ADVANCED CERTIFICATION STUDY GUIDE

Tax Year 2018

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ADVANCED SCENARIO 1: Aiden Smith

Issue #1 – When a dependent, full-time college student receives a scholarship that exceeds their total educational expenses, that "excess" is regarded as income by the IRS. On whose return should this amount be included?

The taxable portion of income from scholarships is included in the dependent's income

References:
Publication 4012 – page J1 for calculation of taxable amount of scholarship

Issue #2 – Are room and board considered qualified education expenses?

The IRS considers the following to be qualified education expenses:

- Tuition and fees required to enroll at or attend an eligible educational institution.
- Course-related expenses, such as fees, books, supplies, and equipment that are required for the courses at the eligible educational institution. These items must be required of all students in your course of instruction.

Qualified education expenses don't include the cost of:

- Room and board
- Meal plans
- Travel
- Research
- Clerical help
- Equipment and other expenses not required for enrollment in or attendance at an eligible educational institution

References:
Publication 4012 – page J1

ADVANCED SCENARIO 2: Sean Yale

Issue #3 – In a multi-generational household, can a grandparent who supports both his child and his grandchild claim the credit for other dependents for his adult child?

Looking at Sonia, the requirements for the credit for other dependents are:

- Does not qualify for the child tax credit (not under age 17)
- Does qualify as a dependent (in this case a qualifying child) based on the following:
  - ❖ Age (under age 19, under 24 if a student - no age requirement of the person is disabled)
  - ❖ Relationship (the taxpayer's descendant, sibling, or sibling's descendent)
  - ❖ Residency (the child lived with the taxpayer for more than half the year)
  - ❖ Support (the child cannot have provided more than half of his/her own support)
- Is a U. S. citizen

For each dependent, you can only claim child tax credit or the credit for other dependents, but not both.

References:
Publication 4012 – pages G13-G16

Issue #4 – In a multi-generational household, who is a qualifying child for the EITC?

The requirements to claim a dependent for EITC purposes are not the same as for claiming a person as a dependent. Check to see if either Sonya and/or Jimmy meet all the tests. The rules to be a qualifying person for EITC are:

- Age (under age 19, under 24 if a student -no age requirement of the person is disabled)
- Relationship (the taxpayer's descendant, sibling, or sibling's descendent)
- Residency (the child lived with the taxpayer for more than half the year)
- Note that there is no support requirement for qualifying child for EITC.
- Has a valid SSN.

Sonya cannot claim the baby for EITC because she is a dependent of another taxpayer (Sean). So, the only taxpayer who can claim the baby for the EITC is the grandparent.

References:
Publication 4012 – pages I1-I6

Issue #5 – What is Sean's most advantageous and correct filing status?

In order to file Married Filing Jointly or Married Filing Separately, the taxpayer must be married on December 31 of the tax year. That does not apply. In order to determine if Sean can file Head of Household, determine if Sonia and Jimmy are considered qualifying children or qualifying relatives for this purpose. The requirements are:

- Age (under age 19, under 24 if a student -no age requirement of the person is disabled).
- Relationship (the taxpayer's descendant, sibling, or sibling's descendent).
- Residency (the child lived with the taxpayer for more than half the year).
- Support (taxpayer provided more than half the cost of maintaining the home).
- Child cannot be claimed by another taxpayer for Head of Household filing status.

References:
Publication 4012 – pages B6-B8
Volunteer Manual – FIW Part II: Filing Status – Determination of Filing Status Interview Tips
Volunteer Manual – Credits: EITC
Volunteer Manual – Credits: Additional Child Tax Credit

ADVANCED SCENARIO 3: Tom and Carol Baker

Issue #6 – Who is eligible to be a qualifying child for the Child Tax Credit for tax year 2018?

