

INDIVIDUAL TAX UPDATE



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2023 INDIVIDUAL FEDERAL TAX UPDATE



Today's Instructor

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Art lectures extensively in the areas of Tax Planning and Compliance as well as Estate and Financial Planning, Financial Planning to CPAs, EAs, and other tax professionals, and has presented well in excess of 2500 eight-hour seminars over the past twenty-five years as well as numerous webinars and video presentations. Mr. Werner has been rated as having the highest speaker knowledge in his home state of Pennsylvania by the Pennsylvania Institute of Certified Public Accountants, was awarded the AICPA Outstanding Discussion Leader Award in the State of Nevada, the Florida Institute of CPAs Outstanding Discussion Leader Award, and the South Carolina Association of CPAs Outstanding Discussion Leader Award.



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New E-File Mandate – 10-Return Threshold

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10-Return Threshold

- Beginning for “information returns” filed in 2024 and later.
- The threshold for mandatory e-file has been dropped from 250 to 10.
- The threshold is no longer based upon each type of return.
 - Instead, it is based on the aggregate number of all the returns included in coming slide.
- Only those included in that slide are counted for the 10-return threshold.
- Once the threshold is reached, all returns capable of being e-filed, including those listed, must be e-filed.
- In addition, all returns currently required to be e-filed must be e-filed whether the 10-return threshold is reached or not.

10-Return Threshold (cont.)

- The following returns are the only ones that are counted to determine if the 10-return threshold has been reached:

1042-S
 1094-series
 1095-B
 1095-C
 1097-BTC
 1098
 1098-G
 1098-E
 1098-Q
 1098-T
 1099 Series
 3921
 3922
 5498 Series
 8027
 W-2G
 W-2 and variations for U.S. territories

<input checked="" type="checkbox"/> DIRECTED (if checked)		OMB No. 1545-2205	2021	Payment Card and Third Party Network Transactions
ZIP	FILER'S TIN	Form 1099-K		
	PAYEE'S TIN			Copy B For Payee 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 taxable income
	1a Gross amount of payment card/third party network transactions			
	\$			
	1b Card Not Present transactions	2 Merchant category code		
	\$			
<input type="checkbox"/>	3 Number of payment transactions	4 Federal income tax withheld		
	\$	\$		
	5a January	5b February		
	\$	\$		
	5c March	5d April		
	\$	\$		
	5e May	5f June		
	\$	\$		

10-Return Threshold – Example #1

- Under the prior rule, an organization filing 200 Forms W-2 and 200 Forms 1099 were previously not required to e-file them.
- That is because each return type did not separately exceed the 250-return threshold.
- Under the new aggregation rule, the number of Forms W-2 and 1099 would be combined to determine whether the threshold is met.
- And the organization in this example would be required to e-file the returns in 2024.

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10-Return Threshold – Example #2

- Company A is required to file five Forms 1099-INT and five Forms 1099-DIV.
- Because Company A is required to file a total of 10 returns included in the list, It must file all its 2023 Forms 1099-INT and 1099-DIV electronically, as well as any other return(s) that are subject to an electronic filing requirement.
- The reason being that Forms 1099 and W-2 are included in the list above and must be aggregated when counting to determine whether the new 10-or-more threshold for electronic filing is met.

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S-Corporations

- The new regulations also include new rules related to e-filing by S corporations (*Reg Sec 301.6037-2*).
- An S corporation income tax return required to be filed in a calendar year beginning after 2023 must be filed electronically if the corporation is required to file at least 10 returns during the calendar year ending with or within the corporation's tax year.
- Previously a corporate income tax return must have been filed electronically if the corporation has assets of at least \$10 million, and the corporation was required to file at least 250 returns during the calendar year ending with or within the corporation's tax year.

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S-Corporations (cont.)

- The determination of whether a corporation is required to file at least the applicable number of returns is made by aggregating all returns, regardless of type, that the corporation is required to file over the calendar year, including **income tax returns**, information returns (for example, Forms W-2 and Forms 1099), excise tax returns, and employment tax returns.
- All members of a controlled group of corporations must file electronically if the aggregate number of returns to be filed by the members is at least 10 during the calendar year ending with or within the tax year of the controlled group.

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S- Corporations – Example

- In 2023, an S-corporation was required to file:
 - Form 1120-S (for 2022),
 - Two Forms W-2,
 - Two Forms 1099-DIV,
 - One Form 940, and
 - Four Forms 941.
- Because the company was required to file 10 returns during the calendar year 2023, it is required to file its 2023 Form 1120-S electronically.

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Penalties

- Penalties under IRC §6721 may apply for non-electronic filing of information returns (e.g., Forms W-2, 1099-series, etc.) when electronic filing is required.
- Such penalties may also apply for non-filing, late filing, or incorrect information.
- The penalty for returns required to be filed in 2024 – generally will be tax year 2023 returns - is up to \$310 per information return (\$60 if filed no more than 30 days late).
- Annual maximum of \$3,783,000 (\$1,261,000 if annual gross receipts are less than \$5 million). (*Rev Proc 2022-38*)

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Additional E-File Provisions

- Corporations
 - Exception for small corporations eliminated.
- Partnerships
 - More than 100 partners - must e-file
 - If must file 10 returns of any type during year must e-file the 1065.
- Form 5500
 - The 5500 and reports must be e-filed – Paper 5500-EZ can be filed if business has less than 10 filings in aggregate.
- 990 Series
 - Must be e-filed without exception.

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Other Issues

- Correcting Information Returns
 - If original was e-filed, correction must be e-filed.
 - If original was paper filed, correction must be paper filed.
- Exceptions
 - Of course, where e-file is not supported that form does not need to be e-filed.
- Hardship Waiver
 - Apply with Form 8508.

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Due Diligence Requirement

FORM 8867

- Must be completed if a tax return claims any of the following:
 - Earned Income Tax Credit (EITC)
 - Child Tax Credit (CTC)
 - Additional Child Tax Credit (ACTC)
 - Other Dependent Credit (ODC)
 - Head of Household (HH)
 - American Opportunity Tax Credit (AOTC)
- The preparer penalty for failure to properly complete and file the 8867 is \$600 (up from \$560 last year) for each violation related to EITC, CTC (ACTC, ODC), HH and AOTC is subject to penalty
- Penalty could be \$2,400 (4 x \$600)

Due Diligence Requirement (cont.)

TAXPAYER EITC PENALTIES - FRAUD OR RECKLESS DISREGARD OF RULES AND REGULATIONS

- The credit is disallowed for:
 - 10 years for those who claimed it in an earlier year due to fraud
 - 2 years due to reckless or intentional disregard of rules and regulations.
- These restrictions are in addition to other penalties imposed,
 - Accuracy-related penalty or
 - Fraud penalty.
- In addition, no credit is allowed where the credit was denied in an earlier year because of IRS deficiency assessment procedures, unless the taxpayer is re-certified by IRS

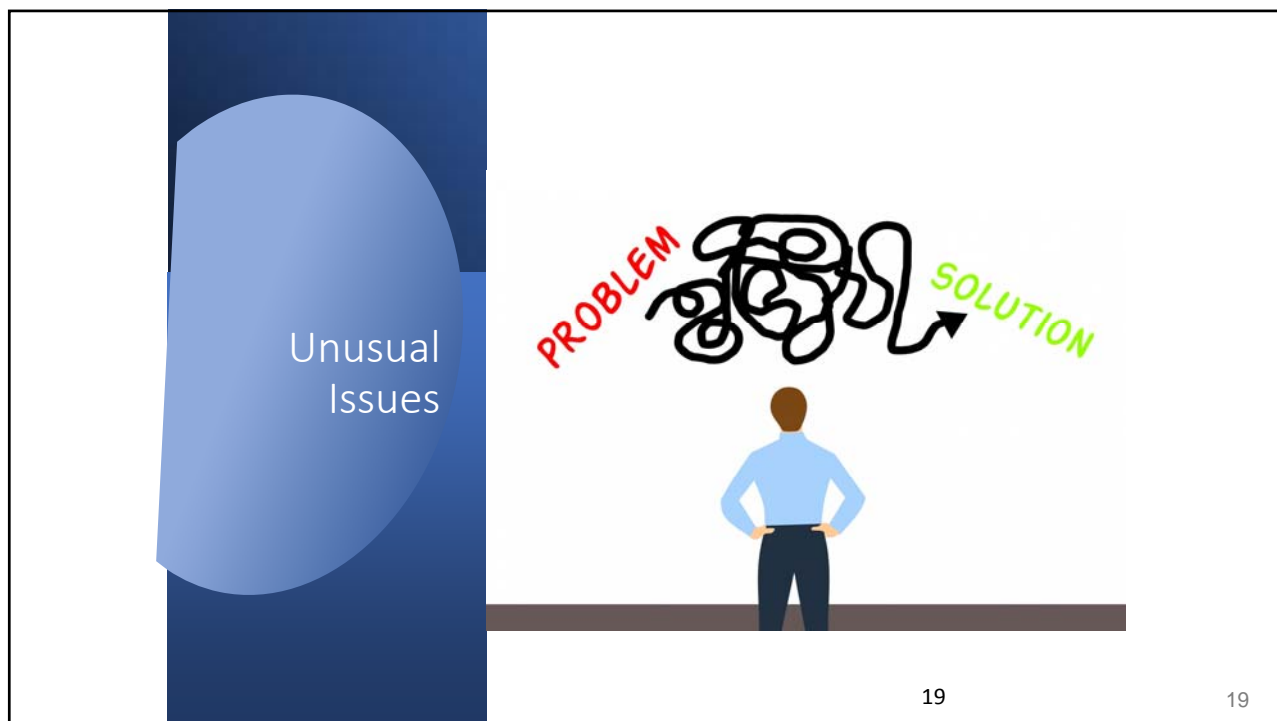
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Due Diligence Requirement (cont.)

TAXPAYER EITC PENALTIES (CONT.)

- **Recertification Process** - No EITC can be claimed by a taxpayer who has lost the credit due to the deficiency procedures for a period unless the taxpayer is recertified:
 - Recertification procedures apply if a taxpayer is subject to the 2- or 10-year disallowance periods.
 - Recertification isn't required if IRS disallows all or part of the credit because of a mathematical or clerical error.
 - To contest an EITC denial a taxpayer must petition Tax Court within 90 days of the mailing date of a statutory notice of deficiency.
 - IRS will send the taxpayer information about how to become recertified.
 - Filing without recertification will result in automatic denial.

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Abnormally Low-Income Year

An abnormally low taxable income for the year can give rise to some interesting tax planning strategies.

- Defer Deductions – If itemizing deductions, the client could defer year-end deductible payments until after the first of the year and preserve the deductions for the next year. Such payments might include:
 - House of worship contributions to satisfy a tithing commitment;
 - Year-end charitable giving, tax payments (but not those incurring late payment penalties);
 - Estimated state income tax payments; and
 - Medical expenses.

Abnormally Low-Income Year (cont.)

- Convert Traditional IRA Funds into a Roth IRA – To the extent of the negative taxable income or even just the lower tax rates, a client could consider converting some or all of their traditional IRA into a Roth IRA. The lower income provides an opportunity to convert to a Roth IRA at a lower tax amount.
- Zero Capital Gains Rate - There is a zero long-term capital gains rate for those taxpayers whose regular tax brackets are 15% or less. This may allow appreciated securities owned for more than a year to be sold and pay no or very little tax on the gain.

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Abnormally Low-Income Year (cont.)

- Business Expenses – The tax code has some very liberal provisions that allow a business to currently expense, rather than capitalize and slowly depreciate, the purchase cost of certain property. In a low-income year it may be appropriate to capitalize rather than expense these current year purchases and preserve the depreciation deduction for higher income years. This is especially true where there is a negative taxable income in the current year.
- **CAUTION:** If the client has obtained medical insurance through a government marketplace, employing any of the strategies mentioned could impact the amount of the allowable premium tax credit.

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Preparing Tax Returns for Ex-Spouses

- Circular 230 §10.29, states that a practitioner may not represent potential conflicting interests in their practice.
- Dealings with spouses and ex-spouses can result in such conflicts of interest.
- Bigger risk is the attorney of one of the spouses.
- Good practice to only prepare one of the spouse's returns, and in some situations neither.
- If you feel you can provide your services without any conflict, it is strongly recommended that you obtain the consent of both spouses to disclose their tax return information to the other spouse.

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Married Filing Separate

STANDARD OR ITEMIZED

- IRC §63(c)(6)(A) provides that a married individual filing a separate return where either spouse itemizes deductions shall have a standard deduction of zero.
 - Thus, if both spouse are filing MFS, if one itemizes the other cannot take the standard deduction.
 - Exception: That does not apply to a spouse filing as HH because that spouse is not considered married under IRC §7703(b).
 - Thus, that spouse can choose between the standard or Itemized deductions and is not required to itemize if the other spouse does.
 - Also, if the HH spouse itemizes then the MFS spouse must itemize.

