CHAPTER 2 – SOLUTIONS

END OF CHAPTER MATERIAL

Discussion Questions

1. What is a *for* AGI deduction? Give three examples.

**Answer:**

**A deduction for AGI is a deduction permitted under the IRC that is used to calculate AGI. It can also be thought of as a deduction from gross income to arrive at AGI. Examples include deductions for IRAs, Keoghs, or other self-employed qualified pension plans; student loan interest; one-half the self-employment tax; self-employed health insurance deduction; penalty on early withdrawal of savings.**

**Learning Objective: 02-01**

**Topic: The Income Tax Formula and Form 1040**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

2. What are the five types of filing status?

**Answer:**

**The five types of filing status are:**

**Single**

**Married filing a joint return**

**Married filing separate returns**

**Head of household**

**Qualifying widow(er) with dependent child**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

3. What qualifications are necessary to file as head of household?

**Answer:**

**To qualify as head of household, the taxpayer must be unmarried at the end of the tax year, be a U.S. citizen or resident throughout the year, not be a qualifying widow(er), and maintain a household that is the principal place of abode of a *qualifying person* for more than half the year or pay more than half the costs of maintaining a separate household for the taxpayer’s mother or father if the mother or father qualifies as a dependent of the taxpayer. Temporary absences, such as attending school do not disqualify the person under this section.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

4. George and Debbie were legally married on December 31, 2023. Can they file their 2023 income tax return using the status of married filing jointly? Why or why not? What other filing status choices do they have, if any?

**Answer:**

**Yes, George and Debbie can file using the filing status of married filing jointly. The requirement for this status is that the couple be legally married on the last day of the tax year. Alternatively, the couple could choose to use the married filing separate status.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

5. Why is it important to determine if the taxpayer has dependents to be claimed on the income tax return?

**Answer:**

**The existence and number of dependents affect the determination of total tax liability in areas such as child credits and filing status.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

6. What are the three general tests that a qualifying person must meet to be a dependent of the taxpayer?

**Answer:**

**To be a dependent of the taxpayer, a qualifying child and a qualifying relative must meet the three general tests: dependent taxpayer test, joint return test and citizen or resident test.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

7. What are the five specific tests necessary to be a qualifying child of the taxpayer?

**Answer:**

**A person is a qualifying child if he or she meets all five of the following tests: relationship test, age test, residency test, support test, and special test for qualifying child of more than one taxpayer.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

8. What age must a child be at the end of the year to meet the age test under the qualifying child rules?

**Answer:**

**At the end of the year, the child must be one of the following: under the age of 19; under the age of 24 and a full-time student; or totally and permanently disabled regardless of age. In addition, the child must be younger than the person claiming the dependency.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

9. What are the four specific tests necessary to be a qualifying relative of the taxpayer?

**Answer:**

**A person qualifies as a qualifying relative if he or she meets all four of the following tests: not a qualifying child test, relationship or member of household test, gross income test, and support test.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

10. What is a multiple support agreement, and what is its purpose?

**Answer:**

**Normally, in order to claim someone as a dependent a taxpayer must provide more than half the support of the person. At times, an individual may receive support from multiple persons, but no one person has provided more than 50% of the support. In such a case, a multiple support agreement can be signed. If every one of the persons providing support could claim the individual as a dependent (absent the support test) then one person who provided more than 10% of the support can receive the nonrefundable family credit if all persons sign a written multiple support agreement.**

**The purpose of the agreement is so someone can claim the dependent rather than no one. Further, the agreement provides a mechanism such that all parties can agree on who that person should be.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

11. Mimi is 22 years old and is a full-time student at Ocean County Community College. She lives with her parents, who provide all of her support. During the summer, she put her Web design skills to work and earned $5,180. Can Mimi’s parents claim her as a dependent on their joint tax return? Why or why not? Assume that all five tests under qualifying child are met.

