2000 Income Tax School

ISSUES FOR OLDER TAXPAYERS

I. THE STANDARD DEDUCTION AND PERSONAL EXEMPTION DEDUCTION

WHEN IS A TAXPAYER CONSIDERED TO BE AGE 65?

A taxpayer must be age 65 or over to receive various tax benefits intended for older Americans. Taxpayers are considered 65 on the day **before** their 65th birthday.

Example 1. A taxpayer born January 1, 1936 will actually "turn 65" on January 1, 2001. However, for federal income tax purposes, that taxpayer is considered to be 65 as of December 31, 2000–and eligible for the benefits available to older taxpayers on his or her 2000 federal income tax return.

INCREASED STANDARD DEDUCTION FOR THOSE 65 AND OVER FOR 2000

Unmarried individuals age 65 or older add $1,100 to the standard deduction.

Example 2

Standard deduction for single individual	$4,400
Plus amount for age 65 or older	1,100
Total standard deduction	**$5,500**

Married individuals age 65 or older add $850 each to the standard deduction.

Example 3

Standard for married filing jointly	$7,350
Plus amount for one spouse age 65 or older	850
Total standard deduction if one spouse 65 or older	**$8,200**
Standard deduction for married filing jointly	$7,350
Plus amount for both spouses age 65 or older	1,700
Total standard deduction if both 65 or older	**$9,050**
Standard deduction for married filing separately	$3,675
Individual 65 or older	850
Total standard deduction filing separately	**$4,525**

WHEN ONE SPOUSE DIES DURING THE YEAR

Surviving Spouse Does Not Remarry. A surviving spouse is considered married for the entire year and therefore may file a joint return with the decedent for the year of death.

> **Practitioner Note.** If both spouses die during the year, the returns may be filed either jointly or separately.

Surviving Spouse Remarries. If the surviving spouse **remarries** prior to the end of the tax year, **he or she may not file a joint return with the decedent.** The surviving spouse may file jointly with the new spouse or each may be considered married filing separately. Regardless, the filing status of the decedent will be considered married filing separately for his or her final return.

Head of Household. An older taxpayer may qualify for head of household filing status if that individual provides support for a grandchild, brother, sister, or other relative. See the discussion of Head of Household in the Divorce chapter.

Qualifying Surviving Spouse. If qualifications are met (taxpayer is unmarried and paying more than half the cost of maintaining the home for a child who can be claimed as a dependent), a surviving spouse may use the married filing jointly tax rates and standard deduction for each of the two years following his or her spouse's death.

> **Practitioner Note.** For all filing statuses other than married filing separately, taxpayers who are age 65 or older have a higher federal filing threshold (see Chart A at the beginning of the Form 1040 instructions). The Internal Revenue Service sends out notices to some taxpayers who file but are below the federal filing threshold, indicating that they are not required to file. Some older taxpayers who have income below the federal filing threshold may still be within the filing requirement for state income taxes. For state income taxes, there may also be more items included in taxable income, such as federal tax-exempt interest.

CAREGIVERS CLAIMING THE PERSONAL EXEMPTION DEDUCTION FOR PARENTS

A taxpayer can claim a parent as a dependent if the following five tests are met:

1. **Taxpayer provides more than half of the parent's support for the year.**

> **Practitioner Note.** Count only what the parent actually spends on his or her support–not the total amount available. Support includes the cost of lodging, food, clothing, education, recreation, transportation, and medical and other necessities.

2. **Parent's gross income is less than the base amount allowed as a personal exemption deduction ($2,800 for 2000).**

> **Practitioner Note.** Tax-exempt income, such as the tax-exempt portion of social security benefits, is not considered in the gross income test–but it is considered for the support test if the older taxpayer uses the tax-exempt income for his or her support.

3. The parent is single or is married and files separately.

Practitioner Note. If the parent files a joint return merely as a claim for a refund and no tax liability would exist for either spouse on separate returns, then the parent can still be claimed for the entire year.

4. The parent is a U.S. citizen or national, or a resident of the United States, Canada, or Mexico.

Practitioner Note. The fifth test for claiming a dependent is met by all taxpayers claiming a parent. It requires the dependent to be a relative of the taxpayer or to live in the taxpayer's home for the entire year.

Example 4. Anne makes a home for herself and her widowed mother, Martha. Martha has taxable interest income of $1,500 per year and social security benefits of $3,800. Martha applies all of her income to her own support. The fair market value of food and lodging that Anne provides her mother is $5,200. Anne meets four of the five dependency tests: Martha is a relative. Martha is single. Martha is a U.S. citizen. Martha's taxable gross income is less than the personal exemption since the tax-exempt social security benefits are not counted. **The support test is problematic.** With these facts, it appears that Martha's total support is $10,500, of which Anne provides $5,200–less than half.

Practitioner Note. The social security is counted for support, even though it is not counted for the gross income test regarding the personal exemption.

Example 4 Breakdown of Contribution to Martha's Support

Anne's Contribution	Martha's Contribution	Total Support
$5,200	$1,500 + $3,800 = $5,300	$10,500

Question. What changes can Anne and Martha make to allow Anne to claim Martha as a dependent?

Answer. Only the amount that a dependent actually spends counts as support–not the amount available. Anne is spending $5,200 on Martha's support. Martha is spending $5,300. If Martha puts $5 of her income each month in a savings account (and does not use it for her support), that will decrease Martha's contribution to her own support to $5,240 ($5,300 – $60). If Anne provides an additional $5 per month, then she is providing more than half of Martha's support and can claim Martha as a dependent.

After Savings Change—Breakdown of Contribution to Martha's Support

Anne's Contribution	Martha's Contribution	Total Support
$5,200 + 60 = $5,260	$5,300 – $60 = $5,240	$10,500

SHARING THE PERSONAL EXEMPTION DEDUCTION

Multiple support agreements allow taxpayers to share the dependency exemption deduction for elderly parents. All taxpayers who contribute over 10% of the parent's support agree to have one member of the contributing group claim the exemption each year. The person claiming the exemption may change, according to new agreements, each year.

Example 5. Helen's children provide the following support:

Jo	$1,500	15%
Meg	1,000	10%
Beth	2,500	25%
Amy	2,000	20%
Martha's social security	3,000	30%
	$10,000	100%

In the absence of a multiple support agreement, no single sister is eligible to claim Helen since no one provides more than half of her support. All but Meg qualify to claim Helen under a multiple support agreement. (Meg paid only 10% of the total. The rules say "more than 10%"–just one dollar more would have made her eligible.)

