2021 NATIONAL INCOME TAX WORKBOOK

CHAPTER 6: INIDIVIDUAL

TAX ISSUES: PART 1

Land Grant University

Tax Education Foundation

LEARNING OBJECTIVES

P. 227

- Know what contributions qualify for a charitable contribution deduction
- Apply the limits on a charitable contribution deduction
- Understand what remodel costs increase basis
- Claim energy credits for improvements to a residence
- Know when gain is excluded on the sale of a principal residence
- Understand the tax treatment on the sale of a residence converted from rental to a principal residence

CHARITABLE CONTRIBUTIONS

P. 228

In 2021 $300 ($600 MFJ) below-the-line deduction for qualified cash contributions

Increased percentage limitations for cash and non-cash contributions are extended through 2021

QUALIFIED CHARITABLE ORGANIZATION

P. 228

Qualified organizations:

US government, state, District of Columbia, US possession, or political subdivision

Corporation, trust, or community chest, fund, or foundation

Post or organization of war veterans

Domestic fraternal society, order or association operating under the lodge system

Cemetery company

INELIGIBLE ORGANIZATIONS

P. 229

Not qualified organizations:

- Political candidates, political parties, lobbying organizations
- Bar associations
- Chambers of commerce
- Civic leagues, country clubs, social clubs
- Homeowner's associations
- Labor unions

CONTRIBUTIONS TO INDIVIDUALS

P. 229

Contributions to individuals do not qualify

Ex. 6.1 Flooding destroyed the home. GoFundMe page to raise money for the family. American Red Cross provided disaster relief services.

A contribution to the American Red Cross is tax deductible, but contributors cannot deduct contributions to the GoFundMe campaign.

DONATIONS WITH BENEFIT TO THE DONOR

P. 230

If payment is partly a contribution and partly for goods or services, it is a quid pro quo contribution. Organization must provide the donor written statement

- Inform the donor the contribution is limited to the excess of the contribution over FMV of goods/services received
- Provide the donor with an estimate of FMV of goods/services received

EX. 6.2 CHARITY BALL

P. 230

Anna bought a $50 ticket to the Rainbow Fashion Show. The show was held to benefit the local Rainbow Pride Organization, a qualified nonprofit organization. Everyone who attended the show had to purchase a $50 ticket.

FMV of the ticket is $50. Anna cannot deduct the cost of the ticket, even if she does not attend the show.

If Anna makes a $50 contribution to the nonprofit organization and refuses the ticket, she can deduct the full contribution [Rev. Rul. 67-246, 1967-2 C.B. 104].

EX. 6.3 CHARITY SYMPHONY CONCERT

P. 230

Mary bought a $75 ticket to a symphony concert to benefit the local symphony, a qualified nonprofit organization. The regular price of a symphony concert ticket is $50.

Mary can deduct $25 ($75 − $50) as a charitable contribution.

DONATIONS FOR RIGHT TO PURCHASE ATHLETIC TICKETS

P. 231

For tax years after December 31, 2017 :

I.R.C. § 170(l) was amended to provide that no charitable deduction is allowed for a payment to an institution of higher education in exchange for which the payer receives the right to purchase tickets or seating at an athletic event.

EX. 6.6 RIGHT TO PURCHASE AND RECEIPT OF ATHLETIC TICKETS

P. 231

Mitch donated $500 to the University of North Dakota for the right to purchase football tickets. He paid $200 for football tickets with a $200 FMV.

Mitch cannot deduct any portion of the $500 donation as a charitable contribution.

CONTRIBUTIONS OF PROPERTY

PP. 231-233

Contributions of property generally must be for the entire interest. Some exceptions apply. Specific rules apply to certain types of assets:

Clothing and Household Items

- Must be in good used condition; Appraisal if over $500

Car, Boat, or Airplane, FMV more than $500

- Valued at lesser of gross sales proceeds or FMV if used by charity

Inventory

- Lesser of FMV or cost basis; special rules for food inventory

CONTRIBUTION OF SERVICES

PP. 233-234

No deduction allowed for time performing services. Certain unreimbursed costs are deductible:

Meals and Lodging

- Incurred while away from home

Automobile Expenses

- Actual out-of-pocket operating expense or $.14/mile standard mileage rate

Travel Expenses

- Actual costs incurred if no "significant element of personal pleasure"

EX. 6.8 CHARITABLE TRAVEL EXPENSES

P. 234

Jasmine volunteered for a qualified charitable organization that was building a house for a low-income family.

