3 HOURS FEDERAL TAX LAW UPDATES CONTINUING PROFESSIONAL EDUCATION COURSE

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Table of Contents

Thank you for choosing IRSTaxTraining.com, Inc. This intermediate self-study course covers Federal tax law updates and is eligible for 3 hours of continuing professional education (CPE) credits. We know your time is important to you, so we have produced the most comprehensive and innovative tax education products on the market today. We focus on customer service and satisfaction and we strive to look for new and responsive ways to make earning your IRS and CTEC requirements as convenient as possible.

Since this is a self-study course, you can complete it at your own pace and on your own schedule. The minimum passing requirement is 70% on the examination questions at the end of the material. The online exam has no time limit and is open book, so you are allowed to look up answers in the text we provide. You do not need to finish the exam in one continuous sitting as all of the answers you enter online are automatically saved. After you submit the exam to us, we will grade it and, upon successful completion, e-mail you a Certificate of Completion and notify the IRS and (if applicable) CTEC that you earned CPE credits.

Course Description

This updates course focuses on key Federal tax law provisions recently enacted or indexed for inflation. The course highlights major tax changes that are of significant importance to a tax practitioner. Among other topics, this course includes information about the American Rescue Plan (ARP) Act of 2021 and Consolidated Appropriations Act, 2021 tax provisions, the most common tax credits and deductions, and important tax law reminders.

All 2021 legislative amendments and changes received as of press time are reflected, and references to Federal tax laws are up to date as of the publication of this course. However, where 2021 tax law information was not available you will find the 2020 tax law for your reference. The focus is on the law applicable to the filing of income tax returns in 2022 for the 2021 tax year. Additionally, if legislation has made changes effective during 2021, we indicate this along with the effective date to avoid confusion.

The course includes a table of contents and comprehensive index to help guide your search for specific topics. Additionally, if you are using the electronic version of the course, you can use the word search function by pressing “CTRL + F” on your keyboard and entering the word(s) you would like to look up.

Along with the extensive course content, you will also find a glossary and a bibliography you can use to find additional reference material when searching for particular topics or answers to review and examination questions. The numbers in parentheses at the end of a sentence correspond to the numbers in the bibliography.

Completion Deadline and Exam: This course, including the examination, must be completed within one year of the date of purchase or by December 31st of the current year if qualifying for the IRS Annual Filing Season Program (AFSP). CTEC Registered Tax Preparers must complete by January 15th which is the late CTEC deadline for annual registration (early registration deadline without penalty is October 31st).

Course Level: This intermediate course is appropriate for existing tax professionals at all knowledge levels.
CPE Credits: 3 Hours
Category: Taxation
Prerequisite: None
Advanced Preparation: None

Course Learning Objectives

1. Identify important tax law changes under the Consolidated Appropriations Act, 2021 including changes to individual tax brackets, increase of the standard deduction, repeal of personal exemption and modifications to itemized deductions.
2. Define the changes affected by inflation and recent tax law especially as they relate to individual tax credits and deductions, certain retirement income and filing the tax return.
3. Review tax law changes and tax planning strategy based on the overview provided for the Affordable Care Act.

Review Questions and Feedback

Throughout the lesson there are several review questions that are designed to help you learn the material you have just studied. Review questions are for instructional use only and you will not be graded on these questions. We provide both the answers to each question and an explanation or feedback as to how we arrived at each answer at the end of the lesson. Review feedback also contains evaluative feedback explaining why incorrect answers are wrong.

Best practice suggests that you should try to answer these questions on your own first, and only then refer to the answer key and feedback to see how well you did in terms of learning the material. As with all self-study CPE courses, you can refer back to the course material to locate the answers - the so called 'open book' learning method is permissible.

Final Examination

The final examination is intended to test your overall comprehension of the course. Each question will relate to topics found throughout the course so all of the answers can be found in the material. Passing the final exam from a self-study course is contingent upon scoring 70% or higher on the exam questions related to the course material. The examination consists of 15 multiple-choice questions, meaning you must correctly answer 11 in order to pass.

How To Submit The Online Examination:

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- Answer questions.
- Submit answers and completed survey.
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The exam has no time limit, and is open book, so you are allowed to look up answers in the text we provide. You do not need to finish the exam in one continuous sitting as all of the answers you enter online are automatically saved. After you submit the online exam to us you will receive a pass/fail message.

If you should fail the exam on your first attempt, you will have the option to re-take the exam at no additional cost. If you score less than 70%, a message will be displayed at the bottom of the page along with a list of incorrect questions. You have unlimited attempts to pass an exam.

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Understanding the Icons Used in this Book

	Important: Update or change
Tip	**Tip**: Significant information
	Note: Additional information
	Review Question: Learning opportunity

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CTEC California Tax Education Council APPROVED EDUCATION PROVIDER

CE IRS-APPROVED CONTINUING EDUCATION PROVIDER

NASBA National Association of State Boards of Accountancy

2021 Federal Tax Legislation and Continuing Changes, Recent Tax Law Update Reminders

American Rescue Plan (ARP) Act of 2021

On March 11, 2021, the President signed the American Rescue Plan (ARP) Act into law. The legislation is one of the most sweeping economic recovery plans in the nation's history.

Among other items, the Act includes provisions that: [1]

- Extend unemployment benefits and related services.
- Make up to $10,200 of 2020 unemployment compensation tax-free.
- Make student loan forgiveness tax-free through 2025.
- Provide a maximum recovery rebate of $1,400 per eligible individual.
- Expand and otherwise modify certain tax credits, including the Child Tax Credit and the Earned Income Tax Credit.
- Provide premium assistance for certain health insurance coverage.
- Require coverage, without cost-sharing, of COVID-19 vaccines and treatment under Medicaid and the Children's Health Insurance Program (CHIP).

Unemployment Benefits

The Act makes the first $10,200 in unemployment benefits tax-free in 2020 for taxpayers making less than $150,000 per year. If both individuals in a married couple who file taxes jointly received unemployment insurance benefits in 2020, each will see taxes waived on the first $10,2000 of that income - for a total of $20,400 - as long as their combined adjusted gross income is less than $150,000.

Recovery Rebate Credit

The Act creates a new round of economic impact payments to be sent to qualifying individuals. The same as last year's two rounds of stimulus payments, the economic impact payments are set up as advance payments of a recovery rebate credit. The Act creates a new Section 6428B that provides individuals with a $1,400 recovery rebate credit ($2,800 for married taxpayers filing jointly) plus $1,400 for each dependent for 2021, including college students and qualifying relatives who are claimed as dependents. As with last year's economic impact payments, the IRS will send out the advance payments of the credit.

For single taxpayers, the credit and corresponding payment will begin to phase out at an adjusted gross income (AGI) of $75,000, and the credit will be completely phased out for single taxpayers with an AGI over $80,000. For married taxpayers who file jointly, the phaseout will begin at an AGI of $150,000 and end at AGI of $160,000. And for heads of household, the phaseout will begin at an AGI of $112,500 and be complete at AGI of $120,000.

The act uses 2019 AGI to determine eligibility unless the taxpayer has already filed a 2020 return.

Child Tax Credit

The act expands the Child Tax Credit in several ways and provides that taxpayers can receive the credit in advance of filing a return. The act makes the credit fully refundable for 2021 and allows taxpayers with qualifying children who are 17 or younger to claim the credit for the 2021 taxable year (changed from 16 or younger).

Additionally, the Act increases the credit amount for each qualifying child for the 2021 taxable year from $2,000 to $3,000 ($3,600 for qualifying children who have not attained age 6 as of the close of the calendar year in which the taxable year of the taxpayer begins). The increased credit amount phases out for taxpayers with incomes over

$150,000 for married taxpayers filing jointly, $112,500 for heads of household, and $75,000 for others, reducing the expanded portion of the credit by $50 for each $1,000 of income over those limits.

The IRS is directed to estimate taxpayers' Child Tax Credit amounts and pay monthly in advance one-twelfth of the annual estimated amount. Payments will run from July through December 2021. The IRS must set up an online portal to allow taxpayers to opt out of advance payments or provide information that would be relevant to modifying the amount.

A taxpayer who earns too much to qualify for the expanded tax credits could still claim the base $2,000 credit for their children provided their incomes are below the current thresholds of $200,000 for single taxpayers and $400,000 for married couples.

Earned Income Tax Credit (EITC)

The act also makes several changes to the Earned Income Tax Credit (EITC). It introduces special rules for individuals with no children: for 2021, the applicable minimum age is decreased to 19 years old, except for students (24 years old) and qualified former foster youth or homeless youth (18 years old). Additionally, the Act, for the 2021 taxable year, eliminates the current maximum age of 64 for receiving the EITC for such taxpayers.

For taxpayers with no qualifying children in the 2021 taxable year, the provision also increases both the credit percentage and phaseout percentage from 7.65% to 15.3%, as well as increases the EITC amount from $4,220 to $9,820 and the phaseout amount from $5,280 to $11,610.

The credit would be allowed for certain separated spouses and the threshold for disqualifying investment income would be raised from $2,200 to $10,000. Lastly, taxpayers would be allowed to use their 2019 income instead of 2021 income in figuring the credit amount.

Child and Dependent Care Credit

Another temporary provision in the Act, applicable only to the 2021 taxable year, increases the credit for dependent care assistance employment expenses, in the case where the taxpayer has one dependent, from $3,000 to $8,000, and, in the case where the taxpayer has two or more dependents, from $6,000 to $16,000. The Act increases the percentage of these expenses that may be claimed as a credit from 35% to 50% and begins to phase out when the taxpayer's adjusted gross income (AGI) exceeds $125,000. For households with income over $400,000, the credit can be reduced below 20%. Also, for the 2021 taxable year, the credit is refundable.

For a taxpayer who receive reimbursements from his or her employer, there is an exclusion from his or her gross income of amounts paid by an employer for dependent care assistance; the Act increases this exclusion amount from $5,000 to $10,500 (or from $2,500 to $5,250 for a separate return filed by a married individual). This change only applies to the 2021 taxable year.

Premium Tax Credit

The Act expands the Premium Tax Credit for 2021 and 2022 by changing the applicable percentage amounts. Also, taxpayers who received too much in advance Premium Tax Credits in 2020 will not have to repay the excess amount. A special rule is added that treats a taxpayer who has received, or has been approved to receive, unemployment compensation for any week beginning during 2021 as an applicable taxpayer. Lastly, taxpayers who receive unemployment compensation during any week beginning in 2021 may be eligible to receive the Premium Tax Credit to help pay for 2021 Marketplace coverage.

Health Insurance Premium Assistance

Another temporary provision in the Act that applies only to the 2021 and 2022 taxable years increases the subsidies for eligible taxpayers with coverage purchased on the Affordable Care Act (ACA) marketplaces by making the insurance indexing adjustments inapplicable to the 2021 and 2022 tax years, as well as reducing the applicable premium percentages that are considered when calculating the premium assistance amount. Also, for 2021 and 2022, the Act further expands the number of taxpayers eligible for assistance by allowing households with taxable income over 400% of the poverty line to claim assistance.

Student Loan Debt

The American Rescue Plan (ARP) adds a temporary exception to the general rule for student loans. From 2021 to 2025, forgiven student loan debt is not subject to Federal income tax. The provision applies to student loans provided by the Federal government, state governments, and eligible educational institutions, as well as certain private education loans as defined in the Truth in Lending Act.

The American Rescue Plan does not forgive any student loan debt. At this time, the tax exemption only applies to debt cancelled under current student loan forgiveness programs.

Consolidated Appropriations Act, 2021

The Consolidated Appropriations Act, 2021, a major government funding bill, also included economic stimulus provisions due to the coronavirus pandemic. The bill passed overwhelmingly and with bipartisan support on December 21, 2020. (2)

Charitable Contributions

This Act extends and modifies the non-itemizer charitable deduction for 2021. The provision increases the maximum amount that may be deducted such that married couples filing a joint return may deduct up to $600 (while non-married filers or married filers who file separately are limited to $300). Additionally, the provision restructures the deduction such that, although it may be claimed only by non-itemizers, the deduction does not reduce adjusted gross income. The Act also extends through 2021 the increased limit from the CARES Act on deductible charitable contributions for corporations and taxpayers who itemize.

Expanded Flexible Spending Arrangements (FSA)

The Act allows taxpayers to carry amounts from FSAs forward into 2021 (and again into 2022). This would apply to FSAs for health care and dependent care.

- Allows plans to permit health and dependent care flexible spending arrangements (FSA) to carryover unused benefits up to the full annual amount from 2020 to 2021 and 2021 to 2022.
- Allows plans to permit a 12-month grace period for unused benefits or contributions in health and dependent care FSAs for plan years ending in 2020 or 2021.
- Allows plans to extend the maximum age of eligible dependents from 12 to 13 for dependent care FSAs for the 2020 plan year and unused amounts from the 2020 plan year carried over into the 2021 plan year.
- Allows plans to permit a prospective change in election amounts for health and dependent care FSAs for plan years ending in 2021.

Medical Expense Deduction Floor

Beginning in 2021, the medical expense deduction floor is moved permanently to 7.5%. That means that the taxpayer can deduct (assuming he or she itemizes) medical expenses which exceed 7.5% of his or her adjusted gross income (AGI).

Education Benefits

Beginning in 2021, the qualified Tuition and Fees Deduction is replaced. Instead, the phase-out limits on the Lifetime Learning Credit are increased to $80,000 ($160,000 for married filing jointly).

Temporary Allowance of Full Deduction for Business Meals

The Act provides a 100% deduction for business meal food and beverage expenses, including any carry-out or delivery meals, provided by a restaurant that are paid or incurred in 2021 and 2022.

Tax Forms

Form 1099-NEC

The IRS has reintroduced Form 1099-NEC - Nonemployee Compensation as the new way to report self-employment income instead of Form 1099-MISC as traditionally had been used. This was done to help clarify the separate filing deadlines on Form 1099-MISC and the new 1099-NEC form will be used starting with the 2020 tax year.

Beginning with the 2020 tax year, the IRS requires business taxpayers to report nonemployee compensation on the new Form 1099-NEC instead of on Form 1099-MISC. Businesses need to use this form if they made payments totaling $600 or more to a nonemployee, such as an independent contractor.

In general, a business must report payments it makes if it meets the following four conditions:

1. The payment is made to someone who is not an employee.
2. The payment is made for services in the course of trade or business.
3. The payment is made to an individual, partnership, estate, or corporation.
4. The payment total is at least $600 for the year.

Additionally, businesses will need to file Form 1099-NEC:

- When they pay an individual at least $10 in royalties, or
- If the business has withheld any federal income tax under the backup withholding rules regardless of the amount of payments for the year to the nonemployee.

Nonemployee compensation can include:

- Fees.
- Benefits.
- Commissions.
- Prizes and awards for services performed by a nonemployee.
- Other forms of compensation for services performed for trade or business by an individual who is not an employee.

Generally, payers need to file these forms by January 31 and have no automatic 30-day extensions to file unless the business meets certain hardship conditions.

Form 1040-NR Revision

Form 1040-NR has been revised to more closely follow the format of Forms 1040 and 1040-SR. Also, beginning in 2020, Form 1040-NR will use Schedules 1, 2, and 3.

Form W-4 - Employee’s Withholding Certificate Redesigned

The new Form W-4 - Employee's Withholding Certificate design reduces the form’s complexity and increases the transparency and accuracy of the withholding system. While it uses the same underlying information as the old design, it replaces complicated worksheets with more straightforward questions that make accurate withholding easier for employees.

Allowances are no longer used for the redesigned Form W-4 to increase transparency, simplicity, and accuracy. In the past, the value of a withholding allowance was tied to the amount of the personal exemption. Due to changes in law, currently the taxpayer cannot claim personal exemptions or dependency exemptions.

Employees who have submitted Form W-4 in any year before 2021 are not required to submit a new form merely because of the redesign. Employers will continue to compute withholding based on the information from the employee’s most recently submitted Form W-4.

Form 1040-SR - U.S. Tax Return for Seniors

Form 1040-SR - U.S. Tax Return for Seniors has larger print, removes shading around boxes, and has lines for specific retirement income streams like Social Security benefits, IRA distributions, and pensions and annuities. Form 1040-SR uses the same schedules and instructions as Form 1040 does.

Form 1040X Electronic Filing Options

For the first time taxpayers will be able to file their Form 1040X - Amended U.S Individual Income Tax Return electronically. The new electronic option will allow the IRS to receive amended returns faster while minimizing errors normally associated with manually completing the form. It will also provide the IRS with more complete and accurate data to help customer service representatives answer taxpayer questions. Only tax year 2019 Forms 1040 and 1040-SR returns can be amended electronically. In general, taxpayers will still have the option to submit a paper version of the Form 1040X and should follow the instructions for preparing and submitting the paper form.

Fewer Numbered Schedules

There are only three numbered schedules instead of six. Schedules 2 and 4 were combined into Schedule 2 and it is where taxpayers will report any additional taxes they may owe. Schedules 3 and 5 were combined into Schedule 3 and it is where taxpayers will report any credits that they did not claim on Form 1040 or 1040-SR.

IRA and Pension Reporting

Taxpayers will now report their IRA distributions and pensions and annuities on separate lines. They use lines 4a and 4b on Form 1040 or 1040-SR to report IRA distributions and the taxable amount. They use new lines 5a and 5b to report pensions and annuities and the taxable amount.

Capital Gain or Loss Reporting

In prior tax years, capital gain or (loss) was reported on Schedule 1 (Form 1040), line 13. In 2021, it will be reported on Form 1040 or 1040-SR, line 7.

2021 Federal Tax Legislation

Tax Rate Schedules for 2021

One of the keys to the Tax Cuts and Jobs Act is a reduction in individual tax rates. While the current number of tax brackets has been retained, each one has been reduced. There are seven tax rates for individual taxpayers. They are: 10%, 12%, 22%, 24%, 32%, 35% and 37%. The tax rate of 37% applies to joint filers with taxable income over $628,300 (single filers over $523,600). The following are the tax rates schedules for tax year 2021 based on certain filing status. [3]

Unmarried Individuals (other than Surviving Spouses and Heads of Households)	
If Taxable Income Is:	**The Tax Is:**
Not over $9,950	10% of the taxable income
Over $9,950 but not over $40,525	$995 plus 12% of the excess over $9,950
Over $40,525 but not over $86,375	$4,664 plus 22% of the excess over $40,525
Over $86,375 but not over $164,925	$14,751 plus 24% of the excess over $86,375
Over $164,925 but not over $209,425	$33,603 plus 32% of the excess over $164,925
Over $209,425 not over $523,600	$47,843 plus 35% of the excess over $209,425
Over $523,600	$157,804.25 plus 37% of the excess over $523,600

Table 1-1 - Revenue Procedure 2020-45 (2021)

Married Individuals Filing Joint Returns and Surviving Spouses	
If Taxable Income Is:	**The Tax Is:**
Not over $19,900	10% of the taxable income
Over $19,900 but not over $81,050	$1,990 plus 12% of the excess over $19,900
Over $81,050 but not over $172,750	$9,328 plus 22% of the excess over $81,050
Over $172,750 but not over $329,850	$29,502 plus 24% of the excess over $172,750
Over $329,850 but not over $418,850	$67,206 plus 32% of the excess over $329,850
Over $418,850 but not over $628,300	$95,686 plus 35% of the excess over $418,850
Over $628,300	$168,993.50 plus 37% of the excess over $628,300

Table 1-2 - Revenue Procedure 2020-45 (2021)

Married Individuals Filing Separate Returns	
If Taxable Income Is:	**The Tax Is:**
Not over $9,950	10% of the taxable income
Over $9,950 but not over $40,525	$995 plus 12% of the excess over $9,950
Over $40,525 but not over $86,375	$4,664 plus 22% of the excess over $40,525
Over $86,375 but not over $164,925	$14,751 plus 24% of the excess over $86,375
Over $164,925 but not over $209,425	$33,603 plus 32% of the excess over $164,925
Over $209,425 not over $314,150	$47,843 plus 35% of the excess over $209,425
Over $314,150	$84,496.75 plus 37% of the excess over $314,150

Table 1-3 - Revenue Procedure 2020-45 (2021)

Heads of Households	
If Taxable Income Is:	**The Tax Is:**
Not over $14,200	10% of the taxable income
Over $14,200 but not over $54,200	$1,420 plus 12% of the excess over $14,200
Over $54,200 but not over $86,350	$6,220 plus 22% of the excess over $54,200
Over $86,350 but not over $164,900	$13,293 plus 24% of the excess over $86,350
Over $164,900 but not over $209,400	$32,145 plus 32% of the excess over $164,900
Over $209,400 not over $523,600	$46,385 plus 35% of the excess over $209,400
Over $523,600	$156,355 plus 37% of the excess over $523,600

Table 1-4 - Revenue Procedure 2020-45 (2021)

Estates and Trusts	
If Taxable Income Is:	**The Tax Is:**
Not over $2,650	10% of the taxable income
Over $2,650 but not over $9,550	$265 plus 24% of the excess over $2,650
Over $9,550 but not over $13,050	$1,921 plus 35% of the excess over $9,550
Over $13,050	$3,146 plus 37% of the excess over $13,050

Table 1-5 - Revenue Procedure 2020-45 (2021)

Long Term Capital Gains and Qualified Dividends		
Tax Bracket	**Short-term**	**Long-term**
10%, 12% brackets	Ordinary rate	0%
22%, 24%, 32%, 35% brackets	Ordinary rate	15%
37% bracket	Ordinary rate	20%

Table 1-6 - Revenue Procedure 2020-45 (2021)

An additional 3.8% Federal Net Investment Income Tax (NIIT) applies to individuals on the lesser of net investment income or modified adjusted gross income (MAGI) in excess of $200,000 (single) or $250,000 (married/filing jointly and qualifying widow(er)s). These threshold amounts are not indexed for inflation. The NIIT for an estate or trust is equal to 3.8% of the lesser of undistributed net investment income or adjusted gross income (AGI) that exceeds the inflation-adjusted threshold for the highest tax rate for estates and trusts.

Standard Mileage Rates

The following are the 2021 optional standard mileage rates used to calculate the deductible costs of operating an automobile for business, charitable, medical or moving purposes during 2021. As of January 1, 2021, the standard mileage rates for the use of a car, van, pickup or panel truck are: (4)

- 56 cents per mile driven for business use, down 1.5 cents from the rate for 2020.
- 16 cents per mile driven for medical or moving purposes, down one cent from the rate for 2020.
- 14 cents per mile driven in service of charitable organizations (currently fixed by Congress).

The business mileage rate decreased 1.5 cents for business travel driven and 1 cent for medical and certain moving expense from the rates for 2020. The charitable rate is set by statute and remains unchanged.

It is important to note that under the Tax Cuts and Jobs Act, taxpayers cannot claim a miscellaneous itemized deduction for unreimbursed employee travel expenses. Taxpayers also cannot claim a deduction for moving expenses, except members of the Armed Forces on active duty moving under orders to a permanent change of station.

The standard mileage rate for business is based on an annual study of the fixed and variable costs of operating an automobile, including depreciation, insurance, repairs, tires, maintenance, gas, and oil. The rate for medical and moving purposes is based on the variable costs, such as gas and oil. The charitable rate is set by law.

Taxpayers always have the option of claiming deductions based on the actual costs of using a vehicle rather than the standard mileage rates. A taxpayer may not use the business standard mileage rate for a vehicle after using any depreciation method under the Modified Accelerated Cost Recovery System (MACRS) or after claiming a Section 179 deduction for that vehicle. In addition, the business standard mileage rate cannot be used for more than four vehicles used simultaneously.

If the taxpayer wants to use the standard mileage rate for a car he or she owns, the taxpayer must choose to use it in the first year the car is available for use in his or her business. Then in later years, the taxpayer can choose to use either the standard mileage rate or actual expenses.

Standard Deduction

Under the Tax Cuts and Jobs Act the standard deduction amounts increased to $12,550 for individuals, to $18,800 for heads of household, and to $25,100 for married couples filing jointly and surviving spouses in 2021. (3)

Standard Deductions 2021 Tax Year	
Filing Status	**Standard Deduction Amount**
Single	$12,550
Married Filing Jointly	$25,100
Married Filing Separately	$12,550
Heads of Household	$18,800
Surviving Spouse	$25,100

Table 1-7 - Revenue Procedure 2020-45 (2021)

For 2021, the additional standard deduction for married taxpayers 65 or over or blind will be $1,350. For a single taxpayer or head of household who is 65 or over or blind, the additional standard deduction for 2021 will be $1,700. For 2021, the standard deduction amount for an individual who may be claimed as a dependent by another taxpayer cannot exceed the greater of $1,100 or the sum of $350 and the individual’s earned income.