IRS Form 2120, Multiple Support Declaration, should be completed each year and attached to the tax return of the individual claiming the dependency exemption.

Form **2120**
(Rev. January 2001)
Department of the Treasury
Internal Revenue Service

Multiple Support Declaration

► Attach to Form 1040 or Form 1040A of person claiming the dependent.

OMB No. 1545-0071

Attachment Sequence No. **114**

Name of person claiming the dependent: ***Beth Little***

Social security number ***111 11 111***

During the calendar year ***2000***, I paid over 10% of the support of:

Helen Little

Name of person supported

I could have claimed this person as a dependent except that I did not pay over half of his or her support. I understand that this person is being claimed as a dependent on the Federal income tax return of:

Beth Little

Name of person claimng the dependent

362 West Third, Hampton, Ohio

Address of person claiming the dependent

I agree not to claim this person as a dependent on my Federal income tax return for any tax year that began in the above calendar year.

Your signature

222 22 222

Your social security number

640 North Duck

Address (number, street, apt. no.)

Date

Ashley, IL 62789

City, state, and ZIP code

STANDARD DEDUCTION FOR PARENT CLAIMED ON CHILD'S TAX RETURN

An elderly parent who can be claimed as a dependent on a grown child's return is allowed a standard deduction of $700, similar to other individuals who can be claimed on someone else's return. However, the "65 and older" standard deduction increment is also included, making the year 2000 standard deduction on a single dependent parent's tax return $1,800 ($700 + $1,100).

10

Standard Deduction Worksheet for Dependents—Line 36 *Keep for Your Records*

Use this worksheet **only** if someone can claim you (or your spouse if married filing jointly) as a dependent.

1.	Add $250 to your **earned income***. Enter the total	**1.**	
2.	Minimum standard deduction	**2.**	700.00
3.	Enter the **larger** of line 1 or line 2	**3.**	
4.	Enter the amount shown below for your filing status. • Single—$4,300 • Married filing separately—$3,600 • Married filing jointly or qualifying widow(er)—$7,200 • Head of household—$6,350	**4.**	
5.	**Standard deduction.**		
a.	Enter the **smaller** of line 3 or line 4. If under 65 and not blind, **stop here** and enter this amount on Form 1040, line 36. **Otherwise,** go to line 5b	**5a.**	
b.	If 65 or older or blind, multiply the number on Form 1040, line 35a, by: $1,050 if single or head of household; $850 if married filing jointly or separately or qualifying widow(er)	**5b.**	*1,100*
c.	Add lines 5a and 5b. Enter the total here and on Form 1040, line 36	**5c.**	*1,800*

***Earned income** includes wages, salaries, tips, professional fees, and other compensation received for personal services you performed. It also includes any amount received as a scholarship that you must include in your income. Generally, your earned income is the total of the amount(s) you reported on Form 1040, lines 7, 12, and 18, minus the amount, if any, on line 27.*

CAREGIVER ELIGIBLE FOR HEAD OF HOUSEHOLD WHEN SUPPORTING PARENT

If a taxpayer meets the requirements for the dependency tests and can claim a parent as a dependent, he or she may also be eligible for head of household status. The taxpayer must pay more than half the cost of keeping up a home for the parent. The parent does not have to live in the same house as the taxpayer.

Example 6. Alex is single and lives alone. His widowed mother Ethel lives alone in her own apartment. Her only income is social security. Alex provides more than half the support for his mother, including paying the rent and utilities for her apartment. The tests for Alex to claim Ethel as a dependent are met (relationship, citizenship, no joint return, gross income, and support) and he may claim her exemption on his return. In addition, he is paying more than half the cost of keeping up a home for his parent for the entire year–this qualifies him for head of household filing status.

Practitioner Note. Dependents **other than parents** must live in the same household as the taxpayer for head of household status to apply.

II. DEDUCTING MEDICAL EXPENSES

MEDICAL EXPENSES

To the extent medical expenses exceed 7.5% of adjusted gross income, they are deductible on Schedule A. The amount is not reduced for the itemized deduction phase-out.

Practitioner Note. The threshold for the alternative minimum tax is 10%.

Medical expenses include:

- Prescription medicines and drugs, as well as insulin, eye glasses, and hearing aids
- Medical services by a medical practitioner
- Hospital services, therapy, nursing services, ambulance hire, laboratory, surgical, diagnostic, dental, and X-ray fees
- Transportation for and essential to medical care
- Insurance for medical care
- Insurance for long-term care

CHILD CLAIMING DEDUCTION FOR PARENT'S EXPENSES

A child who cares for and pays medical expenses for an elderly parent may be eligible to deduct those medical expenses on the child's Schedule A (Form 1040).

Medical expenses paid by a taxpayer for his or her parent are deductible by the taxpayer if the taxpayer paid more than half of that parent's support in either the year the bills were incurred or the year they were paid.

Practitioner Note. If there is a multiple support agreement with respect to the parent, only the taxpayer who is allowed to claim the dependency exemption deduction can claim medical expenses for that year.

LONG-TERM CARE EXPENSES

Qualified long-term care expenses include diagnostic, preventive, therapeutic, curing, treating, and rehabilitative expenses for "chronically ill" patients as well as maintenance and personal care expenses for such patients. A licensed health practitioner must have prescribed such services and care within the previous 12 months.

A "chronically ill" patient is one who is unable to perform two of the following daily living activities without substantial assistance for at least 90 days:

- eating
- toileting
- transferring
- bathing
- dressing
- continence

A "chronically ill" patient may also be an individual who requires substantial supervision to be protected from threats to health and safety due to severe cognitive impairment.

Practitioner Note. An individual who is physically able but has a cognitive impairment such as Alzheimer's disease or another form of irreversible loss of mental capacity is treated similarly to an individual who is unable to perform at least two activities of daily living.

Non-reimbursed expenses for long-term care that meet the criteria are deductible as medical expenses, subject to the 7.5% of adjusted gross income floor.

Practitioner Note. Long-term care services provided by a relative are not deductible as medical expenses unless that relative is a professional licensed to perform those services.

If the main reason for being in a nursing home or similar facility is to get medical care, the cost of medical care as well as the cost of meals and lodging qualifies as medical expenses. If the reason for being in the home is **personal,** the cost of meals and lodging may **not** be deducted. In that case, the part of the cost that is for medical or nursing care may be included in medical expenses.

Rather than moving into a residential facility, many elderly persons hire private nurses to provide the required services in their homes. If the services provided are those that a medical nurse performs, the wages, employment taxes, employee benefits, and related expenses qualify as a medical expense even if the individual hired is not professionally licensed. If the individual also performs personal or housekeeping-type services, the costs must be allocated between deductible and nondeductible expenses.

