

# VITA Volunteer Tax Training #2



# Taxable Income Examples

D-3

- Wages, salaries, bonuses and commissions
- Alimony
- Annuities
- Business income
- Debts forgiven
- Dividends
- Employer-funded disability benefits
- Gain from the sale of property or securities
- Gambling winnings
- Interest
- IRA distributions
- Jury duty fees
- Military pay
- Nonemployee compensation
- Pensions
- Punitive damages
- Refund of state taxes (if itemized the prior year and took a deduction for state taxes paid)
- Rents
- Social Security benefits
- Taxable scholarships and grants
- Tips and gratuities
- **Unemployment compensation**

# Non-Taxable Income Examples D-4

- Child support
- Damages for physical injury
- Federal income tax refunds
- Gifts
- Inheritances
- Insurance proceeds
- Interest on tax-free securities
- Sickness and injury payments
- Supplemental Security Income (SSI)
- Veteran's benefits
- Welfare payments and food stamps
- Worker's compensation

# Common Income Items and Forms

## Form 1040 – Page 1

- Wage income – Form W-2 (line 1a)
- Interest income – Form 1099-INT (line 2b)
- Dividend income – Form 1099-DIV (line 3b)
- IRA distributions – Form 1099-R (line 4b)
- Pension and annuity distribution – Form 1099-R (line 5b)
- Social security benefits – Form 1099-SSA (line 6b)

## Schedule 1

- Alimony received – (Part I, line 2a)
  - Need date of divorce on line 2b
- Unemployment compensation – (Part I, line 7)
- Other income – (Part I, line 8)

**a Employee's social security number**  
501-XX-XXXX

OMB No. 1545-0008

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www.irs.gov/efile

<b>b Employer identification number (EIN)</b> 90-1XXXXXX		<b>1 Wages, tips, other compensation</b> \$23,621.18		<b>2 Federal income tax withheld</b> \$2,362.10	
<b>c Employer's name, address, and ZIP code</b> Westminster & Sons Accounting, Inc 874 Main St Lancaster, PA 17603		<b>3 Social security wages</b> \$23,621.18		<b>4 Social security tax withheld</b> \$1,465.00	
		<b>5 Medicare wages and tips</b> \$23,621.18		<b>6 Medicare tax withheld</b> \$343.00	
		<b>7 Social security tips</b>		<b>8 Allocated tips</b>	
<b>d Control number</b>		<b>9</b>		<b>10 Dependent care benefits</b>	
<b>e Employee's first name and initial Last name</b> Larry T. Jones 456 Orange St Lancaster, PA 17603		<b>11 Nonqualified plans</b>		<b>12a See instructions for box 12</b>	
		<b>13 Statutory employee Retirement plan Third-party sick pay</b> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		<b>12b</b>	
		<b>14 Other</b> LST \$52 SUI \$10		<b>12c</b>	
				<b>12d</b>	
<b>f Employee's address and ZIP code</b>		<b>15 State Employer's state ID number</b> PA 90-2XXXXXX		<b>16 State wages, tips, etc.</b> \$23,621.18	
		<b>17 State income tax</b> \$873.98		<b>18 Local wages, tips, etc.</b> \$23,621.18	
				<b>19 Local income tax</b> \$236.21	
				<b>20 Locality name</b> 36	

Form **W-2** Wage and Tax Statement

**2019**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

VOID  CORRECTED

PAYER'S name, street address, city or town, province or state, country, ZIP or foreign postal code, and telephone no.  <b>Lancaster Bank</b> <b>45 Main St</b> <b>Lancaster, PA 17603</b>		Payer's RTN (optional)  		OMB No. 1545-0112  <b>2019</b>		<b>Interest Income</b>	
		1 Interest income  \$ 56.20		Form 1099-INT			
PAYER'S federal identification number  906-XX-XXXX		RECIPIENT'S identification number  501-XX-XXXX		2 Early withdrawal penalty  \$		<b>Copy 1</b>  <b>For State Tax Department</b>	
RECIPIENT'S name  <b>Larry T. Jones</b>  Street address (including apt. no.) <b>456 Orange St.</b>  City or town, province or state, country, and ZIP or foreign postal code Lancaster PA 17603		3 Interest on U.S. Savings Bonds and Treas. obligations  \$ 25.46		4 Federal income tax withheld  \$			
Account number (see instructions)  		5 Investment expenses  \$		6 Foreign tax paid  \$			
		7 Foreign country or U.S. possession  		8 Tax-exempt interest  \$		9 Specified private activity bond interest  \$	
		10 Tax-exempt bond CUSIP no.  		11 State  		12 State identification no.  	
						13 State tax withheld  \$	

