Module 7:
REFUNDABLE CREDITS

Special thanks to: Brad Martin, Katy Schultz, and Evelyn Mickles for their contributions to this module.

PROSPERITY NOW

By the end of this module you will…

- Understand how refundable tax credits impact a taxpayer's return

- Understand the eligibility requirements and required forms for these refundable tax credits:
  - Earned Income Tax Credit
  - Additional Child Tax Credit
  - Premium Tax Credit

Refundable tax credits

Refundable Tax Credits

- A refundable tax credit is considered a payment made by the taxpayer.
- Refundable credits can reduce the tax liability to zero, pay for other taxes, and amounts greater than income tax are paid to the taxpayer as a refund.
- Taxpayers with no income tax who are eligible for refundable tax credits should file a return even if they are not required to file.

Refundable Tax Credit Example

- Jeremy has federal income tax of $2,600.
- Jeremy can claim a $2,000 nonrefundable Child Tax Credit and a $1,500 refundable Earned Income Tax Credit.
- The total amount of credits Jeremy qualifies for ($3,500) is higher than Jeremy's income tax ($2,600).
- Jeremy can claim the full amount of the Child Tax Credit, which reduces his tax liability.
- Jeremy can also claim the full amount of the Earned Income Tax Credit, which reduces his tax liability to $0 and pays the remaining $900 as a refund.

Additional Child Tax Credit

Additional Child Tax Credit

- Taxpayers who cannot use the maximum nonrefundable Child Tax Credit, may be able to claim the refundable Additional Child Tax Credit.
  - The Child Tax Credit is worth up to $2,000 per qualifying child as a nonrefundable credit.

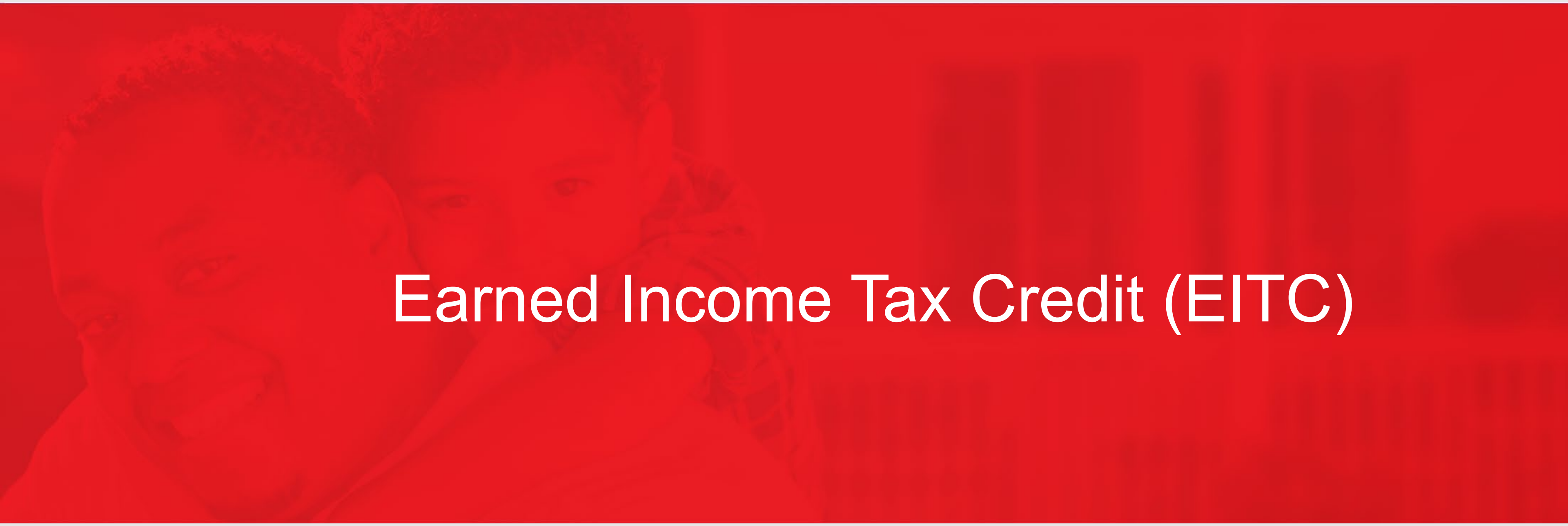
- The Additional Child Tax Credit has a maximum value of $1,400 per qualifying child.

- Qualifications for the Additional Child Tax Credit and the definition of a qualifying child match the qualifications for the Child Tax Credit (covered in Module 6 Nonrefundable Credits).

- To claim the Additional Child Tax Credit, taxpayers must have more than $2,500 in earned income or have three or more qualifying children.