**Answer:**

**All of the dependency tests are met by Mimi’s parents, so they can claim her as a dependent. The fact that Mimi earned $5,180 does not matter since Mimi is under age 24 and she is a full-time student at a qualifying educational institution. Thus, the gross income test is not necessary for a qualifying child as long as Mimi does not provide more than half of her own support.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

12. What is the standard deduction for each filing status?

**Answer:**

**The standard deduction for each filing status for 2023 is:**

**Single $ 13,850**

**Married filing jointly 27,700**

**Married filing separately 13,850**

**Head of household 20,800**

**Qualifying widow(er) 27,700**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

13. Under what circumstances must a taxpayer use a tax rate schedule rather than using a tax table?

**Answer:**

**If the taxable income of a taxpayer is $100,000 or more, a tax rate schedule must be used. Taxable income of less than $100,000 requires the use of the tax table.**

**Learning Objective: 02-05**

**Topic: Tax Due to IRS**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

14. When and at what rate is interest calculated on amounts owed to the IRS?

**Answer:**

**If the taxpayer still owes tax after April 15th, the rate charged is the federal short-term rate plus 3 percentage points.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

15. Prepare a table of the possible IRS penalties listed in the text and give a brief summary of the purpose of each penalty.

**Answer:**

|  |  |
| --- | --- |
| **Penalty** | **Reason for Penalty** |
| **Interest charged on assessments** | **To encourage taxpayers to pay assessments in a timely manner and to compensate the government for the time-value of late payments** |
| **Failure to file a tax return** | **To reprimand taxpayers for failing to file a tax return** |
| **Failure to pay tax** | **To seek retribution from taxpayers who fail to pay tax** |
| **Failure to pay estimated taxes** | **To penalize taxpayers for failing to pay estimated taxes throughout the year** |
| **Accuracy-related penalties** | **To seek retribution from taxpayers for underpayments or submitting tax returns with errors** |
| **Fraud penalties** | **To penalize taxpayers for providing fraudulent information** |
| **Erroneous claim for refund or credit penalty** | **To penalize taxpayers for filing an excessive claim for refund or credit of income tax** |

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 2 Medium**

**Feedback: EA: Yes**

Multiple Choice

16. A single taxpayer is 26 years old and has wages of $18,570 and interest income of $435. Which Form 1040 Schedule must the taxpayer use?

a. Schedule 1.

b. Schedule 2.

c. Schedule 3.

d. The taxpayer does not need to use a Schedule.

**Answer: d.**

**Learning Objective: 02-01**

**Topic: The Income Tax Formula and Form 1040**

**Difficulty: 1 Easy**

**Feedback: Wages and interest are reported on the basic Form 1040. A schedule is not required.**

**EA: Yes**

17. Which Schedule must the taxpayer use to claim a payment made for alimony if the taxpayer was divorced in 2023?

a. Schedule 1.

b. Schedule 2.

c. Schedule 3.

d. The taxpayer does not need to use a Schedule.

**Answer: d.**

**Learning Objective: 02-01**

**Topic: The Income Tax Formula and Form 1040**

**Difficulty: 1 Easy**

**Feedback: Alimony payments are not deductible in 2023.**

**EA: Yes**

18. A taxpayer is married with a qualifying child (dependent), but she has been living separately from her spouse for the last eight months of the year. However, she paid for more than half of the cost of keeping up the household. Her spouse does not want to file jointly. What filing status must she use when filing her tax return? She wants to obtain the maximum legal benefit.

a. Married filing separately.

b. Head of household.

c. Qualifying widow(er).

d. Single.

**Answer: b.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback: A taxpayer is considered unmarried for purposes of this section if the spouse was living apart during the last six months of the tax year.**

**EA: Yes**

19. A taxpayer’s spouse died on December 31, 2022. He has no qualifying child. Which status should the taxpayer select when filing his 2023 tax return?

a. Qualifying widow(er).

b. Married filing jointly.

c. Single.

d. Married filing separately.

**Answer: c.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback: The surviving spouse may be eligible to file as a qualifying widow(er) only if certain conditions are met, which include keeping a household as the principal place of abode for the entire year of both the surviving spouse and a child, stepchild, or adopted child who can be claimed as a dependent by the surviving spouse.**

**EA: Yes**

20. Esmeralda is 20 years of age and a full-time student living with her parents. She had wages of $545 ($50 of income tax withholding) for 2023. Can Esmeralda file a tax return to claim her $50 of income tax withholding even though she is a dependent of her parents?

a. Yes, Esmeralda can file a tax return.

b. No, Esmeralda cannot file a tax return.

c. Esmeralda’s parents can report her wages on their tax return.

d. No, Esmeralda is a dependent of her parents.

