



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

4.19.15

OCTOBER 16, 2024

EFFECTIVE DATE

(10-16-2024)

PURPOSE

- (1) This transmits revised IRM 4.19.15, Liability Determination, Discretionary Programs.

MATERIAL CHANGES

- (1) Updated Wage & Investment (W&I) to new name, Taxpayer Services (TS) throughout.
- (2) IRM 4.19.15.3, Education Tax Benefits - General Requirements and Exam Programs - Added project code 0402 - Duplicate Education Credit & Tuition Deduction and Form 14807 - Education Credit Supporting Documents Hope Credit/Lifetime Learning to the chart.
- (3) IRM 4.19.15.10, Math/Clerical Error - Removed content and provided new IRM reference for guidance regarding Math Error program.
- (4) IRM 4.19.15.11.1, Entity, Filing Status, and Dependent Verification - Removed first paragraph. This subsection is applicable to all Exam secured returns.
- (5) IRM 4.19.15.11.1, Entity, Filing Status, and Dependent Verification - Removed first paragraph. This subsection is applicable to all Exam secured returns.
- (6) IRM 4.19.15.12, Self-Employment Tax (SET) - Removed obsoleted IRM reference 4.4.29, AIMS Procedures and Processing Instructions - Social Security Administration (SSA) Adjustments.
- (7) IRM 4.19.15.15, Unallowable Code (UA) Program - Removed content and provided new IRM reference for guidance regarding the Unallowable Code Program.
- (8) IRM 4.19.15.16, Fuel Tax Credit Claimed on Form 4136 - Removed content and provided new IRM reference for guidance regarding Fuel Tax Credit Claimed on Form 4136.
- (9) IRM 4.19.15.18.1, Initial Contact and General Processing - Removed Non-TDC letters, 3540, 3540A, 3541, and 3541A.
- (10) IRM 4.19.15.18.2, No Reply - Removed content. Duplication of IRM 4.19.13.13.
- (11) IRM 4.19.15.18.2, Processing Taxpayer Replies - Updated chart with appropriate IRM reference to use when transferring a case to Appeals.
- (12) IRM 4.19.15.26.1, Commonly Used Terms - Removed Form 885-T, Adjustment to Social Security on Tip Income Not Reported to Employer and replaced with Form 14980-C, FICA Tax and Penalty. Updated verbiage from 'contract' to 'voluntary agreement' since it is debatable if tip agreements are legally enforceable contracts to be more technically precise.
- (13) IRM 4.19.15.26.3, Case Processing – General Information - Replaced Form 885-T with Form 14980-C.
- (14) IRM 4.19.15.26.3.1, Filed Returns – Initial Contact - Replaced Form 885-T with Form 14980-C.
- (15) IRM 4.19.15.27.1, Procedural Instructions - Added additional research instructions for IRPTR, MFTRA and RTVUE to the chart.

- (16) IRM 4.19.15.28, Gambling Issues (Income and Losses) - General Casual Gamblers - Removed invalid reference link in the note.
- (17) IRM 4.19.15.28.2, Evaluating Gambling Issue Responses - Reworded paragraph to clarify the purpose of the section.
- (18) IRM 4.19.15.34.1.1, Individual Taxpayer Identification Number (ITIN) ACTC - Updated OOU information that identifies the tax years are selected for claiming ACTC for dependents with ITINS from 2007 and prior to 2017 and prior.
- (19) IRM 4.19.15.36.2.2, Time Test - Removed Publication 521 reference.
- (20) IRM 4.19.15.36.3, Additional Information - Updated Publication reference from Pub 321 to Pub 3.
- (21) IRM 4.19.15.38, Qualified Plug-In Electric Drive Motor Vehicle Credit - Updated the name of the Qualified Plug-In Electric Drive Motor Vehicle Credit to Clean Vehicle Credit throughout section.
- (22) IRM 4.19.15.39, Math Error Authority on Clean Vehicle Credit (CVC)- Insertion of new process to provide guidance when working pre-refund, math error cases, for CVC cases where the VIN could not be validated.
- (23) IRM 4.19.15.40, Residential Energy Credits - Added a paragraph to define the newly named credits under the Inflation Reduction Act (IRA) 2022. Updated credit names throughout the section.
- (24) IRM 4.19.15.40.1, Energy Efficient Home Improvement Credit and Residential Clean Energy Credit - Added updated credit names, for the appropriate tax years, for completing Form 5695. Removed table and provided information in paragraph format. Added tax year specific information impacted by the Inflation Reduction Act.
- (25) IRM 4.19.15.42, General Business Credit - Updated reporting line numbers for current tax year forms. Added new paragraph for supporting documentation when the taxpayer is a patron of a subchapter T cooperative corporation.
- (26) IRM 4.19.15.45, Non-filer Program – Added and updated IRM references and links.
- (27) IRM 4.19.15.45.4, Manual Reports - Added new subsection to clarify information that must be included when preparing an SFR and to not allow QBID when generating the report. Incorporated Reissue Interim Guidance Memorandum SBSE-04-1221-0068; Formerly SBSE-04-1219-0054, for the Qualified Business Income Deduction on a Substitute for Return
- (28) IRM 4.19.15.45.9, Return Validation - Added guidance regarding TRDBV prints and Taxpayer Protection Program involvement on non-filer cases.
- (29) IRM 4.19.15.45.10.1 (3), Non-Filer Rejects, or Closure Based on Fact of Filing DC 37 or DC01 - Updated the second sentence to have examiners select the open paragraph option on the 0086c Correspondence letter rather than provide the paragraph letter to select. This will eliminate the need to update when future letter revisions may impact the information.
- (30) IRM 4.19.15.45.10.1 (4), Non-Filer Rejects, or Closure Based on Fact of Filing DC 37 or DC01 - Added clarification that Bankruptcy, Docketed Appeals and Statute imminent cases that have been started by Exam should not be routed to Accounts Management.
- (31) IRM 4.19.15.45.11, Exam Return Processing for Non-Filer Cases - Added information to screen cases for further audit that cannot be routed to Accounts Management for processing.
- (32) IRM 4.19.15.45.11.3, Partial Assessments - Previously Referrals to Exam Classification - Removed entire subsection. Removed first two paragraphs to clarify purpose of procedure.

- (33) IRM 4.19.15.45.11.4, Contact After Partial Assessment - Removed first paragraph.
- (34) Removed obsoleted Forms 2555-EZ, 1040-EZ, 4549-EZ, Schedule C-EZ, 14803, 885-T, 886-A1, and Publication 521.
- (35) Updated broken links and minor editorial changes throughout.

EFFECT ON OTHER DOCUMENTS

This IRM supersedes IRM 4.19.15, Liability Determination, Discretionary Programs, dated June 14, 2023.

AUDIENCE

This IRM is intended for the use of SB/SE (Small Business/Self-Employed) and TS (Taxpayer Services) Campus Examination.

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Small Business/Self-Employed

4.19.15

Discretionary Programs

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4.19.15.1
(02-01-2022)
Program Scope and Objectives

- (1) **Purpose:** This IRM contains procedural steps for Campus Exam employees when reviewing taxpayer's correspondence in response to examination notices or letters. It provides instructions to help examiners accurately review individual income tax returns and to ensure taxpayers are in full compliance with all tax laws and regulations in regard to: reporting all income, claiming legitimate dependents, claiming allowable deductions and valid credits.
- (2) **Audience:** IRS employees who are responsible for processing Campus Exam responses in SB/SE and TS Campus Exam.
- (3) **Policy Owner:** SB/SE Director, Examination - Field and Campus Policy.
- (4) **Program Owner:** SB/SE Campus Exam and Field Support (CEFS).
- (5) **Primary Stakeholders:**
 - SB/SE Campus Examination
 - TS Campus Examination
- (6) **Contact Information:** To recommend changes or make any other suggestions to this IRM subsection, see IRM 1.11.6.5, Providing Feedback About an IRM Section - Outside of Clearance.

4.19.15.1.1
(02-01-2022)
Background

- (1) This section is used by Small Business/Self Employed (SB/SE) and Taxpayer Services (TS) Campus Examination to review and process taxpayers' correspondence received in response to examination notices. Other IRM chapters will be referenced throughout this IRM to provide specific guidance for individual topics. Examination employees are responsible for researching and utilizing information contained in all reference materials. Legal citations, form and letter references, and IRM references are reviewed and updated as necessary.
- (2) IRM 4.19.15, Liability Determination, Discretionary Programs, contains information on examination procedures relative to the Exam Discretionary Programs. It provides a reference for common issues and related items that might be found on tax returns that are not compliant with the current tax laws and regulations for individual income tax returns and their related schedules.

4.19.15.1.2
(12-01-2017)
Authority

- (1) By law, the IRS has the authority to conduct examinations under Title 26, Internal Revenue Code, Subtitle F - Procedure and Administration, Chapter 78, Discovery of Liability and Enforcement of Title, Subchapter A, Examination and Inspection, which includes, but is not limited to, the following IRC sections:
 - IRC 7602, Examination of books and witnesses
 - IRC 7605, Time and place of examination

Note: Additional information related to conducting examinations is contained in Treas. Reg. section 601.105, in the Statement of Procedural Rules.

4.19.15.1.3
(02-01-2022)
Roles and Responsibilities

- (1) Liability Determination - Discretionary Programs is used in Campus Examination Operations by managers, coordinators, examiners, and clerical staff to work, control, and monitor inventory for discretionary tax issues in both SB/SE and TS.

- (2) The Taxpayer Bill of Rights (TBOR) lists rights that already existed in the tax code, putting them in simple language and grouping them into 10 fundamental rights. Employees are responsible for being familiar with and acting in accord with taxpayer rights. See IRC 7803(a)(3), Execution of Duties in Accord with Taxpayer Rights. For additional information about the TBOR, see the *Taxpayer Bill of Rights*.

4.19.15.1.4
(06-14-2023)

**Program Management
and Review**

(1) **Program Reviews:**

- Campus program reviews are conducted to ensure case actions are in accordance with IRM procedures.
- Examination quality reviews are conducted using IRM 21.10.1, Embedded Quality (EQ) Program for Accounts Management, Campus Compliance, Field Assistance, Tax Exempt/Government Entities, Return Integrity and Compliance Services (RICS), and Electronic Products and Services Support.
- AIMS Centralized Information System (ACIS) reports are used by Headquarters Policy to review closure statistics and determine the effectiveness of each program.

(2) **Program Reports:**

- See IRM 4.4.27, Reports.
- See IRM 1.4.29, SB/SE Campus Exam/AUR, and TS Exam Operations.
- Embedded Quality Review System (EQRS) Reports are used by managers to evaluate employee performance and by program analysts to identify error trends and coding inconsistencies.
- National Quality Review System (NQRS) Reports are used by managers and program analysts to identify error trends.

4.19.15.1.5
(11-04-2019)

Program Controls

- (1) IRM 4.19.20, Automated Correspondence Exam (ACE) Processing Guidelines, is used for Campus Exam's automated case creation, monitoring, and closure. Cases set up in ACE generate taxpayers's correspondence. Procedures in this IRM are used to process these replies.
- (2) Report Generation Software (RGS), is used by Campus Exam to open case controls, monitor incoming taxpayer correspondence, and manual review of case files.
- (3) The Audit Information Management System (AIMS), under IDRS command code AMDIS is used to display taxpayer's account information.

4.19.15.1.6
(06-14-2023)

**Terms/Definitions/
Acronyms**

- (1) Acronyms used within IRM 4.19.15 are shown in the table below:

Acronym	Definition
AAR	Administrative Adjustment Request
ACA	Affordable Care Act
ACE	Automated Correspondence Examination
AGI	Adjusted Gross Income
AIMS	Audit Information Management System

Acronym	Definition
AM	Accounts Management
AMT	Alternative Minimum Tax
AOTC	American Opportunity Tax Credit
APTC	Advance Premium Tax Credit
ARC	Aging Reason Code
ARRA	American Rebate Recovery Act
ASED	Assessment Statute Expiration Date
ATAA	Alternative Trade Adjustment Assistance
ATTI	Abusive Transactions and Technical Issues
AVS	ACA Verification System
BMF	Business Master File
BOD	Business Operating Division
CAS	Customer Accounts Service
CDR	Coverage Data Repository
CEAS	Correspondence Examination Automation Support
CFC	Campus Fraud Coordinator
CHIP	Children's Health Insurance Program
CI	Criminal Investigation
CII	Correspondence Imaging Inventory
COBRA	Consolidated Omnibus Budget Reconciliation Act
CRN	Credit Reference Number
CSED	Collection Statute Expiration Date
CSEO	Compliance Services Examination Operations
DC	Disposal Code
DDb	Dependent Database
DEBR	Discretionary Examination Business Rules
DFAS	Defense Finance and Accounting Services
DIF	Discriminant Information Function
DOL	Department of Labor
EBE	Employee Business Expenses
EC	Error Code
ECID	Examination Closing Input Document
EGC	Employee Group Code

Acronym	Definition
EIN	Employer Identification Number
EITC	Earned Income Tax Credit
ERS	Error Resolution System
ERSED	Erroneous Refund Statute Expiration Date
ETNF	Employment Tax Non-Filer
EUP	Employee User Portal
FCR	Federal Case Registry
FEHBP	Federal Employees Health Benefits Program
FICA	Federal Insurance Contributions Act
FITW	Federal Income Tax Withholding
FMV	Fair market Value
FPL	Federal Poverty Line
FAFSA	Free Application Federal Student Aid
FSA	Flexible Spending Account
FTC	Fuel Tax Credit
FTD	Failure to Deposit
FTF	Failure to File
FTHBC	First-Time Home Buyer Credit
FTP	Failure to Pay
FUTA	Federal Unemployment Tax Act
HSA	Health Savings Account
HCTC	Health Coverage Tax Credit
HHS	Health and Human Services
HOH	Head of Household
HQ	Headquarters
ICL	Initial Contact Letter
ICM	Inventory Control Manager
IDT	Identity Theft
IMF	Individual Master File
ITIN	Individual Taxpayer Identification Number
LB&I	Large Business & International
LDC	Lead Development Center
LUQ	Large Unusual Questionable

Acronym	Definition
MAGI	Modified Adjusted Gross Income
MCC	Mortgage Credit Certificate
MeF	Modernized Electronically Filed
NRA	Non-Resident Alien
OASDI	Old Age, Survivors, and Disability Insurance
OPM	Office of Personnel Management
OPR	Office of Professional Responsibility
PBC	Primary Business Code
PBGC	Pension Benefit Guaranty Corporation
PC	Project Code
PCS	Partnership Control System
PTC	Premium Tax Credit
QAE	Qualified Adoption Expenses
QDRO	Qualified Domestic Relations Order
QFM	Qualifying Family Member
QRP	Questionable Refund Program
RA	Revenue Agent
RC	Reasonable Cause
RGS	Report Generation Software
RO	Revenue Officer
RPAT	Return Preparer Analysis Tool
RPP	Return Preparer Program
RRTA	Railroad Retirement Tax Act
RURT	Railroad Unemployment Repayment Tax
SB/SE	Small Business/Self Employed
SC	Source Code
SCHIP	State Children's Health Insurance Program
SDC	Scheme Development Center
SE-DPR	Self-Employment Determination Posting Record
SEHID	Self-Employment Health Insurance Deduction
SFR	Substitute For Return
SLCSP	Second Lowest Cost Silver Plan
SNOD	Statutory Notice of Deficiency

Acronym	Definition
SP	Submission Processing
SPC	Special Processing Code
SQPs	State-Qualified Plans
SSA	Social Security Administration
SSIVL	Statistical Sampling Inventory Validation
SSN	Social Security Number
TAA	Trade Adjustment Assistance
TAS	Taxpayer Advocate Service
TC	Tracking Code
TCJA	Tax Cuts and Jobs Act of 2017
TCO	Tax Compliance Officer
TDC	Taxpayer Digital Communication
TEFRA	Tax Equity and Fiscal Responsibility Act
TETR	Telephone Excise Tax Refund
TIN	Taxpayer Identification Number
TPA	Third party Administrator
UA	Unallowable Code
VEBA	Voluntary Employees' Beneficiary Association
VIN	Vehicle Identification Number
TS	Taxpayer Services
WHBAA	Worker Homeownership and Business Assistance Act
WSD	Workload Selection and Delivery

4.19.15.1.7
(06-14-2023)
References

- (1) Other IRMs referenced within IRM 4.19.15 are:

IRM Number	IRM Title
<i>IRM 1.2.1</i>	Servicewide Policy Statements
<i>IRM 1.2.2</i>	Servicewide Delegations of Authority
IRM 1.4.29	SB/SE Campus Exam/AUR, and TS Exam Operations
IRM 4.10	Examination of Returns

IRM Number	IRM Title
IRM 4.19.6	Minister and Religious Waiver Program
IRM 4.19.10	Examination General Overview
IRM 4.19.11	Examination Classification of Work
IRM 4.19.13	General Case Development and Resolution
IRM 4.19.14	Refundable Credits Strategy
IRM 4.19.16	Claims
IRM 4.23.7	Employment Tax on Tip Income
IRM 4.25	Estate and Gift Tax
IRM 21.1.3	Operational Guidelines Overview
IRM 21.4.5	Erroneous Refunds
IRM 25.6.1	Credits
IRM 21.6.3	Statute of Limitations Processes and Procedures

- (2) Helpful information can be found on the Exam Research Portal, located on SERP at: *Exam Research Portal*.
- (3) Helpful information regarding specific correspondence Exam Project Codes can be found on SERP by accessing the *Exam Project Code Search* tool.

4.19.15.2
(06-14-2023)
**Child and Dependent
Care Credit**

- (1) The following guidelines are used to determine if the taxpayer qualifies for the Child and Dependent Care Credit:
- The limit on the amount of qualifying expenses that can be considered in computing the credit is \$3,000 for one qualifying person or \$6,000 for two or more qualifying persons. The amount of qualifying expenses after applying the limit is reduced by the aggregate amount of dependent care assistance excludable from gross income for the tax year.
 - The credit can be as much as 35 percent of qualifying expenses. Refer to Form 2441, Child and Dependent Care Expenses, for computation.

Note: The American Rescue Plan Act revised the Child and Dependent Care credit rules for tax year 2021 only. For tax year 2021, the limit on the amount of qualifying expenses that can be considered in computing the credit is \$8,000 for one qualifying person or \$16,000 for two or more qualifying persons, and the credit can be as much as 50 percent of qualifying expenses. The amount of qualifying expenses must still be reduced by the aggregate amount of dependent care assistance excludable from gross income for the tax year. Refer to the 2021 Form 2441 and instructions for computation.

- (2) A standard Exam letter will be issued requesting verification of items claimed on the return. Cases will be assigned the following project codes (PC): PC 0393, Child Care Credit and the taxpayer is filing Married Filing Separately; PC 0394, Child turned age 13 during the first half of the year; PC 0400, Child Care Credit/Dependent age greater than 12 years, and PC 0628, duplicate dependent for child tax credit, child and dependent care credit or education credit. See IRM 4.19.15.11, Non-Earned Income Tax Credit Duplicate TIN (Non-EITC DUP TIN), for additional guidance on PC 0628, duplicate dependent cases.
- (3) The charts below will be helpful in determining what can be accepted to verify amounts claimed for the Child and Dependent Care Credit.

Reminder: The Tax Cuts and Job Act amended Section 151, effective for Tax Years 2018 through 2025, suspended the deduction for personal exemptions by reducing the amount of the deduction to zero. The rules for claiming the dependent related credits on the tax return remain the same.

A Qualifying Person is:	Verifying Information:
The taxpayer's dependent qualifying child who was under age 13 when the care was provided. Generally, the taxpayer must claim a dependency exemption for the child to claim the credit. However, if a non-custodial parent claims a dependency exemption for the child under the special rule regarding a child of divorced or separated parents or parents who live apart at all times during the last six months of the year, the child is treated as a qualifying person of the custodial parent, not the non-custodial parent for purposes of the credit. The custodial parent must meet the other requirements for claiming the credit.	Age verification - Birth certificate, school records, or baptismal certificate. Qualifying Child Verification – See IRM 4.19.14.6.5, EITC - Personal Exemptions and Dependents.
The taxpayer's spouse who was physically or mentally not able to care for themselves and who lived with the taxpayer for more than half of the year except for temporary absences.	Marriage certificate (proof of spouse). Proof of disability: doctor's statement or state certification.

A Qualifying Person is:	Verifying Information:
<p>The taxpayer's dependent (1) who was physically or mentally not able to care for themselves, (2) who lived with the taxpayer for more than half of the year except for temporary absences, or an unrelated individual who lived with the taxpayer all year as a member of the taxpayer's household, if the relationship didn't violate local laws and (3) for whom the taxpayer can claim an exemption; (or a person who satisfies (1) and (2) and for whom the taxpayer could claim an exemption except that:</p> <ul style="list-style-type: none"> a. The person had gross income of, \$3,650 or more for 2010, \$3,700 or more for 2011, \$3,800 or more for 2012, \$3,900 for 2013, \$3,950 or more for 2014, \$4,000 or more for 2015, \$4,050 or more for both 2016 and 2017, \$4,150 or more for 2018, or \$4,200 or more for 2019, or \$4,300 or more for 2020 and 2021, \$4,400 for 2022, \$4,700 for 2023. b. The person filed a joint return with the person's spouse, or c. The taxpayer, or the taxpayer's spouse if married filing jointly, was a dependent of another taxpayer). 	<ul style="list-style-type: none"> a. Proof of the person's residence: school records, official mail, or local library card. b. If disabled, doctor's statement or state certification to verify the individual's disability.
<p>The Filing Status of the taxpayer must be Single, Head of Household, Qualifying Widow(er) With Dependent Child(Qualifying Surviving Spouse for tax year 2022 and forward), or Married Filing Jointly. If married, a joint return must be filed unless the taxpayer meets the rules to be considered unmarried.</p>	<p>Information is on the return and IMFOL.</p>
Eligibility Requirements Test:	Verifying Information:
<p>The taxpayer and the taxpayer's spouse, if the taxpayer is married, must have earned income during the year. However, a special rule applies to a spouse who is a full-time student or who is unable to care for themselves.</p>	<p>Form W-2, Wage and Tax Statement, or Form 1099. <i>Schedule C, E, or F</i>, if no Form 1099 income.</p>

Eligibility Requirements Test:	Verifying Information:
The taxpayer must pay child and dependent care expenses so that the taxpayer and the taxpayer's spouse, if the taxpayer is married, can work or look for work.	<p>a. Proof of payment includes receipts or cancelled checks. If the expenses claimed were incurred while looking for work, examine interview sheets, job placement letters/ statements, calendar/log/statements showing interview appointments and dates, or places applied to for work.</p> <p>b. If the expenses claimed were for any month in which the taxpayer or the taxpayer's spouse was a full-time student, examine letters/ transcripts from the school showing full-time course load and the specific number of months of enrollment.</p>

Payments	Verifying Information
The identity of the care provider must be reported on the tax return.	The return must include the name, address, and Taxpayer Identification Number (TIN) of the care provider. If the care provider is an individual, the return must include a Social Security Number (SSN) or an ITIN. If the care provider is an organization/corporation, the return must include an Employer Identification Number (EIN). The EIN/TIN does not have to be provided if the care provider is a tax-exempt organization (such as a church or school). If the care provider information given is incorrect or incomplete, the credit may still be allowed if the taxpayer demonstrates due diligence in trying to supply the information.
The taxpayer must pay child and dependent care expenses to a provider the taxpayer or spouse cannot claim as a dependent. If payments are made to a child of the taxpayer, the child cannot be the taxpayer's dependent and must be age 19 years or older by the end of the year. In addition, payments to the taxpayer's spouse or the parent of the taxpayer's qualifying person if that person is the taxpayer's child and under age 13 do not qualify for the credit.	Name on the receipts or cancelled checks. If the taxpayer and the care provider have the same surname, determine if the taxpayer claimed the care provider as a dependent. If the taxpayer did not claim the care provider as a dependent, verify the age of the care provider using INOLE.
Adjustment must be made for any dependent care assistance (payments or benefits) provided by the employers.	Form W-2 or letter from employer.

- (4) If the above conditions are met, compute the allowable credit.
- (5) Expenses for a child to attend kindergarten or a higher grade do not qualify for the Child and Dependent Care Credit. Expenses for before-school or after-school care of a child in kindergarten or a higher grade may qualify for the credit.

- (6) Cases that are not initiated through ACE (Automated Correspondence Examination) must be worked as follows:
- Issue Letter 566-B/ Letter 566-J with Form 4549, Income Tax Examination Changes, if during initial research (DUPOL, DDBKD), it appears that a duplicate dependent was used to obtain a dependent care expense, or
 - Issue Letter 566-B/ Letter 566-J for TDC cases, if initial research indicates: 1) The credit is for a child who is over 12 years, or 2) The Filing Status is Married Filing Separately
 - If neither of the two conditions mentioned in (a) or (b) are met, issue Letter 566-S/Letter 566-T for TDC cases.
 - Request applicable documentation.
 - Follow normal procedures to work the case.
 - If taxpayer is allowed the credit and a duplicate dependent exists, you must open the other duplicate dependent case and disallow the credit.
- (7) Additional information regarding the Child and Dependent Care Credit is found in:
- Pub 503, Child and Dependent Care Expenses
 - Pub 17, Your Federal Income Tax (For Individuals)
 - Instructions for Form 2441, Child and Dependent Care Expenses*

4.19.15.3
(10-16-2024)

**Education Tax Benefits -
General Requirements
and Exam Programs**

- (1) The law offers a number of tax incentives for taxpayers pursuing post-secondary (after high school) education:
- The Hope Credit was a non-refundable tax credit available for the first two years of post-secondary education only. The Hope Credit was replaced in the 2009 tax year by the American Opportunity Tax Credit (AOTC).
 - The AOTC is available for the first four years of post-secondary education only. Forty percent of the AOTC is refundable. The remainder is a non-refundable credit against the taxpayer's tax liability.
- Note:** Bona Fide residents of U.S. Territories (including Puerto Rico) cannot claim AOTC on Form 1040.
- Congress extended the Tuition and Fees Deduction for 2017 in section 40203 of the Bipartisan Budget Act of 2018, Pub. L. 115–123, div. D, title I, Section 40203(a), Feb. 9, 2018, 132 Stat. 145. Congress again extended the Tuition and Fees Deduction for tax years 2018, 2019, and 2020 in section 104 of the Taxpayer Certainty and Disaster Relief Act of 2019. Congress finally repealed, as part of the Taxpayer Certainty and Disaster Relief Act of 2020 (section 104(b)), the deduction for all tax years after 2020.
 - The Lifetime Learning Credit is a non-refundable tax credit available for any year of post-secondary education.
 - The Tuition & Fees Deduction reduces the taxpayer's adjusted gross income (AGI). It is available for any year of post-secondary education.
- (2) A taxpayer cannot claim the Lifetime Learning Credit, the Hope Credit/AOTC or the Tuition & Fees Deduction if any of the following apply:
- The taxpayer's filing status is married filing separately.
 - The taxpayer is listed as a dependent on another taxpayer's return. **(The taxpayer is ineligible for the Tuition & Fees Deduction if the**

taxpayer can be claimed as a dependent on someone else's return, regardless of whether the taxpayer is actually claimed as a dependent.)

