CTEC CONTINUING PROFESSIONAL EDUCATION COURSE SUPPLEMENT

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Introduction

At Golden State Tax Training, Inc. we focus on customer service and satisfaction. It is important to us that you are apprised of important tax legislation changes that may have occurred since you completed your CTEC continuing professional education course. This course supplement is designed to acquaint you with new tax developments that have occurred since our original course publication.

This supplement focuses on key Federal and California tax law provisions recently enacted or indexed for inflation. Among other topics, this supplement includes information about the Tax Cuts and Jobs Act (TCJA), Annual Filing Season Program, Affordable Care Act, common tax credits, and retirement plan limitations.

All 2019 legislative amendments and changes received as of press time are reflected, and references to Federal and California tax laws are up to date as of the publication of this course. The focus is on tax law applicable to the filing of income tax returns in 2020 for the 2019 tax year.

Understanding the Icons Used in this Book

Important: Update or change

Tip

Tip: Significant information

Note: Additional information

Golden State Tax Training Institute, Inc. is an approved education provider for the California Tax Education Council (CTEC) and the Internal Revenue Service (IRS). Our CTEC provider number is 2040 and can be verified at www.CTEC.org. Our IRS provider number is P619F and can be verified on the IRS list of Approved Continuing Education Providers.

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2019 California Legislation Changes CTEC Requirements for CRTPs

California Assembly Bill 3143 was signed into law in September 2018 with new provisions and requirements that will extend the CTEC program until January 1, 2023. The renamed Tax Preparation Act (California Business and Professions Code Section 22250-22259) stipulates revisions that will impact CTEC Registered Tax Preparers (CRTPs).

CRTPs Must Provide CTEC's Website to Clients

Effective January 1, 2019, CRTPs, prior to rendering any tax preparation services, shall provide their customer, in writing, with the following:

1. The tax preparer's name, address, and telephone number;
2. Evidence of compliance with the bonding requirement including the name of your bond company and the bond policy number; and,
3. The address of the CTEC website, www.ctec.org.

Disciplinary Actions Against CRTPs Made Public

Starting July 1, 2019, CTEC will post the following on its website:

- All disciplinary actions taken against registrants by the Council, including - but not limited to - misconduct that resulted in a suspension or revocation of a CRTP registration.
- A list of registrants on probation, including the misconduct that resulted in the probation and any terms of probation.

Reporting Bond Claims

On or after July 1, 2019, a CRTP is required to report all paid claims against their surety bond to CTEC. CTEC is also required to post a notice of the paid surety bond claims on ctec.org.

Background Checks and Fingerprint Images

Effective July 1, 2020, California Business & Professions Code Section 22251.3 is amended to require new applicants interested in becoming CRTPs to pass a criminal background check and submit fingerprint images to CTEC to determine an individual's eligibility to register as a CRTP. The new requirements are NOT applicable to current CRTPs, only new applicants who register on or after July 1, 2020.

Also beginning July 1, 2020, if a CRTP allows their CTEC registration to expire and they would like to re-register with CTEC, they not only will be required to retake the 60-hour qualifying education (QE) course, but they will also be required to go through a background check and resubmit fingerprint images to CTEC.

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2019 Federal Tax Legislation and Continuing Changes

Tax Cuts and Jobs Act

The Tax Cuts and Jobs Act (TCJA) made several significant changes to the individual income tax. These changes include a nearly doubled standard deduction, new limitations on itemized deductions, reduced income tax rates, and reforms to several other provisions. In all, these changes simplify the individual income tax by eliminating the need for millions of households to itemize their deductions.

With respect to individuals, among other items the TCJA:

- Changed the seven existing tax brackets.
- Increased the standard deduction.
- Repealed the deduction for personal exemptions.
- Increased the Child Tax Credit.
- Repealed the overall limitation on certain itemized deductions.
- Limited the mortgage interest deduction.
- Limited the deduction for state and local income or sales taxes.

The Tax Cuts and Jobs Act tax provisions for individuals, including the new tax rates, began January 1, 2018, and will expire at the end of 2025. At that time, unless Congress extends the legislation, the law will go back to the way it was prior to the new legislation. (1)

Further Consolidated Appropriations Act

In December 2019 Congress passed a spending bill called the Further Consolidated Appropriations Act. It includes a wide range of provisions from healthcare tax repeal to tax extenders.

The Act included the repeal of three Affordable Care Act-related taxes: the so-called "Cadillac" tax on health insurance benefits, an excise tax on medical devices, and the Health Insurance Tax. The three taxes were originally part of the Patient Protection and Affordable Care Act, more commonly called Obamacare. The repeals of the excise tax on medical devices and the Cadillac tax begin January 1, 2020, while the repeal of the Health Insurance Tax is effective in 2021.

The Act also extended many expired tax provisions. These provisions, often referred to as extenders, are now renewed on a short-term basis (and some of them retroactively). Here are some of the highlights:

- If the taxpayer has qualified principal residence indebtedness (in other words, the taxpayer defaulted on a mortgage that he or she took out to buy, build, or substantially improve his or her main home), he or she was previously able to exclude that amount from income. The provision expired in 2017 but has been renewed.
- The mortgage insurance premium (sometimes called PMI) deduction had also been allowed to expire. It is now extended through 2020.
- The medical expenses deduction 7.5% floor has returned (it was previously jumped to 10%) for 2019 and 2020.
- The above-the-line qualified tuition and related expenses deduction returned and has been extended through 2020.
- The employer Credit for Paid Family and Medical Leave and the Work Opportunity Tax Credit were expected to expire in 2019 but have been extended through 2020.
- The biodiesel credit has been extended.

What's New

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

Form 1040-SR - U.S. Tax Return for Seniors has larger print, removes shading around boxes, and has lines for specific retirement income streams like Social Security benefits, IRA distributions, and pensions and annuities. Seniors who itemize deductions or own their own businesses will not be able to use the new form. A taxpayer can use this form if they were born before January 2, 1955. This form generally mirrors Form 1040.

Fewer Numbered Schedules

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

IRA and Pension Reporting

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

Capital Gain or Loss Reporting

In 2018, capital gain or (loss) was reported on Schedule 1 (Form 1040), line 13. In 2019, it will be reported on Form 1040 or 1040-SR, line 6.

Health Care Coverage Shared Responsibility Payment

The taxpayer no longer needs to either make a shared responsibility payment or file Form 8965 if he or she does not have minimum essential health care coverage for part or all of 2019. The "Full-year health care coverage or exempt" box has been removed from Form 1040.

Reminders

Overall Limitation on Itemized Deductions

There is no longer an overall limitation on itemized deductions based on the taxpayer's adjusted gross income; however, there may be other limitations that impact the amount of itemized deductions he or she can claim on Schedule A.

Limitation on the Deduction for State and Local Taxes

The taxpayer cannot deduct more than $10,000 ($5,000 if married filing separate) of his or her total state and local taxes, including income taxes (or general sales taxes, if elected instead of income taxes), real estate taxes, and personal property taxes.

No Deduction for Foreign Taxes Paid for Real Estate

The taxpayer can no longer deduct foreign taxes he or she paid on real estate.

Limitation on Deduction for Home Mortgage Interest

The taxpayer may be able to deduct mortgage interest only on the first $750,000 ($375,000 if married filing separately) of indebtedness. Higher limitations apply if the taxpayer is deducting mortgage interest from indebtedness incurred on or before December 15, 2017.

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No Deduction for Home Equity Loan Interest

No matter when the indebtedness was incurred, the taxpayer can no longer deduct the interest from a loan secured by his or her home to the extent the loan proceeds were not used to buy, build, or improve his or her home.

No Miscellaneous Itemized Deductions Allowed

The taxpayer can no longer claim any miscellaneous itemized deductions, including the deduction for unreimbursed job expenses. Miscellaneous itemized deductions are those deductions that would have been subject to the 2% of adjusted gross income limitation.

Limitation on the Deduction for Casualty and Theft Losses

The taxpayer can no longer deduct a personal casualty or theft loss unless the loss is from a Federally declared disaster.

Higher Limitation Threshold for Certain Charitable Contributions

For most gifts by cash or check, the total amount of such contributions that can be deducted is now limited to 60% of the taxpayer's contributions base, instead of 50%.

Deduction for Mortgage Insurance Premiums

The Further Consolidated Appropriations Act extended the deduction for mortgage insurance premiums through 2020. If certain requirements are met, mortgage insurance premiums (PMI) can be deducted as an itemized deduction on the taxpayer's return.

Standard Mileage Rates

The standard mileage rate allowed for operating expenses for a car when the taxpayer uses it for medical reasons increased to 20 cents a mile and 58 cents per mile for business miles driven. The 2019 rate for use of the taxpayer's vehicle to do volunteer work for certain charitable organizations remains at 14 cents a mile.

Protecting Americans from Tax Hikes Act of 2015 (PATH)

A large number of expired tax provisions have been retroactively extended by the Protecting Americans from Tax Hikes Act of 2015 (the PATH Act). Tax provisions made permanent:

- Child Tax Credit.
- American Opportunity Tax Credit.
- Earned Income Tax Credit.
- Above-the-line deduction for certain expenses of elementary and secondary school teachers.
- Deduction for state and local general sales taxes.
- Enhanced mass transit and parking pass benefits.
- Qualified charitable distributions from individual retirement plans.
- Research and Development Credit.
- Section 179 expensing.
- An exclusion of 100% of gain on certain small business stock.
- The S corporation recognition period for built-in gains tax to five years.

Tax Return Due Date

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

Annual Filing Season Program (AFSP)

The IRS is offering a voluntary Annual Filing Season Program (AFSP) to return preparers. The AFSP is intended to

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

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

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

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

Also, as of 2016, there were changes to the representation rights of return preparers. Attorneys, CPAs, and enrolled agents will continue to be the only tax professionals with unlimited representation rights, meaning they can represent their clients on any matters including audits, payment/collection issues, and appeals.

AFSP participants will have limited representation rights, meaning they can represent clients whose returns they prepared and signed, but only before revenue agents, customer service representatives, and similar IRS employees, including the Taxpayer Advocate Service. PTIN holders without an AFSP – Record of Completion or other professional credential will only be permitted to prepare tax returns. They will not be allowed to represent clients before the IRS. Established state-based return preparer program participants with current testing requirements such as return preparers who are active members of the Maryland State Board of Individual Tax Preparers, the Oregon Board of Tax Practitioners and/or the California Tax Education Council are exempt from taking the Annual Federal Tax Refresher (AFTR) course.

For example, the IRS has exempted California Registered Tax Preparers (CRTP) from having to take the Annual Federal Tax Refresher (AFTR) course and passing the course's competency examination to obtain a Record of Completion because they have already demonstrated their competency by passing a 60-hour qualifying education course and annually maintaining their continuing professional education. These exempt groups are still required to meet other program requirements, including 15 CPE credits (10 Federal Tax Law, 3 Federal Tax Law Updates, and 2 Ethics).

Return preparers who can obtain the AFSP – Record of Completion without taking the AFTR course are:

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

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

Preparer Tax Identification Number (PTIN)

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

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

On June 1, 2017, the United States District court for the District of Columbia upheld the Internal Revenue Service's authority to require the use of a Preparer Tax Identification Number (PTIN), but enjoined the IRS from charging a user fee for the issuance and renewal of PTINs. As a result, there is no fee ($0) for PTIN issuance and renewal. The PTIN application process may be completed online. Form W-12 - IRS Paid Preparer Tax Identification Number Application and Renewal, is available for paper applications and renewals, but takes four to six weeks to process. A tax preparer must renew his or her PTIN every year during the renewal season. The renewal season generally runs from mid-October to December 31. The renewal process can be completed online and only takes a few moments. Failure to have and use a valid PTIN may result in penalties. All enrolled agents, regardless of whether they prepare returns, must have a PTIN in order to maintain their status.

Electronic Filing Identification Number (EFIN)

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

The IRS announced that effective October 1, 2012, they will no longer be accepting paper applications to become an IRS e-file provider and that all applications must be submitted online. Until October 1, 2012, the IRS has allowed tax professionals to fill out Form 8633 - Application to Participate in the IRS e-file Program. With all tax preparers now submitting their applications online, the IRS estimates that the online application process takes four to six weeks to complete and urges tax professionals not to delay.

Authorized IRS e-file Providers do not have to reapply each year as long as they continue to e-file returns. However, if a Provider does not e-file returns for two consecutive years, the IRS will notify the Provider of removal from the IRS active Provider list. The IRS may reactivate a Provider if the Provider replies within sixty days and requests reactivation. Otherwise, the Provider will have to complete and submit a new application. Providers must update their application information within 30 days of the date of any changes to the information on their current application. Make all changes using the IRS e-file Application. See Changes to Your IRS e-file Application.

The EFIN is not transferable and neither is the password. Even if an Authorized IRS e-file Provider transfers his or her business by sale, gift or other disposition, he or she may not transfer his or her EFIN. The Provider must protect his or her EFINS, Electronic Transmitter Identification Numbers (ETINs) and passwords from unauthorized use.

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Identity Theft

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

The taxpayer should be alert to possible identity theft if he or she gets an IRS notice or letter stating: (2)

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

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

Safeguarding Taxpayer Data

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

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

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

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

Note

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

Identity Protection Personal Identification Number (IP PIN)

If a taxpayer received an IRS notice providing him or her with an Identity Protection Personal Identification Number (IP PIN), enter it in the IP PIN spaces provided below daytime phone number on the tax return form. The taxpayer must enter the IP PIN exactly as it is shown on the Notice CP01A. If the taxpayer did not receive a notice containing an IP PIN, leave these spaces blank. An IP PIN is a number the IRS gives to taxpayers who have: (3)

- Reported to the IRS they have been victims of identity theft.

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- Given the IRS information that verifies their identity.
- Had an identity theft indicator applied to their account.

The IP PIN helps to prevent the misuse of a taxpayer's Social Security number or Taxpayer Identification Number on income tax returns. New IP PINs are issued every year. An IP PIN should be used only for the tax year it was issued. IP PINs for 2020 tax returns generally will be sent in December 2019. A new IP PIN will be issued every year for three years after the identity theft incident. If the taxpayer is filing a joint return and both taxpayers receive an IP PIN, only the taxpayer whose Social Security number (SSN) appears first on the tax return should enter his or her IP PIN.

Individual Taxpayer Identification Numbers (ITIN)

In January of 2013 the IRS implemented new procedures that affect the Individual Taxpayer Identification Number (ITIN) application process. The information below highlights improvements to the ITIN program: (4)

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

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

Other examples of individuals who need ITINs include: (5)

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

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

All ITINs not used on a Federal tax return at least once in the last three years will no longer be valid for use on a tax return as of December 31, 2019. In addition, ITINs with middle digits of 83, 84, 85, 86 or 87 (Example: 9NN-83-NNNN) need to be renewed if the taxpayer will have a filing requirement in 2020. No action is needed by ITIN holders who do not need to file a tax return next year. Also, there are new documentation requirements when applying for or renewing an ITIN for certain dependents.

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

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Taxpayers with ITINs set to expire at the end of the year and who need to file a tax return in 2020 must submit a renewal application. Others do not need to take any action.

- ITINs with middle digits 83, 84, 85, 86 or 87 (For example: 9NN-83-NNNN) need to be renewed if the taxpayer will have a filing requirement in 2020.
- Those who must renew their ITIN can choose to renew their family's ITINs together, even if family members have an ITIN with middle digits other than 83, 84, 85, 86 or 87. Family members include the tax filer, spouse and any dependents claimed on the tax return.
- Taxpayers whose ITINs expired due to lack of use should only renew their ITIN if they will have a filing requirement in 2020.
- Taxpayers who are eligible for, or who have, a Social Security number (SSN) should not renew their ITIN but should notify IRS both of their SSN and previous ITIN, so that their accounts can be merged.

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

IRS Direct Pay

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

The taxpayer must have a valid Social Security Number (SSN) to use this application. This application cannot accommodate Individual Taxpayer Identification Numbers (ITINs). IRS Direct Pay currently accepts 1040 series payments, including the 4868 (1040 Extension) and the 1040-ES (1040 Estimated Tax). Direct Pay will also accept form 5329 payments and Shared Responsibility payments. Other form types may be added in the future.

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

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

Installment Agreements

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

The current fees are:

1. A top rate of $225, up from the current rate of $120, applies to taxpayers who enter into installment agreements in person, over the phone, by mail, or by filing Form 9465 - Installment Agreement Request, with the IRS. This includes taxpayers requesting installment agreements with their e-filed returns.
2. A reduced rate of $107, up from $52, applies to a direct debit agreement.
3. A taxpayer who sets up an installment agreement through IRS.gov and agrees to make payments either by mailing a check or through the Electronic Federal Tax Payment System (EFTPS) will pay $149.
4. A taxpayer who sets up an installment agreement online and agrees to make automatic payments through direct debit will pay a $31 fee.

5. The fee for a restructured/reinstated installment agreement is $89, up from the current rate of $50.
6. A low-income taxpayer pays a $43 fee, the same as the current rate, when setting up any type of installment agreement, other than a direct debit online payment agreement or when restructuring or reinstating any installment agreement.

