Chapter 9: Itemized Deductions

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Corrections were made to this workbook through January of 2003. No subsequent modifications were made.

With the increased standard deduction, fewer taxpayers are able to itemize their personal deductions. For those who do itemize, this chapter is designed to cover some of the lesser-known itemized deductions.

MEDICAL EXPENSES

COST OF WEIGHT-LOSS PROGRAM

Despite lobbying by many health organizations, the IRS did not recognize obesity as a disease. However, in recent years, the IRS has softened its position on treatments previously not allowed, such as smoking-cessation programs and alcohol and drug addiction programs. In these instances, the patient had to be directed by his/her physician to stop smoking or to seek help for alcoholism or drug addiction. Beginning in 2002, treatment for obesity is on the list.

On April 2, 2002, the IRS released Rev. Rul. 2002-19, describing situations where taxpayers are able to deduct treatment for weight-loss control. The announcement indicated the IRS will allow the cost of weight-loss programs as a deductible medical expense if prescribed as a treatment for obesity. **More importantly for many taxpayers, it also allows the costs to be paid with pre-tax dollars allocated to the medical-expense portion of a flexible spending account (I.R.C. §125 plan).**

Prior to Rev. Rul. 2002-19, the IRS did not recognize obesity as an illness. Therefore, payments made for weight-loss programs did not qualify as a deductible medical expense. These expenses can cost thousands of dollars each year. Under the new rules, if a medical doctor prescribes a weight-loss program for the treatment of obesity, the payments will be deductible. The **cost of special foods**, taken in conjunction with the program, **will not be deductible** if they are a substitute for food that would normally be consumed.

If the taxpayer joins the program for improvement of their general health or appearance, the costs are still not deductible. However, if the program is prescribed by a physician as treatment for hypertension, even though the person is not obese, the payments will qualify.

Questions remain regarding how the new ruling will be tested in the courts. The definition of obesity is yet to be addressed. At what point does overweight end and obesity start? Will it be based on existing weight/height charts or other means? Other factors not addressed in the ruling are questions about whether a weight-loss program will include an exercise program or whether the purchase of exercise equipment or the cost of membership in a health club will qualify.

Also to be considered is the IRS position for weight-loss programs for previous open years. The IRS says its new position on prescribed weight-loss programs would apply retroactively to past years as well as to future years. For amended returns, taxpayers would need to go back to their physicians who would then review their past medical records.

Example 1. Sam and Amy Moore's 16-year-old daughter, Elizabeth, has been diagnosed as being obese. Elizabeth's physician recommended she join a weight-loss group to facilitate her recommended weight loss. The costs incurred by Elizabeth will not be reimbursed by insurance or other sources. In 2002, Sam and Amy

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have spent $533 at the Weight-Off Program on behalf of Elizabeth. This will be allowed for purposes of medical deductions.

MEDICAL DEDUCTIONS RULINGS

In a 2001 Tax Court Summary Opinion, the courts allowed, as a medical deduction, the cost of cosmetic surgery to remove excess skin from a taxpayer who had lost more than 100 pounds. The weight loss had resulted in a mass of loose, hanging skin. Even though the physician classified the procedure as cosmetic surgery, the surgery promoted the proper function of the individual's body and treated her disease. (*C.S. Al-Murshidi v. Commr.*, TC Summary Opinion 2001-185, December 13, 2001.)

In a 2000 Rev. Rul., the IRS allowed the costs of attending a medical conference as a medical deduction. The conference was related to a chronic disease from which the taxpayer's dependent suffers. The deductible items included the cost of admission and the travel costs to and from the conference. The meal and lodging costs while attending the conference were not deductible. The taxpayer traveled to the conference on the recommendation of the physician that the information gained would be valuable in providing for the treatment and care of the dependent (Rev. Rul. 2000-24).

COST OF CAPITAL IMPROVEMENTS

Capital expenditures are generally not deductible for Federal income tax purposes. However, an expenditure may qualify as a medical expense if its primary purpose is for the medical care of the taxpayer, a spouse, or dependent. Therefore, a capital expenditure which is related only to the sick person and is not related to permanent improvement or betterment of property, may be deductible. Examples include:

- an expenditure for eye glasses,
- a seeing eye dog,
- artificial teeth and limbs,
- a wheelchair or crutches,
- an inclinator, and
- an air conditioner that is detachable from the property and purchased only for the use of a sick person.

A capital permanent improvement that would not ordinarily be for the purpose of medical care may still qualify as a medical expense. It would qualify to the extent that the expenditure exceeds the increase in the value of the property.