**Answer: a.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback: Esmeralda qualifies as a dependent of her parents; however, she can file her own tax return to claim the $50 withheld from her pay.**

**EA: Yes**

21. A taxpayer can claim a dependent if the person is a qualifying child or a qualifying relative and the person meets all of the following tests.

a. Citizen or resident, dependent taxpayer, and age tests.

b. Dependent taxpayer, joint return, and support tests.

c. Joint return, citizen or resident and support tests.

d. Dependent taxpayer, joint return, and citizen or resident tests.

**Answer: d.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback: A qualifying child or a qualifying relative can be claimed as a dependent if the person meets the dependent taxpayer, joint return, and citizen or resident tests.**

**EA: Yes**

22. To be a qualifying child, the taxpayer must meet three general tests and five specific tests. Which of the following is *not* part of the five specific tests?

a. Gross income test

b. Age test

c. Support test

d. Relationship test

**Answer: a.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback: The gross income test does not apply to a qualifying child; only to a qualifying relative.**

**EA: Yes**

23. To be a qualifying relative, who has to live in the home of the taxpayer for the entire year?

a. Child.

b. Cousin.

c. Stepchild.

d. Father.

**Answer: b.**

**Learning Objective: 02-03**

**Topic: Dependent**

**Difficulty: 2 Medium**

**Feedback: A cousin does not meet the relationship test under this area. He/she must live in the taxpayer’s household for the entire year.**

**EA: Yes**

24. Which amount represents the standard deduction for a taxpayer who is 44 years old and claiming head of household status?

a. $22,300.

b. $22,650.

c. $20,800.

d. $13,850.

**Answer: c.**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 1 Easy**

**Feedback: The standard deduction for a taxpayer under age 65 and claiming head of household status is $20,800.**

**EA: Yes**

25. A married couple, both of whom are under 65 years old, decided to file as married filing separately. One of the spouses is going to itemize deductions instead of taking the standard deduction. What is the standard deduction permitted to the other spouse when she files her tax return?

a. $13,850.

b. $15,350.

c. $20,800.

d. $0.

**Answer: d.**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 1 Easy**

**Feedback: When filing as married filing separately, if one of the spouses itemizes, then the other spouse must itemize or receive a standard deduction of zero.**

**EA: Yes**

26. Employers are required to withhold social security taxes from wages paid to employees. What is the amount of the social security wage limitation for 2023?

a. $142,800.

b. $160,200.

c. $137,700.

d. $147,000.

**Answer: b.**

**Learning Objective: 02-05**

**Topic: Tax Due to IRS**

**Difficulty: 1 Easy**

**Feedback: The amount of the social security wage limitation for 2023 is $160,200.**

**EA: Yes**

27. What is the amount of the tax liability for a married couple filing jointly with taxable income of $132,445?

a. $19,753.

b. $23,581.

c. $29,138.

d. $15,453.

**Answer: a.**

**Learning Objective: 02-05**

**Topic: Tax Computation**

**Difficulty: 2 Hard**

**Feedback: The amount is $19,753 computed as follows:**

**($132,445 – $89,450) .22 plus $10,294**

**EA: Yes**

28. What is the percentage of interest the IRS was charging on assessment (amount of unpaid tax liability) during March 2023? You might want to do this research by going to the IRS website (www.irs.gov).

a. 5%

b. 6%

c. 4%

d. 7%

**Answer: d.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 1 Easy**

**Feedback: The interest rate is 7% for underpayments occurring during March of 2023.**

**EA: Yes**

29. When there is negligence on a return, the IRS charges a penalty of \_\_\_\_\_\_\_\_ of the tax due.

a. 25%.

b. 20%.

c. 18%.

d. 10%.

**Answer: b.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 1 Easy**

**Feedback: The IRS can assess a penalty equal to 20% of the tax due when negligence has occurred.**

**EA: Yes**

30. When there is fraud on a return, the IRS charges a penalty of \_\_\_\_\_\_\_\_ on any portion of understatement of tax that is attributable to the fraud.

a. 20%.

b. 25%.

c. 75%.

d. 100%.

**Answer: c.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 1 Easy**

**Feedback: The IRS can impose a penalty of 75% on any portion of understatement of tax that is attributable to fraud.**

**EA: Yes**

Problems

31. The benefits of many deductions, credits, or other benefits are limited to taxpayers with Adjusted Gross Income below certain limits.

