

## SPECIAL ALERTS

### Health Care Reform Confusion

The Tax Enquirer is aware of stories circulating on the Internet and elsewhere that employer-paid health insurance has or will become a taxable benefit to employees. This information is not correct.

Under the Affordable Health Care Act, starting in 2011, employers will be required to report the amount of employer-paid health insurance premiums on Form W-2. This is a disclosure requirement for employers, not an increase in taxable income for employees. Form W-2 reports nontaxable items (such as 401(k) contributions) as well as taxable items (such as wages).

Employer-paid health insurance premiums are generally nontaxable. This tax-free treatment of employer-paid health insurance is provided for in IRC §105. Despite rumors to the contrary, this section was not repealed. In fact, §105 was expanded to provide for tax-free treatment of premiums for employees' children under age 27 (see TAX in the news 5/4/10 for discussion).



## EARLY REPAYMENT OF 2008 FIRST-TIME HOMEBUYER CREDIT

**T**he IRS plans to revise the 2010 Form 5405, First-time Homebuyer Credit and Repayment of the Credit, to accommodate taxpayers who wish to voluntarily accelerate repayment of the 2008 First-Time Homebuyer Credit (FTHC).

Under the law, taxpayers who claimed the FTHC in 2008 based on a 2008 purchase must repay 1/15 of the credit each year starting with the tax return for 2010. A taxpayer who claimed the maximum \$7,500 credit would pay 15 equal installments of \$500 each. Taxpayers wishing to pay more than 1/15 of the credit may do so. However, paying an additional amount will not decrease the following year's installment. For example (assuming a \$500 installment applies), a taxpayer who pays \$1,000 in 2010 cannot skip the 2011 installment. However, the extra amount paid in 2010 would shorten the term of repayment by one year.

Taxpayers who increase the repayment amount will fulfill the repayment obligation sooner, which some taxpayers have requested to do. Otherwise, there is no tax advantage to early repayment because the obligation is interest-free.

We will provide additional information when the IRS releases the revised form.

# For the Tax Pro

## QUESTION OF THE MONTH

*Q. Last year, my client lived with his girlfriend and her two minor children the entire year. They are not my client's biological children and he was never married to their mother. She had a small amount of income (about \$3,800). May he file as head of household, claim dependency exemptions for the children, and claim the child tax credit and EITC for them as well? He provided more than half of their support—in fact, he provided nearly all of it!*

**A.** Although support is an important factor in determining eligibility for dependency exemptions and other child-related tax benefits, it is not the only factor. To claim a dependency exemption, a taxpayer must have a qualifying child (QC) or qualifying relative (QR). Each of these has specific requirements—all of which must be met in order to claim an exemption. These requirements can be found in the “Personal Exemptions and Dependents” chapter of Publication 17. Other child-related benefits generally require that the taxpayer has a qualifying child or, in some instances, a qualifying relative.

For your client's situation, we first look to see if the children are your client's qualifying children. To be a QC, a child must be related to the client in one of several ways, such as a son, daughter, grandchild, stepchild, sibling, etc. Or, the child must be the client's eligible foster child, that is, a child legally placed with the child by a court or authorized agency. You have stated that the children are not your client's biological children and he is not married to their mother. Nor does it appear they were legally placed in his home. Because the relationship requirement is not met, the children are not his qualifying children—even if some of the other QC requirements are met.

We next look to see if the children are your client's qualifying relatives. In addition to the support test (which you indicate is met), the children must be either related to the taxpayer in one of several allowed ways or be members of his household the entire tax year (which you also indicate is met). In addition, the children may not be qualifying children of any other taxpayer. This could be an issue in your case, because the children appear to be qualifying children of their mother. At issue is whether their mother is a “taxpayer.”

For this purpose, an individual is not a taxpayer if 1) she has no filing requirement, and 2) she does not file a return for any reason other than to claim a refund of all withheld taxes. The children's mother does not have a filing requirement, but if she files a return to claim the making work pay credit, EITC, additional child tax credit, or for any reason besides claiming a refund of all withheld taxes, she is a taxpayer and the client may not claim the children as QRs.

If your client is able to claim the dependency exemptions for the children as qualifying relatives, he cannot claim them for any other child-related tax benefit. The child tax credit and EITC specifically require the client to have a qualifying child, which he does not. Head of household filing status is allowed for a taxpayer with a QR, but not if the QR is an unrelated person in the client's household. Therefore, your client cannot file using head of household status even if he can claim the dependency exemptions for the children as QRs.