Example 2. Sam's parents, Alan and Kassie are married. Kassie suffers from a chronic heart condition which restricts her ability to walk. Alan is advised by Kassie's physician to install an elevator in their residence so Kassie will not be required to climb stairs. The cost of installing the elevator is $10,000, and the increase in the value of the residence is determined to be only $7,000. The $3,000 difference is the amount in excess of the value, and is deductible as a medical expense. If, by reason of this expenditure, it is determined that the value of the residence has decreased, the entire cost of installing the elevator would qualify as a medical expense.

Expenditures made for the operation or maintenance of a capital asset are likewise deductible medical expenses if they have as their primary purpose the medical care of the taxpayer, spouse, or dependent. Normally, if a capital improvement qualifies as a medical expense, expenditures for the operation or maintenance of the capital asset also qualify. This is true only if the medical reason for the capital expenditure still exists. The entire amount of such operation and maintenance expenditures qualify, even if none or only a portion of the original cost of the capital asset itself qualified.

Example 3. Amy sustained a back injury in an automobile accident three years ago. Amy worked as a home health care nurse and was traveling from one site to another for her employer at the time of the accident. She has used a wheelchair for the last several years. This year, Amy and her husband, Sam, decided to have a ramp built for easier wheelchair access to their home at both the front and back entrances. The cost of the capital improvement was $1,890. It has been determined that the addition of the two ramps will reduce the value of

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their home, rather than increase it. The entire cost of the capital improvement is allowed for purposes of medical deductions.

CURRENT YEAR MEDICAL REIMBURSEMENTS DEDUCTIONS TAKEN IN A PRIOR YEAR

If a taxpayer claims a medical expense deduction and in a later year is reimbursed for the expense, the reimbursement is gross income to the taxpayer in the year received to the extent of the deduction previously allowed (Reg. §1.213-1(g)(1)). If the taxpayer didn't itemize, or his/her medical expenses didn't exceed 7.5% of AGI, and no medical expense deduction was allowed in the year in which expenses occurred, any reimbursement received in a later year for the medical expenses previously paid is **not** includable in gross income.

Example 4. In 2001, Sam and Amy paid $6,972 for physician and hospital expenses relating to gall bladder surgery for Amy. They had an AGI for 2001 of $70,523. They took a 2001 deduction of $1,683 for medical expenses. In 2002, Acme Insurance sent a check to Sam and Amy for $780.

Payment in 2001 for medical care		$6,972
Less 7.5% of AGI ($70,523)	($5,289)	
Total 2001 medical expense deduction	$1,683	
Total 2002 medical expense reimbursement	$780	
Amount includible in 2002 gross income	$780	

Note. If the amount of the reimbursement had been $1,700, only $1,683 would be includable in gross income this year.

TAXES

POSSIBLE DEDUCTIONS

Taxpayers cannot deduct amounts paid for local benefits that tend to increase the value of their property. Local benefits include construction of streets, sidewalks, or water and sewer systems. Taxpayers must add these amounts to the basis of their property.

Assessments, or taxes for local benefits, **can** be deducted if they are for maintenance, repair, or interest charges related to those benefits. An example is a charge to repair an existing sidewalk and any interest included in that charge.

If only a portion of the assessment is attributed to maintenance, repair, or interest charges, taxpayers must be able to show the specific portion in order to claim the deduction. If they cannot show what portion of the assessment is for maintenance, repair, or interest charges, they cannot deduct any of the charge. An assessment for a local benefit may be listed as an item in a real estate tax bill. In this situation, the rules in this section can be used to determine the amount, if any, that can be deducted.

Taxpayers cannot deduct transfer taxes (or stamp taxes) and charges on the sale of a personal residence. If the buyer pays them, they include the charges in the cost basis of the property. If the seller pays them, they are expenses of the sale and reduce the amount realized on the sale.

Homeowner association assessments are not deductible because the homeowner association, rather than a state or local government, imposes the assessment.

REAL ESTATE TAXES ON VACATION HOMES

If a taxpayer owns a vacation home, real estate taxes are deductible as long as the home meets the qualification for a second residence. If the vacation home is rented for a part of the year, the number-of-days-rented test applies.

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Example 5. Sam and Amy own a vacation home in Canada. They spent two weeks in their cabin during July of 2002. They did not collect rent on the cabin during the year. They paid $2,483 in real estate tax and $3,897 of mortgage interest on the cabin.

Question 5A. Will Sam and Amy be able to deduct mortgage interest and real estate taxes for their second home on their Schedule A?

Answer 5A. Since they did not collect rent on their cabin in 2002, they will be able to deduct the real estate tax and mortgage interest as itemized deductions. However, other rules apply if the home is rented for various periods of time.