She drove her personal automobile 100 miles to the jobsite. She worked on the construction of the house for 3 days, slept at a volunteer's house within walking distance of the construction site, and ate her meals in a local diner. At the end of the 3 days, Jasmine traveled 100 miles back to her home.

Jasmine can deduct the cost of her meals because she was away from home overnight. Additionally, she may deduct $28 (200 miles × 14¢) for travel.

EX. 6.9 CHARITABLE TRAVEL WITH PERSONAL BENEFIT

P. 234

Sofia volunteered for a qualified charitable organization that was building a house for a low-income family.

She drove her personal automobile 75 miles to the jobsite. She worked on the construction of the house for 2 hours per day for 3 days, slept at her sister's house, and visited with family in the evenings. She and her sister ate most of their meals at a local restaurant. At the end of 3 days, Sofia traveled 75 miles back to her home.

The cost of Sofia's meals and travel is not deductible as the trip was partially for personal pleasure.

SUBSTANTIATION

PP. 235-237

Substantiation depends on the nature of the contribution.

Cash
- $250 or more must have contemporaneous acknowledgement

Quid Pro Quo Contributions
- Over $75 must have statement from donee organization

SUBSTANTIATION (CONT.)

PP. 235-237

Noncash Contributions

- < $250 – receipt with name, address, date, location, and description
- $250 - $500 – plus any goods, services, or religious benefit
- > $500 - $5,000 – plus how acquired, cost basis
- > $5,000 –plus qualified appraisal

Qualified Appraisal

- Dated no earlier than 60 days prior to donation and before due date w/extension
- See Treas. Reg. § 1.170A-13(c)(3)

CONTRIBUTION LIMITS

PP. 238-239

Charitable contributions are limited to a percentage of the contribution base depending on the type of property and the type of recipient organization

Practitioner Note - Contribution Base

- AGI under I.R.C. § 62, computed without regard to any net operating loss carryback to the tax year under I.R.C. § 172

CONTRIBUTION LIMITS

PP. 238-239

CARES Act - 100% of the contribution base for cash contributions by individual filers in 2020 and 2021

For tax years beginning before 1/1/26, the limit is 60% of the contribution base for contributions to 50%-limit organizations

General limitation rules:

- 50%-Limit Organizations – churches, education, hospitals, governments, etc.
- 30%-Limit Organizations – Vet groups, fraternal societies, etc.
- 20%-Limit applied to capital gain property to non-50% organizations
- Ordinary Income property – generally limited to basis

EX. 6.11 CALCULATING THE LIMITS

P. 239

In March 2021, Josef gave the local humane society [a section 501(c)(3) organization] $2,000 cash and land with a $28,000 FMV and a $22,000 basis. Josef held the land for investment purposes for more than 1 year.

He did not make the capital gain property election to reduce the land's FMV by the appreciation in value.

Therefore, the amount of Josef's charitable contribution for the land is its $28,000 FMV. Josef also gave $5,000 cash to a private nonoperating foundation to which the 30% limit applies. Josef's 2021 AGI was $50,000.

Pages 240 – 241 calculation of his deduction limit and carryover

SPECIAL CARRYOVER RULES

P. 242

Practitioner Note

Special carryover rules apply to taxpayers who

(1) are married in some years, but not married in others due to marriage, divorce, or death of a spouse;

(2) change from a separate return to a joint return or vice versa;

(3) have a net operating loss carryover; or

(4) claim the standard deduction in a carryover year.

See Treas. Reg. § 1.170A-10 for more information.

QUALIFIED CONSERVATION CONTRIBUTION

PP. 242 -244

A qualified conservation contribution (QCC) is a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. The conservation purpose must be protected in perpetuity. Must be

Qualified Real Property Interest - I.R.C. § 170(h)(2)

Qualified Organization

Conservation Purpose - I.R.C. § 170(h)(4)(A)

- Recreation or education
- Protection of environmental system
- Preservation of open space
- Historic preservation

EX. 6.15 VALUING A CONSERVATION EASEMENT

P. 246

In 2021, Delma donated a conservation easement on 20 acres of undeveloped land that is valued at $200,000 at its highest and best use.

The FMV of the land after the donation is reduced to $110,000.

Accordingly, the value of the easement, and the amount eligible for a deduction under section 170(f), is $90,000 ($200,000 − $110,000).

WENDALL FALLS DEV. VS. COMMISSIONER

P. 246

The taxpayer purchased 1,280 acres for development of a planned community. The taxpayer granted the county a conservation easement that required use of 125 acres as a park, and the taxpayer claimed a QCC deduction for the easement.

The court found that the taxpayer received a substantial benefit from the easement because the park enhanced the value of the residential and commercial properties on the remaining acres.

