

# 2020 NATIONAL INCOME TAX WORKBOOK

CHAPTER 10: INDIVIDUAL TAX ISSUES  
PART 2 P. 321





DEPENDENT RELATED CREDITS

## ISSUE 1: ALLOCATION OF TAX BENEFITS

P. 322

Earned Income Credit (**EIC**) Eligibility

TP must

1. Have AGI below phaseout (Figure 10.1)
2. Have valid SSN
3. Not file MFS
4. Be US citizen or resident alien all year
5. No foreign earned income
6. Have \$3,650 or less investment income
7. Have earned income

## EIC ELIGIBILITY CONT.

PP. 322-323

### Additional Rules with No Qualifying Children

- TP/ spouse if MFJ at least 25 and under 65 years
- Not dependent of another person
- Not qualifying child of another person
- Live in US for more than ½ year

### Additional Rules with Qualifying Children

1. Child must meet relationship, age, residency, & joint return tests
2. Child can only be used once
3. Generally cannot be qualifying child of another TP

## RULES FOR QUALIFYING CHILDREN - SEC. 152

P. 323

### Relationship Test

Must be one of specified family members

### Age Test

Under 19 at end of year

Under 24 if full time student

### Residency Test

Child lived with TP more than 6 months

### Joint Return Test

Child can't file joint return unless return only for a refund of income tax paid

## CHILD TAX CREDIT

P. 323

Nonrefundable credit

Income phaseout threshold with one child

MFJ \$440,000

Other filing status \$240,000

Qualifying child under age 17 and meets dependent tests

Support test - Child cannot furnish more than  $\frac{1}{2}$  support

See 2019 workbook for a discussion of additional CTC

## CREDIT FOR OTHER DEPENDENTS

P. 324

- Nonrefundable credit for person who qualifies as dependent but not eligible for CTC
- MAGI below threshold

### Qualifying Child

Under age 19 or full-time student and under age 24

Use if no SSN, but has ITIN or ATIN

### Qualifying Relative

See list

Includes individual who lives with TP and is a member of household

Gross income limit is \$4,300

## CREDIT FOR OTHER DEPENDENTS CONT.

P. 324

### Ex. 10.1 Parent Living with Child

- Fred lives w/ his father Marvin
- Marvin's income is \$3,000
- Fred pays over  $\frac{1}{2}$  Marvin's support
- Marvin is a qualifying relative for ODC



## OBSERVATION – CANADA AND MEXICO

P. 324

ODC applies to US Citizens or nationals or residents of the US

ODC does not apply to residents of Mexico or Canada who are not US citizens or nationals

## HEAD OF HOUSEHOLD FILING STATUS

PP. 324-325

### Requirements

1. Unmarried or considered unmarried as of the last day of the tax year
2. Paid over  $\frac{1}{2}$  of the household expenses
3. Qualifying person lives in household more than  $\frac{1}{2}$  the year
  - Father or mother – does not have to live with TP, but qualifies a dependent and pays over  $\frac{1}{2}$  of parent's housing
  - Ex. 10.2 Live in girlfriend is not a qualifying relative

## CHILD & DEPENDENT CARE CREDIT

P. 325

Nonrefundable credit for workers and those looking for work

- Pay for care of qualifying person
- Have earned income during the year
- Pay care expenses
- Use qualifying provider
- Cannot file MFS unless meet exception
- Provide identity of provider on return

## OBSERVATION – PAYMENTS TO RELATIVES

P. 325

Payments to relatives or dependents do not qualify.

Include:

- Dependents

- Children under 19

- Spouse

- Parent of the qualifying child under age 13

## QUALIFYING PERSON

P. 325

- Dependent child under age 13 and qualifying child
- Spouse who is unable to care for self and lived with TP more than  $\frac{1}{2}$  of the year
- Person who is unable to care for self, lived with TP more than  $\frac{1}{2}$  year, and
  - Dependent
  - Would have been dependent except for failing certain tests
- Ex. 10.3 Disabled spouse has nursing care and expenses are eligible for the credit.

## QUALIFYING CHILD OF DIVORCED PARENTS

PP. 325-326

If can't claim child as dependent, still qualifying if:

- Child under 13 or unable to care for self
- More than  $\frac{1}{2}$  of support is paid by parents who are divorced, separated, or lived apart
- Parents have custody for more than  $\frac{1}{2}$  of year
- TP is custodial parent – more than  $\frac{1}{2}$  of nights if equal number, higher AGI

## ALLOCATING CREDITS

P. 326

Must go together:

EIC

CTC

ACTC

ODC

H of H

Child and dependent care expense credit

Exclusion for dependent care benefits

Special rules for divorced/separated parents

## TIE BREAKER RULES

P. 326

1. Parents if filing a joint return and claim as qualifying child
2. Parent if only 1 person is the parent, and claims qualifying child
3. Parent where child lived longer
4. Higher AGI parent & their spouse if their time is the same and both parents claim child
5. Person with highest AGI if no parent can claim child
6. Highest AGI person if neither parent does claims child



## PRACTITIONER NOTE - EIC

P. 326



Earned Income Credit

If not able to claim child, TP may be eligible to claim self only EIC

## EXAMPLES OF ALLOCATING CREDITS

PP. 326-327

Ex. 10.4 Amy and her 12 y.o. child, Annie, live with Amy's mom, Ruth. Amy is 25 and has \$12,000 AGI. Ruth has \$15,000 AGI. Annie's father does not live with them. Amy can claim Annie as she is the parent.

Ex. 10.5 Same facts but Amy does not claim Annie as her qualifying child. Ruth's AGI is higher, and she can claim her.

Ex. 10.6 Betty and Burt are unmarried and do not live together. Their 5 y.o. child stays with mother during the week and father on the weekends. Child lives with Betty more time than Burt, so Betty can claim him.

## EXAMPLES CONT.

P. 327

Ex. 10.7 Same facts but Betty and Burt live together with their son. Parent with higher AGI can claim child.

Ex. 10.8 David lives with grandparent, Dorothy who provides more than  $\frac{1}{2}$  his support. Parents do not live w/ them and neither provides more than  $\frac{1}{2}$  support. David is a qualifying child for Dorothy.

## ISSUE 2: PREMIUM TAX CREDIT

P. 328

PTC is refundable credit to purchase health insurance through Marketplace

Can get an advance of the PTC (APTC)

Based on expected income and family size

TP must reconcile PTC with APTC claimed

Form 8962



## GENERAL RECONCILIATION RULES

P. 329

Reconciliation of APTC compares

1. Amount of PTC used during the year
2. PTC actually allowed

PTC = second lowest cost silver plan in the Marketplace less a % of household income

From 1095-A reports the enrollment premiums, SLCSP premium, and APTC amount

NOTE: 1095-A may be blank or wrong, practitioner can look up the SLCSP premium online

## RECONCILIATION RULES CONT. P. 329

Failure to pay the premium starts a 3-month grace period  
The coverage may be cancelled retroactively

### Ex. 10.10 Cancelled Coverage

Fred pays for first 4 months, but does not pay for May, June, and July.  
On the tax return, Fred does not consider the APTC for June or July.

Report an overpayment of APTC on Schedule 2, Additional Taxes

If APTC is less than allowed PTC, the refund is on Schedule 3, Additional Credits and Payments.