If personal use of the home is **greater than 10%** of the number of days in the year the home is rented at fair market value (FMV), or 14 days, the home is considered a residence and the vacation home deductions apply. If Sam and Amy had collected rent for their vacation home for 28 days, their vacation home would still qualify as a second residence, since they occupied it for 14 days (10% × 28 days = 2.8 days).

If personal use of the home is **less than 10%** of the number of days in the year the home is rented at FMV, or 14 days, the taxpayer must use the passive-activity rules and the personal-mortgage-interest rules to maximize deductions. If Sam and Amy collected rent for their vacation home for 280 days, it would be classified as rental property, since 10% of 280 days is greater than the 14 days Sam and Amy occupied the home.

If rental use of the vacation home is less than 15 days, the income generated from the rental is excluded from the taxpayer's income. If Sam and Amy collected rent for their vacation home for 10 days, they would not recognize taxable income.

Note. The IRS allows rent-related deductions based on the ratio of annual rental days to total days of use (personal and rental). However, the Tax Court, upheld by the Ninth Circuit in (*D.D. Bolton*, 82-2 USTC ¶9699, ¶14,858.15) and Tenth Circuit (*E.G.McKinney*, 83-2 USTC ¶9655, ¶14,858.15) disagrees with IRS (Prop. Reg. §1.280A-3(c)(1)) on the allocation of mortgage interest and taxes. In the Tax Court formula, the rental-use portion of property taxes and mortgage interest is determined by dividing annual rental-use days by 365. Thus, the Tax Court's allocation method gives the taxpayers with vacation homes that are primarily used as residences the advantage. This method allows more operating and basis-adjustment expenses to be used currently, while increasing the personal-use portion of mortgage interest and taxes, which are fully deductible on Schedule A.

PAYMENT OF REAL ESTATE TAXES FOR SOMEONE OTHER THAN TAXPAYER

Taxes are deductible only by the person on whom they are imposed or, if imposed on property, by the property owner. There are exceptions for real property tax apportionment between a purchaser and seller, shareholder tax paid by corporation, taxes imposed on cooperative housing corporation, and taxes paid by persons having beneficial interest in property.

Example 6. Sam's brother George has fallen behind on his bills. Sam does not want to see the family name published in the local newspaper on the delinquent property tax list. He tells George he will pay the taxes for him.

Question 6A. Can Sam take a deduction for the real estate taxes he paid on behalf of George?

Answer 6A. Since it is not Sam's debt, he will not be able to take a deduction for the real estate taxes paid for George.

Question 6B. Can George take the deduction?

Answer 6B. Maybe. There is no strict requirement that the person taking the deduction be the person having paid the tax. However, in court cases on this issue, the payor had some type of interest in the property, such as being a mortgage holder. The exception to being a mortgage holder is the case *D.G. Peters v Commr*, 29 TCM 1440, Dec. 30,419(M), TC Memo. 1097-314.

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Note. A better choice might be to gift George the amount of back taxes and have George pay and deduct the tax.

MOTOR VEHICLE REGISTRATION FEES

As a general rule, automobile license fees are nondeductible as a Schedule A deduction. The license fee is assessed on an annual basis and imposed on the ownership of the vehicle or for the privilege of driving it on the state's highways. However, if the tax is based on the value of the automobile, as in Colorado and Missouri, or is based on an age and value classification, as in Indiana, portions of the tax are deductible.

INTEREST EXPENSES

INVESTMENT INTEREST

Investment interest is interest on indebtedness incurred to purchase or carry property held for investment. Generally, it is deductible for alternative minimum tax (AMT) purposes to the same extent as for regular tax purposes. Thus, it is deductible to the extent that it does not exceed net investment income. Investment interest does not include qualified housing interest, even if it is allocable to property held for investment. However, it does include interest expenses attributable to investments in private bonds on which interest is taxable for AMT.

Any investment interest expense that is disallowed for either the regular tax or AMT is carried forward to the next tax year, when it is allowable. Since AMT amounts of investment interest and net investment income may differ from the corresponding regular tax amounts, a separate calculation of investment interest carryforward must be made for minimum tax purposes.

Example 7. Amy and Sam secured a loan in order to invest in Acme Stock. The investment didn't fare very well. They lost $2,345 when they sold the stock, but had $3,456 income on other investments this year. Their interest expense for the investment loan was $567.

Question 7A. Can Sam and Amy at least take a deduction for the investment interest expense on the loan?

Answer 7A. Since their investment income exceeds their investment interest, they are entitled to the deduction.

9

HOME EQUITY DEBT LIMITS

Home Equity Debt. With today's lower interest rates, many home owners look to home equity loans as an appealing source of money for education, vacation or home improvement needs. Home equity debt is considered qualified residence interest. Interest that is paid or accrued on up to $100,000 of home equity debt, secured by either the principal or second residence, is deductible (I.R.C. §163(h)(3)(C)).