1. Explain how the limitation (phaseout) process works.
2. Give two examples of deductions, credits, or other benefits that are limited.
3. Why would Congress wish to limit the benefits of these items?

**Answer:**

1. **Taxpayers with AGI in excess of certain specified amounts are prohibited from utilizing the full amount of many deductions, credits, or other tax benefits. Many tax benefits are structured such that taxpayers with low AGI are not limited, taxpayers with high AGI receive no benefit, and taxpayers in the middle receive a reduced benefit as AGI increases. Sometimes a specified AGI amount represents the dividing line between receiving the full amount of a benefit or not receiving any benefit.**
2. **Examples of benefits which are subject to limitation include: earned income tax credit, child care credit, child tax credit, and deductibility of IRA contributions.**
3. **There may be a number of reasons why Congress might restrict benefits. First, reducing benefits results in higher taxable income and tax liability, thus increasing tax revenues. Second, taxpayers with higher AGI are often deemed to be able to financially afford fewer benefits and higher taxes since they have more money to start with. Third, and somewhat ironically, there are fewer high income voters compared to low- and moderate-income voters.**

**Learning Objective: 02-01**

**Topic: The Income Tax Formula and Form 1040**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

32. List the five types of filing status and briefly explain the requirements for the use of each one.

**Answer:**

**The five types of filing status and requirements are:**

***Single*. Taxpayer must be unmarried on the last day of the tax year and must not qualify as either head of household or qualifying widow(er).**

***Married filing a joint return*. Taxpayers must be legally married on the last day of the tax year. Taxpayers in the process of getting a divorce can file with this classification as long as the divorce is not final. Generally, neither taxpayer can be a nonresident alien at any time during the tax year.**

***Married filing separate returns*. Taxpayers must meet the requirements for married filing jointly and can then choose to file married filing separately.**

***Head of household*. In order to qualify as head of household, the taxpayer must be unmarried at the end of the tax year, be a U.S. citizen or resident throughout the year, not be a qualifying widow(er), and maintain a household that is the principal place of abode of a *qualifying person* for more than half the year. If the mother or father of the taxpayer qualifies as a dependent of the taxpayer, the taxpayer can be eligible for head of household status by paying more than half the costs of maintaining a separate household that is the principal place of abode for the mother or father.**

***Qualifying widow(er) with dependent child.* During the two years following the year of death of a spouse, a taxpayer can file as a qualifying widow(er) if the taxpayer did not remarry and if the taxpayer maintained a household which was the principal place of abode for the entire year of the taxpayer and a dependent child, stepchild, or adopted child. In addition, the taxpayer must have been eligible to file a joint return in the year the spouse died.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

33. In which of the following cases may the taxpayer claim head of household filing status?

1. The taxpayer is single and maintains a household that is the principal place of abode of her infant son.
2. The taxpayer is single, maintains a household for herself, and maintains a separate household that is the principal place of abode of her dependent widowed mother.
3. The taxpayer was married from January to October and lived with his spouse from January to May. From June 1 to December 31, the taxpayer maintained a household that was the principal place of abode of his married son and daughter-in-law, whom the taxpayer can claim as dependents.
4. Same as (c) except the taxpayer lived with his spouse until August and maintained the household from September 1 to the end of the year.

**Answer:**

1. **The taxpayer can claim head of household status.**
2. **The taxpayer can claim head of household status. It is not necessary that her mother live in the same household as the taxpayer.**
3. **The taxpayer can claim head of household status.**
4. **The taxpayer cannot claim head of household status. The son and daughter-in-law must live with the taxpayer for more than half the tax year. And the taxpayer cannot live with his or her spouse during the last 6 months of the year.**

**Learning Objective: 02-02**

**Topic: Filing Status**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

34. What are the three tests a qualifying child or qualifying relative must meet to be claimed as a dependent?

**Answer:**

**A qualifying child or qualifying relative must meet the dependent taxpayer, joint return, and citizen or resident tests.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 1 Easy**

**Feedback:**

**EA: Yes**

35. Roberta is widowed and lives in an apartment complex. She receives $8,000 of social security income that she uses to pay for rent and other household expenses. The remainder of her living expenses is paid by relatives and neighbors. The total amount of support paid by Roberta and the others totals $22,000. Amounts paid for support during the year are as follows:

Roberta $8,000

Ed (neighbor) 4,000

Bill (son) 5,000

Jose (neighbor) 2,000

Alicia (niece) 3,000

a. Which of these persons is entitled to claim Roberta as a dependent absent a multiple support agreement?

b. Under a multiple support agreement, which of these persons is entitled to claim Roberta as a dependent? Explain your answer.

c. If Roberta saved all of her social security income and the other persons paid for the shortfall in the same proportions as shown, which of these persons would be entitled to claim Roberta as a dependent under a multiple support agreement? Explain your answer.