## POLICY PAYMENT ALLOCATIONS

P. 330

- Reconciliation for tax family – changes may require allocation of premiums and APTC
- All but MFS can agree on allocation
- Figure 10.2 default allocations

## PTC IN YEAR OF MARRIAGE

P. 331

- General rule is to add the 1095-A forms together
- Alternative calculation if
  1. Unmarried as of Jan. 1
  2. Married as of Dec. 31
  3. File a joint return
  4. Anyone was enrolled month before marriage
  5. APTC paid
  6. Excess APTC on Worksheet 3 or income 401% of poverty level



## ALTERNATIVE CALCULATION

P. 332

Spouse and dependents of that spouse are included in alt. family size

Alt. family size determines alt. monthly contribution

May reduce excess APTC

Worksheets in Publication 974 and Form 8962 instructions

Worksheet 1 like Part 1 of Form 8962

## ALTERNATIVE CALCULATION CONT. PP. 332-333

- Up to 8 steps
- Consider the month of marriage to be a pre-marriage month
- First compute alt. monthly contribution amount based on  $\frac{1}{2}$  of the income
- Compute the pre-marriage credit for both spouses
- Then compare to regular calculations
- Use alternative if it is less

EX.10.11

P. 333

- Paulette Oak and Quentin Cedar married and combined households on July 18, 2019
- Both had coverage before the marriage
- Paulette had coverage for herself - 1095-A thru July
- Quentin had coverage for himself and 2 children - 1095-A thru July
- They also received a 1095-A for the balance of the year with a family size of 4
- Total income was \$76,000

FIG. 10.3

**Part II, Covered Individuals**

A. Covered Individual	B. Covered Individual SSN	D. Coverage Start Date	E. Coverage Termination Date
Paulette Oak	xxx-xx-xxxx	01/01/19	07/31/19

**Part III, Coverage Information**

Month	A. Monthly Enrollment Premiums	B. Monthly Second-Lowest-Cost Silver Plan (SLCSP) Premium	C. Monthly Advance Payment of PTC
January	500	433	116
February	500	433	116
March	500	433	116
April	500	433	116
May	500	433	116
June	500	433	116
July	500	433	116
Annual Totals	3,500	3,031	812



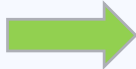
FIG. 10.4

P. 334

**FIGURE 10.4 Quentin Cedar's 1095-A for January through July**

**Part II, Covered Individuals**

A. Covered Individual	B. Covered Individual SSN	D. Coverage Start Date	E. Coverage Termination Date
Quentin Cedar	xxx-xx-xxxx	01/01/19	07/31/19
Ron Cedar	xxx-xx-xxxx	01/01/19	07/31/19
John Cedar	xxx-xx-xxxx	01/01/19	07/31/19



**Part III, Coverage Information**

Month	A. Monthly Enrollment Premiums	B. Monthly Second-Lowest-Cost Silver Plan (SLCSP) Premium	C. Monthly Advance Payment of PTC
January	1,000	833	678
February	1,000	833	678
March	1,000	833	678
April	1,000	833	678
May	1,000	833	678
June	1,000	833	678
July	1,000	833	678
Annual Totals	7,000	5,381	4,746

FIG. 10.5

**FIGURE 10.5 Form 1095-A for August through December**

<b>Part II, Covered Individuals</b>			
Covered Individual	B. Covered Individual SSN	D. Coverage Start Date	E. Coverage Termination Date
Paulette Cedar	xxx-xx-xxxx	08/01/19	12/31/19
Quentin Cedar	xxx-xx-xxxx	08/01/19	12/31/19
Ron Cedar	xxx-xx-xxxx	08/01/19	12/31/19
John Cedar	xxx-xx-xxxx	08/01/19	12/31/19

<b>Part III, Coverage Information</b>			
Month	A. Monthly Enrollment Premiums	B. Monthly Second-Lowest-Cost Silver Plan (SLCSP) Premium	C. Monthly Advance Payment of PTC
August	1,350	1,167	573
September	1,350	1,167	573
October	1,350	1,167	573
November	1,350	1,167	573
December	1,350	1,167	573
Annual Totals	6,750	5,835	2,865



EX. 10.11 CONT.

PP. 333-337

Complete Form 8962 Part 1, lines 1-8 (Figure 10.6) and Table 4 (Figure 10.7)

Line 5 Form 8962 is less than 401% so complete Worksheet 3 to compute allowable PTC (Figure 10.8)

FIG 10.6



Form **8962** **Premium Tax Credit (PTC)** OMB No. 1545-0074  
 Department of the Treasury Internal Revenue Service **2019** Attachment Sequence No. 73  
 Name shown on your return: Paulette and Quentin Cedar Your social security number: XXX-XX-XXXX  
 You cannot take the PTC if your filing status is married filing separately unless you qualify for an exception (see instructions). If you qualify, check the box

**Part I Annual and Monthly Contribution Amount**

<b>1</b> Tax family size. Enter your tax family size (see instructions)		<b>1</b>	<b>4</b>
<b>2a</b> Modified AGI. Enter your modified AGI (see instructions)	<b>2a</b>	76,000	
<b>b</b> Enter the total of your dependents' modified AGI (see instructions)	<b>2b</b>	0	
<b>3</b> Household income. Add the amounts on lines 2a and 2b (see instructions)		<b>3</b>	76,000
<b>4</b> Federal poverty line. Enter the federal poverty line amount from Table 1-1, 1-2, or 1-3 (see instructions). Check the appropriate box for the federal poverty table used. <b>a</b> <input type="checkbox"/> Alaska <b>b</b> <input type="checkbox"/> Hawaii <b>c</b> <input checked="" type="checkbox"/> Other 48 states and DC		<b>4</b>	25,100
<b>5</b> Household income as a percentage of federal poverty line (see instructions)		<b>5</b>	302 %
<b>6</b> Did you enter 401% on line 5? (See instructions if you entered less than 100%.) <input checked="" type="checkbox"/> <b>No.</b> Continue to line 7. <input type="checkbox"/> <b>Yes.</b> You are not eligible to take the PTC. If advance payment of the PTC was made, see the instructions for how to report your excess advance PTC repayment amount.			
<b>7</b> Applicable Figure. Using your line 5 percentage, locate your "applicable figure" on the table in the instructions		<b>7</b>	.0966
<b>8a</b> Annual contribution amount. Multiply line 3 by line 7. Round to nearest whole dollar amount	<b>8a</b>	7,494	
<b>b</b> Monthly contribution amount. Divide line 8a by 12. Round to nearest whole dollar amount	<b>8b</b>		625

Number to beat \$625





## FIGURE 10.7 TABLE 4

P. 336

- Table 4 determines eligibility to use alt. calculation  
Beginning not married, end married, joint return, enrolled, APTC paid

## ADDITIONAL STEPS

PP. 336-340

- Worksheet 3 Fig. 10.8 computes allowable PTC
- Have to pay back \$1,226
- Fig. 10.9 Paulette's alt. monthly contribution amount
- Fig. 10.10 Paulette's alt. credit for the pre-marriage months
- Fig. 10.11 Quentin's alt. monthly contribution amount
- Fig. 10.12 Quentin's alt. credit for pre-marriage months

## STEPS 5 AND 6

PP. 340-342

- Step 5 - Fig. 10.13 compares the total alternative premium assistance to the regular premium assistance for the pre-marriage months
- Column A is \$5,418 and column B is \$4,487, line 14 is yes
- The family will benefit from this computation
- Step 6 - Fig. 10.14 shows Part V, Alternative Calculation for Year of Marriage supports the spouses' alternative monthly contribution amount

## STEPS 7 AND 8

P. 342

- Step 7 – Form 8962 lines 12-23 (Figure 10.15)
- Step 8 – Form 8962 lines 24-29 (Figure 10.15)

FIGURE 10.15  
Form 8962 – Save \$931 reduced to \$295

Monthly Calculation	(a) Monthly enrollment premiums (Form(s) 1095-A, lines 21-32, column A)	(b) Monthly applicable S/CSP premium (Form(s) 1095-A, lines 21-32, column B)	(c) Monthly contribution amount (amount from line 8b or alternative marriage monthly calculation)	(d) Monthly maximum premium assistance (subtract (c) from (b), if zero or less, enter -0-)	(e) Monthly premium tax credit allowed (smaller of (d) or (a))	(f) Monthly advance payment of PTC (Form(s) 1095-A, lines 21-32, column C)
12 January	1,500	1,266	492	774	774	794
13 February	1,500	1,266	492	774	774	794
14 March	1,500	1,266	492	774	774	794
15 April	1,500	1,266	492	774	774	794
16 May	1,500	1,266	492	774	774	794
17 June	1,500	1,266	492	774	774	794
18 July	1,500	1,266	492	774	774	794
19 August	1,350	1,167	625	542	542	573
20 September	1,350	1,167	625	542	542	573
21 October	1,350	1,167	625	542	542	573
22 November	1,350	1,167	625	542	542	573
23 December	1,350	1,167	625	542	542	573
24 Total premium tax credit. Enter the amount from line 11(e) or add lines 12(e) through 23(e) and enter the total here					24	8,128
25 Advance payment of PTC. Enter the amount from line 11(f) or add lines 12(f) through 23(f) and enter the total here					25	8,423
26 Net premium tax credit. If line 24 is greater than line 25, subtract line 25 from line 24. Enter the difference here and on Schedule 3 (Form 1040 or 1040-SR), line 9, or Form 1040-NR, line 65. If line 24 equals line 25, enter -0-. Stop here. If line 25 is greater than line 24, leave this line blank and continue to line 27					26	0
<b>Part III Repayment of Excess Advance Payment of the Premium Tax Credit</b>						
27 Excess advance payment of PTC. If line 25 is greater than line 24, subtract line 24 from line 25. Enter the difference here					27	295
28 Repayment limitation (see instructions)					28	2,650
29 Excess advance premium tax credit repayment. Enter the smaller of line 27 or line 28 here and on Schedule 2 (Form 1040 or 1040-SR), line 2, or Form 1040-NR, line 44					29	295