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First-Time Homebuyer Credit Recapture

- **Credit Claimed in 2008** – The credit was 10% of the home's cost. Max. credit was \$7,500.
- **Payback:** Credit had to be paid back over 15 years – 6.67% per year.
- **Final Year:** Will be 2024.
- **Accelerated Payments:** If the homebuyer sells the home (or neither spouse no longer uses it as a principal residence) any remaining repayment amount must be repaid. Thus for 2023 the accelerated amount would be 13.33% (2 /15) of the credit.
- **Death** – Repayment no longer applies.
- **Transfer in Divorce** – Transferee spouse becomes solely responsible.
- **Sale** - Payback cannot exceed the gain from a home sale.

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Divorce Issues



DIVORCE

Tax Attributes - Divorce

- **Capital Loss Carryovers**

- Allocated to the spouse who originally incurred the loss
- Can be complicated
 - Acquired before or after marriage
 - Community or Separate property

- **Passive Loss Carryovers**

- Separately owned property - to the spouse that owns the property.
- Jointly owned or is community property:
 - Owned by both after the divorce, 50% to each spouse.
 - Where one spouse retains the property as part of a property settlement, 50% of the carryover becomes an adjustment to the basis of the property and the other 50% continues to be carryover for the spouse that retained the property.

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Tax Attributes – Divorce (cont.)

- **Net Operating Loss (NOL) Carryovers**

- If married to each other in all NOL years – 50% to each.
- **If NOT**, the deduction may only be taken by the spouse who incurred the loss and only to offset income generated by that spouse in a carryback or carryforward year.

- **Joint Estimated Tax Payments**

- Made joint estimated tax but file separate returns:
 - Agree - Divide in any way on which they both agree.
 - Cannot agree – Prorate - Total estimated tax paid times the fraction which is the tax on their individual return divided by the sum of the tax shown on their individual returns for the year.

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Tax Attributes – Divorce (cont.)

- **Transfers Incident to a Divorce**

- The recipient spouse's basis is the same as the transferor-spouse's adjusted basis. (IRC §1041(b)). This is the case even if:
 - The transaction is a sale between the spouses;
 - The transferee-spouse pays the transferor-spouse, per the divorce settlement) for the transfer of title to the property (Reg §1.1041-1T(a), Q&A-2); or
 - The adjusted basis of the transferred property is less than, equal to, or greater than its fair market value at the time of transfer.
 - Applies for purposes of determining loss as well as gain, upon later sale by the transferee (Reg § 1.1041-1T(d)).
- There are exceptions that may apply to certain transfers in trust (Sec 1041(e)) and transfers of installment obligations into a trust IRC §453B(g)).

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Basis Issues – Divorce

- Section 121 Home Gain Exclusion – If one of the spouses is awarded sole ownership of the couple's home that spouse assumes the community basis, and as such is responsible for the tax on any gain not excludable under IRC §121. Keep in mind the exclusion just dropped from \$500K to \$250K.
- Spousal Buy-Out Debt - In divorce situations, debt secured by the home to buy out a former spouse's interest in a home is acquisition debt.
- This rule is applied without regard to IRC §1041, which treats certain transfers of property between spouses incident to divorce as nontaxable events. (Notice 88-74, 1988-2 CB 385)

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DEATH OF A TAXPAYER



Tax Attributes

- For married couples: Be sure to separate carryover losses and deductions between the decedent and the surviving spouse according to joint, individual and community property (where applicable) ownership before applying the following rules.
- **Medical Expenses**
 - Expenses paid up to the date of death itemized on final return.
 - Expenses paid by estate within one year of DOD, with executors' approval, can be itemized on the deceased's final return
 - Medical expenses cannot be claimed on a 1041.
- **Investment Interest Carryovers** – Lost if not used on the final 1040.
- **Net Operating Loss Carryover** – Lost if not used on the final 1040.
- **Charitable Carryover** – Lost if not used on the final 1040.
- **Capital Loss Carryover** – Lost if not used on the final 1040.

Tax Attributes (cont.)

- **Business Credit Carryovers** – Accelerated on decedent's final return.
- **Foreign Tax Credit Carryovers** – Can be used by the decedent's estate or heirs.
- **Passive Loss Carryover** - When a passive interest is transferred due to death, the accumulated suspended losses are deducted on the decedent's final return.
 - However, the deduction amount is limited to the excess of the basis of the property in the hands of the transferee (heir) over the decedent's adjusted basis in the property just before death.
- **Minimum Tax Credit Carryovers** - Lost if not used on the individual's final return.
- **Passive Activity Tax Credit** - Effectively lost if not used on final return.
- **Unrecovered Investment in Pensions** - Allowed as a tier 1 miscellaneous deduction on the decedent's final return. If an annuity for joint lives, only deductible on the 1040 of the last to die.

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Tax Attributes (cont.)

- **Cancellation of Debt Income**
 - COD income is reportable on the decedent's return if it occurred prior to death.
 - If married and surviving spouse is also personally liable, the spouse would report the COD income on his or her 1040.
 - If a debt is cancelled after death, the COD income is income to the estate or the non-grantor trust of the decedent and reportable as income on the 1041 return to the extent the estate/trust is solvent.
- **Income in Respect of a Decedent (IRD)**
 - Is income included in estate's gross income (on Form 1041) and is also taxable to the beneficiary. As a result, it is taxed twice.
 - Thus, a beneficiary gets a Tier 1 miscellaneous deduction equal to the estate tax paid on the IRD income.
 - With the estate tax exclusion currently \$12,920,000 (2023), few estates are paying any tax, so a very rare deduction.
 - Typical types of IRD include amounts received after the decedent's death as compensation for his or her personal services, retirement plan distributions, investment income, and income from installment notes.

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Tax Attributes (cont.)

- **Insolvent Estate**

- Tax liability must be paid first.
- Executor is liable for the taxes if they fail to exercise due care in determining if such tax obligations existed before distribution of the estate's assets.
- So, don't distribute any assets before paying the tax liability.

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W-2 After Employee's Death

- Report payments as follows:
 - Payment made after death but in the year of death
 - Withhold SS and Medicare taxes and only report the income in boxes 3 and 5 to ensure proper Social Security and Medicare credit was received.
 - Do not show the payment in box 1.
 - Also Issue a 1099-MISC and report the payment in box 3 for payment to the estate or beneficiary.
 - Payment made after the year of death
 - Do not report it on Form W-2.
 - Instead, issue a 1099-MISC reporting payment to the estate or beneficiary in Box 3.

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MILITARY



Military Spouse Residence or Domicile

- **The Servicemembers Civil Relief Act of 2003** - Provides that a servicemember does not lose or acquire a residence or domicile for tax purposes with respect to his or her person, personal property, or income due to being absent or present in any tax jurisdiction in the U.S. solely to comply with military orders.
- A state (or other tax jurisdiction) may not use the military compensation of a nonresident servicemember to increase the tax liability imposed on other income earned by the nonresident servicemember (or spouse) that is taxed by the state or other jurisdiction.
- **CAUTION:** The Veterans Auto and Education Improvement Act of 2022 (VAEIA) (next slide) has replaced the Veterans Benefits and Transaction Act of 2018 with an even more liberal residence provision for both the servicemember and the servicemember's spouse.
 - However, the legislation was sloppily written and until Congress provides further guidance it is unclear if the VAEIA is effective in 2022 or 2023.

Military Spouse Residence or Domicile (cont.)

- **Veterans Auto and Education Improvement Act of 2022 (VAEIA)**

- Sec 18 of the legislation modifies Sec 511(a) of the Servicemembers Civil Relief Act of 2003, providing substantially more liberal residency options for servicemembers and the servicemember's spouse.
- Under the new law, which became law Jan. 5, 2023, servicemembers and their spouses, regardless of the date on which the marriage of the servicemember and the spouse occurred, are allowed to elect the state in which they pay income taxes from three options, the:
 - Legal residence or domicile of the servicemember;
 - Legal residence or domicile of the spouse; or
 - Current permanent duty station of the servicemember.

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Military Spouse Residence or Domicile (cont.)

- **Veterans Auto and Education Improvement Act of 2022 (VAEIA) (cont.)**

- The Act also expands to spouses a residency protection already offered to servicemembers that allows them to remain tied to a former legal residency, even if they no longer physically live there.
- Thus, if the servicemember and spouse were to be stationed in a state that has no income tax, or low-income tax rates, they can continue to claim that state as their legal residence after moving away, provided they met legal residency requirements while living there.
- As noted above, the legislation does not specify the effective date of this change (2022 or 2023) and is unclear whether the military spouse and the servicemember will be required to file their taxes in the same state. Also not specified is if taxpayers will be able to switch the states in which they file year to year. The IRS (or Congress) will need to provide clarification.

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Employer Military Spouse Credit

- Small employers (no more than 100 employees earning more than \$5,000 per year) are entitled to a tax credit with respect to their defined contribution plans if they:
 - Make military spouses immediately eligible for plan participation within two months of hire;
 - Upon plan eligibility, make the military spouse eligible for any matching or nonelective contribution that they would have been eligible for otherwise at 2 years of service; and
 - Make the military spouse 100% immediately vested in all employer contributions.
- The tax credit equals the sum of:
 - \$200 per military spouse; and
 - 100% of all employer contributions (up to \$300) made on behalf of the military spouse.
- This results in a maximum tax credit of \$500. This credit applies for 3 years with respect to each military spouse.
- This credit does not apply to highly compensated employees (\$150,000 for 2023).
- An employer may rely on an employee's certification that such employee's spouse is a member of the uniformed services.
- **Effective Date: January 1, 2023**

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FOREIGN RELATED REPORTING ISSUES



Social Security and Medicare Foreign Employment

- United States Social Security and Medicare taxes apply to foreign employment only if one of the following applies:
 - Worked for an American employer; or
 - Performed the services on or in connection with an American vessel or aircraft and either
 - Entered an employment contract within the U.S; or
 - The vessel/aircraft touches a U.S. port while employed on it.
 - Working in one of the countries with which the United States has entered into a bilateral social security agreement (also known as a Totalization Agreement).
 - Worked for a foreign affiliate of an American employer under a voluntary agreement between the employer and the U.S. Treasury.

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Social Security and Medicare Foreign Employment (cont.)

- An American employer is defined as:
 - The U.S. Government or any of its instrumentalities,
 - An individual who is a resident of the United States,
 - A partnership of which at least two-thirds of the partners are U.S. residents,
 - A trust of which all the trustees are U.S. residents, and
 - A corporation organized under the laws of the United States, any individual state within the United States, or the District of Columbia, Puerto Rico, the Virgin Islands, Guam, American Samoa, or the Commonwealth of the Northern Mariana Islands .

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Foreign Workers

- **Information Reporting**

- Foreign workers who perform their services for a U.S. business from their native countries are not subject to information reporting requirements (thus no 1099 reporting requirements) or withholding requirements.
- Non-resident aliens working outside the U.S. have no U.S. income tax liabilities and the U.S. employer can deduct the amounts paid.
- IRS Website: As a rule, wages earned by nonresident aliens for services performed outside of the United States for any employer are foreign source income and therefore are not subject to reporting and withholding of U.S. federal income tax. There are some exceptions; these exceptions, however, are rare.

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FinCEN Form 114 (“FBAR”)

- U.S. Persons with a financial interest in or signature authority over any foreign financial accounts that exceed a sum of \$10,000 at any time during the calendar year have a FBAR filing requirement.
- Accounts to watch out for:
 - Online gambling accounts (located in a foreign country).
 - Family accounts – Where a family member resides in a foreign country and puts a U.S. taxpayer’s name on the account.
 - Business accounts.
 - Foreign retirement accounts.
 - Inherited accounts.
 - Temporary gift accounts.

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FinCEN Form 114 (“FBAR”) (cont.)

- **Due Date:** April 15 of the subsequent year.
- **Automatic Extension:** October 15
- **Where Filed:** FBARs are filed online at <https://www.fincen.gov/>
- **Penalties:** Penalty is inflation adjusted. \$15,611 for 2023.
 - Apply to FBAR filing not per foreign account. Bitner vs U.S. (SCOTUS 21-1195).
- **Statute of limitations** - Either willful or negligent failure to file 6 years from the due date of the FBAR report.
- **1040 Sch. B Questions** – Be sure to check the box(es).
- **NOTE:** OPR has made it clear that practitioners have a responsibility to comply with FBAR reporting rules.

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IRS Form 8938 (Reporting Foreign Assets)

- Form 8938 is required if the total value of specified foreign financial assets is greater than the amounts shown in the above table, either as of the end of the tax year or at any time during the tax year, based on marital status and residency in the U.S. or abroad.