The court also found that the highest and best use of the 125 acres was for a park, so the grant did not reduce its value. The taxpayer was not entitled to a charitable contribution deduction.

OTHER PARTIAL INTERESTS

PP. 247-249

Retain life estate – deduct value of remainder to charity

Charitable remainder trust – income for life or term and remainder to charity

Deduction for present actuarial value of interest that will pass to charity

REPORTING CHARITABLE DEDUCTIONS

P. 250

Reporting depends on amount and type.

Non-itemized for 2021, above-the-line for qualifying cash contributions of $300 ($600 MFJ)

Schedule A (Form 1040) Itemized Deductions

Form 8283 for Noncash Charitable Contributions

Form 8282, Donee Information Return

TAX PLANNING W/ CHARITABLE CONTRIBUTIONS PP. 250-252

Contribution to a Donor Advised Fund (DAF)

- This allows the taxpayer to receive a current deduction while giving to the ultimate charity in a future year. Especially useful when “bunching” to itemize in one year and take standard deduction another.

Qualified Charitable Distribution (QCD)

- Making a payment directly from a traditional IRA to a charity
- Distribution meets RMD requirements and is not taxable
- Reduces AGI for numerous computations (SSA, QBI, etc.)

EX. 6.17 DEDUCTION FOR CONTRIBUTIONS TO DAF

P. 251

Sam and Winona file a joint return. The Watsons typically pay $5,000 in state and local taxes and make a $15,000 charitable contribution each year.

Figure 6.3 shows their 2019, 2020, and 2021 deductions claiming the standard deduction, and Figure 6.4 shows their deductions with a $45,000 contribution to a DAF in 2019, and no contributions in 2020 and 2021.

The DAF can then make annual charitable contributions.

$23,900 more in deductions

PLANNING POINTER – CHARITABLE BENEFICIARIES P. 252

If an IRA owner has specified bequests to charitable beneficiaries in his or her estate plan, it may be preferable to fund those bequests from an IRA. The owner can designate the charity as a full or partial beneficiary of the IRA.

Unlike an individual beneficiary, who must pay tax on distributions, distributions to the charity are generally not taxable.

CHAPTER 6 – POLL QUESTION 1

All non-cash contributions require a qualified appraisal be attached to the return.

A. True

B. False

REMODELING A RESIDENCE

P. 253

I.R.C. § 1016 provides that generally:

The cost or other basis of a residence is increased by improvements and betterments. On the contrary,

Repair expenditures that do not add much to the value, utility, or the life of the property and instead keep the property in good condition are not added to basis [*Plainfield-Union Water Co. v. Commissioner*, 39 T.C. 333 (1962)].

See Figure 6.5 Improvements vs. Repairs

NONBUSINESS ENERGY PROPERTY CREDIT – I.R.C. § 45C

PP. 254-255

The nonbusiness energy credit is the sum of:

10% of the amount paid or incurred by the taxpayer for *qualified energy efficiency improvements* installed during the tax year, and

The amount of the *residential energy property expenditures* paid or incurred by the taxpayer during the tax year

Limitations

- Lifetime credit of $500
- $200 for exterior windows
- Other limits

NONBUSINESS ENERGY PROPERTY CREDIT – I.R.C. § 45C

PP. 254-255

Qualified Energy Efficiency Improvements mean:

Any energy efficient building envelope component, if such component is installed in or on a dwelling unit (which includes a house, houseboat, mobile home, cooperative apartment, condominium, and certain manufactured homes) located in the United States and owned and used by the taxpayer as the taxpayer's principal residence (within the meaning of I.R.C. § 121).

NONBUSINESS ENERGY PROPERTY CREDIT – IRC § 45C

PP. 254-255

Residential energy property expenditures means:

Expenditures made by the taxpayer for qualified energy property that is installed on or in connection with a dwelling unit located in the United States and owned and used by the taxpayer as the taxpayer's principal residence (within the meaning of section 121), and originally placed in service by the taxpayer. They include labor costs that are properly allocable to the onsite preparation, assembly, or original installation of the property.

RESIDENTIAL ENERGY EFFICIENT PROPERTY CREDIT – I.R.C. § 25D

P. 256

Installations available for credit on individual returns:

Solar electric

Solar water heating

Fuel cell

Small wind energy

Geothermal heat pump

Biomass fuel

EX. 6.18 ENERGY EFFICIENT WOOD STOVE

P. 256

Mary and Gary remodeled their home in 2021. They purchased and installed an energy efficient wood burning stove. The stove cost $4,500, and they paid $1,000 for installation. Figure 6.6 shows the technical data for the stove.

