United We Thrive

Special Topics Training

United Way of Greater Cincinnati

January 22, 2025

Welcome!

- My name is Jim Yuhas
    - 15+ years with VITA
    - Site Coordinator, Care Center Taxes in Loveland
- Mary Lepper, Charles Lewis, Kathy Lavieri and Keith Gehring will monitor Zoom Chat
- Our United Way of Greater Cincinnati Support Team
    - Matt Long, Sr. Program Manager
    - Adrienne Brandicourt, Program Manager, Free Tax Prep
    - Jessie Welker, Associate, Community Impact

Your Volunteer Pathway: From today through Tax Season

Information Session

Watch the Tech Training Video (will be available soon)

Volunteer Training Session A

Volunteer Training Session B

Take IRS Online Certification Tests

Volunteer at a Tax Site

Optional Returning Volunteer Training

Optional Special Topics Training

Special Topics Agenda

- Education Credits/Kiddie Tax
  - 15 minute break
- Principal Residence
  - Sale
  - Cancellation of Debt
- Residential Energy Credit
- Tax Exempt Interest
- Final Q&A

Education credits – two basic kinds

- American Opportunity Credit – usually of greater benefit, but has several conditions
- Lifetime Learning Credit -- a non-refundable credit when AOC conditions are not met

American opportunity credit

- $2,500 maximum credit per Student
  - 40% of the credit may be Refundable, with the balance Non-Refundable
- Up to $4,000 of Qualified Education Expenses (QEE)
  - Tuition, fees, books/equipment
- 100% credit for first $2,000, then 25% credit for the balance,
  - up to the maximum of $4,000 of QEE
- First 4 years of post-secondary education; only claimed 4 times per student
  - This is not an undergraduate versus graduate school limitation
- Student enrolled at least half time and pursuing degree or certification
- No drug felony

Lifetime Learning Credit

- $2,000 maximum per Return
- Up to $10,000 of Qualified Education Expenses
    - Tuition, fees, books/equipment paid to institution
- 20% credit, but it is Non-Refundable
- As many years as education expenses incurred, post secondary or to improve job skills

Which one do I apply?

- The American Opportunity Credit is almost always better for the family if the student meets all the criteria.

- If the student is a dependent (normal situation for AOC); the credit goes to the parent's return, not the student's return.

Which credit to select and why

- Normal scenario: Taxpayer indicates that their dependent is a college student. They have a copy of the school issued 1098-T.
- Assess with the taxpayer if the student meets all the criteria for the American Opportunity Credit (4012: Tab J)
  - If not, the Lifetime Learning Credit likely applies
- The parent claiming the dependent student gets the education credit, not the student.
- If student is not a dependent, they claim the credit.

Education Credits and issues

- Which credit to select and why

1. No scholarship
2. Scholarship less than tuition
3. Scholarship greater than tuition
4. The dreaded Kiddie Tax
5. Allocation
6. Summary

1098-T

CORRECTED (if checked)

FILER'S name
Street address
City or town, state or province, country, ZIP or Foreign Postal Code
Telephone number
OAKLAND UNIVERSITY
677 OAKLAND BLVD
COLUMBUS OH 43216

1 Payments received for qualified tuition and related expenses
$12,900.00

2

OMB No. 1545-1574

2020

Form 1098-T

Tuition Statement

FILER'S employer identification no.
10-8XXXXXX

STUDENT'S TIN
224-00-XXXX

3 If this box is checked, your educational institution has changed its reporting method for 2020.

Copy B For Student

STUDENT'S name
Street address (including apt. no.)
City or town, state or province, country, ZIP or Foreign Postal Code
COREY EMERSON
200 AMBER PLACE
YOUR CITRY, STATE, ZIP

4 Adjustments made for a prior year

5 Scholarships or grants
$10,000.00

6 Adjustments to scholarships or grants for a prior year

7 Checked if the amount in box 1 or 2 includes amounts for an academic period beginning January-March 2021. >

This is important tax information and is being furnished to the IRS. This form must be used to complete Form 8863 to claim education credits. Give it to the tax preparer or use it to prepare the tax return.

Service Provider/Acct No. (see instr.)