Elderly and/or Blind Taxpayers

The standard deduction chart for people age 65 or older (shown below) lists the additional standard deduction for taxpayers who are age 65 or older and/or blind at the end of the tax year. The standard deduction is calculated by adding the person's standard deduction (based on their filing status), plus the additional amount. Additional standard deduction amounts for 2021 are $1,700 for single or head of household or $1,350 for married filing jointly, married filing separately, or qualifying widow.

For example, if the taxpayer is married, filing a joint return and both he and his wife are 68 years of age, what would their standard deduction amount come to for 2021? When completing his or her income tax return, the taxpayer would check off the box for him as being 65 or older, as well as the same box for his spouse. Two boxes are checked, and looking at the married filing joint return section, we see that their available standard deduction would be $27,800. If one was also blind, the standard deduction for 2021 would be $29,150 having three boxes checked.

Partial blindness qualifies, with a certified statement from an eye doctor (ophthalmologist or optometrist) attesting that the vision in the taxpayer's better eye is 20/200 or worse after being corrected with glasses or contact lenses or that the taxpayer's field of vision is not more than 20 degrees. If the taxpayer's eye condition is not likely to improve beyond these limits, the statement should include this fact. The taxpayer should keep the statement with his or her records. If the taxpayer is blind on the last day of the year, he or she is entitled to the higher standard deduction.

Standard Deduction Chart for People Age 65 or Older or Blind		
Filing Status	Number from the boxes checked on Page 1 of Form 1040	Standard Deduction for 2021
Single	1 2	$14,250 $15,950
Married filing jointly or qualifying widow(er)	1 2 3 4	$26,450 $27,800 $29,150 $30,500
Married filing separately	1 2 3 4	$13,900 $15,250 $16,600 $17,950
Head of household	1 2	$20,500 $22,200

Table 1-8 - Publication 501 - Table 7 – Standard Deduction Chart for People who are 65 or Older or Who are Blind (2021)

Personal Exemption

The Tax Cuts and Jobs Act repeals the personal and dependency exemptions. This suspension of the personal and dependency exemptions will apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.

Changes to Above-the-line Deductions

The Tax Cuts and Jobs Act (TCJA) changed certain above-the-line deductions. The alimony deduction is repealed. The change applies to any divorce or separation instrument executed or modified after December 31, 2018 (the modification must expressly state that the new rule applies). Also, the deduction for moving expenses is also repealed, except for members of the military. The domestic production activities deduction (DPAD) is also repealed. The educator expenses deduction, student loan interest deduction, health savings account (HSA) deduction, IRA deduction and deductions for self-employed taxpayers all stay the same.

Changes to Itemized Deductions

Under the Tax Cuts and Jobs Act (TCJA), the medical expense deduction remained in place with a lower floor of 7.5% for tax years 2017 (retroactively) and 2018 for all taxpayers regardless of age. The Consolidated Appropriations Act, 2021 makes permanent the lower threshold of 7.5% for all taxpayers, originally restored for 2017 and 2018 and then extended for 2019 and 2020.

The deduction for state and local income, property, and sales taxes (SALT) is capped at $10,000. The SALT deduction is a substantial reduction from the former rule allowing all property taxes, plus all state and local income or sales taxes, to be claimed as an itemized deduction.

After passage of the TCJA, cash contributions to public charities were generally limited to 60% of a taxpayer's adjusted gross income (AGI). The Coronavirus Aid, Relief, and Economic Security Act (CARES) allowed such contributions to be deducted up to 100% of AGI for 2020, with any excess contributions available to be carried over to the next five years. The Consolidated Appropriations Act, 2021 extends through 2021 the increased limit from the CARES Act on deductible charitable contributions for corporations and taxpayers who itemize. No deduction is allowed for donations in exchange for college athletic event seating rights. The cents-per-mile rate for driving for charitable purposes has not been changed; it remains at 14 cents per mile.

Also, the casualty loss deduction is repealed, except for losses in Federally declared disasters. Miscellaneous itemized deductions subject to the 2% of adjusted gross income (AGI) floor, such as unreimbursed employee business expenses and tax preparation fees, are repealed.

The TCJA reduced the maximum amount of mortgage debt to acquire a first or second residence for which the taxpayer can claim itemized interest expense deductions from $1 million (or $500,000 if he or she uses married filing separate status) to $750,000 (or $375,000 if he or she uses married filing separate status). However, this change did not affect home acquisition mortgages taken out under binding contracts in effect before December 16, 2017 as long as the home purchase closed before April 1, 2018.

The previous-law of $1,000,000/$500,000 limits continue to apply to home acquisition mortgages that were taken out under the previous-law rules and are then refinanced after this year (as long as the refinanced loan principal does not exceed the old loan balance at the time of the refinancing). The TCJA also eliminated the previous-law rule that allowed interest deductions on up to $100,000 of home-equity loan balances and lines of credit, unless they are used to buy, build, or substantially improve the taxpayer's home that secures the loan.

Itemized Deduction Phase-Out

The Tax Cuts and Jobs Act repeals the phase-out of itemized deductions for high-income taxpayers. This suspension of the overall limitation on itemized deductions will apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.

Review Question 1

Under the Tax Cuts and Jobs Act all of the following above-the-line deductions are unchanged except:

A. Student Loan Interest Deduction
B. Educator Expenses Deduction
C. Alimony Deduction
D. IRA Deduction

See Review Feedback for answer.

Alternative Minimum Tax (AMT) Exemption Amount

Following the passage of the Tax Cuts and Jobs Act, the tax rates for the alternative minimum tax (AMT) are retained, but the exemption amounts are increased.

A specified amount of Alternative Minimum Taxable Income (AMTI) is exempt from alternative minimum taxation. The amount varies according to the taxpayer's filing status and the tax year at hand. The exemption is subtracted from the taxpayer's AMTI to determine the amount of his or her AMTI that is subject to tax at the AMT rates. For 2021, the exemption amounts increase to $114,600 for joint filers, $57,300 for married filing separately, $73,600 for individual filers and $25,700 for estates and trusts. The alternative minimum tax (AMT) exemption amounts are permanently adjusted for inflation.

For taxable years beginning in 2021, the excess taxable income above which the 28% tax rate applies is:

- Married Individuals Filing Separate Returns - $99,950.
- Joint Returns, Unmarried Individuals (other than surviving spouses), and Estates and Trusts - $199,900.

Additionally, the taxpayer's exemption phases out if his or her AMTI exceeds the thresholds indicated below. More specifically, the exemption is reduced by 25% of the amount by which his or her AMTI exceeds the applicable threshold for his or her filing status. For 2021, the phase-out threshold for the exemption increases to $1,047,200 for joint filers, $523,600 for individual filers and $85,650 for estates and trusts.

Filing Status	Threshold Phase-out Amount	Complete Phase-out Amount
Joint Returns or Surviving Spouses	$1,047,200	$1,505,600
Unmarried Individuals (other than Surviving Spouses)	$523,600	$818,000
Married Individuals Filing Separate Returns	$523,600	$752,800
Estates and Trusts	$85,650	$188,450

Table 1-9 - Instructions for Form 6251 (2021)

The AMT exemption for 2021 for a child subject to the kiddie tax will be the lesser of (1) $7,950 (up from $7,900 for 2020) plus the child's earned income, or (2) $73,600 (up from $72,900 for 2020).

If the taxpayer is not liable for AMT this year, but he or she paid AMT in one or more previous years, he or she may be eligible to take a special minimum tax credit against his or her regular tax this year. If eligible, the taxpayer should complete and attach Form 8801 - Credit for Prior Year Minimum Tax - Individuals, Estates, and Trusts, to claim the minimum tax credit. (5)

Flexible Spending Accounts (FSA)

A Flexible Spending Account (also known as a flexible spending arrangement) is a special account the taxpayer puts money into that he or she uses to pay for certain out-of-pocket health care costs. The taxpayer does not have to pay taxes on this money. This means he or she will save an amount equal to the taxes he or she would have paid on the money he or she sets aside. The taxpayer can use funds in his or her FSA to pay for certain medical and dental expenses, including copayments and deductibles.

FSAs are available only with job-based health plans. Employers may make contributions to a taxpayer's FSA. However, a taxpayer cannot spend FSA funds on insurance premiums.

The annual dollar limit on contributions to employer-sponsored health care FSAs remains at $2,750 in 2021. Both employer and employee may contribute to an employee's health FSA, but contributions from all sources combined must not exceed the $2,750 annual limit for 2021. The statutory $2,750 limit under IRC Section 125(i) applies only to salary reduction contributions under a health FSA, and does not apply to certain employer non-elective contributions (sometimes called flex credits), to any types of contributions or amounts available for reimbursement under other types of FSAs, health savings accounts, or health reimbursement arrangements, or to salary reduction contributions to cafeteria plans that are used to pay an employee's share of health coverage premiums (or the corresponding employee share under a self-insured employer-sponsored health plan).

Cafeteria plan rules ordinarily require FSA contributions to be used for expenses incurred within the year of contribution, or else they will be forfeited. The rules include limited exceptions that allow plans to either contain an additional 2.5-month grace period on to the end of the plan year for participants to incur expenses that may be reimbursed from the prior year's contributions or carry up to $550 (recently indexed up from $500) from health FSA contributions over to the next year. The Consolidated Appropriations Act, 2021 expands on these rules and provide several additional, temporary mechanisms that employers may introduce to their plans to avoid forfeitures of FSA contributions: (2)

- *Increased Carryover Opportunities* - Allows plans to permit health and dependent care flexible spending arrangements (FSA) to carryover unused benefits up to the full annual amount from 2020 to 2021 and 2021 to 2022.

- *Expanded Grace Period* - Allows plans to permit a 12-month grace period for unused benefits or contributions in health and dependent care FSAs for plan years ending in 2020 or 2021.
- *Dependent Care Age Limit* - Allows plans to extend the maximum age of eligible dependents from 12 to 13 for dependent care FSAs for the 2020 plan year and unused amounts from the 2020 plan year carried over into the 2021 plan year.
- *Mid-year change* - Allows plans to permit a prospective change in election amounts for health and dependent care FSAs for plan years ending in 2021.

Rules that otherwise apply with regard to cafeteria plans and FSAs remain in effect. For example, it appears that employers must still choose between offering a carryover or a grace period. They may not offer both.

Health Savings Account (HSA)

2021 offers individuals and families additional opportunities to save for current and future health care with a Health Savings Account (HSA):

- HSA holders can choose to save up to $3,600 for an individual and $7,200 for a family (HSA holders 55 and older get to save an extra $1,000 which means $4,600 for an individual and $8,200 for a family) - and these contributions are 100% tax deductible from gross income.
- Minimum annual deductibles are $1,400 for self-only coverage or $2,800 for family coverage.
- Annual out-of-pocket expenses (deductibles, copayments, and other amounts, but not premiums) cannot exceed $7,000 for self-only coverage and $14,000 for family coverage.

2021 HSA Contribution Limits, Deductibles, and Out-of-Pocket Expenses				
	Minimum Deductible	**Maximum Out-of-Pocket**	**Contribution Limit**	**55+ Contribution Limit**
Single	$1,400	$7,000	$3,600	$4,600
Family	$2,800	$14,000	$7,200	$8,200

Table 1-10 - HSA Contribution Limits, Deductibles, and Out-of-Pocket Expenses (2021)

While the Affordable Care Act allows parents to add their adult children (up to age 26) to their health plans, the IRS definition of a qualified dependent (child or relative) who may be covered under an employee's HSA is different. For example, an employee whose 24-year-old child is covered on his HSA-qualified high-deductible health plan may not be eligible to use HSA funds to pay that child's medical bills (unless the child is a full-time student, and therefore a qualified dependent for tax purposes).

Note

Those under age 65 (unless totally and permanently disabled) who use HSA funds for nonqualified medical expenses face a penalty of 20% of the funds used for such expenses. Funds spent for nonqualified purposes are also subject to income tax.

HSAs can pair with high deductible plans (HDHP). As long as the taxpayer holds an HSA eligible high deductible health plan (HDHP) he or she can contribute tax-advantaged dollars to the account up to the annual limit. In 2021 the out-of-pocket limits for HDHP minimum annual deductibles are $1,400 for self-only coverage or $2,800 for family coverage and annual out-of-pocket expenses (deductibles, copayments, and other amounts, but not premiums) cannot exceed $7,000 for self-only coverage and $14,000 for family coverage.

There are several important differences between FSAs and HSAs. Options such as the taxpayer's flexibility in contributing, the ability to keep his or her unused balance and additional tax benefits can make HSAs the wisest choice if the taxpayer has the option. However, both accounts can potentially save the taxpayer money and make budgeting for medical costs easier.

Important Differences Between HSAs and FSAs		
	Health savings account (HSA)	**Flexible spending account (FSA)**
Eligibility requirements	Eligibility requirements include having a high-deductible health plan (HDHP).	No eligibility requirements.
Contribution limit	2021 contributions capped at $3,600 for individuals or $7,200 for families.	2021 contributions capped at $2,750.
Changing contribution amount	The taxpayer can change how much he or she contributes to the account at any point during the year.	Contribution amounts can be adjusted only at open enrollment or with a change in employment or family status.
Rollover	Unused balances roll over into the next year.	Employers may amend their plans to allow employees to carry over all unused amounts in an FSA from a plan year ending in 2020 to a plan year ending in 2021 and from a plan year ending in 2021 to a plan year ending in 2022. This amount is not subject to a dollar cap and applies to dependent care FSAs as well as health FSAs.
Connection to employer	The taxpayer's HSA can follow him or her as he or she changes employment.	In most cases, the taxpayer will lose his or her FSA with a job change. One exception: if the taxpayer is eligible for FSA continuation through COBRA.
Effect on taxes	Contributions are tax-deductible but can also be taken out of the taxpayer's salary pretax. Growth and distributions are tax-free.	Contributions are pretax, and distributions are untaxed.

Table 1-11 - Using a Flexible Spending Account (FSA) - HealthCare.gov (2021)

Review Question 2

All of the following statements are true regarding a Health Saving Account (HSA) except:

A. Cash contributions to an HSA are 100% deductible from the taxpayer's Federal gross income (within legal limits)
B. Interest on savings accumulates tax deferred
C. Withdrawals from an HSA for "qualified medical expenses" are free from Federal income tax
D. The taxpayer will lose his or her HSA with a job change

See Review Feedback for answer.

Pension Plan Limitations

The Internal Revenue Service has set the cost-of-living adjustments affecting dollar limitations for pension plans and other retirement-related items for tax year 2021. Some of the pension plan limitations will change for 2021 because the increase in the cost-of-living index met the statutory thresholds that trigger their adjustment. However, other limitations will remain unchanged because the increase in the index did not meet the statutory thresholds that trigger their adjustment. [6]

Elective Deferral (Contribution) Limits

The elective deferral limit for employees who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan remains at $19,500 in 2021. The catch-up contribution limit for employees aged 50 and over who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan remains at $6,500 in 2021. If the taxpayer is self-employed, the total employer plus employee contributions to all defined contribution plans under Section 415(c)(1)(A) is increased in 2021 from $57,000 to $58,000. (6)

Individual Retirement Arrangements (IRA)

For 2021, the taxpayer's total contributions to all of his or her traditional and Roth IRAs cannot be more than: (7)

- $6,000.
- The taxpayer's taxable compensation for the year.

If the taxpayer was age 50 or older before 2021, the maximum amount that can be contributed to his or her traditional IRA for 2021 will be the smaller of the following amounts:

- $7,000.
- The taxpayer's taxable compensation for the year.

The income ranges for determining eligibility to make deductible contributions to traditional Individual Retirement Arrangements (IRAs) increased for 2021. If the taxpayer is covered by a retirement plan at work, his or her deduction for contributions to a traditional IRA is reduced (phased out) if modified AGI is: (7)

- More than $105,000 but less than $125,000 for a married couple filing a joint return or a qualifying widow(er),
- More than $66,000 but less than $76,000 for a single individual or head of household, or
- Less than $10,000 for a married individual filing a separate return.

If the taxpayer either lives with his or her spouse or files a joint return, and his or her spouse is covered by a retirement plan at work, but the taxpayer is not, the taxpayer's deduction is phased out if his or her modified AGI is more than $198,000 but less than $208,000. If the taxpayer's modified AGI is $208,000 or more, he or she cannot take a deduction for contributions to a traditional IRA.

The IRA contribution limit does not apply to:

- Rollover contributions.
- Qualified reservist repayments.

If the taxpayer files a joint return, he or she may be able to contribute to an IRA even if he or she did not have taxable compensation as long as his or her spouse did. The amount of taxpayer's combined contributions cannot be more than the taxable compensation reported on his or her joint return.

The Setting Every Community Up for Retirement Enhancement (SECURE) Act eliminates the prohibition on traditional IRA contributions for those age 70½ and older as of January 1, 2020. Additionally, the Act increases the age for required minimum distributions (RMD) from individual retirement accounts to age 72 (from age 70½). It also allows part-time workers to participate in 401(k) plans.

Rollovers

Most pre-retirement payments a taxpayer receives from a retirement plan or IRA can be "rolled over" by depositing the payment in another retirement plan or IRA within 60 days. He or she can also have his or her financial institution or plan directly transfer the payment to another plan or IRA. All of the following are methods to complete a rollover:

1. **Direct rollover** - If the taxpayer is getting a distribution from a retirement plan, he or she can ask the plan administrator to make the payment directly to another retirement plan or to an IRA. The taxpayer should contact the plan administrator for instructions. The administrator may issue the taxpayer's distribution in the form of a check made payable to his or her new account. No taxes will be withheld from the transfer amount.

2. **Trustee-to-trustee transfer** - If the taxpayer is getting a distribution from an IRA, he or she can ask the financial institution holding the IRA to make the payment directly from his or her IRA to another IRA or to a retirement plan. No taxes will be withheld from the transfer amount.
3. **60-day rollover** - If a distribution from an IRA or a retirement plan is paid directly to the taxpayer, he or she can deposit all or a portion of it in an IRA or a retirement plan within 60 days. Taxes will be withheld from a distribution from a retirement plan, so the taxpayer will have to use other funds to roll over the full amount of the distribution.

The taxpayer generally cannot make more than one rollover from the same IRA within a 1-year period. He or she also cannot make a rollover during this 1-year period from the IRA to which the distribution was rolled over. If the taxpayer has not elected a direct rollover, in the case of a distribution from a retirement plan, or he or she has not elected out of withholding in the case of a distribution from an IRA, his or her plan administrator or IRA trustee will withhold taxes from the taxpayer's distribution. If the taxpayer later rolls the distribution over within 60 days, he or she must use other funds to make up for the amount withheld. (8)

If the taxpayer decides not to roll over the entire amount of the distribution (including any amount withheld) he or she will report the difference as taxable income. The taxpayer must also pay the 10% additional tax on early distributions on the withheld amount unless he or she qualifies for an exception. If the taxpayer rolls over the full amount of any eligible rollover distribution, he or she receives the entire distribution would be tax-free and the taxpayer would avoid the 10% additional tax on early distributions.

In Revenue Procedure 2016-47, effective August 2016, the IRS has created a new "self-certification" procedure that allows someone who misses the 60-day deadline for rollovers to avoid the expense and delay of obtaining a private letter ruling. Instead, a taxpayer submits a model IRS letter to the new retirement account custodian, checking in that letter one of 11 acceptable excuses for missing the deadline.

A self-certification is not a waiver by the IRS of the 60-day rollover requirement. However, a taxpayer may report the contribution as a valid rollover unless later informed otherwise by the IRS. The IRS, in the course of an examination, may consider whether a taxpayer's contribution meets the requirements for a waiver. The taxpayer must have missed the 60-day deadline because of his or her inability to complete a rollover due to one or more of the following reasons:

- An error was committed by the financial institution receiving the contribution or making the distribution to which the contribution relates.
- The distribution, having been made in the form of a check, was misplaced, and never cashed.
- The distribution was deposited into and remained in an account that the taxpayer mistakenly thought was an eligible retirement plan.
- The taxpayer's principal residence was severely damaged.
- A member of the taxpayer's family died.
- The taxpayer or a member of the taxpayer's family was seriously ill.
- The taxpayer was incarcerated.
- Restrictions were imposed by a foreign country.
- A postal error occurred.
- The distribution was made on account of a levy under Section 6331 and the proceeds of the levy have been returned to the taxpayer.
- The party making the distribution to which the rollover relates delayed providing information that the receiving plan or IRA required to complete the rollover despite the taxpayer's reasonable efforts to obtain the information.

While the reasons are comprehensive, they only apply if the taxpayer was initially eligible to complete a 60-day rollover. As a result of a 2014 U.S. Tax Court decision, taxpayers may only perform one 60-day IRA rollover every 12 months, no matter how many IRAs they have. The contribution must be made to the plan or IRA as soon as practicable after the reason or reasons listed above no longer prevent the taxpayer from making the contribution. This requirement is deemed to be satisfied if the contribution is made within 30 days after the reason or reasons no longer prevent the taxpayer from making the contribution.

One reason the IRS will not allow is that the taxpayer was using his or her retirement money as a short-term loan for some non-retirement purpose, such as a down payment on a house, and missed the 60-day deadline because of a complication or delay.

IRA One-Rollover-Per-Year Rule

Since January 1, 2015, a taxpayer can make only one rollover from a traditional IRA to another (or the same) traditional IRA in any 12-month period, regardless of the number of IRAs he or she owns. A similar limitation will apply to rollovers between Roth IRAs. The taxpayer can, however, continue to make as many trustee-to-trustee transfers between IRAs as he or she wants. Amounts transferred between traditional IRAs, either by rollover or trustee-to-trustee transfer, are excluded from the taxpayer's gross income. The one-per year limit does not apply to: (8)

- Rollovers from traditional IRAs to Roth IRAs (conversions).
- Trustee-to-trustee transfers to another IRA.
- IRA-to-plan rollovers.
- Plan-to-IRA rollovers.
- Plan-to-plan rollovers.

The tax consequences of the rule are: (8)

1. The taxpayer must include in gross income any previously untaxed amounts distributed from an IRA if he or she made an IRA-to-IRA rollover (other than a rollover from a traditional IRA to a Roth IRA) in the preceding 12 months.
2. The taxpayer may be subject to the 10% early withdrawal tax on the amount he or she includes in gross income.

If the taxpayer has not elected a direct rollover, in the case of a distribution from a retirement plan, or he or she has not elected out of withholding in the case of a distribution from an IRA, the plan administrator or IRA trustee will withhold taxes from the distribution. If the taxpayer later rolls the distribution over within 60 days, he or she must use other funds to make up for the amount withheld.

If the taxpayer rolls over the full amount of any eligible rollover distribution he or she receives, the entire distribution would be tax-free and he or she would avoid the 10% additional tax on early distributions.

Note

This change will not affect the taxpayer's ability to transfer funds from one IRA trustee directly to another, because this type of transfer is not a rollover (Revenue Ruling 78-406, 1978-2 C.B. 157). The one-rollover-per-year rule of Internal Revenue Code Section 408(d)(3)(B) applies only to rollovers.

The IRS intends to follow the Tax Court's interpretation of Internal Revenue Code Section 408(d)(3)(B). However, to give IRA owners and trustees time to adjust, the IRS delayed implementation until January 1, 2015. Proposed Treasury Regulation Section 1.408-4(b)(4)(ii) will be withdrawn and Publication 590-B - Distributions from Individual Retirement Arrangements (IRAs) has been revised to reflect the new interpretation.

Qualified Reservist Repayments

If the taxpayer was a member of a reserve component and he or she was ordered or called to active duty after September 11, 2001, he or she may be able to contribute (repay) to an IRA amounts equal to any qualified reservist distributions he or she received. The taxpayer can make these repayment contributions even if they would cause his or her total contributions to the IRA to be more than the general limit on contributions. To be eligible to make these repayment contributions, the taxpayer must have received a qualified reservist distribution from an IRA or from a Section 401(k) or 403(b) plan or a similar arrangement.

Note

The qualified reservist repayments cannot be more than the qualified reservist distributions and the taxpayer cannot make these repayment contributions later than the date that is 2 years after his or her active-duty period ends. Also, the taxpayer cannot deduct qualified reservist repayments.

If the taxpayer repays a qualified reservist distribution, include the amount of the repayment with nondeductible contributions on line 1 of Form 8606 - Nondeductible IRAs.

Roth IRA

The Tax Cuts and Jobs Act eliminated the ability to reverse the conversion of a Roth IRA by recharacterizing it as an

IRA by October 15th of the year after the misguided conversion. Under the TCJA all Roth IRA conversions are permanent. If contributions on the taxpayer's behalf are made only to Roth IRAs, his or her contribution limit for 2021 will generally be the lesser of either: (7)

- $6,000.
- The taxpayer's taxable compensation for the year.