VOID  CORRECTED

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.  <b>EDWARD JONES 100 QUEEN ST LANCASTER, PA. 17601</b>		1a Total ordinary dividends <b>\$ 1256</b>	OMB No. 1545-0110  <b>2019</b>  Form 1099-DIV	<b>Dividends and Distributions</b>	
		1b Qualified dividends <b>\$ 1100</b>			
		2a Total capital gain distr. <b>\$ 100</b>	2b Unrecep. Sec. 1250 gain <b>\$</b>		<b>Copy 1 For State Tax Department</b>
PAYER'S federal identification number  <b>11-XXXXXX</b>	RECIPIENT'S identification number  <b>502-XX-XXXX</b>	2c Section 1202 gain  <b>\$</b>	2d Collectibles (28%) gain  <b>\$</b>		
RECIPIENT'S name  <b>Sally Jones</b>		3 Nondividend distributions <b>\$</b>	4 Federal income tax withheld <b>\$</b>		
Street address (including apt. no.)  <b>456 Orange St.</b>		5 Investment expenses <b>\$</b>	6 Foreign tax paid  <b>\$</b>		
City or town, state or province, country, and ZIP or foreign postal code  <b>LANCASTER, PA. 17603</b>		7 Foreign country or U.S. possession  	8 Cash liquidation distributions <b>\$</b>		
Account number (see instructions)		9 Noncash liquidation distributions <b>\$</b>	10 Exempt-interest dividends  <b>\$</b>		
		11 Specified private activity bond interest dividends  <b>\$</b>			
		12 State	13 State identification no.	14 State tax withheld <b>\$</b> <b>\$</b>	

VOID  CORRECTED

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.  <b>PA Department of Labor 1 Commerce St. Harrisburg, PA 17110</b>		<b>1</b> Unemployment compensation <b>\$ 1022.00</b>	OMB No. 1545-0120  <b>2019</b>  Form 1099-G	<b>Certain Government Payments</b>   <b>Copy 1 For State Tax Department</b>
		<b>2</b> State or local income tax refunds, credits, or offsets <b>\$</b>		
<b>PAYER'S federal identification number</b> 906-XX-XXXX	<b>RECIPIENT'S identification number</b> 502-XX-XXXX	<b>3</b> Box 2 amount is for tax year	<b>4</b> Federal income tax withheld <b>\$ 102.00</b>	
<b>RECIPIENT'S name</b>  <b>Sally Jones</b>  Street address (including apt. no.) <b>456 Orange St</b> City or town, state or province, country, and ZIP or foreign postal code <b>Lancaster, PA 17603</b>		<b>5</b> RTAA payments <b>\$</b>	<b>6</b> Taxable grants <b>\$</b>	
		<b>7</b> Agriculture payments <b>\$</b>	<b>8</b> Check if box 2 is trade or business income <input type="checkbox"/>	
<b>Account number (see instructions)</b> .....		<b>9</b> Market gain <b>\$</b>	<b>11</b> State income tax withheld <b>\$</b> ..... <b>\$</b>	
		<b>10a</b> State .....		<b>10b</b> State identification no. .....

