

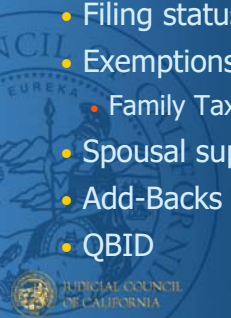
Tax Law 101 for the Child Support Professional


23rd Annual AB 1058 Child Support
Training Conference
August 27–30, 2019



Agenda

- Filing status rules
- Exemptions and credits
 - Family Tax Credit
- Spousal support rules
- Add-Backs
- QBID






Publication 501
Cat. No. 500001

Dependents, Standard Deduction, and Filing Information

For use in preparing
2018 Returns



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What's New

Who must file. In some cases, the amount of income you can receive before you must file a tax return has increased. Table 1 shows the filing requirements for most taxpayers.

Personal exemption suspended. For 2018, you can't claim a personal exemption deduction for yourself, your spouse, or your dependents.

Standard deduction increased. The standard deduction for taxpayers who don't itemize their deductions on Schedule A of Form 1040 is higher for 2018 than it was for 2017. The amount depends on your filing status. You can



Single

- Status determined on 12/31
- Unmarried
- Default status. If you don't qualify for another one



Married filing jointly

- Must be legally married on 12/31
- Can have filed for divorce, but divorce is not final
- Must agree to file jointly



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Married Filing Separately

- Still legally married
- Do not agree to file a joint return



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Head of Household

3-Pronged Test:

- Unmarried or considered unmarried on 12/31
- Pay more than 1/2 cost of keeping a home for 12 months
- Qualifying person lived with you more than half of year



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Qualifying Child

1. Relationship Test
 - Bio child, stepchild, foster child, sibling, half sibling, step sibling, or descendant of one of them
2. Age Test:
 - Under age of 19
 - Under 24 and student
 - Permanently & totally disabled
3. Residency Test
 - Live with you more than half the year
4. Support Test
 - Can't have provided more than 1/2 of own support
5. Joint Return Test
 - Can't file joint return

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Qualifying Child

3. Residency Test
 - Live with you more than half the year

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Qualifying Relative

1. Not a Qualifying Child Test
2. Member of Household or Relationship Test
3. Gross Income Test
4. Support Test



Form 8332 – Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent



8332 Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent

Form No. 8332-001
 Department of Revenue
 Department Fee: \$15
 Effective 01/01/2015

Part I Release of Claim to Exemption for Current Year

I agree not to claim an exemption for _____ for the year ending on _____

Part II Release of Claim to Exemption for Future Years if Custodial, non-Residential Parent on page 21

I agree not to claim an exemption for _____ for the year ending on _____

Part III Revocation of Release of Claim to Exemption for Future Years

I revoke the release of claim to an exemption for _____ for the year ending on _____

General Instructions

What's New

Post-2014 income agreement. If the divorce or separation agreement was entered into after 12/31/14, the custodial parent cannot claim certain credits from the federal or state income tax return (EITC, LHA, and the dependent care credit) for the child.

Release of claim to exemption basis. Custodial parent cannot claim the dependent care credit and the non-refundable credit for child care expenses for the child.

Purpose of Form

This form is to be used by the custodial parent to release or revoke the release of claim to an exemption for the child for the year ending on the date specified on this form.

Release of claim to exemption. This release of claim to exemption is given to the non-custodial parent and is irrevocable. It cannot be changed or amended. It is not a condition to the release of claim to an exemption for the child.

Revocation of release of claim to exemption. This revocation of release of claim to exemption is given to the custodial parent and is irrevocable. It cannot be changed or amended. It is not a condition to the release of claim to an exemption for the child.

Exemption for a Dependent Child

A dependent is either a qualifying child or a qualifying relative. See page 10 of the 2014 Instructions for Form 1040 for more information on the definition of a dependent.

Form 8332 does not allow NCP to:

- File Head of Household Status
- Claim
 - Child Care Credit
 - Earned Income Credit



Hypo #1

Charlie is 13 years old. Mother has an 80% timeshare. Neither party is married.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



Hypo #2a

Juliet is 4 years old. Mother and Father are married, but going through a divorce. Juliet lives 40% of time with Mother.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



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Hypo #2b

Same facts as in Hypo 2b, but parents are not married.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



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Hypo #3a

Mother and Father have two kids, Aliana (17) and Isaac (11). They are going through a divorce. Aliana lives with Mother primarily, and Isaac lives with Father primarily.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



Hypo #3b

Same as 3a, except divorce is final, and Father is remarried with someone else.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



Hypo #4a

Violet is 6 years old and live primarily with Father. Father signs form 8332 to release exemption to Mother. Parties are married, but going through a divorce.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



Hypo #4b

Same as 4, but Father's mother lives with him and is supported by him.

