

# State/Local Income Tax Refunds

Form 1040 Line 10

Pub 4491 Page 69

# The Interview



- **Point of awareness**

Yes	No	Unsure	Check appropriate box for each question in each section
<b>Part III – Income – Last Year, Did You (or Your Spouse) Receive</b>			
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	5. (B) Refund of state/local income taxes? (Form 1099-G)

- **2012 returns**

# State/Local Income Tax Refunds

- Form 1099-G – State or local income tax refund

2012 only

2 State or local income tax refunds, credits, or offsets
\$
3 Box 2 amount is for tax year

# State/Local Income Tax Refunds Interview

## Limitation on Scope

- Box 3 must be “2012” (not older years)\*
- Must have prior year return if not all taxable

### \*Exceptions:

- If taxpayer agrees 100% taxable
- If taxpayer claimed standard deduction for all years (0% taxable)
- If taxpayer claimed sales tax deduction for all years (0% taxable)

# State/Local Income Tax Refunds



- **Tax benefit rule:**
  - Taxable when refund received if it gave tax benefit in year deducted
  - Taxable amount is limited to amount that gave tax benefit

# State/Local Income Tax Refunds

## Tax benefit rule:

- **No benefit if standard deduction was used in 2012**
- **No benefit if Sales Tax was deducted in 2012**
- **No benefit if negative taxable income (Line 41 minus line 42) when stated as a positive number is more than the income tax deduction on 2012 Sch A**

# Any Tax Benefit?

Look at 2012 Form 1040 Page 2 Line 40

- Standard deduction or itemized?

<input type="checkbox"/> If your spouse itemizes on a separate return or you were a dual-status alien, check here		<input type="checkbox"/>	
<b>40</b>	<b>Itemized deductions (from Schedule A) or your standard deduction (see left margin) . . . . .</b>	<b>40</b>	<b>6,293.</b>
<b>44</b>	<b>Subtract line 40 from line 39</b>	<b>44</b>	<b>14,207.</b>

# Any Tax Benefit?

Can't remember last year's standard deduction amounts?

➤ Compare Line 40 to Sch A Line 29 total

<b>Total</b>	<b>29</b>	Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40 .....	<b>29</b>	6,298.
<b>Itemized Deductions</b>	<b>30</b>	If you elect to itemize deductions even though they are less than your standard .....		



# Any Tax Benefit?

**Negative taxable income on Page 2 of 2012 Form 1040:**

<b>Line 41</b>	<b>(5,795)</b>
<b>Less line 42</b>	<b><u>-7,600</u></b>
<b>Total negative taxable income</b>	<b>(13,395)</b>

- **Is refund less than \$13,395?**

41	Subtract line 40 from line 38	41	(5,795.)
42	Exemptions. Multiply \$3,800 by the number on line 6d	42	7,600.
43	Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-	43	0

# State/Local Income Tax Refunds



- **Not taxable?**

(sales tax or standard deduction or negative taxable income)

**Click “no” on 1040 Pg 1 – You’re done!**

Did you itemize deductions last year and receive state or local tax refunds, credits, or offsets? Answer "No" if you deducted state sales tax instead of state income tax

Yes  No

**10** Taxable refunds, credits, or offsets of state and local income taxes.  
F9 for worksheet

# State/Local Income Tax Refunds

## Possibly taxable?

- TaxWise has worksheet to calculate tax benefit
- If both state and local income tax refunds, put both on same worksheet
- If two state income tax refunds, put both on same worksheet