Example 8. Sam and Amy purchased their home several years ago for $240,000, paying $40,000 down and financing $200,000. Over the years, they have paid down the mortgage to $65,000. The current value of their home is $310,000. Sam wants to borrow $110,000, secured by a second mortgage on the home for purposes other than to improve the home. Only $100,000 of debt qualifies as home equity debt and would be deductible.

Example 9. However, if Sam in **Example 8** used $1,890 to construct the wheelchair ramps, the interest on $101,890 would be deductible. Interest on the remaining $8,110 is personal interest and is not deductible.

Amount of equity loan	$110,000
Less base amount	(100,000)
Less amount used for home improvement	(1,890)
Non deductible amount	$8,110

Assuming that Sam and Amy paid $7,700 of interest on their home equity loan, $7,132 will be deductible as home mortgage interest (($101,890 ÷ $110,000) × ($7,700).

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CHARITABLE CONTRIBUTIONS

APPRECIATED PROPERTY

Reduction Rules for Individuals

In certain cases, the amount of deduction for appreciated property is different from the FMV of the property. There is an exception for gifts of ordinary income property and certain gifts of tangible personal property or capital gain property. Basically, the amount of the deduction is limited to the basis the taxpayer has in contributed property. The taxpayer cannot deduct more than the FMV of the property, even if it is less than the basis of the property. Also, the taxpayer is not entitled to a loss deduction if the FMV is less than the basis of the property. The assets that require an adjustment of the deduction include:

- inventory;
- other property held for sale to customers;
- capital assets held for less than the long-term holding period;
- property subject to depreciation, etc. recapture;
- property used in the taxpayers trade or business; and
- artworks, letters, memoranda and similar property created by or for the taxpayer.

The amount of deduction is not reduced if the taxpayer realized income (ordinary or capital gain) on the property.

If the donor contributes long-term capital gain property to a private foundation, other than one described in I.R.C. §170(b)(1)(E), the FMV is reduced by 50% of the gain the donor would have received on sale of the asset. Otherwise, the donor receives a deduction equal to the FMV of the property.

Intangible Personal Property

The above rule also applies to tangible personal property donated to a charitable organization, other than a private foundation, that puts the asset to an unrelated use. If the asset is sold by the organization and the proceeds are used to further the organization's exempt purpose, it is considered to be an unrelated use.

If the reduction rules limit the amount of the taxpayer's contribution to the adjusted basis of the contributed property, the tax benefit from the contribution is the same whether the taxpayer contributes the property in kind or sells it and donates the sales proceeds. However, a sale of the property increases the taxpayer's AGI, thereby increasing his contribution base. Thus, a sale may be favorable if the taxpayer is a large contributor or has contribution carryover from prior years. Nonetheless, certain tax deductions — such as medical expenses and employee business expenses — and other benefits are reduced or eliminated as the taxpayer's AGI increases.

Stock

If a taxpayer delivers, without any conditions, a properly endorsed stock certificate to a qualified organization or to an agent of the organization, the date of the contribution is the date of delivery. If the certificate is mailed and received through the regular mail, it is the date of mailing. If the taxpayer delivers the certificate to a bank or broker acting as their agent or to the issuing corporation or its agent, for transfer into the name of the organization, the date of the contribution is the date the stock is transferred on the books of the corporation.

Future Events

The taxpayer may not consider unexpected events happening after their donation of property in making the valuation. They may consider only the facts known at the time of the gift, and those that could be reasonably expected at the time of the gift.

FILING REQUIREMENTS

Form 8283 must be completed for all non-cash charitable contributions valued over $500.

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NON-CASH CHARITABLE CONTRIBUTIONS IN EXCESS OF $5,000

If a non-cash charitable contribution is deducted on Schedule A, the taxpayer must complete Section B of Form 8283 if the contribution exceeds $5,000.

The $5,000 limit is in total. If the taxpayer donates $3,000 of books to a college and $4,000 of books to a library, an appraisal is required since the $7,000 total contribution exceeds the $5,000 limit. To be a qualified appraisal, the appraisal must be completed 60 days or less before the date of the contribution and no later than the date of the contribution. The appraisal must be signed and dated by the appraiser. The taxpayer must retain the detailed appraisal and submit a summary appraisal attached to their income tax return.

If the gift consists of publicly-traded stock, those whose market quotation is readily available on an established securities market, the taxpayer need only complete a partially completed appraisal summary form.

If the donation consists of non-publicly-traded securities valued at $10,000 or less, only the partially completed appraisal summary form is required.