- 1) What is Mother's filing status?
- 2) What is Father's filing status?
- 3) Whose qualifying child?



Credits



Child Tax Credit

- Qualifying Child under age 17
- \$2,000 per child
- Phased in limits



Child Care Credit

- Limited to \$3000 per child (up to \$6000 total)
- Qualifying Child under 13 at the time the child care is provided.
- Must have earned income.
- Can't claim the credit for payments to following care providers:
 - Your spouse
 - A parent of the dependent child
 - A dependent listed on your tax return
 - Your child 18 or younger, even if not listed on return



Child Care Credit

- Qualifying Child under 13 at the time the child care is provided.



What if Form 8332 signed?

- CP has right to claim credit.



Earned Income Tax Credit

- Filer and child must have valid SSN
- Must have earned income and meet income limitations
- Cannot file MFS
- Must have Qualifying Child or be:
 - Between 25 and 65
 - Live in US for more than 1/2 of year, and
 - Not qualify as dependent of another person



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Family Tax Credit

- Dependent who is not eligible for Child Tax Credit
- \$500 per eligible dependent



Hypo #1

Charlie is 13 years old. Mother has an 80% timeshare. Neither party is married.

Who gets what credits?



Hypo #2a

Juliet is 4 years old. Mother and Father are married, but going through a divorce. Juliet lives 40% of time with Mother.

Who gets what credits?



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Hypo #2b

Same facts as in Hypo 2b, but parents are not married.

Who gets what credits?



Hypo #3a

Mother and Father have two kids, Aliana (17) and Isaac (11). They are going through a divorce. Aliana lives with Mother primarily, and Isaac lives with Father primarily.

Who gets what credits?



Hypo #3b

Same as 3a, except divorce is final, and Father is remarried with someone else.

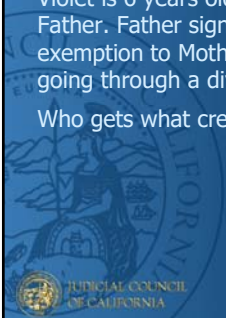
Who gets what credits?



Hypo #4a

Violet is 6 years old and live primarily with Father. Father signs form 8332 to release exemption to Mother. Parties are married, but going through a divorce.

Who gets what credits?



Hypo #4b

Same as 4, but Father's mother lives with him and is supported by him.

Who gets what credits?



Spousal Support Order

Taxable
and Tax
Deductible



January 1,
2019



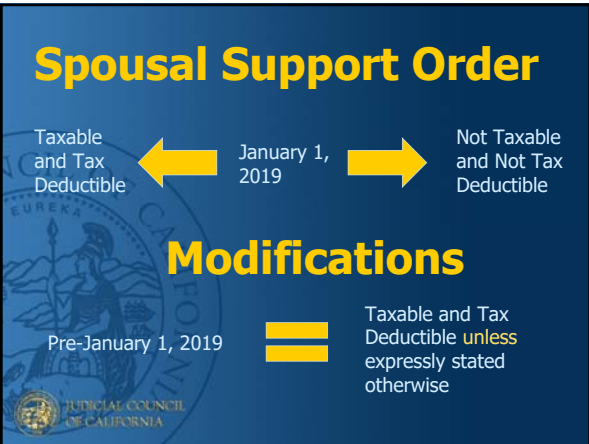
Not Taxable
and Not Tax
Deductible

Modifications

Pre-January 1, 2019



Taxable and Tax
Deductible **unless**
expressly stated
otherwise



Income from Self-Employment Key Factors

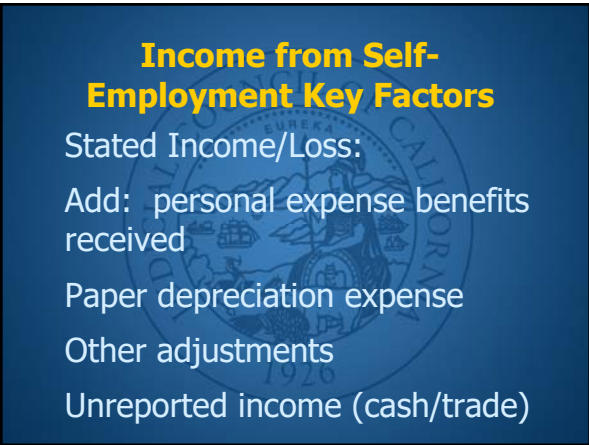
Stated Income/Loss:

Add: personal expense benefits received

Paper depreciation expense

Other adjustments

Unreported income (cash/trade)



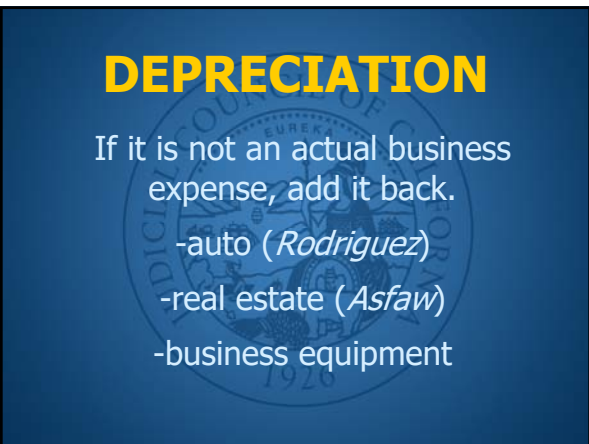
DEPRECIATION

If it is not an actual business expense, add it back.

-auto (*Rodriguez*)

-real estate (*Asfaw*)

-business equipment



RATIONALE

Income tax savings

It is at odds with a child receiving less support when the deduction does not reduce the actual funds available for support.

Business expenses

In general, limit to ones directly related to the day to day conduct of the business.

P&L Exercise

Example 1- Trucking Co.



Additional facts

*rent is for his residence where he has an office

*assume 33% personal use of telephone

Assume I&E shows monthly household expenditures of 4800.

Basic add-backs

Rent

Child support

33% of telephone

-if still in the negative, consider using monthly expenditures or require additional evidence

P&L Exercise

Example 2- Insurance Broker



Additional facts

Assume 33% personal use of car and telephone

Assume insurance is for the business

Assume other business property is rent of outside office

Basic add-backs

Depreciation

33% of both telephone and vehicle costs

Inquiry into travel, business promotions and high office expense and "other" category

P&L Exercise

Example 3- Rental income



Additional facts

Assume 33%
personal use of
vehicle and
telephone

Basic add-backs

Depreciation
% telephone
% vehicle
Inquiry into legal fees, repairs

P&L Exercise

Example 4- Golf Cart Business



Additional facts

Assume 33%
personal use of
vehicle and
telephone

Basic add-backs

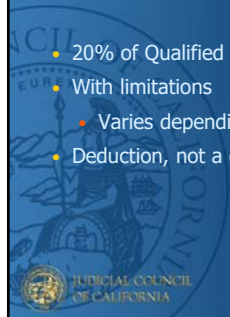
% phone, gas
Inquiry into:
Travel
Credit card expenditures
Meals and entertainment

Paper results:

Monthly incomes:
Trucking: \$-8063.75 mo
Ins broker: \$835.75 mo
Rental prop: \$35. mo
Golf Carts: \$-7611.66 mo

Qualified Business Income Deduction

- 20% of Qualified Business Income
- With limitations
 - Varies depending upon income level
- Deduction, not a credit



Child Support with QBID




Child Support with QBID

Reduced tax liability



Child Support with QBID

Reduced tax liability



↓

More Income available for support



Child Support with QBID

Reduced tax liability



↓

More Income available for support


↓

Increase in child support



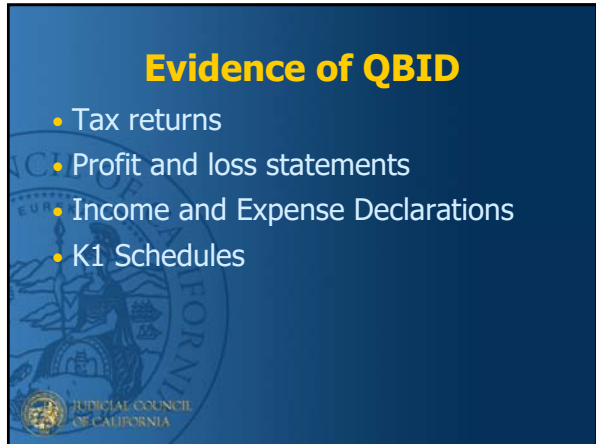
Types of QBI

1. Self-Employment Income
2. Passthrough Entities
 - LLPs, LLCs, Partnerships, S-Corps
3. Trusts/Estates
4. Rental Income*



