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CPE NETWORK TAX REPORT

FEBRUARY 2025 VOLUME 38, ISSUE 2

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Tax Report

Volume 38, Issue 2 **February 2025**

Choose the best response and record your answer in the space provided on the answer sheet.

1. According to Ian Redpath, what did the Fifth Circuit Court of Appeals ultimately decide regarding the nationwide injunction on the Corporate Transparency Act?

   A. It lifted the nationwide injunction permanently.
   B. It deferred to lower court decisions.
   C. It upheld the CTA's immediate enforceability.
   D. It temporarily reinstated the nationwide injunction.

2. According to Ian Redpath, why did the IRS disallow a $23 million deduction for a historic facade easement in the Capital Places II Owner, LLC case?

   A. The building was not in a historic district.
   B. The facade was not certified as historically significant.
   C. The donation did not meet monetary threshold requirements.
   D. The donation occurred after the district lost its historic designation.

3. According to Ian Redpath, what is the IRS standard mileage rate for 2025?

   A. 65 cents per mile
   B. 67 cents per mile
   C. 70 cents per mile
   D. 72 cents per mile

4. According to Ian Redpath, the IRS delayed implementation of certain portions of proposed regulations on required minimum distributions until what year?

   A. 2025
   B. 2026
   C. 2027
   D. 2028

5. According to Ian Redpath, what did the IRS propose under Circular 230 revisions?

   A. Recommending that practitioners establish continuity and succession plans
   B. Mandating practitioners to obtain mental health evaluations
   C. Eliminating the ability to charge contingent fees for refund claims
   D. Penalizing practitioners for cyberattacks on client data

Continued on next page

6. According to Mike Giangrande, what is the filing deadline for 2024 individual tax returns?

   A. March 15, 2025
   B. April 15, 2025
   C. May 15, 2025
   D. June 15, 2025

7. According to Mike Giangrande, what triggers a filing requirement starting in 2024 even without income?

   A. Claiming an advanced vehicle credit at a dealership
   B. Participating in an employer 401(k) plan
   C. Receiving employer dependent care benefits
   D. Participating in a 529 college savings plan

8. According to Mike Giangrande, what is the 2024 unearned income threshold for a child's income to be taxed at their parent's marginal tax rate under Kiddie Tax rules?

   A. $500
   B. $1,000
   C. $2,600
   D. $4,000

9. According to Mike Giangrande, at what percentage are long-term capital gains taxed at for married couples filing jointly with taxable income below $94,050 in 2024?

   A. 0%
   B. 10%
   C. 15%
   D. 20%

10. According to Mike Giangrande, which factor is critical for determining whether a taxpayer qualifies for the foreign earned income exclusion?

    A. Residing in a foreign country for 90 days
    B. Receiving income from a foreign employer
    C. Holding dual citizenship
    D. Having a tax home in a foreign country

Continued on next page

11. According to Mike Giangrande, what is the maximum amount that can be carried over in an FSA to 2025 if the employer allows it?

    A. $640
    B. $1,000
    C. $1,220
    D. $5,000

12. According to Mike Giangrande, what is the child tax credit amount for qualifying children in 2024?

    A. $1,500
    B. $2,000
    C. $2,500
    D. $3,000

13. According to Mike Giangrande, what is the maximum exclusion for dependent care benefits in 2024?

    A. $1,000
    B. $2,000
    C. $3,000
    D. $5,000

14. According to Mike Giangrande, what happens if a taxpayer claims an advanced Clean Vehicle Credit at a dealership but later exceeds the AGI limit?

    A. They keep the credit.
    B. They must repay the credit.
    C. The credit is adjusted based on the taxpayer's new AGI.
    D. They forfeit the vehicle's eligibility for future credits.

15. According to Mike Giangrande, what is the Nanny Tax threshold for 2024, and how does it apply to household employees?

    A. $2,800 for 2024, and it applies only to nannies
    B. $2,700 for 2024, and it applies to all household employees
    C. $2,700 for 2024, and it applies only to nannies
    D. $2,800 for 2024, and it applies only to live-in household employees

EXECUTIVE SUMMARY

PART 1. CURRENT DEVELOPMENTS

The tax landscape is ever changing with new developments or proposals appearing on a regular basis. Practitioners need to be cognizant of changes to properly advise clients. This material covers some of those changes since the last segment. Ian Redpath looks at the latest court rulings on the Corporate Transparency Act and their implications for accountants and their clients. He also examines recent tax court decisions, such as a case addressing deductions for historic preservation easements, and another that scrutinized the business legitimacy of race car expenses as advertising deductions. He delves into proposed regulations and notices, including temporary relief measures for digital asset brokers, updates to transfer pricing methods under Section 482 of the tax code, and proposed changes to Circular 230 rules, including updates to data security policies, business continuity planning, and practitioner competence with technological tools. *[Running time: 47:36]*

Learning Objective:

Upon completion of this segment, the user should be able to:

- Analyze recent tax topics including an update on the latest court rulings on the Corporate Transparency Act, temporary relief for digital asset reporting, updates to transfer pricing methods, and proposed changes to Circular 230 rules.

PART 2. INDIVIDUAL TAXATION

Mike Giangrande, JD, LLM, provides insights into essential individual tax preparation topics for the 2025 filing season. He begins with filing basics, including deadlines, who must file, and the kiddie tax rules. He examines gross income, including exclusions and adjustments, such as capital gains, wash sale rules, the foreign-earned income exclusion, educator expenses, and the student loan interest deduction. Mike covers standard and itemized deductions, tax calculations, and credits, including the Child Tax Credit, Earned Income Credit, education credits, and energy-related incentives. Lastly, he addresses topics such as the premium tax credit, nanny tax, Section 529 qualified expenses, and Section 529 plan rollovers to Roth accounts. *[Running time: 1:21:45]*

Learning Objectives:

Upon completion of this segment, the user should be able to:

- Identify individual federal income tax filing requirements.
- Examine gross income items, exclusions from income, and adjustments to gross income.
- Review the standard deduction, itemized deductions, applicable credits, and address various other tax items.

ABOUT THE SPEAKERS

Ian J. Redpath, JD, LLM, is a nationally recognized tax attorney and consultant from Buffalo, New York, and is a principal in the Redpath Law Offices. Mr. Redpath has published numerous articles on contemporary tax issues and co-authored several books on tax topics. He has extensive national and international experience developing, writing, and presenting professional CPE programs. In addition to his active tax practice, he serves as Chairman of the Department of Accounting, Director of Graduate Accounting Programs, and Professor of Taxation and Forensic Accounting at Canisius College in Buffalo.

Mike Giangrande, JD, LLM, is a California licensed attorney and has been a tax practitioner for over 20 years. He is licensed to practice before the United States Tax Court, has a B.S. in Accounting and an LL.M. (Tax) from Chapman University, and has a J.D. from Whittier Law School with a certificate of concentration in business law. Mike has spent time as an adjunct professor of law at Whittier Law School teaching various tax courses and he served as a member of the Orange County Assessment Appeals Board.

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Learning Objectives (Refer to executive summary)	
Program Description (Refer to executive summary)	
Instructional delivery method	Group Live
Recommended CPE credit	3.0 Credits
Recommended field of study(ies) (Refer to executive summary)	
Program Level	Update
Prerequisites (Circle One)	• Basic Accounting and Auditing professional experience
	• Basic Tax professional experience
	• Basic Governmental professional experience
Advance preparation	None required
Course registration and, where applicable, attendance requirements (1)	

(1) Insert instructions for your students to register for the class and any other attendance requirements (e.g., bring your laptop, be prepared to work in groups, you will be required to sign in and sign out of the session, etc.)

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—From a Declaration of Principles jointly adopted by a *Committee of the American Bar Association* and *Committee of Publishers and Association*

PART 1. CURRENT DEVELOPMENTS

Experts' Forum

Experts' Forum is a popular feature in which we review recent developments in taxation. This month, Ian Redpath looks at the latest court rulings on the Corporate Transparency Act and their implications for accountants and their clients. He also examines recent tax court decisions, such as a case addressing deductions for historic preservation easements, and another that scrutinized the business legitimacy of race car expenses as advertising deductions. He delves into proposed regulations and notices, including temporary relief measures for digital asset brokers, updates to transfer pricing methods under Section 482 of the tax code, and proposed changes to Circular 230, including updates to data security policies, business continuity planning, and practitioner competence with technological tools.

Let's join Ian.

Mr. Ian Redpath

Hi, everybody, welcome to the program. I'm Ian Redpath. This is the segment where we go over a number of things that have happened with the Internal Revenue Service, with the courts, not too much with Congress, but what's been going on since the last time we spoke. So, let's just jump right in and I know it's tax season and you're starting to get really busy. So, I hope tax season is going well so far as you're starting in and that it continues to go well for you.

So, let's jump right in and you know, this seems like an ever never ending story, but it does affect us and it affects our clients in a number of different ways and that is the Corporate Transparency Act and especially as we're going to be affected by it from an accounting standpoint, the BOI, you know, the Beneficial Ownership Rules. Now, the case, you know, there's a number of different cases. So there's a case out of Alabama, there's a case out west, out of Oregon. There's a number of cases actually that are in the district court level.

Initially in Alabama there was a temporary injunction issued. Now a temporary injunction doesn't, it's not on the merits, but the question was the constitutionality of the Corporate Transparency Act. If the Corporate Transparency Act is unconstitutional, then the BOI rules are unconstitutional. So, there was an injunction, but the judge in Alabama said the injunction against enforcement, meaning you don't have to comply with it, apply only to the members of the plaintiff organization, so was somewhat limited. Then we've had some cases in other districts that have said, no, it's constitutional and it, it's enforceable.

So, it, it looked like we had kind of a pendulum swinging that it was going to be upheld as constitutional and then suddenly we get a case out of Texas. Texas Top Cop Shop, Inc. vs. Garland, the Attorney General, and in the district court level, well the court said there's enough to believe that the plaintiffs could be successful, not that they, not that they're going to be, but there was enough to show that they could be successful to issue an injunction. But that judge issued an injunction that was nationwide, meaning it applies to everybody. So, unenforceable, you don't have to comply until the courts have finally rendered a decision on this. So, the appeals courts remember are going to circumvent and supersede any district court decision.

So, the Federal Appeals Court then, in a three-judge panel of the Fifth Circuit, that's where Texas is, the Fifth Circuit Court of Appeals, they said you know what? We don't agree with the District Court judge, and so we are lifting that injunction. Therefore, the BOI rules are enforceable around the country.

Now, it only lifted that one so the Alabama, that limited injunction, still applies to those members. But for the rest of the country, for everybody else, again, the Fifth Circuit lifted that nationwide injunction and they said, you know, they were willing to say that they've met, that the government has made a strong showing, as the court said, the three-judge panel, strong shoring, showing that it's likely to succeed on the merits of the constitutionality, likely to proceed. Now remember, the district court judge said that the plaintiffs were likely to, to succeed on the merits that it was unconstitutional.

So now, you know, this is where we're at except, surprise, the Fifth Circuit Court of Appeals changes their mind. All of a sudden, the Fifth Circuit comes out and the Fifth Circuit says, oh wait a second, we're not going to withdraw that injunction. In fact, we are going to reinstate the nationwide injunction that was issued by the district court judge. So, where we are right now is, this is as I'm speaking, the district court judge has said that there's a nationwide injunction that FinCEN cannot enforce the Corporate Transparency Act. As a result, they can't enforce the BOI rules.

So, you know, they, they kind of left this. A different panel is going to decide whether to uphold the judge's ruling and the court decided to keep enforcement paused to preserve the constitutional status quo while the merits are considered on the substantive issues of the constitutionality. So, you know, FinCEN has said, well, it's still open, you know, the reporting online, it's still open with FinCEN. It's currently voluntary.

So, if it's a very complicated filing and, and you believe, as a lot of the district courts have said, that it is going to be upheld on its constitutionality, that it is constitutional, and that this nationwide adjunction will be ultimately lifted, then you may want to start gathering the information and you can certainly voluntarily file. If you believe that no, I, I think it is unconstitutional or I would just want to wait and see then, you know, we'll wait and see what the result of this is.

So, what will happen, and again, the argument here about is the CTA unconstitutional intrusion into the government, unconstitutionally intrusive into individuals by having you, having to force the reporting of a business you might own, a corporation. So, one of the things that's going on then is, well, if you do have to comply, or if you believe you're going to have to comply, and it's complex, you may want to start gathering the information from your clients so that you have it available. You know probably what will happen is they're going to, if, if this injunction is lifted, there will probably be a period of time, most likely, 30 to 90 days to comply with the BOI rules. So, if it's, if it's lifted, expect a limited period of time in order to comply.

The FinCEN, when it, when it was initially lifted, they extended it for 30 days, the filing requirements. So don't expect to have, you know, a year, expect it to be a relatively short period of time to comply. So, if you want to gather the information now, and again, if it's more complex, you may want to do that just, just in case this is, it, it is not upheld, this injunction. You know, it, it looked like, as I said, there was a pendulum, and we've discussed this previously in other segments, the pendulum was swinging towards district courts that were saying, no it's constitutional, it's constitutional, it's constitutional. So, it looked like that Alabama case was just an outlier, it's just out there, one judge making that decision. But now we've got this case, and this case went to the appeals court, and this appeals court has already ruled that, nope, that injunction nationwide is going to stay. I, I'm not going to say what they'll do on the merits of the constitutionality of it, but we know other district courts around the country in other circuits have upheld the constitutionality, said it is constitution.

One of the things that you should keep in mind, and this is an important issue, is if in fact it is upheld, what's the role of the accountant? Now, the determination of what is the practice of law is really left to the state's bar associations. Some bar associations have said doing BOI work is not legal work. We previously discussed that some states have said the more complicated, when it starts requiring you to make interpretive looks at or interpreting the law to decide what to file, that becomes more complex and that now gets into the area of practicing a law. So, you need to check with your state association to see where we stand on BOI reporting. Your state CPA society should be able to give you that information, what the status is, and I know state CPA societies have been working with the state bar associations to try to work something out on this.

The other issue that's out there is your insurance. Now, the AICPA's insurance carrier, the one who, if you get insurance through the AICPA, your malpractice, CNA, they've said they're going to cover BOI, that they're going to cover it if you do BOI work. The problem is, if that work is determined to be legal work, then your carrier can turn around and say, we're not covering you, that's not accounting, that's legal. We're not covering you if there happens to be an issue and you end up unfortunately getting sued. So, make sure you check with your carrier. Again, the AICPA, CNA has said yes, they're going to cover BOI work for accountants. So, you've got two issues there. One, is it, to what degree is it the practice of law? You know, and again, even the states who have said it could get into practice of law have said if it's a simple matter, simply the information is simple, simple reporting, accountants can do it, that's not practicing law. The more complex it gets, and of course there's no definition, what does that mean? If it requires interpretation of the law in order to comply, okay. Where does that lie, then it becomes the practice of law.

So again, it's very important, it's very important to check with your state association relative to the practice of law and your carrier to make sure that BOI work is going to be covered.

Now we have a case out of the tax court. We haven't seen, we haven't seen a lot for a while, but you know, here we go again. Capital Places II Owner, LLC. This is a tax court case. It involves an interesting situation, something to always keep in mind. And I was involved in something somewhat similar to this when I was approached to look at a particular project. And in this particular case, what happened was the taxpayers, they took a very large charitable contribution on a, the donation of the facade of a building claiming that it qualified as a historic facade preservation easement, and they took a deduction of just over $23 million for the donation of the facade. Well, the problem is that the donation of the facade, and, and this was a building that it was in a historic preservation area in Columbia, South Carolina. The however, you know, it was an early 20th century building located in a historic district in Columbia. It was a three-story classical revival masonry construction, designed by James Urquhart, who was a very famous early 20th century architect, and the problem first, the building's facade had been altered by the addition of stucco in the 1960s. They then later, many years later, decades later, they removed the stucco, but when they did it, they did material damage to the building's brick and the flush stone orient, ornamentation that was on it. So, because of the damage that was done, it didn't qualify as a certified historic structure according to the National Park Service. So the, the second way of looking at it to qualify would be that the building was included as a, and I'm going to use the term, contributing structure, to a commercial historic district. Well, here's the problem. The Secretary of the Interior had not certified the building's historic significance to the district. It was in a historic district in Columbia, but the Secretary of the Interior didn't certify that that building had any historic significance. So since it wasn't a certified historic structure, it wasn't certified as being integral to the certified historic district, there was no certified historic facade easement that is allowed. There's a certain, there are procedures to, that have to be followed for getting that certification from the Interior Secretary, that it was historically significant to the district. They didn't get that. So therefore, for two ways that it could have qualified, it didn't qualify under either.

I had, I was approached to look at a building and we were looking at it as a certified historic structure. And the problem is that it was significant, yes. it was in a historic district, but the historic district it was in was declared by the local county, and there was no other certifications, no federal certifications. The building itself didn't qualify as a certified historic structure for a number of different reasons and the historic district was just a local thing. So, you always have to be careful on that.

One important thing, Notice 2025-7. In Notice 2025-7, the IRS provides temporary relief from the regs dealing with the implementation of the Infrastructure Act. And generally these regs require certain digital asset brokers to file information returns and furnish the payee statements on the gross proceeds and the adjusted basis for distributions or dispositions of digital assets. The final regs provide an ordering rules for determining which units of the same digital asset, you know, like going to a broker and you've purchased 100 shares here, 100 shares, 100 shares, 100 shares. When you go to sell, which 100 shares did you sell? We know that it's FIFO if you can't specifically identify. Well, one of the problems here is it, it's unclear what information from the regs is exactly making adequate identification of digital asset units held in custody of a broker. It has to be done before the units are sold, disposed of, or transferred by reference to a particular identifier and then the broker designates, specifically, to determine the basis of those assets that have been identified, and again, in the regs they call them identifiers. So, what the regs do here or the notice I should say, is the notice says that beginning on January 1, of 2025 and ending at the end of the year so for 2025 adequate identification. So, the client comes in they've got these digital assets that they had disposed of identifying no later than the date and time of sale, disposition or transfer on the taxpayer's books and records so particular units to be sold what am I selling? What am I transferring? What am I disposing of? By reference to any identifier such as the date you purchased them. I'm selling the ones I purchased on this date. What was the purchase price? Another way, the purchase price for the units that are being sold. So, anything that's sufficient to identify the basis and holding period of the units that are sold or transferred or disposed of. Or, second method, recording a standing order on the taxpayer's books and records provided the recorded standing order includes enough information to identify which digital assets are being sold, which units are sold, disposed of, or transferred, and that's entered into the taxpayer's books and records before the units covered by that are sold or disposed of. So, again this is necessary because digital asset brokers said they haven't had the time in order to get their technology in place to comply beginning January 1, and so this is kind of a, this is a temporary relief measure that will apply to 2025. Again, if nothing is, if nothing is, done to do an identifier, you're going to apply FIFO, same as you would with the securities. And again, these are temporary relief for this year.

If you do any international work, and this is, not going to get into the weeds on this, but Notice 2025-4, this proposes a transfer pricing under Section 482. A transfer pricing and if you're not that familiar with transfer pricing generally you know you'd like to get an APA, an advanced pricing arrangement with the government. When you look at these transfer pricing, you're not generally looking at okay, so let's say you get an APA you're not determining the cost of each item. You're determining how we would determine the cost of each item? Oh, we're going to determine it by looking at comparables. We're going to look at the cut method. So, there's different methods in the regulations as to what you can use to determine that price. You don't say, well the widget, A1 widgets are going to be $1.25. A4 widgets are going to be $2.30. That's not how it's done. You're looking at and agreeing on a methodology or you're applying an agreed upon methodology. So advanced transfer pricing is agreeing on the methodology.

What the IRS proposed regs are intended to do is adopt an alternative methodology called the Simplified and Streamlined Approach (SSA) and that's based upon a report by the OECD, the Organization for Economic Cooperation and Development, the international organization and they have a proposed simplified streamline method. So, the proposed regs, they're intended to be consistent with this international standard of the SSA, and that would permit U.S. taxpayers, or I don't say U.S. tax, taxpayers subject to U.S. tax for what's called in-scope transactions. So both the U.S. distributor and U.S. related suppliers elect to apply the SSA for any tax shares beginning after January 1. And it would also incorporate the SSA into the safe, current Safe Harbor application of the Arm's Length Standard. The idea is when you're transferring among related parties, it should be at an Arm's Length transaction. You can't, you can't try to manipulate the how much profit is being taxed in the U.S. versus taxed in a country that might have significantly lower tax. So, the U.S. is 21%, but boy, if we can sell things out of here, well that's at 2%. So, what we'll do is, you know, we're going, we're going to transfer at a very low price subject to the 21% to a related party in another country and then we're going to make sales from there and they'll be taxed at 2%. IRS will come in and say, whoa, whoa, all of your transfers have to be with related parties. They all have to be arm's length so they're recognizing the true profit. So, the proposal would incorporate a safe harbor application of that arm's length and you know, the steps to make the election. So again, you can rely on the guidance that's in here and again, these proposed regs that are reliance, they are going to be effective January 1, of 2025.

All right, so we have Announcement 2025-2 and the IRS in this particular announcement announced that the regulations on the required minimum distributions that were proposed back in July of 2024 are not going to apply until 2026 distribution calendar year. All right, so the proposed distribution rules that were proposed back in July are not going to apply until the 2026 distribution year. And so that, that will have, you know for certain clients, you should look at that and determine, ok you know, we were making, we were looking at distributions based upon the regs in July. They're not going to apply till 2026.

FinCEN, in a FinCEN news release at, towards the end of December, FinCEN said there's a lot of scams going on and FinCEN has identified websites, for example, that are for filing fees, and they're telling people that the BOI, they'll do the BOI work and there's filing fees. So, they'll charge for the BOI work and they'll take a filing fee. Well, there is no filing fee to file the BOI report with FinCEN to begin with and usually they don't file anything there. It's just a scam. So, you should make your clients aware of this, especially right now while this injunction is there, that doesn't mean that clients know that. Clients may very well, and you may very well have told your clients, hey, you know, we're going to have to file, here's the information I need for my, for the BOI, make sure they know that these are scams and so, you know, you can see where they might get a contact saying well we can do this this has to be done, you know this is what we do, we do filings.

Another one which is very, very unique but some businesses have been registering with the, with FinCEN as money services businesses. Well, that's a self-registration. But what they do then is, you know, they're fraudulent, but they use the fact that they have a registration with the, with FinCEN to claim credibility. Well, oh look, we're accepted by FinCEN. We are approved. Well, they don't vet. They don't approve. They don't license. It's simply a registration. It doesn't give approval of the business, but scammers are using that, as money service businesses, are using that as a, as a scam. So, you know, sometimes as part of the virtual asset scams, they will, they'll use this by saying, look we are, we are approved by the, by FinCEN. So those are very common and of course you always get the thing where people call a business and claim that they are FinCEN, you know, calling from FinCEN and try to get information from the client. So just give your clients a warning on this.

All right, IR 2024-312, just so you're aware, the IRS announced that the standard mileage rates for this year are going to be 70 cents a mile, so an increase of 3 cents from 2024. But they did not change the mileage for medical or active duty armed forces, it's still 21 cents and they didn't change charitable, that still remains at 14 cents.

They also note that, keep in mind, that the same rates apply to fully electric and hybrid automobiles. It's not just gas and diesel powered vehicles. It applies also to electric and hybrid. Now with that, you know, what's the, what's the allocation to basis? What do you reduce your basis by? You know if you're using the standard mileage rate, you're not taking depreciation.

Well, it's 33 cents a mile for 2025. So mileage driven in 2025, 33 cents a mile will be considered depreciation, and you need to reduce your basis by that amount. That of course will be relevant if you dispose of it. In addition, the maximum standard automobile cost for computing the FAVR method, the fixed and variable rate plan, is $61,200, cars and trucks and vans and that same number $61,200, is used for employers provided vehicles under the fleet average valuation rule and the cents per mile rule for employer provided vehicles.

All right, the 10th Circuit Court of Appeals, we have an interesting case out of the 10th Circuit. You know, you see, you see cars racing, you see NASCAR, and you know, there's stickers all over there, right, from businesses. In Avery, which is a, is a 10th Circuit Court of Appeals case, this was a tax court case, Avery versus the Commissioner, and the 10th Circuit Court of Appeals upheld the tax court. What this individual did, and this individual, by the way, was a lawyer. He practiced personal injury law and on his income tax returns, he claimed between 50,000 and 70,000 in business expenses for 2008 through 2017, and then from 2008 to 2011, he used his racing car to advertise his law practice, so he took off all the expenses related to his race car. IRS reviewed it and they determined a tax deficiency for these years of almost a million dollars. He, you know, went through all the administrative process, couldn't resolve it, he filed with the tax court and the tax court simply said, look, advertising itself, you know, that can be an ordinary and necessary expense but you haven't proven that the expenses of operating the, a race car, even though your name's on it, that advertise that that all of those expenses for the race car are ordinary and necessary in the carrying on of your trade or business as a lawyer.

So, Avery, you know, he argued that the tax court looked at something that they shouldn't have looked at, because the tax court looked and said, you enjoy car racing, there's a very, you know, this money you spend is primarily personal. So, he said, Avery says, well, you can't look at that. You can't consider my enjoyment of a marketing activity and say, that's not an ordinary and necessary expense simply because I enjoy doing it. The 10th Circuit said, you know what, the tax court, the tax court was right. Personal enjoyment factor helps determine the primary motive for incurring those expenses. So, the court said, you know, the car racing expenses could maybe be ordinary and necessary business expenses for advertising, but you'd have to show. Here's what they said. If you want to show this connection, what's the business connection? What's the clear link between the racing activities and the taxpayer's legal business? What was the promotional intent? Is it simply to promote your business? Or is it part of your personal enjoyment of racing? A reasonable, of course, is the amount reasonable in relation to your gross receipts. The business benefit, what benefit is the business getting from your racing activities? There has to be some tangible benefit that the business is getting and then the primary purpose.

What was the, what's the primary purpose of the race car activities? And this involved the taxpayer and other family members. So, was the primary purpose just promotion of the business? Was the primary purpose personal enjoyment? You know, he failed to establish the primary purpose was business promotion rather than personal enjoyment. And of course, for promotion, is the expense reasonable, especially in relation to the benefit that you're getting? And you know, is there a clear link? And again, you know, if it was just paying a promotion to advertise, I want to stick my sticker on there, you know, that's easy, right? Here's a clause for promotion, you charge a promotional fee, that's advertising for us but he's looking at all the expenses of racing. That's where the, that's where the thing drew, where the court drew its line.

All right, T.D. 10017, 10017. We have final regs have been provided on the supervisory penalty approval rules. So again, generally the IRS can't assess penalties against a taxpayer unless the initial determination of the assessment is personally approved in writing, quote, personally approved in writing by the, quote, immediate supervisor of the individual making that determination or a higher level official. Now, it doesn't apply, this is Code Section 6751. It does not apply to any automatically calculated through an electronic means, like failure to pay, failure to file. Back in 2023, the IRS issued proposed regs relating to what is supervisory approval and, you know, they got very few comments on it and so the IRS has finalized those regs and essentially, the final regs adopt the proposed definition of immediate supervisor. The immediate supervisor simply is the individual who that person is responsible for addressing. In other words, who is their immediate, who do they report to immediately and the IRS rejected any comments that the proposed regs definition of higher level official was too vague because they said the IRS has the discretion to designate which higher official can approve a penalty. So, since the IRS can designate which higher official, it doesn't need to provide any specific language for that. So the, these rules are effective December 23rd, 2024.

Now IR 2024-315, the IRS has proposed reg changes to Circular 230. Now, these changes really are nothing that will affect most of us. Things like the courts' rulings challenging the 230 rules that are obsolete. So, they just are removing those. So, for example, enforcing registered tax preparers that if you're a tax, tax preparers must register with the IRS, that, you know, that was determined that the IRS did not have the authority to require that. So, there's a number of different court cases. Under the regs and subsequent notices, contingent fees could not be charged for preparation of original returns but were permissible for services rendered in connection with IRS examinations or disputes if it was reasonable to believe. So that could be an amended return if it's reasonable to believe that the IRS could examine it. So amended returns, credit claims, the intent of the change was to restrict contingent fee arrangements, but a DC District Court found that the IRS lacked authority to prohibit practitioners from charging contingent fees for ordinary refund claims. Again, not original returns, ordinary refund claims. So, the question is, do you think that there is a high probability that this would be reviewed by the IRS? So, that is no longer required for ordinary refund. You can still charge contingent fees. But they eliminated a lot of those, but what they did do is adopt some best practices that you should be aware of.

So, for example, there's new best practices related to data security policies to maintain those safeguards of client information and plans and procedures for responding to data breaches. So, this has now been put into Circular 230, and they encourage practitioners from, that suffer from any mental impairment, that's the term, to seek and obtain appropriate treatment. So, impairment could be the result of a health condition, age, substance abuse or any other circumstance that could adversely affect a practitioner's ability to effectively represent a client before the IRS. That, according to the regs, encourages seeking mental health help.

Now, another change, practitioners are recommended to establish a business continuity and succession plan. You know if, if you're a sole practitioner and something happens, then what? So, what about if there's a national, natural disaster or cyber-attack? What continuity and succession planning do you have?

And then the IRS expects according to the proposed, the new regs, the IRS expects practitioners to maintain familiarity with technological tools that are used to represent a client and a competent practitioner, the proposed regs clarify as one who understands the benefits and risks associated with the relevant technology. So, these are proposed. The comment period runs up February 24th and the, and that should be done through the federal rulemaking portal at www.regulations.gov. The public hearing is scheduled for March 6th of 2025.

So, there's been a lot of things that have gone on and a lot of it, some of these things that we've talked about today, remember, are applying to the returns that you are doing now for the 2024 year, or you know, are going to have to apply and a lot in for 2025. So, keep this in mind and again, I don't want to say have an enjoyable tax season, but have as little stress as is necessary during tax season and as always, please be safe and we'll see you next month.

GROUP STUDY MATERIALS

A. Discussion Problems

1. Why is it important for accountants to check their state’s rules and insurance coverage when doing Beneficial Ownership Information (BOI) work?

2. What should clients and tax professionals watch out for to avoid scams related to BOI filings and FinCEN registrations?

3. How can tax professionals prepare for the proposed IRS rules that require them to safeguard client data and have business continuity plans?

B. Suggested Answers to Discussion Problems

1. It is crucial for accountants to check their state's rules and insurance coverage when performing Beneficial Ownership Information (BOI) work to ensure compliance and avoid potential risks. Some states classify complex BOI tasks as legal practice, which accountants may not be authorized to perform without violating state bar rules. Additionally, malpractice insurance might not cover BOI-related work if it is determined to fall under the category of legal services rather than accounting.

2. Scammers often target clients and tax professionals with schemes related to BOI filings and FinCEN registrations. One common scam involves charging fake filing fees for BOI reports, even though no fees are required for these filings. Another involves fraudsters registering as money services businesses with FinCEN to falsely claim credibility, as registration with FinCEN does not mean the business is approved or licensed. To prevent falling victim to these scams, tax professionals should educate clients about the lack of filing fees and warn them against unverified services.

3. Tax professionals can prepare for the proposed IRS rules regarding data security and business continuity plans by taking proactive steps to protect client information and ensure operational resilience. Implementing robust data security measures, such as encryption, secure file-sharing platforms, and regular technology audits, is essential to safeguard sensitive client data. Additionally, creating a detailed continuity plan for handling emergencies like natural disasters or cyberattacks ensures that operations can continue with minimal disruption. This plan might also include identifying a backup practitioner or team to handle client needs in case of unforeseen circumstances.

PART 2. INDIVIDUAL TAXATION

Individual Tax Update

Welcome to the second segment of this month's program. In this segment, we'll focus on essential individual tax preparation topics for the 2025 filing season.

We'll start with filing basics, including deadlines, who must file, and the kiddie tax rules. Next, we'll examine gross income, including exclusions and adjustments, such as capital gains, wash sale rules, the foreign-earned income exclusion, educator expenses, and the student loan interest deduction.

We'll also explore standard and itemized deductions, tax calculations, and credits, including the Child Tax Credit, Earned Income Credit, education credits, and energy-related incentives. Finally, we'll address topics such as the premium tax credit, nanny tax, Section 529 qualified expenses, and Section 529 plan rollovers to Roth accounts.

Let's join Mike.

Mr. Mike Giangrande

Digging right into Page 1-1 with our Chapter 1, we do have our filing deadline of April 15th, 2025.

We have a personal exemption deduction that is still suspended through 2025, but remember, the personal exemption amount is still relevant and is adjusted annually for inflation. For example, it's used as part of the gross income test when determining whether a qualifying relative can be claimed as a dependent. So, it is still a relevant metric, certainly much less so pre TCJA when you actually had a personal exemption deduction.

Now, here we are on Page 1-1 in our first topic, and I do want to point out in the margin, what you see there is a little hourglass that says, "TCJA expiring." So, we do have President Trump, right, headed back to the White House. You've got a Republican Senate. You, I'm sorry, Republican majority in the Senate, Republican majority in the House, slim margins, but still a Republican majority. These are the same conditions that were present when the TCJA was first passed back at the end of 2017. So, even though Donald Trump has said that he wants to extend the TCJA permanently, he's got some hurdles he's going to have to get over to be able to do that.

But for now, what I want to impart on you is wherever we have a TCJA provision that is as of right now scheduled to expire at the end of 2025, we have that little hourglass link for you there, scheduled to expire or there's a change coming to it.

Because if we think of the TCJA, we can really put the provisions into two separate camps or buckets, if you prefer. You had your TCJA provisions that applied to businesses and most of the provisions that applied to businesses were permanent provisions. They don't have a sunset date, most of them. They had different, you know, effective dates when they started, but they were permanent provisions.

On the individual side, though, most of the provisions of the TCJA that applied to individuals were temporary provisions, and within that, most of those temporary provisions were temporary for tax years 2018 through 2025. There are some exceptions there. For example, the alimony provision for individuals; right? That was a provision that didn't start until 2019, but it was permanent; right?

So, not everything follows at 2018 to 2025, but where it did, we have, you know, in this individual chapter anyway, that little hourglass for you so you can see quickly as you're going through your materials where there is a change coming.

On Pages 1-2 to 1-3, we have our qualifying child and head of household flow charts for you. We give those to you every year as just quick reference guides to have at your fingertips during tax season. So, that's there for you towards the beginning of Page 1 on Pages 1-2 and 1-3.