Example 10. In 2002, Sam and Amy made several charitable donations. Their donations are as follows:

- $3,000 of inventory from Sam's Schedule C business was donated to a local university.
- $4,500 of stock, held more than 12 months, was donated to the church.
- $2,500 of stock, held more than 12 months, was donated to the local hospital.
- Sam's baseball card collection, valued at $6,000, was donated to the church for their annual auction.

The calculation for the amount of gain that would be recognized if the assets were sold is shown below:

Property	FMV	Adjusted Basis	Recognized Gain if Sold
Inventory	$3,000	$2,000	$1,000
Stock to Church	4,500	4,000	500
Stock to Hospital	2,500	1,000	1,500
Baseball card collection for Auction	6,000	350	5,650
Total	**$16,000**	**$7,350**	**$8,650**

After making the adjustments required by the regulations, the amount of the charitable contribution deduction is shown on the following page:

Property	FMV	Reduction	Contribution Allowed
Inventory	$3,000	$1,000	$2,000
Stock to Church	4,500	0	4,500
Stock to Hospital	2,500	0	2,500
Baseball card collection for Auction	6,000	5,650	350
Total	**$16,000**	**$5,650**	**$9,350**

Note. The deduction for the baseball cards is limited to its basis because they are tangible personal property donated to a qualified exempt organization that immediately sold them. Thus, the baseball cards are not considered used for their exempt purpose. This is true even if they use the resulting cash for their exempt purpose.

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For Example 10

Form **8283** (Rev. October 1998)
Department of the Treasury
Internal Revenue Service

Noncash Charitable Contributions

▶ **Attach to your tax return if you claimed a total deduction of over $500 for all contributed property.**
▶ **See separate instructions.**

OMB No. 1545-0908
Attachment Sequence No. **55**

Name(s) shown on your income tax return: **Sam and Amy Moore**
Identifying number: 333-22-7777

Note: *Figure the amount of your contribution deduction before completing this form. See your tax return instructions.*

Section A—List in this section **only** items (or groups of similar items) for which you claimed a deduction of $5,000 or less. Also, list certain publicly traded securities even if the deduction is over $5,000 (see instructions).

Part I **Information on Donated Property—**If you need more space, attach a statement.

1	(a) Name and address of the donee organization	(b) Description of donated property
A	University of Champaign Foundation, 111 Campus Drive, Anytown, IL 11111	Laser pointer inventory
B	XYZ Church, 434 Main St., Anytown, IL 11111	40 shares of D&D stock
C	General Hospital, 567 State St., Anytown, IL 11111	50 shares of Elf stock
D		
E		

Note: *If the amount you claimed as a deduction for an item is $500 or less, you do not have to complete columns (d), (e), and (f).*

	(c) Date of the contribution	(d) Date acquired by donor (mo., yr.)	(e) How acquired by donor	(f) Donor's cost or adjusted basis	(g) Fair market value	(h) Method used to determine the fair market value
A	5/01/01	1/01	Purchase	2,000	3,000	Comparable sales
B	12/01/01	10/98	Purchase	4,000	4,500	Comparable sales
C	6/30/01	7/96	Purchase	1,000	2,500	Comparable sales
D						
E						

Part II **Other Information—**Complete line 2 if you gave less than an entire interest in property listed in Part I. Complete line 3 if conditions were attached to a contribution listed in Part I.

2 If, during the year, you contributed less than the entire interest in the property, complete lines a–e.

a Enter the letter from Part I that identifies the property ▶ _____. If Part II applies to more than one property, attach a separate statement.

b Total amount claimed as a deduction for the property listed in Part I: **(1)** For this tax year ▶ _____.
(2) For any prior tax years ▶ _____.

c Name and address of each organization to which any such contribution was made in a prior year (complete only if different from the donee organization above):

Name of charitable organization (donee)

Address (number, street, and room or suite no.)

City or town, state, and ZIP code

d For tangible property, enter the place where the property is located or kept ▶ _____

e Name of any person, other than the donee organization, having actual possession of the property ▶ _____

3 If conditions were attached to any contribution listed in Part I, answer questions a – c and attach the required statement (see instructions).

		Yes	No
a	Is there a restriction, either temporary or permanent, on the donee's right to use or dispose of the donated property?		
b	Did you give to anyone (other than the donee organization or another organization participating with the donee organization in cooperative fundraising) the right to the income from the donated property or to the possession of the property, including the right to vote donated securities, to acquire the property by purchase or otherwise, or to designate the person having such income, possession, or right to acquire?		
c	Is there a restriction limiting the donated property for a particular use?		