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

Paid Preparer's Due Diligence Checklist

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

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

Also, the paid tax return preparer due diligence penalty under IRC Section 6695(h) is now indexed for inflation. Therefore, the penalty for failure to meet the due diligence requirements with respect to returns and claims for refund filed in 2019 is $530 per credit per return.

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

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

Fixing America's Surface Transportation (FAST) Act

The Fixing America's Surface Transportation (FAST) Act was signed into law in December 2015. The purpose of the FAST Act was to provide long-term funding for transportation projects, including new highways. Also included in the bill was a new tax law that requires the Department of State to deny a passport (or renewal of a passport) to a seriously delinquent taxpayer or revoke any passport previously issued to a seriously delinquent taxpayer. For purposes of the law, a "seriously delinquent tax debt" is defined as "an unpaid, legally enforceable Federal tax liability" when a debt greater than $52,000 for 2019, including interest and penalties, has been assessed and a notice of lien or a notice of levy has been filed. The limit is adjusted each year for inflation and cost of living. The limit is not per year but cumulative meaning that it is the total tax debt that matters.

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

If the taxpayer is seriously delinquent under the law, the IRS is required to notify him or her in writing at the time that it certifies the debt to the State Department. The State Department will then hold his or her passport application or renewal for 90 days to allow the taxpayer to resolve any errors, make full payment, or enter into a satisfactory payment plan. There is no grace period for resolving the debt before the State Department revokes an existing passport. To

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get off the list, the taxpayer must prove that the debt is fully satisfied, is legally unenforceable or is not seriously delinquent tax debt under the statute.

2019 Federal Tax Legislation

Tax Rate Schedules for 2019

One of the keys to the Tax Cuts and Jobs Act is a reduction in individual tax rates. While the current number of tax brackets has been retained, each one has been reduced. There are seven tax rates for individual taxpayers. They are: 10%, 12%, 22%, 24%, 32%, 35% and 37%.

The tax rate of 37% applies to joint filers with taxable income over $612,350 (single filers over $510,300). The following are the tax rates schedules for tax year 2019 based on certain filing status. [(6)]

Unmarried Individuals (other than Surviving Spouses and Heads of Households)	
If Taxable Income Is:	**The Tax Is:**
Not over $9,700	10% of the taxable income
Over $9,700 but not over $39,475	$970 plus 12% of the excess over $9,700
Over $39,475 but not over $84,200	$4,543 plus 22% of the excess over $39,475
Over $84,200 but not over $160,725	$14,382.50 plus 24% of the excess over $84,200
Over $160,725 but not over $204,100	$32,748.50 plus 32% of the excess over $160,725
Over $204,100 not over $510,300	$46,628.50 plus 35% of the excess over $204,100
Over $510,300	$153,798.50 plus 37% of the excess over $510,300

Table 1 - Revenue Procedure 2018-57 (2019)

Married Individuals Filing Joint Returns and Surviving Spouses	
If Taxable Income Is:	**The Tax Is:**
Not over $19,400	10% of the taxable income
Over $19,400 but not over $78,950	$1,940 plus 12% of the excess over $19,400
Over $78,950 but not over $168,400	$9,086 plus 22% of the excess over $78,950
Over $168,400 but not over $321,450	$28,765 plus 24% of the excess over $168,400
Over $321,450 but not over $408,200	$65,497 plus 32% of the excess over $321,450
Over $408,200 but not over $612,350	$93,257 plus 35% of the excess over $408,200
Over $612,350	$164,709.50 plus 37% of the excess over $612,350

Table 2 - Revenue Procedure 2018-57 (2019)

Married Individuals Filing Separate Returns	
If Taxable Income Is:	**The Tax Is:**
Not over $9,700	10% of the taxable income
Over $9,700 but not over $39,475	$970 plus 12% of the excess over $9,700
Over $39,475 but not over $84,200	$4,543 plus 22% of the excess over $39,475
Over $84,200 but not over $160,725	$14,382.50 plus 24% of the excess over $84,200
Over $160,725 but not over $204,100	$32,748.50 plus 32% of the excess over $160,725
Over $204,100 not over $306,175	$46,628.50 plus 35% of the excess over $204,100
Over $306,175	$82,354.75 plus 37% of the excess over $306,175

Table 3 - Revenue Procedure 2018-57 (2019)

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Heads of Households	
If Taxable Income Is:	**The Tax Is:**
Not over $13,850	10% of the taxable income
Over $13,850 but not over $52,850	$1,385 plus 12% of the excess over $13,850
Over $52,850 but not over $84,200	$6,065 plus 22% of the excess over $52,850
Over $84,200 but not over $160,700	$12,962 plus 24% of the excess over $84,200
Over $160,700 but not over $204,100	$31,322 plus 32% of the excess over $160,700
Over $204,100 not over $510,300	$45,210 plus 35% of the excess over $204,100
Over $510,300	$152,380 plus 37% of the excess over $510,300

Table 4 - Revenue Procedure 2018-57 (2019)

Estates and Trusts	
If Taxable Income Is:	**The Tax Is:**
Not over $2,600	10% of the taxable income
Over $2,600 but not over $9,300	$260 plus 24% of the excess over $2,600
Over $9,300 but not over $12,750	$1,868 plus 35% of the excess over $9,300
Over $12,750	$3,075.50 plus 37% of the excess over $12,750

Table 5 - Revenue Procedure 2018-57 (2019)

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

Table 6 - Revenue Procedure 2018-57 (2019)

An additional 3.8% Federal Net Investment Income Tax (NIIT) applies to individuals on the lesser of net investment income or modified adjusted gross income (MAGI) in excess of $200,000 (single) or $250,000 (married/filing jointly and qualifying widow(er)s). The tax also applies to any trust or estate on the lesser of undistributed net income or AGI in excess of the dollar amount at which the estate/trust pays income taxes at the highest rate.

Standard Mileage Rates

The following are the 2019 optional standard mileage rates used to calculate the deductible costs of operating an automobile for business, charitable, medical or moving purposes during 2019. As of January 1, 2019, the standard mileage rates for the use of a car, van, pickup or panel truck are: (7)

- 58 cents per mile for business miles driven, up from 54.5 cents for 2018.
- 20 cents per mile driven for medical or moving purposes, up from 18 cents for 2018.
- 14 cents per mile driven in service of charitable organizations (currently fixed by Congress).

The business mileage rate increased 3.5 cents for business travel driven and 2 cents for medical and certain moving expense from the rates for 2018. The charitable rate is set by statute and remains unchanged.

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

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

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

Note

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

Standard Deduction

Under the Tax Cuts and Jobs Act the standard deduction amounts increased to $12,200 for individuals, to $18,350 for heads of household, and to $24,400 for married couples filing jointly and surviving spouses in 2019. (6)

Standard Deductions 2019 Tax Year	
Filing Status	**Standard Deduction Amount**
Single	$12,200
Married Filing Jointly	$24,400
Married Filing Separately	$12,200
Heads of Household	$18,350
Surviving Spouse	$24,400

Table 7 - Revenue Procedure 2018-57 (2019)

For 2019, the additional standard deduction for married taxpayers 65 or over or blind will be $1,300 (same as for 2018). For a single taxpayer or head of household who is 65 or over or blind, the additional standard deduction for 2019 will be $1,650 (up from $1,600 for 2018). For 2019, the standard deduction amount for an individual who may be claimed as a dependent by another taxpayer cannot exceed the greater of $1,100 or the sum of $350 and the individual’s earned income.

Elderly and/or Blind Taxpayers

The standard deduction chart for people age 65 or older (shown below) lists the additional standard deduction for taxpayers who are age 65 or older and/or blind at the end of the tax year. The standard deduction is calculated by adding the person's standard deduction (based on their filing status), plus the additional amount. Additional standard deduction amounts for 2019 are $1,650 for single or head of household or $1,300 for married filing jointly, married filing separately, or qualifying widow.

For example, if the taxpayer is married, filing a joint return and both he and his wife are 68 years of age, what would their standard deduction amount come to for 2019? When completing his or her income tax return, the taxpayer would check off the box for him as being 65 or older, as well as the same box for his spouse. Two boxes are checked, and looking at the married filing joint return section, we see that their available standard deduction would be $27,000. If one was also blind, the standard deduction for 2019 would be $28,300 having three boxes checked.

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

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Standard Deduction Chart for People Age 65 or Older or Blind		
Filing Status	Number from the boxes checked on Page 1 of Form 1040	Standard Deduction for 2019
Single	1 2	$13,850 $15,500
Married filing jointly or qualifying widow(er)	1 2 3 4	$25,700 $27,000 $28,300 $29,600
Married filing separately	1 2 3 4	$13,500 $14,800 $16,100 $17,400
Head of household	1 2	$20,000 $21,650

Table 8 - Publication 501 - Table 7 – Standard Deduction Chart for People who are 65 or Older or Who are Blind, (2019)

For an individual taxpayer, he or she will be required to file a tax return if his or her gross income for the taxable year is more than the standard deduction. For a married taxpayer, he or she will be required to file a tax return if his or her gross income, when combined with his or her spouse's gross income, is more than the standard deduction for a joint return, provided that the taxpayer and his or her spouse lived in the same home; his or her spouse does not file a separate tax return; and neither the taxpayer nor his or her spouse is a dependent of another taxpayer who has income other than earned income in excess of $500 (indexed for inflation).

Personal Exemption

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

Changes to Above-the-line Deductions

The Tax Cuts and Jobs Act (TCJA) changed certain above-the-line deductions. The alimony deduction will be repealed but not until 2019. The change applies to any divorce or separation instrument executed or modified after December 31, 2018 (the modification must expressly state that the new rule applies). Also, the deduction for moving expenses is also repealed, except for members of the military. The domestic production activities deduction (DPAD) is also repealed. The educator expenses deduction, student loan interest deduction, health savings account (HSA) deduction, IRA deduction and deductions for self-employed taxpayers all stay the same.

Changes to Itemized Deductions

The Tax Cuts and Jobs Act changed certain itemized deductions. The medical expenses deduction was retained, with the 7.5% of adjusted gross income (AGI) floor retained for all taxpayers for 2017 and 2018. Under the Further Consolidated Appropriations Act of 2020 the 7.5% floor has returned (it was previously changed to 10%) for 2019 and 2020.

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

The percentage of adjusted gross income (AGI) for charitable contributions is increased from 50% to 60% for cash donations, but no deduction is allowed for donations in exchange for college athletic event seating rights. The cents-per-mile rate for driving for charitable purposes has not been changed; it remains at 14 cents per mile.

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

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

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

Itemized Deduction Phase-Out

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

Alternative Minimum Tax (AMT) Exemption Amount

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

A specified amount of Alternative Minimum Taxable Income (AMTI), is exempt from alternative minimum taxation. The amount varies according to the taxpayer's filing status and the tax year at hand. The exemption is subtracted from the taxpayer's AMTI to determine the amount of his or her AMTI that is subject to tax at the AMT rates. For 2019, the exemption amounts increase to $111,700 for joint filers, $55,850 for married filing separately, and $71,700 for individual filers. The alternative minimum tax (AMT) exemption amounts are permanently adjusted for inflation.

Additionally, the taxpayer's exemption phases out if his or her AMTI exceeds the thresholds indicated below. More specifically, the exemption is reduced by 25% of the amount by which his or her AMTI exceeds the applicable threshold for his or her filing status. For 2019, the phase-out threshold for the exemption increases to $1,020,600 for joint filers and $510,300 for individual filers.

Filing Status	AMT Exemption Amount
Joint Returns or Surviving Spouses	$111,700
Singles	$71,700
Married Individuals Filing Separate Returns	$55,850

Table 9 - Instructions for Form 6251 (2019)

The AMT exemption for 2019 for a child subject to the kiddie tax will be the lesser of (1) $7,750 (up from $7,600 for 2018) plus the child's earned income, or (2) $71,700 (up from $70,300 for 2018).

If the taxpayer is not liable for AMT this year, but he or she paid AMT in one or more previous years, he or she may be eligible to take a special minimum tax credit against his or her regular tax this year. If eligible, the taxpayer should complete and attach Form 8801 - Credit for Prior Year Minimum Tax - Individuals, Estates, and Trusts, to claim the minimum tax credit. (8)

Flexible Spending Accounts (FSA)

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

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

The annual dollar limit on contributions to employer-sponsored health care FSAs rises to $2,700 in 2019. Both employer and employee may contribute to an employee's health FSA, but contributions from all sources combined must not exceed the $2,700 annual limit for 2019. The statutory $2,700 limit under IRC Section 125(i) applies only to salary reduction contributions under a health FSA, and does not apply to certain employer non-elective contributions (sometimes called flex credits), to any types of contributions or amounts available for reimbursement under other types of FSAs, health savings accounts, or health reimbursement arrangements, or to salary reduction contributions to cafeteria plans that are used to pay an employee's share of health coverage premiums (or the corresponding employee share under a self-insured employer-sponsored health plan).

The U.S. Treasury Department and the IRS altered the long-standing "use it or lose it" rule, allowing employers to offer a carryover of up to $500 in unused health FSA funds to the following year or to continue a grace period option giving employees a two-and-a-half-month extension to spend remaining FSA funds. FSAs cannot have both a carryover and a grace period option, and employers are not obligated to offer either extension.

Health Savings Account (HSA)

2019 offers individuals and families additional opportunities to save for current and future health care with a Health Savings Account (HSA):

- HSA holders can choose to save up to $3,500 for an individual and $7,000 for a family (HSA holders 55 and older get to save an extra $1,000 which means $4,500 for an individual and $8,000 for a family) - and these contributions are 100% tax deductible from gross income.
- Minimum annual deductibles are $1,350 for self-only coverage or $2,700 for family coverage.
- Annual out-of-pocket expenses (deductibles, copayments, and other amounts, but not premiums) cannot exceed $6,750 for self-only coverage and $13,500 for family coverage.

2019 HSA Contribution Limits, Deductibles, and Out-of-Pocket Expenses				
	Minimum Deductible	**Maximum Out-of-Pocket**	**Contribution Limit**	**55+ Contribution Limit**
Single	$1,350	$6,750	$3,500	$4,500
Family	$2,700	$13,500	$7,000	$8,000

Table 10 - HSA Contribution Limits, Deductibles, and Out-of-Pocket Expenses (2019)

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

Note

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

HSAs can pair with high deductible plans (HDHP). As long as the taxpayer holds an HSA eligible high deductible health plan (HDHP) he or she can contribute tax-advantaged dollars to the account up to the annual limit. In 2019 the out-of-pocket limits for HDHP minimum annual deductibles are $1,350 for self-only coverage or $2,700 for family coverage and annual out-of-pocket expenses (deductibles, copayments, and other amounts, but not premiums) cannot exceed $6,750 for self-only coverage and $13,500 for family coverage.

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

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Important Differences Between HSAs and FSAs		
	Health savings account (HSA)	**Flexible spending account (FSA)**
Eligibility requirements	Eligibility requirements include having a high-deductible health plan (HDHP).	No eligibility requirements.
Contribution limit	2019 contributions capped at $3,500 for individuals or $7,000 for families.	2019 contributions capped at $2,700.
Changing contribution amount	The taxpayer can change how much he or she contributes to the account at any point during the year.	Contribution amounts can be adjusted only at open enrollment or with a change in employment or family status.
Rollover	Unused balances roll over into the next year.	FSAs can allow an individual to carry over up to $500 per year to use in the following year.
Connection to employer	The taxpayer's HSA can follow him or her as he or she changes employment.	In most cases, the taxpayer will lose his or her FSA with a job change. One exception: if the taxpayer is eligible for FSA continuation through COBRA.
Effect on taxes	Contributions are tax-deductible but can also be taken out of the taxpayer's salary pretax. Growth and distributions are tax-free.	Contributions are pretax, and distributions are untaxed.

Table 11 - Using a Flexible Spending Account (FSA) - HealthCare.gov (2019)

Pension Plan Limitations

The Internal Revenue Service has set the cost‑of‑living adjustments affecting dollar limitations for pension plans and other retirement-related items for tax year 2019. Some of the pension plan limitations will change for 2019 because the increase in the cost-of-living index met the statutory thresholds that trigger their adjustment. However, other limitations will remain unchanged because the increase in the index did not meet the statutory thresholds that trigger their adjustment. (9)

Elective Deferral (Contribution) Limits

The elective deferral limit for employees who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan is increased to $19,000 in 2019. The catch-up contribution limit for employees aged 50 and over who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan remains the same at $6,000 in 2019. If the taxpayer is self-employed, the total employer plus employee contributions to all defined contribution plans under Section 415(c)(1)(A) is increased in 2019 from $55,000 to $56,000. (9)

Individual Retirement Arrangements (IRA)

For 2019, the taxpayer's total contributions to all of his or her traditional and Roth IRAs cannot be more than: (10)

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

If the taxpayer was age 50 or older before 2020, the maximum amount that can be contributed to his or her traditional IRA for 2019 will be the smaller of the following amounts:

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

The income ranges for determining eligibility to make deductible contributions to traditional Individual Retirement Arrangements (IRAs), to contribute to Roth IRAs, and to claim the Saver's Credit all increased for 2019. For 2019, if

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the taxpayer is covered by a retirement plan at work, his or her deduction for contributions to a traditional IRA is reduced (phased out) if modified AGI is: (10)

- More than $103,000 but less than $123,000 for a married couple filing a joint return or a qualifying widow(er),
- More than $64,000 but less than $74,000 for a single individual or head of household, or
- Less than $10,000 for a married individual filing a separate return.