Form 1099-G

www.irs.gov/form1099g

Department of the Treasury - Internal Revenue Service



## FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT

<b style="font-size: 1.2em;">2018</b> <ul style="list-style-type: none"> <li>• PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME.</li> <li>• SEE THE REVERSE FOR MORE INFORMATION.</li> </ul>		
Box 1. Name <p style="text-align: center; font-size: 1.1em;">Iodine Element</p>		Box 2. Beneficiary's Social Security Number <p style="text-align: center; font-size: 1.1em;">400-00-8006</p>
Box 3. Benefits Paid in 2015 <p style="text-align: center; font-size: 1.1em;">12333.00</p>	Box 4. Benefits Repaid to SSA in 2015 	Box 5. Net Benefits for 2015 (Box 3 minus Box 4) <p style="text-align: center; font-size: 1.1em;">12333.00</p>
DESCRIPTION OF AMOUNT IN BOX 3  Paid by check or direct deposit: 11189.00  Medicare Part B premium deducted from your benefits: 1000.00  Medicare Prescription Drug premiums (Part D) deducted from your benefits: 144.00		DESCRIPTION OF AMOUNT IN BOX 4  Box 6. Voluntary Federal Income Tax Withheld  Box 7. Address  <p style="text-align: center; font-size: 1.1em;">1003 Helium Drive Phoenix AZ 85001</p> Box 8. Claim Number (Use this number if you need to contact SSA.)

9898

 VOID CORRECTED

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and phone no.  <b>XYZ Bank</b> <b>987 Main Street</b> <b>Lancaster, PA 17601</b>			<b>1</b> Gross distribution \$ <b>1563</b>	OMB No. 1545-0119 <b>20 19</b>		<b>Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.</b>
			<b>2a</b> Taxable amount \$ <b>1563</b>	Form <b>1099-R</b>		
			<b>2b</b> Taxable amount not determined <input type="checkbox"/>	Total distribution <input type="checkbox"/>		<b>Copy A For Internal Revenue Service Center</b>  <b>File with Form 1096.</b>
<b>PAYER'S TIN</b> <b>92-1xxxxxx</b>	<b>RECIPIENT'S TIN</b> <b>509-xx-xxxx</b>		<b>3</b> Capital gain (included in box 2a) \$	<b>4</b> Federal income tax withheld \$ <b>26</b>		
RECIPIENT'S name <b>Ted D. Bear</b>			<b>5</b> Employee contributions/ Designated Roth contributions or insurance premiums \$	<b>6</b> Net unrealized appreciation in employer's securities \$		<b>For Privacy Act and Paperwork Reduction Act Notice, see the 2018 General Instructions for Certain Information Returns.</b>
Street address (including apt. no.) <b>45 Bamboo Street</b>			<b>7</b> Distribution code(s) <b>1</b>	<b>IRA/ SEP/ SIMPLE</b> <input type="checkbox"/>	<b>8</b> Other \$ %	
City or town, state or province, country, and ZIP or foreign postal code <b>Lancaster, PA 17601</b>			<b>9a</b> Your percentage of total distribution %	<b>9b</b> Total employee contributions \$		
<b>10</b> Amount allocable to IRR within 5 years \$	<b>11</b> 1st year of desig. Roth contrib.	<b>FATCA filing requirement</b> <input type="checkbox"/>	<b>12</b> State tax withheld \$	<b>13</b> State/Payer's state no.	<b>14</b> State distribution \$	
Account number (see instructions)		<b>Date of payment</b>	<b>15</b> Local tax withheld \$	<b>16</b> Name of locality	<b>17</b> Local distribution \$	

Form **1099-R** Cat. No. 144380

www.irs.gov/Form1099R

Department of the Treasury - Internal Revenue Service

**Do Not Cut or Separate Forms on This Page — Do Not Cut or Separate Forms on This Page**

# Retirement Income

D-52

## Form 1099 Codes

Code	Description	State and Local Tax
1	Early distribution, no known exception (most cases under 59 ½)	Taxable (cost basis is recovered first)
2	Early distribution, exception applies (under age 59 ½)	Taxable (cost basis is recovered first)
3	Disability	Not taxable
4	Death	Not taxable
6	Tax-free exchange of insurance or annuity	Not taxable*
7	Normal distribution	Not taxable
G	Direct rollover of distribution to a qualified plan	Not taxable
H	Direct rollover of a designated Roth account	Not taxable
Q	Qualified distribution from Roth IRA	Not taxable
W	Purchase of long-term care insurance premiums	Not taxable*
7D	Earnings on nonretirement annuity	Taxable as interest