In order for a taxpayer to be eligible for this credit the qualifying child must meet the following criteria:

- Be under age 17 at the end of the tax year.
- Be claimed as a dependent on the taxpayer's return.
- Is the taxpayer's son or daughter, adopted child, stepchild, eligible foster child, or a descendant of any of them, brother, sister, half-brother, half-sister, stepbrother, stepsister, or a descendant of any of them.
- Did not provide over half of his or her own support.
- Lived with the taxpayer for more than half of the tax year.
- Has a valid social security number by the due date of the return – NEW THIS YEAR

References:
Publication 4012 – page G12
Volunteer Manual – Credits: Child Tax Credit

Issue #7 –What credits are taxpayers who have ITINs eligible to claim?

ITIN holders can claim all benefits except the EITC. Children with an ITIN cannot be a qualifying child for the EITC or the child tax credit. The child must have an SSN for these two benefits

Although they are eligible to claim the Child tax credit, beginning in tax year 2018, the child must have a valid SSN. The *credit for other dependents* and the *child and dependent care credit* do not exclude ITIN holders. In order to claim the EITC, all taxpayers and the qualifying dependent named on the return must have a valid SSN.

References:
Publication 4012 – pages G12, G16, I2-I3

ADVANCED SCENARIO 4: Bill Johnson

Issue #8 – What is Bill's correct filing status, and how does it affect his potential tax credits?

First, determine Bill's correct filing status. He is married on December 31 of the tax year, and he is not legally separated from his wife. In order to file as Head of Household as a legally married taxpayer, he must meet all the following requirements:

- File a separate return from his spouse.
- Provided the main home for more than half the year of a dependent child, stepchild, or foster child (a grandchild does not meet this test).
- Have paid more than half the cost of keeping up the home for the year.
- Lived apart from their spouse during the entire last six months of the tax year.

Since Bill and Michelle lived together until from January to September, he does not meet the last test and must file Married Filing Separately.

Taxpayers who file Married Filing Separately are not eligible for many tax credit and benefits. Among the disallowed credits are education credits and the EITC.

References:
Publication 4012 – pages B6, I3, J5

Issue #9 – Is a taxpayer who files Married Filing Separately eligible for the Child Tax credit, and what is the amount of the refundable portion of the additional child tax credit?

Taxpayers who file Married Filing Separately are eligible for the Child Tax Credit and the Credit for child and dependent care expenses. The 2018 Child Tax credit is $2,000. Of that credit amount, up to $1,400 is refundable.

References:
Publication 4012 – page G12

ADVANCED SCENARIO 5: Fran Emerson

Note For ProSeries Training:

Fran came to a Ladder Up site last year, so you can transfer her file. After transferring, check for changes from year 2017 to 2018, for example, address changes, marital status, dependents, changes in employment and verify all numbers (SSN, bank accounts, EIN, etc). If a form is no longer needed, you should delete it from the return. If a new form is needed, look along the left-hand side of the screen under Common Forms, or use the Forms search feature along the upper toolbar. ***The Where Do I Enter? Cheat Sheet*** will help you to locate the form. (The green “Where Do I Enter” button in ProSeries does not work because we sign into the software offline.)

When transferring a file, if a client had a prior year state tax refund, ProSeries will create a 1099-G Wks and it **cannot be deleted**. The program will know if the client itemized in the previous year and treat it accordingly. You may need to enter the EIN number for the Illinois Dept of Revenue in order to clear errors (the EIN number is in the manual in the state refund section). You can add the 1099-G from unemployment to the same form in ProSeries but in a separate column because Illinois Dept of Employment Security has a different EIN.

This client has a 1099-C (Canceled Debt) and must therefore go to an Advanced Preparer and an Advanced Reviewer. While, that is the only ***document*** in this scenario which requires an Advanced preparer/reviewer, if there is even one document that requires Advanced certification, the client must go to an Advanced Preparer.

However, there are certain circumstances when clients with 1099-Rs need to go to an Advanced Preparer/Reviewer – and this is one of those situations. Do you know why?

