Publication 4491

VITA/TCE **Training Guide**

Volunteer Income Tax Assistance (VITA) / Tax Counseling for the Elderly (TCE)

Volume 10 of 16

2023 RETURNS

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Taxpayer Interview and Tax Law Application

Amanda was relocated to another Air Force base. Here's how a volunteer could help Amanda determine if she had any deductible moving expenses:

Sample Interview

Volunteer Says...	Amanda Responds...
So, you were transferred from Maxwell Air Force Base to Scott Air Force Base last year, right?	Yes, I was reimbursed $400 for travel expenses on the way to Scott Air Force Base.
Did you receive any other allowances?	Yes, I also received a $1,000 dislocation allowance.
Well the reimbursements were	I spent $575 on travel and lodging and

not reported on your W-2. You can only deduct expenses that are larger than your combined reimbursements and allowances. First, let's add all your qualified expenses. How much was your travel and lodging?	another $200 for meals along the way.
Any other expenses?	Yes, I gave a $350 security deposit to my new landlord.
Only the travel and lodging en route can be claimed on Form 3903. The security deposit and meals are not deductible expenses. Your	

reimbursement and dislocation allowances add up to $1,400. Since that's more than your expenses, you don't have anything to deduct. But, you don't have to include any of the excess reimbursement as income, either.	

Summary

This lesson described the types of deductions that members of the Armed Forces can claim as an adjustment to income on Form 1040, Schedule 1.

To gain a better understanding of the tax law, complete the practice returns(s) for your course of study using the Practice Lab on L&LT.

You may not be able to complete the entire exercise if some of the technical issues in the exercise are not covered until later lessons. In these instances, complete as much of the exercise as you can. Come back later to finish the exercise after you cover all the technical topics.

EXERCISE Answers

Answer 1: c. A move by a new enlistee from her home to her first post of duty is considered a PCS.

Answer 2: b. The $1,000 PPM payment should be included as wages. However, nontaxable allowances such as dislocation allowances, temporary lodging allowances and mileage allowances provided by the Armed Forces should not be included as gross income on the service member's tax return, even if they exceed allowable expenses.

Answer 3: c. Because Petty Officer Wharton paid for moving expenses in the year prior to the year of reimbursement, he can claim all of his moving expenses on Form 3903 in either the year he paid or the year

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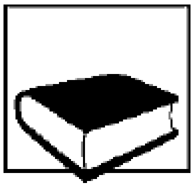
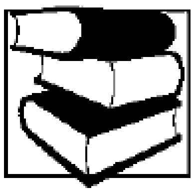
Standard Deduction and Tax Computation

Introduction

This is the first of eight lessons covering computing taxable income, tax, and allowable credits. After completing this lesson on standard deductions and the Itemized Deductions lesson, you will be able to subtract the appropriate deduction, and if the taxpayer qualifies, the qualified business income deduction from the taxpayer’s adjusted gross income (AGI) to figure their taxable income.

Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Determine the standard deduction amount for most taxpayers
- Determine the standard deduction amount for taxpayers claimed as dependents
- Identify how taxable income and income tax are computed and reported
- Determine the amount of qualified business income deduction, if any

What are deductions?

In addition to the deductions covered in the Adjustments lesson, there are additional deductions that are subtractions from a taxpayer's AGI. They reduce the amount of income that is taxed. Most taxpayers have a choice of taking a standard deduction or itemizing their deductions. When taxpayers have a choice, they should use the type of deduction that results in the lower tax. Use the interview techniques and tools discussed in earlier lessons to assist you in determining if the standard deduction will result in the largest possible deduction for the taxpayer.

What is a standard deduction?

A standard deduction for most taxpayers is a set dollar amount based on the taxpayer's filing status. An increased standard deduction is available to taxpayers who are 65 or older or blind. There are limitations on the standard deduction for taxpayers who can be claimed as a dependent on someone else's return. The current year's standard deduction amounts are included in the Volunteer Resource Guide, Tab F, Deductions, and in the Important Changes lesson of this publication. The software will use the applicable standard deduction based on your entries in the software.

James, 44, and Sara, 39, are filing a joint return. Neither is blind, and neither can be claimed as a dependent. They decided not to itemize their deductions. They will use the Married Filing Jointly standard deduction amount. The standard deduction amount can be found in the Standard Deduction Chart in the Volunteer Resource Guide.

What is an itemized deduction?

Itemized deductions allow taxpayers to reduce their taxable income based on specific personal expenses. If the total itemized deductions are greater than the standard deduction, it will result in a lower taxable income and lower tax. In general, taxpayers benefit from itemizing deductions if they have mortgage interest, very large unreimbursed medical or dental expenses when compared to their income, state taxes, or other large expenses such as charitable contributions.

Itemized deductions will be covered in the next lesson.

Who cannot take the standard deduction?

Some taxpayers cannot take the standard deduction and must itemize. During the interview, find out if the taxpayer is:

- Filing as Married Filing Separately and the spouse itemizes regardless of who files first.
- A nonresident or dual-status alien during the year (and not married to a U.S. citizen or resident at the end of the year) – both are out of scope for the VITA/TCE programs
- Filing a return for a short tax year due to a change in the annual accounting period out of scope for the VITA/TCE programs

If any of these situations apply, the taxpayer must itemize personal deductions and complete Schedule A.

A married taxpayer who qualifies to file as Head of Household may claim the standard deduction even though their spouse files as Married Filing Separately and itemizes.

Chase files as Married Filing Separately. Her spouse, Grant, will be itemizing his deductions. Chase cannot use the standard deduction; she will have to itemize her deductions.

The standard deduction is automatically calculated based on entries in the Basic Information section.

How does age or blindness affect the standard deduction?

The standard deduction is higher if the taxpayer or spouse is 65 or older, and if one or both are blind. This information is reported in the check boxes located on Form 1040 or Form 1040-SR. The more check boxes marked, the higher the standard deduction. Be sure to verify the taxpayer’s and spouse’s age and level of blindness as described below.

The Age 65 or older boxes are automatically checked. For software entries, go to the Volunteer Resource Guide, Tab B, Starting a Return and Filing Status.

Sherman is 73 years old and blind. He files as Single using Form 1040. Because Sherman is over 65 and blind, check the appropriate box in the software.

Who qualifies as 65 or older?

Taxpayers are entitled to a higher standard deduction if they are 65 or older at the end of the year. They are considered to be 65 on the day before their 65th birthday. In other words, a person born on January 1 is considered to be 65 on December 31 of the previous year.

The standard deduction for decedents is the same as if they had lived the entire year; however, if taxpayers die before their 65th birthday, the higher standard deduction does not apply.