LONG-TERM CARE INSURANCE

A qualified long-term care insurance contract provides coverage only for qualified long-term care services. The contract

1. Must be guaranteed renewable
2. Must not provide for a cash surrender value or other money that can be paid, assigned, pledged, or borrowed
3. Must provide that refunds, other than refunds on the death of the insured or complete surrender or cancellation of the contract, and dividends under the contract, must be used only to reduce future premiums or increase future benefits
4. Generally must not pay or reimburse expenses incurred for services or items that would be reimbursed under Medicare, except where Medicare is a secondary payer, or the contract makes per-diem or other periodic payments without regard to expenses.

Long-term care premiums are deductible as medical expenses subject to the 7.5% of adjusted gross income floor, but the deductions are limited to the following amounts for 2000:

Age before End of Tax Year	Limit on Deduction for Premium Paid
Age 40 or less	$ 220
Age 41 to 50	$ 410
Age 51 to 60	$ 820
Age 61 to 70	$2,200
Age 71 and above	$2,750

Long-term care insurance provided under an employer's plan is generally treated as an accident and health plan, and the value of coverage is excludible from the employee's income.

Per-Diem Benefits. Some long-term care insurance contracts pay a specific amount per day, without regard to the actual cost of the long-term care being received. This type of benefit can generally be excluded from gross income up to a limit of $190 per day ($69,350 per year) for 2000. The $190 is indexed for inflation.

This limit on the exclusion is ignored if one of the following is true:

1. The actual cost of the long-term care is equal to or more than the per-diem payment, even if the per-diem exceeds the cap.
2. The taxpayer is terminally ill and has been certified by a physician as having a physical condition that reasonably can be expected to result in death within 24 months of the certification date.

Lifetime Care: Advance Payments. Some retirement homes offer a program whereby an individual pays a lifetime-care fee or "founder's fee." The fee is paid either periodically (monthly for instance) or as a lump sum under an agreement with the retirement home. The part of the payment that is properly allocable to medical care may be claimed as a medical deduction. The agreement must require a specific fee as a condition for the home's promise to provide lifetime care that includes medical care.

Practitioner Note. Generally, medical expenses do not include current payments for medical care to be provided substantially beyond the end of the year. This does not apply, however, in situations where the future care is purchased in connection with obtaining lifetime care as described above.

Example 7. Jake Marley purchased a long-term care insurance contract from Wecoveryou Insurance Company early in 1997. Under the terms of the policy, $110 per day was to be paid for any day he was a nursing home resident. This is a per-diem type policy and the $110 per day benefit is to be paid without regard to the actual nursing home expenses incurred.

Jake became ill in 2000 and was certified by his physician in August of 2000 as **chronically ill** due to a disease (Alzheimer's) that resulted in severe cognitive impairment. He entered the Staywithus Nursing Home on September 26, 2000, and remained there through December 31, 2000.

In January of 2001 he received a Form 2000 1099-LTC from the Wecoveryou Insurance Company showing a total paid amount of $7,260 in long-term care benefits.

9393 ☐ VOID ☐ CORRECTED

PAYER'S name, street address, city, state, ZIP code, and telephone no. *Wecoveryou Insurance Company* *4000 6th Avenue West* *Upstate, NY 14890*	**1** Gross long-term care benefits paid $ *7260* **2** Accelerated death benefits paid $	OMB No. 1545-1519 2000 Form **1099-LTC**	**Long-Term Care and Accelerated Death Benefits**
PAYER'S Federal identification number *15-2345678*	POLICYHOLDER'S identification number *636-07-1099*	**3** Check one: ☒ Per diem ☐ Reimbursed amount	INSURED'S social security no.
POLICYHOLDER'S name *Jack Marley*		INSURED'S name *Jake Marley*	
Street address (including apt. no.) *427 Maple Street*		Street address (including apt. no.) *427 Maple Street*	
City, state, and ZIP code *Big Sky, MT 67890*		City, state, and ZIP code *Big Sky, MT 67890*	
Account number (optional)	**4** Qualified contract ☐ (optional)	**5** Check, if applicable: (optional) ☒ Chronically ill ☐ Terminally ill	Date certified *2000 08 13*

Copy A
For Internal Revenue Service Center
File with Form 1096.
For Privacy Act and Paperwork Reduction Act Notice, see the **2001 General Instructions for Forms 1099, 1098, 5498, and W-2G.**

Form **1099-LTC** Cat. No. 23021Z Department of the Treasury - Internal Revenue Service

The insurer paid benefits for the 97 days Jake was in the nursing home in 2000 as follows:

Benefit Month	Days	Rate	Benefits	Check Date
September	5	$110	$550	November 5, 2000
October	31	$110	$3,410	November 22, 2000
November	30	$110	$3,300	December 22, 2000
Box 1 on 2000 1099-LTC			**$7,260**	
December	31	$110	$3,410	January 22, 2001

Jake paid the nursing home regular rate of $125 per day as follows:

Month	Days	Rate	Paid	Date Paid
September	5	$125	$ 625	September 30, 2000
October	31	$125	$ 3,875	October 15, 2000
November	30	$125	$ 3,750	November 15, 2000
December	31	$125	$ 3,875	December 15, 2000
Total 2000 payments			**$12,125**	

Jake is 58 years old as of December 31, 2000. He paid premiums of $2,500 to Wecoveryou Insurance Company during 2000. The completed 2000 Form 8853 (Section C only) is shown below.

Form 8853 (2000) Attachment Sequence No. **39** Page **2**

Name of policyholder (as shown on Form 1040) *Jake Marley* | Social security number of policyholder ► *636 07 1099*

Section C. Long-Term Care (LTC) Insurance Contracts.
See **Filing Requirements for Section C** on page 6 of the instructions before completing this section.