Let's talk about filing issues. So, taxpayer, what I have here is on Page 1-4 is some information on taxpayers who must file a tax return and taxpayers who should file a tax return. Now, anybody who's paying us to do their, to be their tax practitioner is going to be somebody who has a filing requirement. I find in my practice, and, and one of the really cool things about doing this, I'll share with you early on here doing the speaking as, as I have learned over the years since, I think we a in year 9 now, doing the speaking that my practice mirrors many of yours in terms of the type of clients that I see, and, and what, what, where this becomes an issue where I have somebody who, where I have to actually tackle, “Gee, do I have a filing requirement for this person?”

It's usually somebody who comes in and they'd like me to prepare the tax return for maybe their elderly parent who's maybe now, you know, really at the end of their life, or it's, you know, maybe that, that, that first time job, a kid gets and, you know, they give me the kids W-2 and say, “Do I, does this count the file? Can you just take care of it for me if I do?” And, and, and that's why I sometimes have to look at these requirements.

So, we have is on the top of the Page, “Who must file?” And the thing, the only one that's new here on who must file is if you claimed an advanced vehicle credit at the dealership. Starting in 2024, if you bought a, either a new clean vehicle and you're going to be claiming the Section 30D, Clean Vehicle Credit, or a used clean vehicle and you're going to be claiming the Section 25E previously owned Clean Vehicle Credit – I just called it “used Clean Vehicle Credit” – and you claim to the credit at the dealership, because dealers starting in 2024 can give you an advance credit right there on the spot when you buy the car, if you did that, that triggers a filing requirement even if you had no other income.

Now, I will tell you that if you have no income, you have no business buying a car, but that's not the economics of, you know, how everybody in our society works. But we'll talk about the Clean Vehicle Credits and the advance credits and all that, you know, in more detail later, but that's the new item on this list of who must file.

Who should file? Generally, it's people who have, you know, will be getting a refundable credit. Maybe you've got some withholding on a low-income job, you know, like the teenager, for example, and you want to get your money back, but often, you know, for like for me, for what I do, I'm sure for what you do, unless it's a real high dollar client and you’re preparing the kid’s return for free, if there's no, the cost benefit analysis to recover $100 refund on the kid’s withholding, it's just not usually worth it.

Kiddie Tax, though, there's more to Kiddie Tax issues. This is something that we see more often though. Now, if all the requirements that I have listed on Page 1-5 are met, then children are taxed at their parents’ highest marginal tax rate on their unearned income, and the tax rate that's ultimately used is the tax rate of the custodial parent. If we're talking about parents married filing separately or just not married at all, or if living together and filing married filing separately, you've got to use the parent with the higher marginal rate.

So, we look here, the unearned income item that changes the most is the filing threshold for 2024. That's that unearned filing threshold is $2,600. One question I get a lot is, “Does that, is that the, the, the gross or the net,” right.

So, if you got a kid who's, usually this filing requirement kicks in because maybe you've done some investing for the child in a post-tax account, you know, maybe with, you know, Schwab, E*Trade, Merrill, you know, Vanguard, whatever you're doing, you're trading and the kids got, you know, gets that consolidated 1099 at the end of the year. And, and so the question is, “Is that $2,600 dollar filing requirement triggered by the gross sale proceeds of stock or is it the net?” It's the gross. Use the gross, because that's what's going to trigger the IRS.

Now, technically, if you had, if you didn't have the filing requirement because you, you know, you sold the stock at, you know, say no gain, the, if you don't file, there's going to be no harm, but you know, the IRS is usually looking at that gross. So, use that gross.

Moving on. If the kid's only income is from interest, dividends and capital gain distributions, then the parents, if all the requirements of, other requirements are listed on Page 1-6 are met and the parents can use Form 8615 and elect to just report the kid's interest, dividends and capital gain distributions on the parents' income tax return and not file a separate tax return for the kid, if you wanted to, and you could do that. It's optional. You can, or you can just file a tax return for the kid separately and apply the Kiddie Tax rules. It's your choice.

What I have for you, bottom Page 1-6 here in the planning pointer box are some tips to help reduce the Kiddie Tax bites. So, if you do have that child, that minor or that college-age student who is subject to the Kiddie Tax rules and they are being taxed at a much higher rate than they otherwise would have to be, consider your investment strategies. You know, change them up a little bit to try to push off the Kiddie Tax until a time when the kid is not subject to the Kiddie Tax at all.

For example, you know, make investments into growth stock versus dividend paying stock so that you're not going to have any gain until after the kid is maybe out of college, then you sell some stock, and you've got some gains no longer subject to the Kiddie Tax.

If you've got earned income from the child, for the kid, often these are our teenagers. Consider putting your investment dollars into a Roth IRA for them. Those are that growth in the Roth IRA, interest, dividends, capital gains that are that are earned inside the Roth IRA, those are not taxed. While the money is in the IRA, you're not taxed until they pull the money out. Consider some of these alternative investment strategies to reduce having to pay the Kiddie Tax. Some of those other items on the box bottom of Page 1-6 if you're interested.

Let's move on to gross income issues, specifically long-term capital gains, top Page 1-7. So, what I got for you here is our long-term capital gain rate chart and our inflation adjustments. You know, I like this chart. This, I'll tell in you my practice this ends up being one of the charts that I go back to during tax season over and over again. You know, particularly when I'm looking at whether I've got a client who's, you know, bordering between the 15% and the 20% long-term capital gain rate, because what I can do then is, you know, kind of see where, where are we going to fall? Do we want to try to harvest some more capital gains, and they're sitting on gains, or try to make sure or just make sure we don't leak over into the 20% long term capital gain rate bracket?

If you've got clients on the lower end of the scale though, and that can happen, maybe they're hovering between 0% and 15%. If you've got someone who's taxable income is not climbing over the 0% bracket, and if we look at this for 2024, for example, married couple filing jointly, if their taxable income is under $94,050, then the long-term capital gains are taxed as 0%.

So, if you're sitting there and you got someone who's got a nice little portfolio of stocks and their taxable income say is only $80,000, that gives you about $14,000 of wiggle room to, to harvest some gains and know they're going to be taxed at a 0% federal long-term capital gain.

So, don't forget to do that. You know, I'll see that in my practice. Again, sometimes I get clients who get older and maybe all they've got is just some IRA income, Social Security, or they've got maybe a client who's got a lot of net operating losses so it's really pushing their income down. It gives you some opportunity for harvesting that 0% long-term capital gain rate bracket really kind of nice there.

Wash sale rules, let's talk about those. So, taxpayers are prohibited from claiming a loss from a wash sale. So, what is a "wash sale"? A wash sale occurs when a taxpayer sells or trades stock or securities at a loss, and within 30 days before or after the sale either buy substantially identical stock or securities, acquire substantially identical stock or securities in a fully taxable trade, acquires a contract or option to buy substantially identical stock or securities, or acquire substantially identical stock or securities in their IRA or Roth IRA.

Now what is substantially equal stock or securities? Essentially looking at the stock of the same company. The stock of two different companies is really never going to be substantially identical unless those two companies have been merging with one another and there's merged scenarios you could have the wash sale apply.

So, you know, just because you're you know, trading, you know Coca-Cola for Pepsi, for example, does not make that substantially equal. You're really talking about the same company. And so, so that's, those are the wash sale rules.

Now if you're, if you're buying and trading with the same broker, they're going to apply those rules. We've all seen that, right, the disallowed wash sale line on that consolidated 1099. But what's neat is if, if you're working with a, with a broker that is doing a good job, your disallowed wash sale losses are added to the basis of the, the, the acquired stock that triggered the disallowed loss in the previous stock as well as the, the holding period.

So, that wash sale rule shouldn't, those wash sale losses, I should say, shouldn't negatively impact your client in the long run. They should impact, negatively impact them, today's income. They disallow losses, but those losses are added to the basis of the next stock. If you're not sure if your client's losses are, maybe just ask them. "Hey, do you know if your wash sale, is your, is your broker doing a good job tracking those wash sale loss rules?

Where I think you'll probably do a less of a good job is tracking these where you got me two different brokerage accounts, two different companies certainly or maybe within their IRA and not within their IRA, and that can be pretty difficult.

I will confess to you that I'm, I, I, I do not during tax season, take the time for my clients who maybe say have an accountant E*Trade, an account at, you know, Schwab, I don't go and look at all their trades at the end of the year. They don't want me, they don't want to pay me to do all that, I don't do that. The odds of having a wash sale loss are not significant for most of them so, it's not much of an issue. I'm curious if you do a really good job comparing that, let me know.

Now, I do teach enough of these seminars as, as live seminars and I do poll the room on this, and by the way, and I already know that nobody does a good job of tracking these for their clients separately.

So, hopefully they, they, they're do most of their trading within the same broker and the broker is tracking that stuff.

Cryptocurrency still, even this year now, is not subject to the wash sale rules. I know, you know, when Trump got into office and certainly, you know, leaning on Elon Musk quite a bit, you know, Bitcoin and other cryptocurrency seem to have really taken off, you know, in an upward trend. So, so harvesting losses from cryptocurrency and trying to take advantage of them not being subject to the wash sale rules, probably not much of an issue this year, but it can be when, when those cryptos go down in value, so watch out for those

Deferred gains from opportunity zones. Really just want to throw a reminder out there that if you had clients that deferred their gains from capital gains and by investing in qualified opportunity funds, which are therefore investing in qualified opportunity zones, if you've got clients in that situation, remember the, the, the pipers coming due, the taxes coming due at the end of 2026, not 2025, end of 2026, and just get ready for your cash needs on those. Start getting ready to advise your clients that they're going to have to come up with tax dollars to pay the federal government coming up soon.

Home energy rebates starting on Page 1-9. Home energy rebates received through state programs are not includable in income for taxpayers, but the home energy rebates essentially are. These were Inflation Reduction Act provisions, but the federal government is providing dollars to the states. States administer rebate programs for people doing energy improvements to their properties. That's not taxable income. If you get a client that receives those, they shouldn't be getting a 1099. So you really might not notice it, but what I want you to do is be on the lookout just when you've got clients who do energy improvements like solar, for example, if they did get a home energy rebate, what they have to do is they have to reduce what the, the total cost of their solar project that by the amount of their home energy rebate they received and then calculate the credit based on that lower amount.

So, maybe just ask the question this year when you have clients who buy, maybe those, you know, thermal, geothermal heat pumps or they put solar panels on their house or do some kind of improvement, "Did you get some kind of a home energy rebate from the state?" And if they say yes, then you just know that you've got a, a reduced credit that you're allowed to grab. I will tell you right now the IRS is auditing a lot of solar credits and similar credits right now.

Foreign earned income exclusion, starting at the bottom of Page 1-11 here, kicked up to $126,500 for 2024, and then inflation adjusted up even higher to $130,000 for 2025.

Remember, qualified taxpayers who want to claim the foreign earned income exclusion must have a tax home in a foreign country and must meet either the, the bona fide residence test or the 330-day test, which I've got detailed in the materials here for you on Page 1-12.

Where most taxpayers get tripped up here, I'll tell you, is the tax home, because your tax home really has to be in a foreign country. Those clients who are maybe on a temporary assignment because maybe you work for a company, I've seen here in Southern California, maybe a client works for Disney, and they get, and they get sent over to Euro Disney to for a one-year assignment. They still have their home here, their driver's license, everything is here. They're living in company provided housing, you know, in Europe and their tax home is still the United States.

So, maybe they may, may can meet the bona fide residence test, or they can meet the 330-day test. And a lot of taxpayers in that scenario will say, “Awesome, I'm going to claim the foreign earned income exclusion,” and that's not how it works. Your tax home is not in that foreign country.

So, this is really a provision for people who are truly living abroad. And if you're living abroad and you meet one of these two tests, then you can claim the foreign earned income exclusion.

We did see previously a lot of military-type members get in trouble on this as well, people who were on long assignments and, and like Iraq and, and stuff like that, but the Bipartisan Budget Act of 2018, and I've got this in the caution box in the Page 1-12, did amend the definition of tax home.

So, now contractors or employees of contractors supporting U.S. armed forces in designated combat zones can claim the foreign earned income exclusion or housing exclusion, even if they're, you know, quote abode their tax home is within the U.S. So, there is a softening of that rule for people supporting the U.S. military and that, and then that's not terribly new. That's a few years old now.

Tax tips for you, top Page 1-13. If you've got somebody who does qualify for the foreign earned income exclusion and you need some tips on how to claim the exclusion on the income tax return, how to make the election, tips for that top of Page 1-13. It’s there for reference, but I'm not going to walk through it.

Let's move on to Section 104 and compensation for injuries and sickness. We're really on our gross income issues here. So, any compensation received that, or any pay that your client receives that is a compensation for personal physical injuries or sickness, has to be physical injuries or sickness, is excludable from income under Section 104(a). But for workers comp, amounts are only excludable if the four requirements I have listed on Page 1-13 are met. And this is, you must receive your compensation under a workers compensation act, be compensated for personal physical injuries or sickness. That's our Section 104 requirement, not to be related to the employee's age or length of service and be incurred in the course of employment. It's that third one where the questions come up, “be related to the employee's age or length of service.”

If you got somebody who, who goes on a disability retirement, for example, you know, they're let's say they're a fireman. We've all seen like a fireman or a policeman and they get a knee injury or shoulder injury and they go on to disability retirement, that doesn't make all of their compensation tax free, right, as compensation for personal physical injury, injuries or sickness, because the amount of their compensation is calculated not just because they're injured, but it's also calculated because of their age and their length of service within, you know, the fire department or the police department. That's why you'll see some level of their retirement subject to exclusion and some not.

So, when you get somebody who's, you know, a fireman or a policeman and, and those are the easy ones to, to, to, to pick on, we've all seen those, but somebody who has that type of an injury and you get the 1099-R for their retirement, and it shows there's, there's some amount that that's taxable, don’t automatically think that that's wrong because what's happening here is the, you know, the, the, the, the pension administrator is applying these rules here. And so, yeah, there's that.

Okay. Let's move on away from this topic. Let's go on to dependent care assistance. The maximum exclusion here is $5,000. Don't forget dependent care assistance includes employer provided compensation for dependent care, the fair market value of care facilities provided by the employer and any pretax contributions made by an employer under the, under a dependent care flex spending arrangement excluded from income.

Now sticking with the FSAs in general, you know, FSAs are employer benefits that are designed to reimburse employees for expenses incurred for qualified benefits. There are three types of FSAs dependent care FSAs, adoption assistance FSAs, and then the one that we all typically think of when we think of just an FSA are our health FSAs that, that are the design to reimburse your client for medical care.

Now an FSA, unlike an HSA, is a use-it-or-lose-it type program. You set money aside pretax. If you don't use it during the year, it's gone. It goes back into the employers, you know, FSA pool or however the employer administers it.

Now, adoption and health FSAs are limited up to $3,200 in 2024. It kicks up a little bit. Dependent care FSAs have the $5,000 limit, that was not adjusted for inflation. So, is eventually what's going to happen is these two amounts will, you know, kind of marry each other and then the adoption and the health FSAs will exceed the dependent care FSAs at some point in the future because the, as I said, the dependent care FSAs are not adjusted for inflation.

Now I did say FSAs are a use-it-or-lose-it program. That's mostly true because FSAs do permit a small carryover. If the employer allows for a carryover, they can allow no more than $640 to carryover from 2024 to 2025.

Now sometimes clients will, people will ask me, “How can I tell if a client has an FSA on the, if I look at the W-2?” And the answer is really you don't, because the W-2 does not have any required disclosures for an FSA. I mean maybe you'll see something in Box 14, which is an optional disclosure box for most items in there for an employer. So, maybe you'll see something there, but you can't tell generally by looking at a W-2 whether your client has an FSA. So, that's the answer to that one.

Let's talk about our adjustments to income, formerly known as our above the line deductions, also known as Schedule 1 deductions.

Unreimbursed expenses for K through 12 educators got kicked up a couple years ago to from $250 to $300. You know, if you recall it stayed at $250 from its inception in like 2002’ish until 2022’ish, so, I'm not expecting an inflation adjustment on this anytime soon because it's a very slow kick up. So, for now it's $300 for 2024 and 2025. If both spouses are eligible K through 12 educators, then they can both utilize the $300.

This essentially just takes what is an otherwise 2% miscellaneous itemized deduction for unreimbursed employee business expenses and says, “Okay, for K through 12 educators, because we like teachers, we're going to let them take a little small sliver and deduct that as a Schedule 1 deduction above the line.”

So, all unreimbursed employee business expenses of, of everybody, including K through 12 educators, are simply 2% miscellaneous itemized deductions.

Alimony is still one of our permanent items. No changes to that, no talk of any changes to it. So, as long as you've got a written alimony agreement in place or written separation agreement in place after December 31st, 2018, then any payments by the payor for alimony are not deductible at the federal level and it's not income to the recipient.

Student loan deduction. Moving on to Page 1-16, still limited to $2,500. AGI phaseout chart middle to Page 1-16. I have got to say this is one of those ones where I seem to have very few clients that ever get this one. Anybody who's, you know, got a nice college degree, has student loans, gets a good paying job, their AGI just blows them out of the water on this usually but there it is.

Health savings accounts, updated a chart for you bottom Page 1-16 for inflation adjustments, but some planning point is remember HSA is, you know, if you don't, if you have an HSA or if you've got a high deductible health plan and you can match it with an HSA, but you haven't or your client hasn't, you know, you can still put them open that HSA put the money into it by April 15th and count it as a contribution for the prior year. So, like an IRA, IRA contribution made after year end, HSA contributions are one of those few things you can do to max out that account and claim the deduction for the year that has just ended. So, it's kind of neat there.

Also don't forget when it comes to HSAs, if you've got a client who's healthy and they, and they're not using their money for, you know, doctor appointments because they're not really seeing much in the way of doctors and they're maxing out, maxing out their HSA contributions, the HSA kind of works like a backdoor IRA because what happens is once you've built up enough money in that HSA, and it's a pretty low threshold, like, you know, two $3,000, typically, you can then start investing that excess money because the HSA administrator at the bank where you've got it is usually going to have like a menu of mutual funds you can invest in, just like your company's 401k plan.

And so, you can invest those HSAs and they can start earning for you. And it's not taxable to you and, at least not the federal level, because just like an IRA, you know, the money in the HSAs, it grows tax deferred.

Now at the HSA, if you spend the money on health, on healthcare expenses, you'll never pay tax on it. One of the things that I think a lot of people missed out on HSAs. I'm, I'm, I'm a really, I'm really high on HSAs. I like them a lot because if you're young or you've got a young family and, and everybody's healthy, a high deductible health plan is going to have lower premiums for you. And you can really just take the difference in the premiums between the, you know, the HMO-type plan and the PPO-type plan the PPO-type plans are your high deductible health plans and just take the premium difference and put that money and, and use that to fund your HSA account, and if you don't spend the HSA money, you get to keep it. And so, I think that that is a really great option. I get them. I'm really high on HSAs. I think if you're, if you stay healthy, then they, it's, it's a much, much better option than using the HMO type plan.

Quick comment on Medicare. So, if you are eligible, and I think the term is the term is “entitled to benefits under medical care” is the, is the term, then you're not eligible to contribute to an HSA plan. And we see this often for taxpayers who become, turn age 65 during the year, the amount they can contribute to their HSA cuts off, right, it's prorated based on how many months they're on Medicare for the year. But the IRS’s interpretation of the phrase entitled to Medicare, benefits under Medicare is interesting because you and I that might think, “Well as soon as you turn 65, you're entitled to benefits under Medicare. You're sort of automatically enrolled, you know, on it.”

And so even though taxpayer becomes eligible to receive Medicare benefits starting with the age of turns 65, the IRS interprets the term quote, “entitled to receive benefits under Medicare” to mean both eligible and enrolled in Medicare. And when they, when they talk about eligible and enrolled, we're talking about Medicare parts A&B. So, for some reason you turn age 65 and you don't have Medicare A or B, then you can still contribute to a HSA. So, it's a question that has come up.

Deductions starting on Page 1-18, standard deduction chart on Page 1-18, updated inflation figures there for you. Don't forget the overall itemized deduction phaseout, otherwise known as the Pease limitation, is still suspended through 2025. That is a TCJA provision.

Talk about medical expenses starting on Page 1-19. Medical expenses are deductible as itemized deductions to the extent they exceed 7½ percent of our client’s AGI. A deductible medical expenses any expense paid for the diagnosis, cure, mitigation, treatment or prevention of disease or affecting any function of the body, including any transportation to, for that purpose, any long-term care or any medical insurance purposes.

Note there is no requirement that the medical expenses be paid for within the United States. We are, I will often get questions, you know, particularly during tax time when someone has a client in front of them, I'll get the emails, well, we'll see the message board questions that say, “Gee, my client went to abroad to receive medical care, do, can they deduct that?” And the answer is yes. There is no requirement the medical expenses be paid for within the United States.

Medicine though, when you're talking about prescription-type medicine generally has to be prescribed to be classified as a medical expense deduction. Exception there is for insulin. Interestingly enough, I think you can use your HSA funds for like over-the-counter medical expenses. So, you're eligible to use HSA funds, but if you paid for those over-the-counter medicines with just, you know, your regular checking account, those would not be treated as medical expenses for purposes of the itemized deduction.

Medical mileage chart for you on Page 1-19. We just updated inflation amounts there. And don't forget long-term care insurance. We have that chart on Page 1-20. The amount that you can deduct as a medical expense for long-term care insurance depends on how old you are. The younger you are, the less you're allowed to deduct as a medical expense deduction for long-term care. A question I got recently in one of these webinars someone said, "Can you treat long-term care insurance as part of your self-employed health insurance if you've got someone who's a sole proprietor or otherwise has self-employed health insurance deduction, they're claiming that on the new Form 7206 that was new last year?" The answer is, yes, you can.

Also 1035 exchanges, you know, long-term care insurance can be pretty expensive and so often clients will say, "Gee, I want to get long-term care insurance, but I can't. I, I don't, I, I can't afford it, or I don't want to spend the money."

You know, you could do your little bit of, you know, planning advice for your clients if you ask them if they've got a life insurance policy. And not any life insurance policy. Generally, we're talking about a life insurance policy that has an investment component, right, whole life, universal life, something of that nature. You know, a term life insurance isn't going to have any kind of investment feature. So, you can sort of ignore that. But those, those policies that have an investment type feature, if your client just surrenders their policy, maybe they have taxable gain. And in that case, what they could potentially do is they could do a 1035 exchange and surrender the life insurance policy in exchange for a long-term care policy and defer the gain on that life insurance.

So, 1035 exchanges can be a good way to pay for long-term care because you know, how often somebody who's starting to think about long-term care insurance is typically somebody who is, you know, their kids are older now and, and maybe they don't they, they bought the life insurance years ago. Its purpose was to help, you know, raise the kids if something happened to them. Well, the kids are older now. Maybe they don't need the life insurance. So, maybe it might be time to use that 1035 exchange and convert that life insurance policy into a long-term care policy.

State and local taxes are still limited to $10,000 dollars, $5,000 for married filing separately through 2025. Now, this is one of the few ones where I'll, I'll probably, I'll go out on a limb here, mark my word, words, we'll see how this, how well this ages, but I, I don't think the SALT limitation is going to go away. I really don't,

I think that we are likely to see an increase in it. I think we're likely to see the salt go to $20,000 or $30,000 or have some, or maybe goes to, you know, $30,000, but that is phased out, you know, for, you know, you're really high-income taxpayers, something of that nature. So, I think the salt limitation is going to stay with us, but I, I, I have a suspicion that it won't stay just at $10,000.

And, and, and that goes to something that, you know, President Trump said. He said that he wants to extend all the TCJA provisions permanently. He wants to make them all permanent. Personally, I can't help but think that they're going to sit down, the tax writers that they have, I'm sure they've already been starting this, but nothing has been made public yet, that when they look at provisions of the TCJA, they're going to say, you know, eight years in hindsight, maybe there's something that we would prefer to do differently. Maybe we'd like to change something, or maybe just maybe there's some provisions they want to just let expire. So, you know, you got eight years of experience under the TCJA. I can't help but think that they look like they are going to look back and say some things worked and some things didn't. So, we'll see.

Casualty and theft losses. The deduction here is still generally limited to presidentially declared disasters through 2025. Again, TCJA provision taxpayers can elect to claim the deduction for the preceding taxable year for disasters, which tends to be a really nice thing for people who, particularly if they suffer damages from presidentially declared disaster in that early part of the year, maybe before they filed their income tax return.

It's very easy to just claim that deduction on the tax return, make the election to treat the, the, the disaster as if it happened in the prior taxable year, and get an immediate benefit. You can also do it when you file an amended return, but, you know, when you get towards the end of the year, sometimes it's just easier to just wait until the following tax year.

Also, I'll have to, I have this a little separately here, so not in – this one's actually, one of the items I don't have in the book because this one is still new, happened really right before Christmas, and so the President Biden did sign the Federal Disaster Tax Relief Act.

Now, the bill excluded from gross income qualified wildfire relief payments paid to individuals as compensation for losses, expenses or damages for any wildfire declared a federal disaster after December 31st, 2014, treats payments made to victims of the East Palestine, Ohio train derailment, is excludable for income and allows individual victims with net disaster losses from any taxable year to claim an enhanced personal casualty loss.

Now what? Now a couple definitions in there we want to make sure we, we, we hit for you. One is what is a qualified wildfire relief payment? That's payments that are designed to compensate taxpayers for additional living expenses, lost wages, personal injury, death or emotional distress, you know, typically paid for by the utility companies. And then another term is what is an enhanced personal casualty loss? Well, this is, this is any loss from any federally declared disaster occurring after February 15th, 2021, through 60 days after the Federal Disaster Tax Relief Act was passed, which is roughly mid-February 2025. So, special casualty and loss provisions apply to people in those scenarios.

Now, don't forget though, even without a presidentially declared disaster, taxpayers can still deduct casualty and theft losses related to business property, income producing property and Ponzi-type investment schemes. Ponzi-type investment schemes certainly have their own separate rules, but business property, that's pretty easy to understand; right? Your Schedule C business or maybe you've got a home office that's, you know, related to a partnership. For you, your unreimbursed partner expenses will be deducted on Schedule E Page 2. In that case your home goes up in flames from a non-presidential declared disaster, you could take whatever business losses you had there continue to deduct those as unreimbursed partner expenses on Schedule E.

The questions here that that I mostly got in this particular topic to deal with income producing property. What if the theft was of my stocks? What if my, my, my, my stockbroker absconded with my stock? Is that considered income producing property? My opinion is, yes. Your investment portfolio is income producing property. That's my opinion. I have not seen any Tax Court cases on this. I will say, though, the IRS guidance on this topic, whether you're reading the form instructions, IRS tax topics on, you know, on their website or publications, they all repeat the same thing and they only say rental properties.

Now the IRS doesn't say only rental properties qualifies income produced properties, but they'll say they say, what they say is casualty related to income producing property such as rental property. So, the IRS uses rental properties as an example of a type of income producing property, but none of their guidance did they expand on that at all. So, without better guidance, what I say is I would, I would, I would interpret income producing property broadly to be anything that produces income for your client, and that could, that would include stocks and other investments. That's my interpretation there. And that's, that again, I've gotten that question. I think in December, we were doing these webinars. I got that question at least a dozen times. So, I want to make sure I'm expanding on that a bit here.

I'm going to continue moving along and talk about mortgage interest. So, mortgage interest rules haven't changed since the beginning of the TCJA, but interest is still limited to the first $750,000 of acquisition debt, half of that if you married filing separately. And acquisition debt is defined as any debt used to buy, build or improve your, your, your property.

Now, if you have to incur debt to buy out a spouse in a divorce, that additional debt you take on is also qualified as, sorry, defined as acquisition debt. If you have to buy out a spouse in a divorce, you don't get to add that to your basis in the property, but any debt you incur to buy them out is classified as acquisition debt to the spouse who's keeping the property. So, that's nice.

$1 million limitation still applies to anybody whose mortgage was in place on and before December 15th, 2017, or you've refinanced that debt that still counts. Example of that on Page 1-23 if you're interested, but I'm not going to go through it.

And don't forget the limitation is based on per taxpayer, not per residence. Now, a married couple for these purposes is treated as a single taxpayer, but an unmarried couple is not. And I've had this happen where I've had, I think I have one right now as a client, you know, very large home, couple million-dollar mortgage, unmarried couple. They each get to deduct interest in the first $1,000,000 and both on the mortgage. Once they get married, it's kind of a marriage penalty in a way because they will only, they'll essentially lose half of their mortgage interest deduction.

Now I have a discussion here regarding equitable owners. If you are an equitable owner, you can claim a deduction for mortgage interest even if you're not legally obligated on the loan and even if you're not entitled to the home. Generally, generally, in order to deduct mortgage interest, you have to both own the home and be obligated on the mortgage.

There are some factors, and I've got them listed on Page 1-24 towards the top of the page, that, that will allow you to, to claim a deduction if you make the mortgage payments even though you're not on title and even though you're not on the loan.

Do you have a right to possess the property and enjoy its use, friends or profits? Do you have a duty to maintain the property? Do you have responsibility for insuring the property? Do you have a, do you bear the property's risk of loss and so on and so forth.

And so, I'll give you an example from my practice where I, where I won on an IRS audit on this issue. I had a situation where I had a couple that was engaged to be married and that the, the spouse that was on title and on the loan had become disabled and they weren't making any of the payments. The other soon-to-be, you know, this in this case soon-to-be wife was making all the loan payments, but she wasn't on the loan. She wasn't entitled. We were successful in arguing that she was an equitable owner and should be entitled to the mortgage interest deduction.

She lived there. If the, the mortgage wasn't paid, she would have lost the home. Her kids lived in the home, you know, and, and she was going to have an ownership interest in the home once they got married. Now, I didn't tell the IRS they'd been engaged for 12 and a half years, but that was a different story, but that is a situation where we won on the equitable owner issue.

Remember, equitable owner is a facts and circumstances item. In my scenario though, the other thing that really works in your favor if you're on an audit, is make sure that the person who's, who is receiving the 1098 in their name. If they didn't pay the mortgage, don't let them deduct the interest on their own Schedule A because the IRS certainly will not look favorably on your client if two people are trying to deduct the same dollars.

Let's talk about interest tracing. Interest tracing is always confusing to people, and I want to try to make this as easy as possible. So, generally, interest is deductible based on how the loan proceeds are used. And let's do, I want to go through the examples in this section in this detail, and let's lay the groundwork for how interest tracing generally works.

Example bottom of Page 1-24 with Bill. Bill took out a personal loan of $150,000. He used $100,000 of the loan proceeds as a down payment on a rental property and $50,000 of the loan proceeds as seed money to start a sole proprietorship business.

Because 2/3 of the loan proceeds were used for a rental property and 1/3 was used for a sole proprietorship business, it's reasonable for Bill to allocate 2/3 of the interest expense in the loan to Schedule E and 1/3 to Schedule C. What the interest tracing rules allow you to do is allocate based on any reasonable method. In this case, it was easy to trace how the proceeds were used, so just the dollar amount of how it was used, but here's where we come up with our first twist to these rules.

When debt is secured by a personal use residence, that's your first home, second home, third home, 12th home, personal use home, now not a rental property, not a business property, but a personal use residence. When debt is secured by a personal use residence, the interest, the interest is deductible based on how the loan is secured, not based on how the loan is used.

Let's do an example of Betty, top of Page 1-25 to illustrate that point. Betty owns her home free and clear of any loans. So, no loans at the beginning of the year.

In 2024, she decided to take out a new loan secured by her home for $250,000. Betty used $150,000 in loan proceeds to make improvements to her home and used the remaining $100,000 to make a down payment on a rental property. Of the loan proceeds, 60% was used to buy, build, and improve, that's $150,000, and is therefore classified as acquisition debt. The remaining 40% of the loan proceeds was classified as equity debt. Betty can deduct 60% of her interest on Schedule A, and she cannot deduct her remaining 40% on Schedule A at all because it's classified as equity debt. And under the TCJA, there's no interest deduction for equity debt, nor can she trace the interest to Schedule E unless she makes a 10T election, which we will talk about in just a minute or two.

So, when the going one step further, when the total debt secured by the home is greater than the acquisition debt limit, then taxpayers can trace only the portion of the loan proceeds in excess of the debt limit without using a 10T election. This comes from IRS Chief Counsel and Vice Memorandum. I'll tell you I've got it cited here. Between the two examples on Page 1-25, that Chief Counsel and Vice Memorandum from 2012, is the cleanest and most comprehensive explanation you will get from the IRS on the interest tracing rules, by the way. So, if you really like reading the source material, go see, go read that CCA.

Bottom, Page 25, so, let's apply these rules now when our total debt is greater than the limit and how we can use the interest tracing. This is the example of Megan, bottom of Page 1-25. Megan purchased her home in 2020 and has a mortgage of $500,000, all of which is classified as acquisition debt. In 2024, Megan took out another loan of $400,000 secured by her home. Megan used 40% of the loan proceeds from the new loan to make home improvements and the other 60% to purchase a rental property. I like using rental properties in my examples in this scenario because it's just easy to understand.

So, here in the absence of a 10T election, which we'll discuss a little bit later, Megan will deduct the following on Schedule A. First interest on the first loan, which was all classified as acquisition debt. So, interest in the first 500,000 and then interest on 40% of the second loan because those proceeds were used to buy, build, or improve, so, that's also acquisition debt. So, her acquisition debt deductible on Schedule A – I'm sorry, the acquisition debt for which interest is deductible on Schedule A is $660,000.

Now, without using a 10T election, Megan can trace the remaining amount of her second loan to her Schedule E rental property, but only that portion that's in excess of her $750,000 mortgage limit. And so, here, her applicable mortgage limit, as we said, was 750,000 because her loan was taken out after December 15th, 2017. We have her acquisition debt, which we calculated in the prior part of the example of 660,000 leaves us with loan proceeds for which the interest is neither deductible on Schedule A nor traceable to Schedule E without a 10T election. So, therefore, she can only deduct interest on the first. I'm sorry, interest on $150,000 of that second loan over to Schedule E. That's Megan. That's a little confusing here with interest, isn't it?

So, now let's move on to what on earth is the 10T election. Now, I'm going to tell you right up front, the 10T election can be a little confusing, but one of the things that really seems that rub people the wrong way, if I can say it, is the fact that when we go through this entire process, how do you make a 10T election? And the answer is, you don't. I know that sounds strange.

The IRS doesn't actually require you to attach any kind of an election statement to your tax return. Now, I recommend that you do anyway just because I like having that paper trail there on the tax return. I, I attach a statement to my returns where this applies, but the IRS doesn't require it. You just sort of apply the tracing rules with a 10T election or not, and then keep good records in case you're audited, which is a horrible answer, but that's all that is required by the IRS. I know that's, that's terrible.

But what is a 10T election? So, the 10T election is an election to treat any debt that's secured by a qualified home as if it is not secured by the home. So, what you do is you take a personal use home, a loan on that home, you make a 10T election, and essentially what you're doing is you're severing that secure, that from a, sort of a, a fictional tax scenario, severing the fact that loan is secured by the home, allowing you to therefore trace the proceeds to how the loan was actually used.