Armando died on November 24. He would have been 65 if he had reached his birthday on December 12 of that same year. He does not qualify for a higher standard deduction for being 65 because he died before reaching his 65th birthday.

Who qualifies as blind?

Taxpayers are entitled to a higher standard deduction if they are considered blind on the last day of the year and they do not itemize their deductions. A taxpayer who is not totally blind must have a certified statement from an eye doctor (ophthalmologist or optometrist) that:

- The taxpayer cannot see better than 20/200 in the better eye with glasses or contact lenses or
- The field of vision is not more than 20 degrees

If the eye condition is not likely to improve beyond these limits, the statement should include that fact. Taxpayers should keep the statement for their records.

If vision can be corrected beyond those limits only by contact lenses and the taxpayer can only wear the lenses briefly because of pain, infection, or *ulcers, the taxpayer can take the higher standard deduction for blindness.*

What if only one spouse is over 65 or blind?

Taxpayers can take the higher standard deduction if one spouse is 65 or older, or blind, and if:

- The taxpayer files a joint return, or
- The taxpayer files a separate return and can claim an exemption for the spouse because the spouse had no gross income and an exemption for the spouse could not be claimed by another taxpayer

What is the standard deduction based on age or blindness?

The standard deduction for taxpayers who are 65 or older or are blind increases for each box checked for age or blindness. This amount can be found in the Standard Deduction Chart in the Volunteer Resource Guide, Tab F, Deductions.

Tim is 67 and is filing as Single. He is not blind and he cannot be claimed as a dependent on someone else's return. He is able to check one box and his standard deduction is computed using the chart in the Volunteer Resource Guide, Tab F, Deductions.

Kevin and Jane are both 60, and Jane is blind. They are filing as Married Filing Jointly. Neither can be claimed as a dependent on someone else's return. They are entitled to the regular standard deduction for married filing jointly plus an additional amount for being blind.

EXERCISES

Use the Standard Deduction Chart in the Volunteer Resource Guide, Tab F, Deductions to complete the following exercises. Answers are at the end of the lesson summary.

Question 1: Roderick is 64 and blind. Can he claim an additional deduction?

a. Yes

b. No

Question 2: Leticia died in May just before reaching her 65th birthday. Does she qualify as age 65?

a. Yes

b. No

What about individuals who can be claimed as dependents?

The standard deduction is generally lower for an individual who can be claimed as a dependent by another taxpayer. Taxpayers who can be claimed as a dependent must use the Standard Deduction Worksheet for Dependents to determine their standard deduction. The worksheet can be found in the Volunteer Resource Guide, Tab F, Deductions and the dependent's standard deduction can be summarized as:

- $400 plus earned income
- Minimum: $1,150
- Maximum: the regular standard deduction amount
- Plus the additional amount for age 65 or older or blind, if applicable

A dependent's standard deduction will be automatically calculated, as long as the box indicating they can be claimed as a dependent by another taxpayer has been checked. For software entries, go to the Volunteer Resource Guide, Tab B, Starting a Return and Filing Status.

Janet is single, 22, a full-time student, and not blind. Her parents claimed her as a dependent on their current year tax return. She has no itemized deductions, so she will compute her standard deduction using the Standard Deduction Worksheets for Dependents.

How do I determine which deduction is best for the taxpayer?

If taxpayers are not required to itemize, they should take the higher of the standard deduction or the itemized expenses deduction. In general, taxpayers will benefit from itemizing their deductions if they have mortgage interest, state taxes, qualified charitable contributions, or if unreimbursed medical/dental expenses are large compared to their income. During the interview, ask the taxpayer if any of the following were applicable during the tax year:

- Large out-of-pocket medical and dental expenses
- State and local income taxes or state and local general sales tax plus real estate and personal property taxes
- Qualified home mortgage interest
- Gifts to charity
- Certain other miscellaneous deductions

If the taxpayer's expenses qualify, itemizing may be a better choice.

The taxpayer's standard deduction is automatically calculated and displayed on page 1 of the Form 1040 screen. The software automatically selects the deduction method that gives the taxpayer the best result, but only if Schedule A information is entered. For software entries, go to the Volunteer Resource Guide, Tab F, Deductions.

What is the deduction for qualified business income (QBI)?

For taxable years beginning after December 31, 2017 and before January 1, 2026, there is a deduction for "pass through" businesses. Sole proprietors are categorized as "pass through" businesses.

- A sole proprietor will be able to take up to 20% of qualified business income (QBI) as a deduction on the tax return
- REIT dividends (Sec. 199A dividends) are also eligible for the 20% QBI deduction

- The calculations on Schedule C and Schedule SE are not affected by the deduction
- Taxable income is not reduced below zero by the 20% deduction
- The 20% deduction is limited for higher incomes
- The deduction will also be limited for specified service trades or businesses when the applicable threshold is exceeded

For taxable income that does not exceed the applicable threshold amount, the QBI deduction is the lesser of:

- 20% of qualified business income (for example, it is the net profit reported on a Schedule C) plus 20% of qualified REIT (Sec. 199A) dividends or
- 20% of taxable income (equals adjusted gross income minus the applicable standard or itemized deduction) minus net

capital gains and qualified dividends. See Form 1040 instructions for details.

Qualified business income is reduced by the deductible part of the self-employment tax, the self-employment health insurance deduction, and by contributions to certain qualified retirement plans (not traditional IRA deductions). Based on the taxpayer's entries, the software will compute the QBI if applicable.

The tax software computes the QBI deduction and completes Form 8995, Qualified Business Income Deduction Simplified Computation. Taxpayers with pass-through business income from an entity on a Schedule K-1, income over the threshold amount, or who require Form 8995-A, Qualified Business Income Deduction, should be referred to a professional tax preparer. Refer to the Important Changes lesson or to the Volunteer Resource Guide, Tab F for the threshold amounts.

How are taxable income and tax determined?

Tax is based on the amount of taxable income, which is determined by subtracting from the AGI:

- Standard or itemized deductions
- Deduction for qualified business income (QBI)

How is tax computed?

Tax on taxable income is figured using the tax tables or the tax rate schedule for higher incomes. Separate worksheets are used to calculate the tax for taxpayers with certain types of income, such as capital gains and qualifying dividends, or foreign earned income. There are other tax computations listed in the instructions to Form 1040, which are out of scope for the VITA/TCE programs.

The software automatically calculates tax based on previous entries. It is important to enter all income, deduction, and credit information correctly for the tax to be computed accurately.

Please see the Premium Tax Credit lesson contained in this publication for additional information on calculating the Excess Advance Premium Tax Credit Repayment.