**Answer:**

1. **Absent a multiple support agreement, no one is allowed to claim Roberta as a dependent.**
2. **If a multiple support agreement were executed, no one would be able to claim Roberta as a dependent. A person is entitled to claim a dependent under a multiple support agreement if (1) over half the dependent’s support was received from a group of people who would each have been entitled to claim the person as a dependent absent the support test, (2) no one person in the group provided over half the support, and (3) the person claiming the exemption paid over 10% of the support. In this instance, the only persons entitled to claim Roberta as a dependent absent the support test are Bill and Alicia since neither Ed and Jose meet the relationship test (this assumes that Roberta is Alicia’s aunt by blood and not by marriage). Bill and Alicia contributed only 36% of Roberta’s support ([$5,000 + $3,000] $22,000). Thus, criterion #1 above is not met and no one is entitled to claim Roberta as a dependent.**
3. **Here, the amount paid in support of Roberta is recalculated as follows (percentages are rounded to the nearest full percent):**

**Original Percentage Revised**

**Amount of Original Amount**

**Paid Total Paid**

**Ed (neighbor) $4,000 29% $ 6,380**

**Bill (son) 5,000 36% 7,920**

**Jose (neighbor) 2,000 14% 3,080**

**Alicia (niece) 3,000 21% 4,620**

**--------- ---------**

**$14,000 $22,000**

**As in case (b), either Bill or Alicia is entitled to claim her as a dependent absent the support test. Between them, they provided over 50% of the support of Roberta and each one of them provided over 10% of her support. Thus, either Bill or Alicia would be entitled to claim Roberta if a multiple support agreement were executed.**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

36. Akiko is a U.S. citizen and is the 68-year-old widowed mother of Janet. After retirement, Akiko decided to fulfill a lifelong dream and move to Paris. Akiko receives $1,000 of interest income, but all of her other living expenses (including rent on her Paris apartment with spectacular views of the Eiffel Tower) are paid by Janet. Janet resides in Chicago. Can Janet claim Akiko as a dependent? Explain your answer.

**Answer:**

**Yes, Janet is entitled to claim Akiko as a dependent.**

**The four specific criteria to be able to claim a qualifying relative as a dependent are:**

***Not a qualifying child test.* Akiko is not the qualifying child of another taxpayer.**

***Relationship test.* Akiko meets the relationship test since she is the mother of Janet.**

***Gross income test*. Akiko does not earn equal to or more than the exemption amount.**

***Support test*. Janet provides over 50% of Akiko’s support.**

**In addition, the general tests are also met:**

***Joint return*. Akiko is widowed and will not file a joint return.**

***Citizenship test*. Akiko is a U.S. citizen.**

***Dependent taxpayer test*. Janet cannot be claimed as a dependent by another person.**

**The fact that Akiko lives in Paris does not matter. It is not important that a dependent live in the U.S., only that he or she is a citizen of the U.S. (or be a certain resident or national).**

**Learning Objective: 02-03**

**Topic: Dependents**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

37. Fred is a 22-year-old full-time college student. During 2023, he earned $2,850 from a part-time job and $1,150 in interest income. If Fred is a dependent of his parents, what is his standard deduction amount? If Fred supports himself and is not a dependent of someone else, what is his standard deduction amount?

**Answer:**

**Fred’s standard deduction amount if he is a dependent of his parents is the greater of $1,250 or his earned income plus $400. Fred’s earned income is $2,850 so his standard deduction will be $3,250.**

**If Fred is self-supporting, his standard deduction amount will be $13,850.**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

38. Raphael and Martina are engaged and are planning to travel to Las Vegas during the 2023 Christmas season and get married around the end of the year. In 2023, Raphael expects to earn $45,000 and Martina expects to earn $15,000. Their employers have deducted the appropriate amount of withholding from their paychecks throughout the year. Neither Raphael nor Martina has any itemized deductions. They are trying to decide whether they should get married on December 31, 2023, or on January 1, 2024. What do you recommend? Explain your answer.