- c. The taxpayer (or the taxpayer's spouse) was a nonresident alien for any part of the tax year unless the taxpayer elected to be treated as a resident alien for tax purposes or a treaty applies. More information on nonresident aliens can be found in Publication 519, U.S. Tax Guide for Aliens.

Note: Restrictions specific to each credit/deduction are addressed in the appropriate section.

(3) Eligible educational institution,

- a. An eligible educational institution is any college, university, vocational school, or other postsecondary educational institution eligible to participate in a student aid program administered by the U.S. Department of Education. It includes virtually all accredited public, nonprofit, and proprietary (privately owned profit-making) postsecondary institutions.
- b. Certain educational institutions located outside the United States. See if the school is listed on the *U.S. Department of Education's Federal Student Loan Program list*.

(4) The following table provides an overview of the Education Credit/Deduction Programs currently worked in Exam:

Project Code	Description	Initial Contact Letter	Document Request Form
0351	Hope Credit or AOTC: Taxpayers must demonstrate that they are eligible for the credit.	Letter 566-S/566-T for TDC cases	Form 886-H-AOC and Form 14807
0405	Education Credit – Age Related: Taxpayers must demonstrate they are eligible for the credit.	Letter 566-S/566-T for TDC cases	Form 886-H-AOC and Form 14807
0406	Hope/AOTC claimed for more than 4 years	Letter 566-S/566-T for TDC cases	Form 886-H-AOTC-MAX and/or Form 14807

(5) Additional resources include:

- Pub 970, Tax Benefits for Education
- "What is an Eligible Educational Institution" [irs.gov](https://www.irs.gov) page which includes a link to the Department of Education's list of accredited schools.
- Form 8863, Education Credits (American Opportunity and Lifetime Learning Credits)
- Form 8917, Tuition and Fees Deduction, available 2020 and prior, it cannot be used if credit is taken on Form 8863.
- IRM 21.6.3.4.1.5, Form 8863 Education Credits

4.19.15.3.1
(02-01-2022)

(1) Overview of the Education Tax Credits:

**American Opportunity
Tax Credit (AOTC) and
Lifetime Learning Credit**

Category	AOTC	Lifetime Learning Credit
Maximum Credit	For Tax Years 2009 and forward: Up to \$2,500 credit per eligible student (Calculated as 100 percent of first \$2,000 of qualified expenses and 25 percent on next \$2,000 of qualified expenses, per student).	Up to \$2,000 credit per return (Calculated as 20 percent of qualified expenses up to \$10,000)
Refundable or nonrefundable	40 percent of credit is refundable (limited to \$1,000 per student). The rest is nonrefundable.	Non-refundable credit limited to the amount of tax liability.
Number of years of postsecondary education	Available ONLY for the first 4 years of postsecondary education. Student must not have completed first 4 years of postsecondary education before the beginning of the tax year.	Student does not need to be pursuing a program leading to a degree or other recognized education credential if the course(s) is taken to acquire or improve job skills.
Number of years credit available	Available starting in 2009, ONLY for 4 tax years per eligible student (including any year(s) Hope Credit was claimed).	Available for unlimited number of years.
Type of program required	Student must be pursuing a program leading to a degree or other recognized education credential.	Student does not need to be pursuing a program leading to a degree or other recognized education credential.
Number of courses	Student must be enrolled at least half time for at least one academic period that begins during the tax year.	Available for one or more courses.
Felony drug conviction	No felony drug convictions on student's records.	N/A
Qualified Expenses	Tuition, required enrollment fees, and course materials that the student needs for a course of study whether or not the materials were bought at the educational institution as a condition of enrollment or attendance.	Tuition and fees required for enrollment attendance (including amounts required to be paid to the institution for course-related books, supplies, and equipment). Additional expenses allowed for students in Midwestern disaster areas.

Note: For additional information on tax years prior to 2008, refer to Pub 970, Tax Benefits for Education, for the appropriate year.

- (2) The Hope Credit was available for tax years 2003 through 2008. The American Opportunity Tax Credit (AOTC) replaced the Hope Credit for most taxpayers starting with the 2009 tax year. However, a larger Hope Credit (\$3,600 maximum) was available in 2009 for taxpayers meeting the special rules for the Midwestern disaster areas. In order to claim the Hope credit for 2009 a taxpayer had to:

- Claim the Hope Credit for at least one student attending an eligible institution in a Midwestern disaster area, and
- Choose not to claim the AOTC for any student in 2009.

- (3) The American Opportunity Tax Credit (AOTC) was first available during the 2009 tax year.

Note: The PATH Act made the AOTC permanent.

- (4) The Hope Credit, AOTC, and the Lifetime Learning credit are phased out (gradually reduced) if the taxpayer's Modified Adjusted Gross Income (MAGI), is as follows:

Hope Credit and Lifetime Learning Credit

Tax Year	MAGI
2008	Between \$48,000 and \$58,000 (joint return: \$96,000 and \$116,000)
2009	Between \$50,000 and \$60,000 (joint return: \$100,000 and \$120,000)

Lifetime Learning Credit ONLY

Tax Year	MAGI
2010	Between \$50,000 and \$60,000 (joint return: \$100,000 and \$120,000)
2011	Between \$51,000 and \$61,000 (joint return: \$102,000 and \$122,000)
2012	Between \$52,000 and \$62,000 (joint return: \$104,000 and \$124,000)
2013	Between \$53,000 and \$63,000 (joint return: \$107,000 and \$127,000)
2014	Between \$54,000 and \$64,000 (joint return: \$108,000 and \$128,000)
2015	Between \$55,000 and \$65,000 (joint return: \$110,000 and \$130,000)
2016	Between \$55,000 and \$65,000 (joint return: \$111,000 and \$131,000)
2017	Between \$56,000 and \$66,000 (joint return: \$112,000 and \$132,000)
2018	Between \$57,000 and \$67,000 (joint return: \$114,000 and \$134,000)

Tax Year	MAGI
2019	Between \$58,000 and \$68,000 (joint return: \$116,000 and \$136,000.
2020	Between \$59,000 and \$69,000 (joint return: \$118,000 and \$138,000)
2021 forward	Between \$80,000 and \$90,000 (joint return: \$160,000 and \$180,000)

AOTC ONLY

Tax Year	MAGI
2009 forward	Between \$80,000 and \$90,000 (joint return: \$160,000 and \$180,000)

4.19.15.3.1.1
(11-04-2019)

**Education Tax Credits -
Evaluating Taxpayer
Responses**

(1) General guidelines:

- The two different education credits (the AOTC and the Lifetime Learning Credit) cannot be taken in the same year for the same student. In contrast, more than one credit may be taken on the same return if they are for different students. For instance, a taxpayer may claim the AOTC for an eligible student for whom they claim a dependency exemption, and also claim the Lifetime Learning Credit for themselves.
- Expenses are considered paid by the taxpayer who claims the dependency exemption for the student. If a taxpayer claims the dependency exemption for an eligible student, any expenses paid by the student, or a third party, are considered paid by the taxpayer. If a taxpayer does not claim a dependency exemption for an eligible student, then the student can claim the education credit on the student's return.
- Taxpayers may not take a double benefit for expenses paid. For instance, a taxpayer cannot take a credit for an expense that is allowed as a deduction to the taxpayer.

Caution: AOTC cases selected for exceeding the 4 year rule for claiming AOTC/ Hope Credit should NOT be allowed even if the taxpayer verifies the expenses paid. AOTC is available ONLY for 4 tax years per eligible student including any year(s) that the Hope credit was claimed. When processing these cases, please also check the current year to see if the same SSN is being used to claim the credit again. If so, and the credit decrease would result in a deficiency over tolerance, open the current year, using Tracking Code 9219. Use IDRS command code DLITE with definer E to determine if a student has been claimed for the American Opportunity Credit.

Caution: AOTC cases selected for this issue include:

#

(2) Acceptable documentation of qualified expenses:

Qualified Expenses	Accepted Proof for: AOTC, HOPE, and Lifetime Learning
Qualified tuition and related expenses paid to the academic institution.	Tuition receipts, transcripts to verify enrollment, proof of payment of expenditures via cancelled check or electronic funds payment confirmation, credit card statement, or paid receipt from the institution. Form 1098-T, Tuition Statement, is also acceptable proof if the issuer completes Box 1 of that form. (Note: The educational institution is not required to complete Box 1. A different proof of payment is required if there is no amount in Box 1. See above.)
Fees for course-related books, supplies, and equipment.	For AOTC: Receipts and documentation to support the need for the course of study. For instance: class outline, school program guide, and/or letter from institution. Fees do NOT have to be paid to the institution. For HOPE and Lifetime Learning: Receipts and documentation to support the requirement for enrollment in attendance. For instance: class outline, school program guide, and/or letter from institution -- only if the fees must be paid to the institution as a condition of enrollment or attendance
Prepaid expenses paid in the prior year for an academic period that begins in the first three months of the next year are allowed as a part of the prior year's credit.	Tuition receipts and receipts for qualifying expenses as listed above.
Payments made with borrowed funds are allowed in the year that the expenses are paid, not in the year the loan is repaid.	Receipts and transcripts to determine the year applied.

- (3) Following are expenses that generally do not qualify for an education credit. Note that textbooks and supplies are qualifying expenses for the AOTC, even if they are not purchased from the institution as a requirement for enrollment:

Expenses which generally do not qualify for the credit include:	Accepted proof when allowable
Cost of insurance, medical expenses (including student health fees), room and board, transportation or similar personal, living or family expenses, even if the fee or expenses must be paid to the institution as a condition of enrollment or attendance.	N/A
Expenses related to any course of instruction or other education that involves sports, games or hobbies, or any noncredit course. However, if the instruction or other education is part of the student's degree program or is taken by the student to acquire or improve job skills, these expenses can qualify.	School transcripts and curriculum or catalog demonstrating courses required for the degree program.
For Hope and Lifetime Learning: Textbooks and supplies, even though purchased at the school bookstore, are generally not allowable, unless they are paid to the institution as a requirement for enrollment or attendance. For AOTC: Textbooks and supplies qualify as expenses for the AOTC even if they are NOT required to be purchased from the institution as a condition of enrollment or attendance.	For AOTC: Receipts, cancelled checks, or other proof of payment. To qualify as expenses for the AOTC, textbooks and supplies do NOT have to be purchased from the institution as a condition of enrollment or attendance. For Hope and Lifetime Learning: In addition to proof of payment, documentation to support that textbooks and supplies are required as a condition of enrollment or attendance.

Note: Expenses paid with the tax-free portion of a distribution from a Coverdell educational savings account or qualified tuition program or with tax-free educational assistance, such as a scholarship, grant, or assistance provided by an employer, cannot be used to figure the credit.

- (4) Additional qualifications and conditions for AOTC and Hope Credit (these restrictions do not apply to the Lifetime Learning credit):

Qualifications and conditions for AOTC and Hope credit	Accepted Proof
For AOTC: The taxpayer did not claim an AOTC and/or Hope credit for 4 earlier tax years for the AOTC. For Hope Credit: The taxpayer did not claim a Hope Credit for two earlier tax years for this student.	For AOTC: All prior years' returns for tax years during which the first four academic years of post-secondary studies were not completed. For Hope Credit: All prior years' returns for tax years during which the first two academic years of post-secondary studies were not completed.
The student has not completed the first two years of postsecondary education if claiming a Hope Credit or the first four years of postsecondary education if claiming the AOTC.	School academic transcripts.
The student was enrolled at least half time in a program that leads to a degree, certificate, or other recognized educational credential, for at least one academic period that begins during the taxable year.	School transcripts or Form 1098-T, Tuition Statement
The student was free of any federal or state felony conviction for possessing or distributing a controlled substance as of the end of the tax year in which the credit is claimed.	If any documentation indicates that this has occurred, the credit is not allowable.

- (5) Effective for tax years after 2015, if the taxpayer's claim for AOTC is due to reckless or intentional disregard of rules and regulations, a 2-year ban may apply. If the claim is fraudulent, a 10-year ban may apply. The 2 and 10-year bans do not apply to the Lifetime Learning Credit or the tuition and fees deduction. See IRC 25A(b)(4)(A), and IRM 4.19.14.7.1, 2/10 Year Ban - Correspondence Guidelines for Examination Technicians (CET).

4.19.15.3.2
(02-01-2022)
**Tuition and Fees
Deduction**

- (1) Taxpayers may claim a Tuition and Fees Deduction as an adjustment to income on Form 1040. Beginning in TY 2004 through 2020 certain Tuition and Fees deductions can reduce income, depending on the amount of the taxpayer's modified adjusted gross income (MAGI) – if it does not exceed \$65,000 (\$130,000 for a joint return), \$4000. In the case of a taxpayer whose MAGI is up to \$80,000 (\$160,000 for a joint return), \$2000. In all other cases, the reduction amount is 0. See Pub 970, Tax Benefits for Education, for an explanation of the term, MAGI.
- (2) Generally, taxpayers can claim a deduction if all three of the following requirements are met:

- a. Payments were for qualified education expenses for higher education.
 - b. Education expenses are for an eligible student.
 - c. The eligible student is the taxpayer, the taxpayer's spouse, or a dependent for whom the taxpayer may claim the exemption.
- (3) An eligible educational institution is any college, university, vocational or other post-secondary educational institution.
- (4) Generally qualifying expenses are limited to tuition and fees.
- (5) The taxpayer may not file married filing separately.
- (6) The deduction is phased out between \$65,000 and \$80,000 (\$130,000 - \$160,000 for joint returns).
- (7) No double benefit is allowed:
 - The taxpayer cannot claim a Tuition and Fee expense for a student if they or anyone else claimed the Hope or Lifetime Learning Credit for that same student in the same tax year.
 - Taxpayer cannot use the following expenses to claim the Tuition and Fee expense: expenses paid by tax-free portion of distribution from a Coverdell Educational Savings Account or a qualified tuition program, or expenses paid with tax-free interest on U.S. Savings Bonds, or expenses which have been paid by a tax-free scholarship, grant, or employer-provided educational assistance.

Note: For additional information, refer to Pub 970, Tax Benefits for Education.
- (8) Acceptable Documentation:
 - Transcripts showing name and identifying information of student and period of enrollment
 - Proof of payment for tuition and fees, i.e., cancelled check and invoices from education institution

Note: Form 1098-T, Tuition Statement, is also acceptable as proof of payment if the issuer completes Box 1 of the form. (The educational institution is not required to complete Box 1. A different proof of payment is required if there is not an amount in Box 1. See above.)
- (9) Evaluating Taxpayer Responses:
 - Review the name and SSN on transcripts and payment vouchers to ensure they are the same as those on the tax return.
 - Ensure payments were made by taxpayer.

Note: In contrast to the Education Credits, expenses used for claiming the Tuition & Fees Deduction must have been paid by the person claiming the deduction. Payments made by the student or on their behalf by a third party are not considered to have been paid by the person who claims an exemption for the student. Compare to IRM 4.19.15.3.1.1, Education Tax Credits - Evaluating Taxpayer Responses. So, for instance, if a student pays their own expenses but can be claimed as a dependent on their

parent's tax return, then neither the student nor their parent may claim the Tuition & Fees Deduction.

- Ensure fees are for post-secondary courses.
 - Review return to ensure the same expenses for the same student are not used to claim additional educational benefits such as the Hope/ AOTC or Lifetime Learning Credit; with managerial approval to expand audit to apparent duplicated expenses if needed.
 - Disallow all other expenses other than tuition and fees.
- (10) After the Taxpayer Certainty and Disaster Relief Act of 2019 extended the Tuition and Fees for tax year 2018, 2019, and 2020, Form 8917, Tuition and Fees Deduction, was revised in January of 2020 for taxpayers to retroactively claim the deduction for 2018.

4.19.15.4
(12-01-2017)

Mortgage Interest Credit

- (1) The Mortgage Interest Credit helps lower-income taxpayers afford home ownership. The taxpayer must have received a qualified Mortgage Credit Certificate (MCC) from a state or local government unit or agency.
- Certificates issued by the Federal Housing Administration, Department of Veterans Affairs, Farmers Home Administration and Homestead Staff Exemption Certificates do not qualify for the credit.

4.19.15.4.1
(02-01-2022)

Initial Contact

- (1) For the initial contact, send Letter 566-S/Letter 566-T for TDC cases, and Form 14809, Interest you Paid, to the taxpayer.
- (2) The Form 14809 contains the following language: We need to verify that you are eligible to claim the deduction for **Interest You Paid** taken on Schedule A-Itemized Deductions. Please provide the following information to support the amounts claimed.
- Send copies of mortgage interest statements, equity credit lines/loans, land and mortgage contracts, and amortization schedules for loan outstanding. Send copies of cancelled checks, receipts or other evidence of payments made for the year under examination.
 - Send copies of closing statement verifying points paid.
 - Send copies of statements from financial institutions, investment brokerages or persons to verify your total investment interest deductions.

4.19.15.4.2
(12-01-2017)

Conducting the Examination

- (1) If qualified, the taxpayer may claim the credit each year for part of the home mortgage interest paid. Form 8396, Mortgage Interest Credit, is used to compute the amount of the credit. If the certified indebtedness amount (loan) shown on the Mortgage Credit Certificate (MCC) is less than the total mortgage loan, the credit is figured on only the part of the interest paid that is applicable to the MCC loan.
- (2) The credit is an amount equal to the product of:
1. The certificate credit rate (which may not be less than 10 percent or more than 50 percent), and
 2. The interest paid or accrued by the taxpayer for the year on the remaining principal of the certified indebtedness (plus a limited carry forward, if any).

- (3) If the credit rate exceeds 20 percent, the tax credit for any year may not exceed \$2,000 (IRC 25(a)(2)(A)).
- (4) A three-year carry forward is provided IRC 25(e)(1)(A), for the unused portion of such credit caused by the limitation imposed by IRC 26(a), and IRC 25(a)(2)(A), as amended by Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L.107-16). In essence, the credit and carryover are limited to the tax less the following credits: Foreign Tax Credit, Credit for Child and Dependent Care, Credit for the Elderly or Disabled, Education Credits, Retirement Savings Contributions Credit, Child Tax Credit, and the Adoption Credit. Form 8396, Mortgage Interest Credit, should be used to assist in the calculation of the allowable credit amount.
- (5) If the taxpayer itemized on *Schedule A*, they must reduce the home mortgage interest deduction by the amount of the Mortgage Interest Credit shown on Line 3 of Form 8396. They must do this even if part of that amount must be carried forward.
- (6) If the taxpayer sells the home during the first nine years after the closing date, they may be required to recapture all or part of the benefit received from the program. See Pub 523, *Selling Your Home*, for more information.

4.19.15.4.3
(01-01-2014)
**Evaluating Taxpayer
Responses**

- (1) Use the following to evaluate taxpayer responses:
 - 1. Determine that the taxpayer owns the home and is making the payments by reviewing the Mortgage Interest Statement from the lender on Form 1098, Mortgage Interest Statement, obtained from the taxpayer or through IRPTRL.
 - 2. Review addresses, etc., to ensure the credit is taken on the taxpayer's primary residence.
 - 3. Request and review the Mortgage Credit Certificate to ensure it was issued by the state or local government.
 - 4. Review the certificate credit rate on the Mortgage Credit Certificate to ensure this is the rate applied in the computation and not the rate of interest listed on the mortgage statement from the lender.
 - 5. Review the Schedule A and/or C to ensure the taxpayer has not duplicated the interest deduction and that they have properly reduced the interest deduction claimed by the amount of mortgage interest credit.
 - 6. Review originating year information if the credit is a carryover.
 - 7. Review carryover amounts in subsequent years to ensure accuracy and requisition those returns if errors exist which are significant.
 - 8. Review the computation to ensure the taxpayer is taking the correct amount of credit each year and that applicable credits are not carried over for more than 3 years.
 - 9. If the taxpayer claimed the District of Columbia First-Time Home buyer Credit as a Mortgage Interest Credit, see Form 8859, Carryforward of the District of Columbia First-Time Homebuyer Credit, for proper application of that credit and disallow the Mortgage Interest Credit.

4.19.15.4.4
(03-11-2019)
**Form 886-A
Explanations and Tax
Resources**

- (1) RGS Standard Paragraphs 6306 - 6309 should be used as applicable on Form 886-A, Explanations of Items.
- (2) Tax Resources:

Reference items (Publications, Regulations, existing training materials, existing IRM references, etc.)

- IRC 25, Interest on Certain Home Mortgages
- Pub 530, Tax Information for Homeowners
- Pub 936, Home Mortgage Interest Deduction
- Pub 17, Your Federal Income Tax (For Individuals), Instructions to the Form 8396, Mortgage Interest Credit
- Pub 523, Selling Your Home

4.19.15.5
(02-01-2022)

**Adoption Credit and
Qualified Adoption
Expenses (QAE)**

- (1) The Adoption Credit is nonrefundable for most years but was refundable in 2010 and 2011. Regardless of the year involved, the rules for the Adoption Credit are generally the same. However, the income and dollar limitations change year to year based on inflation. Also, taxpayers who claim a refundable credit for 2010 or 2011 were required to file their returns on paper and to include substantiation when filing their returns.

Note: For more information on the income and dollar limitations, see IRM 4.19.15.5.6, Credit Limitations, and IRM 4.19.15.5, Adoption Credit and Qualified Adoption Expenses (QAE). For more information on substantiation, see IRM 4.19.15.5.3, Evaluating Responses.

- (2) The Adoption Credit was nonrefundable for all taxable years which began on or after January 1, 1997 and ended before January 1, 2010. The Adoption Credit also is nonrefundable for taxable years which begin after December 31, 2011.
- The Adoption Credit was refundable for taxable years which began after December 31, 2009 and ended before January 1, 2012. See the Patient Protection and Affordable Care Act (PL 111-148).
 - Adoption Credit carryforwards from taxable years 2005 - 2009 were also refundable in 2010. See Notice 2010-66, 2010-42 I.R.B. 437.
- (3) The credit is subject to an income limitation based on the taxpayer's modified adjusted gross income (MAGI). See IRM 4.19.15.5.6, Credit Limitations, for more information.
- (4) The credit is also subject to a dollar limitation. See IRM 4.19.15.5.6, Credit Limitations, for more information.
- (5) The Adoption Credit and any employer-provided adoption benefits that can be excluded from income are computed on Form 8839, Qualified Adoption Expenses. The credit then is entered on Form 1040; for tax year 2018 and forward, the credit is entered on *Schedule 3* of Form 1040.
- (6) For refundable years, the Form 8839 instructions advise the taxpayer that they must include documentation, attached to the return, to substantiate the Adoption Credit. Because of the documentation requirement for refundable years, taxpayers must file a paper return when claiming an Adoption Credit for 2010 or 2011.
- (7) The credit will post to Master File as a Transaction Code (TC) 766 with a Credit Reference Number (CRN) 261.

Note: The (TC) 766 with a (CRN) 261 will only be applicable to tax years 2010 and 2011 in which the credit was refundable.

- (8) Command Code (CC) DLITE identifies filters fired through Dependent DataBase (DDB) used in selecting the case for examination. Not all filters are shown, and the fact that a filter has been fired does not mean that the credit is unallowable. Examiners should use this information in evaluating the information submitted by the taxpayer. IRM 4.19.15.5.2, Research and Initial Contact, for more information on CC DLITE.
- (9) The Adoption Credit in SB/SE Campus Exam is worked under Project Code (PC) 0355.
- (10) For further details regarding the Adoption Credit, see Pub 17, Your Federal Income Tax (For Individuals), and the instructions for Form 8839. Additional information about the credit can also be found on <https://www.irs.gov/>, and entering **adoption credit** in the search window.

4.19.15.5.1
(03-12-2018)

Eligible Child – Claiming the Credit or Exclusion

- (1) An eligible child for the purposes of claiming Adoption credit is an individual who:
 - Has not attained age 18, or
 - Is disabled physically or mentally and unable to take care of themself
- (2) Taxpayers may claim the credit for as many children as qualify.
- (3) The proper year for claiming the adoption credit or exclusion depends on whether the eligible child is a citizen or resident of the United States (including U.S. possessions) at the time the adoption effort begins and whether the adoption is final or in process. See the following tables.

Note: If the eligible child is a U.S. citizen or resident, you can take the credit or exclusion even if the adoption never becomes final. See the following tables.

Child who is a U.S. Citizen or Resident

IF the qualified expenses are paid in:	THEN the credit is taken in:
Any year before the year the adoption becomes final	The year after the year of the payment
The year the adoption becomes final	The year the adoption becomes final
Any year after the year the adoption becomes final	The year of the payment

IF the employer paid for qualifying expenses under an adoption assistance program in:	THEN the exclusion is taken in:
Any year	The year of the payment

- (4) **NOTE:** If the eligible child is not a U.S. citizen or resident, you cannot take the adoption credit or exclusion unless the adoption becomes final. See the following tables. Generally, foreign adoptions are either non-Hague adoptions or Hague adoptions. IRM 4.19.15.5.1, Eligible Child - Claiming the Credit or

Exclusion, See the instructions for Form 8839, Qualified Adoption Expenses, for more information regarding foreign adoptions.