Issue #10 – What filing status' can Fran use? Which one is most advantageous?

Use the interview tips on page B-6 of Publication 4012 or flow chart on page XXX of the Volunteer Manual in order to determine the best filing status. The most advantageous filing status is generally the one that provides the highest standard deduction for which the taxpayer qualifies.
Remember that a child/relative may be a qualifying person for one filing status but not another. But the taxpayer only has to have one qualifying person to qualify them for a specific filing status. For instance, they only have to have one qualifying son or daughter to be a qualifying widow(er) and can use that filing status even though they may have other dependents which may (by themselves) not allow that filing status.

References:
Publication 4012 – page B6

Issue #11 – Are there different requirements for each "dependency" benefit or credit?

Review the charts summarizing the dependency requirements to assist in determining whether an individual is a qualifying person for the Credit for other Dependents, Child Tax Credit, or Earned Income Credit. Remember, there is not support requirement for an unmarried qualifying child for the EITC.

References:
Publication 4012 – pages G12-G16, I2-I4

Issue #12 – Where are the Child and Dependent Care Expenses entered on the tax return?

The credit for child and dependent care expenses is often beneficial for clients with younger children who had to pay for day care or after school care for young children. Remember that this is a non-refundable credit so clients will only receive it if they had taxable income, a fact that can sometimes be confusing to clients and preparers alike.

While it doesn't apply to this scenario, one of the rules for couples filing jointly is that both parents have to work or be students in order to receive the credit. So you have to make sure that you code all W-2 forms to the correct parent, and also complete any relevant student information for each parent.

Child and Dependent Care Expenses, such as day care expenses, are entered in TWO places in ProSeries. The dollar value(s) must be entered on the Information Worksheet, Part III, under "Qualified Child/dep care expenses…" for the appropriate dependent. The dollar values must also be entered on Form 2441 along with information about the facility/person (including tax ID number) which provided the services.

References:
Publication 4012 – pages G5-G8

Issue #13 – What payments are allowable as "qualified educational expenses" for the American Opportunity Credit?

"Qualified educational expenses" are defined differently for the American Opportunity Credit, Lifetime Learning Credit, and for excluding scholarships from taxable income. In ProSeries, the educational expenses will be either directly entered or carried over from the 1098-T onto the Student Info Worksheet and can be seen in the table in Part VI. The total amount of qualified expenses USED in the calculation for the credits (also known as the adjusted qualified expenses) are after subtracting the scholarships and is on line 20 of the ProSeries Student Info or Line 27 of Form 8863.

References:
Publication 4012 – pages J2-J6

Issue #14 – Is Fran required to pay the Shared Responsibility Payment?

The Tax Cuts and Jobs Act reduced the Shared Responsibility Payment to zero for the 2019 tax year. However for the 2018 tax year (tax returns typically prepared in the Spring of 2019), taxpayers are still required to have minimum essential coverage or an exemption in order avoid paying the Shared Responsibility Payment.

The Amount of the Shared Responsibility Payment has a minimum value, but could be as high as 2.5% of the household income above the filing threshold.

References:
Publication 4012 – page H22

Issue #15 – Where is the federal withholding totaled on the tax return?

The total withholding is listed on line 16 of the 1040. This value will include withholding from W-2s, 1099-R, SSA-1099, W-2G, and any other income source where the income provider sent a portion of the taxpayer's income directly to the IRS.

Note: Look at the individual income documents to identify which box contains the federal withholding

Issue #16 – Where is Cancelled Debt reported on the tax return?

All income, unless specifically excluded by law, must be reported on the tax return. Any amounts entered on the 1099-C worksheet will generally flow through to line 21 of Schedule 1.

References:
Publication 4012 – pages D58-D59

Issue #17 – What are the exceptions which allow a taxpayer to avoid the 10% additional tax on early IRA distributions?