But remember, in order to deduct interest on Schedule A, the properties, the, the, the loan has to be secured by the home. So, once you make a 10T election, the 10T election is made per loan. So, it's for a, for a single loan and it's a permanent election for that loan. Once you make a 10T election for that loan, you cannot deduct any interest on that loan on Schedule A because you've severed that security on the property. It's sort of a, a tax fiction that you created by the election.

So, again, if the election is made, the entire loan is treated as not secured by the residence, and the loan proceeds can be traced as to how they're used instead of secured. So, let's give you an example on Page 1-26. This is really a continuation of Megan.

So, assume the facts are the same as the Megan example above, except that Megan makes a 10T election with respect to her second loan. In this case now after the 10T election, Megan has one loan of $500,000. It's classified as acquisition debt. That was her first loan, it was already in place, and now her second loan of $400,000, that is treated as if it is not secured by her home and is therefore not classified as acquisition debt.

So, here with the 10T election, Megan is free to trace the entire $240,000 of loan proceeds that was used to purchase a rental property over to Schedule E, but she cannot therefore then deduct anything on Schedule A from that loan because it's no longer treated as secured by the home.

So, what's the planning pointer here? If you're going to have a client who wants to do something like Megan is doing, take out two new loans on your home if you if possible; right? One that's going to be for the home improvements and a separate loan, that's going to be for the rental property. Make the 10T election for the rental property and therefore you would be able to deduct all of the interest on both of the loans.

Now, there's one more step in the process that we want to talk about here, and that is our debt payoff ordering rules. Because under the regulations there is an ordering to the debt as it's being paid off through the life of the loan, and the ordering I have listed for you in the, in the correct order there at the very bottom of Page 1-26 also comes from the regulations.

So, any time any portion of a debt is repaid, and the debt is allocated to more than one type of expenditure because you've traced it or you've got some equity debt in there, then the debt is deemed repaid in the order we have listed. And this, the debt payoff ordering rules are actually taxpayer friendly because if we look the, the first one is, amounts allocated to personal expenditures. That's the most nondeductible interest, and the last one is acquisition debt. So, if you've got some equity, that's an acquisition that you're deemed to pay off the equity debt first.

And let's look at an example on how that's beneficial to taxpayers. Top of Page 1-27,the last example in this section.

I told you I was going to go through all these examples, but here's the last one.

Nicole is a homeowner and has an, and has had a home – Let's try that again because I'm fumbling my words.

Nicole is a homeowner and has had a home equity line of credit since 2020 that is secured by her home. Nicole drew on her equity line twice. First in 2020 she used $20,000 to renovate her kitchen, classified as acquisition debt right buy, build, or improve the home, and in 2021 she used $10,000 for a European vacation which is personal purposes nondeductible equity debt. The principal balance on Nicole's line of credit on December 31st, 2023, was only $18,000 and the balance on December 31st, 2024, is 13,000, but let's look at this, set the stage at the beginning. She had $20,000 of acquisition debt, $10,000 of equity debt. That was, you know, how she had spent the money.

At the beginning of 2024, the balance was $18,000, which is less than the acquisition debt, which means therefore that she is deemed to have paid off all of the equity debt already. Which therefore means that for the year 2024, all of the remaining debt is classified as acquisition debt, and therefore she has to deduct all of the interest on that debt on Schedule A as acquisition debt. That's how the debt payoff ordering rules are very beneficial to taxpayers.

Okay. Let's move on to charitable contributions.

Page 1-27. Taxpayers can deduct charitable contributions to, quote, what are known as 50% charities for up to 60% of their contribution based to 2025. That was a TCJA provision that totally took our 50% charities and temporarily turned them into 60% charities. You still have the 30 percent, 20% charities, but most of your public charities, those are your 50% charities.

All 2% miscellaneous itemized inductions are still suspended through 2025. I do have for you, top of Page 1-28, though, a list of common non 2% miscellaneous itemized inductions, and those are all still allowed through the TCJA, even during the TCJA years.

199A deduction. We have not had any real new good solid information on 199A ever since COVID hit. Once COVID hit and like PPP and ERC became all the rage, the IRS just started ignoring 199A. Before that they were putting out new guidance and stuff, and they just put that to the back burner. And I'll be honest, over the last four years I've got very few questions from practitioners on 199A.

I think, I'm guessing what happened with 199A with all of our practices is once everybody sort of got the basics figured out in 2018-2019, they sort of put their clients on, you know, okay. You're SSTB, you've got this or that sort of, sort of a set-it-and-forget-it sort of thing, and that's what I think most people have done. But just as a reminder, 199A allows a deduction of up to 20% against the lesser of our clients' qualified business income or their taxable income calculated before 199A and after reducing for net capital gains.

Bottom Page 1-28. What I've got for you is the 199A phaseout chart, updated inflation figures for you.

Yes, so move on to alternative minimum taxes. Our AMT exemption and our AMT exemption phaseout charts are updated there for inflation, middle of Page 1-29. Remember the TCJA heavily, you know, increased our AMT exemption and the AMT exemption phaseout. These are set to expire right now at the end of 2025, you know, barring any extensions or expansion of TCJA provisions. So, get ready right now, get ready. As the law stands now, we're going to see a lot more taxpayers subject to AMT in 2026, unless there's changes.

That investment income tax. Don't forget this. I, for some reason, you know, the, the phone calls I get during the year from clients when they want to sell an asset, whether it's a piece of real estate they own or stocks, they say, "I'm taxing 15%; right?" And that's sort of where they end the discussion. Well, don't forget you could have clients subject to 15% long-term capital gain, 20 percent, 3.8% net investment income tax.

So, don't forget that investment income tax. The net investment income tax thresholds I have for you, chart in the middle of Page 1-30. These ones are actually not adjusted for inflation. So, you are subject to that investment income tax for a married couple filing jointly at $250,000 of income. To give you an idea of what this means when a tax provision is not adjusted for inflation, what that essentially is a, is a slow tax increase over time.

So, applying annual inflation adjustments over the last, oh, eleven years, I think, yeah, eleven years, because the net investment income tax came in in 2013, in today's dollars, a married couple filing jointly, if the net investment income tax had been adjusted for inflation, they wouldn't be subject to it until they hit $339,000 of income, but because the net investment income tax is not subject to inflation adjustments, you still are hitting it in only $250,000 of income. So, every year more and more taxpayers are subject to the net investment income tax on their, well, their investments.

Child tax credit, still $2,000 for children qualifying children, $500 for other dependents for 2024 and 2025. Qualifying children cannot be 17 years old by the end of the year. The credit phaseouts missed it on Page 1-31. If you remember pre TCJA the child tax credit was only $1,000. There was no credit for other dependents, only qualifying children, and it started phasing out once your income hit, AGI hit $110,000 for married couples filing jointly.

So, having a $2,000 credit that doesn't kick in for a married couple, sorry, doesn't phaseout for a married couple until you get $400,000 of AGI is really a big deal, or a really big difference. So, get ready to lose the child tax credit for many people after 2025 without some kind of extension of TCJA provisions.

We still have the child dependent care credit that's available. It's a small credit up to $1,200 maximum. Married couples, though, generally must have filed jointly to claim the credit. The credit, again, is between 20 and 35%, although it goes down to 20% of pretty low-income levels. So, for the most part, we're talking about 20% credit on your eligible expenses. Maximum eligible expenses of $3,000 per child, up to two children maximum. Use Form 2441 for that credit.

Adoption credit updated phaseout charts for you on Page – I'm sorry, updated charts for you, I should say, Page 1-32. Quite simply, you can claim 100% credit or 100% exclusion if, for benefits provided by an employer for costs associated with adopting a child up to the credit limit amounts as shown on that chart of Page 1-32.

Earned income credit. All I've got for you here is updated charts, Page 1-33. Nothing new on the earned income credit, updated charts.

Education credits, nothing changed this year, and we did have a couple of decent changes a couple years ago, if you remember, mainly where the credit phaseout, the AGI phaseout amounts for both the American Opportunity Tax Credit and the Lifetime Learning Credit was sort of married together and had one equal phaseout. And that's shown on the chart that I have for you on Page 1-34. Mainly just a comparison chart here, these two credits because there is nothing new here.

Saver's credit is still available for those lower income clients. Typically, it's going, it's going to be usually, you know, one of the kids that comes in and is starting a job and, you know, they're young, 20s, early job and we're going to claim the credit for them if they put in their retirement account. The big change here, though, is that the Saver's credit in 2026 is going to go away. So, for contributions made after 2026, I guess it's 2027, really, the credit is going to turn into an IRS credit – let me rephrase that, a federal government matching program instead of a tax credit. The IRS still has quite a bit of guidance to put out on this one, and they've got some couple more years to do it and they've got more priorities now. So, we haven't gotten much guidance on this. We'll have more to say on this probably next year or the year after.

Let's move on to the Clean Vehicle Credit. So, I'm going to talk about here mainly the Clean Vehicle Credit under Section 30D and the Used Clean Vehicle Credit under Section 25E. Stan will talk about the qualified commercial Clean Vehicle Credit under Section 45W when he gets to the business chapter in Part 3 of the webinar because that's obviously more business related. I will tell you, though, right up front for a, for a business-passenger-type vehicle, right not your big, you know large commercial trucks over 14,000 pounds, but your, you know, your, your cars, your pickups, your van, you know your smaller vans. Most of the cars that qualify for a Clean Vehicle Credit will qualify for those businesses under either the Section 30D or the 45W credit. You generally want to claim the 45W credit for those business vehicles because the 45W credit does not contain all the same limitations. There's no AGI limitation under 45W. There is no North American assembly requirement. There is no critical component sourcing materials requirement. So, generally the 45W credit will be available for more vehicles and have fewer limitations. But technically for a business vehicle you under 14,000 pounds you could claim the Section 30D credit as well.

Anyway, really quick, Clean Vehicle Credits are nonrefundable credit, maximum credit is $7,500. Businesses who do use the Section 30D to claim their credit, they claim the credit as a general business credit. So, general business credits can be, they do have a little bit of a carryover component, but if you're claiming this credit as an individual credit, which I'm talking about here in Part 1 here, there is no carryover of unused credits.

All three Clean Vehicle Credits, whether it's the 30D, 25E or 45W credits, all claimed on Form 8936. Lessees of clean vehicles do not qualify for the credit. I can't believe people are still asking me that. You lease a vehicle; you don't get a credit.

Now, if the dealer wants to take the credit they get as the owner of the vehicle and pass that credit on to you through savings of some sort when you lease a vehicle, fine, but that's between you and the dealer. That is not you claiming any form of tax credit.

Now, we talked last year a great deal about eligible vehicles, where the materials are sourced and this and that and the other. I don't care about any of that this year, and I don't want you to care about any of that 99% of the time. I'm going to talk about it shortly, but really what I want you to do is I want you to get a copy of Form 15400. For clean vehicles that were sold in 2023, dealers had to provide their clients with, I'm sorry, the buyers with what was known as a “clean vehicle seller's report.” There was no IRS form in 2023, for that. You know, so, dealers just gave it to you on, you know, their letter head and it contained some information that the IRS said it had to contain.

For vehicles sold in 2024 and after, the IRS requires dealers to provide Form 15400. That Form 15400 is given to the buyer at the point of sale for any vehicle that qualifies for either the Section 30D Clean Vehicle Credit or the Section 25E Used Clean Vehicle Credit. If your client gets a copy of that form and you have that form in hand, your life is infinitely easier because you know when you have that form in hand that the vehicle qualifies. Now, both the Clean Vehicle Credit Section 30D and the Used Clean Vehicle Credit Section 25E have an AGI requirement. You still have to worry about whether your client qualifies for the credit because of the, their AGI limitation. But when you have the Form 15400 in hand, you know right then and right there that the car qualifies, meaning the car meets the MSRP requirement. The car's critical components are in are, are sourced where they're supposed to be. The car was assembled in North America, all those requirements.

If the car does not qualify, the dealers are instructed not to fill out the form. So, what I want you to do is to tell your client, “Give me a copy of Form 15400.” If your client says, “Well the dealer didn't give me one.” “Guess what? The car doesn’t qualify, and you can't claim the credit.” So, put the onus on your client, make them go get the form. If they cannot produce a Form 15400, then that nice plug-in car they bought doesn't qualify because it wasn't, you know, assembled in North America, or it's got some defect that makes it not qualify for the credit your client is trying to convince you that it does qualify for. So, get a copy of the form.

When it comes to AGI limitations for the Clean Vehicle Credit under Section 30D, in the Page 1-38, filing status cannot be greater than the amounts I have listed at the chart in the middle of Page 1-38 for, um, cannot exceed those amounts. And so, as long as your client's income is, for example, married couple filing jointly, is $300,000 or less in either the year they bought the car or the prior taxable year, then they qualify. So, only if they're over that AGI limitation in both years do they not qualify.

But again, if you have got the Form 15400 in hand, this is going to be the only thing you have to worry about. Do we qualify for basically AGI? And these amounts are not adjusted for inflation, which means that fewer people are going to be able to claim the Clean Vehicle Credits over time.

If the, your client's filing status has changed during that two-year testing period for the AGI, the year they bought the car the prior year, you apply the AGI limitation based on your client's filing status for those two years. So, if your client was single last year in 2023, you apply the AGI limitation to a single person, and then they're married in 2024, you apply the AGI limitation to a married person to determine whether they meet that two-year testing period.

When a passthrough entity claims a Clean Vehicle Credit, if that passthrough entity is going to claim the 30D credit, which I don't recommend, I, I said earlier, if it's a business vehicle, you should generally be claiming that 45W credit 99% of the time, but if you do claim the Section 30D Clean Vehicle Credit for passthrough entity, that passthrough entity, either on 1065 or the 1120-S is going to file the Form 8936 to claim the vehicle as a credit, your client's going to get a K-1 that says, “Here's your share of the credit for the vehicle.” And then your client has to apply that, has to then file their own Form 8936, which sort of, that 8936 is used as sort of the AGI filter to see if your client qualifies for AGI purposes, and then the credit's going to go down to Form 8300 – I'm sorry 3800, to determine whether you can use the credit for the general business credit, because there's a general business credit, if we're claiming the credit as a business on a business vehicle.

The vehicle MSRP for the Clean Vehicle Credit cannot exceed the, the dollar amount listed on Page 1-39. Again, I don't care. Don't spin your wheels figuring out the MSRP. Just get from your client the Form 15400. If the vehicle’s

MSRP qualifies, your client will receive a Form 15400. The MSRP does not qualify, the dealer will not provide a Form 15400. Now, I'll will say it 100 times if I have to. The Form 15400, if you have that in hand, you know that the vehicle qualifies for the credit. The only question there is does the taxpayer qualify, and that's for you to figure out.

We can, starting in 2024, claim advanced credits at the dealership for either the 30D credit or the 25E Used Clean Vehicle Credit. Can only claim the credit at the time of sale. You can't go back to the dealer later. If you claim the credit of the dealer, you've got to claim the entire credit.

The IRS says you can only claim two advanced credits at the dealership during the year. So, if you buy three vehicles that qualify, and miraculously if you buy three and your AGI still qualifies you, you can still claim three vehicle credits, but only two can you claim as advanced credits at the dealership.

Now, unfortunately with the Form 15400, it will not tell you on the form, the face of the form does not indicate whether your client claimed an advanced credit. That is a bit of a bummer. I wish it did. It'd make things a little easier for us but get a copy of the form. If your client can't produce it, then the car does not qualify because of the car, the vehicle – let me rephrase it. If the, if the dealer does not provide or won't provide form 15400, then the vehicle does not qualify for the credit. So, get a copy of the form. If the client can't produce it, tell them, "I'm sorry. You have to have this form to file. If you don't have it, you don't qualify for the credit. Doesn't matter what the salesman said."

Joint ownership. Only one taxpayer can claim the Clean Vehicle Credit. It cannot be split, exception though, for passthrough entities. Remember I said each person or each owner on a passthrough entity will get their share of the credit. That's sort of an exception there, but the bottom line is this is another reason for you to get a copy of the Form 1540, because the Form 15400 only lists one taxpayer and one social or EIN. Whoever is listed on the Form 15400, that is the taxpayer who must claim the credit.

So, if you and your, as if you, you're the parents and you cosign for a car for your mid-20s, you know, kid, because they don't have any credit yet because they just got out of college. If your name is the one listed on the 15400, you're the one that can claim the credit. Your kid cannot.

Also, this is an issue with small business clients. They want to buy a car. "Oh, yeah. I bought a car for my business," but they didn't actually buy it for their business. They bought it personally, and they're just using it in their business. So, are you going to try to claim the Clean Vehicle Credit on, do you say their Form 1120-S corporate return on their 1040? Get a copy of the Form 15400. If the Form 15400 has their personal name and social, you better not try to claim that credit on the Form 1120 Yes, the IRS will reject it because it won't meet the matching system. You only claim that vehicle on the taxpayers listed on the Form 15400.

Credit Recapture. If it turns out your client claimed an advance credit at the dealer but their AGI wasn't high enough. In that case, they have to pay the credit – I'm sorry, if their AGI was too high, they will have to pay the credit back when they file their income tax return.

There is an exception here where if your client claims an advance credit at the dealership, but it turns out that when you file the income tax return, your client's taxable income is low enough they can't claim the entire credit, the IRS won't make them pay back the excess. So, because of that it does, it is to your client's advantage to claim the credit at the dealership whenever possible.

Used claim vehicle credit, very similar requirements, lower dollar amounts, nonrefundable credit, unused credits can be carried forward. The credit is 30% of the purchase price up to $4,000. Maximum car's price cannot exceed $25,000, but once again, I don't want you to worry about that. If that car qualifies, get a copy of the Form 15400 because one of the, one of the requirements, for example, for a Used Clean Vehicle Credit is the, the car can only be, you – I'm sorry, let me rephrase that – The car only qualifies for the Used Clean Vehicle Credit for the first qualifying resale of the vehicle. If this is the second qualifying resale, the dealer's not going to give your client form, copy of Form 15400, only if the vehicle qualifies. So, if your client can't produce Form 15400, no credit, don't claim the credit. Get a copy of that form.

Don't you let, don't let your client tell you that the car qualifies while also telling you that the, the dealer refuses to provide Form 15400. Those two things cannot be true at the same time.

So, like I said, if you've got the Form 15400 in hand, when it comes to the Clean Vehicle Credit under Section 30D, you only have to worry about whether your client's AGI limitation qualifies.

The used Clean Vehicle Credit you have two things to worry about. One, whether your client's AGI qualifies, and whether this is on, they purchased another used clean vehicle within three years because you can only claim the 25E credit on a vehicle purchased once every three years. That's based on the purchase date of the prior vehicle, not the tax year. AGI limitations for the used Clean Vehicle Credit, middle of Page 1-44, if you're interested.

Move on the energy efficient home improvement credit. This is the credit for energy efficient windows and doors. This used to be a $500 lifetime credit that everybody claimed four times. It is now a $3,200 annual credit. Credit is 30% multiplied by the cost of whatever improvements they made, but you can't just take the improvements multiplied by 30% and get yourself a $3,200 annually.

There are separate limitations within each type of property, which combined can get you to $3,200. For example, your maximum credit for an efficient air conditioning unit is $600. You put in a $10,000 air conditioning unit, multiplied by 30%, you can't claim a $3,000 credit. It's still limited to $600 because that's the limit for AC units. And I have the limitation for listed for each type of property, top of Page 1-46. There is a list for you, so, keep that in mind when it comes to this credit.

The home must be located in the United States, and it's got to be an existing home. You cannot claim a credit for energy improvements installed by the home builder.

Moving on to the residential clean energy credit, we all know this as the solar credit. The reality, though, is this applies to much more than just solar. It applies to solar energy property, qualified fuel cell property, small wind energy property, geothermal heat pump property, biomass stoves, water heaters and a qualified battery storage. Think of your home batteries in that scenario. That's what qualifies under this credit. This credit, though, you do simply take the total amount multiplied by 30%. There is no maximum credit. There is no maximum lifetime credit.

Now while the, the residential clean energy credit is nonrefundable, any unused credits do carry forward indefinitely. So, you can claim this credit on, on any personal-use property. So, if you own 10 homes and you put solar on all 10 homes this year, you can claim a very large solar credit on all of those ten homes. The only requirement here though, so the only hitch is the fuel cell property. If you install fuel cell property, that particular line item must be your principal residence. All other items can be first home, second home. You could even be a renter in putting on solar and claim the solar credit. Weird if you did that, but technically you could do it. Let's move on to I want to move past this premium tax credits starting on Page 1-51. What I've got here for you is just updated the charts for you on the premium tax credit. Remember, the federal government still does not charge for not having health insurance.

Nanny Tax threshold for 2024 is $2,700. It kicks up the $2,800 for 2025. Don't forget applies to any household employees, not just nanny as we call it the "Nanny Tax," but you know, if you got a client who's got, you know, 10 acres of, of gardens and they got a couple of full-time gardeners that could they that, that would qualify for them as well. Federal taxes can be reported and paid annually on the taxpayer Schedule H.

College savings. The SECURE 2.0 Act does now allow us to take excess 529 funds and roll them over into Roth IRA starting in 2024. You've got a $35,000 lifetime limit and an annual IRA, IRA contributions apply, so, you can only put it up to $7,000 a year if you're under age 50. AGI limits don't apply though. So, ideally here, let's say you've got a kid graduates college, has excess 529 funds because maybe they got scholarships or something. So, good for them, and they get a high paying job out of college. So, maybe they make too much to put into a Roth IRA, but they have 529 funds leftover. They can still put into the company's 401k that they have and then take $7,000 a year and put that into the Roth IRA every year from their 529 until they reach the $35,000 lifetime limit. So, kind of a cool thing to do there.

On Page 1-55, I've got a chart of allowable 529 expenses. If you are paying for college with 529 funds. We've got a list of those items that you're allowed to spend on.

On Page 1-56 to 1-58, I have some tips for you. I don't really want to go through them, but I put them here just as a reference. And this is for taxpayers who receive administrative adjustment request, if they receive a pushed-out adjustment either from an audit or an administrative adjustment request on that Form 8986. How do you go about taking that Form 8986 and reporting those adjustments on your client's current income tax return and filling out that Form 8978? How do you do it as a staff member? And so, what I have here for you is a, just a six-step process.

If you get a client who's a partner in a partnership and you get that Form 8986 in the hand and you say, “What on earth do I do with this thing?” Go right here to, to, to where, to my materials, and just follow my 6 steps. Do this, do that, do the other thing. It will walk you through the process of making the adjustments and what to attach to that tax return. It's a very practical guide there at the end of the individual chapter. That is a question that has come up quite a bit lately in the last couple years, you know, now that CPAR is really, really in full swing, and so I've got that for you.

SUPPLEMENTAL MATERIALS

Individuals

FILING DEADLINE IS APRIL 15, 2025

The filing deadline for 2024 personal income tax returns is Tuesday, April 15, 2025.

California Conformity

California conforms to the April 15, 2025, filing deadline for individuals.

PERSONAL EXEMPTIONS AND DEPENDENTS

NO PERSONAL EXEMPTION DEDUCTION

TCJA EXPIRING

The Tax Cuts and Jobs Act (TCJA) suspended the personal and dependent exemption deduction for taxable years 2018 through 2025. For tax year 2024, it remains at zero. (IRC §151(d)(5))

Even though the personal exemption deduction is suspended, the personal exemption amount is still adjusted annually for inflation for other purposes:

- It is used as part of the gross income test when determining whether a qualifying relative can be claimed as a dependent (IRC §152(d)(1)); and

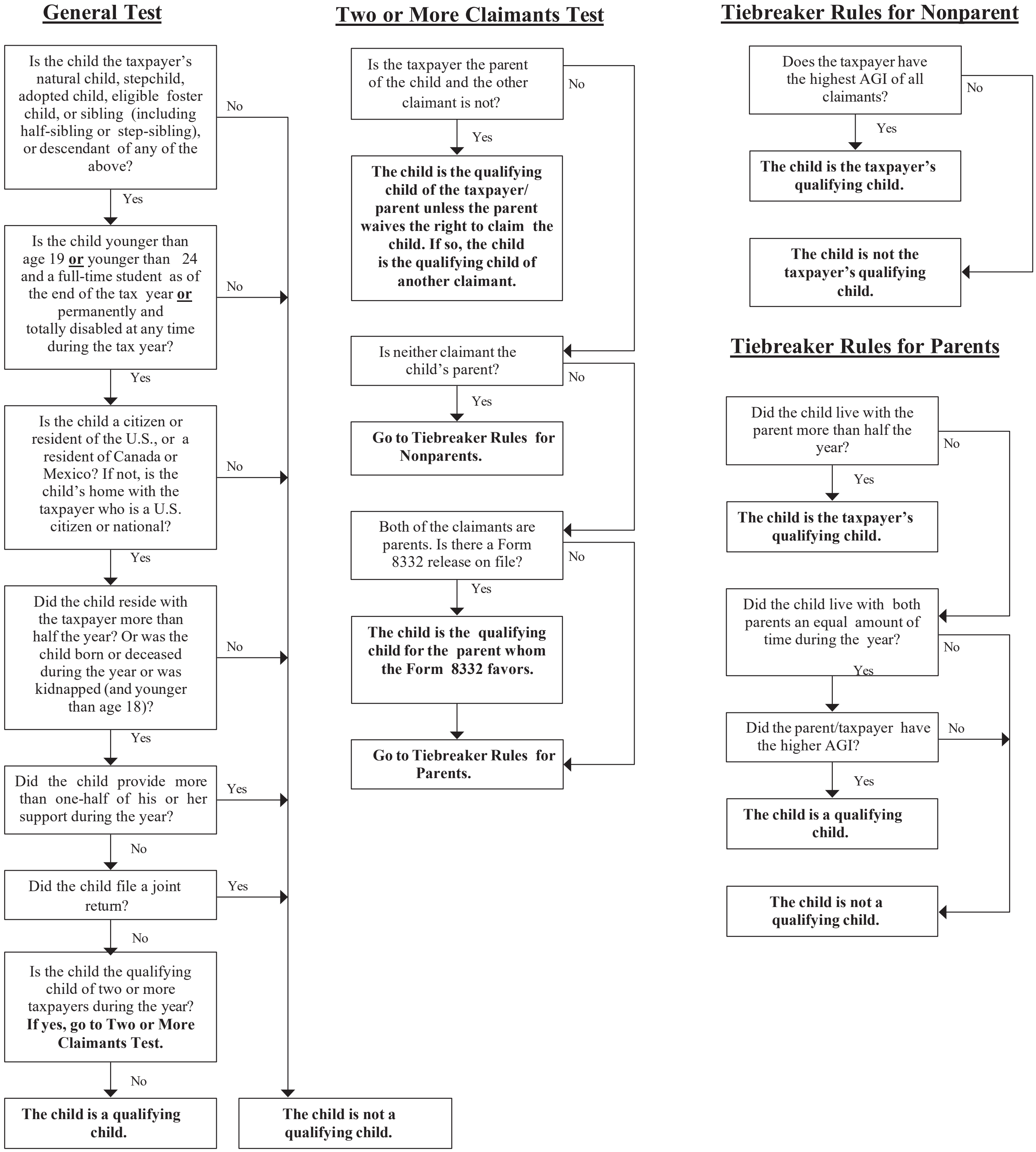
- For purposes of the maximum $500 credit for an "other dependent" under the Child Tax Credit (see discussion beginning on page 1-31). (IRC §24(h)(4))

Personal Exemption Amount	
2024 (Rev. Proc. 2023-34)	**2025 (Rev. Proc. 2024-40)**
$5,050	$5,200

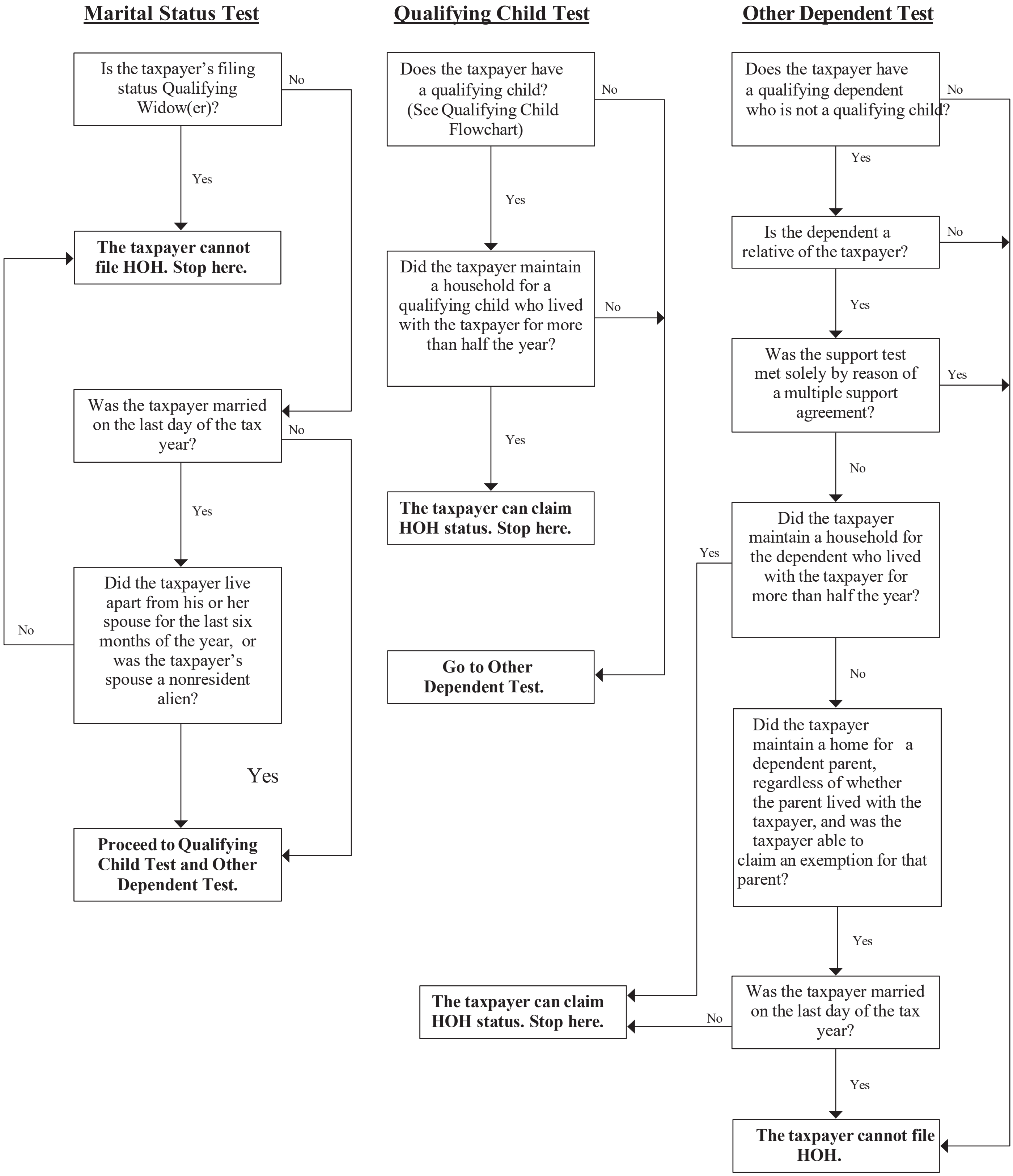
California Nonconformity

California provides personal exemption credits rather than a deduction. (R&TC §17054) These credits are phased out when a taxpayer's federal AGI exceeds a threshold amount (see page 12-39). (R&TC §17054.1)

Qualifying Child Flowchart: California Conforms



Head of Household Flowchart: California Conforms



<u>FILING ISSUES</u>

FILING REQUIREMENTS

Taxpayers Who Must File

A taxpayer must file an income tax return if their gross income is greater than their applicable standard deduction. (IRS Publication 501, Table 1) However, in the case of a married taxpayer filing separately, a return must be filed if the taxpayer's gross income is at least $5.

If a taxpayer's gross income is not greater than their standard deduction (or $5 in the case of a married taxpayer filing separately), then the taxpayer must nevertheless file a return if any of the following applies:

- The taxpayer owes any special taxes reported on Schedule 2 (if any line on Schedule 2 applies);
- The taxpayer (or spouse if filing jointly) received Archer medical savings account (MSA), Medicare Advantage MSA, or health savings account (HSA) distributions;
- The taxpayer had net earnings from self-employment of at least $400;
- The taxpayer had wages of $108.28 or more from a church or qualified church-controlled organization that is exempt from employer Social Security and Medicare taxes;
- Advanced payments of the Premium Tax Credit were made for the taxpayer, spouse, or dependent who enrolled in coverage through the health insurance Marketplace;
- The taxpayer has a net tax liability under the TCJA's IRC §965 transition tax (applicable to U.S. shareholders of controlled foreign corporations) that they are paying in installments under IRC §965(h) or deferred by making an election under IRC §965(i); or
- The taxpayer claimed an advanced clean vehicle credit at a dealership. See page 1-36 for a complete discussion of clean vehicle credits. (IRS Publication 501, Table 3)

Taxpayers who *should* file

Taxpayers who are not required to file an income tax return should still file if they are entitled to claim a refund or a refundable credit. (IRS Publication 501) Taxpayers who don't have to file but should file include those who:

- Had income tax withholding;
- Made estimated tax payments for the year or had overpayments applied from the prior year; or
- Qualify for a refundable tax credit, including the:
  - Earned Income Credit;
  - Refundable Child Tax Credit;
  - Refundable American Opportunity Tax Credit;
  - Credit for federal tax on fuels;
  - Premium Tax Credit; or
  - Child and Dependent Care Credit.

Practice Pointer

While not specifically listed in IRS Publication 501 as reasons taxpayers should file a return, taxpayers should consider filing if:

- They think they will have a filing requirement in the next year or two (to avoid missing tax return notices); and
- The taxpayer has carryovers of tax attributes, such as capital loss carryovers, passive loss carryovers, or other tax attributes that are beneficial to track year over year.

Kiddie Tax Rules

Children who meet the following listed requirements must attach Form 8615, Tax for Certain Children Who Have Unearned Income, to their income tax return. If the requirements are met, the child's unearned income is taxed at their parents' highest marginal income tax rate. All of the following conditions must be met:

- The child's unearned income was more than $2,600 in 2024 ($2,700 for 2025);
- The child meets one of the following age requirements:
  - Under age 18 at the end of the tax year;
  - At least age 18 at the end of the tax year and didn't have earned income that was more than one-half of the child's support; or
  - Was a full-time student at least age 19 and under age 24 at the end of the tax year and didn't have earned income that was more than one-half of the child's support;
- At least one of the child's parents was alive at the end of the tax year;
- The child is required to file a tax return for the year; and
- The child didn't file a joint return for the year. (IRC §1(g)(2)).