What is the tax for certain children who have unearned income (Kiddie Tax)?

For children under age 18 and certain older children, unearned income over a certain amount is taxed using the tax rates applicable to their parent(s). For this purpose, “unearned income” includes all taxable income other than earned income, such as taxable interest, ordinary dividends, capital gains, rents, royalties, etc.

It also includes taxable Social Security benefits, pension and annuity income, taxable scholarship and fellowship grants not reported on Form W-2, unemployment compensation, alimony, and income received as the beneficiary of a trust.

Form 8615, Tax for Certain Children who have Unearned Income, is in scope for Native Americans receiving per capita payments and Alaska residents receiving permanent fund dividends. Form 8814, Parent's Election to Report Child's Interest and Dividends, is in scope for Alaska residents receiving permanent fund dividends. In all

other circumstances, tax returns for children subject to the Kiddie Tax or a parent's election to include their child's income are out of scope for the VITA/TCE programs. The following information is presented for awareness.

The Kiddie Tax might apply if all the following are true:

1. The child's unearned income was more than the ceiling amount.
2. The child is required to file a return for the tax year.
3. The child either:
    - Was under age 18 at the end of the year,
    - Was age 18 at the end of the year and did not have earned income that was more than half of his or her support, or
    - Was a full-time student at least age 19 and under age 24 at the end of the tax year and did not have earned income that was more than half of the child's support.

- At least one of the child's parents was alive at the end of the tax year.
- The child does not file a joint return for the tax year.

Refer to the Volunteer Resource Guide, Tab A, Chart B for the filing requirements for dependents. Refer to Do you have to use Form 8615 to figure your child's tax? in the Volunteer Resource Guide, Tab H, Other Taxes, Payments, and Refundable Credits.

Summary

You should be able to identify those who can take the standard deduction, and how the deduction is affected by their filing status, age, blindness and status as a dependent. All of this will make it easier for you to help taxpayers understand how their deduction is computed and how it affects their tax.

You should also understand that the tax computation is based on taxable income and may be computed using a worksheet if the taxpayer has qualifying dividends, capital gains, or foreign earned income. The tax may be further reduced by tax credits to be covered in an upcoming lesson.

Students who opt to include scholarships in income that exceed the unearned income ceiling amount may be subject to the Kiddie Tax, in which case the return is out of scope.

Taxpayers who are considered sole proprietors may take up to 20% of their qualified business income as a deduction on the return. Taxpayers with qualifying REIT dividends may also be eligible for the QBI deduction.

You are now ready to work with itemized deductions in the next lesson.

What situations are out of scope for the VITA/TCE programs?

The following are out of scope for this lesson. While this list may not be all inclusive, it is provided for your awareness only.

- Pass-through business income shown on any Schedule K-1 (Sec. 199A dividends are in scope)
- Taxable income before the QBI deduction that is greater than the threshold amounts
- Form 8995-A or its schedules
- Forms 8615 or 8814, except for Native Americans or Alaska residents as noted above

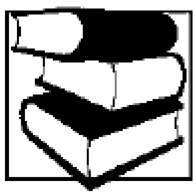
To gain a better understanding of the tax law, complete the practice return(s) for your course of study using the Practice Lab on L&LT.

EXERCISE Answers

Answer 1: a, Yes. Roderick is entitled to an additional standard deduction amount for blindness.

Answer 2: b, No.

Itemized Deductions



Introduction

This lesson will assist you in determining if a taxpayer should itemize deductions. Generally, taxpayers should itemize if their total allowable deductions are higher than the standard deduction amount.

Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Determine if a taxpayer should itemize deductions
- Determine the type of expenses that qualify as itemized deductions
- Accurately report itemized deductions on Schedule A, Itemized Deductions

- Explain the recordkeeping requirements for claiming charitable contributions

What do I need?

- Form 13614-C
- Publication 4012
- Publication 17
- Form 1040
- Schedule A
- Publication 502
- Publication 526
- Publication 936

Optional:

- Publication 529
- Publication 530
- Publication 561

What are itemized deductions?

Itemized deductions are subtractions from a taxpayer's Adjusted Gross Income (AGI) that reduce the amount of income that is taxed. Most taxpayers have a choice of taking a standard deduction or itemizing deductions.

Taxpayers should use the type of deduction that results in the lowest tax.

Who must itemize?

Taxpayers who have a standard deduction of zero should itemize their deductions. Taxpayers who normally fall within this category are:

- Married, filing a separate return, and their spouse is itemizing — regardless of who files first
- Filing a return for a short tax year due to a change in the annual accounting period (out of scope)

- Considered to be nonresident aliens or dual status aliens during the year (and not married to a U.S. citizen or resident at the end of the tax year) (out of scope)

How do I decide if a taxpayer should itemize deductions?

In general, taxpayers who have deductible mortgage interest, state taxes, charitable contributions, or a very large amount of unreimbursed medical/dental expenses compared to their income would benefit from itemizing their deductions.

Use the Interview Tips – Itemized Deductions in the Volunteer Resource Guide, Tab F, Deductions, to determine if itemizing deductions would be more beneficial for the taxpayer. If you think the taxpayer may benefit from itemizing, enter the qualified expenses on Schedule A. The tax software will automatically select the larger of itemized versus standard deduction.

For taxpayers using the Married Filing Separately status, if one spouse itemizes, the other must also itemize (even if their itemized deduction amount is zero). However, a taxpayer using the Head of Household status can use the standard deduction even when their spouse, who is filing married separately, itemizes their deductions.

Itemized deductions include amounts paid for qualified:

- Medical and dental expenses
- Certain taxes paid
- Home mortgage interest
- Gifts to charity
- Casualty and theft losses (only losses derived from federally declared disaster areas are allowed)
- Certain miscellaneous deductions

Casualty and theft losses are outside the scope of the VITA/TCE programs. Refer taxpayers with these losses to a professional tax preparer.

What medical and dental expenses are deductible?

Taxpayers can deduct only the amount of unreimbursed medical and dental expenses that exceeds 7.5% of their Adjusted Gross Income (AGI).

The standard mileage rate allowed for out-of-pocket expenses for a car when used for medical reasons can be found in the Volunteer Resource Guide, Tab F, Deductions. Taxpayers can also deduct parking fees and tolls.

Whose expenses are covered?

Qualified medical and dental expenses paid by the taxpayer during the tax year can be included for:

- The taxpayer
- The taxpayer's spouse
- Dependents claimed at the time the medical services were provided or at the time the expenses were paid
- Individuals who could be the taxpayer's dependent except:
    - They do not meet the gross income test, or
    - They do not meet the joint return test, or
    - The taxpayers, or their spouse if filing jointly, could be claimed as a dependent on someone else's return

If a child of divorced or separated parents is claimed as a dependent on either parent's return, each parent may deduct the medical expenses that they individually paid for the child.