If the taxpayer was age 50 or older before 2021 and contributions on his or her behalf were completed only to Roth IRAs, the taxpayer's contribution limit for 2021 will generally be the lesser of either of the following: (7)

- $7,000.
- The taxpayer's taxable compensation for the year.

For 2021, the taxpayer's Roth IRA contribution limit is reduced (phased out) in the following situations: (7)

- His or her filing status is married filing jointly or qualifying widow(er) and his or her modified AGI is at least $198,000. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $208,000 or more.
- His or her filing status is single, head of household, or married filing separately and he or she did not live with his or her spouse at any time in 2021 and his or her modified AGI is at least $125,000. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $140,000 or more.
- His or her filing status is married filing separately, he or she lived with his or her spouse at any time during the year, and his or her modified AGI is more than $0. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $10,000 or more.

Regardless of the taxpayer's age, he or she may be able to establish and make nondeductible contributions to a Roth IRA. The taxpayer does not report Roth IRA contributions on his or her return.

Contribution Limits

The Internal Revenue Service announced cost-of-living adjustments affecting dollar limitations for pension plans and other retirement-related items for tax year 2021. Most pension limitations such as those governing 401(k) plans and IRAs changed because the increase in the Consumer Price Index met the statutory thresholds for their adjustment.

Contribution Limits	2020	2021
IRA contributions under age 50	$6,000	$6,000
IRA contributions age 50 and over	$7,000	$7,000
SIMPLE Contributions	$13,500	$13,500
SEP, Keogh Maximum Dollar Allocations	$57,000	$58,000
401(k), 403(b), Profit-Sharing Plans Elective deferrals	$19,500	$19,500
Elective catch-up contributions		
SIMPLE IRAs	$3,000	$3,000
401(k), 403(b), 457 plans	$6,500	$6,500

Table 1-12 - Pension Plan Limitations (2021)

Designated Roth Accounts - In-Plan Rollovers to Designated Roth Accounts

A plan with a designated Roth program may allow participants to transfer eligible rollover distributions to a designated Roth account from another account in the same plan. The Roth contribution program must be in place before a plan can offer in-plan Roth rollovers. A Roth program cannot be set up solely to accept in-plan rollovers - it must also accept elective deferrals from participants. Not all pre-tax plan balances can be transferred to a designated Roth account. To be eligible for an in-plan rollover, the amount must be eligible for distribution to the participant under the terms of the plan and must be otherwise eligible for rollover (an eligible rollover distribution).

The 20% mandatory withholding does not apply to an in-plan Roth direct rollover. However, if the taxpayer receives his or her distribution in cash, 20% withholding will apply even if the amount is rolled over to a designated Roth account within 60 days. (9)

Inherited IRAs Not Excludable In Bankruptcy

In Clark v. Rameker. the U.S. Supreme Court unanimously ruled that inherited IRAs do not qualify under the "retirement funds" bankruptcy exemption. As a result, non-spouses inheriting an IRA may no longer protect the funds from creditors after filing bankruptcy and spouses have more incentive to roll over inherited IRA funds. The new decision does not leave those wishing to transfer IRAs on their death without options. Spouses inheriting IRAs retain the option to roll over the inherited IRA into their own or a new IRA. If a current IRA owner wishes to leave his or her IRA to a beneficiary upon the owner's death, the best course of action is to leave the IRA to a trust for the benefit of the individual instead of directly to an individual.

Section 529 Plans

A 529 plan is a tax-advantaged savings plan designed to encourage saving for future college costs. 529 plans, legally known as "qualified tuition plans," are sponsored by states, state agencies, or educational institutions and are authorized by Section 529 of the Internal Revenue Code. The Tax Cuts and Jobs Act expanded these plans in two ways:

1. Tax-free distributions up to $10,000 can be made for tuition at elementary and secondary schools, whether public, private, or religious.
2. Rollovers of funds from 529 plans to ABLE accounts, special savings accounts for the benefit of a qualified disabled individual, can be made on a tax-free basis.

Previously, 529 plans could be used only to cover costs for college. The TCJA expands the qualified use of 529 accounts by allowing withdrawals for public, private or religious schools. Home schooling families are also allowed to use 529 funds towards educational expenses. If the taxpayer plans to take advantage of this expanded ruling, note the limit of $10,000 per year, per child. Qualified education expenses generally do not include expenses that relate to any course of instruction or other education that involves sports, games, or hobbies, or any noncredit course.

The Tax Cuts and Jobs Act (TCJA) also supports funding of ABLE accounts designed for use by people with disabilities. Under the TCJA, the taxpayer can roll over 529 plan assets to an ABLE account. Both accounts must have the same beneficiary or a member of the same family, and the taxpayer can roll over up to the annual gift exclusion amount, which is $15,000 in 2021. Now families will have more flexibility in planning for special needs, where predicting the level of future needs can be a challenge.

While not new in this tax bill, higher-income earners may want to note that 529 plan contributions are not subject to any income limits. While other tax-advantaged savings accounts like IRAs and Roth IRAs restrict higher-income families from contributing, 529 plans can be used regardless of the taxpayer's income level. With the flexibility provided by the TCJA, parents not currently setting aside money for education may want to reconsider earmarking some savings toward a 529 plan.

The Setting Every Community Up for Retirement Enhancement (SECURE) Act expanded Section 529 education savings accounts to cover costs associated with registered apprenticeships; homeschooling; up to $10,000 of qualified student loan repayments (including those for siblings); and private elementary, secondary, or religious schools as of January 1, 2020.

Review Question 3

Pamela Stevens is a 52-year-old, single taxpayer. Her annual income for 2021 is $57,600. During the year, Pamela participates in a SIMPLE IRA established by her employer. Pamela does not participate in any other employer plan during the year and catch-up contributions are permitted by the SIMPLE IRA plan. The amount Pamela contributes from her salary to her SIMPLE IRA cannot exceed what amount?

A. $10,000
B. $12,000
C. $13,500
D. $16,500

See Review Feedback for answer.

Affordable Care Act Tax Provisions for Individuals

The Tax Cuts and Jobs Act (TCJA) made significant changes to the Federal tax code. The bill does not impact the majority of the Affordable Care Act (ACA) tax provisions. However, it reduced the ACA's individual shared responsibility (or individual mandate) penalty to zero. This action effectively eliminates the individual mandate penalty for the 2019 tax year and beyond. As a result, individuals will no longer be penalized for failing to obtain acceptable health insurance coverage for themselves and their family members.

Also, despite the repeal of the individual mandate penalty, employers and individuals must continue to comply with all other ACA provisions. The tax reform bill does not impact any other ACA provisions, including the Patient-Centered Outcomes Research Institute (PCORI) fees and the health insurance providers' fee. In addition, the employer shared responsibility (pay or play) rules and related Section 6055 and Section 6056 reporting requirements are still in place.

The taxpayer may be eligible to claim the Premium Tax Credit if he or she, his or her spouse (if filing jointly), and his or her dependents enrolled in health insurance through the Health Insurance Marketplace. Advance payments of the Premium Tax Credit may have been made to a health insurer to help pay for the insurance coverage of the taxpayer, his or her spouse (if filing jointly), or his or her dependents. If advance payments of the Premium Tax Credit were made, the taxpayer must file a 2021 income tax return and Form 8962 - Premium Tax Credit (PTC).

If the taxpayer, his or her spouse (if filing jointly), or his or her dependents enrolled in health insurance through the Health Insurance Marketplace, the taxpayer should have received Form 1095-A - Health Insurance Marketplace Statement. If the taxpayer receives Form(s) 1095-A, he or she should save it. Form(s) 1095-A will help the taxpayer figure his or her Premium Tax Credit. If the taxpayer did not receive a Form 1095-A, he or she should contact the Marketplace.

Premium Tax Credit (PTC)

Since 2014, individuals and families have been able to claim the Premium Tax Credit (PTC) to help them afford health insurance coverage purchased through an Affordable Insurance Exchange. Exchanges will operate in every state and the District of Columbia. This tax credit can help make the cost of purchasing health insurance coverage more affordable for individuals and families with low to moderate incomes. Additionally, the Premium Tax Credit is refundable so taxpayers who have little or no income tax liability can still benefit. The credit also can be paid in advance to a taxpayer's insurance company to help cover the cost of premiums. In general, the taxpayer may be eligible for the credit if he or she meets all of the following: [10]

1. Purchases coverage through the Marketplace.
2. Has household income that falls within a certain range.
3. Is not able to get affordable coverage through an eligible employer plan that provides minimum value.
4. Is not eligible for coverage through a government program, like Medicaid, Medicare, CHIP or TRICARE.
5. Files a joint return, if married.
6. Cannot be claimed as a dependent by another person.

The American Rescue Plan will expand the availability of the Premium Tax Credit (PTC) to eligible individuals whose income is above 400% of the Federal Poverty Leve (FPL) for 2021 and 2022. Previously, the PTC was only available to individuals whose annual income is between 100% and 400% of the FPL (between about $12,760 and $51,040 for one person).

The Act does not change the sliding scale nature of the PTC. But, for 2021 and 2022, it reduces the premium percentage at all income levels (above 100% FPL). Those with incomes from 100% to 150% FPL are eligible for no-premium coverage (i.e., he or she contributes no income towards premiums for a silver benchmark plan). The premium contribution increases as income increases but is ultimately capped at no more than 8.5% of income for those with higher incomes (including those with income above 400% FPL). Unlike the current ACA, these levels are not indexed to increase annually, meaning the percentages (e.g., 0 percent to 8.5%) will remain the same for both 2021 and 2022.

There is no upper income limit on the PTC, meaning that all middle- and upper-income taxpayers who purchase their own coverage can access the PTC if their premiums exceed 8.5% of their overall household income.

The American Rescue Plan also creates a "special rule" regarding PTC eligibility for those who receive unemployment compensation during 2021. If a taxpayer receives (or is approved to receive) unemployment benefits during 2021, his or her income will be treated as no higher than 133% of the FPL. This means that those who receive unemployment benefits can receive maximal subsidies for ACA coverage, including no-premium coverage.

If the taxpayer is eligible for the credit, he or she can choose to either: (10)

- **Claim It Now** - have all or some of the credit paid in advance directly to his or her insurance company to lower what he or she pays out-of-pocket for his or her monthly premiums during 2021.
- **Claim It Later** - wait to get all of the credit when he or she files his or her 2021 tax return in 2022.

Note

Whether the taxpayer chooses to claim the Premium Tax Credit now at the Marketplace or claim it later, he or she must file a Federal income tax return.

To claim the credit, the taxpayer must get insurance through the Marketplace. During enrollment through the Marketplace, using information the taxpayer provides about his or her projected income and family composition for 2021, the Marketplace will estimate the amount of the Premium Tax Credit he or she will be able to claim for the 2021 tax year that he or she will file in 2022. The taxpayer will then decide whether he or she wants to have all, some or none of the estimated credit paid in advance directly to his or her insurance company.

The taxpayer should report income and family size changes to the Marketplace throughout the year. Reporting changes, increases or decreases, will help the taxpayer get the proper type and amount of financial assistance and will help him or her avoid getting too much or too little in advance. For example, if the taxpayer does not report income or family size changes to the Marketplace when they happen in 2021, the advance payments may not match his or her actual qualified credit amount on his or her Federal tax return that he or she will file in 2022. This might result in a smaller refund or balance due.

If the taxpayer chooses to claim the Premium Tax Credit now, when he or she files his or her 2021 tax return in 2022, he or she will subtract the total advance payments he or she received during the year from the amount of the Premium Tax Credit calculated on his or her tax return. If the Premium Tax Credit computed on the return is more than the advance credit paid on the taxpayer's behalf during the year, the difference will increase his or her refund or lower the amount of tax he or she owes. If the advance credit payments are more than the Premium Tax Credit, the difference will increase the amount the taxpayer owes and result in either a smaller refund or a balance due.

If the taxpayer chooses to claim the Premium Tax Credit later, he or she will claim the full amount of the Premium Tax Credit when he or she files his or her 2021 tax return in 2022. This will either increase his or her refund or lower his or her balance due. If the taxpayer's state runs its own Marketplace, he or she will use the state's website, not the Marketplace. The taxpayer should use Form 8962 - Premium Tax Credit (PTC) to figure the amount of his or her Premium Tax Credit and to reconcile any advance payments of the Premium Tax Credit. (10)

Advance Payments of the Premium Tax Credit

If the taxpayer or a family member enrolled in health insurance through the Marketplace and advance payments of the Premium Tax Credit were made to his or her insurance company to reduce his or her monthly premium payment, the taxpayer should attach Form 8962 to his or her return to reconcile (compare) the advance payments with his or her Premium Tax Credit for the year, which the taxpayer figures on Form 8962. The Marketplace is required to send Form 1095-A by January 31, 2021, listing the advance payments and other information the taxpayer needs to figure his or her Premium Tax Credit. The taxpayer should use Form 1095-A to complete Form 8962. Also, the taxpayer should attach Form 8962 to his or her return. The taxpayer does not attach Form 1095-A to the income tax return.

Health Coverage Tax Credit (HCTC)

The Health Coverage Tax Credit (HCTC) was extended one year as part of the Consolidated Appropriations Act, 2021 and will expire on December 31, 2021. This means that all advanced payments of the HCTC end on December 31, 2021. However, eligible taxpayers who did not request advance monthly payments in 2021 and instead paid 100% of their health insurance premiums can claim the HCTC when they file their 2021 Federal income tax return in 2022. The refundable HCTC is equal to 72.5% of the premiums paid by certain individuals for coverage of the individual and qualifying family members under qualified health insurance. The taxpayer should use Form 8885 - Health Coverage Tax Credit to elect and figure the amount, if any, of his or her HCTC.

Net Investment Income Tax

The Net Investment Income Tax is imposed by Section 1411 of the Internal Revenue Code (IRC) that took effect on January 1, 2013. The NIIT applies at a rate of 3.8% to certain net investment income of individuals, estates and trusts that have income above the statutory threshold amounts. In general, investment income includes, but is not limited to interest, dividends, capital gains, rental and royalty income, non-qualified annuities, taxable mutual fund distributions, income from businesses involved in trading of financial instruments or commodities, and businesses that are passive activities to the taxpayer.

Tip

The amount subject to the 3.8% tax is the lesser of the taxpayer's net investment income or the amount by which modified adjusted gross (MAGI) exceeds the applicable threshold. Individuals will owe the tax if they have Net Investment Income and also have modified adjusted gross income over the following thresholds: (11)

Filing Status	Threshold Amount*
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$250,000
*Taxpayers should be aware that these threshold amounts are not indexed for inflation. These amounts will stay the same from year to year unless Congress specifically changes these amounts through new legislation.	

Table 1-13 - IRS.GOV Net Investment Income Tax FAQs (2021)

Note

If an individual is exempt from Medicare taxes, he or she still may be subject to the Net Investment Income Tax if he or she has Net Investment Income and also has modified adjusted gross income over the applicable thresholds.

Nonresident Aliens (NRAs) are not subject to the Net Investment Income Tax. If an NRA is married to a U.S. citizen or resident and has made, or is planning to make, an election under IRC Section 6013(g) to be treated as a resident alien for purposes of filing as Married Filing Jointly, the proposed regulations provide these couples special rules and a corresponding IRC Section 6013(g) election for the NIIT.

Estates and Trusts will be subject to the Net Investment Income Tax if they have undistributed Net Investment Income and also have adjusted gross income over the dollar amount at which the highest tax bracket for an estate or trust begins for such taxable year. Generally, the threshold amount for the upcoming year is updated by the IRS each fall in a revenue procedure. For tax year 2021, the threshold amount is $13,050. The taxpayer should be aware that there are special computational rules for certain unique types of trusts, such as Charitable Remainder Trusts and Electing Small Business Trusts. The following trusts are not subject to the Net Investment Income Tax:

1. Trusts that are exempt from income taxes imposed by Subtitle A of the Internal Revenue Code (e.g., charitable trusts and qualified retirement plan trusts exempt from tax under IRC Section 501, and Charitable Remainder Trusts exempt from tax under IRC Section 664).
2. A trust in which all of the unexpired interests are devoted to one or more of the purposes described in IRC Section 170(c)(2)(B).
3. Trusts that are classified as grantor trusts under IRC Sections 671-679.
4. Trusts that are not classified as trusts for Federal income tax purposes (e.g., Real Estate Investment Trusts and Common Trust Funds).

In general, investment income includes, but is not limited to: interest, dividends, capital gains, rental and royalty income, non-qualified annuities, income from businesses involved in trading of financial instruments or commodities, and businesses that are passive activities to the taxpayer (within the meaning of IRC Section 469).

To the extent that gains are not otherwise offset by capital losses, the following gains are common examples of items taken into account in computing Net Investment Income:

- Gains from the sale of stocks, bonds, and mutual funds.
- Capital gain distributions from mutual funds.
- Gain from the sale of investment real estate (including gain from the sale of a second home that is not a primary residence).
- Gains from the sale of interests in partnerships and S corporations (to the extent the taxpayer was a passive owner).

The Net Investment Income Tax will not be applicable to any amount of gain that is excluded from gross income for regular income tax purposes. The pre-existing statutory exclusion in IRC Section 121 exempts the first $250,000 ($500,000 in the case of a married couple) of gain recognized on the sale of a principal residence from gross income for regular income tax purposes and, therefore, from the NIIT.

Wages, unemployment compensation; operating income from a non-passive business, Social Security Benefits, alimony, tax-exempt interest, self-employment income, Alaska Permanent Fund Dividends and distributions from certain Qualified Plans are some common types of income that are not investment income.

In order to arrive at Net Investment Income, Gross Investment Income is reduced by deductions that are properly allocable to items of Gross Investment Income. Examples of properly allocable deductions include investment interest expense, investment advisory and brokerage fees, expenses related to rental and royalty income, and state and local income taxes properly allocable to items included in Net Investment Income.

Taxpayers will determine any applicable NIIT on the new Form 8960 - Net Investment Income Tax - Individuals, Estates and Trusts, when they file their income tax return. Taxpayers whose AGI may exceed the threshold amounts and who have investment income may need to adjust their withholding or make estimated tax payments to ensure the new tax on investment income does not prompt a balance due when filing taxes next year.

Additional Medicare Tax

Effective January 2013, Additional Medicare Tax applies to an individual's Medicare wages that surpass a threshold amount based on the taxpayer's filing status. All wages that are currently subject to Medicare Tax are subject to Additional Medicare Tax if they are paid in excess of the applicable threshold for an individual's filing status. Employers are responsible for withholding the 0.9% Additional Medicare Tax on an individual's wages paid in excess of $200,000 in a calendar year. An employer is obligated to begin withholding Additional Medicare Tax in the pay period in which it pays wages in excess of $200,000 to an employee. There is no employer match for Additional Medicare Tax.

An individual is responsible for Additional Medicare Tax if the individual's wages, compensation, or self-employment income (together with that of his or her spouse if filing a joint return) surpass the threshold amount for the individual's filing status.

Filing Status	Threshold Amount
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$200,000

Table 1-14 - Questions and Answers for the Additional Medicare Tax (2021)

The Additional Medicare Tax statute mandates an employer to withhold Additional Medicare Tax on wages it pays to an employee in excess of $200,000 in a calendar year. An employer has this withholding obligation even though an employee may not be liable for Additional Medicare Tax because, for example, the employee's wages together with that of his or her spouse do not exceed the $250,000 threshold for joint return filers. Any withheld Additional Medicare Tax will be credited against the total tax liability shown on the individual's income tax return (Form 1040).

An employee who foresees liability for Additional Medicare Tax may ask that his or her employer withhold an additional amount of income tax withholding on Form W-4 - Employee's Withholding Certificate. This additional income tax withholding will be applied against all taxes shown on the individual's income tax return (Form 1040), including any Additional Medicare Tax liability.

Compensation subject to RRTA taxes and wages subject to FICA tax are not combined to determine Additional Medicare Tax liability. The threshold applicable to an individual's filing status is applied separately to each of these categories of income.

Review Question 4
In general, all of the following are included in net investment income except:
A. Interest
B. Dividends
C. Social Security benefits
D. Capital gains

See Review Feedback for answer.

Changes to Itemized Deduction for Medical Expenses

The Consolidated Appropriations Act, 2021 makes permanent the lower threshold of 7.5% for all taxpayers, which means the taxpayer can only deduct those expenses which exceed 7.5% of his or her adjusted gross income (AGI).

Medical Device Excise Tax

The Further Consolidated Appropriations Act, 2020 included the repeal of the excise tax on medical devices. The repeal of the excise tax on medical devices began January 1, 2020.

Cadillac Tax

The Further Consolidated Appropriations Act, 2020 included the repeal of the so-called "Cadillac" tax on health insurance benefits. The repeal of the Cadillac tax began January 1, 2020.

Affordable Care Act Tax Provisions Employers

The Affordable Care Act (ACA), or health care law, includes many tax and other provisions for employers. The IRS will administer the tax provisions included in the law.

Small Business Health Care Tax Credit

The Small Business Health Care Tax Credit helps small businesses and small tax-exempt organizations afford the cost of covering their employees and is specifically targeted for those with low- and moderate-income workers. The credit is designed to encourage small employers to provide health insurance coverage for the first time or maintain coverage they already have. In general, the credit is available to small employers that pay at least half the cost of single coverage for their employees. For taxable years beginning in 2014 and forward:

- The maximum credit is 50% of the employer's premium payments made on behalf of its employees under a qualifying arrangement for a Qualified Health Plan (QHP) offered through a Small Business Health Options Program (SHOP) Marketplace.
- The maximum credit is 35% of the tax-exempt employer's premium payments made on behalf of its employees under a qualifying arrangement for a QHP offered through a SHOP Marketplace.
- To be eligible for the credit, a small employer must pay premiums on behalf of employees enrolled in a qualified health plan provided through the SHOP Marketplace.
- The credit will be available to eligible employers for two consecutive taxable years.

To be eligible, the small business must cover at least 50% of the cost of single (not family) health care coverage for each of the employees. The business must also have fewer than 25 full-time equivalent employees (FTEs). Those employees must have average wages of less than certain thresholds (as adjusted for inflation) per year.

Also, the credit provides that the maximum credit is phased out based on the employer's number of full-time equivalent employees in excess of 10 and the employer's average annual wages in excess of annual thresholds.

The small business taxpayer must use Form 8941 - Credit for Small Employer Health Insurance Premiums, to calculate the credit. A small business can include the amount as part of the general business credit on the income tax return. If the business is a tax-exempt organization, include the amount on line 51f of the Form 990-T - Exempt Organization Business Income Tax Return. The business must file the Form 990-T in order to claim the credit, even if they do not ordinarily do so.

Tip

A small business employer may be able to carry the credit back or forward. A tax-exempt employer may be eligible for a refundable credit.

Employer Shared Responsibility Provisions

For 2016 and after, employers employing at least a certain number of employees (generally 50 full-time employees or a combination of full-time and part-time employees that is equivalent to 50 full-time employees) will be subject to the Employer Shared Responsibility provisions under Section 4980H of the Internal Revenue Code (added to the Code by the Affordable Care Act). As defined by the statute, a full-time employee is an individual employed on average at least 30 hours of service per week. An employer that meets the 50-full-time employee threshold is referred to as an applicable large employer (ALE).

Under the Employer Shared Responsibility provisions, if these employers do not offer affordable health coverage that provides a minimum level of coverage to their full-time employees (and their dependents), the employer may be subject to an Employer Shared Responsibility payment if at least one of its full-time employees receives a Premium Tax Credit for purchasing individual coverage on one of the new Affordable Insurance Exchanges, also called a Health Insurance Marketplace (Marketplace). Mid-size employers (i.e., employers with between 50 and 99 full-time employees and full-time equivalent employees) are not required to comply with the Employer Shared Responsibility provisions until the first day of the employer's 2021 plan year.

Large Employer Health Coverage Excise Tax

Large employers, generally those with 50 or more full-time employees in the prior calendar year, that (1) do not offer coverage for all its full-time employees, (2) offer minimum essential coverage that is unaffordable (employee contribution is more than 9.5% of the employee's household income) or (3) offer minimum essential coverage where the plan's share of the total allowed cost of benefits is less than 60% will be required to pay a penalty if any of its full-time employees were certified to the employer as having purchased health insurance through a state exchange and qualified for either tax credits or a cost-sharing subsidy.

Individual reporting requires health insurers and employers sponsoring self-funded group health plans to annually report to the IRS and responsible individuals (i.e., the enrolled employees and other primary insureds) whether the group health plan coverage constitutes minimum essential coverage under Health Care Reform. This reporting requirement will assist the IRS to enforce the individual mandate penalty.