Foreign Child

IF the qualified expenses are paid in:	THEN the credit is taken in:
Any year before the year the adoption becomes final	The year the adoption becomes final
The year the adoption becomes final	The year the adoption becomes final
Any year after the year the adoption becomes final	The year of the payment

IF the employer paid for qualifying expenses under an adoption assistance program in:	THEN the exclusion is taken in:
Any year before the year the adoption becomes final	The year the adoption becomes final
The year the adoption becomes final	The year the adoption becomes final
Any year after the year the adoption becomes final	The year of the payment

**4.19.15.5.1.1
(03-12-2018)
Determining the Year a
Foreign Adoption
Becomes Final**

- (1) In general, the year of finality of a foreign adoption is determined either under Rev. Proc. 2005-31 (non-Hague Adoptions), or under Rev. Proc. 2010-31 (Hague Adoptions).

**4.19.15.5.1.2
(01-01-2014)
Non-Hague Adoptions**

- (1) In most non-Hague adoptions, there is an adoption proceeding in the foreign country (and the country is one that is not a party to the Hague Adoption Convention, discussed later) before the child is permitted to come to the United States. There may also be a re-adoption proceeding in the United States, either in the same year as the foreign adoption or in a later year.
- (2) Rev. Proc. 2005-31 generally allows taxpayers to choose as the year of finality:
- the year of the foreign-sending country adoption proceeding; or
 - the year of the re-adoption, if the re-adoption occurs in either the first or second year following the year of the foreign-country proceeding.
- (3) The expenses of re-adoption are qualified adoption expenses in the year in which the expenses are paid, subject to the dollar limitation.

**4.19.15.5.1.3
(11-04-2019)
Hague Adoption
Convention, Adoptions**

- (1) The Hague Convention on Protection of Children and Cooperation in Respect of Inter-country Adoption (Hague Adoption Convention) entered into force for the United States on April 1, 2008. The Hague Adoption Convention applies to a taxpayer who adopted a child from a country that is party to the Hague Adoption Convention and who filed their application and petition (Forms I-800A and I-800) with the U.S. Citizenship and Immigration Service after March 31, 2008.
- (2) See <https://travel.state.gov/content/travel/en/Intercountry-Adoption.html>, for more information on the Hague Adoption Convention, the application and petition, and a complete list of countries that are parties to the Convention.

- (3) In Hague adoptions, there is usually an adoption proceeding in the sending country (and the country is one that is a party to the Hague Adoption Convention, discussed later) before the child is permitted to come to the United States. Rev. Proc. 2010-31 generally allows taxpayers to choose as the year of finality:
- the year in which the sending country enters a final decree of adoption; or
 - the year in which the U.S. Secretary of State issues a certificate under section 301(a) of the Intercountry Adoption Act of 2000, 42 U.S.C. sections 14901-14954.

4.19.15.5.1.4
(12-01-2017)
**Custodial Agreements
Followed by Adoption in
the United States**

- (1) In a few cases, the sending country may permit the child to come to the United States under a custodial agreement. If so, the child will be adopted later in a state court in the United States. Both Rev. Proc. 2005-31 and Rev. Proc. 2010-31 allow the adoptive parent(s) to treat the year of the state-court adoption as the year of finality.

4.19.15.5.2
(02-01-2022)
**Research and Initial
Contact**

- (1) IDRS CC DLITE, using the primary SSN, may provide information and identify filters **fired**. Examiners should research CC DLITE to assist in identifying the selection criteria. Examiners should refer to the tracking codes displayed on DLITE as guidance in evaluating the taxpayer's documentation. Holding cursor over the rule, then hitting XMIT, will display the list of Adoption Credit rules. The tracking codes identifying the filters fired are:
- 0379 - The Federal Case Registry (FCR) file indicates the taxpayer is the custodial parent, non-custodial parent, or putative father.
 - 0381 - 5 year look back period where the credit claimed and carried over to subsequent years exceeded the maximum allowable.
 - 0383 - The primary and/or secondary taxpayer is the father or mother of the child, the date of birth of the child listed on the Form 8839 is less than a year after the update date on the Data Master(DM1)/Kidlink.
- (2) Send Letter 566-S/Letter 566-T for TDC cases, as the initial contact letter (ICL) with a fill-in issue box for Adoption Credit.
- (3) Form 14806, Adoption Credit Documentation Requirements, is sent with the ICL requesting Adoption Credit documentation.

4.19.15.5.3
(03-12-2018)
Evaluating Responses

- (1) Taxpayers being audited must verify that a legal adoption has either been finalized or is in process. In addition, taxpayers must provide verification either of their expenses or of any special needs determination. If part of the credit claimed is a carryforward from a prior year, the taxpayer must provide a worksheet explaining how the carryforward was computed. As the credit was refundable for tax years 2010 and 2011, no carryforward is allowable for tax years 2011 and 2012.

Note: See IRM 4.19.15.5.5 , Carry Forwards, for additional carry forward information.

- (2) Proper documentation must be provided for each child claimed. Follow the guidelines below for acceptable documentation:

Final Adoption

IF	THEN acceptable documentation is:
Domestic or Foreign adoption finalized in the United States	<ul style="list-style-type: none">• Adoption certificate, report or final decree signed by a representative of the State Court, showing the names of the adoptive child and parent, or• Hague Adoption Certificate (Immigrating Child), or• IH 3 Visa
Foreign adoption from a country that is not party to the Hague Convention	<ul style="list-style-type: none">• Translated decree of adoption from a foreign court or other document, issued by the competent authority establishing that a parent-child relationship has been created, or• IR 2 or IR 3 Visa
Special Needs Adoption	See IRM 4.19.15.5.4, Special Needs Adoptions.

In-Process Adoption

IF	THEN
In-Process Adoption (Applicable to the attempted or not-yet-finalized adoption of an eligible child who is a U.S. citizen or resident.)	<p>Taxpayers will provide one or more of the following:</p> <ul style="list-style-type: none"> • A copy of, or a receipt from, a home study completed by an authorized placement agency • A placement agreement with an authorized placement agency • A document signed by a hospital official authorizing the release of a newborn child from the hospital for legal adoption • A court document ordering or approving the placement of the child with the taxpayer for legal adoption • An affidavit or notarized statement signed under penalties of perjury from an adoption attorney, government official, or other authorized person. The documents must state that the signor either placed or is placing a child with you for legal adoption, or is facilitating the adoption process in an official capacity, with a description of the actions taken to facilitate the process.

(3) Tax law requires the taxpayer to claim QAE that they pay for an In-Process adoption for the year after the expense is paid. Examiners need to be aware of the timing of the expense and that the documentation the taxpayer provides may be for a prior year.

(4) Qualifying adoption expenses include:

- Adoption fees
- Court costs
- Attorney fees
- Travel expenses (including amounts spent for meals and lodging) while away from home
- Other expenses directly related to, and whose principal purpose is for, the legal adoption of an eligible child

Note: An expense may be a qualified adoption expense even if the expense is paid before an eligible child has been identified. For

example, prospective adoptive parents who pay for a home study at the outset of an adoption effort may treat the fees as qualified adoption expenses.

- (5) Acceptable proof of expenses include checks and receipts showing proof of payment.
- (6) The following expenses are not allowable and do not qualify for the Adoption Credit:
 - That violate state or federal law
 - For the purpose of carrying out any surrogate parenting arrangement
 - For the adoption of a spouse's child
 - Paid using funds received from any federal, state, or local program
 - Allowed as a credit or deduction under any other provision of federal income tax law
 - Reimbursed by an employer
 - Any other expense that is not directly related to, and whose principal purpose is not for, the legal adoption of an eligible child

4.19.15.5.4
(03-12-2018)
**Special Needs
Adoptions**

- (1) If the adoption is domestic and final, and is of a special needs child (as determined by the state where the adoption occurs), the taxpayer is entitled to claim the maximum amount of the credit (minus any amounts claimed for that child in a previous year) even if the taxpayer paid no qualified adoption expenses.
- (2) A child meets the definition of special needs if **all of the following statements** are true:
 - The child was a citizen or resident of the United States or its possessions at the time the adoption process began **and**
 - A state (including the District of Columbia) has determined that the child cannot or should not be returned to their parents' home **and**
 - The state has determined that the child is unlikely to be adopted unless assistance is provided to the adoptive parents
- (3) The taxpayer must provide **both** of the following documents when substantiating the credit for a special needs child. Do not request verification of any expenses:
 - a. Adoption certificate, report or final decree signed by a representative of the State Court showing the names of the adoptive child and parent and,
 - b. The state's determination of special need designation. See (4) for acceptable documentation of the state's determination of special needs.
- (4) The following are acceptable documentation of the state's determination of special needs (this list not all inclusive)
 - A signed adoption assistance or subsidy agreement issued by the state or county
 - Certification from the state or county welfare agency verifying that the child is approved to receive adoption assistance
 - Certification from the state or county welfare agency verifying that the child has special needs

Caution: For these purposes, an order or decree must include information establishing that the taxpayer's adoption of the eligible child has been finalized

and the date it was finalized. A special needs determination must include information establishing that the state has made a determination of special needs for the eligible child.

- (5) Don't confuse "children with special needs" for purposes of the adoption credit with the definitions of "children with special needs" for other purposes. Foreign children aren't considered to have special needs for purposes of the adoption credit. Even U.S. children who have disabilities may not have special needs for purposes of the adoption credit. Generally, "**special needs adoptions**" are the adoptions of children whom the state's child welfare agency considers **difficult to place for adoption**.

4.19.15.5.5
(02-01-2022)
Carry Forwards

- (1) The nonrefundable adoption credit allows any unused adoption credit to be carried forward for up to five years.
- For taxable year 2010, a refund was allowed for all adoption credit properly carried forward from 2005 through 2009. However, no adoption credit carried forward from 2010 into 2011.
 - Adoption credit properly allowable for the first time in taxable year 2011 was refundable for that year. However, no adoption credit carried forward from 2011 to 2012.
 - In 2012, the adoption credit reverted to being nonrefundable. Adoption credit properly allowable for the first time in 2012 will be allowed if the taxpayer has enough tax liability to use the credit. Any remaining allowable adoption credit will be carried forward to 2013 (the first year of the five-year carryforward period). Similarly, adoption credit first allowable in 2013 will be carried forward into 2014 if the taxpayer does not have enough tax liability to use all the allowable adoption credit in 2013. The same rule applies to later years. For example, adoption credit first allowable in 2014 will be carried forward into 2015 if the taxpayer does not have enough tax liability to use all the allowable adoption credit in 2014.
 - Taxpayers claiming a credit carryforward must provide the same documentation for the carryforward years as a current year adoption. In addition to an explanation or worksheet showing how the carryforward credit was calculated, verification of the adoption and verification of qualified adoption expenses for all years is required.
- (2) The year in which adoption expenses are first eligible to be claimed is the determining year for the maximum credit amount as well as the income limitation restriction. If the taxpayer qualifies for the full credit one year, they cannot increase that amount by carrying it forward to another year. Likewise, if they are limited or disqualified from taking the credit based on their MAGI, they cannot change that restriction, by moving the credit into another year. However, if the taxpayer pays additional adoption credit in a subsequent year, the allowable credit for those expenses is subject to the limitations for the year in which they are eligible to be claimed. Any allowable credit must always be reduced by prior credits taken for the same child.

Note: Most individuals use the cash method of accounting. Therefore, the relevant date for determining whether adoption credit is allowable is the date the adoption credit is **paid**, rather than the date the adoption credit is incurred. The date adoption credit is incurred is relevant only if the taxpayer uses the accrual method of accounting.

- (3) Adoption credit is allowable only if paid in connection with the adoption of an eligible child. Generally, an eligible child is an individual under the age of 18. The relevant date for determining a child's eligibility is when the adoption credit is paid. For example, suppose that adoption credit is paid in year 1, when the child is 16, and the adoption credit becomes allowable in year 2, when the child is 17. Suppose further that the adoptive parent has too little tax liability to use the credit in year 2 and that the credit carries forward into years 3 and 4. In year 5, the adoptive parent has enough tax liability to use the full carried-forward credit. The entire carried-forward credit will be allowable in year 5, even though the child who was adopted is now 20 years old.
- (4) In order to claim adoption credit in the year it is first allowable, individuals must file as single, married filing jointly, head of household, or as qualifying widow(er). If the individual's filing status is married filing separately in the year that particular adoption credit first become allowable, the individual will never be eligible to claim a credit or exclusion for that adoption credit unless they file an amended return, using married filing jointly status, within the period of the statute of limitations. However, an individual who is married filing separately may claim an adoption credit carryforward from a prior year or years, provided that, if the individual was married in the year in which the adoption credit first became allowable, the individual filed a joint return for that year. For more information, see Topic 607, Adoption Credit and Adoption Assistance Programs, available at *Topic No. 607 Adoption Credit and Adoption Assistance Programs*.

4.19.15.5.6
(06-14-2023)

Credit Limitations

- (1) Adoption credit current and prior year limitations:

Current and Prior Year Credit Limitations

Year Range	Maximum Tax Credit (Dollar Limitation)	MAGI Phaseout
2023	\$15,950	\$239,230 - \$279,230
2022	\$14,890	\$223,410 - \$263,410
2021	\$14,440	\$216,660 - \$256,660
2020	\$14,300	\$214,520 - \$254,520
2019	\$14,080	\$211,160 - \$251,160
2018	\$13,810	\$207,140 - \$247,140
2017	\$13,570	\$203,540 - \$243,540
2016	\$13,460	\$201,920 - \$241,920
2015	\$13,400	\$201,010 - \$241,010
2014	\$13,190	\$197,880 - \$237,880
2013	\$12,970	\$194,580 - \$234,580
2012	\$12,650	\$189,710 - \$229,710
2011	\$13,360	\$185,210 - \$225,210

Year Range	Maximum Tax Credit (Dollar Limitation)	MAGI Phaseout
2010	\$13,170	\$182,520 - \$222,520
2009	\$12,150	\$182,180 - \$222,180
2008	\$11,650	\$174,730 - \$214,730
2007	\$11,390	\$170,820 - \$214,820
2006	\$10,960	\$164,410 - \$204,410
2005	\$10,630	\$159,450 - \$199,450

4.19.15.6
(11-04-2019)

Tax Benefits for Kidnapped Children

- (1) Following are guidelines to determine the allowance of tax benefits for kidnapped children for tax years ending after December 21, 2000.

Guidelines for Determining Allowance of Kidnapped Children Tax Benefits

If	And	Then, for all tax years during which the kidnapped child is missing and the treatment has not terminated
The child is presumed by law enforcement authorities to have been kidnapped by someone who is not a member of the family of the taxpayer or the child	The child was the taxpayer's qualifying relative for the part of the year before the kidnapping or	Treat the child as the taxpayer's qualifying relative or
The child is presumed by law enforcement authorities to have been kidnapped by someone who is not a member of the family of the taxpayer or the child	The child had the same principal place of abode as the taxpayer for more than one half of the part of the year before the date of kidnapping	Treat the child as meeting the residency test in the definition of qualifying child.

- (2) Termination of treatment shall apply if there is a determination that the child is deceased, or that the child would have reached the age of 18.

Note: The treatment applies for purposes of (1) the Dependency Exemption, (2) the Child Tax Credit, (3) head of Household filing status, (4) Qualifying widow(er) filing status, and (5) the Earned Income Tax Credit.

4.19.15.7
(01-01-2010)

Questionable Refund Cases

- (1) See IRM 4.19.14.9, Questionable Refund Program (QRP), for program procedures on Questionable Refund cases.

- 4.19.15.8
(01-01-2010)
Alternative Minimum Tax
- (1) The Alternative Minimum Tax (AMT) program cases are identified by Submission Processing as taxpayers who are liable for the AMT but have not completed or attached Form 6251, Alternative Minimum Tax - Individuals.
 - (2) Submission Processing will notify the taxpayers that they appear to be liable for the AMT by issuing Letter 12-C , Individual Return Incomplete for Processing: Forms 1040 & 1040-SR. The case is suspended for a response. If the taxpayer does not respond timely, the return is coded as an Audit Code P, generating the AIMS (Audit Information Management System) opening in Source Code 26.
 - (3) AIMS will open in the Andover Campus (TS) or Philadelphia Campus (SB/SE) based on the Master File Business Operating Division (BOD) Code for the return.
 - (4) For TS, the AMT cases are worked under Project Code 0631.
- 4.19.15.8.1
(02-01-2022)
Alternative Minimum Tax Procedures
- (1) Prepare Letter 2194, Alternative Minimum Tax Proposal, and Form 4549, Examination Report, and issue to the taxpayer for the initial contact.
 - (2) Based on the information reported on the return, the Examination Report (Form 4549) should include the largest determinable amount(s) as adjustments and tax preference items when computing the AMT on Form 6251, Alternative Minimum Tax-Individuals.

If	Then
Taxpayer responds agreeing to the AMT by signing exam report	Process assessment and close case agreed.
Taxpayer responds with tax preference items within 30 days from the issuance of Letter 2194	
No response	<ul style="list-style-type: none"> • 30 day letter - after the suspense time has expired, issue Letter 3219, Notice of Deficiency. • 90 day letter - after the suspense time has expired, process assessment and close case as a default. <p>See IRM 4.19.10.1.7.2, Standard Suspense Periods for Correspondence Examination, for suspension periods for the various letters and time frames to issue letters/notices.</p>

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- 4.19.15.9
(10-01-2001)
Estate and Gift Tax
- (1) Refer to IRM 4.25, Estate and Gift Tax, for information on estate and gift tax audits and procedures.

- 4.19.15.10
(10-16-2024)
Math/Clerical Error
- (1) General procedures for the establishment and processing of unsubstantiated math/clerical error cases are presented in IRM 4.19.14.10, Math/Clerical Error Program.

4.19.15.11

(03-11-2019)

**Non-Earned Income Tax
Credit Duplicate TIN
(Non-EITC DUP TIN)**

- (1) The Non-EITC DUP TIN program includes a population of taxpayers who have claimed a dependent who has been claimed on another taxpayer's tax return. Generally, these cases involve two or more uses of a TIN to claim a dependent.

Program	Duplication of TIN	Tracking Code
Duplicate TIN	2 - 3 times	None
Multi-Duplicate TIN	4 - 10 times	7669
Ten-plus Duplicate TIN	> 10 times	6450
Duplicate Dependent Used for CTC, CCC, Education Credit	1 or more times	6545

- (2) There are two types of the Non-EITC DUP TIN cases, the Dependent/Dependent and Dependent/Primary. For the Dependent/Dependent cases, the same individual is claimed as a dependent by two or more taxpayers. Dependent/Primary cases involve an individual who claimed a personal exemption for themselves and another person who also claimed a dependency exemption for that same individual.
- (3) Definitions for the DUPTIN Program are as follows:
- Non-entitled taxpayer - the taxpayer who is not entitled to claim the dependent or the personal exemption.
 - Entitled taxpayer - the taxpayer who is entitled to claim the dependent or the personal exemption.
 - Abused SSN - the SSN of the person who has been claimed as a dependent by more than one taxpayer in the same tax year or who has claimed a personal exemption and has been claimed as a dependent.
- (4) The Dependent/Dependent cases are assigned Project Code 0097 or 0628 and the Dependent/Primary cases are assigned Project Code 0098 on AIMS.
- (5) Whipsaw cases are established on AIMS under Project Code 0059.

4.19.15.11.1

(02-01-2022)

Initial Contact

- (1) Cases in Project Code 0097 and Project Code 0098 are systemically processed using Automated Correspondence Exam (ACE) processing. The initial contact, Letter 566-S/Letter 566-T for TDC cases, is issued to the taxpayers and the cases are updated to Status 10 on AIMS. For guidance on initiating PC 0628 cases that are not initiated using ACE, refer to IRM 4.19.15.2, Child and Dependent Care Credit, paragraph (6).
- (2) Whipsaw cases in Project Code 0059 are manually processed by preparing Letter 566-B/Letter 566-J for TDC cases, Form 4549 Report of Income Tax Examination Changes, and Form 886-H-DEP. The package is issued to taxpayers and the cases are updated to Status 22 on AIMS. The adjustments in the Examination Report include the disallowance of all duplicated dependents claimed on the returns and any other tax benefits claimed attributable to the dependency exemption such as Child Care Credit, Child Tax Credit, Education Credit or Filing Status. Refer to IRM 4.19.15.11.3, Related Taxpayer, before issuing the Examination Report.

4.19.15.11.2
(03-11-2019)
**Processing Taxpayer
Replies**

- (3) Refer to IRM 4.19.14.6.5, EITC - Personal Exemptions and Dependents, for rules on claiming a personal exemption or dependency exemption and for recommended supporting documentation.

- (1) Refer to IRM 4.19.13.11, Taxpayer Replies, for procedures for processing replies from the taxpayer
- (2) For a child of divorced or separated parents or parents who live apart at all times during the last 6 months of the calendar year, a noncustodial parent claiming a child as a dependent must file a Form 8332, Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent, or substantially similar statement with their return, if the special rule for divorced or separated parents or parents who live apart applies. See Residency Test - Children of divorced or separated parents (or parents who live apart), in Pub 501, Dependents, Standard Deduction and Filing Information.
- (3) Form 8332, Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent, is a written declaration signed by the custodial parent releasing a claim to an exemption for the child to the noncustodial parent for a single year, a specified number of years, or all future years. The noncustodial parent must attach a copy of the signed Form 8332 or similar statement to their return for each year that the non-custodial parent is claiming an exemption for the child.

Note: A copy of this form or similar statement must be requested during the audit since the return is not included in the examination case file. A Form 8332 executed after the return has been filed should be considered in the overall context of the examination when determining which parent is entitled to the exemption.

- (4) The filing requirements for attaching Form 8332 or similar statement to the noncustodial parent's return are based upon the year in which the divorce decree or separation agreement went into effect:

DECREE or AGREEMENT YEAR	IF	THEN
Post-1984 but pre-2009 decree or agreement.	<p>The decree/agreement:</p> <ul style="list-style-type: none"> a. States that the noncustodial parent can claim the child as a dependent without regard to any condition, such as the payment of support, and b. Specifies the year or years in which the noncustodial parent can claim the child as a dependent, and c. Is otherwise substantially similar to Form 8332, and d. Is signed by the custodial parent to indicate that the custodial parent agrees not to claim the child as a dependent for the year. 	<ul style="list-style-type: none"> a. If submitted in lieu of Form 8332, the noncustodial parent must attach certain pages of the decree or agreement to the tax return. b. For additional information, see Custodial parent and noncustodial parent in the chapter on Personal Exemptions and Dependents in Pub 17.
Post-2008 decree or agreement.	<p>The decree/agreement:</p> <ul style="list-style-type: none"> a. States that the noncustodial parent can claim the child as a dependent without regard to any condition, such as the payment of support, and b. Specifies the year or years in which the noncustodial parent can claim the child as a dependent, and c. Is otherwise substantially similar to Form 8332, and d. Is signed by the custodial parent to indicate that the custodial parent agrees not to claim the child as a dependent for the year. 	<ul style="list-style-type: none"> a. The noncustodial parent cannot attach pages from decree/agreement, in lieu of Form 8332. b. The noncustodial parent must attach a Form 8332 or similar statement to their return. c. The custodial parent must sign either Form 8332 or a similar statement whose only purpose is to release the custodial parent's claim to the dependency exemption for the child without any conditions.

- (5) Effective for tax years after 2015, if the taxpayer's claim for ACTC or AOTC is due to reckless or intentional disregard of rules and regulations, a 2-year ban may apply. If the claim is fraudulent, a 10-year ban may apply. The 2- and 10-year bans do not apply to the Lifetime Learning Credit or the tuition and fees deduction. See IRC 24(g)(1), IRC 25A(b)(4)(A) and IRM 4.19.14.7.1, 2/10 Year Ban - Correspondence Guidelines for Examination Technicians (CET).

4.19.15.11.3
(01-01-2016)
Related Taxpayer(s)

- (1) The scope of the examination must be expanded to include returns for taxpayers who, from previous audits, have been determined not to be entitled to the dependency deduction. Consideration must also be given to expanding the examination to returns of taxpayers who, based on analysis of internal information, may not be entitled to the dependency exemption. These cases

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System (AIMS) under Project Code 0059 and started within 30 days from the closure of the previous audit. For related returns claiming EITC, refer to IRM 4.19.14.21.1, DUPTIN Related Taxpayers.

- a. The workpapers on the initial audit must document the reasons the examination was expanded or why it was not expanded.
- b. If opening the custodial TIN per Federal Case Registry (FCR) or the TIN of one of the child's parents per Kidlink, the initial audit must be closed as a "No Change" to tax.

4.19.15.12
(10-16-2024)
**Self-Employment Tax
(SET)**

- (1) IRC 1401 establishes the legal authority for assessing Self-Employment Tax (SET), as defined in IRC 1402. See IRM 25.6.1.9.11, Self-Employment Contributions Act (SECA), for special case situations.
- (2) SET is a tax consisting of Social Security and Medicare taxes primarily for individuals who work for themselves. It is similar to the Social Security and Medicare taxes withheld from the pay of most wage earners. The SET program identifies income that might be subject to SET. The income may be reported on Schedules C or F.
- (3) SET is required when:
 - a. Net earnings from self-employment (excluding church employee income) are \$400 or more, or
 - b. Church employee income is \$108.28 or more. (Income from services performed as a minister, member of a religious order, or Christian Science practitioner isn't church employee income.)
- (4) The SET rate on net earnings is 15.3 percent (12.4 percent Social Security Tax plus 2.9 percent Medicare Tax). See IRM 4.19.15.26, Correspondence Exam Tip Program, for information regarding Additional Medicare Tax on self-employment income.

