10,000 at any one time, both accounts would have to be reported.

Penalties. If non-willful, up to \$14,489; if willful, up to the greater of \$144,886 or 50 percent of account balances; criminal penalties may also apply.

Gross Income

Foreign Source Income

Foreign Account and Asset Reporting (Form 8938). Use Form 8938 to report specified foreign financial assets if the total value of all the specified foreign financial assets in which the taxpayer has an interest is more than the appropriate reporting threshold. A T/P who fails to file a complete and correct Form 8938 is subject to a \$10,000 penalty. Failure to file a correct and complete Form 8938 after the IRS mails a notice of failure to file can result in an additional \$10,000 penalty for each 30-day period up to a maximum penalty of \$60,000.

Reporting threshold for Form 8938. Specified individuals living in the US:

- ▶ Unmarried individual (or married filing separately): Total value of assets was more than \$50,000 on the last day of the tax year, or more than \$75,000 at any time during the year.
- ▶ Married individual filing jointly: Total value of assets was more than \$100,000 on the last day of the tax year, or more than \$150,000 at any time during the year.

Reporting threshold for Form 8938. Specified individuals living outside the US:

- ▶ Unmarried individual (or married filing separately): Total value of assets was more than \$200,000 on the last day of the tax year, or more than \$300,000 at any time during the year.
- ▶ Married individual filing jointly: Total value of assets was more than \$400,000 on the last day of the tax year, or more than \$600,000 at any time during the year.

Gross Income

Foreign Earned Income Exclusion

Requirements. To exclude up to \$112,000 of foreign earned income, foreign housing exclusion, or the foreign housing deduction, a taxpayer must satisfy all three of the following requirements:

1. Tax home must be in a foreign country.
2. Must have foreign earned income.
3. Must be one of the following:
 - a) A U.S. citizen who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year.
 - b) A U.S. resident alien who is a citizen or national of a country with which the United States has an income tax treaty in effect and who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year.
 - c) A U.S. citizen or a U.S. resident alien who is physically present in a foreign country or countries for at least 330 full days during any period of 12 consecutive months.

Foreign earned income is pay for personal services performed, such as wages, salaries, or professional fees received for services performed.

30% Withholding tax. U.S. payers of income other than wages, such as dividends and royalties are required to withhold tax at a flat 30% on nonwage income paid to nonresident aliens.

Gross Income Canceled Debts

If a debt owed is canceled or forgiven, other than as a gift or bequest, include the canceled amount in income. There is no income from the canceled debt if it is intended as a gift. A debt includes any indebtedness for which the taxpayer is liable or which attaches to property held by the T/P.

Discounted mortgage loan. If a financial institution offers a discount for the early payment of a mortgage loan, the amount of the discount is canceled debt. Include the canceled amount in income.

Exceptions

Student loans. Certain student loans contain a provision that all or part of the debt incurred to attend the qualified educational institution will be canceled if the T/P works for a certain period of time in certain professions for any of a broad class of employers.

Deductible debt. Do not include in income the cancellation of a debt if the payment of the debt would be deductible. This exception applies only if the T/P uses the cash method of accounting.

Gross Income Canceled Debts

Excluded debt. Do not include a canceled debt in gross income in the following situations:

- ▶ The debt is canceled in a bankruptcy case under title 11 of the U.S. Code.
- ▶ The debt is canceled when the T/P is insolvent. However, the T/P cannot exclude any amount of canceled debt that is more than the amount by which the T/P is insolvent.
- ▶ The debt is qualified farm debt and is canceled by a qualified person.
- ▶ The debt is qualified real property business debt.
- ▶ The cancellation is intended as a gift.
- ▶ The debt is qualified principal residence indebtedness (up to \$2 million).

Gross Income Canceled Debts

Reporting Canceled Debt

Form 1099-C. If a Federal Government agency, financial institution, or credit union cancels or forgives a debt of \$600 or more, the taxpayer will receive a Form 1099-C, Cancellation of Debt. The amount of the canceled debt is shown in box 2.

Canceled nonbusiness bad debt. If the canceled debt is a nonbusiness debt, report the canceled amount as other income on Schedule 1 (Form 1040 or 1040-SR), line 8c.

Canceled business bad debt. If the canceled debt is a business debt, report the amount on Schedule C (Form 1040 or 1040-SR), Profit or Loss From Business, or on Schedule F (Form 1040 or 1040-SR), Profit or Loss From Farming, if the debt is farm debt and T/P is a farmer.

Gross Income

Barter Income

Bartering is an exchange of property or services. Include in income the fair market value (FMV) of property or services received in bartering. If services are exchanged and both parties agree ahead of time as to the value of the services, that value will be accepted as FMV unless the value can be shown to be otherwise.

Reporting barter income. Generally barter income is reported on Schedule C (Form 1040 or 1040-SR), Profit or Loss From Business.

Form 1099-B from barter exchange. Use Form 1099-B, Proceeds From Broker and Barter Exchange Transactions, to report the barter exchange.

Gross Income Partnership Income

A partnership generally is not a taxable entity. The income, gains, losses, deductions, and credits of a partnership are passed through to the partners based on each partner's distributive share of these items.

Partner's distributive share. A T/P's distributive share of partnership income, gains, losses, deductions, or credits generally is based on the partnership agreement. T/P must report his or her distributive share of these items on his or her return whether or not they actually are distributed to the T/P. However, the T/P's distributive share of the partnership losses is limited to the adjusted basis of T/P's partnership interest at the end of the partnership year in which the losses took place.

Partnership return. Although a partnership generally pays no tax, it must file an information return on Form 1065, U.S. Return of Partnership Income. This shows the result of the partnership's operations for its tax year and the items that must be passed through to the partners.

Schedule K-1 (Form 1065). Each partner should receive from the partnership a copy of Schedule K-1 (Form 1065), Partner's Share of Income, Deductions, Credits, etc., showing the partner's share of income, deductions, credits, and tax preference items of the partnership for the tax year.

Partner's return. A partner generally must report partnership items on his or her individual return the same way as they are reported on the partnership return. That is, if the partnership had a capital gain, the partner reports his or her share on Schedule D (Form 1040 or 1040-SR). The partner reports his or her share of partnership ordinary income on Schedule E (Form 1040 or 1040-SR).

Gross Income Partnership Income

Publicly traded partnerships. The passive activity limitations are applied separately for items (other than the low-income housing credit and the rehabilitation credit) from each publicly traded partnership (PTP). Thus, a net passive loss from a PTP may not be deducted from other passive income. Instead, a passive loss from a PTP is suspended and carried forward to be applied against passive income from the same PTP in later years. If the partner's entire interest in the PTP is completely disposed of, any unused losses are allowed in full in the year of disposition.

Gross Income S Corporation Income

In general, an S corporation does not pay tax on its income. Instead, the income, losses, deductions, and credits of the corporation are passed through to the shareholders based on each shareholder's pro rata share. Shareholders must report their share of these items on their returns. Generally, the items passed through to the shareholders will increase or decrease the basis of the shareholder's S corporation stock as appropriate.

S corporation return. An S corporation must file a return on Form 1120S, U.S. Income Tax Return for an S Corporation. This shows the results of the corporation's operations for its tax year and the items of income, losses, deductions, or credits that affect the shareholders' individual income tax returns.

Schedule K-1 (Form 1120S). A shareholder should receive from the S corporation a copy of Schedule K-1 (Form 1120S), Shareholder's Share of Income, Deductions, Credits, etc., showing his or her share of income, losses, deductions, and credits, of the S corporation for the tax year.

Shareholder's return. A shareholder's distributive share of the items of income, losses, deductions, or credits of the S corporation must be shown separately on the shareholder's Form 1040 or 1040-SR. The character of these items generally is the same as if the shareholder had realized or incurred them personally.

Gross Income Estate and Trust Income

An estate or trust, unlike a partnership and most S corporations, may have to pay federal income tax. If a T/P is a beneficiary of an estate or trust, the T/P may be taxed on his or share of its income distributed or required to be distributed to the T/P. However, there is never a double tax.

Estate or trust return (Form 1041). Estates and trusts file their returns on Form 1041, U.S. Income Tax Return for Estates and Trusts, and the taxpayer's share of the income is reported to him or her on Schedule K-1 (Form 1041).

How to report. Treat each item of income the same way that the estate or trust would treat it. For example, if a trust's dividend income is distributed to the T/P, report the distribution as dividend income on the T/P's Form 1040 or 1040-SR. The same rule applies to distributions of tax-exempt interest and capital gains. The fiduciary of the estate or trust must tell the T/P the type of items making up his or her share of the estate or trust income and any credits allowed on the T/P's individual income tax return.

Losses. Losses of estates and trusts generally aren't deductible by the beneficiaries.

Grantor trust. Income earned by a grantor trust is taxable to the grantor, not the beneficiary, if the grantor keeps certain control over the trust. (The grantor is the one who transferred property to the trust.) This rule applies if the property (or income from the property) put into the trust will or may revert (be returned) to the grantor or the grantor's spouse.

Gross Income Court Awards & Damages

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The following settlement amounts received by compromise or judgment must be included in income:

1. Interest on any award.
2. Compensation for lost wages or lost profits.
3. Punitive damages. It does not matter if they relate to a physical injury or physical sickness.
4. Amounts received in settlement of pension rights (if T/P did not contribute to plan).
5. Damages for:
 - a) Patent or copyright infringement operations,
 - b) Breach of contract, or
 - c) Interference with business operations.
6. Back pay and damages for emotional distress received to satisfy a claim under Title VII of the Civil Rights Act of 1964.
7. Attorney fees and court costs (including contingent fees) where the underlying recovery is included in income.
8. Attorney fees and costs relating to whistleblower awards where the underlying recovery is included in gross income.

The following compensatory damages are not included in income:

1. Personal physical injury or physical sickness, and
2. Emotional distress due to physical injury or sickness.

Gross Income Scholarship and Fellowship Grants

Exclusion from income. Only a candidate for a degree can exclude amounts received as a qualified scholarship. The amounts excluded must be used for the following:

1. Tuition and fees.
2. Fees, books, supplies, and equipment required for courses at the educational institution.

Room and board. Amounts used for room and board do not qualify for the exclusion.

Payment for services. In most cases, include in income the part of any scholarship or fellowship that represents payment for past, present, or future teaching, research, or other services. This applies even if all candidates for a degree must perform the services to receive the degree.

VA payments. Allowances paid by the Department of Veterans Affairs are not included in income. These allowances are not considered scholarship or fellowship grants.

Gross Income Recoveries

A recovery is a return of an amount the T/P deducted or took a credit for in an earlier year. The most common recoveries are refunds, reimbursements, and rebates of itemized deductions. Recoveries also include non-itemized deductions (such as payments on previously deducted bad debts) and recoveries of items for which a tax credit was previously claimed.

Tax benefit rule. Include a recovery in income in the year received up to the amount by which the deduction or credit was taken reduced the T/P's tax in the earlier year. For this purpose, any increase to an amount carried over to the current year that resulted from the deduction or credit is considered to have reduced the T/P's tax in the earlier year.

State tax refund. If T/P received a refund, credit, or offset of state or local income taxes in the tax year, the T/P may receive a Form 1099-G. If the refund was for a tax paid in the previous year and T/P deducted state and local income taxes on line 5 of his or her Schedule A, all or part of the refund may be taxable. The amount of the refund that is taxable is the amount of the state or local income tax deduction in the previous year that actually reduced the T/P's income tax for that year.

Note: None of the refund is taxable if, in the year the state or local income tax is paid:

1. T/P did not itemize deductions, or
2. T/P elected to deduct state and local general sales taxes instead of state and local income taxes.

Gross Income Rents From Personal Property

If a T/P rents out personal property, such as equipment or vehicles, how to report the income and expenses is in most cases determined by:

- ▶ Whether or not the rental activity is a business, and
- ▶ Whether or not the rental activity is conducted for profit.

In most cases, if the primary purpose is income or profit and the T/P is involved in the rental activity with continuity and regularity, the rental activity is a business.

Reporting business income and expenses. If in the business of renting personal property, report income and expenses on Schedule C (Form 1040 or 1040-SR).

Reporting nonbusiness income. If not in the business of renting personal property, report rental income as other income on Schedule 1 (Form 1040 or 1040-SR), line 8I.

Reporting nonbusiness expenses. If renting personal property for profit, include rental expenses in the total amount enter on Schedule 1 (Form 1040 or 1040-SR), line 24b.

Note: If not renting personal property for profit, deductions are limited and losses cannot offset other income.

Gross Income

Other Income

Gross income includes all income received in the form of money, goods, property, and services that is not exempt from tax. Common types of other income include but are not limited to:

- ▶ Barter income
- ▶ Canceled debt (except if payment of debt would have been deductible)
- ▶ Gain on the sale of personal items
- ▶ Gambling winnings
- ▶ Lotteries and raffles
- ▶ Prizes and awards
- ▶ Virtual Currency (such as bitcoin)
- ▶ Recoveries of amounts previously deducted
- ▶ Royalties
- ▶ Jury duty pay
- ▶ Bribes
- ▶ Discounted mortgage loan (canceled debt)
- ▶ Kickbacks
- ▶ Alimony (if divorce or separation agreement executed before 2019)
- ▶ Sales parties at which T/P is the host or hostess
- ▶ Life insurance proceeds if the policy was turned over to T/P for a price or interest income received on the policy
- ▶ Unemployment compensation
- ▶ Activity not got profit (hobby income). Deduct expenses up to income on Schedule A
- ▶ Credit card or unemployment insurance benefits
- ▶ Fees for services
- ▶ Gig economy income (paid in any form)

Gross Income

Items Excluded from Gross Income

Items that are generally excluded from income include, but are not limited to:

- ▶ Accident and health proceeds
- ▶ Gifts and inheritances
- ▶ Housing allowances for members of the clergy
- ▶ Interest on state and local government obligations
- ▶ Life insurance proceeds (any interest received on installment payments is taxable)
- ▶ Meals and lodging provided by employer
- ▶ Military allowances
- ▶ Part of scholarships and fellowship grants
- ▶ Disaster relief grants
- ▶ Cash rebates (must reduce basis in property)
- ▶ Payments made by a state to qualified people to reduce cost of winter energy
- ▶ Veteran's benefits
- ▶ Welfare and other public assistance benefits
- ▶ Workers' compensation and similar payments for sickness and injury
- ▶ Child support
- ▶ Casualty insurance and other reimbursements.
- ▶ Damages for physical injury or sickness
- ▶ Employee achievement awards (if employer can deduct award)
- ▶ Employer contributions to a medical savings account
- ▶ Energy conservation measure

Gross Income

Qualified Business Income (QBI) Deduction

Owners of sole proprietorships, partnerships, S corporations (not C corporations) and some trusts and estates may be eligible for a qualified business income (QBI) deduction (Section 199A) for tax years beginning after December 31, 2017. The QBI deduction has two components:

1. **QBI Component.** This component of the deduction equals 20% of QBI from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust or estate. The QBI Component is subject to limitations, depending on the T/P's taxable income, that may include the type of trade or business, the amount of W-2 wages paid by the qualified trade or business and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business.
2. **REIT/PTP Component.** This component of the deduction equals 20% of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. This component is not limited by W-2 wages or the UBIA of qualified property. Depending on the taxpayer's taxable income, the amount of PTP income that qualifies may be limited depending on the PTP's trade or business.

Qualified Business Income (QBI). QBI is the net amount of qualified items of income, gain, deduction and loss from any qualified trade or business, including income from partnerships, S corporations, sole proprietorships, and certain trusts. Generally this includes, but is not limited to, the deductible part of self-employment tax, self-employed health insurance, and deductions for contributions to qualified retirement plans (e.g. SEP, SIMPLE and qualified plan deductions).

Gross Income

Qualified Business Income (QBI) Deduction

QBI does not include the following items:

- ▶ Items that are not properly includable in taxable income
- ▶ Investment items such as capital gains or losses or dividends
- ▶ Interest income not properly allocable to a trade or business
- ▶ Wage income (except for statutory employees where Form W-2, box 13 is checked)
- ▶ Income that is not effectively connected with the conduct of business within the U.S.
- ▶ Commodities transactions or foreign currency gains or losses
- ▶ Certain dividends and payments in lieu of dividends
- ▶ Income, loss, or deductions from notional principal contracts
- ▶ Annuities, unless received in connection with the trade or business
- ▶ Amounts received as reasonable compensation from an S corporation
- ▶ Amounts received as guaranteed payments from a partnership
- ▶ Payments received by a partner for services other than in a capacity as a partner
- ▶ Items treated as capital gains or losses
- ▶ Qualified REIT dividends
- ▶ Qualified PTP income

Gross Income

Qualified Business Income (QBI) Deduction

Form 8995

Deduction limits. The deduction is limited to the lesser of the QBI component plus the REIT/PTP component or 20 percent of the taxable income minus net capital gain. For the QBI component, if the trade or business is a specified trade or business (SSTB), the T/P can claim the credit only if his or her taxable income is less than or equal to \$170,050 (\$340,100 if married filing jointly). For business owners with taxable income in excess of \$220,050 (\$440,100 if married filing jointly), no deduction is allowed against income earned in a SSTB.

SSTB. An SSTB is a trade or business involving health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of the trade or business is the reputation or skill of one or more of its owners or employees.

Form 8995. Individuals and eligible estates and trusts that have QBI use Form 8995 to figure the QBI deduction.

Exclusions from Gross Income

Qualified Tuition Program (529 plans)

A qualified tuition program (also known as a 529 plan or program) is a program set up to allow a taxpayer to either prepay, or contribute to an account established for paying, a student's qualified education expenses at an eligible educational institution. QTPs can be established and maintained by states (or agencies or instrumentalities of a state) and eligible educational institutions.

Designated beneficiary. The designated beneficiary is generally the student (or future student) for whom the QTP is intended to provide benefits. The designated beneficiary can be changed after participation in the QTP begins.

Contributions. Contributions to a QTP on behalf of any beneficiary cannot be more than the amount necessary to provide for the qualified education expenses of the beneficiary. There are no income restrictions on the individual contributors.

Distributions. The part of a distribution representing the amount paid or contributed to a QTP does not have to be included in income. This is a return of the investment in the plan. The designated beneficiary generally does not have to include in income any earnings distributed from a QTP if the total distribution is less than or equal to adjusted qualified education expenses.

Qualified elementary and secondary education expenses. Qualified education expenses may include up to \$10,000 paid for elementary or secondary school tuition.

Exclusions from Gross Income Qualified Tuition Program (529 plan)

Qualified higher educational expenses. These expenses are the tuition, fees, books, supplies, and equipment required for enrollment or attendance at an eligible educational institution. They also include the reasonable costs of room and board for a designated beneficiary who is at least a half-time student. Qualified education expenses include expenses paid or incurred for the purchase of computer or peripheral equipment, computer software, or Internet access and related services to be used primarily by the beneficiary while enrolled at an eligible educational institution.

Coordination with American opportunity and lifetime learning credits. An American opportunity or lifetime learning credit can be claimed in the same year the beneficiary takes a tax-free distribution from a QTP, as long as the same expenses are not used for both benefits. This means that after the beneficiary reduces qualified education expenses by tax-free educational assistance, he or she must further reduce them by the expenses taken into account in determining the credit.

Coordination with Coverdell ESA distributions. If a designated beneficiary receives distributions from both a QTP and a Coverdell ESA in the same year, and the total of these distributions is more than the beneficiary's adjusted qualified higher education expenses, the expenses must be allocated between the distributions. For purposes of this allocation, disregard any qualified elementary and secondary education expenses.

Additional tax on taxable distributions. Generally, if a T/P receives a taxable distribution, the T/P also must pay a 10% additional tax on the amount included in income.

Information Returns

Form W-2 and Form 1099-R (What to Do if Incorrect or Not Received). Employers/payers have until January 31 to issue certain informational documents. If a T/P does not receive the Form W-2 or Form 1099-R by January 31, or the information is incorrect on these forms, the T/P should contact his or her employer/payer. If the T/P does not receive the missing or corrected form by February 14 from the employer/payer, the T/P should call the IRS for assistance. After February 14, the IRS will contact the employer/payer for the T/P and request the missing form. IRS will also send the T/P a Form 4852, Substitute for Form W-2 or Form 1099-R, along with a letter containing instructions. If the missing form is not received in sufficient time to file the tax return timely, use the Form 4852 to complete the return. If the missing or corrected Form W-2 or Form 1099-R is received after the return is filed and a correction is needed, use Form 1040X, Amended U.S. Individual Income Tax Return.

Form 1099-MISC (What to do if incorrect). If Form 1099-MISC is incorrect or has been issued in error, contact the payer. If the taxpayer cannot get this form corrected, attach an explanation to the tax return and report the income correctly.

Purchase of Property

Cost basis. The cost basis of property is the amount of cash paid and the FMV of other property or services provided in the transaction. The following must also be included in the basis:

1. Sales and excise taxes on the purchase.
2. Freight charges to obtain the property.
3. Installation and testing charges.
4. Excise taxes.
5. Legal and accounting fees (when they must be capitalized).
6. Revenue stamps.
7. Recording fees.
8. Real estate taxes (if assumed for the seller).