Stewart and Carmen are divorced. Their son, Raymond, lives with Carmen, who claims him as a dependent. Carmen paid for and deducted Raymond's standard medical and dental bills. Stewart deducted the emergency bill he paid when Raymond broke his arm.

What types of expenses are covered?

Refer to the Volunteer Resource Guide, Tab F, or Publication 17 for the medical and dental expenses checklist, and Publication 502, Medical and Dental Expenses, for more information on medical, dental, and other expenses.

Premiums for long-term care insurance are deductible up to a limit amount based on the age of the insured. Refer to the Important Changes lesson in this publication or to the Volunteer Resource Guide, Tab F, Deductions for those limits.

Retired public safety officers cannot include as medical expenses any health or long-term care premiums they elected to have paid with tax-free distributions from their retirement plan.

Some taxpayers may receive reimbursements from their employers, prior employers or insurance companies. Only unreimbursed costs qualify for deduction.

If you and a taxpayer disagree as to whether a particular expense is deductible, discuss the issue with the Site Coordinator. The taxpayer may be correct, but you should not deduct an *expense if you believe it would lead to a false return.*

EXERCISES

Answers are at the end of the lesson summary.

Question 1: Bill and Kathy Ferris file a joint return. They paid the medical and dental bills listed below. The total of Bill and Kathy’s qualified medical expenses is $ __________ .

Medical Expenses	Amount	Deductible?
Unreimbursed doctors’ bills	$500	

Unreimbursed orthodontist bill for braces	$1,200	
Hospital insurance premiums	$300	
Life insurance premiums	$500	
Unreimbursed prescription medicines	$100	
Vitamins	$70	
Hospital bill (before insurance company's	$2,000	

reimbursement of $1,000)		
Smoking-cessation program	$150	
Total	$4,820	

Taxpayers may only deduct unreimbursed medical expenses. They may not deduct medical insurance premiums or expenses paid with pretax dollars, reimbursed by an insurance company, reimbursed by a current or prior employer, or reimbursed through a tax-advantaged account, such as an flexible spending account (FSA) or health savings account (HSA).

For taxpayers who receive the premium tax credit (PTC), only the premiums paid out of pocket by the taxpayer and not covered by the PTC, may be used as a medical expense when itemizing deductions. For example, if the taxpayer's insurance policy premium was $12,000 and they received a PTC of $10,000, they would only be able to deduct the $2,000 premiums paid out of pocket by the taxpayer as a medical expense deduction, subject to the appropriate applicable adjusted gross income threshold for itemized medical expenses.

Taxpayers may also deduct the excess APTC they have to repay on the return and must reduce their deduction for any additional net PTC they claim on the return.

What taxes may be deductible?

Taxpayers can deduct certain taxes if they itemize. To be deductible, the tax must have been imposed on and paid by the taxpayer during the current tax year. Taxes that are deductible include:

- State and local income taxes – This includes withheld taxes, estimated tax payments, or other tax payments (such as a prior year state or local income tax refund that the taxpayer chose to credit to their estimated tax for the following year). Do not include penalties or interest.

- Sales taxes – It may be possible to deduct sales taxes in lieu of state and local income taxes (from the optional sales tax tables or actual sales tax paid). Taxpayers who use the tables may be able to add the state and local general sales taxes paid on any motor vehicle, boat, aircraft, or home construction or improvement to the tax table amounts.

Taxpayers may deduct either sales tax or state and local income tax, but not both.

- Real estate taxes
    - State and local real estate taxes based on the assessed value of the taxpayer’s real property, such as the

taxpayer’s house or land, are deductible.

- Taxes based on other than the assessed value of the property may be deductible in certain circumstances if they are levied:
  - For the general public welfare
  - By a proper taxing authority
  - At a similar rate on owners of all properties in the taxing authority’s jurisdiction
- Real estate taxes, which may be reported on Form 1098, Mortgage Interest Statement, or a similar statement from the mortgage holder, are deductible. If the taxes are not paid through the mortgage company, the taxpayer should have a record of what was paid during the year.

- Some real estate taxes or charges that may be included on the real estate tax bill are not deductible. These include taxes for local benefits and improvements that tend to increase the value of the property, itemized charges for services, transfer taxes, rent increases due to higher real estate taxes, and homeowners' association fees.

Real estate taxes reported on Form 1098 may include nondeductible amounts. Use the interview techniques with taxpayers to determine if nondeductible amounts such as sanitation pickup and water fees are included in their Form 1098. These items should not be included on Schedule A.

- Personal property taxes
  - The state and local personal property taxes paid, but only if the taxes were based on value alone

and were imposed on a yearly basis.

Which taxes are not deductible?

Not all taxes are deductible and some items aren’t actually classified as taxes. Some examples include employment taxes, federal income taxes, and license fees. No deduction is allowed for foreign property taxes unless it relates to a trade or business or for the production of income.

How do I handle taxes that are deductible?

Deductible taxes are reported on Form 1040, Schedule A in the Taxes You Paid section. The aggregate deduction for state or local income (or sales taxes in lieu of income taxes) and state or local property taxes is limited to $10,000 ($5,000 if Married Filing Separately) per return.

State and local income taxes or state and local sales taxes

Include tax withheld, estimated tax payments to a state or local government, and tax payments for an earlier year paid during the current tax year. Do *not* include penalties or interest. Enter both the state and local income taxes and the state and local sales taxes. The software will use the greater amount.

The total deduction for state and local income, sales, and property taxes is limited to a combined, total deduction of $10,000 ($5,000 if Married Filing Separately). Any state and local taxes paid above this amount cannot be deducted as an itemized deduction. Taxes claimed on Schedule C, on Schedule E, or for the production of income on Schedule A are not subject to the limitation.

Foreign income taxes

Generally, income taxes that were paid to a foreign country can be taken as an itemized deduction on Schedule A, or as a credit against U.S. income tax on Form 1040. More information will be provided on this credit in subsequent lessons. You should compare claiming the foreign taxes paid as a nonrefundable credit to taking it as an itemized deduction and use whichever results in the lowest tax. Only the Simplified Limitation Election for the foreign tax credit is in scope for Advanced certification. To be eligible for this election, qualified foreign taxes must be $300 ($600 if MFJ) or less.

See the Taxes chapter in Publication 17 for more information.