Form 1095-B - Health Coverage is used to complete the individual mandate reporting requirement with respect to responsible individuals and the IRS. Information to be provided includes the responsible individual's name, address and Social Security number. Identifying information concerning the employer-plan sponsor and issuer-coverage provider must be supplied, along with a list of the responsible individual's enrolled family members and the months during the year when they had coverage.

When submitting Form 1095-B to the IRS, the reporting entity must also submit IRS Form 1094-B - Transmittal of Health Coverage Information Returns. Form 1094-B is a "transmittal" form that provides information about the reporting entity and the number of Form 1095-B submitted.

Applicable Large Employers (ALE) with 50 or more full-time and full-time equivalent employees are required to report to the IRS and full-time employees for two purposes:

1. To assist the IRS to enforce the Employer Shared Responsibility provisions.
2. To assist full-time employees to determine their eligibility for the Premium Tax Credit.

Applicable Large Employers (ALE) should use IRS Form 1095-C - Employer-Provided Health Insurance Offer and Coverage to complete the reporting requirement with respect to full-time employees and the IRS.

Similar to the individual mandate reporting requirement, when submitting Form 1095-C to the IRS, large employers must also submit Form 1094-C - Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns. Form 1094-C is also a "transmittal" form that provides the IRS with a summary of the information contained in Form 1095-C. If an employer is part of a "controlled group" of commonly owned entities, information regarding the other employers must be included.

Same-Sex Married Couples

The U.S. Department of the Treasury and the Internal Revenue Service (IRS) ruled that same-sex couples, legally married in jurisdictions that recognize their marriages, will be treated as married for Federal tax purposes. The ruling applies regardless of whether the couple lives in a jurisdiction that recognizes same-sex marriage or a jurisdiction that does not recognize same-sex marriage. The ruling implements Federal tax aspects of the June 26 Supreme Court Obergefell v. Hodges decision invalidating a key provision of the 1996 Defense of Marriage Act.

Under the ruling, same-sex couples will be treated as married for all Federal tax purposes, including income and gift and estate taxes. The ruling applies to all Federal tax provisions where marriage is a factor, including filing status, the standard deduction, employee benefits, contributing to an IRA and the Earned Income Tax Credit or Child Tax Credit.

Note

Any same-sex marriage legally entered into in one of the 50 states, the District of Columbia, a U.S. territory or a foreign country will be covered by the ruling. However, the ruling does not apply to registered domestic partnerships, civil unions or similar formal relationships recognized under state law. Also, A taxpayer's same-sex spouse cannot be a dependent of the taxpayer.

A same-sex spouse cannot file using head of household filing status. However, a married taxpayer may be considered unmarried and may use the head of household filing status if the taxpayer lives apart from his or her spouse for the last 6 months of the taxable year and provides more than half the cost of maintaining a household that is the principal place of abode of the taxpayer's dependent child for more than half of the year. Also, if a taxpayer's spouse itemized his or her deductions, the taxpayer cannot claim the standard deduction. Additionally, employees who purchased same-sex spouse health insurance coverage from their employers on an after-tax basis may treat the amounts paid for that coverage as pre-tax and excludable from income. [12]

Individuals who were in same-sex marriages may, but are not required to, file original or amended returns choosing to be treated as married for Federal tax purposes for one or more prior tax years still open under the statute of limitations. Taxpayers who wish to file a refund claim for income taxes should use Form 1040X - Amended U.S. Individual Income Tax Return. Taxpayers who wish to file a refund claim for gift or estate taxes should file Form 843 - Claim for Refund and Request for Abatement.

Note

A taxpayer usually may file a claim for refund for three years from the date the return was filed or two years from the date the tax was paid, whichever is later. Also, some taxpayers may have special circumstances, such as signing an agreement with the IRS to keep the statute of limitations open, that permit them to file refund claims for earlier tax years.

Other 2021 Tax Update Information

Miscellaneous Deductions

Under the Tax Cuts and Jobs Act miscellaneous deductions which exceed 2% of the taxpayer's adjusted gross income (AGI) will be eliminated. This provision includes deductions for unreimbursed employee expenses and tax preparation expenses. Additionally, this provision includes expenses that the taxpayer incurs in his or her job that are not reimbursed, such as tools and supplies, required uniforms not suitable for ordinary wear, dues and subscriptions, and job search expenses. These expenses also include unreimbursed travel and mileage, as well as the home office deduction.

Note

The elimination of unreimbursed employee expenses only affects taxpayers who claim an employee-related deduction on Schedule A. If, as a business owner, the taxpayer typically files a Schedule C, his or her business-related deductions are not affected by the elimination of Schedule A deductions.

Qualified Business Income (QBI) Deduction - Section 199A

Most American businesses are organized as "pass-through" companies in which the income from the business is "passed through" to the business owner's individual tax return. S corporations, LLCs, partnerships and sole proprietorships are all examples of pass-through businesses. Under the Tax Cuts and Jobs Act these entities will be taxed at their individual tax rates less a 20% deduction for qualified business income (QBI), subject to certain wage limits and exceptions. Qualified business income includes domestic income from a trade or business. Employee wages, capital gain, interest and dividend income are excluded. The new deduction, referred to as the Section 199A deduction or the deduction for qualified business income, is available for tax years beginning after December 31, 2017.

The deduction is generally available to eligible taxpayers whose 2021 taxable incomes fall below $329,800 for joint returns, $164,925 for married filing separately, and $164,900 for all other taxpayers. It is generally equal to the lesser of 20% of their qualified business income plus 20% of their qualified real estate investment trust dividends and qualified publicly traded partnership income or 20% of taxable income minus net capital gains.

A single taxpayer should use Form 8995 - Qualified Business Income (QBI) Deduction Simplified Computation to figure his or her qualified business income (QBI) deduction if his or her taxable income before the QBI deduction is less than or equal to $164,900 ($329,800 for joint filers). Individual taxpayers and some trusts and estates may be entitled to a deduction up to 20% of their net QBI from a trade or business, including income from a pass-through entity, but not from a C corporation, plus 20% of qualified real estate investment trust (REIT) dividends and qualified publicly trade partnership (PTP) income. However, the taxpayer's total QBI deduction is limited to 20% of his or her taxable income, calculated before the QBI deduction, minus net capital gain.

The taxpayer should use Form 8995-A - Qualified Business Income Deduction to figure his or her qualified business income (QBI) deduction. He or she includes the following schedules as appropriate:

- Schedule A (Form 8995-A), Specified Service Trades or Businesses (SSTB).
- Schedule B (Form 8995-A), Aggregation of Business Operations.
- Schedule C (Form 8995-A), Loss Netting and Carryforward.
- Schedule D (Form 8995-A), Special Rules for Patrons of Agricultural or Horticultural Cooperatives.

Depending on the taxpayer's taxable income, his or her QBI component may also be limited based on the type of trade or business, W-2 wages paid by that business, and unadjusted basis immediately after acquisition (UBIA) of qualified property held by the business.

The deduction would be disallowed for businesses offering "professional services", such as law firms, doctor's offices and investment offices, above certain threshold amounts. The W-2 wage limit does not apply in the case of a taxpayer with taxable income not exceeding $329,800 for married individuals filing jointly ($164,900 for single, head of household and married filing separately). The application of the W-2 wage limit is phased in for individuals with taxable income exceeding these thresholds, over the next $100,000 of taxable income for married individuals filing jointly ($50,000 for other individuals).

Note

The 20% deduction is not allowed in computing adjusted gross income (AGI), but rather is allowed as a deduction reducing taxable income.

Social Security and Medicare Tax

The employee tax rate for Social Security in 2021 is 6.2%. The employer tax rate for Social Security remains unchanged at 6.2%. The Social Security wage base limit rises to $142,800 for 2021. The new wage base translates into a maximum of $8,853.60 withheld from a highly paid employee's 2021 paychecks. The Medicare tax rate is 1.45% each for the employee and employer, unchanged since 2012. There is no wage base limit for Medicare tax. If the taxpayer's only income is from self-employment, the Social Security maximum is still in effect. That is, the Social Security portion of his or her self-employment tax is capped at the maximum profit of the company, depending on the maximum for that year. For 2021, the self-employment tax rate on net earnings is 15.3% (12.4% Social Security tax plus 2.9% Medicare tax). (13)

Review Question 5
Royce is self-employed and the net earnings on his Schedule C are $158,000 for 2021. The Social Security tax portion of his self-employment tax would be based on which amount of his self-employment earnings?

A. $0
B. $66,000
C. $142,800
D. $158,000

See Review Feedback for answer.

Tax for Certain Children Who Have Unearned Income (Kiddie Tax)

The Tax Cuts and Jobs Act changed the Kiddie Tax, which taxes a child's unearned income at the tax rates of the child's parents. Starting in 2018, however, the Kiddie Tax was based on the much higher tax rates for estates and trusts. This significantly increased the tax rates that apply to the taxable portion of college grants, scholarships and fellowships and to military survivor benefits of Gold Star families. It also caused low- and middle-income children to be taxed at much higher rates than their parents.

The Setting Every Community Up for Retirement Enhancement (SECURE) Act repeals the change to the Kiddie Tax, reverting to the rules that were in effect before 2018. This change is effective for tax years that begin after December 31, 2019. However, the legislation allows taxpayers to elect to have the change apply retroactively to the 2018 and/or 2019 tax years. Taxpayers will probably have to file amended Federal income tax returns to claim a refund of the excess tax.

Kiddie Tax	
Tax Bracket	**Tax**
$0 to $1,100	0%
Earned income > $1,100	Child's tax rate
Unearned income > $1,100 ≤ $2,200	Child's tax rate
Unearned income > $2,200	Generally, the parent's highest marginal tax rate

Table 1-15 - Publication 929 - Tax for Certain Children Who Have Unearned Income (2021)

The exemption from the Kiddie Tax for 2021 will be $2,200. The first $1,100 of a child's unearned income is tax-free, and the next $1,100 is subject to the child's tax rate. Any additional earnings above $2,200 are taxed at the child's parents' marginal tax rate. Families who have unearned income that is subject to the Kiddie Tax must file IRS Form 8615 with their Federal tax return. A separate tax return must be filed for children who have unearned income that is greater than $11,000 or any amount of earned income. If a child's unearned income is less than $11,000 and greater than $1,100, the child's unearned income can be included on their parents' income tax return.

Form 8615 - Tax for Certain Children Who Have Unearned Income must be filed for anyone who meets all of the following conditions: (14)

1. The taxpayer had more than $2,200 of unearned income.
2. The taxpayer is required to file a tax return.
3. The taxpayer was either:
   a. Under age 18 at the end of 2021,
   b. Age 18 at the end of 2021 and did not have earned income that was more than half of his or her support, or
   c. A full-time student at least age 19 and under age 24 at the end of 2021 and did not have earned income that was more than half of his or her support.
4. At least one of the taxpayer's parents was alive at the end of 2021.
5. The taxpayer did not file a joint return for 2021.

These rules apply if the taxpayer was legally adopted and a stepchild. These rules also apply whether or not the taxpayer is a dependent. These rules do not apply if neither of taxpayer's parents were living at the end of the year.

Qualified Long-Term Care Insurance Premiums

The amount of qualified long-term care insurance premiums a taxpayer can include is limited. He or she can include the following as medical expenses on Schedule A (Form 1040) as determined by age (as of the close of the tax year) of the taxpayer:

Age Group	2021 Eligible Premium Amount
Age 40 and under	$450
Ages 41 through 50	$850
Ages 51 through 60	$1,690
Ages 61 through 70	$4,520
Age 71 and over	$5,640
Note: The limit on premiums is for each person.	

Table 1-16 - Publication 502 - Medical and Dental Expenses (2021)

For 2021, the stated dollar amount of the per diem limitation regarding periodic payments received under a qualified long-term care insurance contract or periodic payments received under a life insurance contract that are treated as paid by reason of the death of a chronically ill individual is $400.

Series EE and I Savings Bonds Income Exclusion

For 2021, the exclusion under IRC Section 135, regarding income from United States Series EE and I Savings Bonds for taxpayers who pay qualified higher education expenses, begins to phase out for modified adjusted gross income (MAGI) above $124,800 for joint returns and $83,200 for all other returns. The exclusion phases out completely at AGI levels of $154,800 for joint returns and $98,200 for other returns.

Rates on Long-Term Gains and Dividends

Under the Tax Cuts and Jobs Act the 15% and 20% tax rates on long-term capital gains and qualified dividends have been retained. Those in the 10% or 12% tax bracket pay zero tax on these gains and dividends. Also, there had been proposals to require the use of first-in, first-out (FIFO) in determining basis on the sale of stock and mutual fund shares rather than allowing investors to designate which shares are being sold when shares were acquired at different times. This measure was not included in the final law.

For 2021, the rate brackets for capital gains are as follows:

Filing Status	Single	Joint	Head of Household	Estate or Trust
0% Tax Bracket	$0 - $40,400	$0 - $80,800	$0 - $54,100	$0 - $2,700
Beginning of 15% Bracket	$40,401	$80,801	$54,101	$2,701
Beginning of 20% Bracket	$445,851	$501,601	$473,751	$13,251

Table 1-17 - Revenue Procedure 2020-45 (2021)

Transportation Fringe Benefits

An employer can exclude the value of any de minimis transportation benefit he or she provides to an employee from the employee's wages. A de minimis transportation benefit is any local transportation benefit the employer provides to an employee if it has so little value (taking into account how frequently the employer provides transportation to his or her employees) that accounting for it would be unreasonable or administratively impracticable. For example, it applies to occasional transportation fare an employer gives an employee because the employee is working overtime if the benefit is reasonable and is not based on hours worked.

This exclusion applies to the following benefits: (15)

- A ride in a commuter highway vehicle between the employee's home and workplace.
- A transit pass.
- Qualified parking.

The exclusion applies whether the employer provides only one or a combination of these benefits to his or her employees.

An employer can generally exclude the value of transportation benefits that he or she provides to an employee during 2021 from the employee's wages up to the following limits: (15)

- $270 per month for combined commuter highway vehicle transportation and transit passes.
- $270 per month for qualified parking.

If the value of a benefit for any month is more than its limit, the employer must include in the employee's wages the amount over the limit minus any amount the employee paid for the benefit. The employer cannot exclude the excess from the employee's wages as a de minimis transportation benefit.

The Tax Cuts and Jobs Act included the suspension of the Qualified Bicycle Commuting Reimbursement Exclusion beginning after December 31, 2017, and before January 1, 2026.

The Further Consolidated Appropriations Act, 2020 repeals the Section 512(a)(7) provision which had resulted in a tax on employer-provided parking for nonprofit organizations. Under the TCJA provision, employee parking for nonprofits, including churches, had been subject to a 21% unrelated business income tax (UBIT), however, this is no longer the case.

Foreign Earned Income Exclusion

If the taxpayer is a U.S. citizen or a resident alien of the United States and he or she lives abroad, the taxpayer is taxed on his or her worldwide income. However, the taxpayer may qualify to exclude from income up to an amount of his or her foreign earnings that is adjusted annually for inflation. The foreign earned income exclusion rises to $108,700 for tax year 2021, up from $107,600 for 2020.

In addition to the foreign earned income exclusion, the taxpayer can also claim an exclusion or a deduction from gross income for his or her housing amount if his or her tax home is in a foreign country and he or she qualifies for the exclusions and deduction under either the bona fide residence test or the physical presence test.

The housing exclusion applies only to amounts considered paid for with employer-provided amounts, which includes any amounts paid to the taxpayer or paid or incurred on his or her behalf by his or her employer that are taxable foreign earned income to the taxpayer for the year (without regard to the foreign earned income exclusion). The housing deduction applies only to amounts paid for with self-employment earnings.

The taxpayer's housing amount is the total of his or her housing expenses for the year minus the base housing amount. The computation of the base housing amount (line 32 of Form 2555) is tied to the maximum foreign earned income exclusion. The amount is 16% of the maximum exclusion amount (computed on a daily basis) multiplied by the number of days in the taxpayer's qualifying period that fall within his or her tax year. The base amount for 2021 is $17,392 or $47.65 per day.

To claim the foreign earned income exclusion, the foreign housing exclusion, or the foreign housing deduction, the taxpayer must meet all three of the following requirements.

1. His or her tax home must be in a foreign country.
2. He or she must have foreign earned income.
3. He or she must be either:
    a. A U.S. citizen who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year, or

b. A U.S. resident alien who is a citizen or national of a country with which the United States has an income tax treaty in effect and who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year, or
c. A U.S. citizen or a U.S. resident alien who is physically present in a foreign country or countries for at least 330 full days during any period of 12 consecutive months.

Note

The taxpayer does not automatically acquire bona fide resident status merely by living in a foreign country or countries for 1 year. Also, the taxpayer cannot exclude income he or she receives after the end of the year following the year, he or she does the work to earn it.

Expatriate Health Plans

On June 10, 2016, the Treasury Department and Internal Revenue Service, the Department of Health and Human Services, and the Department of Labor (the Departments) issued proposed regulations that implement the Expatriate Health Coverage Clarification Act of 2014 (EHCCA). The EHCCA generally provides that most ACA provisions do not apply to expatriate health plans covering individuals traveling to or from the United States. More specifically, the EHCCA provides that the requirements of the ACA do not apply to expatriate health plans, expatriate health insurance issuers for coverage under expatriate health plans, and employers in their capacity as plan sponsors of expatriate health plans, except that: (10)

1. An expatriate health plan shall be treated as minimum essential coverage under Section 5000A(f) of the Code and any other section of the Code that incorporates the definition of minimum essential coverage.
2. The employer shared responsibility provisions of Section 4980H of the Code continue to apply.
3. The health care reporting provisions of Sections 6055 and 6056 of the Code continue to apply but with certain modifications relating to the use of electronic media for required statements to enrollees.
4. The excise tax provisions of Section 4980I of the Code continue to apply with respect to coverage of certain qualified expatriates who are assigned (rather than transferred) to work in the United States.
5. The annual health insurance providers fee imposed by Section 9010 of the ACA takes into account expatriate health insurance issuers for certain purposes for calendar years 2014 and 2015 only.

The EHCCA proposed regulations provide that the market reform provisions enacted as part of the ACA generally do not apply to expatriate health plans, any employer solely in its capacity as a plan sponsor of an expatriate health plan, and any expatriate health insurance issuer with respect to coverage under an expatriate health plan. Further, the EHCCA proposed regulations define the benefit and administrative requirements for expatriate health issuers, expatriate health plans, and qualified expatriates, and provide clarification regarding the applicability of certain fee and reporting requirements.

Direct Deposit Limits

In an effort to combat fraud and identity theft, IRS procedures that took effect January 2015 limited the number of refunds electronically deposited into a single financial account or pre-paid debit card to three. The fourth and subsequent refunds automatically will convert to a paper refund check and be mailed to the taxpayer. Taxpayers also will receive a notice informing them that the account has exceeded the direct deposit limits and that they will receive a paper refund check in approximately four weeks if there are no other issues with the return.

The vast majority of taxpayers will not be affected by this limitation, and the IRS would encourage taxpayers and tax preparers to continue to use direct deposit. It is the fastest, safest way for taxpayers to receive refunds. The direct deposit limit is intended to prevent criminals from easily obtaining multiple refunds. The limit applies to financial accounts, such as bank savings or checking accounts, and to prepaid, reloadable cards or debit cards.

Virtual Currency

In some environments, virtual currency (such as Bitcoin) operates like “real” currency (i.e., the coin and paper money of the United States or of any other country that is designated as legal tender, circulates, and is customarily used and accepted as a medium of exchange in the country of issuance) but it does not have legal tender status in any jurisdiction. For Federal tax purposes, virtual currency is treated as property. General tax principles applicable to property transactions apply to transactions using virtual currency. A taxpayer who receives virtual currency as payment for goods or services must, in computing gross income, include the fair market value of the virtual currency, measured in U.S. dollars, as of the date that the virtual currency was received.

This also means that:

- Wages paid to employees using virtual currency are taxable to the employee, must be reported by an employer on a Form W-2, and are subject to Federal income tax withholding and payroll taxes.
- Payments using virtual currency made to independent contractors and other service providers are taxable and self-employment tax rules generally apply. Normally, payers must issue Form 1099.
- The character of gain or loss from the sale or exchange of virtual currency depends on whether the virtual currency is a capital asset in the hands of the taxpayer.
- A payment made using virtual currency is subject to information reporting to the same extent as any other payment made in property.

If the fair market value of property received in exchange for virtual currency exceeds the taxpayer's adjusted basis of the virtual currency, the taxpayer has taxable gain. The taxpayer has a loss if the fair market value of the property received is less than the adjusted basis of the virtual currency.

The IRS issued additional detailed guidance to help taxpayers better understand their reporting obligations for specific transactions involving virtual currency. The guidance included Revenue Ruling 2019-24 established the following rules that cryptocurrency is a type of virtual currency that utilizes cryptography to secure transactions that are digitally recorded on a distributed ledger, such as a blockchain. Units of cryptocurrency are generally referred to as coins or tokens. Distributed ledger technology uses independent digital systems to record, share, and synchronize transactions, the details of which are recorded in multiple places at the same time with no central data store or administration functionality.

A hard fork is unique to distributed ledger technology and occurs when a cryptocurrency on a distributed ledger undergoes a protocol change resulting in a permanent diversion from the legacy or existing distributed ledger. A hard fork may result in the creation of a new cryptocurrency on a new distributed ledger in addition to the legacy cryptocurrency on the legacy distributed ledger. Following a hard fork, transactions involving the new cryptocurrency are recorded on the new distributed ledger and transactions involving the legacy cryptocurrency continue to be recorded on the legacy distributed ledger.

An airdrop is a means of distributing units of a cryptocurrency to the distributed ledger addresses of multiple taxpayers. A hard fork followed by an airdrop results in the distribution of units of the new cryptocurrency to addresses containing the legacy cryptocurrency. However, a hard fork is not always followed by an airdrop.

Cryptocurrency from an airdrop generally is received on the date and at the time it is recorded on the distributed ledger. However, a taxpayer may constructively receive cryptocurrency prior to the airdrop being recorded on the distributed ledger. A taxpayer does not have receipt of cryptocurrency when the airdrop is recorded on the distributed ledger if the taxpayer is not able to exercise dominion and control over the cryptocurrency. For example, a taxpayer does not have dominion and control if the address to which the cryptocurrency is airdropped is contained in a wallet managed through a cryptocurrency exchange and the cryptocurrency exchange does not support the newly created cryptocurrency such that the airdropped cryptocurrency is not immediately credited to the taxpayer's account at the cryptocurrency exchange. If the taxpayer later acquires the ability to transfer, sell, exchange, or otherwise dispose of the cryptocurrency, the taxpayer is treated as receiving the cryptocurrency at that time.

For example, if the taxpayer owns 100 units of Crypto A. Crypto A experiences a hard fork and Crypto B is created. 50 units of Crypto B are airdropped to the taxpayer. The taxpayer must report ordinary income equal to the fair market value of Crypto B. [16]

The IRS announced another compliance measure for taxpayers who engage in transactions involving virtual currency: a checkbox on Form 1040. The checkbox is at the top of Schedule 1, which is used for reporting income or adjustments to income that cannot be entered directly on the front page of Form 1040.

Report of Foreign Bank and Financial Accounts (FBAR)

The Financial Crimes Enforcement Network (FinCEN) distributed a rule that amends the Bank Secrecy Act (BSA) implementing regulations regarding the Report of Foreign Bank and Financial Accounts (FBAR). The FBAR form is utilized to report a financial interest in, or signature or other authority over, one or more financial accounts in foreign countries. A report is not mandatory if the aggregate value of the accounts does not exceed $10,000. Therefore, if a

U.S. person who has a financial interest in or signature authority over a foreign financial account, including a bank account, brokerage account, mutual fund, trust, or other type of foreign financial account that exceeds $10,000 at any time during the calendar year, the Bank Secrecy Act may require him or her to report the account yearly to the Internal Revenue Service by filing a Report of Foreign Bank and Financial Accounts (FBAR). FBARs must be electronically filed through the Bank Secrecy Act (BSA) E-Filing System using the electronic FinCEN Form 114 - Report of Foreign Bank and Financial Accounts (FBAR), which supersedes the now-obsolete paper Treasury Department Form 90-22.1.

As of December 31, 2015, the due date of FinCEN Report 114 (relating to Report of Foreign Bank and Financial Accounts) is April 15 with a maximum extension for a 6-month period ending on October 15 and with provision for an extension under rules similar to the rules in Treasury Regulation Section 1.6081–5. For any taxpayer required to file such Form for the first time, any penalty for failure to timely request for, or file, an extension, may be waived by the Secretary. United States persons are required to file an FBAR if both of the following apply: (17)

1. The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States.
2. The aggregate value of all foreign financial accounts exceeded $10,000 at any time during the calendar year to be reported.