Purchase of Real Property

If property purchased is real property the following fees and other expenses are part of the basis in the property:

1. Real estate taxes owed by the seller paid by the buyer.
2. Assumption of existing mortgage. Basis includes amount paid on the mortgage assumed.
3. Settlement costs. The following are some of the settlement costs included in basis:
 - ▶ Abstract fees.
 - ▶ Charges for installing utility services.
 - ▶ Surveys.
 - ▶ Transfer taxes.
 - ▶ Title insurance.
 - ▶ Recording fees.
 - ▶ Legal fees (including title search and preparing sales contract and deed).
 - ▶ Any amounts the seller owes the purchaser pays such as back taxes, closing costs, sales commissions, interest, etc.

Settlement costs do not include amounts placed in escrow for future payments such as taxes and insurance. The following settlement costs cannot be included in the basis of the property:

1. Casualty insurance premiums.
2. Rent for occupancy of the property before closing.
3. Charges for utilities or other services relating to occupancy of the property before closing.
4. Charges connected with getting a loan, such as points, mortgage insurance premiums, loan assumption fees, cost of a credit report, and fees for an appraisal required by lender.
5. Fees for refinancing a mortgage.

Property Received by Gift

Figuring the basis. The following three amounts must be known to figure the basis:

1. FMV of property at time of gift.
2. Adjusted basis in hand of donor.
3. Amount of gift tax paid.

FMV less than donor's adjusted basis:

1. Basis is donor's adjusted basis in figuring depreciation and gain when sold, and
2. Basis is FMV when figuring loss when sold.

FMV equal to or more than the donor's adjusted basis:

1. Basis is donor's adjusted basis, and
2. Part of the gift tax paid, depending on the date of gift:
 - a) Gift received before 1977: Increase basis by the total gift tax paid.
 - b) Gift received after 1976: Increase basis by part of the gift tax paid:

$$\text{Donee's basis} = \text{Donor's adj. basis} + \text{gift tax} \times ((\text{FMV} - \text{Donor's adj. basis}) \div (\text{FMV} - \text{the annual gift tax exclusion for the year of the gift}))$$

Inherited Property

Basis in property inherited from a decedent is generally one of the following:

1. FMV at the date of the decedent's death.
2. FMV at the alternative valuation date, if the estate elects to use alternative valuation on the federal estate tax return.
3. The value under the special-use valuation method for real property used in farming or a closely held business if chosen for estate tax purposes.
4. The decedent's adjusted basis in land to the extent of the value excluded from the decedent's taxable estate as a qualified conservation easement.

Note: If a federal estate tax return does not have to be filed, the basis in the property is its appraised value at the date of death for state inheritance or transmission taxes.

Appreciated property. The above rule does not apply to appreciated property received from a decedent if a T/P or T/P's spouse originally gave the property to the decedent within 1 year before the decedent's death. T/P's basis in this property is the same as the decedent's adjusted basis in the property immediately before his or her death, rather than its FMV. Appreciated property is any property whose FMV on the day it was given to the decedent is more than its adjusted basis.

Inherited Property (cont.)

Community property. In community property states (AZ, CA, ID, LA, NV, NM, TX, WA, & WI), married individuals are each usually considered to own half the community property. When either spouse dies, the total value of the community property, even the part belonging to the surviving spouse, generally becomes the basis of the entire property. For this rule to apply, at least half the value of the community property interest must be includable in the decedent's gross estate, whether or not the estate must file a return.

Qualified joint interest. Include one-half of the value of a qualified joint interest in the decedent's gross estate. It does not matter how much each spouse contributed to the purchase price. Also, it does not matter which spouse dies first. A qualified joint interest is any interest in property held by married individuals as either of the following.

- ▶ Tenants by the entirety, or
- ▶ Joint tenants with right of survivorship if the married couple are the only joint tenants.

Basis. The surviving spouse's basis in the property owned with his or her spouse as a qualified joint interest is the cost of the surviving spouse's half of the property with certain adjustments. Decrease the cost by any deductions allowed to the surviving spouse for depreciation and depletion. Increase the reduced cost by the basis in the half inherited.

Property Received for Services

Property received for services must be included in income at its FMV. The FMV becomes the basis in the property. If the services were performed for a price agreed on beforehand, it will be accepted as the FMV of the property if there is no evidence to the contrary.

Property purchased from employer below FMV. Include in income the difference between the purchase price and the FMV.

Exception: The difference represents a qualified employee discount.

Restricted property. If property received for services is subject to certain restrictions, the basis in the property is its FMV when it becomes substantially vested unless the T/P makes a section 83(b) election. The property is substantially vested when it is transferable or not subject to a risk of forfeiture (losing the property).

Section 83(b) election. The T/P can choose under IRC section 83(b) to include the property in income in the year of transfer. If the election is taken the basis of the property will be the FMV at the date of transfer.

Stock Dividends, Rights, and Splits

Basis of stock. The basis is the purchase price plus the cost of the purchase such as commissions or recording fees.

Taxable distribution. The basis in a taxable stock dividend or stock right is its FMV at the time of the distribution.

Nondividend distribution. Considered a return of capital; Reduce basis by distribution amount.

Stock dividend or split. The basis per share of stock must be adjusted if additional stock is received through stock dividend or splits.

Example: Purchased 50 shares of ABC Corp stock for \$1,500 or \$30 a share in 2019

Purchased 100 shares of ABC Corp stock for \$4,500 or \$45 a share in 2020

ABC declares a 3-for-2 stock split in 2022.

Basis in stock in 2022:

$50 \times 3/2 = 75$ shares with a basis of $\$1,500 \div 75 = \20 a share

$100 \times 3/2 = 150$ shares with a basis of $\$4,500 \div 150 = \30 a share

Note: The total basis amount does not change.

Property Transfers between Spouses

No gain or loss is recognized on a transfer of property from an individual to (or in trust for the benefit of) a spouse, or if incident to a divorce, a former spouse. This nonrecognition rule does not apply in the following situations:

- ▶ The recipient spouse or former spouse is a nonresident alien.
- ▶ Property is transferred in trust and liability exceeds basis. Gain must be recognized to the extent the amount of the liabilities assumed by the trust, plus any liabilities on the property, exceed the adjusted basis of the property.

Basis in transferred property. The transferee's basis in the property will be the same as the adjusted basis of the transferor. However, for property transferred in trust, the basis is adjusted for any gain recognized by the transferor if the liabilities assumed, plus the liabilities to which the property is subject, are more than the adjusted basis of the property transferred.

Property Changed to Business or Rental Use

Basis for depreciation. The basis for depreciation is the lesser of the following amounts.

- ▶ The FMV of the property on the date of the change, or
- ▶ The adjusted basis on the date of the change.

Basis for the sale of the property. The basis of the property sold will depend on whether the taxpayer is figuring a gain or loss.

Gain. The basis for figuring a gain is the adjusted basis when the property is sold.

Loss. Figure the basis for a loss by starting with the smaller of the adjusted basis or the FMV of the property at the time of the change to business or rental use. Then adjust this amount for the period after the change in the property's use to arrive at a basis for loss.

Nontaxable Exchanges (Section 1031)

A nontaxable exchange is an exchange of real property used in a business or held for investment for other real property used for business or investment real property of a like-kind.

Like-kind exchanges. To be nontaxable, a like-kind exchange must meet all of the following conditions:

1. Both the property transferred and the property received must be real property used in a trade or business or investment property.
2. The real property must not be held primarily for sale.
3. There must be an exchange of like-kind real property.
4. Property to be received must be identified within 45 days after the date of transfer of property given up in the exchange.
5. The exchange must be completed on or before the earlier of:
 - a) The 180th day after the date the property being exchanged was transferred, or
 - b) The due date, including extensions, for filing that year's tax return.

Basis in property received. The basis of the property received is the same as the basis of the property given up.

Capital Gains & Losses

Capital Assets & Noncapital Assets

Capital assets. For the most part, everything owned and used for personal purposes, pleasure, or investment is a capital asset.

Noncapital assets. Any property owned is a capital asset, except the following noncapital assets:

1. Property held for sale to customers or property that will physically become part of merchandise for sale to customers.
2. Depreciable property used in trade or business.
3. Real property used in trade or business.
4. A certain patent; an invention, model, or design (whether or not patented); or a secret formula or process.
5. A copyright, a literary, musical, or artistic composition, a letter or memorandum that is created by personal efforts, prepared or produced, or acquired under circumstances entitling T/P to the basis of the person who created the property or for whom it was prepared or produced.
6. Accounts or notes receivable acquired in the ordinary course of a trade or business for services rendered or from the sale of property described in (1).
7. U.S. Government publications received free or at a discount.
8. Certain commodities derivative financial instruments held by commodities derivatives dealers.
9. Hedging transactions, but only if the transaction is clearly identified as a hedging transaction before the close of the day on which it was acquired, originated, or entered into.
10. Supplies of a type regularly used or consumed in the ordinary course of a trade or business.

Capital Gains & Losses

Holding Period

Short-term. Property held for one year or less. Report gains or losses on Form 8949 & Schedule D.

Long-term. Property held for more than one year. Report gains or losses on Form 8949 & Schedule D.

Holding Period for Different Types of Acquisitions

Type of acquisition:	When the holding period starts:
Stocks and bonds bought on a securities market	Day after trading date the security was bought. Ends on trading date the security is sold.
US Treasury notes and bonds	If purchased at auction, day after notification of bid acceptance. If purchased through subscription, day after subscription was submitted.
Nontaxable exchanges	Day after date the old property was acquired.
Gift	If the basis is giver's adjusted basis, same day as giver's holding period began. If basis is FMV, day after date of gift.
Inherited	Treated as long-term regardless of how long the property is held.
Real property bought	Generally, day after date the title to the property is received.
Real property repossessed	Day after date originally received title to the property but does not include time between the original sale and date of repossession.

Capital Gains & Losses

Capital Gain Tax Rate

Maximum Long-Term Capital Gain Rate

If net capital gain is from...	Then maximum capital gain rate is...
collectibles gain	28%
eligible gain on qualified small business stock minus the section 1202 exclusion	28%
unrecaptured section 1250 gain	25%
other gain (if T/P's regular tax rate is 37%)	20%
other gain (if T/P's regular tax rate is 22%, 24%, 32%, or 35%)	15%
other gain (if T/P's regular tax rate is 10% or 12%)	0%

Net short-term capital gains. Net short-term capital gains are taxed as ordinary income.

Capital Gains & Losses

Sale of Stock

Mutual fund stock. Mutual fund investors must report as capital gain any amounts that the fund allocates as a capital gain distribution, even if the investor did not actually receive the distribution. Increase the basis in the fund by the difference between the undistributed capital gain included in income and the amount of tax paid for the investor by the fund. Report capital gain distributions as long-term gain regardless of how long the shares in the fund have been owned.

Wash sales. A wash sale occurs when a T/P (or spouse) sells or trades stock or securities at a loss and within 30 days before or after the sale buys substantially identical stock or securities. Losses from a wash sale are not deductible.

Return of capital. A return of capital reduces the basis of the stock. It is not taxable until basis in the stock is reduced to zero.

Capital gain distributions only. Do not file Form 8949 or Schedule D if both the following are true:

- ▶ The only amounts to report on Schedule D are capital gain distributions from box 2a of Form 1099-DIV (or substitute statement).
- ▶ No amounts are shown in box 2b (unrecaptured section 1250 gain), 2c (section 1202 gain, or 2d (collectibles (28%) gain) of any Form 1099-DIV (or substitute statement).

Capital Gains & Losses

Capital Gain Computation

How to Figure Capital Gains and Losses

Amount Recognized: Recognized gain is taxable income. Recognized losses are deductible from gross income.

Amount Realized: Money + FMV of property or service received + liabilities assumed by buyer.

Adjusted basis: Original cost or other basis + additions - deductions.

Amount Recognized: Amount Realized - Adjusted Basis.

Net gain or loss. The totals for short-term gains and losses and the totals for long-term gains and losses are figured separately. Merge short-term capital gains and losses by adding all short-term capital gains, then adding short-term capital losses. Subtract one total from the other. The result is net short-term capital gain or loss. Use the same steps to figure long-term gains or losses. Then merge short-term capital gains or losses with long-term capital gains or losses.

Capital Gains & Losses

Capital Loss Limitations and Carryovers

Capital Loss Limits

Maximum yearly limit: \$3,000 (\$1,500 if married filing separately)

Capital Loss Carryover

Capital loss exceeds the yearly limit. If net capital loss exceeds the yearly limit, carry over the excess to later years until it is completely used up. The carryover loss retains its original character as either long-term or short-term. When figuring capital loss carryover, use short-term losses first. If the yearly limit is not yet reached after using short-term losses, then use long-term loss until the limit is reached.

Decedent's capital loss. A capital loss sustained by a decedent during his or her last tax year (or carried over to that year from an earlier year) can be deducted only on the final income tax return filed for the decedent. The capital loss limits still apply in this situation. The decedent's estate cannot deduct any of the loss or carry it over to following years.

Joint and separate returns. If a T/P and his or her spouse once filed separate returns and are now filing a joint return, combine the separate capital loss carryovers. However, if the T/P and spouse once filed a joint return and are now filing separate returns, any capital loss carryover from the joint return can be deducted only on the return of the spouse who actually had the loss.

Capital Gains & Losses

Nonbusiness Bad Debt

Nonbusiness bad debts are bad debts that did not come from operating a trade or business. They are deductible as short-term capital losses. To be deductible, nonbusiness bad debts must be totally worthless. A partly worthless nonbusiness debt is not deductible.

Genuine debt required. A debt must be genuine to deduct a loss. A debt is genuine if it arises from a debtor-creditor relationship based on a valid and enforceable obligation to repay a fixed or determinable sum of money.

Basis in bad debt required. To deduct a bad debt, the T/P must have a basis in it. That is, the T/P must have already included the amount in income or loaned out cash. Cash method T/P's cannot take a bad debt deduction for unpaid salaries, wages, rents, fees, interest, dividends, and similar items.

When deductible. A bad debt is deducted only in the year the debt becomes worthless. A debt becomes worthless when there is no longer any chance that the amount owed will be paid.

How to report bad debts. Deduct nonbusiness bad debts as short-term capital losses on Form 8949.

Filing a claim for refund. If a T/P did not deduct a bad debt on his or her original return for the year it becomes worthless, the T/P can file a claim for a credit or refund due to the bad debt by filing Form 1040X to amend the return for the year the debt became worthless. The amended return must be filed within 7 years from the date the original return had to be filed, or 2 years from the date the taxes were paid, whichever is later.

Capital Gains & Losses

Small Business Stock (Section 1244)

Qualifications of Section 1244 Stock:

1. Stock must have been issued for money or property (other than stock and securities) in a domestic small business corporation,
2. During its 5 most recent tax years before the loss, the corporation must have derived more than 50% of its gross income from sources other than rents, royalties, dividends, interest, annuities and gains from sales and exchanges of stocks or securities,
3. Stock issued before July 19, 1984 must have been common stock, and
4. The corporation must have been largely an operating company for ordinary loss treatment to apply.

Treating Losses on Section 1244 Stock:

1. The stock must be issued to the individual taking the loss (must be original owner of the stock).
2. Deduct a loss on the sale, exchange, or worthlessness of small business stock as an ordinary loss.
3. The ordinary loss is reported on Form 4797.
4. The ordinary loss is limited to \$50,000. The limit is \$100,000 if married filing jointly even if only one spouse has this type of loss.

Capital Gains & Losses

Small Business Stock (Section 1244)

Contributed property. To determine ordinary loss on section 1244 stock received in a trade for property, reduce the basis of the stock if:

- ▶ The adjusted basis (for figuring loss) of the property, immediately before the trade, was more than its fair market value, and
- ▶ The basis of the stock is determined by the basis of the property.

Reduce the basis of the stock by the difference between the adjusted basis of the property and its fair market value at the time of the trade. Reduce the basis only to figure the ordinary loss. Do not reduce the basis of the stock for any other purpose.

Contributions to capital. If the basis of section 1244 stock has increased, through contributions to capital or otherwise, treat this increase as applying to stock that is not section 1244 stock when figuring an ordinary loss on its sale

Section 1202 exclusion. A T/P can exclude from income up to 50% of gain from the sale or trade of qualified small business stock held for more than 5 years. The exclusion can be up to 75% for stock acquired after February 17, 2009, and no later than September 27, 2010, and up to 100% for stock acquired after September 27, 2010.

Recordkeeping. The T/P must keep records that shows the stock qualifies as section 1244 stock. The records must also distinguish section 1244 stock from any other stock owned in the corporation.

Capital Gains & Losses Related Party Transactions

Property sold or traded to a related party. Cannot deduct a loss on the sale or trade of property to a related party (e.g. family member).

Property received from a related party. If property received from a related party is sold or traded at a gain, recognize the gain only to the extent that it is more than the loss previously disallowed to the related party.

Related parties include the following:

- ▶ **Family members.** This includes only brothers and sisters, half-brothers and half-sisters, spouse, ancestors (parents, grandparents, etc.), and lineal descendants (children, grandchildren, etc.).
- ▶ **A partnership** in which a person directly or indirectly owns more than 50% of the capital interest or the profits interest.
- ▶ **A corporation** in which a person directly or indirectly owns more than 50% in value of the outstanding stock.
- ▶ **A tax-exempt charitable or educational organization** directly or indirectly controlled, in any manner or by any method, by a person or by a member of that person's family, whether or not this control is legally enforceable.

Continued on next card

Capital Gains & Losses Related Party Transactions

In addition, a loss on the sale or trade of property is not deductible if the transaction is directly or indirectly between the following related parties:

- ▶ A grantor and fiduciary, or the fiduciary and beneficiary, of any trust.
- ▶ Fiduciaries of two different trusts, or the fiduciary and beneficiary of two different trusts, if the same person is the grantor of both trusts.
- ▶ A trust fiduciary and a corporation of which more than 50% in value of the outstanding stock is directly or indirectly owned by or for the trust, or by or for the grantor of the trust.
- ▶ A corporation and a partnership if the same persons own more than 50% in value of the outstanding stock of the corporation and more than 50% of the capital interest, or the profits interest, in the partnership.
- ▶ Two S corporations if the same persons own more than 50% in value of the outstanding stock of each corporation.
- ▶ Two corporations, one of which is an S corporation, if the same persons own more than 50% in value of the outstanding stock of each corporation.
- ▶ An executor and a beneficiary of an estate (except in the case of a sale or trade to satisfy a pecuniary bequest).
- ▶ Two corporations that are members of the same controlled group. (Under certain conditions, however, these losses are not disallowed but must be deferred.)
- ▶ Two partnerships if the same persons own, directly or indirectly, more than 50% of the capital interests or the profit interests in both partnerships.

Capital Gains & Losses

Installment Sales

An installment sale is a sale of property where one or more payments are received after the close of the tax year.

Payments. Each payment received usually consists of three parts:

1. Interest.
2. Return of investment (basis).
3. Gain on the sale.

Unstated interest. If an installment sale with some or all payments due more than one year after the date of sale does not provide for interest, part of each payment due more than 6 months after the date of sale will be treated as unstated (imputed) interest. The selling price and contract price must be reduced by any unstated (imputed) interest.

Capital Gains & Losses

Installment Sales

Figuring Gross Profit Percentage

To determine what part of the payment is gain, first determine the gross profit percentage:

$$\text{Gross profit percentage} = \text{Gross profit} \div \text{Contract price}$$

$$\text{Gross profit} = \text{Selling price} - (\text{Basis of property} + \text{Selling expenses})$$

$$\text{Selling price} = \text{Money rec'd} + \text{FMV of property rec'd} + \text{Mortgage assumed by buyer}$$

$$\text{Contract price} = \text{Down payment} + \text{Principal payments}$$

1. Selling price (money + FMV of property + mortgage assumed) \$ _____

2. Less the sum of:

Basis of property sold \$ _____

Selling expenses _____

Depreciation Recapture Income _____ \$ _____

3. Gross profit (line 1 - line 2) _____

4. Contract price (Down payment + principal payments) _____

5. Gross profit percentage (line 3 ÷ line 4) \$ _____

Capital Gains & Losses

Installment Sales

Dispositions of Installment Obligations

An installment obligation is the buyer's note, deed of trust, or other evidence that the buyer will make future payments. If the obligation is disposed of, a gain or loss is recognized. The gain or loss is the difference between the basis in the obligation and the amount realized.

The character of the gain or loss depends on the original installment sale. If the original installment sale of the property produced ordinary income, the disposition of the obligation will result in ordinary income or loss. If the original sale resulted in a capital gain, the disposition of the obligation will result in a capital gain or loss.

Repossession of Real Property

The repossession of real property cancels out the tax treatment that applied to the original installment sale and puts the T/P in the same tax position he was in before the sale. The T/P recovers his entire adjusted basis when he resells the repossessed property. Payments received from the buyer of the original sale must be included in income. Report, as gain from the repossession, any part of the payments that have not already been included in income.

Reporting an Installment Sale. Use Form 6252, Installment Sale Income, to report a sale of property on the installment method. The form is used to report the sale in the year it takes place and to report payments received in later years. Also, if the property is sold to a related person, the T/P may have to file the form each year until the installment debt is paid off.