# REPAYMENT LIMITATIONS

P. 344

Fig. 10.16 repayment limits (Rev. Proc. 2019-44)

2020 Tax Returns	
Single Filing Status	Any Other Filing Status
\$325	\$650
\$800	\$1,600
\$1,350	\$2,700
No Limitation	No Limitation
Rev. Proc. 2019-44 (2019-47 I.R.B. 1093)	

## CHANGE IN CIRCUMSTANCES

P. 344

Report when circumstance change

- Household Income changes – lump sum payments or IRA withdrawals or unemployment
- Marriage or divorce
- Birth or adoption, death in family
- Change in coverage from government or employer plans
- Move to different address

NOTE: Consider using Tax Advocate Service web site calculator



## EDUCATION CREDITS AND LOANS



## ISSUE 3: TAX BENEFITS FOR EDUCATION EXPENSES P. 345

TP can claim tax benefits for payments of education expenses

- American opportunity tax credit
- Lifetime learning credit
- Deductions (expires end of 2020)
- Exclusions

## AMERICAN OPPORTUNITY TAX CREDIT

P. 345

TP can claim AOTC for self, spouse, or dependent

Maximum \$2,500 per eligible student, which is 100% of first \$2,000, and 25% of next \$1,000

Up to 40% of credit or \$1,000 is refundable unless the child subject to tax on unearned income \*\*\*\* changed for 2020\*\*\*\*

### Eligibility

In degree program

½ time for 1 academic period (all qualifying expense for entire year)

Not yet finished first four years of post-secondary schooling

Not have claimed AOTC for more than 4 years

No felony drug conviction

AOTC CONT.

P. 346



PRACTITIONER NOTE Graduate Students

Semester of undergrad senior year may still qualify for the entire year

Check IRS website for Q&A

### Income Limit

MAGI unmarried \$80,000 or less (MFJ less than \$160,000) then phased out at \$90,000 unmarried (\$180,000 MFJ)

MAGI- add back of foreign income exclusion, housing exclusion and deduction, American Samoa or Puerto Rico income exclusions

## AOTC QUALIFIED EXPENSES

P. 346

- Tuition
- Nonacademic fees required pay to school as condition of enrollment
- Books, supplies, and equipment

(OBSERVATION: Books and equipment don't have to be paid to the educational institution)

Expenses must be incurred for academic period that begins in tax year or first 3 months of the following year

Expenses cannot be paid with tax-free educational assistance or other credit/deduction amounts

## AOTC QUALIFIED EXPENSES CONT.

P. 348-9

Not room or board, transportation, medical

Include expenses paid by the student

## AOTC ELIGIBLE INSTITUTION

P. 346

Eligible Educational institution

Check Dept. of Education list

Claim the Credit

Institution reports on Form 1098-T Box 1

Boxes 8 and 9 reflect  $\frac{1}{2}$  time student, graduate student

P. 347 List of institutions not required to file Form 1098

Taxpayer files Form 8863

EX. 10.12

P. 347

Ella Easton lived at home and attend college in the fall

Tuition \$5,200

Books \$1,100 (TP's records)

Scholarship (\$2,000)

Net expenses \$4,300

Parents can claim max credit of \$2,500, refundable \$1,000

# EXAMPLE 10.12 CONT.

P. 347

## Ella's 1098-T

FIGURE 10.17 Form 1098-T

CORRECTED

FILER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone number  <b>State University</b> <b>1234 University Drive</b> <b>College Town, USA 12345</b>		<b>1</b> Payments received for qualified tuition and related expenses <b>\$ 5,200.00</b> <b>2</b>	OMB No. 1545-1574  <div style="font-size: 2em; font-weight: bold; text-align: center;">2020</div> Form <b>1098-T</b>	<b>Tuition Statement</b>
FILER'S employer identification no. XX-XXXXXXX	STUDENT'S TIN XXX-XX-XXXX	<b>3</b>		<b>Copy B For Student</b>  This is important tax information and is being furnished to the IRS. This form must be used to complete Form 8863 to claim education credits. Give it to the tax preparer or use it to prepare the tax return.
STUDENT'S name  <b>Ella Easton</b>		<b>4</b> Adjustments made for a prior year <b>\$</b>	<b>5</b> Scholarships or grants  <b>\$ 2,000.00</b>	
Street address (including apt. no.)  <b>890 Stratford Road</b>		<b>6</b> Adjustments to scholarships or grants for a prior year <b>\$</b>	<b>7</b> Checked if the amount in box 1 includes amounts for an academic period beginning January–March 2021 <input type="checkbox"/>	
City or town, state or province, country, and ZIP or foreign postal code  <b>College Town, USA 12345</b>		<b>8</b> Check if at least half-time student <input checked="" type="checkbox"/>	<b>9</b> Checked if a graduate student <input type="checkbox"/>	
Service Provider/Acct. No. (see instr.)		<b>10</b> Ins. contract reimb./refund <b>\$</b>		

Form **1098-T**
(keep for your records)
[www.irs.gov/Form1098T](http://www.irs.gov/Form1098T)
Department of the Treasury - Internal Revenue Service



## EXAMPLE 10.12 CONT., EXAMPLE 10.13

PP. 348-350

Ella's parents file Form 8863 (Figure 10.18)

Example 10.13

Same facts, but AGI is \$172,000

In phaseout range – max is \$1,000

## AMERICAN OPPORTUNITY TC

P. 350

### Credit Recapture

If refund or tax-free assistance in subsequent year,  
report the refund in the subsequent year

### Ex. 10.14 AOTC Recapture

Sandra paid \$7,000 for Matthew's tuition and claimed a \$2,500 credit on her 2020 return. In 2021, she received a \$4,000 refund. She recalculates her credit to be \$2,250

Include \$250 on 2021 return

## LIFETIME LEARNING CREDIT

P. 350

Credit has no limit for the number of years TP can claim

Maximum yearly credit is \$2,000 (20% of first \$10,000)

Credit only offsets tax, not refundable

Who is eligible – TP, spouse, or dependent

Courses to acquire or improve job skills or get a degree

Ex. 10.15 Esther took classes to keep her real estate license and James, her son, got a loan to cover his tuition. She can claim a \$1,000 lifetime learning credit (20% of \$5,000). Or she can take \$2,125 AOTC and her own lifetime learning credit of \$300.

## LIFETIME LEARNING CREDIT CONT. PP. 350-351

Phaseout begins at \$59,000 (\$118,000 MFJ)\*\*\*2020 changed\*\*\*

Qualified expenses are tuition and related expenses

The expenses must be paid to the institution for enrollment

Only payments in the current year

Not eligible for any other exclusion, credit, or deduction

Report on Form 8863

Subsequent refund must recapture credit just like AOTC

## EDUCATION DEDUCTIONS

P. 351

If credit is not available or not elected, TP may claim a deduction

Student Loan Interest (\*\*NOT EXTENDED for 2021\*\*)

\$2,500 of qualified student loan interest – adjustment to AGI

Includes required and voluntary interest



NOTE:

CARES Act suspended temporarily payments  
from March 13 – Sept. 30, 2020.