If more than one Section C is attached, check here . . . ► ☐

14a Name of insured ► *Jake Marley* **b** Social security number of insured ► *636 07 1099*

15 In 2000, did anyone other than you receive payments on a per diem or other periodic basis under a qualified LTC insurance contract covering the insured or receive accelerated death benefits under a life insurance policy covering the insured? . . . ☐ **Yes** ☒ **No**

16 Was the insured a terminally ill individual? . . . ☐ **Yes** ☒ **No**

Note: *If "Yes" and the* ***only*** *payments you received in 2000 were accelerated death benefits that were paid to you because the insured was terminally ill, skip lines 17 through 25 and enter -0- on line 26.*

17 Gross LTC payments received on a per diem or other periodic basis. Enter the total of the amounts from box 1 of all Forms 1099-LTC you received with respect to the insured on which the "Per diem" box in box 3 is checked . . . **17** *7,260*

Caution: *Do* ***not*** *use lines 18 through 26 to figure the taxable amount of benefits paid under an LTC insurance contract that is not a* ***qualified*** *LTC insurance contract. Instead, if the benefits are not excludable from your income (for example, if the benefits are not paid for personal injuries or sickness through accident or health insurance), report the amount not excludable as income on Form 1040, line 21.*

18 Enter the part of the amount on line 17 that is from **qualified** LTC insurance contracts . . . **18** *7,260*

19 Accelerated death benefits received on a per diem or other periodic basis. Do not include any amounts you received because the insured was terminally ill. See page 5 of the instructions . **19**

20 Add lines 18 and 19 . . . **20** *7,260*

Note: *If you checked "Yes" on line 15 above, see the instructions for line 15 on page 5 before completing lines 21 through 25.*

21	Multiply $190 by the number of days in the LTC period	21	12,540
22	Enter the costs incurred for qualified LTC services provided for the insured during the LTC period (see page 7 of the instructions).	22	8,250
23	Enter the **larger** of line 21 or line 22	23	12,540
24	Enter the total reimbursements received for qualified LTC services provided for the insured during the LTC period	24	
	Caution: *If you received any reimbursements from LTC contracts issued before August 1, 1996, see page 7 of the instructions.*		
25	Per diem limitation. Subtract line 24 from line 23	25	12,540
26	**Taxable payments.** Subtract line 25 from line 20. If zero or less, enter -0-. Also include this amount in the total on Form 1040, line 21. On the dotted line next to line 21, enter "LTC" and the amount	26	0

Calculation of Line 21, Form 8853. The **contract period method** was used to compute the figure entered on line 21 of the Form 8853 above–the number of days in the LTC multiplied by the allowable amount.

Under this method, the LTC period is the same period the insurance company used under the contract to compute the benefits paid to the insured. Jake's contract computed benefits on a daily basis ($110 for every day he was in the nursing home). Thus, the LTC period for line 21 is the number of days for which the insurer paid during 2000, not necessarily the number of days Jake was in the nursing home.

Box 1 of the 2000 Form 1099-LTC shows that Jake was paid $7,260, or $110 per day for 66 days in 2000. Therefore, the LTC period (line 23, Form 8853) is 66 days. The entry for line 21 of Form 8853 is calculated as follows:

2000 Daily limitation	$ 190
Days in the LTC period	66
Line 21 amount	$12,540

Calculation of Line 22, Form 8853. Line 22 is the cost of qualified long-term care services during the LTC period of 66 days.

Because the payment from the insurer for the month of December 2000 (received in January 2001) was not counted, neither is the amount Jake paid the nursing home for December.

Jake **paid** the nursing home regular rate of $125 per day as follows:

Month	Days	Rate	Paid	Date Paid
September	5	$125	$625	September 30, 2000
October	31	$125	$3,875	October 15, 2000
November	30	$125	$3,750	November 15, 2000
December	31	$125	$3,875	December 15, 2000
Total paid for 2000			$12,125	
Less December payment			($3,875)	
Amount for Line 22			**$8,250**	

Question 7A. How much of the 2000 long-term care benefits is taxable on the joint 2000 tax return of Jake and his wife Judith?

Answer 7A. None, as shown on line 26 on Form 8853.

10

Question 7B. Can Jake and Judith deduct any nursing home-related medical expenses on Schedule A of their 2000 joint return?

Answer 7B. Yes, as shown below, subject to the 7.5% of adjusted gross income floor.

Qualified long-term care premiums—Jake (age 58 - see limitations on page 338)	$ 820
Non-reimbursed nursing home expense (see chart below)	1,455
Amount to be included on line 1 of Schedule A	**$2,275**

The non-reimbursed nursing home expense is calculated as follows:

Line 22, Form 8853	$8,250
Less Line 17, Form 8853	(7,260)
Plus Jake's December nursing home expense paid in December	3,875
Less expected insurance reimbursement for December	(3,410)
Total to Schedule A as non-reimbursed nursing home expense	**$1,455**

III. SOCIAL SECURITY BENEFITS

Practitioner Note. This discussion addresses monthly survivor and disability benefits and the equivalent railroad retirement benefits. Supplemental security income payments (SSI) are not taxable and are not considered part of the formula when determining the taxable portion of social security benefits. See the Retirement chapter for further discussion of social security benefits.

Social security benefits are taxed under a two-tier system that taxes up to 50% of the benefits if the taxpayer's **combined income** exceeds the first threshold and up to 85% of the benefits if the taxpayer's combined income exceeds a second, higher threshold.

Combined Income. For purposes of calculating taxes on social security benefits, **combined income** is the sum of two figures:

1. The taxpayer's modified adjusted gross income
2. 50% of the taxpayer's social security benefits

Modified adjusted gross income is the taxpayer's adjusted gross income with the following modifications.

1. **The following exclusions are not allowed:**
   a. Income from U.S. savings bonds used to pay higher education tuition and fees (I.R.C. §135)
   b. Employer-paid qualified adoption expenses (I.R.C. §137)
   c. Foreign earned income (I.R.C. §911)
   d. Income from sources within Guam, American Samoa, the Northern Mariana Islands, and Puerto Rico (I.R.C. §§931 and 933)
2. The deduction for interest paid on qualified student loans is not allowed.
3. Tax-exempt interest is included.

The thresholds for 2000 vary by the taxpayer's filing status as follows:

Filing Status	If Combined Income is:	Then up to:
Single	More than $25,000 but not more than $34,000	50% of benefits are taxable
Single	More than $34,000	85% of benefits are taxable
Married filing jointly	More than $32,000 but not more than $44,000	50% of benefits are taxable
Married filing jointly	More than $44,000	85% of benefits are taxable
Head of household	More than $25,000 but not more than $34,000	50% of benefits are taxable
Head of household	More than $34,000	85% of benefits are taxable
Married filing separately*	More than $25,000 but not more than $34,000	50% of benefits are taxable
Married filing separately*	More than $34,000	85% of benefits are taxable

* If taxpayers who are married filing separately live together at any time during the year, then the threshold is zero. Consequently, up to 85% of social security benefits are included in taxable income.