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For Example 10

Form 8283 (Rev. 10-98) Page 2

Name(s) shown on your income tax return: **Sam and Amy Moore** | Identifying number: **333-22-7777**

Section B—Appraisal Summary—List in this section only items (or groups of similar items) for which you claimed a deduction of more than $5,000 per item or group. **Exception.** Report contributions of certain publicly traded securities only in Section A.

If you donated art, you may have to attach the complete appraisal. See the **Note** in Part I below.

Part I Information on Donated Property—To be completed by the taxpayer and/or appraiser.

4 Check type of property:

- ☐ Art* (contribution of $20,000 or more)
- ☐ Art* (contribution of less than $20,000)
- ☐ Real Estate
- ☐ Coin Collections
- ☐ Gems/Jewelry
- ☐ Books
- ☐ Stamp Collections
- ☑ Other

*Art includes paintings, sculptures, watercolors, prints, drawings, ceramics, antique furniture, decorative arts, textiles, carpets, silver, rare manuscripts, historical memorabilia, and other similar objects.

Note: *If your total art contribution deduction was $20,000 or more, you must attach a complete copy of the signed appraisal. See instructions.*

5	(a) Description of donated property (if you need more space, attach a separate statement)	(b) If tangible property was donated, give a brief summary of the overall physical condition at the time of the gift	(c) Appraised fair market value
A	**Baseball Card Collection**	**Excellent**	**6,000**
B			
C			
D			

	(d) Date acquired by donor (mo., yr.)	(e) How acquired by donor	(f) Donor's cost or adjusted basis	(g) For bargain sales, enter amount received	See instructions: (h) Amount claimed as a deduction	See instructions: (i) Average trading price of securities
A	**Various**	**Purchase**	**350**			
B						
C						
D						

Part II Taxpayer (Donor) Statement—List each item included in Part I above that the appraisal identifies as having a value of $500 or less. See instructions.

I declare that the following item(s) included in Part I above has to the best of my knowledge and belief an appraised value of not more than $500 (per item). Enter identifying letter from Part I and describe the specific item. See instructions. ▶ _____

Signature of taxpayer (donor) ▶ Date ▶

Part III Declaration of Appraiser

I declare that I am not the donor, the donee, a party to the transaction in which the donor acquired the property, employed by, or related to any of the foregoing persons, or married to any person who is related to any of the foregoing persons. And, if regularly used by the donor, donee, or party to the transaction, I performed the majority of my appraisals during my tax year for other persons.

Also, I declare that I hold myself out to the public as an appraiser or perform appraisals on a regular basis; and that because of my qualifications as described in the appraisal, I am qualified to make appraisals of the type of property being valued. I certify that the appraisal fees were not based on a percentage of the appraised property value. Furthermore, I understand that a false or fraudulent overstatement of the property value as described in the qualified appraisal or this appraisal summary may subject me to the penalty under section 6701(a) (aiding and abetting the understatement of tax liability). I affirm that I have not been barred from presenting evidence or testimony by the Director of Practice.

Sign Here Signature ▶ Title ▶ Date of appraisal ▶

Business address (including room or suite no.): **125 E. Main** | Identifying number: **337894561**

City or town, state, and ZIP code: **Somewhere, IL 11112**

Part IV Donee Acknowledgment—To be completed by the charitable organization.

This charitable organization acknowledges that it is a qualified organization under section 170(c) and that it received the donated property as described in Section B, Part I, above on ▶ **8/17/01** (Date)

Furthermore, this organization affirms that in the event it sells, exchanges, or otherwise disposes of the property described in Section B, Part I (or any portion thereof) within 2 years after the date of receipt, it will file **Form 8282,** Donee Information Return, with the IRS and give the donor a copy of that form. This acknowledgment does not represent agreement with the claimed fair market value.

Does the organization intend to use the property for an unrelated use? . . . . . ▶ ☐ Yes ☐ No

Name of charitable organization (donee)	Employer identification number
General Hospital	**11-1234567**
Address (number, street, and room or suite no.)	City or town, state, and ZIP code
567 State St.	**Anytown, IL 11111**
Authorized signature	Title / Date

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MISCELLANEOUS ITEMIZED DEDUCTIONS

LEGAL FEES

Married taxpayers are allowed to deduct legal fees incurred to the extent that they produce taxable income. Therefore, legal fees incurred to obtain Social Security benefits are deductible if the Social Security benefits are included in taxable income. The fees are deducted as an itemized deduction subject to the 2% limitation.

> **Example 11.** Sam and Amy have had difficulty in obtaining Social Security Disability Benefits for Amy. They hired an attorney who specializes in this area. Mr. Black, their attorney, charged them $750 to help them obtain the benefits they requested. Sam and Amy are entitled to deduct their legal fees as a miscellaneous itemized deduction (subject to the 2% floor). Also, they need to be aware that if Amy collects workers' compensation benefits for her disability, it will affect the Social Security Disability benefits she will collect. For example, if she collects $2000 in worker's compensation, her $6000 of Social Security Benefits will be reduced by that amount. However, she will take the full $6000 of benefits in account in determining the amount of Social Security benefits received for that year.