Note: For 2011 and 2012, the SET rate was reduced to 13.3 percent (10.4 percent Social Security Tax plus 2.9 percent Medicare Tax).

- (5) Taxpayers may deduct half of the self-employment tax amount when determining their adjusted gross income.

Note: For 2011 and 2012, taxpayers may deduct the employer-equivalent portion of the self-employment tax amount when determining their adjusted gross income. The amount that may be deducted varies based upon the amount of self-employment tax the individual paid. See Form 1040 (Schedule SE) for tax year 2012. For tax years beginning after 2012, the deduction for one-half of self-employment tax will be computed without regard to the 0.9 percent Additional Medicare Tax on self-employment income.

4.19.15.12.1
(06-14-2023)
**Self-Employment Tax
Procedures**

- (1) Pull IDRS cc IRPTR (Information Returns Processing Transcript Requests) if available.
- (2) These cases will start in AIMS Status 10 through the Automated Correspondence Exam (ACE) system.

- (3) Letter 718 will be the initial contact letter and will include Form 9549, Explanation of Other Income, which the taxpayer is asked to complete.

Reminder: This information is required for closing so that the Social Security Administration (SSA) records are updated accordingly.

- (4) Case processing:

If	Then
No response is received in 45 days to Letter 718	Prepare Letter 525/Letter 525-T for TDC cases, and report Form 4549.
No response is received to Letter 525/Letter 525-T for TDC cases	Prepare Statutory Notice of Deficiency (SNOD) from the information available.
Taxpayer responds to initial contact and income is determined to be self-employment income	Prepare Letter 525/Letter 525-T for TDC cases, Exam report and propose correct self-employment tax.
Taxpayer responds to initial contact letter with a Form 1040X agreeing that the income is from Self Employment	Close Case agreed. See IRM 4.19.13.11, Taxpayer Replies
Taxpayer substantiates the income is not from self-employment or the taxpayer is not liable for the employee share of FICA (Federal Insurance Contributions Act) tax	Close the case no change and issue Letter 590
Taxpayer claims an employee-employer relationship existed, but the employer did not withhold FICA tax	Request further information to show employee status. Consider referral to SB/SE Compliance Area Office if warranted. IRM 4.19.15.13, SS-8 Determination of Worker Status.
Taxpayer claims to be exempt from self-employment tax due to a previous filing of Form 4361, Application for Exemption From Self-Employment Tax for Use by Ministers, Members of Religious Orders and Christian Science Practitioners, or Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits	Research Master File to verify if indicator is on file. For a list of indicators, see IRM 4.19.6.3, Minister/Religious Waivers Overview. If no indicator, request approved copy of Form 4361, or Form 4029 from taxpayer.
Taxpayer has not retained approved copy of Form 4361 or Form 4029 and there is <ul style="list-style-type: none"> No indicator on Master File No verification of approval is available For a list of indicators, see IRM 4.19.6.3, Minister/Religious Waiver Overview.	Determine tax year form was filed. Research Master File entity information to verify indicator is on file. <ul style="list-style-type: none"> Pull return from files to see if exemption form is attached Continue with the proposed self-employment tax and issue appropriate letter per IRM 4.19.13.11.1, Taxpayer Responses - Prior to Status 24
Reply is a copy of an approved Form 4361 but the MIN-SE-TX-EXEMP-CD field on IDRS cc ENMOD displays a value other than "1", the Form 4361 has NOT been approved.	Route Form 4361 to Philadelphia Campus Mail Stop 4-G08.151 for processing. For general information about Form 4361 see IRM 4.19.6.4.1, General Guidelines for Form 4361.

If	Then
Reply is a copy of an approved Form 4029 but the MIN-SE-TX-EXEMP-CD field on IDRS cc ENMOD displays a value other than “4”, the Form 4029 has NOT been approved.	Route Form 4029 to Philadelphia Campus, Mail Stop 4-G08.151 for processing. For general information about Form 4029 see IRM 4.19.6.5.1, Form 4029-Procedures.
No response.	After the suspension period has expired, process the assessment and close case as a default.

4.19.15.13
(06-14-2023)
**SS-8 Determination of
Worker Status**

- (1) A worker or business files Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding to request a determination on worker status as either an independent contractor or employee. If the business or worker sends a letter to request a worker status determination, send them a Form SS-8 and advise them to resubmit their request for determination to the appropriate office.
- (2) The SS-8 Program is centralized at Brookhaven Campus. Form SS-8 requests involving Federal agencies and instrumentalities or their workers are reviewed by the Associate Chief Counsel (CC:EEE) at the address provided in IRM 7.50.1.1.1, Background.
- (3) Worker classification determinations involving state and local government workers are under the sole purview of the SSA. The SS-8 unit will redirect state or local government workers and agencies requesting a Form SS-8 determination to their local State and Social Security Administrator. See IRM 7.50.1.5.7, Cases Involving State and Local Governments Overview.
- (4) Rev Proc 202X-1 provides guidance and procedures for issuing rulings, determination letters, and information letters. IRS updates this Revenue Procedure annually and can be viewed at *IRS Online Bulletins*.
- (5) If IRS determines a worker (or class of workers) is an employee, correct employment tax returns may be solicited from the respective business employer. If the business does not respond, the business information is available to other IRS offices, which could take further actions, including conducting an employment tax examination.

4.19.15.14
(02-01-2022)
**Partnership-level
Proceedings**

- (1) Refer to IRM 4.29, Pass-through Control System (PCS), IRM 4.31, Pass-Through Entity Handbook, and IRM 4.31.9, Centralized Partnership Audit Regime (BBA) Field Examination Procedures, for additional information for partnerships subject to TEFRA (Tax Equity and Fiscal Responsibility Act of 1982) for tax years beginning before January 1, 2018 or the centralized partnership audit regime enacted by the Bipartisan Budget Act of 2015 (BBA) for tax years beginning on or after January 1, 2018.

4.19.15.14.1
(02-01-2022)

Form 8082, Notice of Inconsistent Treatment and Administrative Adjustment Request (AAR)

- (1) The Form 8082, Notice of Inconsistent Treatment and Administrative Adjustment Request is filed by taxpayers for two different purposes. It is used by taxpayers to report when they are taking a position on their return that is inconsistent with the way the partnership or S- Corporation treated and reported the same item on its return. It is also used by a TEFRA partnership or one of its partners to reflect changes to partnership items. It is also used by BBA partnerships when correcting a previously filed return.
- (2) Notice of Inconsistent Treatment.
 - a. TEFRA and BBA Partners, under IRC 6222 and S corporation shareholders, under IRC 6037(c), are generally required to file their returns consistently with the partnership or S- Corporation return. However, there may be reasons why a member wishes to report items differently. Form 8082, Notice of Inconsistent Treatment or Administrative Adjustment Request (AAR) is used for this purpose. (For tax periods prior to 201812 a partner in an electing large partnership must also file in a manner consist with the partnership, per IRC 6241.)

Note: TEFRA was repealed as part of the BBA of 2015 and replaced with a new centralized partnership audit regime. The repeal of TEFRA became effective for partnership tax years beginning after December 31, 2017.
 - b. Refer to IRM 4.31, Pass-Through Entity Handbook, for additional information.
- (3) Administrative Adjustment Request (AAR).
 - a. An AAR is filed to correct items on the original partnership return, or may be filed by a partner to correct partnership items that have passed through to their return. Form 8082, Notice of Inconsistent Treatment or Administrative Adjustment Request (AAR) is used for this purpose.
 - b. The BBA regime also allows BBA partnerships to file AARs.
 - c. Refer to IRM 4.31.4, TEFRA Administrative Adjustment Request (AAR) for additional information on TEFRA AARs and BBA AARs.

4.19.15.15
(10-16-2024)

Unallowable Code (UA) Program

- (1) The Unallowable Code (UA) Program is a pre-refund program that identifies items for potential audit during return processing. It is a Compliance initiative used to prevent the issuance of erroneous tax refunds on both Individual Master File (IMF) and Business Master File (BMF) tax returns. The program requires coordination between headquarters analysts in TS Campus Examination, SB/SE Campus Examination, Large Business & International (LB&I) and Submission Processing (SP) to ensure the correct types of Unallowable Conditions are being identified. For procedures, refer to IRM 4.19.14.18, Unallowable Code (UA) Program.

4.19.15.16
(10-16-2024)

Fuel Tax Credit Claimed on Form 4136

- (1) Refer to IRM 4.19.14.19, Fuel Tax Credit Claimed on Form 4136 for information.

4.19.15.17
(11-04-2019)

Erroneous Refunds

- (1) The Erroneous Refund Program in Correspondence Examination involves cases that had incorrect refunds issued to taxpayers due to a variety of reasons. The potential for erroneous refunds may occur in the following situations: misapplied payments, incorrect tax adjustments/assessments, incorrect credit refunds, taxpayers filing fraudulent returns, or taxpayers using incorrect TINs. For more information on Erroneous Refunds and causes refer to IRM 21.4.5, Erroneous Refunds, and IRM 5.1.8.7.1, Recovery of Unassessable Erroneous Refunds.
- (2) Erroneous refunds cases are processed according to categories based on characteristics on the tax module. Erroneous refunds are generally classified as either:
 - Assessable – Requires a recalculation of tax liability.
 - Unassessable – No Requirement for a recalculation of tax liability.
- (3) The Correspondence Examination program involves assessable erroneous refunds. These errors arise when the IRS made a downward recomputation of the taxpayer's tax liability based on a substantive determination and later discovers that the determination was incorrect. The adjustment to the tax liability or recapture of a refundable credit will require Statutory Notice of Deficiency processing.
- (4) The assessable erroneous refunds generally are referred to Examination as Category A1 or A2 referrals. There are situations in which Examination closes a case incorrectly and thereby creates an erroneous refund. If the case was closed with an erroneous refund, the case reopening criteria in Rev. Proc. 2005-32, and in IRM 1.2.1.5.1, Policy Statement 4-3, Cases closed by District Directors or Service Center Directors will not be reopened except under certain circumstances, must be followed. Also, see IRM 1.2.2.5.7, Delegation Order 4-7(Rev.1), Notice of Additional Inspection of Books of Account.
- (5) Before examination contact with the taxpayer and initiation of the Statutory Notice of Deficiency processing, each case will be screened to determine if the erroneous refund was correctly classified as assessable or non-assessable. Refer to IRM 21.4.5.5, Erroneous Refund Categories and Procedures, for more information on the categorizing of erroneous refunds.
- (6) Examination will determine if the statutory period for assessment has expired. Since Examination accepts only assessable erroneous refunds with tax liability changes, the ASED becomes the statute of limitations for the erroneous refund and is used in the selection criteria. For informational purposes, the following are the statute of limitations issues involved with erroneous refunds:
 - ASED – Assessment Statute Expiration Date
 - CSED – Collection Statute Expiration Date
 - ERSER – Erroneous Refund Statute Expiration Date
- (7) If the taxpayer did not cause the erroneous refund, and the amount of the erroneous refund is \$50,000 or less, under IRC 6404(e)(2), the IRS must abate interest accruing from the date of the refund to date of notice and demand. If the amount of the erroneous refund is more than \$50,000, the IRS may abate the interest accruing before the date of notice and demand in its discretion, see IRM 20.2.7.7, IRC 6404(e)(2), Erroneous Refunds. The classifier or examiner must determine whether the taxpayer in any way caused the erroneous refund and the **workpapers** must document this determination.

(8) The following procedures should be used in erroneous refunds:

If	Then
Non-assessable erroneous refund or assessment statute period has expired	<ul style="list-style-type: none">• Return transcripts back to initiator.• Non-assessable erroneous refunds are not worked by Examination.
Assessable and statute period of assessment has not expired	<ul style="list-style-type: none">• Submit Form 5345-B, Examination Request Non-ERCS Users, or Form 5345-D, Examination Request-ERCS (Examination Returns Control System) Users, to obtain the examination assembly.• The cases should be opened with the following AIMS information: Source Code: 20 Status Code: 08 Project Code: 0044 for Non-EITC Related or 0045 for EITC Related (EITC is the subject of the erroneous refund) Employee Group Code: 5000

If	Then
Assessable Erroneous Refunds on Individual Income Tax Returns	<ol style="list-style-type: none"> The initial contact letter should be issued as follows: <ul style="list-style-type: none"> Non-EITC Discretionary PC 0044 cases, issue Letter 566-B with examination report. EITC PC 0045 cases, issue Letter 566-S. On Letter 566-B for discretionary or Letter 566-S for EITC, include the following explanation "Erroneous Refund" and "See Form 886-A." Enclose Form 886-A with the following explanation titled <i>Erroneous Refund</i>: <i>"The refund check we mailed to you for your (tax year) overpayment was incorrect."</i> <p>Note: EITC case must follow the three letter exam process; i.e. ICL, 30 Day Letter, and Statutory Notice of Deficiency.</p> When preparing Examination Report, Form 4549, Income Tax Examination Report, use the following suggested explanation: <i>"We are sorry but the refund we sent you is incorrect because we overpaid you by the amount shown in the attached report. We regret the error and thank you for helping us correct it. Since the erroneous overpayment was due to IRS error, no interest will be charged if you pay the amount refunded in error within 21 days from the date of this letter. If the amount due is not received within 21 days, interest will be assessed from the date of this letter demanding repayment."</i> Include in the explanation to the taxpayer, on what line of the tax return or on what schedule the error occurred. Update case to the appropriate AIMS status following general examination procedures.
Assessable Erroneous Refunds on other Federal Tax Returns	<ul style="list-style-type: none"> Refer to IRM 21.4.5, Erroneous Refunds.
Erroneous Refunds to individuals who are Bona Fide residents of Puerto Rico	Contact: LB&I WIIC Planning & Special Programs

- (9) Complete Form 3198, Special Handling Notice for Examination Case Processing, identifying the Erroneous Refund. Special handling is required to abate all interest charges if erroneous refund is repaid within 21 days or within 10 days (when the unpaid amount is \$100,000 or more) of the request for repayment.

4.19.15.18
(06-14-2023)
Alimony

- (1) Alimony or separate maintenance is a payment to or for a spouse or former spouse that satisfies the requirements of IRC 71. The term payer refers to the taxpayer who claims the alimony deduction. The term recipient refers to the spouse or ex-spouse whom the payer states received the alimony. Alimony or separate maintenance must be paid under a divorce or separation instrument. The term, "instrument", means a (i) a decree of divorce or separate maintenance, (ii) a written separation agreement, or (iii) a decree not described in (i) requiring a spouse to make payments of support or maintenance to the other spouse. Different alimony rules apply based upon the date an instrument was executed or modified. The Tax Cuts and Jobs Act of 2017 repealed IRC 71 and IRC 215, removing both the responsibility of including alimony received as income and the ability to declare alimony paid as a deduction to income for any agreement executed after December 31, 2018. The law also applies to agreements executed on or before that date which modified alimony after that date to provide that the alimony is not includable in, or deductible from, income. Beginning with 2019, Form 1040, Schedule 1 requires a payer claiming a deduction for alimony paid to provide the date of the original divorce or separation agreement. See Pub 504, Divorced or Separated Individuals, for additional information.

Note: Alimony modified after 2018 can still be deductible unless the modified agreement states TCJA law applies.

- (2) The correspondence examiner should resolve discrepancies between the amount deducted as alimony by one taxpayer (the payer) and the amount reported as income by the other taxpayer (the recipient). Beginning tax year 2018, receipts and payments of alimonies are reportable on *Schedule 1 of Form 1040*.
- (3) Two of the current Alimony Programs are referenced below.
 - a. Inventory for the Alimony SSN Program involves cases where the recipient of the alimony, as identified by the payer's return, apparently has an invalid SSN. The Project Code for the payer is 0141, and the Project Code for the recipient is 0142.
 - b. Inventory for the Alimony Matching Program involves cases where there is a substantial difference between the alimony deduction claimed by the payer and alimony income reported by the payee. The Project Code for the payer is 0231, and the Project Code for the recipient is 0232.

4.19.15.18.1
(10-16-2024)
**Initial Contact and
General Processing**

- (1) **Payers** - Payer cases are initiated through ACE (Automated Correspondence Exam) processing.
 - a. Payer cases are started in Status 10 with Letter 3541-E, Initial Request For Verification on Alimony Deductions.
 - b. Letter 3541-E, solicits records supporting the deduction claimed by the payer including proof of alimony payment and a copy of the instrument(s) authorizing payment. It also requests identification of the alimony recipient(s).
 - c. Cases will be suspended for 45 days in Status 10.
 - d. When the case moves into Status 22 or when a tax examiner is responding to a reply to the Letter 3541-E, the Letter 3541-D along with the Form 4549 will be mailed.

- e. ACE generated reports include a substantial understatement penalty when applicable. Examiners should consider the application of accuracy penalties and information return penalties when processing responses.
- (2) **Recipients** - Open recipient cases on AIMS and initiate manually only upon verification by a payer of unreported alimony or pension income which would

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cessing IRM 4.4.23.2.1.1, Input Forms, and the IDRS Command Code AM424 Job Aid.

- a. Create the recipient case on AIMS no later than 30 days after closure of the related payer case.
- b. Initiate recipient cases in Status 10 with Letter 3540-E, Initial letter Inquiring about Unreported Alimony Income.
- c. Letter 3540-E, requests a copy of instruments if income is disputed as well as identification of any payers.
- d. Cases will be suspended for 45 days.
- e. After the suspense period, the case will be manually updated to Status 22 and Letter 3540-D cases along with the Form 4549 will be mailed manually by the campus. The case can be introduced into ACE after the Status 22 action is completed.
- f. Recipient workpapers must detail the supporting information for the unreported income provided by the payer and include the payer's name and SSN from initial contact. Include both the ex-spouse's (or spouse's) SSN and the primary TIN of a joint payer return if the ex-spouse filed as the secondary taxpayer.
- g. Include a copy of all relevant supporting documents provided by the payer in the recipient's case file.
- h. Examiners should consider the application of accuracy penalties from initial contact.
- i. Complete appropriately the Related Return Information Section of Form 5344, Examination Closing Record.

Form 5344 field:	Form 5344 entry should be: <i>Note:</i> Overwrite the default entries.
405	Payer's SSN
406	Payer's MFT (Master File Tax)
407	Payer's tax period
408	S

- (3) **All** - Suspend all cases after initial contact for 45 days awaiting taxpayer response.
- (4) **Recipient Return Not Filed** - If the recipient has not filed a return, initiate manually only upon verification by a payer of unreported alimony or pension

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No later than 30 days after closure of the related payer case, open on AIMS per IRM 4.19.15.45.2, Non-Filer Source and Project Codes, and follow examination procedures per IRM 4.19.15.45, Non-Filer Program.

4.19.15.18.2
(10-16-2024)

**Processing Taxpayer
Replies**

- (1) Use the following table when reviewing a taxpayer's reply.

If	Then
The taxpayer signs the report or, prior to the mailing of a Statutory Notice of Deficiency, pays the full amount	Close the case agreed using normal procedures.
The taxpayer submits documentation and you need additional information	Follow procedures in IRM 4.19.13.11.1, Taxpayer Response – Prior to Status 24. Note: Treat Letter 3540/Letter 3540-D for TDC cases, and Letter 3541/Letter 3541-D for TDC cases the same as Letter 525/Letter 525-T for TDC cases.
The taxpayer appeals the determination	Follow relevant procedures in IRM 4.19.13.17, Appeals - Non Docketed Cases.
The taxpayer submits sufficient verification that the return is substantially correct.	Close using "no change" procedures.

Note: If at any time during the examination of a Payer it is discovered that the Payer listed an incorrect Recipient TIN on their tax return, inform the taxpayer of this. Notification can be given at any time before closing and may be accomplished through correspondence or a phone call. Examiners must document on the workpapers that this has been done. Notifying the taxpayer of their TIN reporting error will help prevent them from making the same error year-to-year, and potentially triggering audit selection rules unnecessarily.

- (2) Open a recipient case under the conditions noted in IRM 4.19.15.18.1, Initial Contact and General Processing, paragraph (2). The related payer case need not be closed first. For example, alimony payments may be resolved with respect to one recipient and not another, or the payer case remains open for expanded issues only. Monitor a payer case through default if necessary when the conditions to open a recipient case have been met but additional supporting records are required to resolve the remainder of payments purported to be made to the same recipient. Copy all pertinent documents provided by the payer for inclusion in the recipient's file in case the latter files an appeal.

Note: The burden of proof is on the IRS for disputed income.

4.19.15.18.3
(02-01-2022)
Workpapers

- (1) While thorough workpaper documentation is important regardless of the issue, it is particularly critical for alimony deductions/income because the outcome of one taxpayer's case may impact one or more other taxpayers.
- (2) Examiners should note the following when applicable on Form 4700, Examination Workpapers (not all inclusive):

- The type of each document received (e.g., divorce decree, separate maintenance agreement, written separation agreement, QDRO (Qualified Domestic Relations Order), cancelled check, pay statement, etc.).
- The date of an instrument, the state in which it was executed, and the parties who signed it.
- The name and SSN of the other party affected by an instrument or QDRO. (Also if the other party filed as the secondary taxpayer on a joint return, note the primary TIN of that return.)
- The nature of the payments ordered by an instrument (e.g., pension, periodic alimony (in general, applicable for instruments executed on or before December 31, 1985), lump-sum alimony (see IRC 71(f) recharacterizing deductible alimony as a nondeductible property settlement), unallocated family support (in general, for instruments executed after December 31, 1984, see IRC 1.71-1T, Q/As 15 through 18, describing the circumstances in which an amount of unallocated family support is fixed as child support and not alimony), etc.) and the amounts specified by type.

Note: It is not necessary to detail a property settlement unless the payer deducted it or to note any other type of payment if the payer only claimed a pension split.

- The presence or absence of a child support order (not applicable for pension splits). If child support is ordered, it must be verified as paid before allowing a deduction for any direct payments for alimony.
- The presence or absence of a death contingency (not applicable for pension splits). If there's a death contingency, explain whether it is specifically stated in an instrument or it applies by operation of state law.
- The presence or absence of a child-related contingency if unallocated support was ordered in an instrument.

- (3) Taxpayers often deduct payments made to more than one spouse/former spouse. Record documentation received concerning each recipient separately in the payer's workpapers.

Note: Copy/paste can be used when creating the recipient's workpapers to transfer information from the payer's workpapers.

- (4) If the payer audit results in a no-change, audit consideration of the recipient taxpayer(s) must be documented in the payer's workpapers. The workpapers must indicate whether the audit was or was not expanded to the recipient taxpayer(s) and why.
- (5) Refer to IRM 4.19.13.3.3, Standard 3 - Workpapers Support Conclusions and IRM 4.19.13.6, Workpapers for All Cases for more information concerning workpapers.

4.19.15.18.4
(02-01-2022)
Research

- (1) **Payers** - Since payer cases are initiated systemically, it's important to thoroughly research IDRS when processing the first response.
- a. Screen each recipient's RTVUE/TRDBV and IRPTR to determine if alimony income was substantially reported on any income line of a recipient's return.
 - b. Review each recipient's account to determine if an amended return was filed to report the alimony income.

- c. After verification of payments made, meet IRC 71 requirements, close the payer case as a “no change” if alimony income reported by the recipient(s) substantially matches the alimony deduction claimed by the payer.
 - d. Screen the payer’s RTVUE/TRDBV and IRPTR to determine if there are large, unusual or questionable items (LUQs) other than the alimony deduction and revise the report if warranted. Do not introduce new deficiency issues when sending Letter 555.
- (2) **Recipients** - Perform IDRS research prior to establishing a recipient case on AIMS.
- a. Review the recipient’s account to determine if an amended return was filed. It is common for payers to inform recipients of their examinations, often prompting recipients to amend their returns.
 - b. Screen the recipient’s RTVUE/TRDBV and IRPTR to determine if there are any LUQs other than the alimony income and expand the scope of the audit if warranted.
- (3) **All** - Review all related CEAS records including any for prior and subsequent years and for the cross-reference taxpayer(s) to determine if they contain pertinent information. However, do not “no change” a case solely because the same issue was examined for another tax year and not adjusted. Each year stands on its own merits.

4.19.15.18.5
(11-04-2019)
Documentation

- (1) Documentation must include the instrument that orders the payment of alimony with all amendments and proof of payment in the form of:
- Copies of cancelled checks identifying who received the funds, the dollar amount and the date the payment cleared the bank, the front and back of money orders, or proof of direct deposit that specifically identifies the recipient by name;
 - Court receipts or statements from state or county agencies to which payments were made; or
 - Pay statements showing the name of the recipient or court document docket number.
- (2) The instrument may require payments to third parties that could qualify as alimony. Documentation can include, but is not limited to:
- Copy of a deed to verify home ownership for mortgage, real estate taxes and home insurance payments;
 - Receipts, utility statements, lease agreement, etc., for living expenses;
 - Registration and receipts for education expenses;
 - Proof of recipient’s ownership for life insurance premiums;
 - Bills and receipts for medical and dental expenses;
 - Statements for health insurance premiums;
 - Proof of ownership of other property such as car, boat, recreational vehicle, etc. The recipient must be the sole owner of said property.
- (3) Payments designated as not alimony on or before December 31, 2018, can only be excluded from income if the recipient attaches a copy of the instrument designating the payments as not alimony, on instruments executed to their return. The instrument must be attached to the return for each tax year for which the designation applies.
- (4) Unacceptable documentation includes but is not limited to:

- Unsigned (by either a judge or both affected parties), undated, or incomplete instruments,
- Letters unexecuted testifying to verbal agreements,
- Retroactive instruments unless a judge indicates the correction was due to a clerical error made by the court or there is a nunc pro tunc order revising the original decree to conform to the intent of the court at the time of entry.

4.19.15.18.6
(01-01-2015)

Legal Terminology

- (1) Instruments of divorce or separation often contain legal terminology. Some frequently used terms relevant to alimony include:

- *Decree nisi* - a provisional decree that will become final unless cause is shown why it should not.