**Answer:**

**From a tax perspective, it would be more advantageous for Raphael and Martina to marry in 2023.**

**The tax liability of Raphael and Martina under each scenario would approximate the following:**

**---- Single Returns ----**

**Martina Raphael Joint Return**

**Adjusted Gross Income….. $ 15,000 $ 45,000 $ 60,000**

**Standard deduction ……… (13,850) (13,850) (27,700)**

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**Taxable Income………….. $ 1,150 $ 31,150 $ 32,300**

**Tax liability ……………… $ 118 $ 3,521 $ 3,439**

**If Raphael and Martina get married in 2023 and file a joint return, they will pay $3,439 in federal income tax. If they wait until January 1, 2024, their collective tax liability in 2023 would be $3,639. Thus, for tax purposes, it makes more sense for Raphael and Martina to get married in 2023.**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

39. Determine the amount of the standard deduction for each of the following taxpayers for tax year 2023:

1. Christina, who is single.
2. Adrian and Carol, who are filing a joint return. Their son is blind.

c. Peter and Elizabeth, who are married and file separate tax returns. Elizabeth will itemize her deductions.

d. Karen, who earned $1,100 working a part-time job. She can be claimed as a dependent by her parents.

e. Rodolfo, who is over 65 and is single.

f. Bernard, who is a nonresident alien with U.S. income.

g. Manuel, who is 70, and Esther, who is 63 and blind, will file a joint return.

h. Herman, who is 75 and a qualifying widower with a dependent child.

**Answer:**

1. **Christina, $13,850.**
2. **Adrian and Carol, $27,700. They do not get an additional amount for their son.**
3. **Peter and Elizabeth, $0. Since Elizabeth itemizes, Peter must also itemize so both are entitled to no standard deduction, only an itemized deduction.**
4. **Karen, $1,500 (her earned income plus $400).**
5. **Rodolfo, $15,700 ($13,850 + $1,850).**
6. **Bernard, $0, since he is a nonresident alien.**
7. **Manuel and Esther, $30,700 ($27,700 + $1,500 + $1,500). Each is entitled to an additional standard deduction; Manuel because he is over 65 and Esther because she is blind.**
8. **Herman, $29,200 ($27,700 + $1,500).**

**Learning Objective: 02-04**

**Topic: Standard Deduction**

**Difficulty: 2 Medium**

**Feedback:**

**EA: Yes**

40. Using the appropriate tax tables or tax rate schedules, determine the amount of tax liability in each of the following instances.

a. A married couple filing jointly with taxable income of $32,991.

b. A married couple filing jointly with taxable income of $192,257.

c. A married couple filing separately, one spouse with taxable income of $43,885 and the other with $56,218.

d. A single person with taxable income of $79,436.

e. A single person with taxable income of $297,784.

f. A head of household with taxable income of $96,592.

g. A qualifying widow with taxable income of $14,019.

h. A married couple filing jointly with taxable income of $11,216.

**Answer:**

**All answers rounded to the nearest dollar.**

1. **$3,517 from the tax table.**
2. **$32,942 from the tax rate schedule.**
3. **$5,045 and $7,677 from the tax table.**
4. **$12,781 from the tax table.**
5. **$76,119 from the tax rate schedule.**
6. **$14,972 from the tax table.**
7. **$1,403 from the tax table.**
8. **$1,123 from the tax table.**

**Learning Objective: 02-05**

**Topic: Tax Due to IRS**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

41. Determine the average tax rate and the marginal tax rate for each instance in question.

**Answer:**

**Answers are rounded to the nearest tenth of a percent. Average rates are determined by dividing the tax liability by the taxable income. Marginal rates are determined by reference to the appropriate tax rate schedule.**

1. **Average = 10.7% Marginal = 12%**
2. **Average = 17.1% Marginal = 24%**
3. **Average = 11.5% and 13.7% Marginal = 12% and 22%**
4. **Average = 16.1% Marginal = 22%**
5. **Average = 25.6% Marginal = 35%**
6. **Average = 15.5% Marginal = 24%**
7. **Average = 10% Marginal = 10%**
8. **Average = 10% Marginal = 10%**