If a taxpayer's combined income exceeds the 50% threshold but not the 85% threshold listed above, then the taxpayer must include in taxable income the lesser of the following:

1. 50% of social security benefits
2. 50% of the amount by which combined income exceeds the 50% threshold

If the taxpayer's combined income exceeds the 85% threshold listed above, then the taxpayer must include in taxable income the lesser of the following:

1. 85% of social security benefits
2. The sum of the following:
   a. 50% of the amount by which the 85% threshold exceeds the 50% threshold
   b. 85% of the amount by which combined income exceeds the 85% threshold

Tiered System Increases Marginal Tax Rate. Since the taxability of social security benefits is dependent on other income, some taxpayers are surprised to find that a relatively small amount of additional income pushes them over the threshold for taxing social security benefits and increases the incremental rate of tax.

Example 8. Anne is single and receives $12,000 per month in social security benefits in 2000. She prepared for her retirement by investing in an IRA, from which she draws $1,500 per month.

At this income level, her social security will **not** be taxed since the $18,000 IRA distribution plus 50% of her social security ($6,000) equals $24,000, which is **below** the threshold for taxing her social security.

Anne's 2000 federal income tax is $1,624 as shown below.

Adjusted gross income (IRA distributions)	$18,000
Standard deduction	($4,400)
Personal exemption deduction	($2,800)
Taxable income	**$10,800**
Income tax from Tax Table	**$1,624**

10

Social Security Benefits Worksheet—Lines 20a and 20b *Keep for Your Records*

Before you begin:

√ Complete Form 1040, lines 21, 23, and 25 through 31a, if they apply to you.
√ Figure any amount to be entered on the dotted line next to line 32 (see page 29).
√ If you are married filing separately and you **lived apart** from your spouse for all of 2000, enter "D" to the left of line 20a.
√ Be sure you have read the **Exceptions** on page 24 to see if you must use a publication instead of this worksheet to find out if any of your benefits are taxable.

1. Enter the total amount from **box 5** of **all** your **Forms SSA-1099** and **RRB-1099** **1.** *12,000*

2. Is the amount on line 1 more than zero?

☐ **No.** STOP None of your social security benefits are taxable.

☒ **Yes.** Enter one-half of line 1 . . . . . **2.** *6,000*

3. Add the amounts on Form 1040, lines 7, 8a, 9 through 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099 . . . . . **3.** *18,000*

4. Enter the amount, if any, from Form 1040, line 8b **4.** *0*

5. Add lines 2, 3, and 4 . . . . . **5.** *24,000*

6. Add the amounts on Form 1040, lines 23, and 25 through 31a, and any amount you entered on the dotted line next to line 32 . . . . . **6.** *0*

7. Subtract line 6 from line 5 . . . . . **7.** *24,000*

8. Enter: $25,000 if single, head of household, qualifying widow(er), or married filing separately and you **lived apart** from your spouse for all of 2000; $32,000 if married filing jointly; -0- if married filing separately and you lived with your spouse at any time in 2000 . . . . . **8.** *25,000*

9. Is the amount on line 8 less than the amount on line 7?

☒ **No.** STOP None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. **But** if you are married filing separately and you **lived apart** from your spouse for all of 2000, enter -0- on line 20b. Be sure you entered "D" to the left of line 20a.

Example 9. Assume the same facts as in Example 8 except that now Anne also has Series HH savings bonds that matured. She cashes them and receives $10,000 of interest income.

The calculation to determine if any of her social security benefits will be taxed has a different result. **Anne's combined income is $9,000 over the 50% threshold as shown below**.

IRA distribution	$18,000
Savings bond interest	$10,000
50% of social security benefits	$6,000
Combined income	**$34,000**
Less: 50% threshold	($25,000)
Excess over threshold	**$9,000**

Fifty percent of that excess ($4,500) is added to taxable income. Therefore, Anne's 2000 federal income tax is $3,799 as shown below.

IRA distribution	$18,000
Savings bond interest	$10,000
Taxable social security benefits	$4,500
Adjusted gross income	$32,500
Standard deduction	($4,400)
Personal exemption deduction	($2,800)
Taxable income	**$25,300**
Income tax from Tax Table	**$3,795**

Social Security Benefits Worksheet—Lines 20a and 20b

Keep for Your Records

Before you begin:

√ Complete Form 1040, lines 21, 23, and 25 through 31a, if they apply to you.

√ Figure any amount to be entered on the dotted line next to line 32 (see page 29).

√ If you are married filing separately and you **lived apart** from your spouse for all of 2000, enter "D" to the left of line 20a.

√ Be sure you have read the **Exceptions** on page 24 to see if you must use a publication instead of this worksheet to find out if any of your benefits are taxable.

1. Enter the total amount from **box 5** of **all** your **Forms SSA-1099** and **RRB-1099** **1.** *12,000*

2. Is the amount on line 1 more than zero?

☐ **No.** STOP None of your social security benefits are taxable.

☒ **Yes.** Enter one-half of line 1 . . . **2.** *6,000*

3. Add the amounts on Form 1040, lines 7, 8a, 9 through 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099 . . . **3.** *28,000*

4. Enter the amount, if any, from Form 1040, line 8b . . . **4.** *0*

5. Add lines 2, 3, and 4 . . . **5.** *34,000*

6. Add the amounts on Form 1040, lines 23, and 25 through 31a, and any amount you entered on the dotted line next to line 32 . . . **6.** *0*

7. Subtract line 6 from line 5 . . . **7.** *34,000*

8. Enter: $25,000 if single, head of household, qualifying widow(er), or married filing separately and you **lived apart** from your spouse for all of 2000; $32,000 if married filing jointly; -0- if married filing separately and you lived with your spouse at any time in 2000 . . . **8.** *25,000*

9. Is the amount on line 8 less than the amount on line 7?

☐ **No.** STOP None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. **But** if you are married filing separately and you **lived apart** from your spouse for all of 1999, enter -0- on line 20b. Be sure you entered "D" to the left of line 20a.

☒ **Yes.** Subtract line 8 from line 7 . . . **9.** *9,000*

10. Enter: $9,000 if single, head of household, qualifying widow(er), or married filing separately and you **lived apart** from your spouse for all of 2000; $12,000 if married filing jointly; -0- if married filing separately and you lived with your spouse at any time in 2000 . . . **10.** *9,000*

11. Subtract line 10 from line 9. If zero or less, enter -0- . . . **11.** *0*

12. Enter the **smaller** of line 9 or line 10 . . . **12.** *9,000*

13. Enter one-half of line 12 . . . **13.** *4,600*

14. Enter the **smaller** of line 2 or line 13 . . . **14.** *4,500*

15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0- . . . **15.** *0*

16. Add lines 14 and 15 . . . **16.** *4,500*

17. Multiply line 1 by 85% (.85) . . . **17.** *10,200*

18. **Taxable social security benefits.** Enter the **smaller** of line 16 or line 17 . . . **18.** *4,500*

- Enter the amount from line 1 above on Form 1040, line 20a.
- Enter the amount from line 18 above on Form 1040, line 20b.