# State/Local Income Tax Refunds

Form 1040 – answer question above Line 10

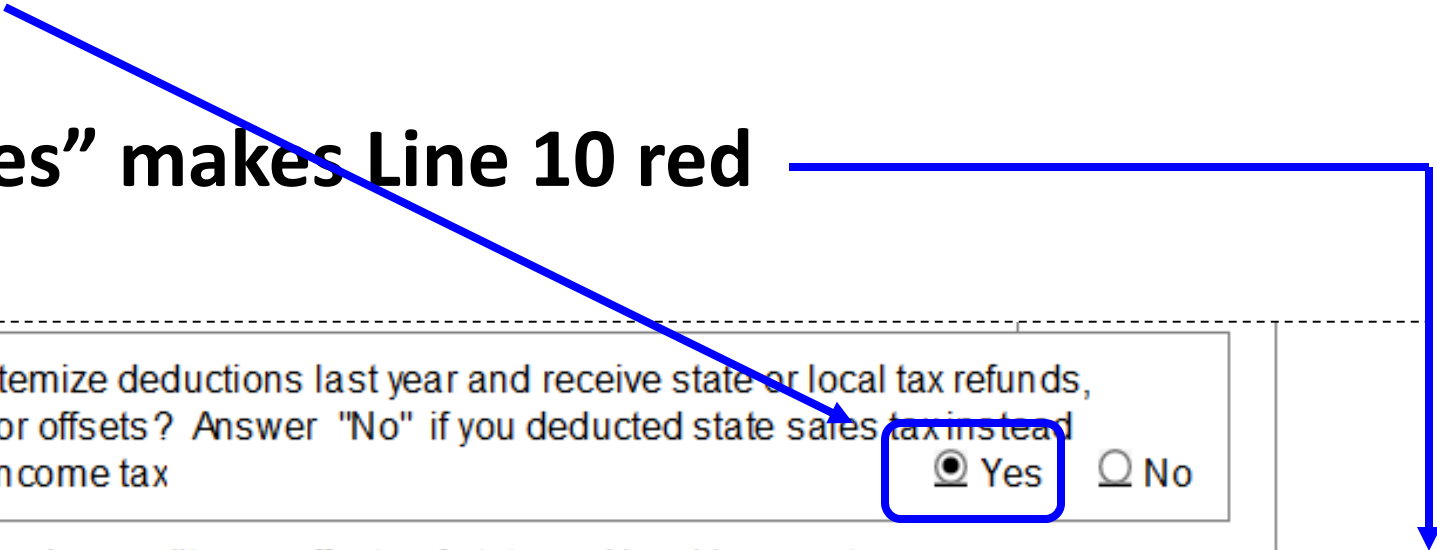
- “Yes” makes Line 10 red

Did you itemize deductions last year and receive state or local tax refunds, credits, or offsets? Answer "No" if you deducted state sales tax instead of state income tax

Yes  No

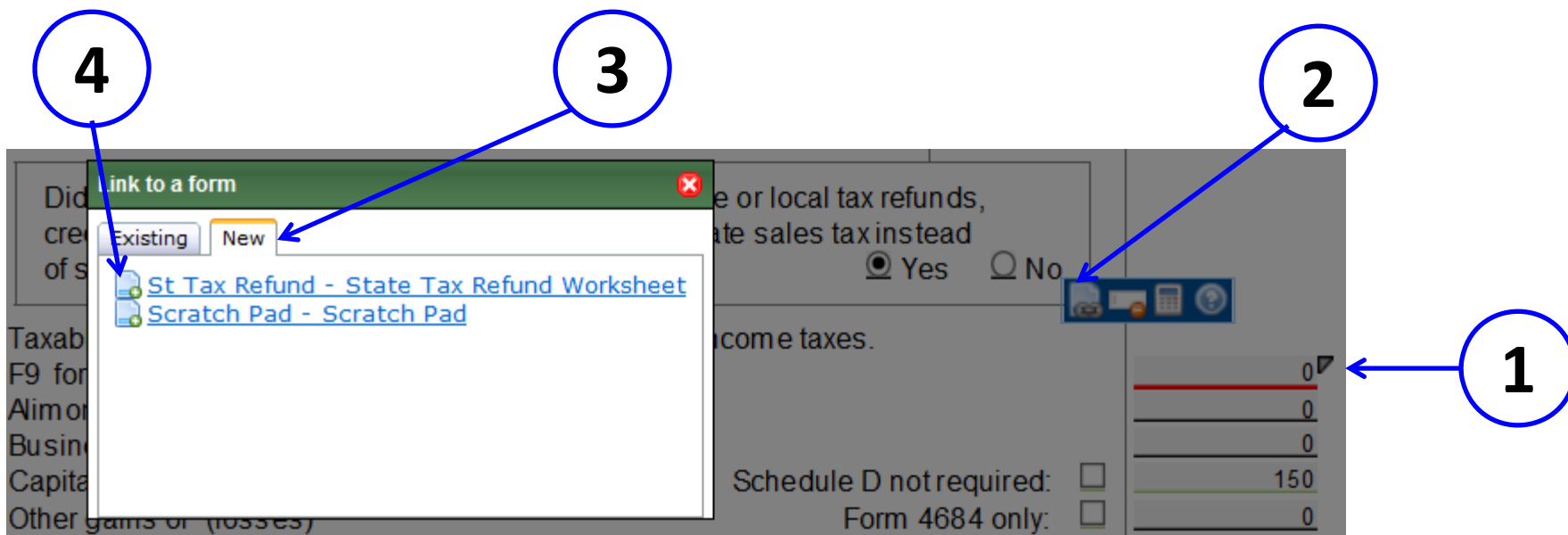
**10** Taxable refunds, credits, or offsets of state and local income taxes.  
F9 for worksheet