Nontaxable Property Transactions Like-Kind Exchanges

Like-kind exchanges between related parties. Special rules limit whether certain exchanges made between related parties are nontaxable. Under these rules, if either party disposes of the property within 2 years after the exchange, the exchange is disqualified from nonrecognition treatment. Exceptions to these rules are the following:

1. Dispositions due to the death of either related party.
2. Involuntary conversions.
3. Exchanges or dispositions if it is established that their main purpose is not the avoidance of federal income tax.

Partially nontaxable exchange. Any money or unlike property received in a like-kind exchange is taxable, but only to the extent of the gain realized in the transaction. To figure the amount of the taxable gain, first determine the FMV of any unlike property received and add it to the amount of any money received then subtract any exchange expenses paid along with the adjusted basis of the property transferred. In a like-kind, if a T/P paid any money in addition to giving up like property, there is no taxable gain or deductible loss.

Assumption of liabilities. If the other party to a nontaxable exchange assumes any liabilities on property they receive, treat this transfer of liabilities as cash received in the amount of the liability.

Exclusion of gain. A T/P can exclude up to \$250,000 the gain on the sale of a main home if all of the following are true:

1. T/P owned the home for at least 2 of the last 5 years (the ownership test).
2. T/P lived in the home as his or her main home for at least 2 of the last 5 years (the use test).
3. T/P did not exclude gain from the sale of another home during the 2-year period ending on the date of the sale.

T/Ps filing jointly can exclude up to \$500,000 of the gain if all of the following are true:

1. Married and file a joint return for the year.
2. **Either** spouse meets the ownership test.
3. **Both** spouses meet the use test.
4. **Both** spouses did not exclude gain from the sale of another home during the 2-year period ending on the date of the sale.

Temporary absences. Short temporary absences for vacations or other seasonal absences, even if renting out the property during the absences, are counted as periods of use.

Ownership and use tests met at different times. A T/P can meet the ownership and use tests during different 2-year periods. However, the T/P must meet both tests during the 5-year period ending on the date of the sale.

Exceptions to ownership and use tests for T/P with a disability. There is an exception to the use test if:

- ▶ T/P becomes physically or mentally unable to care for himself or herself, and
- ▶ Owned and lived in the home as a main home for a total of at least 1 year during the 5-year period before the sale of the home.

Under this exception, the T/P is considered to live in his or her home during any time within the 5-year period that the T/P own the home and live in a facility (including a nursing home) licensed by a state or political subdivision to care for persons in the T/P's condition.

If the T/P meets this exception to the use test, the T/P still has to meet the 2-out-of-5-year ownership test to claim the exclusion.

Reduced maximum exclusion. If the T/P fails to meet the requirements to qualify for the exclusion, the T/P can still qualify for a reduced exclusion. To qualify for a reduced exclusion, the sale of the home must be due to one of the following reasons:

1. A change in place of employment.
2. Health.
3. Unforeseen circumstances (occurrence of an event that could not have been reasonably anticipated before buying the home such as loss of employment).

Exclusion on sale of main home by surviving spouse. If spouse dies, surviving spouse may qualify to exclude up to \$500,000 of any gain from the sale of a main home. To qualify, surviving spouse must not remarry, meet all the requirements for exclusion and the sale takes place within 2 years after the date of death of spouse.

Home acquired through transfer from spouse. If a T/P's home was transferred by a spouse or former spouse (whether in connection with a divorce or not), the T/P can count any time when the spouse owned the home as time owned by the taxpayer to meet the ownership test.

Death of a spouse. If a T/P sell his or her home within 2 years of the death of a spouse and the taxpayer has not remarried as of the sale date, the taxpayer can count any time the deceased spouse owned the home as time owned by the taxpayer to meet the ownership test.

Business use or rental of home. A T/P can exclude a gain from the sale of a home that was used for business or to produce rental income if the T/P meets the ownership and use tests.

Depreciation for business use after May 6, 1997. A T/P cannot exclude part of the gain equal to any depreciation allowed or allowable as a deduction for periods after May 6, 1997.

Loss on sale. A loss on the sale of a main home is not deductible.

Foreclosure. If a home is abandoned, foreclosed on, or repossessed, it is treated as a sale or a disposition and any gain must be realized.

Trading homes. Trading an old home for a new home is treated as a sale and purchase.

Vacant land next to home. Vacant land adjacent to the land on which a main home sits qualifies as part of the sale of a main if ALL of the following are true.

- ▶ The vacant land is used and owned by the taxpayer as part of the main home.
- ▶ The sale of the vacant land and the sale of the main home happened within 2 years of each other.
- ▶ Both sales either meet the eligibility test or qualify for partial tax benefits.

If the sale of vacant land meets all these requirements, the taxpayer must treat that sale and the sale of the main home as a single transaction for tax purposes.

Like-kind/1031 exchange. A T/P cannot claim the exclusion if:

- ▶ The T/P acquired the home in a like-kind exchange (also known as a section 1031 exchange), or the basis in the home is determined by reference to the basis of the home in the hands of the person who acquired the property in a like-kind exchange (e.g., received home as a gift), and
- ▶ The T/P sold the home during the 5-year period beginning with the date the home was acquired in the like-kind exchange.

Reporting the sale. Do not report the sale of a main home on the tax return unless:

- ▶ There is a gain on the sale and the gain does not qualify for full exclusion,
- ▶ There is a gain and the T/P chooses not to exclude it, or
- ▶ The T/P receives Form 1099-S.

Report the entire gain or loss on Form 8949, Sales and Other Dispositions of Capital Assets, and Schedule D (Form 1040 or 1040-SR), Capital Gains and Losses.

Capital Gains & Losses Reporting Gains & Losses

A T/P reports gains and losses depending on his or her following classification:

- ▶ Investor
- ▶ Trader
- ▶ Securities Dealer

Investor. Investors typically buy and sell securities and expect income from dividends, interest, or capital appreciation. They buy and sell these securities and hold them for personal investment. They are not conducting a trade or business. Sales of these securities result in capital gains and losses that must be reported on Form 1040 or 1040-SR, Schedule D, Capital Gains and Losses and on Form 8949, Sales and Other Dispositions of Capital Assets.

Trader. Special rules apply if the T/P is a trader in securities, in the business of buying and selling securities for his or her own account. The law considers this to be a business, even though a trader does not maintain an inventory and does not have customers. Traders report their business expenses on Form 1040 or 1040-SR, Schedule C, Profit or Loss From Business. The Schedule A limitations on investment interest expense, which apply to investors, do not apply to interest paid or incurred in a trading business. Commissions and other costs of acquiring or disposing of securities are not deductible but must be used to figure gain or loss upon disposition of the securities.

Capital Gains & Losses

Reporting Gains & Losses

Dealers. Dealers in securities may be individuals or business entities. Dealers purchase, hold, and sell securities to their customers in the ordinary course of their trade or business. Sometimes they maintain an inventory. Dealers are distinguished from investors and traders because they have customers and derive their income from marketing securities for sale to customers. Section 475 requires dealers to keep and maintain records that clearly identify securities held for personal gain versus those held for use in their business activity. Dealers must report gains and losses associated with dispositions of securities by using the mark-to-market rules.

The Mark-to-Market Election. Traders can choose to use the mark-to-market rules, investors cannot. If a trader does not make a valid mark-to-market election under section 475(f), then he or she must treat the gains and losses from sales of securities as capital gains and losses and report the sales on Form 1040 or 1040-SR, Schedule D and on Form 8949 as appropriate. When reporting on Schedule D, both the limitations on capital losses and the wash sales rules continue to apply. However, if a trader makes a timely mark-to-market election, then he or she can treat the gains and losses from sales of securities as ordinary gains and losses (except for securities held for investment) that must be reported on Part II of Form 4797, Sales of Business Property. Neither the limitations on capital losses nor the wash sale rules apply to traders using the mark-to-market method of accounting. In general, a trader must make the mark-to-market election by the due date (not including extensions) of the tax return for the year prior to the year for which the election becomes effective. A trader can make the election by attaching a statement either to his or her income tax return.

Adjustments to Gross Income

Traditional IRAs

An individual retirement account is a trust or custodial account set up in the U.S. for the exclusive benefit of the T/P or the benefit of the T/P's beneficiaries. The account is created by a written document. The document must show that the account meets all the following requirements:

1. The trustee or custodian must be a bank, a federally insured credit union, a savings and loan association, or an entity approved by the IRS to act as trustee or custodian.
2. The trustee or custodian generally cannot accept contributions of more than the deductible amount for the year. However, rollover contributions and employer contributions to a simplified employee pension (SEP) can be more than this amount.
3. The contributions must be in cash, except that rollover contributions can be property other than cash.
4. The amount in the account must be fully vested (T/P must have a nonforfeitable right to the amount) at all times.
5. Money in the account cannot be used to buy a life insurance policy.
6. Assets in the account cannot be combined with other property, except in a common trust fund or common investment fund.
7. T/P must start receiving distributions from the account by April 1 of the year following the year in which age 72 is reached.

Adjustments to Gross Income

Traditional IRAs

Contributions. A T/P regardless of age can contribute up to \$6,000 (\$7,000 if T/P is age 50 or older) or 100% of taxable compensation, whichever is less in each year. The contribution must be made by the due date for filing his or her return (excluding extensions).

Compensation includes:

1. Wages and salaries, etc.
2. Commissions.
3. Self-employment income.
4. Taxable alimony and separate maintenance under a decree executed before 2019.
5. Nontaxable combat pay.

Note: Self-employment loss should not be subtracted from wages and salaries received when figuring total compensation.

Compensation does not include:

1. Earnings and profits from property, such as rental income, interest income, and dividend income.
2. Pension or annuity income.
3. Deferred compensation received (compensation payments postponed from a past year).
4. Income from a partnership for which a T/P provides no services that are a material income-producing factor.
5. Any amounts excluded from income, such as foreign earned income and housing costs.

Adjustments to Gross Income

Spousal IRAs

Spousal IRA limit. In the case of a married couple with unequal compensation who file a joint return, the deduction for contribution to the traditional IRA of the spouse with less compensation is limited to the smaller of the following two amounts:

1. \$6,000 (7,000 if T/P is age 50 or older), or
2. The total compensation includible in gross income of both spouses for the year reduced by the following three amounts.
 - a) The IRA deduction of the spouse with the greater compensation.
 - b) Any designated nondeductible contribution for the year made on behalf of the spouse with the greater compensation.
 - c) Any contribution to a Roth IRA on behalf of the spouse with the greater compensation.

Both spouses have compensation. If both spouses have compensation each can set up an IRA. An IRA cannot be set up for spouses to use jointly. If filing a joint return, only one spouse needs to have compensation.

Combined contributions. The total combined contributions for T/P's IRA and spousal IRA is the smaller of \$12,000 (\$14,000 if both are age 50 or older) or taxable compensation for the year.

Adjustments to Gross Income

Traditional IRAs

Not covered by employer plan. If the T/P is not covered by an employer retirement plan, the T/P can take a full deduction on the amount contributed.

Covered by employer plan. If T/P is covered by an employer retirement plan, the amount of contribution that can be deducted depends on the T/P's modified AGI and filing status (see next card for AGI limits).

Married taxpayers. If a T/P is not covered by an employer retirement plan, but his or her spouse is, the T/P's IRA deduction is reduced or eliminated entirely depending on the T/P's modified AGI and filing status (see next card for AGI limits).

Modified AGI. The amount of AGI without taking into account the follow amounts:

1. IRA deduction.
2. Student loan interest deduction.
3. Foreign earned income exclusion from Form 2555.
4. Foreign housing exclusion or deduction from Form 2555.
5. Exclusion of qualified savings bond interest from Form 8815.
6. Exclusion of employer-paid adoption expenses from Form 8839.

Adjustments to Gross Income

Traditional IRAs—Deductible Contribution

Worksheet for reduced IRA deduction (If T/P or T/P's spouse is covered by an employer)

If T/P is covered and Filing status is:	Phaseout range modified AGI	Top phaseout range
S or H/H	\$68,000 to \$78,000	\$78,000
MFJ or QSS	\$109,000 to \$129,000	\$129,000
MFS	\$0 to \$10,000	\$10,000
If T/P's spouse is covered, but T/P is not and filing status is:	Phaseout range modified AGI	Top phaseout range
MFJ	\$204,000 to \$214,000	\$214,000
MFS	\$0 to \$10,000	\$10,000

- Enter top phaseout range. \$ _____
- Enter modified AGI (combined, if married filing jointly). \$ _____
- Subtract line 2 from line 1. \$ _____
- If MFJ or QSS, Multiply line 3 by 30% (.30) (by 35% (.35) if age 50 or older)
All others, multiply line 3 by 60% (.60) (by 70% (.70) if age 50 or older).. \$ _____
- Enter compensation \$ _____
- Enter contributions made \$ _____
- IRA deduction. (The smaller of 4, 5 & 6). \$ _____

Adjustments to Gross Income

Traditional IRAs

Nondeductible Contributions

Nondeductible contributions. Although a deduction for IRA contributions may be reduced or eliminated, contributions can be made to an IRA of up to the general limit or, if it applies, the spousal IRA limit. The difference between the total permitted contributions and the IRA deduction is the nondeductible contribution.

Form 8606. To designate contributions as nondeductible, Form 8606 must be filed. Form 8606 must be filed to report nondeductible contributions even if the taxpayer does not have to file a tax return for the year.

Failure to report nondeductible contributions. If a T/P does not report nondeductible contributions, all of the contributions to the taxpayer's traditional IRA will be treated like deductible contributions when withdrawn. All distributions from the IRA will be taxed unless the T/P can show, with satisfactory evidence, that nondeductible contributions were made.

Penalty for failure to file Form 8606. A T/P will have to pay a \$50 penalty if he or she does not file a required Form 8606, unless the T/P can prove that the failure was due to reasonable cause.

Cost Basis. A T/P will have a cost basis in his or her traditional IRA if they made any nondeductible contributions. The cost basis is the sum of the nondeductible contributions to the IRA minus any withdrawals or distributions of nondeductible contributions.

Adjustments to Gross Income

Traditional IRAs

Excess Contributions

An excess contribution is the amount contributed to a traditional IRA for the year that is more than the smaller of:

1. \$6,000 (\$7,000 if age 50 or older), or
2. T/P's taxable compensation for the year.

The taxable compensation limit applies whether the contributions are deductible or nondeductible.

Tax on excess contributions. If the excess contribution is not withdrawn by the due date of the tax return (including extensions), the T/P will be subject to a **6% tax**.

Excess contributions withdrawn by the due date of return. T/P will not be subject to the 6% tax if the excess contribution made during a tax year is withdrawn and any interest or other income earned on the excess contribution is also withdrawn by the due date of the return (including extensions).

How to treat withdrawn interest or other income. Include in gross income the interest or other income that was earned on the excess contribution. Report it on the return for the year in which the excess contribution was made. The withdrawal of interest or other income may be subject to an additional 10% tax on early distributions.

Adjustments to Gross Income

Traditional IRAs

Excess Contributions (Cont.)

Form 1099-R. T/P will receive Form 1099-R indicating the amount of the withdrawal. If the excess contribution was made in a previous tax year, the form will indicate the year in which the earnings are taxable.

Deducting an excess contribution in a later year. A T/P cannot apply an excess contribution to an earlier year even if the T/P contributed less than the maximum amount allowable for the earlier year. However, the T/P may be able to apply it to a later year if the contributions for that later year are less than the maximum allowed for that year. The amount to deduct this year is the lesser of the following two amounts.

- ▶ The maximum IRA deduction for this year minus any amounts contributed to an traditional IRAs for this year.
- ▶ The total excess contributions in the IRAs at the beginning of this year.

This method lets the T/P avoid making a withdrawal. It does not, however, let the T/P avoid the 6% tax on any excess contributions remaining at the end of a tax year.

Adjustments to Gross Income

Traditional IRAs - Prohibited Transactions

A prohibited transaction is any improper use of T/P's IRA account or annuity by the T/P or any disqualified person. There is a 15% excise tax on the amount of the prohibited transaction and a 100% additional tax if the transaction is not corrected.

Disqualified persons. Disqualified persons include the T/P's fiduciary and his or her family members (spouse, ancestor, lineal descendant, and any spouse of a lineal descendant).

Prohibited transactions. Examples of prohibited transactions with an IRA:

1. Borrowing money from it.
2. Selling property to it.
3. Receiving unreasonable compensation for managing it.
4. Using it as security for a loan.
5. Buying property for personal use (present or future) with IRA funds.

IRA ceases to be an IRA. Generally, if T/P or a beneficiary engages in a prohibited transaction in connection with a traditional IRA account at any time during the year, the account stops being an IRA as of the first day of that year. The account is treated as distributing all its assets to T/P at their fair market values on the first day of the year. If the total of those values is more than the T/P's basis in the IRA, the T/P will have a taxable gain that is included in income. The T/P may also have to pay the 10% tax on premature distribution.

Retirement Plan Rules for 2022

Type of Plan	Last Date for Contribution	Maximum Contribution	Maximum Deduction	When to Set Up Plan
SEP	Due date of employer's return (including extensions).	Smaller of \$61,000 or 25% of participants compensation.	25% of all participants compensation	Any time up to due date of employer's return (incl. ext).
SIMPLE IRA and SIMPLE 401(k) Plan	<p>Salary reduction contributions: 30 days after the end of the month for which the contributions are to be made.</p> <p>Matching or nonelective contributions: Due date of employer's return (including extensions)</p>	<p>Employee: Salary reduction contribution, up to \$14,000 (\$17,000 if age 50 or over).</p> <p>Employer contribution: Either dollar-for-dollar matching contributions, up to 3% of employee's compensation, or fixed nonelective contributions of 2% of compensation.</p>	Same as maximum contribution.	<p>Any time between 1/1 and 10/1 of the calendar year.</p> <p>For a new employer coming into existence after 10/1, as soon as administratively feasible.</p>
Qualified Plan: Defined Contribution Plan	<p>Elective deferral: Due date of employer's return (including extension).</p> <p>Employer contribution: Due date of employer's return (including extensions)</p>	<p>Employee contribution: Elective deferral up to \$20,500 (\$27,000 if age 50 or older).</p> <p>Employer contribution: Smaller of \$61,000 or 100% of participant's compensation</p>	25% of all participants' compensation, plus amount of elective deferrals made.	By the end of the year.
Qualified Plan: Defined Benefit Plan	Contributions generally must be paid in quarterly installments, due 15 days after the end of each quarter.	Smaller of \$245,000 or 100% of participant's compensation for highest 3 consecutive calendar years.	Based on actuarial assumptions and computations.	By the end of the year.

Adjustments to Gross Income

Alimony

Nondeductibility of alimony. Generally, for divorce or separation agreements executed after December 31, 2018, a T/P can no longer deduct an amount equal to the alimony or separate maintenance payments paid during the tax year, nor will the alimony or separate maintenance payments be included in the gross income of the recipient spouse.

Alimony requirements. A payment to a spouse under a divorce or separation instrument is alimony if the spouses do not file a joint return and all the following are met:

1. The payments are required by a divorce or separation instrument.
2. Payer and recipient spouse do not file a joint return or live with each other.
3. The payment is in cash only (including checks and money orders).
4. The instrument does not designate the payment as not alimony.
5. Spouses legally separated under a decree of divorce or separate maintenance are not members of the same household when payments are made.
6. Payments are not required after the death of recipient spouse.
7. The payment is not treated as child support.

Payments to a third party. Payments to a third party on behalf of a spouse under the terms of a divorce or separation instrument may be alimony, if they otherwise qualify. This includes payments for spouse's medical expenses, housing costs, taxes, tuition, etc. The payments are treated as received by the spouse and then paid to the third party.

Adjustments to Gross Income

Health Savings Account

Requirements. A health savings account (HSA) is a tax-exempt trust or custodial account that a T/P sets up with a qualified HSA trustee to pay or reimburse certain medical expenses. To qualify for a HSA, a T/P must meet the following requirements:

1. Have a high deductible health plan (HDHP).
2. Have no other health coverage that is not a HDHP (with some exceptions).
3. Have not enrolled in Medicare.
4. T/P cannot be claimed on someone else's tax return.

Benefits of an HSA:

1. Contributions made by T/P are tax deductible as an adjustment to gross income.
2. Contributions made by employer may be excluded from gross pay.
3. Contributions remain in T/P's account from year to year until the T/P uses them.
4. Interest or other earnings on assets in the account are tax free.
5. Distributions may be tax free if used to pay qualified medical expenses.
6. An HSA stays with the T/P if T/P changes employers or leaves the work force.

Last-month rule. Under the last-month rule, if a T/P is an eligible individual on the first day of the last month of his or her tax year (December 1 for most taxpayers), the T/P is considered an eligible individual for the entire year.

Adjustments to Gross Income

Health Savings Account

High deductible health plan (HDHP). An HDHP has:

- ▶ A higher annual deductible than typical health plans, and
- ▶ A maximum limit on the sum of the annual deductible and out-of-pocket medical expenses that a T/P must pay for covered expenses. Out-of-pocket expenses include copayments and other amounts, but do not include premiums.