Evidence of QBID

- Tax returns
- Profit and loss statements
- Income and Expense Declarations
- K1 Schedules



2018 Thresholds and Limitations

Threshold 1

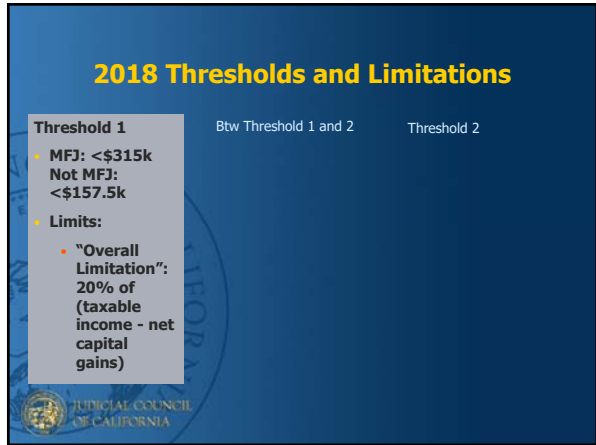
- MFJ: <\$315k
- Not MFJ: <\$157.5k

Limits:

- "Overall Limitation": 20% of (taxable income - net capital gains)

Btw Threshold 1 and 2

Threshold 2



2018 Thresholds and Limitations

Threshold 1

- MFJ: <\$315k
- Not MFJ: <\$157.5k

Limits:

- "Overall Limitation": 20% of (taxable income - net capital gains)

Single Status

Self-Employment Income: \$120,000
Taxable Income: \$100,000
Net Capital Gains: \$10,000

Lesser of:


- a) 20% of \$120,000 = \$24,000
- or
- b) 20% of (\$100,000 - \$10,000) = \$18,000

QBID = \$18,000 per year (\$1,500 per month)



2018 Thresholds and Limitations

<p>Threshold 1</p> <ul style="list-style-type: none"> MFJ: <\$315k Not MFJ: <\$157.5k Limits: <ul style="list-style-type: none"> "Overall Limitation": 20% of (taxable income - net capital gains) 	<p>Btw Threshold 1 and 2</p> <ul style="list-style-type: none"> MFJ: \$315k-415k Not MFJ: \$157.5k-207.5k Limits: <ul style="list-style-type: none"> Overall Limitation Greater of <ul style="list-style-type: none"> 50% of W-2 Wages, or 25% of W-2 Wages + 2.5% of unadjusted basis of qualified property <p>Note: Limit phased-in</p>	<p>Threshold 2</p>
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2018 Thresholds and Limitations

<p>Btw Threshold 1 and 2</p> <ul style="list-style-type: none"> MFJ: \$315k-415k Not MFJ: \$157.5k-207.5k Limits: <ul style="list-style-type: none"> Overall Limitation Greater of <ul style="list-style-type: none"> 50% of W-2 Wages, or 25% of W-2 Wages + 2.5% of unadjusted basis of qualified property <p>Note: Limit phased-in</p>	<p>MFJ Status</p> <p>Net Capital Gains: \$20,000</p> <p>Passthrough Income: \$350,000</p> <p>W2-Wages: \$200,000</p> <p>Taxable Income: \$400,000</p> <p>Unadjusted basis of qualified property: \$500,000</p> <p>Lesser of:</p> <p>a) 20% of \$350,000 = \$70,000</p> <p>or</p> <p>b) 20% of (\$400,000 - \$20,000) = \$76,000</p> <p>or</p> <p>c) the greater of:</p> <p>50% of \$200,000 = \$100,000 (phased-in)</p> <p>or</p> <p>(25% of \$200k) + (2.5% of \$500k) = \$62.5k (phased-in)</p> <p>QBID = \$70,000 per year (\$5,833 per month)</p>	
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2018 Thresholds and Limitations

