

2021 NATIONAL INCOME TAX WORKBOOK

CHAPTER 8 INDIVIDUAL TAX ISSUES:
PART TWO



LEARNING OBJECTIVES

P. 311

- Earned Income Tax Credit**
 - Understand the rules a taxpayer must satisfy to claim the earned income tax credit (EIC) with or without children
 - Understand the phasein and phaseout properties of the EIC
 - Know the new rules that expand EIC eligibility
- Tax Issues for Ministers**
 - Understand how a minister's income and housing are taxed
- International Tax Issues**
 - Recognize when a US person can claim a foreign tax credit or foreign housing exclusion
 - Understand the tax issues for a non-US person with US real estate rental income
 - Apply the tax laws that characterize the gain on currency exchanges
 - Understand how tax treaties and international social security agreements override or modify the Internal Revenue Code

EARNED INCOME TAX CREDIT ELIGIBILITY

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All taxpayers claiming the earned income tax credit (EIC) must:

1. Have an AGI below the phaseout limit for 2021
2. Have a valid SSN
3. Not be filing as MFS (with a limited exception)
4. Be a US citizen or resident alien for the entire tax year
5. Not file Form 2555, Foreign Earned Income, or Form 2555-EZ, Foreign Earned Income Exclusion
6. Have investment income of \$10,000 or less, and
7. Have earned income

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EIC 2021 AGI LIMITATIONS

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Number of Qualifying Children	AGI Limitation for 2021
3 or more	\$51,464 (\$57,414 for MFJ)
2	\$47,915 (\$53,865 for MFJ)
1	\$42,158 (\$48,108 for MFJ)
0	\$21,430 (\$27,380 for MFJ)

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EIC RULES

PP. 313-314

Valid SSN

- Not an ITIN
- Must be issued by due date of return, including extensions
- Child must have SSN also

MFS – may be considered unmarried (similar to HOH exclusions)

US citizen or resident alien – OK if nonresident filing MFJ w/citizen or resident

Can't claim foreign earned income exclusion on Form 2555 or Form 2555-EZ

Investment income limit \$10K – see Figure 8.1

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WHAT IS EARNED INCOME?

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Earned Income includes:

- Wages, salaries, tips, taxable employee pay
- Net earnings from self-employment
- Gross income received as a statutory employee

Earned Income does not include:

- Interest and dividends
- Pensions and annuities
- Social security and railroad retirement benefits
- Alimony and child support
- Welfare benefits
- Worker's comp and unemployment
- Veteran's benefits

Practitioner Note - Minister's Housing

The rental value of a home or a housing allowance provided to a minister is included in earned income for the EIC

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CLAIMING THE EIC **WITH NO QUALIFYING CHILD** P. 315

Four additional rules:

1. AGE - must be at least 19 years old
 - a) Specified student – age 24
 - b) Qualified former foster youth- age 18
 - c) Qualified homeless youth- age 18
2. NOT A DEPENDENT
3. NOT A QUALIFYING CHILD
4. RESIDENCE in US for more than one-half of the year
Special rules apply to military personnel

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CLAIMING THE EIC **WITH A QUALIFYING CHILD** PP. 316-317

The qualifying child must meet the following tests:

1. Relationship – see the list
2. Age
 - Under age 19 at the end of 2021 (24 for student)
 - Any age if permanently and totally disabled
3. Residency - Must have lived in US with taxpayer for more than one-half the year
4. Joint return – only to claim a refund of income
5. Cannot be claimed by more than one person
6. Not qualifying child of another

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CLAIMING THE EIC

PP. 317-319

Can use 2019 income to calculate 2021

Example 8.1 Lucy is HoH w/ 2 children. 2019 income was higher. Uses EIC tables. 2019 income results in higher credit. Reports on Schedule EIC.

Cross-Reference – Due Diligence

HoH, EIC, CTC, ACTC, AOTC

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TAX ISSUES FOR MINISTERS P. 320

A minister could be a priest, rabbi, or any other ordained, commissioned, or licensed member of a religious order who provides ministerial services. The terms minister and church are not specific to any particular religion.