The following shows the minimum annual deductible and maximum annual deductible and other out-of-pocket expenses for HDHPs for 2022:

<u>Type of coverage</u>	<u>Minimum Annual Deductions</u>	<u>Maximum Annual Deduction and Other Out of Pocket Expenses</u>
Self-only	\$1,400	\$7,050
Family	\$2,800	\$14,100

Contributions to an HSA. Any eligible individual can contribute to an HSA. For an employee's HSA, the employee, the employee's employer, or both may contribute to the employee's HSA in the same year. For an HSA established by a self-employed (or unemployed) individual, the individual can contribute. Family members or any other person may also make contributions on behalf of an eligible individual. Contributions to an HSA must be made in cash not stock or property.

Limits on contributions. The amount that can be contributed to an HSA depends on the type of HDHP coverage, T/P's age, the date on becoming an eligible individual, and the date the T/P ceases to be an eligible individual. For 2022, self-only HDHP coverage can contribute up to \$3,650 and family HDHP coverage can contribute up to \$7,300.

Adjustments to Gross Income Health Savings Account

When To Contribute. A T/P can make contributions to an HSA for 2022 until April 15, 2023. If a T/P fails to be an eligible individual during the tax year, the T/P can still make contributions until April 15, 2023 for the months he or she were an eligible individual. An employer can make contributions to an employee's HSA from January 1, 2023, through April 15, 2023, that are allocated to 2022. The employer must notify the employee and the trustee of the HSA that the contribution is for 2022. The contribution will be reported on the employee's 2023 Form W-2.

Form 8889. Report all contributions to on Form 8889 and file it with Form 1040 or 1040-SR.

Distributions From an HSA. Distributions from an HSA are tax-free distributions if used to pay or be reimbursed for qualified medical expenses incur after establishing the HSA. If the T/P is no longer an eligible individual, he or she can still receive tax-free distributions to pay or be reimbursed qualified medical expenses.

Qualified medical expenses. Qualified medical expenses are those expenses that generally would qualify for the medical and dental expenses deduction. Amounts paid for over-the-counter medicine (whether or not prescribed) and menstrual care products are considered medical care and are considered a covered expense. Medical expenses paid with tax-free distributions from an HSA are not deductible as an itemized deduction on Schedule A (Form 1040 or 1040-SR).

Insurance premiums. Insurance premiums are not qualified medical expenses unless the premiums are for long-term care insurance, health care continuation coverage (i.e., COBRA), health care coverage while receiving unemployment compensation under federal or state law, or Medicare and other health care coverage if T/P is 65 or older (other than premiums for a Medicare supplemental policy).

Adjustments to Gross Income

Education Related Adjustments

Student Loan Interest Deduction

Requirements. A T/P can deduct up to \$2,500 interest on a student loan if all of the following apply:

1. T/P paid interest on a qualified student loan.
2. T/P's filing status is any status except married filing separate.
3. T/P is not claimed as a dependent on someone's tax return.
4. T/P is legally obligated to pay interest on a qualified student loan.

Loan qualifications. The student loan must have been taken out solely to pay qualified education expenses and cannot be from a related person or made under a qualified employer plan.

Student qualifications. The student must be T/P, spouse or dependent and enrolled at least half-time in a program leading to a degree, certificate, or other recognized educational credential at an eligible educational institution. Exception: For purposes of the student loan interest deduction, the following are exceptions to the general rules for dependents:

- ▶ An individual can be the T/P's dependent even if the T/P is the dependent of another T/P.
- ▶ An individual can be the T/P's dependent even if the individual files a joint return with a spouse.
- ▶ An individual can be the T/P's dependent even if the individual had gross income for the year that was equal to or more than (\$4,400 for 2022).

Adjustments to Gross Income

Education Related Adjustments

Student Loan Interest Deduction (cont.)

Qualified education expenses. For purposes of the student loan interest deduction, these expenses are the total costs of attending an eligible educational institution, including graduate school. They include amounts paid for the following items:

- ▶ Tuition and fees.
- ▶ Room and board.
- ▶ Books, supplies, and equipment.
- ▶ Other necessary expenses (such as transportation).

The cost of room and board qualifies only to the extent that it is not more than:

- ▶ The allowance for room and board, as determined by the eligible educational institution, that was included in the cost of attendance (for federal financial aid purposes) for a particular academic period and living arrangement of the student, or
- ▶ If greater, the actual amount charged if the student is residing in housing owned or operated by the eligible educational institution.

Adjustments to Qualified Education Expenses. Qualified education expenses must be reduced by certain tax-free items (such as the tax-free part of scholarships and fellowships).

Income phaseout. The amount of student loan interest deduction is phased out if modified AGI is between \$70,000 and \$85,000 (\$145,000 and \$175,000 if married filing jointly).

Adjustments to Gross Income

Education Related Adjustments

Educator Expenses

Eligible educators can deduct up to \$300 of qualified expenses paid as an adjustment to gross income. If T/P and spouse are filing jointly and both are eligible educators, the maximum deduction is \$600. However, neither spouse can deduct more than \$300 of his or her qualified expenses.

Eligible educator. An eligible educator is a kindergarten through grade 12 teacher, instructor, counselor, principal, or aide who worked in a school for at least 900 hours during a school year.

Qualified expenses. Qualified expenses include ordinary and necessary expenses paid in connection with books, supplies, equipment (including computer equipment, software, and services), and other materials used in the classroom. Qualified expenses do not include expenses for home schooling or for nonathletic supplies for courses in health or physical education.

Adjustments to Gross Income

Self-employment tax. One-half of self-employment tax is deducted as an adjustment to gross income.

Penalties on early withdrawal of savings. Report the total interest received as income on Schedule B without subtracting the penalty. Deduct the penalty as an adjustment to income. The entire penalty is deductible even if it exceeds the interest income.

Self-employed health insurance. A self-employed person, a partner with net earnings from self-employment, or a shareholder receiving wages from an S corporation in which he or she owns more than a 2% of the outstanding stock can deduct all of the health insurance premiums paid for themselves and their family as a business expense. The deduction cannot exceed the person's earned income.

Note: A T/P cannot take the deduction for any month in which he or she was eligible to participate in any subsidized health plan maintained by his or her employer or a spouse's employer.

Moving expense deduction eliminated, except for certain Armed Forces members. Moving expenses are not deductible unless the T/P is a member of the Armed Forces on active duty and, due to a military order, moved because of a permanent change of station. Reimbursements for certain moving expenses are no longer excluded from gross income of nonmilitary T/Ps.

Deductions from AGI 2022 Standard Deduction Chart

Pub17Pg93

Filing Status	Standard Deduction	65 or older*	Blind
S	\$12,950	Add \$1,750	Add \$1,750
MFJ or QSS	\$25,900	Add \$1,400	Add \$1,400
MFS	\$12,950	Add \$1,400	Add \$1,400
H/H	\$19,400	Add \$1,750	Add \$1,750

*If T/P turns 65 on January 1, 2023, T/P is considered 65 at end of 2022.

Standard deduction for dependents. The standard deduction for a person who can be claimed as a dependent on another person's tax return is limited to the greater of:

1. \$1,150, or
2. The dependent's earned income for the year plus \$400 (but not exceeding the regular standard deduction amount shown above for each filing status).

Note: A dependent T/P receives an addition standard deduction of \$1,750 (\$1,400 if married) for being 65 or older or blind.

Deductions from AGI

Itemized Deductions

Medical & Dental Expenses

Deductible Medical Expenses

- ▶ Bandages
- ▶ Birth control pills prescribed by doctor
- ▶ Body scan
- ▶ Braille books
- ▶ Doctors, dentists, and other medical practitioners fees
- ▶ Prescription medicines and insulin
- ▶ Transportation for needed medical care
- ▶ Wages for nursing services
- ▶ Treatment in a drug or alcohol center (includes meals & lodging provided by the center)
- ▶ Meals and lodging provided by a hospital during medical treatment
- ▶ Legal abortion
- ▶ Expenses of an organ donor
- ▶ Eye surgery—to promote the correct function of the eye
- ▶ Fertility enhancement, certain procedures
- ▶ Guide dogs or other animals aiding the blind, deaf, and disabled
- ▶ Hospital services fees (lab work, therapy, nursing services, surgery, etc.)
- ▶ Lead-based paint removal
- ▶ Legal operation to prevent having children such as a vasectomy or tubal ligation
- ▶ Long-term care contracts, qualified
- ▶ Nursing services
- ▶ Oxygen equipment and oxygen
- ▶ Pregnancy test kit
- ▶ Psychiatric and psychological treatment
- ▶ Special items (artificial limbs, false teeth, glasses, contact lenses, hearing aids, crutches, wheelchair, etc.)
- ▶ Special education for mentally or physically disabled persons
- ▶ Stop-smoking programs
- ▶ Wages for nursing services
- ▶ Weight-loss, certain expenses for obesity
- ▶ Part of life-care fee paid to retirement home designated for medical care

Deductions from AGI

Itemized Deductions

Medical & Dental Expenses (cont.)

Nondeductible Medical Expenses

- ▶ Expenses for general health (even if following doctor's advice) such as:
 - Health club dues
 - Household help
 - Social activities, such as dancing or swimming lessons
 - Trip for general health improvement
- ▶ Illegal operation, treatment, or medicine
- ▶ Surgery for purely cosmetic reasons
- ▶ Nonprescription medicine
- ▶ Prescription drugs purchased in (or ordered shipped) from another country, in most cases
- ▶ Maternity clothing
- ▶ Health savings account payments for medical expenses
- ▶ Contributions to Archer MSAs
- ▶ Flexible spending account reimbursements for medical expenses (if contributions were on a pre-tax basis)
- ▶ Teeth whitening
- ▶ Toothpaste, toiletries, cosmetics, etc.
- ▶ Baby sitting and childcare
- ▶ Nursing care for a healthy baby
- ▶ Diaper service
- ▶ Funeral, burial, or cremation expenses
- ▶ Weight loss program unless for obesity or other disease
- ▶ Nutritional supplements, vitamins, herbal supplements, "natural medicines," etc., unless recommended by a medical practitioner as a treatment for a specific medical condition diagnosed by a physician

Deductions from AGI

Itemized Deductions

Medical & Dental Expenses (cont.)

Deductible Insurance Premiums:

- ▶ Hospital, surgical fees, and other medical and dental expenses.
- ▶ Prescription drugs and insulin.
- ▶ Replacement of lost or damaged contact lens.
- ▶ Qualified long-term care insurance contracts.
- ▶ Medicare B - supplemental medical insurance.
- ▶ Medicare D - voluntary prescription drug insurance.

Nondeductible Insurance Premiums:

- ▶ Life insurance policies.
- ▶ Policies providing payment for loss of earnings.
- ▶ Policies for loss of life, limb, sight, etc.
- ▶ Policies that pay a guaranteed amount each week for a stated number of weeks if hospitalized for sickness or injury.
- ▶ The part of car insurance that provides medical insurance coverage for all persons injured.
- ▶ Health or long-term care insurance if the premiums are paid with tax-free distributions from a retirement plan made directly to the insurance provider and these distributions would otherwise have been included in income.

Deductions from AGI Itemized Deductions

Medical & Dental Expenses (cont.)

When to deduct medical expenses. Deduct medical expenses in the year paid regardless of when the services were provided.

Medical deduction limit. A T/P can deduct on Schedule A (Form 1040 or 1040-SR) only the amount of medical and dental expenses that is more than 7.5% of the T/P's AGI.

Paying others' medical expenses:

Spouse. T/P must have been married at the time expenses were incurred or when they were paid.

Dependents. T/P can deduct medical expenses for a person (including a child before adoption) who can be claimed as a dependent at the time expenses were incurred or when they were paid. T/P can also deduct medical expenses paid for a person who could be claimed as a dependent except that the person had gross income of \$4,400 or more or had filed a joint return.

Deceased spouse or dependent. T/P can deduct medical expenses in the year paid.

Child of divorced or separated parents. If both divorced or separated parents combine to provide more than half the child's support, either parent can deduct medical expenses paid for that child.

Deductions from AGI Itemized Deductions

Medical & Dental Expenses (cont.)

When to deduct decedent's medical expenses. Medical expenses for a decedent that are paid from his or her estate are treated as paid at the time the medical services were provided if they are paid within the one-year period beginning with the day after the date of death.

Capital expenses. Cost of special equipment installed in the home is deductible if it is for medical care for T/P, spouse or dependent. Cost of the equipment must be reduced by the increase in property value.

Medical savings account. Amounts contributed to a medical savings account are not deducted as medical expenses. The amount is deducted as an adjustment to gross income.

Transportation expense. Include in medical expense the cost of transportation primarily for, and essential to, medical care including bus, taxi, train, or plane fares. T/P can include out-of-pocket car expenses used for medical reasons or can use the standard medical mileage rate of 18 cents per mile.

Lodging and meals. Include in medical expenses the cost of meals and lodging at a hospital or similar institution if a principle reason for being there is to receive medical care. T/P can include in medical expenses the cost of lodging not provided in a hospital if the lodging is for and essential to medical care. The amount for lodging cannot be more than \$50 for each night for each person. Meals are not included.

Deductions from AGI

Itemized Deductions

TAXES

Test to deduct any tax. The following two tests must be met to deduct any tax.

- ▶ The tax must be imposed on T/P.
- ▶ T/P must pay the tax during the tax year.

Deductible Taxes:

- ▶ State and local income taxes or general sales tax (but not both).
- ▶ Foreign income taxes.
- ▶ Employee contribution to state disability fund or state unemployment fund.
- ▶ State or local real estate taxes.
- ▶ State and local personal property taxes.
- ▶ Tenant's share of real estate taxes paid by cooperative housing corporations (co-ops).
- ▶ Taxes that are expenses of business or producing income.
- ▶ Taxes on property producing income.
- ▶ Occupational taxes.
- ▶ State or local personal property taxes that is:
 1. Charged on personal property,
 2. Based only on the value of the personal property, and
 3. Charged on a yearly basis, even if collected more or less than once a year.

TAXES**Nondeductible Taxes and Fees:**

- ▶ Federal income taxes.
- ▶ Employee contribution to private or voluntary disability plans.
- ▶ Federal excise taxes.
- ▶ Foreign real estate taxes.
- ▶ Per capita taxes.
- ▶ Social Security and other employment taxes for household workers.
- ▶ Gift taxes.
- ▶ Estate or inheritance taxes.
- ▶ Fines and penalties.
- ▶ Real Estate-Related Items:
 - Trash or pickup fees.
 - Homeowners association fees.
 - Rent increase due to higher real estate taxes.
 - Taxes for local benefits (e.g. property improvements).
 - Transfer taxes.

Deductions from AGI Itemized Deductions

State and local real estate taxes. Real estate taxes must be divided between the buyer and seller according to the number of days each owned the property in the property tax year. Neither buyer nor seller can deduct taxes paid before or after ownership.

Taxes placed in escrow. If monthly mortgage payments include amounts put in escrow for real estate taxes, a T/P can only deduct the real estate tax that the third party actually paid to the taxing authority in the year it is paid.

Delinquent taxes. If the buyer agrees to pay delinquent taxes, the buyer cannot deduct them. The buyer must add them to the cost of the property. The seller can deduct these taxes paid by the buyer.

Tenants by the entirety. If a married couple held a property as tenants by the entirety and file separate federal returns, each spouse can deduct only the taxes each paid on the property.

Refund (or rebate). If a T/P received a refund or rebate of real estate taxes paid, the T/P must reduce the deduction by the amount refunded. If the T/P received a refund or rebate of real estate taxes deducted in an earlier year, include the refund or rebate in income in the year it is received.

Limitation on deduction for state and local taxes. The deduction for state and local taxes is limited to \$10,000 (\$5,000 if married filing married separately). State and local taxes include state and local income tax or general sales taxes, real estate taxes, and personal property taxes.

Deductions from AGI Itemized Deductions

Interest Expense

Mortgage interest. Home mortgage interest is any interest paid on a loan secured by a main home or second home that the T/P has an ownership interest. If all of the T/P's mortgages fit into one or more of the following three categories at all times during the year, the T/P can deduct all of the interest on those mortgages. The three categories are the following:

1. **Grandfathered debt.** Mortgages taken out on or before October 13, 1987.
2. **Home acquisition debt.** Mortgages taken out after 10/13/87 and prior to 12/16/17, to buy, build, or improve a home but only if throughout the year these mortgages plus any grandfathered debt totaled \$1 million or less (\$500,000 or less if married filing separately).
3. **Home acquisition debt.** Mortgages taken out after 12/15/17, to buy, build, or improve T/P's home but only if throughout the year these mortgages totaled 750,000 or less (\$375,000 or less if married filing separately).

Note: The dollar limits for the second and third categories apply to the combined mortgages on T/P's main home and second home.

No deduction for home equity loan interest. No matter when the indebtedness was incurred, a T/P cannot deduct the interest from a loan secured by a home to the extent the loan proceeds were not used to buy, build, or substantially improve the home.

Deductions from AGI Itemized Deductions

Interest Expense (cont.)

Qualified home. To take a home mortgage interest deduction, the debt must be secured by a qualified home. This means a main home or second home. A home includes a house, condominium, cooperative, mobile home, house trailer, boat, or similar property that has sleeping, cooking, and toilet facilities.

Late payment charge on mortgage payment. Late payment charges are deductible as home mortgage interest.

Mortgage prepayment penalty. Mortgage prepayment penalty is deductible as home mortgage interest.

Reverse mortgages. Interest on reverse mortgages is not deductible.

Refinanced home acquisition debt. Any secured debt use to refinance home acquisition debt is treated as home acquisition debt. However, the new debt will qualify as home acquisition debt only up to the amount of the balance of the old mortgage principal just before the refinancing. Any additional debt not used to buy, build, or substantially improve a qualified home is not home acquisition debt.

Deductions from AGI

Itemized Deductions

Interest Expense (cont.)

Mortgage insurance premiums. The itemized deduction for mortgage insurance premiums has expired and cannot be deducted in 2022.

Business interest. All interest related to a business is deductible.

Investment interest. Deduction is limited to amount of net investment income. Determine the amount of net investment income by subtracting investment expenses (other than interest expense) from investment income. Investment income includes property held for investment such as interest, dividends, annuities, and royalties.

Deductions from AGI

Itemized Deductions

Interest Expense (cont.)

Nondeductible Interest Expenses:

- ▶ Points charged for specific services:
 - Lender's appraisal fees.
 - Points charged for services of obtaining a VA or FHA loan.
 - Preparation cost of loan papers.
 - Settlement fees and notary fees.
- ▶ Service charges.
- ▶ Nonredeemable ground rent.
- ▶ Interest on income tax paid to the IRS or to a state or local tax agency.
- ▶ Annual fees on credit cards.
- ▶ Loan fees.
- ▶ Credit investigation fees.
- ▶ Mortgage insurance premiums
- ▶ Interest relating to tax-exempt income.
- ▶ Interest to purchase or carry tax-exempt securities.
- ▶ Interest to purchase or carry certain straddle positions.
- ▶ Personal interest:
 - Interest on car loan (nonbusiness use).
 - Interest on federal, state, or local income tax.
 - Finance charges on credit cards, consumer loans incurred for personal expenses.
 - Late payment charges by a utility.

Deductions from AGI

Itemized Deductions

Points

Points are prepaid interest and cannot be fully deducted when paid, but must be amortized over the life of the mortgage.

Exception: Points can be fully deducted in the year paid if all of the following tests are met:

1. The loan is secured by the T/P's main home.
2. The payment of points is an established business practice in the area where the loan was made.
3. The points paid did not exceed the number of points charged in that area.
4. T/P uses the cash method of accounting.
5. Points were not paid in place of amounts that are stated separately on the settlement statement, such as appraisal fees, inspection fees, title fees, attorney fees, and property taxes.
6. The funds provided at closing, plus any points the seller paid, were at least as much as the points charged. The funds cannot be borrowed from the lender or mortgage broker.
7. The loan was used to buy or build a main home.
8. The points were computed as a percentage of the principal amount of the mortgage.
9. The points are clearly shown on the settlement statement.

Deductions from AGI

Itemized Deductions

Points (cont.)

Second home. Points paid on loans secured by a second home must be amortized over the life of the loan.

Refinancing. Points paid to refinance a mortgage are not deductible in full in the year paid. This is true even if the new mortgage is secured by a main home. Points must be amortized over the life of the loan. However, if part of the refinanced mortgage proceeds was used to improve the main home and the first 6 tests listed on the previous card, the T/P can fully deduct the part of the points related to the improvement in the year paid if they are paid with the T/P's own funds. The rest of the points must be deducted over the life of the loan.

Mortgage ending early. If points are deducted over the life of the mortgage, deduct any remaining balance in the year the mortgage ends.

Points paid by seller. If a buyer meets the requirements on the previous card, he or she may deduct points paid by the seller. The buyer must reduce the basis of the home by the amount of seller-paid points. The seller cannot deduct these points as interest but can deduct them as selling expenses that reduce the amount realized by the seller.