United States person includes U.S. citizens; U.S. residents; entities, including but not limited to, corporations, partnerships, or limited liability companies, created or organized in the United States or under the laws of the United States; and trusts or estates formed under the laws of the United States.

The Federal tax treatment of an entity does not determine whether the entity has an FBAR filing requirement. For example, an entity that is disregarded for purposes of Title 26 of the United States Code must file an FBAR, if otherwise required to do so. Similarly, a trust for which the trust income, deductions, or credits are taken into account by another person for purposes of Title 26 of the United States Code must file an FBAR, if otherwise required to do so.

A financial account contains, but is not limited to, securities, brokerage, savings, demand, checking, deposit, time deposit, or other account maintained with a financial institution (or other person performing the services of a financial institution). A financial account also is comprised of commodity futures or options account, an insurance policy with a cash value (such as a whole life insurance policy), an annuity policy with a cash value, and shares in a mutual fund or similarly pooled fund (i.e., a fund that is available to the general public with a regular net asset value determination and regular redemptions).

A foreign financial account is a financial account located outside of the United States. For example, an account maintained with a branch of a United States bank that is physically located outside of the United States is a foreign financial account. An account maintained with a branch of a foreign bank that is physically located in the United States is not a foreign financial account. Exceptions to the FBAR reporting requirements are located in the FBAR instructions.

There are filing exceptions for the following United States persons or foreign financial accounts: (17)

- Certain foreign financial accounts jointly owned by spouses.
- United States persons included in a consolidated FBAR.
- Correspondent/nostro accounts.
- Foreign financial accounts owned by a governmental entity.
- Foreign financial accounts owned by an international financial institution.
- IRA owners and beneficiaries.
- Participants in and beneficiaries of tax-qualified retirement plans.
- Certain individuals with signature authority over but no financial interest in a foreign financial account.
- Trust beneficiaries (but only if a U.S. person reports the account on an FBAR filed on behalf of the trust).
- Foreign financial accounts maintained on a United States military banking facility.

A U.S. person who has a foreign financial account may have a reporting obligation even though the account produces no taxable income. The reporting obligation is met by answering questions on a tax return about foreign accounts (for example, the questions about foreign accounts on Schedule B (Form 1040) and by filing an FBAR.

The FBAR is a calendar year report, which must be filed with the Department of Treasury on or before April 15 of the year following the calendar year reported. Generally, extensions of time to file an FBAR are allowed. The law affords an extension of up to six months to be available to all taxpayers, which coincides with the October 15 extension due date for individual income tax returns. While the due dates for the FBAR and individual income tax returns now coincide, the method of filing FBARs has not changed. FBARs must be filed electronically through the FinCEN BSA E-Filing System.

Those required to file an FBAR who fail to properly file a complete and correct FBAR may be subject to civil monetary penalties. For penalties that are assessed in **2020 (2021 information has not been published)**, the IRS may assess an inflation-adjusted civil penalty not to exceed $12,921 per violation for non-willful violations that are not due to reasonable cause. For willful violations, the inflation-adjusted penalty may be the greater of $129,210 or 50% of the balance in the account at the time of the violation, for each violation.

Taxpayers with specified foreign financial assets that exceed $50,000 on the last day of the tax year or $75,000 at any time during the tax year (higher threshold amounts apply to married individuals filing jointly and individuals living abroad) must report those assets to the IRS on Form 8938 - Statement of Specified Foreign Financial Assets, which is filed with an income tax return. The new Form 8938 filing requirement is in addition to the FBAR filing requirement.

Section 179 Deduction

Essentially, Section 179 of the IRS tax code allows businesses to deduct the full purchase price of qualifying equipment and/or software purchased or financed during the tax year. That means that if the taxpayer buys (or leases) a piece of qualifying equipment, he or she can deduct the full purchase price from his or her gross income. The deduction is an incentive created by the U.S. government to encourage businesses to buy equipment and invest in themselves.

With the passage and signing into law of the Tax Cuts and Jobs Act, the deduction limit for Section 179 increased from $1,040,000 to $1,050,000 for tax year 2021. The limit on equipment purchases likewise has increased, from $2,590,000 to $2,620,000. In addition, the deduction now includes any of the following improvements to existing nonresidential property (i.e., the improvement must be placed in service after the date the property itself was first placed in service): roofs; heating, air-conditioning, and ventilation systems; fire protection, alarm, and security systems. Further, the bonus depreciation increases from 50% to 100%. This part is retroactive to September 27, 2017 and is good through 2022. The bonus depreciation also now includes used equipment.

The total cost that can be deducted under Section 179 is also limited to the taxable income earned from the taxpayer's trade or business during the year. Taxable income (including salaries and wages paid to the taxpayer(s) from the business and reported as W-2 income) is figured without regard to any available Section 179 expense deduction. However, the amount of any disallowed deduction in this tax year can be carried over to next tax year and be added to the amount of qualified Section 179 property placed in service in that next tax year. To elect the Section 179 Deduction a taxpayer needs to fill out Part One of IRS Form 4562 - Depreciation and Amortization.

The definition of property eligible for the Section 179 Deduction includes:

- Computers.
- Computer off-the-shelf software.
- Office furniture.
- Office equipment.
- Equipment (machines, etc.) purchased for business use.
- Tangible personal property used in business.
- Business Vehicles with a gross vehicle weight in excess of 6,000lbs (Section 179 Vehicle Deductions).
- Property attached to the taxpayer’s building that is not a structural component of the building (i.e.: a printing press, large manufacturing tools and equipment).
- Partial Business Use (equipment that is purchased for business use and personal use: generally, the taxpayer’s deduction will be based on the percentage of time he or she uses the equipment).
- Improvements to existing nonresidential property.

The TCJA also expanded the definition of Section 179 property to allow the taxpayer to elect to include the following improvements made to nonresidential real property after the date when the property was first placed in service:

- Qualified improvement property, which means any improvement to a building's interior. However, improvements do not qualify if they are attributable to:
    - the enlargement of the building,
    - any elevator or escalator, or
    - the internal structural framework of the building.
- Roofs, HVAC, fire protection systems, alarm systems and security systems.

These changes apply to property placed in service in taxable years beginning after December 31, 2017.

Off-the-shelf computer software put in service during the tax year is qualifying property for purposes of the Section 179 deduction. This includes computer software that is readily available for purchase by the general public, is subject to a nonexclusive license, and has not been substantially modified. It is any program designed to cause a computer to perform a desired function. However, a database or similar item is not considered computer software unless it is in the public domain and is incidental to the operation of otherwise qualifying software.

The Tax Cuts and Jobs Act (TCJA) removed computer or peripheral equipment from the definition of listed property. This change applies to property placed in service after December 31, 2017.

The TCJA also changed depreciation limits for passenger vehicles, trucks, and vans (not meeting the guidelines below), that are used more than 50% in a qualified business use and placed in service after December 31, 2017.

For passenger automobiles placed in service in **2020** (information for 2021 has not been released) for which the Section 168(k) bonus first-year depreciation deduction does not apply, the depreciation limit under Section 280F(d)(7) is:

- $10,100 for the first year,
- $16,100 for the second year,
- $9,700 for the third year, and
- $5,760 for each later taxable year in the recovery period.

For passenger automobiles to which the Section 168(k) bonus first-year depreciation deduction applies and that are acquired after September 27, 2017, and placed in service during **calendar year 2020** (information for 2021 has not been released), the depreciation limit under Section 280F(d)(7) is:

- $18,100 for the first year,
- $16,100 for the second year,
- $9,700 for the third year, and
- $5,760 for each later taxable year in the recovery period.

Exceptions include the following vehicles:

- Taxis, transport vans, and other vehicles used to specifically transport people or property for hire.
- Ambulance or hearse used specifically in a taxpayer's business.
- Qualified non-personal use vehicles specifically modified for business (i.e., van without seating behind driver, permanent shelving installed, and exterior painted with company's name).

Also, the maximum Section 179 expense deduction for sport utility vehicles (SUV) placed in service in tax years beginning in 2021 is $26,200.

Many vehicles that by their nature are not likely to be used for personal purposes qualify for full Section 179 deduction including the following vehicles:

1. Heavy non-SUV vehicles with a cargo area at least six feet in interior length (this area must not be easily accessible from the passenger area.).
2. Vehicles that can seat nine-plus passengers behind the driver's seat (i.e., Hotel / Airport shuttle vans, etc.).
3. Vehicles with a fully enclosed driver's compartment / cargo area, no seating at all behind the driver's seat, and no part of the body Section protruding more than 30 inches ahead of the leading edge of the windshield.

Some of the property and equipment that does not qualify for the Section 179 Deduction is:

- Property used outside the United States generally does not qualify for the Section 179 Deduction.
- Property that is used to furnish lodging is generally not qualified for the Section 179 Deduction.
- Real Property does not qualify for the Section 179 Deduction. Real Property is typically defined as land, buildings, permanent structures, and the components of the permanent structures (including improvements). Other examples of property that would not qualify for the Section 179 Deduction include paved parking areas and fences.
- Property acquired by gift or inheritance, as well as property purchased from related parties does not qualify for the Section 179 Deduction (No, a taxpayer cannot sell equipment to him or herself and qualify for Section 179).
- Any property that is not considered to be personal property may not qualify for the Section 179 Deduction.

Note

Used Equipment (that is new to the taxpayer) qualifies for Section 179. Under the TCJA, used equipment also qualifies for Bonus Depreciation.

Bonus Depreciation

The Tax Cuts and Jobs Act (TCJA) increased the bonus depreciation percentage from 50% to 100% for qualified property acquired and placed in service after September 27, 2017, and before January 1, 2023. The bonus depreciation percentage for qualified property that a taxpayer acquired before September 28, 2017, and placed in service before January 1, 2018, remains at 50%. Special rules apply for longer production period property and certain aircraft. The amount of allowable bonus depreciation is then phased down over four years: 80% will be allowed for property placed in service in 2023, 60% in 2024, 40% in 2025, and 20% in 2026. (For certain property with long production periods, the above dates will be pushed out a year.)

The 100% depreciation deduction generally applies to depreciable business assets with a recovery period of 20 years or less and certain other property. Machinery, equipment, computers, appliances, and furniture generally qualify. The definition of property eligible for 100% bonus depreciation was expanded to include used qualified property acquired and placed in service after September 27, 2017, if all the following factors apply:

- The taxpayer or its predecessor did not use the property at any time before acquiring it.
- The taxpayer did not acquire the property from a related party.
- The taxpayer did not acquire the property from a component member of a controlled group of corporations.
- The taxpayer's basis of the used property is not figured in whole or in part by reference to the adjusted basis of the property in the hands of the seller or transferor.
- The taxpayer's basis of the used property is not figured under the provision for deciding basis of property acquired from a decedent.
- Also, the cost of the used property eligible for bonus depreciation does not include the basis of property determined by reference to the basis of other property held at any time by the taxpayer (for example, in a like-kind exchange or involuntary conversion).

The TCJA added qualified film, television and live theatrical productions as types of qualified property that may be eligible for 100% bonus depreciation. This provision applies to property acquired and placed in service after September 27, 2017. No bonus depreciation is allowed for property acquired before September 28, 2017 and placed in service after 2019.

Under the TCJA, certain types of property are not eligible for bonus depreciation in any taxable year beginning after December 31, 2017. One such exclusion from qualified property is for property primarily used in the trade or business of the furnishing or sale of:

- Electrical energy, water or sewage disposal services,
- Gas or steam through a local distribution system, or
- Transportation of gas or steam by pipeline.

This exclusion applies if the rates for the furnishing or sale have to be approved by a Federal, state or local government agency, a public service or public utility commission, or an electric cooperative.

The TCJA also added an exclusion for any property used in a trade or business that has had floor-plan financing indebtedness if the floor-plan financing interest was taken into account under Section 163(j)(1)(C). Floor-plan financing indebtedness is secured by motor vehicle inventory that in a business that sells or leases motor vehicles to retail customers.

As corrected by the Coronavirus Aid, Relief, and Economic Security Act (CARES), qualified improvement property is treated as 15-year property, and, therefore, bonus depreciation eligible. The change is made as if included in TCJA, and thus is effective for property placed in service after December 31, 2017.

Bonus Depreciation is useful to very large businesses spending more than the Section 179 Spending Cap on new capital equipment. Also, businesses with a net loss are still qualified to deduct some of the cost of new equipment and carry-forward the loss. When applying these provisions, Section 179 is generally taken first, followed by Bonus Depreciation - unless the business had no taxable profit, because the unprofitable business is allowed to carry the loss forward to future years.

Unrecovered Basis

There are limits on the amount a taxpayer can deduct for depreciation of his or her car, truck, or van. The Section 179 deduction is treated as depreciation for purposes of the limits. The maximum amount a taxpayer can deduct each year depends on the year he or she puts the car in service. If the depreciation deductions for the taxpayer's car are reduced, he or she will have unrecovered basis in his or her car at the end of the recovery period. If the taxpayer continues to use his or her car for business, he or she can deduct that unrecovered basis (subject to depreciation limits) after the recovery period ends.

Unrecovered basis is the taxpayer's cost or other basis in the car reduced by any clean-fuel vehicle deduction (for vehicles placed in service before January 1, 2006), alternative motor vehicle credit, electric vehicle credit, gas guzzler tax, and depreciation and Section 179 deductions that would have been allowable if the taxpayer had used the car 100% for business and investment use. For 5-year property, the taxpayer's recovery period is 6 calendar years. A part year's depreciation is allowed in the first calendar year, a full year's depreciation is allowed in each of the next 4 calendar years, and a part year's depreciation is allowed in the 6th calendar year.

Under the Modified Accelerated Cost Recovery System (MACRS), the taxpayer's recovery period is the same whether he or she utilizes declining balance or straight line depreciation. The taxpayer determines his or her unrecovered basis in the 7th year after he or she placed the car in service.

If the taxpayer continues to use his or her car for business after the recovery period, he or she is due a depreciation deduction in each succeeding tax year until he or she recovers the basis in the car. The maximum amount the taxpayer can deduct each year is determined by the date he or she placed the car in service and his or her business-use percentage. For example, no deduction is allowed for a year the taxpayer uses a car 100% for personal purposes.

Per Revenue Procedure 2011-26 the IRS provides a safe harbor accounting method. This procedure provides guidance with respect to the 100% additional first year depreciation deduction under Section 168(k)(5) of the Code, and the extension of the 50% bonus depreciation deduction for qualified property placed in service in 2010. This procedure defines which property is eligible for the 100% bonus depreciation deduction and provides guidance regarding the time and manner for making certain elections under Sections 168(k)(2) and (5). The procedure also provides a safe harbor method of accounting for passenger automobiles that qualify for the 100% additional first year depreciation deduction and that are subject to first-year limitations under Section 280F.

The taxpayer selects the safe harbor method by choosing it to deduct depreciation on a passenger car on the return of the year that follows the placed-in-service year of the car when the cost exceeded the first-year luxury auto limit and the 100% bonus depreciation deduction was claimed.

Review Question 6
Within the specified dollar limits of Section 179, a business can deduct, for the current tax year, what amount of the purchase price of financed or leased equipment and off-the-shelf software that was placed into service in the same tax year that the deduction is being taken and qualifies for the deduction?

A. 25% of the purchase price
B. 50% of the purchase price
C. 75% of the purchase price
D. 100% of the purchase price

See Review Feedback for answer.

2021 Tax Credits and Deductions Updates

Child Tax Credit (CTC)

Under the American Rescue Plan, the CTC will be expanded to $3,600 for each child under 6 and $3,000 for each child between 6 to 17 years old (the credit previously excluded children who were 17.) Those amounts will also be available to all low-income families, marking a shift from its prior limits for poor families.

The provision also includes income cutoffs for higher-income households. Single taxpayers earning up to $75,000 and married couples earning up to $150,000 would receive the full credit of either $3,000 or $3,600 per child, but the payments would be reduced for people with earnings above those thresholds.

Taxpayers who earn too much to qualify for the expanded tax credits could still claim the base $2,000 credit for their children provided their incomes are below the current thresholds of $200,000 for single taxpayers and $400,000 for married couples.

Additionally, the CTC will be partially paid out on a monthly basis, rather than claimed once per year when taxpayers file their tax returns. In other words, a family with two children under 6 would qualify for $7,200 in CTC payments, or $600 in monthly payments. The monthly payments will run only from July through December 2021, with the other half of the CTC paid when taxpayers file their tax returns. In other words, taxpayers would receive six months of monthly income, and then would receive the rest of the CTC through their tax refund.

The taxpayer's child must have a Social Security Number issued by the Social Security Administration (SSA) before the due date of the taxpayer's tax return (including extensions) to be claimed as a qualifying child for the Child Tax Credit or Additional Child Tax Credit. Children with an Individual Taxpayer Identification Number (ITIN) cannot be claimed for either credit. If the taxpayer's child's immigration status has changed so that his or her child is now a U.S. citizen or permanent resident, but the child's Social Security card still has the words "Not valid for employment" on it, the taxpayer should ask the SSA for a new Social Security card without those words.

If the taxpayer's child does not have a valid SSN, his or her child may still qualify him or her for the Credit for Other Dependents (ODC). This is a non-refundable credit of up to $500 per qualifying person. If the taxpayer's dependent child lived with him or her in the United States and has an Individual Taxpayer Identification Number (ITIN), but not an SSN, issued by the due date of his or her 2021 tax return (including extensions), he or she may be able to claim the Credit for Other Dependents (ODC) for that child.

Spouses and dependents residing outside the United States who use ITINs, a tax processing number issued by the IRS, should review the information on IRS.gov/ITIN to determine whether they need to renew an ITIN before filing a tax return next year. Here are some important facts from the IRS about the Child Tax Credit and how it may benefit a taxpayer's family. (18)

1. *Amount* - With the Child Tax Credit, a taxpayer may be able to reduce his or her Federal income tax by up to $3,600 for each qualifying child under the age of 18 for 2021 only.
2. *Qualification* - A qualifying child for this credit is someone who meets the qualifying criteria of six tests: age, relationship, support, dependent, citizenship, and residence.

3. *Age Test* - To qualify, a child must have been under age 18 – age 17 or younger – at the end of 2021.
4. *Relationship Test* - To claim a child for purposes of the Child Tax Credit, they must either be the taxpayer's son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister or a descendant of any of these individuals, which includes a grandchild, niece or nephew. An adopted child is always treated as a taxpayer's own child. An adopted child includes a child lawfully placed with him or her for legal adoption.
5. *Support Test* - In order to claim a child for this credit, the child must not have provided more than half of their own support.
6. *Dependent Test* - The taxpayer must claim the child as a dependent on his or her Federal income tax return.
7. *Citizenship Test* - To meet the citizenship test, the child must be a U.S. citizen, U.S. national, or U.S. resident alien and the taxpayer must provide a valid Social Security number (SSN) for the child by the tax return due date.
8. *Residence Test* - The child must have lived with the taxpayer for more than half of 2021. There are some exceptions to the residence test, which can be found in IRS Publication 972 - Child Tax Credit.

The expanded Child Tax Credit is limited if the taxpayer's modified adjusted gross income (MAGI) is above a certain amount. Single taxpayers earning up to $75,000 and married couples earning up to $150,000 would receive the full credit of either $3,000 or $3,600 per child, but the payments would be reduced for people with earnings above those thresholds. Phase-out means that the credit is reduced as the taxpayer's income increases. For 2021, the increased payment goes down by $50 for every $1,000 earned above the limit.

2021 Child Tax Credit Phase-out Amounts - Child under 6 years old			
	Full Credit	**Partial Credit**	**No Credit**
Single	Up to $75,000	$75,001 - $147,000	Over $147,000
Married Filing Jointly	Up to $150,000	$150,001 - $222,000	Over $222,000
Head of Household	Up to $112,500	$112,501 - $184,500	Over $184,500
Married Filing Separately	Up to $75,000	$75,001 - $147,000	Over $147,000

Table 1-18 - American Rescue Plan (ARP) (2021)

2021 Child Tax Credit Phase-out Amounts - Child between 6 to 17 years old			
	Full Credit	**Partial Credit**	**No Credit**
Single	Up to $75,000	$75,001 - $135,000	Over $135,000
Married Filing Jointly	Up to $150,000	$150,001 - $210,000	Over $210,000
Head of Household	Up to $112,500	$112,501 - $172,500	Over $172,500
Married Filing Separately	Up to $75,000	$75,001 - $135,000	Over $135,000

Table 1-19 - American Rescue Plan (ARP) (2021)

The previous credit of $2,000 per child is still available subject to an upper income limit of $400,000 for married couples and $200,000 for individuals. For married taxpayers filing a joint return, the phase-out begins at $400,000. For all other taxpayers, including married taxpayers filing a separate return, the phase-out begins at $200,000. In this case, the reduction is $50 for each $1,000 by which the taxpayer's MAGI exceeds the threshold amount. The credit is completely phased out for married taxpayers when MAGI reaches $440,000 and $240,000 for all other taxpayers.

2021 Child Tax Credit Phase-out Amounts - Higher Income Earners			
	Full Credit	**Partial Credit**	**No Credit**
Single	Up to $200,000	$200,001 - $240,000	Over $240,000
Married Filing Jointly	Up to $400,000	$400,001 - $440,000	Over $440,000
Head of Household	Up to $200,000	$200,001 - $240,000	Over $240,000
Married Filing Separately	Up to $200,000	$200,001 - $240,000	Over $240,000

Table 1-20 - Tax Cuts and Jobs Act (2021)

Credit for Other Dependents (ODC)

The Tax Cuts and Jobs Act provided a $500 Credit for Other Dependents (e.g., elderly or disabled dependents or children over 17). This credit is to provide some relief to those families who will lose the now defunct personal exemption and are not eligible for the expanded Child Tax Credit (CTC). Both the CTC and ODC can be claimed for eligible dependents for 2021. Like the CTC, this $500 “non-child” credit is subject to income eligibility thresholds and will phase out for taxpayers with adjusted gross incomes (AGI) above $200,000 (single) and $400,000 (married).

Child and Dependent Care Credit

The American Rescue Plan (ARP) makes a number of enhancements to the Child and Dependent Care Credit for the 2021 tax year. First of all, the new stimulus law makes the credit refundable for 2021. The Act also increases the maximum credit percentage up from 35% to 50% for 2021.

Additionally, more of the taxpayer’s childcare expenses are subject to the credit. Instead of up to $3,000 in childcare expenses for one child and $6,000 for two or more, the American Rescue Plan allows the credit for up to $8,000 in expenses for one child and $16,000 for multiple children in 2021. When combined with the 50% maximum credit percentage, that puts the maximum credit for this tax year at $4,000 if the taxpayer has just one child and $8,000 for two or more children.

For higher income earners, the credit percentage is reduced, but not below 20%, regardless of the amount of adjusted gross income. A taxpayer’s child and dependent care expenses must be for the care of one or more qualifying persons.

A qualifying person is: [19]

- A taxpayer’s qualifying child who is his or her dependent and who was under age 13 when the care was provided.
- A spouse who was not physically or mentally able to care for him or herself and lived with the taxpayer for more than half the year.
- A person who was not physically or mentally able to care for him or herself, lived with the taxpayer for more than half the year, and either:
    - Was his or her dependent.
    - Would have been his or her dependent except that:
        - He or she received gross income above annual threshold level.
        - He or she filed a joint return.
        - He or she, or his or her spouse if filing jointly, could be claimed as a dependent on someone else's 2021 return.

Adoption Credit

The American Taxpayer Relief Act of 2012 (H.R.8) passed on January 2, 2013 permanently extended the Adoption Credit and the adoption assistance programs for tax years beginning after December 31, 2012. Tax benefits for adoption include both a tax credit for qualified adoption expenses paid to adopt an eligible child and an exclusion for employer-provided adoption assistance. The credit is nonrefundable, which means it is limited to the taxpayer’s tax liability for the year. The maximum amount (dollar limit) for 2021 is $14,440 per child. For both the credit and the exclusion, qualified adoption expenses, defined in Section 23(d)(1) of the Code, include: [20]

- Reasonable and necessary adoption fees,
- Court costs and attorney fees,
- Traveling expenses (including amounts spent for meals and lodging while away from home), and
- Other expenses that are directly related to and for the principal purpose of the legal adoption of an eligible child.
- An eligible child is an individual who is under the age of 18 or is physically or mentally incapable of self-care.

Qualified adoption expenses do not include: [20]

- Expenses for which the taxpayer received funds under any state, local, or Federal program.
- Expenses that violate state or Federal law.
- Expenses for carrying out a surrogate parenting arrangement.
- Expenses for the adoption of a taxpayer’s spouse's child.
- Expenses paid or reimbursed by a taxpayer’s employer or any other person or organization.
- Expenses allowed as a credit or deduction under any other provision of Federal income tax law.