**Learning Objective: 02-05**

**Topic: Tax Due to IRS**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

42. Using the appropriate tax tables or tax rate schedules, determine the tax liability for tax year 2023 in each of the following instances. In each case, assume the taxpayer can take only the standard deduction.

a. A single taxpayer with AGI of $23,493 and one dependent.

b. A single taxpayer, not head of household, with AGI of $169,783 and no dependents.

c. A married couple filing jointly with AGI of $39,945 and two dependents.

d. A married couple filing jointly with AGI of $162,288 and three dependents.

e. A married couple filing jointly with AGI of $301,947 and one dependent.

f. A taxpayer filing married filing separately with AGI of $68,996 and one dependent.

g. A qualifying widow, age 66, with AGI of $49,240 and one dependent.

h. A head of household with AGI of $14,392 and two dependents.

i. A head of household with AGI of $59,226 and one dependent.

**Answer:**

1. **Taxpayer is entitled to a standard deduction of $13,850. Taxable income is $9,643 and tax liability is $963 according to the tax tables.**
2. **Taxpayer is entitled to a standard deduction of $13,850. Taxable income is $155,933 and tax liability is $30,824 according to the tax rate schedules.**
3. **Taxpayer is entitled to a standard deduction of $27,700. Taxable income is $12,245 and tax is $1,223 according to the tax tables.**
4. **Taxpayer is entitled to a standard deduction of $27,700. Taxable income is $134,588 and tax is $20,224 according to the tax rate schedules.**
5. **Taxpayer is entitled to a standard deduction of $27,700. Taxable income is $274,247 and tax is $52,619 according to the tax rate schedules.**
6. **Taxpayer is entitled to a standard deduction of $13,850. Taxable income is $55,146 and tax is $7,435 according to the tax tables.**
7. **Taxpayer is entitled to a standard deduction of $29,200 ($27,700 + $1,500) Taxable income is $20,040 and tax is $2,003 according to the tax tables.**
8. **Taxpayer is entitled to a standard deduction of $20,800. Taxable income is zero and tax is zero.**
9. **Taxpayer is entitled to a standard deduction of $20,800. Taxable income is $38,426 and tax is $4,297 according to the tax tables.**

**Learning Objective: 02-05**

**Topic: Tax Due to IRS**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

43. Victoria’s 2023 tax return was due on April 15, 2024, but she did not file it until June 12, 2024. Victoria did not file an extension. The tax due on the tax return when filed was $8,500. In 2023, Victoria paid in $12,000 through withholding. Her 2022 tax liability was $11,500. Victoria’s AGI for 2023 is less than $150,000. How much penalty will Victoria have to pay (disregard interest)?

**Answer:**

**Victoria must pay a failure to file penalty and failure to pay penalty calculated as follows:**

**$12,000 withholding paid**

**+ $ 8,500 tax due**

**$20,500 total tax for 2023**

**$ 8,500 underpayment**

**10% 2 months late × 5% penalty per month (both penalties**

**are combined)**

**$ 850 Failure to file and pay penalties**

**In order to avoid the underpayment penalty, Victoria must have paid the lesser of 90% of the current year’s tax ($18,450) or 100% of the prior year’s tax ($11,500). Since she paid $12,000 in withholding, she does not have to pay the underpayment penalty.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

44. Vinitpaul has the following information:

AGI for 2023 $155,000

Withholding for 2023 = $ 23,000

Total tax for 2022 = $ 29,000

Total tax for 2023 = $ 27,276

1. How much must Vinitpaul pay in estimated taxes to avoid a penalty?
2. If Vinitpaul paid $1,000 per quarter, would he have avoided the estimated tax penalty?

**Answer:**

**a. In order to avoid the underpayment penalty, Vinitpaul must pay the lesser of 90% of the current year tax ($24,548) or 100% of the prior year’s tax ($29,000). His withholding for 2023 will be $23,000. Thus, Vinitpaul must pay at least $1,548 in estimated payments in 2023.**

**b. Yes. Assuming Vinitpaul’s income was earned evenly throughout the year, he would need to pay at least $387 (1,548 4) per quarter in estimated payments to avoid the estimated income tax penalty.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

45. Charles and Joan Thompson file a joint return. In 2022, they had taxable income of $92,370 and paid tax of $11,557. Charles is an advertising executive and Joan is a college professor. During the fall 2023 semester, Joan is planning to take a leave of absence without pay. The Thompsons expect their taxable income to drop to $70,000 in 2023. They expect their 2023 tax liability will be $7,963, which will be the approximate amount of their withholding. Joan anticipates that she will work on academic research during the fall semester.