The stove has a thermal efficiency rating of 78%. Mary and Gary can claim a residential energy efficient property credit equal to 26% of the $5,500 ($4,500 + $1,000) cost of the stove and installation.

Value = $1,430 tax credit

FIGURE 6.8 COMPARE 25C AND 25D CREDITS

P. 258

	Section 25C	Section 25D
Amount of the credit	10% of qualified energy efficiency improvements Residential energy property expenditures	26% of eligible expenditures for 2021
Refundable credit	No	No
Excess carries forward	No	Yes
Lifetime limit	$500 ($200 for windows)	No
Dollar limits	$50 for any advanced main air circulating fan $150 for any qualified natural gas, propane, or oil furnace or hot water boiler $300 for any item of energy-efficient building property	No
Claim for new construction	No (addition or renovation to existing allowed)	Yes
Claim for second home	No	Yes, except fuel cell
Labor included	Includes costs for onsite preparation, assembly, original installation. Not building envelope component	Includes costs for onsite preparation, assembly, or original installation, piping and wiring to connect to dwelling unit
IRS form to claim credit	Form 5695	Form 5695

ENERGY EFFICIENT HOME CREDIT – I.R.C. § 45L

P. 258

Qualified new energy efficient home

Eligible contractor

$2,000 credit ($1,000 manufactured home)

CHAPTER 6 – QUESTION 2

Which of the following is an example of an improvement that increases the basis of your personal residence?

A. Replacing some damaged boards on your deck

B. Chimney cleaning

C. Paving the driveway

D. Replacing a broken window pane

EXCLUSION OF GAIN ON SALE OF PERSONAL RESIDENCE

P. 259

A taxpayer’s principal residence is a

Personal capital asset

Sold at a loss it is a nondeductible personal loss

Sold at a gain it is a capital gain subject to tax

- Long-term or short-term capital gains rates
- Net investment income tax, when applicable
- Exclusion under I.R.C. § 121 possible up to $250,000 ($500,000 MFJ)

TESTS FOR PERSONAL RESIDENCE EXCLUSION

PP. 259-260

Ownership and Use tests:

Owned 2 of 5 prior years

Principle residence 2 of 5 prior years

Minimum 2 years since last exclusion

Principle place of residence

- Facts and circumstances
- May include adjacent land

EXCEPTIONS

PP. 260-263

Exceptions to the 2-year test may allow for a partial exclusion:

- Work-related move
- Health-related move
- Unforeseeable events

Surviving spouse sale

- I.R.C. § 121(b)(4)

EX. 6.21 REDUCED EXCLUSION AMOUNT

P. 262

Gerald and Emily bought their North Carolina principal residence on October 1, 2020, for $200,000.

On August 1, 2021, they sold the residence for $350,000 and moved to Kansas for Gerald's new job.

They realized a $150,000 ($350,000 − $200,000) gain on the sale.

They can exclude up to $208,333 [$500,000 × (10 months ÷ 24 months)] gain and do not have any taxable income on the sale.

SALE OF RESIDENCE WITH BUSINESS USE

P. 264

When part of the home is used as an office, there may be additional computations:

Business use within the living space

- Recapture section 1250 gain

Separate structure

- Allocate sale price as two separate transactions

Safe harbor using Rev. Proc. 2013-13

- No allocation or recapture

SALE OF VACATION HOME

P. 267

The sale of a 2nd home or vacation home does not qualify for the exclusion.

Converting a vacation home or investment property may gain access to partial exclusion

See Ex. 6.25

FIGURE 6.12 SALE OF FORMER VACATION HOME

P. 267

Jack Bourbon's Gain on Sale of Former Vacation Rental Home

Sale price	\$375,000
Cost basis before depreciation	(250,000)
Total gain for proration	\$125,000
Eligible for exclusion [(6 ÷ 11) × \$125,000]	(68,182)
Gain allocable to nonqualified use	\$ 56,818
Accumulated depreciation	18,000
Total reportable gain	\$ 74,818

CHAPTER 6 – POLL QUESTION 3

Which of the following is not an exception to the two-year test?

A. Change of employment

B. Change in health

C. Unforeseen circumstances

D. Incarceration for tax fraud

CROSS-REFERENCE - DEFERRAL OF GAIN

P. 269

Gain on real estate can be deferred if structured under I.R.C. section 1031.

Relinquished property and replacement property held for investment or business

Principal residence does not qualify

Vacation home may qualify

- See Rev. Proc. 2008-16 for safe harbor

See "Business Tax Issues" chapter for additional guidance

QUESTIONS?