0



# State Tax Refund Worksheet

1. Link from Line 10 – arrow head on right
2. Click Link to another form icon
3. New tab
4. St Tax Refund – State Tax Refund Worksheet



# State Tax Refund Worksheet

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- **Must have 2012 federal return!**
- **TaxWise fills in much of what you need – confirm it is correct**
- **Complete worksheet**

# State Tax Refund Worksheet

**Refund to test**

Use the spouse column if this is a married joint return for this year and the spouse filed separately last year.		Joint or Taxpayer	Spouse
<b>1</b>	<input type="text"/> 2012 state / local income tax refund	500	0
	<input type="text"/> 2012 state / local income tax refund	0	0
	Total state / local income tax refund for 2012	500	0
<b>2</b>	<b>Enter amounts from the 2012 tax return</b>		
	Schedule A, line 5a, income taxes	0	
	Schedule A, line 5b, general sales tax	0	
	Difference - the state tax refund is only taxable to the extent the state tax deduction exceeds the sales tax deduction	0	0
<b>3</b>	Net state / local income tax refund	0	0
<b>4</b>	Enter the total of all other Schedule A refunds or reimbursements	0	
<b>5</b>	Add lines 3 and 4	0	0

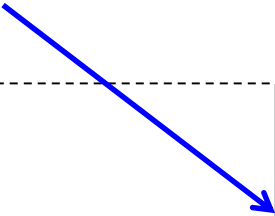
**Need both**

**If any**

# State Tax Refund Worksheet

- Most common error: forget to input sales tax that could have been deducted
- If TaxWise doesn't fill, need to calculate and input (unless no sales tax in your state)

<b>2 Enter amounts from the 2012 tax return</b>		
Schedule A, line 5a, income taxes	0	0
Schedule A, line 5b, general sales tax	0	0
Difference - the state tax refund is only taxable to the extent the state tax deduction exceeds the sales tax deduction		
	0	0





# Calculate Sales Tax

- Take total income from 2012 F1040 Line 22
- Add income not taxed (interest, soc. sec.)
- Go to Sch A instructions, look up your state in sales tax tables for number of exemptions on 2012 return
- Input in wksht

Income		Exemptions					
At least	But less than	1	2	3	4	5	Over 5
		<b>Alabama</b>					<b>4.0000%</b>
\$0	\$20,000	235	274	300	320	337	360
20,000	30,000	346	401	438	467	491	524
30,000	40,000	399	463	505	538	565	603
40,000	50,000	444	514	561	597	628	668

# State Tax Refund Worksheet

- Complete worksheet using 2012 tax return information
- Line 8 often missed

<p><b>7</b> Filing status for 2012. Enter 1, 2, 3, 4, or 5. 1 = Single                                      4 = Head of household 2 = Married filing jointly                      5 = Qualifying widow(er) 3 = Married filing separately If the 2012 filing status was married filing separately, and itemized deductions were required to be used because the spouse itemized, check here</p>	<input type="text" value="0"/>	<input type="text" value="0"/>
<p><b>8</b> Age 65 or blind, enter amount from the 2012 Form 1040, page 2, line 39a</p>	<input type="checkbox"/>	<input type="checkbox"/>
	<input type="text" value="0"/>	<input type="text" value="0"/>