- To claim the credit, use Form 8812. This form collects information about income, tax liability, and the number of eligible children to figure the Child Tax Credit and Additional Child Tax Credit.

Earned Income Tax Credit (EITC)



Earned Income Tax Credit (EITC)

- The EITC is a tax benefit that can serve as a financial supplement for taxpayers with low to moderate incomes, particularly those individuals with children.
- The two main factors when calculating the EITC are income and family size.
- To claim the credit, use Schedule EIC. This form collects information about income and the number of eligible children to figure the amount of the credit.
  - Filers without qualifying children can claim the credit without Schedule EIC and report the credit directly on Form 1040.

Form 1040 (2021) Page **2**

16	**Tax** (see instructions). Check if any from Form(s): 1 ☐ 8814 2 ☐ 4972 3 ☐		16
17	Amount from Schedule 2, line 3		
18	Add lines 16 and 17		
19	Nonrefundable child tax credit or credit for other dependents from Schedule 8812		
20	Amount from Schedule 3, line 8		
21	Add lines 19 and 20		
22	Subtract line 21 from line 18. If zero or less, enter -0-		
23	Other taxes, including self-employment tax, from Schedule 2, line 21		
24	Add lines 22 and 23. This is your **total tax**		
25	Federal income tax withheld from:		
a	Form(s) W-2	25a	
b	Form(s) 1099	25b	
c	Other forms (see instructions)	25c	
d	Add lines 25a through 25c		
26	2021 estimated tax payments and amount applied from 2020 return		
27a	Earned income credit (EIC)	27a	

If you have a qualifying child, attach Sch. EIC.

SCHEDULE EIC (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Earned Income Credit

Qualifying Child Information

▶ **Complete and attach to Form 1040 or 1040-SR only if you have a qualifying child.**

▶ **Go to *www.irs.gov/ScheduleEIC* for the latest information.**

1040 1040-SR EIC

OMB No. 1545-0074

2021

Attachment Sequence No. **43**

Name(s) shown on return | **Your social security number**

If you are separated from your spouse, filing a separate return and meet the requirements to claim the EIC (see instructions), check here ☐

Before you begin:

- See the instructions for Form 1040, lines 27a, 27b, and 27c, to make sure that **(a)** you can take the EIC, and **(b)** you have a qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 800-772-1213.
- If you have a child who meets the conditions to be your qualifying child for purposes of claiming the EIC, but that child doesn't have an SSN as defined in the instructions for Form 1040, lines 27a, 27b, and 27c, see the instructions.

CAUTION

- *You can't claim the EIC for a child who didn't live with you for more than half of the year.*
- *If your child doesn't have an SSN as defined in the instructions for Form 1040, lines 27a, 27b, and 27c, see the instructions.*
- *If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See the instructions for details.*
- *It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.*

Qualifying Child Information	**Child 1**	**Child 2**	**Child 3**
1 Child's name If you have more than three qualifying children, you have to list only three to get the maximum credit.	First name Last name	First name Last name	First name Last name
2 Child's SSN The child must have an SSN as defined in			

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EITC previously disallowed

- If the EIC was denied or reduced for any reason other than a math or clerical error, the taxpayer must include Form 8862.
- This form asks additional questions to confirm the taxpayer qualifies for the credit in this tax year. It's uncommon to need this form!
- Form 8862 collects information about where the taxpayer and any qualifying children lived during the year and confirms the number of days with shared residence.

Form **8862**
(Rev. December 2021)
Department of the Treasury
Internal Revenue Service

Information To Claim Certain Credits After Disallowance

Earned Income Credit (EIC), Child Tax Credit (CTC), Refundable Child Tax Credit (RCTC), Additional Child Tax Credit (ACTC), Credit for Other Dependents (ODC), and American Opportunity Tax Credit (AOTC)

▶ Attach to your tax return. ▶ Go to *www.irs.gov/Form8862* for instructions and the latest information.

OMB No. 1545-0074
Attachment Sequence No. **43A**

Name(s) shown on return	**Your social security number**

You must complete Form 8862 and attach it to your tax return to claim the EIC, CTC/RCTC/ACTC/ODC, or AOTC if both of the following apply.

✓ Your EIC, CTC/RCTC/ACTC/ODC, or AOTC was previously reduced or disallowed for any reason other than a math or clerical error.

✓ You now want to claim the credit that was previously reduced or disallowed and you meet all the requirements for the credit.

Part I All Filers

1 Enter the tax year for which you are filing this form (for example, 2021) . . . . ▶ ☐☐☐☐

2 Check the box(es) that applies to the credit(s) you are claiming and complete the part(s) that matches the box(es) you marked.