The taxpayer should use Form 8839 - Qualified Adoption Expenses to figure his or her Adoption Credit and any employer-provided adoption benefits he or she can exclude from his or her income on Form 1040, 1040-SR, or 1040-NR. (21)

The credit and exclusion are each subject to an income limitation and a dollar limitation. The income limit on the adoption credit or exclusion is based on taxpayer's modified adjusted gross income (MAGI). For tax year 2021, the MAGI phase-out begins at $216,660 and ends at $256,660. Thus, if the taxpayer's MAGI amount is below $216,660 for 2021, his or her credit or exclusion will not be affected by the MAGI phase-out but if the taxpayer's MAGI amount for 2021 is above $256,660, his or her credit or exclusion will be zero.

The taxpayer should reduce the dollar limit for a particular year by the amount of qualified adoption expenses used in the previous years for the same adoption effort. Also, when computing the dollar limitation, qualified adoption expenses paid and claimed in connection with an unsuccessful domestic adoption effort must be combined with qualified adoption expenses paid in connection with a subsequent domestic adoption attempt, whether or not the subsequent attempt is successful.

The dollar limitation applies separately to both the credit and the exclusion, and the taxpayer may be able to claim both the credit and the exclusion for qualified expenses. However, he or she must claim any allowable exclusion before claiming any allowable credit. Expenses used for the exclusion reduce the amount of qualified adoption expenses available for the credit. As a result, the taxpayer cannot claim both a credit and an exclusion for the same expenses.

Because the adoption credit is not refundable after 2011, the taxpayer may be able to carry-forward any unused credit amounts to future tax years. The 2021 Form 8839 and its instructions will have information on the credit carry-forward. (20)

Coverdell Education Savings Accounts

The American Taxpayer Relief Act made permanent the $2,000 per year total contributions to a Coverdell ESA. There is no limit to the number of accounts that can be established for a beneficiary; however, the total contribution to all accounts on behalf of a beneficiary in any year cannot exceed $2,000. The taxpayer's contribution limit may be reduced. If his or her modified adjusted gross income (MAGI) is between $95,000 and $110,000 (between $190,000 and $220,000 if filing a joint return), the $2,000 limit for each designated beneficiary is gradually reduced. If the taxpayer's MAGI is $110,000 or more ($220,000 or more if filing a joint return), he or she cannot contribute to a Coverdell ESA in 2021.

To figure the limit on the amount the taxpayer can contribute for each designated beneficiary, multiply $2,000 by a fraction. The numerator (top number) is the taxpayer's MAGI minus $95,000 ($190,000 if filing a joint return). The denominator (bottom number) is $15,000 ($30,000 if filing a joint return). Subtract the result from $2,000. This is the amount the taxpayer can contribute for each beneficiary. The taxpayer can use Worksheet 7-2 - Coverdell ESA Contribution Limit in Publication 970 to figure the limit on contributions.

Contributions to a Coverdell ESA are not deductible but amounts deposited in the account grow tax free until distributed. The beneficiary will not owe tax on the distributions if they are less than a beneficiary's qualified education expenses at an eligible institution.

This benefit applies to qualified higher education expenses as well as to qualified elementary and secondary education expenses.

Amounts remaining in a CESA must be dispersed within 30 days after the beneficiary reaches age 30 or 30 days after the death of the beneficiary. One method a taxpayer can use to avoid taking an unwanted distribution is to take advantage of the rollover provision for Coverdell ESAs.

Distributed amounts are not subject to Federal income taxes if they are rolled over to another ESA for the benefit of the same beneficiary or a member of the beneficiary's family that is under the age of 30 including: (22)

- Son, daughter, stepchild, foster child, adopted child, or a descendant of any of them.
- Brother, sister, stepbrother, or stepsister.

- Father or mother or ancestor of either.
- Stepfather or stepmother.
- Son or daughter of a brother or sister.
- Brother or sister of father or mother.
- Son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law.
- The spouse of any individual listed above.
- First cousin.

An amount is rolled over if it is paid to another Coverdell ESA within 60 days after the date of the distribution. The age limit does not apply to beneficiaries with special needs.

Student Loan Interest Deduction

The American Taxpayer Relief Act made permanent the Student Loan Interest Deduction. Generally, the amount a taxpayer may deduct is the lesser of $2,500 or the amount of interest he or she actually paid. For purposes of the student loan interest deduction, these expenses are the total costs of attending an eligible educational institution, including graduate school. The expenses include amounts paid for the following items: (23)

- Tuition and fees.
- Room and board.
- Books, supplies and equipment.
- Other necessary expenses (such as transportation).

The cost of room and board qualifies only to the extent that it is not more than the greater of: (23)

- The allowance for room and board, as determined by the eligible educational institution, that was included in the cost of attendance (for Federal financial aid purposes) for a particular academic period and living arrangement of the student.
- The actual amount charged if the student is residing in housing owned or operated by the eligible educational institution.

For 2021, the $2,500 maximum deduction for interest paid on student loans begins to phase out if the taxpayer's modified adjusted gross income (MAGI) is between $70,000 and $85,000 ($140,000 and $170,000 if he or she files a joint return). The taxpayer cannot take a student loan interest deduction if his or her MAGI is $85,000 or more ($170,000 or more if he or she files a joint return). Generally, the taxpayer figures the deduction using the Student Loan Interest Deduction Worksheet in the Form 1040 instructions. (24)

American Opportunity Tax Credit

The American Opportunity Tax Credit (AOTC) modifies the existing Hope Scholarship Credit. The AOTC makes the Hope Credit available to a broader range of taxpayers, including many with higher incomes and those who owe no tax. It also adds required course materials to the list of qualifying expenses and allows the credit to be claimed for four post-secondary education years instead of two. Many of those eligible will qualify for the maximum annual credit of $2,500 per student.

The Protecting Americans from Tax Hikes Act of 2015 made the American Opportunity Tax Credit permanent. The bill also adds a provision barring individuals from claiming the credit for 10 years if they fraudulently claim the credit and for two years if they are found to have claimed the credit with reckless or intentional disregard of the rules.

The American Opportunity Tax Credit is a partially refundable tax credit for undergraduate college education expenses. This credit provides up to $2,500 in tax credits on the first $4,000 of qualifying educational expenses. The amount of the American Opportunity tax credit is comprised of:

- 100% of the first $2,000 in qualifying education expenses, plus
- 25% of the next $2,000 in qualifying expenses.

Thus, the taxpayer's maximum credit could be $2,500 based on $4,000 in qualifying expenses.

Also, a taxpayer's modified adjusted gross income (AGI) in excess of $80,000 ($160,000 for a joint return) is used to determine a reduction in the amount of the American Opportunity Tax Credit. The credit is completely phased out and not available for taxpayers with AGI of $90,000 ($180,000 for joint filers).

Up to 40% of the American Opportunity Tax Credit is refundable. Therefore, up to $1,000 of the American Opportunity Tax Credit can be refunded to a taxpayer, even if his or her tax liability is zero. This potential refund could make the American Opportunity Tax Credit more valuable than the Lifetime Learning Credit, which is non-refundable.

Lifetime Learning Credit

The Lifetime Learning Credit equals 20% of adjusted qualified education expenses, up to a maximum of $10,000 of adjusted qualified education expenses per return. Therefore, the maximum Lifetime Learning Credit the taxpayer can claim on his or her return for the year is $2,000, regardless of the number of students for whom he or she paid qualified education expenses.

The Consolidated Appropriations Act, 2021 changes the income phaseouts for the Lifetime Learning Tax Credit (LLTC) to be the same as the income phaseouts for the American Opportunity Tax Credit (AOTC). Therefore, the amount of the taxpayer's credit for 2021 is gradually reduced (phased out) if his or her modified adjusted gross income (MAGI) is between $80,000 and $90,000 ($160,000 and $180,000 if he or she files a joint return). The taxpayer cannot claim a credit if his or her MAGI is $90,000 or more ($180,000 or more if he or she files a joint return). The new income phaseouts will not be adjusted for inflation.

The taxpayer cannot claim the Lifetime Learning Credit for any student if he or she claims the American Opportunity Tax Credit for that student for the same tax year. To get either credit, the taxpayer or student usually must receive Form 1098-T - Tuition Statement, from the school attended.

Tuition and Fees Deduction

The Consolidated Appropriations Act, 2021, repeals the Tuition and Fees Deduction, effective with tax years that begin in 2021. This is a permanent repeal, so the Tuition and Fees Deduction will not return in the next tax extenders bill. Instead, the phase-out limits on the Lifetime Learning Credit are increased to $80,000 ($160,000 for married filing jointly).

Deduction for Educator Expenses

The Protecting Americans from Tax Hikes Act of 2015 made the above-the-line deduction for certain expenses of elementary and secondary school teachers permanent. If the taxpayer is an eligible educator, he or she can deduct up to $250 ($500 if married filing joint and both spouses are educators, but not more than $250 each) of any unreimbursed expenses (otherwise deductible as a trade or business expense) he or she paid or incurred for books, supplies, computer equipment (including related software and services), other equipment, and supplementary materials that he or she uses in the classroom. For courses in health and physical education, expenses for supplies are qualified expenses only if they are related to athletics. This deduction is for expenses paid or incurred during the tax year.

The taxpayer is an eligible educator if, for the tax year, he or she meets the following requirements: [25]

1. He or she is a kindergarten through grade 12:
    a. Teacher
    b. Instructor
    c. Counselor
    d. Principal
    e. Aide
2. He or she works at least 900 hours a school year in a school that provides elementary or secondary education, as determined under state law.

The taxpayer may be able to deduct certain expenses for professional development courses he or she has taken related to the curriculum he or she teaches or to the students he or she teaches. See the instructions for line 10 of Schedule 1 (Form 1040) for more information.

Retirement Savings Contributions Credit (Saver's Credit)

A taxpayer can claim the credit for 50%, 20% or 10% of the first $2,000 ($4,000 if married filing jointly) contributed during the year to a retirement account. Therefore, the maximum credit amounts that can be claimed are $1,000, $400 or $200 per person. The maximum credit a married couple filing jointly can claim together is $2,000. The applicable percentage is determined by the taxpayer's filing status and adjusted gross income (AGI).

The credit may be used against the taxpayer's regular and alternative minimum tax liability. For 2021, the maximum applicable percentage is 50%, which is completely phased out when AGI exceeds $66,000 for joint filers, $49,500 for head of household filers, and $33,000 for single and married filing separately filers. The applicable percentage is the percentage as determined in accordance with the following table: (26)

2021 Saver's Credit AGI Thresholds						
Joint Return		Head of Household		Single or Married, Filing Separately		Credit Rate
Over	Not Over	Over	Not Over	Over	Not Over	
$0	$39,500	$0	$29,625	$0	$19,750	50%
$39,500	$43,000	$29,625	$32,250	$19,750	$21,500	20%
$43,000	$65,000	$32,250	$49,500	$21,500	$33,000	10%
$66,000	-----	$49,500	------	$33,000	----	0%

Table 1-21 - Retirement Savings Contributions Credit (Saver's Credit) (2021)

Review Question 7

In 2021, Marisela pays $13,190 of qualified adoption expenses in connection with an adoption of an eligible child and the adoption becomes final. Her employer reimburses her for $3,190 of those expenses. Marisela's modified adjusted gross income (MAGI) amount for 2021 is $97,880 and she meets all other requirements, so she can exclude $3,190 from her gross income for 2021. The expenses allowable for the Adoption Credit are what amount?

A. $0
B. $10,000
C. $13,190
D. $14,440

See Review Feedback for answer.

Earned Income Tax Credit (EITC)

The American Rescue Plan (ARP) expands the 2021 Earned Income Tax Credit (EITC) for taxpayer with no children in a few ways. First, the new law generally lowers the minimum age from 25 to 19 (except for certain full-time students). Therefore, for 2021, the applicable minimum age is decreased to 19, except for students (24 years old) and qualified former foster youth or homeless youth (18 years old). The Act also eliminates the maximum age limit (65), so older people without qualifying children can claim the 2021 credit, too. The maximum credit available for childless workers is also increased from $543 to $1,502 for the 2021 tax year.

As with the 2020 EITC, the taxpayer can use his or her 2019 earned income instead of his or her 2021 income if that will increase his or her credit amount. This provision could help many people who were laid off, furloughed, or otherwise suffer an income loss this year. Lastly, there are a few permanent EITC changes in the American Rescue Plan. For instance, workers who otherwise would not be able to claim the credit because their children cannot satisfy the identification requirements can now claim the childless EITC. Certain married but separated couples can now claim the EITC on separate tax returns, too.

For tax year 2021, the maximum Earned Income Tax Credit (EITC) for low and moderate-income workers and working families rises to $6,728, up from $6,660 in 2020. The EITC is a refundable tax credit for certain people who work and have earned income under $57,414. The credit varies by family size, filing status and other factors, with the maximum credit going to joint filers with three or more qualifying children.

Income Qualification Item	Number of Qualifying Children			
	None	One	Two	Three or More
Earned Income Base Amount	$9,820	$10,640	$14,950	$14,950
Maximum Amount of Credit	$1,502	$3,618	$5,980	$6,728
Threshold Phaseout Amount (Single, Surviving Spouse, Head of Household)	$11,610	$19,520	$19,520	$19,520
Completed Phaseout Amount (Single, Surviving Spouse, Head of Household)	$21,430	$42,158	$47,915	$51,464
Threshold Phaseout Amount (Married Filing Jointly)	$17,560	$25,470	$25,470	$25,470
Completed Phaseout Amount (Married Filing Jointly)	$27,380	$48,108	$53,865	$57,414

Table 1-22 - American Rescue Plan (ARP) (2021)

The American Rescue Plan (ARP) increased the maximum amount of investment income a taxpayer can have and still get the credit to $10,000 for 2021. Use Publication 596 - Earned Income Tax Credit (EITC) to determine eligibility.

Paid preparers must complete Form 8867 - Paid Preparer's Due Diligence Checklist when filing Federal income tax returns or claims for refund involving the EITC. Paid preparers must meet due diligence requirements in determining the taxpayer's eligibility for, and the amount of, the EITC. Failure to do so could result in a $545 penalty for each failure in 2021. The IRS adjusted the penalty for taxable year returns beginning in 2015 for cost of living.

Exclusion of Capital Gains Tax on Principal Residences

The Tax Cuts and Jobs Act preserved the valuable provision that allows taxpayers to potentially exclude from Federal income taxation up to $250,000 of gain from a qualified home sale, or $500,000 if he or she is a married joint filer. Single homeowners are able exclude up to $250,000 of the gain (other than gain allocated to periods of nonqualified use) on the sale of his or her main home. A taxpayer may be able to exclude up to $500,000 of the gain (other than gain allocated to periods of nonqualified use) on the sale of his or her main home if he she or is married and file a joint return and meet the requirements listed in the special rules for joint returns in Publication 523 - Selling Your Home.

A single taxpayer can exclude the gain on the sale of his or her main home if **all** of the following are true: [27]

1. Meet the ownership test.
2. Meet the use test.
3. During the 2-year period ending on the date of the sale, the taxpayer did not exclude gain from the sale of another home.

If the taxpayer sells his or her home at a loss, the money he or she receives is not taxable. However, the taxpayer cannot deduct the loss from other income. Use Publication 523 - Selling Your Home to figure the exclusion of capital gains on the tax return.

State and Local Income Tax Deduction (SALT)

Under previous tax law the taxpayer could claim an itemized deduction for an unlimited amount of personal state and local income and property taxes. He or she could also choose to forego any deduction for state and local income taxes and instead deduct state and local general sales taxes. The Tax Cuts and Jobs Act limits the taxpayer's deduction for state and local income and property taxes to a combined total of $10,000 ($5,000 if he or she uses married filing separate status). Foreign real property taxes can no longer be deducted. However, the taxpayer can still choose to deduct state and local sales taxes instead of state and local income taxes.

The TCJA provides that for tax years beginning after December 31, 2017 until January 1, 2026, state, local, and foreign property taxes, and state and local sales taxes, are fully deductible only when paid or accrued in carrying on a trade or business or an activity relating to expenses for the production of income. Therefore, taxpayers may only fully claim deductions for state, local and foreign property taxes, and sales taxes that are presently deductible in computing income on an individual's Schedule C, Schedule E, or Schedule F on the individual's tax return. For example, an individual taxpayer may only deduct property taxes if these taxes were imposed on residential rental property which qualifies as a business asset.

Residential Energy Credits

Residential Energy Efficient Property Credit (Part I) - The taxpayer may be able to take the Residential Energy Efficient Property Credit if he or she made energy saving improvements to his or her home located in the United States. The credit currently applies to solar electric property and solar water heating property and is available for property placed in service through December 31, 2021, based on an applicable percentage. The applicable percentages are:

- In the case of property placed in service after December 31, 2016, and before January 1, 2020, 30%.
- In the case of property placed in service after December 31, 2019, and before January 1, 2021, 26%.
- In the case of property placed in service after December 31, 2020, and before January 1, 2022, 22%.

Nonbusiness Energy Property Credit (Part II) - The Nonbusiness Energy Property Credit for installing insulation, storm windows, etc., is extended through 2021 as part of the Consolidated Appropriations Act, 2021.

In 2021, an individual may claim a credit for (1) 10% of the cost of qualified energy efficiency improvements and (2) the amount of the residential energy property expenditures paid or incurred by the taxpayer during the taxable year (subject to the overall credit limit of $500).

Qualified energy efficiency improvements include the following qualifying products:

- Energy-efficient exterior windows, doors, and skylights.
- Roofs (metal and asphalt) and roof products.
- Insulation.

Residential energy property expenditures include the following qualifying products:

- Energy-efficient heating and air conditioning systems.
- Water heaters (natural gas, propane, or oil).
- Biomass stoves.

Please note that qualifying property must meet the applicable standards in the law.

Charitable Donations from IRAs

The Protecting Americans from Tax Hikes Act of 2015 made permanent the tax exemption of distributions from individual retirement accounts for charitable purposes. Individuals age 70½ or over can exclude up to $100,000 from gross income for donations paid directly to a qualified charity from their IRA. Key points about qualified charitable distributions (QCDs) include:

- Married individuals filing a joint return could exclude up to $100,000 donated from each spouse's own IRA ($200,000 total).
- The donation satisfies any IRA required minimum distributions for the year.
- The amount excluded from gross income is not deductible.
- Donations from an inherited IRA are eligible if the beneficiary is at least age 70½.
- Donations from a SEP or SIMPLE IRA are not eligible.
- Donations from a Roth IRA are eligible.

The SECURE Act preserved the ability to make qualified charitable distributions (QCDs) at age 70½ even though the required minimum distribution age was increased to age 72. Qualified charitable distributions can satisfy all or part the amount of the taxpayer's required minimum distribution (RMD) from his or her IRA.

Foreign Tax Credits

The Tax Cuts and Jobs Act (TCJA), legislation passed in December 2017, made major changes to the way the U.S. taxes foreign activities. Significant new provisions include a dividends-received deduction for dividends from foreign subsidiaries and the addition of Global Intangible Low-Taxed Income rules, which subject to current U.S. taxation certain foreign earnings that would have been deferred under previous law.

The TCJA also modified the Foreign Tax Credit rules, which allow U.S. taxpayers to offset their taxes by the amount of foreign income taxes paid or accrued, in several important ways to reflect the new international tax rules. These changes include repeal of rules for computing deemed-paid foreign tax credits on dividends on the basis of foreign subsidiaries' cumulative pools of earnings and foreign taxes, and the addition of two separate foreign tax credit limitation categories for foreign branch income and amounts includible under the new Global Intangible Low-Taxed Income provisions. The TCJA also modified how taxable income is calculated for the foreign tax credit limitation by disregarding certain expenses related to income eligible for the dividends-received deduction and repealing the use of the fair market value method for allocating interest expense.

Deduction for Mortgage Insurance Premiums

The Consolidated Appropriations Act, 2021 extended the deduction for mortgage insurance premiums through 2021. The provision extends a rule treating qualified mortgage insurance premiums as interest for purposes of the mortgage interest deduction. This deduction phases out for taxpayers with adjusted gross income (AGI) over $100,000 ($50,000 if married filing separately).

Qualified Principal Residence Indebtedness Exclusion

The Consolidated Appropriations Act, 2021 includes an extension of the qualified principal residence indebtedness exclusion through 2025. Typically, when debt is forgiven, the discharged amount is included in a taxpayer's gross income. The provision reduces the maximum amount that may be excluded from $2,000,000 to $750,000. Generally, indebtedness must be the result of acquisition, construction, or substantial improvement of primary residence. Many short sales and mortgage modifications include debt forgiveness that falls under the qualified principal residence indebtedness exclusion.

Gift and Estate Tax

Although initial tax plan discussions considered complete elimination of taxes on estates, the Tax Cuts and Jobs Act keeps the Federal estate tax in place, but it doubles the threshold at which that tax applies. For an estate of any decedent dying during calendar year 2021, the basic exclusion from estate tax amount is $11,700,000 ($23,400,000 for married couples), up from a total of $11,580,000 for estates of decedents who died in 2020. The American Taxpayer Relief Act of 2012 permanently increased the top gift and estate tax rate from 35% to 40%. The annual exclusion for gifts remains the same at $15,000.

Decedents dying in:	Estate Tax Exemption Amount	Tax Rate
2017	$5,490,000	40%
2018	$11,180,000	40%
2019	$11,400,000	40%
2020	$11,580,000	40%
2021	$11,700,000	40%

Table 1-23 - Estate Tax Exemption Amounts (2021)

The following is a list of gifts that are not considered "taxable gifts" and, therefore, do not count as part of the taxpayer's lifetime exemption total:

- *Present-interest gift of $15,000 in 2021*. "Present-interest" means that the person receiving the gift has an unrestricted right to use or enjoy the gift immediately. In 2021 the taxpayer could give amounts up to $15,000 to each person, gifting as many different people as he or she wants, without triggering the gift tax.

- *Charitable gift.*
- *Gifts to a political organization for its use.*
- *Gifts to the taxpayer's spouse.*
- *Gifts to a spouse who is a U.S. citizen*. Gifts to foreign spouses are subject to an annual limit of $159,000 in 2021. This amount is indexed for inflation and can change each year.
- *Gifts for educational expenses*. To qualify for the unlimited exclusion for qualified education expenses, the taxpayer must make a direct payment to the educational institution for tuition only. Books, supplies and living expenses do not qualify. If the taxpayer wants to pay for books, supplies and living expenses in addition to the unlimited education exclusion, he or she can make a 2021 gift of $15,000 to the student under the annual gift exclusion.
- *Gifts for medical expenses.*

Charitable Gifts

The Consolidated Appropriations Act, 2021 extends and modifies the non-itemizer charitable deduction for 2021. The provision increases the maximum amount that may be deducted such that married couples filing a joint return may deduct up to $600 (while non-married filers or married filers who file separately are limited to $300).

After passage of the TCJA, cash contributions to public charities were generally limited to 60% of a taxpayer's adjusted gross income (AGI). The Coronavirus Aid, Relief, and Economic Security Act (CARES) allowed such contributions to be deducted up to 100% of AGI for 2020, with any excess contributions available to be carried over to the next five years. The Consolidated Appropriations Act, 2021 extends through 2021 the increased limit from the CARES Act on deductible charitable contributions for corporations and taxpayers who itemize.

Also, under the Tax Cuts and Jobs Act no charitable deduction would be allowed for any payment to an institution of higher education in exchange for which the payor receives the right to purchase tickets or seating at an athletic event. The TCJA also repeals the donee-reporting exemption from the contemporaneous written acknowledgment requirement for tax years beginning after December 31, 2017.

A taxpayer can only deduct gifts he or she gives to qualified charities. Gifts of money include those made in cash or by check, electronic funds transfer, credit card and payroll deduction. The taxpayer must have a bank record or a written statement from the charity to deduct any gift of money on his or her tax return. This is true regardless of the amount of the gift. The statement must show the name of the charity and the date and amount of the contribution. Bank records include canceled checks, or bank, credit union and credit card statements. If the taxpayer gives by payroll deductions, he or she should retain a pay stub, a Form W-2 wage statement or another document from his or her employer. It must show the total amount withheld for charity, along with the pledge card showing the name of the charity.

Household items include furniture, furnishings, electronics, appliances, and linens. If the taxpayer donates clothing and household items to charity, they generally must be in at least good used condition to claim a tax deduction. If he or she claims a deduction of over $500 for an item, it does not have to meet this standard if the taxpayer includes a qualified appraisal of the item with his or her tax return.

The taxpayer must get an acknowledgment from a charity for each deductible donation (either money or property) of $250 or more. Additional rules apply to the statement for gifts of that amount. This statement is in addition to the records required for deducting cash gifts. However, one statement with all of the required information may meet both requirements.