Which parent's tax rate applies?

In the case of parents who are not married, the tax rate of the custodial parent is used to determine the kiddie tax. (IRC §1(g)(5)(A))

In the case of married taxpayers living together and filing separately, the parent with the greater taxable income is the one whose tax rate applies to determine the kiddie tax. (IRC §1(g)(5)(B))

Parents' Election to Report Child's Interest And Dividends

Instead of filing Form 8615 and attaching it to their child's income tax return, parents can elect to report their child's income on their own return using Form 8814, Parents' Election to Report Child's Interest and Dividends. Parents are eligible to make the election if their child meets all of the following conditions:

- At the end of the tax year the child was under age 19 (or under age 24 if a full-time student);
- The child's gross income was less than the standard deduction for a single filer ($14,600 for the 2024 tax year);
- The child had income only from interest and dividends (including capital gain distributions and Alaska Permanent Fund dividends);
- No estimated tax payments were made for the child for the tax year, and no overpayments from the previous tax year (or from any amended return) were applied to the current tax year under the child's name and Social Security number;
- No federal income was withheld from the child's income under the backup withholding rules;
- The child is required to file a federal return unless this election is made;
- The child does not file a joint return for the tax year; and
- The parent is qualified to make the election because they are either the custodial parent, the parent with higher taxable income when the parents' filing status is married filing separate, or both the child's parents file a joint return.

California Conformity

California conforms to the kiddie tax rules currently in effect. (R&TC §17041)

Planning Pointer

Taxpayers can limit the kiddie tax bite by making investment decisions that will reduce the child's unearned income, including:

- Deferring capital gains to the following year or until the child is old enough that the kiddie tax rules no longer apply to them;
- Defer gifts of income-producing property until the dependent is old enough to not be subject to the kiddie tax rules;
- Utilize tax-deferred investments, such as U.S. savings bonds or certificates of deposit or Treasury bonds that won't mature in the current year;
- If the child has earned income, make investments for them into a Roth IRA so the account appreciation is not taxable; and
- Consider putting investment dollars into a §529 college savings account, which will grow tax-deferred, and the earnings will never be taxed if used for qualifying expenses. And thanks to the SECURE 2.0 Act, up to $35,000 of excess §529 funds can be rolled over into a Roth IRA (see page 1-54).

GROSS INCOME

CAPITAL GAINS

Gain or loss from the sale of capital gain property (such as investments) held more than one year is treated as a long-term capital gain or loss. (IRC §1222(3) and (4)) Property held one year or less is treated as short-term. (IRC §1222(1) and (2))

Long-term capital gains (as well as qualified dividends) are taxed at preferential tax rates that are lower than the ordinary income tax rates and detailed in the following chart. Short-term capital gains are taxed at ordinary income rates.

TCJA EXPIRING

Individual Long-Term Capital Gains Rates (IRC §1(h))		
Rate	**Taxable income breakpoint (2024) (Rev. Proc. 2023-34)**	**Taxable income breakpoint (2025) (Rev. Proc. 2024-40)**
0%	Single: $47,025 MFS: $47,025 MFJ: $94,050 HOH: $63,000 Estates and trusts: $3,150	Single: $48,350 MFS: $48,350 MFJ: $96,700 HOH: $64,750 Estates and trusts: $3,250
15%	Single: $518,900 MFS: $291,850 MFJ: $583,750 HOH: $551,350 Estates and trusts: $15,450	Single: $533,400 MFS: $300,000 MFJ: $600,050 HOH: $566,700 Estates and trusts: $15,900
20%	No breakpoint	No breakpoint

WASH SALE RULES

Taxpayers are prohibited from claiming a loss from a wash sale. A wash sale occurs when a taxpayer sells or trades stock or securities at a loss and within 30 days before or after the sale:

- Buys substantially identical stock or securities;
- Acquires substantially identical stock or securities in a fully taxable trade;
- Acquires a contract or option to buy substantially identical stock or securities; or
- Acquires substantially identical stock in the taxpayer's IRA or Roth IRA. (IRC §1091)

Ordinarily, stocks or securities of one corporation are not considered substantially identical to stocks or securities of another corporation. However, they may be substantially identical in some cases. For example, in a reorganization, the stocks and securities of the predecessor and successor corporations may be substantially identical. (IRS Publication 550)

Example #1 of wash sale rules

Jack owns 100 shares of X Corp. stock that he purchased for $10,000. On January 12, 2024, Jack sold the 100 shares for $7,500, thus generating a $2,500 capital loss.

On January 30, 2024, Jack bought 100 shares of the same X Corp. stock for $8,000.

Because Jack bought substantially identical stock within 30 days of January 12, 2024 (the date he sold his first 100 shares of X Corp. stock for a loss), he cannot deduct his $2,500 loss on the sale.

However, Jack's disallowed losses aren't gone forever. Jack must add the disallowed loss of $2,500 to the cost of the new stock, as follows:

Cost of substantially identical stock purchased on 1/30/24	$ 8,000
Disallowed wash sale losses	2,500
Basis of stock acquired on 1/30/24	$10,500

Example #2 of Wash Sale Rules

Shelly is an employee of M Corp., which has a stock incentive plan for its employees. Under the stock incentive plan, Shelly was given 100 shares of M Corp. stock valued at $15,000 as a bonus award on March 31, 2022.

Shelly included the $15,000 fair market value of the stock in her gross income as additional taxable compensation in 2022, which was reflected on her W-2 for that year.

On December 10, 2024, Shelly sold the 100 shares received on March 31, 2022, for $9,000, thus generating a $6,000 capital loss. On December 31, 2024, Shelly received another bonus award for 100 more shares of M Corp. stock valued at $11,000.

The wash sale rules apply in this scenario because Shelly acquired substantially identical stock in the December 31, 2024, bonus award as the shares she sold within 30 days before. As such, the $6,000 capital losses generated from the December 10, 2024, stock sale are disallowed, but Shelly will add the $6,000 wash sale loss to her basis of the shares acquired on December 31, 2024, as follows:

Value of substantially identical stock acquired on 12/31/24	$11,000
Disallowed wash sale losses	6,000
Basis of stock acquired on 12/31/24	$17,000

Cryptocurrency

Wash sale rules do not apply currently to cryptocurrency because cryptocurrency is not a security. Because the wash sale rules do not apply to cryptocurrency transactions, cryptocurrency owners can sell their cryptocurrency at a loss, lock in the loss amount to apply against the taxpayer's other capital gain, and then turn around and purchase the same cryptocurrency at the reduced rate without having to wait 30 days to do so.

Money Market Funds

The IRS will not treat the redemption of one or more shares of any money market fund as part of a wash sale. (IRC §1091; Rev. Proc. 2023-35)

DEFERRED GAIN FROM QUALIFIED OPPORTUNITY ZONE INVESTMENTS

TCJA EXPIRING

Under the TCJA, taxpayers with income from capital gains from 2018 through 2026 could elect to defer their capital gains until December 31, 2026, if:

- The proceeds (or a portion thereof) from the sale of any property to an unrelated party giving rise to their capital gain is reinvested in a Qualified Opportunity Fund within 180 days; and

- The capital gain arises from non-Opportunity Zone assets before December 31, 2026 (this can be capital gain from any property including, for example, the sale of publicly traded stock). (IRC §1400Z-2(a))

Taxpayers who made the election must begin planning ahead for their cash needs when the gain deferral comes due on December 31, 2026.

Example of QOZ Cash Needs

Paul realized capital gains of $500,000 in 2019 that he invested in a Qualified Opportunity Fund and elected to defer the gains under the TCJA's Qualified Opportunity Zone rules laid out in IRC §1400Z-2.

The gain deferral rules allowed Paul to put off federal recognition of the $500,000 of capital gain until December 31, 2026. Paul must be ready to recognize and pay federal income tax on the $500,000 of capital gain on his 2026 income tax return.

Practice Pointer

Taxpayers make the election to defer capital gains invested in Qualified Opportunity Zones on Form 8949, Sales and Other Dispositions of Capital Assets. If you are unsure whether a client has made the gain deferral election, then reviewing Form 8949 for each tax return from 2018 through the present will provide the answer.

California Nonconformity

California does not conform to most TCJA provisions, including the capital gain deferral provision for investments in Qualified Opportunity Zones. As such, taxpayers who made the capital gain deferral election on their federal return would have already paid California tax on the gain and will not incur an additional tax burden in 2026 when the federal gain recognition comes into play

HOME ENERGY REBATES

The IRS announced that the home energy rebates authorized under the Inflation Reduction Act of 2022 (IRA '22) are treated as reductions in purchase price even if paid directly to the purchaser and not the manufacturer or installer. As such, these amounts are not includible in gross income under IRC §61. Furthermore, state agencies granting the rebates are not required to provide 1099s for these rebates. However, the rebates will result in a reduction in basis for any items purchased. (IRS Announcement 2024-19)

California Conformity

California conforms to this exclusion.

In contrast, payments of these home energy rebates made directly to a business taxpayer, such as a contractor, in relation to their sale of energy efficiency products or services are includable in the business's gross income under IRC §61 and may be subject to information reporting requirements.

The IRA '22 provides $4.3 billion of funding to state governments to provide Home Owners Managing Energy Savings (HOMES) rebates to low- and moderate-income homeowners. The rebates are available for both whole-house energy saving retrofits and high-efficiency home electrification projects.

The rebate programs are administered by the states.

Which states are offering rebates?

The rebate programs have just recently become available in certain states. All states, other than South Dakota, have indicated they are applying to the U.S. Department of Energy to offer these rebates. The DOE has released an interactive map that shows which states have applied, have been approved, or are currently offering the rebates. The map is available at:

Website

www.energy.gov/save/rebates

Maximum Allowable Home Energy Rebates		
Type of home energy project	**Per household below 80% area median income (AMI)**	**Per household above 80% area median income (AMI)**
Home efficiency project with at least 20% predicted energy savings	80% of project costs up to $4,000	50% of project costs up to $2,000 (maximum of $200,000 for a multifamily building)
Home efficiency project with at least 35% predicted energy savings	80% of project costs up to $8,000	50% of project costs up to $4,000 (maximum of $400,000 for a multifamily building)
Home electrification project qualified technologies (only households with an income below 150% of AMI are eligible	100% of project costs up to technology cost maximums (see note below); up to $14,000	50% of project costs up to technology cost maximums (see note below); up to $14,000 (households with incomes above 150% AMI are not eligible

Note: The maximum rebated costs for home electrification project qualified technologies:

- ENERGY STAR electric heat pump water heater, up to $1,750;
- ENERGY STAR electric heat pump for space heating and cooling, up to $8,000;
- ENERGY STAR electric heat pump clothes dryer, up to $840;
- ENERGY STAR electric stove, cooktop, range, or oven, up to $840;
- Electric load service center, up to $4,000;
- Electric wiring, up to $2,500; and
- Insulation, air sealing, and ventilation, up to $1,600.

A low- or moderate-income household is an individual or family whose total annual income is less than 80% of the median income of the area in which the individual or family resides. (IRA ’22§50121(d)(3))

To put the program income level eligibility criteria in context, below are the 2024 80%-of-median income figures for an individual and a household of four in the following cities:

80% of Area Median Income (AMI) Figures		
City	**Individual**	**Family of four**
Atlanta	$54,000	$77,120
Chicago	$62,800	$89,700
Dallas	$61,800	$88,250
Los Angeles	$77,700	$110,950
Miami	$63,550	$90,800
New York City	$86,960	$124,240
San Francisco	$83,900	$119,900
Seattle	$77,700	$110,950

Interplay with credit for energy efficient homes

Taxpayers who claim the Energy Efficient Home Improvement Credit under IRC §25C and received a HOMES rebate for the same property must reduce the cost of the energy efficient property by the amount of the rebate when calculating their tax credit.

Example of rebate and credit interplay

Malcolm purchases an electric heat pump water heater for $2,000 and receives a $400 home energy rebate toward the purchase. Malcolm does not include the $400 in his taxable income. His IRC §25C credit is $480 ($1,600 × 30%).

Additional information available

Additional information about these rebates is available on the U.S. Department of Energy’s website at

Website
www.energy.gov/scep/home-energy-rebates-programs

<u>EXCLUSIONS FROM INCOME</u>

FOREIGN-EARNED INCOME EXCLUSION

In 2024, a U.S. individual living abroad can exclude up to $126,500 of foreign-earned income if the taxpayer’s tax home is in a foreign country and the taxpayer satisfies either the *bona fide* residence test or the physical presence test. (IRC §911; Rev. Proc. 2023-34) The exclusion applies separately to spouses; as such, if both spouses are qualified individuals, they may exclude up to $253,000 on a jointly filed return.

The 2025 foreign-earned income exclusion amount is $130,000. (Rev. Proc. 2024-40)

California nonconformity

California does not conform to the foreign-earned income exclusion. (R&TC §17024.5) California taxes California residents on their worldwide income. Each year, the IRS provides the FTB with a list of taxpayers who took the foreign-earned income exclusion on the federal return.ir worldwide income. Each year, the IRS provides the FTB with a list of taxpayers who took the foreign-earned income exclusion on the federal return.

Qualified taxpayers

The foreign-earned income exclusion can be claimed by a qualified individual, who is defined as one whose tax home is in a foreign county and who is:

- A U.S. citizen with a *bona fide* residence in a foreign country for an uninterrupted period which includes an entire taxable year (*bona fide* residence test); or
- A U.S. citizen or resident who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period (physical presence test).

An individual is not treated as having a tax home in a foreign country for any period for which their domestic ties (i.e., familial, economic, and personal ties) to the U.S. outweigh the ties to the foreign country they claim as their tax home.

Caution

Taxpayers often claim the foreign-earned income exclusion based on the two qualification tests but lose their exclusion on audit because they are not treated as having a tax home in a foreign country.

Determining whether a taxpayer has a tax home in a foreign country is a facts and circumstances test. Often members of the military or those working for multinational businesses on multiyear assignments will claim the foreign-earned income exclusion but cannot prove that their tax home is in the foreign country. Examples include:

- An American pilot working for Korean Airlines in South Korea was unable to prove that his tax home was in South Korea because he owned a home in New Hampshire where his family lived, and he lived in employer-provided housing while in South Korea (***Acone v. Comm.*****,** TCM 2017-162); and
- A taxpayer who worked as a government contractor and who lived on a military base in a foreign country was unable to prove that her tax home was in the foreign country because she maintained her driver's license, home, and bank accounts in Arizona. (***Haskins v. Comm.*** (September 8, 2020) U.S. Court of Appeals, Eleventh Circuit, Case No. 20-10692, aff'g ***Haskins v. Comm.*****,** TCM 2019-87)

The ***Haskins*** case was decided before the Bipartisan Budget Act of 2018, which amended the definition of "tax home." Now, contractors or employees of contractors supporting U.S. Armed Forces in designated combat zones may claim the foreign-earned income or housing exclusion, even if their "abode" is within the U.S. (IRC §911(d)(3)) These contractors/employees must still meet the *bona fide* residence test or the physical presence test to claim the exclusion.

Claiming the Exclusion

In addition to meeting the qualification requirements for the foreign-earned income exclusion, a taxpayer must also make an affirmative election to exclude foreign-earned income. (IRC §911(a)(1))

In order to make a valid election, it must be made:

1. With an income tax return that is timely filed (including any extensions of time to file);
2. With an amended return within the applicable statute of limitations;
3. With an original income tax return that was filed within one year after the due date of the return (determined without regard to any extension of time to file); or
4. If a taxpayer makes the foreign-earned income election on a return filed after the periods specified above, the election will still be valid if:
   a. The taxpayer owes no federal income tax after taking into account the exclusion; or
   b. The taxpayer owes federal income tax after taking into account the exclusion and files Form 1040 with Form 2555, Foreign Earned Income, or a comparable form attached to the return before the IRS discovers that the taxpayer failed to elect the exclusion. (Treas. Regs. §1.911-7(a)(2)(i))

   The election is made by attaching to a timely filed return Form 2555, Foreign Earned Income. (Treas. Regs. §1.911-7(a)(1))

Practice Pointer

A taxpayer filing under the fourth method above must print, at the top of the first page of Form 1040, "Filed Pursuant to Section 1.911-7(a)(2)(i)(D)."

COMPENSATION FOR INJURIES OR SICKNESS

Under IRC §104, gross income does not include amounts received under workers' compensation acts as compensation for personal injuries or sickness unless the compensation offsets amounts deducted as medical expenses under IRC §213. (IRC §104(a)(1))

To be excluded for workers' compensation, the payments must:

- Be received under a workers' compensation act or under a statute in the nature of a workers' compensation act;
- Be compensation for personal injuries or sickness;
- Not be related to the employee's age or length of service; and
- Be incurred in the course of employment. (Treas. Regs. §1.104-1(b))

Wrongful Termination due to Health Issues

In a Tax Court Summary opinion, a taxpayer argued that the settlement she received from her former employer for wrongful termination was excludible as compensation for injuries or sickness under IRC §104(a). (***Quevy v. Comm.***, TCS 2023-34)

Following a years-long series of injuries and health setbacks, the taxpayer's employer terminated her, which led to her claim of discrimination and wrongful termination. The company the taxpayer worked for agreed to pay her $75,000, which was characterized as severance compensation. Neither the settlement agreement nor the initial demand letters from the taxpayer's attorney referred to "physical injury."

On her return for the year in which the settlement was paid, the taxpayer excluded 90% of the settlement payment because she believed it was paid on account of personal injury or sickness, or as compensation for amounts paid for medical care attributable to emotional distress. The court held that the facts and circumstances showed that the taxpayer was compensated for wrongful termination and not personal physical injuries or physical illness.

DEPENDENT CARE ASSISTANCE

Taxpayers can exclude up to $5,000 of employer-provided dependent care assistance from their gross income ($2,500 for married taxpayers filing separately). (IRC §129(a)(2))

Dependent care assistance includes:

- Amounts paid by an employer directly to either the employee or the employee's care provider for the care of a qualifying person while at work;
- The fair market value of care in a daycare facility provided or sponsored by the employer; and
- Pretax contributions made by the employer under a dependent care flexible spending arrangement.

The maximum income exclusion for dependent care benefits is the smallest of:

- The total dependent care benefits received during the year;
- The total amount of qualified dependent care expenses incurred during the year;
- The taxpayer's earned income;
- The taxpayer's spouse's earned income; or
- The maximum dependent care exclusion ($5,000, or $2,500 in the case of married taxpayers filing separately).

California conformity

California conforms to the IRC §129 dependent care assistance exclusion. (R&TC §17131)

FLEXIBLE SPENDING ACCOUNTS

Employer cafeteria plans can include one or more flexible spending accounts (FSAs). An FSA is an employer benefit designed to reimburse employees for expenses incurred for certain qualified benefits. (Prop. Treas. Regs. §1.125-5(a))

Employer flex-credits are nonelective contributions that an employer makes available for every employee eligible to participate in the cafeteria plan, to be used at the employee's discretion only for one or more qualified benefits through the plan (but not as cash or other taxable benefits). (Prop.Treas. Regs. §1.125-5(b))

There are three types of FSAs:

- Dependent care assistance;
- Adoption assistance; and
- Medical care reimbursements (health FSAs).

A health FSA may be limited to a subset of permitted IRC §213(d) medical expenses, or it may be an HSA-compatible limited-purpose health FSA or post-deductible health FSA. (Prop. Treas. Regs.§1.125-5(m)) A health FSA cannot reimburse premiums for accident and health insurance or long-term care insurance. (IRC §125(f))

An employee who chooses to participate in either an adoption assistance FSA or a health FSA can contribute up to \$3,200 through payroll deductions during the 2024 plan year (\$3,300 in 2025). (Rev. Procs. 2023-34, 2024-40) Amounts contributed are not subject to federal income tax, Social Security tax, or Medicare tax. Unused FSA funds are forfeited and revert back to the employer at the end of the FSA's plan year.

The limit for dependent care FSAs is \$5,000 (\$2,500 for married taxpayers filing separately). The dependent care FSA limit is not indexed annually for inflation.

For FSAs that permit the carryover of unused amounts, the maximum 2024 carryover amount to 2025 is \$640.

FSA Reporting on W-2

FSAs allow employees to be reimbursed for medical, dependent care, or adoption assistance from an account the employee sets up with pretax dollars. The salary reduction contributions made by the employee aren't included in taxable wages, so they are not required to be reported on the employee's W-2. However, it is possible that the employer will include the FSA on box 14, but it's an information item only.

Note that dependent care FSAs are different from employer paid dependent care benefits, which are reported on Form W-2, box 10.

<u>ADJUSTMENTS TO GROSS INCOME</u>

UNREIMBURSED EXPENSES OF K–12 EDUCATORS

The maximum above-the-line deduction for eligible educator expenses is \$300 (\$600 per spouse if both taxpayers on a joint return are eligible educators) for 2024 and 2025. (IRC §62(a)(2)(D))

California nonconformity

California has never conformed to the above-the-line educator expenses deduction. (R&TC§17072) Because California does not conform to the suspension of the 2% miscellaneous itemized deductions enacted by the TCJA, K-12 educators can claim a miscellaneous itemized deduction for unreimbursed employee expenses on their California return.

ALIMONY

Alimony is not deductible by the payor spouse nor included in the recipient spouse's gross income if the divorce or written separation agreement is executed after December 31, 2018. (IRC §§71, 215) In California, a separation or property settlement agreement can be executed and effective before a divorce becomes final.

Alimony paid pursuant to a divorce or written separation agreement in place on or before December 31, 2018, remains deductible by the payor spouse and included in the income of the recipient spouse (grandfathered agreements). This is also true for grandfathered agreements that are modified after December 31, 2018. However, if the modified agreement expressly provides that the TCJA applies to the modification, then the agreement will lose its grandfathered status

The alimony rules in effect after 2018 were created by the TCJA and are one of the few TCJA provisions for individual taxpayers that are permanent changes to the Internal Revenue Code.

Practice Pointer

Request a copy of your client's alimony agreement and keep it in your permanent file no matter when it was executed. Do this for any clients either paying or receiving alimony

California nonconformity

California has not conformed to the TCJA provision that changed how alimony is taxed.

Alimony is deductible by the payor and included in the recipient's income no matter the date of the divorce or separation agreement for California income tax purposes. (R&TC §17024.5)

STUDENT LOAN INTEREST

A taxpayer may deduct up to $2,500 of interest on debt incurred solely to pay qualified higher education expenses. (IRC §221)

AGI Phaseout Ranges for Student Loan Interest Deduction		
Beginning taxable year	**Single, HOH, MFS (did not live with spouse)**	**MFJ**
2024 (Rev. Proc. 2023-34)	$80,000–$95,000	$165,000–$195,000
2025 (Rev. Proc. 2024-40)	$85,000–$100,000	$170,000–$200,000

California conformity

California fully conforms to the student loan interest deduction. (R&TC §§17024.5, 17201)

HEALTH SAVINGS ACCOUNTS

The inflation-adjusted limitations for health savings accounts (HSAs) under IRC §223(g) are listed in the following table:

Inflation-Adjusted Limitations for HSAs						
	2023 (Rev. Proc. 2022-24)		**2024 (Rev. Proc. 2023-23)**		**2025 (Rev. Proc. 2024-25)**	
	Family	**Self only**	**Family**	**Self only**	**Family**	**Self only**
Contribution limit	$7,750	$3,850	$8,300	$4,150	$8,550	$4,300
Additional catch-up contribution for taxpayer age 55 or older	$1,000 per qualifying spouse	$1,000	$1,000 per qualifying spouse	$1,000	$1,000 per qualifying spouse	$1,000
Minimum health insurance deductible	$3,000	$1,500	$3,200	$1,600	$3,300	$1,650
Maximum out of pocket	$15,000	$7,500	$16,100	$8,050	$16,600	$8,300

HSA Planning

HSA plans allow participants to invest in mutual funds. Similar to an employer's 401(k) plan, the HSA plan will contain a menu of mutual fund investments the participant can choose.

For taxpayers who remain healthy and do not spend all their HSA funds on health insurance each year, the account can grow tax-deferred in the same way a 401(k) or IRA plan does. If the taxpayer spends their HSA funds on qualifying medical expenses, then none of the distribution is taxable, even the earnings on the account.

At age 65, taxpayers can take distributions from their HSA for any reason without penalty. However, the distributions are taxable if not used for medical purposes.

✐ **Practice Pointer**

Taxpayers who accumulate funds in their HSA must be proactive when it comes to investing their money. HSA plans will typically have options for taxpayers to invest accumulated HSA funds in mutual funds, but this doesn't happen automatically.

Talk to clients about whether their HSA has accumulated funds, and if it has, make the client aware of their investment options. Otherwise, the client may find their funds sitting in an account paying only a low rate of interest.

HSAs and Medicare

Taxpayers are ineligible to contribute to an HSA in any month during which the taxpayer is both eligible for benefits under Medicare and is enrolled to receive benefits under Medicare. (IRS Notice 2008-59, Q&A #5; IRS Notice 2004-50, Q&A #s 2 and 3)

✐**Practice Pointer**

IRC §223(b)(7) states that a taxpayer ceases to be eligible to contribute to an HSA starting with the month the taxpayer becomes entitled to receive benefits under Medicare. Even though taxpayers become eligible to receive Medicare benefits starting with the month they turn age 65 (earlier in the case of disability), the IRS interprets the term "entitled to benefits under Medicare" to mean both eligible and enrolled in Medicare. (Notice 2004-50, Q&A #2)

Thus, an otherwise eligible individual who is not actually enrolled in Medicare can still contribute to an HSA until the month that individual is actually enrolled in Medicare.

California nonconformity

California does not conform to the federal tax rules for HSAs. (R&TC §§17131.4, 17131.5) Thus, a taxpayer with an HSA must:

Include annual income or loss from investments in HSA accounts in California AGI;

Increase the medical expense deduction for any qualified expenses paid out of the HSA account; and

Reduce California income by any taxable distributions from an HSA.

Caution

California W-2 wages must be increased by the amount of the employer's federal HSA contribution. This is one more reason it's important to always check the California wages box on the W-2 when preparing personal returns, in addition to reporting amounts that contain a code W in box 12 on the Form W-2. Verify that your software has made the adjustment on Schedule CA (540).

STANDARD DEDUCTION AND ITEMIZED DEDUCTIONS

STANDARD DEDUCTION

TCJA EXPIRING

Standard Deductions (IRC §63)			
Filing status	**2023 (Rev. Proc. 2022-38)**	**2024 (Rev. Proc. 2023-34)**	**2025 (Rev. Proc. 2024-40)**
Married filing joint and qualifying widow(er)	$27,700	$29,200	$30,000
Head of household	$20,800	$21,900	$22,500
Single	$13,850	$14,600	$15,000
Married filing separate	$13,850	$14,600	$15,000

Additional Standard Deductions for Elderly and/or Blind			
Filing status	**2023**	**2024**	**2025**
Unmarried			
Elderly or blind	$1,850	$1,950	$2,000
Elderly and blind	$3,700	$3,900	$4,000
Married			
Elderly or blind (per taxpayer)	$1,500	$1,550	$1,600
Elderly and blind (per taxpayer)	$3,000	$3,100	$3,200

California nonconformity

California does not increase standard deductions for the elderly or blind. (R&TC §17073.5(b)) Instead, California allows an additional exemption credit for age and blindness. (R&TC §17054) See page 12-39 for California standard deduction amounts.

TCJA EXPIRING

ITEMIZED DEDUCTION PHASEOUT

The overall limitation on itemized deductions is suspended through December 31, 2025. (IRC §68)

California Nonconformity

California continues to phase out itemized deductions using 6% of federal AGI as reported on the federal return. (R&TC §17077) Generally, a taxpayer's itemized deductions are reduced by the lesser of:

- 6% of the excess federal AGI over the threshold amount (see page 12-39); or
- 80% of the itemized deductions otherwise allowable.

MEDICAL EXPENSES

Out-of-pocket medical expenses that are not reimbursed by insurance are deductible as an itemized deduction to the extent they exceed 7.5% of the taxpayer's adjusted gross income. (IRC §213(a))

Eligible expenses

Eligible medical expenses are those paid for:

- The diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body;
- Transportation primarily for and essential to medical care;
- Qualified long-term care services; or
- Insurance. (IRC §213(d)(1))

Medicine and drugs are only classified as eligible medical expenses if they are prescribed by a doctor or are insulin. (IRC §213(b)) However, HSA, FSA, Archer MSA, and HRA funds can be used to pay for, or reimburse the taxpayer for, over-the-counter drugs, medicine, and menstrual care products.

California Conformity

California conforms to the 7.5% of AGI threshold. Remember, California uses *federal* AGI to compute this threshold. (R&TC §17241)

Medical Mileage Rates

Medical Mileage Rate	
Beginning taxable year	**Rate per mile**
2024 (IRS Notice 2024-08)	$0.21
2025 (IRS Notice 2025-05)	$0.21

California Conformity

California automatically conforms to the federal medical mileage rates. (R&TC §§17024.5, 17201)

Long-Term Care Insurance

For 2024, up to $5,880 in premiums paid for long-term care insurance, per person, can qualify as a deductible medical expense. (IRC §213; Rev. Proc. 2023-34) The maximum deduction for 2025 is $6,020. (Rev. Proc. 2024-40)

Self-employed individuals may include their qualified long-term care insurance premiums in the self-employed health insurance deduction, subject to the maximum deduction limits listed here. (IRC §162(l)(1))

Keep three things in mind:

1. The deduction is limited based on the taxpayer's age;

2. Only premiums paid for "qualified long-term care" plans are deductible;

3. Qualified long-term care premiums can be included as part of a taxpayer's self-employed health insurance deduction on Form 7206.

Long-Term Care Premium Deduction Limits		
Age of individual before close of tax year	**Maximum deductible premium for 2024 (Rev. Proc. 2023-34)**	**Maximum deductible premium for 2025 (Rev. Proc. 2024-40)**
40 or less	$470	$480
More than 40 but not more than 50	$880	$900
More than 50 but not more than 60	$1,760	$1,800
More than 60 but not more than 70	$4,710	$4,810
More than 70	$5,880	$6,020

California Conformity

California automatically conforms to the federal long-term care deduction limitations. (R&TC §§17024.5, 17201)

Funding Long-Term Care Insurance

Long-term care insurance can be costly, and taxpayers often have difficulty finding room in their budget to fund the premiums. For taxpayers who have life insurance, a §1035 exchange may be the right answer.

Typically, selling or surrendering a life insurance contract can give rise to taxable gain if the sale proceeds or surrender value of the contract is greater than the taxpayer's adjusted basis in the contract.

IRC §1035 allows taxpayers to exchange their life insurance policy tax-free for another life insurance policy, an endowment contract, an annuity contract, or a qualified long-term care contract. (IRC §1035(a)(1))

STATE AND LOCAL TAXES (SALT)

TCJA EXPIRING

For taxable years 2018 through 2025, taxpayers may claim an itemized deduction of up to$10,000 ($5,000 in the case of married taxpayers filing separately) for the aggregate of state and local income taxes and property taxes (the "SALT" limitation). (IRC §164(b)(6))

Taxpayers may still make an election to deduct sales and use tax rather than income tax (also subject to the $10,000 limit).

California Nonconformity

Although California does not allow a deduction for state and local income taxes, it does allow an unlimited deduction for real and personal property taxes. (R&TC §17220)

California SALT Cap Workaround

In 2021, California enacted a passthrough entity elective tax, which is its version of the SALT cap workaround allowable by IRS Notice 2020-75. (AB 150 (Ch. 21-82)) See page 10-1 for a discussion of California's passthrough entity elective tax. See page 5-44 for a discussion of how a passthrough entity should report passthrough entity elective taxes on the business return.

California's passthrough entity elective tax sunsets automatically on the earlier of December 31, 2025 (when the TCJA's $10,000 SALT limitation sunsets) or when the federal government repeals its SALT limitation.

CASUALTY AND THEFT LOSSES

TCJA EXPIRING

For taxable years 2018 through 2025, casualty losses are limited only to losses sustained in Presidentially declared disasters. (IRC §165(h)(5)(A))

Personal casualty and theft losses attributable to a federally declared disaster are subject to the $100 per casualty and 10% of AGI deductions unless they are attributable to a qualified disaster that occurred in 2020 or earlier. (Form 4684 instructions) Qualified disasters are specifically identified disasters that are afforded additional beneficial treatment and are specifically listed in the Form 4684, Casualties and Thefts, instructions.

Election to Take Deduction for Preceding Year

Taxpayers who suffer casualty losses incurred due to a Presidentially declared disaster can elect to take the deduction for the preceding taxable year. (IRC §165(i)) This provision is designed to help taxpayers who sustain losses during major disasters to get immediate tax relief via refunds if they file this election.

The election is made on Form 4684, Casualties and Thefts, Section D, Part I.

California Nonconformity

California does not conform to the TCJA regarding casualty and theft losses. Therefore, taxpayers can still claim casualty losses on their California return without regard to whether the casualty or theft loss occurred in a Presidentially declared disaster. (R&TC §§17024.5, 17201)

Non-Personal Use Property

The casualty and theft loss limitation under the TCJA for taxable years 2018 through 2025 does not apply to casualty and theft losses on:

- Business property;
- Income-producing property; and
- Ponzi-type investment schemes.

Emerging Artificial Intelligence Schemes

A.I. schemes are on the rise and are being used to fraudulently induce taxpayers to pay fake ransoms or make other payments under false pretenses. In one very scary emerging scheme, thieves use A.I. to mimic a loved one's voice on a phone call and claim to hold the loved one hostage, demanding an immediate ransom payment. Such ransom payments are classified as theft, but the theft generally is personal in nature and is therefore not deductible through 2025 because the theft isn't from a Presidentially declared disaster.

However, if the fake ransom were paid in a business setting, then the ransom can be deductible as a business theft loss. For example, where hackers take control of a business's computer systems and demand a ransom before giving control back to the business, the ransom would be deductible.

TCJA EXPIRING

HOME MORTGAGE INTEREST

For tax years 2018 through 2025, taxpayers may treat no more than $750,000 as deductible acquisition indebtedness ($375,000 for married taxpayers filing separately). (IRC §163(h)(3))

Interest on home equity debt is not deductible for tax years 2018 through 2025 no matter when the debt was incurred under additional changes made by the TCJA.