CLAIM OF RIGHT

If a taxpayer must repay an amount that they included in income in a prior year, they may be able to deduct the payment from their income in the year it was originally paid. If the amount repaid is greater than $3,000, they may be able to take a credit against their tax for the year in which they paid the tax.

The type of deduction taken is determined by the type of income reported in the earlier year. The amount repaid is typically deducted on the same form where the income was reported. If it was reported as non-business income it is deducted on Schedule A as a miscellaneous itemized deduction, not subject to the 2% limitation.

If the repayment is $3,000 or less, it is deducted from income in the year paid. If it must be deducted as a miscellaneous itemized deduction, it is deducted on line 22 of Schedule A.

If the deduction is more than $3,000, it can either be deducted as mentioned previously, or a tax credit can be claimed for the additional taxes paid in the years being refunded. If a taxpayer qualifies for this method, he/she calculates the current year's taxes both ways. Either the deduction or the credit that results in the least amount of tax can be used.

Method One. The tax is calculated claiming a deduction for the repaid amount. If it must be treated as a miscellaneous itemized deduction, deduct it on line 27.

Method Two. Calculate the tax claiming a credit for the repaid amount. The procedure is as follows:

1. Calculate the current year's tax without the repaid amount.
2. Recalculate the tax from the earlier year without including in income the amount repaid in the current year.
3. Subtract the tax in Step 2 from the tax shown on the return for the earlier year. This is the credit.
4. Subtract the answer in Step 3 from the current year tax calculated without the deduction (Step 1).

If Method One results in less tax, deduct the amount repaid. If Method Two results in less tax, claim a credit for the amount repaid on line 65 of Form 1040, and write "**I.R.C. §1341**" next to line 68.

If the repayment is for Social Security benefits, and the repayment results in a negative amount, the taxpayer can take an itemized deduction for the part of the negative amount that represents benefits received in a prior year that were included in gross income.

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If this deduction is $3,000 or less, it is subject to the 2% AGI limit that applies to certain miscellaneous itemized deductions.

If the amount is over $3,000, the tax is calculated in two ways:

A. Calculate the current year tax with the itemized deduction included on line 27 of Schedule A.

B. Calculate the current year tax in the following steps:

1. Calculate the tax without the itemized deduction included on line 27 of Schedule A.
2. For each year after 1983 for which part of the negative amount represents a repayment of benefits, recalculate the taxable benefits as if the total benefits for the year were reduced by that part of the negative figure. Then refigure the tax for that year.
3. Subtract the total of the recalculated tax amounts in (b) from the total of the actual tax amounts.
4. Subtract the result in (c) from the result in (a).

After comparing the two methods, choose the one creating the least amount of tax and follow the same procedure as discussed above.

Example 12. Amy normally receives $6,000 per year of Social Security benefits. Since she received $8,000 in back workers' compensation benefits, she was required to repay this amount to Social Security. Therefore her 2002 form from SSA shows ($2,000). She will claim this as a miscellaneous itemized deduction on line 22 of Schedule A.

UNIFORMS AND WORK CLOTHES

Uniforms

The cost of clothing is generally a nondeductible personal expense. However, the IRS allows an employee to deduct uniforms — as a miscellaneous itemized deduction subject to the 2% limitation — if the clothing is both:

- required by the employer specifically as a condition of employment, and
- is not suitable to wear as normal clothing.

For the cost of the clothing to be deductible, both of the above conditions must be met. The employer's requiring of the employee to wear specific clothing does not necessarily make the clothing deductible. For example, military clothing is required, but it can be a substitute for regular clothing. The deduction is not allowed if the uniform is suitable for ordinary wear.

Example 13. Amy's job as a visiting nurse required her to wear a white uniform and white shoes while on duty. She is able to deduct the cost of the shoes and uniforms and the cost of dry cleaning the uniforms.

Work Clothing

Work clothing is distinguished between clothing that protects the worker and clothing that just protects the worker's normal apparel. Deductible clothing must protect the worker. No deduction is allowed because a worker's clothing wears out faster than normal because of their occupation. An example of work clothing that is deductible is clothing worn by a chemical employee to protect them from chemical splashes, and another example is the steel-toed work shoes worn by construction workers.

INVESTMENT MANAGEMENT FEES

An individual investor's expenses incurred for the production of income, such as investment fees, are deductible as itemized deductions, subject to the 2% AGI limit.