If the taxpayer either lives with his or her spouse or files a joint return, and his or her spouse is covered by a retirement plan at work, but the taxpayer is not, the taxpayer's deduction is phased out if his or her modified AGI is more than $193,000 but less than $203,000. If the taxpayer's modified AGI is $203,000 or more, he or she cannot take a deduction for contributions to a traditional IRA.

The IRA contribution limit does not apply to:

- Rollover contributions.
- Qualified reservist repayments.

If the taxpayer files a joint return, he or she may be able to contribute to an IRA even if he or she did not have taxable compensation as long as his or her spouse did. The amount of taxpayer's combined contributions cannot be more than the taxable compensation reported on his or her joint return. Also, a taxpayer cannot make regular contributions to a traditional IRA in the year he or she reaches 70½ and older. However, the taxpayer can still contribute to a Roth IRA and make rollover contributions to a Roth or traditional IRA regardless of his or her age.

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

Rollovers

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

1. **Direct rollover** - If the taxpayer is getting a distribution from a retirement plan, he or she can ask the plan administrator to make the payment directly to another retirement plan or to an IRA. The taxpayer should contact the plan administrator for instructions. The administrator may issue the taxpayer's distribution in the form of a check made payable to his or her new account. No taxes will be withheld from the transfer amount.
2. **Trustee-to-trustee transfer** - If the taxpayer is getting a distribution from an IRA, he or she can ask the financial institution holding the IRA to make the payment directly from his or her IRA to another IRA or to a retirement plan. No taxes will be withheld from the transfer amount.
3. **60-day rollover** - If a distribution from an IRA or a retirement plan is paid directly to the taxpayer, he or she can deposit all or a portion of it in an IRA or a retirement plan within 60 days. Taxes will be withheld from a distribution from a retirement plan, so the taxpayer will have to use other funds to roll over the full amount of the distribution.

The taxpayer generally cannot make more than one rollover from the same IRA within a 1-year period. He or she also cannot make a rollover during this 1-year period from the IRA to which the distribution was rolled over. If the taxpayer has not elected a direct rollover, in the case of a distribution from a retirement plan, or he or she has not elected out of withholding in the case of a distribution from an IRA, his or her plan administrator or IRA trustee will withhold taxes from the taxpayer's distribution. If the taxpayer later rolls the distribution over within 60 days, he or she must use other funds to make up for the amount withheld. (11)

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

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In Revenue Procedure 2016-47, effective August 2016, the IRS has created a new "self-certification" procedure that allows someone who misses the 60-day deadline for rollovers to avoid the expense and delay of obtaining a private letter ruling. Instead, a taxpayer submits a model IRS letter to the new retirement account custodian, checking in that letter one of 11 acceptable excuses for missing the deadline. A self-certification is not a waiver by the IRS of the 60-day rollover requirement. However, a taxpayer may report the contribution as a valid rollover unless later informed otherwise by the IRS. The IRS, in the course of an examination, may consider whether a taxpayer's contribution meets the requirements for a waiver.

The taxpayer must have missed the 60-day deadline because of his or her inability to complete a rollover due to one or more of the following reasons:

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

While the reasons are comprehensive, they only apply if the taxpayer was initially eligible to complete a 60-day rollover. As a result of a 2014 U.S. Tax Court decision, taxpayers may only perform one 60-day IRA rollover every 12 months, no matter how many IRAs they have.

The contribution must be made to the plan or IRA as soon as practicable after the reason or reasons listed above no longer prevent the taxpayer from making the contribution. This requirement is deemed to be satisfied if the contribution is made within 30 days after the reason or reasons no longer prevent the taxpayer from making the contribution.

Note

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

IRA One-Rollover-Per-Year Rule

Since January 1, 2015, a taxpayer can make only one rollover from a traditional IRA to another (or the same) traditional IRA in any 12-month period, regardless of the number of IRAs he or she owns. A similar limitation will apply to rollovers between Roth IRAs. The taxpayer can, however, continue to make as many trustee-to-trustee transfers between IRAs as he or she wants. Amounts transferred between traditional IRAs, either by rollover or trustee-to-trustee transfer, are excluded from the taxpayer's gross income. The one-per year limit does not apply to: (11)

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

The tax consequences of the new rule are: (11)

1. The taxpayer must include in gross income any previously untaxed amounts distributed from an IRA if he or she made an IRA-to-IRA rollover (other than a rollover from a traditional IRA to a Roth IRA) in the preceding 12 months.

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2. The taxpayer may be subject to the 10% early withdrawal tax on the amount he or she includes in gross income.

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

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

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

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

Qualified Reservist Repayments

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

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

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

Roth IRA

The Tax Cuts and Jobs Act eliminated the ability to reverse the conversion of a Roth IRA by recharacterizing it as an IRA by October 15th of the year after the misguided conversion. Under the TCJA all Roth IRA conversions are permanent.

If contributions on the taxpayer's behalf are made only to Roth IRAs, his or her contribution limit for 2019 will generally be the lesser of either: [10]

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

If the taxpayer was age 50 or older before 2020 and contributions on his or her behalf were completed only to Roth IRAs, the taxpayer's contribution limit for 2019 will generally be the lesser of either of the following: [10]

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

For 2019, the taxpayer's Roth IRA contribution limit is reduced (phased out) in the following situations: [10]

- His or her filing status is married filing jointly or qualifying widow(er) and his or her modified AGI is at least $193,000. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $203,000 or more.

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- His or her filing status is single, head of household, or married filing separately and he or she did not live with his or her spouse at any time in 2019 and his or her modified AGI is at least $122,000. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $137,000 or more.
- His or her filing status is married filing separately, he or she lived with his or her spouse at any time during the year, and his or her modified AGI is more than $0. The taxpayer cannot make a Roth IRA contribution if his or her modified AGI is $10,000 or more.

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

Contribution Limits

The Internal Revenue Service announced cost-of-living adjustments affecting dollar limitations for pension plans and other retirement-related items for tax year 2019. Most pension limitations such as those governing 401(k) plans and IRAs changed because the increase in the Consumer Price Index met the statutory thresholds for their adjustment.

Contribution Limits	2018	2019
IRA contributions under age 50	$5,500	$6,000
IRA contributions age 50 and over	$6,500	$7,000
SIMPLE Contributions	$12,500	$13,000
SEP, Keogh Maximum Dollar Allocations	$55,000	$56,000
401(k), 403(b), Profit-Sharing Plans Elective deferrals	$18,500	$19,000
Elective catch-ups		
SIMPLE IRAs	$3,000	$3,000
401(k), 403(b), 457 plans	$6,000	$6,000

Table 12 - Pension Plan Limitations (2019)

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

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

20% mandatory withholding does not apply to an in-plan Roth direct rollover. However, if the taxpayer receives his or her distribution in cash, 20% withholding will apply even if the amount is rolled over to a designated Roth account within 60 days. [12]

Inherited IRAs Not Excludable In Bankruptcy

In Clark v. Rameker. the U.S. Supreme Court unanimously ruled that inherited IRAs do not qualify under the "retirement funds" bankruptcy exemption. As a result, non-spouses inheriting an IRA may no longer protect the funds from creditors after filing bankruptcy and spouses have more incentive to roll over inherited IRA funds.

The new decision does not leave those wishing to transfer IRAs on their death without options. Spouses inheriting IRAs retain the option to roll over the inherited IRA into their own or a new IRA. If a current IRA owner wishes to leave his or her IRA to a beneficiary upon the owner's death, the best course of action is to leave the IRA to a trust for the benefit of the individual instead of directly to an individual.

Section 529 Plans

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

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

Previously, 529 plans could be used only to cover costs for college. The TCJA expands the qualified use of 529 accounts by allowing withdrawals for public, private or religious schools. Home schooling families are also allowed to use 529 funds towards educational expenses. If the taxpayer plans to take advantage of this expanded ruling, note the limit of $10,000 per year, per child.

The Tax Cuts and Jobs Act (TCJA) also supports funding of ABLE accounts designed for use by people with disabilities. Under the TCJA, the taxpayer can roll over 529 plan assets to an ABLE account. Both accounts must have the same beneficiary or a member of the same family, and the taxpayer can roll over up to the annual gift exclusion amount, which is $15,000 in 2019. Now families will have more flexibility in planning for special needs, where predicting the level of future needs can be a challenge.

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

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

Affordable Care Act Tax Provisions for Individuals

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

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

Premium Tax Credit (PTC)

The Premium Tax Credit helps pay premiums for health insurance purchased from the Marketplace. Eligible individuals may have advance payments of the Premium Tax Credit made on their behalf directly to the insurance company. If the taxpayer or a family member enrolled in health insurance through the Marketplace and advance payments of the Premium Tax Credit were made to his or her insurance company to reduce his or her monthly premium payment, the taxpayer must attach Form 8962 - Premium Tax Credit (PTC) to his or her return to reconcile (compare) the advance payments with his or her Premium Tax Credit for the year.

The Marketplace is required to send Form 1095-A by January 31, 2020, listing the advance payments and other information the taxpayer needs to complete Form 8962.

1. He or she will need Form 1095-A from the Marketplace.
2. He or she completes Form 8962 to claim the credit and to reconcile his or her advance credit payments.
3. He or she includes Form 8962 with his or her Form 1040, Form 1040-SR, or Form 1040-NR. (The taxpayer does not include Form 1095-A.)

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In general, the taxpayer may be eligible for the credit if he or she meets all of the following: (13)

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

In general, individuals and families whose household income for the year is between 100% and 400% of the Federal poverty line for their family size may be eligible for the Premium Tax Credit. An individual who meets these income requirements must also meet the other eligibility criteria. The taxpayer should use the 2018 Federal Poverty Guidelines (FPL) to determine 2019 Premium Tax Credit eligibility.

For residents of one of the 48 contiguous states or Washington, D.C., the following illustrates some examples of when household income would be between 100% and 400% of the Federal poverty line: (13)

- $12,140 (100%) up to $48,560 (400%) for one individual.
- $16,460 (100%) up to $65,840 (400%) for a family of two.
- $20,780 (100%) up to $83,120 (400%) for a family of three.
- $25,100 (100%) up to $100,400 (400%) for a family of four.

If the taxpayer is eligible for the credit, he or she can choose to either: (13)

- **Claim It Now -** have all or some of the credit paid in advance directly to his or her insurance company to lower what he or she pays out-of-pocket for his or her monthly premiums during 2019.
- **Claim It Later -** wait to get all of the credit when he or she files his or her 2019 tax return in 2020.

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

To claim the credit, the taxpayer must get insurance through the Marketplace. During enrollment through the Marketplace, using information the taxpayer provides about his or her projected income and family composition for 2019, the Marketplace will estimate the amount of the Premium Tax Credit he or she will be able to claim for the 2019 tax year that he or she will file in 2020. The taxpayer will then decide whether he or she wants to have all, some or none of the estimated credit paid in advance directly to his or her insurance company.

The taxpayer should report income and family size changes to the Marketplace throughout the year. Reporting changes, increases or decreases, will help the taxpayer get the proper type and amount of financial assistance and will help him or her avoid getting too much or too little in advance. For example, if the taxpayer does not report income or family size changes to the Marketplace when they happen in 2019, the advance payments may not match his or her actual qualified credit amount on his or her Federal tax return that he or she will file in 2020. This might result in a smaller refund or balance due.

If the taxpayer chooses to claim the Premium Tax Credit now, when he or she files his or her 2019 tax return in 2020, he or she will subtract the total advance payments he or she received during the year from the amount of the Premium Tax Credit calculated on his or her tax return. If the Premium Tax Credit computed on the return is more than the advance credit paid on the taxpayer's behalf during the year, the difference will increase his or her refund or lower the amount of tax he or she owes. If the advance credit payments are more than the Premium Tax Credit, the difference will increase the amount the taxpayer owes and result in either a smaller refund or a balance due.

If the taxpayer chooses to claim the Premium Tax Credit later, he or she will claim the full amount of the Premium Tax Credit when he or she files his or her 2019 tax return in 2020. This will either increase his or her refund or lower his or her balance due. If the taxpayer's state runs its own Marketplace, he or she will use the state's website, not the Marketplace. The taxpayer should use Form 8962 - Premium Tax Credit (PTC) to figure the amount of his or her Premium Tax Credit and to reconcile any advance payments of the Premium Tax Credit. (13)

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Advance Payments of the Premium Tax Credit

If the taxpayer or a family member enrolled in health insurance through the Marketplace and advance payments of the Premium Tax Credit were made to his or her insurance company to reduce his or her monthly premium payment, the taxpayer should attach Form 8962 to his or her return to reconcile (compare) the advance payments with his or her Premium Tax Credit for the year, which the taxpayer figures on Form 8962. The Marketplace is required to send Form 1095-A by January 31, 2020, listing the advance payments and other information the taxpayer needs to figure his or her Premium Tax Credit. The taxpayer should use Form 1095-A to complete Form 8962. Also, the taxpayer should attach Form 8962 to his or her return. The taxpayer does not attach Form 1095-A to the income tax return.

Health Coverage Tax Credit (HCTC)

The Trade Preferences Extension Act of 2015 extended and modified the expired Health Coverage Tax Credit (HCTC). Previously, those eligible for the HCTC could claim the credit against the premiums they paid for certain health insurance coverage through 2013. The HCTC can now be claimed for coverage through 2019. The taxpayer should use Form 8885 - Health Coverage Tax Credit to elect and figure the amount, if any, of his or her HCTC. The Health Coverage Tax Credit (HCTC) is a tax credit that pays 72.5% of qualified health insurance premiums for eligible individuals and their families. A taxpayer may only elect to take the HCTC if he or she is one of the following:

- An eligible trade adjustment assistance (TAA) recipient, alternative (ATAA) recipient, reemployment (RTAA) recipient.
- An eligible Pension Benefit Guaranty Corporation (PBGC) pension payee.
- The family member of a TAA, ATAA, or RTAA recipient or PBGC pension payee who is deceased or who finalized a divorce with him or her.

The taxpayer is not eligible if he or she could have been claimed as a dependent on another person's Federal income tax return.

All plans that were previously qualified for the HCTC qualify for the HCTC through 2019. This includes individual - private and non-group - health insurance that the taxpayer purchases for him or herself or his or her family from an insurance company, agent, or broker.

There are several types of health insurance that qualify for the HCTC. However, contributions by the taxpayer's employer or his or her spouse's employer may limit qualification.

Types of health insurance qualify for the HCTC include:

1. Coverage under a COBRA continuation provision.
2. Coverage under a group health plan available through the employment of the taxpayer's spouse.
3. Coverage under an employee benefit plan funded by a voluntary employees' beneficiary association (VEBA) that was established through the bankruptcy of the taxpayer's former employer.
4. Coverage obtained in the non-group (individual) health insurance market other than coverage offered through the Health Insurance Marketplace.
5. Coverage under certain state-qualified health plans established prior to January 1, 2014.

A qualified health insurance plan does not include a flexible spending or similar arrangement and any insurance if substantially all of its coverage is of excepted benefits described in Section 9832(c) of the Internal Revenue Code. For example, dental or vision benefits purchased separately are not part of a qualified health insurance plan for the HCTC. But premiums paid for a comprehensive package that includes dental or vision benefits may be eligible for the HCTC if the dental or vision benefits do not represent substantially all of its coverage. For 2014 and 2015 only, qualified coverage included qualified health plans offered through a Federally facilitated or a state-based Health Insurance Marketplace. For 2016 and beyond, Health Insurance Marketplace coverage is no longer qualified coverage for the HCTC.

The taxpayer cannot claim the HCTC for any month that, on the first day of the month, he or she was covered under an employer-sponsored health insurance plan (including any employer-sponsored health insurance plan of a spouse) and the employer paid 50% or more of the cost of coverage. Also, if the taxpayer is an Alternative Trade Adjustment Assistance (ATAA) or Reemployment Trade Adjustment Assistance (RTAA) recipient, he or she cannot claim the HCTC for any month that, on the first day of the month, he or she was eligible for certain kinds of coverage (including

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any employer-sponsored health insurance plan of the taxpayers spouse) where the employer would have paid 50% or more of the cost of the coverage or he or she was covered under certain kinds of coverage (including any employer-sponsored health insurance plan of the taxpayer's spouse) where the employer paid any part of the cost of coverage.

Tip

Advance payments of the HCTC began July 2016. The taxpayer could choose Marketplace coverage for the first part of 2016 to receive advance payments of the Premium Tax Credit (PTC) even though Marketplace coverage was not eligible for the HCTC in 2016. The taxpayer may then switch coverage into an HCTC-eligible plan after advance payments of the HCTC begin. The election required to claim the HCTC can be made for any coverage month and does not prevent the taxpayer from claiming the PTC in earlier months in the year. Once the taxpayer makes the election to take the HCTC for an eligible coverage month, he or she cannot take the Premium Tax Credit (PTC) for the same coverage in that coverage month and for all subsequent eligible coverage months during his or her tax year in which he or she is eligible to take the HCTC.