FORM 8938 – REPORTING REQUIREMENT – INDIVIDUALS WITH FOREIGN ASSETS (SEC 6038(D))				
	Living in The U.S.		Living Abroad	
Filing Status	Year-End Value	During Year Value	Year-End Value	During Year Value
Married Filing Joint	\$100,000	\$150,000	\$400,000*	\$600,000*
Others	\$50,000	\$75,000	\$200,000	\$300,000

**Applies even if only one spouse lives abroad*

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COMMONLY ENCOUNTERED FOREIGN REPORTING REQUIREMENTS		
	FORM 8938	FinCEN FORM 114 (FBAR)
Financial (deposit and custodial) accounts held at foreign financial institutions	Yes	Yes
Financial account held at a foreign branch of a U.S. financial institution	No	Yes
Financial account held at a U.S. branch of a foreign financial institution	No	No
Foreign financial account for which you have signature authority	No, unless you otherwise have an interest in the account as described above	Yes, subject to exceptions
Foreign stock or securities held in a financial account at a foreign financial institution	The account itself is subject to reporting, but the contents of the account do not have to be separately reported	
Foreign stock or securities not held in a financial account	Yes	No
Foreign partnership interests	Yes	No
Indirect interests in foreign financial assets through an entity	No	Yes, if sufficient ownership or beneficial interest (i.e., a greater than 50 percent interest) in the entity. See instructions for further detail.
Foreign mutual funds	Yes	Yes
Domestic mutual fund investing in foreign stocks and securities	No	No
Foreign accounts and foreign non-account investment assets held by foreign or domestic grantor trust for which you are the grantor	Yes, as to both foreign accounts and foreign non-account investment assets	Yes, as to foreign accounts
Foreign-issued life insurance or annuity contract with a cash-value	Yes	Yes
Foreign hedge funds and foreign private equity funds	Yes	No
Foreign real estate held directly	No	No
Foreign real estate held through a foreign entity	No, but the foreign entity itself is a specified foreign financial asset and its maximum value includes the value of the real estate	No
Foreign currency held directly	No	No
Precious Metals held directly	No	No
Personal property, held directly, such as art, antiques, jewelry, cars and other collectibles	No	No
'Social Security'-type program benefits provided by a foreign government	No	No

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Foreign Rental Properties

- **Depreciation**
 - Building (placed in service before 2018): 40 years
 - Placed in service after 2017: 30 years
- **Passive Loss Rules** – Same as U.S. rental.
- **RE Professional** – Difficult to qualify for.
- **1031 Exchange** – Foreign and domestic rentals are not like kind
- **Sec 199A Deduction** – Not qualified.
- **FBAR** – Not for the rental, but perhaps operating bank account.
- **Form 8938** – Not for the rental itself but perhaps entity owning it

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Foreign Pensions

- **Taxable Amount** - Generally is the Gross Distribution minus the Cost (investment in the contract) unless there is a tax treaty provision covering the pension.
- **Tax Treaties:**
 - **General Rule** - most tax treaties allow the country of residence to tax the pension or annuity under its domestic laws.
 - **Special Treaty Rules** – Practitioners need to check the tax treaty for special treatment.
 - **Foreign Social Security Pensions** - Unless specified otherwise in a tax treaty, foreign SS is generally taxed like foreign pensions or annuities.

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Foreign Gift Reporting

- If aggregate foreign gifts by a U.S. person exceeds the following amounts, then the U.S. person must report the following gifts:
 - More than \$100,000 from a nonresident alien individual or foreign estate.
 - More than \$18,567 (2023 inflation-adjusted amount) from foreign corporations or foreign partnerships (including foreign persons related to such foreign corporations or foreign partnerships) that are treated as gifts.
- Amounts do not include any qualified tuition or medical payments made on behalf of a U.S. person (same as normal gift tax rules).
- Penalties – 5% per month, 25% maximum
 - Excused for reasonable cause.

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Foreign Gift Reporting - Forms

- 1040 Schedule B – Individuals with foreign gifts need to answer the line 8 question correctly at the bottom of the Schedule B.
- Form 3520 - Complete the identifying information on page 1 of Form 3520 and Part IV. See the instructions for Part IV.
 - Due date: April 15.
 - Not filed with the 1040. See instructions for filing address.
 - 6-month extension with Form 7004.
- FBAR - Taxpayers may also be required to file FinCEN Form 114 if the conditions of transfer and account balance require it.
- Form 3520 is also used:
 - By a U.S. Person or the executor of the estate of a U.S. Person to report ownership in a foreign trust; or
 - Transactions carried out with a foreign trust.

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Foreign Gift Reporting – Forms (cont.)

- Form 3520-A is used by a U.S. owner to satisfy annual information reporting requirements.
- Form 709 is used by a non-resident alien if subject to gift tax when they make a gift of real or tangible personal property situated in the U.S.
- Form 5471 is an information return of U.S. persons with an ownership interest, voting power, officer or director of a foreign corporation.

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1099-K Reporting

RETRACTED (if checked)

ZIP	FILER'S TIN	OMB No. 1545-2205	2021 Form 1099-K	Payment Card and Third Party Network Transactions
	PAYEE'S TIN			
	1a Gross amount of payment card/third party network transactions \$			
	1b Card Not Present transactions \$	2 Merchant category code	Copy B For Payee 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 taxable income	
<input type="checkbox"/>	3 Number of payment transactions	4 Federal income tax withheld \$		
<input type="checkbox"/>	5a January \$	5b February \$		
	5c March \$	5d April \$		
	5e May \$	5f June \$		

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1099-K Reporting - The IRS Saves the Day!

- On November 21, 2023, the IRS issued NOTICE-2023-74.
 - This notice delays the new 1099-K rules and extends the prior 1099-K rules.
 - For 2023 the threshold was scheduled to be severely reduced to a flat \$600; the threshold now remains at \$20,000 or more than 200 transactions for 2023.
 - In addition, the IRS announced that they are planning for a threshold of \$5,000 for 2024.
- The \$600 threshold is now scheduled to be implemented for 2025.

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Incorrect 1099-K

- Reasons a TP may receive an incorrect or erroneous Form 1099-K:
 - A TP may receive a 1099-K for a private transaction, like the sale of used personal items, or for a cost-sharing transaction between friends or family, which aren't covered by the Form 1099-K reporting rules.
 - A taxpayer may receive a Form 1099-K that contains incorrect information, such as a wrong name, address, tax identification number or reported transaction amounts.
- A TP who receives an erroneous Form 1099-K or one that contains incorrect information should contact the entity that issued the Form 1099-K and attempt to obtain a corrected Form 1099-K.
- Can't obtain a corrected 1099-K?
 - Report the amount on 1040 Sch 1 Part 1 line 8z as additional Income, and:
 - Back it out on Schedule 1 Part I - Line 8z - Other Income – “Form 1099-K Received in Error”, **or**
 - Part II - Line 24z - Other Adjustments – “Form 1099-K Received in Error”.
- **Note:** The IRS has also updated FAQs related to Form 1099-K (IR 2023-53; Fact Sheet 2023-06). Search IR 2023-53 on the Internet.

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Incorrect 1099-K (cont.)

- Personal items sold at a loss. If the taxpayer received a Form 1099-K for personal items sold at a loss, the information should be reported the same as a 1099-K received in error as described above.
- Personal items sold for profit. If the taxpayer received a Form 1099-K for personal items sold at a profit, such as a car, refrigerator, furniture, stereo, jewelry, silverware, etc., should report that profit as capital gain on Form 8949.
- **CAUTION:** Gains from personal asset sales cannot be offset by losses from personal asset sales.

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Cryptocurrency



Broker Reporting – Beginning 2023

- Crypto exchange reporting will be like stock brokerage accounts.
- Form 1099-B at the end of the year.
- Tax Treatment – Reported on Form 8949/Schedule D .
- Reporting - Gain or loss must be determined for each transaction:
 - If it is held for investment, then capital gain; or
 - If held as inventory for sale to others, then ordinary income.
- Foreign reporting issues (if held in foreign accounts):
 - May have an FBAR and Form 8938 reporting requirement.

Tax Reporting

- Tax Treatment – Like property transactions; reported on Form 8949/Schedule D .
- Reporting - Gain or loss must be determined for each transaction.
- Capital Gain or Ordinary Income?
 - If it is held for investment, then capital gain.
 - If held as inventory for sale to others, then ordinary income.
- Foreign reporting issues (if held in foreign accounts):
 - FBAR - FinCEN's opinion is the FBAR is not required. But Tax Court overturned their “opinion” related to FBAR and online gambling accounts.
 - Form 8938 - Cryptocurrency held in foreign exchanges requires reporting on Form 8938 if the reporting threshold is reached.

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Business Issues

- Employee payments – Subject to tax and FICA withholding and W-2 reporting as normal and reporting in U.S. Dollars.
- Independent Contractor Payments – Subject to 1099-NEC reporting in U.S. dollars.
- 1040 Question – Don't overlook the Yes/No question on page 1 of Form 1040.
 - **Could face penalties or even criminal charges if caught lying.**

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Income Issues



INCOME

2023 Tax Brackets

2023 Federal Tax Brackets			
Tax Bracket/Rate	Single	Married Filing Jointly	Head of Household
10%	\$0 - \$11,000	\$0 - \$22,000	\$0 - \$15,700
12%	\$11,000 - \$44,725	\$22,001 - \$89,450	\$15,701 - \$59,850
22%	\$44,726 - \$95,375	\$89,451 - \$190,750	\$59,851 - \$95,350
24%	\$95,376 - \$182,100	\$190,751 - \$364,200	\$95,351 - \$182,100
32%	\$182,101 - \$232,250	\$364,201 - \$462,500	\$182,101 - \$231,250
35%	\$231,251 - \$578,125	\$462,501 - \$693,750	\$231,251 - \$578,100
37%	\$578,126+	\$693,751+	\$578,101+

Social Security Wage Base

Tax Rate	2022	2023
Employee	7.65%	7.65%
Self-Employed	15.30%	15.30%

	2022	2023
Maximum Taxable Earnings		
Social Security (OASDI only)	\$147,000	\$160,200
Medicare (HI only)	No Limit	
Quarter of Coverage		
	\$1,510	\$1,640
Retirement Earnings Test Exempt Amounts		
Under full retirement age	\$19,560/yr. (\$1,630/mo.)	\$21,240/yr. (\$1,770/mo.)
NOTE: One dollar in benefits will be withheld for every \$2 in earnings above the limit.		

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General Welfare Exclusion

- In general, all kinds of income, including earned, found, or won is income for tax purposes (IRC §61).
 - Consequently, income is broadly defined with exclusions generally limited to those specified in the Internal Revenue Code.
- However, there is a little-known administrative exception, called the general welfare exception (GWE), which allows some payments to be excluded from income.
 - The classic example of this type of payment is a government payment made to victims of a natural disaster.
- Other examples:
 - Temporary Assistance for Needy Families (TANF) payments;
 - Food benefits - the Nutrition Program for the Elderly; and
 - Mortgage assistance payments - the National Housing Act.

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General Welfare Exclusion - Qualifications

- To qualify under the GWE, payments must:
 - Be made from a government fund.
 - Be for the promotion of the general welfare, based on individual or family need.
 - Not be made as payment for services.
- Origin of Payments
 - Made because of need.
 - Food
 - Medical
 - Housing, heating
 - Payments to businesses do not qualify

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General Welfare Exclusion – Subjective Determination

- What any individual taxpayer “needs” is a subjective determination.
- The IRS has applied the GWE to many different contexts:
 - Education assistance.
 - Facilitate adoption.
 - Economic development.
 - Payments to crime victims.
 - Disaster victims.
- **Note:** Age, in and of itself, is not a demonstrated need.

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Preserving Capital Loss Carryovers (“CLCOs”)

- **Verbatim from Publication 550:** -*“When you figure the amount of any capital loss carryover to the next year, you must take the current year’s allowable deduction into account, whether or not you claimed it and whether or not you filed a return for the current year”.*
- To claim a CLCO, Sch. D instructions indicate a copy of the taxpayer’s prior year 1040 and Sch. D are needed to complete the capital loss worksheet for how much loss is carried forward from the prior year.
- The amount of the capital loss carryover is the amount of taxpayer’s total net loss that is more than the **lesser** of the taxpayer’s:
 - Allowable capital loss deduction for the year (\$3,000/\$1500 MFS); or
 - Taxable income increased by the taxpayer’s allowable capital loss deduction for the year and for years other than 2018 through 2025, the taxpayer’s deduction for personal exemptions.

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Preserving Capital Loss Carryovers (“CLCOs”) (cont.)

- **Bottom Line:**
 - There appears to be no actual requirement to file a return, where one is not otherwise required to be filed.
 - However, since the carryover is based upon the results of a prior year return, if the CLCO amount is challenged by IRS, the taxpayer would have to be able to reconstruct the prior year return to prove the amount of the carryover.
- **Best Practice:**
 - That leads us to believe that the best practice may be to actually file a return and run the statute of limitations even though it is not actually required.

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Schedule D Transaction Strategies

- **Gift Appreciated Stock:**

- To provide support for low-income parent(s), instead of (adult) child selling stock and using after-tax cash.
 - Parent's basis is the child's basis.
 - Parent(s) pays the tax on the stock appreciation.
 - Tax may be zero because of the large standard deduction and zero capital gains tax bracket.
 - Child avoids the capital gains tax while providing support.