# Additional Details on Pensions and Annuities

- Distribution Code 7D
  - Code represents earnings on nonretirement annuity contract.
  - These plans are generally purchased from life insurance companies as a structured payment plan
  - Taxable amounts on line 2a are also **taxable** for Pennsylvania as interest income
- Distribution Code F
  - Code represents earnings on charitable gift annuities.
  - Taxable amounts on line 2a are also **taxable** for Pennsylvania as interest income
- Distribution Code 4
  - Code represents amounts received as a beneficiary
  - No early distribution penalty applies even if the recipient is under 59 ½
  - Amount is **not** taxable for Pennsylvania or local taxes

# Additional Details on Insurance Contracts

- Distribution Code 6
  - Code represents a tax-free exchange of life insurance, annuity, long-term care insurance or other endowments under Code Sec. 1035
  - This code generally arises as taxpayers change insurance companies or insurance brokers
  - While the amounts should not be taxable for Pennsylvania, they may impact Schedule SP and PA-1000
- Distribution Code W
  - Code represents charges or payments for purchasing qualified long-term care insurance contracts generally arising from cash value of annuities or cash surrender value of a life insurance contract.
  - These amounts are **tax-free** for federal, state and local income purposes.

# Additional Details on Pensions and Annuities

- Pension and annuity payments include distributions from 401(k), 403(b) and governmental 457(b) plans
  - Distributions from these plans will be taxable in full to recipients if no after-tax contributions were made to the plan or all costs were previously recovered.
  - Report taxable amount on 1040.
- Exclusion for insurance premiums for Retired Public Safety Officers (PSO) – See Pub. 4012 D-47
  - Exception exists for insurance premiums for retired public safety officers if part of distribution was used for health, accident or long-term care premiums.
  - Smaller of premiums paid or \$3,000 may be excluded from income.
  - Click on “Calculate your taxable amount” for next screen
- Partially Taxable Annuities
  - Payer may show taxable amount on line 2a
  - Taxpayer may use either simplified method or general rule method for calculation

# Retirement Income – Reporting Issues

- Taxable amount reported in Box 2a on Form 1099-R
  - The taxable amount will carry to Form 1040, page 1, line 4b or line 5b
- Taxable amount **not** reported in Box 2a on Form 1099-R
  - If the taxpayer made a contribution with pre-tax dollars (401(k) and thrift savings plan), then the distribution is fully taxable
  - If the taxpayer made a contribution with after-tax dollars, then the distribution is partially taxable\*
- Roth IRA distributions are tax free if the following are met
  - Distribution is made 5 years after the first contribution was made
  - Distribution is after age 59½, due to disability, estate beneficiary or to pay certain first-time home buyer amounts
  - If tests are not met, the distribution could be partially taxable\*

\*Taxable calculations are complex and outside scope for VITA

# Partially Taxable Pensions and Annuities

- Applicable if there is an investment in the contract
  - Total premiums, contributions or other amounts paid after tax should be reflected on line 9b in **first year payments are received**
- Simplified Method **must** be used under either circumstance
  - Annuity started after July 1, 1986 and the simplified method was used to figure taxable amount in a prior tax year
  - Annuity started after November 16, 1996 and **both** the following apply:
    - Payments are from a qualified employee plan, qualified employee annuity or tax-sheltered annuity plan (403(b) plan) AND
    - On annuity starting date, recipient was under age 75 **or** the number of guaranteed years is fewer than 5
- If an investment in the contract exists but the simplified rule cannot be used, then the general rule method must be calculated. **Pub. 939**



# Simplified Method

- Information needed
  - Prior Form 1040 if simplified method has been used for taxable calculations
  - Details of annuity payment program to determine guaranteed payments and whether single or joint life annuity
  - Age of recipient at start of annuity payments
    - Need ages of both recipients if the annuity is based on joint lives
  - Net investment in annuity (post-tax contributions) generally shown on box 9b
- Use of tables for payments over life expectancy
  - Single life annuity – use Table 1
  - Joint life annuity – use Table 2
- For fixed period annuity (no reference to annuitant's life), use total of monthly annuity payments under the contract

# Simplified Method Example

**Example.** Bill Smith, age 65, began receiving retirement benefits in 2024 under a joint and survivor annuity. Bill's annuity starting date is January 1, 2024. The benefits are to be paid for the joint lives of Bill and his wife, Kathy, age 65. Bill had contributed \$31,000 to a qualified plan and had received no distributions before the annuity starting date. Bill is to receive a retirement benefit of \$1,200 a month, and Kathy is to receive a monthly survivor benefit of \$600 upon Bill's death.