Net Investment Income Tax

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

Tip

The amount subject to the 3.8% tax is the lesser of the taxpayer's net investment income or the amount by which modified adjusted gross (MAGI) exceeds the applicable threshold. Individuals will owe the tax if they have Net Investment Income and also have modified adjusted gross income over the following thresholds: (14)

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

*Taxpayers should be aware that these threshold amounts are not indexed for inflation. These amounts will stay the same from year to year, unless Congress specifically changes these amounts through new legislation.

Table 13 - IRS.GOV Net Investment Income Tax FAQs (2019)

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

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

Estates and Trusts will be subject to the Net Investment Income Tax if they have undistributed Net Investment Income and also have adjusted gross income over the dollar amount at which the highest tax bracket for an estate or trust begins for such taxable year. Generally, the threshold amount for the upcoming year is updated by the IRS each fall in a revenue procedure. For tax year 2019, the threshold amount is $12,950. The taxpayer should be aware that there are special computational rules for certain unique types of trusts, such as Charitable Remainder Trusts and Electing Small Business Trusts. The following trusts are not subject to the Net Investment Income Tax:

1. Trusts that are exempt from income taxes imposed by Subtitle A of the Internal Revenue Code (e.g., charitable trusts and qualified retirement plan trusts exempt from tax under IRC Section 501, and Charitable Remainder Trusts exempt from tax under IRC Section 664).

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2. A trust in which all of the unexpired interests are devoted to one or more of the purposes described in IRC Section 170(c)(2)(B).
3. Trusts that are classified as grantor trusts under IRC Sections 671-679.
4. Trusts that are not classified as trusts for Federal income tax purposes (e.g., Real Estate Investment Trusts and Common Trust Funds).

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

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

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

The Net Investment Income Tax will not be applicable to any amount of gain that is excluded from gross income for regular income tax purposes. The pre-existing statutory exclusion in IRC Section 121 exempts the first $250,000 ($500,000 in the case of a married couple) of gain recognized on the sale of a principal residence from gross income for regular income tax purposes and, therefore, from the NIIT. Wages, unemployment compensation; operating income from a non-passive business, Social Security Benefits, alimony, tax-exempt interest, self-employment income, Alaska Permanent Fund Dividends and distributions from certain Qualified Plans are some common types of income that are not investment income.

In order to arrive at Net Investment Income, Gross Investment Income is reduced by deductions that are properly allocable to items of Gross Investment Income. Examples of properly allocable deductions include investment interest expense, investment advisory and brokerage fees, expenses related to rental and royalty income, and state and local income taxes properly allocable to items included in Net Investment Income. Taxpayers will determine any applicable NIIT on Form 8960 - Net Investment Income Tax - Individuals, Estates and Trusts, when they file their income tax return. Taxpayers whose AGI may exceed the threshold amounts and who have investment income may need to adjust their withholding or make estimated tax payments to ensure the new tax on investment income does not prompt a balance due when filing taxes next year.

Additional Medicare Tax

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

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

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

Table 14 - Questions and Answers for the Additional Medicare Tax (2019)

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

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

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

Changes to Itemized Deduction for Medical Expenses

Under the Tax Cuts and Jobs Act (TCJA), the medical expense deduction remained in place with a lower floor of 7.5% for tax years 2017 (retroactively) and 2018 for all taxpayers regardless of age. Under the Further Consolidated Appropriations Act of 2020 the 7.5% floor has returned (it was previously changed to 10%) for 2019 and 2020.

Medical Device Excise Tax

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

Cadillac Tax

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

2019 Tax Credits and Deductions Updates

Child Tax Credit (CTC)

Under the Tax Cuts and Jobs Act (TCJA), the amount of the Child Tax Credit (CTC) is increased to $2,000 per qualifying child; The income levels at which the credit phases out were increased to $400,000 for married taxpayers filing jointly ($200,000 for all other taxpayers) (not indexed for inflation). A $500 nonrefundable Credit for Other Dependents (ODC) is provided for certain non-child dependents.

The portion of the Child Tax Credit that is refundable after 2017 and before 2026 is still referred to as the Additional Child Tax Credit (ACTC) but is limited to $1,400 per qualifying child, and this amount is indexed for inflation, up to the $2,000 base credit amount. The earned income threshold for the refundable portion of the credit was decreased from $3,000 to $2,500.

The taxpayer's child must have a Social Security Number issued by the Social Security Administration (SSA) before the due date of the taxpayer's tax return (including extensions) to be claimed as a qualifying child for the Child Tax Credit or Additional Child Tax Credit. Children with an Individual Taxpayer Identification Number (ITIN) cannot be claimed for either credit.

If the taxpayer's child's immigration status has changed so that his or her child is now a U.S. citizen or permanent resident but the child's Social Security card still has the words "Not valid for employment" on it, the taxpayer should ask the SSA for a new Social Security card without those words.

If the taxpayer's child does not have a valid SSN, his or her child may still qualify him or her for the Credit for Other Dependents. This is a non-refundable credit of up to $500 per qualifying person. If the taxpayer's dependent child lived with him or her in the United States and has an Individual Taxpayer Identification Number (ITIN), but not an SSN, issued by the due date of his or her 2019 tax return (including extensions), he or she may be able to claim the new Credit for Other Dependents for that child. Spouses and dependents residing outside the United States who use ITINs,

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a tax processing number issued by the IRS, should review the information on IRS.gov/ITIN to determine whether they need to renew an ITIN before filing a tax return next year.

Here are some important facts from the IRS about the Child Tax Credit and how it may benefit a taxpayer's family. (15)

1. *Amount* - With the Child Tax Credit, a taxpayer may be able to reduce his or her Federal income tax by up to $2,000 for each qualifying child under the age of 17.
2. *Qualification* - A qualifying child for this credit is someone who meets the qualifying criteria of six tests: age, relationship, support, dependent, citizenship, and residence.
3. *Age Test* - To qualify, a child must have been under age 17 – age 16 or younger – at the end of 2019.
4. *Relationship Test* - To claim a child for purposes of the Child Tax Credit, they must either be the taxpayer's son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister or a descendant of any of these individuals, which includes a grandchild, niece or nephew. An adopted child is always treated as a taxpayer's own child. An adopted child includes a child lawfully placed with him or her for legal adoption.
5. *Support Test* - In order to claim a child for this credit, the child must not have provided more than half of their own support.
6. *Dependent Test* - The taxpayer must claim the child as a dependent on his or her Federal income tax return.
7. *Citizenship Test* - To meet the citizenship test, the child must be a U.S. citizen, U.S. national, or U.S. resident alien and the taxpayer must provide a valid Social Security number (SSN) for the child by the tax return due date.
8. *Residence Test* - The child must have lived with the taxpayer for more than half of 2019. There are some exceptions to the residence test, which can be found in IRS Publication 972 - Child Tax Credit.

The Child Tax Credit is limited if the taxpayer's modified adjusted gross income (MAGI) is above a certain amount. The amount at which this phase-out begins varies depending on the filing status. Phase-out means that the credit is reduced as the taxpayer's income increases. In this case, the reduction is $50 for each $1,000 by which the taxpayer's MAGI exceeds the threshold amount.

For married taxpayers filing a joint return, the phase-out begins at $400,000. For all other taxpayers, including married taxpayers filing a separate return, the phase-out begins at $200,000. The credit is completely phased out for married taxpayers when MAGI reaches $440,000 and $240,000 for all other taxpayers.

2019 Child Tax Credit Phase-out Amounts			
	Full Credit	Partial Credit	No Credit
Single	0 - $200,000	$200,001 - $240,000	$240,001 +
Married Filing Jointly	0 - $400,000	$400,001 - $440,000	$440,001 +
Head of Household	0 - $200,000	$200,001 - $240,000	$240,001 +
Married Filing Separately	0 - $200,000	$200,001 - $240,000	$240,001 +

Table 15 - Tax Cuts and Jobs Act (2019)

Credit for Other Dependents (ODC)

The Tax Cuts and Jobs Act provided a $500 Credit for Other Dependents (e.g. elderly or disabled dependents or children over 17). This credit is to provide some relief to those families who will lose the now defunct personal exemption and are not eligible for the expanded Child Tax Credit (CTC). Both the CTC and ODC can be claimed for eligible dependents for 2019. Like the CTC, this $500 "non-child" credit is subject to income eligibility thresholds and will phase out for taxpayers with adjusted gross incomes (AGI) above $200,000 (single) and $400,000 (married).

Additional Child Tax Credit

Under the Tax Cuts and Jobs Act, the portion of the Child Tax Credit that is refundable after 2017 and before 2026 is still referred to as the Additional Child Tax Credit (ACTC) but is limited to $1,400 per qualifying child, and this amount is indexed for inflation, up to the $2,000 base credit amount. The earned income threshold for the refundable portion of the credit was decreased from $3,000 to $2,500.

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The Additional Child Tax Credit is a refundable tax credit for people who have a qualifying child and did not receive the full amount of the Child Tax Credit. The Additional Child Tax Credit is equal to the lesser of: [16]

- The unclaimed portion of the nonrefundable Child Tax Credit amount.
- 15% of the person's earned income over $2,500.
- For taxpayers with three or more qualifying children, the excess of the taxpayer's Social Security taxes for the tax year over his or her Earned Income Tax Credit for the year.

Any refund the taxpayer receives as a result of taking the Additional Child Tax Credit cannot be counted as income when determining if the taxpayer or anyone else is eligible for benefits or assistance, or how much the taxpayer or anyone else can receive, under any Federal program or under any state or local program financed in whole or in part with Federal funds. These programs include Temporary Assistance for Needy Families (TANF), Medicaid, Supplemental Security Income (SSI), and Supplemental Nutrition Assistance Program (food stamps). In addition, when determining eligibility, the refund cannot be counted as a resource for at least 12 months after the taxpayer receives it. An individual should check with his or her local benefits coordinator to find out if his or her refund will affect his or her benefits. For more information on the Additional Child Tax Credit, see Schedule 8812 - Child Tax Credit.

Child and Dependent Care Credit

The American Taxpayer Relief Act made the Child and Dependent Care Credit permanent. The Dependent Care credit is also an important tax credit that may be worth up to $1,050 or 35% of $3,000 of eligible expenses in 2019. For two or more qualifying dependents, the taxpayer can claim up to 35% of $6,000 (or $2,100) of eligible expenses. For higher income earners, the credit percentage is reduced, but not below 20%, regardless of the amount of adjusted gross income. A taxpayer's child and dependent care expenses must be for the care of one or more qualifying persons.

A qualifying person is: [17]

- A taxpayer's qualifying child who is his or her dependent and who was under age 13 when the care was provided.
- A spouse who was not physically or mentally able to care for him or herself and lived with the taxpayer for more than half the year.
- A person who was not physically or mentally able to care for him or herself, lived with the taxpayer for more than half the year, and either:
  - Was his or her dependent.
  - Would have been his or her dependent except that:
    - He or she received gross income above annual threshold level.
    - He or she filed a joint return.
    - He or she, or his or her spouse if filing jointly, could be claimed as a dependent on someone else's 2019 return.

Earned Income Tax Credit (EITC)

The Protecting Americans from Tax Hikes Act of 2015 made the Earned Income Tax Credit (EITC) permanent. The bill contained provisions that include an increased amount for families with three or more children and an increased phase-out range for married taxpayers filing jointly. The phase-out range is indexed for inflation for years after 2015.

For tax year 2019, the maximum Earned Income Tax Credit (EITC) for low and moderate-income workers and working families rises to $6,557, up from $6,431 in 2018. The EITC is a refundable tax credit for certain people who work and have earned income under $55,952. The credit varies by family size, filing status and other factors, with the maximum credit going to joint filers with three or more qualifying children.

The maximum amount of income a taxpayer can earn and still get the credit has increased: [18]

- Taxpayer has three or more qualifying children and he or she earned less than $50,162 ($55,952 if married filing jointly).
- Taxpayer has two qualifying children and he or she earned less than $46,703 ($52,493 if married filing jointly).
- Taxpayer has one qualifying child and he or she earned less than $41,094 ($46,884 if married filing jointly).
- Taxpayer does not have a qualifying child and he or she earned less than $15,570 ($21,370 if married filing jointly).

For tax year 2019 the maximum Earned Income Tax Credit is: [18]

- $6,557 with three or more qualifying children.
- $5,828 with two qualifying children.
- $3,526 with one qualifying child.
- $529 with no qualifying children.

The maximum amount of investment income a taxpayer can have and still get the credit has increased to $3,600. Use Publication 596 - Earned Income Tax Credit (EITC) to determine eligibility.

Paid preparers must complete Form 8867 - Paid Preparer's Due Diligence Checklist when filing Federal income tax returns or claims for refund involving the EITC. Paid preparers must meet due diligence requirements in determining the taxpayer's eligibility for, and the amount of, the EITC. Failure to do so could result in a $530 penalty for each failure in 2019. The IRS adjusted the penalty for taxable year returns beginning in 2015 for cost of living.

Due Diligence Requirements

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

Form 8867 - Paid Preparer's Due Diligence Checklist, has been modified to account for these changes. In addition, Form 8867 has been streamlined. Completing the form is not a substitute for actually performing the necessary due diligence and completing all required forms and schedules when preparing the return.

The IRS created Form 8867 to help preparers meet the requirement by obtaining eligibility information from their clients. Preparers have been required to keep copies of the form, or comparable documentation, which is subject to review by the IRS. To help ensure compliance with the law and that eligible taxpayers receive the right credit amount, the new regulations require preparers, effective January 1, 2012, to file the Form 8867 with each return claiming the EITC. Further details can be found in Treasury Decision 9570, published in the Federal Register. [19]

The paid tax return preparer due diligence penalty under IRC Section 6695(h) is now indexed for inflation. Therefore, the penalty for failure to meet the due diligence requirements with respect to returns and claims for refund filed in 2019 is $530 per credit per return.

To meet the due diligence requirements a paid tax return preparer must complete the four following steps:

1. **Completion of Eligibility Checklist** - Prepare form 8867, the paid preparer Earned Income Tax Credit Checklist. The paid tax return preparer must ask and explain to his or her clients all the questions in Part I and all the questions that apply in Part II and III. He or she must personally answer the due diligence questions in Part IV.
2. **Computation of the Credit** - Complete the EITC worksheet, which is available in most tax preparation software programs.
3. **Knowledge** - For the knowledge requirement, the paid tax return preparer must not know or have reason to know that the information used to compute the EITC is incorrect. If there is any doubt, he or she must ask his or her client additional questions. A knowledgeable tax return preparer should be able to conclude if the information given seems incorrect, inconsistent or incomplete.
4. **Record Retention** - The paid tax return preparer must keep the 8867, the EITC worksheet and a record of how he or she received the information used to prepare the return for three years from June 30 following the date he or she presented the return to his or her client to sign. The paid tax return preparer can keep these records in either paper or electronic format. It is a good idea to keep a back-up of these records at an off-site, secure location.

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Completing the Form 8867

Form 8867 covers the HOH filing status, EITC, the AOTC, and the CTC/ACTC/ODC. A tax preparer should only complete columns corresponding to credits actually claimed on the taxpayer's return that he or she prepared. Only paid tax return preparers should complete Form 8867. Form 8867 is divided into questions that relate to all four topics and has questions that are specifically related to HOH filing status only, EITC only, CTC/ACTC/ODC only, and the AOTC only.

Due Diligence Questions for Returns Claiming EITC

A paid tax return preparer must exercise due diligence to determine whether a taxpayer meets all of the eligibility requirements for the EITC. Although lines 9a, 9b and 9c only ask three specific questions about EITC eligibility related to claiming a qualifying child, the tax preparer's client must meet all of the eligibility requirements for claiming the EITC. Therefore, the tax preparer's client cannot claim the EITC if all of the eligibility requirements for the EITC are not satisfied, even if the tax preparer answers "yes" to 9a, 9b and 9c.

Credit Eligibility Certification

The tax preparer must certify that all of the answers on Form 8867 are, to the best of his or her knowledge, true, correct and complete. Failure to meet due diligence requirements with respect to claiming the EITC, the AOTC, and the CTC/ACTC/ODC could result in a $530 penalty for each failure in 2019. For example, if a paid tax return preparer prepares a return claiming the EITC, the AOTC and the CTC/ACTC/ODC and he or she failed to meet the due diligence requirements for all of these credits, the tax preparer could be subject to a penalty of $1,590.

Document Retention

To meet the due diligence requirements for the HOH filing status, EITC, the AOTC, and the CTC/ACTC/ODC, you must keep all of the following records: (20)

1. A copy of Form 8867.
2. The applicable worksheet(s) or your own worksheet(s) for any credits claimed specified in Due Diligence Requirements.
3. Copies of any taxpayer documents you may have relied upon to determine eligibility for and the amount of the credit(s).
4. A record of how, when, and from whom the information used to prepare Form 8867 and worksheet(s) was obtained.
5. A record of any additional questions you may have asked to determine eligibility for and amount of the credits, and the taxpayer's answers.

You must keep those records for three years from the latest of the following dates: (20)

- The due date of the tax return (not including extensions).
- The date the return was filed (if you are a signing tax return preparer electronically filing the return).
- The date the return was presented to the taxpayer for signature (if you are a signing tax return preparer not
- electronically filing the return).
- The date you submitted to the signing tax return preparer the part of the return for which you were responsible (if you are a nonsigning tax return preparer).