- **Offset Short-Term Capital Gains with Long-Term Capital Losses:**

- Short-term capital gains are taxed at regular rates.
- Long-term capital losses if used to offset LTCG reduce 10% or 15% income.
- Therefore, taxpayers achieve a better overall tax benefit if they can arrange their transactions so as to offset short-term capital gains with long-term capital losses.

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Schedule D – Zero Tax Long-term Capital Gain

- **Example:**

- Suppose a married couple is filing jointly and has projected taxable income for the year of \$50,000.
- From tax rates for 2023, we find that the 15% capital gains tax bracket threshold for married joint filers is \$89,251.
- That means they could add \$39,251 ($\$89,251 - \$50,000$) of long-term capital gains to their income and pay zero tax on the capital gains.

- **Potential Side Issues:**

- Based on projected income (best late in the tax year)
- Numerous AGI based tax limitations
- ACA premium tax credit (based on household income)
- Medicare premiums (based on 2 years prior AGI)
- SS Taxation

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2023 Capital Gain Rate Table

Long-term capital gains rate	Taxable income
Single filers	
0%	\$0 to \$44,625
15%	\$44,626 to \$492,300
20%	\$492,301 or higher
Married filing jointly	
0%	\$0 to \$89,250
15%	\$89,251 to \$553,850
20%	\$553,851 or higher

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Qualified Opportunity Funds (“QOF”) Issues

- Unfortunately, the benefits of a QOF are waning.
 - Deferred gain becomes taxable the earlier of when the QOF investment is sold or December 31, 2026.
 - Thus, if an investment is made in 2023, only 4 years remain before the deferred gain becomes taxable at the end 2026.
 - This means an investor just now investing in a QOF doesn’t have enough time to hold the investment the required 5 or 7 years.
 - Thus, there is no benefit from the 10% or 15% step up in basis.
 - However, the gain deferral is still available and is not taxable until the 2026 return is filed.

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This Year's Income Supplements



Supplement 1 – Employee Stock
Options



Supplement 2 – Home Sale Issues



Supplement are located at the end
of the PowerPoint Presentation
after the contact information slide.

Deduction Issues



DEDUCTIBLE

Filing Status	2022 tax year, <65	2022 tax year, 65 and older	2023 tax year, <65	2023 tax year, 65 and older
Single	\$12,950	\$14,700	\$13,850	\$15,700
Head of Household	\$19,400	\$21,150	\$20,800	\$22,650
Married filing jointly	\$25,900	\$27,300 for 1 or \$28,700 for both	\$27,700	\$29,200 for 1 or \$30,700 for both
Married filing separately	\$12,950	\$14,700	\$13,850	\$15,700

Standard Deduction

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Unusual Medical Expenses

- **Acupuncture**
- **Alcoholism**
 - Inpatient treatment including meals & lodging
 - Travel – AA Meeting
- **Adoption Medical**
 - Child is a dependent when services are rendered or paid.
 - Natural mother's childbirth expenses are not allowed.
- **Birth Control** – Prescribed by a doctor
- **Body Scan** – Even if not experiencing any symptoms
- **Chiropractor**
- **Christian Science Practitioner**
- **Cosmetic Surgery**
 - Improving appearance – No!
 - Correcting a deformity - Yes!

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Unusual Medical Expenses (cont.)

- **Disabled Dependent Care**
 - Can be used either as medical, or
 - The dependent care credit
 - No double dipping allowed
- **Egg Donor Expenses** – Cost of obtaining eggs plus legal expenses and donor expenses directly related to obtaining the eggs.
- **Elderly Devices** – Deductible without prescription if they meet the definition of a medical device.
 - Phones with big buttons
 - Medical alert devices
 - Amplifiers for hard of hearing
 - But not over the counter magnifying glass
 - Other items like glasses, TTY devices, etc., may require an prescription

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Unusual Medical Expenses (cont.)

- **Fertility Enhancement**
 - Procedures such as in vitro fertilization (including temporary storage of eggs or sperm).
 - Surgery, reverse prior surgery that prevented the person from having children.
- **Guide Dog**
 - For visually, hearing, or disabled person is allowed.
 - Emotional support animals do not, unfortunately, qualify.
- **Gender Identity Disorder** - The costs of gender reassignment surgery and hormone replacement are considered qualified medical expenses for persons with gender identity disorder.
- **Genetic (DNA) Testing** - PLR allocation.
 - Cost of a kit must be allocated between ancestry and health services using a percentage (cost of the health services/total cost of ancestry plus health services) using a reasonable method of allocation.
- **Health Care Ministry** – Deductible as medical insurance

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Unusual Medical Expenses (cont.)

- **Household Help as a Medical Expense** - The cost of household help cannot be included in medical expenses, even if such help is recommended by a doctor. **But see nursing services later.**
- **Kidney Transplant** - Kidney donor's surgical, hospital, and transportation expenses paid by kidney recipient are deductible by recipient. Rev Rul 68-452
- **Self-employed Health Insurance**
- **Impairment Related Expenses**
 - Special equipment installed in the home, only to the extent it does not increase the value of the home.
 - Some home impairment modifications do not increase the value of the home and are fully deductible.

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Unusual Medical Expenses (cont.)

- **Insurance Premiums**
 - Medical, hospital, dental and limited long-term care.
 - Lost or damaged contact lenses, prescription drugs, insulin.
 - Medicare-B, Medicare-D and additional part C.
 - Marketplace premiums net of PTC.
 - Medical insurance premiums (and other medical expenses) paid by flexible spending arrangement are not deductible because they are paid with pre-tax dollars.
- **Learning Disability** (Special Education)
 - Tutoring fees recommended by a doctor (teacher trained to work with severe learning disabilities).
- **Medical Marijuana** (Controlled Substance) – Is not allowed.

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Unusual Medical Expenses (cont.)

- **Non-Hospital Institutions**

- Private Home - All amounts to maintain mentally disabled son in a specially selected private home (qualified as an "institution") by recommendation of the psychiatrist.
- Hotel meals and lodging - Taxpayer received nursing service in the hotel, after appendicitis and being discharged from the hospital because it needed his hospital room. Attending physician said taxpayer was too weak to travel home. (*Kelly, Daniel vs. Com. (1971)*)
- Halfway House - Paid to maintain a child at a halfway house, including room and board. Required the recommendation of a psychiatrist and continued psychiatric supervision during the stay.

- **Nursing Home** - Inpatient care at a hospital or similar institution if the main reason is to receive medical care. Includes meals and lodging.

- **Nursing Services** - Services need not be performed by a nurse if the services are of a kind generally performed by a nurse.

- These services can be provided in the home or another care facility.
- If the attendant also provides personal and household services, these amounts must be allocated.
- If incurred to allow taxpayer to work, may qualify for dependent care credit, but no double dipping.

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Unusual Medical Expenses (cont.)

- **Physical Exam** - Even though not experiencing any symptoms of illness, is allowed.

- **Pregnancy Test** - The costs of self-administered pregnancy tests are deductible.

- **Marketplace Insurance less the Premium Tax Credit**

- **Schools and Education – Special** – Payments to a special school for a mentally impaired or physically disabled person if the main reason for using the school is its resources for relieving the disability.

- Disciplinary Programs - Do not include the cost of sending a problem child to a special school or program.

- **Smoking-Cessation Programs**

- Programs - Smoking-cessation programs and prescribed drugs designed to alleviate nicotine withdrawal are eligible medical expenses.
- Nonprescription drugs, such as nonprescription nicotine gum and certain nicotine patches, are NOT deductible.

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Unusual Medical Expenses (cont.)

- **Spouse - Prior or Current** – medical expenses paid for a prior or current spouse provided the taxpayer was married to the spouse either at:
 - The time the spouse received the medical services or
 - At the time the taxpayer paid the medical expenses.
- **Stem Cell Therapy and Storage**
 - Cord blood contains stem cells that doctors may use to treat disease. Thus, expenses for banking cord blood to treat an existing or imminently probable disease may qualify as deductible medical expenses.
 - Banking cord blood as a precaution to treat a disease that might possibly develop in the future does not satisfy the existing legal standard and is not deductible.
- **Sterilization** - The cost of a legally performed sterilization is deductible.

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Unusual Medical Expenses (cont.)

- **Surrogate Mother Expenses**
 - The Code does tell us that medical expenses are only deductible for the taxpayer, spouse and dependents.
 - Definition of a dependent for medical purposes (medical dependent) ignores the gross income and joint return tests.
 - If not a dependent, the expenses are NOT deductible.
 - An unborn fetus is not a dependent until born.
- **Weight-Loss Programs**
 - To be deductible, the program must be undertaken as treatment for a specific disease (including obesity) diagnosed by a physician.
 - Costs that are NOT deductible:
 - Weight-loss programs for general health or appearance.
 - Diet food item costs.
 - Gym, health club, or spa membership dues.

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Unusual Medical Expenses (cont.)

- **Medical Dependent**

- Medical expenses paid for dependents may be deducted
- An individual may be a medical dependent even if their gross income precludes a dependency exemption.

Example – The taxpayers' adult son was seriously injured in a motorcycle accident and did not have medical insurance. His parents paid all of his medical expenses for the year. Their son meets all of the dependent qualifications except for the gross income test. However, under the exception, the parents can still deduct the medical expenses on their 1040.

- **Divorced Parents** – Both parents can deduct the expenses they pay regardless of who claims their child.

- **Medical Reimbursement**

- Same year – Reduces year's expenses.
- Later year – Report as income, but not to extent of medical expense that was not deductible in the prior year because of the AGI limit; not taxable if claimed standard deduction.

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“SALT” Limitations (Tax Deductions)

- **State and Local Taxes (SALT)** are limited to \$10,000. This includes:

- Domestic real property tax,
- Foreign income tax (if not claimed as a tax credit),
- State and local income tax OR sales tax, and
- Personal property taxes

- **Attempts to Circumvent** - States and some local governments attempted to circumvent the SALT limitation by giving taxpayers credit against their state or local tax by making a charitable gift to a state or local charity and then having an unlimited charitable contribution.

- However, the states overlooked the 1986 Supreme Court holding where the taxpayer receives something in return (quid pro quo) for a contribution, making the contribution not tax deductible.

- Thus the \$10,000 limitation still applies pending any law change.

- **IRS Notice 2020-75** – Confirmed the viability of an entity's state tax being deductible at the entity level without the SALT limitation.

- **States Reactions** – Several states have passed legislation to take advantage of Notice 2020-75.

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Individual Tax Credits



DEDUCTIBLE

Child and Dependent Care Credit - Overview

- **Nonrefundable Tax Credit** – For expenses the taxpayer incurred for the care of a child, spouse, or other dependent while the taxpayer is gainfully employed (or is job seeking).
- **Maximum Expenses** (reduced by any dependent care benefits under a qualified employer plan):
 - \$3,000 for one qualifying child or dependent.
 - \$6,000 for two or more.
 - The expenses need NOT be evenly spent per child or dependent.
- **Earned Income (EI) Limit:**
 - Expenses limited to the taxpayer's EI.
 - For married taxpayers, the EI of lowest earning spouse.
 - Includes non-taxable combat pay.
 - Includes amounts less than \$400 net profit for Schedule C filers.
 - Includes imputed amount for TP using optional SE tax method.

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Child and Dependent Care Credit - Rules

- **Tax Year** - Credit only allowable in the **later of the tax year...**
 - The services are provided or
 - The expenses are paid.

AGI Adjusted Applicable Percentage

AGI Over	But Not Over	Applicable Percent	AGI Over	But Not Over	Applicable Percent
0	15,000	35	29,000	31,000	27
15,000	17,000	34	31,000	33,000	26
17,000	19,000	33	33,000	35,000	25
19,000	21,000	32	35,000	37,000	24
21,000	23,000	31	37,000	39,000	23
23,000	25,000	30	39,000	41,000	22
25,000	27,000	29	41,000	43,000	21
27,000	29,000	28	43,000	No Limit	20

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Child and Dependent Care Credit – Who can Claim

- **Married Taxpayers** (must file joint)
 - Taxpayers who are separated under a decree of divorce or separate maintenance are not married for purposes of the childcare credit.
- **Divorced or Separated Parents:**
 - Only the custodial parent can claim the credit.
 - Custodial parent is the one with custody the greater part of the year.
 - True even if the other parent claims the dependency.
- **Principal Place of Abode** – Must be same principal place of abode as the taxpayer's for more than half of the tax year.
- **Divorced or Separated Parents** – Only the custodial parent may claim the credit even if:
 - The custodial parent has waived the child's dependency to the non-custodial parent.
 - The child resides with the non-custodial parent for part of the year.
- **Custodial Parent** - Custodial parent is the parent with whom a child shares the same principal place of abode for the greater portion of the calendar year. (Reg. Sec. 1.21-1(b)(5)(ii))

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Child and Dependent Care Credit – Qualifying Individual

- TP's dependent who is under age 13 when care is provided;
- TP's spouse who was physically or mentally unable to care for themselves and lived with the TP for more than 1/2 the yr.
- A disabled person physically or mentally unable to care for themselves who lived with TP over half the year and who is either the taxpayer's dependent or would be a dependent except:
 - The person has gross income in excess of the year's limit (\$4,700 for 2023, up from \$4,400 in 2022),
 - The person filed a joint return, or
 - The taxpayer, or spouse if filing MFJ, could be claimed as a dependent on someone else's return.