Generally, the additional tax (10% penalty) applies if the taxpayer is under age 59 ½ years old at the time of distribution. There are exceptions if distributions are taken for certain reasons. The list of possible exceptions can be found in the instructions to Form 5329 (Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts). If no exception applies, the 10% penalty is assessed in the "Other Taxes" section of Schedule 4, Line 59.

References:
Publication 4012 – pages H3-H4

Issue #18 – What criteria must be met in order to qualify for the Earned Income Tax Credit? What criteria must be met for the Child Tax Credit and Credit for other dependents?

The earned income credit can be very valuable to our clients, but it is not always obvious whether they qualify or not. Page I-2 of Publication 4012 has a chart that gives the qualification criteria that all taxpayers need to meet regardless of whether or not they have a qualifying child. Page I-4 of Publication 4012 provide the criteria for determining whether someone can be a taxpayer's qualifying child for the purposes of this credit.

Under the Tax Cuts and Jobs Act, the value of personal exemption deduction was reduced to zero and instead the child tax credit was increased (for those who qualify) and the credit for other dependents was added. The qualification criteria for these credits are on page G-12 through G-16 of Publication 4012.

References:
Publication 4012 – pages G12-G16, I2, I4

Issue #19 – Do Mary and Ryan qualify for an exemption for the shared responsibility payment?

The exemptions for not having to pay the shared responsibility payment because an individual does not have minimum essential coverage are in the reference materials (see page numbers below). The exemption for the short term gap (which is a Code B) is generally automatically entered by the software if all individuals had a gap of less than 3 months.

Note: that only one Code B exemption per individual per tax year – so if an individual had two gaps of one month each, they could only use the Code B exemption for the first gap in coverage.

References:
Publication 4012 – page H15

Issue #20 – What tax forms might be used to report a Capital gain / loss?

The most common tax form reporting a capital gain or loss is the 1099-B (Proceeds from Broker and Barter Exchange Transactions) which is used to report the sale of stocks, bonds, and mutual funds. However, capital gains may also result from the sale of a home (where the taxpayer does not meet the criteria to exclude income from the sale of a principal residence) and may be reported on other tax forms such as the 1099-DIV.

References:
Publication 4012 – pages D26, D38, D46, O6

Issue #21 – What information is needed in order to use the Simplified Method for calculating the taxable amount of a retirement distribution?

When box 2a of the 1099-R is blank and/or if the taxable amount not determined box is checked, the volunteer preparer should evaluate what the taxable amount of the retirement distribution should be. In addition, if the 1099-R has an employee contribution amount in box 9b, a portion of the distribution may not be taxable. In these cases you will need to use the simplified method to determine how much of the distribution is taxable. When asked about the age(s), make sure to evaluate the age(s) when the first distribution is paid, not the end of the tax year.

Note: Quite a bit of supplemental information is required for this calculation, and you may need to work with the client to develop the information.

References:
Publication 4012 – pages D33-D34, D37

Issue #22 – How is the taxable amount of Social Security determined?

Social Security benefits are reported on Form SSA-1099 (Social Security Benefit Statement) (not to be confused with 1099-SA which is related to Health Savings Accounts). Depending on what other sources of income a taxpayer has and their filing status, a portion of their Social Security income may be taxable. Even Warren Buffet doesn't pay taxes on his entire social security, but many clients are not required to pay taxes on their social security at all. Make sure you finish the tax return in its entirety – enter **all** income, complete all worksheets, etc. before answering this question. But once all income has been entered, the tax software will calculate the taxable amount of social security (if any) and report it on line 5b of the 1040.

References:
Publication 4012 – pages D30, D40-D42

Issue #23 – Can refunds be split between accounts?

Taxpayers receiving a refund have the ability to deposit the refund in multiple accounts (e.g., checking and savings). Additionally, taxpayers have the ability to use their refund to purchase US Savings Bonds. The Manual indicates the procedures for the form (Allocation of Refund, including Savings Bond Purchases) used for this purpose.