These records may be kept on paper or electronically in the manner described in Revenue Procedure 97-22 (or later update). (21)

Consequences of Filing EITC Returns Incorrectly

People who come to you, a tax return preparer, expect you to know the tax law and prepare an accurate return. Also, if you are paid and prepare EITC claims, you must meet EITC due diligence requirements. If the IRS examines your client's return and denies all or a part of EITC, your client: (22)

- Must pay back the amount in error with interest.
- May need to file the Form 8862 - Information to Claim Earned Income Tax Credit after Disallowance.

- May be banned from claiming EITC for the next two years if the IRS finds the error is because of reckless or intentional disregard of the rules.
- May be banned from claiming EITC for the next ten years if the IRS finds the error is because of fraud.

If the IRS examines the EITC claims you prepared and finds you did not meet all four due diligence requirements, you can get: (22)

- A $530 penalty for each failure to comply with EITC due diligence requirements. The penalty amounts are covered in IRC Section 6695(g). (The IRS adjusted the penalty for taxable year returns beginning in 2015 for cost of living.)
- A minimum penalty of $1,000 if you prepare a client return and IRS finds any part of the amount of taxes owed is due to an, unreasonable position (For reference see IRC Section 6694(a)).
- A minimum penalty of $5,000 if you prepare a client return and IRS finds any part of the amount of taxes owed is due to your reckless or intentional disregard of rules or regulations (For reference see IRC Section 6694(b)).

The IRS can also penalize an employer or employing firm if an employee fails to comply with the EITC due diligence requirements. However, there are only specific circumstances when an employer is subject to the due diligence penalty: (23)

- Management participated in or, prior to the time the return was filed, knew of the failure to comply with the due diligence requirements.
- The firm failed to establish reasonable and appropriate procedures to ensure compliance with the due diligence requirements.
- The firm establishes appropriate compliance procedures but disregards those procedures through willfulness, recklessness, or gross indifference, including ignoring facts that would lead a person of reasonable prudence and competence to investigate or figure out the employee was not complying.

Adoption Credit

The American Taxpayer Relief Act of 2012 (H.R.8) passed on January 2, 2013 permanently extended the Adoption Credit and the adoption assistance programs for tax years beginning after December 31, 2012. Tax benefits for adoption include both a tax credit for qualified adoption expenses paid to adopt an eligible child and an exclusion for employer-provided adoption assistance. The credit is nonrefundable, which means it is limited to the taxpayer's tax liability for the year. The maximum amount (dollar limit) for 2019 is $14,080 per child. (24)

For both the credit and the exclusion, qualified adoption expenses, defined in Section 23(d)(1) of the Code, include:

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

Qualified adoption expenses do not include: (24)

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

If the taxpayer is filing Form 8839 - Qualified Adoption Expenses, he or she cannot file the income tax return and Form 8839 electronically. The taxpayer must file a paper return. Mail the return to the address listed in the tax return instructions. (25)

The credit and exclusion are each subject to an income limitation and a dollar limitation. The income limit on the adoption credit or exclusion is based on taxpayer's modified adjusted gross income (MAGI). For tax year 2019, the

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MAGI phase-out begins at $211,160 and ends at $251,160. Thus, if the taxpayer's MAGI amount is below $211,160 for 2019, his or her credit or exclusion will not be affected by the MAGI phase-out but if the taxpayer's MAGI amount for 2019 is above $251,160, his or her credit or exclusion will be zero.

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

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

Because the adoption credit is not refundable after 2011, the taxpayer may be able to carry-forward any unused credit amounts to future tax years. The 2019 Form 8839 and its instructions will have information on the credit carry-forward. [24]

Retirement Savings Contributions Credit (Saver's Credit)

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

The credit may be used against the taxpayer's regular and alternative minimum tax liability. For 2019, the maximum applicable percentage is 50%, which is completely phased out when AGI exceeds $65,000 for joint filers, $48,750 for head of household filers, and $32,500 for single and married filing separately filers. The applicable percentage is the percentage as determined in accordance with the following table: [26]

2019 Saver's Credit AGI Thresholds						
Joint Return		Head of Household		Single or Married Filing Separately		Credit Rate
Over	Not Over	Over	Not Over	Over	Not Over	
$0	$39,000	$0	$29,250	$0	$19,500	50%
$39,000	$42,500	$29,250	$31,875	$19,500	$21,250	20%
$42,500	$65,000	$31,875	$48,750	$21,250	$32,500	10%
$65,000	-----	$48,750	------	$32,500	----	0%

Table 16- Retirement Savings Contributions Credit (Saver's Credit) (2019)

Tuition and Fees Deduction

The Tuition and Fees Deduction allows eligible taxpayers to deduct up to $4,000 from taxable income to help cover higher education costs for themselves, a spouse and dependent children. Qualified expenses for the Tuition and Fees Deduction generally include tuition and fees required for enrollment or attendance at an eligible educational institution. The Further Consolidated Appropriations Act extended the deduction through 2020.

Deduction for Educator Expenses

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

For courses in health and physical education, expenses for supplies are qualified expenses only if they are related to athletics. This deduction is for expenses paid or incurred during the tax year.

The taxpayer is an eligible educator if, for the tax year, he or she meets the following requirements: (27)

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

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

State and Local Income Tax Deduction (SALT)

Under previous tax law the taxpayer could claim an itemized deduction for an unlimited amount of personal state and local income and property taxes. He or she could also choose to forego any deduction for state and local income taxes and instead deduct state and local general sales taxes.

The Tax Cuts and Jobs Act limits the taxpayer's deduction for state and local income and property taxes to a combined total of $10,000 ($5,000 if he or she uses married filing separate status). Foreign real property taxes can no longer be deducted. However, the taxpayer can still choose to deduct state and local sales taxes instead of state and local income taxes.

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

Residential Energy Credits

Residential Energy Efficient Property Credit (Part I) - The taxpayer may be able to take the Residential Energy Efficient Property Credit if he or she made energy saving improvements to his or her home located in the United States.

The credit currently applies to solar electric property and solar water heating property and is available for property placed in service through December 31, 2021, based on an applicable percentage. The applicable percentages are:

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

Nonbusiness Energy Property Credit (Part II) - The credit for nonbusiness energy property for installing insulation, storm windows, etc., which expired at the end of 2017, has not been extended by the Tax Cuts and Jobs Act.

Charitable Donations from IRAs

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

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Key points about qualified charitable contributions (QCDs) include:

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

Qualified charitable distributions can satisfy all or part the amount of the taxpayer's required minimum distribution (RMD) from his or her IRA.

Other 2019 Tax Update Information

Miscellaneous Deductions

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

Note

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

Pass-Through Entities

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

The deduction is generally available to eligible taxpayers whose 2019 taxable incomes fall below $321,400 for joint returns, $160,700 for single and head-of-household returns and $160,725 if married filing separately. It is generally equal to the lesser of 20% of their qualified business income plus 20% of their qualified real estate investment trust dividends and qualified publicly traded partnership income or 20% of taxable income minus net capital gains.

The deduction would be disallowed for businesses offering "professional services", such as law firms, doctor's offices and investment offices, above certain threshold amounts. The W-2 wage limit does not apply in the case of a taxpayer with taxable income not exceeding $321,400 for married individuals filing jointly ($160,700 for single and head-of-household). The application of the W-2 wage limit is phased in for individuals with taxable income exceeding these thresholds, over the next $100,000 of taxable income for married individuals filing jointly ($50,000 for other individuals).

Note

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

Social Security and Medicare Tax

The employee tax rate for Social Security in 2019 is 6.2%. The employer tax rate for Social Security remains unchanged at 6.2%. The Social Security wage base limit rises to $132,900 for 2019. The new wage base translates into a maximum of $8,239.80 withheld from a highly paid employee's 2019 paychecks. The Medicare tax rate is 1.45% each for the employee and employer, unchanged since 2012. There is no wage base limit for Medicare tax.

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If the taxpayer's only income is from self-employment, the Social Security maximum is still in effect. That is, the Social Security portion of his or her self-employment tax is capped at the maximum profit of the company, depending on the maximum for that year. For 2019, the self-employment tax rate on net earnings is 15.3% (12.4% Social Security tax plus 2.9% Medicare tax). (28)

Gift and Estate Tax

Although initial tax plan discussions considered complete elimination of taxes on estates, the Tax Cuts and Jobs Act keeps the Federal estate tax in place, but it doubles the threshold at which that tax applies. For an estate of any decedent dying during calendar year 2019, the basic exclusion from estate tax amount is $11,400,000 ($22,800,000 for married couples), up from a total of $11,180,000 for estates of decedents who died in 2018. The American Taxpayer Relief Act of 2012 permanently increased the top gift and estate tax rate from 35% to 40%. The annual exclusion for gifts also remains the same at $15,000. (29)

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

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

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

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

Table 17 - Publication 929 - Tax for Certain Children Who Have Unearned Income (2018)

The exemption from the Kiddie Tax for 2019 will be $2,200 (up from $2,100 for 2018). A parent will be able to elect to include a child's income on the parent's return for 2019 if the child's income is more than $1,100 and less than $11,000 (up from $1,050 and $10,500 for 2018).

Form 8615 - Tax for Certain Children Who Have Unearned Income must be filed for anyone who meets all of the following conditions: (30)

1. The taxpayer had more than $2,200 of unearned income.
2. The taxpayer is required to file a tax return.
3. The taxpayer was either:
    a. Under age 18 at the end of 2019,
    b. Age 18 at the end of 2019 and did not have earned income that was more than half of his or her support, or
    c. A full-time student at least age 19 and under age 24 at the end of 2019 and did not have earned income that was more than half of his or her support.
4. At least one of the taxpayer's parents was alive at the end of 2019.
5. The taxpayer did not file a joint return for 2019.

Note

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

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Qualified Long-Term Care Insurance Premiums

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

Age Group	2019 Eligible Premium Amount
Age 40 and under	$420
Ages 41 through 50	$790
Ages 51 through 60	$1,580
Ages 61 through 70	$4,220
Age 71 and over	$5,270
Note: The limit on premiums is for each person.	

Table 18 - Publication 502 - Medical and Dental Expenses (2019)

Amounts received under a qualified long-term care insurance contract are generally excludible as amounts received for personal injuries and sickness, subject to a per diem limitation, which will be $370 in 2019.

Series EE and I Savings Bonds Income Exclusion

For 2019, the exclusion under IRC Section 135, regarding income from United States Series EE and I Savings Bonds for taxpayers who pay qualified higher education expenses, begins to phase out for modified adjusted gross income (MAGI) above $121,600 for joint returns and $81,100 for all other returns. The exclusion phases out completely at MAGI levels of $151,600 for joint returns and $96,100 for other returns.

Rates on Long-Term Gains and Dividends

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

For 2019, the rate brackets for capital gains are as follows:

Filing Status	Single	Joint	Head of Household	Estate or Trust
0% Tax Bracket	$0 - $39,374	$0 - $78,749	$0 - $52,749	$0 - $2,649
Beginning of 15% Bracket	$39,375	$78,750	$52,750	$2,650
Beginning of 20% Bracket	$434,550	$488,850	$461,700	$12,950

Table 19 - Revenue Procedure 2018-57 (2019)

Transportation Fringe Benefits

An employer can exclude the value of any de minimis transportation benefit he or she provides to an employee from the employee's wages. A de minimis transportation benefit is any local transportation benefit the employer provides to an employee if it has so little value (taking into account how frequently the employer provides transportation to his or her employees) that accounting for it would be unreasonable or administratively impracticable. For example, it applies to occasional transportation fare an employer gives an employee because the employee is working overtime if the benefit is reasonable and is not based on hours worked. This exclusion applies to the following benefits: [31]

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

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

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An employer can generally exclude the value of transportation benefits that he or she provides to an employee during 2019 from the employee's wages up to the following limits: [31]

- $265 per month for combined commuter highway vehicle transportation and transit passes.
- $265 per month for qualified parking.

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

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

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

Foreign Earned Income Exclusion

If the taxpayer is a U.S. citizen or a resident alien of the United States and he or she lives abroad, the taxpayer is taxed on his or her worldwide income. However, the taxpayer may qualify to exclude from income up to an amount of his or her foreign earnings that is adjusted annually for inflation. The foreign earned income exclusion rises to $105,900 for tax year 2019, up from $103,900 for 2018.

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

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

The taxpayer’s housing amount is the total of his or her housing expenses for the year minus the base housing amount. The computation of the base housing amount (line 32 of Form 2555) is tied to the maximum foreign earned income exclusion. The amount is 16% of the maximum exclusion amount (computed on a daily basis) multiplied by the number of days in the taxpayer’s qualifying period that fall within his or her tax year. The base amount for 2019 is $16,944 or $46.42 per day.

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

1. His or her tax home must be in a foreign country.
2. He or she must have foreign earned income.
3. He or she must be either:
    a. A U.S. citizen who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year, or
    b. A U.S. resident alien who is a citizen or national of a country with which the United States has an income tax treaty in effect and who is a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year, or
    c. A U.S. citizen or a U.S. resident alien who is physically present in a foreign country or countries for at least 330 full days during any period of 12 consecutive months.

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

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Qualified Principal Residence Indebtedness Exclusion

The Further Consolidated Appropriations Act includes an extension of the qualified principal residence indebtedness exclusion that had expired at the end of 2018. Typically, when debt is forgiven, the discharged amount is included in a taxpayer's gross income. The qualified principal residence indebtedness exclusion in 26 U.S.C. Section 108(a)(1)(E), however, allows a taxpayer to exclude up to $2 million of the forgiven debt related to a decline in the value of the residence or to the financial condition of the taxpayer. Many shorts sales and mortgage modifications include debt forgiveness that falls under the qualified principal residence indebtedness exclusion.

Expatriate Health Plans

On June 10, 2016, the Treasury Department and Internal Revenue Service, the Department of Health and Human Services, and the Department of Labor (the Departments) issued proposed regulations that implement the Expatriate Health Coverage Clarification Act of 2014 (EHCCA). The EHCCA generally provides that most ACA provisions do not apply to expatriate health plans covering individuals traveling to or from the United States. More specifically, the EHCCA provides that the requirements of the ACA do not apply to expatriate health plans, expatriate health insurance issuers for coverage under expatriate health plans, and employers in their capacity as plan sponsors of expatriate health plans, except that: [13]

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

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

Direct Deposit Limits

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

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

Virtual Currency

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

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This also means that:

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

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

Report of Foreign Bank and Financial Accounts (FBAR)

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

Therefore, if a U.S. person who has a financial interest in or signature authority over a foreign financial account, including a bank account, brokerage account, mutual fund, trust, or other type of foreign financial account that exceeds $10,000 at any time during the calendar year, the Bank Secrecy Act may require him or her to report the account yearly to the Internal Revenue Service by filing a Report of Foreign Bank and Financial Accounts (FBAR).

FBARs must be electronically filed through the Bank Secrecy Act (BSA) E-Filing System using the electronic FinCEN Form 114 - Report of Foreign Bank and Financial Accounts (FBAR), which supersedes the now-obsolete paper Treasury Department Form 90-22.1.

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

United States persons are required to file an FBAR if both of the following apply: [32]

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

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

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

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

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

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

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

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

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

Those required to file an FBAR who fail to properly file a complete and correct FBAR may be subject to civil monetary penalties. For penalties that are assessed after August 1, 2016, whose associated violations occurred after November 2, 2015, the IRS may assess an inflation-adjusted civil penalty not to exceed $12,459 per violation for non-willful violations that are not due to reasonable cause. For willful violations, the inflation-adjusted penalty may be the greater of $124,588 or 50% of the balance in the account at the time of the violation, for each violation. (32)

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

Tax Calendars

A tax calendar is a 12-month calendar divided into quarters. The calendar gives specific due dates for filing tax forms, paying taxes and taking other actions required by Federal tax law. Publication 509 - Tax Calendars contains a section on how to use the tax calendars, three tax calendars including a General Tax Calendar, an Employer's Tax Calendar and an Excise Tax Calendar and a table showing the semiweekly deposit due dates for payroll taxes for 2019.

Publication 1518 - IRS Tax Calendar for Small Businesses and Self-Employed is no longer published after 2013. An IRS Tax Calendar and most the information previously included in Publication 1518 can be found at www.irs.gov/taxcalendar.

Section 179 Deduction

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

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With the passage and signing into law of the Tax Cuts and Jobs Act, the deduction limit for Section 179 increased from $1,000,000 to $1,020,000 for 2019. The limit on equipment purchases likewise has increased, from $2,500,000 to $2,550,000. In addition, the deduction now includes any of the following improvements to existing nonresidential property (i.e., the improvement must be placed in service after the date the property itself was first placed in service): roofs; heating, air-conditioning, and ventilation systems; fire protection, alarm, and security systems. Further, the bonus depreciation increases from 50% to 100%. This part is retroactive to September 27, 2017 and is good through 2022. The bonus depreciation also now includes used equipment.

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

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

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

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

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

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

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

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

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

If the taxpayer does not claim bonus depreciation, the greatest allowable depreciation deduction in 2019 is:

- $10,100 for the first year,
- $16,100 for the second year,

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- $9,700 for the third year, and
- $5,760 for each later taxable year in the recovery period.