Acquisition Debt

Acquisition debt is defined as any debt that is:

- Used to buy, build or substantially improve a qualified residence of the taxpayer; and
- Is secured by the qualified residence. (IRC §163(h)(3)(B))

A qualified residence is the taxpayer's principal residence, plus up to one additional residence, which is selected by the taxpayer and is used by the taxpayer as a residence. (IRC §163(h)(4)(A))

> **Practice Pointer**
>
> Debt secured by the residence that used to buy out a former spouse (usually due to divorce) is classified as acquisition debt (up to the acquisition debt limit). This is true even though buying out a former spouse pursuant to a divorce does not provide additional basis to the spouse who keeps the property.

Debt Incurred on or Before December 15, 2017

In the case of acquisition indebtedness incurred on or before December 15, 2017, the $1 million limitation ($500,000 for married taxpayers filing separately) still applies. Pre-December 16, 2017, debt includes refinanced pre-December 16, 2017, debt but only to the extent of the balance of the debt prior to refinancing. (IRC §163(h)(3)(F)(iii)(I))

Example of Refinancing Pre-December 16, 2017, Debt

Prior to December 16, 2017, Arnold bought his personal residence by taking out a mortgage of $1 million. In 2024, when the mortgage balance is $800,000, he refinances the loan taking out a mortgage of $950,000. Arnold uses the additional $150,000 cash generated from his new loan to make a combination of home improvements and for other personal expenses. He is limited to deducting interest on only $800,000 of the debt.

Assume instead that Arnold had originally taken out a mortgage of $500,000, and in 2024, the mortgage had a balance of $350,000. In 2024, he refinanced the mortgage with a new $450,000 mortgage. How much interest Arnold can deduct depends on how much of the extra $100,000 he uses to improve the property. Assume that he uses $75,000 to improve the property and the remaining $25,000 for personal purposes. Arnold will deduct interest on $425,000 of the mortgage.

Equity indebtedness is not deductible, even if it was incurred prior to December 16, 2017.

California nonconformity

California does not conform to the TCJA limits on mortgage interest, so taxpayers may continue to claim a deduction for interest on acquisition debt of $1 million and equity debt of $100,000, regardless of the date of the loan. (R&TC §§17024.5, 17201) California does not allow a deduction for mortgage insurance premiums. (R&TC §17225)

Deduction is Per Taxpayer, Not Per Residence

The limitation of indebtedness for qualified residence interest is determined on a per-taxpayer basis and not on a per-residence basis. (IRB 2016-31; ***Voss v. Comm.*** (2015) 796 F.3d 1051) Married taxpayers are deemed to be a single taxpayer for these purposes. Thus, two (or more) unmarried co-owners are individually limited to a deduction for interest paid on the first $750,000 of acquisition debt ($1 million for acquisition debt incurred on or before December 15, 2017).

Practice Pointer

If two people own a home and deduct mortgage interest on two separate returns, then each person should report the mortgage interest differently on Schedule A to avoid an automated matching problem by the IRS.

The person whose name appears first on Form 1098, Mortgage Interest Statement (the one whose SSN or TIN is on Form 1098), should report mortgage interest on Form 1040, Schedule A, line 8a (Home mortgage interest and points reported to you on Form 1098).

The person(s) whose name does not appear first on the Form 1098 should report mortgage interest on Form 1040, Schedule A, line 8b (Home mortgage interest not reported to you on Form 1098).

Mortgage Interest Deduction for Nonowners

Taxpayers who are "equitable owners" of a property are entitled to a deduction for mortgage interest paid, even when they do not hold legal title to the property as an owner or are liable for the mortgage

Generally, for interest payments to be deductible, two conditions must be met:

- The taxpayer must make the payments; and
- The underlying debt must be an obligation of the taxpayer.

However, the regulations provide that "interest paid by the taxpayer on a mortgage upon real estate of which he is the legal or equitable owner, even though the taxpayer is not directly liable upon the bond or note secured by such mortgage, may be deducted as interest on his indebtedness." (Treas. Regs. §1.163-1(b); ***Uslu v. Comm.***, TCM 1997-551)

Factors contributing to establishing equitable ownership include:

- The right to possess the property and to enjoy its use, rents, or profits;
- A duty to maintain the property;
- Responsibility for insuring the property;
- Whether the taxpayer bears the property's risk of loss;
- An obligation to pay property taxes, assessments, or charges;
- The right to improve the property without the owner's consent; and
- The right to obtain legal title at any time by paying the balance of the purchase price. (***Blanche v. Comm.***, TCM 2001-63; ***Uslu v. Comm.***, TCM 1997-551)

It is important to note that these are only factors that are weighed in a court's decision and do not represent an exhaustive list of requirements that must be met.

State Law is Important

State law determines the nature of property rights, and federal law determines the tax consequences of those rights, so it is important for a practitioner to become familiar with areas of state law that may affect property rights, such as community property and probate laws. (***United States v. Nat'l Bank of Commerce*** (1982) 472 U.S. 713, 722; ***Blanche v. Comm.***, TCM 2001-63)

Interest Tracing

When a taxpayer uses loan proceeds for more than one purpose, they can trace the loan proceeds to where they were used and deduct interest accordingly. (Treas. Regs. §1.163-8T(a)(3)) When allocating interest between more than one use, taxpayers can use any reasonable calculation method, but must use the same method year over year.

Example of simple interest tracing

Bill took out a personal loan of $150,000. He used $100,000 of the loan proceeds as a down payment on a rental property and $50,000 of the loan proceeds as seed money to start a sole proprietorship business.

Because two-thirds of the loan proceeds were used for a rental property and one-third was used for a sole-proprietorship business, it is reasonable for Bill to allocate two-thirds of the interest expense from the loan to Schedule E and one-third to Schedule C.

Home Mortgage Rules Create a Complicated Twist

Generally, interest on a loan is allocated based on the use of the loan proceeds, as illustrated in the example of Bill above. (Treas. Regs. §1.163-8T(a)(3)) There is an exception to this rule: The character of interest on a personal residence is determined by how the debt is *secured*. If the debt is secured by a personal residence, the interest is deductible as home mortgage interest on Schedule A, but only if the debt is acquisition debt and only up to the mortgage interest limitation, which is currently $750,000 for debt incurred after December 15, 2017. (IRC §163(h)(3))

When the total debt secured by the home is equal to or less than the home mortgage debt limitation ($750,000 of acquisition debt for debt incurred after December 15, 2017), then interest cannot be traced away from Schedule A without a "10T" election, discussed later. (CCA 201201017)

Example of Interest Deduction When Total Loan is Under $750,000

Betty owns her home free and clear of any loans. In 2024, she decides to take out a new loan secured by her home for $250,000. Betty uses $150,000 (60%) of the loan proceeds to make improvements to her home and uses the remaining $100,000 (40%) to make a down payment on a rental property.

Of the loan proceeds, 60% ($150,000) was used to buy, build, or improve Betty's home and is therefore classified as acquisition debt. The remaining 40% of the loan proceeds ($100,000) is classified as equity debt.

Betty can deduct 60% of her loan interest on Schedule A, and she cannot deduct the remaining 40% on Schedule A (because it's classified as equity debt) nor can she trace the interest to Schedule E unless she makes a 10T election (discussed later).

When the total debt secured by the taxpayer's home is greater than the mortgage interest debt limitation ($750,000 of acquisition debt for debt incurred after December 15, 2017), then taxpayers can trace the portion of the loan proceeds in excess of the home mortgage debt limitation away from Schedule A without having to use a 10T election. (CCA 201201017; Treas. Regs. §1.163-10T(e)(4))

Example of Interest Deduction When Total Loan is in Excess of $750,000

Megan purchased her home in 2020 and has a mortgage of $500,000, all of which is classified as acquisition debt. In 2024, Megan took out another loan of $400,000 secured by her home.

Megan uses 40% of the loan proceeds ($160,000) from the new loan to make home improvements and uses the other 60% ($240,000) to purchase a rental property.

In the absence of a 10T election (discussed later), Megan will deduct the following interest on Schedule A:

Interest on first loan (all acquisition debt)	$500,000
Interest on 40% of second loan (all acquisition debt)	160,000
Acquisition debt for which interest is deductible on Sch. A	$660,000

Without using a 10T election (discussed later), Megan can trace the remaining amount of her second loan to her Schedule E rental property that is in excess of her $750,000 mortgage interest limitation, calculated as follows:

Applicable mortgage interest limitation	$750,000
Acquisition debt (see above)	(660,000)
Loan proceeds not deductible on Sch. A nor traceable to Sch. E	$ 90,000

Therefore, only $150,000 of the new loan proceeds can be traced to Schedule E, and only interest on that portion is deductible on Schedule E:

Loan proceeds used to acquire rental property	$240,000
Loan proceeds not deductible on Sch. A nor traceable to Sch. E (see above)	(90,000)
Loan proceeds that traceable to Schedule E	$150,000

The 10T Election

A taxpayer can choose to treat any debt secured by a qualified home as not secured by the home—this is also known as the "10T election." (Temp. Treas. Regs. §1.163-10T(e)(4)) If the election is made, then the entire loan is treated as not secured by the residence, and the debt proceeds can be traced to their use without the mortgage interest limitation illustrated in the preceding Megan example.

The election under Treas. Regs. §1.163-10T(o)(5) applies to the whole amount of a loan and not to part. The election is made on a loan-by-loan basis. This treatment begins with the tax year for which the election is made and continues for all later tax years. The election may be revoked only with the consent of the IRS.

Example of Interest Deduction When Total Loan is in Excess of $750,000 Limitation

Assume the facts are the same as the Megan example above, except that Megan makes the 10T election with respect to her second loan.

After the 10T election, Megan has one loan of $500,000 of acquisition debt and one loan of $400,000 that is treated as if it is not secured by her home and is therefore not acquisition debt.

With the 10T election, Megan is free to trace the entire $240,000 of loan proceeds used to purchase her rental property to Schedule E, but she cannot deduct any portion of the loan on Schedule A because only debt that is secured by Megan's residence is deductible on Schedule A

☑ Planning Pointer

Megan from the prior two examples could have maximized her interest deduction by taking out two additional loans instead of one: One loan for the $160,000 of home improvements and another loan for the $240,000 rental property acquisition.

By doing so, Megan could deduct all of the interest on the $160,000 loan as acquisition debt on Schedule A, and then she could have made a 10T election for the second loan, allowing her to trace the entire additional loan to Schedule E.

Debt Payoff Ordering Rules

The regulations provide that if, at any time, any portion of a debt is repaid and the debt is allocated to more than one expenditure (such as acquisition debt and equity debt), then the debt is treated as repaid in the following order:

- Amounts allocated to personal expenditures;
- Amounts allocated to investment expenditures and passive activity expenditures (other than passive activity expenditures described in the next bullet point);
- Amounts allocated to passive activity expenditures in connection with a rental real estate activity with respect to which the taxpayer actively participates;
- Amounts allocated to former passive activity expenditures;
- Amounts allocated to trade or business expenditures and to expenditures with respect to certain low-income housing projects; and lastly
- Acquisition debt. (Treas. Regs. §1.163-8T(d)(1)).

Example of Using Debt Repayment Ordering Rules to Determine Equity Debt

Nicole is a homeowner and has had a home equity line of credit since 2020 that is secured by her home. Nicole drew on her equity line twice: In 2020, she used $20,000 to renovate her kitchen (acquisition debt), and in 2021 she used $10,000 for a European vacation (equity debt).

The principal balance on Nicole's line of credit on December 31, 2023, was $18,000, and the balance on December 31, 2024, is $13,000.

The debt-payoff ordering rules allow Nicole to allocate payments on her equity line to personal expenditures first (equity debt). Therefore, because the principal balance on Nicole's line of credit for all of 2024 was less than the amount she spent for her kitchen renovation (acquisition debt), she can treat the entire balance of her equity line as acquisition debt in 2024. Her equity debt was extinguished prior to 2024 according to the repayment ordering rules.

CHARITABLE CONTRIBUTIONS

TCJA EXPIRING

Taxpayers who itemize their deductions may deduct charitable contributions to qualified charities of up to 60% of their "contribution base." A taxpayer's contribution base is their adjusted gross income computed without regard to any net operating loss carryback. (IRC §170(b)(1)(H)) Net operating loss carryforwards to the current tax year are computed as part of the taxpayer's contribution base.

California Conformity

California conforms, with modifications, to the IRC §170 charitable contributions deduction prior to any COVID-19 legislation, meaning that California's deduction is limited to 50% of their contribution base. (R&TC §§17024.5, 17201, 17275.5)

Charitable Remainder Trusts

Charitable remainder trusts remain a popular tax and income planning tool for sophisticated taxpayers. Charitable remainder trusts and new proposed regulations cracking down on specific transactions within them are discussed in more detail at page 3-46.

TCJA EXPIRING

MISCELLANEOUS ITEMIZED DEDUCTIONS

All 2% miscellaneous itemized deductions, without exception, are disallowed for tax years 2018 through 2025. (IRC §67(g)) Generally, miscellaneous itemized deductions not subject to the 2% floor remain fully deductible. Some of the most common non-2% miscellaneous itemized deductions include:

- **Casualty and theft losses from income-producing property:** This includes property held for investment, such as stocks, notes, bonds, gold, silver, vacant lots, and works of art (see page 1-21 for disallowance of casualty losses for loss of personal property);
- **Federal estate tax on income in respect of a decedent;**
- **Loss from other activities from Schedule K-1 (Form 1065-B), box 2 (large partnerships);**
- **Unrecovered investment in an annuity:** In the event of a retired taxpayer who dies before the entire investment in an annuity is recovered tax-free, any unrecovered amount is deducted on the retiree's final income tax return;
- **Claim of right deductions;** and
- **Gambling losses.**

California Nonconformity

California does not conform to the suspension of the 2% miscellaneous deductions. These deductions may still be claimed on the California return. (R&TC §§17024.5, 17076)

TCJA EXPIRING

QUALIFIED BUSINESS INCOME DEDUCTION

IRC §199A allows taxpayers to claim a deduction of up to 20% against qualified business income (QBI). Taxpayers whose taxable income is above a phaseout threshold may have their QBI deduction limited or completely phased out.

Taxpayers whose income is below the phaseout range receive a QBI deduction of 20% of the lesser of:

- QBI; or
- Taxable income before the IRC §199A deduction and after reduction for net capital gains (this is referred to as the taxable income limitation).

How much of a taxpayer's QBI deduction is phased out depends on many factors, including whether a taxpayer's qualified business income is deemed to be from a specified service trade or business (SSTB) and/or the amount of the W-2 wages paid by the taxpayer's business and the unadjusted basis of assets immediately before acquisition.

IRC §199A Phaseout Range		
Filing status	**2024 (Rev. Proc. 2023-34)**	**2025 (Rev. Proc. 2024-40)**
Married filing joint	$383,900–$483,900	$394,600–$494,600
Married filing separate	$191,950–$241,950	$197,300–$247,300
Single and HOH	$191,950–$241,950	$197,300–$247,300
Note: The above are taxable income amounts immediately before the IRC §199A deduction and are not reduced for net capital gains		

California Nonconformity

California does not conform to IRC §199A, so there is no QBI deduction. (R&TC §§17024.5, 17201)

TAX CALCULATION

ALTERNATIVE MINIMUM TAX AND CREDITS

AMT Exemption

The AMT exemption amount is adjusted annually for inflation.

AMT Exemption Amounts		
Filing status	**2024 (Rev. Proc. 2023-34)**	**2025 (Rev. Proc. 2024-40)**
Single, HOH	$85,700	$88,100
MFJ, surviving spouse	$133,300	$137,000
MFS	$66,650	$68,500
Estates and trusts	$29,900	$30,700

AMT Exemption Phaseout		
Filing status	**2024 (Rev. Proc. 2023-34)**	**2025 (Rev. Proc. 2024-40)**
Single, HOH	$609,350–$952,150	$626,350–$978,750
MFJ, surviving spouse	$1,218,700–$1,751,900	$1,252,700–$1,800,700
MFS	$609,350–$875,950	$626,350–$900,350
Estates and trusts	$99,700–$219,300	$102,500–$225,300

California Nonconformity

California law provides for an annual inflation adjustment of AMT phaseout and exemption numbers. California's numbers are different than federal (see page 12-39). (R&TC §17062(b)(5)(A)–(C) and (b)(6)(A)–(C))

SELF-EMPLOYMENT TAX

Taxpayers are subject to the self-employment tax if their net earnings from self-employment are $400 or greater ($100 for church employees). (IRC §1402(b) and (j)(2)(B)) Taxpayers are self-employed if they:

- Carry on a trade or business as a sole proprietor or independent contractor;
- Are partners of a partnership that carries on a trade or business; or
- Are otherwise in business for themselves (including part-time businesses). (IRC §1402(a))

The Limited Partner Exception

Taxpayers who are limited partners in a partnership (including non-managing members of an LLC) are generally not subject to self-employment tax on their distributive share of net income. (IRC §1402(a)(13))

The Tax Court analyzed the limited partner exception in a case decided at the end of 2023 dealing with a limited partnership. (***Soroban Capital Partners, LP, et al., v. Comm.*** (November 28, 2023) 161 T.C. 12) See page 5-6 for a complete discussion of the limited partner exception, as well as a discussion of the ***Soroban*** case and others.

NET INVESTMENT INCOME TAX (NIIT)

The 3.8% net investment income tax is imposed on an individual for the lesser of:

- Net investment income; or
- The excess of modified adjusted gross income for the taxable year, over the threshold amount. (IRC§1411(a)(1))

The threshold amounts are:

NIIT Threshold Amounts	
Filing status	**NIIT threshold**
MFJ and qualifying widow(er)	$250,000
MFS	$125,000
Single and HOH	$200,000
Note: The NIIT thresholds are not adjusted annually for inflation	

For estates and trusts, the net investment income tax is imposed on the lesser of:

- The undistributed net investment income; or
- The excess of modified adjusted gross income over the dollar amount at which the highest tax bracket begins for an estate or trust for the tax year ($15,200 for 2024 and $15,650 for 2025).

Modified adjusted gross income, for purposes of the NIIT, is defined as the taxpayer's adjusted gross income for regular income tax purposes increased by the foreign-earned income exclusion (but also adjusted for certain deductions related to the foreign-earned income). (IRC §1411(d))

IRC §1411(c)(1) defines "net investment income" as gross income from interest, dividends, annuities, royalties, and rents, other than such income that is derived in the ordinary course of a trade or business not described in IRC §1411(c)(2). The IRS has held that all dividends paid by a C corporation, even those paid by a closely held C corporation where the shareholder was a material participant, are subject to the net investment income tax. (CCA 202118009)

IRC §1411(c)(2) provides that the net investment income tax applies to income derived in the ordinary course of business if that business is a passive activity with respect to the taxpayer.

INDIVIDUAL TAX CREDITS

TCJA EXPIRING

CHILD TAX CREDIT

The maximum Child Tax Credit is $2,000 per qualifying child and $500 for other dependents for the 2024 and 2025 taxable years. (IRC §24(h)).

Qualifying children must have a Social Security number that is issued by the due date of the taxpayer's income tax return, including extensions. Taxpayers who fail to obtain an SSN for their qualifying child by the due date of their income tax return, for whatever reason, are still eligible for the $500 credit available for other dependents under IRC §24(h)(4)(A).

Qualifying Child

A qualifying child is an individual who has not reached age 17 during the taxable year. (IRC §24)

Phaseouts of the Credit

The Child Tax Credit is phased out, but not below zero, by $50 for each $1,000, or fraction thereof, by which the taxpayer's modified AGI exceeds the following thresholds, which are not adjusted annually for inflation:

- $400,000 if MFJ;
- $200,000 if single, HOH, or surviving spouse; and
- $200,000 if MFS.

Refundable Credit

Up to $1,700 of the Child Tax Credit available for qualifying children is refundable in 2024. (Rev.Proc. 2023-34) The refundable portion is unchanged at $1,700 for 2025. (Rev. Proc. 2024-40) No portion of the $500 Child Tax Credit that is available for other dependents is refundable.

California Nonconformity

California has no comparable Child Tax Credit but continues to allow a personal exemption credit for dependents. (R&TC §17054) In addition, taxpayers are not required to have earned income to claim California's Young Child Tax Credit. (R&TC §17052.1)

CHILD AND DEPENDENT CARE CREDIT

The nonrefundable Child and Dependent Care Credit is available to taxpayers who paid expenses for the care of a qualifying individual to enable the taxpayer (and their spouse, if filing a joint return) to work, actively look for work, or attend school full time. (IRC §21)

Generally, married taxpayers must file a MFJ return to claim the credit unless the couple is:

- Legally separated; or
- Married and living apart, and the taxpayer's home is the qualifying person's home for more than half the year, the taxpayer pays more than half the cost of keeping up the home for the year, and the spouse doesn't live in the home for the last six months of the year.(IRC §21(e)(3) and (4))

A qualifying individual is:

- A dependent qualifying child who was under age 13 when the care was provided;
- A spouse who was physically or mentally incapable of self-care and lived with the taxpayer for more than half of the year; or
- An individual who was physically or mentally incapable of self-care, lived with the taxpayer for more than half of the year, and either:
    - Was the taxpayer's dependent; or
    - Could have been the taxpayer's dependent except that they received gross income equal to or greater than the personal exemption amount ($5,050 for 2024), or filed a joint return, or the taxpayer (or taxpayer's spouse, if filing jointly) could have been claimed as a dependent on another taxpayer's return. (IRC §21(b)(1))

Only the custodial parent may claim the Child and Dependent Care Credit, even if the child is a dependent of the noncustodial parent. The custodial parent must actually pay the childcare expenses to claim the credit.

California Partial Conformity

California conforms to the Child and Dependent Care Credit, with modifications. (R&TC §17052.6)

ADOPTION CREDIT (AND EXCLUSION)

Federal law provides for an Adoption Credit or exclusion from gross income for qualified adoption expenses. (IRC §§23, 137) Generally taxpayers may take the credit when they pay the adoption expenses out of their own funds, and amounts paid to them by their employer under a qualified adoption assistance program are excludable.

Adoption Credit and Exclusion			
	Maximum credit (IRC §23(b)(1))	**Maximum exclusion (IRC §137(b)(1))**	**Phaseout amounts (credit and exclusion)**
2024 (Rev. Proc. 2023-34)	$16,810	$16,810	$252,150–$292,150
2025 (Rev. Proc. 2024-40)	$17,280	$17,280	$259,190–$299,190

The Credit

A credit for 100% of qualified adoption expenses, up to the maximum, may be claimed for each eligible child, including a special needs child. (IRC §23) Any unused credit may by carried forward for five years.

California Partial Conformity

California has its own Adoption Credit, which is different from the federal credit. (R&TC§17052.25) However, California fully conforms to the federal exclusion from income for employer- reimbursed adoption expenses. (R&TC §17131)

EARNED INCOME CREDIT

Eligible low-income workers can claim a refundable Earned Income Credit (EIC). (IRC §32) The amount depends upon the taxpayer's income and whether the taxpayer has qualifying children and how many. In addition, no EIC is allowed if an eligible individual is the qualifying child of another taxpayer.

The credit is based on a percentage of earned income up to a "plateau" amount of earned income.

Earned Income Plateau Amounts			
Qualifying children	**Credit percentage**	**2024 (Rev. Proc. 2023-34)**	**2025 (Rev. Proc. 2024-40)**
None	7.65%	$8,260	$8,490
One	34%	$12,390	$12,730
Two	40%	$17,400	$17,880
Three or more	45%	$17,400	$17,880

Beginning Point of Phaseout Range for Joint Filers

The EIC is reduced by a percentage of the amount by which earned income (or AGI, if higher) exceeds a phaseout amount.

EIC Phaseout Ranges				
	2024 (Rev. Proc. 2023-34)		**2025 (Rev. Proc. 2024-40)**	
Qualifying children	**Other than joint returns**	**Joint returns**	**Other than joint returns**	**Joint returns**
None	$10,330–$18,591	$16,370–$24,210	$10,620–$19,104	$17,730–$26,214
One	$22,720–$49,084	$28,120–$53,120	$23,350–$50,434	$30,470–$57,554
Two	$22,720–$55,768	$28,120–$59,478	$23,350–$57,310	$30,470–$64,430
Three or more	$22,720–$59,899	$28,120–$63,398	$23,350–$61,555	$30,470–$68,675

California Conformity

California provides a refundable state EITC to qualified taxpayers. (R&TC §17052) The availability of the credit is dependent on the Legislature providing for the credit in the annual Budget Act, which has been approved for the 2024 taxable year.

The California credit is similar to the federal Earned Income Credit (EIC) but with different income limitations and credit amounts, including limiting the credit to individuals who have a qualifying principal place of abode in California.

EDUCATION CREDITS

Two credits are available for taxpayers who pay for higher education expenses for themself, their spouse, or dependents: the American Opportunity Tax Credit (AOTC) and the Lifetime Learning Credit. The AOTC is available per student, but the Lifetime Learning Credit is available per taxpayer (i.e., per return).

Comparison of Education Tax Benefits (IRC §25A)		
Feature	**American Opportunity Tax (Hope) Credit**	**Lifetime Learning Credit**
Type of benefit	Refundable tax credit (up to 40% refundable)	Nonrefundable tax credit (cannot exceed tax liability)
Maximum benefit	$2,500 (100% of first $2,000 in qualified expenses, 25% of second $2,000) per student	$2,000 (20% of first $10,000 in qualified expenses) per return
Number of tax years credit is available	Available only for four tax years per eligible student (not four school years, which typically span five tax years)	Available for an unlimited number of years
Income limit	Credit begins to phase out at $80,000 modified AGI and is fully phased out at $90,000 ($160,000 and $180,000 thresholds for joint returns); phaseout is not adjusted for inflation	
Postsecondary education expenses qualifying for benefit	Tuition, fees, computers, and course materials required for enrollment	Tuition and fees required for enrollment
Type of postsecondary education	First four years of undergraduate education when enrolled on at least a half-time basis in a program leading to a degree, credential, or certificate	For any year of undergraduate or graduate enrollment for one or more courses

California Nonconformity

California has no comparable education credits.

SAVER'S CREDIT

Eligible taxpayers can claim a nonrefundable tax credit for contributions they make to a qualified retirement plan. (IRC §25B) The credit offsets both regular tax and AMT and is in addition to any applicable deduction.

The maximum annual contribution eligible for the credit is $2,000. An eligible taxpayer must be:

- Age 18 or over; and
- Not a full-time student or claimed as a dependent on another's return. The rate of credit is determined by modified AGI

The credit is available for elective contributions to any of these plans:

- 401(k) plan;
- 403(b) annuity or eligible deferred compensation arrangement of a state or local government (457 plan);
- IRA (traditional and Roth)
- SEP IRA (traditional and Roth);
- SIMPLE IRA (traditional and Roth); and
- Voluntary after-tax contributions to a qualified retirement plan.

Practice Pointer

The IRS classifies California's CalSavers program as a Roth IRA. As such, taxpayers who have withholding from their employer and participate in the CalSavers program are eligible for the Saver's Credit under IRC §25B if the taxpayer meets the AGI requirements listed below. CalSavers is discussed in more detail at page 10-28. For more information, see:

Website
https://saver.calsavers.com/home/savers/program-details.html

Taxpayers who elect to have withholding from their paycheck placed into a CalSavers account but who do not qualify to contribute to a Roth IRA can have their contributions recharacterized as traditional IRA contributions if the recharacterization is made prior to the due date of the tax return, not including extensions. Taxpayers can also elect to have their contributions treated as traditional IRA contributions instead of having to reclassify them.

With limited exceptions, the qualified contribution is reduced by distributions from the plan made:

- During the year the credit applies;
- During the two preceding years; or
- Prior to the due date of the return for the year in which the credit applies. (IRC §25B(d)(2)(B))

Saver's Credit Rate Chart				
	AGI			
Year	**Joint**	**Head of household**	**All other filers**	**Credit %**
2024 2025	\$0–\$46,000 \$0–\$47,500	\$0–\$34,500 \$0–\$35,625	\$0–\$23,000 \$0–\$23,750	50%
2024 2025	\$46,001–\$50,000 \$47,501–\$51,000	\$34,501–\$37,500 \$35,626–\$38,250	\$23,001–\$25,000 \$23,751–\$25,500	20%
2024 2025	\$50,001–\$76,500 \$51,001–\$79,000	\$37,501–\$57,375 \$38,251–\$59,250	\$25,001–\$38,250 \$25,501–\$39,500	10%
2024 2025	Over \$76,500 Over \$79,000	Over \$57,375 Over \$59,250	Over \$38,250 Over \$39,500	0%
2024: IRS Notice 2023-75; 2025: IRS Notice 2024-80				

2024 Credit for 2025 Action

The credit pertains to the year for which the contribution is made. Because a contribution may be made for a tax year up to the due date of the return, the Saver's Credit may be the only one available that will provide a credit for action taken after the end of the taxable year. For example, a taxpayer may make an IRA, SEP IRA, SIMPLE IRA, or pension contribution for the 2024 taxable year up until April 15, 2025, and be entitled to 2024 credit.

California Nonconformity

California has no comparable credit.

SECURE 2.0 Act Changes to Saver's Credit

The Saver's Credit is repealed for contributions made after 2026 and replaced with a new government matching program. (SECURE 2.0 Act §103(e)(1)) Eligible individuals who make qualified retirement savings contributions for the taxable year will be eligible for a matching contribution from the federal government equal to the applicable percentage of contributions of up to $2,000 in total, effective for post-2026 taxable years. (SECURE 2.0 Act §103; IRC §6433)

For most individuals, the "match" will be credited by the federal government to the individual's "applicable retirement savings vehicle" once the taxpayer files their tax return making a claim for the matching contribution. (IRC §6433(a)(2))

Matching contributions of less than $100 will be treated as an income tax credit on the individual's tax return. An applicable retirement savings vehicle is one of the following retirement plans that accepts matching contributions under IRC §6433 and that is for the benefit of and is designated by the eligible individual:

- IRAs (traditional and Roth);
- 401(k), 403(b), and 457(b)s;
- SEP and SIMPLE IRAs (traditional and Roth); and
- 501(c)(18) pension plans.

Comment

The federal government's matching contribution provisions of the SECURE 2.0 Act don't go into effect until 2027.

CLEAN VEHICLE CREDIT

The Clean Vehicle Credit generally applies to new four-wheel vehicles placed in service after December 31, 2022, and sunsets at the end of 2032. (IRC §30D) A new clean vehicle is generally deemed to be placed in service on the date the taxpayer takes possession of the vehicle.

The Clean Vehicle Credit can only be claimed once per vehicle, but taxpayers can claim a Clean Vehicle Credit for every eligible new vehicle they purchase, even if multiple vehicles are purchased in the same year.

The credit is nonrefundable and cannot be carried forward if claimed for a personal-use vehicle. As we discuss on page 1-39, transferring the credit to the dealer at the time of purchase provides a valuable workaround to these limitations in certain circumstances.

IRS FAQs regarding the new Clean Vehicle Credit are available at:

Website
www.irs.gov/pub/taxpros/fs-2024-26.pdf

Claiming the Credit

The credit is claimed on Form 8936, Clean Vehicle Credits. Even taxpayers who transfer the credit to the dealer at the time of sale must complete the Form 8936 and attach it to their return.

Leased Vehicles

The Clean Vehicle Credit under IRC §30D is not available to the lessee of a qualifying vehicle.

Credit Amount

The maximum amount of the Clean Vehicle Credit is $7,500 per qualified vehicle if the vehicle's critical materials and battery components are manufactured, processed, extracted, or produced in the U.S. or in countries with which the U.S. has entered a free trade agreement. (IRC §30D(b))

If the vehicle only meets one of the requirements, then the credit is limited to $3,750.

Comment

Tax professionals should not waste their time trying to understand the technical aspects of the critical material and battery components requirements. This task is best left for the manufacturers and the Department of the Treasury to fight out.

For new vehicles, dealers must provide buyers with Form 15400, Clean Vehicle Seller's Report, if the vehicle qualifies for the Clean Vehicle Credit. If the vehicle does not qualify, then the dealer will not provide Form 15400.

It's good to have a working knowledge of the requirements to claim the Clean Vehicle Credit, but don't get too bogged down in the details. The key piece of information is whether your client has received Form 15400 from the dealer. If they did, then the vehicle qualifies for the credit. If they didn't receive Form 15400, then the vehicle does not qualify.

The federal government also maintains a website with a list of all vehicles eligible for all three of the clean vehicle credits at:

Website
https://fueleconomy.gov/feg/tax2023.shtml

Final Assembly Point

Beginning with vehicles purchased after August 16, 2022, the final assembly of the vehicle must occur within North America to qualify for either the pre- or post-IRA '22 versions of the credit. (IRA '22 §13401(b)) "North America" is defined as the United States, Canada, and Mexico and includes any state or territory of those three countries, even if not strictly part of the continent of North America (i.e., Hawaii, Puerto Rico, or other similarly situated states or territories of the three countries). (Treas. Regs. §1.30D-2(d))

IRS Notice 2023-1 provides a technical definition of "final assembly," but generally provides that taxpayers may rely on the following information to determine a qualifying vehicle's final assembly point:

- The vehicle's plant of manufacture as reported in the vehicle identification number (VIN); or
- The final assembly point reported on the label affixed to the vehicle. (Treas. Regs. §1.30D-2(b))

Caution

Even though a particular make/model of a car may generally qualify for the credit, if the actual vehicle purchased does not satisfy the final assembly requirement, the Clean Vehicle Credit cannot be claimed for that particular vehicle. This is why the dealer's report, discussed on page 1-41 is critical. The dealer's report, which the taxpayer may rely upon, contains all the information a vehicle buyer needs to determine whether the vehicle they seek to purchase qualifies for a clean vehicle credit.

Modified AGI Limit

Applicable to vehicles placed in service after December 31, 2022, taxpayers are eligible for the Clean Vehicle Credit only if their modified AGI does not exceed the following amounts in either the year they purchased the vehicle or the prior tax year:

Clean Vehicle Credit AGI Limitations	
Filing status	**AGI limit**
Married filing joint	$300,000
Head of household	$225,000
All others	$150,000

Comment

The Clean Vehicle Credit AGI limits are not adjusted annually for inflation. (IRC §30D(f)(10))

Modified AGI is the taxpayer's AGI, increased for any foreign income exclusion claimed under IRC §911, §931, or §933.

Planning Pointer

The modified AGI thresholds are a cliff. A married couple filing jointly whose modified AGI in either the current or prior year is $300,000 will qualify for the full Clean Vehicle Credit. If the same couple's modified AGI is $300,001 or above for both the prior and current year, they will receive zero credit.

Modified AGI Where Filing Status Changes During Two-Year Testing Period

When a taxpayer's filing status changes during the two-year testing period (the taxable year prior to the year the vehicle is purchased and the year the vehicle is purchased), the taxpayer must apply the AGI limitation based on their filing status for each of those years. (Rev. Proc. 2023-33).