TIP If part of your benefits are taxable for 2000 **and** they include benefits paid in 2000 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

10

Observation. The additional $10,000 of interest income increased Anne's taxes by $2,175 ($3,799 – $624). **Even though Anne is in the 15% bracket, the effective marginal tax rate on the additional $10,000 is over 21%!**

LUMP-SUM PAYMENTS FOR RETROACTIVE SOCIAL SECURITY BENEFITS

The taxable part of a lump-sum (retroactive) payment of benefits received in 2000 are included in 2000 income, even if the payment includes benefits for an earlier year.

Practitioner Note. Don't confuse this lump-sum benefit payment with the lump-sum death benefit paid by social security to the surviving spouse. That death benefit is **not** taxable.

Election To Report as Earlier Year. Generally, a taxpayer's 2000 income is used to calculate the taxable part of the total benefits received in 2000. However, **the taxable part of a lump-sum payment for an earlier year may be calculated separately, using the taxpayer's income for the earlier year.** A taxpayer can elect this method if it **lowers** his or her taxable social security benefits.

Under the lump-sum election method, the taxable part of the taxpayer's benefits for the earlier year (including the lump-sum payment) is calculated using that year's income. Then any taxable benefits for that year that were previously reported are subtracted. The remainder is the taxable part of the lump-sum payment. Add it to the taxable part of social security benefits for 2000.

Practitioner Note. Since the earlier year's taxable benefits are included in 2000 income, no adjustment is made to the earlier year's return. Do **not** file an amended return for the earlier year.

Worksheets for this calculation are available in IRS Publication 915, *Social Security and Equivalent Railroad Retirement Benefits.*

The lump-sum election can be revoked only with the consent of the Internal Revenue Service.

Form SSA-1099 shows the lump-sum payment broken down by the applicable years for the settlement. Form RRB-1099 does not show a breakdown by year. Contact the Railroad Retirement Board for the appropriate amount per year.

See the Retirement chapter for a comprehensive example on lump-sum payments of retroactive social security benefits.

REPAYMENTS MORE THAN GROSS BENEFITS

In some situations, Form SSA-1099 or Form RRB-1099 will show that the total benefits repaid (box 4) are more than the gross benefits (box 3) received. If this occurs, the net benefits in box 5 will be a negative figure and none of the benefits will be taxable. If the taxpayer receives more than one form, a negative figure in box 5 of one form is used to offset a positive figure in box 5 of another form for that same year. If a joint return is filed, the negative and positive figures in box 5 from both spouses' Form SSA-1099 or Forms RRB-1099 are netted.

Repayment of Benefits Received in an Earlier Year. If the total amount (shown in box 5) of the combination of all a taxpayer's (and spouse's if a joint return) benefits is a negative figure, the taxpayer can take an itemized deduction for the amount of the negative figure that represents benefits included in gross income in an earlier year.

If this deduction is $3,000 or less, it is subject to the 2%-of-adjusted-gross-income limit and is claimed on line 22 of Schedule A (Form 1040).

If the deduction is more than $3,000, the tax should be calculated in two ways:

1. Calculate the tax for 2000 with the itemized deduction. This more-than-$3,000 deduction is not subject to the 2%-of-adjusted-gross-income limit that applies to certain other miscellaneous itemized deductions.
2. Calculate the tax for 2000 as follows:
   - **a.** Figure the tax without the itemized deduction.
   - **b.** For each year after 1983 for which part of the negative figure represents a repayment of benefits, refigure taxable benefits as if the taxpayer's total benefits for the year were reduced by that part of the negative figure. Then recalculate the tax for that year.
   - **c.** Subtract the total of the recalculated tax amounts in (b) from the total of the actual tax.
   - **d.** Subtract the result in (c) from the result in (a).

Compare the tax calculated in methods (1) and (2). The tax for 2000 is the smaller of the two amounts. If method (1) results in less tax, take the itemized deduction on line 27, Schedule A (Form 1040). If method (2) results in less tax, claim a credit for the applicable amount–the amount calculated in 2(c)–on line 63 of Form 1040 and write "I.R.C. §1341" in the margin to the left of line 63. If both methods produce the same tax, deduct the repayment on line 27, Schedule A (Form 1040).

Practitioner Note. See page 305 in the 1996 *Farm Income Tax Workbook* for an example of this issue.

HOW RAILROAD RETIREMENT BENEFITS FIT IN

Equivalent tier 1 railroad retirement benefits are the part of tier 1 benefits that a railroad employee or beneficiary would have been entitled to receive under the social security system. They are commonly called the social security equivalent benefit (SSEB) portion of tier 1 benefits.

The RRB-1099 reports as separate items both the SSEB portion and the other portion of railroad retirement benefits, which is taxed as normal retirement income.

VOLUNTARY WITHHOLDING

Taxpayers who receive social security benefits or tier 1 railroad retirement benefits may request that federal income tax be withheld by completing Form W-4V, Voluntary Withholding Request.

The taxpayer may choose to have federal income tax withheld at the following percentages:

7%, 15%, 28%, or 31% of benefits received

The form is filed with the payer of the benefits.

UNDER 65—EARNINGS STILL RESTRICTED FOR 2000

Although the earnings cap for those working and drawing social security benefits was eliminated as of January 2000 for those age 65 and over, the restriction still applies to workers under age 65.

For the year 2000, the maximum amount a person under age 65 can earn and still receive full benefits is $10,080.

Special Payments after Retirement. In some cases, special payments are received for work done prior to the time that the individual began drawing benefits. Usually these payments do not affect benefits if the Social Security Administration knows that the payments are for work done prior to retirement. Bonuses, vacation pay, commissions, accumulated sick pay, and carryover crops might fall in this category. Although such payments are taxable for federal income tax purposes, they normally do not count as earned income toward the earnings limit for drawing full benefits.

There has been some confusion with **carryover grain sales** made by retired farmers. Here are the rules.

Grain sales are excluded from earnings from self-employment for purposes of reducing social security benefits if **both** of the following are true:

1. The grain was produced and in storage before or during the first month the individual begins drawing benefits.
2. The grain is sold in a year after the first year the individual draws social security benefits (see 20 CFR 404.429(b)(2)(ii)(A)).

Practitioner Note. These carryover grain sales must be reported on Schedule F and are subject to self-employment tax.

WHEN WILL TAXPAYERS BE ELIGIBLE TO DRAW FULL BENEFITS?