8. Checked if at least half-time student X

9 Checked if a graduate student

10 Ins. contract reimb./refund

Form 1098-T

Box 1 – Payments Received

Box 5 – Scholarship or Grants

Box 8 – Whether more than Half-Time Student

No Scholarship

Normal Scenario Example:

- Tuition (Box 1): $12,000
- Books: $2,000
- Scholarship/Grant: $0
- Qualified Education Expenses thus total: $14,000

- Potential credit:

	American Opportunity Credit	Lifetime Learning Credit
Maximum QEE	$4,000	$10,000
Credit calculation	100% of first $2,000 + 25% of remainder = $2,500	20% of QEE = $2,000
Refundable portion	40% of $2,500 = $1,000	- None -

Scholarship less than tuition

- Tuition (Box 1): $12,000
- Books: $2,000
- Scholarship (Box 5): $6,000
- Qualified Education Expenses thus total: $8,000

- Potential credit:

	American Opportunity Credit	Lifetime Learning Credit
Claimed QEE	$4,000	$8,000
Credit calculation	100% of first $2,000 + 25% of remainder = $2,500	20% of QEE = $1,600
Refundable portion	40% of $2,500 = $1,000	- None -

Scholarship greater than tuition

- Tuition (Box 1): $12,000
- Books: $2,000
- Scholarship (Box 5): $19,000
- Qualified Education Expenses thus total: $0
- Scholarship Income of $5,000

- When scholarship/grant exceeds education expenses:
  - there is no education credit for the parent
  - but now taxable scholarship income for the student.

Kiddie tax??

This is a provision of the tax law that taxes the child's unearned (investment) income at the parent's tax rate. It only is applied when both:

The child's unearned income, plus taxable scholarships and grants, exceeds $2,600

2024 limitations

AND

The child has a filing requirement:

(earned income, including taxable scholarships, over $14,600) or
(unearned income, not counting taxable scholarships, over $1,300) or
(gross income more than (a) $1,300, or (b) earned income (up to $14,150) plus $450)

Form 8615, Tax for Certain Children Who Have Unearned Income (Kiddie Tax)

4012: H-5

Do you have to use Form 8615 to figure your child's tax on your child's tax return?

Step	Probe / Ask the Taxpayer	Action
1	Was the child's unearned income, including taxable scholarships and grants, more than $2,600?	**YES** – Go to Step 2 **NO** – Don't use Form 8615 to figure the child's tax.
2	Is the child required to file a tax return for the tax year? See Chart B - For Children and Other Dependents in Tab A.	**YES** – Go to Step 3 **NO** – Don't use Form 8615 to figure the child's tax.
3	Was the child under age 18 at the end of the tax year?	**YES** – Go to Step 8 **NO** – Go to Step 4
4	Was the child age 18 at the end of the tax year?	**YES** – Go to Step 7 **NO** – Go to Step 5
5	Was the child under age 24 at the end of the tax year?	**YES** – Go to Step 6 **NO** – Don't use Form 8615 to figure the child's tax.
6	Was the child a full-time student during the tax year?	**YES** – Go to Step 7 **NO** – Don't use Form 8615 to figure the child's tax.
7	Did the child have earned income that was more than half of his or her support?	**YES** – Don't use Form 8615 to figure the child's tax. **NO** – Go to Step 8
8	Was at least one of the child's parents alive at the end of the tax year?	**YES** – Go to Step 9 **NO** – Don't use Form 8615 to figure the child's tax.
9	Is the child filing a joint return?	**YES** – Don't use Form 8615 to figure the child's tax. **NO** – Go to Step 10
10	Form 8615 must be used to figure the tax on the child's tax return. Form 8615 is in scope for Native Americans receiving per capita payments and Alaska residents receiving permanent fund dividends. For all other purposes, Form 8615 remains Out of Scope for the child's tax return (but does not make the parents' tax return Out of Scope).	

Kiddie Tax
with scholarship greater than tuition

- Tuition (Box 1): $12,000
- Books: $2,000
- Scholarship (Box 5): $19,000
- Qualified Education Expenses thus total: $0
- Scholarship Income of $5,000

Kiddie Tax limitation exceeded? Yes, Because the scholarship income of $5,000 exceeds the Kiddie Tax limitation of $2,600.