Example of Changed Filing Status

Danielle was single in 2023 and had an AGI of $165,000. In 2024, she married Kevin and their combined AGI was $350,000. Danielle purchased a qualifying clean vehicle in 2024, but Danielle cannot claim the Clean Vehicle Credit because her AGI was over the

$150,000 limit for her single filing status in 2023, and her AGI was over the $300,000 AGI limit in 2024 for married filing joint.

Danielle cannot use the AGI threshold for joint filers for 2023 to determine whether she qualifies for the Clean Vehicle Credit in 2024.

AGI Limit Where Passthrough Entity Claims Clean Vehicle Credit

If a passthrough entity claims the Clean Vehicle Credit under IRC §30D, then the credit is passed through to the entity's owners who must then apply the AGI limitation on their Form 1040. See page 5-33 for a more detailed discussion of the clean vehicle credits that may be claimed by businesses.

Vehicle Price Limitation

The Clean Vehicle Credit cannot be claimed for vehicles whose manufacturer's suggested retail price (MSRP) exceeds:

Clean Vehicle Credit Vehicle Price Limitations	
Vehicle type	**MSRP limit**
Vans, pickup trucks, or SUVs	$80,000
All other vehicles	$55,000

Comment

The Clean Vehicle Credit price limitations are not adjusted annually for inflation. (IRC §30D(f)(10))

Comment

Similar to the critical material and battery components requirements, tax professionals should not waste their time trying to determine whether their vehicle qualifies as a van, pickup truck, or SUV. We merely have to review the vehicle seller's report (IRS Form 15400) or look up the vehicle on the federal government's website, which will tell us whether the vehicle in question is subject to the $80,000 MSRP limit or the $55,000 MSRP limit:

Website
https://fueleconomy.gov/feg/taxcenter.shtml

Advanced Credits Claimed at Dealership

Individual taxpayers can transfer the Clean Vehicle Credit under IRC §30D and the Previously Owned Clean Vehicle Credit under IRC §25E to licensed dealers that have registered with the Secretary of the Treasury and that disclose specified information to the taxpayer at the time of the purchase. Businesses can claim the Clean Vehicle Credit, but they cannot claim advanced credits at the dealership.

The election to transfer the credit must be made no later than the time of sale. The seller may not reduce the amount of any other offered incentive, rebate, or discount as a result of this credit transfer. (IRC §30D(g))

Comment

Taxpayers can claim advanced clean vehicle credits at the dealership for credits claimed under IRC §§30D and 25E (but only if the taxpayer attests to the dealer that the vehicle will be used predominantly for personal use). (Rev. Proc. 2023-33, Sec. 5.02)

Additionally, taxpayers and auto dealers cannot transfer partial credits. Either the entire credit must be transferred to the dealer or none of it.

Practice Pointer

As will be discussed starting on page 5-38, many cars will qualify for both the Clean Vehicle Credit under IRC §30D and the Qualified Commercial Clean Vehicle Credit under IRC §45W. However, only the Clean Vehicle Credit under IRC §30D allows taxpayers to claim the credit at the dealership.

While the IRS has not provided specific guidance, it appears that once a taxpayer claims an advanced vehicle credit at the dealership, they cannot later claim the Qualified Commercial Clean Vehicle Credit under IRC §45W. This is because, as a condition of claiming the advanced credit at the dealership, the vehicle's buyer must attest that the vehicle will be used predominantly for personal use.

Two-Vehicle Limitation

The IRS has limited taxpayers to making no more than two clean vehicle credit transfer elections per taxable year, consisting of either two Clean Vehicle Credits or one Clean Vehicle Credit and one Previously Owned Clean Vehicle Credit. (Rev. Proc. 2023-33, Sec. 6.02; Treas. Regs. §§1.25E-3(i), 1.30D-5(h)) In the case of a joint income tax return, the two-vehicle limit applies separately for each spouse. (IRS Fact Sheet FS-2024-26, Topic A, Q&A #16)

The two-vehicle limitation only means that taxpayers cannot claim more than two advanced credits through a dealership per year. Clean vehicle credits for additional vehicles must be claimed directly on the taxpayer's income tax return.

Comment

Taxpayers are unable to make two credit transfer elections in the same taxable year for the Previously Owned Clean Vehicle Credit because taxpayers are only eligible for one Previously Owned Clean Vehicle Credit every three years. (IRC §25E(c)(3)(D))

Advanced Credit Triggers Income Tax Filing Requirement

One of the requirements of claiming the advanced credit at the dealership is that the buyer must attest that they will file a timely income tax return for the year and report the credit (using Form 8936, Clean Vehicle Credits). Therefore, buyers must file an income tax return for the year they claim an advanced clean vehicle credit at the dealership, even if the taxpayer would not otherwise have a filing requirement.

Practice Pointer

Don't forget to ask your client if they purchased a clean vehicle during the year. Clients who claim advanced credits at the dealership may not realize that they still must report the credit on their income tax returns and won't think to notify their tax professional.

Clean Vehicle Seller's Report—Form 15400

The dealer must provide the buyer with IRS Form 15400, Clean Vehicle Seller's Report, at the time of purchase. The report is only prepared by the dealer if the vehicle qualifies for the credit. The report contains all information necessary for the taxpayer to prepare Form 8936, Clean Vehicle Credit, when the taxpayer files their income tax return.

Form 8936 must be completed by the taxpayer even if they claim an advanced credit at the dealership. In the case of advanced credits at the dealership, Form 8936 serves to compute any credit recapture for taxpayers whose AGI does not qualify them for the credit. (Rev. Proc. 2023-33, Secs., 4.02(e)(2), 4.02(3)(c))

Practice Pointer

Form 15400 is provided for vehicle sales after December 31, 2023. For clean vehicles sold before January 1, 2024, the dealer's disclosures to a buyer were provided on a dealer's self-created report that should have contained this same information.

Vehicles with Joint Ownership

Through FAQs, the IRS has stated that where multiple taxpayers purchase a qualifying clean vehicle and jointly hold title to the vehicle, only one of the taxpayers can claim the Clean Vehicle Credit. (IRS FAQs, Topic A, Q&A 11) The credit cannot be prorated between multiple taxpayers, even for spouses who file MFS.

According to the IRS FAQs, the name and taxpayer identification number of the owner claiming the applicable clean vehicle credit must be the one listed on Form 15400, Clean Vehicle Seller's Report. In fact, Form 15400 only allows one taxpayer to be listed.

Practice Pointer

The IRS's requirement that only the purchaser listed on the dealer's report is entitled to claim the Clean Vehicle Credit makes it all that much more important that the tax professional obtain a copy of the report from the client, especially in situations where a family member may also be on title to help secure financing, where an unmarried couple jointly purchases the vehicle, or where a married couple purchases a clean vehicle and then files separate income tax returns.

Remember, dependents cannot claim a clean vehicle credit, so taxpayers who purchase a qualifying clean vehicle with a dependent want to make sure that the taxpayer, and not the dependent, is listed as the buyer on the Form 15400.

California Nonconformity

California does not offer any clean vehicle tax credits.

Credit Recapture Rules

Taxpayers who claim either the advanced Clean Vehicle Credit or the Previously Owned Clean Vehicle Credit at the dealership but do not qualify for the credit must recapture (i.e., repay) the credit when they file their income tax return for the year. Dealers are not liable for credit recapture where the taxpayer is ineligible for the credit. (Rev. Proc. 2023-33)

Example of Credit Recapture

Emma purchased a vehicle on January 10, 2024, that qualifies for a $7,500 Clean Vehicle Credit. Emma elected to transfer her credit to the dealer, and she used the $7,500 as her vehicle down payment.

If it turns out that Emma's AGI for both 2023 and 2024 were over the AGI limitation, she must repay the $7,500 credit when she files her 2024 income tax return because she is not eligible for the credit.

Credit Recapture Exception

The IRS has created an interesting exception to the recapture rules where a taxpayer elects to transfer their credit to the dealer but does not have sufficient taxable income to use their credit when they file their income tax return. In this scenario, the taxpayer is not subject to recapture of the credit. (Treas. Regs. §§1.25E-3(e)(1)(i), 1.30D-5(d)(1)(i))

Remember, the clean vehicle credits are not refundable, and unused credits do not carry forward. This recapture exception provides an additional incentive for taxpayers to elect to claim their clean vehicle credits at the dealership instead of waiting to file their income tax returns.

These recapture rules apply to both the Clean Vehicle Credit and the Previously Owned Clean Vehicle Credit.

Example of Exception to Credit Recapture

Lonnie purchased a vehicle on August 31, 2024, that qualifies for a $7,500 Clean Vehicle Credit. Lonnie's AGI is low enough to claim the credit, but his tax liability for the year is only $3,500 before the credit.

If Lonnie does not transfer the Clean Vehicle Credit to the dealership, then he can only claim a credit of $3,500 when he files his 2024 income tax return because the credit is nonrefundable, and any unused portion of the credit does not carry over.

But, if Lonnie elected to transfer the credit to the dealership, then he is not required to recapture the $4,000 excess credit he received ($7,500 maximum credit, less $3,500 tax liability on his 2024 income tax return).

By electing to transfer the credit to the dealership, Lonnie received a benefit of $4,000 that would have otherwise been lost.

PREVIOUSLY OWNED CLEAN VEHICLE CREDIT

The Previously Owned Clean Vehicle Credit under IRC §25E is available for the purchase of qualifying used clean vehicles by buyers with modified AGI below specified levels. The credit is available for qualified vehicles purchased after December 31, 2022, and before 2033. (IRC §25E)

Only sales by a licensed dealer of vehicles sold for $25,000 or less qualify for the credit. In addition, only the first qualifying resale of the vehicle is eligible for the credit. Sales by private sellers do not qualify for the credit.

Credit Amount

The credit is equal to 30% of the vehicle's sales price, up to a $4,000 maximum credit. (IRC §25E(a))

Qualified Vehicles

To qualify for this credit:

- The vehicle's sales price cannot exceed $25,000;
- The vehicle's model year must be at least two years earlier than the calendar year in which it was purchased;
- The original use of the vehicle must not have commenced with the taxpayer;
- The vehicle must be a qualifying clean vehicle; and
- The sale is the first qualifying sale of the vehicle (defined as the first resale of the vehicle since the date of enactment of the Inflation Reduction Act on August 16, 2022).

Vehicle Sales Price

The sales price of a previously owned clean vehicle means the total sales price agreed upon by the buyer and seller in a written contract at the time of sale, including any delivery charges and after the application of any incentives, but excluding separately stated taxes and fees required by state or local law. (Treas. Regs. §1.25E-1(b)(9)) It also includes the retail price for each accessory or item of optional equipment physically attached to the vehicle at the time of sale. Additionally, the sales price of a previously owned clean vehicle is determined before the application of any trade-in value and does not include separate financing, extended warranties, or insurance.

✐ Practice Pointer

Similar to the Clean Vehicle Credit under IRC §30D for new vehicles, dealers must provide buyers with Form 15400, Clean Vehicle Seller's Report if the vehicle qualifies for the Previously Owned Clean Vehicle Credit under IRC §25E.

If the vehicle does not qualify, then the dealer will not provide Form 15400.

It's good to have a working knowledge of the requirements to claim the Previously Owned Clean Vehicle Credit, but don't get too bogged down in the details. The key piece of information is whether your client has received Form 15400 from the dealer. If they did, then the vehicle qualifies for the credit. If they didn't receive Form 15400, then the vehicle does not qualify.

For example, assume the vehicle meets all the requirements of a qualifying vehicle listed above except that the vehicle's sales price was more than $25,000. In this scenario, the taxpayer will not receive Form 15400 from the dealer. (Instructions to Form 15400)

Qualified Buyers

Qualified buyers are those:

- Who are individuals (business entities cannot claim the Previously Owned Clean Vehicle Credit) (IRC §25E(c)(3)(A));
- Who purchase the vehicle for use and not for resale (IRC §25E(c)(3)(B));
- Who cannot be claimed as the dependent of another taxpayer—even if the buyer is not actually claimed as a dependent, they are ineligible to claim the credit if they could be claimed as a dependent (IRC §25E(c)(3)(C));
- Who has not claimed the Previously Owned Clean Vehicle Credit for another vehicle during the three-year period ending on the date they purchased the vehicle at issue (IRC§25E(c)(3)(D)); and
- Whose modified AGI (AGI increased for any foreign-earned income exclusion) for the current taxable year or preceding taxable year did not exceed:

Previously Owned Clean Vehicle Credit AGI Limitations	
Filing status	**AGI limit**
Married filing joint	$150,000
Head of household	$112,500
All others	$ 75,000

Comment

The Previously Owned Clean Vehicle Credit AGI limits are not adjusted annually for inflation. (IRC §25E(b))

The modified AGI limitation is a cliff, not a phaseout. If the taxpayer's modified AGI is even $1 over the threshold, then they are ineligible for the credit.

✏ **Practice Pointer**

The one-purchase-every-three-years rule is tied to the date of the sale of the vehicle, not the taxable year. (IRC §25E(c)(3)(D))

For example, a taxpayer who purchases a previously owned clean vehicle on January 27, 2025, and claims the credit under IRC §25E cannot claim the Previously Owned Clean Vehicle Credit on another car purchase before January 28, 2028.

Be sure to advise your clients that the precise date of purchase matters when claiming the Previously Owned Clean Vehicle Credit.

✐ **Practice Pointer**

As previously discussed, taxpayers will receive Form 15400 from the dealership if the vehicle meets all the requirements of a qualifying vehicle. However, that does not mean that the taxpayer is automatically eligible to claim the Previously Owned Clean Vehicle Credit.

It is up to the tax professional to determine whether the taxpayer is a qualifying buyer who meets all the requirements listed above.

If the taxpayer is not a qualifying buyer, then they cannot claim the Previously Owned Clean Vehicle Credit. If the taxpayer claimed an advanced credit at the dealership, then the taxpayer must repay the credit when they file their income tax return.

Once-Every-Three-Year Requirement for Joint Returns

The once-every-three-year requirement applies per taxpayer. So, each spouse on a joint return qualifies to claim the Previously Owned Clean Vehicle Credit once every three years.

Credit Transfer

Beginning with vehicles acquired after 2023, purchasers may transfer the Previously Owned Clean Vehicle Credit to the dealer (similar to the transfer allowed for the Clean Vehicle Credit discussed on page 1-39).

Other Issues

Like the Clean Vehicle Credit:

- Taxpayers must provide the vehicle identification number (VIN) on the tax return for the year the credit is claimed;
- The vehicle's basis must be reduced by the amount of the credit claimed;
- Any other deduction or credit allowed for the vehicle must be reduced by the amount of the credit for previously owned clean vehicles;
- The credit cannot be claimed for vehicles used predominantly outside the U.S.; and
- The vehicle must meet applicable air quality and motor vehicle safety standards.

California Nonconformity

California has no similar tax credit.

ENERGY EFFICIENT HOME IMPROVEMENT CREDIT

The Energy Efficient Home Improvement Credit is available through 2032 and is available for various home improvements. (IRC §25C(g)(2)) The credit is equal to 30% of qualified expenses, with limitations, including:

- Qualified energy efficient improvements installed during the year;
- Residential energy property expenses; and
- Home energy audits

The annual credit limits are $3,200 overall, with no lifetime limit:

- $2,000 for heat pumps, heat pump water heaters, and biomass stoves/boilers:
    - $2,000 for heat pumps;
    - $2,000 for heat pump water heaters; and
    - $2,000 for biomass stoves/boilers;
- Plus, $1,200 (for all other qualifying home improvements):
    - $600 for efficient AC units;
    - $600 for efficient furnaces/boilers;
    - $600 for efficient water heaters;
    - $600 for electric panel/circuit upgrades;
    - $1,200 for insulation/air sealing;
    - $500 for exterior doors ($250 each);
    - $600 for exterior windows/skylights; and
    - $150 for home energy audits.

✐ Practice Pointer

The Energy Efficient Home Improvement Credit is only available for qualifying improvements made to the taxpayer's existing home. The credit is not available for qualifying property installed on a newly built home purchased by the taxpayer.

The credit is claimed on Form 5695, Part II and is claimed in the year qualifying property is installed, not the year the qualifying property is purchased.

Qualifying Taxpayers

Taxpayers can claim the Energy Efficient Home Improvement Credit for improvements to their principal residence home that is:

- Located in the United States; and
- An existing home (not a new home).

Business Use of Home

Taxpayers can claim the full amount of the Energy Efficient Home Improvement Credit for which they are eligible if the business use of their home does not exceed 20% of the home. If more than 20% of the home is used for business, then the cost of the improvements must be allocated between business and personal use, and the credit can only be claimed against the personal use of the energy efficient property. (IRC §25C(f)(1)).

Practice Pointer

IRC §25C(f)(1) states that rules similar to the rules under IRC §25D(e)(4) through (8) shall apply to the Energy Efficient Home Improvement Credit. IRC §25D governs the Residential Clean Energy Credit (solar credits, etc.).

IRC §25D(e)(4)(7) provides the rule that if more than 20% of the use of an item is for business purposes, then the portion allocable to business purposes is not eligible for the credit.

Even though taxpayers cannot claim the Energy Efficient Home Improvement Credit for the business use portion of their expenses, they can claim a business deduction for the expenses (or capitalize and depreciate them).

Qualifying Home Improvements

To qualify, home improvements must meet energy efficiency standards. They must be new systems and materials, not used. Some improvements have specific credit limits detailed in the following discussion.

Practice Pointer

Taxpayers can rely on information provided by the manufacturer or seller of the energy efficient home improvements to determine whether the improvements meet the necessary energy efficient standards.

Subsidies, Rebates, and Incentives

When calculating the Energy Efficient Home Improvement Credit, taxpayers must subtract subsidies, rebates, or other financial incentives from their qualified property expenses because they're considered a purchase price adjustment.

Rebates are subtracted from qualified expenses if all of the following apply:

- The rebate is based on the cost of the property;
- It comes from someone connected to the sale such as the manufacturer, distributor, seller or installer; and
- It isn't given as payment for services you provide.

State energy efficiency incentives are generally not subtracted from qualified costs unless they qualify as a rebate or purchase price adjustment under federal income tax law. Many states label energy efficiency incentives as rebates even though they don't qualify under that definition. See IRS Notice 2013-70 for additional information.

California Nonconformity

California has no similar credit.

Manufacturer's PIN Requirement

For "specified property items" placed in service after 2024, the Energy Efficient Home Improvement Credit can only be claimed if:

- The item is produced by a qualified manufacturer (those that register with the IRS and provide a "qualified product identification number (PIN)" for each item and report them to the IRS); and
- The taxpayer includes the item's PIN on their tax return. (IRC §25C(h))

Credits claimed without the requisite PIN will be disallowed and treated as a mathematical or clerical error, meaning that the IRS can summarily make the change unless the taxpayer requests an abatement within 60 days of receiving a math error notice.

The PIN applies to the following types of property:

- Electric or natural gas heat pump water heater;
- Electric or natural gas heat pump;
- Central air conditioner;
- Natural gas, propane, or oil water heater;
- Natural gas, propane, or oil furnace or hot water boiler;
- Biomass stove or boiler;
- Improvements to, or replacement of, a panelboard, sub-panelboard, branch circuits, or feeders;
- Exterior windows, including skylights; and
- Exterior doors.

Practice Pointer

The IRS has issued Rev. Proc. 2024-31 that provides guidance to manufacturers of energy efficient property. The guidance provides rules and procedures for manufacturers to become "qualified manufacturers", which is a requirement for any property to be eligible for the Residential Energy Credits.

Rev. Proc. 2024-31 is not aimed at taxpayers or tax professionals, but it moves the ball forward on the mandate that energy property must have a PIN starting for the 2025 taxable year.

RESIDENTIAL CLEAN ENERGY CREDIT

The Residential Clean Energy Credit is available for new qualifying property placed in service prior to January 1, 2035. (IRC §25D(g)(2)) The Residential Clean Energy Credit is often referred to as the Solar Energy Credit, although it applies to:

- Solar energy property;
- Qualified fuel cell property;
- Qualified small wind energy property;
- Geothermal heat pump property;
- Biomass stoves;
- Water heaters; and
- Beginning with the 2023 tax year, qualified battery storage technology (home batteries with a capacity of not less than three kilowatt hours). (IRC §25D(a))

Principal Residence Requirement

Except for fuel cell property, each type of property eligible for the Residential Clean Energy Credit can be claimed for property installed on any personal use residence, even if it is not the taxpayer's principal residence.

Fuel cell property must be installed on the taxpayer's principal residence.

> ✐ **Practice Pointer**
>
> For all property, including fuel cell property, taxpayers can claim the credit even if they do not own the residence—so renters qualify. However, landlords must claim the Energy Investment Tax Credit discussed on page 5-59.

Labor and Related Installation Costs

Labor and installation costs allocable to the onsite preparation, assembly, or original installation of the qualified residential clean energy property and for piping or wiring to connect to the residence can be taken into account in computing the credit. (IRC §25D(e)(1))

However, the credit cannot be claimed for:

- Financing costs, including interest and origination fees;
- Extended warranty costs; or
- Roof repairs and replacements.

Business Use Allocation

If more than 20% of the property's use is for business, the qualified expenditures must be allocated between business and nonbusiness purposes. Only the nonbusiness expenditures are eligible for the Residential Clean Energy Credit. (IRC §25D(e)(7)) The business expenditure portion is eligible for the Energy Investment Tax Credit under IRC §48, discussed on page 5-59.

Timing of Expenditures

All expenditures qualifying for the Residential Clean Energy Credit are treated as made when the original installation of the property is completed (when final permits are approved and the property is hooked up to the energy grid in the case of solar). (IRC §25D(e)(8)) This is significant for taxpayers undertaking large projects toward the end of a tax year. If the project is not completed before December 31, then the taxpayer must wait another tax year to claim the credit.

Basis Adjustments

The home's basis must be reduced by the amount of any credit allowed. (IRC §25D(f))

Example of Basis Adjustment

Daren purchases and installs qualifying solar electric property (solar panels) on his principal residence at a cost of $70,000. At the time of the installation, Daren's basis in his home was $1.2 million. Daren's new basis is $1,249,000, calculated as follows:

Basis of home at time of solar installation	$1,200,000
Solar installation (capital improvement)	70,000
Less: solar credit ($70,000 × 30%)	(21,000)
Adjusted basis	$1,249,000

Taxpayer Limitations

The Residential Clean Energy Credit carries very few limitations. As such, it is a credit that high income taxpayers can take without fear of reduction. The main points are as follows:

- There is no maximum credit any taxpayer can take (annually or lifetime);
- The credit is not limited by the taxpayer's AGI;
- The credit can offset AMT; and
- The credit is nonrefundable, but any unused portion may be carried forward indefinitely (even into years after new solar credits have expired).

California Nonconformity

California has no comparable credit.

Double Benefit Disallowed Where Subsidies are Received

There is no credit allowed for residential clean energy property to the extent that an energy conservation subsidy for that expenditure was excluded from income. (IRC §136(b)) An excluded subsidy is one that a public utility provides, directly or indirectly, to a customer to buy or install energy conservation property.

The rule applies whether a third-party contractor receives the subsidy on behalf of the taxpayer or the taxpayer receives the subsidy directly. (Notice 2013-70)

Looking to the phrase "directly or indirectly," the IRS has concluded that state subsidies paid to solar installation contractors, rather than to the system owners, are excludible to the system owners under IRC §136. (PLR 201607004) IRC §136 provides that gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure. Because the subsidies paid to the contractors bring down the cost to the end user (the homeowner), the legislative intent of IRC §136 is met.

Example of Subsidy

Zack pays for and installs solar panels on his principal residence. The cost for the panels and installation is $78,000, but Zack receives an excludable energy conservation subsidy of $8,100 from his electric company. Zack's Residential Clean Energy Credit is $20,970 calculated as follows:

Cost	$78,000
Subsidy	(8,100)
Net cost to Zack	69,900
Credit	30%
Total	$20,970

California Partial Conformity

California conforms to the IRC §136 exclusion for energy subsidies. (R&TC §24326) If a grant received by an individual from a city to install solar panels qualifies for the IRC §136 exclusion, it would not be taxable for California. There are no California-specific exclusions for solar subsidies, nor does California have a solar credit.

Investment and Rental Properties

Taxpayers cannot claim the Residential Clean Energy Property Credit for expenditures for improvements made to an investment property, such as rental property, that is not also used as a residence by the taxpayer. (Notice 2013-70, Q&A-6) In other words, the credit is available to taxpayers who install qualifying property on a multifamily dwelling that serves as both the taxpayer's primary residence and a rental property, subject to the 20% business use allocation previously discussed.

Taxpayers who install solar property on an investment or rental property may still claim a solar credit under the Energy Investment Tax Credit. (IRC §48) The Energy Investment Tax Credit is discussed in more detail starting on page 5-59.

New Homes

Taxpayers can claim the Residential Clean Energy Credit if qualifying property is installed in or on an existing home or a newly constructed home. For property installed on a new home, the taxpayer may request that the homebuilder make a reasonable allocation—or the taxpayer may use any other reasonable method—to determine the cost of the property that is eligible for the credit. (Notice 2013-70) The credit is allowed in the year the taxpayer occupies the residence.

AFFORDABLE CARE ACT (ACA)

ACA INDIVIDUAL MANDATE

Shared Responsibility Payment

The ACA's individual shared responsibility payment is zero. Taxpayers without health insurance are not penalized by the Internal Revenue Code.

California Nonconformity

California has charged a tax penalty for failure to have health insurance since 2020.

PREMIUM TAX CREDIT

Taxpayers are allowed an advanceable and refundable Premium Tax Credit to help subsidize the purchase of health insurance through exchanges. (IRC §36B)

The credit is:

- Determined by reference to the premium amount for the second lowest cost silver plan offered by an exchange in the rating area where the taxpayer resides; and
- Based on the percentage of income the cost of premiums represents

The credit is computed in four steps:

1. Determine the taxpayer's "household income" as a percentage of the poverty line for the taxpayer's family size;

2. Determine the "applicable percentage" relative to household income (expressed as a percentage of the poverty line determined in step 1);

3. Multiply the applicable percentage by household income. This determines the taxpayer's "expected contribution" (the amount the taxpayer is expected to pay for insurance for the taxpayer's household); and

4. Subtract the expected contribution from the "benchmark premium" (the cost of the second lowest cost silver plan).

The taxpayer's contribution amount (household income for the tax year times the applicable percentage) is determined using the taxpayer's household income and family size at the end of the current tax year.

Enhanced Credit for 2021 Through 2025

For 2021 through 2025, the American Rescue Plan Act of 2021, extended by the Inflation Reduction Act of 2022, expanded the Premium Tax Credit by:

- Increasing the amount of subsidies people can receive when purchasing the plans through the health care exchange by decreasing the taxpayer's maximum income contribution toward the premiums (ARPA §9661; IRC §36B(b)(3)(A)); and

- Repealing the 400% federal poverty level cap on receiving subsidies. Under pre-ARPA law there was a cliff, and taxpayers whose modified AGI exceeds 400% of the poverty level must pay 100% of their premiums for insurance coverage through the Marketplace. By repealing the cap, all taxpayers with incomes above the 400% federal poverty level will not have to pay more than 8.5% of their income on health insurance premiums. (ARPA §9661; IRC §36B(b)(3)(A))

Under current law, the Premium Tax Credit is calculated as the difference between the benchmark premium (the premium for the second lowest cost silver plan available in the Marketplace in the area of residence) and a specified percentage of income for a person with income at a given percentage of the federal poverty level. By lowering the specified percentage, the ARPA increases the amount of the subsidies/Premium Tax Credit available.

The following table shows the contribution rate for specified levels of the federal poverty level (FPL).

Maximum Income Contribution Percentage by Household Income for Premium Tax Credits for 2021–2025 (Rev. Procs. 2023-37 & 2024-35)	
Income range (percentage of FPL)	**Range of maximum income contribution (percentage of income)**
100%–150%	0%
150%–200%	0%–2%
200%–250%	2%–4%
250%–300%	4%–6%
300%–400%	6%–8.5%
400%+	8.5%

2024 Federal Applicable Percentage Per Income Range for ACA Subsidies						
ACA applicable percentage	**Income range (FPL percentage)**	**1 Person**	**2 People**	**3 People**	**4 People**	**5 People**
0%	100%–150%	$14,580–$21,870	$19,720–$29,580	$24,860–$37,290	$30,000–$45,000	$35,140–$52,710
0%–2%	150%–200%	$21,870–$29,160	$29,580–$39,440	$37,290–$49,720	$45,000–$60,000	$52,710–$70,280
2%–4%	200%–250%	$29,160–$36,450	$39,440–$49,300	$49,720–$62,150	$60,000–$75,000	$70,280–$87,850
4%–6%	250%–300%	$36,450–$43,740	$49,300–$59,160	$62,150–$74,580	$75,000–$90,000	$87,850–$105,420
6%–8.5%	300%–400%	$43,740–$58,320	$59,160–$78,880	$74,580–$99,440	$90,000–$120,000	$105,420–$140,560
8.5%	400%+	$58,320	$78,880	$99,440	$120,000	$140,560

Limitation of Payback of Excess Advance Credits for 2024 (Rev. Proc. 2023-34)		
Household income relative to poverty line	**All filing statuses except single**	**Single**
Less than 200%	$750	$375
At least 200% but less than 300%	$1,900	$950
At least 300% but less than 400%	$3,150	$1,575
400% or more	No limit	No limit

Limitation of Payback of Excess Advance Credits for 2025 (Rev. Proc. 2024-40)		
Household income relative to poverty line	**All filing statuses except single**	**Single**
Less than 200%	$750	$375
At least 200% but less than 300%	$1,950	$975
At least 300% but less than 400%	$3,250	$1,625
400% or more	No limit	No limit

California Nonconformity

California does not provide a credit. Prior to the ARPA expansion of the credit, California provided subsidies to taxpayers below specified income levels and will likely reinstate these subsidies if the ARPA expansion is not continued.

NANNY TAX

For 2024, the nanny tax threshold is $2,700. For 2025, it is $2,800. (www.ssa.gov/OACT/COLA/ CovThresh.html)

This is the applicable wage threshold for purposes of FICA withholding for wages paid to household employees (health care workers, butlers, maids, drivers, cleaning people, gardeners, babysitters, etc.).

People who hire others to help them in their homes may be household employers, whether they realize it or not. Hiring individuals to help out with children, elderly parents, or household duties in general is becoming more and more the norm. Unfortunately, most people still don't realize that when they hire someone to work in their home, the IRS may consider them "household employers" responsible for paying and reporting payroll taxes.

A "household employer" is an individual who has hired someone to do household work and controls not only what work is done, but how it is done. (IRC §3510)

California Conformity

California does not allow household employers to pay household employment taxes on the California income tax return. Household employers must register with the EDD and report household employees by filing Form DE 1HW, Registration Form for Employers of Household Workers, when they employ one or more individuals and pay cash wages of $750 or more in a calendar quarter. (California UIC §684) Household employers must also file Form DE 34, Report of New Employee(s), for each new employee within 20 days of hire.

Household employers who pay less than $20,000 in wages per year may elect to pay taxes annually by checking the "yes" box in Item D on Form DE 1HW or, if previously registered with the EDD, may complete Form DE 89, Employer of Household Worker Election.

COLLEGE SAVINGS

§529 PLAN ROLLOVERS TO ROTH ACCOUNTS

Individuals who have maintained §529 accounts for at least 15 years can make a direct trustee-to-trustee rollover from the §529 plan to the beneficiary's Roth IRA effective for distributions made after December 31, 2023. (IRC §§408A(e)(1)(C), 529(c)(3)(E)) The exclusion only applies to the amount contributed to the §529 plan (and earnings attributable thereto) before the five-year period ending on the date of the distribution.

Limitations

Rollovers from §529 plans toward a taxpayer's Roth IRA count toward the taxpayer's annual IRA contribution limits ($7,000 for 2024 for taxpayers under age 50). (IRC §529(c)(3)(E)(ii)) However, the Roth contribution AGI limitation does not apply to these rollovers.

Rollovers from a §529 plan are subject to an aggregate lifetime limit of $35,000 per beneficiary

§529 QUALIFIED EXPENSES

§529 Distributions			
	Postsecondary (college) and registered apprenticeships	**K–12**	**Student loan repayments**
Tuition	No limit	Limited to $10,000 annually	N/A
Fees, books, supplies, and equipment required for enrollment or attendance	Eligible expenses	Not eligible expenses (§529 distributions used for these purposes are taxable)	N/A
Expenses for special needs services of beneficiary in connection with enrollment or attendance	Eligible expenses	Not eligible expenses	N/A
Expenses for the purchase of computer or peripheral equipment, software, internet access and related services, if used during enrollment at education institution	Eligible expenses (but not for software designed for sports, games, or hobbies unless it is predominantly educational in nature; for example, if student is studying video game development)	Not eligible	N/A
Student loan repayments	N/A	N/A	$10,000 per lifetime, per student

California Partial Conformity

California generally conforms to the IRC §529 provisions. However, California does not conform to the following changes made to §529 accounts over the last few years:

- Tax-free rollover into a Roth account, so any earnings included in the distributions are taxable and subject to penalties on the California return;
- §529 distributions to be used for K–12 tuition, so California residents who use distributions from §529 accounts for K–12 tuition are subject to California’s 2.5% early withdrawal penalty on the earnings withdrawn from the account. (R&TC §§17024.5, 17140, 17140.3)

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PARTNER REPORTING OF ADMINISTRATIVE ADJUSTMENT REQUESTS

The centralized partnership audit regime (CPAR) provisions generally prohibit partnerships subject to CPAR from amending their returns (thus, all partnerships are prohibited except partnerships that have elected out). Instead of filing an amended return, the partnership must file an administrative adjustment request (AAR).

Partnerships that file an AAR are treated much like a partnership that is subject to an audit assessment; that is, the partnership must pay tax at the partnership level unless it elects to push out the adjustment to its partners.

✏ **Practice Pointer**

CPAR partnerships should consider filing annual extensions, even if they timely file their returns. This will enable the partnership to file a superseding original return if the partnership uncovers any errors on the original return or K-1s prior to the extended deadline, rather than have to go through the administrative adjustment request procedures described later.

A superseding original return is not an amended return. It is an original return filed after the taxpayer has already filed its income tax return for the year but is filed on or before the due date including extensions for the year. When a superseding original return is filed, the IRS (and FTB) replaces the first return with the superseding original return, and the superseding original return becomes the original return of record for the taxpayer.