Deductions from AGI

Itemized Deductions

Charitable Contributions

The contribution (money or property) must be made to qualified organizations. Examples of qualified Organizations (all 50% limit organizations):

- ▶ Churches and religious organizations.
- ▶ Most nonprofit charitable organizations such as Salvation Army, Red Cross, CARE, Goodwill Industries, United Way, etc.
- ▶ Most nonprofit educational organizations such as Boy & Girl Scouts, Boys and Girls Club of America, colleges, and museums.
- ▶ War veterans' organizations.
- ▶ Nonprofit schools and hospitals.
- ▶ Federal, state, and local governments (if the gifts are solely for public purposes).
- ▶ Civil defense organizations.
- ▶ Public parks and recreation facilities.
- ▶ Nonprofit volunteer fire companies.

Certain foreign charitable organizations. Under income tax treaties with Canada, Israel, and Mexico, a T/P may be able to deduct contributions to certain Canadian, Israeli, or Mexican charitable organizations. Generally, the T/P must have income from sources in that country.

Deductions from AGI

Itemized Deductions

Charitable Contributions (cont.)

Nonqualifying Organizations

- ▶ Country clubs and other social clubs
- ▶ Cost of raffle, bingo, or lottery tickets
- ▶ Tuition
- ▶ Value of time or services
- ▶ Value of blood given to a blood bank
- ▶ Donations to homeowner's associations
- ▶ Political contributions
- ▶ Any contribution that is earmarked for the use of a specific individual
- ▶ Groups that are run for personal profit
- ▶ Contributions for lobbying
- ▶ Individuals
- ▶ Foreign organizations (except certain Canadian, Israeli, and Mexican charities)
- ▶ Organizations run for profit
- ▶ Civic leagues, social and sports clubs, labor unions
- ▶ Chamber of commerce and other business organizations
- ▶ Athletic events seating rights

Deductions from AGI

Itemized Deductions

Charitable Contributions (cont.)

Nondeductible Charitable Contributions

Value of time or services. A person cannot claim a deduction for the value of his or her time or services contributed to a qualified organization including blood donations and the value of lost income while working as an unpaid volunteer.

Personal Expenses. A T/P cannot deduct personal, living, or family expenses while performing services for a qualified organization unless it is necessary for the T/P to be away from home overnight while performing the services.

Appraisal Fees. A T/P cannot deduct as a charitable contribution any fees paid to find the fair market value of donated property.

Athletic events. No deduction is allowed, if a T/P makes any payment to, or for the benefit of, a college or university in exchange for tickets (or the right to buy tickets) to an athletic event in an athletic stadium of the college or university.

Deductions from AGI

Itemized Deductions

Charitable Contributions (cont.)

Expenses paid for student living with T/P. T/P can deduct qualifying expenses (up to \$50 a month) for a foreign or American student who:

1. Lives in T/P's home under a written agreement between T/P and a qualified organization as part of a program of the organization to provide educational opportunities for the student,
2. Is not T/P's relative or dependent, and
3. Is a full-time student in the twelfth or any lower grade at a school in the U.S.

Out-of-pocket-expenses. Some expenses incurred while providing services to a qualified organization are deductible if they are:

1. Unreimbursed,
2. Directly connected with the service,
3. Solely attributable to the service, and
4. Not personal, living, or family expenses.

Deductions from AGI Itemized Deductions

Charitable Contributions (cont.)

Car expenses. Deduct actual car expenses or the standard rate of 14 cents a mile.

Travel expenses. Deduct travel expenses only if there was no significant element of personal pleasure, recreation, or vacation in such travel.

Benefits Received From Contribution. If a benefit is received from a contribution, deduct only the amount that is more than the fair market value of the benefit received.

Membership fees or dues. A T/P may be able to deduct membership fees or dues paid to a qualified organization. Deduct only the amount that is more than the value of the benefits received.

Foster parents. Foster parents may be able to deduct as a charitable contribution some of the costs of being a foster parent (foster care provider) if they have no profit motive in providing the foster care and are not, in fact, making a profit. A qualified organization must select the individuals the foster parents take into their home for foster care.

Costs of raffles, bingo, lottery, etc. A T/P cannot deduct as a charitable contribution amounts paid to buy raffle or lottery tickets or to play bingo or other games of chance.

Clothing and household items. A T/P cannot take a deduction for clothing or household items donated unless the clothing or household items are in good used condition or better.

Deductions from AGI

Itemized Deductions

Charitable Contributions (cont.)

Contributions of property. The amount of a charitable contribution of property is its FMV. If the FMV is greater than its adjusted basis on ordinary income property (held 1 year or less) the amount of deduction is the FMV less any short-term gain that would have been recognized if sold. If the property was a capital gain property (held more than 1 year) the amount of the deduction is generally the FMV of the property. A deduction of more than \$5,000 for one property requires a written appraisal be obtained and attached to the return.

Limits on deductions. The amount of the contribution cannot be more than 60% of AGI. Contribution can be further limited to either 20%, 30%, or 50% of AGI depending on the type of property donated and the type of organization. The 60% limitation does not apply to noncash contributions.

50% limit: Contributions (other than capital gain property) to 50% limit organizations.

30% limit:

1. Contributions for the use of any qualified organization.
2. Contributions to all qualifying organizations other than 50% limit organizations.
3. Contributions of capital gain property to 50% limit organizations.

20% limit: Contributions of capital gain property to organizations other than 50% limit organizations.

Carryovers. Contributions that cannot be deducted in the tax year because of the AGI limitations can be deducted in each of the next **5 years** until used up, but not beyond that time.

Deductions from AGI

Itemized Deductions

Charitable Contributions (cont.)

Recordkeeping requirements for cash contributions. A T/P cannot deduct a cash contribution, regardless of the amount, unless T/P keeps one of the following:

1. A bank record that shows the name of the qualified organization, the date of the contribution, and the amount of the contribution. Bank records may include canceled checks, bank statements, or credit card statements.
2. A receipt (or a letter or other written communication) from the qualified organization showing the name of the organization, the date of the contribution, and the amount of the contribution.
3. Payroll deduction records that shows, name of charity, date and amount of the contribution.

Written Acknowledgment Required. A T/P cannot deduct a contribution of \$250 or more unless T/P has a written acknowledgment of the contribution from the qualified organization or certain payroll deduction records. In figuring whether a contribution is \$250 or more, do not combine separate contributions to the same charitable organization. Each payment is a separate contribution. A written acknowledgment for a contribution of \$250 or more must be received before the due date of the return (including extensions) and must include:

1. The amount of cash contribution,
2. Whether the qualified organization gave the donor any goods or services (other than certain token items and membership benefits), and
3. A description and good faith estimate of the value of any goods or services provided to the donor.

Deductions from AGI Itemized Deductions

Casualty & Theft Losses - Nonbusiness

Casualty. A casualty is the damage, destruction, or loss of property resulting from an identifiable event that is sudden, unexpected, or unusual.

- ▶ A sudden event is one that is swift, not gradual or progressive.
- ▶ An unexpected event is one that is ordinarily unanticipated and unintended.
- ▶ An unusual event is one that isn't a day-to-day occurrence and that isn't typical.

Limitation on personal casualty and theft losses. Personal casualty and theft losses of an individual are deductible only to the extent they're attributable to a federally declared disaster. The loss deduction is subject to the \$100 limit per casualty and 10% of the T/P's adjusted gross income (AGI) limitation.

Exception: An exception to the rule limiting the deduction for personal casualty and theft losses to federal casualty losses applies where the T/P has a personal casualty gains. In this case, the T/P may deduct personal casualty losses that are not attributable to a federally declared disaster to the extent they don't exceed personal casualty gains.

Deductions from AGI Itemized Deductions

Casualty & Theft Losses - Nonbusiness (cont)

Types of casualty losses. There are three types of casualty losses.

1. ***Federal casualty loss.*** A federal casualty loss is an individual's casualty or theft loss of personal-use property that is attributable to a federally declared disaster.
2. ***Disaster loss.*** A disaster loss is a loss that is attributable to a federally declared disaster and that occurs in a an area eligible for assistance pursuant to the Presidential declaration.
3. ***Qualified disaster loss.*** A qualified disaster loss is an individual's casualty or theft loss of personal-use property that is attributable to a major disaster declared by the President under section 401 of the Stafford Act in 2016, as well as from Hurricane Harvey, Tropical Storm Harvey, Hurricanes Irma and Maria, or the California wildfires.

Deductions from AGI Itemized Deductions

Casualty & Theft Losses - Nonbusiness

Proof of Loss

Casualty loss proof. For a casualty loss, T/P's records should show all the following:

- ▶ The type of casualty (car accident, fire, storm, etc.) and when it **occurred**.
- ▶ That the loss was a direct result of the casualty.
- ▶ T/P was the owner of the property or, if T/P leased the property from someone else, T/P was contractually liable to the owner for the damage.
- ▶ Whether a claim for reimbursement exists for which there is a reasonable expectation of recovery.

Theft loss proof. For a theft loss, records should show all the following:

- ▶ When T/P **discovered** the property was missing.
- ▶ Proof when property was stolen.
- ▶ Proof of ownership of property.
- ▶ Whether a claim for reimbursement exists for which there is a reasonable expectation of recovery.

Deductions from AGI

Itemized Deductions

Casualty & Theft Losses - Nonbusiness

Loss on deposits (with insolvent financial institutions). T/P can choose one of the following ways to deduct the loss.

- ▶ As a nonbusiness bad debt deducted as a short-term capital loss on Form 8949 and Schedule D.
- ▶ As a casualty loss (to the extent the loss does not exceed personal casualty gain).

Deducted loss recovered. If any loss deducted in previous years is recovered, include the recovered amount in income.

When to deduct a loss. Deduct the part of a casualty or theft loss that is not reimbursable in the tax year the casualty occurred or the theft was discovered.

Deductions from AGI

Itemized Deductions

Casualty & Theft Losses - Nonbusiness

Insurance Reimbursements

Failure to file a claim for reimbursement. If property is covered by insurance, T/P must file a timely insurance claim for reimbursement of a loss. If a claim is not filed, no deduction can be taken. However, this rule does not apply to the portion of the loss not covered by insurance (for example, a deductible).

Gain from reimbursement. If reimbursement is more than the basis in the property, there is a gain, even if the decrease in the FMV of the property is more than the basis.

Postpone reporting gain. T/P must buy a replacement property within the replacement period. The replacement period begins on the date of casualty/theft and ends 2 years after the tax year in which gain is realized. The replacement property must be related in service or use to the property on which the gain is to be postponed.

Property used partly for business and partly for personal purposes. When property is used partly for personal purposes and partly for business or income-producing purposes, the casualty or theft loss deduction must be figured separately because the losses attributed to these two uses are figured in two different ways. When figuring each loss, allocate the total cost or basis, the FMV before and after the casualty or theft loss, and the insurance or other reimbursement between the business and personal use of the property. The \$100 rule and the 10% rule apply only to the casualty or theft loss on the personal-use portion of the property.

Deductions from AGI

Itemized Deductions

Casualty & Theft Losses - Nonbusiness

Limits on casualty & theft losses. Casualty and theft losses must be reduced by the following:

1. \$100 (\$500 for qualified disaster) for each casualty or theft loss, and
2. 10% of AGI for the total of all casualty or theft losses.

Figuring the amount of loss:

1. The smaller of:
 - a) The decrease in fair market value after the casualty/theft (FMV before minus FMV after casualty/theft), or
 - b) Adjusted basis in the property before the casualty or theft.
2. Subtract any insurance or other reimbursement received or expected to be received.
3. Reduce each casualty/theft loss by \$100 (\$500 for qualified disaster).
4. Reduce total casualty/theft losses by 10% of AGI.

Disaster Area Loss. If a T/P has a casualty loss in a federally declared disaster area, he or she can choose to deduct the loss on his or her return for either the year the disaster occurred or the year immediately preceding the year the disaster occurred.

How to report gains and losses. Use Form 4684, Casualty and Thefts, to report a gain or loss from a casualty or theft. Report a gain on Schedule D (Form 1040 or 1040-SR). Report a loss on Schedule A (Form 1040 or 1040-SR).

Deductions from AGI

Itemized Deductions

Other Itemized Deductions

No deduction for miscellaneous itemized deductions subject to 2% AGI. Unless the taxpayer falls into one of the qualified categories of employment under unreimbursed employee expenses, miscellaneous itemized deductions that are subject to the 2% of adjusted gross income limitation can no longer be claimed.

Unreimbursed employee expenses. Unreimbursed employee expenses are no longer deductible unless they fall into one of the following categories of employment.

- ▶ Armed Forces reservists. Members of a reserve component of the Armed Forces of the U.S. (Army, Navy, Marine Corps, Air Force, Coast Guard Reserve, Army National Guard or the Reserve Corps of the Public Health Service).
- ▶ Qualified performing artists. Must met the following qualifications:
 1. Performed services in the performing arts as an employee for at least two employers during the tax year,
 2. Received from at least two of the employers' wages of \$200 or more per employer,
 3. Had allowable business expenses attributable to the performing arts of more than 10% of gross income from the performing arts, and
 4. Had AGI of \$16,000 or less before deducting expenses as a performing artist.
- ▶ Fee-basis state or local government officials.
- ▶ Employees with impairment-related work expenses.

Deductions from AGI

Itemized Deductions

Nondeductible Itemize Deductions

- ▶ Appraisal Fees.
- ▶ Education that is work related.
- ▶ Legal fees related to job.
- ▶ Personal legal expenses.
- ▶ Voluntary unemployment benefit fund contributions.
- ▶ Licenses and regulatory fees.
- ▶ Malpractice insurance premiums.
- ▶ Occupational taxes.
- ▶ Passport for a business trip.
- ▶ Tax preparation fees.
- ▶ Legal expenses related to producing or collecting income.
- ▶ Excess Deductions of an Estate.
- ▶ Investment Fees and Expenses.
- ▶ Hobby Expenses.
- ▶ Adoption expenses (can take a credit).
- ▶ Depreciation on computers even if:
 - For the convenience of employer, and
 - Required as a condition of employment.
- ▶ Safe Deposit Box Rent.
- ▶ Trustee's Administrative Fees for IRA
- ▶ Job search expenses.
- ▶ Union dues and expenses.
- ▶ Club Dues.
- ▶ Commuting Expenses.
- ▶ Home office for an employee.
- ▶ Clerical Help and Office Rent
- ▶ Fines and Penalties.
- ▶ Investment-Related Seminars.
- ▶ Professional Accreditation Fees.
- ▶ Lobbying Expenses.
- ▶ Personal disability insurance premiums.
- ▶ Burial or funeral expenses.

Deductions from AGI Itemized Deductions

Deductible itemize deductions:

- ▶ Amortizable premium on taxable bonds.
- ▶ Casualty and theft losses from income-producing property.
- ▶ Excess deductions of an estate or trust.
- ▶ Federal estate tax on income in respect to a decedent.
- ▶ Gambling losses up to the amount of gambling winnings.
- ▶ Impairment-related work expenses of persons with disabilities.
- ▶ Losses from Ponzi-type investment schemes.
- ▶ Repayments of more than \$3,000 under a claim of right.
- ▶ Unlawful discrimination claims.
- ▶ Unrecovered investment in an annuity.

Deductions from AGI

Itemized Deductions

Itemized Deductions (cont.)

Gambling losses up to the amount of gambling winnings. A T/P cannot reduce gambling winnings by gambling losses and report the difference. The T/P must report the full amount of winnings as other income on Schedule 1 (form 1040 or 1040-SR) line 8b and claim gambling losses (up to the amount of winnings) as an itemized deduction (Schedule A).

Diary of winnings and losses. T/P must keep an accurate diary or similar record of losses and winnings. The diary should contain at least the following information:

- ▶ The date and type of specific wager or wagering activity.
- ▶ The name and address or location of the gambling establishment.
- ▶ The names of other persons present with T/P at the gambling establishment.
- ▶ The amount(s) won or lost.

Proof of winnings and losses. In addition to a diary, T/P should also have other documentation to prove winnings and losses through Form W-2G, Certain Gambling Winnings, Form 5754, Statement by Person(s) Receiving Gambling Winnings, wagering tickets, canceled checks, substitute checks, credit records, bank withdrawals, and statements of actual winnings or payment slips provided by the gambling establishment.

Credits

Earned Income Credit

Qualifications for the Credit

Rules for everyone. All taxpayers must meet the following seven rules to qualify for the earned income credit:

1. T/P's AGI must be less than:
 - ▶ \$16,480 (\$22,610 if married filing jointly) if taxpayer does not have a qualifying child.
 - ▶ \$43,492 (\$49,622 if married filing jointly) if taxpayer has one qualifying child.
 - ▶ \$49,399 (\$55,529 if married filing jointly) if taxpayer has two qualifying children.
 - ▶ \$53,057 (\$59,187 if married filing jointly) if taxpayer has three or more qualifying children.
2. Have a valid social security number by the due date of the return (including extensions).
3. Must meet certain requirements if separated from spouse and not filing a joint return.
4. Must be a U.S. citizen or resident alien for the entire year.
5. Cannot claim the earned income credit if filing Form 2555, Foreign Earned Income.
6. Investment income must be \$10,300 or less.
7. Must have earned income.

Credits

Earned Income Credit

Qualifications for the Credit

Investment income. Investment income is the total of the following amounts:

- ▶ Taxable interest
- ▶ Tax-exempt interest
- ▶ Dividend income
- ▶ Capital gain net income
- ▶ Net royalty income
- ▶ Net rental income of personal property
- ▶ Net income from passive activities

Credits

Earned Income Credit

Earned income. Earned income when figuring the earned income credit includes the following:

1. Wages, salaries, and tips.
2. Net earnings from self-employment.
3. Gross income received as a statutory employee.
4. Strike benefits paid by a union that are taxable.
5. Nontaxable combat pay if T/P elects to include in earned income.
6. Long-term disability benefits. Disability benefits received from an employer's disability retirement plan are considered earned income until the T/P reaches minimum retirement age.

Income that is not earned income. The following are **not** earned income:

1. Interest and dividends.
2. Pension and annuities.
3. Social security and railroad retirement benefits.
4. Alimony and child support.
5. Workfare benefits.
6. Worker's compensation and unemployment compensation.
7. Employee compensation that is nontaxable and earnings while an inmate.
8. Nontaxable combat pay.

Credits

Earned Income Credit

Qualifications for the Credit (cont.)

Rules if T/P has a qualifying child. Additional rules if the taxpayer has a qualifying child:

1. Child must meet the relationship, age, residency, and joint return test.
2. Qualifying child cannot be used by more than one person to claim the EIC.
3. Taxpayer cannot be a qualifying child of another person.

Rules if T/P has no qualifying child. Additional rules for taxpayers with no qualifying child:

1. Must be at least age 25 but under age 65 (if MFJ only one spouse must meet age rule).
2. Taxpayer cannot be the dependent of another person.
3. Taxpayer cannot be a qualifying child of another person.
4. Must have lived in the U.S. for more than half of the year (does not include Puerto Rico or U.S. possessions such as Guam).

Credits

Earned Income Credit

Qualifying Child

A qualifying child must meet the following four tests:

1. Relationship test.
2. Residency test.
3. Age test.
4. Joint Return test.

Relationship test. Child must be T/P's:

- ▶ Child, adopted child, stepchild, eligible foster child, or a descendant of any of them, or
- ▶ Sibling, half sibling, step sibling, or a descendant of any of them.

Residency test. Child must live with T/P for more than half the year and the home must be in the U.S. **not** including Puerto Rico or U.S. possessions such as Guam. Exception: Military personnel.

Age test. Qualifying child must be one of the following:

1. Under age 19 at the end of year and younger than T/P (or spouse, if filing jointly).
2. Under age 24 at year end, a full-time student, and younger than T/P (or spouse, if filing jointly).
3. Permanently or totally disabled at any time during the year, regardless of age.

Joint return test. The qualifying child cannot file a joint return for the year. **Exception:** A joint return is filed only as a claim for refund.

Note: T/P must provide a correct and valid social security number for each qualifying child.

Credits

Earned Income Credit

Receiving the credit. To get the credit, a T/P must file a tax return even if he or she did not owe any tax or did not earn enough money to file a return.

EIC questioned by IRS. The IRS may ask the T/P to provide documents to prove the T/P is entitled to claim the EIC. These may include birth certificates, school records, medical records, etc.

If improper claim made in prior year. If T/P's EIC for any year after 1996 was denied or reduced for any reason other than a math or clerical error, T/P must attach a completed Form 8862 to his or her next tax return to claim the EIC. If T/P's EIC for any year after 1996 was denied and it was determined that the error was due to reckless or intentional disregard of the EIC rules, then T/P cannot claim the EIC for the next 2 years. If error was due to fraud, then T/P cannot claim the EIC for the next 10 years.

Schedule EIC. Complete and attach to Form 1040 or 1040-SR only if the T/P has a qualifying child.

Credits

Child and Dependent Care Credit

Tests to claim the credit. To claim the credit for child and dependent care expenses, a T/P must file Form 1040 or 1040-SR and meet all of the following tests:

1. **Qualifying person test.** The care must be for one or more qualifying persons.
2. **Earned income test.** Must have earned income during the year.
3. **Work-related expense test.** Must pay child and dependent care expenses in order to work or look for work.
4. **Cannot make payments for child and dependent care to a spouse or someone who can be claimed as a dependent.** If payment is to the taxpayer's child, the child cannot be a dependent and must be age 19 or older by the end of the year.
5. **Can be any filing status except married filing separate.** Must file a joint return if married.
6. **Provider identification test.** Must identify the care provider on the tax return.
7. If excluding dependent care assistance benefits provided by employer (up to \$5,000), the exclusion must be less than the dollar limit for qualifying expenses (\$3,000 if one qualifying person, \$6,000 if two or more qualifying persons).