- Should simplified method be used?
- What is the taxable amount of the annuity in 2024?

# Early Distribution from Retirement Plan

- Indication of early distribution would be total distribution box on line 2b checked and code 1 in box 7
- Federal treatment includes total distribution in ordinary income plus a 10% early withdrawal penalty.
  - Penalty will automatically calculate with entry in TaxSlayer. No Form 5329.
- Pennsylvania and local will also tax early distribution
  - Pennsylvania reports on Form W-2S and flows to compensation
  - Local can be reported as other income
  - Any employee contributions to the plan are tax-free and deemed to be distributed before taxable amounts (cost-recovery method)

# Exceptions to Early Withdrawal Penalty

- Common penalty exceptions include:
  - Distribution from IRA that was converted to Roth IRA (Code 2)
  - Full or partial indirect rollover to a qualified plan (taxpayer received fund) within 60 days of initial distribution. Indicate ROLLOVER in TaxSlayer
  - Payment of IRS levies (Code 2)
  - Death of participant/IRA owner (Code 4)
  - Total and permanent disability of participant/IRA owner (May need Form 5329)
- Entry in TaxSlayer
  - From the Federal Section of the program Other Taxes > Tax on Early Distribution.
  - Enter the amount that is exempt in the field for "Early Distributions that are not subject to 10% tax" under Part 1, and select the reason from the drop-down menu for the field "Select the reason for exemption".

# Using Form 5329 Exceptions to Penalty

- If Form 1099-R shows Code 1 in Box 7, Form 5329 must be used to reduce or eliminate penalty.
- Codes to be used on Form 5329:
  - Code 05 – qualified unreimbursed medical expenses paid during the year that exceed 7.5% of AGI
  - Code 07 – **IRA** distributions for health insurance for unemployed individuals
  - Code 08 – **IRA** distributions made for qualified higher education expenses (tuition, fees, books, supplies, required equipment and reasonable room and board)
    - Reduce education expenses by any tax-free scholarships, grants or employer assistance
  - Code 09 – **IRA** distributions for purchase of first home (up to \$10,000)
  - Code 19 – Other items, such as up to \$5,000 for the birth or adoption of a child

# Social Security and Railroad Benefits

- For Social Security Benefits (SSA-1099) and Railroad Retirement Benefits Tier 1 (RRB-1099) (Blue form), enter the information from the government form into TaxSlayer
  - Federal Section>Income>1099-R, RRB, SSA>Social Security Benefits/RRB-1099
  - Use keyword “SSA”
- For Railroad Retirement Benefits Tier 2 (RRB-1099-R) (Green form), enter the information from the government form into TaxSlayer
  - Federal Section>Income>1099-R, RRB, SSA>RRB-1099-R
  - Use keyword “RR”

# Capital Gain or Loss

D-32

- Capital gains and losses are reported on Schedule D and Form 8949
- Transactions within scope for VITA:
  - Sale of stock
  - Sale of mutual funds
  - Sale of principal residence
- The following information is needed to appropriately report capital gains and losses:
  - Sales price
  - Adjusted basis of asset (See Publication 551 for details)
  - Short-term or long-term holding period
  - Any capital loss carryovers
  - Principal residence exclusions

# Capital Gain or Loss

- Proceeds from sale will typically be reported on 1099-B for stock and securities and 1099-S for real estate
- Basis determination:
  - Original cost of the asset
  - Plus any increases or decreases such as commissions, fees, depreciation or improvements
  - Brokers must report cost or other basis on Form 1099-B unless the securities sold were noncovered
  - Taxpayers must use the codes on Form 8949 to report if 1099-B was received and whether or not it showed basis reported to IRS
- Holding periods:
  - Short-term property is held one year or less
  - Long-term property is held for more than one year
  - Long-term capital gains are taxed at a lower rate than short-term capital gains