Note: Some states grant divorces using decrees nisi. The decree nisi creates a time period (such as three months) allowing for possible reconciliation or for completion of various arrangements (such as custody).

- *Separation a mensa et thoro* - a separation of spouses which does not involve a dissolution of the marriage but in which certain arrangements (such as for maintenance and custody) are ordered by the court (also called legal separation, judicial separation).
- *Divorce a vinculo matrimonii* - a divorce that completely and permanently dissolves the marital relationship and terminates marital rights (such as property rights) and obligations (such as fidelity); absolute divorce.
- *Ex parte* - on behalf of or involving only one party to a legal matter and in the absence of and usually without notice to the other party.

Example: an ex parte motion;

Example: relief granted ex parte (used in citations to indicate the party seeking judicial relief in a case).

- *Nunc pro tunc* - now for then (used in reference to a judicial or procedural act that corrects an omission in the record, has effect as of an earlier date, or takes place after a deadline has expired).

Example: a nunc pro tunc order;

Example: permitted to file the petition nunc pro tunc.

- *Pendente lite* - during the suit: while litigation continues.

Example: awarded joint legal custody of the child pendente lite;

Example: pendente lite child support.

- *Interlocutory* - not final or definitive.

Example: an interlocutory order.

- *Joint tenancy* - a tenancy in which two or more parties hold equal and simultaneously created interests in the same property and in which title to the entire property is to remain with the survivors upon the death of one of them (such as a spouse) and so on to the last survivor.

Example: a right to sever the joint tenancy.

- *Tenants in common* - a tenancy in which two or more parties share ownership of property but have no right to each other's interest (such as upon the death of another tenant).
- *Tenants by the entirety* - a tenancy that is shared by spouses who are considered one person in law and have the rights of survivorship inherent in joint tenancy and that become a tenancy in common in the event of divorce.

Example: Property subject to a tenancy by the entirety cannot be encumbered by one tenant acting alone.

4.19.15.18.7
(02-01-2022)
Death Contingency

- (1) Prior to the repeal of IRC 71 by TCJA, IRC 71 required, in part, that for a payment to qualify as alimony, the payment must immediately cease upon the death of the payee. The termination requirement was satisfied if set forth in the applicable instrument or occurred by operation of state law or, in certain cases, federal law. Typically, the state, in which the instrument was executed, applies to determine whether alimony immediately ceases upon the death of the payee. In general, this requirement is applicable only to instruments executed on or before December 31, 2018. See Pub 504.

4.19.15.18.8
(02-01-2022)
Pension Income

- (1) **Qualified Domestic Relations Order (QDRO)** - If pension income is paid from a qualified retirement plan that is a private industry plan, an instrument can provide for the division of the retirement benefit or distribution between the plan participant and a non-participant spouse (or former spouse). This instrument is referred to as a qualified domestic relations order (QDRO), and transfers the applicable percentage of distributions or other amounts from the plan to an alternate payee who may be the non-participant spouse (or former spouse) or a child or other dependent. Although pension income paid to a non-participant spouse (or former spouse) is not alimony, it is frequently deducted as such. A distribution that is paid under a QDRO to an alternate payee who is a spouse (or former spouse), is taxed to the spouse (or former spouse). A distribution that is paid under a QDRO to an alternate payee who is a child or other dependent is taxed to the plan participant. However, the participant may be ordered to pay the required percentage directly to a non-participant spouse after distribution. Under a QDRO, separate Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., should be issued to each individual, the plan participant and non-participant spouse, showing only the amount of their respective distributions. If a distribution is paid under a QDRO to a non-spouse, such as a child, only one Form 1099-R is issued to the participant showing the entire distribution. Unlike other property settlements, pension distributions are taxable to the recipients because those distributions were based on amounts previously contributed on a tax-deferred basis.
- (2) A QDRO is not a divorce decree. It is the document used to authorize a qualified retirement plan to distribute funds to an alternate payee. However, the participant may be ordered to pay the required percentage directly to a non-participant spouse (or former spouse) after distribution. Unlike other property settlements, pension distributions from a qualified retirement plan generally are taxable to the recipients because those distributions were based on amounts previously contributed to the plan on a tax-deferred basis (unless the participant made after-tax employee contributions). If a plan distributes a portion of a participant's pension to a participant spouse and, under a QDRO, a portion of the participant's pension to the non-participant spouse (or former spouse),

separate Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., should be issued to each individual, the plan participant and non-participant spouse (or former spouse), showing only the amount of their respective distributions. If the distribution of the pension income under the QDRO is to a non-spouse, such as a child, only one Form 1099-R is issued to the participant showing the entire distribution. Retirement plans that are maintained by governments or churches can also divide a retirement benefit or distribution between the plan participant and non-participant spouse under a domestic relations order as if the document were a QDRO. In such a case, the tax treatment described above applies to distributions from the plan made under the domestic relations order.

- (3) **Defense Finance and Accounting Services (DFAS) Reporting** - A portion of a military pension can be paid by the Defense Finance and Accounting Services (DFAS) directly to a former spouse under a domestic relations order for child support, alimony, or as a division of the retired pay as property. Under these circumstances, DFAS will issue a Form 1099-R to each individual reflecting their shares of the retirement and taxes withheld. If the domestic relations order instead requires a portion of the military retirement pay to be paid to a non-spouse, such as a child, that portion is included in the participant's taxable income and only one Form 1099-R is issued to the participant showing the entire distribution. A copy of both the front and back of the Retiree Account Statement (DFAS-CL) must be received to verify the taxpayer claimed the entire pension amount. The plan participant can obtain the copies from **MyPay** at <https://mypay.dfas.mil/>
- (4) **State and Local Government/Private Industry Pensions** - Total distributions from the plan must be verified to ensure the taxpayer claimed the full amount received by all parties.
- (5) **Disability Pensions** - Disability pensions paid from any retirement plan other than a military plan are taxable. Certain military disability retirement payments are nontaxable to the participant. However, the non-taxable nature of a disability pension paid from a military plan does not transfer to the non-participant spouse (or former spouse). The disabled participant spouse cannot take a deduction for a non-taxable distribution transferred to a non-participant spouse (or former spouse) unless it is first reported in taxable income. The non-participant spouse (or former spouse) is required to report the income on their tax return.

Note: Do not use alimony language when adjusting pension income. For additional information refer to IRM 21.6.6.2.19.1 , Extension of Statute of Limitations to File Claims for Refunds Relating to Disability Determinations by Department of Veterans Affairs (Section 106 of public law 110-245, codified at IRC 6511(d)(8)).

4.19.15.19
(03-10-2017)
What is DIF CORR
(Source Code 06)

- (1) Discriminant Information Function (DIF) examines non-complex credits, deductions and/or expenses on Nonbusiness returns. Some examples are:
 - Interest
 - Taxes
 - Contributions
 - Medical Expenses
 - Simple miscellaneous expenses such as union dues, work clothes, and small tools

- (2) DIF order could be utilized to select high income taxpayers with high DIF score for audit.
- (3) DIF returns require classification.

4.19.15.19.1
(06-14-2023)

**Procedures for DIF
CORR (Source Code 06)**

- (1) Use Initial Contact Letter 566-S to notify taxpayer of review.
- (2) Check off the issues identified on the classification sheet on Letter 566-S.

If	Then
Adjustment is required after information is submitted by the taxpayer	Send Letter 525, Form 4549, and appropriate attachments, and retain copy of letter and report in the RGS case file.
Case is a single issue information return	Send Letter 525 and Form 4549, and with adjustment and standard explanation(s).
Evaluating Taxpayer Replies/No Replies/Closing Procedures etc.	Refer to IRM 4.19.13, General Case Development and Resolution and IRM 4.19.15.20, Schedule A for guidelines.

4.19.15.20
(10-16-2024)
Schedule A

- (1) For all examined *Schedule A* items, the examiner should check for:

- Altered photocopies of paid bills.
- Bank statements or cancelled checks coinciding with the amount claimed as paid.

Reminder: An altered document is an indicator of fraud, and a fraud referral or civil fraud penalty should be considered. Refer to IRM 4.19.10.4, Fraud Referrals.

- (2) **Medical and Dental Expenses:** The examiner should have the taxpayer send in the following documentation (Form 14808, Schedule A - Medical and Dental Expenses):

- Copies of bank statements or cancelled checks, receipts or statements for all medical savings accounts, medical and dental expenses (including medical insurance) showing the person for whom each expense was incurred, the name and address of each person to whom payment was made, and the amount and date of payment in each case.
- Any insurance or employer reimbursement records, and
- Verification of medical and dental insurance premiums paid.

Note: The Archer Medical Savings Account program expired on December 31, 2007. Some existing Archer MSAs may still be in effect. See IRC 220(i)(1).

- (3) When the requested documentation is received, the examiner should:

- Ensure that insurance reimbursements are excluded from deductions. Ensure medical or dental insurance premiums were not paid pre-tax. Ensure the expenses are for the taxpayer, spouse, dependent, adopted

child, child of divorced or separated parents, or a decedent who, when living, was the taxpayer, spouse, dependent, adopted child, or child of divorced or separated parents.

- Ensure that the medical expenses are for a person.

Exception: Costs of a guide dog or other animal to be used by a visually impaired or hearing impaired person are allowable. Also allowable are expenses to care for an animal trained to assist persons with any other physical disabilities.

Note: Amounts paid for Personal Protective Equipment, (PPE) such as masks, hand sanitizer and sanitizing wipes for the primary purpose of preventing the spread of Coronavirus, are qualified medical expenses.

- If there is a multiple support agreement, the taxpayer may be able to claim medical expenses even if the taxpayer cannot claim that person as a dependent (IRC 152 and IRC 213).
- Refer to Pub 502, Medical and Dental Expenses, for additional information regarding medical and dental expenses you claim on Schedule A.

4.19.15.20.1
(06-14-2023)

(1) This list is not all inclusive.

Nondeductible Medical Expenses

Nondeductible Purchases	Explanation
Baby-sitting, child care, and nursing services for a normal, healthy baby	Personal expenses are not allowable, even if the expenses enable the taxpayer to get medical treatment.
Controlled substances	Purchase of any substance in violation of federal law is not deductible, e.g., marijuana, laetrile, etc. Taxpayers can't include medical expense amounts paid for controlled substances that aren't legal under federal law, even if such substances are legalized by state law.
Cosmetic surgery, electrolysis or hair removal, hair transplant	Medical expenses paid for cosmetic surgery are deductible only if they are necessary to improve a deformity arising from, or directly related to, a congenital abnormality, or a personal injury resulting from an accident, trauma, or a disfiguring disease
Dancing lessons or swimming lessons	Not allowed, even if recommended by a doctor for the improvement of general health. These are deductible only if prescribed for a specific medical condition.
Diaper service	Allowed only if needed to relieve the effects of a particular disease.

Nondeductible Purchases	Explanation
Health club dues	A fee charged by a health club is deductible only if it is a fee for a specific service, such as a fee for a trainer service to treat a particular medical problem.
Household help	Allowed only if paid for nursing-type services. Certain maintenance or personal care services provided for qualified long-term care can be included in medical expenses.
Illegal operations and treatments	Not allowed, even if medically prescribed.
Insurance Premiums	Not deductible if for the following insurance benefits: <ul style="list-style-type: none"> • Payments for loss of life, limb, sight, etc. • Payments for loss of earnings. Guaranteed payment for each day of hospitalization. • Pre-tax insurance premiums.
Maternity clothes	Not allowed.
Medical Savings Accounts (MSA) or Flexible Spending Arrangement	Not allowed. <ul style="list-style-type: none"> • Any expense paid from a medical savings account is not deductible. • The taxpayer cannot deduct medical expenses as itemized deductions that are included in the tax-free amount of a distribution from a Health Savings Account (HSA). If taxpayer has deducted medical expenses or insurance premiums elsewhere on the return, these expenses cannot be used again as a deduction on <i>Schedule A</i>.
Nonprescription drugs and medicines	Not allowed.
Nutritional supplements	Allowed if they are recommended by a medical practitioner as treatment for a specific medical condition diagnosed by a physician. See Publication 502.
Personal use items	Allowed only when an item is purchased in a special form primarily to relieve a physical defect. The excess of the cost of the special form over the cost of the normal form is a medical expense.
Weight-loss program	Allowed only if the program is undertaken to treat an existing disease (such as obesity) diagnosed by a physician.
Funeral Expenses	Not allowed.

4.19.15.20.2
(06-14-2023)
Taxes Paid

- (1) Taxpayers are allowed to deduct certain taxes when they itemize deductions on *Schedule A* (Form 1040). These taxes include:

- State and local income taxes
- General sales taxes
- Real estate taxes
- Personal property taxes

Note: For tax years beginning in 2018 through 2026, the deduction is limited to \$10,000 (\$5,000 for a married individual filing separately. See IRC 164(b)(6).)

- (2) For additional information on deductible taxes refer to IRM 21.6.4.4.1.4, Taxes and Fees –Deductible and Nondeductible and *Instructions for Schedule A (Form 1040), Itemized Deductions*.
- (3) For taxes paid, the examiner should consider having the taxpayer send in the following documentation:

Category	Documentation
For State and Local Income Tax deductions:	<ul style="list-style-type: none"> • Copies of state or local returns for the years involved. • Copies of cancelled checks and receipts for taxes paid during the year. • Form W-2 or other statement showing state and local income tax withheld during the year.
For State Sales Tax Deduction: (Optional sales tax table)	<ul style="list-style-type: none"> • Sales receipts for the year involved if actual state and local general sales taxes are claimed. • Statements from the payer for non-taxable income which includes: tax exempt interest, veterans' benefits, non-taxable combat pay, workers' compensation, non-taxable part of Social Security and Railroad Retirement Benefits. If the taxpayer used the Optional State Sales Tax Table and indicates they had non-taxable income and the non-taxable income was not shown on the return. The General Sales Tax Tables are in the <i>Form 1040 Instructions</i>. • Sales receipts for motor vehicles, mobile and prefabricated homes, or home building materials. The actual sales tax paid on these items can be added to the amount in the Optional State Sales Tax Tables, but only include the amount of tax paid at the general sales tax rate.

Category	Documentation
For State and Local General Sales Tax Deduction: (Actual Expenses)	<ul style="list-style-type: none"> Documentation to support state and local sales taxes paid on a motor vehicle, aircraft, boat, home, or home building materials, if claimed in addition to table amount. This includes purchase contracts and bills of sale. If the taxpayer claimed actual sales taxes, then the taxpayer needs to provide actual sales receipts and support for the purchase of large items. If the receipts are too numerous to photocopy, the taxpayer may provide an itemized list. The list should identify the item purchased, date, total cost, and the amount of sales tax paid.
For Taxes on Qualified Motor Vehicles-State or Local Sales or Excise	<ul style="list-style-type: none"> Documentation to support state and local sales and excise taxes paid on a qualified new motor vehicle, include purchase contracts and bills of sale. <p>Note: This provision expired in 2009. The vehicle must have been purchased before the end of 2009. However, the vehicle sales taxes may still be deducted as a general sales tax if the taxpayer elects to deduct general sales taxes.</p>
For Real Estate and Personal Property Taxes deduction (list is not all inclusive):	<ul style="list-style-type: none"> Verification of legal ownership of the property. Copies of cancelled checks, mortgage statements or receipts for taxes paid. Copy of property tax bill and documentation of any property tax rebates or refunds. Copy of the settlement statement if real property was sold or purchased during the year. Verification of any special assessments deducted as taxes and an explanation for their purpose.

Note: See Form 14810 – Taxes You Paid.

(4) The following is a list of nondeductible taxes (not all inclusive):

- Federal Income and Excise taxes, Social Security Taxes, Federal estate and gift taxes, Federal Unemployment Tax (FUTA), Railroad Retirement Taxes (RRTA), and Medicare.
- Customs duties.
- Tax on gasoline and Car inspection fees.
- Assessments for sidewalks or other improvements to property.
- Tax paid for another taxpayer.
- License fees (marriage, driver's, dog, etc.).

- Penalties or interest.
- Homestead Exemption – this is not a tax but is used to reduce state or local real property taxes for qualified homeowners.
- For tax years beginning after 2017 through 2026, foreign real property taxes.

(5) Taxpayers should not reduce their deduction by:

- Any refund of, or credit for, prior year state and local income taxes received in the tax year of the return.
- Tax refunds from prior year State returns. When the taxpayer has state and local taxes on the prior year Schedule A, it should be reported on the appropriate line of Form 1040. Beginning in tax year 2018 it is reported on *Form 1040 Schedule 1*.
- Refunds of real estate taxes deducted in prior years should be reported on the “Other Income” line of the Form 1040, beginning in tax year 2018 use *Form 1040 Schedule 1*.

(6) Evaluating Taxpayer Responses:

- For 2004 and subsequent tax years, taxpayers can elect to deduct either state and local general sales taxes, or state and local income taxes. The taxpayer cannot deduct both. For tax years beginning in 2018 through 2026, a taxpayer’s total deduction of either type of tax is limited. See IRM 4.19.15.20.2, paragraph 2.
- If the taxpayer deducts state and local income taxes, the taxpayer reports the sales or excise taxes for a new motor vehicle on line 6 of the Schedule A.
- If the taxpayer elects to claim a general sales tax deduction using the general sales tax table amount, the taxpayer can add the sales tax paid for a new motor vehicle to the general sales tax table amount, and report it on line 5(b) of Schedule A.
- Ensure the taxpayer has not duplicated the deductions elsewhere on the return such as on Schedule E or C.
- If taxpayer has a Schedule E, ensure taxes and interest related to that property have not been placed erroneously, double deducted, on Schedule A.
- State and Local Sales Tax Deduction:

If	Then
The state or locality imposes a general sales tax on the sale of a home,	The “closing statement” from the sale of the home should show the amount of sales tax due from the seller.
The state or locality imposes sales tax due to a major/substantial renovation,	The taxpayer should provide a statement from the state or locality for the sales tax paid.
A contractor was authorized by contract to act in the taxpayer’s behalf to build or substantially improve the taxpayer’s home,	The taxpayer should provide a copy of the contract designating the contractor, a statement from the contractor indicating the items purchased and amount of sales tax paid.

If	Then

#

If	Then

#4.19.15.20.3
(06-14-2023)**Home Mortgage Interest Deductions**

- (1) Taxpayers are allowed to deduct mortgage interest paid for their main home and a second home. The deduction is reported on *Schedule A* of the Form 1040 as an itemized deduction. Personal interest, i.e., for credit cards, unsecured loans, car loans, mortgage interest on a third home, and excess mortgage interest is not deductible. Refer to Pub 936, Home Mortgage Interest Deduction for additional information. During examinations, tax examiners will need to determine the correct amount of mortgage interest allowable as a deduction. In some instances, the mortgage interest deduction including deductible points is limited, as discussed below.

Note: See Form 14809, Interest you Paid

- (2) Use IDRS CC IRPTR to search for Form(s) 1098, Mortgage Interest Statement(s), verifying that the taxpayer paid mortgage interest in the year under examination. If there is no data on IRPTR to indicate that mortgage interest was paid by the taxpayer, or if the taxpayer's name is not on Form 1098, or if the transcribed Form(s) 1098 do not verify the amount deducted, the examiner should request copies of:
- mortgage interest statements for the year being examined
 - mortgage or loan contracts
 - equity line of credit agreements
 - amortization schedules for loans outstanding
 - cancelled checks, receipts, or other evidence of payments made for the year under examination

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4.19.15.20.3.1
(12-01-2017)
General Requirements

- (1) **Taxpayer Liable.** There must be a true debtor-creditor relationship between the taxpayer and the lender, and the taxpayer must be legally liable for the loan. If the taxpayer is not liable for the debt, the interest is not deductible. It is not necessary that the taxpayer be the party making the payments, but if the taxpayer is not filing a joint return and is a co-owner with a party other than a spouse, the taxpayer may need to verify the specific amount they paid. (See IRM 4.19.15.20.3.2, Evaluating Taxpayer Responses.)
- (2) **Secured Debt.** The mortgage must be a secured debt, it usually is if reported on Form 1098. Generally, a secured debt is one for which an instrument is signed such as a mortgage, deed of trust, land contract, promissory note, security instrument, or home equity line of credit. The home must be collateral for the interest of the lender; if the loan is not repaid, the lender can foreclose on the mortgage and the home can then serve as payment for the debt.
- (3) **Qualified Home.** The taxpayer’s debt must be secured by a main home or a second home. A home includes a house, condominium, cooperative, mobile home, house trailer, and boat, or similar property that has sleeping, cooking, and toilet facilities. The taxpayer can choose their second home, but special rules apply to rented homes, home offices, and homes under construction. (See Pub 936, Home Mortgage Interest Deduction.)
- (4) **Points** (also known as Loan Origination Fees, Loan Discount, Maximum Loan Charges, or Discount Points) are deductible as interest. Generally, points are deducted ratably over the life of the loan. Points are deductible in full in the year of payment if all of the criteria in the following table are met:

If	AND all of the following are met	Then
The points are paid to acquire a main home in connection with a loan that is secured by that home.	<ul style="list-style-type: none"> a. Paying points is an established business practice in the area and the points were not more than points generally charged in the area, b. The taxpayer uses the cash method of accounting, c. The amount is clearly shown on the settlement statement (reported as points, loan origination fees, loan discount, discount points), d. The points are not paid in place of amounts ordinarily stated separately on the settlement statement for items such as real estate taxes, inspection, appraisal fee, e. The points are calculated as a percentage of the principal loan and, f. The points are paid directly by the taxpayer and not derived from loan proceeds. 	The points are deductible in full for the year paid. However, if mortgage interest is limited then points will also be limited. See Pub 936, Home Mortgage Interest Deduction and IRM 4.19.15.20.3.3, Limits on the Home Mortgage Interest Deduction below.

4.19.15.20.3.2
(02-01-2022)

Evaluating Taxpayer Responses

- (1) The documentation provided by the taxpayer must verify that all of the requirements listed under IRM 4.19.15.20.3.1, General Requirements, are met. Request additional documentation as needed using standard examination procedures.
- (2) The interest must have been paid in the year under examination. The taxpayer may not deduct prepaid interest. However, the allowable portion of interest deferred from a prior year may be deducted in the current year. Accept the amounts shown on Form 1098, Mortgage Interest Statement(s) unless other documentation shows that all or part of the interest was prepaid.
- (3) The taxpayer may deduct interest only on a main home and a second home. If the taxpayer submits mortgage documentation for more than two residences, then the taxpayer must identify the principal residence (as defined under IRC 1.121-1(b)(2) of the Income Tax Regulations) and may select up to one other residence that the taxpayer uses as a residence. See IRC 163(h)(4)(A).
- (4) The only part of the home that is considered a qualified home is the part used for residential living. If part of the home is used for any activity other than residential living, such as a home office, an allocation is required.

- (5) Ensure that the taxpayer did not deduct the same interest on other Schedules such as *Schedule C, E, or F*, or as a Mortgage Interest Credit on Form 8396 in the Tax and Credits section of Form 1040, beginning in tax year 2018 use *Form 1040 Schedule 3* . If there is a duplicate deduction, then the interest should be adjusted to reflect the correct amount. Duplicate Mortgage Interest is worked under PC 0049, Form 886-H-MIE, *Mortgage Interest Expense* is sent with the initial contact letter.
- (6) Taxpayers are allowed to deduct interest paid on a qualifying foreign home if the property and the loan meet the requirements detailed in IRM 4.19.15.20.3.1. Interest paid in foreign currency must be converted to U. S. Dollars. Ask the taxpayer to provide this computation. You will have to calculate the conversion yourself if the taxpayer does not provide one.
- (7) If the taxpayer is deducting mortgage interest and is also a co-owner of a qualified property, then accept the taxpayer’s statement for the amount of interest paid. However, if there is a discrepancy in deductions by co-owners resulting in a combined deduction exceeding the amount of interest actually paid, the taxpayer will need to verify the amount they paid.
- (8) Even if the taxpayer meets all the general requirements for deducting home mortgage interest, their deduction may be limited. Refer to the following sections if:

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- The documentation provided by the taxpayer indicates that the deduction is subject to the limits described in IRM 4.19.15.20.3.3, Limits on the Home Mortgage Interest Deduction, or
- You are processing a Project Code 0417 case for Excess Mortgage Interest Deduction.

4.19.15.20.3.3
(11-04-2019)
**Limits on the Home
Mortgage Interest
Deduction**

- (1) The following table describes when the taxpayer’s home mortgage interest deduction is limited based on the type of mortgage debt as defined in IRC 163(h)(3)(F):

If ...	Then ...
It is Grandfathered Debt , which applies to mortgages taken out on or before October 13, 1987,	Interest paid in that year is fully deduct-ible.