Question 2: Which of the following taxes are deductible on Schedule A?

a. Federal income tax

b. State, local, and foreign income tax and real estate tax

c. Tax on alcohol and tobacco

d. Foreign sales tax

Question 3: For a tax to be deductible, a tax must be __. (Select all that apply.)

a. Imposed during the tax year

b. Imposed on the taxpayer

c. Paid during the tax year

d. Paid by the taxpayer

How do I handle interest paid?

Certain types of interest payments qualify as itemized deductions. Home mortgage interest, points (paid as a form of interest), and investment interest can be deducted on

Schedule A. Investment interest is outside the scope of the VITA/TCE programs and taxpayers with investment interest should be referred to a professional tax preparer.

Home Mortgage Interest

Generally, home mortgage interest is any interest paid on a loan, line of credit, or home equity loan on the taxpayer's main home or second home that is secured by the taxpayer's main home or second home, respectively. The deduction for home equity mortgage interest is not allowed unless the loan proceeds were used to build, buy, or substantially improve the taxpayer's qualified residence. The flow chart Is My Home Mortgage Interest Fully Deductible? in Publication 936, Home Mortgage Interest Deduction, will help you determine if interest paid by the taxpayer should be included on Schedule A.

Taxpayers who received a Mortgage Credit Certificate must be referred to professional tax preparer.

Members of the clergy and military can deduct qualified mortgage interest even if they receive a nontaxable housing allowance. Returns for members of the clergy are out of scope.

If a taxpayer refinances their qualified home mortgage increasing the loan to take out cash used for nonqualified purposes, the interest on the qualified home mortgage amount is deductible. See Publication 936 for details.

Generally, the total amount of home mortgage interest paid by a taxpayer is shown on Form 1098. Only taxpayers who are legally liable for the debt can deduct the interest in the year it is paid. Remember that taxpayers may have more than one mortgage or may have refinanced during the year and may have multiple Mortgage Interest Statements.

When the taxpayer does not receive a Form 1098, such as a seller-financed mortgage, additional information is needed to complete Schedule A. See Form 1040 Schedule A instructions.

A taxpayer may be able to deduct interest on a main home ***and*** *a second home. A home can be a house, cooperative apartment, condominium, mobile home, house trailer, or houseboat that has sleeping, cooking, and toilet facilities.*

Any interest (including original issue discount) accrued on a reverse mortgage is not deductible until the loan is paid in full. When paid, interest on a reverse mortgage must satisfy the qualified home mortgage interest criteria to be deductible. See Publication 936 for information on reverse mortgages.

From 1991 through 1998, Alfredo and Cindy Kendall obtained home equity loans totaling $91,000. Alfredo and Cindy used the loans to pay off gambling debts, overdue credit payments, and some medical expenses.

The current balance of Alfredo and Cindy's home equity loan is $72,000. The fair market value of their home is $230,000, and they carry $30,000 of outstanding acquisition debt (the amount used to buy, build, or improve their home).

If Alfredo and Cindy file a joint return, they cannot deduct the interest on their home equity loans because none of the loan proceeds was used to build, buy, or improve the taxpayer's qualified residence. The interest on the acquisition debt is deductible.

What are points?

Points are the charges paid by a borrower and/or seller to a lender to secure a loan. They are also called:

- Loan origination fees (including VA and FHA fees)
- Maximum loan charges
- Premium charges
- Loan discount points
- Prepaid interest

When are points deductible?

Only points paid as a form of interest (for the use of money) can be deducted on Schedule A. Generally, points must be spread over the life of the mortgage. However, if the loan is used to buy or build a taxpayer's main home, the taxpayer may be able to deduct the entire amount in the year paid.

Points paid to refinance a mortgage are generally not deductible in full the year they were paid, unless the points were paid in connection with the improvement of a main home and certain other conditions are met. Beware of certain charges that some lenders call points. Points paid for specific services, such as appraisal fees, preparation fees, VA funding fees or notary fees, are *not* interest and are *not* deductible.

Use the flow chart in Publication 936 to help determine if points are fully deductible.

What types of interest are not deductible?

Interest that *cannot* be deducted includes:

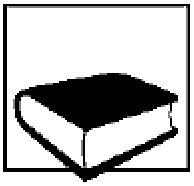
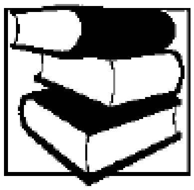
- Interest on car loans where the car is used for nonbusiness purposes
- Other personal loans
- Credit investigation fees

- Loan fees for services needed to get a loan
- Interest on a debt the taxpayer is not legally obligated to pay
- Finance charges for nonbusiness credit card purchases

Question 4: Joe and Angela file a joint return. During the year, they made the interest payments listed below. The total of Joe and Angela's fully deductible interest for the tax year is $ ________________.

Interest Payments	Amount	Deductible?
Qualified interest on their home mortgage, reported on Form 1098	$2,180	

Credit card interest used for personal purchases	$400	
Points paid to refinance their mortgage for a better interest rate (None of the points qualify as interest.)	$1,500	
Interest on a car loan	$2,000	
Total	$6,080	

How do I handle gifts to charity?

A charitable contribution is a donation or gift to a **qualified organization**, which may be deductible if the taxpayer itemizes. Cash, check, and noncash contributions should be reported on Schedule A on either the Gifts by cash or check line or the Other than by cash or check line, respectively. Deductions may be taken for contributions to:

- Organizations that operate exclusively for religious, charitable, educational, scientific, or literary purposes
- Organizations that work to prevent cruelty to children or animals
- Organizations that foster national or international amateur sports competition if they do not provide athletic facilities or equipment
- War veterans' organizations

- Certain nonprofit cemetery companies or corporations
- The United States, or any state, the District of Columbia, a U.S. territory (including Puerto Rico), a political subdivision of a state or U.S. territory, or an Indian tribal government or any of its subdivisions that perform substantial government functions

To be deductible, contributions must be made to a qualifying organization, not an individual.

Qualified organizations are listed in Publication 78, Cumulative List of Organizations. An online version is offered to help taxpayers efficiently search organizations that are eligible to receive tax-deductible charitable contributions. To find out if the organization is a qualified charity, go to ***www.irs.gov***.

Deductible items include:

- Monetary donations
- Dues, fees, and assessments paid to qualified organizations above the value of benefits received
- Fair market value of used clothing, furniture, and other items in good condition
- Cost and upkeep of uniforms that have no general use but must be worn while performing services donated to a charitable organization
- Unreimbursed transportation expenses that relate directly to the services the taxpayer provided for the organization
- Part of a contribution above the fair market value for items received such as merchandise and tickets to charity balls or sporting events

- Transportation expenses, including bus fare, parking fees, tolls, and either the cost of gas and oil or the standard mileage deduction may be taken. Refer to the Volunteer Resource Guide, Tab F for the standard mileage deduction for charitable contributions.