Example 14. Amy and Sam pay their investment advisor 1% of the value of their brokerage account each year. In 2002 this amounted to $3,018.

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UNRECOVERED ANNUITY BASIS

The basis in most retirement plans is recovered over the period of time the taxpayer is receiving payments from the plan. However, if the taxpayer dies prior to recovering all of the basis, they are entitled to deduct the remaining basis on their final income tax return. The basis is claimed as a miscellaneous itemized deduction and is not subject to the 2% of AGI limitation.

If a taxpayer began receiving retirement benefits from his annuity, under a joint and survivor annuity to be paid for the joint lives of the taxpayer and his spouse, and if both the taxpayer and spouse die before the contributed amount had been recovered, the remaining unrecovered cost would be a miscellaneous itemized deduction on the last to die's final income tax return. This deduction is not subject to the 2% AGI limit.

COMPLETED SCHEDULE A

Example 15. Assume Sam and Amy's 2002 AGI is $83,862. The real estate tax on their principal residence is $3,850 and the mortgage interest is $6,786. Sam and Amy have other medical expenses of $3,899 that were not reimbursed by insurance. Their deductible state and local taxes are $2,514 and their cash charitable contributions total $2,287.

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Using the information on the previous page and information provided from other examples throughout this chapter, a completed 2002 Schedule A follows:

SCHEDULES A&B (Form 1040)
Department of the Treasury Internal Revenue Service (99)

Schedule A—Itemized Deductions

(Schedule B is on back)

► Attach to Form 1040. ► See Instructions for Schedules A and B (Form 1040).

OMB No. 1545-0074

2002

Attachment Sequence No. 07

Name(s) shown on Form 1040: **Sam and Amy Moore**

Your social security number: **333 22 7777**

Draft as of 5/06/2002

Medical and Dental Expenses	1	**Caution.** Do not include expenses reimbursed or paid by others. Medical and dental expenses (see page A-2)	1	6,322		
	2	Enter amount from Form 1040, line 36	2	83,862		
	3	Multiply line 2 above by 7.5% (.075)	3	6,290		
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-			4	32
Taxes You Paid (See page A-2.)	5	State and local income taxes	5	2,514		
	6	Real estate taxes (see page A-2)	6	6,333		
	7	Personal property taxes	7			
	8	Other taxes. List type and amount ►	8			
	9	Add lines 5 through 8			9	8,847
Interest You Paid (See page A-3.)	10	Home mortgage interest and points reported to you on Form 1098	10	17,815		
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ►	11			
Note. Personal interest is not deductible.	12	Points not reported to you on Form 1098. See page A-3 for special rules	12			
	13	Investment interest. Attach Form 4952 if required. (See page A-3.)	13	567		
	14	Add lines 10 through 13			14	18,382
Gifts to Charity If you made a gift and got a benefit for it, see page A-4.	15	Gifts by cash or check. If you made any gift of $250 or more, see page A-4	15	2,287		
	16	Other than by cash or check. If any gift of $250 or more, see page A-4. You **must** attach Form 8283 if over $500	16	9,350		
	17	Carryover from prior year	17			
	18	Add lines 15 through 17			18	11,637
Casualty and Theft Losses	19	Casualty or theft loss(es). Attach Form 4684. (See page A-5.)			19	0
Job Expenses and Most Other Miscellaneous Deductions (See page A-5 for expenses to deduct here.)	20	Unreimbursed employee expenses—job travel, union dues, job education, etc. You **must** attach Form 2106 or 2106-EZ if required. (See page A-5.) ►	20			
	21	Tax preparation fees	21	250		
	22	Other expenses—investment, safe deposit box, etc. List type and amount ►	22	5,768		
	23	Add lines 20 through 22	23	6,018		
	24	Enter amount from Form 1040, line 36	24	83,862		
	25	Multiply line 24 above by 2% (.02)	25	1,677		
	26	Subtract line 25 from line 23. If line 25 is more than line 23, enter -0-			26	4,341
Other Miscellaneous Deductions	27	Other—from list on page A-6. List type and amount ►			27	0
Total Itemized Deductions	28	Is Form 1040, line 36, over $137,300 (over $68,650 if married filing separately)? ☐ **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 27. Also, enter this amount on Form 1040, line 38. ☐ **Yes.** Your deduction may be limited. See page A-6 for the amount to enter.			28	43,239

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11330X **Schedule A (Form 1040) 2002**

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2002	Federal Statements	Page 1
Client Sam	Sam and Amy Moore	333-22-7777

8/12/02 12:55 p.m

Investment fees	$	3,018.
Legal fees Re: SS Benefits		750.
SS Claim of Right		2,000.
	Total $	5,768.

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