If a taxpayer was born in 1937 or earlier, he or she is part of the last group of people who can retire with full benefits at age 65.

Worker Born in:	Age to Collect Full Benefits
1938	65 years, 2 months
1939	65 years, 4 months
1940	65 years, 6 months
1941	65 years, 8 months
1942	65 years, 10 months
1943 through 1954	66 years, 0 months
1955	66 years, 2 months
1956	66 years, 4 months
1957	66 years, 6 months
1958	66 years, 8 months
1959	66 years, 10 months
1960 and later	67 years, 0 months

QUICK POINTS ON SOCIAL SECURITY

1. **Timing of benefit checks.** Individuals already receiving benefits **prior to May 1997** are paid on the third of the month. If the third falls on a Saturday, Sunday, or Monday holiday, the payment is made on the preceding Friday.

   For individuals who begin drawing benefits **after April 1997,** checks are paid based on the birth date of the individual on whose account the checks are based.

Date of Birth	Benefits Paid on:
1st–10th	Second Wednesday
11th–20th	Third Wednesday
21st–31st	Fourth Wednesday

2. Social security provides the equivalent of a $198,000 disability policy and a $313,000 life insurance policy for the average earner with a family of four.

3. Average social security benefits for 2000:

Retired worker	$804
Retired worker & spouse	$1,348
Disabled worker	$754
Disabled worker, spouse & children	$1,255
Widow(er) of worker	$775
Widow(er) with two children	$1,611

4. Social security tele-service: 800-72-1213
5. Wage earners and self-employed individuals earn one quarter credit for each $780 of earnings in 2000, for up to four quarters per year.

IV. MEDICARE/MEDICAID

MEDICARE BASICS

The Health Care Financing Administration (HCFA) administers Medicare, the nation's largest health insurance program, which covers 39 million Americans.

Medicare is a health insurance program for people 65 years of age and older, some disabled people under 65 years of age, and people with end-stage renal disease (permanent kidney failure treated with dialysis or a transplant).

Medicare coverage includes Part A (Hospital Insurance) and Part B (Medical Insurance).

Part A covers the following:

Hospital stays: semiprivate room, meals, general nursing, and other hospital services and supplies.

The patient is responsible for:

First $776 as a deductible for a hospital stay of 1–60 days

$194 per day for days 61–90 of a hospital stay

$388 per day for days 91–150 of a hospital stay

All cost for each day beyond 150 days

Skilled nursing facility care: semiprivate room, meals, skilled nursing, rehabilitative services, and other services and supplies (after a 3-day hospital stay)

The patient is responsible for:

Nothing for the first 20 days

Up to $97 per day for days 21–100

All costs beyond the 100th day in the benefits period

Home health care: part-time skilled nursing care, physical therapy, speech-language therapy, home health aide services, and durable medical equipment and supplies

The patient is responsible for:

Nothing for home health care services

20% of approved amount for durable medical equipment

Hospice care: medical and support services from a Medicare-approved hospice, drugs for symptom control and pain relief, short-term respite care, and care in a hospice facility, hospital, or nursing home when necessary

The patient is responsible for:

A co-payment of up to $5 for outpatient prescription drugs and 5% of the Medicare payment amount for inpatient respite care (short term care given to a hospice patient by another caregiver so that the usual caregiver can rest)

Blood: given at a hospital or skilled nursing facility during a covered stay

The patient is responsible for:

The first three pints of blood

Part B covers the following:

Medical and other services: doctors' services (except for routine physical exams), outpatient medical and surgical services and supplies, diagnostic tests, ambulatory surgery center facility fees for approved procedures and durable medical equipment, and outpatient physical and occupational therapy including speech-language therapy and mental health services

The patient is responsible for:

$100 deductible (paid once per calendar year)

20% of approved amount after the deductible, except in the outpatient setting

20% for all outpatient physical and speech therapy services and 20% for all outpatient occupational therapy services

50% for most outpatient mental health

Clinical laboratory services: blood, urinalysis, and so on

The patient is responsible for:

Nothing for services

Home health care: part-time skilled care, home health aide services, durable medical equipment when supplied by a home health agency while getting Medicare-covered home health care, and other supplies and services

The patient is responsible for:

Nothing for services

20% of approved amount for durable medical equipment

Outpatient hospital services: services for the diagnosis or treatment of an illness or injury

The patient is responsible for:

20% of the charged amount (after the deductible); during the year 2000, this will be changed to a set copayment amount

Blood: pints of blood needed as an outpatient, or as part of a Part B–covered service

The patient is responsible for:

The first three pints of blood, then 20% of the approved amount for additional pints of blood (after the deductible)

TRANSFERRING ASSETS AND LONG-TERM CARE ASSISTANCE

Clients often ask their tax preparers about transferring assets in order to qualify for medical assistance. Transfers can be made for this purpose, but the rules that govern such transfers are complex. Both state and federal laws must be studied before a preparer can give good advice on such transfers. That discussion is beyond the scope of these materials.

V. LIFE INSURANCE PROCEEDS

Life insurance proceeds paid because of the death of the insured are not subject to federal income tax unless the policy was turned over to the beneficiary for a price.

If death benefits are paid to the beneficiary in a lump sum or other than at regular intervals, the taxable amount is the difference between the amount received and the amount that was receivable at the time of the insured person's death. If the benefit payable at death was not specified, the benefit payments that are more than the present value of the payments at the time of death are included in income.

INSTALLMENT PAYMENTS

Set Number of Installments. If the insurance proceeds are received in installments, a part of each installment is excluded from income. To determine the excluded part, divide the amount held by the insurance company (generally, the total lump sum payable at the death of the insured) by the number of installments to be paid. Include anything over this excluded part in income as interest.

Installments for Life. If the beneficiary under the insurance contract is entitled to receive the proceeds in installments for the rest of his or her life, without a refund or period-certain guarantee, calculate the excluded part of each installment by dividing the amount held by the insurance company by the beneficiary's life expectancy. If there is a refund or period-certain guarantee, the amount held by the insurance company for this purpose is reduced by the actuarial value of the guarantee.

Older Contracts. There are still some old insurance contracts on decedents who died prior to October 23, 1986, with the spouse as beneficiary and the proceeds payable in installments with a special tax benefit. Surviving spouses currently collecting on these contracts can exclude up to $1,000 per year of the interest included in the installments. Even if the surviving spouse remarries, he or she can continue to make the exclusion.

SURRENDER OF POLICY FOR CASH VALUE

If a life insurance policy is surrendered for cash, the excess received over the cost of the policy is reported as income. In such a situation, there should be a Form 1099-R from the insurance company included with the return.