If ...	Then ...
<p>It is Home Acquisition Debt, which applies to mortgages secured by a main or second home. The limit on the amount of debt eligible to be treated as Home Acquisition Debt depends, in part, on when the debt secured the home:</p> <ul style="list-style-type: none"> • If the debt was incurred after October 13, 1987 but before December 16, 2017 to buy, build, or improve the home, but only if throughout the year, these mortgages plus any Grandfathered Debt totaled \$1 million or less (\$500,000 or less if married filing separately) ("Pre-2018 Limits"). • For mortgages secured after December 15, 2017, the limit is \$750,000 (\$375,000 if married filing separately) reduced by: (1) Grandfathered Debt ("2018-2025 Limits"). The dollar limits apply to the combined mortgages on the taxpayer's main home and second home. • Exception: The higher Pre-2018 Limits applies to home acquisition debt that would otherwise be subject to the 2018-2025 Limits, if: (1) the taxpayer entered into a written binding contract before December 15, 2017, to close on the purchase of a home before January 1, 2018, and (2) the taxpayer, in fact, purchased such home before April 1, 2018. If the above conditions are satisfied, the debt is considered to be home acquisition that was incurred prior to December 16, 2017. • Refinanced home acquisition debt qualifies only up to the amount of the home acquisition debt of the old mortgage just before the refinancing. If the refinanced amount is higher than the home acquisition debt, the additional amount may be treated as home acquisition debt if the proceeds were used to build or substantially improve the home. 	<p>Interest paid in that year is fully deductible.</p>

If ...	Then ...
<p>It is Home Equity Debt, which applies to mortgages secured by a main or second home taken out after October 13, 1987, and before January 1, 2018, but only if throughout the year these mortgages totaled \$100,000 or less (\$50,000 or less if married filing separately) and totaled no more than the fair market value of the home reduced by outstanding Grandfathered Debt and Home Acquisition Debt. (See IRM 4.19.15.20.3.4.2, Evaluating Excess Mortgage Interest Taxpayer Responses, for a discussion of fair market value).</p> <p>Note: For tax years 2018 through 2025, interest paid on home equity debt is not deductible. However, home equity debt may be treated as home acquisition debt if it is used to buy, build, or substantially improve the home which secures the debt, but only to the extent that the amount of the home equity debt, along with any other home acquisition debt and grandfathered debt, do not exceed either the Pre-2018 Limits of the 2018-2025 Limits, whichever are applicable.</p> <p>Reminder: For tax years before 2018, in appropriate circumstances, the \$100,000 limit for Home Equity Debt, can be utilized to increase the \$1 million limit for Home Acquisition Debt to \$1.1 million.</p>	<p>Interest paid in that year is fully deductible.</p>
<p>The mortgages do not fit into the above categories,</p>	<p>Interest paid in that year is limited. Refer to Pub 936, Home Mortgage Interest Deduction and IRM 4.19.15.20.3.4, Excess Mortgage Interest Deduction – IRC 163 below.</p>

- (2) In order to compute the limit on the home mortgage interest deduction, where applicable, obtain information on the average outstanding mortgage balance(s) for the year under examination.

Note: Use the highest mortgage balance if it is more beneficial for the taxpayer, but generally the average balance provides the most benefit. This information is only available from taxpayer documents. Refer to IRM 4.19.15.20.3.4, Excessive Mortgage Interest Deduction – IRC 163, for detailed procedures.

4.19.15.20.3.4
(02-01-2022)
**Excess Mortgage
Interest Deduction – IRC
163**

- (1) Home Mortgage Interest reported on *Schedule A* can be limited in some circumstances, therefore the taxpayer cannot deduct the full amount reported on Form 1098. Points count as interest and can also be limited. A tax examiner may receive this issue (home mortgage interest deducted in excess of the allowable limits) because of Discretionary Examination Business Rules (DEBR) Project Code 0417 or because of other *Schedule A* projects.
- (2) If the taxpayer deducted mortgage interest in excess of allowable limits, or if initiating Project Code 0417 cases, the examiner should request copies of the following information:

- a detailed year-end interest statement showing the beginning and ending principal balances or interest rates for each loan on which interest was deducted,
 - Form HUD-1 Settlement Statements, and
 - worksheet(s) used by the taxpayer to compute the mortgage interest deduction limitation.
- (3) Initiate Project Code 0417 cases by sending Letter 566-S /Letter 566-T for TDC cases, with Form 886-H-INT, Limited Home Mortgage Interest Deduction Supporting documents and, Form 14900, Worksheet for Qualified Loan Limit and Deductible Home Mortgage Interest for Tax Years Beginning after 2017.

Note: Additional information can be found in the *Exam Project Code Search Tool*.

4.19.15.20.3.4.1
(11-29-2011)

Computing the Limit on the Mortgage Interest Deduction

- (1) Determine the **Average Mortgage Balance** of each loan for which the taxpayer is claiming a mortgage interest deduction using one of the following:
- Average of the first and last balance method
 - Interest paid divided by the interest rate method
 - Provider statements
- (2) For part year loans, yearly average balance = (number of days loan held) x (average loan balance)/365.
- (3) **Simplified Method** - Determine the allowable mortgage interest deduction using the worksheet in Table 1 of Pub 936, Home Mortgage Interest Deduction. This worksheet uses a simplified method for computing the limit by totaling the average balances of all the qualified mortgages and then determining the percentage of the total mortgage interest which is deductible.
- (4) **Exact Method** - The limit may be computed using an exact method which determines the limit on each qualified mortgage separately, starting with the oldest outstanding mortgage. The taxpayer may have used an exact method when computing the limit on the mortgage interest deduction. Verify the worksheet or formula provided by the taxpayer.
- (5) Apply the limit on deductible mortgage interest to deductible points as well.

4.19.15.20.3.4.2
(11-04-2019)

Evaluating Excess Mortgage Interest - Taxpayer Responses

- (1) The documentation provided by the taxpayer must verify that all of the requirements listed under IRM 4.19.15.20.3.1, General Requirements are met.
- (2) Process responses to the initial contact letter as follows:

If ...	And ...	Then ...
No Reply,	NA	Disallow the entire mortgage interest deduction.
Taxpayer replies with insufficient information to determine average balance of at least one of the mortgages,	NA	Research IRPTR for the required information.

If ...	And ...	Then ...
Taxpayer replies with sufficient information to determine average balance of mortgages,	Worksheet determines the mortgage interest deduction should have been limited,	Issue examination report disallowing the excess mortgage interest deduction.
Taxpayer replies with sufficient information to determine average balance of mortgages,	The mortgage interest deduction is not limited, or the tax reported on the taxpayer's return is substantially correct,	Close the examination using No Change procedures.
Taxpayer used an exact method to determine the allowable mortgage interest deduction,	You are able to verify the taxpayer's computation, or there is substantial agreement between the limit the taxpayer computed and the limit determined using the simplified method,	Close the examination using No Change procedures.

- (3) Observe the following guidelines when determining the extent of an excess mortgage interest deduction:
- If you do not have an Average Balance for a loan, do not use the interest for that loan in the worksheet. There must be information for an average balance on at least one loan in order to complete the worksheet.
 - Accept the taxpayer's explanation for how the loan proceeds were used unless the documentation shows otherwise.
 - If two unmarried taxpayers are deducting mortgage interest on a loan for property jointly owned by them, use the average balance of the entire loan for all parties and multiply the limitation by the amount of interest the taxpayer actually paid (i.e., do not compute the limitation using only one taxpayer's share of the loan). Accept the taxpayer's statement for the amount of interest the taxpayer actually paid, unless it is not consistent with the deduction the other owner is claiming.
 - For tax years before 2018 if the acquisition debt exceeds \$1,000,000, the taxpayer may treat up to \$100,000 of the excess acquisition debt as Home Equity Debt, for an effective limit of \$1,100,000 on the mortgage debt on which interest may be deducted. However, the taxpayer may not treat actual Home Equity Debt in excess of \$100,000 as Home Acquisition Debt.
- Example:** For tax year 2017 if the taxpayer has Home Equity Debt of \$200,000 and Home Acquisition Debt of \$800,000, only the interest on \$900,000 of mortgage debt is deductible – i.e., \$800,000 in Home Acquisition Debt + \$100,000 in Home Equity Debt – even though the total mortgage debt is less than \$1,100,000.
- The taxpayer may be eligible to deduct the limited mortgage interest as an investment interest expense in certain circumstances. If the limited mortgage interest qualifies as investment interest expense, the amount that may be deducted is generally limited to the amount of the taxpayer's net investment income. The taxpayer should use Form 4952, Investment Interest Expense, to figure the deduction for investment interest. Investment interest disallowed for the year under examination may be carried

forward to future years. Refer to Pub 550, Investment Income and Expenses, for information on determining net investment income and limits on investment interest.

- f. The fair market value (FMV) of a home is the price at which the home would change hands between a seller and a buyer, neither having to sell

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4.19.15.21
(02-01-2022)

Charitable Contributions

- (1) Taxpayers may claim an itemized deduction for contributions or gifts made to or for the use of qualified charitable organizations and governments, other than foreign governments. Payments to qualified organizations are contributions if they are made without the taxpayer getting, or expecting to get, anything of equal value.
- (2) For 2020, individuals who do not itemize their deductions may deduct from gross income, up to \$150 (for married filing separately) or up to \$300 (for single, head of household, qualifying widow(er), or married filing jointly) of their qualified cash charitable contributions to public charities, private operating foundations, and federal, state, and local governments. Contributions to establish or maintain a donor advised fund and contributions to supporting organizations do not qualify for this above-the-line deduction. See Pub 526, Charitable Contributions, for additional details on what contributions qualify for the deductions for non-itemizers.
- (3) For 2021, individuals who do not itemize their deductions may deduct from gross income, up to \$300 (for married filing separately, single, head of household, or qualifying widow(er), or up to \$600 (for married filing jointly) of their qualified cash charitable contributions to public charities, private operating foundations, and federal, state, and local governments. Contributions to establish or maintain a donor advised fund and contributions to supporting organizations do not qualify for this above-the-line deduction.
- (4) Contributions of non-cash property and contributions carried forward from prior years do not qualify for a deduction for taxpayers who do not itemize.

4.19.15.21.1
(01-01-2016)

Qualifying Payments

- (1) The following table provides some examples of qualifying and non-qualifying payments.

Qualifying payments	Non-qualifying payments
Out of pocket expenses paid when serving as a volunteer for a qualified organization	Bingo, raffles, lottery tickets
Expenses paid for a student living with you, if the student was placed by a qualified organization	Membership dues or fees paid to country clubs or fraternal lodges

Qualifying payments	Non-qualifying payments
Gifts that are to or for the use of a qualified organization for its religious, charitable, educational, scientific, or literary purposes	Tuition and registration fees, Temporary use of property
Gifts to or for the use of federal, state, and local governments	The value of your volunteer services
Certain automobile and travel expenses incurred when doing volunteer work	Personal living expenses incurred while performing services for a qualified organization
Cost and upkeep of uniforms required when doing volunteer work	Amounts paid for the benefit of an individual selected by the taxpayer
N/A	Under TD 9864, 2019-27 I.R.B. 6., certain donations made in exchange for state or local tax credits or deductions do not qualify for charitable contribution deductions.
N/A	Amounts paid in exchange for college or university athletic event seating rights.

4.19.15.21.2
(06-14-2023)

Qualifying Organizations

- (1) Refer to Pub 526, Charitable Contributions for information related to organizations that qualify to receive deductible contributions.
- (2) If an organization provided by the taxpayer is questionable, verification may be obtained using an on-line search tool for exempt organizations called *Tax Exempt Organization Search (TEOS)*. This site identifies organizations eligible to receive tax-deductible charitable contributions. If a search is unsuccessful, the taxpayer should be able to obtain a copy of the letter issued to the organization by the IRS granting it “qualifying organization” status.
- (3) Qualified and non-qualified organizations can include, but are not limited to:

Qualified Organizations	Non-qualified Organizations
Churches, synagogues and other religious organizations	Civic leagues, sports clubs, labor unions, chambers of commerce
Federal, state and local governments	Most foreign organizations
Organizations organized in the U.S. that are created and operated only for charitable or certain other purposes, public parks and recreation facilities	Lobbying groups
Salvation Army, Red Cross, CARE, Goodwill, Boy Scouts, Girl Scouts, United Way	Individuals, political groups, or specific candidates for public office.
Volunteer fire departments	Any profit group or Homeowner Associations
Nonprofit schools and hospitals	NA

4.19.15.21.3
(06-14-2023)

**Cash and Non-cash
Contributions**

- (1) Contributions can be in the form of cash or non-cash. Examples of the types of contributions are:

Type of Contribution	Example
Cash	Cash, check, money order, credit card, payroll deductions such as for the Combined Federal Campaign (CFC), electronic funds transfers
Non-cash (property)	Clothes, automobiles, household goods, artwork, stock, real estate, conservation easements
Qualified Conservation Contribution (QCC)	A qualified real property interest donated to a qualified organization to be used for conservation purposes.

- (2) Out of pocket expenses incurred when volunteering services were provided by the taxpayer to a qualified organization are deductible. Refer to Pub 526, Charitable Contributions for details.

4.19.15.21.4
(08-04-2017)

**Amount of Contribution
Deduction**

- (1) In general, a taxpayer can deduct the full amount of a properly substantiated cash contribution, subject to percentage limitations.
- (2) If the taxpayer paid the qualified organization more than the fair market value of an item they received in return, such as merchandise or tickets to sporting events, the deduction is limited to the amount in excess of the fair market value.
- (3) For non-cash contributions, the deduction is usually equal to the fair market value of the non-cash contribution on the date of the donation.
- (4) For contributions of clothing and household goods, the items must be in good used condition or better. If an item is not in good used condition or better, then a deduction may be allowed if the amount claimed for the item is more than \$500, and the taxpayer includes a qualified appraisal with their return and a completed Form 8283.
- (5) For contributions of motor vehicles, including an automobile, boat, and airplane, the claimed value of which exceeds \$500, the deduction is generally equal to the lesser of the gross proceeds from the sale of the vehicle, or the vehicle's fair market value on the date of the contribution. See the chart below for specific rules.

If ...	And ...	Then ...
The taxpayer donates a motor vehicle and deducts more than \$500	the qualified organization sells the vehicle without any significant intervening use or material improvement.	the deduction is the smaller of <ol style="list-style-type: none"> the fair market value on the date of the contribution, or the gross proceeds from the sale of the vehicle by the organization. Form 1098-C, Contributions of Motor Vehicles, Boats, and Airplanes, will show the gross proceeds and must be attached to the return.
The deduction for the motor vehicle is more than \$500	the vehicle is to be significantly used, or improved by the organization	in general, the taxpayer can deduct the fair market value of the vehicle on the date of the contribution. Form 1098-C will show if the vehicle is to be significantly used or improved by the organization and must be attached to the return.
The deduction for the motor vehicle is more than \$500	the vehicle is to be given to a needy individual by the organization or sold to a needy individual by the organization for a price much lower than the vehicle's fair market value, in furtherance of the organization's charitable purpose.	in general, the taxpayer may deduct the fair market value of the vehicle on the date of the contribution. Form 1098-C will show if the vehicle is to be transferred to a needy individual.

4.19.15.21.4.1
(06-14-2023)

(1) The following table lists examples of acceptable documentation for charitable contributions.

**Acceptable
Documentation for
Charitable Contributions**

Type of Contribution	Types of Documentation
All cash contributions	Cancelled checks, receipts, verification of electronic funds transfer, bank records, credit card statements or a statement from a qualified charity. The documentation must show the name of the organization, the date, and the amount of the contribution. Refer to IRM 4.19.15.21.4.1, Acceptable Documentation for Charitable Contributions, paragraph (6) and (9) below for additional information about verifying contributions, if there is doubt regarding the authenticity of the statement provided.

Type of Contribution	Types of Documentation
Cash contribution of \$250 or more in a single payment	For each such donation -the taxpayer must obtain an acknowledgement/statement or receipt from the organization showing the date of the contribution, amount of the contribution, a description of any goods or services provided to the taxpayer by the organization, and an estimate of the value of the goods and services received, or if the goods and services provided are solely intangible religious benefits then a statement to that effect. The taxpayer must obtain the statement from the organization by the earlier of the filing of the return or the due date for the filing of the return (including extensions). Refer to IRM 4.19.15.21.4.1, Acceptable Documentation for Charitable Contributions, paragraph (6) and (9) below for additional information about verifying contributions, if there is doubt regarding the authenticity of the statement provided.
Expenses of less than \$250 incurred while volunteering for a charitable organization	Taxpayer's own records, showing the name of the donee, the date that services were performed, the amount of the expense, and the amount of reimbursement received, if any.
Expenses of \$250 or more incurred while volunteering for a charitable organization.	Taxpayer's own records, showing the name of the donee, the date that services were performed, the amount of the expense, and the amount of reimbursement received, if any, and a statement from the organization describing the services provided as well as providing a description of any goods or services provided by the organization in consideration and a good faith estimate of the value of those goods or services, or if the goods and services provided are solely intangible religious benefits then a statement to that effect.
Non-cash contribution less than \$250	A receipt from the charity showing the name of the organization, the date and location of the contribution and a reasonably detailed description of the non-cash contribution. If a receipt was impracticable to obtain (such as clothing left at an unattended Goodwill dropbox), the taxpayer must maintain a reliable written record that includes: <ul style="list-style-type: none"> a. the name and address of the donee, b. the date of the contribution, c. a description of the property, d. the fair market value of the property at the time of the contribution, e. the method using in determining the fair market value, and f. in the case of a contribution of clothing or household items, the condition of that item.
Non-cash contributions of \$250 or more.	Taxpayer must obtain a written statement from the organization. Refer to IRM 4.19.15.21.4.1, Acceptable Documentation for Charitable Contributions paragraphs (6) through (8) below.

Type of Contribution	Types of Documentation
Non-cash contributions over \$500 but not more than \$5,000, and Contributions of certain readily valued property.	Taxpayer must obtain a written statement from the organization showing all the information required for non-cash contributions of \$250 or more. In addition, Form 8283, Noncash Charitable Contribution, Section A, must be completed and attached to the return. See Pub 526 and Pub 561 for a description of the types of readily valued property.
Non-cash contributions over \$5,000, but not more than \$500,000 (other than contributions of certain readily valued property).	The taxpayer must obtain a written statement from the organization showing all the information required for non-cash contributions of \$250 or more. In addition, Form 8283, Section B, must be completed and attached to the return. The taxpayer must also obtain a qualified appraisal. (See Pub 561, Determining the Value of Donated Property).
Non-cash contribution of property over \$500,000 (other than contributions of readily valued property).	Taxpayer must attach a qualified appraisal to return unless contribution meets the readily valued property exception. Form 8283, section B, must also be completed and attached to the return. The taxpayer must obtain a written statement from the organization showing all the information required for non-cash contributions of \$250 or more.
Contributions of motor vehicles, including automobiles, boats and airplanes, whose claimed value is more than \$500 and the deduction is limited to the gross proceeds from the vehicle's sale.	<p>Taxpayer must attach Form 1098-C, Contributions of Motor Vehicles, Boats, and Airplanes, or an equivalent statement from the charitable organization and a completed Form 8283 (Section A) to the taxpayer's return on which the deduction is claimed.</p> <p>Note: See special rule described below for certain contributions on motor vehicles.</p> <p>If the taxpayer does not attach Form 1098-C, the taxpayer must include the vehicle identification number on Line 1, column(b) of Form 8283 Section A.</p>
Special rule for contributions of motor vehicles, including automobiles, boats and airplanes, whose claimed value (a) is more than \$5,000 and (b) whose deduction is not limited to the gross proceeds from its sale.	If the claimed value of the donated motor vehicle is more than \$5,000 and the deduction is not limited to the gross proceeds from its sale, the taxpayer must attach Form 1098-C and obtain a qualified appraisal and attach a completed Form 8283 (Section B) to the return on which the deduction is claimed. If the claimed value of the vehicle is more than \$500,000, the taxpayer also must attach a copy of the qualified appraisal to the return on which the deduction is claimed.
A single item of clothing or a household item, not in good used condition or better, for which a deduction of more than \$500 is claimed.	(1) a written statement from the organization showing all the information required for non-cash contributions of \$250 or more; (2) a completed Form 8283 (Section B); and (3) a copy of a qualified appraisal
Easements in Registered Historic Districts for claimed deductions greater than \$10,000	A \$500 filing fee, a qualified appraisal, photographs of the entire exterior of the building, and a description of all restrictions on the building must be included with the return. See IRC 170(f)(13)(B).

Type of Contribution	Types of Documentation
Qualified Conservation Contribution (QCC)	A statement to show how you determined the Fair Market Value of the property before and after the contribution and the conservation purpose furthered by the contribution. Refer to Pub 561, Determining the value of Donated Property.

- (2) Form 14804, Schedule A - Gifts to Charity.
- (3) Taxpayers can provide information via mail, fax, e-mail or telephone.
- (4) Contributions are deductible only in the year they are made. Checks, receipts and other documentation provided by taxpayers should indicate a contribution made during the tax year in question. See IRM 4.19.15.21.4.2 paragraph 2, for rules allowing the deduction of excess contributions in later tax years.
- (5) Written statements from charitable organizations must be received by the taxpayer on or before the earlier of:
 - the date the return is filed for the year contribution was made, or
 - the due date of the return, including extensions.
- (6) For contribution of cash, acceptable charitable organization statements are bank records, credit card statements, or written receipts from charitable organization and include:
 - Name of the organization
 - Amount of the contribution
 - Date of the contribution
- (7) For all non-cash contributions of \$250 or more each. In addition to the above listed requirements:
 - Description of any property contributed
 - Whether goods or services were provided by the organization in return for the contribution
 - Description and good faith estimate of the value of goods or services, if any, that the organization provided in return for the contribution
 - Statement that goods or services, if any, that organization provided in return for the contribution consisted entirely of intangible religious benefits, if that was the case
- (8) Unless you question the authenticity of the acknowledgement/statement, when above items are present, do not request any additional information from the organization (official letterhead, signature, etc.). See IRM 4.19.15.21.4.1, Acceptable Documentation For Charitable Contributions, paragraph (10) below.
- (9) There may be instances when you question the authenticity of the statement submitted by the taxpayer. In those instances, it is appropriate to request additional documentation to substantiate the contribution has been made. Some examples of circumstances in which to request additional information are when:
 - the amount of the contribution is excessive in comparison to reported income;
 - documents appear altered;

- unreadable receipts and/or statement, or
- the statement or receipts do not include date, amount, or the name of the organization.

Note: Some religious organizations support the concept of tithing or giving 10 percent of one's income. A taxpayer's deduction of 10 percent of income, alone, is not a basis to question documentation without considering other factors.

Note: The workpapers **must be documented** to explain the reasons why additional documentation was requested and reasons that the statement appears questionable.

(10) If you question the authenticity of the acknowledgement/statement:

- Verification can be requested from the organization to ascertain it provided the acknowledgement/statement submitted by the taxpayer. Refer to IRM 4.19.13.10, IRC 7602(c)(1) Third Party Contacts.

(11) Many taxpayers make cash contributions for which they have no bank records, credit card statements or receipts. These contributions are not deductible. Taxpayers must maintain, as a record of a contribution, a bank statement, a canceled check, a scanned image of a canceled check, a credit card statement, an electronic funds transfer receipt, or a written communication from the donee showing the name of the donee organization, the date of the contribution, and the amount of the contribution.

4.19.15.21.4.2
(06-14-2023)
**Limitations on
Contributions**

- (1) For individuals, the limitation that applies to contributions depends upon the type of property donated and the category of the qualified organization donated to.
- (2) The total charitable contribution deduction cannot exceed adjusted gross income. (AGI). If the contributions are subject to more than one of the limits below, include all or part of each contribution in a certain order, carrying over any excess to a subsequent year (if allowed). Refer to Publication 526, Worksheet 2.
- (3) If total contributions for the year are 20% or less of AGI, additional limits do not apply.
- (4) The following table identifies the two types of qualified organizations:

Organization Type	Description	AGI Limitation
50% Organization	Churches, Educational organizations, Hospitals and certain medical research organizations, Private operating foundations. Refer to Pub 526.	50% limit

Organization Type	Description	AGI Limitation
Non 50% Organization	Any qualified organization that is not in the first category.	Limitation depends upon the type of property donated

- (5) The following table lists the deduction limitations for cash contributions made to both organization types and specifies the length of time carryover contributions may be claimed in subsequent years:

Type of Donation	Type of Organization	Deduction limitation	Carryover permitted?
Cash to the organization	50% Organization (Election not to treat donation as a 2021 Qualified cash contribution)	Limited to 60% of AGI.	Yes, up to 5 years.
Cash to the organization	50% Organization (Election to treat as 2021 Qualified Cash Contribution)	Limited to 100% of AGI minus deductions for all other charitable contributions.	Yes, up to 5 years.
Cash to the organization	50% Organization (Elected to treat the donation for Relief Efforts of 2018 & 2019 & 2020 Disasters.) (2018 & 2019 Disaster definition - Declared before 2/19/20 by the President but does not include 2018 wildfires in California)(2020 Non-COVID Disaster – declared before 2/26/21 occurring after 12/27/19 and before 12/28/2020.)	Limited to 100% of AGI minus deductions for all other charitable contributions.	Yes, up to 5 years.

Type of Donation	Type of Organization	Deduction limitation	Carryover permitted?
Cash to the organization	Non 50% Organization	Lesser of 1. 30% of AGI 2. 50% of AGI minus all donations to 50% organizations.	Yes, up to 5 years.
Cash "for the use of" the organization. (Cash is held in a trust for the qualified organization)	50% Organization (elect not to treat it as a 2021 Qualified cash contribution)	Limited to 30% of AGI	Yes, up to 5 years.

- (6) The following table lists the deduction limitations for non-cash contributions made to both organization types and specifies the length of time carryover contributions may be claimed in subsequent years:

Type of Donation	Type of Organization	Deduction limitation	Carryover?
Noncash property	50% Organization	Limited to 50% of your AGI minus your cash contributions subject to the 60% limit.	Yes, up to 5 years.
Non-cash property	Non 50% Organization	Lesser of: 1. 30% of AGI 2. 50% of AGI minus all gifts to 50% organizations.	Yes, up to 5 years.

Type of Donation	Type of Organization	Deduction limitation	Carryover?
Capital gain property (computed using FMV with no reduction for appreciation)	To 50% Organization	Limited to 30% of AGI minus all contributions to 50% organizations that are subject to the 60% and 50% limit. Note: Special Election available to use 50% limit but FMV is reduced by appreciation amount that would be LTCG if property was sold.	Yes, up to 5 years. If 50% election made, a recalculation is needed. Refer to Pub 526.
Capital gain property	Non 50% Organization	Lesser of: 1. 20% of AGI 2. 30% of AGI minus all 30% limit contributions 3. 30% of AGI minus all capital gain contributions subject to 30% limit.	Yes, up to 5 years.
Capital gain property donated "for the use of" the organization. (is held in a trust for the qualified organization)	50% Organization	Limited to 20% of AGI minus your cash contributions subject to the 50% limit.	Yes, up to 5 years.

