Section 3: Deductions and Credits

3.2 Credits

1. Child and Dependent Care Credit

The credit provides tax relief to taxpayers so that they can be employed.

Child and Dependent Care Credit Amount of Credit and Reductions

- Expenses may not exceed $ 3,000 ($6,000 if more than one qualified individual)

  Reductions:

  - Credit amount is 35% of qualified expense
  - Percentage is reduced as AGI exceeds $15,000, but never below 20%
  - 35% - (1% X (AGI - $15,000/$2,000)
  - 20-percent minimum credit limit is reached when the taxpayer's adjusted gross income exceeds $43,000

Child and Dependent Care Credit Qualifications

Two qualifying conditions must be met:

- Expenses must be incurred so that taxpayer can be employed
- Expenses must be for the care of qualified individuals

Qualified individuals are

- Dependents younger than 13 years old, or
- A dependent or spouse who is physically or mentally incapacitated

Section 3 Deductions and Credits

3.2 Credits

2. Child Tax and Additional Child Tax Credit

Child Tax Credit

This is a non-refundable $ 2000 credit for each qualifying child *who is under age 17 and $500 per qualifying dependent.*

The credit will be refundable up to $1,400 subject to phased-outs. The phaseouts are not indexed for inflation and will begin with modified adjusted gross income of more than $400,00 and $200,000 for all others

The child credit may be refundable with one or two children. The refund amount = 15% (Earned Income - $2,500) with three or more children

- Greater of 15% (Earned Income – $2,500 or
- Social Security Tax paid – Earned Income Credit
- The Refunded amount does not exceed the tax liability

Child Tax Credit

A qualifying child for purposes of the child tax credit is a child who:

- Is your son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, half brother, half sister, or a descendant of any of them (for example, your grandchild, niece, or nephew),
- Was under age 17 at the end of 2019,
- Did not provide over half of his or her own support for 2019

Child Tax Credit

A qualifying child is also is a child who:

- Lived with you for more than half of 2019
- Is claimed as a dependent on your return,
- Does not file a joint return for the year (or files it only to claim a refund of withheld income tax or estimated tax paid), and
- Was a U.S. citizen, a U.S. national, or a U.S. resident alien.

Additional Child Tax Credit

This credit is for certain individuals who get less than the full amount of the child tax credit. The additional child tax credit may result in a refund even if you do not owe any tax.

Contributions to Heath Care Plans

The annual dollar limit on employee contributions to employer-sponsored healthcare flexible spending arrangements (FSA) rises to $2,700 for 20119, up $ 2,650 for 2018. Under the small business health care tax credit:

- Employers must have fewer than 25 full-time employees
- The employer can pay at least 50% of the full-time employees’ premium cost.
- Employers can offer SHOP coverage to all full-time employees whose average annual wages in excess of $ 50,000 for tax year 2019.

Section 3: Deductions and Credits

3.2 Credits

3. Education Credits

Higher Education Credits

There are two credits

- American Opportunity Tax Credit (formerly known as the Hope Scholarship credit)
- Lifetime Learning Credit

One credit can be claimed for one qualifying student only. To be eligible a student:

- Must be enrolled at least one semester
- Must be enrolled at least half-time

Higher Education Credits Qualifying Expenses

Expenses must be for higher education of taxpayer, spouse, or dependent

- For **American Opportunity Tax Credit**
  - Tuition, related fees, and course materials
- For **Lifetime Learning Credit**
  - Tuition and related fees only

The credit is reduced by the amount of any scholarship or fellowship received

Lifetime Learning Credit

- Maximum non-refundable $2,000 credit 20% of the first $10,000 of qualifying expenses
- Only one credit per return (regardless of number of students in household)
- Expenses can be for any course work to acquire or improve skills
- Phased out for AGI greater than
  - $116,000 if MFJ
  - $58,000 if other
  - Possible credit x [1 - {(AGI - phase-out) / 20,000}]

American Opportunity Tax Credit

- Maximum non-refundable $2,500 credit 100% of the first $2,000, + 25% of the second $2,000
- May be claimed by student or qualifying taxpayer
- Separate credit for each student
- Limitations
  - Available for first four years of post-secondary education
  - Phased-out for AGI greater than
    - $ 193,000- $203,000 for MFJ
    - $ 122,000-$ 137,000 for all others
    - Possible credit x [1 - {(AGI - phase-out) / 20,000}]

Section 3: Deductions and Credits

3.2 Credits

4. Foreign Tax Credit

Foreign Tax Credit

US taxpayers claimed over $90 billion of foreign tax credits on US individual and corporate tax returns. Foreign tax credits allow US taxpayers to avoid or reduce double taxation. You may choose to take a deduction for foreign taxes paid instead of choosing a credit. In most cases, it is to your advantage to take foreign income taxes as a tax credit.

Mitigation of Double Tax. The purpose of the foreign tax credit is to mitigate double taxation, since income of a U.S. taxpayer earned in a foreign country is subject to both U.S. and foreign taxes.

a. Worldwide income. Double taxation results because the U.S. taxes worldwide income of its citizens and residents. Many other countries follow the territorial approach and only tax income derived from within the country.

b. Exclusion versus credit. U.S. persons working abroad (known as expatriates) may prefer to choose the § 911 exclusion instead of the foreign tax credit.

Foreign Tax Credit

(1)This could be the case for the first $105,900 of foreign earned income in 2019.

c. Credit versus deduction. As an alternative, a taxpayer may claim a deduction instead of a credit.

Qualifying Taxes. Only foreign income taxes qualify for the foreign tax credit. Other types of taxes (e.g., value added tax, severance, property), however, might qualify as deductions under § 164.