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Child and Dependent Care Credit – Qualifying Expenses

- **School Expenses** – Below the level of kindergarten count.
- **Part-Time Employment** - Allocate expenses between days worked and days not worked.
 - However, if required to pay for care on a periodic basis that includes days worked and days not worked, the taxpayer is not required to allocate the expenses.
- **Payments to Related Individuals** – A credit is not allowed for amounts paid to the taxpayer's spouse or the parent of the taxpayer's child who is a qualifying individual.
- **Agency and Application Fees** - Application and agency fees may be employment-related expenses if the taxpayer is required to pay the expenses to obtain the care. Forfeited deposits do not qualify.

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Child and Dependent Care Credit – Special Situations

- **Summer School** - Is educational in nature and does not qualify.
- **Day Camp**
 - Must comply with laws where care is supplied for 6 or more.
 - Qualifies even though it might specialize in an activity such as sports, reading, math, etc.
 - Overnight camps are not a qualifying expense.
- **Care Centers for Sick Children** – Unanswered question by IRS.
- **Absence from Work** - Generally expenses must be allocated daily.
 - Exception - Short temporary absence – Safe harbor is up to 2 consecutive weeks. Only those costs required to be paid during the absence qualify for the exception.
- **Family Medical Leave Act** – Costs while on paid medical or maternity leave are not employment-related expenses. **Shift Workers** - Costs of child's overnight care and day care for parents who work at night and sleep during the day may be qualifying expenses.

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Child and Dependent Care Credit – Special Situations (cont.)

- **Kindergarten Expenses** – Kindergarten is considered educational whether part-time or full-time and therefore the costs do not qualify.
- **Private School Expenses** – Do not qualify, even if the taxpayer lives overseas and public education is unavailable.

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Child and Dependent Care Credit – Special Situations (cont.)

- **Live-In Caregivers** – The increased cost of the taxpayer's utilities attributable to providing room and board to a caregiver may constitute a qualifying expense.
- **Care Outside the Home** - For a qualifying individual who is a dependent or spouse incapable of self-care who regularly spends at least eight hours each day in the TP's household may qualify for the credit.

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Child and Dependent Care Credit – Dependent Care Assistance Program

- **Employer Program** – A dependent care assistance program is a written plan to provide dependent care assistance for the exclusive benefit of employees. The payments received under the plan and used by employees to pay dependent care expenses are excludable from the employees' income.
- **Employees** – Employees can contribute the lesser of:
 - Employee's earned income (lower earning spouse's earned income for married taxpayers) **OR**
 - \$5,000 (\$2,500 MFS)
- **Excess** – If amount contributed exceeds expenses, the excess must be included in income for the year.
 - (In 2022, this would have been reported on line 1e of Form 1040.)

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Child and Dependent Care Credit – Dependent Care Assistance Program (cont.)

- **Other Requirements:**
 - No more than 25% of the assistance the plan provides during the year may be paid on behalf of owners (including spouses and dependents) of more than 5% interest in the employer's business;
 - The program cannot discriminate in favor of "highly-compensated" employees or their dependents.
- **Married Filing Separate:**
 - Cannot claim the credit:
 - Unless legally separated.
 - Except custodial parent can exclude dependent care benefits.
 - Except those qualifying as head of household can claim the credit or exclude the dependent care benefits.

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Child and Dependent Care Credit – Split Schedule C Strategy

- When both spouses are involved in the operation of an unincorporated business, it is common, but incorrect, to be reported on one spouse's Sch C.
- The spouse not filing a Sch C loses out on their own eligibility for Social Security benefits and the ability to fund a SEP account.
- In addition, to claim a childcare credit, both spouses on a joint return must have earned income (or imputed income if one is a full-time student or is disabled), so unless the non-Schedule C spouse has another source of earned income, the couple will not be allowed a childcare credit.
- There are 2 ways to remedy this situation, either:
 - By filing as a partnership or
 - Doing a joint venture where each files a Schedule C. Both spouses must materially participate.
- **Observations:**
 - If the net income from the business exceeds the annual cap on income subject to the Social Security tax, the combined self-employment tax for the spouses with split Schedule Cs will exceed what a single spouse would have paid if he or she had filed a single Schedule C.
 - In addition, when filing split Schedule Cs, be aware of the different allocation of income for purposes of retirement plans and the opportunity for both spouses to participate in IRAs and SE Retirement Plans.

100

Child Tax Credit for 2018 – 2025 (Except 2021)

- **Maximum** - per qualifying child is \$2,000, nonrefundable unless qualifies for the refundable portion of the credit:
- **Maximum Refundable Portion 2023**
 - \$1,600 per eligible child, up from \$1,500 in 2022
 - **Inflation Adjusted** – Refundable amount is inflation adjusted, but not the \$2,000 credit.

101

Child Tax Credit – Qualified Child

- Son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, or a descendant of any of them (e.g., grandchild),
- Was under age 17 at the end of the tax year,
- Child did not provide over half of his or her own support,
- Lived with the taxpayer for more than half of the tax year,
- Was a U.S. citizen, a U.S. national, or a resident of the U.S.,
- Was claimed as the taxpayer's dependent, and
- Has a Social Security number.
-
- **Adopted child** - An adopted child is always treated as the taxpayer's own child.
- **Time Lived with the Taxpayer** – A child is considered to have lived with the taxpayer for the entire tax year if the child was born or died during the year and the taxpayer's home was this child's home for the entire time he or she was alive.
- **Temporary Absences** - Special circumstances, such as school, vacation, medical care, military service, or business, also count as time lived with the taxpayer.

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Child Tax Credit – Qualified Child (cont.)

- There are also special rules for kidnapped and missing children.
 - **Kidnapped Child** - If presumed by law enforcement to have been kidnapped by someone other than a family member.
 - **Children of Divorced or Separated Parents** – Only the parent who claims the child as a dependent can claim the Child Credit. Generally, will be the custodial parent unless waived the dependency to the noncustodial parent.
 - **Foreign Earned Income or Foreign Housing Costs Limitation** - a taxpayer who excludes foreign earned income or foreign housing costs is prohibited from claiming the refundable part of the child tax credit.

103

Child Tax Credit – Identification Requirements

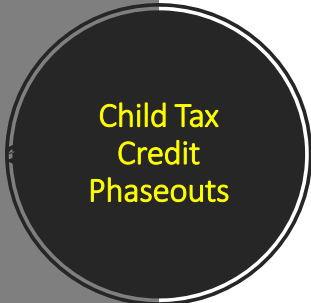
- **Child**
 - Although Sec 24(h)(7)(B) – SSN Required – says a child's SSN must be obtained before due date of the return (no mention of extensions), the 2022 Form 8812 includes the following language:
 - *If you have a qualifying child who does not have the required SSN, you cannot use the child to claim the CTC or ACTC on either your original or an amended 2022 return. The required SSN is one that is valid for employment and is issued before the due date of your 2022 return (including extensions).*
 - The IRS apparently has taken a liberal interpretation of “due date of the return” and includes returns where a Form 4868 extension has been filed extending the due date.
- **Parent(s)**
 - The parents must have either an SSN or an ITIN to claim the credit.
 - You Must Have a TIN by the Due Date of Your Return - If you, or your spouse if filing jointly, do not have an SSN or ITIN issued on or before the due date of your return (including extensions), you cannot claim the CTC, ODC, or ACTC on either your original or an amended return. If you apply for an ITIN on or before the due date of your return (including extensions) and the IRS issues you an ITIN as a result of the application, the IRS will consider your ITIN as issued on or before the due date of your return.
 - Thus, a taxpayer with an ITIN can qualify for the credit if the qualifying child has an SSN.

104

Child Tax Credit – Other Dependent Credit

- **Credit**
 - \$500
 - Non-refundable
- **Includes and individual who:**
 - Is claimed as a dependent...examples:
 - Qualified children exceeding age limits for CTC
 - Dependent without an SSN
 - Parent
 - Did not qualify for the CTC/ACTC
 - Has an SSN or ITIN
 - Is a U.S. citizen, U.S. national, or U.S. resident alien.
- The credit is reduced by \$50 for each \$1,000 (or fraction of \$1,000) of modified AGI over the thresholds.
- Modified AGI is AGI increased by amounts excluded from gross income under IRC § 911, 931, or 933 (the foreign exclusions).

105



Child Tax Credit Phaseouts

Child & Dependent Tax Credits Phaseout Thresholds

Filing Status	2021	2018 - 2025 (Except 2021)
Married joint & SS	\$150,000	\$400,000
Married Separate	\$75,000	\$200,000
Head of Household	\$112,500	\$200,000
All Others	\$75,000	\$200,000

106

Child Tax Credit – Refundable Credit

- Applies to certain taxpayers who are unable to claim the full amount of the child tax credit because it is limited to tax liability.
- Can be as much as \$1,400 (adjusted for inflation to **\$1,600** for 2023) of the tax credit.
- Based on an earned income computation.
- If 3 or more qualifying children, amount of SS and Medicare taxes and earned income credit claimed are also factors.
- **Earned income also includes:**
 - Excluded combat zone pay.

107

Savers Credit – Qualifying Contributions

- 401(k) plan,
- 403(b) annuity (TSA), or eligible deferred compensation arrangement of a state or local government (a 457 plan),
- Tax-exempt employee-funded pension plan (typically a union plan),
- SIMPLE IRA or salary reduction SEP,
- Traditional or Roth IRA, and
- Voluntary after-tax employee contributions to a qualified retirement plan.

108

Savers Credit – Eligibility and Amount

- Any individual who has reached age 18 as of the close of the tax year except :
 - Dependent of Another
 - Full-Time Student
- The credit is equal to the applicable percentage of the first \$2,000 of the qualified retirement savings contributions.
- Married taxpayers can each qualify for the full credit.

2023 APPLICABLE PERCENTAGE						
Modified Adjusted Gross Income						Applicable Percentage
Joint Return		Head of Household		Others		
Over	Not Over	Over	Not Over	Over	Not Over	
\$ 0	43,500	\$ 0	32,626	\$ 0	21,750	50
43,500	47,500	32,626	\$35,625	21,750	23,750	20
47,500	73,300	\$35,625	54,750	23,750	36,500	10
73,300		54,750		36,500		0

109

Savers Credit – Changes After 2026

- The credit will be eliminated
- Replaced with a federal government retirement plan contribution
- The match is 50% of IRA or retirement plan contributions up to \$2,000 per individual.
- **Not effective until 2027** – So plenty of time for more detail.
- Until then, the credit continues to be 50%, 20%, 10% or 0%, depending on MAGI, of the first \$2,000 of retirement plan contributions.

110

Adoption Credit

- **Credit** – 100% of qualified adoption expenses.
 - Can be taken over several years.
 - But the total for all years is limited to the max credit.

CREDIT & PHASE-OUT RANGES			
Year	2022	2023	2024
Max Credit	\$14,890	\$15,950	\$16,810
Phase-out:			
Threshold	\$223,410	\$239,230	\$252,150
Complete	\$263,410	\$279,230	\$292,150

111

Adoption Credit – Eligible Child

- **Eligible Child:**
 - Either a person under the age of 18 at the time a qualified expense is paid or incurred, **or**
 - A person physically or mentally incapable of self-care.
- **U.S. child with Special Needs** - May be able to exclude up to \$15,950 (2023) and claim a credit for additional expenses up to \$15,950 (minus any qualified adoption expenses claimed for the same child in a prior year). See the instructions for Form 8839.
 - Max. credit allowed regardless of amount of expenses paid.

112

Adoption Credit – Qualified Expenses

- **Reasonable and Necessary**
 - Adoption fees, court costs,
 - Attorney fees,
 - Expenses required by a state as a condition of adoption, and
 - Other directly related adoption expenses.
- **When Expenses Are Paid Determines Year Credit is Allowed**
 - Paid in a year before adoption is final - The credit is allowed for the tax year **following** the year in which it is paid or incurred.
 - Paid in the year the adoption is final - The credit is allowed for tax year in which it's paid or incurred.
 - Paid in a year after the adoption is final - The credit is allowed for the tax year in which it's paid or incurred.
- **Failed Adoption of a U.S. Child –**
 - Expenses are eligible for the credit.
 - Follows the same rules as to when the credit is allowed.
 - However, the unsuccessful/successful adoptions are treated as one for purposes of the dollar limit on the credit.

113

Adoption Credit – Foreign Adoption

- **Credit**
 - Only allowed in the year the adoption is final.
 - Except expenses paid or incurred in year after adoption is final are allowed in the year paid or incurred.
- **Re-adoption Expenses** - Many parents incur expenses for home state re-adoptions for practical reasons, such as obtaining a birth certificate issued in English. The re-adoption expenses are treated as qualified expenses.

