

Credits for Families with Children

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Credits vs Deductions

- **Deductions:**
 - Reduce the amount of taxable income dollar for dollar, which reduces the tax liability.
- **Credits:**
 - Reduce the taxpayers tax liability dollar for dollar.

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Types of Credits:

- Non Refundable Credits – cannot reduce the taxpayers liability below zero.
 - Child and Dependent Care Credit
 - Lifetime Learning Credit
 - Retirement Savings Credit
 - Child Tax Credit
 - Other Dependent Credit
 - Credit for the Elderly or Disabled
 - Foreign Tax Credit
 - Adoption Credit
 - Other

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Types of Credits:

- Refundable Credits – can reduce the taxpayers tax liability below zero, and the difference is refunded to the taxpayer.
 - Earned Income Credit
 - Additional Child Tax Credit
 - American Opportunity Tax Credit
 - Premium Tax Credit

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Child & Dependent Care Credit

- To qualify, a taxpayer must meet all of the following:
 - Incur expense while working or looking for work
 - Must have earned income (taxpayer and spouse both must have earned income, if filing MFJ.)
 - Maintained a home for more than half the year for:
 - *A dependent under age 13*
 - *A dependent, or person who could have been a dependent if gross income had been less than \$4,150, who is physically or mentally incapable of self care*
 - *A spouse who is incapable of self care*

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Child & Dependent Care Credit

- To qualify, a taxpayer must meet all of the following:
 - Filed a joint return, if married, unless eligible to file head of household.
 - Paid someone the taxpayer cannot claim as a dependent.

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Child & Dependent Care Credit

- The credit is calculated on the **lesser** of:
 - \$3,000 (\$6,000 for two or more qualifying persons)
 - Amount actually paid to the care provider
 - Taxpayers earned income or
 - Spouses earned income if filing MFJ

Once this amount has been determined the credit is based on the taxpayers AGI. There is no AGI Limit on who can claim the credit, instead, the amount of AGI only determines the credit %. Even hing-income taxpayer can claim the credit.

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Child & Dependent Care Credit

- SPECIAL CONSIDERATIONS:
 - Daycare expenses may increase state refunds (Not Michigan)
 - Spouse is a full-time student or disabled
 - Relative is providing daycare
 - Dependent Care Benefits on W-2, box 10.

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Child & Dependent Care Credit

- Qualifying Expenses:
 - Dependent care center
 - Household services – Include expenses for household services for the care of a qualifying individual. Costs of a maid, housekeeper, babysitter or cook ordinarily qualify if they are at least partly for the well being of and protection of a qualifying individual. The qualifying expense includes the cost incurred to provide meals and lodging for the in home provider

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Child & Dependent Care Credit

- Qualifying Expenses: (cont)
 - School costs – Expenses for a child in nursery school, pre-school or similar program below the level of kindergarten qualify. Costs to attend kindergarten or a higher grad do not qualify, HOWEVER the cost for before or after school care may be for the care of a qualifying individual.
 - Camp – The cost of sending a child to an overnight camp is not a work related expense. The cost of a day camp is a qualifier expense even if it specializes in a particular activity. Summer schools and tutoring programs do not qualify.

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Child & Dependent Care Credit

- Qualifying Expenses: (cont)
 - Special school expenses – Special school expenses may qualify for either a child and dependent care credit or a medical deduction.

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Child Tax Credit

After TCJA, the child tax credit consists of 3 parts:

- Child Tax Credit (non – refundable)
- Additional Child tax Credit (ACTC) (refundable)
- Other Dependent Credit (ODC) (non-refundable)

*ALL 3 PARTS ARE SUBJECT TO
TAX PREPARER DUE DILIGENCE REQUIREMENTS.*

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Child Tax Credit

	<u>2017</u>	<u>2018</u>
Child Tax Credit	\$1,000 / qualifying child	\$2,000 / qualifying child
Additional Child Tax Credit	Up to \$1,000 per qualifying child, if not used to reduce tax liability to zero.	Up to \$1400 per Qualifying child, if not used to reduce tax liability to zero
Other Dependent Credit	N/A	\$500 / qualifying person

*ALL 3 PARTS ARE SUBJECT TO
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Child Tax Credit- Qualifying Child Defined

Child Tax Credit may be worth up to \$2,000 per qualifying child. That's double last year. A qualifying child must meet all of the following:

- Age Test – Child must be under age 17 as of Dec 31.
- Dependency Test – Taxpayer must claim the child as a dependent, with the following tweaks:
 - Relationship test – Child must be related to taxpayer (*son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, or a descendant of any of these individuals.*)

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Child Tax Credit- Qualifying Child Defined

- *AND*
- Residence test – Child must have lived with taxpayer for more than half of the tax year. (Yes there are exceptions!)
- *PLUS*
- SSN Requirement Test – Child must be a US citizen, US National or US resident alien and taxpayer must provide a valid social security number for the child by the tax return due date

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Additional Child Tax Credit

- Available for taxpayers whose earned taxable income exceeds \$2,500.00
- Maximum refundable amount is equal to the lesser of:
 - The remaining child tax credit up to \$1,400. or
 - 15% of the excess of earned income over \$2,500.