If a taxpayer claims bonus depreciation, the greatest allowable depreciation deduction in 2019 is:

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

Exceptions include the following vehicles:

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

Also, the maximum Section 179 expense deduction for sport utility vehicles (SUV) placed in service in tax years beginning in 2019 is $25,500.

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

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

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

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

Note

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

Bonus Depreciation

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

The 100% depreciation deduction generally applies to depreciable business assets with a recovery period of 20 years or less and certain other property. Machinery, equipment, computers, appliances and furniture generally qualify.

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The definition of property eligible for 100% bonus depreciation was expanded to include used qualified property acquired and placed in service after September 27, 2017, if all the following factors apply:

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

The TCJA added qualified film, television and live theatrical productions as types of qualified property that may be eligible for 100% bonus depreciation. This provision applies to property acquired and placed in service after September 27, 2017.

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

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

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

The TCJA also added an exclusion for any property used in a trade or business that has had floor-plan financing indebtedness if the floor-plan financing interest was taken into account under Section 163(j)(1)(C). Floor-plan financing indebtedness is secured by motor vehicle inventory that in a business that sells or leases motor vehicles to retail customers. The TCJA eliminated qualified improvement property acquired and placed in service after December 31, 2017 as a specific category of qualified property.

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

Unrecovered Basis

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

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

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balance or straight line depreciation. The taxpayer determines his or her unrecovered basis in the 7th year after he or she placed the car in service.

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

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

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

Tax Court Decisions

South Dakota v. Wayfair

On June 21, 2018, the United States Supreme Court ruled 5-4 in South Dakota v. Wayfair that states can mandate that businesses without a physical presence in a state with more than 200 transactions or $100,000 in-state sales collect and remit sales taxes on transactions in the state. This decision overturned the Court's 1992 decision in Quill v. North Dakota and 1967 decision in National Bellas Hess. According to the Court's majority opinion, the South Dakota law did not have an unreasonable burden on retailers because of the following:

- It is not retroactive, meaning South Dakota cannot look back and require collection and remittance of sales and use tax on previously purchased items.
- Only merchants who have considerable amount of business are required to collect (according to the South Dakota law in question that means $100,000 in in-state sales or over 200 orders in the state).
- South Dakota is one of 20 states that have adopted the Streamlined Sales and Use Tax Agreement, which provides certain standardization within the sales and use tax statutes "to reduce administrative and compliance costs" for remote sellers.

McGuigan v. Commission of Internal Revenue

For McGuigan, T.C. Summary Opinion 2019-27, 9/30/19, the Tax Court examined the facts involving a worker who had a long-term relationship with an employer. The taxpayer, who was a diesel technology specialist, had a long-standing business relationship with an entrepreneur. After the entrepreneur started a new company, he invited the taxpayer to work for him. Based on an oral agreement, the taxpayer performed gas recovery services for this employer at multiple oil well sites across Montana and North Dakota. The Tax Court listed the following factors to be examined in deciding whether an employer-employee relationship exists:

- The degree of control exercised by the principal over the details of the work.
- Which party invests in the facilities used in the work.
- The opportunity of the taxpayer for profit or loss.
- Whether the principal has the right to discharge the taxpayer.
- Whether the work is part of the principal's regular business.
- The permanency of the relationship.
- The relationship the parties believe they are creating.

In its analysis, the Tax Court determined that the majority of the factors indicated that the taxpayer was an employee, even though he worked without any supervision. Thus, he could only deduct unreimbursed employee business expenses as miscellaneous expenses.

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2019 California Tax Legislation and Continuing Changes

Tax Cuts and Jobs Act (TCJA)

The Tax Cuts and Jobs Act (TCJA) made multiple changes to the Internal Revenue Code (IRC). In general, California Revenue and Taxation Code (R&TC) **does not conform** to the changes. California taxpayers continue to follow the IRC as of the specified date of January 1, 2015, with modifications.

Most of the provisions in the Tax Cuts and Jobs Act took effect on January 1, 2018 and are operative for income tax returns filed in 2019. In general, the bill provides new tax brackets, larger standard deduction amounts and adjusted credit amounts. It scales back a popular deduction for state and local taxes, repeals a key tenet of the Affordable Care Act and cuts the corporate tax rate from 35% to 21%.

The bill also removed the personal exemption, permanently adjusted the alternative minimum tax (AMT) exemption amounts for inflation and increased the Child Tax Credit (California does not offer this credit). These tax provisions for individual taxpayers, including the new tax rates, **started January 1, 2018, and will expire at the end of 2025.**

Temporary Reduction in Medical Expense Deduction Floor and Alternative Minimum Tax (AMT)

The Tax Cuts and Jobs Act (TCJA) provides that, for taxable years beginning after December 31, 2016, and ending before January 1, 2019, the threshold for deducting medical expenses was 7.5% of AGI for all taxpayers. For these years, this threshold applies for purposes of the alternative minimum tax (AMT) in addition to the regular tax. Under the Further Consolidated Appropriations Act of 2020 the 7.5% floor has returned (it was previously changed to 10%) for 2019 and 2020.

California conforms, under the Personal Income Tax Law (PITL), relating to the itemized deduction for unreimbursed medical expenses under IRC Section 213, as of the “specified date” of January 1, 2015, with modifications. California's modified conformity allows a deduction for the amount of medical expenses unreimbursed by insurance that exceed 7.5% of Federal adjusted gross income (AGI). As a result, the threshold percentage of unreimbursed medical expenses is the same for both Federal and state purposes for the 2019 and 2020 tax years for purposes of the personal income tax.

California conforms, under the PITL, relating to the alternative minimum tax (AMT) under IRC Section 56, as of the “specified date” of January 1, 2015, with modifications. However, California did not conform to the Federal change to the AMT medical expense threshold from 10% to 7.5% of AGI for 2019 and 2020. For California AMT purposes, the unreimbursed medical expense threshold remains 10% of Federal AGI. [33]

Limitation on Deduction for State and Local Taxes

The Tax Cuts and Jobs Act (TCJA) provides that an individual may claim an itemized deduction of up to $10,000 ($5,000 for married taxpayers filing a separate return) for the aggregate of (i) state and local property taxes not accrued in carrying on a trade or business, or an activity described in Section 212, and (ii) state and local income, foreign, income, war profits, and excess profits taxes (or sales taxes in lieu of income, etc. taxes) paid or accrued in the taxable year. Individuals are also not allowed a deduction for foreign real property taxes. The above rules apply to taxable years beginning after December 31, 2017 and beginning before January 1, 2026.

The limitations above do not apply to state and local property taxes, state and local personal property taxes, foreign property taxes, or sales taxes paid or accrued in the taxable year if paid or accrued in carrying on a trade or business or an activity described in IRC Section 212. For instance, in the case of property taxes, an individual may deduct such items in full only if these taxes were imposed on business assets (such as residential rental property). Income taxes have never been deductible for California tax purposes.

The provision also provides that, in the case of an amount paid in a taxable year beginning before January 1, 2018, with respect to a state or local income tax imposed for a taxable year beginning after December 31, 2017, the payment shall be treated as paid on the last day of the taxable year for which such tax is so imposed for purposes of applying the provision limiting the dollar amount of the deduction. Thus, under the provision, an individual may not claim an itemized deduction for the 2017 tax year on a prepayment of income tax for a future taxable year in order to avoid the dollar limitation applicable for taxable years beginning after 2017.

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California conforms, under the PITL, relating to the deductibility of taxes under IRC Section 164, as of the "specified date" of January 1, 2015, with modifications. However, California does not allow a deduction for state and local, foreign, income, war profits, and excess profits taxes or the election to deduct sales taxes. However, California does allow deductions for state and local real and personal property taxes and does not conform to the $10,000 limitation placed by Federal law. (33)

Repatriation

The Tax Cuts and Jobs Act made sweeping changes to the Federal income tax law, including changes to the international tax provisions under the Internal Revenue Code (IRC). The Act:

- Added new IRC Section 245A permitting tax-free repatriations of future foreign profits of foreign corporations to their 10% U.S. shareholders that are domestic corporations.
- Amended IRC Section 965 imposing an immediate one-time tax at a reduced rate on all U.S. shareholders on accumulated earnings of foreign corporations that are controlled foreign corporations (CFCs) or which have 10% U.S. shareholders via a one-time deemed repatriation of those earnings.
- Added IRC Section 951A imposing a current tax, similar to subpart F,17 on a U.S. shareholder's "global intangible low-taxed income" (GILTI) of a CFC.
- Modified certain aspects of the "subpart F" anti-deferral rules.
- Enacted several new provisions intended to prevent erosion of the U.S. tax base.

Generally, when California's CTL incorporates provisions of the IRC by reference, it is done by specified conformity date. Currently, general conformity is to the IRC as of January 1, 2015 One exception to the general conformity by specified date rule applies to the water's-edge election provisions. When water's-edge provisions refer to an IRC provision, it is the IRC provision that is not otherwise applicable, it is the IRC provision in effect for Federal purposes for the same taxable period. The FTB's long-standing position interprets this special conformity exception as only conforming to the IRC provisions for those IRC provisions specifically referred to in the water's-edge provisions. The IRC provisions not specifically referred to in the water's-edge provisions are subject to conformity by specified date. Existing California CTL does not incorporate by reference IRC sections 245A, 951A, and 965. In addition, the water's-edge provisions within the California CTL do not specifically refer to IRC sections 245A, 951A, and 965; therefore, existing California water's-edge provisions do not conform to those repatriation provisions.

Miscellaneous Itemized Deductions Subject to the 2% Floor

The Tax Cuts and Jobs Act suspends all miscellaneous itemized deductions that are subject to the 2% floor under present law. Thus, under the new provision, taxpayers may not claim any items as itemized deductions for the taxable years to which the suspension applies. Previous law and IRS guidance provided examples of items that were deductible under the old provision.

This non-exhaustive list includes: (34)

- Appraisal fees for a casualty loss or charitable contribution.
- Casualty and theft losses from property used in performing services as an employee.
- Clerical help and office rent in caring for investments.
- Depreciation on home computers used for investments.
- Excess deductions (including administrative expenses) allowed a beneficiary on termination of an estate or trust.
- Fees to collect interest and dividends.
- Hobby expenses, but generally not more than hobby income.
- Indirect miscellaneous deductions from pass-through entities.
- Investment fees and expenses.
- Loss on deposits in an insolvent or bankrupt financial institution.
- Loss on traditional IRAs or Roth IRAs, when all amounts have been distributed.
- Repayments of income.
- Safe deposit box rental fees, except for storing jewelry and other personal effects.
- Service charges on dividend reinvestment plans.
- Trustee's fees for an IRA, if separately billed and paid.

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Tip

California continues to allow miscellaneous itemized deductions subject to 2% of Federal AGI, while Federal law has eliminated these deductions.

Tax Preparation Expenses

For regular income tax purposes, individuals are allowed an itemized deduction for expenses for the production of income. These expenses are defined as ordinary and necessary expenses paid or incurred in a taxable year: (1) for the production or collection of income; (2) for the management, conservation, or maintenance of property held for the production of income; or (3) in connection with the determination, collection, or refund of any tax as defined in IRC Section 212. The provision suspends all miscellaneous itemized deductions that are subject to the 2% floor under present law. Thus, under the provision, taxpayers may not claim the above-listed items as itemized deductions for the taxable years to which the suspension applies. California conforms, under the PITL, to the Federal rules relating to miscellaneous itemized deductions under IRC Section 67, as of the specified date of January 1, 2015, with modifications, but does not conform to the Federal suspension of all miscellaneous itemized deductions.

Unreimbursed Business Expenses

In general, unreimbursed business expenses incurred by an employee are deductible, but only as an itemized deduction and only to the extent the expenses exceed 2% of adjusted gross income. Previous law and IRS guidance provide examples of items that may be deducted under this provision.

This non-exhaustive list includes: (34)

- Business bad debt of an employee.
- Business liability insurance premiums.
- Damages paid to a former employer for breach of an employment contract.
- Depreciation on a computer a taxpayer's employer requires him to use in his work.
- Dues to a chamber of commerce if membership helps the taxpayer perform his job.
- Dues to professional societies.
- Educator expenses.
- Home office or part of a taxpayer's home used regularly and exclusively in the taxpayer's work.
- Job search expenses in the taxpayer's present occupation.
- Laboratory breakage fees.
- Legal fees related to the taxpayer's job.
- Licenses and regulatory fees.
- Malpractice insurance premiums.
- Medical examinations required by an employer.
- Occupational taxes.
- Passport fees for a business trip.
- Repayment of an income aid payment received under an employer's plan.
- Research expenses of a college professor.
- Rural mail carriers' vehicle expenses.
- Subscriptions to professional journals and trade magazines related to the taxpayer's work.
- Tools and supplies used in the taxpayer's work.
- Purchase of travel, transportation, meals, entertainment, gifts, and local lodging related to the taxpayer's work.
- Union dues and expenses.
- Work clothes and uniforms if required and not suitable for everyday use.
- Work-related education.

The provision suspends all miscellaneous itemized deductions that are subject to the 2% floor under present law. Thus, under the provision, taxpayers may not claim the above-listed items as itemized deductions for the taxable years to which the suspension applies.

California conforms, under the PITL, to the Federal rules relating to miscellaneous itemized deductions under IRC Section 67, as of the specified date of January 1, 2015, with modifications, but does not conform to the Federal suspension of all miscellaneous itemized deductions.

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Therefore, valid employee business expenses are defined as:

- Paid or incurred during the taxpayer's tax year.
- Required to carry on a trade or business.
- Ordinary and necessary.
- Not reimbursed by the taxpayer's employer.
- Not eligible to obtain reimbursement from the taxpayer's employer.

Modification of Deduction for Personal Casualty Losses

The Tax Cuts and Jobs Act temporarily modifies the deduction for personal casualty and theft losses. Under the provision, a taxpayer may claim a personal casualty loss only if such loss was attributable to a disaster declared by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act. California conforms, under the PITL, relating to the treatment of personal casualty loss deductions under IRC Section 165(h), as of the "specified date" of January 1, 2015, with modifications, but does not conform to the temporary federal modification to only allow a deduction for presidentially declared disasters as personal casualty losses. California tax law identifies specific events as disasters and excess disaster losses are allowed special carry forward treatment. That is, 100% of the excess disaster loss may be carried over for up to 15 taxable years. In addition, IRC Section 165(i), relating to the election to take a loss deduction in the preceding year, applies to disasters that were the subject of a Governor's proclamation, but not the subject of a Presidential disaster declaration.

Claim of Right

Under Section 1341, if the taxpayer had to repay an amount that the taxpayer included in his or her income in an earlier year, because at the time he or she thought he or she had an unrestricted right to it, the taxpayer may be able to deduct the amount repaid from his or her income for the year in which he or she repaid it. Or, if the amount the taxpayer repaid is more than $3,000, he or she may take a credit against his or her tax for the year in which he or she repaid it, whichever results in the least tax.

If the amount repaid was not taxed by California, then no credit is allowed. If the taxpayer is eligible to take the credit for California, he or she adds the credit amount on the total payment line of the Form 540. If the taxpayer claimed a credit for the repayment on his or her Federal tax return and are deducting the repayment for California, enter the allowable deduction as a positive amount on Part II of Schedule CA (540). Deductions of $3,000 or less are subject to the 2% Federal adjusted gross income (AGI) limit.

However, under the Tax Cuts and Jobs Act (TCJA), for tax years beginning after December 31, 2017 until January 1, 2026, the deduction for miscellaneous itemized deductions that are subject to the 2% floor is suspended. Therefore, no miscellaneous itemized deductions may be claimed by an individual on Schedule A of Form 1040 for tax years 2018 through 2025. Consequently, if the amount the taxpayer repaid was $3,000 or less, the taxpayer will no longer deduct it as a miscellaneous itemized deduction on Schedule A (Form 1040). Repayments of income received under a claim of right as repayments are subject to the 2% floor if less than $3,000. California conforms, under the PITL, to the Federal rules relating to miscellaneous itemized deductions under IRC Section 67, as of the specified date of January 1, 2015, with modifications, but does not conform to the Federal suspension of all miscellaneous itemized deductions.

Investment Expenses

Investment expenses are the taxpayer's allowed deductions, other than interest expense, directly connected with the production of investment income. For example, depreciation or depletion allowed on assets that produce investment income or software or online services used to manage the taxpayer's investments are investment expenses. The taxpayer includes investment expenses reported to him or her on Schedules K-1 (100S, 541, 565, or 568). Investment expenses do not include any deductions taken into account in determining the taxpayer's income or loss from a passive activity. If the taxpayer has investment expenses that could have been included as miscellaneous itemized deduction on Federal Schedule A (Form 1040) - Itemized Deductions, they are no longer allowed. Under the Tax Cuts and Jobs Act (TCJA), for tax years beginning after December 31, 2017 until January 1, 2026, the deduction for miscellaneous itemized deductions that are subject to the 2% floor is suspended. Therefore, no miscellaneous itemized deductions may be claimed by an individual on Schedule A of Form 1040 for tax years 2018 through 2025. California conforms, under the PITL, to the Federal rules relating to miscellaneous itemized deductions under IRC

Section 67, as of the specified date of January 1, 2015, with modifications, but does not conform to the Federal suspension of all miscellaneous itemized deductions.