✏ **Practice Pointer**

Taxpayers, individuals and businesses can timely file their income tax return for the year and then decide to file an extension as long as the extension is filed by the original due date of the return. There are a couple of reasons why taxpayers may file an extension after filing their original return:

- The taxpayer needs additional time to make employer retirement contributions for employer-sponsored plans;
- The taxpayer wants to provide breathing room for filing a superseding return (as discussed in the immediately preceding Practice Pointer pertaining to CPAR partnerships); or
- A staff member inadvertently e-files a return for a client instead of filing the extension. The extension can still be e-filed and, similar to the previous bullet point, provides breathing room to file a superseding return.

When an AAR is filed by a CPAR partnership, unless a push-out election is made, the partnership pays any imputed underpayment of tax on the AAR in the year the administrative adjustment request is filed (the adjustment year).

But what happens if the AAR adjustment results in a taxpayer-friendly adjustment? Generally, taxpayer-friendly adjustments (those that reduce income or credits or increase deductions) are not taken into account when calculating an imputed underpayment of tax. For this reason, most partnerships will prefer to make a push-out election and push adjustments out to partners, who can take advantage of taxpayer-friendly adjustments (to an extent).

When a push-out election is made, partners must calculate their reduction in tax for the reviewed year (the year the adjustment relates to) but claim the reduction as a nonrefundable tax credit in the adjustment year (the year the AAR is filed). This obviously creates a potentially lost benefit if the taxpayer-friendly adjustment cannot be fully taken in the adjustment year.

Example of Negative Adjustments from a Push-Out Election

Anne is a partner in a CPAR partnership. The partnership was audited by the IRS in 2024 (the reporting year) for the 2022 taxable year (the reviewed year), which resulted in a significant reduction of the partnership's income.

Under the CPAR rules, the audit results in zero imputed underpayment of tax at the partnership level because the CPAR rules only take into account adjustments that benefit the IRS when calculating an imputed underpayment of tax.

Instead of losing the benefit of the reduced income, the partnership makes a push-out election and issues Form 8986, Partner's Share of Adjustment(s) to Partnership-Related Item(s). Form 8986 issued to Anne reflects her share of the reduced partnership income.

Anne will use the Form 8986 issued to her in 2024 to complete Form 8978, Partner's Additional Reporting Year Tax, on her personal income tax return for 2024. Form 8978 is used to calculate the reduction of Anne's reviewed-year tax, which must be claimed as a credit on her reporting year (2024) income tax return.

After Anne uses Form 8978 to calculate her 2024 tax credit, the credit flows to Schedule 3, line 6l as a nonrefundable credit and cannot be carried forward under current law. So, if the negative partnership adjustment is large enough, Anne will permanently lose out on the benefit.

The end result is the same whether Anne's share of the partnership adjustment was made during a CPAR audit or as the result of an AAR.

Making the Adjustment on the Partner's Return

There is a six-step process to making partnership push-out adjustments on the partner's adjustment-year return. For these purposes, assume you are preparing a client's 2024 personal income tax return, and the client provides you with a Form 8986, Partner's Share of Adjustment(s) to Partnership-Related Item(s).

Step 1: Determine which year to make the adjustments to the partner's income tax return

Part II of Form 8986 contains three important dates in boxes D, E, and F. They are:

- **Box D:** Reviewed tax year-end date, which is the year to which the partnership adjustment relates;
- **Box E:** Adjustment tax year-end date, which is the year the partnership made its adjustment on its income tax return; and
- **Box G:** Date the partnership furnished Form 8986 to its partners.

Partners must make their adjustments on their income tax return for their reporting year, which is the partner's taxable year within which the date on Box G falls.

Example of Partner Reporting Year

The ABC partnership is a calendar-year partnership and timely filed its 2021 income tax return. On December 30, 2023, it filed an administrative adjustment request. On January 3, 2024, it mailed Forms 8986 to its partners to push out each partner's share of the partnership adjustments. Part II of Form 8986 will show the following dates:

- **Box D (reviewed year):** December 31, 2021;
- **Box E (adjustment year):** December 31, 2023; and
- **Box G (date Form 8986 furnished to partners):** January 3, 2024.

Joe is an individual partner of the ABC partnership. Because the date on Form 8986, Part II, Box G falls within Joe's 2024 taxable year, he must report the adjustments on Form 8978 of his 2024 income tax return.

Step 2: Prepare current-year return

Use your tax software to prepare the client's current-year return as normal, leaving out the partnership adjustments reported on Form 8986 for now. Using Joe from the example, this is the 2024 tax year.

Step 3: Calculate the change in reviewed-year tax liability

Open the client's reviewed-year personal income tax return, and copy it to a new file. Using Joe from the example, this is the 2021 taxable year. In the copied-return file for the reviewed year, make the adjustments reported on Form 8986 as if you were preparing an amended return for the client. Make a note of the client's original income tax liability for the reviewed year and their newly calculated liability for the reviewed year using the partnership adjustments from Form 8986. If the client's tax liability increased, then the increase will ultimately be reported as an additional tax on the partner's reporting-year return (the 2024 year using Joe from our example). If the client's tax liability decreased, then the decrease will ultimately be reported as a nonrefundable credit on the partner's reporting-year return.

Step 4: Complete Form 8978 for the reporting year

In order to complete Form 8978, Partner's Additional Reporting Year Tax, you will need:

- The taxpayer's originally filed return for the reviewed year (using our example, this would be Joe's originally filed 2021 return);
- The recalculated reviewed-year return from Step 3; and
- Form 8986 issued by the partnership.

Completing Form 8978 is just a matter of pulling figures from the three items listed above.

Step 5: Double-check that additional tax or credit is carrying to Form 1040

Be sure any increased or decreased tax is correctly shown on Form 8978, line 14. If the result is an increase in tax, then the amount on Form 8978, line 14 should flow to Form 1040, line 16. On line 16, check Box 3 and enter the amount of the additional tax liability and "Form 8978" in the space next to Box 3. If the result is a decrease in tax, then the amount on Form 8978, line 14 should be reported as a nonrefundable credit on Form 1040, Schedule 3, line 6l.

Step 6: Attach copies

The calculation of the recomputed tax from Step 3 must be attached to Form 8978. Be sure to attach a copy of both the client's originally filed return for the reviewed year (2021 from our example of Joe) as well as the recomputed reviewed-year return. These will serve as support for the change in tax calculation.

GROUP STUDY MATERIALS

A. Discussion Questions

1. What is the significance of the April 15, 2025, filing deadline for individuals?

2. Why is the personal exemption deduction set at zero for tax years 2018 through 2025?

3. What determines whether a child qualifies as a dependent for Head of Household status?

4. What are the tax implications of a wash sale?

5. What are the key features of the home energy rebates, and how do they interact with the Energy Efficient Home Improvement Credit?

6. How does the Partner Reporting of Administrative Adjustment Requests (AARs) work under the centralized partnership audit regime (CPAR), and what options do partnerships have for handling adjustments?

B. Suggested Answers to Discussion Questions

1. The April 15, 2025, deadline is the due date for filing federal income tax returns for the 2024 tax year. Taxpayers must either submit their return or request a filing extension by this date to avoid penalties. Those who owe taxes and miss the deadline could face interest and late payment penalties, whereas those eligible for refunds must file within three years to claim them

2. The Tax Cuts and Jobs Act (TCJA) suspended the personal exemption deduction to simplify tax calculations and offset the costs of other tax benefits, such as the expanded standard deduction and increased Child Tax Credit. Although set to zero, the personal exemption amount still plays a role in determining whether a dependent qualifies for certain benefits. For instance, it is used as part of the gross income test for dependents and for calculating the $500 nonrefundable credit for "other dependents.

3. To claim Head of Household (HOH) status, a taxpayer must maintain a household for a qualifying child or dependent relative for more than half the year. The qualifying child must meet criteria such as age (under 19 or 24 if a full-time student), relationship (child, sibling, or descendant), residency (lived with the taxpayer for more than half the year), and support (the child cannot provide over half of their own financial support). If two taxpayers claim the same child, tie-breaker rules apply based on factors like relationship, time lived with the taxpayer, and income

4. A wash sale occurs when a taxpayer sells or trades stock or securities at a loss and then repurchases substantially identical securities within 30 days before or after the sale. Under IRS rules, losses from a wash sale are disallowed, but they are not permanently lost. Instead, the disallowed loss is added to the basis of the repurchased securities, effectively deferring the loss until the new securities are sold. This rule ensures that taxpayers cannot immediately benefit from a tax deduction while maintaining an identical investment.

5. Home energy rebates, authorized under the Inflation Reduction Act (IRA) of 2022, provide financial incentives for homeowners to make energy-efficient upgrades. These rebates, treated as reductions in purchase price, are not taxable under federal law and do not require state agencies to issue Form 1099s. However, the rebate amount must be subtracted from the qualifying expenses when calculating the Energy Efficient Home Improvement Credit.

   In cases where a taxpayer claims both a home energy rebate and the Energy Efficient Home Improvement Credit for the same property, the rebate reduces the cost basis used to calculate the credit. For example, if a taxpayer installs a heat pump for $2,000 and receives a $400 rebate, the cost basis for the credit would be $1,600, yielding a credit of $480 (30% of $1,600).

6. Under the CPAR, partnerships subject to these rules cannot amend their returns. Instead, they must file an Administrative Adjustment Request (AAR) to report any adjustments.

   Key details include:

   - **Treatment of Adjustments:** If the AAR results in an underpayment, the partnership must pay the tax at the partnership level in the adjustment year (taxpayer-friendly adjustments generally are not taken into account when calculating an imputed underpayment of tax) unless it elects to "push out" the adjustment to the individual partners.

   - **Push-Out Election:** With this election, partners report their share of the adjustment for the reviewed year but apply any tax reductions as nonrefundable credits in the adjustment year. This option is preferred when adjustments are taxpayer-friendly (e.g., reducing income or increasing deductions). However, if the credit exceeds the partner's liability in the adjustment year, the benefit may be partially lost.

   - **Superseding Returns:** Partnerships can file a superseding original return (if within the extended deadline) to avoid needing an AAR. This superseding return replaces the initial return as the official filing

GLOSSARY OF KEY TERMS

Beneficial Ownership Information (BOI)

Beneficial Ownership Information is the identifying information of the individuals who directly or indirectly own or control a reporting entity. Beneficial ownership information that an entity must report includes the full legal names, dates of birth, and addresses of all individuals who have "substantial control" or who own at least 25% of the entity.

Financial Crimes Enforcement Network (FinCEN)

A bureau of the United States Department of the Treasury that collects and analyzes information about financial transactions in order to combat money laundering, terrorist financiers, and other financial crimes.

Specific Identification Method

When less than the entire holdings of stock is sold, a taxpayer may use the specific identification method to determine the basis and holding period of stock sold by specifically identifying which shares were sold. Adequate identification must be made by the taxpayer.

Transfer Pricing Methods

Transfer pricing methods are ways of establishing arm's length prices or profits from transactions between associated enterprises.

Required Minimum Distributions

Distributions from qualified plans and IRAs that generally must commence at age 73 to avoid a 25% penalty.

Circular 230

Circular 230 describes the government's expectations, the rights, and the professional obligations of those who represent taxpayers before the IRS.

Qualifying Child (QC)

A child who meets the relationship, age, residency, support, joint return, and the special tests with regard to a taxpayer to determine the taxpayer's eligibility to claim the dependency exemption, child tax credit, earned income credit, or child and dependent care credit with regard to the child, or to use the head of household filing status.

Kiddie Tax Rules

Rules that require unearned income of certain children to be taxed at the parents' marginal tax rate.

Wash Sale

A wash sale is the purchase of substantially similar stock or other securities within 30 days before or after the sale of the similar stock or security at a loss. A taxpayer cannot claim a wash sale loss. Instead, the loss is added to the basis of the most recently purchased substantially similar securities. A wash sale gain, however, is taxable.

Foreign Earned Income Exclusion

A U.S. citizen or resident alien of the United States living abroad may qualify to exclude from income up to an amount of their foreign earnings adjusted annually for inflation. Form 2555 is used to calculate the foreign earned income exclusion.

Dependent Care Assistance

Payment for or provision of services by the employer that if paid for by the employee would be considered employment-related expenses under the child and dependent care credit rules. Within limits, payments incurred by an employer for dependent care assistance under a written plan are excluded from an employee's gross income.

Alimony

Alimony is an amount paid to a spouse or former spouse under a divorce or separation agreement. Payments made under any of the following may be considered alimony: a decree of divorce or separate maintenance or written instrument incident to divorce, a written separation agreement, or a support decree.

Long-Term Care Insurance

An insurance policy to cover nursing home or other long-term home health care.

Casualty Loss

The complete or partial destruction of property resulting from an identifiable event of a sudden, unexpected, or unusual nature. Examples include floods, storms, fires, earthquakes, auto accidents, and terrorist attacks. Individuals may deduct a casualty loss if the loss is incurred in a trade or business or is incurred in a transaction entered into for profit. For tax years 2018-2025, personal casualty losses are only deductible if incurred in a federally declared disaster area. A taxpayer who suffers a personal casualty loss from a disaster declared by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act will still be able to claim an itemized deduction for tax years 2018–2025. Individuals deduct personal casualty losses as itemized deductions on Schedule A. Use of Form 4684, *Casualties and Thefts*, is required.

Charitable Contributions

An itemized deduction is allowed for donations to qualifying charities. For property donations, the amount of the deduction depends on the type of property and donee organization, the holding period, and in some cases, how the property is used.

Net Investment Income Tax

IRC §1411 adds an additional 3.8% tax on top of an individual taxpayer's ordinary income and capital gains taxes. The tax is applied to the lesser of the following two items for most individuals: A taxpayer's net investment income (as defined by IRC §1411) or The taxpayer's modified adjusted gross income (again as computed under IRC §1411) over a threshold amount which is set at $250,000 for a married couple filing a joint return or a surviving spouse, $125,000 for a married individual filing a separate return, or $200,000 for all other taxpayers (that is, single and head of household filing status). **[IRC §7701(a)(1)]**

Section 529 Plans

Qualified tuition plans set up by states or private institutions as either prepaid tuition plans or savings-type plans. While contributions are not deductible for federal income tax purposes, distributions used to pay qualified higher education costs are tax free.

Centralized Partnership Audit Rules

These rules provide for the audit and assessment at the partnership rather than the partner level. Under IRC § 6221(b) a partnership with 100 or fewer partners during the year, and all its partners are “eligible partners” at all times during the tax year may elect out of the Centralized Partnership Audit rules

CPE Network®
Tax Report
Volume 38, Issue 2 **February 2025**

SUBSCRIBER SURVEY

Evaluation Form

Please take a few minutes to complete this survey related to the **CPE Network® Tax Report** and return with your quizzer or group attendance sheet to CeriFi, LLC. All responses will be kept confidential. Comments in addition to the answers to these questions are also welcome. Please send comments to **CPLgrading@cerifi.com**.

How would you rate the topics covered in the February 2025 issue of **CPE Network® Tax Report?** Rate each topic on a scale of 1–5 (5=highest):

	Topic Relevance	**Topic Content/ Coverage**	**Topic Timeliness**	**Video Quality**	**Audio Quality**	**Written Material**
Experts' Forum	|______|	|______|	|______|	|______|	|______|	|______|
Individual Tax Update	|______|	|______|	|______|	|______|	|______|	|______|

Which segments of the February 2025 issue of **CPE Network® Tax Report** did you like the most, and why?

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Which segments of the February 2025 issue of **CPE Network® Tax Report** did you like the least, and why?

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What would you like to see included or changed in future issues of **CPE Network® Tax Report**?

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Are there any other ways in which we can improve **CPE Network® Tax Report**?

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How would you rate the effectiveness of the speakers in the February 2025 **CPE Network® Tax Report**? Rate each speaker on a scale of 1–5 (5=highest):

	Overall	**Knowledge of Topic**	**Presentation Skills**
Ian Redpath	|_______|	|_______|	|_______|
Mike Giangrande	|_______|	|_______|	|_______|

Are you using **CPE Network® Tax Report** for: CPE Credit ☐ Information ☐ Both ☐ ____________________

Were the stated learning objectives met? Yes ☐ No ☐ ____________________

If applicable, were prerequisite requirements appropriate? Yes ☐ No ☐ ____________________

Were program materials accurate? Yes ☐ No ☐ ____________________

Were program materials relevant and contribute to the achievement of the learning objectives? Yes ☐ No ☐ __________

Were the time allocations for the program appropriate? Yes ☐ No ☐ ____________________

Were the supplemental reading materials satisfactory? Yes ☐ No ☐ ____________________

Were the discussion questions and answers satisfactory? Yes ☐ No ☐ ____________________

Were the audio and visual materials effective? Yes ☐ No ☐ ____________________

Specific Comments: ____

____

Name/Company ____

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Once Again, Thank You…
Your Input Can Have a Direct Influence on Future Issues!

CPE Network®

CPE Group Attendance Sheet

Firm/Company Name: ______________________________

Account #: ______________________________

Location: ______________________________

Program Title: CPE Network Tax Report, February 2025 Date: __________

Name	Email	Total Hrs	IRS PTIN ID (if applicable Tax only)	Sign In	Sign Out

I certify that the above individuals viewed and were participants in the group discussion with this issue/segment of the CPE Network® newsletter, and earned the number of hours shown.

Instructor Name: ______________________________ Date: __________

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CPE Network/Webinar Delivery Tracking Report

Course Title	
Course Date:	
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Moderator Name, Credentials, and Signature Attestation of Attendance:	
Delivery Method:	Group Internet Based
Total CPE Credit:	3.0
Instructions:	During the webinar, the moderator must verify student presence a minimum of 3 times per CPE hour. This is achieved via polling questions. Sponsors must have a report which documents the responses from each student. The timing of the polling questions should be random and not made known to students prior to delivery of the course. Record the polling question responses below. Refer to the CPL Network User Guide for more instructions. Partial credit will not be issued for students who do not respond to at least 3 polling questions per CPE hour.
Brief Description of Method of Polling	Example: Zoom: During this webinar, moderator asked students to raise their hands 3 times per CPE hour. The instructor then noted the hands that were raised in the columns below.

			First CPE Hour			**CPE Hour 2**			**CPE Hour 3**			**FOR TR USE ONLY**
First Name	**Last Name**	**Student Email**	**Poll 1**	**Poll 2**	**Poll 3**	**Poll 1**	**Poll 2**	**Poll 3**	**Poll 1**	**Poll 2**	**Poll 3**	**Certificate Issued?**

CHECKPOINT LEARNING NETWORK

CPE NETWORK®
USER GUIDE

REVISED December 31, 2023

Welcome to CPE Network!

CPE Network programs enable you to deliver training programs to those in your firm in a manageable way. You can choose how you want to deliver the training in a way that suits your firm's needs: in the classroom, virtual, or self-study. You must review and understand the requirements of each of these delivery methods before conducting your training to ensure you meet (and document) all the requirements.

This User Guide has the following sections:

- **"Group Live" Format:** The instructor and all the participants are gathered into a common area, such as a conference room or training room at a location of your choice.
- **"Group Internet Based" Format:** Deliver your training over the internet via Zoom, Teams, Webex, or other application that allows the instructor to present materials that all the participants can view at the same time.
- **"Self-Study" Format:** Each participant can take the self-study version of the CPE Network program on their own computers at a time and place of their convenience. No instructor is required for self-study.
- **Transitioning From DVDs:** For groups playing the video from the online platform, we suggest downloading the video from the Checkpoint Learning player to the desktop before projecting.
- **What Does It Mean to Be a CPE Sponsor?:** Should you decide to vary from any of the requirements in the 3 methods noted above (for example, provide less than 3 full CPE credits, alter subject areas, offer hybrid or variations to the methods described above), <u>Checkpoint Learning Network will not be the sponsor and will not issue certificates.</u> In this scenario, your firm will become the sponsor and must issue its own certificates of completion. This section outlines the sponsor's responsibilities that you must adhere to if you choose not to follow the requirements for the delivery methods.
- **Getting Help:** Refer to this section to get your questions answered.

IMPORTANT: This User Guide outlines in detail what is required for each of the 3 formats above. Additionally, because you will be delivering the training within your firm, you should review the Sponsor Responsibilities section as well. To get certificates of completion for your participants following your training, you must submit all the required documentation. (This is noted at the end of each section.) Checkpoint Learning Network will review your training documentation for completeness and adherence to all requirements. If all your materials are received and complete, certificates of completion will be issued for the participants attending your training. Failure to submit the required completed documentation will result in delays and/or denial of certificates.

IMPORTANT: If you vary from the instructions noted above, your firm will become the sponsor of the training event and you will have to create your own certificates of completions for your participants. In this case, you do not need to submit any documentation back to CeriFi, LLC.

If you have any questions on this documentation or requirements, refer to the "Getting Help" section at the end of this User Guide **BEFORE** you conduct your training.

We are happy that you chose CPE Network for your training solutions.
Thank you for your business and HAPPY LEARNING!

Copyrighted Materials

CPE Network program materials are copyrighted and may not be reproduced in another document or manuscript in any form without the permission of the publisher. As a subscriber of the **CPE Network Series,** you may reproduce the necessary number of participant manuals needed to conduct your group study session.

“Group Live” Format

CPE Credit

All CPE Network products are developed and intended to be delivered as 3 CPE credits. You should allocate sufficient time in your delivery so that there is no less than 2.5 clock hours:

50 minutes per CPE credit TIMES 3 credits = 150 minutes = 2.5 clock hours

If you wish to have a break during your training session, you should increase the length of the training beyond 2.5 hours as necessary. For example, you may wish to schedule your training from 9 AM to 12 PM and provide a ½ hour break from 10:15 to 10:45.

***Effective November 1, 2018:** Checkpoint Learning CPE Network products ‘group live’ sessions must be delivered as 3 CPE credits and accredited to the field(s) of study as designated by Checkpoint Learning Network. Checkpoint Learning Network will not issue certificates for “group live” deliveries of less than 3 CPE credits (unless the course was delivered as 3 credits and there are partial credit exceptions (such as late arrivals and early departures). Therefore, if you decide to deliver the “group live” session with less than 3 CPE credits, your firm will be the sponsor as Checkpoint Learning Network will not issue certificates to your participants.

Advertising / Promotional Page

Create a promotion page (use the template after the executive summary of the transcript). You should circulate (e.g., email) to potential participants prior to training day. You will need to submit a copy of this page when you request certificates.

Monitoring Attendance

You must monitor individual participant attendance at “group live” programs to assign the correct number of CPE credits. A participant’s self-certification of attendance alone is not sufficient.

Use the **attendance sheet.** This lists the instructor(s) name and credentials, as well as the first and last name of each participant attending the seminar. The participant is expected to initial the sheet for their morning attendance and provide their signature for their afternoon attendance. If a participant arrives late, leaves early, or is a “no show,” the actual hours they attended should be documented on the sign-in sheet and will be reflected on the participant’s CPE certificate.

Real Time Instructor During Program Presentation

"Group live" programs must have a **qualified, real time instructor while the program is being presented.** Program participants must be able to interact with the instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A "group live" program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Make-Up Sessions

Individuals who are unable to attend the group study session may use the program materials for self-study online.

- If the emailed materials are used, the user should read the materials, watch the video, and answer the quizzer questions on the CPE Quizzer Answer Sheet. Send the answer sheet and course evaluation to the email address listed on the answer sheet and the CPE certificate will be mailed or emailed to the user. Detailed instructions are provided on Network Program Self-Study Options.
- If the online materials are used, the user should log on to her/his individual Checkpoint Learning account to read the materials, watch the interviews, and answer the quizzer questions. The user will be able to print her/his/their CPE certificate upon completion of the quizzer. (If you need help setting up individual user accounts, please contact your firm administrator or customer service.)

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded by Checkpoint Learning Network after the "group live" documentation is received (and providing the course is delivered as 3 CPE credits). The certificate of completion will reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early.

Subscriber Survey Evaluation Forms

Use the evaluation form. You must include a means for evaluating quality. At the conclusion of the “group live” session, evaluations should be distributed and any that are completed are collected from participants. Those evaluations that are completed by participants should be returned to Checkpoint Learning Network along with the other course materials. While it is required that you circulate the evaluation form to all participants, it is NOT required that the participants fill it out. A preprinted evaluation form is included in the transcript each month for your convenience.

Retention of Records

Regardless of whether Checkpoint Learning Network is the sponsor for the “group live” session, it is required that the firm hosting the “group live” session retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (Group Study Attendance sheets; indicating any late arrivals and/or early departures)
- Copy of the program materials
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name and credentials
- Results of program evaluations.

Finding the Transcript

Note: DVDs no longer ship with this product effective 3/1/2023.

When the DVD is inserted into a DVD drive, the video will immediately begin to play and the menu screen will pop up, taking the entire screen. Hitting the Esc key should minimize it to a smaller window. To locate the pdf file of the transcript either to save or email to others, go to the start button on the computer. In My Computer, open the drive with the DVD. The Adobe Acrobat files are the transcript files. If you do not currently have Adobe Acrobat Reader (Mac versions of the reader are also available), a free version of the reader may be downloaded at:

- https://get.adobe.com/reader/

The entire transcript is also available as a pdf in the Checkpoint Learning player in the resource toolbox at the top of the screen, or via the link in the email sent to administrators.

Requesting Participant CPE Certificates

When delivered as 3 CPE credits, documentation of your "group live" session should be sent to Checkpoint Learning Network by the following means:

Email: CPLgrading@cerifi.com

When sending your package to CeriFi, you must include ALL of the following items:

Form Name	**Included?**	**Notes**
Advertising / Promotional Page		Complete this form and circulate to your audience before the training event.
Attendance Sheet		Use this form to track attendance during your training session.
Subscriber Survey Evaluation Form		Circulate the evaluation form at the end of your training session so that participants can review and comment on the training. Return to CeriFi any evaluations that were completed. You do not have to return an evaluation for every participant.

Incomplete submissions will be returned to you.

"Group Internet Based" Format

CPE Credit

All CPE Network products are developed and intended to be delivered as 3 CPE credits. You should allocate sufficient time in your delivery so that there is no less than 2.5 clock hours:

50 minutes per CPE credit TIMES 3 credits = 150 minutes = 2.5 clock hours

If you wish to have a break during your training session, you should increase the length of the training beyond 2.5 hours as necessary. For example, you may wish to schedule your training from 9 AM to 12 PM and provide a ½ hour break from 10:15 to 10:45.

***Effective November 1, 2018:** Checkpoint Learning CPE Network products 'group live' sessions must be delivered as 3 CPE credits and accredited to the field(s) of study as designated by Checkpoint Learning Network. Checkpoint Learning Network will not issue certificates for "group live" deliveries of less than 3 CPE credits (unless the course was delivered as 3 credits and there are partial credit exceptions (such as late arrivals and early departures). Therefore, if you decide to deliver the "group live" session with less than 3 CPE credits, your firm will be the sponsor as Checkpoint Learning Network will not issue certificates to your participants.

Advertising / Promotional Page

Create a promotion page (use the template following the executive summary in the transcript). You should circulate (e.g., email) to potential participants prior to training day. You will need to submit a copy of this page when you request certificates.

Monitoring Attendance in a Webinar

You must monitor individual participant attendance at "group internet based" programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient.

Use the **Webinar Delivery Tracking Report.** This form lists the moderator(s) name and credentials, as well as the first and last name of each participant attending the seminar. During a webinar you must set up a monitoring mechanism (or polling mechanism) to periodically check the participants' engagement throughout the delivery of the program. Participants' two-way video should remain on during the entire presentation.

In order for CPE credit to be granted, you must confirm the presence of each participant **3 times per CPE hour and the participant must reply to the polling question**. Participants that respond to less than 3 polling questions in a CPE hour will not be granted CPE credit. For example, if a participant only replies to 2 of the 3 polling questions in the first CPE hour, credit for the first CPE hour will not be granted. (Refer to the Webinar Delivery Tracking Report for examples.)

Examples of polling questions:

1. You are using **Zoom** for your webinar. The moderator pauses approximately every 15 minutes and asks that participants confirm their attendance by using the "raise hands"

feature. Once the participants raise their hands, the moderator records the participants who have their hands up in the **webinar delivery tracking report** by putting a YES in the webinar delivery tracking report. After documenting in the spreadsheet, the instructor (or moderator) drops everyone's hands and continues the training.

2. You are using **Teams** for your webinar. The moderator will pause approximately every 15 minutes and ask that participants confirm their attendance by typing "Present" into the Teams chat box. The moderator records the participants who have entered "Present" into the chat box into the **webinar delivery tracking report**. After documenting in the spreadsheet, the instructor (or moderator) continues the training.
3. If you are using an application that has a way to automatically send out polling questions to the participants, you can use that application/mechanism. However, following the event, you should create a **webinar delivery tracking report** from your app's report.

Additional Notes on Monitoring Mechanisms:

1. The monitoring mechanism does not have to be "content specific." Rather, the intention is to ensure that the remote participants are present and paying attention to the training.
2. You should only give a minute or so for each participant to reply to the prompt. If, after a minute, a participant does not reply to the prompt, you should put a NO in the webinar delivery tracking report.
3. While this process may seem unwieldy at first, it is a required element that sponsors must adhere to. And after some practice, it should not cause any significant disruption to the training session.
4. **You must include the Webinar Delivery Tracking report with your course submission if you are requesting certificates of completion for a "group internet based" delivery format.**

Real Time Moderator During Program Presentation

"Group internet based" programs must have a **qualified, real time moderator while the program is being presented.** Program participants must be able to interact with the moderator while the course is in progress (including the opportunity to ask questions and receive answers during the presentation). This can be achieved via the webinar chat box, and/or by unmuting participants and allowing them to speak directly to the moderator.

Where individual participants log into a group live program they are required to enable two-way video to participate in a virtual face-to-face setting (with cameras on), elements of engagement are required (such as group discussion, polling questions, instructor posed questions with time for reflection, or a case study with engagement throughout the presentation) in order to award CPE credits to the participants. Participation in the two-way video conference must be monitored and documented by the instructor or attendance monitor in order to authenticate attendance for program duration. The participant-to-attendance monitor ratio must not exceed 25:1, unless there is a dedicated attendance monitor in which case the participant-to-attendance monitor ratio must not exceed 100:1.

Make-Up Sessions

Individuals who are unable to attend the "group internet based" session may use the program materials for self-study either in print or online.

- If emailed materials are used, the user should read the materials, watch the video, and answer the quizzer questions on the CPE Quizzer Answer Sheet. Send the answer sheet and course evaluation to the email address listed on the answer sheet and the CPE certificate will be mailed or emailed to the user. Detailed instructions are provided on Network Program Self-Study Options.
- If the online materials are used, the user should log on to her/his individual Checkpoint Learning account to read the materials, watch the interviews, and answer the quizzer questions. The user will be able to print her/his CPE certificate upon completion of the quizzer. (If you need help setting up individual user accounts, please contact your firm administrator or customer service.)

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded by Checkpoint Learning Network after the "group internet based" documentation is received (and providing the course is delivered as 3 CPE credits). The certificate of completion will reflect the credit hours earned by the individual, with special calculation of credits for those who may not have answered the required amount of polling questions.

Subscriber Survey Evaluation Forms

Use the evaluation form. You must include a means for evaluating quality. At the conclusion of the "group live" session, evaluations should be distributed and any that are completed are collected from participants. Those evaluations that are completed by participants should be returned to Checkpoint Learning Network along with the other course materials. While it is required that you circulate the evaluation form to all participants, it is NOT required that the participants fill it out. A preprinted evaluation form is included in the transcript each month for your convenience.

Retention of Records

Regardless of whether Checkpoint Learning Network is the sponsor for the “group internet based” session, it is required that the firm hosting the session retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (Webinar Delivery Tracking Report)
- Copy of the program materials
- Timed agenda with topics covered
- Date and location (which would be “virtual”) of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name and credentials
- Results of program evaluations

Finding the Transcript

Note: DVDs are no longer shipped effective 3/1/2023

When the DVD is inserted into a DVD drive, the video will immediately begin to play and the menu screen will pop up, taking the entire screen. Hitting the Esc key should minimize it to a smaller window. To locate the pdf file of the transcript either to save or email to others, go to the start button on the computer. In My Computer, open the drive with the DVD. It should look something like the screenshot below. The Adobe Acrobat files are the transcript files. If you do not currently have Adobe Acrobat Reader (Mac versions of the reader are also available), a free version of the reader may be downloaded at:

- https://get.adobe.com/reader/

Alternatively, for those without a DVD drive, the email sent to administrators each month has a link to the pdf for the newsletter. The email may be forwarded to participants who may download the materials or print them as needed.

Requesting Participant CPE Certificates

When delivered as 3 CPE credits, documentation of your "group internet based" session should be sent to Checkpoint Learning Network by the following means:

Email: CPLgrading@CeriFi.com

When sending your package to CeriFi, you must include ALL the following items:

Form Name	**Included?**	**Notes**
Advertising / Promotional Page		Complete this form and circulate to your audience before the training event.
Webinar Delivery Tracking Report		Use this form to track the attendance (i.e., polling questions) during your training webinar.
Evaluation Form		Circulate the evaluation form at the end of your training session so that participants can review and comment on the training. Return to CeriFi any evaluations that were completed. You do not have to return an evaluation for every participant.

Incomplete submissions will be returned to you.

“Self-Study” Format

If you are unable to attend the live group study session, we offer two options for you to complete your Network Report program.