ENDOWMENT PROCEEDS

Endowment proceeds paid in a lump sum at maturity are taxable only if the proceeds are more than the cost of the policy. To determine the cost, add the aggregate amount of premiums or other consideration paid for the contract and subtract any amount that was previously received under the contract and excluded from income. Include any amount of the lump-sum payment over the cost in income.

Endowment proceeds that the taxpayer chooses to receive in installments instead of a lump sum at the maturity of the policy are taxed as an annuity. For this treatment to apply, the taxpayer must choose to receive the proceeds in installments before receiving any part of the lump sum. This election must be made within 60 days after the lump-sum payment first becomes payable.

Survivor Benefits. Generally, payments made by or for an employer because of an employee's death must be included in income.

ACCELERATED DEATH BENEFITS

Certain payments received under a life insurance contract on the life of a **terminally or chronically ill** insured person **before** his or her death can be **excluded** from income. For a chronically ill individual, the payments must be for costs incurred for qualified long-term services or made on a periodic basis without regard to the costs.

Also, if any portion of a death benefit under a life insurance contract on the life of a terminally or chronically ill individual is sold or assigned to a viatical settlement provider, the amount received is also excluded from income. Generally, a viatical settlement provider is one who regularly engages in the business of buying or taking assignment of life insurance contracts on the lives of insured individuals who are terminally or chronically ill.

To claim an exclusion for accelerated death benefits made on a per-diem or other periodic basis, you must file **Form 8853,** Medical Savings Accounts and Long-Term Care Insurance Contracts, with the return. The accelerated death benefits are reported on line 19, Section C of the form (see pages 340–341).

What is Terminally or Chronically Ill? A terminally ill person is one who has been certified by a physician as having an illness or physical condition that can reasonably be expected to result in death within 24 months from the date of certification.

A chronically ill person is one who is not terminally ill but has been certified by a licensed health care practitioner as meeting either of the following conditions:

1. The person is unable to perform (without substantial help) at least two activities of daily living for a period of 90 days or more because of a loss of functional capacity
2. The person requires substantial supervision to protect himself or herself from threats to health and safety due to severe cognitive impairment

Exception to the accelerated death benefit rule:

The exclusion does not apply to any amount paid to a person other than the insured if that other person has an insurable interest in the life of the insured due to either of the following circumstances:

- The insured is a director, officer, or employee of the other person.
- The insured has a financial interest in the business of the other person.

VI. CREDITS

CREDIT FOR THE ELDERLY OR DISABLED

The credit for the elderly or disabled is for low-income taxpayers age 65 or older, or for permanently and totally disabled persons.

The credit is claimed by filing Schedule R, Credit for the Elderly or Disabled.

Nontaxable social security must be less than $7,800 for married filing jointly if both spouses are eligible. Adjusted gross income may not exceed the following:

Filing Status	Amount
Single, Head of Household, Qualifying Widow(er)	$17,500
Married Filing Jointly (one spouse eligible)	20,000
Married Filing Jointly (both spouses eligible)	25,000
Married Filing Separately (lived apart entire year)	12,500

Who Qualifies for the Credit?

- Persons age 65 or older
- Persons **under 65** who are retired because of permanent and total disability and meet the following criteria:
  1. Received taxable disability income
  2. Did not reach mandatory retirement age before the tax year (mandatory retirement age is the age set by the employer at which the individual would have had to retire had he or she not become disabled)
- Must be a U.S. citizen or resident (in most cases)
- If married at the end of the year, must normally file a joint return, unless the taxpayers did not live together at any time during the year

What is Permanent and Total Disability? A taxpayer is permanently and totally disabled if he or she cannot engage in any substantial gainful activity because of a physical or mental condition. A physician must certify that the condition has lasted or can be expected to last continuously for 12 months or that the condition can be expected to result in death.

What is Substantial Gainful Activity? Substantial gainful activity is the performance of significant duties over a reasonable period of time while working for pay or profit, or in work generally done for pay or profit.

Full-time work (or part-time work done at the employer's convenience) in a competitive work situation for at least the minimum wage conclusively shows that the taxpayer is able to engage in substantial gainful activity.

Substantial gainful activity is not work the taxpayer does to take care of himself or herself or the taxpayer's home. It is not unpaid work on hobbies, institutional therapy or training, school attendance, clubs, social programs, and similar activities. However, doing this kind of work may show that the taxpayer is able to engage in substantial gainful activity.

CHILD AND DEPENDENT CARE CREDIT

Care for a Dependent Parent. The same credit that is available for parents who pay someone to care for a child or children under age 13 so that the parents can work is available for the care of a spouse or dependent (possibly an elderly parent) who is not able to care for himself or herself.

The credit can be up to 30% of the expenses paid so that the taxpayer could work or look for work. The individual cared for must live in the same home as the taxpayer. The credit is not available for money paid to the taxpayer's spouse, a person the taxpayer can claim as a dependent, or to the taxpayer's child who is under age 19 at the end of the year.

The individual cared for must be eligible to be claimed as a dependent on the taxpayer's return. There is an **exception** for a person who is physically or mentally unable to care for himself or herself and could be claimed as a dependent on taxpayer's return were it not for the gross income limitation.

To claim the credit, **file Form 2441** with the tax return and include the care provider's name, address, tax identification number, and the amount paid, as well as the name and tax identification number of the person cared for.

Note that the dependent care credit is available to married couples living together in the same household only if they file jointly.

The credit on which the expense is based is limited to the earned income of the lower-earning spouse. There is an exception for a student or disabled spouse: if one spouse is a full-time student or one spouse is disabled, you can count that person as having made $200 per month with one qualifying individual and $400 per month with two or more qualifying individuals to care for.

EARNED INCOME CREDIT

Although we do not normally think of the earned income credit in connection with older taxpayers, there are at least two possible applications.

1. **Many grandparents are now raising grandchildren. If they qualify for the earned income credit, the same rules will apply to them as apply to parents.**
2. If there are no qualifying children, the couple may be eligible for the limited earned income credit.

   - The modified AGI and earned income must be less than $10,200 (1999 figure)
   - Must be at least 25 years old but **less than 65** at the end of the year
   - Taxpayer cannot qualify as a dependent on any other return.
   - On a joint return, only one spouse must be under age 65 to qualify for limited EIC

SOURCES OF INFORMATION

IRS publications

Older Americans' Tax Guide–Publication 554
Insurance Proceeds–Publication 525
Annuities–Publication 575
Social Security and Equivalent Railroad Retirement Benefits–Publication 915

RETIREMENT