## STUDENT LOAN INTEREST DEDUCTION

PP. 351-352

Eligibility (\*\*FSFA rules have changed for 2021\*\*)

TP must be legally required to repay qualified loan

Loan must be for a degree program, ½ time enrollment

TP cannot be a dependent, not MFS, or nonresident alien

Income limits

Phase out between \$70,000 and \$85,000 (\$140,000 to \$170,000 MFJ)

## QUALIFIED EDUCATION LOAN

P. 352

At the time of the loan, it must be used by TP, spouse, or dependent

Diff. criteria for dependent

Expenses must be incurred within a reasonable time

No loans from related parties, including corporations or partnerships owned directly or indirectly by TP

Qualified expenses are tuition, fees, books, supplies, equipment, transportation

Room and board, limited to federal financial aid amounts or actual amount charged by the school

## QUALIFIED INTEREST

PP. 352-353

Simple interest, loan origination fees that are not for property or services, and capitalized interest



### NOTE

Credit card interest if used only for qualified expenses, borrower secures W9-S, Request for Borrower's TP ID #

Loan Origination Fee – when made for use of money, not services, include ratably over payments on the loan

Capitalized Interest –Added to loan and deductible when paid



# CLAIMING STUDENT LOAN INTEREST DEDUCTION P. 353

Lender sends Form 1098-E Figure 10.19

TP reports on Form 1040 Schedule 1 (limited to \$2,500)

CORRECTED (if checked)

RECIPIENT'S/LENDER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone number		OMB No. 1545-1576  <span style="font-size: 2em; font-weight: bold;">2020</span>  Form 1098-E	<p style="text-align: center;"><b>Student Loan Interest Statement</b></p> <p style="text-align: center;"><b>Copy B For Borrower</b></p> <p style="font-size: 0.8em;">This is important tax information and is being furnished to the IRS. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if the IRS determines that an underpayment of tax results because you overstated a deduction for student loan interest.</p>
RECIPIENT'S TIN	BORROWER'S TIN	<b>1</b> Student loan interest received by lender \$	
BORROWER'S name  Street address (including apt. no.)  City or town, state or province, country, and ZIP or foreign postal code		<b>2</b> If checked, box 1 does <b>not</b> include loan origination fees and/or capitalized interest for loans made before September 1, 2004. <input type="checkbox"/>	
Account number (see instructions)			
Form <b>1098-E</b> (keep for your records)		www.irs.gov/Form1098E	Department of the Treasury - Internal Revenue Service

## EXAMPLE 10.16

P. 354

Rachel has \$27,500 student loan. Payments of \$285 per month start in November 2020. No 1098-E required because payment is under \$600

Stated interest	\$170
Loan origination fee	\$ 2
Capitalized interest	<u>\$198</u>
Total deduction	\$570

## LIMITS ON STUDENT LOAN INTEREST DEDUCTION

P. 354

Cannot claim if amounts otherwise deductible or tax-free i.e. Sec. 529 Plans

If paid for qualified higher education expenses, not subject to tax

Expanded to elementary or secondary schools up to \$10,000

SECURE Act adds apprenticeships

Update to text – SECURE Act **homeschooling expenses not** in the final law

Beneficiaries cannot deduct the interest on student loans

Employer Payment of Student Loans per written plan

Not included in employee's income and no interest is deductible

## TUITION AND FEES DEDUCTION

P. 355

### Eligibility

TP, spouse, or dependents

- Cannot file MFS
- Not if claimed by another person
- MAGI single \$80,000, joint \$160,000
- Cannot be a nonresident alien
- No education credit for the same expenses

MAGI for deduction of tuition and fees- AGI exclude tuition deduction and add foreign income see Fig. 10.20 (P. 356)

## WORK RELATED EDUCATION

P. 355

Deduction for classes that improve or maintain skills

Not to qualify for new trade or business

Education credit or deduction, but not both

Tuition and Fees Deduction

Deduction (adjustment to AGI) up to \$4,000 on **Form 8917**, Form 1040  
Schedule 1

Deduction expires 12/31/2020

FIGURE 10.20

P. 356

**FIGURE 10.20 Income Limit for Tuition and Fees Deduction**

<b>If the filing status is</b>	<b>And MAGI is</b>	<b>Then the maximum tuition and fees deduction is</b>
Single, head of household or qualifying widow(er)	not more than \$65,000	\$4,000
	more than \$65,000 but not more than \$80,000	\$2,000
	more than \$80,000	\$ 0
Married filing joint return	not more than \$130,000	\$4,000
	more than \$130,000 but not more than \$160,000	\$2,000
	more than \$160,000	\$ 0

# FIGURE 10.21

P. 356

Who can claim the deduction

**FIGURE 10.21 Claiming the Student as a Dependent**

<b>If your dependent is an eligible student and you</b>	<b>and</b>	<b>then</b>
claim your dependent on your tax return	you paid all qualified education expenses for your dependent	only you can deduct the qualified education expenses that you paid. Your dependent cannot take a deduction.
claim your dependent on your tax return	your dependent paid all qualified education expenses	no one is allowed to take a deduction.
do not claim your dependent on your tax return	you paid all qualified education expenses for your dependent	no one is allowed to take a deduction.
do not claim your dependent on your tax return	your dependent paid all qualified education expenses	no one is allowed to take a deduction.

## TUITION & FEES DEDUCTION

P. 356

Ex. 10.17 Elizabeth paid \$4,500 tuition for her daughter who meets the dependent tests. Elizabeth files as head of household and MAGI is \$55,000. She can claim the \$4,000 tuition and fees deduction.



### Planning Pointer

Deduction reduces AGI. Could increase financial aid eligibility, qualify for more EIC, or other tax benefits limited by AGI.



## EMPLOYER PROVIDED EDUCATION BENEFITS

P. 357

Employer's plan may exclude education benefits from employee's income

Limited to \$5,250 per year

Non-discrimination

Limits on owner & related parties

Undergraduate or graduate education

Sports and games if reasonable relationship to employer's business or required as part of the degree program

CARES expanded exclusion to student loan interest & principal paid by employer after March 27, 2020 before Jan.1 2021

## DISCHARGE OF STUDENT LOAN DEBT & REPAYMENT ASSISTANCE

P. 357

Exception to gross income inclusion of discharge of indebtedness  
– certain student loans

Cancellations of qualified debt by qualified lender due to

- Death or total disability
- Canceled in return for services for a length of time for certain professions
- School closed

Eligible institution – Regular faculty, curriculum, student body engaged in education

## DISCHARGE OF STUDENT LOAN DEBT & REPAYMENT ASSISTANCE CONT.

P. 357

### Qualified lenders

- a. Government
- b. State or division of the state
- c. Sec. 501(c)(3) hospital whose employees are public employees
- d. Educational institution
  - a. part of agreement with those listed above
  - b. program to encourage students to work in underserved areas
- e. Private lender if loan is cancelled due to death or disability

## LENDER RECEIVES SERVICES

PP. 357-358

Cancellation of loan because of services performed for the lender must be included in borrower's gross income

See Financial Distress chapter for other exclusions that may apply

## SCHOOL CLOSURE

P. 358

Since 2015 various schools have closed leaving students with loans but benefits were not received

If the student was attending the school or withdrew shortly before, the cancelled debt does not have to be recognized in income

## STUDENT LOAN REPAYMENT ASSISTANCE

P. 358

Borrower does not recognize income when repayments are made by

- National Health Service Corps Loan Repayment Program
- State repayment under Public Health Services Act
- Any other state loan repayment program to increase health services in areas w/ shortage

## FINANCIAL AID

P. 358

Scholarships, grants, tuition reduction

Taxable vs non-taxable depends how money is used

Scholarships and Fellowships

Scholarship allows student to attend to study

Fellowship is for research purposes

Either covers tuition and related expenses and may cover room and board or family allowance

Qualified scholarships and fellowships are excludable

## FINANCIAL AID CONT.

PP. 358-359

Scholarships and fellowships not excluded if

- Amount exceeds eligible costs
- Amount is designated for nonqualified expenses (room and board)
- Amount is payment for teaching or research activities