During September, Joan decides to perform consulting services for some local businesses. Charles and Joan had not anticipated this development. Joan is paid a total of $35,000 during October, November, and December for her work.

What estimated tax payments are Charles and Joan required to make, if any, for tax year 2023? Do you anticipate that the Thompsons will be required to pay an underpayment penalty when they file their 2023 tax return? Explain your answer.

**Answer:**

**Charles and Joan will be required to make estimated payments for tax year 2023. Estimated payments are required equal to the lesser of 90% of the tax shown on the current year return (which we will calculate below) or 100% of the prior year tax (which was $11,557).**

**The amount of estimated payments required for tax year 2023 (using the tax rate schedules) is:**

**Estimated year 2023 taxable income is $105,000 ($70,000 + $35,000)**

**Tax on $89,450……………………………………… $10,294.00**

**Tax on $15,550 ($105,000 – $89,450) 22%……… 3,421.00**

**--------------**

**Estimated 2023 tax liability…..……………. $13,715.00**

**90%**

**----------**

**90% of estimated year 2023 tax liability… $12,343.50**

**========**

**Thus, Charles and Joan will need to pay estimated taxes based on $11,557 (which is the lesser of $12,343.50 or $11,557). Since they will have paid $7,963 in withholding payments, they will have to pay the difference of $3,594 in estimated payments. Because the tax liability shortfall was a result of income earned in the final quarter of the tax year, the estimated payment can be made in one payment on or before January 15, 2024.**

**If Charles and Joan make the estimated payment determined above, it is unlikely they will have an underpayment penalty on their year 2023 tax return.**

**Learning Objective: 02-06**

**Topic: Interest and Tax Penalties**

**Difficulty: 3 Hard**

**Feedback:**

**EA: Yes**

46. Many tax items are subject to annual adjustments for inflation. These include tax brackets, retirement contributions, standard deductions, and many others. What effect do certain inflation adjustments have on tax liability from year-to-year?

A married couple has combined W-2 income of $68,220.

a. For tax year 2023, determine their tax liability.

b. In tax year 2022, the tax tables and amount of standard deduction were different from tax year 2023. Locate the 2022 tax tables and determine the 2022 standard deduction amount. The web is a good place to start your search. If the couple had $68,220 of W-2 income in tax year 2022, what would have been their tax liability?

c. What is the difference between 2022 tax liability and 2023 tax liability?

d. How much of that difference is the result of changes to the tax tables? How much of that difference is the result of the change to the standard deduction?

**Answer:**

**a. $4,423. Taxable income is $40,520 ($68,220 – $27,700).**

**b. $4,668. Taxable income is $42,320 ($68,220 – $25,900).**

**c. $245. 2022 tax of $4,668 minus 2023 tax of $4,423.**

**d. There are a few ways that students can approach these questions.**

**One approach is to hold the standard deduction constant at the 2022 amount ($25,900) and then determine tax liability using the tax tables for both years. If the standard deduction is consistent, then 2023 taxable income is $42,320 ($68,220 – the 2022 standard deduction of $25,900). 2023 tax on $42,320 is $4,639. The difference between the “real” 2023 tax of $4,423 and the amount of tax if the standard deduction is constant ($4,639) is $216. The remaining $29 ($245 – 216) is a result of the change to the tax tables.**

**Another approach (actually imbedded in the approach above) is to notice that the marginal rate in both years is 12%. So, the effect of the $1,800 change to the standard deduction is to save $216 of tax ($1,800 additional deduction multiplied by the 12% marginal rate). Then the remaining $29 ($245 – $216) is a result of the change to the tax tables.**

**Learning Objective: 02-05**

**Learning Objective: 02-06**

**Topic: Tax Due to IRS**

**Topic: Interest and Tax Penalties**

**Difficulty: 3 Hard**

**Feedback:**

**EA: No**