<p>Threshold 1</p> <ul style="list-style-type: none"> MFJ: <\$315k Not MFJ: <\$157.5k Limits: <ul style="list-style-type: none"> "Overall Limitation": 20% of (taxable income - net capital gains) 	<p>Btw Threshold 1 and 2</p> <ul style="list-style-type: none"> MFJ: \$315k-415k Not MFJ: \$157.5k-207.5k Limits: <ul style="list-style-type: none"> Overall Limitation Greater of <ul style="list-style-type: none"> 50% of W-2 Wages, or 25% of W-2 Wages + 2.5% of unadjusted basis of qualified property <p>Note: Limit phased-in</p>	<p>Threshold 2</p> <ul style="list-style-type: none"> MFJ: >\$415k Not MFJ: >\$207.5k Limits: <ul style="list-style-type: none"> Overall Limitation Greater of <ul style="list-style-type: none"> 50% of W-2 Wages, or 25% of W-2 Wages + 2.5% of unadjusted basis of qualified property
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2018 Thresholds and Limitations

Threshold 2

- MFJ: >\$415k
- Not MFJ: >\$207.5k

Limits:

- Overall Limitation
- Greater of
 - 50% of W-2 Wages, or
 - 25% of W-2 Wages + 2.5% of unadjusted basis of qualified property

MFS Status
 Passthrough Income: \$350,000
 Taxable Income: \$400,000

Net Capital Gains: \$20,000
 W2-Wages: \$60,000
 Unadjusted basis of qualified property: \$0

Lesser of:

- a) 20% of \$350,000 = \$70,000
- or
- b) 20% of (\$400,000 - \$20,000) = \$76,000
- or
- c) the greater of:
 - 50% of \$60,000 = \$30,000
 - or
 - (25% of \$60,000) + (2.5% of \$0) = \$15,000

QBID = \$30,000 per year (\$2,500 per month)



But wait....there's more!

- For top two income levels only:
 - Additional limitations on specified service trade or business income
 - A "specified service trade or business," or
 - Defined in Section 1202(e)(3)(A), without regard to engineering and architecture
 - The trade or business of performing services as an employee.




DEFINITION OF SPECIFIED SERVICE TRADE OR BUSINESS (SSTB) INELIGIBLE FOR SECTION 199A QUALIFIED BUSINESS INCOME (QBI) DEDUCTION

- | | |
|-------------------|---|
| Health | Financial Services |
| Law | Brokerage Services |
| Accounting | Investing & Investment Management |
| Actuarial Science | Trading |
| Performing Arts | Dealing in Securities, Partnerships or Commodities |
| Consulting | Any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners (Celebrity Endorsements/Appearances) |
| Athletics | |

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Calculating QBID



- Step 1 – Calculate Support without QBID
- Step 2 - Place Federally Taxable Income (and any other necessary inputs) into QBID Calculator
- Step 3 - Place QBID result into CS calculation
- Step 4 - Calculate Support with QBID

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Scenario 1

- Self-employed contractor
- \$9,000 per month after expenses
- Averages \$500 in short-term capital gains per month

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Scenario 2

- NCP has private law practice, which is organized as a sole proprietorship, through which she nets about \$6,000 per month.
- NCP's firm employs two assistants. The firm pays out \$60,000 in W-2 wages per year.

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Scenario 2a

- NCP has private law practice, which is organized as a sole proprietorship, through which she nets about \$16,000 per month.
- NCP's firm employs two assistants. The firm pays out \$60,000 in W-2 wages per year.



What about rental income?

"The Treasury Department and the IRS are aware that whether a rental real estate enterprise is a trade or business for purposes of section 199A is the subject of uncertainty for some taxpayers." Notice 2019-07

Proposed Revenue Procedure for taxable years after December 31, 2017.





Guidance:
Treasury Department
SAFE HARBOR PROVISIONS
(see handout)



Scenario 3

- NCP owns 8 rental properties and nets \$8,000 per month in rental income.
- She maintains separate books for rental properties and is actively and regularly involved in upkeep, hiring independent contractors to make improvements as needed.
- NCP is a dentist with a sole proprietorship, making \$14,000 per month net income. She employs 4 staff members, paying out in total \$180,000 in W-2 wages. She also has a qualified property through her business with an unadjusted basis of \$750,000.



Scenario 3a

- Same facts as Scenario 3, except for the following:
 - NCP's sole proprietorship is an engineering firm.