Credits

Child and Dependent Care Credit

Qualifying person test. A qualified person is one of the following:

1. A qualifying child who is the T/P's dependent under age 13 when the care was provided.
2. A spouse who was not physically or mentally able to care for himself or herself and lived with the T/P for more than half the year.
3. A person who was not physically or mentally able to care for himself or herself, lived with the T/P for more than half the year, and either:
 - a. Was a dependent, or
 - b. Would have been a dependent except that the dependent received gross income of \$4,400 or more, had filed a joint return, or T/P (or T/P's spouse if filing jointly) could be claimed as a dependent on someone else's return.

Earned income test. Earned income includes wages, salaries, tips, other taxable employee compensation, and net earnings from self-employment. A net loss from self-employment reduces earned income. Earned income also includes strike benefits and any disability pay reported as wages. Generally, only taxable compensation is included. However, a T/P can elect to include nontaxable combat pay in earned income.

Credits

Child and Dependent Care Credit

Work-related expenses test. Child and dependent care expenses must be work-related. Expenses are work-related if they:

- ▶ Allow the taxpayer to work or look for work, and
- ▶ Are for a qualifying person's care.

Volunteer work. A taxpayer is not considered to be working if doing unpaid volunteer work or volunteer work for a nominal salary.

Work for part of year. If a taxpayer works or actively looking for work during only part of the period covered by the expenses, then figure expenses for each day. For example, if a taxpayer works or looking for work for only 2 months and 15 days during the year and pays expenses of \$250 a month, his or her work-related expenses are limited to \$625 ($2\frac{1}{2}$ months \times \$250).

Expenses prepaid in an earlier year. Count expenses paid for services before they are provided only in the year the care is received. Claim the expenses for the later year as if they were actually paid in that later year.

Expenses not paid until the following year. Don't count 2021 expenses paid in 2022 as work-related expenses for 2022. A taxpayer may be able to claim an additional credit for them on in 2022, but they must be figured separately.

Credits

Child and Dependent Care Credit

Examples of Expenses for Care of a Qualified Person:

- ▶ **Household services** (e.g., cleaning service, maid, cook, and housekeeper's wages) if they are at least partly responsible for the well-being and protection of a qualifying person.
- ▶ **Dependent care centers**, if the center complies with all state and local regulations.
- ▶ **Education**. Expenses for a child in nursery school, preschool, or similar programs for children below the level of kindergarten are expenses for care. Expenses to attend kindergarten or a higher grade are not expenses for care.
- ▶ **Transportation**. Count transportation costs if by care provider. Transportation costs incurred by T/P of getting a qualified person from home to the care location and back are not considered work-related expenses.

Expenses not for care. Expenses for care don't include amounts paid for food, lodging, clothing, education, and entertainment. However, include small amounts paid for these items if they are incidental to and can't be separated from the cost of caring for the qualifying person.

Provider identification test. To identify the care provider, T/P must give the provider's:

1. Name.
2. Address.
3. Taxpayer identification number.

Due diligence. If the care provider information the T/P gives is incorrect or incomplete, the credit may not be allowed. However, if the T/P can show that he or she used due diligence in trying to supply the information, the T/P can still claim the credit.

Credits

Child and Dependent Care Credit

Dependent Care Benefits

Exclusion or deduction. If a T/P's employer provides dependent care benefits under a qualified plan, the T/P may be able to exclude these benefits from income. To claim the exclusion, the T/P must complete Part III of Form 2441. If T/P is self-employed and receives benefits from a qualified dependent care benefit plan, the T/P is treated as both employer and employee. Therefore, T/P would not get an exclusion from wages. Instead, the taxpayer would get a deduction on Form 1040 or 1040-SR, Schedule C, line 14; Schedule E, line 19 or 28; or Schedule F, line 15. To claim the deduction, the T/P must use Form 2441. The amount that can be excluded or deducted is limited to the smallest of:

1. The total amount of dependent care benefits received during the year,
2. The total amount of qualified expenses incurred during the year,
3. The T/P's earned income,
4. The spouse's earned income, or
5. \$5,000 (\$2,500 if married filing separately).

Reduced dollar limit. If a T/P received dependent care benefits that were excluded or deducted from income, the T/P must subtract that amount from the dollar limit (\$3,000 for one qualifying person, or \$6,000 for two or more qualifying persons) that applies to the T/P.

Credits

Child and Dependent Care Credit

How to Figure the Credit

The credit is a percentage of work-related expenses. First figure the earned income limit and the dollar limit on those expenses. Then figure the applicable percentage for the credit.

Earned income limit. The amount of work-related expenses cannot be more than:

1. Earned income for the year, if single, or
2. The smaller of each spouse's earned income, if married.

Student-spouse or spouse not able to care for self. A spouse who is either a full-time student or not able to care for himself or herself is treated as having earned income. His or her earned income for each month is considered to be at least \$250 if there is one qualifying person in the home, or at least \$500 if there are two or more.

Community property laws. Disregard community property laws when figuring earned income for this credit.

Credits

Child and Dependent Care Credit

How to Figure the Credit (cont.)

Dollar limit:

1. \$3,000 for one qualifying person.
2. \$6,000 for two or more qualifying persons.

Amount of Credit:

$$\text{Credit} = \text{Work-related expenses limit} \times \text{Applicable percentage}$$

T/P's AGI	Applicable Percentage	T/P's AGI	Applicable Percentage
\$0 - \$15,000	35%	\$29,001 - \$31,000	27%
\$15,001 - \$17,000	34%	\$31,001 - \$33,000	26%
\$17,001 - \$19,000	33%	\$33,001 - \$35,000	25%
\$19,001 - \$21,000	32%	\$35,001 - \$37,000	24%
\$21,001 - \$23,000	31%	\$37,001 - \$39,000	23%
\$23,001 - \$25,000	30%	\$39,001 - \$41,000	22%
\$25,001 - \$27,000	29%	\$41,001 - \$43,000	21%
\$27,001 - \$29,000	28%	\$43,001 - No Limit	20%

Note: Applicable % starts at 35% if AGI is \$15,000 and decreases 1% for every \$2,000 increase in AGI up to \$43,001

Credits

Child Tax Credits (CTC)

Qualifying child. A qualifying child must meet **all** of the following:

1. Be the T/P's son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, or a descendant of any of them (e.g., grandchild, niece or nephew).
2. Was under age 17 at the end of the year.
3. Did not provide over half of his or her own support for the year.
4. Lived with the T/P for more than half the year. **Exception:** The noncustodial parent can claim the child tax credit for a child if the custodial parent released a claim for the child as a dependent on Schedule 8332, and the noncustodial parent attached the release to his or her return.
5. Is claimed as a dependent on the T/P's return.
6. Does not file a joint return for the year (or files it only as a claim for refund).
7. Was a U.S. citizen, a U.S. national, or U.S. resident alien.

Exceptions to time lived with T/P. A child is considered to have lived with the T/P for more than half of year if the child was born or died during the year and the T/P's home was this child's home for more than half the time he or she was alive. Temporary absences by the T/P or the child for special circumstances, such as for school, vacation, business, medical care, military service, or detention in a juvenile facility, count as time the child lived with the T/P.

Credits

Child Tax Credits (CTC)

Amount of credit. The maximum credit claimed is \$2,000 for each qualifying child. The tax credit will be refundable only up to \$1,500, depending on T/P's income, and the T/P must have earned income of at least \$2,500 to even be eligible for the refund.

Additional child tax credit (ACTC). This credit is for certain individuals who get less than the full amount of the CTC. The additional child tax credit is a refundable tax credit. This credit may give the T/P a refund even if the T/P does not owe any tax. The additional child tax credit is figured on Schedule 8812 and carried to Form 1040 or 1040-SR. The maximum amount of the additional child tax credit is \$1,500 per qualifying child.

Social security number (SSN) required for child tax credit. A child must have an SSN issued before the due date of the 2022 return (including extensions) to be claimed as a qualifying child for the child tax credit or additional child tax credit. If the dependent child has an ITIN, but not an SSN, issued before the due date of the 2022 return (including extensions), the T/P may be able to claim the new Credit for Other Dependents for that child (see next card).

Credits

Credit for Other Dependents (ODC)

Qualifying person for the ODC. A person qualifies a T/P for the ODC if the person meets all of the following conditions.

1. The person is claimed as a dependent on the T/P's return.
2. The person cannot be used by the T/P to claim the child tax credit or the additional child tax credit.
3. The person is a U.S. citizen, U.S. national, or U.S. resident alien.

Amount of credit. The maximum credit claimed is \$500 for each eligible dependent.

Limits on the CTC and ODC credit. The credit amount may be reduced if modified adjusted gross income is more than the amounts shown for each filing status.

- ▶ Married filing jointly - \$400,000
- ▶ All other filing statuses - \$200,000

Note: A T/P cannot take the child tax credit and the credit for other dependents for the same person. A T/P cannot take the credit for other dependents credit if he or she claims a foreign earned income or housing exclusion on Form 2555.

Credits

Education Credits

American Opportunity Credit

A T/P can claim an American opportunity credit of up to \$2,500 for qualified tuition and related expenses paid for himself, his spouse and any dependent required for enrollment or attendance at any accredited college, university vocational school, or other accredited postsecondary educational institution. This credit can be claimed for the first four years of postsecondary education for each eligible student.

Eligible student. An eligible student must meet the following requirements:

1. Did not have expenses that were used to figure an American opportunity credit or Hope credit in at least 4 prior years.
2. Has not completed the first 4 years of postsecondary education.
3. For at least one academic period beginning in the year, the student was enrolled at least half-time in a program leading to a degree, certificate, or other recognized educational credential.
4. Is free of any felony conviction for possessing or distributing a controlled substance.

Amount of the credit. The amount of the credit is 100% of the first \$2,000 plus 25% of the next \$2,000 paid for each eligible student's qualified tuition and related expenses. The maximum credit that can be claimed is \$2,500 times the number of eligible students.

Income phaseout. The American opportunity credit is phased out (gradually reduced) if the T/P's modified AGI is between \$80,000 and \$90,000 (\$160,000 and \$180,000 if MFJ).

Credits

Education Credits

American Opportunity Credit (cont.)

Qualified education expenses. Qualified expenses are tuition and certain related expenses required for enrollment at an eligible educational institution. Student-activity fees are included in qualified education expenses only if the fees must be paid to the institution as a condition of enrollment or attendance. However, expenses for books, supplies, and equipment needed for a course of study are included in qualified education expenses whether or not the materials are purchased from the educational institution. Qualified education expenses paid in 2022 for an academic period that begins in the first 3 months of 2023 can be used in figuring an education credit for 2022 only. Reduce the qualified educational expenses for each academic period by the amount of tax-free educational assistance allocable to that academic period.

Refundable part of credit. 40% of the American opportunity credit is refundable for taxpayers. A T/P does not qualify for the refundable part of the credit all if the following apply:

1. T/P was:
 - a) Under age 18 at year end, or
 - b) Age 18 at year end and earned income was less than half of total support, or
 - c) A full-time student over age 18 and under age 24 at year end and earned income was less than half of total support.
2. At least one of the T/P's parents was alive at year end.
3. T/P is not filing a joint return for the year.

Credits

Education Credits

Lifetime Learning Credit

A T/P can claim a lifetime learning credit of up to \$2,000 for qualified tuition and related expenses paid for himself, his spouse and any dependent required for enrollment or attendance at any accredited college, university vocational school, or other accredited postsecondary educational institution. Unlike the American opportunity credit:

1. The lifetime learning credit is not based on the student's work load. It is allowed for one or more courses.
2. The lifetime learning credit is not limited to students in the first four years of postsecondary education.
3. Expenses for graduate-level degree work are eligible.
4. There is no limit on the number of years for which the lifetime learning credit can be claimed for each student.
5. Expenses for course-related books, supplies, and equipment are qualified education expenses only if paid to the institution as a condition of enrollment or attendance.

Amount of credit. The amount of the credit is 20% of the first \$10,000 paid for qualified tuition and related expenses for all students in the family.

Income phaseout. The lifetime learning credit is phased out (gradually reduced) if the T/P's modified AGI is between \$80,000 and \$90,000 (\$160,000 and \$180,000 if married filing jointly).

Credits

Education Credits

Who can claim an educational credit? In any one year, only one person can claim a higher education credit for a student's expenses. If a T/P is paying higher education costs for a dependent child, either the T/P or the child, but not both, can claim a credit for a particular year. If the T/P claims the child as a dependent, only the T/P can take the credit. If the T/P claims the child as a dependent, any expenses paid by the child are treated as paid for by the T/P when figuring the amount of the American opportunity or lifetime learning credit.

Choosing which credit to claim. For each student, a T/P can elect for any tax year only one of the higher education credits or a tax-free withdrawal from an education IRA. If a T/P pays qualifying expenses for more than one student, the T/P can choose to take credits on a per-student, per-year basis. This means that a T/P can claim the American opportunity credit for one student and the lifetime learning credit for another student in the same tax year.

Form 1098-T requirement. To be eligible to claim the American opportunity credit or the lifetime learning credit, the law requires a T/P (or a dependent) to have received a Form 1098-T from an eligible educational institution. However, a T/P may claim one of these education benefits if the student does not receive a Form 1098-T because the student's educational institution isn't required to send a Form 1098-T to the student under existing rules. If a student's educational institution is not required to provide a Form 1098-T to the student, a T/P may claim one of these education benefits without a Form 1098-T if the T/P otherwise qualifies.

Credits

Comparison of Education Credits

	American Opportunity Credit	Lifetime Learning Credit
Maximum credit	Up to \$2,500 credit per eligible student .	Up to \$2,000 credit per return .
Limit on modified adjusted gross income (MAGI)	\$180,000 if married filing jointly; \$90,000 if single, head of household, or qualifying surviving spouse.	\$180,000 if married filing jointly; \$90,000 if single, head of household, or qualifying surviving spouse.
Refundable or nonrefundable	40% of credit may be refundable.	Credit limited to the amount of tax owed.
Number of years of postsecondary education	Available ONLY for the first 4 years of postsecondary education.	Available for all years of postsecondary education and for courses to acquire or improve job skills.
Number of tax years credit available	Available ONLY for 4 tax years per eligible student.	Available for an unlimited number of years.
Type of degree required	Student must be pursuing an undergraduate degree or other recognized education credential.	Student does not need to be pursuing a degree or other recognized education credential.
Number of courses	Student must be enrolled at least half time for at least one academic period beginning during the tax year.	Available for one or more courses.
Felony drug conviction	No felony drug convictions on student's records.	Felony drug convictions are permitted.
Qualified expenses	Tuition and required enrollment fees. Course-related books, supplies, and equipment do not need to be purchased from the institution in order to qualify.	Tuition and required enrollment fees, including amounts required to be paid to the institution for course-related books, supplies, and equipment.
Payments for academic periods	Payments made in 2022 for academic periods in 2022 and the first 3 months of 2023.	

Credits

Credit for the Elderly or the Disabled

Qualifying Individual. Must be a U.S. citizen or resident and:

1. Age 65 or older by the end of the tax year, or
2. Under age 65 at the end of the year and all three of the following statements are true:
 - a) Retired on permanent and total disability,
 - b) Did not reach mandatory retirement age during the tax year, and
 - c) Received taxable disability benefits during the tax year.

Permanent and total disability. T/P cannot engage in any substantial gainful activity because of a physical or mental condition. A physician must certify that the condition has lasted or can be expected to last continuously for 12 months or more, or that the condition can be expected to result in death.

Substantial gainful activity. The performance of significant duties over a reasonable period of time while working for pay or profit.

Married persons. If married at the end of the year, T/P must file a joint return to receive the credit. If T/P and spouse did not live together at any time during the year, T/P can file either jointly or separately and still get the credit. Only one spouse needs to be over 65 to qualify for the credit.

Credits

Credit for the Elderly or the Disabled

Figuring the Credit:

1. Base amount, less
2. The total of:
 - a) Social Security and other nontaxable pensions
 - b) Excess AGI ((AGI minus AGI limit amount) divided by 2)
3. Multiply by 15%

Base Amount:

- \$ 5,000 Filing Status: S, H/H, or QSS
- \$ 5,000 Filing Status: MFJ and one spouse qualifies for the credit
- \$ 7,500 Filing Status: MFJ and both spouses qualify for the credit
- \$ 3,750 Filing Status: MFS and did not live with spouse during the year

AGI Limit Amount:

- \$ 7,500 Filing Status: S, H/H, or QSS
- \$10,000 filing status: MFJ
- \$ 5,000 filing status: MFS and did not live with spouse during the year

Credits

Premium Tax Credit

Premium tax credit (PTC). The PTC is a tax credit for T/Ps who enroll, or whose family member enrolls, in a qualified health plan offered through a Marketplace. The credit provides financial assistance to pay the premiums by reducing the amount of tax owe.

Advance payments of the premium tax credit (APTC). APTC is a payment made to the T/P's insurance provider for coverage during the year that pays for part or all of the premiums for the coverage of the T/P, spouse and dependents. The APTC eligibility is based on the Marketplace's estimate of the PTC the T/P will be able to take on his or her tax return. If advance payments of the premium tax credit were made, the T/P must file a tax return and Form 8962, Premium Tax Credit.

Tax family. For purposes of the PTC, a tax family consists of the T/P, a spouse if filing a joint return, and dependents).

Form 1095-A. A T/P will need Form 1095-A, Health Insurance Marketplace Statement, to complete Form 8962. The Marketplace is required to provide or send Form 1095-A to the T/P.

Form 1095-C, Employer-Provided Health Insurance Offer and Coverage. Part II of the Form 1095-C indicates whether the employer offered health insurance coverage and, if so, includes information about the offer. If a T/P purchased health insurance coverage through a Marketplace and wish to take the PTC, this information may assist the T/P in determining whether he or she is eligible for the PTC.

Credits

Premium Tax Credit

Who can take the PTC? A T/P can take the PTC if he or she meets all the conditions:

1. For at least one month of the year, all of the following were true:
 - a) An individual in the tax family was enrolled in a qualified health plan offered through the Marketplace.
 - b) The individual was not eligible for minimum essential coverage, other than coverage in the individual market.
 - c) The portion of the enrollment premiums was paid by the due date of the tax return (not including extensions).
2. No one can claim the T/P as a dependent on their tax return for the year
3. The individual is an applicable T/P. To be an applicable T/P, the individual must meet all of the following requirements.
 - a) The taxpayer, or his or her spouse if filing a joint return, received or were approved to receive unemployment compensation for any week beginning during 2022, or your household income for 2022 is at least 100% of the federal poverty line for the family size.
 - b) If married at the end of the year, generally the T/P must file a joint return. However, filing a separate return from spouse will not disqualify T/P from being an applicable T/P if certain requirements are met.

Credits

Foreign Tax Credit

Deducting foreign tax paid. A T/P can choose to deduct foreign taxes paid on his or her Schedule A (Form 1040 or 1040-SR) or take a foreign tax credit. A T/P cannot take a credit or deduction for foreign taxes paid on income that the T/P excluded from U.S. tax under any of the following:

1. Foreign earned income exclusion.
2. Foreign housing exclusion.
3. Income from Puerto Rico exempt from U.S. tax.
4. Possession exclusion.

How to claim the credit. The foreign tax credit is claimed on Form 1116 (Form 1040 or 1040-SR).

Election not to file Form 1116. A T/P can elect to claim the foreign tax credit without using Form 1116 if all of the following requirements are met:

1. All foreign source gross income was passive category income (which includes most interest and dividends).
2. The foreign tax paid on it were reported on Form 1099-INT, Form 1099-DIV, or Schedule K-1 (Form 1041), Schedule K-3 (Form 1065 or Form 1120-S), or similar substitute statements.
3. The foreign taxes for the tax year are not more than \$300 (\$600 if filing a joint return).

Note: This election is not available to estates or trusts.

Credits

Adoption Credit

Amount of credit. Up to \$14,890 for qualified expenses paid to adopt an eligible child.

Qualified adoption expenses. Qualified adoption expenses are expenses directly related to, and whose principal purpose is for, the legal adoption of an eligible child. These expenses include:

1. Adoption fees.
2. Court costs.
3. Attorney fees.
4. Travel expenses (including amounts spent for meals and lodging) while away from home.
5. Re-adoption expenses to adopt a foreign child.

Nonqualified expenses. Qualified adoption expenses do not include the following expenses:

1. That violate state or federal laws.
2. For carrying out any surrogate parenting arrangement.
3. For the adoption of a spouse's child.
4. Which T/P received funds under any federal, state, or local program.
5. Allowed as a credit or deduction under any other federal income tax rule.
6. Paid or reimbursed by an employer or any other person or organization.

Eligible child. An eligible child is any individual under age 18 or an individual incapable of physically or mentally caring for himself or herself.

Income phaseout. The adoption credit is phased out if T/P's AGI is between \$223,410 and \$263,410.