114

Home Solar Credit – Revised Sunset

- Credit applies to:
 - Solar electric panels, solar hot water,
 - Fuel cells, small wind energy,
 - Geothermal heat pumps, and
 - Biomass fuel property
- Before IR Act 2022
 - Credit was being phased out from 30% to 22%
 - Sunsetting after 2023
- Inflation Reduction Act of 2022 Extension:
 - Back to 30% in 2022 (up from 26%)
 - Won't sunset until after 2034

115

Home Solar Credit – Extension and Future Phaseout

Applicable Year	Credit Percentage
Thru 2019	30%
2020 - 2021	26%
2022 - 2032	30%
2033	26%
2034	22%
AFTER 2034	0%

116

Home Solar Credit – Other Issues

- Applies to primary & second homes located in the U.S.
- Installation costs
- Roof
- Resident (need not be owner to qualify for credit)
- Swimming pools & hot tubs
- Basis adjusted by amount of credit
- Leased Installations – Lessor gets the credit, not the resident.
- Multiple Installations – Any original ok, but not replacements
- Timing - Expenditures treated as made when the original installation is completed except home construction or reconstruction.
- Mixed Use

117

Home Solar Credit – Battery Guidance

- **IRS Letter Ruling 201809003**
 - Battery attached to solar system is qualified property
 - Included with original installation or later
 - But...to be qualifying property it can only be charged with solar energy...not from the grid.
- **Inflation Reduction Act Changes**
 - Adds the term “qualified battery storage technology expenditure”.
 - Effective after December 31, 2022,
 - Covers the cost of battery storage technology which:
 - Is installed in connection with a dwelling unit in the United States that is used as a residence by the taxpayer, and
 - Has a capacity of not less than 3 kilowatt hours.
 - Unlike the letter ruling, the Inflation Reduction Act makes no mention of the battery only being allowed if charged by solar energy.

118

Home Solar Credit – Additional Issues

- **Builder Pass-Through**

- Can be taken for newly constructed homes if the costs can be separated from the home construction **and**
- The required certification documents are available.
- The credit for the identifiable solar expenditures in connection with the construction or reconstruction of a structure are treated as made when the taxpayer's original use of the constructed or reconstructed structure begins.

- **Residential Rentals**

- Don't qualify for Sec 25D credit
- May qualify under Sec 48 as part of the Sec 38 general business credit

119

Home Solar Credit – Additional Issues (cont.)

- **Resident Gets the Credit**

- The taxpayer need not own the property to qualify for the credit, as the taxpayer need only be a "resident" of the home.
- For the Residential Clean Energy Credit, the code does not specify that an individual must own the home, only that it is the taxpayer's residence.
- **IRC §25D(d)(2) - Qualified solar electric property expenditure** - The term "qualified solar electric property expenditure" means an expenditure for property which uses solar energy to generate electricity for use in a dwelling unit located in the United States and used as a residence by the taxpayer.

Example: Son lives with his mother who owns the home. Son pays to have the solar system installed. The son gets the credit.

120

Energy Efficient Home Modification Credit

• **Enhanced Credit**

- The new legislation did away with the minimal \$500 lifetime limit by replacing it with a \$1,200 annual limit and increased the credit rate from 10% to 30%.
- This credit is a nonrefundable personal tax credit and there are no credit carryover provisions.
- As before, under prior law, there are certain credit limits that apply to the various types of energy-saving improvements.
- After 2021, this credit can be claimed by the home resident.

• **Home Energy Audit**

- Addition of up to a \$150 maximum credit
- Identifies the most significant and cost-effective energy efficiency improvements with respect to a dwelling unit, including an estimate of the energy and cost savings with respect to each such improvement.
- Conducted by a home energy auditor
 - Meets the certification or requirements to be specified by IRS.
 - Specifications available within 365 days of Enactment, i.e., by 8/15/2023.
 - Law eliminates treatments of roofs as creditable after 2022.
- Identification Number Requirement – No credit after December 31, 2024, without a qualified product identification number.

121

Energy Efficient Home Modification Credit – Creditable Expenditures

- \$600 credit for windows, and skylights.
- \$250 credit for any exterior door (\$500 total for all exterior doors).
- \$300 credit for residential qualified energy property expenses
- Notwithstanding a \$2,000 annual limit applies to specified heat pumps, heat pump water heaters, and biomass stoves and boilers.
- The new law eliminates treatment of roofs as creditable after 2022
- The new law adds air sealing insulation as a creditable expense.
- **Residential energy property** (30% of costs, including labor, up to \$600 for each item) satisfying the energy efficiency requirements in Q1 under the Energy Efficiency Requirements section:
 - Central air conditioners;
 - Natural gas, propane, or oil water heaters;
 - Natural gas, propane, or oil furnaces and hot water boilers; and
 - Improvements to or replacements of panelboards, sub-panelboards, branch circuits, or feeders that are installed along with building envelope components or other energy property listed in the IRS's FAQs and enable its installation and use.

122

Energy Efficient Home Modification Credit – Creditable Expenditures (cont.)

- **Heat pumps and biomass stoves and biomass boilers** - (30% of costs, including labor) satisfying the energy efficiency requirements in Q1 under the Energy Efficiency Requirements section:
 - Electric or natural gas heat pump water heaters;
 - Electric or natural gas heat pumps; and
 - Biomass stoves and biomass boilers.

123

Energy Efficient Home Modification Credit – Other Issues

- Nonrefundable personal credit.
- No carryover.
- Offsets AMT.
- No specific prohibition: Swimming pools & hot tubs.
- Basis adjustment – By amount of the credit.
- Principal residence only
- Modifications originally placed in service by the taxpayer.
- Located in the U.S.
- Taxpayer can claim credit for the residence even though they do not own it after 2021.

124

Credit for Buying Energy Efficient Homes

- The Inflation Reduction Act of 2022 retroactively applied the Sec 45L credit to 2022 and extends it through 2032.
- Credit limits have changes post-2021:
 - **\$2,500 Credit** - for single family and manufactured homes when constructed per the standards set by the Energy Star Residential New Construction Program or the Manufactured Homes Program.
 - **\$5,000 Credit** - for single family and manufactured homes when they are certified by the Department of Energy as a Zero Energy Ready Home.
 - **\$500 Credit** - For multifamily homes when meeting the Energy Star Single Family New Homes Program.
 - **\$1,000 Credit** - for multifamily homes when they are certified by the Department of Energy as a Zero Energy Ready Home

125

Credit for Buying Energy Efficient Homes – Prevailing Wage Requirements

- Prevailing Wage Requirements Introduces a new requirement to claim the credit.
 - For any qualified residence, the taxpayer must ensure that any laborers and mechanics employed by the taxpayer or any contractors and subcontractor in the construction of the residence are paid wages at rates not less than the prevailing rates for construction, alteration, or repair of a similar character in the locality in which the residence is located as determined by the Secretary of Labor.
 - Failure to satisfy the prevailing wage requirements can be cured by paying to each affected worker an amount equal to the difference between the amount actually paid and the amount which would have been paid under the prevailing wages rules, plus interest, and paying a \$5,000 penalty per affected worker.

126

Credit for Buying Energy Efficient Homes – Other Issues

- Basis must be adjusted by amount of the credit
- Home must be in the U.S.
- Credit claimed on Form 8908...transferred to Form 3800
- General Business Credit
 - Amount not used in current year carried back one year and forward 20.
- Notice 2022-61 provides initial guidance related to the administration of the prevailing wage requirement to receive increased tax credits for certain incentives including this credit.

127

Alternative Fuel Refueling Property Credit

- Credit through 2022
 - Includes alternative refueling property, including electric vehicles.
 - Must be located where the vehicle is recharged.
 - Includes installation of a home charging station for an EV.
 - The creditable cost includes labor.
 - The credit is 30% of the cost and claimed on Form 8911.
 - Maximum credit is:
 - Personal use - limited to \$1,000 per home and is a non-refundable personal credit allowed against the AMT.
 - Business use - limited to \$30,000
 - Credit must be split between the personal and business use credits.
-

128

Alternative Fuel Refueling Property Credit (cont.)

- Credit 2023 through 2032
 - The credit for depreciable property is at a rate of 6%
 - 30% if prevailing wage and apprenticeship requirements are met.
 - Subject to a limit of \$100,000.
 - Definition includes bidirectional charging equipment and provides that the credit is available for electric charging stations for two- and three-wheeled vehicles that are intended for use on public roads.
 - Under the Act, the credit limitation applies per single item of qualified alternative fuel vehicle refueling property instead of all such property at an individual location.

Charging or refueling property will only be eligible for the credit if placed in service within a low-income or rural census tract.

-

129

Clean Vehicle Credit - Transition Rule

- As part of the Inflation Reduction Act of 2022, a taxpayer who, from January 1, 2022, and before August 16, 2022, entered a written binding contract to purchase, a new plug-in electric drive motor vehicle and placed that vehicle in service on or after August 16, 2022, may elect to use the credit rules in effect before the Inflation Reduction Act changes.
- This allows a taxpayer to claim the original EV tax credit without the new restrictions on:
 - MSRP,
 - Buyer income (MAGI), or
 - Manufacturing Location (Within North America).
- Even if delivery isn't taken until 2023 or later.
- However, the 200,000 vehicles sold by a manufacturer limitation will still apply when claiming the credit.

130

Clean Vehicle Credit - Transition Rule (cont.)

- We are aware of two EV manufacturers that offered these contracts: Fisker and Rivian.
- To elect the credit under the prior rules the credit must be claimed on the taxpayer's 2022 tax return after the taxpayer takes delivery of the vehicle, even if that delivery is in 2023. Depending on the date the vehicle is delivered, the credit is claimed on an original, superseding, or amended 2022 tax return.
- Taxpayers with written contracts in 2022 who took delivery in 2023 or after must use August 15, 2022, as the date placed in service when filling out Form 8936, line 3.

131

Clean Vehicle Credit - Starters

- Beginning in 2023 the 200,000-manufacturer limit is gone – So all manufacturers are back in play...
- **BUT**...there are some stringent manufacturing and component rules.
- The credits are no longer available to higher income taxpayers.
- More expensive vehicles will not qualify for the credit.
- There is a credit for both new and used qualifying vehicles.

132

New Clean Vehicle Credit - Amount

- **Effective:** 2023 and through 2032.
- **Code Title:** Changed from Qualified Plug-in Electric Drive Vehicles to Clean Vehicle Credit.
- **Credit Amount:** Total still a maximum of \$7,500 but in 2 parts:
 - \$3,750 if the Critical Minerals requirement is met, and
 - \$3,750 if the Battery Component requirement is met
- **Minimum Battery Capacity: 7 kilowatt-hours**, up from 4 kilowatt-hours under prior law.
- **Fuel Cell Motor Vehicle** - The term "new clean vehicle" includes any new qualified fuel cell motor vehicle that also meets the final assembly and report requirements.

133

New Clean Vehicle Credit - Critical Mineral Requirement

- A portion of the credit, \$3,750, is based upon the percentage of the value of the applicable critical minerals contained in the battery that were:
 - Extracted or processed in the United States or in any country with which the United States has a free trade agreement in effect, or
 - Recycled in North America
 - Is equal to or greater than the applicable percentage

APPLICABLE PERCENTAGES						
Year	2023	2024-2025	2026	2027	2028	Later Years
Percentage	50	60	70	80	90	100

134

New Clean Vehicle Credit – Battery Component Requirement

- This second portion of the credit, also \$3,750, is based upon the percentage of the value of the components contained in the battery that is used in the vehicle that:
 - Were manufactured or assembled in North America is equal to or greater than
 - The applicable percentage (same percentage as the critical minerals).

APPLICABLE PERCENTAGES						
Year	2023	2024-2025	2026	2027	2028	Later Years
Percentage	50	60	70	80	90	100

135

New Clean Vehicle Credit – Final Assembly Requirement

- Final assembly of the vehicle occurs in North America.
- Manufacturer produces a new clean vehicle at, or using, a plant, factory, or other place from which the vehicle is delivered to a dealer or importer.
- Including all component parts necessary for the mechanical operation of the vehicle included with the vehicle, whether the component parts are permanently installed in or on the vehicle.
- **IMPORTANT:** The final assembly requirement applies to vehicles sold after the date of enactment, August 16, 2022.
 - Get final assembly information either from the VIN or the assembly plant listed on the sticker affixed to the vehicle.

136

New Clean Vehicle Credit – Foreign Entity of Concern

- The term "new clean vehicle" does not include any vehicle placed in service after December 31, 2023, where any of the components contained in the battery of the vehicle were manufactured or assembled by a "foreign entity of concern".