Filing Requirement? Only if the student has other earned income in excess of $9,600 ($14,600 – $5,000). Some do, some don't.

So, it almost always comes down to whether or not the student has a filing requirement. If no filing requirement, the student's return is In-Scope even though the Kiddie Tax threshold of $2,600 is exceeded.

Allocation

- Even more complexity (and potential benefit) occurs if the scholarship/grant is **unrestricted.**
- Some scholarships, including all Pell Grants, are allowed to be claimed as income, if doing so is of benefit to taxpayer(s).
  - $$ don't have to be solely allocated to tuition and fees.
  - Some $$ can be used for living expenses (e.g. room & board).
- WHAT? We should consider adding income that we could exclude?
  - Yes, because the tax on that added income may be lower than the increase in the Education Credit.
- How do we know if a scholarship or grant is "allowed" to be allocated to income?
  - Pell Grant, yes.
  - All others, we need to rely on taxpayer's knowledge.
  - If uncertain, assume that allocation to income is NOT allowed.

Extreme, but possible, example:

Joe is a college sophomore.	
Tuition: $12,000	
Books: $1,000	
Pell Grant: $5,000	
Other Scholarship: $8,000	
Expenses less Grant/Scholarship: -$0-	
Joe's other income: $3,000 W-2 summer job	
	Without Allocation
QEE for parents:	$0
AOC for parents*:	$0
Joe's taxable scholarship:	$0
Joe's AGI:	$3,000
Joe has filing requirement?	no
Kiddie Tax?	no
Joe's income tax:	$0
Joe's refund:	all withholding
Benefit to family:	base
*assumes parent's income below full AOC limits	

Extreme, but possible, example:

Joe is a college sophomore.		
Tuition: $12,000		
Books: $1,000		
Pell Grant: $5,000		
Other Scholarship: $8,000		
Expenses less Grant/Scholarship: -$0-		
Joe's other income: $3,000 W-2 summer job		
	Without Allocation	With Allocatiion
QEE for parents:	$0	$4,000
AOC for parents*:	$0	$2,500
Joe's taxable scholarship:	$0	$4,000
Joe's AGI:	$3,000	$7,000
Joe has filing requirement?	no	no
Kiddie Tax?	no	no
Joe's income tax:	$0	$0
Joe's refund:	all withholding	all withholding
Benefit to family:	base	$2,500 AOC
*assumes parent's income below full AOC limits		

Shifting $4,000 of Pell Grant to living expenses (taxable scholarship) reduces the impact of scholarship, and QEE increases by same $4,000.

If grant/scholarship allocation to income is allowed – how much?

- Okay, here's where it gets tricky.

- There's a key $4,000 threshold that makes an initial decision for us.
  - If more than $4,000, then next steps are straightforward (see next slides)
  - If less than $4,000, then we recommend the use of an off-line calculator.

Process for a particular taxpayer

The more than $4,000 threshold:

- If QEE exceeds the Scholarship/Grant by more than $4,000, enter the difference on the parent's return for a possible education credit.

or

- If the Scholarship/Grant exceeds QEE by more than $4,000, then that amount is taxable scholarship income and is included on the student's tax return. Check for possible Kiddie Tax; if so, the return is out-of-scope.

Process for a particular taxpayer

Less than the $4,000 threshold (requires calculations that are discussed on next slides)

- If QEE exceeds the Scholarship/Grant by <u>less than</u> $4,000, determine amount of scholarship/grant to claim as taxable scholarship income on the student's return and enter the resulting QEE on the parent's return for a possible education credit.

- If the Scholarship/Grant exceeds QEE by <u>less than</u> $4,000, determine amount of scholarship/grant to claim as taxable scholarship income on the student's return and enter the remaining QEE on the parent's return for a possible education credit

- With both scenarios, check for possible Kiddie Tax; if yes, try to adjust to eliminate the Kiddie Tax. If adjustment is not possible, the return is out-of-scope.