Earned Income Credit (Complete Part II)	**Child Tax Credit (nonrefundable or refundable)/Additional Child Tax Credit/Credit for Other Dependents** (Complete Part III)	**American Opportunity Tax Credit** (Complete Part IV)
☐	☐	☐

Part II Earned Income Credit

3 If the **only** reason your EIC was reduced or disallowed was because you incorrectly reported your earned income or investment income, check "Yes." Otherwise, check "No." . . . . ▶ ☐ **Yes** ☐ **No**

Caution: If you checked "Yes," **do not** complete the rest of Part II. Attach this form to your tax return to claim the EIC. If you checked "No," continue.

4 Could you (or your spouse if filing jointly) be claimed as a qualifying child of another taxpayer for the year entered on line 1? . . . . ▶ ☐ **Yes** ☐ **No**

Caution: See the instructions before answering. If you (or your spouse if filing jointly) answer "Yes" to question 4, you cannot claim the EIC.

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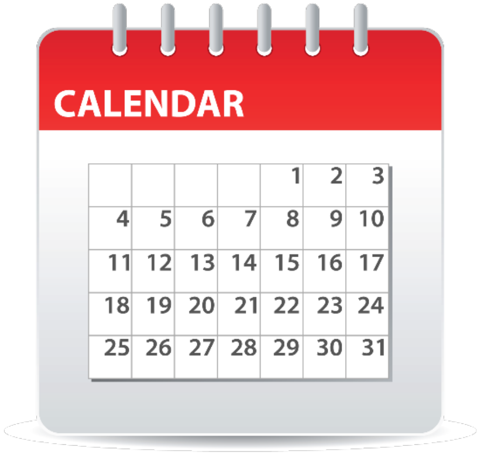
EITC Maximum Credit

- The **maximum** amount of credit for the 2023 Tax Year is:
  - $7,430 with three or more children
  - $6,604 with two children
  - $3,995 with one child
  - $600 with no children



PROSPERITY NOW

How a Taxpayer Qualifies for the EITC

In order to qualify for the Earned Income Tax Credit, an individual must meet all the following criteria:

- Have earned income in the tax year
- Been a citizen of the U.S. or a resident alien for the entire duration of the tax year
- Have a valid Social Security number for yourself, your spouse, and any qualifying child by the due date of your 2022 return (including extensions).
- Investment income cannot exceed $10,300.
- The taxpayer cannot use the MFS filing status (unless the taxpayer lived apart from their spouse for the last 6 months of the year and they have a qualifying child for the credit).
- The taxpayer cannot file Form 2555 – related to foreign income
- If no qualifying children:
    - For earlier tax years the individual must be at least 25 but less than 65
    - Can't be a dependent of another person
    - Can't be a qualifying child of another person
    - Must have lived in the United States more than half of the year

EITC Income Limts

For the 2023 tax year, the Earned Income and Adjusted Gross Income must not exceed the following thresholds.

- $56,838 ($63,398 if Married Filing Jointly) with three or more qualifying children
- $52,918 ($59,478 if Married Filing Jointly) with two qualifying children
- $46,560 ($53,120 if Married Filing Jointly) with one qualifying child
- $17,640 ($24,210 if Married Filing Jointly) with no qualifying child

Qualifying Child Rules

Relationship

- The following will satisfy the relationship requirement.
  - Your son, daughter, adopted child, stepchild, foster child or a descendant of any of the previously stated relationships (e.g., your grandchild).
  - Your brother, sister, half brother, half sister, step brother, step sister or a descendant of any of them (e.g., a niece or nephew).

Age

- At the end of the filing year, your child was younger than you and younger than 19.
- At the end of the filing year, your child was younger than you, younger than 24 and a full-time student.
- At the end of the filing year, your child was any age and permanently and totally disabled.

Residency

- Your child must have lived with you for more than half of the year.

Joint Return

- The child can’t file a joint return for the year

What Qualifies as Earned Income

- Earned Income is income you received from work.

- Income that is generated from interest, rental income, investment dividends, unemployment, worker's compensation and pensions will **not** count as earned income.

- The IRS explicitly defines the following as earned income:
  - Income earned as an employee (Form W-2)
  - Net Earnings from operating a business (Form 1099-NEC, 1099-K, and cash)
  - Some Union strike benefits qualify

What Doesn't Qualify?

As mentioned earlier in this module, the IRS has explicit classifications for unearned income.