137

New Clean Vehicle Credit – Manufacture Qualification Responsibility

- **The preceding limits will not be your responsibility to determine. The dealer report (certification) will take care of that, and the IRS will provide a list of qualifying vehicles and qualifying credit amounts as they have done for the plug-in electric vehicle credit in the past.**
- The dealer (seller) of the vehicle must furnish a report (certification) to the buyer **and** the IRS that includes:
 - The name and taxpayer identification number of the buyer;
 - The vehicle identification number (VIN) of the vehicle, unless, by U.S. Department of Transportation rules, the vehicle is not assigned a VIN;
 - The battery capacity of the vehicle;
 - Verification that the original use of the vehicle commences with the taxpayer; and
 - The maximum Clean Vehicle credit allowable to the buyer with respect to the vehicle.

138

New Clean Vehicle Credit – MSRP Limitations

- No credit for a vehicle with an MSRP more than the following:

MANUFACTURER'S SUGGESTED RETAIL PRICE LIMITATION	
Vans, sport utility vehicles, and pickups	\$80,000
Other vehicles	\$55,000

- The IRS FAQs on its website defines MSRP for this purpose as:
 - The base retail price suggested by the manufacturer, **plus**
 - The retail price suggested by the manufacturer for each accessory or item of optional equipment physically attached to the vehicle at the time of delivery to the dealer.
 - It does not include destination charges or optional items added by the dealer, or taxes and fees.

139

New Clean Vehicle Credit – MAGI Limitations

- No credit if the lesser of the MAGI for the:
 - Current tax year, **or**
 - The preceding tax year that exceeds the threshold amounts
- No phaseout; one dollar over limit and no credit will be allowed.

MAGI LIMITATION	
Filing Status	MAGI
Married Filing Joint & SS	\$300,000
Head of Household	\$225,000
Others	\$150,000

140

Used Clean Vehicle Credit – Definition

- Previously Owned Clean Vehicle is a motor vehicle:
 - The model year is at least two years earlier than the calendar year in which the taxpayer acquires it.
 - Original use of which starts with a person other than the TP.
 - Has a gross vehicle weight rating of less than 14,000 pounds,
 - Powered to a significant extent by an electric motor with a battery capacity of seven kilowatt hours or more,
 - Capable of being recharged from an external source.
 - Must be purchased from a dealer
 - Dealer must provide a certification and vehicle information to the purchasing taxpayer and to the IRS,
 - Or is a clean fuel-cell vehicle with a gross weight rating of less than 14,000 pounds.

141

Used Clean Vehicle Credit – Amount

- Credit Amount - Acquired and placed in service after 2022 and before 2033, the credit is equal to the lesser of:
 - \$4,000 or
 - 30% of the vehicle's sale price.
- Modified AGI Limit - No credit is allowed if the lesser of the MAGI of the taxpayer for the:
 - Current tax year, OR
 - The preceding tax year exceeds the threshold amount below:

MAGI LIMITATION FOR PREVIOUSLY OWNED CLEAN VEHICLE CREDIT	
Filing Status	MAGI
Married Filing Joint & SS	\$150,000
Head of Household	\$112,500
Others	\$75,000

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Used Clean Vehicle Credit – Qualified Sale to a Qualified Buyer

- A qualified sale is a sale:
 - By a dealer,
 - For a price of \$25,000 or less, and
 - Which is the first transfer since 8/16/2022 to a qualified buyer other than the original buyer of the vehicle.
- A qualified buyer is an individual who:
 - Purchases the vehicle for use and not for resale,
 - Is not a dependent of another taxpayer*, and
 - Has not been allowed a credit for a previously owned clean vehicle during the three-year period ending on the sale date.

143

Clean Vehicle Credit – Credit Transfer to Dealer

- Available for vehicles acquired after 2023
 - Election made on or before purchase date
 - Buyer can transfer credit to dealer
 - Thus, reducing initial purchase costs
 - If AGI limit later precludes taxpayer from claiming the credit, the credit must be recaptured on the taxpayer's tax return for year of purchase.
 - Applies to New and Used vehicle purchases
- Procedure to accomplish this will be forthcoming.

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This Year's Credit Supplement



Supplement 3 – Earned Income Tax Credit



Supplement is located at the end of the PowerPoint Presentation after the contact information slide.

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Supplement 1 – Employee Stock Options



Employee Stock Options

NONSTATUTORY OPTIONS

- When a non-statutory option is exercised:
 - The difference between exercise price and option price is treated as wages and employer includes it in the employee's W-2 income and Box 12 as code V.
 - Difference is subject to usual withholding including FICA.
 - The basis in the purchased stock is the amount paid + the amount included in income when exercised.
 - Holding period begins on the date of exercise.
- Employees will generally exercise and sell on the same day. Sale is usually handled by a brokerage firm and will result in a loss equal to the sales costs



Employee Stock Options

RESTRICTED STOCK UNITS (RSUs)

- Employer will grant a specific number of shares to an employee.
- Stock is not issued until the employee satisfies vesting requirements.
- Vesting requirements can include both time and performance.
- If the vesting requirements are not met, the stock goes back to the company.
- When the stock is issued, the tax treatment is the same as a nonqualified option.
- Holding period begins when stock is issued.
- Short- or long-term capital gain depending upon holding period.

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Employee Stock Options

RESTRICTED OPTIONS (and IRC §83b Election)

- Where an employer compensates an employee for services with stock, the excess of the FMV of the stock over any amount paid for the stock is treated as income when the stock is received.
- If the stock can't be sold or is at substantial risk, the income is deferred until the earlier of:
 - When it is no longer subject to that risk, or
 - It becomes transferable free of the risk.
- If the IRC §83(b) election is made within 30 days of the transfer of the restricted stock, the income recognized is the FMV of the shares on the date of grant less any amount the employee paid for the stock. This amount becomes the basis of the stock.

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Employee Stock Options

INCENTIVE (STATUTORY) OPTIONS – PART ONE

- **Income Recognition** - Generally no income recognized at the time the option is exercised if the stock is held for:
 - More than 1 year after the option was exercised, and
 - More the 2 years after the option is granted.
- **AMT** – However, an AMT deferral preference applies in the year of exercise.
 - The preference income is equal to fair market value of the stock at exercise over the exercise price.
- **Payroll Tax** - The exercise is not subject to FICA or the extra 0.9% Medicare tax.
- **Dual Basis:**
 - Regular Tax Basis: exercise (option) price
 - AMT Basis: FMV at date of exercise

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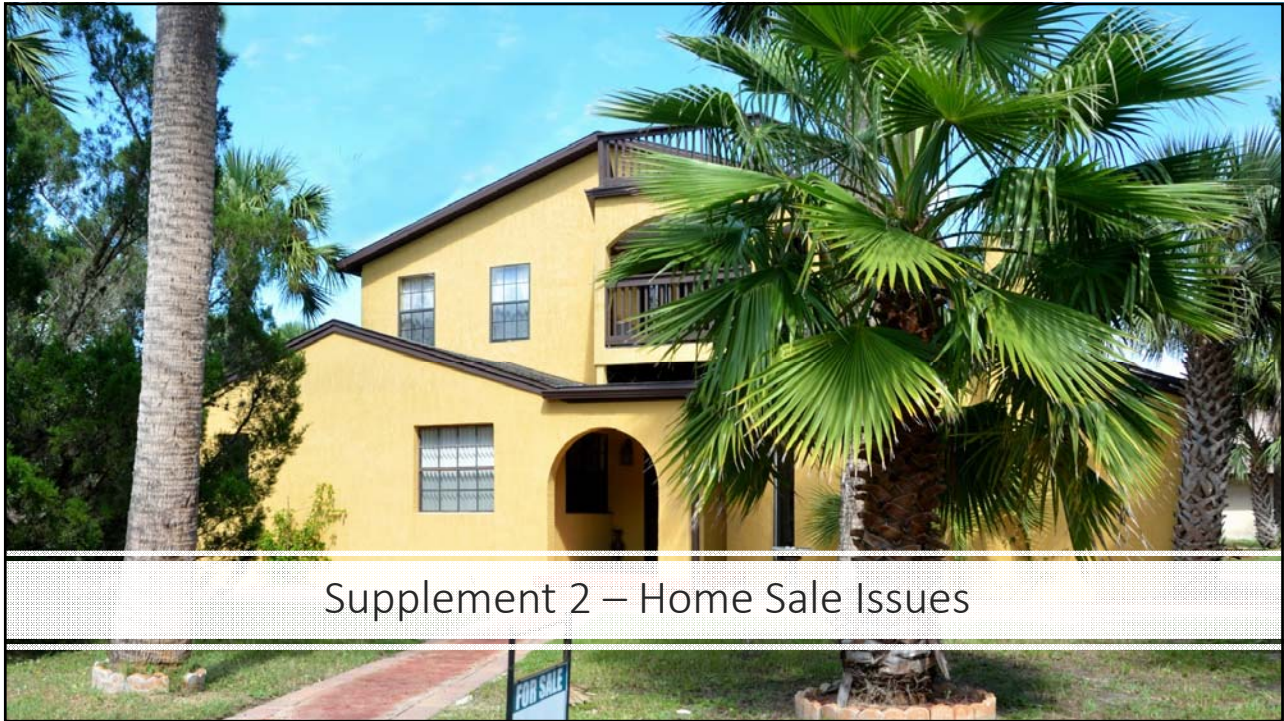


Employee Stock Options

INCENTIVE (STATUTORY) OPTIONS – PART TWO

- **Big Problem** – The AMT in the year of exercise will in many cases create a significant tax liability without the stock sale proceeds, thus creating a cash flow problem for most.
 - Can be overcome by selling in small quantities to avoid the AMT.
 - Many forego the incentive option treatment and sell the stock upon exercise; in which case it is treated like a nonqualified option.
- For sales where there is an AMT, an AMT Credit carryover will be created.

152



Supplement 2 – Home Sale Issues



Home Sale

HOME GAIN EXCLUSION QUIRK

Question - Unmarried couple living together for several years, but only one of them owns the home they are living in. They decide to get married and sell the home. Does it make any difference if they sell the home before or after they get married?

- Oh yes, a big difference.
 - If sold before they marry the max exclusion is limited to \$250,000.
 - If they wait until married the exclusion is \$500,000 if:
 - **Either** the taxpayer or spouse meets the **ownership test**.
 - **Both** the taxpayer and spouse meet the **use test**.
 - During the 2-year period ending on the date of the sale, neither excluded gain from another sale.

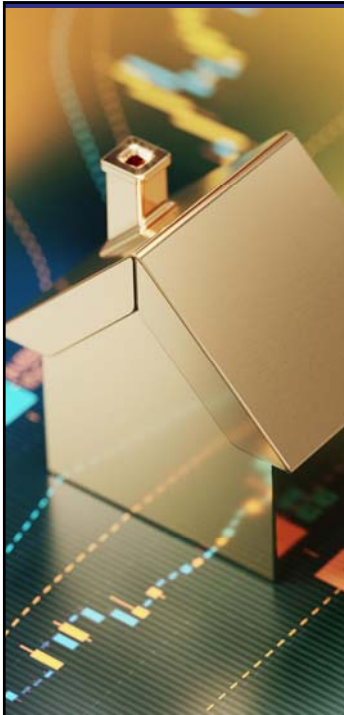


Home Sale

RENTAL CONVERTED TO PRINCIPAL RESIDENCE

- Must still meet 2 out 5 years use and ownership tests.
- Non-qualified periods are periods of time the home was rented.
- Gain attributable to non-qualified periods is not excludable
- Non-qualified periods do NOT include:
 - Periods before January 1, 2009.
 - Periods after the last date the property is used as the principal residence of the taxpayer or spouse (regardless of use during that period), and
 - Not to exceed two years that the taxpayer is temporarily absent by reason of a change in place of employment, health, or, to the extent provided in regulations, unforeseen circumstances.

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Home Sale

INHERITED HOME

- **Basis** – The basis of an inherited home is generally the FMV of the home at the date of decedent's death.
- **Appraisal** – If sold almost immediately to an unrelated party, the basis can generally be justified to be the sales price. Otherwise, a certified appraisal is appropriate.
- **Gain/Loss** – A sale of an inherited home rarely results in a gain because:
 - Sales price and basis generally are either the same or nearly the same and
 - Sales expenses will often cause a loss.

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Home Sale

LOSS ON THE SALE – INHERITED HOME

Is a Loss Deduction Allowed?

- Generally, a beneficiary will sell the residence through a broker and will have substantial sales costs which usually equates to a loss.
- A frequent question is whether a loss is allowed on the sale.
- The answer to that question depends upon the beneficiary's use of the property after inheriting it.
- Campbell (1945) TC 272 – Loss allowed if the beneficiary immediately attempts to rent or sell the property.
- Crawford (1951) TC 678 - Loss allowed if the beneficiary indicates his intention to move and does so as soon as he can locate other quarters.