Income vs. Gifts to Ministers

Example 8.2 Payment to a Minister
Rev. Gomez is a visiting minister. "Love offering" is compensation for her services and must be included in taxable income.

Example 8.3 Gift to a Minister
Rev. Greenburg retired. Special offering to thank her for her years of service is a gift.

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TAX ISSUES FOR MINISTERS PP. 321-323

Tax Withholding	SE Tax	Housing Exclusion
<ul style="list-style-type: none"> A minister's salary is not subject to federal tax withholding Duly ordained Payment for ministerial services 	<ul style="list-style-type: none"> SE earnings SECA not FICA Claim exemption on Form 4361 	<ul style="list-style-type: none"> Exclude housing allowance for income tax purposes, but must include in income for SE tax purposes

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HOUSING EXCLUSION PP. 322-323

Excluded amount is lesser of

- Amount actually used
- Designated allowance
- Fair rental value

For housing provided, exclude fair rental value (not more than reasonable pay)

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HOUSING EXCLUSION

PP. 323-324

REPORT ON SCHEDULE SE – excess allowance is income

Example 8.6 Rabbi Bitran gets a \$24,000 housing allowance, but fair rental value is only \$22,000. Includes excess \$2,000 in gross income.

Example 8.7 Rabbi Allen gets use of home. Exclude if reasonable compensation. Exclude housing allowance paid in retirement

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HOUSING EXCLUSION - REPORTING

PP. 324-326

Example 8.8 Pastor Allen \$22,000 salary and SS equivalent [less 403(b) deferral] reported in Box 1 Form W-2, housing allowance in Box 14

Schedule SE also includes housing allowance and SE income

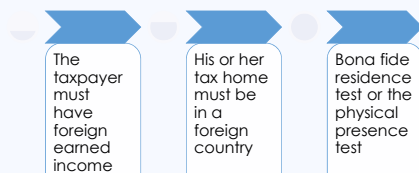
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FOREIGN EARNED INCOME EXCLUSION

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FOREIGN EARNED INCOME

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Foreign Earned Income Includes

1. Wages, salaries, and professional fees
2. Non-cash income (e.g., employer-provided vehicle)

Foreign Earned Income Does Not Include

1. Distribution of E&P
2. Excluded value of meals and lodging
3. Pension or annuity payments, including social security benefits
4. US government employee pay
5. Beneficiary income from a non-exempt trust or certain annuities
6. Disallowed international moving costs that are included in income
7. Payments received the next year

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TAX HOME

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Location of the taxpayer's regular or principal place of business, employment, or post of duty

If a taxpayer does not have a regular or main place of business due to the nature of his or her business, the tax home is the taxpayer's regular place of abode

Temporary presence in US/maintenance of dwelling in US does not necessarily mean US is abode

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FOREIGN EARNED INCOME EXCLUSION

P. 328-330

Bona Fide Residence Test

- Bona fide resident of a foreign country for an uninterrupted period which included an entire tax year
- Look at intention or purpose of trip and nature and length of stay abroad
- Reported on Form 2555, Part II

Physical Presence Test

- Physically present in a foreign country for 330 full days (12 AM – 12AM) during a period of 12 consecutive months
- Qualifying days do not have to be consecutive
- Reported on Form 2555, Part III

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CALCULATING THE EXCLUSION

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The amount of the foreign earned income exclusion is the lesser of:

1. The limit on the excludable amount, or
2. Foreign earned income for the tax year minus the foreign housing exclusion

For 2021, the foreign earned income exclusion is up to \$108,700 for each qualifying person

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CLAIMING THE EXCLUSION

P. 331

- Form 2555 Foreign Earned Income or Form 2555-EZ Foreign Earned Income Exclusion
- Form 673 Statement for Claiming Exemption From Withholding on Foreign Earned Income Eligible for the Exclusion(s)
 - Used by US taxpayer who is working abroad to request reduced withholding

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FOREIGN TAX CREDIT

PP. 331- 332

Prevent double taxation applies to tax on foreign income that is also subject to US tax

Eligible taxes paid to a foreign country:

- Income tax
- War profits tax
- Excess profits tax

Claim on Form 1116

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FOREIGN TAX CREDIT P. 332

Practitioner Note - Tax Treaties
Some tax treaties specifically define which taxes qualify for foreign tax credit treatment. US citizens living in certain treaty countries may be able to take an additional credit for foreign tax imposed on certain US income. Review the tax treaty.