Concept of Overall Limitation.

a. In working with the overall limitation, several observations are in order.

(1) Taxable income of an individual is determined without any reduction for personal or dependency exemptions.

(2) The premium is on maximizing foreign source income (the numerator of the fraction).

Foreign Tax Credit

(3) Unused foreign tax credits may be carried back one year and forward ten years.

b. The overall limitation is calculated as follows:

Foreign-source taxable income X U.S. tax before FTC

Worldwide taxable income

Section 3 Deductions and Credits

Part 3.2 Credits

5. Earned Income tax Credit

Earned Income Credit

- Earned income credit provides tax relief to low-income taxpayers
- Credit is refundable
- Taxpayer may receive a refund if the credit exceeds the tax liability

Earned Income Credit Eligibility Requirements

The taxpayer or spouse:

- Must live more than half the year in the U.S.
- Must be older than 24 and younger than 65
- Cannot be a dependent of another
- For 2019 There are certain limits and AGI phase-out amounts.
- Married taxpayers must file jointly
- The credit amounts for qualifying children are $ 6,557 for three children, $ 5,828 for two children, $ 3,536 for one child and $ 529 with no children.

Earned Income Credit Amount of Credit

Amount depends on:

- Taxpayer's *earned income*
- Phased-out after maximum limit is reached
- Number of qualifying children living in taxpayer's home
  - Child must be under 19 years old (24 if full-time student)
  - Must be a natural, step, or foster child and reside with taxpayer more than half of the year
  - Amount is determined using an IRS table

Section 3: Deductions and Credits

3.2 Credits

6. Retirement Saving Contribution Credit

Retirement Saving Contribution Credit

The tax credit for Qualified Retirement Savings is available if taxpayers make eligible contributions to an IRA or employer-sponsored retirement plan.

The credit can be taken if you're:

- Age 18 or older;
- Not a full-time student; and
- Not claimed as a dependent on another person's return.

Retirement Saving Contribution Credit

The Saver's Credit can be taken for your contributions to a traditional or Roth IRA; your 401(k), SIMPLE IRA, SARSEP, 403(b), 501(c)(18) or governmental 457(b) plan; and voluntary after-tax employee contributions to a qualified retirement and 403(b) plans. The amount of the credit is 50%, 20% or 10% of your retirement plan or IRA contributions up to $2,000 ($4,000 if married filing jointly), depending on your adjusted gross income (reported on your Form 1040 or 1040A).

Section 3: Deductions and Credits

3.2 Credits

7. Adoption Credits (e.g., Carryovers, Limitations, Special Needs)

Adoption Credits (e.g., Carryovers, Limitations, Special Needs)

Qualifying expenses paid or incurred by a taxpayer may give rise to the adoption expenses credit. The provision is intended to assist taxpayers who incur nonrecurring costs directly associated with the adoption process.

Qualifications and Limitations.

a. The costs must be incurred to adopt an eligible child. An eligible child is one who is:

Under 18 years of age at the time of the adoption or

Physically or mentally incapable of taking care of himself or herself.

Up to $13,810 for 2019 of costs qualify for the credit. Examples of qualifying costs include adoption fees, court costs, social service review costs, and transportation costs.

Adoption Credits (e.g., Carryovers, Limitations, Special Needs)

The credit may be claimed in the year qualifying expenses were paid or incurred if they were paid or incurred during or after the year in which the adoption was finalized. For qualifying expenses paid or incurred in a tax year prior to the year when the adoption was finalized, the credit must be claimed in the tax year following the tax year during which the expenses are paid or incurred.

- The credit is phased out for taxpayers whose AGI (modified for this purpose) exceeds $ 211,160 in 2019 and is completely eliminated when MAGI reaches $251,160 in 2019.
- A married couple must file a joint return.
- Unused credits can be carried over for a 5-year period on a FIFO basis.

8. Affordable Care Act (ACA) Provisions Reconciliation of the advanced Premium Tax Credit

In order to reconcile The Advance Credit Payments of the Premium Tax Credit taxpayers must file a tax return to reconcile any advance credit payments received in 2019 and to maintain your eligibility for future premium assistance. If you do not file, you will not be eligible for advance payments of the premium tax credit In 2019.

Affordable Care Act (ACA) Provisions Reconciliation of the advanced Premium Tax Credit

Individuals and families whose household incomes are at least 100 percent but no more than 400 percent of the Federal poverty level (also called the Federal poverty line, or FPL) may be eligible to receive a Federal subsidy (the premium tax credit, or PTC) if they purchase insurance via the Health Insurance Marketplace (the Marketplace).

Section 3: Deductions and Credits

3.2 Credits

9. Other Credits (Refundable and Non-Refundable)

Other Credits (Refundable and Non-Refundable)

Tax Credit for Elderly or Disabled Taxpayers

Qualifying Taxpayers. Retired or permanently and totally disabled taxpayers with taxable retirement income are allowed a credit designed to partially equate their tax treatment with that of retired persons whose retirement income consists of nontaxable Social Security benefits (or other nontaxable retirement pay).

Calculation. The credit is equal to a specified initial amount (e.g., $5,000 for a single taxpayer) minus certain reductions (e.g., Social Security benefits and one-half of excess AGI) times 15 percent. Because the credit is nonrefundable, the allowable credit cannot exceed the taxpayer's tax liability.

Tax Credit for Elderly or Disabled Taxpayers

- Retired or disabled. The credit, which originally covered only retired taxpayers (age 65 or older), now also includes taxpayers with a permanent and total disability.
- As of 2017 the maximum tax credit for the Elderly and Disabled Tax Credit ranges between $3,750 and $7,500