Noncash contributions over $5,000 must be substantiated with a contemporaneous written acknowledgement, with a qualified appraisal prepared by a qualified appraiser, and a completed Form 8283, Section B, that is filed with the return claiming the deduction. However, the taxpayer does not need a written appraisal for a qualified vehicle - such as a car, boat, or airplane - if his or her deduction for the qualified vehicle is limited to the gross proceeds from its sale and he or she obtained a contemporaneous written acknowledgment. (28)

The taxpayer can deduct contributions in the year he or she makes them. If the taxpayer charges his or her gift to a credit card before the end of the year it will count for 2021. This is true even if he or she does not pay the credit card bill until 2022. Also, a check will count for 2021 as long as the taxpayer mails it in 2021. Use the following lists for a quick check of whether the taxpayer can deduct a contribution.

Examples of Charitable Contributions	
Deductible As Charitable Contributions	**Not Deductible As Charitable Contributions**
Money or property the taxpayer gives to: • Churches, synagogues, temples, mosques, and other religious organizations. • Federal, state, and local governments, if the taxpayer's contribution is solely for public purposes (for example, a gift to reduce the public debt or maintain a public park). • Nonprofit schools and hospitals. • The Salvation Army, American Red Cross, CARE, Goodwill Industries, United Way, Boy Scouts of America, Girl Scouts of America, Boys and Girls Clubs of America, etc. • War veterans' groups.	Money or property the taxpayer gives to: • Civic leagues, social and sports clubs, labor unions, and chambers of commerce. • Foreign organizations (except certain Canadian, Israeli, and Mexican charities). • Groups that are run for personal profit. • Groups whose purpose is to lobby for law changes. • Homeowners' associations. • Individuals. • Political groups or candidates for public office. • Donations in exchange for college athletic event seating rights.
Expenses paid for a student living with the taxpayer, sponsored by a qualified organization.	Cost of raffle, bingo, or lottery tickets.
Out-of-pocket expenses when the taxpayer serves a qualified organization as a volunteer.	Dues, fees, or bills paid to country clubs, lodges, fraternal orders, or similar groups.
	Tuition
	Value of the taxpayer's time or services
	Value of blood given to a blood bank

Table 1-24 - Publication 526 - Table 1 - Examples of Charitable Contributions - A Quick Check (2021)

Portability Election of Unused Estate Tax Exemption

The portability election allows estates of married taxpayers to pass along the unused part of their exclusion amount, normally $11,700,000 in 2021, to their surviving spouse. This provision eradicates the need for spouses to retitle property and create trusts solely to take full advantage of each spouse's exclusion amount. The first estate tax returns for estates eligible to make the portability election (because the date of death is after December 31, 2010) were due as early as Monday, October 3, 2011. This date was the earliest eligible because the estate tax return is due nine months after the date of death. The IRS highlighted that estates of those who died before 2011 are not eligible to make this election.

As a reminder, estates unable to meet the nine-month deadline can request an automatic six-month filing extension by filing Form 4768 - Application for Extension of Time To File a Return and/or Pay U.S. Estate (and Generation-Skipping Transfer) Taxes. For example, assume Heidi's husband dies in 2021 having made lifetime gifts to children, consuming $2 million of his exemption. At death, he leaves his remaining $9,700,000 estate to Heidi. The executor of Heidi's husband's estate may elect to permit her to use his unused $9,700,000 million exemption, giving Heidi an $21,400,000 exemption (her original $11,700,000 exemption for 2021, plus the deceased spouse's $9,700,000 unused exemption).

Although the portability of the estate tax exemption is designed to prevent married couples from wasting some or all their respective exemption amounts, trust planning for married couples may still provide meaningful benefits, such as eliminating estate taxes on post-mortem appreciation, and protecting the inheritance of heirs.

Review Question 8
In 2021, an uncle who wants to help his nephew attend medical school sends $16,000 directly to the school for a year's tuition. He also sends his nephew $14,000 for books, supplies and other expenses. What amount of these payments is reportable for gift tax purposes?

A. $0
B. $14,000
C. $16,000
D. $30,000

See Review Feedback for answer.

Tax Court Decisions

Oakbrook Land Holdings, LLC v. Commissioner

The taxpayer in 2008 donated a conservation easement to a qualified organization and claimed a charitable contribution deduction under Section 170(a), Charitable, Etc., Contributions and Gifts.

The easement deed provided that, if the conservation restriction were to be extinguished at some future date, the donee would receive a share of the proceeds equal to the fair market value of the easement on the date the contribution was made. The deed further provided that the donee's share as thus determined would be reduced by the value of any improvements made by the donor after granting the easement.

The IRS disallowed the deduction, contending (among other things) that the extinguishment clause violated the requirements of Section 1.170A-14(g)(6), Qualified conservation contributions.

Reminders

Tax Return Due Date

The April 15 tax deadline is set by statute and will remain in place. If the due date falls on a Saturday, Sunday, or legal holiday, the due date is delayed until the next business day. The IRS reminds taxpayers that anyone can request an automatic six-month extension to file their tax return. The request is easily done with Form 4868 - Application for Automatic Extension of Time To File U.S. Individual Income Tax Return, which can be filed electronically or on paper.

Annual Filing Season Program (AFSP)

The IRS is offering a voluntary Annual Filing Season Program (AFSP) to return preparers. The AFSP is intended to recognize and encourage the voluntary efforts of non-credentialed tax return preparers to increase their knowledge and improve their filing season competency through continuing education. To obtain the voluntary certification, credentialed tax preparers (CPA, attorney, enrolled agent, etc.) or tax return preparers who have successfully completed a national or state test (RTRP, CTEC, OBTP, DLLR, Part 1 of the SEE, etc.) would need to have an active Preparer Tax Identification Number (PTIN) and complete 15 credit hours of continuing professional education annually through an IRS approved provider.

Non-credentialed/non-exempt or unenrolled tax preparers must complete an 18-hour course consisting of 2 hours of Ethics and Professional Conduct, 10 hours of Federal taxation and 6 hours of Annual Federal Tax Refresher (AFTR) course that includes a 100-question comprehension test with a 3-hour time limit. Unenrolled return preparers can elect to voluntarily take continuing professional education each year in preparation for the filing season and receive an Annual Filing Season Program – Record of Completion.

The program is important for a number of reasons. It encourages unregulated return preparers who do not have to meet continuing professional education requirements to stay up to date on tax laws and changes. It helps lessen the risk to taxpayers from preparers who have no education in Federal tax law or filing requirements. And it allows preparers without professional credentials to stand out from the competition by giving them a recognizable record of completion that they can show to their clients.

Preparers who complete the AFSP will also be included in a public directory that will be added to IRS.gov each year for taxpayers to use in searching for qualified tax return preparers. The Directory of Federal Tax Return Preparers with Credentials and Select Qualifications will only include attorneys, certified public accountants (CPAs), enrolled agents, enrolled retirement plan agents (ERPAs), enrolled actuaries and individuals who have received an Annual Filing Season Program – Record of Completion.

Also, as of 2016, there were changes to the representation rights of return preparers. Attorneys, CPAs, and enrolled agents will continue to be the only tax professionals with unlimited representation rights, meaning they can represent their clients on any matters including audits, payment/collection issues, and appeals. AFSP participants will have limited representation rights, meaning they can represent clients whose returns they prepared and signed, but only before revenue agents, customer service representatives, and similar IRS employees, including the Taxpayer Advocate Service. PTIN holders without an AFSP – Record of Completion or other professional credential will only be permitted to prepare tax returns. They will not be allowed to represent clients before the IRS.

Established state-based return preparer program participants with current testing requirements such as return preparers who are active members of the Maryland State Board of Individual Tax Preparers, the Oregon Board of Tax Practitioners and/or the California Tax Education Council are exempt from taking the Annual Federal Tax Refresher (AFTR) course.

For example, the IRS has exempted California Registered Tax Preparers (CRTP) from having to take the Annual Federal Tax Refresher (AFTR) course and passing the course's competency examination to obtain a Record of Completion because they have already demonstrated their competency by passing a 60-hour qualifying education course and annually maintaining their continuing professional education. These exempt groups are still required to meet other program requirements, including 15 CPE credits (10 Federal Tax Law, 3 Federal Tax Law Updates, and 2 Ethics). Return preparers who can obtain the AFSP – Record of Completion without taking the AFTR course are:

- Anyone who passed the Registered Tax Return Preparer test administered by the IRS between November 2011 and January 2013.
- Established state-based return preparer program participants currently with testing requirements: Return preparers who are active registrants of the Oregon Board of Tax Practitioners, California Tax Education Council, and/or Maryland State Board of Individual Tax Preparers.
- SEE Part I Test-Passers: Tax practitioners who have passed the Special Enrollment Exam Part I within the past two years as of the first day of the upcoming filing season.
- VITA volunteers: Quality reviewers and instructors with active PTINs.
- Other accredited tax-focused credential-holders: The Accreditation Council for Accountancy and Taxation's Accredited Business Accountant/Advisor (ABA) and Accredited Tax Preparer (ATP) programs.

Note

California Tax Education Council (CTEC) education requirements will meet the IRS requirements. Therefore, a CRTP in good standing will have already met all of the IRS requirements of the new program and will have a simplified process to obtain a Record of Completion. Also, a CRTP was granted the authority to represent, before the IRS, clients whose returns the CRTP prepared, as long as the CRTP is properly registered with CTEC for both the year the tax return was prepared as well as the year the review takes place.

Preparer Tax Identification Number (PTIN)

On January 18, 2013, the United States District Court for the District of Columbia enjoined the Internal Revenue Service from enforcing the regulatory requirements for registered tax return preparers. In accordance with this order, tax return preparers covered by this program are not required to complete competency testing or secure continuing education. The ruling does not affect the regulatory practice requirements for CPAs, attorneys, enrolled agents, enrolled retirement plan agents or enrolled actuaries or the continuing professional education requirements of individual states.

On February 1, 2013, the court modified its order to clarify that the order does not affect the requirement for all paid tax return preparers to obtain a preparer tax identification number (PTIN). IRS regulations still require all paid tax return preparers (including attorneys, CPAs, and enrolled agents) to apply for a Preparer Tax Identification Number (PTIN) before preparing any future Federal tax returns.

In 2017, the United States District court for the District of Columbia upheld the Internal Revenue Service's authority to require the use of a Preparer Tax Identification Number (PTIN), but enjoined the IRS from charging a user fee for the issuance and renewal of PTINs. In 2019, the D.C. Circuit reversed the district court decision invalidating the fee charged by the IRS to tax return preparers for obtaining a PTIN. The D.C. Circuit concluded that the IRS acted within its authority and was not arbitrary and capricious in implementing the PTIN fee and remanded to the district court for an assessment of whether the amount of the fee is excessive.

The PTIN application process may be completed online. Form W-12 - IRS Paid Preparer Tax Identification Number Application and Renewal, is available for paper applications and renewals, but takes four to six weeks to process. A tax preparer must renew his or her PTIN every year during the renewal season. The renewal season generally runs from mid-October to December 31. The renewal process can be completed online and only takes a few moments. Failure to have and use a valid PTIN may result in penalties. All enrolled agents, regardless of whether they prepare returns, must have a PTIN in order to maintain their status.

Electronic Filing Identification Number (EFIN)

The IRS assigns an EFIN to identify firms that have completed the IRS e-file Application to become an Authorized IRS e-file Provider. After the provider completes the application and passes a suitability check, the IRS sends an acceptance letter, including the EFIN, to the provider. Providers need the EFIN to electronically file tax returns. The firm owns the EFIN. The principals of the firm use either their Social Security Number or Employer Identification Number to apply for an EFIN. On their application, the firm's "Doing Business As" name and business address should be used, not a personal address.

Authorized IRS e-file Providers do not have to reapply each year as long as they continue to e-file returns. However, if a Provider does not e-file returns for two consecutive years, the IRS will notify the Provider of removal from the IRS active Provider list. The IRS may reactivate a Provider if the Provider replies within sixty days and requests reactivation. Otherwise, the Provider will have to complete and submit a new application.

Providers must update their application information within 30 days of the date of any changes to the information on their current application. Make all changes using the IRS e-file Application. See Changes to Your IRS e-file Application. The EFIN is not transferable, and neither is the password. Even if an Authorized IRS e-file Provider transfers his or her business by sale, gift or other disposition, he or she may not transfer his or her EFIN. The Provider must protect his or her EFINS, Electronic Transmitter Identification Numbers (ETINs) and passwords from unauthorized use.

Review Question 9

All of the following are return preparers who can obtain the AFSP - Record of Completion without taking the AFTR course except:

A. Anyone who passed the Registered Tax Return Preparer test administered by the IRS between November 2011 and January 2013
B. Tax practitioners who have passed the Special Enrollment Exam Part I within the past two years
C. Non-credentialed tax return preparers who previously participated in continuing professional education (CPE) courses
D. Return preparers who are active registrants of the Oregon Board of Tax Practitioners or the California Tax Education Council

See Review Feedback for answer.

Identity Theft

Identity theft occurs when another person uses the taxpayer's personal information such as his or her name, Social Security number (SSN) or other identifying information, without the taxpayer's permission, to commit fraud or other crimes. Usually, an identity thief utilizes a legitimate taxpayer's identity to fraudulently file a tax return and claim a refund. Generally, the identity thief will use a stolen SSN to file a forged tax return and try to get a fraudulent refund early in the filing season. The taxpayer may not be aware that an identity theft has happened to him or her until he or she files a return later in the filing season and discovers that two returns have been filed using the same SSN. The taxpayer should be alert to possible identity theft if he or she gets an IRS notice or letter stating: [29]

- More than one tax return for the taxpayer was filed.
- The taxpayer has a balance due, a refund offset, or has had collection actions taken against him or her for a year he or she did not file a tax return.
- IRS records indicate the taxpayer received wages from an employer unknown to him or her.

If the taxpayer receives a notice from the IRS, respond immediately. If he or she believes someone may have used his or her SSN fraudulently, the taxpayer should notify the IRS immediately by responding to the name and number printed on the notice or letter. The taxpayer will need to fill out the Form 14039 - Identity Theft Affidavit.

Safeguarding Taxpayer Data

Federal law requires tax preparers to create and follow a written information security plan to protect their clients' data. Tax professionals should review Publication 4557 - Safeguarding Taxpayer Data. It details critical security measures that all tax professionals should enact. The publication also includes information on how to comply with the Federal Trade Commission (FTC) Safeguards Rule, including a checklist of items for a prospective data security plan. Tax professionals are asked to focus on key areas such as employee management and training; information systems; and detecting and managing system failures.

The FTC-required information security plan must be appropriate to the company's size and complexity, the nature and scope of its activities and the sensitivity of the customer information it handles. According to the FTC, each company, as part of its plan, must:

- Designate one or more employees to coordinate its information security program.
- Identify and assess the risks to customer information in each relevant area of the company's operation and evaluate the effectiveness of the current safeguards for controlling these risks.
- Design and implement a safeguards program and regularly monitor and test it.
- Select service providers that can maintain appropriate safeguards, make sure the contract requires them to maintain safeguards and oversee their handling of customer information.
- Evaluate and adjust the program in light of relevant circumstances, including changes in the firm's business or operations, or the results of security testing and monitoring.

The FTC says the requirements are designed to be flexible so that companies can implement safeguards appropriate to their own circumstances. The Safeguards Rule requires companies to assess and address the risks to customer information in all areas of their operations.

Note: The FTC currently is re-evaluating the Safeguards Rule and has proposed new regulations. Tax professionals should be alert to any changes in the Safeguards Rule and its effect on the tax preparation community.

Identity Protection Personal Identification Number (IP PIN)

If a taxpayer received an IRS notice providing him or her with an Identity Protection Personal Identification Number (IP PIN), enter it in the IP PIN spaces provided below daytime phone number on the tax return form. The taxpayer must enter the IP PIN exactly as it is shown on the Notice CP01A. If the taxpayer did not receive a notice containing an IP PIN, leave these spaces blank.

An IP PIN is a number the IRS gives to taxpayers who have:

- Reported to the IRS they have been victims of identity theft.
- Given the IRS information that verifies their identity.
- Had an identity theft indicator applied to their account.

Note: The IP PIN helps to prevent the misuse of a taxpayer's Social Security number or Taxpayer Identification Number on income tax returns. New IP PINs are issued every year. An IP PIN should be used only for the tax year it was issued. IP PINs for 2022 tax returns generally will be sent in December 2021. A new IP PIN will be issued every year for three years after the identity theft incident. If the taxpayer is filing a joint return and both taxpayers receive an IP PIN, only the taxpayer whose Social Security number (SSN) appears first on the tax return should enter his or her IP PIN.

Individual Taxpayer Identification Numbers (ITIN)

In January of 2013, the IRS implemented new procedures that affect the Individual Taxpayer Identification Number (ITIN) application process.

The information below highlights improvements to the ITIN program: (30)

- If the taxpayer is applying directly to the IRS for an ITIN, they will only accept original identification documents or certified copies of these documents from the issuing agency along with a completed Form W-7 - Application for IRS Individual Taxpayer Identification Number and Federal tax return.
- In addition to direct submission of documents to the IRS centralized site or use of Certifying Acceptance Agents (CAAs), ITIN applicants will have several other avenues for verification of key documents. These options include some key IRS Taxpayer Assistance Centers (TACs), U.S. Tax Attachés in London, Paris, Beijing, and Frankfurt and at Low-Income Taxpayer Clinics (LITCs) and Volunteer Income Tax Assistance (VITA) Centers that use CAAs.
- New ITINs will now be issued for a five-year period rather than an indefinite period. This change will help ensure that ITINs are being used for legitimate tax purposes.
- There are four exceptions to this new documentation requirement. Applicants who are not impacted by these changes include:
    - U.S. military spouses and U.S. military dependents.
    - Non-resident aliens applying for ITINs for the purpose of claiming tax treaty benefits.
    - Noncitizens that have approved TY 2011 extensions to file their tax returns. These are temporary ITINs.
    - Student Exchange Visitors Program (SEVP) participants.

The IRS issues ITINs to foreign nationals and others who have Federal tax reporting or filing requirements and do not qualify for SSNs. A non-resident alien individual not eligible for an SSN who is required to file a U.S. tax return only to claim a refund of tax under the provisions of a U.S. tax treaty needs an ITIN.

Other examples of individuals who need ITINs include: (31)

- A nonresident alien required to file a U.S. tax return.
- A U.S. resident alien (based on days present in the United States) filing a U.S. tax return.
- A dependent or spouse of a U.S. citizen/resident alien.
- A dependent or spouse of a nonresident alien visa holder.

The IRS processes returns showing SSNs or ITINs in the blanks where tax forms request SSNs. IRS no longer accepts, and will not process, forms showing "SSA205c," "applied for," "NRA," blanks, etc.

All ITINs not used on a Federal tax return at least once in the last three consecutive years and those with middle digits of 88 will no longer be valid for use on a tax return as of December 31, 2020. In addition, ITINs with middle digits of 90, 91, 92, 94, 95, 96, 97, 98 or 99 (Example: 9NN-90-NNNN) that were assigned before 2013 will need to be renewed if the taxpayer will have a filing requirement in 2021. No action is needed by ITIN holders who do not need to file a tax return next year. Also, there are new documentation requirements when applying for or renewing an ITIN for certain dependents.

If taxpayers have an expired ITIN and do not renew before filing a tax return next year, they could face a refund delay and may be ineligible for certain tax credits, such as the Child Tax Credit and the American Opportunity Tax Credit, until the ITIN is renewed. The ITIN changes are required by the Protecting Americans from Tax Hikes (PATH) Act enacted by Congress in December 2015. The IRS emphasizes that no action is needed by ITIN holders if they do not need to file a tax return next year.

Taxpayers with ITINs set to expire at the end of the year and who need to file a tax return in 2021 must submit a renewal application. Others do not need to take any action.

- ITINs with middle digits 90, 91, 92, 94, 95, 96, 97, 98 or 99 (For example: 9NN-90-NNNN) need to be renewed if the taxpayer will have a filing requirement in 2021.
- Those who must renew their ITIN can choose to renew their family's ITINs together, even if family members have an ITIN with middle digits other than 90, 91, 92, 94, 95, 96, 97, 98 or 99. Family members include the tax filer, spouse and any dependents claimed on the tax return.
- Taxpayers whose ITINs expired due to lack of use should only renew their ITIN if they will have a filing requirement in 2021.
- Taxpayers who are eligible for, or who have, a Social Security number (SSN) should not renew their ITIN but should notify IRS both of their SSN and previous ITIN, so that their accounts can be merged.

A taxpayer whose ITIN has been deactivated and needs to file a U.S. return can reapply using Form W-7 - Application for IRS Individual Taxpayer Identification Number. As with any ITIN application, original documents, such as passports, or copies of documents certified by the issuing agency must be submitted with the form.

IRS Direct Pay

IRS Direct Pay is a payment application that allows individual taxpayers with a valid Social Security Number to make IRS payments directly from their checking or savings accounts. It is free, secure and provides an electronic payment confirmation while reducing processing costs. Only Form 1040 payments and associated penalties can be made through IRS Direct Pay.

The taxpayer must have a valid Social Security Number (SSN) to use this application. This application cannot accommodate Individual Taxpayer Identification Numbers (ITINs).

IRS Direct Pay currently accepts 1040 series payments, including the 4868 (1040 Extension) and the 1040-ES (1040 Estimated Tax). Direct Pay will also accept form 5329 payments and Shared Responsibility payments. Other form types may be added in the future.

A taxpayer can make a tax payment towards a 1040 tax return for the last 20 years for most of the Reason for Payment options found on irs.gov. There are two exceptions: Estimated Tax Payments and Requests for Extension of Time to File. Estimated Tax Payments are paid to the IRS in the current calendar year, while Requests for Extension of Time to File payments are generally for the current tax year.

Taxpayers receive instant confirmation that the payment has been submitted, and the system is available 24 hours a day, 7 days a week. Bank account information is not retained in any IRS systems after payments are completed. IRS Direct Pay also offers 30-day advance payment scheduling, payment rescheduling or cancellations, and a payment status search. Future plans include an option for e-mailed payment confirmation, a Spanish version and one-time registration with a login and password to allow quick access on return visits.

Installment Agreements

The fee schedule applies to installment agreements entered into, restructured, or reinstated on or after January 2, 2017. The final regulations increase the existing user fees (except for low-income taxpayers) and create two new types of online installment agreements, each subject to a separate fee. Five of these rates are based on the full cost of establishing and monitoring installment agreements, while the sixth rate is for low-income taxpayers. The new fees are:

1. A top rate of $225 applies to taxpayers who enter into installment agreements in person, over the phone, by mail, or by filing Form 9465 - Installment Agreement Request, with the IRS. This includes taxpayers requesting installment agreements with their e-filed returns.
2. A reduced rate of $107 applies to a direct debit agreement for taxpayers who apply by phone, mail, or in-person.
3. A taxpayer who sets up an installment agreement through IRS.gov and agrees to make payments either by mailing a check or through the Electronic Federal Tax Payment System (EFTPS) will pay $149.
4. A taxpayer who sets up an installment agreement online and agrees to make automatic payments through direct debit will pay a $31 fee.
5. The fee for a restructured/reinstated installment agreement completed online is $10. The fee for a restructured/reinstated installment agreement completed by phone, mail or in-person is $89.
6. A low-income taxpayer pays a $43 fee, when setting up any type of installment agreement, other than a direct debit online payment agreement or when restructuring or reinstating any installment agreement.

Taxpayers with income at or below 250% of the Department of Health and Human Services poverty guidelines may apply for a reduced user fee of $43.

Paid Preparer's Due Diligence Checklist

The due diligence requirement was originally designed to reduce errors on returns claiming the Earned Income Tax Credit (EITC). Legislation in 2015 expanded the due diligence requirements to include the Child Tax Credit (CTC), Additional Child Tax Credit (ACTC), and American Opportunity Tax Credit (AOTC). Under the Tax Cuts and Jobs Act (TCJA), the due diligence requirement now also applies to individual income tax returns claiming the head of household (HOH) filing status and Credit for Other Dependents (ODC).

Paid tax preparers must submit Form 8867 - Paid Preparer's Due Diligence Checklist with every tax return claiming any of the covered tax benefits. The form is designed as a checklist to help paid preparers meet the requirement by obtaining eligibility information from their clients. Paid preparers are required to keep copies of the form or comparable documentation for their records, which is also subject to review by the IRS. Completing the form is not a substitute for actually performing the necessary due diligence and completing all required forms and schedules when preparing the return.