Unless from listed organization with work-learning-service program



## EX. 10.18

P. 359

Justin received \$14,500 scholarship

Tuition 11,500

Books 1,500

Car exp. 1,500

Total 14,500

He lived at home and earned \$9,400

\$13,000 for tuition and books excluded

Add \$1,500 to wages



NOTE: Qualifies for dependent's standard deduction

Only qualifies for EIC if W-2 lists the amount

## GRANTS

P. 359

Awarded because of financial need

Pell Grants do not have to be repaid

If allocated to living expenses, then it must be included in taxable income

If allocated to tuition etc., then education credits are not allowed

Ex. 10.19

Walter, age 25, received \$2,625 grant and \$3,000 scholarship = \$5,675

Allocate \$5,200 to tuition, net taxable \$475 and no credit

Instead allocate to living expenses, include in income but eligible for credit

## HIGHER EDUCATION EMERGENCY RELIEF

P. 360

CARES Act allows higher ed institutions funds to support students with financial needs related to coronavirus pandemic

Student can receive qualified disaster relief payments - not taxable

No credits or deductions for the expenses paid with this money

NOTE: Emergency grants from Dept. of Ed not taxable, no deduction for expense covered



## TUITION REDUCTIONS

P. 360

Colleges and universities offer reduced or free tuition as a non-taxable fringe to employees and retirees

Undergraduate students get exclusions from income if

- Current employees

- Disabled former employees

- Retired employees

- Surviving spouses of eligible employee (current and former)

- Current spouse and dependents of eligible employees

- Children under 25 qualify if parents divorce or are deceased

## TUITION REDUCTIONS CONT.

P. 360

Graduate students who teach or do research qualify for exclusion

Paid wages, report in income

Work Study Jobs

Wages paid are taxable compensation

If employed by school where enrolled are generally exempt from social security and Medicare

Off-campus work are subject to social security and Medicare, even if receive academic credit

QUESTIONS?

# 2020 NATIONAL INCOME TAX WORKBOOK

CHAPTER 8: RETIREMENT AND  
INVESTMENT ISSUES P. 261



IRA HOLDINGS – NOT COVERED IN BOOK

**Master limited partnerships (MLPs) in an IRA.**

Vanguard, custodian for IRAs, is responsible for IRS Form 990-T tax filings for MLPs.

They will begin charging a \$300 fee per account for these filings.\*\* Vanguard will deduct the fee from a client's brokerage account when a filing is required.



Here's a "Closer Look" at some of the special services...

### Helping People: IRS Taxpayer Relief Initiatives

- The IRS is highlighting reasonable cause assistance available through IRS procedures for failure to file, failure to pay and failure to deposit penalties. First time abatement relief is also available for the first time a taxpayer is subject to one or more of these tax penalties.
- For individual taxpayers receiving notices (letters about a tax bill) with tax liabilities up to \$250,000 for Tax Year 2019 only, the IRS can offer one Installment Agreement opportunity with no lien filed.
- The IRS is extending the short-term payment plan timeframe to 180 days (normally 120 days).
- The IRS is easing paperwork requirements to allow individuals more flexibility to get non-streamlined Installment Agreements up to \$250,000 without financial verification, if their case is not yet assigned to a revenue officer.
- Extend guidance to automatically include new tax year balances accrued in existing Installment Agreements. (Individuals and Out of Business entities only)
- The IRS will provide relief for taxpayers having difficulty meeting the terms of previously accepted offers.

COVID RELIEF FROM COLLECTION BY IRS 11/2/2020

## CHAPTER 8 RETIREMENT & INVESTMENT TOPICS

Issue 1: Required Minimum Distributions

Issue 2: IRA Beneficiary Designations

Issue 3: Early Distributions

Issue 4: Qualified Charitable Distributions

Issue 5: Investments

Appendix A: Stimulus Relief Resources

## INTRODUCTION

SECURE Act encourages retirement savings & helps employers offer retirement plans to employees

CARES Act, reduces COVID-19 impact by makes short-term changes to RMDs and access to retirement funds.

Taxation of investment options to mitigate stock market volatility.

## ISSUE 1: REQUIRED MINIMUM DISTRIBUTIONS

P. 262

For 2020 the age is **72** for beginning date of RMDs

- April 1 of calendar year following the later of the calendar year in which the employee turns 72, or retirement year
- If owner dies, & spouse inherits account, distributions must start when employee would have turned 72
- 2020 applies to RMDs made after 12/31/19 for individuals turning 70 ½ after that date (birth date **July 1, 1949**)
- See Law Change box - transition rules **Notice 2020-51**.

## FIRST YEAR RMD PLANNING

P. 262

For 2020 **no RMD** discussed later (COVID related), not during 2020 or by April of 2021

Rules revert for 2021 for owner who turns 72, can take first RMD until April 1 of next year However, individual must take 2 RMDs in second year; first delayed distribution & “regularly” scheduled RMD 2<sup>nd</sup> year.

If employee has **defined benefit** plan and continues to work, RMD is delayed until later of turning 72 or retirement year

## POLLING QUESTION 1 CGW PM CH 8

For 2020, the Required Minimum Distribution (RMD) was cancelled?

Yes

No

## MAXIMUM AGE TO MAKE IRA CONTRIBUTIONS P. 263

- Beginning in 2020 there is **no maximum age** for traditional IRA contributions
- COMPENSATION
- Taxable compensation paid to individuals pursuing graduate or postdoctoral studies, can be used as income to make IRA contributions after 12/31/19

## RMD CONSIDERATIONS

P. 263

Penalty for failing to take an RMD is 50% of required amount required to be distributed but was not actually distributed.

- The IRS can waive this penalty for good cause: illness, old age, memory problems, trustee fails to send a reminder, etc. (IRM)

**No RMD in 2020** for anyone.

- This provision waives RMDs for lifetime distributions to employees, IRA owners, & beneficiaries after death of owner.
- Next RMD is required for calendar year 2021.



## RMD CONSIDERATIONS CONTINUED

PP. 263-264

NO required distribution for beginning date in 2020

- Turn 72 in 2020, no RMD required by April 1, 2021 per CARES Act  
Now first RMD by 12/31/21 or April 2022
- Death of Owner –Extension of 5-year period
- 2020 doesn't count, e.g. death in 2018, 5-year period ends in 2024, not 2023.

Eligible Rollover Distributions

- For eligible rollover distributions from qualified plans in 2020, the 20% withholding is waived.
- INSERT RMD tables will have longer life expectancy in 2022 T.D.9930

## CALCULATING RMDS – NONE FOR 2020

P. 264

RMDS per Joint Life and Last Survivor Expectancy Table (Table II) if spouse is sole beneficiary, & > 10 years younger than account owner.

RMDS per Uniform Lifetime Table (Table III) if spouse is not the only beneficiary or if spouse is not more than 10 years younger.

### Example 8.1 Calculating the RMD

- Faye Goodman, turns 73 Oct. 15, 2020. She has \$255,000 in her IRAs. Her RMD is \$10,324 ( $\$255,000 / 24.7$ ) Using Table III

## ISSUE 2: IRA BENEFICIARY DESIGNATIONS

P. 266

Beneficiary of a retirement account can be any person or entity account holder chooses *If none, 5 years.*

Prior law, beneficiaries could withdraw amounts from inherited accounts over lifetime of beneficiary

The 2020 SECURE Act shortens time period allowed for withdrawal of inherited IRA. These rules apply to all defined contribution plans i.e. qualified retirement, 403(b), and 457(b) plans. Only Defined Benefit plans are exempted.

## DESIGNATING THE SURVIVING SPOUSE

P. 266

Calculation important. Three choices. Best if converted to own IRA if younger than descendant

- Treat IRA as beneficiary's own and become the account owner
- Treat IRA as beneficiary's own and roll it over to a traditional IRA or other deferred tax retirement plan (see list on Page 266)
- Treats him/herself as the beneficiary of IRA

## SPOUSAL ELECTION

P. 266

Surviving spouse may elect to treat spouse's entire interest as a beneficiary in an individual's IRA (the decedent) as the spouse's own IRA.

- This may be a wise choice if the surviving spouse is younger than the IRA owner because the surviving spouse is not required to take an RMD until age 73.
- Example 8.2 Later RMD Start Date
  - Jennifer dies in 2020, she was 68. Melissa, Jennifer's wife was designated beneficiary and is 60 years old.
  - With spousal election Melissa can use April **2033 after** she turns 72,
  - Rather than April 1, 2025 when decedent would have turned 72 **(2025)**.

## SPOUSAL ELECTION: LONGER DEFERRAL PERIOD PP. 266-267

The spousal election allows the surviving spouse to use Table III, thus a longer deferral period.