Determining the "adjustment"

- Some simply try to limit AOC QEE to $2,000 (which is 100% portion) and see if that improves taxpayers' results. But, an alternative to numerous iterations…
- You may choose to use the following:
  - https://cotaxaide.org/tools/Education%20Calculator.html

- Some data from the parent's return is needed (or at least a good approximation)
- Ensure that you add at least $4,000 in Room and board on the Expense tab

Again the KIDDIE TAX

- So, if we add taxable scholarships for either reason – due to scholarships exceeding QEE or due to “allocation” of scholarships – do we invoke the Kiddie Tax? If so, the return becomes Out-Of-Scope for VITA.

- If due to “allocation”, does not ”allocating” or a reduced ”allocation” keep the return under the Kiddie Tax thresholds?

- The cotaxaide tool, shown before, is quite helpful in determining if the Kiddie tax is invoked.

Demo of cotaxaide tool

https://cotaxaide.org/tools/Education%20Calculator.html

To summarize

- Determine the student's education expenses from their 1098-T and books/equipment purchases.
- Is there a scholarship/grant?
  - No, enter QEE and claim appropriate education credit.
- If Yes, is it unrestricted?
  - No, apply it solely to tuition/fees (or taxable scholarship)

TO SUMMARIZE (CONT'D)

- If Unrestricted, assess the $4,000 threshold;
  - if exceeds $4,000: either the parent gets Education Credit or Child assessed Scholarship income
  - If doesn't exceed $4,000 threshold: examine more options to lower tax

- Was there any taxable scholarship?
  - Assess possible Kiddie Tax implication

closing

- This topic just gets more confusing and more complex the further down the rabbit hole we go.
- Most of the complexity comes when there is an unrestricted scholarship/grant involved (possible allocation).
- Or when there is a taxable scholarship/grant involved (possible Kiddie Tax).
- Every taxpayer's unique situation (and other incomes) will determine their "best" answer. My best practice is to talk it through slowly with a peer/site coordinator.
- Questions? Send email to jimyuhas@gmail.com.

Special Topics Agenda

- Education Credits/Kiddie Tax
  - 15 minute break
- Principal Residence
  - Sale
  - Cancellation of Debt
- Residential Energy Credit
- Tax Exempt Interest
- Final Q&A

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Sale of home

Normally, we don't need to report the sale of a taxpayer's home as it has no taxable income or loss. But, in a few instances we do need to:

- **1099-S:** the taxpayer presents this form as issued by the bank/mortgage company. This is covered on the next slide.
- **1099-C:** the taxpayer presents this form as issued by the bank/mortgage company related to a foreclosure on the home. See subsequent slides.

4012: D-40

Sale of home: 1099-S

When presented with a **1099-S,** we have to report the sale of the home on Schedule D

Gain on Sale of home

- If the taxpayer lived in the home for 2 of the last 5 years, we exclude the first $250,000 of gain ($500,000 of gain if MFJ)
  - Use adjustment code H to reduce the gain on Sch D

4012: D-42

Loss on Sale of home:

- Losses on the sale of a principal residence are not allowed.
- Use adjustment code L to eliminate the loss on Sch D

4021: D-43

Sale of home: 1099-C

- Taxpayer presents you with a **1099-C (cancellation of debt)**. In your interview, you determine that it is due to a foreclosure on their home mortgage.
- You and the taxpayer determine the following:
  - FMV of the home: $225,000
  - Mortgage principal outstanding: $250,000
  - Debt cancelled: $25,000

- This matches the numbers on the 1099-C:
  - Box 7: $225,000
  - Box 2: $25,000
  - Box 5 is checked: taxpayer is personally liable

- As you'll see later, you also need to determine whether or not they still live in the home.

Sale of Home: 1099-C

- We learned in Part B training that a 1099-C for credit card debt is fully taxable.
- What about for a home mortgage? The extra tax on a $25,000 debt forgiveness is particularly punishing when you just foreclosed.
- Using the IRS worksheet on 4012 pg Ext-5, we determine that we can exclude this income.
  - Taxpayer received an accurate 1099-C
  - The home was never used in a business or as a rental
  - Box 3 does not show any interest
  - Box 6 does not indicate bankruptcy
  - Mortgage was used solely to buy/build/improve the home and was secured by the home
  - The home was the taxpayer’s principal residence
  - The mortgage amount was less than $750,000.