Itemized Deduction Phase-out

The Tax Cuts and Jobs Act repeals the overall limitation on itemized deductions. California conforms, under the PITL, to the overall limitation on itemized deductions as of the "specified date" of January 1, 2015, with modifications, but does not conform to the Federal repeal of the overall limitation on itemized deductions. California provides its own indexed-for-inflation limitation amounts. For 2019, the amount of otherwise allowable itemized deductions (other than medical expenses, investment interest, and casualty, theft, or wagering losses) is reduced by 6% of the amount of the taxpayer's Federal AGI in excess of $200,534 for single or married-filing-separate/RDP taxpayers, $401,072 for married/RDP taxpayers filing a joint return, and $300,805 for taxpayers who file under the head-of-household status.

What's New

Minimum Essential Coverage Individual Health Care Mandate

By enacting Senate Bill 78 (Chapter 38, Statutes of 2019), the Legislature created the Minimum Essential Coverage Individual Mandate ("Mandate"). The Mandate takes effect on January 1, 2020 and requires Californians to maintain minimum essential coverage for each month on or after that date. Californians who fail to have qualifying health coverage will owe a state penalty for each month they lack coverage. In addition, those responsible for ensuring their spouse or dependents maintain coverage may owe a penalty if their spouse or dependents do not have minimum essential coverage. Californians who owe a penalty will pay when they file their tax year 2020 state income tax return in early 2021.

To avoid this penalty, California residents need to have monthly qualifying health insurance for themselves, their spouse and their dependents beginning on January 1, 2020.

Covered California (https://www.healthforcalifornia.com/covered-california), the state's insurance marketplace, will provide financial assistance to some households that meet certain income requirements, and issue certificates of exemptions to individuals who are exempt from the Mandate.

Young Child Tax Credit (YCTC)

The Young Child Tax Credit (YCTC) is a new credit that could mean up to $1,000 additional in the taxpayer's refund for parents with at least one child younger than age 6 as of December 31, 2019. The credit is available to families making less than $30,000 and can be worth up to $1,000. Like California Earned Income Tax Credit (CalEITC), the Young Child Tax Credit YCTC phases out as income rises

Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA)

The Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA), SB 94, passed on June 27, 2017. It established a comprehensive system to control and regulate the cultivation, distribution, transport, storage, manufacturing, processing, and sale of medicinal and adult-use cannabis, and related products. The MAUCRSA defines the power and duties of the various state agencies responsible for controlling and regulating the commercial medicinal and adult-use cannabis industry.

Cannabis businesses that have already received any required licenses or permits from their local jurisdiction may apply for state licenses to operate from various agencies.

Businesses operating under these state licenses can choose any form of valid business structure for their business. They are able to operate on a for-profit or not-for-profit basis. They are not eligible for California franchise and income tax exemption, as they do not meet the requirements as described in Internal Revenue Code Section 501(c) or California Revenue and Taxation Code (R&TC) Section 23701.

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Other Important Information

California Earned Income Tax Credit (CalEITC)

For 2019, the CalEITC is "refundable," meaning that the taxpayer will receive a refund if the amount of the credit is greater than the tax he or she owes. This credit is available to California households with Federal adjusted gross incomes (AGI) of less than $30,000 regardless of the number of qualifying children. For the CalEITC, eligible sources of earned income are W-2 wages, self-employment income, salaries, tips and other employee compensation subject to California withholding. The 2017 tax year was the first time self-employment income can be used to qualify for CalEITC.

Payments and Credits Applied to Use Tax

For taxable years beginning on or after January 1, 2015, if a taxpayer includes use tax on their personal income tax return, payments and credits will be applied to use tax first, then towards income tax, interest, and penalties.

Financial Incentive for Seismic Improvement

For taxable years beginning on or after January 1, 2015, taxpayers can exclude from gross income any amount received as loan forgiveness, grant, credit, rebate, voucher, or other financial incentive issued by the California Residential Mitigation Program or the California Earthquake Authority to assist a residential property owner or occupant with expenses paid, or obligations incurred, for earthquake loss mitigation.

Natural Heritage Preservation Credit

For qualified contributions made on or after January 1, 2015, the credit carryover period has been extended to 15 years or until exhausted, whichever occurs first. Any unused credits remaining before January 1, 2015, will remain subject to an eight-year carryover provision. In addition, the period for when a qualified contribution is made, for which a tax credit will be allowed, has been extended to June 30, 2020.

Disaster Losses

For taxable years beginning on or after January 1, 2014, and before January 1, 2024, taxpayers may deduct a disaster loss for any loss sustained in any city, county, or city and county in California that is proclaimed by the Governor to be in a state of emergency. For these Governor-only declared disasters, subsequent state legislation is not required to activate the disaster loss provisions.

Taxpayers affected by declared disasters are automatically eligible for qualifying disaster loss treatment. Special tax rules apply to disaster losses. Victims may claim a loss in either the year the disaster occurred or in the prior year. Those who choose the latter can reduce their tax liability for the prior year, allowing FTB to quickly issue a refund. Taxpayers who need copies of lost or damaged state tax returns should complete FTB Form 3516 - Request for Copy of Personal Income or Fiduciary Tax Return, which can be downloaded online.

Generally, California law follows Federal law regarding the treatment of losses incurred as a result of a casualty or a disaster. However, for California purposes, a casualty loss becomes a disaster loss when both of the following occur:

- The loss is sustained in an area the President of the United States or the Governor of California declares a state of emergency.
- The loss is sustained because of the declared disaster.

Head of Household

For taxable years beginning on or after January 1, 2015, California requires taxpayers who use head of household (HOH) filing status to file FTB Form 3532 - Head of Household Filing Status Schedule, to report how the HOH filing status was determined.

Financial Incentive for Turf Removal

For taxable years beginning on or after January 1, 2014, and before January 1, 2019, taxpayers can exclude from

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gross income any amount received as a rebate, voucher, or other financial incentive issued by a local water agency or supplier for participation in a turf removal water conservation program.

Penalty Assessed by Professional Sports League

For taxable years beginning on or after January 1, 2014, an owner of all or part of a professional sports franchise will not be allowed a deduction for the amount of any fine or penalty paid or incurred, that was assessed or imposed by the professional sports league that includes that franchise.

Repeal of Geographically Targeted Economic Development Area Tax Incentives

The California legislature repealed and made changes to all of the Geographically Targeted Economic Development Area (G-TEDA) Tax Incentives. Enterprise Zones (EZ) and Local Agency Military Base Recovery Areas (LAMBRA) were repealed on January 1, 2014. The Targeted Tax Areas (TTA) and Manufacturing Enhancement Areas (MEA) both expired on December 31, 2012.

Form 3840 - California Like-Kind Exchanges

For taxable years beginning after January 1, 2014, California requires taxpayers who exchanged real or tangible personal property located in California for like-kind property located outside of California, and that meet all the requirements of Internal Revenue Code Section 1031, to file an annual information return with the Franchise Tax Board (FTB). The FTB has finalized the new FTB Form 3840 - California Like-Kind Exchanges to help taxpayers keep track of their California source deferred gains from like-kind exchanges involving like-kind property located outside of California and meet this new reporting requirement. All taxpayers who complete a like-kind exchange of California property for non-California property are required to file FTB Form 3840. The mandatory filing requirement applies to all individuals, estates, trusts and all business entities regardless of their residency status or commercial domicile.

Enterprise Zone Credits

Assembly Bill 93 repeals all enterprise zones on January 1, 2014. Although the enterprise zone credits are repealed beginning with the 2014 tax year, unused hiring and sales and use tax credits may be carried over for 10 years after 2013. This 10-year carryover limitation applies to flow-through entity owners as well. Even though the enterprise zones are repealed beginning January 1, 2014, the credit carryover may only be used against the net tax that would have been imposed on the income attributable to activities within the respective former enterprise zone.

Qualifying and vouchered employees hired prior to January 1, 2014, will continue to generate credits for any remaining portion of the 60-month period from the commencement of employment. As always, the credit carryover is subject to the business income limitation. Specifically, the credit carryover may only be used against the net tax that would have been imposed on the income attributable to activities within the respective former enterprise zone.

Cancellation of Debt Income (CODI)

For taxable years beginning on or after January 1, 2014, and before January 1, 2019, California did not conform to the Federal recognition of CODI under IRC Section 108(i). If the taxpayer recognized the CODI for Federal tax purposes, then he or she must deduct the Federal CODI amount.

Governor Declared Disasters

For taxable years beginning on or after January 1, 2014, and before January 1, 2024, taxpayers may deduct a disaster loss for any loss sustained in any city, county, or city and county in California that is proclaimed by the Governor to be in a state of emergency. For these Governor-only declared disasters, subsequent state legislation is not required to activate the disaster loss provisions. Any law that suspends, defers, reduces, or otherwise diminishes the deduction of a net operating loss (NOL) shall not apply to a NOL attributable to these specified disaster losses. The President's declaration continues to activate the disaster loss provisions.

Net Operating Loss (NOL) Carryback

For NOLs incurred in taxable years beginning on or after January 1, 2015, the carryback amount shall be 100% of the NOL. Individuals, Estates, and Trusts compute the NOL carryback in Part IV of FTB Form 3805V - Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations - Individuals, Estates, and Trusts. [35]

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Tip

Any taxpayer entitled to a carryback period pursuant to Internal Revenue Code (IRC) Section 172(b)(3) may elect to relinquish/waive the entire carryback period with respect to an NOL incurred in the 2013 taxable year. By making the election, the taxpayer is electing to carry an NOL forward instead of carrying it back in the previous two years. To make the election, the taxpayer should check the box in Part I under Section C - Election to Waive Carryback, of FTB Form 3805V - Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations - Individuals, Estates, and Trusts, and attach FTB Form 3805V to the tax return.

2019 California Tax Rates and Exemptions

The rate of inflation in California, for the period from July 1, 2018, through June 30, 2019, was 3.1%. The 2019 personal income tax brackets are indexed by this amount. The maximum rate for individuals is 12.3%, the AMT rate for individuals is 7% and the Mental Health Services Tax Rate is 1% for taxable income in excess of $1,000,000. The tax rate for corporations other than banks and financials is 8.84%. For banks and financial institutions, the tax rate is 10.84%. The corporate Alternative Minimum Tax (AMT) rate is 6.65%. The S corporation tax rate is 1.5% and the S corporation bank and financial rate is 3.5%.

Schedule X — Single or married/RDP filing separately				
Over	**But not over**	**Tax is**		**Of amount over**
$0	$8,809	$0.00	Plus 1.00%	$0
$8,809	$20,883	$88.09	Plus 2.00%	$8,809
$20,833	$32,960	$329.57	Plus 4.00%	$20,833
$32,960	$45,753	$812.65	Plus 6.00%	$32,960
$45,753	$57,824	$1580.23	Plus 8.00%	$45,753
$57,824	$295,373	$2,545.91	Plus 9.30%	$57,824
$295,373	$354,445	$24,637.97	Plus 10.30%	$295,373
$354,445	$590,742	$30,722.39	Plus 11.30%	$354,445
$590,742	And over	$57,423.95	Plus 12.30%	$590,742

Table 20 - California Tax Rate Schedules (2019)

Schedule Y — Married/RDP filing jointly, or qualifying widow(er) with dependent child				
Over	**But not over**	**Tax is**		**Of amount over**
$0	$17,618	$0.00	Plus 1.00%	$0
$17,618	$41,766	$176.18	Plus 2.00%	$17,618

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$41,766	$65,920	$659.14	Plus 4.00%	$41,766
$65,920	$91,506	$1625.30	Plus 6.00%	$65,920
$91,506	$115,648	$3160.46	Plus 8.00%	$91,506
$115,648	$590,746	$5,091.82	Plus 9.30%	$115,648
$590,746	$708,890	$49,275.93	Plus 10.30%	$590,746
$708,890	$1,181,484	$61,444.76	Plus 11.30%	$708,890
$1,181,484	And over	$114,847.88	Plus 12.30%	$1,181,484

Table 21 - California Tax Rate Schedules (2019)

Schedule Z — Head of Household				
Over	**But not over**	**Tax is**		**Of amount over**
$0	$17,629	$0.00	Plus 1.00%	$0
$17,629	$41,768	$176.29	Plus 2.00%	$17,629
$41,768	$53,843	$659.07	Plus 4.00%	$41,768
$53,843	$66,636	$1,142.07	Plus 6.00%	$53,843
$66,636	$78,710	$1,909.65	Plus 8.00%	$66,636
$78,710	$401,705	$2,875.57	Plus 9.30%	$78,710
$401,705	$482,047	$32,914.11	Plus 10.30%	$401,705
$482,047	$803,410	$41,189.34	Plus 11.30%	$482,047
$803,410	And over	$77,503.36	Plus 12.30%	$803,410

Table 22 - California Tax Rate Schedules (2019)

Filing requirement thresholds, the standard deduction, and certain credits were adjusted along with income tax brackets based on the inflation rate of 3.1%, as measured by the California CPI for all urban consumers from July 2018 to June 2019. In the previous year, California had an inflation rate that measured 3.1%. Below are some of the changes to various items:

Standard Deduction, Personal Exemption, Renter's Credit	2018 Amounts	2019 Amounts
Standard deduction for single or married, filing separate	$4,401	$4,537

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Standard deduction for joint, surviving spouse, head of household	$8,802	$9,074
The minimum standard deduction for dependents	$1,050	$1,050
Personal exemption credit for single, separate, head of household	$118	$122
Personal exemption credit for joint filers, surviving spouses	$236	$244
Dependent exemption credit	$367	$378
Nonrefundable Renter's Credit available for single filers with AGI	$41,641 or less	$42,932 or less
Nonrefundable Renter's Credit available for joint filers with AGI	$83,282 or less	$85,864 or less

Table 23 - FTB State Income Tax Rate Schedules Adjusted (2019)

California Exemption Credits

Tax credits are allowed for personal exemptions. The credits are deducted from the tax computed on taxable income before exemptions are applied. The credit applies to the separate tax on lump-sum distributions. The exemption credits for 2019 are shown below:

Filing Status/Qualification	2018	2019
Single person	$118	$122
Married/RDP, separate return	$118	$122
Married/RDP, joint return	$236	$244
Head of household	$118	$122
Qualifying widow(er)	$236	$244
Dependent	$367	$378
Blind person - additional	$118	$122
Age 65 or older - additional	$118	$122
Estates*	$10	
Trusts*	$1	
*Estates and Trusts exemption credits are considered "Special credits allowed" under R&TC Section 17733.		

Table 24 - State of California Franchise Tax Board - California Tax Rates and Exemptions (2019)

Reduction of Exemption Credits for High-Income Taxpayers

Tip

The exemption credits are reduced if a taxpayer's Federal adjusted gross income exceeds a threshold amount. For 2019, in the case of single taxpayers, each credit is reduced by $6 for each $2,500 or fraction thereof by which the taxpayer's Federal adjusted gross income exceeds $200,534. For married/RDP taxpayers or a surviving spouse filing a joint return, each credit is reduced by $12 for each $2,500 or fraction thereof by which the taxpayer's Federal adjusted gross income exceeds $401,072.

For married/RDP taxpayers filing separately, each credit is reduced by $6 for each $1,250 of Federal adjusted gross income over $200,534. For a head of household, each credit is reduced by $6 for each $2,500 of Federal adjusted gross income over $300,805. The threshold amounts are adjusted annually for inflation. California conforms to this procedure in principle.

A worksheet is provided by the California FTB to assist in determining the amount of the exemption credit reduction. When applying the phase-out amount, apply the $6/$12 amount to each exemption credit, but do not reduce the credit below zero. If a personal exemption credit is less than the phase-out amount, do not apply the excess against a dependent exemption credit. (36)

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Nonresidents and Part-Year Residents

Nonresidents and part-year residents are allowed reduced credits for personal exemptions on the basis of prorated taxable income. The phase-out of exemption credits for high-income taxpayers must be applied before the proration of the credits.

California Standard Deduction

The taxpayer should decide whether to itemize his or her charitable contributions, medical expenses, mortgage interest paid, taxes, etc., or take the standard deduction. The taxpayer's California income tax will be less if he or she takes the **larger** of:

- His or her California itemized deductions.
- His or her California standard deduction.

California itemized deductions may be limited based on Federal AGI. To compute limitations, the taxpayer should use Schedule CA (540). A Registered Domestic Partner (RDP) should use his or her recalculated Federal AGI to figure his or her itemized deductions. On Federal tax returns, individual taxpayers who claim the standard deduction are allowed an additional deduction for net disaster losses. For California, deductions for disaster losses are only allowed for those individual taxpayers who itemized their deductions. If married/or an RDP and filing separate tax returns, the taxpayer and his or her spouse/RDP must either both itemize their deductions (even if the itemized deductions of one spouse/RDP are less than the standard deduction) or both take the standard deduction. If someone else can claim the taxpayer as a dependent, he or she may claim the greater of the standard deduction or his or her itemized deductions. To figure his or her standard deduction, the taxpayer should use the FTB Form 540 - California Standard Deduction Worksheet for Dependents.

The 2019 California standard deduction for a head of household, a surviving spouse, or a married couple filing a joint return is $9,074. For single filers or married/RDP filing separately, the deduction is $4,537. The minimum standard deduction for dependents is $1,050. Both Federal and California law limit the standard deduction of a person who is claimed as a dependent.