- Example 8.3 Longer Deferral Period
- Frank elects to treat inherited IRA from his wife as his own, therefore, his RMD is \$6,818 as compared to \$11,811 if he treated the IRA as if he was the beneficiary.

## SPOUSAL ELECTION CONSIDERATIONS

P. 267

Requirements: Sole beneficiary, unlimited right to withdraw

Effect of Election - Early distribution penalty applies if the surviving spouse treats IRA as his/her own & distributions occur before age of 59  $\frac{1}{2}$  years See Planning Pointer

Making the Election

- Redesignate inherited account in name of surviving spouse, or if
  - The amount in the IRA is not distributed within the RMD time period
  - The surviving spouse makes contribution to the IRA

## SPOUSAL ROLLOVER

PP. 267-269

If the surviving spouse receives a distribution (other than an RMD) it can be rolled into the surviving spouse's IRA.

- Must be done within 60 days (See discussion on page 268)
- May postpone RMDs

### Example 8.4 Estate as Sole Heir

- Barry Brooks did not designate a beneficiary on his IRA. Betty Brooks, his wife, was personal representative and sole beneficiary of Barry's estate.
- Effectively, Betty is the only beneficiary, and thus may rollover any distribution to her IRA.
- Waiver of the 60-day requirement if beyond reasonable control



## SPOUSAL ROLLOVER

PP. 268-269

Spouse as Beneficiary -Begin RMDs by the later of

- 12/31 of year following year of death, or
- 12/31 of the year in which the decedent would have turned age 72 had he or she lived
- Example 8.5 Distributions over Surviving Spouse's Life Expectancy
  - Spouse as beneficiary, revisit Example 8.3
  - Frank, calculates the RMD based on Table I and must take \$11,811 ( $\$150,000 / 12.7$ )

## ELIGIBLE DESIGNATED BENEFICIARIES

P. 270

Starting in 2020 if employee or IRA owner dies before distributions; the account must be distributed to beneficiaries within **10 years of date of death.**

Except for eligible beneficiary: No 10-year rule for

- Surviving spouse of the employee or IRA owner
- Child of the employer or IRA owner who has not reached majority (age 18)
- Disabled within the meaning of I.R.C. § 72(m)(7)
- Chronically ill individual
- Individual who is not more than 10 years younger than the employee or IRA owner.
- Example 8.6 Death of Eligible Designated Beneficiary

## OTHER BENEFICIARIES

P. 270

Within 10 years of D.O.D., qualified retirement account or IRA must be distributed in total

See chapter for discussion of “see-through trust.”

## OTHER ISSUES TO CONSIDER

PP. 271-272

### No Designated Beneficiary

- No changes were made by the SECURE Act. Entire account must be distributed **within 5 years** of date of death if owner had not started distributions, or life expectancy of decedent if distributions had started

### Charitable Remainder Trust as Beneficiary

- Requirements of the CRT; Taxation of the CRT; CRT Reporting  
CRT as Beneficiary of IRA – can pay income over the life of the beneficiary
- **Planning Pointer** Charitable Beneficiaries – from IRA

## ISSUE 3: EARLY DISTRIBUTIONS

PP. 272-273

General Rule-If under 59 ½ years old, then a 10% penalty applies (unless there is an exception)

- Example 8.7 shows penalty fact and then the Roth treatment
- If ROTH, then no penalty if contributions were withdrawn after 5 years- Contributions first

◦ NOTE: NOT in text.

Remember Roth 401 (k) is not an IRA. If taxpayer rolls 401 (k)Roth over tax free to IRA Roth, 5 years starts on the date of transfer.

Do not go mingle the funds with an old Roth IRA.


## COVID ONLY EARLY DISTRIBUTIONS FORM 8915-E

PP. 272-273

**Coronavirus-Related** Distributions – **No Penalty** for early withdrawal

- CARES Act waives 10% penalty to maximum is \$100,000 for coronavirus-related withdrawals. January 1, 2020 to December 31, 2020
- TP, spouse, or dependent diagnosed with COVID-19
- Experiences adverse financial consequences (Cross-Reference Notice 2020-50 for others)
- Included income ratably over 3-tax years (unless elect out)

# COVID 19 – QUALIFIED 2020 DISASTER DISTRIBUTION FROM RETIREMENT

Form <b>8915-E</b> Department of the Treasury Internal Revenue Service	<b>Qualified 2020 Disaster Retirement                  Plan Distributions and Repayments</b> (Use for Coronavirus-Related Distributions) ▶ Go to <a href="http://www.irs.gov/Form8915E">www.irs.gov/Form8915E</a> for instructions and the latest information. ▶ Attach to 2020 Form 1040, 1040-SR, or 1040-NR.	OMB No. 1545-0074 <b>2020</b> Attachment Sequence No. <b>915</b>
Name. If married, file a separate form for each spouse required to file 2020 Form 8915-E. See instructions.		Your social security number
<b>Fill in Your Address Only                  if You Are Filing This                  Form by Itself and Not                  With Your Tax Return</b>	Home address (number and street, or P.O. box if mail is not delivered to your home)	
	City, town or post office, state, and ZIP code. If you have a foreign address, also complete the spaces below (see instructions).	
	Foreign country name	
	Foreign province/state/county	Foreign postal code
Apt. no.		
If this is an amended return, check here <input type="checkbox"/>		
<b>Before you begin:</b> <ul style="list-style-type: none"> <li>• Complete 2020 Form 8915-D, Qualified 2019 Disaster Retirement Plan Distributions and Repayments, and 2020 Form 8915-C, Qualified 2018 Disaster Retirement Plan Distributions and Repayments, if applicable.</li> <li>• If you completed Part I of 2020 Form 8915-D, or of 2020 Form 8915-C, see the Caution in Column (a) in the instructions to figure the amounts for column (a).</li> </ul>		
<b>Part I Total Distributions From All Retirement Plans (Including IRAs).</b>		
Complete lines 1 through 4 of one column before going to the next column.		
 <b>CAUTION</b>	Form 8915-E only covers 2020 coronavirus-related distributions. The distribution must be made before December 31, 2020. See instructions.	
(a) <b>Total distributions                  in 2020</b> (see instructions)	(b) <b>Qualified                  2020 disaster                  distributions                  made in 2020</b>	(c) <b>Allocation of                  column (b)</b> (see instructions)

## FORM 8915 – E APPLIES FOR 2020

Part I is for 2020 withdrawals; Part III is for those from IRAs

No penalty for first \$100,000. Any excess follows regular rules.

Part II is for regular pension withdrawals. Include in income over 3 years unless elects out on this form.



17 If you elect NOT to spread the taxable amount over 3 years, check this box  and enter the amount from line 16 (see instructions). You must check this box if you checked the box on line 9. Otherwise, divide line 16 by 3.0 . . . . . 17

If taxpayer previously had prior year qualified disaster withdrawals, form 8915 A-D are required. Follow instructions for applicable old years. Generally Michigan taxpayers didn't have many federally declared disaster areas.

The example in the instructions is a family from Texas which had qualified disasters in the last 3 years.



## EARLY DISTRIBUTION EXCEPTIONS FOR IRA

PP. 273-274

Beneficiary

Higher-Education Expenses

Disabled

First-Time Homebuyer

Substantially Equal Payments

Qualified Reservist

IRS Levy

\*Birth or Adoption of a Child\*

Unreimbursed Medical Expenses

Medical Insurance for Unemployed Person

## QUALIFIED PLAN PENALTY EXCEPTIONS

P. 274

Beneficiary

Disabled

Substantially Equal Payments

IRS Levy

Unreimbursed Medical Expenses

Qualified Reservist

\*Birth or Adoption of a Child\* same rules as IRA

## OTHER QUALIFIED PLAN EXCEPTIONS

P. 275

Only for qualified plans (not IRAs)

- Distribution made after employee separation and 55 or older (50 if public safety employee)
- \*\*\* COVID 2020 expanded application of 55 defined benefit for construction workers\*\*\*
- Distribution made to alternate payee under a QDRO
- Distribution of dividends from employee stock ownership plan

## OTHER QUALIFIED PLAN EXCEPTIONS

P. 275

### Qualified plans (not IRAs) penalty

- Example 8.8 Qualified Plan Distribution for Educational Purposes
- Ellie, age 52, takes \$5,000 from 401 (k) to pay for qualified education expense for her son. However, this is not an exception for her 401 (k) and she is subject to a \$500 penalty plus income tax.