References:
Publication 4012 – page K13

Issue #24 – Is federal income tax withholding only reported on W-2s?

Taxpayers typically have withholding from their jobs, which is reported on their W-2. However, they may elect to have withholding from other income sources, including: pensions, gambling winnings, social security, other government payments, etc.

Note: There is no special reference on withholding – you need to carefully check each income document and enter any withholding into the tax software.

Issue #25 – *What types of income have to be reported on Schedule C?*

Taxpayers generally must report all of the income that they receive in cash, regardless of whether or not the income is reported on a form 1099-MISC (Miscellaneous Income) or 1099-K (Payment Card and Third Party Network Transactions). Where to report the income on the tax return depends on what type of income it is. On the Schedule C Worksheet volunteers can enter income not reported on a tax document (i.e. cash income) on Line 1a, 1099-MISC is reported on Line 1b, and 1099-K income is reported on Line 1c.

References:
Publication 4012 – pages D13-D16

Issue #26 – *How is the mileage expense deduction calculated?*

The 2018 standard mileage rate is 54.5 cents per business mile. In general, mileage can be claimed only between work locations. Mileage from home to a first job site, and from the last job site to home is considered commuting and is not deductible. Mileage is entered on the Schedule C (Profit or Loss from Business), Part II Expenses line 9 "Car and Truck." This will link you to a Car-Truck worksheet in which you will enter the information for the client's mileage. The details of how to do this are shown in the referenced pages of the Manual. Remember, if clients want to claim actual expenses on the car (gas, oil, repairs, etc.) other than tolls, parking, and the business portion of auto loan interest, or if they claimed actual expenses on the car in a prior tax year, then the return is out of scope and the client should be referred to a paid preparer.

References:
Publication 4012 – pages H3-H4

Issue #27 – *What business expenses are deductible?*

In general, the IRS expects to see business expenses that are reasonable and ordinary for the type of business. Things like advertising, insurance, licenses, travel, and supplies can all easily be connected to the business. Something like haircuts are much harder to justify – is the haircut specific to the type of work? Required? Anything that is generally more of a personal expense such as grooming products, vitamins, clothing that can be worn outside the work environment, etc. are generally not deductible.

The section of Publication 4491 (VITA/TCE Training Guide) on Car and Truck expenses (page 10-8) was changed significantly for TY 2018. It says "Self-employed taxpayers can also deduct the business part of interest on a car loan, state and local personal property tax on the car, parking fees, and tolls, whether or not they claim the standard mileage." In previous IRS publications, the IRS specifically allowed taxpayers to deduct tolls and parking fees specifically attributable to their business, in addition to the standard mileage rate.

References:
Publication 4491 – pages 10-7, 10-8, 10-9
Publication 4012 – page D18

Issue #28 – *How is the self-employment tax calculated?*

Taxpayers who are self-employed have to pay their own Social Security and Medicare taxes (both the employer and the employee share). These are calculated and paid as part of the submission of form 1040 (U.S. Individual Income Tax Return) and are referred to as the self-employment tax. The tax software will calculate the tax which will appear on Schedule SE (Self-Employment Tax) and on line 57 of Schedule 4 of Form 1040, provided that self-employment income and expenses are properly reported on Schedule C (Profit or Loss from Business). Complete the Schedule C, and once you have done this you should be able to see the self-employment tax on Form 1040, Schedule 1, line 57. Since the taxpayer is paying the additional, normally employer-paid Social Security and Medicare tax, one-half of the self-employment tax is deducted on line 27 of Schedule 1 of the Form 1040.

References:
Publication 4491 – page 10-16
Publication 4012 – page D13

Issue #29 – How does the Qualified Business Income deduction affect the tax return?