This type of income does not involve direct forms of active work or a business venture/activity to receive that income. Some examples of these income sources are:

- Alimony or Child Support
- Unemployment or Worker's Compensation
- Any income that has been received while incarcerated
- Inheritances
- Gifts, gambling winnings, and awards
- Investment Income, Dividends, Interests
- Pension or annuity from deferred compensation plans

Premium Tax Credit

Premium Tax Credit (PTC)

- The PTC is a refundable credit that certain taxpayers may receive to help them pay for health insurance through the Affordable Care Act (ACA).
- Advanced certification is required to prepare returns with this credit.
- Insurance is purchased either from the federal Health Insurance Marketplace or a state-based exchange.
- Qualified taxpayers receive subsidies to help them pay for their insurance; these subsidies are sent directly to the insurance provider, unless the taxpayer chooses to receive the assistance as a tax credit when filing the year's tax return, which rarely happens. The typical process is as follows:
  - The taxpayer signs up for insurance through the ACA Healthcare Marketplace or a state-based exchange, and estimates their total income for the coming year.
  - The Marketplace or exchange figures the amount of premium assistance the taxpayer should receive based on that estimate.
  - At tax filing time, taxpayers must reconcile their actual income with the estimate they made when they initially registered for health insurance.
  - If the taxpayer made less money than they expected, they may receive additional Premium Tax Credits that would have been paid to the insurer if the estimate had been on point.
  - If the taxpayer made more money than expected, the taxpayer may have to repay some or all of the premium assistance they received.

Who qualifies for the PTC?

- To qualify for the premium tax credit:
  - The taxpayer must not be eligible for employer-sponsored health coverage, coverage through a family member's employer sponsored coverage, or government provided coverage such as Medicare, Tricare, or CHIP.
  - The taxpayer must purchase health coverage either from a state-based exchange, or from the federally facilitated Marketplace in states that do not have their own exchanges.
  - The taxpayer's income should be between 100% and 400% of the federal poverty guideline amounts determined for their region and tax family size. See Publication 4012 for exact figures.
  - Taxpayers cannot be married filing separately, unless an exception for spousal abuse or abandonment applies.

Notes:

1. Taxpayers whose income is above 400% of their federal poverty guideline may not have to repay all of the premium tax credit this year.
2. When figuring the income used to calculate this credit, tax exempt interest and dividends and nontaxable social security are included. Also, choosing the Lump Sum Benefit Worksheet for reducing taxable social security does not affect the premium tax credit; for PTC purposes, all social security benefits received in the year, including those paid for prior years, are included in the income calculation.

Figuring the PTC

- The taxpayer should have one or more forms 1095-A showing, among other information:
  - Who is covered by the insurance policy
  - The cost of the taxpayer's insurance policy
  - The second lowest cost silver plan amount (used in figuring the correct amount of premium assistance)
  - The amount of premium assistance that has already been paid, and
  - The months that the person was insured.
- Form 8962 is used to figure the credit. It captures the information from Form 1095-A, and includes calculations to determine the amount of the credit the taxpayer should have received, and it figures the amount that needs to be repaid if excess assistance was provided throughout the year.
- If a Form 1095-A appears to be unusual, such as an amount being missing in Column A for a month, or if you have multiple forms 1095-A, see Publication 4012 for guidance on handling these and other unusual situations.

Caution: If a taxpayer's 1095-A includes the name of a covered individual who is not on the tax return you are preparing, or if the taxpayer has gotten married during the tax year and wishes to elect to use the alternative calculation for year of marriage, the return is out of scope.

Knowledge Check

- Gregory, age 35, is single.
- Gregory's mother, Helen, age 63, lives with Gregory. Helen's only income is $14,500 wages, which she uses to pay for her medical and other personal expenses.
- Gregory's brother, George, is 30 years old. George is totally and permanently disabled. George's income comes from nontaxable supplemental security income (SSI).
- Gregory provides all the cost of keeping up the home for himself, Helen, and George.
- In terms of health insurance, Gregory purchased a plan from the Marketplace and received Advance Premium Tax Credits to help him pay for it.
- Helen's insurance is from Tricare, and George's insurance is from Medicaid.

Question: For the purposes of completing Form 8962, what is Gregory's tax family size?

A. 1, because only Gregory is covered by a Marketplace plan.
B. 2, because Gregory can claim George as a dependent, but Helen's income is too high to qualify her to be Gregory's dependent.
C. 2, because Helen is older than Gregory and cannot be his dependent.
D. 3, because there are three members of the household.

Answer on the next slide.

Knowledge Check Answer:

- B. Form 8962 asks about the tax family size, which means only those individuals whom Gregory can claim on his tax return, including himself. Helen's income is too high to allow him to claim her as a dependent. This has nothing to do with Helen's age. But for the sated reason, Helen is not a member of Gregory's tax family.

Up Next…
Module 8: Education Benefits Overview