Several acts, beginning in early 2017, address disaster relief and allow distributions, exempt from the 10% penalty, up to \$100,000.

Distributions are included in taxable income over 3 years.

Plan participants may repay the distribution back to the plan within 3 years; the repayment is treated as a trustee-to-trustee transfer.

## CALCULATING THE PENALTY

P. 275

The penalty for early withdrawal is 10%. The taxpayer uses IRS Form 5329, Part 1 to make the calculation. The penalty is in addition to any income tax on the withdrawal.

### Example 8.9 Early Distribution Penalty with Exception

- Barbara, 40, withdraws \$8,400 from her IRA. Barbara pays \$6,000 of tuition remaining after a scholarship & buys a car with the remaining \$2,400.
- Barbara is subject to the early withdrawal penalty (\$240) on the amount used for the car because it is not a qualified education expense.

## ISSUE 4: QUALIFIED CHARITABLE DISTRIBUTIONS P. 276

A qualified charitable distribution (QCD) is transferred directly from an IRA to a qualified charity & satisfies RMD requirement

A QCD allows an IRA owner who is **at least 70 ½** years old to contribute up to **\$100,000** from the IRA to the charity without paying federal or state income tax on distribution.

The IRA owner does not receive a charitable contribution deduction (no double dipping).

List of 6 benefits of a QCD – Not taxed by state of Michigan

## POLLING QUESTION 2 CAROL PM CHAPTER 8

Qualified Charitable Distributions ( QDC) can be made from a traditional IRA at the age of 70 ½ years. It can be made out to the owner who gives the cash to the charitable organization.

YES

NO



## QUALIFIED CHARITABLE ORGANIZATION

PP. 276-277

List in text or see IRS.gov Publication 78

Irs.gov Tax Exempt Organization Search

501(c)(3) orgs

War veterans' orgs

Domestic fraternal societies(if nonprofit purpose)

Certain nonprofit cemetery companies or corporations

The United States, or political division or an Indian tribal government or its subdivisions (with funds used for public purposes)

## PROCEDURE TO DONATE A QCD

P. 277

Owner of the IRA requests the IRA trustee to make the QCD. Trustee writes a check to the qualified organization.

Owner will receive a 1099-R and reports the distribution on 1040, line 4a and writes "QCD" beside line 4b and reports \$0.

Note, married couples, filing jointly, may exclude up to \$100,000 each.

### Example 8.10 Claiming the QCD

- Myron requested the QCD to be issued by the trustee of his IRA to the charity. Myron delivered the check to the charity. Myron's RMD qualified as a QCD because the check was written to the charity.

## ELIGIBLE IRAS

P. 277

Traditional IRAs qualify as contributions deductions have been taken. IRAs where the owner has basis, because the deduction was disallowed in the year of the contribution also are eligible.

ROTH IRAs are eligible, but only to the amount of earnings. Why?

SEPs and SIMPLE IRAs are not eligible for a QCD.

Example 8.11 Nondeductible IRAs No law change.

- Nancy requests a \$25,000 QCD from her IRA. Value of IRA at time of donation was \$30,000 with \$10,000 basis. Reports \$20,000 on Line 4(a) and \$0 on Line 4(b). Using form 8606, she may be able to take \$5,000 charitable donation on Schedule A for the remainder.
- **Note Law Change** (P. 278) \$300 above the line deduction for non-itemizers

## STATE OF MICHIGAN TAXATION OF PENSIONS P. 64

Taxpayers born  
after 1952  
(Tier 3)  
before the taxpayer reaches age 67

- Social Security is exempt.
- Railroad and Michigan National Guard pensions are exempt.
- Military compensation and pensions are exempt.
- Not eligible for the senior citizen subtraction for interest, dividends, and capital gains.
- Not eligible for public or private pension subtraction.
- At age 62, pensions from employment with governmental agencies not covered by the SSA. \$15,000 for single or joint filer or \$30,000 for joint filers if both spouses worked for an "uncovered" agency.

- Beginning in 2018, pension from employment with governmental agencies not covered by the SSA for persons retired as of January 1, 2013, \$35,000 for single filer, \$55,000 for joint filer, or \$70,000 for joint filers if both spouses worked for an "uncovered" agency.

All people born before 1953 are already 67. The middle tier will be on the next page

# STATE OF MICHIGAN BOOK PAGE 65

Tier 2 After the taxpayer reaches Age 67	Tier 3 After the taxpayer reaches Age 67
<ul style="list-style-type: none"> <li>• Social Security is exempt.</li> <li>• Railroad and Michigan National Guard pensions are exempt (see below).</li> <li>• Military compensation and pensions are exempt (see below).</li> <li>• Not eligible for the senior citizen subtraction for interest, dividends, and capital gains.</li> </ul> <p>Eligible for <b>Standard deduction</b>:</p> <ul style="list-style-type: none"> <li>• Subtraction against all income of \$20,000 for single filers and \$40,000 for joint filers.</li> <li>• Subtraction increased to \$35,000 for single filers and \$55,000 for joint filers with pensions from employment with governmental agencies not covered by the SSA, or</li> </ul>	<ul style="list-style-type: none"> <li>• Not eligible for the senior citizen subtraction for interest, dividends, and capital gains.</li> <li>• Not eligible for public or private pension subtraction.</li> <li>• Income exemption election:               <ul style="list-style-type: none"> <li>- Elect exemption against all income of \$20,000 for single filers or \$40,000 for joint filer</li> </ul> </li> </ul> <p><b>Note:</b> No exemption for Social Security, Military compensation and pension, and Railroad/Michigan National Guard pension. No personal exemptions.</p> <p><b>OR</b></p>

Tier 2

Tier 3

- Subtraction increased to \$35,000 for single filers and \$55,000 for joint filers with pensions from employment with governmental agencies not covered by the SSA, or to \$70,000 for joint filers if both spouses worked for an "uncovered" agency.
- Not eligible for this income subtraction to the extent Military income and Railroad/Michigan National Guard pension exemption are claimed.

Railroad/Michigan National Guard pension. No personal exemptions.

**OR**

- Elect to exempt Social Security, Military compensation and pension, and Railroad/Michigan National Guard pension. May claim personal exemptions.

- Beginning in 2018, persons retired as of January 1, 2013 and receiving pension from employment with governmental agencies not covered by SSA may claim standard deduction of \$35,000 for single filer, \$55,000 for joint filer, or \$70,000 for joint filers if both spouses worked for an "uncovered" agency.

## **ISSUE 5: INVESTMENTS**

P. 278-291

When the stock market is volatile, investors may look elsewhere to diversify their investment holdings to mitigate risk.

Savings Accounts, Savings Bonds, Mutual Funds

This issue discusses alternative investments and how these are taxed, and the reporting of taxable income generated by these investments. Also Expense & Interest

## INTEREST-BEARING BANK ACCOUNTS

PP. 278-279

Banks, credit unions and others use Form 1099-INT to report interest to the owner of the account.

Partnerships, LLCs and Sub-s corporations may report pro rata interest earnings on business accounts to the owners on Schedule K-1.

Schedule B is used if the taxpayer received over \$1,500 of interest income.

- Additionally, there are 7 circumstances where the taxpayer must attach Schedule B.
- See **Practitioner Note** – Called dividends but may be interest
- Gifts may be includible as interest: See Example 8.12 Gift for Opening Account

## CERTIFICATES OF DEPOSIT (CDS)

P. 279

A CD is a federally insured savings account paying a premium interest rate with a fixed date of withdrawal.

If the CD is withdrawn prior to the maturity date a penalty typically is imposed.

If CDs pay interest annually or more frequently, the taxpayer reports the income when received.

If the CD has a term of longer than one year, the taxpayer includes in income each year the part of total interest due that year as OID. The issuer of the CD typically reports OID interest to the owner.

Depending on the MAGI of the taxpayer, interest may be subject to NIIT.



## US SAVINGS BONDS

PP. 279-280

US Savings Bonds are low risk savings instruments. Typically, the owner reports the interest when the bonds are cashed in.

Bond owners using the accrual method of accounting report each year's interest as it accrues.