The Qualified Business Income deduction is new for the 2018 tax year. This deduction can be used by anyone with self-employment income from a Schedule C, but also those with income reported on a K-1 from S-corporations or partnerships (which are both out-of-scope for VITA programs). The Qualified Business Income deduction reduces taxable income by 20% of business income or taxable income, whichever is less.

References:
Publication 4491 – pages 20-4, 20-5, 20-6
Publication 4012 – page F11

Issue #30 – Where is self-employed health insurance reported on the tax return?

When a taxpayer works for a company and pays for health insurance through work, their income reported Box 1 of the W-2 is typically reduced by the amount they pay for insurance. However, the health insurance payments typically do not reduce Box 3 and Box 5 (Social Security and Medicare wages). The tax law is written so that self-employed individuals receive a similar benefit as an adjustment to income on their tax return

References:
Publication 4491 – pages 18-4, 18-5
Publication 4012 – pages D18, E4

Issue #31 – What are taxpayer's options to pay the balance due?

Taxpayers should still file a tax return, even if they are unable to pay (the penalties for not filing a tax return are significantly higher than not paying). In addition, there are no penalties if the taxpayer pays by the due date of the tax return (generally April 15). The IRS encourages taxpayers to pay as much as they can at the time of filing. Any unpaid balance can be paid by using the Online Payment Agreement application on IRS.gov to request an installment agreement.

A taxpayer may also request an installment agreement by sending in form 9465 with their tax return. An installment agreement allows the taxpayer to make payments over time, rather than paying in one lump sum.

Note: Filing for a tax extension does not extend the due date for paying any balance owed.

References:
Publication 4012 – pages K14-K15

ADVANCED SCENARIO 8: Roberta Wilson

Issue #32 – How much can taxpayers deduct in 2018 for state income taxes and real estate taxes?

New in 2018, the combined amount that a taxpayer can deduct for state income taxes and real estate tax is limited to $10,000. State income taxes include both the amount withheld and paid with the prior year return. In order to calculate the total Roberta is eligible to deduct, you must add her real estate taxes and her state income taxes together.

References:
Publication 4012 – page F7

Issue #33 – What is the standard deduction of the most advantageous filing status Roberta is eligible to use?

Roberta is unmarried, so she can only file Single, or Head of Household if she has a qualifying person. Is Jacob a qualifying child for Head of Household filing status? The requirements are:

- Age (under age 19, under 24 if a student -no age requirement of the person is disabled).
- Relationship (the taxpayer's descendant, sibling, or sibling's descendent).
- Residency (the child lived with the taxpayer for more than half the year).
- Support (taxpayer provided more than half the cost of maintaining the home).
- Child cannot be claimed by another taxpayer for Head of Household filing status.

References:
Publication 4012 – pages B6-B7

Issue #34 – What expenses qualify as itemized deductions on Schedule A?

Not all expenses are considered itemized deductions that can be included on Schedule A. Some of the most common itemized deductions are listed below:

- Medical and dental expenses (if in excess of 7.5% of the taxpayer's adjusted gross income).
- State and local income taxes + real estate taxes (max combined deduction in 2018 = $10,000).
- Home mortgage interest.
- Home equity line interest only if money was used to buy, build or improve the home.
- Charitable contributions to registered charities.

References:
Publication 4012 – pages F5-F10

Issue #35 – Can a taxpayer claim the EITC in 2018 if it was disallowed in 2 years ago?

Form 8862, Information to Claim Certain Refundable Credits After Disallowance, must be completed for any taxpayer whose EIC, child tax credit (CTC)/additional child tax credit (ACTC), or American opportunity tax credit, was previously reduced or disallowed due to an unintentional error. If the IRS determined a taxpayer claimed the credit(s) due to reckless or intentional disregard of the rules (not due to math or clerical errors) the taxpayer can't claim the credit(s) for 2 tax years. If the error was due to fraud, then the taxpayer can't claim the credit(s) for 10 tax years.

References:
Publication 4012 – page I6