# Sale of a Principal Residence

D-40

- Sale of a main home should be reported on Form 8949 and Schedule D if the taxpayer does not meet the exclusion **or** they received a 1099-S reporting the sale
- Exclusion rules for sale of main home:
  - Property must be home where taxpayer lived most of the time
  - Taxpayer must have owned the home for 2 of the last 5 years
  - Taxpayer must have lived in the home for 2 of the last 5 years
  - Maximum exclusion is \$250,000 per taxpayer (\$500,000 for MFJ)
- Determining gain from sale of main home:
  - Selling price is the total amount the seller received for the home
  - Amount realized is the selling price less selling expenses (commissions, advertising fees, legal fees)
  - Basis is the amount that the taxpayer paid to buy or build the home plus additions and improvements

# Business Income

D-21

- Business income is reported on Schedule C
- Form 8995-A (Simplified QBID 20% deduction)
- The following areas are out of scope for VITA:
  - Greater than \$10,000 in business expenses
  - Have a loss from the business
  - Have employees
  - Returns and allowances (non-cash method of accounting)
  - Cost of goods sold (involves inventory)
  - Farm income
  - Depreciation of furniture and equipment
  - Home office
  - Self employment health insurance
- 2-1-1 will screen for these items, but some may slip through

# Business Income

D-22

- Form 1099-NEC reports nonemployee compensation.
- Reports amount of nonemployee compensation on line 1 of the form.
- 1099-MISC will still be used for rental income and other income
- To enter 1099-NEC in TaxSlayer
  - Federal Section>Income>Form 1099-NEC or
  - Keyword “SC”
- Income from 1099-NEC can be linked to Schedule C
  - See screenshot on D-23
- Form 1099-K will be issued more frequently based on reduced filing thresholds. This form reports payments received from payment card transactions (debit or credit). See D-24 and D-25 for more information.

# Business Expenses

D-28

- Business expenses within scope for VITA:
  - Advertising
  - Car and truck expenses based on standard mileage rates
  - Commissions and fees
  - Insurance
  - Other interest
  - Legal and professional services
  - Office expense (does not include office-in-home)
  - Rent or lease of vehicle, machinery and equipment
  - Repairs and maintenance
  - Supplies
  - Taxes and licenses
  - Travel
  - Meals – subject to limitation
  - Utilities

# Uber Drivers

- Drivers for Uber (or other car services) are independent contractors for income tax purposes
- Tax returns must be filed if net earnings > \$400
- Income is reported to drivers on Form 1099-NEC and/or Form 1099-K and reported on Schedule C
- Expenses typically include:
  - Car and truck expenses based on standard mileage rates
  - Commissions and credit card service fees
  - Additional insurance purchased specifically for business
  - Business portion of car loan interest
  - Office expense (does not include office-in-home)
  - Supplies (including items provided to passengers)
  - Utilities (business portion of cell phone)
- **The client's Uber page will have a list of expenses, clients can often retrieve this from their phone.**

# Gambling Winnings and Other Income

- Gambling winnings reported on a Form W2-G are reported under Federal Section>Income>Less Common Income
- Gambling losses are only allowed to the extent of gambling winnings and must be reported on Schedule A as an itemized deduction
  - If the taxpayer cannot itemize, they do not receive benefits for the losses
- Additional income to be reported under Other Income Not Reported Elsewhere:
  - Jury duty pay
  - Gambling winnings not reported on Form W2-G
  - Other income not entered elsewhere on return
- Form 1099-MISC may report awards and prizes in box 3

# Debt Cancellation

D-71

- Personal debts cancelled may be subject to income
- Taxpayer should receive Form 1099-C if the cancelled debt exceeds \$600
- Debt cancellation within VITA scope:
  - Personal debt
  - Reported on Form 1099-C
  - No interest in connection with debt cancellation
  - Not business related
  - Not under bankruptcy
  - Not claiming insolvency exemption (See D-70)
  - Certain student loan debt forgiveness is in scope for 2023
- Amount of debt cancellation should be reported on Schedule 1, line 8c (Other income)