Sale of Home: 1099-C

TaxSlayer entries: Other Income->1099-C-> on the “Cancellation of Debts” screen:

4012: D-71

Select Form 1099-C, then

- For each 1099-C indicate if it is for Taxpayer or Spouse
- Add name of bank and its ID number
- Enter the amount of debt cancelled

These are the same steps you take if it was cancelled credit card debt

The amount of debt cancelled will now temporarily show as taxable income on the 1040

Sale of Home: 1099-C

4012: D-71

4012: EXT-6

BUT ALSO:

on that “Cancellation of Debts” screen:

Select Form 982, then

- Check the box “Discharge of qualified principal residence indebtedness”
- Enter the amount of debt cancelled

This eliminates the cancellation of debt as income on the1040; no longer taxable.

Further, If the taxpayer still lives in the home, an adjustment to basis needs to occur.

If so, further down on form 982, in Part II:

- Enter the amount of debt cancelled in “Basis of your principal residence”.
  - But, only do this if the taxpayer still lives in the home!

The IRS entitles this 982 form: Reduction of Tax Attributes Due to Discharge of Indebtedness

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Residential Energy Credits

4012 G -20,21

- Lots of home improvement installations may qualify for this credit.
- Includes:
  - Improvements: exterior doors, exterior windows and skylights, insulation
  - Home energy audits
  - Energy Property: central air conditioners, furnaces, water heaters.
  - Heat pumps and biomass stoves
- All offer a 30% credit; some include labor costs, some don't; all subject to an individual cap or to an aggregate cap
- Out-of-Scope for VITA: solar panels, solar water heaters, wind turbines, geothermal, battery storage, and electric vehicles.
- No lifetime limitations - so every year starts again.
- No rollovers from year to year - has to be a separate installation each year.

Residential Energy Credits

4012 G -20,21

- "Improvements" must be in your main home.
- "Energy Property" must be in the home you live in; includes renters.
- Placed in service during tax year; not based on payment.
- Does not apply to newly constructed homes.

- Does it qualify as Energy Efficient?
  - As part of our due diligence, we always ask the taxpayer if meets the efficiency requirements.
  - If they say "yes", we include it without verifying.
  - If they are hesitant, we refer them to:
    - *www.irs.gov/credits-deductions/frequently-asked-questions-about-energy-efficient-home-improvements-and-residential-clean-energy-property-credits-energy-efficiency-requirements*
    - Or to: https://www.energystar.gov/about/federal-tax-credits

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Tax Exempt Interest

Some taxpayers, especially those with brokerage statements, have invested in tax-exempt securities. The most common type is municipal bonds.

So, why are we talking about these, if they are tax-exempt?

1. They still need to be entered on the tax return.
2. Just because they are tax-exempt on the federal return, does NOT mean they are also tax-exempt on the state return.
3. Only in-state bonds are also tax-exempt to the taxpayer's state.
   - Example, only Ohio muni-bond dividends are also tax-exempt for an OH resident.
4. Each of our states, OH/KY/IN, require a manual calculation and entry in TaxSlayer for the state-taxable amount.

Tax Exempt Interest

Steps required of the tax preparer:

1. Determine the state-taxable amount
   - Based upon data from the taxpayer or from the details in the brokerage statement (usually on one of the very back pages).
   - If not known, we assume that it is 100% state-taxable.
2. Enter the state-taxable amount in the state section of TaxSlayer:
   - OH: "Additions to Income"->"Enter federally tax-exempt interest and dividend income from other states" (It's the topmost entry block)
   - KY: "Additions to Federal AGI" -> "Adjustment to calculated interest income from bonds issued by Other States and their Political Subdivisions on Married Filing Combined returns" (It's the topmost entry block)
   - IN: "Additions to Income" -> "OOS municipal obligation interest add-back" (It's the third entry block)

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Need help – we are here!

- Send a request for assistance or question(s) to:
  - freetax@uwgc.org
  - Include your name, e-mail, and phone.

- A trainer will contact you.

- Our team of trainers is here to help you. You will not know every aspect of tax law – none of us do! We will ensure you are supported when you come to volunteer at a site. You got this!

Thank You