Retirement Savings Contributions Credit

Who can take this credit? If a T/P makes eligible contributions to a qualified retirement plan, an eligible deferred compensation plan, or an IRA, the T/P can claim the credit if all of the following apply:

1. T/P is age 18 or older.
2. T/P was not a full-time student.
3. No one else can claim the T/P as a dependent.
4. T/P's AGI is not more than:
 - a) \$68,000 if filing status is married filing jointly.
 - b) \$51,000 if filing status is head of household.
 - c) \$34,000 if filing status is single, married filing separately, or qualifying surviving spouse.

Credit amount. A taxpayer can take a nonrefundable tax credit of up to \$1,000 (\$2,000 if married filing jointly) for making eligible contributions to an employer-sponsored retirement plan or to an individual retirement arrangement (IRA).

How to figure and report the credit. The amount of the credit is based on the contributions made and the credit rate. The credit rate can be as low as 10% or as high as 50%. The credit rate depends on the T/P's income and filing status. Figure the credit on Form 8880. Report the credit on Schedule 3 (Form 1040 or 1040-SR), line 4 and attach Form 8880 to the return.

Credits

Retirement Savings Contributions Credit

Eligible contributions. These include:

1. Contributions to a traditional or Roth IRA,
2. Salary reduction contributions (elective deferrals, including amounts designated as after-tax Roth contributions) to the following:
 - a) A 401(k) plan (including a SIMPLE 401(k)).
 - b) A section 403(b) annuity.
 - c) An eligible deferred compensation plan of a state or local government (a governmental 457 plan).
 - d) A SIMPLE IRA plan.
 - e) A salary reduction SEP.
3. Contributions to a section 501(c)(18) plan.

Contributions reduced. Eligible contributions must be reduced by the total taxable and nontaxable distributions received in the two years before the year the credit is claimed, the year the credit is claimed, and the period after the end of the credit year but before the due date (including extensions) for filing the return for the credit year.

Maximum eligible contributions. After the contributions are reduced, the maximum annual contribution on which the credit can be based is \$2,000 per person.

Credits

Credit for Prior Year Minimum Tax

Tax laws give special treatment to some kinds of income and allow special deductions and credits for some kinds of expenses. A T/P who benefits from these laws has to pay at least a minimum amount of tax through an additional tax known as the alternative minimum tax. The special treatment of some items of income and expenses only allows a T/P to postpone paying tax until a later year. If in prior years a T/P pays alternative minimum tax because of these tax postponement items, the T/P may be able to take a credit for prior year minimum tax against his or her current year's regular tax. A T/P may be able to take a credit against regular tax if for 2021 the T/P had:

- ▶ An alternative minimum tax liability and adjustments or preferences other than exclusion items,
- ▶ A minimum tax credit that the T/P is carrying forward to 2022, or
- ▶ An unallowed qualified electric vehicle credit.

Exclusion items. The exclusion items are the following adjustments and preference items:

1. The standard deduction.
2. Itemized deductions (including any investment interest expense reported on Schedule E).
3. Tax-exempt interest from certain activity bonds.
4. Depletion.
5. The section 1202 exclusion.

Carryover the credit. Any unused credit for prior year minimum tax can be carried over to later years until it is completely used.

Taxes

Alternative Minimum Tax

Subject to Alternative Minimum Tax (AMT). The tax law gives special treatment to some kinds of income and allows special deductions and credits for some kinds of expenses. Taxpayers who benefit from this special treatment may have to pay at least a minimum amount of tax through an additional tax called AMT. The AMT is the excess of the tentative minimum tax over the regular tax.

The tentative minimum tax is figured separately from the regular tax. In general, the tentative minimum tax is computed by:

1. Starting with taxable income for regular tax purposes.
2. Eliminating or reducing certain exclusions, deductions, and credits (generally, business-related credits) that are allowed in computing the regular tax.
3. Subtracting the AMT exemption amount.
4. Multiplying the amount computed in (3) by the AMT rate.
5. Subtracting AMT foreign tax credit.

The AMT exemption amount and AMT rate are set by law. For capital gains and certain dividends, the rates in effect for the regular tax are used.

See next card

Taxes

Alternative Minimum Tax

Figuring the Alternative Minimum Tax

Begin with		Taxable Income
Add or subtract	+/-	Adjustments
Add	+	Tax preferences
Equals	=	Alternative minimum taxable income
Subtract	-	Exemption amount
Multiply	x	26%*
Subtract	-	Foreign tax credit
Equals	=	Tentative minimum tax
Subtract	-	Regular tax
Equals	=	Alternative minimum tax

*26% for AMTI up to \$206,100 (\$103,050 for MFS), 28% for AMTI over \$206,100 (103,050 for MFS)

Taxes

Alternative Minimum Tax

Adjustments to taxable income. The following are adjustments to taxable income in computing alternative minimum tax:

1. Add standard deduction (if claimed).
2. Add itemized deductions claimed for state and local taxes, certain interest, most miscellaneous deductions, and part of medical expenses.
3. Subtract refund of state and local taxes included in gross income.
4. Add accelerated depreciation that is more than straight line.
5. Difference between gain or loss on the sale of property reported for regular tax purposes and AMT purposes.
6. For stock acquired and not sold during the year through the exercise of an incentive stock option, add the amount of any fair market value of the stock that is more than the amount that was paid for it.
7. Change in certain passive activity losses.
8. Add certain depletion that is more than the adjusted basis of the property.
9. Add part of the deduction for certain intangible drilling costs.
10. Add tax-exempt interest on certain private activity bonds.
11. Add 7% of qualified small stock (section 1202) gain if purchase stock before 9/28/10.

Taxes

Alternative Minimum Tax

Tax preference items. Tax preference items are income items and deductions that receive special treatment under tax laws. They must be added back to taxable income. Tax preference items include the following:

1. Excess accelerated depreciation over straight-line for real property placed in service before 1987.
2. Tax-exempt interest on certain private activity bonds.
3. Excess of depletion deduction over adjusted basis in property.
4. Part of any deduction for intangible drilling costs.
5. 7% of gain on the sale of small business stock (section 1202 exclusion) if purchases before 9/28/10.

Taxes

Alternative Minimum Tax

Exemption amounts:

IF filing status is...	AND alternative minimum taxable income is not over...	THEN exemption amount is...
Single or head of household	\$539,900	\$75,900
Married filing jointly or qualifying surviving spouse	\$1,079,800	\$118,100
Married filing separately	\$539,900	\$59,050

Note: The AMT exemption is reduced by 25% of the amount by which alternative minimum taxable income (AMTI) exceeds \$539,900 for single or head of household, \$1,079,800 for married filing jointly or qualifying surviving spouse and \$539,900 for married filing separately.

AMT tax rates. The first \$206,100 of alternative minimum taxable income (AMTI) (\$103,050 if married filing separately) in excess of the exemption amount is taxed at a rate of 26%. AMTI in excess of the first \$206,100 (\$103,050 if married filing separately) above the exemption amount is taxed at a rate of 28%.

Social security and Medicare taxes. If a T/P who pays cash wages of \$2,400 or more in 2022 to any one unrelated household employee, the cash wages paid (regardless of when the wages were earned) are subject to social security and Medicare taxes.

Federal unemployment tax (FUTA) . If a T/P pays cash wages to household employees totaling \$1,000 or more in any calendar quarter of 2022, the T/P must pay federal unemployment tax on the first \$7,000 of cash wages paid to each household employee.

Cash wages. Cash wages includes wages paid by checks, money orders, etc. Cash wages do not include the value of food, lodging, clothing, and other noncash items given to a household employee. The value of these items is not subject to social security and Medicare tax or FUTA tax.

Federal income tax. A T/P is not required to withhold federal income tax from wages paid to a household employee. T/P should withhold federal income tax only if the household employee requests withholding and the T/P agrees. The employee must give T/P a completed Form W-4. If the T/P does withhold federal income taxes, he or she is responsible for paying it to the IRS.

Forms to file. If a T/P is required to report social security and Medicare wages, FUTA, or withheld federal income tax, he or she must file either Form 941, Employer's Quarterly Federal Tax Return, or Schedule H (Form 1040 or 1040-SR). A T/P uses Schedule H, Household Employment Taxes, to figure his or her total household employment taxes (social security, Medicare, FUTA, and withheld federal income taxes). These household taxes are added to the T/P's income taxes on Form 1040 or 1040-SR. Schedule H must be attached to Form 1040 or 1040-SR.

Who Must Pay Estimated Tax?

A T/P must make estimated tax payments if he or she expects to owe, after subtracting withholding and credits, at least \$1,000 in tax and expects withholding and credits to be less than the smaller of:

1. 90% of the tax liability for that year, or
2. 100% of the tax liability in the previous year.

Estimated tax for higher income individuals. If a T/P's 2021 adjusted gross income was more than \$150,000 (\$75,000 if married filing a separate return for 2022), the T/P will have to make estimated tax payments if he or she expects to owe, after subtracting withholding and credits, at least \$1,000 in tax in 2022 and expects withholding and credits to be less than the smaller of:

1. 90% of the tax liability for 2022, or
2. 110% of the tax liability in 2021.

No income subject to estimated tax during first period. A T/P starts making estimated payments only in the period in which he or she has income subject to estimated tax.

Separate returns. In a noncommunity property state, if both spouses make separate estimated tax payments each spouse can only take credit for the estimated tax payment made by that spouse.

Estimated tax payment dates for calendar-year taxpayer

For the Period	Due Date
January 1 - March 31	April 15
April 1 - May 31 (2 months)	June 15
June 1 - August 31	September 15
September 1 - December 31 (4 months)	January 15 next year

January payment. If a T/P files his tax return by January 31, he need not make the January 15th payment.

Estimated tax payment dates for fiscal-year taxpayer:

1. The 15th day of the 4th month of fiscal year.
2. The 15th day of the 6th month of fiscal year.
3. The 15th day of the 9th month of fiscal year.
4. The 15th day of the 1st month after the end of fiscal year.

How to Figure Each Payment

Figure the payment by using either of the following two methods:

1. **Regular installment method.** If the first estimated tax payment is due April 15, figure the required payment by dividing the annual estimated tax due by 4. Use this method only if income is received evenly throughout the year.
2. **Annualized income installment method.** If income is not received evenly throughout the year, each tax payment would vary. This method annualizes the tax at the end of each period based on a reasonable estimate of income, deductions, and other items relating to events that occurred from the beginning of the tax year through the end of the period. Figure the tax payments using Form 2210, Underpayment of Estimated Tax by Individuals, Estates, and Trusts.

Underpayment Penalty. The penalty is figured separately for each installment due date. Therefore, a T/P may owe the penalty for an earlier due date even if the T/P paid enough later to make up the underpayment or gets a refund when filing the tax return. The penalty is figured from the date the amount was due to the date the payment was made.

Other Taxes

Additional Medicare tax (Form 8959). A 0.9% Additional Medicare Tax applies to Medicare wages, railroad retirement (RRTA) compensation, and self-employment income that are more than:

- ▶ \$125,000 if married filing separately.
- ▶ \$250,000 if married filing jointly.
- ▶ \$200,000 for any other filing status.

Net Investment Income Tax (Form 8960). Taxpayers may be subject to Net Investment Income Tax (NIIT). The NIIT is 3.8% of the smaller of:

1. Net investment income, or
2. The excess of modified adjusted gross income over:
 - ▶ \$125,000 if married filing separately
 - ▶ \$250,000 if married filing jointly or qualifying surviving spouse
 - ▶ \$200,000 if any other filing status

Net investment income. Investment income includes, but is not limited to: interest, dividends, capital gains, rental and royalty income, non-qualified annuities, income from businesses involved in trading of financial instruments or commodities and businesses that are passive activities to the taxpayer. To calculate net investment income, investment income is reduced by certain expenses properly allocable to the income.

Tax on Unearned Income of Certain Children

Parent's Election to Report Child's Interest and Dividends (Form 8814). Parents may be able to elect to include their child's interest and dividend income (including capital gain distributions) on their tax return using Form 8814. If they do, their child will not have to file a return. This election can be made if all of the following conditions are met:

1. Child was under age 19 (or under age 24 if a full-time student) at the end of the year.
2. Child is required to file a return, unless the parent(s) makes this election.
3. Child had income only from interest and dividends (including capital gain distributions and Alaska Permanent Fund dividends).
4. The child's gross income was less than \$11,500.
5. The child does not file a joint return for the year.
6. No estimated tax payment was made for the year and no overpayment from the previous year was applied to this year under the child's name and social security number.
7. No federal income tax was taken out of the child's income under the backup withholding rules.
8. The taxpayer is the parent whose return must be used when applying the special tax rules for children.

Tax on Unearned Income of Certain Children

Tax for Certain Children Who Have Unearned Income (Form 8615). Part of a child's investment income may be subject to tax at the parent's tax rate instead of the child's tax rate. Form 8615 must be filed for a child if all of the following statements are true:

1. The child's investment income was more than \$2,300.
2. The child is required to file a return for the year.
3. The child either:
 - a) Was under age 18 at the end of the year,
 - b) Was age 18 at the end of the year and did not have earned income that was more than half of his or her support, or
 - c) Was a full-time student over age 18 and under age 24 at the end of the year and did not have earned income that was more than half of his or her support.
4. At least one parent was alive at the end of the tax year.
5. The child does not file a joint return for the year.

Form 8615. If the parent does not or cannot choose to include the child's income on the parent's tax return, use Form 8615, Tax for Certain Children Who Have Unearned Income, to figure the child's tax rate and attached the completed form to the child's Form 1040 or Form 1040NR.

Change in tax rate. After tax year 2019, dependent children with unearned income above \$2,300 are taxed at the parents' individual tax rate if the parent's rate is higher than the child's.

Tax on Unearned Income of Certain Children

Which Parent's Return To Use. If a child's parents are married to each other and file a joint return, use the joint return to figure the tax on the child's investment income.

Parents are married. If the child's parents file separate returns, use the return of the parent with the greater taxable income.

Parents not living together. If the child's parents are married to each other but not living together, and the parent with whom the child lives (the custodial parent) is considered unmarried, use the return of the custodial parent. If the custodial parent is not considered unmarried, use the return of the parent with the greater taxable income.

Parents are divorced. If the child's parents are divorced or legally separated, and the parent who had custody of the child for the greater part of the year (the custodial parent) has not remarried, use the return of the custodial parent.

Custodial parent remarried. If the custodial parent has remarried, the stepparent (rather than the noncustodial parent) is treated as the child's other parent. Therefore, if the custodial parent and the stepparent file a joint return, use that joint return. Do not use the return of the noncustodial parent.

Parents never married. If a child's parents have never been married to each other, but lived together all year, use the return of the parent with the greater taxable income.

Estate & Gift Tax Estate Tax (Form 706)

Form 706

Federal estate tax applies to the transfer of property at death. The estate of the decedent is liable for the tax on the entire taxable estate. If the estate tax is not paid when due, the executor can be held personally liable for the total tax. In addition, all persons receiving property from the estate are liable for the tax to the extent of the value of the property on the date of the decedent's death.

Gross estate. The gross estate includes the fair market value of all property to the extent of the decedent's interest in the property at the time of death.

What is included in the estate? The gross estate includes property that was owned by a decedent at the time of death and was transferred at death by will or by intestacy laws. It may also include other property interest that the decedent did not own at death. The following are items included in the estate:

1. Certain transfers made during the decedent's life without an adequate and full consideration in money or money's worth.
2. Annuities.
3. The includable portion of joint estates with right of survivorship.
4. The includable portion of tenancies by the entirety.
5. Certain life insurance proceeds (even though payable to beneficiaries other than the estate).
6. Property over which the decedent possessed a general power of appointment.
7. Dower or curtesy (or statutory estate) of the surviving spouse.
8. Community property to the extent of decedent's interest as defined by applicable law.

Estate & Gift Tax Estate Tax (Form 706)

What is excluded from the estate? Generally, the gross estate does not include the following:

- ▶ Property owned solely by the decedent's spouse or other individuals.
- ▶ Lifetime gifts that are complete (no powers or other control over the gifts are retained).
- ▶ Life estates given to the decedent by others in which the decedent has no further control or power at the date of death

Taxable estate. The gross estate minus the following:

1. Administration and funeral expenses.
2. Debts of the decedent.
3. Mortgages and liens.
4. Casualty and theft losses.
5. Marital deduction (all property that is included in the gross estate and passes to the surviving spouse is eligible for the marital deduction).
6. Charitable deduction (if the decedent leaves property to a qualifying charity, it is deductible from the gross estate).
7. Net losses during estate administration.
8. State death tax deduction.

Estate & Gift Tax Estate Tax (Form 706)

Estate tax return. An estate must file Form 706, United States Estate tax return, if the value of the gross estate at time of death plus any adjusted taxable gifts made after 1976 is more than \$12,060,000.

Due date and extension. The return is due 9 months after date of death unless an extension is granted. Use Form 4768, Application for Extension of Time To File a Return and/or Pay U.S. Estate (and Generation-Skipping Transfer) Taxes, to apply for an automatic 6-month extension of time to file.

Extension of time to pay estate tax (Form 4768). The usual extension of time to pay is up to 12 months, but the IRS may extend the time up to 10 years for reasonable cause. The following illustrate reasonable causes:

1. Estate includes liquid assets located in several jurisdictions which are not within executor's immediate control. Consequently, such assets cannot readily be collected by the executor, even with reasonable effort.
2. Most of an estate's assets consist of rights to receive payments in the future (e.g., annuities, royalties, accounts receivables). These assets do not provide enough cash to pay the tax due.
3. An estate includes a claim to substantial assets that cannot be collected without litigation.
4. Executor made a reasonable effort to convert the decedent's assets into cash. But the estate would have to borrow funds at an interest rate higher than generally available to satisfy claims against the estate that are due and payable.

Estate & Gift Tax Estate Tax (Form 706)

Valuation

The value of the decedent's property interest for estate tax purposes is its fair market value (FMV) at the date of death or at the alternate valuation date.

Alternate valuation. An executor may elect to use the alternate valuation date. Under this method, property included in the decedent's gross estate is valued at FMV at a date other than that of death. This election is effective only if a return is required to be filed. The alternate valuation may not be elected unless it will decrease both the value of the gross estate and the total net estate taxes due after application of all allowable credits. If an election is made to use the alternate valuation method, then all property in the estate is valued according to the following rules:

1. Any property distributed, sold, exchanged or otherwise disposed of within 6 months after the decedent's death is valued as of the date of distribution, sale, exchange or other disposition.
2. Any property not distributed, sold, exchanged or otherwise disposed of within 6 months after the decedent's death is valued as of 6 months after the date of the decedent's death.
3. Any property, interest, or estate that is affected by mere lapse of time is valued as of the date of the decedent's death or on the date of its distribution, sale, exchange, or other disposition, whichever occurs first. However, the date of death value may change to account for any change in value that is not due to a "mere lapse of time" on the date of its distribution, sale, exchange, or other disposition.

Estate & Gift Tax Estate Tax (Form 706)

Marital deduction. The marital deduction is a deduction from the gross estate of the value of property that is included in the gross estate but that passes, or has passed, to the surviving spouse. Generally, there is no limit on the amount of the marital deduction. Community property passing to the surviving spouse qualifies for the marital deduction. The marital deduction is generally not allowed if the surviving spouse is not a U.S. citizen. The unlimited marital deduction is allowed for property passing to such a surviving spouse in a qualified domestic trust (QDOT) or if such property is transferred or irrevocably assigned to such a trust before the estate tax return is filed.

Credits against the tax. The following credits are deducted from the gross estate tax to determine the net estate tax payable:

1. Applicable credit amount (unified credit).
2. Credit for tax on prior transfers.
3. Credit for foreign death taxes.

Estate & Gift Tax Estate Tax (Form 706)

Applicable Credit Amount (Unified Credit). The applicable credit amount is allowable credit against estate and gift taxes. It is calculated by determining the tentative tax on the applicable exclusion amount, which is the amount that can be transferred before an estate tax liability will be incurred. The applicable exclusion amount equals the total of:

1. The basic exclusion amount. In 2022, the basic exclusion amount, as adjusted for inflation is \$12,060,000.
2. The deceased spousal unused exclusion amount (DSUE).

Deceased spousal unused exclusion amount (DSUE). If the decedent had a spouse who died on or after January 1, 2011, whose estate did not use all of its applicable exclusion against gift or estate tax liability, a DSUE amount may be available for use by the decedent's estate. If the predeceased spouse died in 2011, the DSUE amount was calculated and attached to his or her Form 706.

Year	Exclusion Amounts	Credit Amounts
2019	\$11,400,000	\$4,505,800
2020	\$11,580,000	\$4,577,800
2021	\$11,700,000	\$4,625,800
2022	\$12,060,000	\$4,769,800

Note: Any credit amount used against gift tax in one year reduces the amount of credit that can be used against estate tax.

Estate & Gift Tax Estate Tax (Form 706)

Distributions to Beneficiaries

A beneficiary of an estate, that must distribute all its income currently, must report his or her share of the distributable net income whether or not it was actually received. Any other amount paid, credited, or required to be distributed to the beneficiary, must also be included in the beneficiary's gross income. Each item of income keeps the same character in the beneficiaries' hands as it had in the hands of the estate. Each beneficiary who receives a distribution from the estate for the tax year or to whom any item is allocated must receive a Schedule K-1. Gifts or a bequest that meets the conditions described below are not taxable.