Type of Donation	Type of Organization	Deduction limitation	Carryover?
Capital gain property donated "for the use of" the organization. (is held in a trust for the qualified organization)	Non 50% Organization	LESSER of: 1. 20% of AGI 2. 30% of AGI minus all 30% limit gifts 3. 30% of AGI minus capital gains gifts subject to 30% limit. 4. 50% of AGI minus all gifts subject to 60%, 50%, and 30% of AGI.	Yes, up to 5 years.
Qualified Conservation contributions, (QCC)	Qualified Organization (Governmental unit or publicly supported charity. See Pub 526 for qualifying criteria.)	Limited to 50% of AGI minus the deductions for all other charitable contributions. (A qualified appraisal must be filed with the return.)	Yes, up to 15 years
Qualified Conservation contributions, (QCC) by a farmer & rancher. (>50% of gross income is from farming)	Qualified Organization (Governmental unit or publicly supported charity. See Pub 526 for qualifying criteria.)	Limited to 100% of AGI minus the deductions for all other charitable contributions. (A qualified appraisal must be filed with the return.)	Yes, up to 15 years

- (7) Appraisal Fees to determine the fair market value of donated property is not deductible as a charitable contribution.
- (8) If the contributions are subject to more than one of the limits, include all or part of each contribution in a certain order, carrying over any excess to a subsequent year (if allowed). Refer to Pub 526, Worksheet 2.

- (9) Contributions carried over are subject to the same percentage limits in the next year. Carryover contributions are deducted after deducting all allowable contributions in each category for the current year. Any unused contribution that has not been deducted by the fifth succeeding year (or fifteenth year if QCC) is lost.

Note: If a taxpayer claims the standard deduction, (does not file a Schedule A) in a tax year where the carryover may have been claimed, the remaining carryover amount is reduced by any amount they could have been claimed during that year.

- (10) Special additional carryover rules exist for computing carryovers when certain circumstances change. (E.g., married in some years but not others, different spouse in different years, filing status changes, NOL years, and claiming the standard deduction in a subsequent year.) Refer to Pub 526 for special rules.
- (11) If a deduction is disallowed for the current year, and the examiner determines that it has been carried forward, the carryforward year should be opened if the carryover deduction is substantial, and the approval of the manager is obtained.

Note: Taxpayers are required to keep records (such as copies of tax returns and worksheets) to verify any carryover deductions.

- (12) Certain non-cash contributions are limited to the taxpayer's adjusted basis in the property. These include contributions such as:
- Contributions of ordinary income property (such as inventory or short-term capital gain property)
 - Contributions of property to charities that are not public charities
 - Contributions of tangible personal property that is not used by the charity in its charitable function (such as property that is sold by the charity)
- (13) Qualified Charitable Distributions, (QCD) are made directly by a trustee of an individual retirement arrangement, (IRA) other than a SEP or SIMPLE IRA, to certain qualified organizations. The total QCD for the year cannot be more than \$100,000 and the taxpayer must have been 70.5 years of age when the distribution was made. A QCD is non-taxable, but the taxpayer cannot claim a charitable contribution deduction for a QCD. See Pub 590-B, Distributions from IRAs.

4.19.15.21.4.3
(10-01-2003)
**Additional Research
Material**

- (1) For additional information on allowable deductions refer to Pub 526, Charitable Contributions, for the tax year you are examining.

4.19.15.21.4.4
(04-26-2016)
**Charitable Contribution
Rules - Project Code
0391, Project Code 0392,
and Project Code 0629**

- (1) Project Code 0391 is Charitable contributions carryover with no prior year *Schedule A*.
- (2) Project Code 0392 is Charitable contributions carryover with prior year contributions of less than 50 percent of AGI.

- (3) Project Code 0629 is Charitable contributions and identifies returns with a deduction for cash contributions. PC 0629 cases are automated for ACE processing.
- (4) The examination of these cases will begin with case selection from the Dependent Database (DDb). The selected returns will have broken one of the contribution business rules indicated above. DDb should also provide *Schedule A*, Line 18 amounts claimed on the taxpayer's prior three tax returns. Each case will be established on AIMS in Source Code 06 with the appropriate Project Code.

4.19.15.21.4.4.1
(02-01-2022)
Initial Contact

- (1) The following table shows the Initial Contact Letter to send to the taxpayer.

Project Code	Issue Letter	Amount to Disallow
PC 0391 PC 0392	Letter 566-S/Letter 566-T for TDC cases and Form 886-A with applicable explanation	<i>Schedule A</i> , Line 13 - Carryover from prior year
PC 0629	Initial Contact Letter 566-S/Letter 566-T and Form 886-A Documents Request	<i>Schedule A</i> , Line 11 - Gifts by Cash or Check.

4.19.15.21.4.4.2
(02-01-2022)
No Response Cases

- (1) Take the following action if the taxpayer has not replied to the most recent letter by the normal purge date.

Latest Letter issued	Action
Letter 566-S/Letter 566-T for TDC cases	Issue Letter 525/Letter 525-T for TDC cases with Form 4549.
Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, and the Form 4549 reflects a deficiency	Follow normal procedures to have Statutory notice issued based on the adjustments shown on Form 4549.

4.19.15.21.4.4.3
(02-01-2022)
**Processing Taxpayer
Replies to Letter
566-S/566-T for TDC
cases**

- (1) The following describes the processing of taxpayer replies to Letter 566-S/ Letter 566-T for TDC cases, for Project Codes 0391, 0392 and 0629 cases:

If	And	Then
The taxpayer responds to Letter 566-S/Letter 566-T for TDC cases	You are able to verify that the taxpayer is entitled to all of the amount as a contribution deduction.	Follow procedures in IRM 4.19.13.30, Campus Closing Actions.
The taxpayer responds to Letter 566-S/Letter 566-T for TDC cases	You are able to verify that the taxpayer is entitled to part of the amount as a contribution deduction.	Issue Letter 525/Letter 525-T for TDC cases, with a Form 4549 and an appropriate explanation to the taxpayer. Follow normal procedure for mail out and suspense.
The taxpayer responds to Letter 566-S/Letter 566-T for TDC cases	You are unable to verify that the taxpayer is entitled to any part of the amount claimed as a contribution deduction.	Issue Letter 525/Letter 525-T for TDC cases, with the Form 4549 and an appropriate explanation to the taxpayer. Follow normal Letter 525/Letter 525-T for TDC cases, procedures for mail out and suspense.
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases, with information they are entitled to an additional deduction for contributions	You are able to verify that the taxpayer is entitled to an additional deduction.	Issue Letter 525/Letter 525-T for TDC cases, with a Form 4549 and an appropriate explanation to the taxpayer. Follow normal Letter 525/Letter 525-T for TDC cases, procedures for mail out and suspense.

4.19.15.21.4.4.4
(02-01-2022)

(1) Take the necessary action to close the case based on the chart below.

Closing Actions

If the Taxpayer	Then
Signs the Form 4549 , reflecting a deficiency or overpayment	Follow normal procedures for Closed Agreed cases.
Does not reply to Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, and Form 4549 reflects an overpayment	Follow normal procedure for Disposal Code 08 closings.
Does not reply to the 90 Day letter	Follow normal procedures for defaulting cases.
Verifies that the contribution is allowable as a carryover deduction	Follow normal procedures for No-Change cases.
Files a Form 1040-X removing the contribution deduction and Accounts Management (AM) assesses the additional tax.	Close the case using Disposal Code 08. In Field 35 of Form 5344, Examination Closing Record show the entire amount of the assessment.

4.19.15.22
(06-14-2023)
**Casualty and Theft
Losses**

- (1) The Taxpayer Certainty and Disaster Tax Relief Act of 2019 included retroactive disaster tax relief for tax year 2018. This relief provides special rules and return procedures for claiming qualified disaster-related personal casualty losses for major disasters declared before February 19, 2020, by the President under section 401 of the Stafford Act and that occurred in 2018 and before December 21, 2019, and continued no later than January 19, 2020. See Publication 547 and the Instructions for Form 4684 for more information.
- (2) Personal casualty losses sustained in tax years 2018, 2019 and 2020 as a result of qualified disaster losses may be claimed on Form 4684.
- (3) A casualty occurs when your property is damaged as a result of a disaster such as a storm, fire, car accident or similar event. A theft occurs when someone steals your property.

Note: For tax years 2018 through 2025, uninsured losses arising from personal casualties, such as primary residence or vacation property destroyed by fire not due to a federally declared disaster are no longer deductible. Theft losses must also be attributable to a federally declared disaster in order to be deductible. See *Tax Relief in Disaster Situations* for date-specific declarations associated with these disasters and for more information.

- (4) The examiner must keep in mind the following:
 - If the taxpayer's property was covered by insurance and the taxpayer fails to file a timely claim for reimbursement, the taxpayer cannot take a deduction.
 - For disaster losses sustained in:

Tax Years	Dollar Requirements for Deduction
2010-2015, & 2018*, and all other years	The amount of each separate casualty or theft loss exceeds \$100 (\$500 for tax year 2009) and the total amount of all losses during the year exceeds 10 percent of the adjusted gross income.
2016, 2017, 2019, and 2020	The net qualified disaster losses for the year exceed \$500. The standard deduction for individuals is also increased by the amount of that particular individual's net qualified disaster losses.

Note: *For tax year 2018, losses attributable to the California wildfires, the deduction limitation is \$500 total. See Pub. L. No. 115-123, Section 20104(b).

- The taxpayer may deduct Nonbusiness casualty or theft losses only to the extent that:

Note: Simple disappearance of money or property (lost or mislaid) is not a theft. See Pub 547 for definitions of casualty and theft as it applies to Form 4684.

Note: See Form 14814, Supportive Documents to Verify Personal Casualty or Theft Loss, Pub 976, Disaster Relief, and Pub 547, Casualties, Disasters, and Thefts for the particular year under audit, to determine special rules for claiming qualified disaster losses.

- (5) In order to deduct a **casualty loss**, the taxpayer must be able to show verification of the following:
- The type of casualty (car accident, fire storm, etc.) and when it occurred.
 - That the loss was a direct result of the casualty.
 - That the taxpayer was the owner of the property, or if it was leased property that the taxpayer was contractually liable to the owner for the damage.
 - The amount of any insurance reimbursement.
 - Whether a claim for reimbursement exists for which there is a reasonable expectation of recovery.
- (6) In order to deduct a **theft loss**, the taxpayer must be able to show verification of the following:
- When the property was discovered missing.
 - The property was stolen.
 - The property belonged to the taxpayer.
 - Whether a claim for reimbursement exists for which there is a reasonable expectation of recovery.
 - The amount of any insurance reimbursement.
- (7) The following situations can result in casualty losses:
- Car accidents.
 - Earthquakes, volcanic eruptions, floods, hurricanes, tornados, and storms.
 - Fires.
 - Government-ordered demolition or relocation of a home that is unsafe to use because of a disaster.
 - Mine cave-ins.
 - Shipwrecks.
 - Sonic booms.
 - Vandalism.
- (8) The following are three types of casualty losses that refer to federally declared disasters:
- **Federal Casualty Loss** is an individual's casualty and theft loss of personal-use property that is attributable to a disaster. The casualty loss must occur in a state receiving a federal disaster declaration.
 - **Disaster Loss** is attributable to a federally declared disaster and that occurs in an area eligible for assistance pursuant to the Presidential declaration. The loss must occur in a county eligible for public and individual assistance (or both). *The loss is not limited to personal-use property. The loss may be claimed for individual business or income-producing property and by corporations, S-Corp and partnerships.* The individual may claim the loss in the preceding tax year.
 - **Qualified Disaster Loss** is an individual's casualty or theft loss or personal-use property that is attributable to a major disaster declared by

the President under Section 401 of the Stafford Act. For special rules, date specific declarations and expanded return procedures, see *Form 4684 Instructions*, Pub 976, Disaster Relief, or Pub 547.

- (9) Considerations when taxpayer qualifies for a **Federally Declared** Disaster Loss:

- A Federally Declared Disaster is a disaster that occurred in an area designated by the President to be eligible for federal assistance under the Robert T. Stafford Disaster Relief and Emergency Assistance Act. This includes a major disaster or an emergency declaration under the Act. If the casualty loss is attributable to a federally declared disaster and is sustained in a federally declared disaster area, the taxpayer can elect to deduct the disaster loss for the preceding year. Ensure that the taxpayer is not claiming the same loss for both years.
- The taxpayer must reduce the casualty loss by funds received under any disaster provision and by any insurance reimbursement.

- (10) Refer to Pub 584, Casualty, Disaster and Theft Loss Workbook for information related to the computation for personal-use property.

4.19.15.23
(06-14-2023)
**Employee Business
Expense (EBE) Cases**

- (1) These are cases with Form 2106, Employee Business Expenses, expenses included in *Schedule A* Miscellaneous Deductions, and the miscellaneous deductions do not appear consistent with the taxpayer's occupation or income. For any taxable year beginning after December 31, 2017, and before January 1, 2026, Form 2106 is for use by employees who are (1) Armed Forces reservists, (2) qualified performing artists, (3) fee-basis state or local government officials, or (4) employees with impairment-related work expenses. Due to the suspension of miscellaneous itemized deductions subject to the 2% floor under section 67(a), employees who do not fit into one of the listed categories may not use Form 2106. Because the Form 2106 and many lines on the 1040 *Schedule A* are not transcribed, you may see a combination of employee business expenses and miscellaneous expenses.
- (2) Returns may be requested for this issue.
- a. Returns will be reviewed to determine if expenses appear in line with the occupation on the Form 2106.
 - b. Returns will be classified for other issues.
- (3) Initial Contact Letter 566-S/Letter 566-T for TDC cases (ICL), Form 13825, Employee Business Expense Questionnaire, and Form 886-I, Employee Business Expenses, explains the substantiation required to support the employee business expense, and will be issued to the taxpayer.
- (4) Follow normal suspense time frames. If there is no response to the ICL, issue a report disallowing the entire employee business expense amount and other questioned miscellaneous expenses.

Note: The Tax Cuts and Jobs Act of 2017 (TCJA) removed the ability to deduct the cost of using your car as an employee due to the suspension of miscellaneous itemized deductions that are subject to the 2 percent floor under section 67. The suspension applies to tax years beginning after December 2017 and before January 2026. Deductions for expenses that are deductible

in determining adjusted gross income are not suspended (Form 1040, *Schedule 1*, line 24). Refer to Project Code 1520 in the Exam Project Code search tool for additional details.

Note: A fee-based government official is compensated by collecting fees for their services, rather than being paid a salary or wages. Under IRC 62(a)(2)(C), a “fee-based” public official is an official who receives (and retains) fees directly from members of the public as compensation for services provided. For example, a state-court judge, who is paid for performing a marriage ceremony directly by the persons being married, would be considered a fee-based employee. See *Jones v. Commissioner* 146 T.C. 39 (2016). When a public official receives payment for services from government funds in the form of wages or a salary, and no portion of any monies collected by them belongs to, or can be retained by them as compensation, that remuneration is not considered to be a fee.

4.19.15.23.1
(02-01-2022)
**Evaluating EBE
Taxpayer Responses**

- (1) TCJA removed the ability to deduct entertainment, amusement or recreational expenses paid or incurred after December 31, 2017. Business meal expenses remain deductible, generally subject to the 50 percent disallowance. The deductibility of entertainment expenses in the remainder of this subsection only applies to entertainment expenses paid or incurred prior to January 1, 2018.

Note: Amounts paid or incurred after December 31, 2020, and before January 1, 2023, for food or beverages provided by a restaurant are 100% deductible. For more information, see Notice 2021-25.

- (2) All responses need to be evaluated using good judgment and consideration of what is known about the occupation.
- (3) The reimbursement policy of the employer is the starting point for all EBE audits and MUST be secured.
- (4) Employees and self-employed individuals claiming un-reimbursed travel expenses may claim the government per diem rate for the meals and incidental expenses (M&IE) portion of travel expenses, provided they have supported the travel. However, employees and self-employed individuals claiming un-reimbursed lodging expenses must provide receipts for lodging expenses and may not use the government per diem rates for lodging expenses.
- (5) An expenditure for travel, meals, or entertainment, to the extent it is lavish or extravagant, shall not be allowable as a deduction.
- (6) Unless the taxpayer is eligible to use and does use the government per diem rates, documentary evidence is required for:
 - a. Any expense for lodging while traveling away from home, and
 - b. Any other expenditure of \$75 or more.
- (7) IRC 274(d) provides that no deduction shall be allowed for entertainment, gifts, listed property or travel unless the taxpayer substantiates the following elements of the expenditures:
 - a. Amount of each expenditure.
 - b. Time and place of the travel. (Prior to January 1, 2018, entertainment, amusement, recreation, or use of the facility or property.)

- c. Date and description of the gift.
 - d. Business purpose for each expenditure.
 - e. Business relationship to the taxpayer of each person receiving the benefit.
- (8) Many expenses not listed in (5) above can be summarized or aggregated. See Pub 463, Travel, Gift, and Car Expenses, Section 5, Record Keeping, for a table that shows the substantiation requirement for specific expenses.
 - (9) The deduction for business-related meal and entertainment expenses are generally subject to a 50 percent limit or 80 percent if taxpayer is subject to the Department of Transportation's "hours of service" limits. Caution: See Notice 2021-25 pertaining to food or beverage provided by a restaurant.
 - (10) Travel expenses are deductible when taxpayers are temporarily away from their tax home. However, an indefinite assignment to another location is a change in tax home, thus travel expenses are not deductible.
 - (11) Travel expenses for conventions, seminars, and similar meetings are deductible under IRC 162 if the taxpayer's attendance benefits or advances the taxpayer's trade or business. No deduction is allowable if a taxpayer is attending for social, political, or other purposes not related to the taxpayer's trade or business.
 - (12) IRC 274(c)(1) states foreign travel must first be deductible under IRC 162 or IRC 212. The travel must be ordinary and necessary in the pursuit of a trade or business, or for the production of income. If the expense meets those requirements, then the business portion of the travel is deductible.
 - (13) Travel outside of the United States generally must be allocated between business and personal. IRC 274(c)(2) provides two exceptions to the rule that travel expenses be allocated between business and personal. No allocation is made if foreign travel does not exceed one week, or if less than 25 percent of the trip is personal, then travel to and from the business destination is allowed in full.
 - (14) Any issues beyond the expertise of the examiner assigned the case should be referred to the lead examiner to secure the appropriate technical guidance.
 - (15) It is not necessary to fully allow or disallow any expenses. Expenses can be partially allowed when revising the report. Special care should be taken to explain these revisions to the taxpayer.
 - (16) Additional Items to consider. Consider the following points when processing EBE cases.

Employee Business Expense Auditing Techniques
a - When examining employee business expenses, you must consider whether the employer has an expense allowance or reimbursement plan.
b - You must be able to determine if the plan is accountable or non-accountable. When examining expenses you believe are under a non-accountable plan (See Chapter 6 of Pub 463, Travel, Gift, and Car Expenses), you may encounter nondeductible expenses that were reimbursed.

Employee Business Expense Auditing Techniques
c - Always request a written statement explaining the requirements of the expense allowance or reimbursement plan from the employer. The written statement can be an excerpt from the employee handbook or a statement prepared for the purpose of the examination.
d - If the statement is prepared for the purpose of examination, be sure the author has sufficient knowledge of the expense allowance or reimbursement plan.
e - If the statement presented from the employer is vague, discuss with your manager or lead about the possibility of making a third party contact.
f - Be logical in organizing the examination. It may be better to structure the examination of these expenses into categories i.e., travel, entertainment, business meals, listed property, gifts, than by time periods (all of May's expenses or July's expenses). Examining by topic will allow you to see inconsistencies in the taxpayer's records. It will also allow you to determine the credibility of the taxpayer's record keeping.
g - Look for recurring names for entertainment and business meals, as well as recurring locations for travel. Recurring names may indicate a family member or a friend.
h - Be mindful of travel dates. Are the dates during holiday periods? If travel dates are during holiday seasons, this may indicate personal expenses.
i - Does the taxpayer use a travel agent on some occasions and not at other times? If they use a travel agent regularly, this may be a source of documentation. A travel agent may or may not be used by their company. Do they use more than one travel agent? Most companies use one travel agent; if there are two or more, there may be some personal expenses intermingled with valid business travel.
j - Hotel receipts will often show how many people stayed in a room. If friends or family were staying with the taxpayer while they were away from home, you must determine if there was a business purpose for their stay and what, if any, additional charges were incurred.
k - Airline tickets and travel agency statements will show departure dates and who actually traveled. Compare the dates of the business meetings with the actual length of the trip. You could discover that the taxpayer extended their stay for a personal vacation. Request a detailed itinerary.
l - For employees on "accountable" plans, evaluate any reimbursement records. In most cases, the expenses reimbursed by the employer should be accepted up to the amount of reimbursement on face value since it is assumed that they were incurred for a business purpose. However, look to see if any changes were made to the employee's compensation structure (i.e., where the employee's wages reduced by the amount of the "reimbursement") to determine if the purported reimbursements were merely re-characterized wages. Special attention should be paid when they exceed the reimbursement policy. This may also be used to establish the business portion of the use of an automobile where the employee is taking an actual expense deduction vs. a mileage deduction.
m - Be alert for altered documents. Look for erasures of dates, times, places or amounts. Look for possible consecutive numbered receipts, especially for high entertainment costs.
n - Taxpayer should provide documentary evidence along with account book, diary and log to support each element of an expense.
o - A cancelled check by itself doesn't prove a business expense without other evidence to show that it was for a business purpose.
p - To verify total miles for the year, the taxpayer should provide repair receipts, inspection slips or any other records showing total mileage at the beginning of the year as well as at the end of the year.

- (17) The employer's letter regarding the company's reimbursement policy helps to establish:

- a. the business expenses were ordinary and necessary, and
- b. the taxpayer is deducting a legitimate "out of pocket" expense.

Note: If the taxpayer does not provide the employer's letter regarding the reimbursement policy, the expenses should be disallowed.

Note: *There may be instances when the taxpayer is unable to provide an employer's reimbursement policy letter because the employer is out of business, or in receivership. In these instances, if the taxpayer has provided enough corroborating information which shows the expenses are: a) ordinary and necessary, and b) the taxpayer is "out of pocket" for the expenses, then allow the verified expenses.*

4.19.15.23.2
(02-01-2022)
Additional Information

- (1) Additional EBE information and materials should be referenced when processing EBE cases. These include:
- Pub 463, Travel, Gift, and Car Expenses.
 - Training courses available: Training Doc 55421-102, CET Basic Income Tax Law, Standard and Itemized Deductions.
 - Pub 529, Miscellaneous Deductions.
 - Pub 17, Your Federal Income Tax (For Individuals).
 - Treasury Regulation 1.274-5T(c)(6)(i)(B) (Aggregation of Expenditures)
 - Treasury Regulations. 1.274-11,12 (Sporting Events).

4.19.15.24
(06-14-2023)
**Miscellaneous
Deductions - IRC 67**

- (1) The examiner should have the taxpayer send in the following documentation:
- Copies of cancelled checks and paid bills of the expenses claimed.
 - A complete explanation of the purpose of the expense.
 - Form 14983, Schedule A - Other Miscellaneous Deductions.
 - Form 886-I, Employees Business Expense Explanation of Items.
 - Form 13825, Employee Business Expense Questionnaire.
- (2) For taxable years 2018 through 2025, miscellaneous deductions subject to the 2 percent AGI limitation are suspended. See IRC 67(g).
- (3) The table below lists deductions subject to the two-percent AGI limitation, deductions not subject to the two-percent AGI limitation, and nondeductible expenses, for tax years prior to January 1, 2018.

Deductions Subject to the Two-percent of AGI Limitation	Deductions Not Subject to the Two-percent of AGI limitation	Nondeductible Expenses
<p>Unreimbursed employee expenses (Line 21 of Schedule A): Deductible unreimbursed employee expenses must be ordinary and necessary expenses paid or incurred during the tax year in carrying on a trade of business of being an employee.</p>	<p>Deductible expenses not subject to the two-percent of AGI limitation are:</p> <ul style="list-style-type: none"> • Amortizable premium on taxable bonds. • Casualty and theft losses from income-producing property. <p>See Pub 17, for an all-inclusive list of expenses.</p>	<p>Examples of nondeductible expenses are:</p> <ul style="list-style-type: none"> • Broker's commissions to buy investment property or to sell securities • Burial or funeral expenses • Campaign expenses • Capital expenses • Check writing fees • Club dues • Commuting expenses. If the taxpayer hauls tools, instruments, or other items in an auto to and from work, the taxpayer can deduct only the additional cost of hauling the items (such as the rent for a trailer to carry the items).

Deductions Subject to the Two-percent of AGI Limitation	Deductions Not Subject to the Two-percent of AGI limitation	Nondeductible Expenses
<p>Examples are:</p> <ul style="list-style-type: none"> • Business bad debt of an employee. • Expense of education that is work related if the education is not necessary to meet minimum requirements to qualify the taxpayer in the taxpayer's trade or business, and does not qualify the taxpayer for a new trade or business, and 1) it maintains or improves skills required in the taxpayer's present work, or 2) it is required by the employer or the law to keep the taxpayer's current salary, status, or job, and the requirement serves a business purpose of the employer. • Legal fees related to your job. • Licenses and regulatory fees. • Malpractice insurance premiums. • Medical examinations required by employer. • Occupational taxes. • Passport for a business trip. • Work-related subscriptions to professional journals and trade magazines. • Work-related travel, transportation, and entertainment. • Business liability Insurance premiums. • Damages paid to a former employer for breach of an employment contract. • Depreciation on computers if for the convenience of employer and required as a condition of employment. • Dues to a chamber of commerce and professional societies. • Educator expenses over the limit on the amount that may be taken as an adjustment to gross income. • Job search expenses for a job in the taxpayer's present occupation. • Repayment of income aid payment under an employer's plan. • Research expenses of a college professor directly related to your teaching duties. • Tools used in the taxpayer's work. • Union dues and expenses. • Work clothes and uniforms if required and not suitable for everyday use. 	<ul style="list-style-type: none"> • Impairment-related work expenses of persons with disabilities. • Losses from other activities from Schedule K-1, box 2 • Repayments of more than \$3,000 under a claim of right. • Unrecovered investment in an annuity. • Losses from Ponzi-type investment schemes <p>Note: See Pub 17, for an all-inclusive list of expenses.</p>	<ul style="list-style-type: none"> • Fees and licenses such as car or marriage licenses and dog tags. • Fines or penalties. • Health Spa expenses. • Hobby losses • Home repairs, insurance, and rent. • Home security system. • Illegal bribes and kickbacks. • Investment-related seminars. • Life insurance premiums. • Lobbying Expenses. • Losses from the sale of your personal home, personal furniture, or personal car. • Lost or mislaid items. • Lunches with coworkers • Meals while working late. • Personal disability insurance premiums. • Personal legal expenses. • Personal, living or family expenses. • Political contributions. • Professional accreditation fees. • Professional reputation. • Relief fund contributions. • Residential telephone service. • Stockholders meetings. • Tax-exempt income expenses. • Education expenses of a dependent (but see Education Tax Benefits). • The value of wages never received or lost vacation time. • Adoption expenses, also see Adoption Credit. • Personal accounts. • Travel expenses for another individual. • Voluntary unemployment benefit contributions. • Cost of a wristwatch.