Form 1098-C, Contributions of Motor Vehicles, Boats and Airplanes, is out of scope. Taxpayers who have made these contributions should be referred to a professional tax preparer.

Which gifts are *not* deductible?

Contributions to the following types of organizations are *not* deductible as charitable contributions:

- Business organizations, such as the Chamber of Commerce
- Civic leagues and associations
- Political organizations and candidates

- Social clubs
- Foreign organizations
- Homeowners' associations
- Communist organizations

Amounts that may *not* be deducted as charitable contributions include:

- Cost of raffle, bingo, or lottery tickets
- Tuition
- Value of a person's time or service
- Blood donated to a blood bank or Red Cross
- Car depreciation, insurance, general repairs, or maintenance
- Direct contributions to an individual
- Sickness or burial expenses for members of a fraternal society

- Part of a contribution that benefits the taxpayer, such as the fair market value of a meal eaten at a charity dinner

Susan ran a 10K organized by the Chamber of Commerce to benefit a qualified charitable organization. She paid the race organizers a $30 entry fee and received a "free" T-shirt and pancake breakfast after the race.

Susan did not make a contribution to the qualifying organization. She paid the Chamber of Commerce, which allotted funds to the benefiting organization. Therefore, none of Susan's entry fee is tax deductible. If the race had been organized by the qualifying organization itself, part of her entry fee may have been deductible.

What limits apply to charitable deductions?

Taxpayers whose charitable contributions total more than 20% of their AGI may be able to deduct only a percentage of their contributions and must carry over the remainder to a later tax year. The percentage varies depending on the type of gift and the type of charitable organization. More information on these limitations is available in Publication 526, Charitable Contributions. Individuals affected by limits on charitable deductions should be referred to a professional tax preparer.

What records must the taxpayer keep for charitable contributions?

Taxpayers must keep records to verify the cash and noncash contributions they make during the year. Advise taxpayers that they cannot deduct a cash contribution, regardless of the amount, unless one of the following records of the contribution is kept:

- A credit card statement or a bank record, such as a canceled check, a bank copy of a canceled check, or a bank statement containing the name of the charity, the date, and the amount
- A written communication or receipt from the charity, which must include the name of the charity, date of the contribution, and amount of the contribution

Single monetary contributions of $250 or more

Taxpayers can claim a deduction of $250 or more only if they have a contemporaneous written acknowledgment from the charitable organization showing the amount of any money contributed and whether the organization did or did not provide any goods or services in return for the contribution. During the interview, be sure to review the documentation requirements with the taxpayer and confirm that they have the appropriate documentation.

Out-of-pocket expenses related to donated services

For unreimbursed expenses related to donated services, the taxpayer must have:

- Adequate records of the expenses
- Organization’s written acknowledgment and description of the taxpayer’s services for unreimbursed expenses of more than $250

Only out-of-pocket expenses that are directly related to the donated services can be deducted. The value of time or services donated cannot be deducted. See Publication 526 for the rules applicable to out-of-pocket expenses incurred when rendering services to a qualifying organization.

What records must the taxpayer keep for noncash contribution deductions?

Deductions are not allowed for the charitable contribution of clothing and household items if the items are not in good used condition or better.

Noncash contributions less than $250

For any single contribution of less than $250, the taxpayer must keep:

- A receipt or other written communication from the organization or the taxpayer’s own reliable written records for each donation, showing:
  - Name and address of the organization
  - Date and location of the contribution
  - Reasonably detailed description of the donated property
  - Fair market value of the donated property

If the taxpayer is donating capital gain property or property that was previously depreciated, refer them to a professional tax preparer. See exception below for members of the military.

Noncash contributions of at least $250 but not more than $500

For any single contribution of at least $250 and not more than $500, the taxpayer must have all the documentation described for noncash contributions less than $250. In addition, the organization’s written acknowledgment must state whether the taxpayer received any goods or services in return and a description and good faith estimate of any such items.

Noncash contributions of more than $500

Taxpayers with more than $500 in total noncash contributions must file Form 8283, Noncash Charitable Contribution, and should be referred to a professional tax preparer.

See exception below for members of the military.

Question 5: Julia made the following contributions last year:

- $600 to St. Martin’s Church (The church gave her a letter verifying the amount.)
- $32 to Girl Scouts (not for cookies!)
- $40 to a family whose house burned
- $50 for lottery tickets at a fundraiser
- $100 for playing bingo at her church

The amount that Julia can claim as deductible monetary contributions is $_____________.

Noncash contributions of more than $500?

Noncash charitable contributions of more than $500 but not over $5,000 are in scope for active military taxpayers. In figuring whether the deduction is $500 or more, combine claimed deductions for all similar items of property donated to any qualified organization during the year.

If taxpayers claim a deduction over $500 but not over $5,000 for a noncash charitable contribution, Form 8283 must be completed and taxpayers must have a contemporaneous written acknowledgment (defined earlier).

Form 8283 must include:

- Taxpayer's name and taxpayer identification number,
- The name and address of the qualified organization,
- The date of the charitable contribution, and
- The following information about the contributed property:
    a. A description of the property in sufficient detail under the circumstances (taking into account

the value of the property) for a person not generally familiar with the type of property to understand that the description is of the contributed property;

b. The fair market value of the property on the contribution date and the method used in figuring the fair market value;

c. In the case of real or tangible property, its condition;

d. In the case of tangible personal property, whether the donee has certified it for a use related to the purpose or function constituting the donee's basis for exemption under Section 501 of the Internal Revenue Code or, in the case of a governmental unit, an exclusively public purpose;

e. In the case of securities, the name of the issuer, the type of securities, and whether they were publicly traded as of the date of the contribution;

f. How the taxpayer got the property, for example, by purchase, gift, bequest, inheritance, or exchange;

g. The approximate date the taxpayer got the property or, if created, produced, or manufactured by or for the taxpayer, the approximate date the property was substantially completed; and

h. The cost or other basis, and any adjustments to the basis, of property held less than 12 months and, if available, the cost or other basis of property held 12 months or more. This requirement, however, doesn’t apply to publicly traded securities.

What about casualty and theft losses?

Only casualty losses derived from federally declared disaster areas are deductible. All other losses are not allowed except to the extent of casualty gains. Taxpayers with deductible casualty and theft losses should be referred to a professional tax preparer.

What miscellaneous expenses are deductible?

Examples of miscellaneous itemized deductions include:

- Gambling losses and expenses (through 2025) to the extent of gambling winnings (taxpayers must have a record of their losses)
- Work-related expenses for disabled individuals that enables them to work, such as attendant care services at their workplace

All itemized deductions subject to the 2% of AGI limitation are not allowed through the end of 2025. This includes employee business expenses.