## TAXWORKS TIP OF THE MONTH - Simple Tax Return Wizard



The Simple Tax Return Wizard (STaR) is new for 2009. The wizard allows you to quickly enter simple 1040 returns by working through an input wizard. Intuitive screens present follow-up screens based on input entries. The feature assists in reducing errors and keystrokes, and the entire return can be prepared using only the keyboard.

When starting a new client in TaxWorks, STaR is off by default. If you would like to set this as your default screen, click the **Settings** menu, select **Control Data**, and click the **Switches** Tab. Check the box **STaR Wizard as default**.

There are two ways to access STaR: While in a return, click the **STaR** button on the button bar. From the Client Selection screen, highlight a client and click the **STaR** button on the Client Selection button bar.

## IRS TO APPEAL QUALITY STORES DECISION

In *U.S. v. Quality Stores, Inc.*, a U.S. District Court for the Western District of Michigan upheld a bankruptcy court's ruling that severance payments by Quality Stores, Inc. to its former employees were not subject to FICA (social security and Medicare tax) withholding. According to an IRS spokesperson, the Service will not follow the Quality Stores holding when examining this issue for other taxpayers and will continue to assert that severance payments are subject to FICA. The spokesperson also indicated IRS plans to appeal the Quality Stores case.

## LEGISLATION WATCH

**Extenders**—Congress has not, and is not expected to pass legislation this week to extend popular tax breaks that expired December 31, 2009. These include the \$250 deduction for educator's expenses, the tuition and fees deduction, the deduction for state and local sales taxes, and the tax-free qualified charitable contributions distribution from IRAs. At issue is the cost of extending these tax breaks as well as "pay-fors" to raise revenue. It is possible that a stand-alone extenders bill will be discussed after Congress returns from the July recess (July 5—12).

## HOMEBUYER CREDIT CLOSING DEADLINE

Taxpayers who entered into a binding contract by April 30, 2010, must close (in other words, settle) on the home under contract on or before June 30, 2010 in order to qualify for the homebuyer credit. While Congress considered extending the closing deadline for taxpayers who had already entered into a binding contract by April 30, 2010, no extension was passed by Congress or enacted into law. The IRS cannot extend the closing deadline.

# Power Seminar Dates

### Don't Wait to Register

Fifteen years ago we started our Power Training Seminars. Our purpose and goals were many, but two main objectives remain: 1) provide clients training on topics they may not otherwise receive; 2) give clients the opportunity to meet one-on-one with the decision makers of the tax software they use for their livelihood.

Although we receive requests regarding other locations, our responses are overwhelmingly positive in preserving the locations we currently hold the seminars. That stated, our 2010 seminars will be held at the following locations on the dates specified:

#### LAYTON, UT—MON. & TUES. DECEMBER 6th & 7th, 2010

Davis Convention Center—Rooms \$99 per night Single/Double occupancy at the adjoining Hilton Garden Inn. For reservations call: 1-800-861-8712.

#### LAS VEGAS, NV—THURS. & FRI. DECEMBER 9th & 10th, 2010

Treasure Island Resort—Rooms \$89 per night Single/Double occupancy. For reservations call: 1-888-503-8999

#### ORLANDO, FL—MON. & TUES. DECEMBER 13th & 14th, 2010

Walt Disney's Coronado Springs Resort® Rooms \$119 per night Single/Double occupancy. For reservations call: 1-407-939-1020

### Special Rates

Special rates apply for the night prior to, and the first night of the seminars. If staying at the seminar location you **MUST CALL THE SPECIFIED HOTEL LINE FOR RESERVATIONS, NO LATER THAN NOVEMBER 1, 2010**, to receive the TaxWorks special discount. Remember to mention TaxWorks for our special rate. Includes up to 16 hours of CPE\* credit, luncheon, continental breakfast, and materials.

### Registration fee is only \$295 per person

A basic understanding of computer use and tax law is required for attending this seminar. Topics will range from basic to advanced courses. Beginning topics include: Boot Camp for New Users (which covers the basics of the program), use of new technology, electronic filing, sample returns, etc. Advanced topics include:

Asset Manager, 1040 returns, Business returns, etc. Refer to [www.taxworks.com](http://www.taxworks.com) for topics and their level of complexity. This program is a "live-group" offering, and will include interaction between attendees and presenters.



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