Bequest. A bequest is the act of giving or leaving property to another through the last will and testament. It will not be an allowable deduction to the estate or taxable to the beneficiary if the bequest is:

1. Required by the terms of the will,
2. A gift or bequest of specific sum of money or property, and
3. Paid out in three or fewer installments under the terms of the will.

Estate tax deduction. Income that a decedent had a right to receive is included in the decedent's gross estate and is subject to estate tax. This income in respect of a decedent is also taxed when received by the recipient (estate or beneficiary). However, an income tax deduction is allowed to the recipient for the estate tax paid on the income.

Estate & Gift Tax Gift Tax (Form 709)

Filing the return. A T/P must file a gift tax return (Form 709) if any of the following apply:

1. Giving a gift that is more than the annual exclusion (\$16,000) to someone.
2. A married T/P who is splitting a gift with his or her spouse.
3. Giving someone (other than to a spouse) a gift that he or she cannot actually possess, enjoy, or receive income from until some time in the future.
4. Giving a spouse an interest in property that will be ended by some future event.

Exception: The following are not taxable gifts. Form 709 is not required to be filed:

1. The first \$16,000 given to someone during the calendar year (the annual exclusion).
2. Tuition or medical expenses paid directly to an educational or medical institution for someone else.
3. Gifts to spouse.
4. Gifts to a political organization for its use.
5. Gifts to charities.
6. Gifts to certain exempt organizations described in 501(c)(4), 501(c)(5), and 501(c)(6).

Estate & Gift Tax Gift Tax (Form 709)

Due date. Form 709 must be filed on or after January 1 but no later than April 15 of the year after the year the gift was made.

Extension to file. There are two methods of extending the time to file the gift tax return. Neither method extends the time to pay the gift or generation-skipping transfer (GST) taxes:

1. **By extending the time to file income tax return.** Any extension of time granted for filing a calendar year federal income tax return will also automatically extend the time to file a federal gift tax return. Income tax extensions are made by using Form 4868, Application for Automatic Extension of Time To File U.S. Individual Income Tax Return, or Form 2350, Application for Extension of Time To File U.S. Income Tax Return.
2. **By filing Form 8892.** If a T/P does not request an extension for his or her income tax return, use Form 8892, Application for Automatic Extension of Time To File Form 709 and/or Payment of Gift/Generation-Skipping Transfer Tax, to request an automatic 6-month extension of time to file a federal gift tax return. In addition to containing an extension request, Form 8892 also serves as a payment voucher (Form 8892-V) for a balance due on federal gift taxes.

Note: Neither method extends the time to pay the gift or GST taxes. If a T/P wants an extension of time to pay the gift or GST taxes, he or she must request that separately.

Value of gift. For calculating gift tax, the value of the gift is its FMV.

Estate & Gift Tax

Gift Tax (Form 709)

Annual exclusion. The first \$16,000 of gifts made to any one person during the calendar year (except gifts of future interests in property) is excluded in determining the total amount of gifts for the calendar year.

Education exclusion. The gift tax does not apply to amounts paid on behalf of an individual to a qualifying domestic or foreign educational organization. The payment must be made directly to the educational organization and it must be for tuition only. No educational exclusion is allowed for amounts paid for books, supplies, or room and board. Contributions to a qualified tuition program (529 plan) on behalf of a designated beneficiary do not qualify for the educational exclusion. However, if a T/P contributed more than \$16,000 to a 529 plan on behalf of any one person, the T/P may elect to treat up to \$80,000 of the contribution for that person as if the T/P made it ratably over a 5-year period. The election allows the T/P to apply the annual exclusion to a portion of the contribution in each of the 5 years starting with the year of the contribution.

Medical exclusion. The gift tax does not apply to amounts paid on behalf of an individual to a person or institution that provides medical care. The payment must be made directly to the care provider.

Marital deduction. A T/P can deduct from taxable gifts the value of gifts made to a spouse. To qualify the spouses must be married and the spouse receiving the gift must be a U.S. citizen at the time the gift was made. The spouse making the gift need not be a U.S. citizen. For gifts made to spouses who are not U.S. citizens, the annual exclusion is \$164,000 for 2022.

Estate & Gift Tax Gift Tax (Form 709)

Gift by Husband or Wife to Third Party - Gift Splitting

A gift made by a person to someone other than a spouse may be considered as made one-half by each spouse. This is known as gift splitting and both spouses must consent to its use.

Requirement. The spouses must be legally married at the time of the gift. If they are divorced during the year, they still may split the gift so long as neither remarries during the year. Both spouses must be citizens or residents of the U.S. on the date of gift.

All gifts must be split. If the spouses consent to gift splitting, all gifts made during the year must be split.

Consent. The consent to split gifts cannot be made after a gift tax return has been filed and the due date for filing the return has passed. A married couple cannot file a joint gift tax return. Each spouse must file separate gift tax returns to show that they both agree to use gift splitting. The separate individual gift tax returns should be mail together (in the same envelope) to help the IRS process the returns and to avoid correspondence from the IRS. The consent may be revoked, but not after April 15 of the year following the year of the gift.

Annual exclusion. Spouses who consent to gift splitting can exclude up to \$32,000 of gifts to any one person without any gift tax liability. A gift of a future interest (i.e., Restricted right to the gift) does not qualify for the annual exclusion.

Estate & Gift Tax Applicable Credit

Forms 706 & 709

The applicable credit is an amount that eliminates or reduces tax. The credit applies to both gift and estate tax. Any applicable credit used against gift tax in one year reduces the amount of credit that can be used against gift or estate tax in a later year. In 2022, the applicable credit for gift and estate tax is \$4,769,800, which exempts \$12,060,000 from tax. The following table shows the applicable credit and the applicable exclusion amount for the year in which a gift is made or a decedent dies.

	For Estate & Gift Tax Purposes	
Year	Credit Amounts	Exclusion Amount
2016	\$2,125,800	\$5,450,000
2017	\$2,141,800	\$5,490,000
2018	\$11,180,000	\$4,417,800
2019	\$11,400,000	\$4,505,800
2020	\$11,580,000	\$4,577,800
2021	\$11,700,000	\$4,625,800
2022	\$12,060,000	\$4,769,800

Estate & Gift Tax

Generation-Skipping Transfer Tax

Forms 706 & 709

Generation-Skipping Transfer Tax (GST). The GST tax may apply to gifts during a taxpayer's life or transfers occurring at death, called bequests, made to skip persons. A skip person is a person who belongs to a generation that is two or more generations below the generation of the donor. For instance, a grandchild will generally be a skip person. The GST tax is figured on the amount of the gift or bequest transferred to a skip person, after subtracting any GST exemption allocated to the gift or bequest at the maximum gift and estate tax rates. Each individual has a GST exemption equal to the basic exclusion amount, as indexed for inflation, for the year involved.

Generation assignment where intervening parent is deceased. If property is transferred to an individual who is a descendant of a parent of the transferor, and that individual's parent (who is a lineal descendant of the parent of the transferor) is deceased at the time the transfer is subject to gift or estate tax, then for purposes of generation assignment, the individual is treated as if he or she is a member of the generation that is one generation below the lower of:

- ▶ The transferor's generation or
- ▶ The generation assignment of the youngest living ancestor of the individual, who is also a descendant of the parent of the transferor.

Failure-to-file penalty. If a return is not filed by the due date (including extensions), T/P is subject to a penalty of 5% per month for each month or part of the month that the return is late, but not more than 25%. The penalty is based on the tax not paid by the due date (without regard to extensions). The penalty is based on the tax not paid by the due date (without regard to extensions).

Fraud. If the failure to file is due to fraud, the penalty is 15% for each month or part of a month that the return is late up to a maximum of 75%.

Return over 60 days late. If the return is more than 60 days late after the due date or extended due date, the minimum penalty is the smaller of \$450 or 100% of the unpaid tax.

Failure-to-pay penalty. A penalty of .5% of the unpaid taxes for each month or part of a month, after the due date that the tax is not paid. This penalty does not apply during the automatic 6-month extension of time to file period if paid at least 90% of actual tax liability on or before the due date of the return and pay the balance when the return is filed. The monthly rate of the failure-to-pay penalty is half the usual rate (.25% instead of .50%) if an installment agreement is in effect for that month. Return must be filed by the due date (including extensions) to qualify for this reduced penalty. The penalty is increased to 1% per month if a notice of levy is issued.

Combine penalties. If both the failure-to-file penalty and the failure-to-pay penalty apply in any month, the 5% (or 15%) failure-to-file penalty is reduced by the failure-to-pay penalty. However, if the return is filed more than 60 days after the due date or extended due date, the minimum penalty is the smaller of \$450 or 100% of the unpaid tax.

Accuracy-related penalty. A T/P is subject to an accuracy-related penalty if the underpayment of tax is because of one of the following:

1. Negligence or disregard of the rules or regulations. Failure to make a reasonable attempt to comply with the tax law or to exercise ordinary and reasonable care in preparing a return. Negligence also includes failure to keep adequate books and records.
2. Substantially understate income tax. The understatement is substantial if it is more than the larger of 10% of the correct tax or \$5,000.
3. Claimed tax benefits for a transaction that lacks economic substance.
4. Failure to disclose a foreign financial asset.

The penalty is equal to 20% of the underpayment. The penalty is 40% of any portion of the underpayment that is attributable to an undisclosed noneconomic substance transaction or an undisclosed foreign financial asset transaction. The penalty will not be figured on any part of an underpayment on which the fraud penalty is charged.

Fraud. If there is any underpayment of tax on the return due to fraud, a penalty of 75% of the underpayment due to fraud will be added to the tax owed. The fraud penalty on a joint return does not apply to a spouse unless some part of the underpayment is due to the fraud of that spouse.

Frivolous return. The penalty for filing a frivolous return is \$5,000. A frivolous return is one that does not include enough information to figure the correct tax or that contains information clearly showing that the tax reported is substantially incorrect.

Failure to supply social security number. If T/P does not include his or her SSN or the SSN of another person where required on a return, statement, or other document, the T/P will be subject to a penalty of \$50 for each failure. The T/P will also be subject to a penalty of \$50 if the T/P does not give his or her SSN to another person when it is required on a return, statement, or other document.

Criminal penalties. T/P may be subject to criminal prosecution (brought to trial) for actions such as the following:

1. Tax evasion.
2. Willful failure to file a return, supply information, or pay any tax due.
3. Fraud and false statements.
4. Preparing and filing a fraudulent return.
5. Identity theft.

Criminal convictions may result in fines up to \$250,000 and/or up to five years in prison for each offense.

Due diligence. Preparers who prepare tax returns claiming the Earned Income Tax Credit (EITC), the child tax credit (CTC), the additional child tax credit (ACTC), the credit for other dependents (ODC), the American opportunity tax credit (AOTC), and head of household (HOH) filing status must meet four due diligence requirements. Failure to meet the due diligence requirements for claiming the EIC, the CTC/ACTC/ODC, the AOTC, and/or HOH filing status could result in a \$530 penalty for each failure.

1. ***Compute the Credits Based on the Facts.*** Compute the credits and complete the applicable worksheet(s) or a preparer's own worksheet(s) for any EITC, CTC/ACTC/ ODC or AOTC claimed on the return or claim for refund. Most professional tax return preparation software includes the worksheets.
2. ***Complete and Submit Form 8867.*** Complete Form 8867, Paid Preparer's Due Diligence Checklist, and submit this completed form to the IRS with every electronic or paper return or claim for refund prepared that claims the EITC, CTC/ACTC/ODC, AOTC, or HOH filing status.
 - ▶ Make sure that the software used includes Form 8867 and file the completed form with every electronic return or provide the completed form with every paper return or claim for refund prepared that claims the EITC, CTC/ACTC/ODC, AOTC, or HOH filing status.
 - ▶ Answer each question on the form based on information from the client and information the preparer knows is true.
 - ▶ The preparer must also personally complete Part VI, Eligibility Certification.

Continued on next card

3. **Keep records. Keep copies of the following records either electronically or on paper:**
- ▶ Form 8867.
 - ▶ The applicable worksheet(s) or the preparer's own worksheet(s) for the EITC, CTC/ACTC/ODC, or AOTC claimed on the return or claim for refund.
 - ▶ Any taxpayer documents that the preparer may have relied on to determine eligibility for the credit(s) and/or HOH filing status or to compute the amount of the credit(s).
 - ▶ A record of how, when, and from whom the information used to prepare Form 8867 and the applicable worksheet(s) was obtained.

Keep these documents for **3 years** from the latest of:

- ▶ The due date of the tax return.
 - ▶ The date the tax return was electronically filed.
 - ▶ For a paper return, the date the return or claim for refund was presented to the client for signature.
 - ▶ If the preparer is a non-signing tax return preparer, the date the non-signing preparer submitted to the signing tax return preparer the part of the return for which the non-signing preparer was responsible.
4. ***Ask all the right questions.*** The preparer, in interviewing the taxpayer, should ask adequate questions and document the taxpayer's responses to determine eligibility for the credit(s) and/or HOH filing status.

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 1

▶ Type of Form	Purpose of Form—Reporting the following:
Part I - Additional Income and Adjustments to Income	Additional Income <ul style="list-style-type: none">▶ Taxable refunds, credits, or offsets of state and local income taxes▶ Alimony received▶ Business income or (loss) from Schedule C▶ Other gains or (losses) from Form 4797▶ Rental real estate, royalties, partnerships, S corporations, trusts, etc from Schedule E▶ Farm income or (loss) from Schedule F▶ Unemployment compensation▶ Other income

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 1

▶ Type of Form	Purpose of Form—Reporting the following:
Part II - Additional Income and Adjustments to Income	Adjustments to Income <ul style="list-style-type: none"> ▶ Educator expenses ▶ Certain business expenses of reservists, performing artists, and fee-basis government officials from Schedule 2106 ▶ Health savings account deduction from Form 8889 ▶ Moving expenses for members of the Armed Forces from Form 3903 ▶ Deductible part of self-employment tax ▶ Self-employed SEP, SIMPLE, and qualified plans ▶ Self-employed health insurance deduction ▶ Penalty on early withdrawal of savings ▶ Alimony paid ▶ IRA deduction ▶ Student loan interest deduction

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 2

► Type of Form	Purpose of Form—Reporting the following:
Part I - Tax	<ul style="list-style-type: none">► Alternative minimum tax from Form 6251► Excess advance premium tax credit repayment from Form 8962

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 2

▶ Type of Form	Purpose of Form—Reporting the following:
Part II - Other Taxes	<ul style="list-style-type: none"> ▶ Self-employment tax from Schedule SE ▶ Unreported social security and Medicare tax from: <ul style="list-style-type: none"> • Form 4137 - Social Security and Medicare Tax On Unreported Tip Income • Form 8919 - Uncollected Social Security and Medicare Tax on Wages ▶ Additional tax on IRAs, other qualified retirement plans, and other tax-favored accounts ▶ Household employment taxes from Schedule H ▶ Repayment of first-time homebuyer credit from Form 5405 ▶ Additional Medicare Tax from Form 8959 ▶ Net Investment Income Tax from Form 8960 ▶ Uncollected social security and Medicare or RRTA tax on tips or group-term life insurance from Form W-2, box 12

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 3

▶ Type of Form	Purpose of Form—Reporting the following:
Part I - Nonrefundable Credits	<ul style="list-style-type: none"> ▶ Foreign tax credit ▶ Credit for child and dependent care expenses. Attach Form 2441 ▶ Education credits from Form 8863, line 19 ▶ Retirement savings contributions credit from Form 8880 ▶ Residential energy credit from Form 5695 ▶ Other credits from: <ul style="list-style-type: none"> • Form 3800 - General Business Credit • Form 8801 - Credit for Prior Year Minimum Tax • Form 8839 - Adoption Credit • Schedule R - Credit for the Elderly or Disabled • Form 8910 - Alternative motor vehicle Credit • Form 8836 - Qualified Plug-in Motor Vehicle Credit • Form 8396 - Mortgage Interest Credit • Form 8834 - Qualified Electric Vehicle Credit

Forms & Schedules at a Glance

Individuals

Form 1040 or 1040-SR Schedule 3

► Type of Form	Purpose of Form—Reporting the following:
Part II - Other Payments and Refundable Credits	<ul style="list-style-type: none">► Net premium tax credit from Form 8962► Amount paid with request for extension to file► Excess social security and tier 1 RRTA tax withheld► Credit for federal tax on fuels from Form 4136► Credit for qualified sick and family leave wages paid in 2022 from Schedule(s) H for leave taken before April 1, 2021► Credit for repayment of amounts included in income from earlier years► Deferred amount of net 965 tax liability► Credit for qualified sick and family leave wages paid in 2022 from Schedule(s) H for leave taken after March 31, 2021, and before October 1, 2021► Other payments or refundable credits

Forms & Schedules at a Glance

Individuals

Income

- ▶ **Schedule B** - Interest and Ordinary Dividends
- ▶ **Schedule D** - Capital Gains and Losses
- ▶ **Form 8949** - Sales and Other Disposition of Capital Assets
- ▶ **Form 4797** - Sales of Business Property
- ▶ **Schedule E** - Supplemental Income and Loss (from rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)

Business Income or Loss

- ▶ **Schedule C** - Profit or loss From Business
- ▶ **Schedule F** - Profit or Loss From Farming
- ▶ **Form 4562** - Depreciation and Amortization
- ▶ **Form 8829** - Expenses for Business Use of Your Home
- ▶ **Form 8582** - Passive Activity Loss Limitations
- ▶ **Form 8594** - Asset Acquisition Statement Under Section 1060
- ▶ **Form 8995** - Qualified Business Income Deduction Simplified Computation
- ▶ **Form 8995-A** - Qualified Business Income Deduction

Forms & Schedules at a Glance

Individuals

Adjustments to Gross Income

- ▶ **Form 8889** - Health Savings Account (HSAs)
- ▶ **Form 2106** - Certain business expenses of reservists, performing artists, and fee-basis government officials
- ▶ **Form 3903** - Moving expenses for members of the Armed Forces
- ▶ **Schedule SE** - Deductible part of self-employment tax

Credits

- ▶ **Schedule EIC** - Earned Income Credit
- ▶ **Schedule R** - Credit for the Elderly or the Disabled
- ▶ **Form 2441** - Child and Dependent Care Expenses
- ▶ **Form 8863** - Education Credits (American Opportunity and Lifetime Learning Credits)
- ▶ **Schedule 8812** - Child Tax Credit
- ▶ **Form 8801** - Credit for Prior Year Minimum Tax - Individuals, Estate, and Trusts
- ▶ **Form 8962** - Premium Tax Credit (PTC)
- ▶ **Form 1116** - Foreign Tax Credit (Individuals, Estate, and Trusts)
- ▶ **Form 8839** - Qualified Adoption Expenses
- ▶ **Form 5695** - Residential Energy Credit

Forms & Schedules at a Glance

Individuals

Itemize deductions

- ▶ **Schedule A** - Itemize Deductions
- ▶ **Form 4952** - Investment Interest Expense Deduction
- ▶ **Form 4684** - Casualties and Thefts
- ▶ **Form 8283** - Noncash Charitable Contributions

Qualified business income deduction

- ▶ **Form 8995 or Form 8995-A**

Taxes

- ▶ **Form 6251** - Alternative Minimum Tax - Individuals
- ▶ **Schedule SE** - Self-Employment Tax
- ▶ **Form 4137** - Social Security and Medicare Tax On Unreported Tip Income
- ▶ **Form 8919** - Uncollected Social Security and Medicare Tax on Wages
- ▶ **Form 5329** - Additional Taxes on Qualified Plans (Including IRAs), and Other Tax-Favored Accounts
- ▶ **Form 2210** - Underpayment of Estimated Tax By Individuals, Estates, and Trusts
- ▶ **Form 8959** - Additional Medicare Tax
- ▶ **Form 8960** - Net Investment Tax - Individuals, Estates, and Trusts

Forms & Schedules at a Glance Individuals

Refunds

- ▶ **Form 1040X** - Amended U.S. Individual Income Tax Return
- ▶ **Form 843** - Claim for Refund and Request for Abatement
- ▶ **Form 1045** - Application for Tentative Refund (used for NOL carryback)

Kiddie Tax

- ▶ **Form 8615** - Tax for Certain Children Who Have Unearned Income
- ▶ **Form 8814** - Parent's Election To Report Child's Interest and Dividends

Forms & Schedules at a Glance

Individuals

Type of Form	Purpose of Form	Filing Date
Form 1040-SR - U.S. Tax Return for Seniors	Use this form if age 65 or older. The form generally mirrors Form 1040	April 15
Form 706 - United States Estate (and Generation-Skipping Transfer) Tax Return	Use Form 706 to figure a decedent's estate tax imposed on the entire estate valued at more than \$12,060,000 in 2022.	9 month after the date of the decedent's death.
Form 709 - United States Gift (and Generation Skipping Transfer) Tax Return	Use for 709 to report transfers subject to the federal gift and certain generation-skipping transfers.	No earlier than January 1 but no later than April 15.