Gambling losses plus gambling expenses in excess of winnings are not deductible. The full amount of winnings must be reported as income and the losses (up to the amount of winnings) can be claimed as an itemized deduction.

Question 6: Philip had the expenses shown below. What is the total of Philip's qualified miscellaneous itemized expenses? $______ .

Expense	Amount	Deductible?
Income tax preparation fee	$100	
Safe deposit box rental (to store bonds)	$75	

Life insurance premiums	$300	
Credit card convenience fee for income tax payment	$70	
Loss on sale of personal home	$1,800	
Investment journals and newsletters	$250	
Investment expenses	$200	
Attorney fees for preparation of a will	$100	
Total	$2,895	

Summary

Medical and Dental Expenses

Unreimbursed medical and dental expenses that exceed 7.5% of the taxpayer’s AGI are deductible; they are reported on lines 1 through 4 of Schedule A.

Qualified medical and dental expenses are those paid during the tax year for the taxpayer, spouse, dependents and certain nondependents.

Taxes

Deductible taxes are reported on Schedule A and include the following:

- State and local income taxes, or state and local general sales taxes
- State or local real estate taxes
- Personal property taxes

These taxes are subject to an aggregate limitation of $10,000 ($5,000 if Married Filing Separately).

Note: Taxes paid as part of a trade or business or for the production of income and foreign income taxes are not subject to the aggregate $10,000 limit.

Interest

Deductible interest is reported on Schedule A.

Generally, the taxpayer receives Form 1098, Mortgage Interest Statement, which shows the total amount of interest paid. To be deductible, the loan proceeds must be used to buy, build or improve the home and the interest must be paid by the taxpayer during the tax year. Only taxpayers who are legally liable for the debt can deduct the interest.

Only points paid as a form of interest (for the use of money) can be deducted on Schedule A. Generally, points must be spread over the life of the mortgage. However, if the loan is used to buy or build a taxpayer's main home, and certain other conditions are met, the taxpayer may be able to deduct the entire amount in the year paid.

Gifts to Charity

Qualified charitable contributions are reported on Schedule A. Taxpayers should be made aware of the documentation requirements that apply to charitable contributions.

The contributions to **qualifying organizations** that taxpayers can deduct include:

- Monetary donations
- Dues, fees, and assessments paid to qualified organizations above the value of benefits received
- Fair market value of used clothing and furniture at the time of donation
- Cost and upkeep of uniforms that have no general use but must be worn while

performing donated services for a charitable organization

- Unreimbursed transportation expenses or out of pocket expenses that relate directly to the services the taxpayer provided for the qualifying organization
- Part of a contribution above the fair market value for items received such as merchandise and tickets to charity balls or sporting events

Taxpayers are required to keep receipts and records of all their contributions.

Miscellaneous Deductions

Only gambling losses and gambling expenses (through 2025) to the extent of gambling winnings and certain other items are in scope as miscellaneous deductions.

What situations are out of scope for the VITA/TCE programs?

The following is out of scope for this lesson. While this list may not be all inclusive, it is provided for your awareness only.

- Casualty and theft losses
- Taxpayers with a Mortgage Credit Certificate
- Investment interest
- Form 1098-C, Contributions of Motor Vehicles, Boats and Airplanes
- Taxpayers affected by limits on charitable deductions
- Taxpayers that file Form 8283 to report noncash contributions of more than $500, except for active Military returns with Military certification
- If the taxpayer is donating property that was previously depreciated

- If the taxpayer is donating capital gain property such as appreciated stock or artwork
- Repayment of income over $3,000. Note there is also a credit that may be better – see Publication 525, Taxable and Nontaxable Income
- Loss or termination of an annuity by a deceased annuitant – see Publication 575, Pension and Annuity Income

To gain a better understanding of the tax law, complete the practice return(s) for your course of study using the Practice Lab on L&LT.

EXERCISE Answers

Answer 1: The total of qualified medical and dental expenses is $3,250, which does not include life insurance premiums, vitamins, or reimbursed hospital expenses.

Answer 2: b. State, local, foreign income tax, and real estate taxes are all deductible on Schedule A.

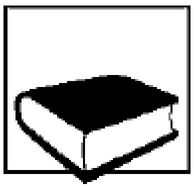
Answer 3: b, c, and d. Taxpayers cannot deduct a tax they did not owe, did not pay, or that they paid during another year. However, the tax may have been imposed in a prior year.

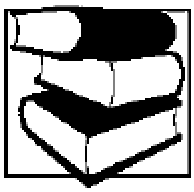
Answer 4: $2,180. The only interest that is fully deductible for the tax year is Joe and Angela’s home mortgage interest. The points they paid to refinance are not deductible because they don’t qualify as interest, and the other interest paid was personal interest and is not deductible.

Answer 5: The amount that Julia can claim as deductible cash contributions is $632 (donations to her church and to the Girl Scouts). Bingo, lottery tickets, and donations to individuals in need are not deductible.

Answer 6: Zero. None of these expenses are qualified miscellaneous itemized deductions.

Credit for Child and Dependent Care Expenses





Introduction

This lesson covers the credit for child and dependent care expenses. Some taxpayers may not be aware of this credit. Your time and effort may result in a lower tax for the taxpayers. Calculate the credit using Form 2441, Child and Dependent Care Expenses.

Don’t confuse this credit with the child tax credit!

Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Determine if a taxpayer is eligible for the credit

- Calculate the amount of the credit

What do I need?

- Form 13614-C
- Publication 4012
- Publication 17
- Form 2441 and instructions

Optional:

- Publication 503
- Form 1040 Instructions

What is the difference between a refundable and a nonrefundable credit?

A nonrefundable credit is a dollar-for-dollar reduction of the tax liability. A nonrefundable credit can only reduce the tax liability to zero. A refundable credit can reduce the tax liability and result in a refund to the taxpayer. The credit discussed in this lesson is a nonrefundable credit.

Omar has a tax liability of $100 before credits. A nonrefundable credit of $150 can reduce the liability to zero, but not produce a refund. A refundable credit of $150 can zero out Omar's tax liability and produce a refund of $50.

The software will calculate these credits, but the correct information must be input. The volunteer tax preparer must make the correct determinations by using the intake and interview sheet and resource materials.

What is the child and dependent care credit?

