

State/Local Income Tax Refunds

Form 1040 Line 10

Pub 4491 Part 3



The Interview



- Point of awareness

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

- 2013 returns

State/Local Income Tax Refunds

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

2013 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 “2013” (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 2013**
 - **No benefit if Sales Tax was deducted in 2013**
 - **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 2013 Sch A**

Any Tax Benefit?

Look at 2013 Form 1040 Page 2 Line 40

- Standard deduction or itemized?

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

Any Tax Benefit?

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

- Compare Line 40 to Sch A Line 29 total

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

Any Tax Benefit?

Negative taxable income on Page 2 of 2013 Form 1040:

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

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

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

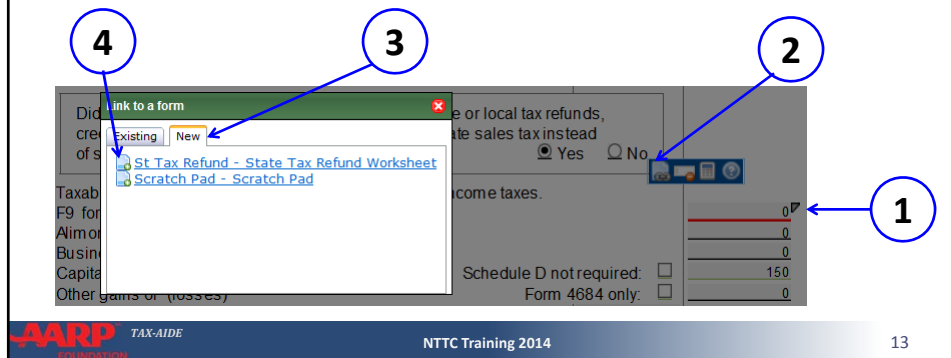
Yes No

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

- **Must have 2013 federal return!**
- **TaxWise fills in much of what you need – confirm it is correct**
- **Complete worksheet**

State Tax Refund Worksheet

Identify State

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
1 2013 state / local income tax refund	500	0
2013 state / local income tax refund	0	0
Total state / local income tax refund for 2013	500	0
2 Enter amounts from the 2013 tax return		
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
3 Net state / local income tax refund	0	0
4 Enter the total of all other Schedule A refunds or reimbursements	0	
5 Add lines 3 and 4	0	0

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15

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)**

2 Enter amounts from the 2013 tax return

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

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16

Calculate Sales Tax

- Take total income from 2013 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 2013 return
- Input in wksht

Income		Exemptions					
At least	But less than	1	2	3	4	5	Over 5
		Alabama					4.0000%
\$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	626	668

State Tax Refund Worksheet

- Complete worksheet using 2013 tax return information
 - Some Data will Carryforward
- Line 8 often missed

7 Filing status for 2013 . 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 2013 filing status was married filing separately, and itemized deductions were required to be used because the spouse itemized, check here

<input type="text" value="0"/>	<input type="text" value="0"/>
<input type="checkbox"/>	<input type="checkbox"/>

8 Age 65 or blind, enter amount from the 2013 Form 1040, page 2, line 39a

<input type="text" value="0"/>	<input type="text" value="0"/>
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State Tax Refund Worksheet

- Enter 2013 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

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

State Tax Refund Worksheet

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

13	Amount to include in income for 2013	1000
14	Taxable state / local income tax refund	1000

- Need to double check tax credits



Unused Tax Credits in 2013?



- If there were unused tax credits in 2013, 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 2013?



- Confirm that there were unused tax credits – look at 2013 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 2013 return**
- **Return to 2014 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 2012 itemized deductions

13716

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 2014

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

- 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 2013**
- **Review prior year's return**
 - **Itemized? Income tax deducted?**
 - **Negative taxable income?**
 - **Any unused credits?**
- **Review entries in state tax refund worksheet**



Taxpayer Summary – State/Local Income Tax Refunds



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

State And Local Income Tax Refunds

Questions?



Comments?