Deductions of Nonresidents

The California tax on nonresidents and part-year residents is determined on the basis of the taxable income of a nonresident or part-year resident. In computing either California adjusted gross income or a nonresident's or part-year resident's taxable income for this purpose, only deductions that are attributable to California are allowable.

Nonresidents and part-year residents may prorate their itemized deductions, including deductions for alimony paid, or the standard deduction by the ratio that California adjusted gross income bears to total adjusted gross income. To compute the percentage of itemized or standard deductions available to be claimed, divide California AGI by the Federal AGI (the result cannot exceed 1.0).

In computing the tax that would be payable if the taxpayer were a full-year resident, the usual rules for itemizing deductions are applicable, that is, deductions should normally be itemized if they amount to more than the standard deduction.

California Itemized Deductions

Overall Limitation for High-Income Taxpayers

The itemized deductions of taxpayers in high-income brackets will be limited to the lesser of 6% of the excess of adjusted gross income over the threshold amount or 80% of the amount of itemized deductions otherwise allowable for the tax year. The 2019 California threshold amounts are: (37)

- $200,534 for a single taxpayer or a married taxpayer filing a separate return.
- $300,805 for a head of household.
- $401,072 for a surviving spouse or a married taxpayer filing a joint return.

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The California threshold amounts are adjusted annually for inflation. Also, California does not incorporate the Federal repeal of the limitation on high-income taxpayers claiming itemized deductions under the Tax Cuts and Jobs Act (TCJA).

Other California 2019 Tax Update Information

Nonrefundable Renter's Credit

The Nonrefundable Renter's Credit is a personal income tax credit that can only be used to offset tax liability; therefore, a taxpayer must have a tax liability to claim the credit.

To qualify for the full Nonrefundable Renter's Credit, the taxpayer must meet **all** the following: (38)

1. Was a resident of California.
2. Have California adjusted gross income (AGI) under certain levels. For 2019 the limit is $42,932 or less if the taxpayer's filing status is single or married/RDP filing a separate return; or $85,864 or less if he or she is a married/RDP filing jointly, a head of household, or a qualified widow(er).
3. Paid rent for at least half of 2019 for property in California that was his or her principal residence.
4. Did not live with another person for more than half the year (such as a parent) who claimed him or her as a dependent in 2019.
5. Not a minor living with and under the care of a parent, foster parent, or legal guardian.
6. Rented property for more than half the year that was not exempt from California property tax in 2019.
7. Married and neither taxpayer nor his or her spouse/RDP was granted a homeowner's property tax exemption during 2019. (The taxpayer can still qualify for the credit, even though his or her spouse/RDP claimed a homeowner's exemption, as long as each maintained a separate residence for the entire year in 2019).

If the taxpayer met the income requirements the credit for 2019 is:

- Single, $60.
- Head of household or widow(er), $120.
- Married/registered domestic partner filing separately, $60.
- Married/registered domestic partner filing jointly, $120.

If the taxpayer was a resident of California for at least six months in 2019 and paid rent on property in California, which was his or her principal residence, he or she may qualify for a reduced amount of the credit, when filing, Form 540NR, based on the number of full months he or she was a resident of and rented property in California.

Senior Head of Household Credit

For 2019, California allowed a senior head of household to claim a credit equal to 2% of taxable income, with a maximum California AGI of $78,894, and a maximum credit of $1,478. To qualify for the credit in 2019, a taxpayer must: (37)

- Be 65 years of age or older on December 31, 2019.*
- Qualify as a head of household in 2017 or 2018 by providing a household for a qualifying individual who died during 2017 or 2018.
- Not have California AGI over $78,894 for 2019.

*If the taxpayer's 65th birthday is on January 1, 2020, he or she is considered to be age 65 on December 31, 2019.

Credits for Joint Custody Head of Household/Dependent Parent

For the 2019 tax year, the California joint custody head of household/dependent parent credits equaled the lesser of 30% of the net tax or a maximum of $494. The credits cover both dependent children and dependent parents. The credits are subject to the same annual inflation adjustment as the exemption credits. However, neither may be claimed if the taxpayer used either the head of household or qualifying widow(er) filing status.

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California Earned Income Tax Credit (CalEITC)

California offers its own Earned Income Tax Credit (CalEITC). This credit is offered in addition to the existing Federal EITC. The CalEITC is "refundable," meaning that the taxpayer will receive a refund if the amount of the credit is greater than the tax he or she owes. This credit is available to California households with adjusted gross incomes (AGI) of less than $30,000 regardless of the number of qualifying children.

The taxpayer qualifies for CalEITC for the 2019 tax year if: [39]

1. He or she has wages, self-employment income and adjusted gross income within certain limits, AND
2. He or she, his or her spouse, and any qualifying children each have a Social Security Number issued by the Social Security Administration that is valid for employment, AND
3. He or she does not use the “married/RDP filing separately” filing status, AND
4. He or she lived in California for more than half the tax year.

For the CalEITC, eligible sources of earned income are W-2 wages, self-employment income, salaries, tips and other employee compensation subject to California withholding. The 2017 tax year was the first time self-employment income can be used to qualify for CalEITC. The taxpayer can find his or her filing status in the next table to see how much he or she may qualify for or he or she can use the CalEITC4Me online calculator to estimate his or her credit:

2019 California Earned Income Tax Credit Maximum Amounts			
Number of Qualifying Children	CA Maximum Income	CalEITC (up to)	IRS EITC (up to)
None	$30,000	$240	$529
1	$30,000	$1,605	$3,526
2	$30,000	$2,651	$5,828
3 or more	$30,000	$2,982	$6,557

Table 25 - California Earned Income Tax Credit Amounts (2019)

The Young Child Tax Credit (YCTC) was introduced in tax year 2019. If the taxpayer qualifies for CalEITC and has a child under the age of 6 as of the end of the tax year, he or she may qualify for up to $1,000 through this credit.

California Earned Income Tax Credit Qualifications

- The taxpayer must file a state tax return, even if he or she does not owe any tax or are not otherwise required to file.
- The taxpayer must have earned income from W-2 wages, self-employment, salaries, tips, or other employee compensation subject to California withholding. (The 2017 tax year was the first-time self-employment income can be used to qualify for CalEITC.)
- The taxpayer, his or her spouse, and any qualifying children must each have a Social Security number issued by the Social Security Administration that is valid for employment.
- The taxpayer must file using the single, married/registered domestic partner (RDP) filing jointly, or head of household filing status. The “married/RDP filing separately” status may not be used.
- The taxpayer must either:
  - Meet the rules for those without a qualifying child; or
  - Have an individual that meets all of the qualifying child rules for him or herself or his or her spouse if he or she files a joint return.
- The taxpayer’s principal residence must be in California for more than half the tax year.
- For 2019, both the taxpayer’s adjusted gross income and earned income (defined above) must be no more than $30,000 regardless of the number of qualifying children.

California Earned Income Tax Credit Qualifying Child Rules

In general, to be a taxpayer’s qualifying child, a person must meet three criteria:

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- **Relationship** - Is the taxpayer's child or stepchild (whether by blood or adoption), foster child, sibling or stepsibling, or a descendant of any of them.
- **Residence** - Has the same principal residence as the taxpayer in California for more than half the tax year. Certain exceptions apply.
- **Age** - Must be younger than the taxpayer and either a) under the age of 19 at the end of the tax year, or b) under the age of 24 if a full-time student for at least 5 months of the year. A permanently and totally disabled child may be included at any age.

One Return – The child only qualifies for one return. If the child can be claimed by more than one taxpayer, the child's qualification goes to:

- The parent.
- If more than 1 taxpayer is the child's parent, the one with whom the child lived for the longest time during the year, or if the time was equal, the parent with the highest adjusted gross income (AGI).
- If no eligible parent claims the child, the individual claiming the child, if the individual's AGI exceeds the AGI of any parent eligible to claim the child.

If no taxpayer is the child's parent, the taxpayer with the highest AGI.

The taxpayer will need to file a California income tax return and complete an FTB Form 3514 - Earned Income Tax Credit to claim the credit. California does not offer a state Earned Income Tax Credit for tax years prior to 2015.

California Motion Picture and Television Production Credit

On February 20, 2009, SB X3 15 was chaptered, creating a credit based on expenditures incurred for film and television productions, which will be allowable to offset California income, franchise or sales and use tax liabilities for taxable years beginning on or after January 1, 2011. This credit is referred to as the "old credit". The amount of credit allocated for distribution was $100 million for each fiscal year starting July 1, 2009. The fiscal year for California is from July 1st to June 30th of the following year.

Subsequently, AB 1839, chaptered on September 18, 2014, expanded the credit. This credit is referred to as the "new credit." The amount available for allocation was increased to $330 million starting fiscal year 2015/2016. The new bill is effective from taxable year beginning January 1, 2016 and will continue until fiscal year 2019/2020.

To claim the credit, qualified taxpayers must first apply to the California Film Commission (CFC). CFC issues credit certificates (certificate) to qualified taxpayers who claim the credit in the taxable year CFC issues the certificate. Under limited circumstances, qualified taxpayers may assign or sell their credit.

A qualified taxpayer may elect to assign a credit to an affiliated corporation, which includes either a corporation:

- That owns, directly or indirectly, 100% of the assignor's voting common stock.
- In which the assignor owns, directly or indirectly, 100% of the voting common stock.
- That is wholly owned by a corporation or individual owning 100% of the voting common stock of the assignor.
- That is a stapled entity as defined in R&TC Section 25105.

Revenue and Taxation Code allows qualified taxpayers to sell a credit attributable to an independent film to an unrelated party.

To qualify as an independent film, the film and producing company must meet the following criteria:

- The film must have a minimum budget of one million dollars ($1,000,000) and a maximum budget of ten million dollars ($10,000,000).
- The film must be produced by a company that is not publicly traded.
- Publicly traded companies cannot directly or indirectly own more than 25% of the company producing the film.

The qualified taxpayer selling the credit shall report the following information to the Franchise Tax Board prior to the sale of the credit: [40]

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- The Social Security number or taxpayer identification number of the unrelated party purchasing the credit.
- The amount of the credit.
- The amount of consideration the qualified taxpayer will receive for sale of the credit.

This nonrefundable credit may not be claimed until it is certain that there is a tax liability against which to claim the credit. Therefore, the first time the credit can be claimed is when the liability is assessed against the taxpayer who earned the credit. For example, the credit can be claimed when the tax return is filed, or the tax liability is assessed in some other manner.

For taxable years beginning on or after January 1, 2016, a new film credit against tax will be allowed. The new tax credit is allocated and certified by the California Film Commission (CFC).

The qualified taxpayer can:

- Offset the credit against income tax liability.
- Sell the credit to an unrelated party (independent films only).
- Assign the credit to an affiliated corporation.
- Apply the credit against qualified sales and use taxes.

The credit amount is:

- 25% of the qualified expenditures attributable to the production of either a television series that relocated to California in its first year of receiving a tax credit allocation or an independent film.
- 20% of the qualified expenditures attributable to the production of a qualified motion picture in California or a television series that relocated to California that is in its second or subsequent years of receiving a tax credit allocation.

Additional credits, not to exceed a total of 5% of qualified expenditures, may be allowed:

- 5% of qualified expenditures relating to music scoring or music track recording attributable to the production of a qualified motion picture in California.
- 5% of qualified expenditures relating to qualified visual effects attributable to the production of a qualified motion picture in California.
- 5% of qualified expenditures relating to original photography outside the “Los Angeles Zone”.

Kiddie Tax

For taxable years beginning on or after January 1, 2010, California conforms to the provision in the Small Business and Work Opportunity Tax Act of 2007 that increased the age of minor children whose unearned income is taxed as if it were the parents’ income to apply to children who are either under the age of 19 or full-time students who are between 19 and 24. California also conformed to the Federal provision permitting a parent an election to include child’s *interest and dividends* between $1,100 and $11,000 on the parent(s) return. The threshold for child’s unearned income is adjusted annually for inflation.

For the 2019 tax year Kiddie Tax is owed if all the following apply: (41)

- The child is under the age of 19 or a student under age 24 at the end of the year.
- The child has investment income taxable by California of more than $2,200
- At least one of the child's parents was alive at the end of the year.
- The child does not have earned income that exceeds over half of their support.

If the child’s unearned income is $1,100 or greater, but includes items other than interest and dividends, or if the taxpayer’s child has earned income (wages or non-employee compensation) in excess of $12,200, then the child must file their own return. A child´s investment income is usually taxed as: (42)

- The first $1,100 of the child´s income is not taxable.
- The next $1,100 is taxed at the child´s rate.
- Any income that is more than $2,200 is taxed at the parental tax rate.

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Investment income is all income other than wages, salaries, professional fees, and other amounts received as pay for work actually done.

Net investment income is investment income reduced by the greater of:

- $2,200.
- $1,100 plus the child's itemized deductions that are directly connected with the production of his or her investment income.

Parental tax is the difference in tax on the parent's income figured with and without the child's net investment income. For certain children, investment income over $2,200 is taxed at the parent's rate if the parent's rate is higher. Use FTB Form 3800 - Tax Computation for Certain Children with Investment Income, to figure the child's tax. If Federal Form 8615 - Tax for Certain Children Who Have Unearned Income, was filed with the child's Federal tax return, enter the name and SSN or ITIN of the same parent who was identified at the top of Federal Form 8615 on FTB Form 3800.

A parent may elect to include on the parent's return the unearned income of a child whose income is more than $1,100 but less than $11,000 and consists solely of interest, dividends, or Alaska Permanent Fund dividends. The child is treated as having no gross income and does not have to file a tax return if the child's parent makes the election. However, the election is not available if estimated tax payments were made in the child's name and taxpayer identification number for the tax year or if the child is subject to backup withholding.

To report the unearned income of a child on the parent's return, FTB Form 3803 - Parents' Election to Report Child's Interest and Dividends (comparable to Federal Form 8814 - Parents' Election To Report Child's Interest and Dividends) must accompany the parent's return.

Tip

The taxpayer is not required to report the same as Federal. For example, if the taxpayer reported Federal Kiddie Tax on the parent's return, they can choose to report it on the child's return for California and vice versa. Schedule CA adjustments would be needed. For example, if the parents elect to report a child's income on the Federal income tax return, but not on the California income tax return, they must be sure to make an adjustment on Schedule CA (540 or 540NR).

Net Operating Loss (NOL) Carryback

For NOLs incurred in taxable years beginning on or after January 1, 2015, the carryback amount shall be 100% of the NOL. Individuals, Estates, and Trusts compute the NOL carryback in Part IV of FTB Form 3805V - Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations - Individuals, Estates, and Trusts. [35]

Tip

Any taxpayer entitled to a carryback period pursuant to Internal Revenue Code (IRC) Section 172(b)(3) may elect to relinquish/waive the entire carryback period with respect to an NOL incurred in the 2013 taxable year. By making the election, the taxpayer is electing to carry an NOL forward instead of carrying it back in the previous two years. To make the election, the taxpayer should check the box in Part I under Section C - Election to Waive Carryback, of FTB Form 3805V - Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations - Individuals, Estates, and Trusts, and attach FTB Form 3805V to the tax return.

California Alternative Minimum Tax (AMT)

The alternative minimum tax, which is in addition to regular tax, is imposed under California and Federal law in an amount equal to the excess (if any) of the tentative minimum tax for the taxable year over regular tax for the taxable year. For California, alternative minimum tax purposes, regular tax is the personal income tax before reduction for any credits against tax.

In 2019, the California alternative minimum tax rate is 7%. For Federal purposes, the alternative minimum tax rate is 26% of the first $194,800 ($97,400, in the case of married individuals filing separately) of a taxpayer's alternative minimum taxable income (AMTI) in excess of the applicable exemption amount and 28% of any additional AMTI in excess of the exemption amount. However, the Federal, but not California, minimum tax rate is lowered to reflect the reduction in the Federal capital gains rate and the reduced rate applied to qualified dividends.

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Alternative Minimum Tax Exemption Amounts

The California and Federal alternative minimum tax is imposed on alternative minimum taxable income minus the exemption amount. For both California and Federal purposes, the exemption amounts are reduced by 25 cents for each $1 that alternative minimum taxable income exceeds the beginning phase-out level, until the exemption is completely phased out.

The 2019 exemption phase-out amounts for California tax purposes are: [36]

Filing Status	Exemption Amount	Phase-out begins at
Married/RDP filing jointly or qualifying widow(er)	$98,330	$368,727
Single and head of household	$73,748	$276,552
Married/RDP filing separately, estates, or trusts	$49,163	$184,365

Table 26 - AMT Exemption Amounts (2019)

The California Alternative Minimum Tax is filed on Schedule P (540) - Alternative Minimum Tax and Credit Limitations - Residents. The taxpayer should complete Schedule P (540) to see if AMT applies to him or her. He or she attaches the Schedule P (540) to Form 540 only if any one of the following apply:

- The taxpayer owes AMT.
- The taxpayer has more than two credits.
- The taxpayer has credits that are reported in Part III, Section A1, Section A2, or Section C.
- The total of Part I is negative and the taxpayer would be liable for AMT without taking those lines into account.
- Schedule P (540), Part I, Alternative Minimum Taxable Income, (AMTI), is more than Part II, Exemption Amount, and the taxpayer has one or more adjustments on Part I.

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