### Types of Savings Bonds

- HH, no longer issued, but last ones will mature in 2024, interest paid 2x /yr, direct deposit
- EE Bonds, issued at face value, interest paid upon redemption, penalty for early cashing out.
- I Bonds, inflation indexed bonds, face value plus interest at maturity, penalty for early cash out

## SAVINGS BOND INTEREST INCOME

P. 280

Interest on Series EE and Series I bonds is payable when the taxpayer cashes the bond.

The difference between the purchase price and the redeemed value is the taxable interest income.

Two methods allowed for reporting of income

- Postpone reporting of interest until the bond is cashed or disposed of, or the year of maturity.
- Taxpayer chooses to report increase in value annually.

The same method must be used for all Series EE and Series I bonds.

**Practitioner Note regarding exclusion for education savings**

## INTEREST INCOME CONTINUED

P. 281

### Changing Reporting Method

- IRS allows, without asking for permission, a change from method 1 to method 2.
- IRS requires permission for changing from method 2 to method 1. Permission is usually granted automatically if a statement is attached with 5 required items.

### Child as Owner

- Interest on US savings bond bought for and registered in the name of a child is the income of the child.
- Example 8.13 Children as Owners of Bonds – Method 2

# JOINT OWNERSHIP OF US SAVINGS BONDS

P. 282

**FIGURE 8.3 Who Pays the Tax on Savings Bond Interest Income**

Ownership	Who Owes the Tax
The purchaser is the only owner of the bond	The purchaser
The purchaser purchases a bond and puts it in the name of the purchaser and the co-owner	The purchaser
The purchaser purchases a bond and puts it in someone else's name as the only owner	The person who is named as the owner
The purchaser and another person buy a bond together and are both named as co-owners	Each purchaser reports interest in proportion to the amount he or she paid for the bond
The purchaser and his or her spouse live in a community property state, buy a bond that is community property, and file separate tax returns	Each spouse reports one-half the interest

Source: [www.treasurydirect.gov/indiv/research/indepth/ebonds/res\\_e\\_bonds\\_eetaxconsider.htm](http://www.treasurydirect.gov/indiv/research/indepth/ebonds/res_e_bonds_eetaxconsider.htm)

## TRANSFER OF OWNERSHIP

PP. 282-283

If Series EE or Series I bonds are purchased but then reissued to the beneficiary or spouse subject to a divorce, all interest earned must be included in the taxpayer's gross income.

Example 8.14 Transfer Incident to a Divorce

Transfer to a Trust – must include in income (unless owner of the trust)

Decedents – surviving owner can wait to cash

Example 8.15 Inherited Bond – No Election to Include

Example 8.16 Inherited Bond – Election to Include

## INFORMATION REPORTING

PP. 283-284

When a US savings bond is cashed, the bank or other payer redeeming the bond must issue a 1099-INT if the accrued interest is \$10 or more.

Box 3 of Form 1099-INT shows the interest as the difference between the amount received and the amount paid for the bond.

There may be 5 reasons for the 1099-INT showing more interest than the taxpayer needs to include.

- See list on PP. 283-284

## MUTUAL FUNDS

P. 284

Mutual funds allow investors to pool money with other investors to purchase a portfolio of stocks, bonds, and other securities. Mutual funds generally provide lower risk by creating investment diversity.

Mutual fund returns are generally paid out as:

- Dividends: ordinary and qualified
- Capital gain income

# TAX ON QUALIFIED DIVIDENDS

P. 284

**FIGURE 8.4 Qualified Dividends Maximum Tax Rates For 2020 Taxable Incomes**

Maximum Tax Rate	2020 Taxable Income				
	Single	Married Filing Jointly	Married Filing Separately	Head of Household	Estates and Trusts
0%	Not over \$40,000	Not over \$80,000	Not over \$40,000	Not over \$53,600	Not over \$2,650
15%	\$40,001–\$441,450	\$80,001–\$496,600	\$40,001–\$248,300	\$53,601–\$469,050	\$2,651–\$13,150
20%	Over \$441,450	Over \$496,600	Over \$248,300	Over \$469,050	Over \$13,150



## DIVIDEND INCOME REPORTING

P. 285

Mutual funds will report on Form 1099-DIV. Taxpayers will use Schedule B if ordinary dividends are more than \$1,500.

- January Dividends: declared in October, November, or December are considered received on December 31 of the year, even if actually paid in January of the following year.
- Partnerships, LLCs and S corporations may pass through dividends on Schedule K-1.

## SALE OF MUTUAL FUND SHARES

PP. 285-286

Basis is used to calculate gain or loss on sale of mutual fund shares.

- Purchased Stock: Initial purchase plus any sales load, commission, or fees
- Inherited Stock: generally FMV on the DOD (or alternate valuation date)
- Gifted Stock: generally the carryover basis of the donor, if FMV is less at time of gift, the FMV is used to calculate a loss on disposition by the donee
- Example 8.17 Basis of Gifted Stock
- **Practitioner Note:** Gift tax increase in basis
- Example 8.18 No Gain or Loss



## BASIS CONTINUED

PP. 286-287

Dividend Reinvestment – must still report as income

Undistributed Capital Gains – also included in income

Calculating Gain on the Sale of Mutual Fund Shares

- Can use cost basis or average basis
- Example 8.19

**FIGURE 8.5 Record of Purchases**

Date	Action	Price per Share	Number of Shares	Cost
January 15, 2018	Purchase	\$10	1,000	\$10,000
December 15, 2018	Reinvestment	\$12	100	\$1,200
July 15, 2019	Purchase	\$10	1,000	\$10,000
December 15, 2019	Reinvestment	\$8	200	\$1,600

## BASIS CONTINUED

P. 287

### Using Average Basis

- Shares are sold on a **FIFO** basis
- Example 8.20 Average Basis
- **Practitioner Note:** Election requirements to use Average Method (P. 288)

**FIGURE 8.6 Andy's Average Basis Calculation**

1. Total adjusted basis of all shares owned in the fund before the sale	\$4,800
2. Total number of shares owned in the fund before the sale	300
3. Divide the amount on line 1 by the amount on line 2	\$16
4. Enter the number of shares sold	150
5. Multiply the amount on line 3 by the amount on line 4	\$2,400

## INVESTMENT EXPENSES - NOT IN 2020

P. 288

General rule allows for ordinary and necessary expense deductions

- Reasonable amounts
- Proximate to the production of income
- Management, conservation, and maintenance

Fees for investment counsel, custodial fees, clerical help may be deductible as a miscellaneous itemized deduction if greater than 2% of AGI.

- For tax years 2018 – 2025 these deductions are eliminated.

## INVESTMENT INTEREST

PP. 289-290

Investment interest is deductible subject to limitations

- Allocation of interest expense to the investment debt
  - Example 8.23 Allocation of Investment and Personal Interest
- When to deduct Investment Interest
  - Cash when paid, accrual when accrued
- Limit on Investment Interest Deduction
  - Generally limited to net investment income (investment income less investment expenses, not including interest)
  - See IRS Form 4952 on page 289
  - Example 8.24 Interest Deduction Limit

# REPORTING INVESTMENT INTEREST EXPENSES

P. 290

To deduct investment interest expenses, the taxpayer must itemize deductions on Schedule A and attach Form 4952

FIGURE 8.9 Schedule A (Form 1040)

<b>Interest You Paid</b> <small>Caution: Your mortgage interest deduction may be limited (see instructions).</small>	<b>8</b> Home mortgage interest and points. If you didn't use all of your home mortgage loan(s) to buy, build, or improve your home, see instructions and check this box . . . . . <input type="checkbox"/>		
	<b>a</b> Home mortgage interest and points reported to you on Form 1098. See instructions if limited . . . . .	8a	
	<b>b</b> Home mortgage interest not reported to you on Form 1098. See instructions if limited. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address . . . . . ▶	8b	
	<b>c</b> Points not reported to you on Form 1098. See instructions for special rules . . . . .	8c	
	<b>d</b> Mortgage insurance premiums (see instructions) . . . . .	8d	
	<b>e</b> Add lines 8a through 8d . . . . .	8e	
<b>9</b> Investment interest. Attach Form 4952 if required. See instructions .	9		
<b>10</b> Add lines 8e and 9 . . . . .		10	



QUESTIONS?