Self-Study—Email

Follow these simple steps to use the printed transcript and video:

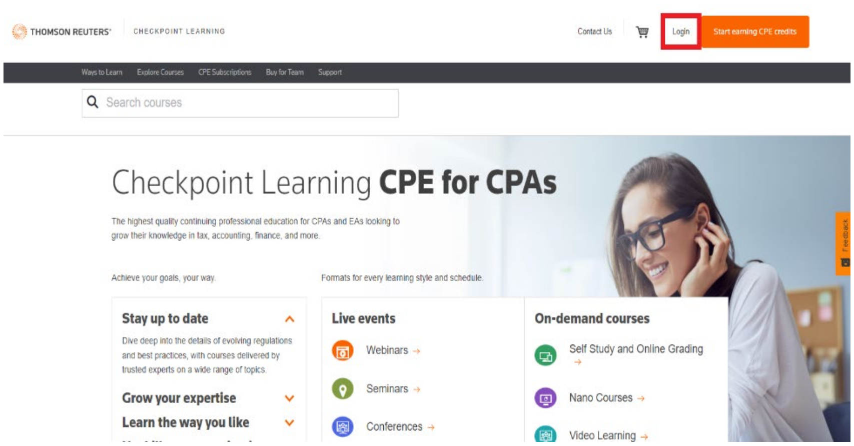
- Watch the video.
- Review the supplemental materials.
- Read the discussion problems and the suggested answers.
- Complete the quizzer by filling out the bubble sheet enclosed with the transcript package.
- Complete the survey. We welcome your feedback and suggestions for topics of interest to you.
- E-mail your completed quizzer and survey to:

  CPLgrading@cerifi.com

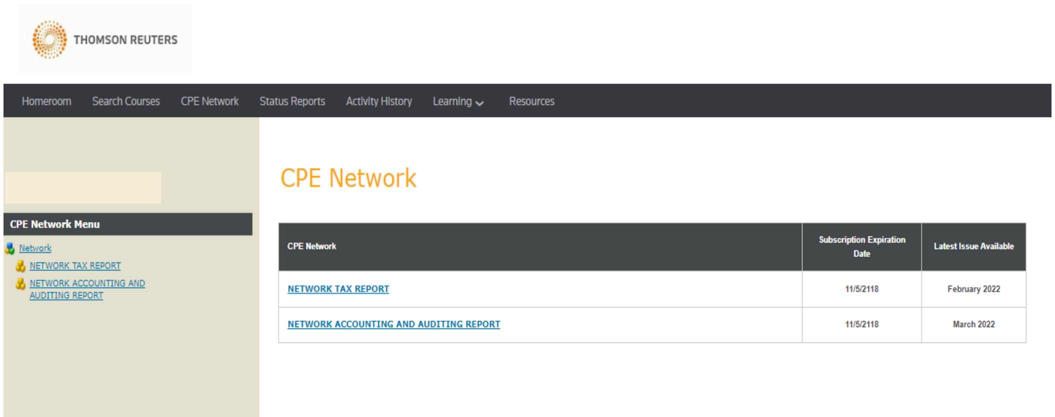
Self-Study—Online

Follow these simple steps to use the online program:

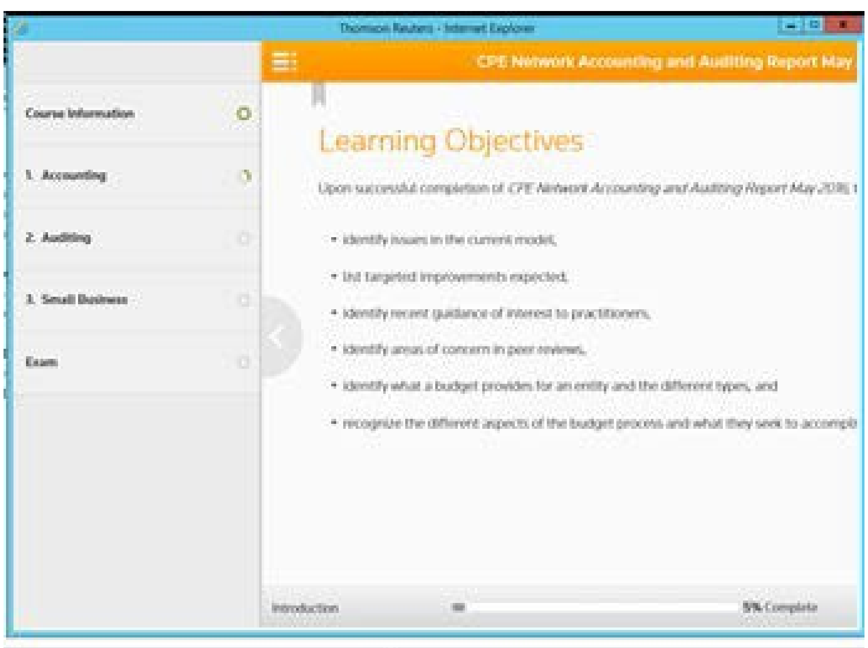
- Go to www.checkpointlearning.thomsonreuters.com .
- Log in using your username and password assigned by your firm’s administrator in the upper right-hand margin (“Login or Register”).



- In the **CPE Network** tab, select the desired Network Report and then the appropriate edition.

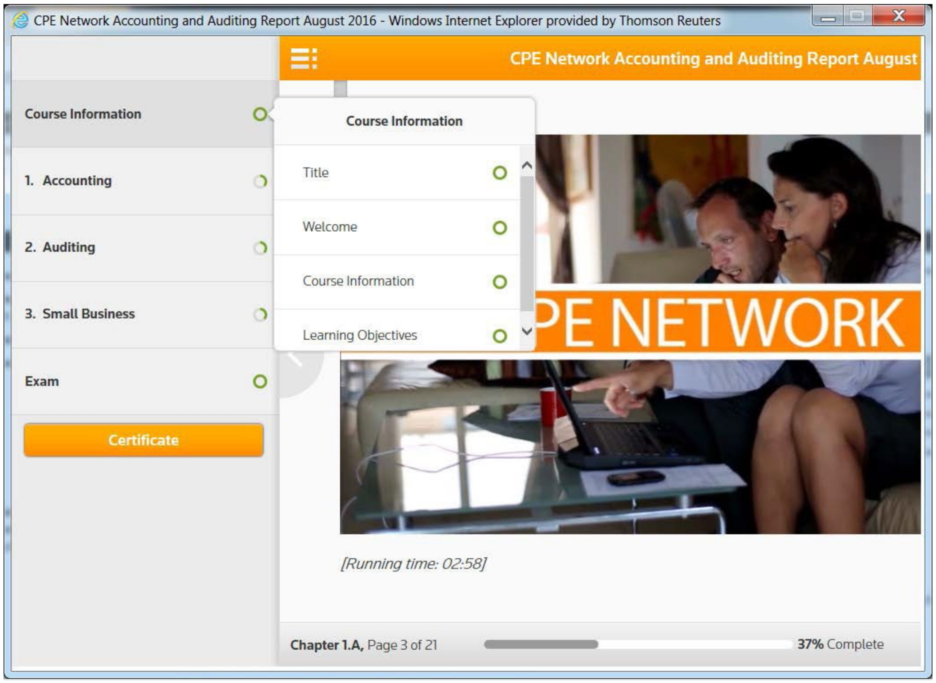


The Chapter Menu is in the gray bar at the left of your screen:

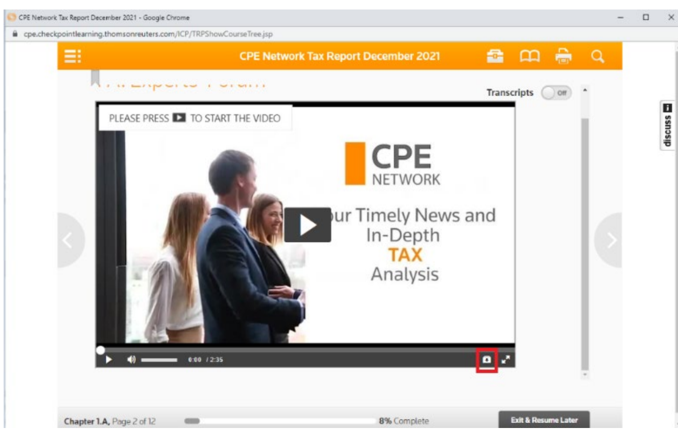


Click down to access the dropdown menu and move between the program Chapters.

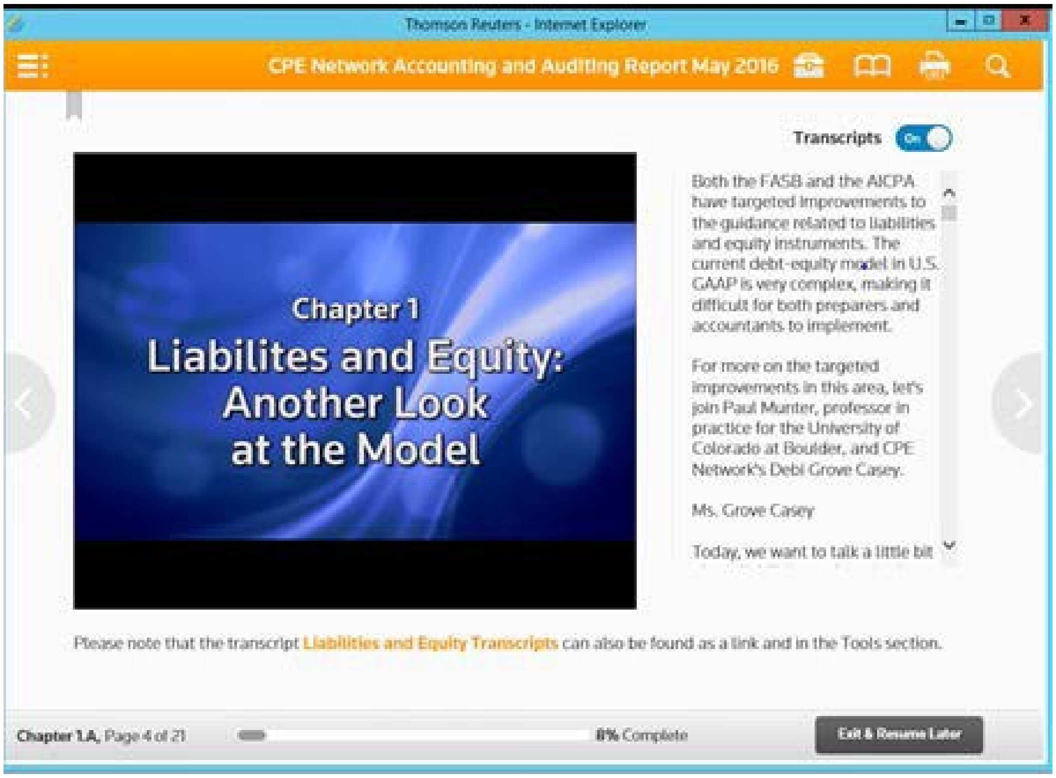
- **Course Information** is the course Overview, including information about the authors and the program learning objectives



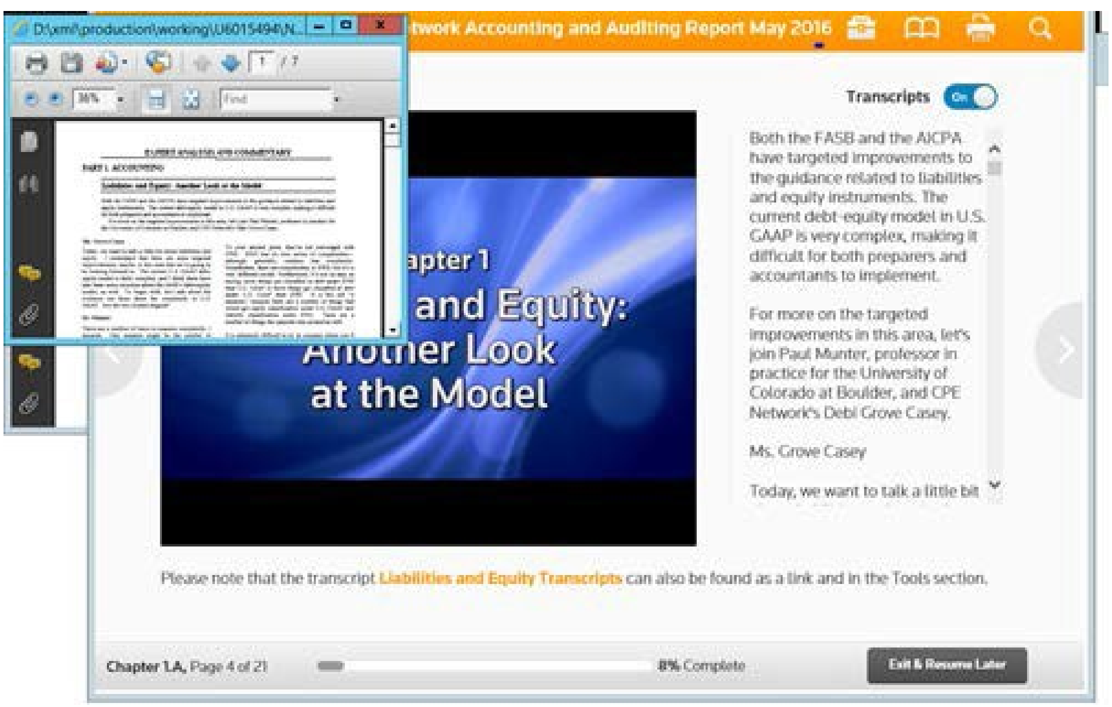
- **Each Chapter is self-contained.** Each chapter contains the executive summary and learning objectives for that segment, followed by the interview, the related supplemental materials, and then the discussion questions. This streamlined approach allows administrators and users to more easily access the related materials.



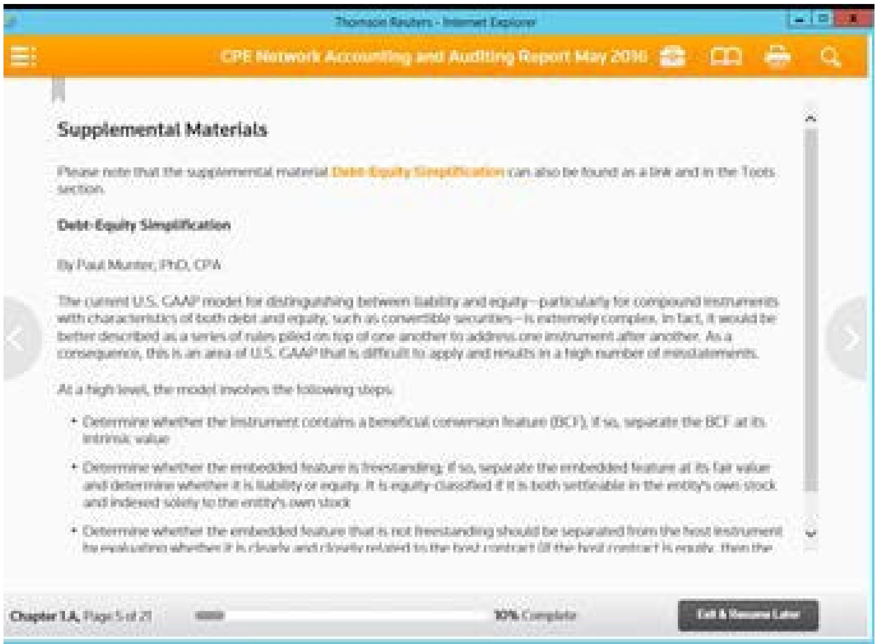
Video segments may be downloaded from the CPL player by clicking on the download button. Tip: you may need to scroll down to see the download button.

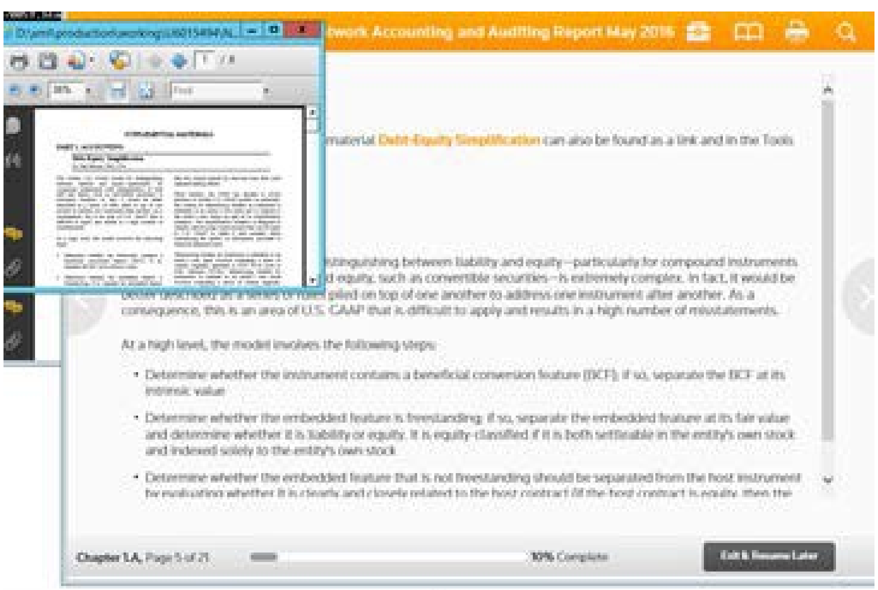


Transcripts for the interview segments can be viewed at the right side of the screen via a toggle button at the top labeled **Transcripts** or via the link to the pdf below the video (also available in the toolbox in the resources section). The pdf will appear in a separate pop-up window.



Click the arrow at the bottom of the video to play it, or click the arrow to the right side of the screen to advance to the supplemental material. As with the transcripts, the supplemental materials are also available via the toolbox and the link will pop up the pdf version in a separate window.





Continuing to click the arrow to the right side of the screen will bring the user to the Discussion p roblems related to the segment.

The Suggested Answers to the Discussion Problems follow the Discussion Problems.

Suggested Answers to Discussion Problems

1. ASC 320 requires that, at acquisition, an enterprise classify debt and marketable equity securities into one of three categories:

   - Held-to-maturity
   - Trading
   - Available-for-sale

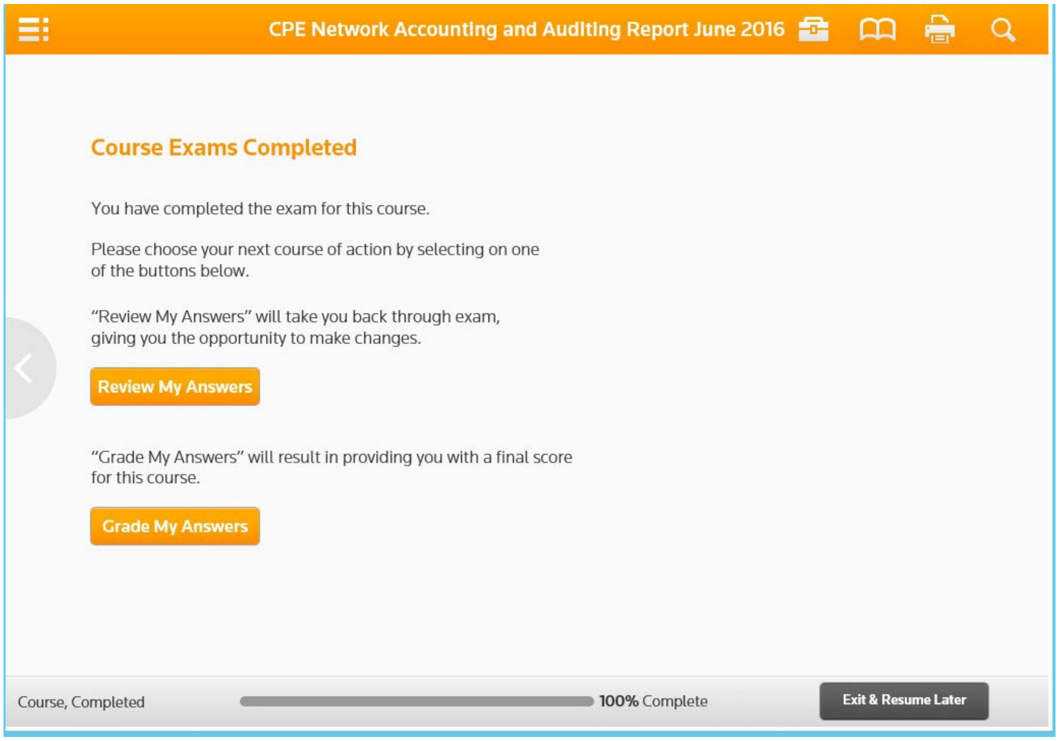
   An entity decides how to classify securities based on its intended holding period for each individual security, using the framework in ASC 320. In establishing its intent, an entity should consider relevant trends and experience, such as previous sales and transfers of securities. Classification decisions should be made at acquisition and, preferably, formally documented. It is not appropriate to use "hindsight" to classify securities transactions, perhaps by considering changes in value after acquisition.

2. The trading securities category includes securities that are bought and held principally for the purpose of selling them in the short term. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price. "Short-term," in this context, is intended to be measured in hours and days, rather than in months or years, according to ASC 320. However, an entity is not precluded from classifying as trading a security it plans to hold for a longer period, as long as that designation occurs at acquisition.

3. Impairment is recognized in earnings when a decline in value has occurred that is deemed to be other than temporary, and the current fair value becomes the new cost basis for the security. An investment is considered to be impaired if the fair value of the investment is less than its cost basis. Cost includes adjustments made for

The **Exam** is accessed by clicking the last gray bar on the menu at the left of the screen or clicking through to it. Click the orange button to begin.

When you have completed the quizzer, click the button labeled **Grade or the Review button**.



- Click the button labeled **Certificate** to print your CPE certificate.
- The final quizzer grade is displayed and you may view the graded answers by clicking the button labeled **view graded answer**.

Additional Features Search

Checkpoint Learning offers powerful search options. Click the **magnifying glass** at the upper right of the screen to begin your search. Enter your choice in the **Search For:** box.

Search Results are displayed with the number of hits.

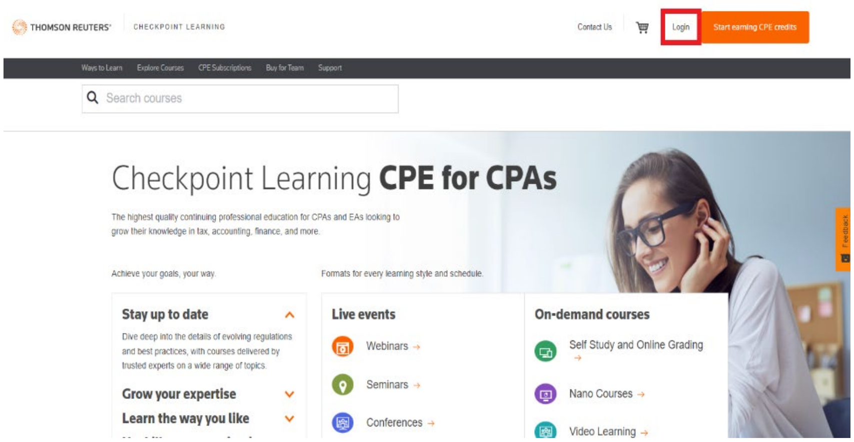
Print

To display the print menu, click the printer icon in the upper bar of your screen. You can print the entire course, the transcript, the glossary, all resources, or selected portions of the course. Click your choice and click the orange **Print**.

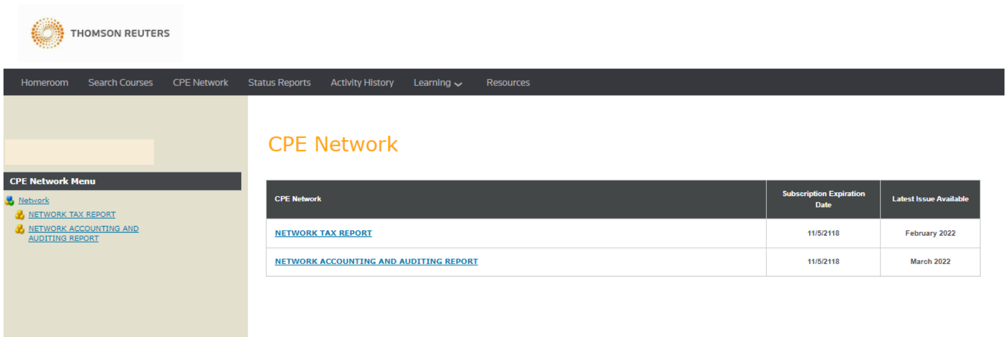
Transitioning From DVDs

Follow these simple steps to access the video and pdf for download from the online platform:

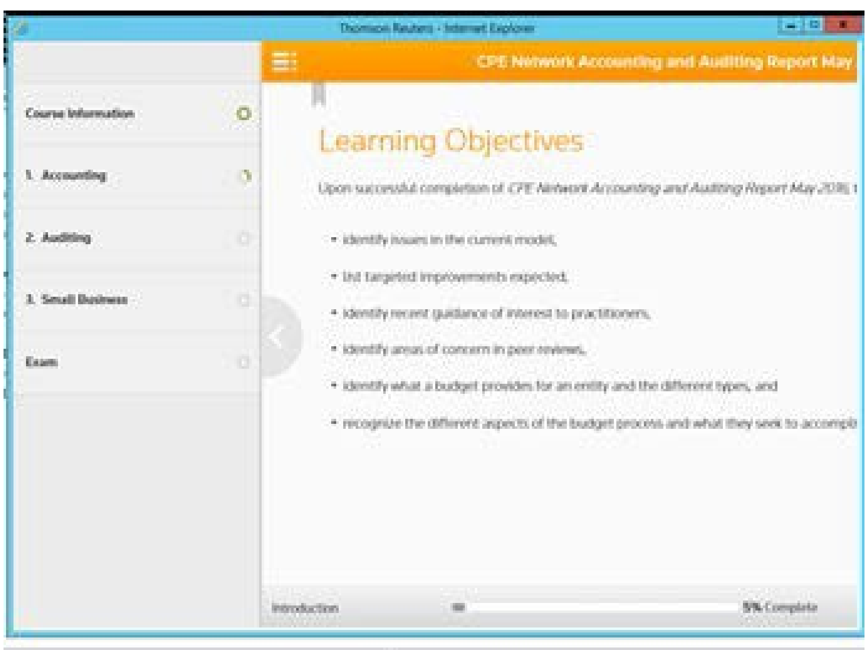
- Go to www.checkpointlearning.thomsonreuters.com .
- Log in using your username and password assigned by your firm's administrator in the upper right-hand margin ("Login").



- In the CPE **Network** tab, select the desired Network Report by clicking on the title, then select the appropriate edition.

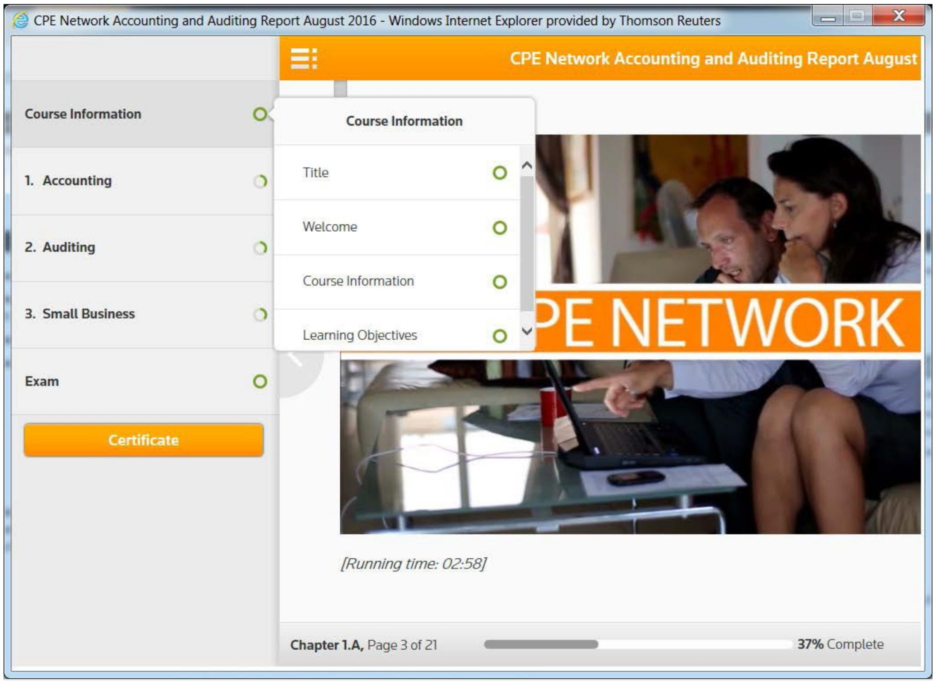


The Chapter Menu is in the gray bar at the left of your screen:

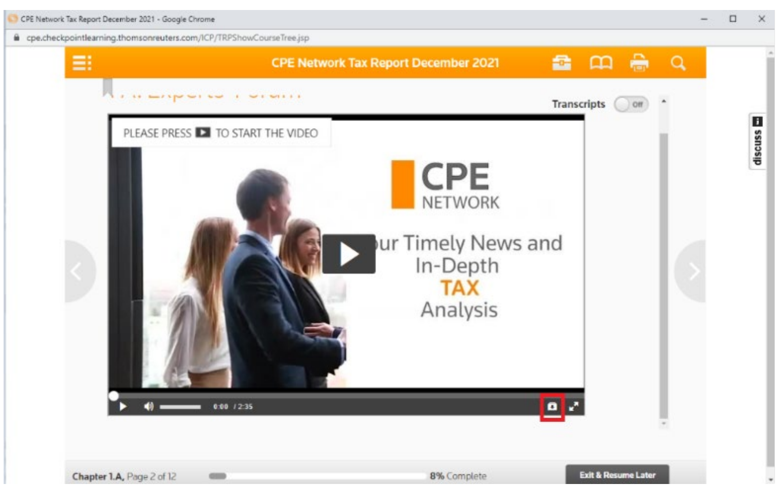


Click down to access the dropdown menu and move between the program Chapters.

- **Course Information** is the course Overview, including information about the authors and the program learning objectives



- Each Chapter is self-contained. Each chapter contains the executive summary and learning objectives for that segment, followed by the interview, the related supplemental materials, and then the discussion questions.



Video segments may be downloaded from the CPL player by clicking on the download button noted above. You may need to use the scroll bar to the right of the video to see the download button. **Tip: You may need to use the scroll bar to the right of the video to see the download button.**

PDFs may be downloaded from either the course toolbox in the upper right corner of the Checkpoint Learning screen or from the email sent to administrators with each release.

What Does It Mean to Be a CPE Sponsor?

If your organization chooses to vary from the instructions outlined in this User Guide, your firm will become the CPE Sponsor for this monthly series. The sponsor rules and requirements noted below are only highlights and reflect those of NASBA, the national body that sets guidance for development, presentation, and documentation for CPE programs. **For any specific questions about state sponsor requirements, please contact your state board. They are the final authority regarding CPE Sponsor requirements.** Generally, the following responsibilities are required of the sponsor:

- Arrange for a location for the presentation
- Advertise the course to your anticipated participants and disclose significant features of the program in advance
- Set the start time
- Establish participant sign-in procedures
- Coordinate audio-visual requirements with the facilitator
- Arrange appropriate breaks
- Have a real-time instructor during program presentation
- Ensure that the instructor delivers and documents elements of engagement
- Monitor participant attendance (make notations of late arrivals, early departures, and “no shows”)
- Solicit course evaluations from participants
- Award CPE credit and issue certificates of completion
- Retain records for five years

The following information includes instructions and generic forms to assist you in fulfilling your responsibilities as program sponsor.

CPE Sponsor Requirements

<u>Determining CPE Credit Increments</u>

Sponsored seminars are measured by program length, with one 50-minute period equal to one CPE credit. One-half CPE credit increments (equal to 25 minutes) are permitted after the first credit has been earned. Sponsors must monitor the program length and the participants’ attendance in order to award the appropriate number of CPE credits.

Program Presentation

CPE program sponsors must provide descriptive materials that enable CPAs to assess the appropriateness of learning activities. CPE program sponsors must make the following information available in advance:

- Learning objectives.
- Instructional delivery methods.
- Recommended CPE credit and recommended field of study.
- Prerequisites.
- Program level.
- Advance preparation.
- Program description.
- Course registration and, where applicable, attendance requirements.
- Refund policy for courses sold for a fee/cancellation policy.
- Complaint resolution policy.
- Official NASBA sponsor statement, if an approved NASBA sponsor (explaining final authority of acceptance of CPE credits**).**

Disclose Significant Features of Program in Advance

For potential participants to effectively plan their CPE, the program sponsor must disclose the significant features of the program in advance (e.g., through the use of brochures, website, electronic notices, invitations, direct mail, or other announcements). When CPE programs are offered in conjunction with non-educational activities, or when several CPE programs are offered concurrently, participants must receive an appropriate schedule of events indicating those components that are recommended for CPE credit. The CPE program sponsor's registration and attendance policies and procedures must be formalized, published, and made available to participants and include refund/cancellation policies as well as complaint resolution policies.

Monitor Attendance

While it is the participant's responsibility to report the appropriate number of credits earned, CPE program sponsors must maintain a process to monitor individual attendance at group programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient. The sign-in sheet should list the names of each instructor and her/his credentials, as well as the name of each participant attending the seminar. The participant is expected to initial the sheet for their morning attendance and provide their signature for their afternoon attendance. If a participant leaves early, the hours they attended should be documented on the sign-in sheet and on the participant's CPE certificate.

Real Time Instructor During Program Presentation

"Group live" programs must have a qualified, real-time instructor while the program is being presented. Program participants must be able to interact with the real time instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A "group live" program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded at the conclusion of the seminar. It should reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early.

CFP credit is available if the firm registers with the CFP board as a sponsor and meets the CFP board requirements. IRS credit is available only if the firm registers with the IRS as a sponsor and satisfies their requirements.

Seminar Quality Evaluations for Firm Sponsor

NASBA requires the seminar to include a means for evaluating quality. At the seminar conclusion, evaluations should be solicited from participants and retained by the sponsor for five years. The following statements are required on the evaluation and are used to determine whether:

1. Stated learning objectives were met.
2. Prerequisite requirements were appropriate (if any).
3. Program materials were accurate.
4. Program materials were relevant and contributed to the achievement of the learning objectives.
5. Time allotted to the learning activity was appropriate.
6. Individual instructors were effective.
7. Facilities and/or technological equipment were appropriate.
8. Handout or advance preparation materials were satisfactory.
9. Audio and video materials were effective.

You may use the enclosed preprinted evaluation forms for your convenience.

Retention of Records

The seminar sponsor is required to retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (the original sign-in sheets, now in an editable, electronic signable format)
- Copy of the program materials
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name(s) and credentials
- Results of program evaluations

Appendix: Forms

Here are the forms noted above and how to get access to them.

Delivery Method	Form Name	Location	Notes
"Group Live" / "Group Internet Based"	Advertising / Promotional Page	Transcript	Complete this form and circulate to your audience before the training event.
"Group Live"	Attendance Sheet	Transcript	Use this form to track attendance during your training session.
"Group Internet Based"	Webinar Delivery Tracking Report	Transcript	Use this form to track the 'polling questions' which are required to monitor attendance during your webinar.
"Group Live" / "Group Internet Based"	Evaluation Form	Transcript	Circulate the evaluation form at the end of your training session so that participants can review and comment on the training.
Self Study	CPE Quizzer Answer Sheet	Transcript	Use this form to record your answers to the quiz.

Getting Help

Should you need support or assistance with your account, please see below:

Support Group	Phone Number	Email Address	Typical Issues/Questions
Technical Support	844.245.5970	Cplsupport@cerifi.com	• Browser-based • Certificate discrepancies • Accessing courses • Migration questions • Feed issues
Product Support	844.245.5970	Cplsupport@cerifi.com	• Functionality (how to use, where to find) • Content questions • Login Assistance
Customer Support	844.245.5970	Cplsupport@cerifi.com	• Billing • Existing orders • Cancellations • Webinars • Certificates