Also, the paid tax return preparer due diligence penalty under IRC Section 6695(h) is now indexed for inflation. Therefore, the penalty for failure to meet the due diligence requirements with respect to returns and claims for refund filed in 2021 is $545 per credit per return.

A paid tax return preparer is required to exercise due diligence when preparing any client's return or claim for refund. As part of exercising due diligence, the tax preparer must interview the client, ask adequate questions, and obtain appropriate and sufficient information to determine correct reporting of income, claiming of tax benefits (such as deductions and credits), and compliance with the tax laws.

A paid tax return preparer must meet specific due diligence requirements set forth in Treasury Regulations when he or she prepares returns and claims for refund involving the HOH filing status, EITC, the AOTC and/or the CTC/ACTC/ODC. To meet these due diligence requirements, the tax preparer may need to ask additional questions and obtain additional information to determine eligibility for and the amount of the HOH filing status, EITC, AOTC, and CTC/ACTC/ODC. [32]

Fixing America's Surface Transportation (FAST) Act

The Fixing America's Surface Transportation (FAST) Act was signed into law in December 2015. The purpose of the FAST Act was to provide long-term funding for transportation projects, including new highways. Also included in the bill was a new tax law that requires the Department of State to deny a passport (or renewal of a passport) to a seriously delinquent taxpayer or revoke any passport previously issued to a seriously delinquent taxpayer. For purposes of the law, a "seriously delinquent tax debt" is defined as "an unpaid, legally enforceable Federal tax liability" when a debt greater than $54,000 for 2021, including interest and penalties, has been assessed and a notice of lien or a notice of levy has been filed. The limit is adjusted each year for inflation and cost of living. The limit is not per year but cumulative meaning that it is the total tax debt that matters.

There are some exceptions under the law. Tax debt which is being paid on time as part of an installment agreement or under an Offer In Compromise does not count. It also does not include any tax debt for which a Collection Due Process hearing is timely requested in connection with a levy or a debt where the collection has been suspended due to an innocent spouse claim.

If the taxpayer is seriously delinquent under the law, the IRS is required to notify him or her in writing at the time that it certifies the debt to the State Department. The State Department will then hold his or her passport application or renewal for 90 days to allow the taxpayer to resolve any errors, make full payment, or enter into a satisfactory payment plan. There is no grace period for resolving the debt before the State Department revokes an existing passport. To get off the list, the taxpayer must prove that the debt is fully satisfied, is legally unenforceable or is not seriously delinquent tax debt under the statute.

Review Feedback

Review feedback provides both the answers to each question and an explanation or feedback as to how we arrived at each answer at the end of the lesson. Review feedback also contains evaluative feedback explaining why incorrect answers are wrong. You are also provided the course topic from which we derived our answer and the external source material we used for verification.

If you are using the online version of the course, Ctrl+click on the topic to find the section from which we arrived at the answer for the question. You can also Ctrl+click on the question number to return to the specific review question.

Question 1 - C. Alimony Deduction
Under the Tax Cuts and Jobs Act, the deductions for student loan interest and out-of-pocket teacher expenses will be retained with the current caps. The alimony deduction (Choice C) is repealed. The change applies to any divorce or separation instrument executed or modified after December 31, 2018 (the modification must expressly state that the new rule applies).

The educator expenses deduction, student loan interest deduction, health savings account (HSA) deduction, IRA deduction and deductions for self-employed taxpayers all stay the same.

Topic - Changes to Above-the-line Deductions
Source - Topic 452 - Alimony

Question 2 - D. The taxpayer will lose his or her HSA with a job change
There are three major tax advantages to a taxpayer's Health Saving Account (HSA):

1. Cash contributions to an HSA are 100% deductible from his or her Federal gross income (within legal limits) (Choice A).
2. Interest on savings accumulates tax deferred (Choice B).
3. Withdrawals from an HSA for "qualified medical expenses" are free from Federal income tax (Choice C).

Also, the taxpayer's HSA can follow him or her as he or she changes employment therefore Choice D is false and the correct answer.

Topic - Health Savings Account (HSA)
Source - Publication 969 - Health Savings Accounts and Other Tax-Favored Health Plans

Question 3 - D. $16,500
The amount an employee contributes from their salary to a SIMPLE IRA cannot exceed $13,500 in 2021. If permitted by the SIMPLE IRA plan, participants who are age 50 or over at the end of the calendar year can also make catch-up contributions. The catch-up contribution limit for SIMPLE IRA plans is $3,000 in 2021. Therefore, Choice D is the correct response as only it contains the correct dollar amount of $16,500 ($13,500 + $3,000).

Topic - Contribution Limits
Source - Retirement Topics - SIMPLE IRA Contribution Limits

Question 4 - C. Social Security benefits
Wages, unemployment compensation; operating income from a non-passive business, Social Security Benefits (Choice C), alimony, tax-exempt interest, self-employment income, Alaska Permanent Fund Dividends (see Revenue Ruling 90-56, 1990-2 CB 102) and distributions from certain Qualified Plans are some common types of income that are not Net Investment Income. In general, investment income includes, but is not limited to interest (Choice A), dividends (Choice B), capital gains (Choice D), rental and royalty income, non-qualified annuities, income from businesses involved in trading of financial instruments or commodities, and businesses that are passive activities to the taxpayer.

Topic - Net Investment Income Tax
Source - Questions and Answers on the Net Investment Income Tax

Question 5 - C. $142,800
If the taxpayer's only income is from self-employment, the Social Security maximum is still in effect. That is, the Social Security portion of his or her self-employment tax is capped at the maximum profit of the company, depending on the maximum for that year.

In this example, if the taxpayer has only self-employment, and the net earnings on his or her Schedule C is $158,000 for 2021, he or she would only be taxed for self-employment tax on the 2021 maximum of $142,800. Therefore, Choice C is the correct response as only it contains the correct dollar amount.

Topic - Social Security and Medicare Tax
Source - Self-Employment Tax (Social Security and Medicare Taxes)

Question 6 - D. 100% of the purchase price
Section 179 of the IRS Tax Code allows a business to deduct, for the current tax year, the full purchase price of financed or leased equipment and off-the-shelf software that qualifies for the deduction. Therefore, Choice D, 100% of purchase price, is the only correct response. Also, the equipment purchased, financed or leased must be within the specified dollar limits of Section 179, and the equipment must be placed into service in the same tax year that the deduction is being taken.

Topic - Section 179 Deduction
Source - Section 179 FAQ's

Question 7 - B. $10,000
The dollar limitation applies separately to both the credit and the exclusion, and the taxpayer may be able to claim both the credit and the exclusion for qualified expenses. However, he or she must claim any allowable exclusion before claiming any allowable credit. Expenses used for the exclusion reduce the amount of qualified adoption expenses available for the credit. As a result, the taxpayer cannot claim both a credit and an exclusion for the same expenses. In this question, the expenses allowable for the Adoption Credit are limited to $10,000 (Choice B) ($13,190 total expenses paid less $3,190 employer reimbursement).

Topic - Adoption Credit and Exclusion
Source - Topic 607 - Adoption Credit and Adoption Assistance Programs

Question 8 - A. $0
To qualify for the unlimited exclusion for qualified education expenses, the taxpayer must make a direct payment to the educational institution for tuition only. Books, supplies and living expenses do not qualify. If the taxpayer wants to pay for books, supplies and living expenses in addition to the unlimited education exclusion, he or she can make a 2021 gift of $15,000 to the student under the annual gift exclusion. In this case neither payment is reportable for gift tax purposes. Therefore, only Choice A contains the correct amount of $0.

Topic - Gift and Estate Tax
Source - Publication 559 - Survivors, Executors, and Administrators - Estate and Gift Tax

Question 9 - C. Non-credentialed tax return preparers who previously participated in continuing professional education (CPE) courses
Return preparers who can obtain the AFSP – Record of Completion without taking the AFTR course are:

- Anyone who passed the Registered Tax Return Preparer test administered by the IRS between November 2011 and January 2013 (Choice A).
- Established state-based return preparer program participants currently with testing requirements: Return preparers who are active registrants of the Oregon Board of Tax Practitioners, California Tax Education Council, and/or Maryland State Board of Individual Tax Preparers (Choice B).
- SEE Part I Test-Passers: Tax practitioners who have passed the Special Enrollment Exam Part I within the past two years (Choice D).
- VITA volunteers: Quality reviewers and instructors with active PTINs.
- Other accredited tax-focused credential-holders: The Accreditation Council for Accountancy and Taxation's Accredited Business Accountant/Advisor (ABA) and Accredited Tax Preparer (ATP) programs.

The Annual Filing Season Program is intended to recognize and encourage the voluntary efforts of non-credentialed tax return preparers to increase their knowledge and improve their filing season competency through continuing education. Therefore, Choice C is false and the correct response.

Topic - Annual Filing Season Program (AFSP)
Source - Frequently Asked Questions: Annual Filing Season Program

Accrual method of accounting: The accounting method under which revenues are recognized on the income statement when they are earned (rather than when the cash is received).

Adjusted gross income (AGI): Gross income minus adjustments to income.

Alternative minimum tax (AMT): An income tax imposed by the United States Federal government on individuals, corporations, estates, and trusts. AMT is imposed at a nearly flat rate on an adjusted amount of taxable income above a certain threshold (also known as exemption). This exemption is substantially higher than the exemption from regular income tax.

Attorney: Any person who is a member in good standing of the bar of the highest court of any state, territory or possession of the United States, including a Commonwealth and the District of Columbia.

Basis: Generally, the amount of the taxpayer's capital investment in a property for tax purposes. The taxpayer uses his or her basis to figure depreciation, amortization, depletion, casualty losses, and any gain or loss on the sale, exchange or other disposition of the property.

Cash method of accounting: The accounting method that recognizes revenues and expenses at the time physical cash is actually received or paid out.

Certified Public Account: Any person who is duly qualified to practice as a certified public accountant in any state, territory or possession of the United States, including a Commonwealth and the District of Columbia.

Client: Any person or entity, other than an employer, that engages a practitioner or practitioner's firm to perform professional services.

Commissioner: The Commissioner of the Internal Revenue Service.

Confidential client information: Any information disclosed by the client that is not available to the public.

Depreciation: An income tax deduction that allows a taxpayer to recover the cost or other basis of certain property. It is an annual allowance for the wear and tear, deterioration, or obsolescence of the property.

Earned income: All the taxable income and wages a taxpayer gets from working or from certain disability payments. The two ways a taxpayer can get earned income are working for someone who pays him or her or owning or running a business or farm. Taxable earned income includes wages, salaries, tips, and other taxable employee pay, union strike benefits, long-term disability benefits received prior to minimum retirement age and net earnings from self-employment.

Enrolled Agent: Any individual who is enrolled under the provisions of Treasury Department Circular 230 to practice before the IRS.

Expatriate: (often shortened to expat) is a person temporarily or permanently residing, as an immigrant, in a country other than that of their citizenship. The expatriation tax provisions under Internal Revenue Code (IRC) Sections 877 and 877A apply to U.S. citizens who have renounced their citizenship and long-term residents (as defined in IRC 877(e)) who have ended their U.S. resident status for Federal tax purposes.

Filing status: Used to determine a taxpayer's filing requirements, standard deduction, eligibility for certain credits, and his or her correct tax. There are five filing statuses: Single, Married Filing Jointly, Married Filing Separately, Head of Household and Qualifying Widow(er) with Dependent Child.

Gross income: All income from any sources a taxpayer derives.

Head of household: One of five filing status options from which a taxpayer must chose when filing his or her taxes. To qualify for the head of household filing status the taxpayer must be unmarried or considered unmarried on the last day of the year, have paid more than half the cost of keeping up a home for the year and have had a qualifying person live with him or her in the home for more than half the year (except for temporary absences, such as school). However, if the qualifying person is the taxpayer's dependent parent, he or she does not have to live with taxpayer.

Health Insurance Marketplace: Also known as the Exchange, is the place where an individual will find information about private health insurance options, purchase health insurance, and obtain help with premiums and out-of-pocket costs if he or she is eligible.

Household income: Household income is the taxpayer's modified adjusted gross income (MAGI) plus the MAGI of each individual in his or her tax household whom the taxpayer claims as a dependent and who is required to file his or her own tax return.

Identity theft: Occurs when someone uses the taxpayer's personal information such as his or her name, Social Security number (SSN) or other identifying information, without his or her permission, to commit fraud or other crimes.

Income tax: is a government levy (tax) imposed on individuals or entities (taxpayers) that varies with the income or profits (taxable income) of the taxpayer.

Itemized deduction: An itemized deduction is an eligible expense that individual taxpayers in the United States can report on their Federal income tax returns in order to decrease their taxable income. Most taxpayers are allowed a choice between the itemized deductions and the standard deduction.

Medicare: The Federal health insurance program for people who are 65 or older, certain younger people with disabilities, and people with End-Stage Renal Disease (permanent kidney failure requiring dialysis or a transplant, sometimes called ESRD).

Minimum value standards: A health plan meets this standard if it is designed to pay at least 60% of the total cost of medical services for a standard population. Starting in 2014, individuals offered employer-sponsored coverage that provides minimum value and that is affordable will not be eligible for a Premium Tax Credit.

Necessary expense: Expense that is helpful and appropriate for the taxpayer's business. An expense does not have to be required to be considered necessary**.**

Ordinary expense: Expense that is common and accepted in the taxpayer's field of trade, business, or profession.

Personal exemption: The now defunct exemption was a tax deduction composed of amounts for the individual taxpayer, the taxpayer's spouse, and the taxpayer's child. The personal exemption was deducted against the taxpayer's income to arrive at the taxable income - the amount against which the tax rates are applied to compute the total tax liability.

Placed in service: The point in time when an asset that can be depreciated is first placed in use. The date the asset is placed in service marks the beginning of the depreciation period. The date of purchase usually marks when an asset is placed in service.

Practice before the Internal Revenue Service: All matters connected with a presentation to the IRS or any of its offices or employees relating to a taxpayer's rights, privileges or liabilities under laws or regulations administered by the IRS. Such presentations include, but are not limited to, preparing and filing documents, corresponding and communicating with the IRS, rendering written advice with respect to any entity, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion, and representing a client at conferences, hearings and meetings.

Practitioner: Generally, an attorney, CPA, enrolled agent, or enrolled actuary authorized to practice before the IRS. Other individuals may qualify to practice temporarily or engage in limited practice before the IRS, however, they are not referred to as practitioners.

Qualifying child: May enable a taxpayer to claim several tax benefits, such as head of household filing status, the exemption for a dependent, the child tax credit, the child and dependent care credit and the earned income tax credit. In general, to be a taxpayer's qualifying child, a person must satisfy four tests: relationship, residence, age and support.

Qualifying relative: Four tests must be met for a person to be a taxpayer's qualifying relative. The four tests are: not a qualifying child test, member of household or relationship test, gross income test and support test. Unlike a qualifying child, a qualifying relative can be any age. There is no age test for a qualifying relative.

Recapture: The procedure for collecting income tax on a gain realized by a taxpayer when the taxpayer disposes of an asset that had previously provided an offset to ordinary income for the taxpayer through depreciation.

Recognized representative: An individual who is recognized to practice before the IRS.

Same-sex marriage: Marriage between two people of the same biological sex and/or gender identity. For Federal tax purposes, the IRS looks to state or foreign law to determine whether individuals are married. The IRS has a general rule recognizing a marriage of same-sex spouses that was validly entered into in a domestic or foreign jurisdiction whose laws authorize the marriage of two individuals of the same sex even if the married couple resides in a domestic or foreign jurisdiction that does not recognize the validity of same-sex marriages. For tax year 2013 and going forward, same-sex spouses generally must file using a married filing separately or jointly filing status.

Service: The Internal Revenue Service

Social Security: The foundation of economic security for millions of Americans - retirees, disabled persons, and families of retired, disabled or deceased workers. About 158 million Americans pay Social Security taxes and 57 million collect monthly benefits. About one household in four receives income from Social Security.

Standard deduction: A dollar amount that reduces the amount of income on which taxpayers are taxed. In general, the standard deduction is adjusted each year for inflation and varies according to the taxpayer's filing status. A taxpayer cannot take the standard deduction if he or she itemizes deductions.

Tax household: A tax household generally includes the taxpayer, his or her spouse (if filing a joint return), and any individual he or she claims as a dependent on his or her tax return. It also generally includes each individual the taxpayer can, but does not, claim as a dependent on his or her tax return.

Tax return: Reports filed with the IRS or with the state or local tax collection agency containing information used to calculate income tax or other taxes. Tax return also includes an amended tax return and a claim for refund.

Tax year: An annual accounting period for keeping records and reporting income and expenses.

Unenrolled return preparer: An individual other than an attorney, CPA, enrolled agent, enrolled retirement plan agent, or enrolled actuary who prepares and signs a taxpayer's return as the preparer, or who prepares a return but is not required (by the instructions to the return or regulations) to sign the return.

Unemployment compensation: Any amounts received under the unemployment compensation laws of the United States or of a state. It includes state unemployment insurance benefits and benefits paid to a taxpayer by a state or the District of Columbia from the Federal Unemployment Trust Fund. It also includes railroad unemployment compensation benefits, but not worker's compensation.

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A

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C

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E

F

Examination Instructions - 3 Hour Federal Tax Updates

Earning your CPE credits from a self-study course is contingent upon scoring 70% or higher on the exam questions related to the course material. This examination covering Federal tax law updates consists of 15 multiple-choice questions, meaning you must correctly answer 11 in order to pass.

The exam has no time limit, and is open book, so you are allowed to look up answers in the text we provide. You do not need to finish the exam in one continuous sitting as all of the answers you enter online are automatically saved. Please keep in mind, it is necessary to click the “Next” button after changing an incorrect or unanswered question to save the new response. After you submit the online exam to us you will receive a pass/fail message.

If you should fail the exam on your first attempt, you will have the option to re-take the exam at no additional cost. If you score less than 70%, a message will be displayed at the bottom of the page along with a list of incorrect questions. You have unlimited attempts to pass an exam.

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*** Important: Your PTIN and name must match EXACTLY what is in the IRS system.**

Examination Questions - 3 Hour Federal Tax Updates

1. The standard deduction is increased for individuals who are age 65 and older and/or which of the following?
   A. Receiving unemployment compensation
   B. Retired from the military
   C. A beneficiary of a trust
   D. Blind

2. Which of the following is a false statement regarding a Flexible Spending Account (FSA) (also known as a flexible spending arrangement)?
   A. The taxpayer does not have to pay taxes on money put into an FSA that he or she uses to pay for certain out-of-pocket health care costs
   B. The taxpayer can use funds in his or her FSA to pay for copayments and deductibles
   C. The taxpayer can use FSA funds to pay for insurance premiums
   D. Employers may make contributions to the taxpayer's FSA

3. Violette buys a family health insurance coverage plan in 2021. The annual deductible for the family plan is $5,500. To be eligible to pair this family plan with her Health Savings Account (HSA) and allow her to contribute tax-advantaged dollars to the account the family plan must qualify as a high deductible health plan (HDHP). To qualify as an HDHP, Violette's family coverage plan must have an out-of-pocket limit for the minimum annual deductible of what amount?
   A. $1,400
   B. $2,800
   C. $7,000
   D. $7,200

4. John, 42, has both a traditional IRA and a Roth IRA. His taxable income is $57,000. Therefore, during 2021 he can only contribute a total of what amount to both of his IRAs?
   A. $0
   B. $1,000
   C. $5,500
   D. $6,000

5. Jordan, age 42, received a $10,000 eligible rollover distribution from her retirement plan. Her employer withheld $2,000 from her distribution. Within 60 days, Jordan decides to roll over the $8,000, but she does not contribute the $2,000 withheld by her employer to the new plan. Jordan will report what amount as taxable income on her tax return?
   A. $0
   B. $1,000
   C. $2,000
   D. $10,000

6. The Setting Every Community Up for Retirement Enhancement (SECURE) Act expanded Section 529 education savings accounts to cover costs associated with all of the following except:
   A. Registered apprenticeships
   B. Homeschooling
   C. Clubs sports programs
   D. Up to $10,000 of qualified student loan repayments

7. Which of the following statements is correct regarding Form 8995 - Qualified Business Income (QBI) Deduction Simplified Computation?
   A. C corporations should complete the Form 8995 in order to claim the Qualified Business Income Deduction on their corporate returns
   B. Taxpayers will receive the Form 8995 from the IRS, if they are determined to be eligible for the deduction
   C. A single individual with qualified business income (QBI) whose taxable income before the QBI deduction is less than or equal to $164,900 should generally use the form
   D. A partnership is required to attach Form 8995 to their partnership tax return in order to claim the deduction

8. The Setting Every Community Up for Retirement Enhancement (SECURE) Act modified the tax rates and brackets that the taxpayer will use to figure the Tax for Certain Children Who Have Unearned Income (Kiddie Tax) on his or her 2021 unearned income. Under the SECURE Act, all of a child's net unearned income over a threshold amount is taxed using the brackets and rates for which of the following?
   A. Capital gains
   B. Child's parents
   C. Estates and trusts
   D. Partnerships

9. Which of the following is an incorrect statement regarding Bonus Depreciation?
   A. Bonus Depreciation is useful to very large businesses spending more than the Section 179 spending limit
   B. Businesses with a net loss in a given tax year qualify to carry-forward the Bonus Depreciation to a future year
   C. Bonus Depreciation only covers new equipment
   D. When applying these provisions, Section 179 is generally taken first, followed by Bonus Depreciation

10. If the taxpayer has a dependent that he or she cannot claim for the Child Tax Credit, the dependent may still qualify him or her for which $500 credit?
   A. The Alternative Minimum Tax Credit
   B. The State and Local Income Tax Credit
   C. The Credit for Other Dependents
   D. The Credit for Foreign Dependents

11. In 2021, Wesley Pickett has a modified adjusted gross income (MAGI) of $58,500. During the year he paid $5,000 of student loan interest. What amount can Wesley deduct from his taxable income for the interest paid on his student loan?
   A. $0
   B. $1,000
   C. $2,500
   D. $5,000

12. The Consolidated Appropriations Act, 2021, repeals the Tuition and Fees Deduction, effective with tax years that begin in 2021. This is a permanent repeal so the Tuition and Fees Deduction will not return with future tax extenders. Instead, the phase-out limits for which of the following are increased to $80,000 ($160,000 for married filing jointly)?
   A. Student Loan Interest Deduction
   B. Lifetime Learning Credit
   C. Deduction for Educator Expenses
   D. Coverdell Education Savings Account (CESA)

13. Curtis and Norma are married and file jointly. Curtis contributed $1,000 to his 401(k) plan in 2021. Norma contributed $1,000 to an IRA in 2021. Their 2021 combined adjusted gross income is $33,500. What amount are Curtis and Norma eligible to claim for the Credit for Qualified Retirement Savings Contributions (Saver's Credit) on their income tax return?
   A. $0
   B. $100
   C. $500
   D. $1,000

14. Which of the following items can a taxpayer deduct as a charitable contribution?
   A. Out-of-pocket expenses the taxpayer incurs when serving a qualified organization as a volunteer
   B. Dues, fees, or bills paid to country clubs, lodges, fraternal orders, or similar groups
   C. Tuition
   D. Cost of raffle, bingo, or lottery tickets

15. The Consolidated Appropriations Act, 2021 includes an extension of the qualified principal residence indebtedness exclusion through 2025. Typically, when debt is forgiven, the discharged amount is included in a taxpayer's gross income. The provision reduces the maximum amount that may be excluded to what amount?
    - A. $250,000
    - B. $500,000
    - C. $625,000
    - D. $750,000

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CTEC Course Number: 6224-CE-0004

Instructions: Please comment on all of the following evaluation points for this course and select a number grade, using the 1-5 scale, with 5 being the highest.

Were the stated learning objectives met?..	5 4 3 2 1 N/A
Were the course materials accurate and relevant, and did they contribute to the achievement of the learning objectives?..	5 4 3 2 1 N/A
Was the time allocated to learning adequate?..	5 4 3 2 1 N/A
Were the facilities/equipment appropriate (if applicable)?..................................	5 4 3 2 1 N/A
Was the course syllabus or handout materials satisfactory?...............................	5 4 3 2 1 N/A
Were the audio and visual materials effective (if applicable)?.............................	5 4 3 2 1 N/A
If applicable, were individual instructors knowledgeable and effective?	
Instructor (enter name)	5 4 3 2 1 N/A
Instructor (enter name)	5 4 3 2 1 N/A

Number of Hours/Minutes it took you to study and complete course. ☐

Additional comments:

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Part of the course you found *most* beneficial:

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Part of the course you found *least* beneficial:

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Would you like us to contact you about your comments after the course? ☐ YES ☐ NO

Name: ______________________________ Phone: ______________________________

Please complete and include with exam at the conclusion of the course.