**VITA BASIC TRAINING ANSWER**

**OVERVIEW OF FEDERAL TAXATION**

**EXAMPLE 1:** Sheldon Cooper’s filing status is single with no dependents. In 2016, he had salary income of $70,000 and municipal bond interest income of $300. He made a $500 contribution to IRA, paid property taxes of $ 1,000, made a charitable contribution of $900, and paid state income tax of $8,000.

1. What is his taxable income for the year 2016?

*Municipal bond interest is not taxable so it is excluded from gross income. Contribution to IRA is a “for” AGI deduction, therefore his AGI is:*

|  |  |
| --- | --- |
| *Salary Income* | *$ 70,000* |
| *Minus: Contribution to IRA* | *$ 500* |
| *AGI* | *$ 69,500* |

*Property taxes paid, charitable contribution, and state income tax paid are all itemized deductions. Therefore, his itemized deduction is:*

|  |  |
| --- | --- |
| *Property Taxes Paid* | *$ 1,000* |
| *Plus: Charitable Contribution* | *$ 900* |
| *Plus: State Income Tax* | *$ 8,000* |
| *Total Itemized Deduction* | *$ 9,900* |

*$9,900 > $6,300 (Standard deduction for single person)*

*Therefore, he will choose to use itemized deduction instead of standard deduction, and his taxable income is:*



1. Suppose state income tax paid is $2,000, what’s his taxable income for 2016?

*His itemized deduction will now become:*

|  |  |
| --- | --- |
| *Property Taxes Paid* | *$ 1,000* |
| *Plus: Charitable Contribution* | *$ 900* |
| *Plus: State Income Tax* | *$ 2,000* |
| *Total Itemized Deduction* | *$ 3,900* |

*$3,900 < $6,300 (Standard deduction for single)*

*Therefore, he will choose to use standard deduction instead of itemized deduction. His taxable income will become:*



**EXAMPLE 2:** Michael and Stacey are married with one child from Michael’s previous marriage. In August *2015*, Michael went to get a beer and never returned. The child continues to live in Stacey’s home.Michael did not return for the whole year of 2016.

1. What is Stacey’s filling status for 2015?

*This example is testing on abandoned spouse rule. In 2015, Michael only left home for 4 months. Therefore, Stacey does not qualify for Head of Household rates. Therefore, she can only file Married-Separate. She cannot file married joint as she cannot find him to sign the return. She cannot file single or HofH as she is married.*

1. What is Stacey’s filling status for 2016?

*Head of Household because Michael was not home for the last six months of the year.*

**EXAMPLE 3:** John and Jane are married with a 3-year-old son. At 11:59 pm on December 31, 2016, Jane gives birth to a daughter. How many exemptions do they get?

*Four – husband, wife, son, and the newborn daughter*

*Newborn daughter is a qualifying child because of rule exception to newborns*

**EXAMPLE 4:** Determine if the following individuals are dependents (assume that the support test is met for all of them and that they all are US citizens) and if they qualify for the child credit.

* 1. Uncle John who has income from City of St. Louis bonds of $100,000. There is a particular provision in the Internal Revenue Code which exempts this income.

*Yes – he is a qualifying relative and he has gross income of zero as municipal bonds are excluded.*

*No child credit.*

* 1. Uncle Bob who has income from renting an apartment of $4,500 and rental expenses of $2,000.

*No, Bob has too much gross income to be a Qualifying Relative.*

*No child credit.*

* 1. Cousin Julie who lives with the taxpayer and has no income.

*Yes (qualifying relative) - although not a relative she is a member of the household.*

*No child credit.*

* 1. Peter, the taxpayer’s son, who is 20, a full-time student and has gross income of $5,000. Peter lives with the taxpayer.

*Yes - qualifying child.*

*No child credit – too old. Is there an income limit? No.*

* 1. Same as 4, except Peter is 25.

*No, Peter is too old to be a Qualifying Child and has too much income to be a Qualifying Relative.*

*No child credit - too old.*

* 1. Katie, the taxpayer’s granddaughter, who is 12 and has no income. Katie lives with the taxpayer

*Yes – qualified child.*

*Yes for child credit.*

* 1. Allison, the taxpayer’s child, who is 25 and has no income.

*Yes- she is a qualified relative.*

*No for child credit – too old.*

**EXAMPLE 5:** Determine Judy’s filing status and how many exemptions she gets for each of the following years:

2013—She is married to Jeff and has a 5-year-old child

*Married – Joint with three exemptions (Judy, Jeff, and child)*

2014—Jeff dies in April 2014; she continues to maintain the support for the child

*Married – Joint with three exemptions (Judy, Jeff, and child)*

2015—She continues to provide support for her child

*Married – Joint (Surviving Spouse) with two exemptions (Judy and child)*

2016—She continues to provide support for her child

*Married – Joint (Surviving Spouse) with two exemptions (Judy and child)*

2017—She continues to provide support for her child

*Head of Household with two exemptions (Judy and child)*

**EXAMPLE 6:** Adam and Whitney are married. They have one child, Ellie who is 7 years old. In 2015 they get a divorce. The divorce papers are silent as to who gets to claim Ellie as a dependent.

1. Whitney is Ellie’s custodian. Who gets to decide who claims Ellie as a dependent?

*Whitney since she is the custodian.*

1. Let’s suppose Whitney claims Ellie. What is her filing status and how many exemptions does she get?

*Head of Household and two exemptions – one for herself and one for Ellie.*

1. Whitney signed papers saying that Adam can claim Ellie as a dependent. Whitney still is Ellie’s custodian. What’s Adam’s filing status and how many exemptions does he get?

*Adam still has the filing status single because Ellie doesn’t live with him. However, he can now claim two exemptions since Whitney signed over that right to Adam.*