•*EXAMPLE: Taxpayer earned income is \$10,000 with zero tax liability, how much does refundable credit does the taxpayer qualify for?*

$$\$10,000 - \$2,500 \times 15\% = \$1,125$$

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OTHER DEPENDENT CREDIT

- Other Dependent Credit (ODC) defined: *\$500 non refundable credit for qualifying dependents, other than qualifying children.*
 - Allows taxpayer to claim a non refundable credit for “other dependents” that do not meet the definition of qualifying child.
 - For purposes of the “other Dependent Credit”
 - 5 Dependency tests still apply
 - No requirement to provide a SSN
 - Must be a US Citizen, National, or resident of U.S.
 - Credit is not allowed for non resident alien children residing in Canada or Mexico even if they qualify as dependents.

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Child Tax Credit Phased Out

- CTC & ODC are limited if MAGI exceeds certain thresholds.
- CTC & ODC are reduced by \$50 of every \$1,000 of fraction over the threshold amount.

<u>Phase Outs</u>	<u>Full Credit</u>	<u>Partial Credit</u>	<u>No Credit</u>
Single HOH QW	0 - \$200,000	\$200,001 - \$240,000	\$240,001
MJF	0 - \$400,000	\$400,001 - \$440,000	\$ 440,001
MFS	0 - \$200,000	\$200,001 - \$240,000	\$ 240,001

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Earned Income Credit (EIC)

- Refundable credit that is treated like a payment such as withheld income tax.
- Taxpayer's may receive a refund even though they never paid any tax or had any withheld.
- Available to both individuals:
 - With qualifying children and
 - Without children

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Earned Income Credit (EIC)

Seven Basic Rules For Taxpayers To Qualify For EIC

- Taxpayer must have earned income.
- AGI must be less than:
 - \$49,194 (\$54,884 for MFJ) if three qualifying children
 - \$45,802 (\$51,492 for MFJ) if two qualifying children,
 - \$40,320 (\$46,010 for MFJ) if one qualifying child, or
 - \$15,270 (\$20,950 for MFJ) if no qualifying child

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Earned Income Credit (EIC)

Seven Basic Rules For Taxpayers To Qualify For EIC

- The taxpayer, spouse and all qualifying child(ren) must have valid SSN by the due date of the tax return. ITINs do not qualify for EIC.
- Filing status cannot be "Married Filing Separately"
- Taxpayer must be US Citizen or Resident Alien all year
- Taxpayer cannot file Form 2555 – Foreign Earned Income Exclusion
- Taxpayer investment income must be less than \$3,500

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Earned Income Credit (EIC)

EIC WITH NO QUALIFYING CHILD

Individuals who do not have a qualifying child may receive the credit if:

- Taxpayer is at least 25 years old and under age 65.
- Taxpayer cannot be a dependent of another person.
- Taxpayer cannot be an EIC qualifying child of another person.
- Taxpayer must have lived in the US more than half of the year.

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Earned Income Credit (EIC)

EIC WITH ONE or MORE QUALIFYING CHILD

Individuals who have one or more qualifying children are eligible if:

- Child meets the:
 1. relationship,
 2. age and
 3. residency tests.
 (i.e. Meets the tests to be a Qualifying Child)
- Qualifying child cannot be used by more than one person to claim the EIC.
- Taxpayer cannot be a qualifying child of another person.

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Earned Income Credit (EIC)

QUALIFYING CHILD TESTS FOR EIC

A QUALIFYING CHILD MUST MEET ALL THREE OF THE FOLLOWING TESTS:

1. Age Test
2. Residency Test
3. Relationship Test

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Earned Income Credit (EIC)

QUALIFYING CHILD TESTS FOR EIC

AGE TEST:

To pass the age test the qualifying child must meet one of the following rules:

- 1) Must be under the age of 19 at the end of the tax year, or
 - 2) Must be a full-time student and under the age of 24 at the end of the year, or
 - 3) Must be permanently and totally disabled. AND
- Child must be younger than the taxpayer.
 - Unless the child is permanently and totally disabled

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Earned Income Credit (EIC)

QUALIFYING CHILD TESTS FOR EIC

RESIDENCY TEST:

To pass the residency test:

- The child must have lived with the taxpayer in the US for more than half the year.

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Earned Income Credit (EIC)

QUALIFYING CHILD TESTS FOR EIC

RELATIONSHIP TEST:

To meet the relationship test:

- The child must have lived with the taxpayer in the US for more than half the year and be the taxpayer's:

Son, Daughter, Stepchild, Fosterchild, Brother, Sister, Half Brother/Sister, Stepbrother, Stepsister or Descendant of any of these.

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Earned Income Credit (EIC)

Earned Income Included for Calculating the EIC

- Wages, salaries, and tips.
- Net earnings from self-employment
- Non-taxable Combat Pay (*optional election to include as EIC income to optimize EIC*)
- Disability Benefits Paid (*prior to reaching minimum retirement age, typically 59 ½ and reported on form 1099-R Distribution code 3*)
- What about social security disability ??

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Earned Income Credit (EIC)

Earned Income Included for Calculating the EIC

- What about social security disability ??
- **What Disability Benefits Qualify as Earned Income for EITC?**
- IRS considers disability retirement benefits as earned income until you reach minimum retirement age. Minimum retirement age is the earliest age you could have received a pension or annuity if you did not have the disability.

After you reach minimum retirement age, IRS considers the payments your pension and **not** earned income.

Benefits such as Social Security Disability Insurance, SSI, or military disability pensions are **not** considered earned income and cannot be used to claim the EITC. You may qualify for the credit only if you, or your spouse, if filing a joint return, have other earned income.

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Earned Income Credit (EIC)

Income NOT Included for Calculating the EIC

- Interest and dividends
- Social Security Benefits
- Unemployment Comp
- Child Support
- Workers Comp benefits
- Welfare benefits
- Pension & Annuities

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