This credit is available to eligible taxpayers as a portion of their child and dependent care expenses. The credit may be claimed by taxpayers who, in order to work or look for work, pay someone to take care of their qualifying person. A qualifying person is a:

- Qualifying child under age 13
- Spouse who is incapable of self-care
- Dependent who is incapable of self-care

The meaning of "incapable of self-care" is not the same as "permanently and totally disabled." Persons who can't dress, clean, or feed themselves because of physical or mental problems are considered not able to care for themselves. Also, persons who must have constant attention to prevent them from injuring themselves or others are considered not able to care for themselves.

The credit ranges from 20% to 35% of the taxpayer's expenses. The percentage is based on the taxpayer's earned income and adjusted gross income. The amount of the credit cannot be more than the amount of income tax on the return. It can reduce an individual’s tax to $0, but it will not give the taxpayer a refund.

Some taxpayers receive dependent care benefits from their employers, which may also be called “flexible spending accounts” or “reimbursement accounts.” Taxpayers may be able to exclude these benefits from their income. Employer-provided dependent care benefits appear in the taxpayer’s Form W-2, Box 10.

Because the child and dependent care credit is a nonrefundable credit, only taxpayers with taxable income can claim the credit. However, all taxpayers who receive employer-provided dependent care benefits are required to complete Form 2441, Part III to determine if they can exclude all or part of these benefits from their taxable income.

How do I determine if a taxpayer is eligible?

The information gathered from the intake and interview sheet, along with the screening sheet in the Volunteer Resource Guide, Tab G, Nonrefundable Credits, will help you determine the taxpayer's eligibility. Be sure to ask whether the taxpayer has paid for *any* type of dependent care for a spouse or another qualifying person.

The Volunteer Resource Guide screening sheet covers the five eligibility tests the taxpayer must meet to qualify for the credit:

- Qualifying person test
- Earned income test
- Work-related expense test
- Joint return test
- Provider identification test

Keep in mind that the taxpayer must pass all five of the tests to qualify for the credit.

What is the qualifying person test?

The taxpayer's child and dependent care expenses must be for the care of one or more qualifying people. Refer to the Volunteer Resource Guide, Tab G, Nonrefundable Credits, Child and Dependent Care Credit Expenses, to determine who is a qualifying person. Any of the following are qualifying persons:

- A qualifying child who is the taxpayer's dependent and under age 13 when the care was provided. If the child is being claimed as a dependent by the noncustodial parent under the special rules for children of divorced and separated parents, only the custodial parent may treat the child as a qualifying person for this credit.

- Someone who was physically or mentally incapable of self-care who the taxpayer claims as a dependent or for whom the taxpayer could claim, except that:
  - The person had income greater than the current year threshold amount (gross income test for a qualifying relative)
  - The person filed a joint return
  - The taxpayer or spouse, if Married Filing Jointly, could be claimed as a dependent on someone else’s current year tax return
- Spouses who were physically or mentally unable to care for themselves and lived with the taxpayer more than half the year.

Jim paid someone to care for his wife, Janet, so he could work. Janet is physically unable to care for herself. Jim also paid to have someone prepare meals *for their 12-year-old daughter, Jill. Both Janet and Jill are qualifying persons for the credit.*

See the rules for Qualifying Child and the special rules for children of divorced or separated parents or parents who live apart in the Dependents lesson of this publication.

What questions should I ask?

Ask the questions from the screening sheet in the Volunteer Resource Guide, Tab G, Nonrefundable Credits, and the intake and interview sheet. The sample interview shown uses these questions.

Sample Interview

Volunteer Says...	Dorothy Responds...
I see you indicated on your intake sheet that you had child and	Yes, I did.

dependent care expenses.	
You may qualify for the child and dependent care credit. Let me ask you a few questions about that. Which of your dependents received the care?	My daughter.
Now, she is 16 years old, correct?	Yes, but she was diagnosed with a severe mental condition. She just can’t take care of herself.

Even though Dorothy’s daughter is over age 13, she meets the qualifying person test because she cannot care for herself.

Once you’ve determined if the taxpayer had eligible expenses for the child and dependent care credit, confirm that the appropriate box on the intake and interview sheet is checked.

What is the earned income test?

The taxpayer (and spouse, if married filing jointly) must both have earned income during the year. Earned income includes:

- Wages
- Salaries
- Tips
- Other taxable employee compensation
- Net earnings from self-employment
- Strike benefits
- Disability pay reported as wages

Earned income does not include amounts reported as wages that are excluded as foreign earned income on Form 2555, Foreign Earned Income.

Earned income does not include income earned while incarcerated or in a work release program. Refer to the Volunteer Resource Guide, Tab I, Earned Income Credit, Earned Income Table for the list of earned income.

What if spouses are full-time students or are unable to care for themselves?

A taxpayer's spouse is treated as having earned income for any month the spouse is physically or mentally incapable of self-care, or is a full-time student. The spouse's income is considered to be $250 for each month if there is one qualifying person in the home or $500 each month if there are two or more qualifying people. A full- time student is defined as enrolled and attending a school for the number of hours or classes the school considers full time. The spouse must be a full-time student for some part of five calendar months during the year.

If, in the same month, both the taxpayer and the taxpayer's spouse are full-time students or are not able to care for themselves, only one spouse can be considered to have earned income of either $250 for one qualifying person or $500 for two qualifying persons for that month.

What questions should I ask?

Ask the questions from the screening sheet in the Volunteer Resource Guide, Tab G, Nonrefundable Credits and the intake and interview sheet. Here is how a volunteer might interview a taxpayer about the earned income test.

Sample Interview

Volunteer Says...	Dorothy Responds...
I believe you mentioned earlier that you and your husband both work. Is that correct?	Yes.
Did you both work while your daughter was in day care?	Yes and no. My husband just changed careers. He went to school the first half of the year, but he began working full time within a month of finishing his program in July.
So, he was a full-time student for the first six	Yes. Does that disqualify us?

months of the tax year?	
No. That does not disqualify you.	

Dorothy and her husband meet the earned income test because her husband was a full-time student for at least five months and is considered to have earned income for those months.

What is the work-related expense test?

Expenses are considered work-related only if both of the following are true:

- The expenses allow the taxpayer (and spouse, if married filing jointly) to work or look for work and
- The expenses are for a qualifying person's care, and to provide for that person's well-being and protection

For married taxpayers, generally both must work or be looking for work. Taxpayers' spouses are treated as working during any month the spouses were full-time students or were physically or mentally unable to take care of themselves.

There is a limit on the amount of work-related expenses that can be used to figure the credit. The limit is $3,000 for one qualifying person and $6,000 for two or more qualifying persons. This $6,000 limit does not need to be divided equally among them.

If qualified expenses for the previous year were paid in the current tax year, the total credit may be increased. The software will ask for details including provider information and information from the previous year tax return.