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Home Sale

EXCEPTIONS TO USE TEST

Individuals with a Disability

- If, during the 5-year period before the sale of the home the taxpayer:
 - Becomes physically or mentally unable to care for themselves, and
 - Owned & lived in the home as their main home for at least 1 year.
 - Taxpayer is considered to have lived in the home during any time that they owned the home and lived in a licensed facility (including a nursing home).
 - Living with a friend or relative in their home won't qualify.
 - Must still also meet the ownership requirement.
- **Temporary Absence** – Short temporary absences, such as for vacation or other seasonal absence (even though accompanied with rental of the residence), are counted as periods of use.

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Home Sale

EXCEPTIONS TO USE TEST - Continued

- **Home Used as Rental After Home Use** – Where an individual uses a home and then subsequently rents it before sale, the sale will still qualify for the IRC §121 exclusion if the individual meets the ownership and use periods.
- **Depreciation** – Of course any gain attributed to depreciation cannot be excluded by IRC §121.
- **CAUTION** – This does not apply if the rental period occurs before the use as the taxpayer's primary residence. If that occurs, then the non-qualified use provisions apply as previously discussed.

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Home Sale

ADDITIONAL ISSUES

- **Buyer defaults** – Upon reacquisition of the home the excluded amount will be taxable as a LTCG. (*Debough, 2014 TC17*)
- **Out-spouse** – Where an ex-spouse retains the home for a period before selling, the out-spouse's use period mirrors that of the ex-spouse and thus will qualify for an exclusion when the home is sold.
- **Home Jointly Owned** – Unmarried Taxpayers - Each can qualify for a \$250K exclusion if otherwise qualified.
- **Sale of Partial Interest** – If an individual sells a part interest in a home and the exclusion is less than the maximum allowed, the balance can be used in a subsequent sale.
- **Sale of Vacant Land Adjacent to a Home** – Is a sale of a partial interest if: the land is part of the home, not used for non-residential purposes and the other IRC §121 qualifications are met.

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Home Sale

ADDITIONAL ISSUES - Continued

- **Home Held in a Revocable Trust** – Can qualify for an exclusion.
- **Home Held in an Irrevocable Trust** – A private ruling reveals a potential pitfall where a married couple transfers their residence to a revocable trust which becomes irrevocable at first spouse's death – the \$250,000 home sale exclusion may be completely lost or available only to a limited extent even though the surviving spouse has the continued right to occupy the residence.
- **Mixed Use Property (Home & Business)**
 - Same structure – The exclusion applies to entire gain except for gain as the result of depreciation. A loss is not allowed.
 - Separate structure – Treat as two sales. The exclusion only applies to the home structure. If the business portion results in a loss, it is deductible.

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Supplement 3 – Earned Income Tax Credit



EITC QUALIFICATIONS

Taxpayers

- TP and spouse (if filing jointly) are U.S. citizens or resident aliens all year.
- Have a valid SSN by the return due date (including extensions).
- Childless Claimant - Must be age 25 or over, but not over 65.
- Have earned income.
- No foreign earned income or foreign housing exclusion.
 - If the taxpayer claims either, they will not qualify for the EITC for the year.

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EITC QUALIFICATIONS - Continued

Qualifying Children:

- Have a valid SSN by the return due date (including extensions, if an extension is filed).
- Must be related to the taxpayer (see full list in the BB).
- Live with the TP in the U.S. more than half the year (except for temporary absences).
- Born or died during the year is treated as living with the taxpayer the entire year.
- Must be younger than the claimant
- Cannot file a joint return unless solely for refund.

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EITC

QUALIFICATIONS - Continued

- **Qualifying Children:**
- Under age 19 or a full-time student under age 24 end of the tax year.
 - A full-time student is enrolled for the number of hours or courses a school considers full-time during some part of 5 calendar months during the year. Months need not be consecutive.
 - Age test does not apply to permanently and totally disabled.
 - A child is permanently and totally disabled if **both** apply:
 - Cannot engage in any substantial gainful activity because of a physical or mental condition, and
 - A doctor determines the condition has lasted or can be expected to last continuously for at least a year **or** can lead to death.

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EITC

EARNED INCOME REQUIREMENT

Year	Qualifying Children	Credit %	Earned Income	Maximum Credit
2023	None	7.65	7,840	600
	1	34.00	11,750	3,995
	2	40.00	16,510	6,604
	3	45.00	16,510	7,430

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EITC

CREDIT PHASEOUT

- The EITC can't exceed the excess (if any) of:
 - The credit percentage times the earned income amount over
 - The phase-out percentage times the amount by which the taxpayer's AGI (or, if greater, the taxpayer's earned income) exceeds the phase-out amount.

Year	Qualifying Children	Phase-out Percentage	Phase-out Threshold	Phase-out Complete
2023	None	7.65	16,370 - Joint 9,800 - Others	24,210 17,640
	1	15.98	28,120 - Joint 21,560 - Others	53,120 46,550
	2	21.06	28,120 - Joint 21,560 - Others	59,478 52,918
	3	21.06	28,120 - Joint	62,398
			21,560 - Others	56,838

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EITC

CREDIT DISALLOWANCE

- **Disqualified Income** - Credit isn't available when "disqualified income" (i.e., investment income) is more than the amount illustrated.

Year	2020	2021	2022	2023	2024
Disqualifying Income	3,650	10,000	10,300	11,000	11,600

- **Foreign Income Exclusion** - If the taxpayer claims either the foreign earned income or foreign housing exclusion, they will not qualify for the earned income credit for the year.

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EITC

FEDERAL OFFSETS

- All or part of the overpayment shown on Form 1040 may be used (offset) to pay past-due federal offsets. Offsets for federal taxes are made by the IRS and all other offsets are made by the Treasury Department's Financial Management Service (FMS).
- Examples of offsets and the agencies that collect them:
 - Back Taxes (IRS)
 - Child Support (FMS)
 - Spousal Support (FMS)
 - Student Loans (FMS)

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EITC

DISABLED

- **Earned Income for EITC Purposes** - IRC Sec 32
- There are several requirements to qualify for the EITC, one of which is to have earned income.
- Many overlook that long-term disability benefits received prior to the minimum retirement age (generally age 55) are treated as earned income for EITC.
- Which earned income is included for EITC purposes?
- Disability Benefits - Attributable to the employer's disability policy premiums (CCA199916041) are eligible earned income.
- Nontaxable Disability Income – If attributable to premiums paid by an employee, these disability payments are not “earned income”
- Long-term disability - Benefits to an individual retired on disability are earned income only until the individual reaches minimum retirement age,

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EITC

DISABLED - Continued

- Individuals often don't file a return because their income is below the filing threshold, and therefore, miss out on claiming the credit.
- Some people also mistakenly believe that receiving the EITC may impact their eligibility for Social Security disability benefits, Medicaid, food stamps, or housing assistance (IRC §32(l)).
- If overlooked in the past...amend.

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EITC

CUSTODIAL PARENT

- If a custodial parent releases a qualifying child's exemption to the non-custodial parent, the custodial parent still qualifies for the EITC if otherwise qualified to claim it.

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EITC

TWO WITH SAME QUALIFYING CHILD

- If child **can be claimed by two or more taxpayers**, the child will be treated as the qualifying child of the taxpayer who is:
 - A parent of the individual.
 - If 1) does not apply, the taxpayer with the highest AGI.
- If **parents do not file a joint return** the child will be treated as the qualifying child of:
 - The parent with whom the child resided for the longest period during the tax year, or
 - If the child resides with both parents for the same amount of time during that tax year, the parent with the highest AGI.

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EITC

TWO WITH SAME QUALIFYING CHILD

- If a parent can claim the child as a qualifying child but does not do so, 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 parent of the child.
- **Note:** This is the same tie-breaker rule that applies under the uniform definition of a child for the purpose of the dependency exemption.

Example – Unmarried parents living together – Where the unmarried parents of a qualifying child live together, the child would be the qualified child of the parent with the higher AGI and that parent would be the one to claim the EITC if otherwise qualified.

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EITC

SEPARATED SPOUSES

- A separated spouse will not be treated as married for purposes of the earned income tax credit if the individual:

(1a) Does not file a joint return, and

(1b) Resides with a qualifying child for more half the year, and

(1c) Does not reside with the spouse for the last 6 mo. of the year.

- OR -

(2) Has a formal separation agreement (other than a decree of divorce) and is not a member of the same household at the end of the year.

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EITC

MEDICAID WAIVER PAYMENTS

- **Feigh Case** - The Feighs received Medicaid waiver payments as wages for caring for their disabled adult children in their own home.
- Feighs excluded the income per Notice 2014-7.
- But treated it as EI for EITC and refundable child tax credit.
- The IRS took umbrage to that position - ended up in Tax Court.
- The Tax Court held that Notice 2014-7 could not reclassify the taxpayer's Medicaid waiver payment to remove a statutory tax benefit.
- IRS cannot reclassify that income through a Notice so that it no longer qualifies as "earned income" for the purpose of determining tax credits.
- The Court reasoned that IRS cannot remove a statutory benefit provided by Congress.

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EITC

MEDICAID WAIVER PAYMENTS

TAS (Taxpayer Advocate Service) Reporting Tip

- Generally, W-2s are no longer issued for MWP. But if one is received...
- On line 1 of the tax return (wages) include MWP received as wages that the taxpayer chooses to include in earned income even if a Form W-2 was not received reporting these payments.
- On Schedule 1, line 8z, (other income) subtract the nontaxable amount of the MWP.
- Enter "Notice 2014-7" as an explanation for the MWP amount reported on Schedule 1, line 8z.

Note: The 1040 Schedule 1 has subsequently been substantially modified and it is suggested it can be backed out on line 24z.

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EITC

SPECIAL EARNED INCOME RULES

- **Household Employees** - If a household employee did not receive a W-2 because an employer paid less than \$2,600 (2023), EITC may still be available. Include amount on the "Medicaid Waiver Payments Not Reported on Form(s) W-2, Box 1" 1040 line (line 1d on the 2022 version – 2023 draft is same). Also enter the amount on 1040 Sch. 1, line 8s.
- **Combat Pay Election** - A taxpayer may elect to treat combat pay that is otherwise excluded from gross income as earned income for purposes of the EITC. Making this election for EITC purposes may or may not be advantageous.
- If the TP has EI below the max used to calculate the credit including the combat pay will increase the credit.
- On the other hand, if the TP's EI is already in the phase-out range, electing to include combat pay as EI will decrease the amount of credit.

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EITC SPECIAL EARNED INCOME RULES

- **Taxpayer or Qualifying Child Dies During Tax Year** - Will not necessarily preclude claiming the EITC.
 - if the child fails the more than half the year rule because the child died or was born during the year, the child meets that rule if the child lived with the taxpayer for the entire time the child was alive for the year, including temporary absences.
 - As for the death of the taxpayer, Sec 32(e) provides that a taxable year must be a full taxable year - except in the case of a taxable year closed by the reason of the taxpayer's death.

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EITC SPECIAL EARNED INCOME RULES

- **Voluntary Salary Reductions Under Cafeteria Plans** - A cafeteria plan is a benefit plan that allows choosing among two or more benefits consisting of cash and benefits that aren't taxed. If a taxpayer chooses a benefit that isn't taxed (such as accident and health insurance), the amount of the voluntary salary reduction is **NOT** earned income when figuring this credit.
- **Earnings While an Inmate** - Amounts paid to inmates in penal institutions for their work are not earned income when figuring the earned income credit (*IRC Sec 32(c)(2)(B)(iv)*).

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EITC

DUE DILIGENCE REQUIREMENT

- **FORM 8867**
- Must be completed if a tax return claims any of the following:
 - Earned Income Tax Credit (EITC)
 - Child Tax Credit (CTC)
 - Additional Child Tax Credit (ACTC)
 - Other Dependent Credit (ODC)
 - Head of Household (HH)
 - American Opportunity Tax Credit (AOTC)
- The preparer penalty for failure to properly complete and file the 8867 is \$600 (up from \$560 in 2022) for each violation related to EITC, CTC (ACTC, ODC), HH and AOTC is subject to penalty
- Penalty could be \$2,400 (4 x \$600)

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EITC

TAXPAYER EITC PENALTIES

- **Fraud or Reckless Disregard of Rules & Regulations**
- The credit is disallowed for:
 - 10 years for those who claimed it in an earlier year due to fraud
 - 2 years due to reckless or intentional disregard of rules and regulations.
- These restrictions are in addition to other penalties imposed,
 - Accuracy-related penalty or
 - Fraud penalty.
- In addition, no credit is allowed where the credit was denied in an earlier year because of IRS deficiency assessment procedures, unless the taxpayer is re-certified by IRS

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EITC RECERTIFICATION

- **Recertification Process** - No EITC can be claimed by a taxpayer who has lost the credit due to the deficiency procedures for a period unless the taxpayer is recertified:
 - Recertification procedures apply if a taxpayer is subject to the 2- or 10-year disallowance periods.
 - Recertification isn't required if IRS disallows all or part of the credit because of a mathematical or clerical error.
 - To contest an EITC denial a taxpayer must petition Tax Court within 90 days of the mailing date of a statutory notice of deficiency.
 - IRS will send the taxpayer information about how to become recertified.
 - Filing without recertification will result in automatic denial.

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