Practitioner Note - Foreign Source Qualified Dividends and Gains
If the taxpayer received foreign sourced qualified dividends and/or capital gains (including long term capital gains, unrecaptured section 1250 gain, and/or section 1231 gains) that are taxed in the US at a reduced tax rate, the taxpayer must make an adjustment on Form 1116.

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FOREIGN TAX CREDIT- CLAIMING THE CREDIT P. 333

A taxpayer may be exempt from the foreign tax credit limit and can claim the credit without filing Form 1116 if :

All foreign source gross income for the year is passive category income	All income and any foreign taxes paid are reported on a payee statement	Qualified foreign taxes are not more than \$300 (or \$600 MFJ)
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Cross-Reference - Net Investment Income Tax
No offset of the net investment income tax (NIIT) with a credit for foreign taxes paid.

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FOREIGN CURRENCY AND EXCHANGES P. 333

EXCHANGE RATE -
Generally, use prevailing exchange rate when received, paid, or accrued
The IRS has no official exchange rate
It generally accepts any posted exchange rate that is consistently used

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FOREIGN CURRENCY AND EXCHANGES

PP. 333-334

Example 8.10 Glenda and Scott report the sale of a vacation home in US dollars as of the date of sale.

Foreign currency exchange gain or loss is realized due to a change in exchange rates between the booking date and the payment date.

- Example 8.11 US vendor sends a \$1,000 invoice.
- Using the exchange rate at the time the invoice was accrued, the invoice was \$1,100. - Disagree with this, it should be the same as when the invoice was sent.
 - The customer paid the invoice when the exchange rate was \$1,100.
 - The resulting \$100 gain is ordinary income.

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FOREIGN OWNERS OF US RENTAL PROPERTIES

P. 335

Fixed or determinable annual or periodical (FDAP) income

- passive investment income
 - Taxed at 30% rate
 - PAYER required to withholding 30% and remit to IRS
- Effectively connect income (ECI)
- if foreign person is engagement in a trade or business or elects to treat as ECI
 - Taxed at graduated rates on a net basis
 - Must provide form W-8 ECI Certification by payee to payor

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ECI

PP. 335 - 336

Form W-8ECI to certify rental income is includable in gross income

If no trade or business (FDAP income) and all tax withheld at the source, no return is required

If rental income is ECI, must file annual return and pay tax on net

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TAX TREATIES

PP. 336 - 337

Intended to reduce double taxation, treaties change the general rules and are generally reciprocal

Treaties apply to
Residents of foreign countries that receive income from US sources and
Non-resident aliens that receive US income

Most follow model rules

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INTERNATIONAL SOCIAL SECURITY AGREEMENTS

PP. 337 -338

Eliminate Double Coverage

- If work covered under 2 SS systems

Self Employment Rules

- Coverage is assigned to the worker's country of residence

Certificates of Coverage

- Document exemption by obtaining certificate from country that will cover them

Totalization Benefits

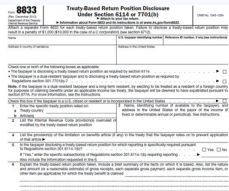
- Partial US or foreign benefits based on combined coverage credits from both countries

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TREATY BASED RETURN POSITION DISCLOSURES

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- File Form 8833 to explain why social security and Medicare taxes are not being paid
- To disclose any other treaty-based position required to be disclosed
- Penalties for failure to disclose



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QUESTIONS?

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