# State Tax Refund Worksheet

- Enter 2012 taxable income on Line 12 of worksheet
  - Form 1040 Line 43
  - If Line 43 is -0-, subtract line 42 from Line 41 and enter as a negative number on line 12 of worksheet

<b>12</b>	Enter the taxable income for 2012 , adjusted for any NOL carryover. If less than -0-, show the amount as a negative number	0	0
<b>13</b>	Amount to include in income for 2013 :	0	0
<b>14</b>	<b>Taxable state / local income tax refund</b>	0	0
<b>15</b>	<b>Taxable amount of other income</b>	0	0

# State Tax Refund Worksheet

- Almost done...
- Is part or all of refund taxable?

13 Amount to include in income for 2013!

14 Taxable state / local income tax refund

1000
1000

- Need to double check tax credits

# Unused Tax Credits in 2012?

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- **If there were unused tax credits in 2012, part or all of state income tax refund may have produced no benefit**
- **TaxWise worksheet doesn't handle this**
- **Must manually test**

# Unused Tax Credits in 2012?

- **Confirm that there were unused tax credits – look at 2012 tax return**
  - **Child tax credit line 48 plus line 65**
    - ✱ **Was it less than \$1,000 per child?**
  - **Foreign tax credit line 47 was greater than tax shown on line 46?**
  - **Was education credit line 49 greater than line 46 reduced by line 47?**
  - **Other nonrefundable credits?**

# Unused Tax Credits – Manual Test

- **Open prior year's return in TaxWise\***
  - **Note net tax overpaid or amount owed (1040 P2 line 73 or 76)**
  - **Note amount of income tax deducted on Sch A**
  - **Reduce income tax deducted on Sch A by amount of refund**

# Unused Tax Credits – Manual Test

**Did tax overpayment or amount owed change? If not – no benefit**

- **Restore amount of deduction on Sch A and close 2012 return**
- **Return to 2013 return, check box above line 6 on State Tax Refund wkst and you're done!**

tax refund may be tax-free. Check here if the ENTIRE state tax refund is nontaxable. Stop here  
6 2011 itemized deductions





# Unused Tax Credits – Manual Test

**Did tax overpayment or amount owed change? Yes – some benefit!**

- **Note amount of change**
- **Look at summary sheet in form tree line 33 marginal rate**
- **Divide change amount by tax rate**
- **Result is part of refund that gave tax benefit**

# Unused Tax Credits – Manual Test

- **Example of tax benefit received:**
  - **Amount owed with tax deduction** **475**
  - **Amount owed without tax deduction** **500**
  - **Equals net change of** **25**
  - **Divide by tax rate 10% =** **250**
- **\$250 of tax refund is taxable in 2013**

# Unused Tax Credits –Manual Test

- Need to override Line 14 of State Tax Refund worksheet
- Make a note for reviewer

a negative number	25000
13 Amount to include in income for 2013	1000
14 Taxable state / local income tax refund	250
15 Taxable amount of other income	0

# State and Local Income Tax Refunds

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- **TaxWise carries taxable portion of state and/or local income tax refund to 1040 Pg 1 Line 10**



# Quality Review – State/Local Income Tax Refunds



- **Confirm tax refund was only for 2012**
- **Review prior year's return**
  - **Itemized? Income tax deducted?**
  - **Negative taxable income?**
  - **Any unused credits?**
- **Review entries in state tax refund worksheet**

# Client Summary – State/Local Income Tax Refunds



- **Show taxpayer portion of refund that is taxable, if any**

# State And Local Income Tax Refunds

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Questions?



Comments?

# Let's Practice In TaxWise



- Under direction of the instructor:
  - Open the return for Kent/Bryant in TaxWise
  - From **Pub 4491W**, enter state tax refund
  - Verify tax liability