Deductions Subject to the Two-percent of AGI Limitation	Deductions Not Subject to the Two-percent of AGI limitation	Nondeductible Expenses
<p>Other expenses (Line 23 of Schedule A). A taxpayer can deduct certain other expenses as miscellaneous itemized deductions subject to the two-percent of AGI limitation. These other expenses are:</p> <ol style="list-style-type: none"> 1. expenses to produce or collect income that must be included in the taxpayer's gross income, 2. expenses to manage, conserve or maintain property for producing gross income, and 3. expenses to determine, contest, pay, or claim a refund of tax. The expenses in (1) and (2) must be reasonable and closely related to these purposes. <p>Examples are:</p> <ul style="list-style-type: none"> • Appraisal fees for a casualty loss or charitable contribution. • Clerical help and office rent to manage investments. • Depreciation on home computer. • Excess deductions allowed a beneficiary on termination of an estate or trust. • Fees to collect interest and dividends. • Hobby expenses limited, in part, by hobby income. • Indirect deductions from pass-through entities. • Investment fees and expenses. • Legal expenses to produce or collect taxable income or to obtain tax advice. • Repayments of \$3,000 or less when the amount was included in income in the earlier year. • Repayments of social security benefits included in income in an earlier year. • Safe Deposit Box rent, but not for storing personal effects or tax-exempt securities. • Service charges on dividend reinvestment plans. • Trustee's administrative fees for IRA. 	<ul style="list-style-type: none"> • Impairment-related work expenses of persons with disabilities. • Losses from other activities from Schedule K-1, box 2 • Repayments of more than \$3,000 under a claim of right. • Unrecovered investment in an annuity. • Losses from Ponzi-type investment schemes • Tax preparation Fees are placed on Line 22 of Schedule A. 	<ul style="list-style-type: none"> • Fees and licenses such as car or marriage licenses and dog tags. • Fines or penalties. • Health Spa expenses. • Hobby losses. • Home repairs, insurance, and rent. • Home security system. • Illegal bribes and kickbacks. • Investment related seminars. • Life insurance premiums. • Lobbying Expenses. • Losses from the sale of your personal home, personal furniture, or personal car. • Lost or mislaid items. • Lunches with coworkers. • Meals while working late. • Personal disability insurance premiums. • Personal legal expenses. • Personal, living or family expenses. • Political contributions. • Professional accreditation fees. • Professional reputation. • Relief fund contributions. • Residential telephone service. • Stockholders meetings. • Tax-exempt income expenses. • Education expenses of a dependent (but see Education Tax Benefits). • Value of loss of wages. • Adoption expenses, but see Adoption Credit. • Personal accounts. • Travel expenses for another individual. • Voluntary unemployment benefit contributions. • Cost of a wristwatch.

4.19.15.25
(11-04-2019)
**Return Preparer
Referrals**

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4.19.15.25.1
(11-04-2019)
**Role of the Exam RPP
Coordinator**

- (1) The Exam RPP Coordinator at each site will be the liaison between Campus Exam and HQ and will elevate any issues for resolution. RPP Coordinator can be any individual (manager, lead, TCO, P&A, TE) as designated by management.
- (2) RPP Coordinator's primary role is to provide technical assistance to Correspondence Exam in processing these cases.

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4.19.15.25.2
(06-14-2023)
**Referral Process and
AIMS Opening**

- (1) Cases will be opened on AIMS by SB/SE HQ Campus Workload Identification (CWI) team and controlled under Project Code 0133, Source Code 70. Any scheme that is related to EITC will be controlled under Project Code 0132. The AIMS will reflect the respective PBC for each site and an Employee Group Code (EGC) of 5000.
- (2) AIMS Tracking Codes may be assigned to identify the scheme.
- (3) Returns will be electronically forwarded and established through RGS.

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4.19.15.25.3

(11-04-2019)

Controlling RPP Returns#

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4.19.15.25.4

(02-01-2022)

**Procedures for
Examining RPP Cases**

- (1) Normal Exam procedures will apply to processing these cases.

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- (4) Consult the RPP Coordinator, Classification TCO (Tax Compliance Officer) or manager and notate workpapers about the additional issues included in the audit.

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- (3) The examiners are required to familiarize themselves with *Schedule A* See IRM 4.19.15.20, Schedule A. This IRM subsection will provide information related to the allowable and unallowable deductions on the Schedule A.

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4.19.15.25.6

(11-04-2019)

**Examining the Schedule
C on Preparer Referrals**#

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4.19.15.26

(02-01-2022)

**Correspondence Exam
Tip Program**

- (1) Cases worked in the Tip Program are initiated based on information received from Area Offices. Revenue Agents (RAs) and/or Revenue Officer Examiners (ROEs) gather data from the employers of tipped employees and use this information to determine each employee's correct tip income. If the employee did not report the correct amount of tips, Correspondence Exam will issue a report reflecting the increase in income tax and FICA taxes (which includes Social Security and Medicare) based on the unreported tip income. All other unreported income as identified on IRPTR should be addressed and included on the examination report per normal procedures.
- (2) The following conditions will apply:
- The inventory will also include cases where the tipped employee has not filed a return.
 - In all cases, normal non-ACE case processing procedures will be used.
 - Penalties will be asserted as required or deemed appropriate. Refer to IRM 20.1, Penalty Handbook, and IRM 4.19.13.7.1.1, Supervisory Approval of Bans.
 - The terms "taxpayer" and "employee" are used interchangeably in this subsection.
 - All correspondence to the taxpayer should contain the name and telephone number of the examiner who prepared the report.
 - If a taxpayer has reached the wage base limit for Social Security wages, they are still subject to Medicare tax on all wages (including tips) received. There is no wage base limit for Medicare wages.
 - All forms that are specific to the Tip Program and are not currently available through Report Generation Software (RGS) will be loaded onto workstations and attached to the taxpayer's file. These forms include

Form 14980, Employee Tip Examinations Worksheet, Form 14980-C, For Information Purpose Only, and Form 14980-A, Unreported Tip Income. If the examination is based on the percentage of gross sales method, Form 14980-B, Computation of Tip Income, Using McQuatter’s Formula, should be used to demonstrate how the unreported tip income was computed using the McQuatter’s Formula. Form 14980-B, should be used for other Tipping Industries such as Food and Beverage cases, and Form 14980-A, Explanation of Tip Income, should be used for Gaming cases.

- (3) The program will consist of the following types of cases:
- Tipped employees who do not participate in a tip agreement and have unreported tip income.
 - Tipped employees who do not participate in a tip agreement and are non-filers.
 - Tipped employees who participate in a tip agreement (GITCA/TRDA) and are non-filers.

Note: Gaming Industry cases will be assigned Project Code 0360 if they are from Casino’s other than Indian Tribal Casinos. If they are from Indian Tribal Casinos, they will be assigned Project Code 0916, Cosmetology Industry cases will be assigned Project Code 0672, and Food and Beverage Industry cases will be assigned Project Code 0364. Non-filer cases will be assigned the same Project Codes; however, Source Code 24 is used to identify these cases.

- (4) Original returns will not be ordered. RTVUE will be used unless it is necessary to review the original return during audit. If the taxpayer filed a Form 4137, Social Security and Medicare Tax on Unreported Tip Income, with their individual income tax return, follow the instructions in the table below to determine the unreported tip income. On joint returns where both taxpayers are tip earners and have unreported tips, make a separate calculation for each taxpayer.

If	And	Then
The payer on the Employee Data Report matches a payer on IRPTR	That employer is the only one on IRPTR where the taxpayer would have received tip income	Consider the amount of tip income reported on Form 4137 when determining the unreported tip income.

If	And	Then
The payer on the Employee Data Report matches a payer on IRPTR	There is more than one employer on IRPTR where the taxpayer would have received tip income	Consider the amount of tip income reported on Form 4137 when determining the unreported tip income. Note: Instruct the taxpayer to provide a copy of Form 4137 and a breakdown on tips reported for each employer with the response to the letter if the Form 4137 was incomplete because it did not identify the employers and the tips reported for each employer.
It cannot be determined that the employer on Form 4137 is the same employer on the Employee Data Report	There is one or more than one employer on IRPTR where the taxpayer would have received tip income	When determining the unreported tip income for each employer, do a pro-rata allocation of the tip income reported on Form 4137 and apply the ratios to each employer.

(5) The Tip Extension database will contain the following:

a. Employees Participating in a Tip Agreement(GITCA/TRDA):

Conditions for Participating Employees
On joint returns where both taxpayers are tipped employees and their participant status is different, an Employee Data Report will only be generated for the employee who has unreported tip income regardless of participation status.
For taxpayers who worked for several employers and had different participation statuses with each employer, an Employee Data Report will only be generated for employers where the taxpayer under-reported tip income.
If the tipped employee is shown as participating but has reported tip income less than the amount on the agreement, the taxpayer will be treated as a non-participant.

b. Primary and Secondary SSNs will be identified.
c. Amounts reported on Form 4137 will be identified.

- (6) The Forms 14439 prepared by the field agents for the Food and Beverage Industry are computed by establishing a tip rate based on both charged and cash sales and assigned to each employee based on position and hours worked. A stiff factor and a tip out rate may also be factored into the computation.
- (7) Tip extension reports are no longer provided. These cases are delivered on Form 14439 , Employee Data Report. Forms 14439 will contain the percent of

gross sales or an hourly rate, the venue, the position, hours worked, and shift. This information will be loaded onto the Form 14980, Employee Tip Income Examinations Worksheet, which will then be used as the allocation sheet.

- (8) Form 4137, Social Security and Medicare tax on Unreported Tip Income, is used by an employee to compute the social security and Medicare tax owed on tips not reported to the employer. Unreported tip income, reported on Form 4137, is carried over to Form 8959, Additional Medicare Tax, which is used by an employee to compute Additional Medicare Tax owed on tips not reported to the employer.
- (9) Additional Medicare Tax. A 0.9 percent Additional Medicare Tax (under IRC 1401(b)(2)(B)) applies to Medicare wages, Railroad Retirement Tax Act (RRTA) compensation, and self-employment income that are more than:
 - \$125,000 if married filing separately,
 - \$250,000 if married filing jointly, or
 - \$200,000 for any other filing status .
- (10) Tips are subject to Additional Medicare Tax, if, in combination with other wages and self-employment income, they exceed the individual's applicable threshold. RRTA compensation and tips are separately compared to the threshold.

4.19.15.26.1
(10-16-2024)

- (1) The following table lists terms used in the Tip Income Program:

Commonly Used Terms

Term	Definition/Description
(1) Tip Agreement	<p>Voluntary agreement between an employer (of tipped employees) and the IRS.</p> <p>Note: There are various tip agreements between the IRS and the employer where employees and employers work together to improve tip reporting compliance. Under a TRDA or GITCA, the employer must secure written statements from at least 75 percent of its employees stating they agree to participate in either the TRDA or GITCA. There are 4 types of tip compliance agreements:</p> <ul style="list-style-type: none"> • TRAC - Tip Reporting Alternative Commitment • TRDA - Tip Rate Determination Agreement • EmTRAC - Employer-designed TRAC • GITCA - Gaming Industry Tip Compliance Agreement
(2) Participating Employee	A tipped employee who states in writing that they will report to their employer no less than the amount of tip income for their job classification, etc., as set forth in the Tip Agreement. This only applies to either a TRDA or GITCA. A Participating employee in a GITCA or TRDA who is compliant with the terms of their agreement will receive tip audit protection.
(3) Non-participating Employee	A tipped employee who is not reporting tips at the rate specified in the employer's tip agreement and who declines to participate in the employer's tip agreement because they choose to instead report actual tips received to their employer.

Term	Definition/Description
(4) Venue	Location where employee works, (i.e., Sunrise Cafe, Pool, Salon or Slots).
(5) Job Classification/Position	Employee's job title i.e., food, server, maitre d', bellman, bartender, colorist, nail technician etc.
(6) Tip rate for all 1040 referrals	<p>Amount of tip income per hour, shift, drink, car, etc., that is assigned to each employee, based on their job classification and venue.</p> <ul style="list-style-type: none"> • The examiner reviews the information provided by the employer and determines this amount. • These rates may be related to a general tip examination or for non-participants associated with a tip agreement. • The tip rate is multiplied by the number of hours, etc., the employee worked to determine the minimum amount of tip income the employee should have reported as income to their employer.
(7) Reported Tips	The amount of tip income an employee reports to the employer is included on their Form W-2.
(8) Unreported Tips	In the case of a Non-participating employee, Unreported Tips are the difference between the Reported Tips and the amount of tips determined based on the Tip Rate for 1040 Referrals. Additional tip income is shown on the employee's Form W-2.
(9) Allocated Tips	<p>Large food or beverage employees may be subject to tip allocation if the employee reports tips to their employer at a rate less than 8 percent of the employee's tipped sales. Allocated tips are included in box 8 of the employee's Form W-2 and must be included on the employee's tax return and Form 4137 unless the employee has adequate records to show that they received less tips in the year than the allocated amount. If an employee does not include the allocated tips on Form 4137, the allocated tips should not be considered in a tip exam. If an employee asserts that the allocated tips are already accounted for in their Form 1040, ask the employee to show where the tips were included for income tax and social security tax purposes.</p> <p>Note: Refer to Pub 531, Reporting Tip Income. If an employee's Form W-2 shows allocated tips, the employee is required to report the allocated tips on Form 4137, unless the employee has adequate records to show that the employee received less tips in the year than the allocated amount (see page 6 of Pub 531).</p>

Term	Definition/Description
(10) Form 4137	Form 4137, Social Security and Medicare Tax on Unreported Tip Income is used by the employee to report tip income (and the related FICA/Medicare taxes) not reported to their employer(s) during the year. Note: This includes any allocated tips shown in box 8 of their Form(s) W-2. Use Form 4137 to figure the social security and Medicare tax owed on those tips.
(11) Employee Data Report	Information from the Employee Data Report for each selected employee. Includes: <ul style="list-style-type: none"> • Employer's name • Employee's position • Shift • Hours worked • Tips reported • Tip rate This information is used to determine the amount of unreported tip income. The report also indicates if they are the Primary or Secondary taxpayer and whether they are a participating employee.
(12) Form 2504	Form 2504, Agreement to Assessment and Collection of Additional Tax, provides the adjustment to the employee's share of FICA and Medicare taxes and the related penalties. This form is generated in RGS.
(13) Form 14980-C	Form 14980-C, FICA Tax and Penalty, provides details of the computations for the taxes and penalties on Form 2504 .
(14) Form 14980 Tracking Sheet	Note: The examiner/clerk will photocopy the Form 14980, Employee tip Examination Worksheet, from the closing file and indicate the disposal code on the form. This form will be mailed to the tip program coordinator/analyst.
Form 8959	This form is used to compute and report Additional Medicare Tax on tips.

4.19.15.26.2
(02-01-2022)
Contents of Case File

- (1) Tip Income Information – The Area Offices will accumulate employer and employee data, on non-participating employees of a tip agreement and rarely on a participating non-filer, to determine which employees will be selected for examination. Data for employee audits will be available on the Employee Data Report based on the Tip Agreement. The Employee Data Report and the list of selected employees will be provided to TS headquarters/ Workload Development and Delivery team. The Food and Beverage and Cosmetology Industry tipped employee audits, referred from Area Offices, will contain a tip allocation worksheet or an Excel spreadsheet.
- (2) The following information will be provided for taxpayers selected for examination:

- Employee's name and SSN
- Employee's position, venue, and shift
- Number of hours worked or sales (if applicable)
- Form 14980, Employee Tip Examinations Worksheet
- Employer's name
- Tip agreement date and RTVUE of tax return, if filed
- Tip rate for employee's position, venue and shift per the Tip Agreement
- Fact of filing

(3) Other Case File Information - Case files may also include the following information:

- AMDISA for the selected year(s)
- IMFOLT for the selected tax year(s)
- IRPTR information for the selected year(s)
- McQuatter's allocation sheet for the Food and Beverage cases
- Employee Data Report
- Tracking sheet. Form 14980, Employee Tip Examinations Worksheet. (Two copies are required: one copy is to be used as a tracking sheet and another copy as part of the administrative file).

4.19.15.26.3
(10-16-2024)
Case Processing
–General Information

- (1) The following information describes procedures specific to the Tip Income Program. Unless otherwise stated, normal case processing procedures should be followed.
- (2) Due to the specific procedures for assessing FICA taxes, all cases in the Tip Program should be filed separately from other cases or flagged for easy identification.
- (3) Adjustments to tip income involve both income tax and FICA taxes. Therefore, two sets of report forms are required:

Type of Tax	Report Form	Agreement Form
Income tax	Form 4549	Form 4549
Social Security	Calculated in RGS	Form 2504
Medicare	Calculated in RGS	Form 2504
Additional Medicare Tax	Form 14980-C	Form 2504

- (4) As the chart shows, report forms must be prepared and sent to the taxpayer (tipped employee): along with Form 2504, Agreement to Assessment and collection of Additional Tax and Acceptance of Over assessment Form 886-A, Explanation of Items, and Form 14980, Employee Tip Examinations Worksheet, must also be sent. If the examination was based on the percentage of gross sales, a Form 14980-B will need to be completed and sent to the taxpayer. Form 14980-A, Explanation of Tip Income, shows how the tip income was computed using the McQuatter's Formula. This provides the taxpayer a detailed computation of the unreported tip income. Make sure your workpapers clearly explain how you arrived at your adjustments. This information will be extremely important if the taxpayer requests a transfer to an Area Office, requests an Appeals conference, or petitions the court.

- (5) Research AIMS to determine if another tax year is open for examination. If so, the cases should be worked by the same examiner.

4.19.15.26.3.1
(10-16-2024)

**Filed Returns – Initial
Contact**

- (1) Compare the tip income reported on Form 1040, including amounts reported on Form 4137, Social Security and Medicare Tax on Unreported tip Income, to the tip income identified by the Area Office.

If	And	Then
The tip income identified by the Area Office exceeds the amount reported on the tax return, including Form 4137	NA	Include the unreported amount in the examination report.
The taxpayer worked for more than one employer where tips were received	The taxpayer participates in the tip agreement at one employer but does not participate at another	Only the tip income reported by the employer for which the employee had unreported tip income should be included.
Both the taxpayer and the spouse on a joint return worked in a tipped occupation and a joint return was filed	There is tip income information for one taxpayer but not the other	Perform the necessary research to determine if there is unreported tip income for the other taxpayer and include all unreported tip income in the report.

- (2) Follow the instructions below when allocated tips are shown on the taxpayer's Form W-2:

If	And	Then
The payer is the same payer as shown on the tip Employee Data Report or other source document	The taxpayer included the allocated tip amount from Form W-2 as income on Form 1040	Give the taxpayer credit for the allocated tips reported on Form 1040 when determining the unreported tip amount.
The payer is the same payer as shown on the tip Employee Data Report or other source document	The taxpayer did not include the allocated tip amount from Form W-2 as income on Form 1040	Disregard the allocated tip amount. Use the information from the Employee Data Report to determine the unreported tip income.
The payer is not the same payer as shown on the Employee Data Report or other source document	The taxpayer did not include the allocated tip amount from Form W-2 as income on Form 1040	Include the allocated tips as a separate issue when determining the unreported tip income.
The payer is not the same payer as shown on the Employee Data Report or other source document	The taxpayer included the allocated tip amount from Form W-2 as income on Form 1040	Assert the FICA penalty on the reported allocated tips.

- (3) Instructions for non-filers

- If the payer is the same payer as shown on the tip Employee Data Report or other source document, disregard the allocated tip amount. Use the information from the Employee Data Report or other source document to determine the unreported tip income.
- If the payer is not the same payer as shown on the Employee Data Report or other source document, include the allocated tips as a separate issue when identifying the unreported tip income.

(4) Use the following table to determine other audit issues:

If	Then
The information on IRPTR shows allocated tips from a different type of property than the one that generated the unreported tip income.	That amount should be included in the unreported income with the appropriate explanation(s) on Form 886-A. For example – if the unreported tips are from a casino venue and IRPTR shows allocated tips from a restaurant, include the allocated tips from the restaurant as unreported tip income on the exam report.
Any other items on the return require examination	Include them on the report with the appropriate explanation(s) on Form 886-A.

- (5) RGS categorization for unreported tip income is: AGI Adjustment/Taxable Earned or Personal Service Income/Unreported Tips from Form 4137. Choose “Primary Taxpayer” or “Secondary Taxpayer” as appropriate and answer “Yes” to the “Assert FICA Penalty” question. This categorization will generate the preparation of Form 2504 and the proper transaction codes on Form 5344.
- Form 2504 will reflect a late filing penalty if it is applicable.
 - The taxpayer may be subject to a penalty equal to 50 percent of the FICA tax due on unreported tips reported on Form 4137 filed with the return. Write in and identify the applicable amount on the Form 2504 generated by RGS and recompute the total penalty amount shown on the Form 2504. Change the TC 310 amount on Form 5344 to reflect the correct amount.
 - Proper categorization of the tip income will generate Reference Codes 891, 892, 898 and 899 as necessary for the Primary or Secondary taxpayers on Form 5344 partial. Do not delete the Reference Codes as they are required entries for the partial assessment and may need to be adjusted.
- (6) Use the following standard explanations for the tip income issues in your initial contact with the taxpayer and in subsequent contacts as necessary.

Explanation	Description
1101	Tips are includible in income
8107	IRC 6652(b) penalty – 50 percent of the FICA taxes on the unreported tip income.
8201	IRC 3101 – Employee’s share of the FICA taxes on the unreported tip income.

Explanation	Description
Custom Explanation	Explanation of tip income examination, examination reports and options available to the taxpayer. This is not currently an RGS paragraph. It is attached to the RGS file through MS Word.

- (7) Prepare the Form 14980, Employee Tip Examinations Worksheet. Enter the name(s) of the employer, taxpayer's position, location worked, shift, hours, tip rate, amount of tips reported to the employer and amount of tips reported on Form 4137. The remaining calculations will be completed by the formulas built into the spreadsheet. The amount on the "Unreported Tips" line should be the same amount shown on Form 4549 and Form 14980-C, FICA Tax and Penalty, as unreported tip income.
 - Taxpayers contacted in this program have been advised of their reporting requirements by their employers and were given the opportunity to participate in the tip compliance agreement program. Choosing not to participate in a tip agreement is a tipped employee's choice. If the tipped employee does not accurately report their tip income, the failure to report income *may* constitute intentional disregard of rules or regulations, or otherwise be subject to a civil penalty.
- (8) Consider asserting the IRC 6662(d) if requirements for the Substantial Understatement Penalty are met. If requirements for Substantial Understatement Penalty are not met, assert the Accuracy Related Penalty for Negligence, IRC 6662(b) (1), on the amount of unreported tip income, based on facts and circumstances surrounding the case.
- (9) Consider any fraudulent/altered documents provided by the taxpayer for fraud penalty referral. Refer to IRM 25.1, Fraud Handbook, and IRM 4.19.10.4, Fraud Referrals, for a list of indicators of fraud and the referral process.
- (10) Letter 525/Letter 525-T for TDC cases, is the initial contact letter for these cases. Prepare the mail-out package using normal procedures and include Form 14980-A, Explanation of Tip Income (Unreported Tip Income) and the custom explanation.
 - RGS auto-populates the deficiency, penalty and interest from Form 4549 as the balance due on Letter 525. Correct this amount to include the Form 4549 amount plus the taxes and penalty shown on Form 2504.
- (11) Follow normal Letter 525/Letter 525-T for TDC cases, procedures for mail-out and suspense.
- (12) Prepare a Form 886-A1, Employee Tip Examinations Worksheet, for each employee. This form can hold up to 5 venues. Complete the form with Employer name, and Employer Identification Number. Leave a copy of each Form 14980, Employee Tip Examinations Worksheet, that has been completed loose in the case file to be used as a tracking sheet. If multiple tracking sheets are prepared, please staple them together so that they can be forwarded as one package.
 - On joint returns, enter the SSN of the taxpayer who received the tip income on the Form 14980, Employee Tip Examinations Worksheet.

- If the unreported tip income, per the information provided by the Area Office, was included on Form 4137 filed with the return, you must still complete a tracking sheet for the tips and FICA taxes shown on Form 4137 so the corresponding employer's share of FICA taxes can be assessed. Attach the Form 4137 filed with the return to the tracking sheet. No other documents or reports should be attached to the tracking sheet.
 - When the case is ready to close, the tracking sheet Form 14980, Employee Tip Examinations Worksheet, should match the closing actions and determination on Form 5344. These tracking sheets will be sent to the originating Area Offices' Tip Coordinator monthly and quarterly to Indian Tribal Gaming (ITG) Tip Compliance Coordinator from TE/GE. Tracking sheets are generally not needed for PC 0364 and 0672 since the employer received their Notice and Demand, unless instructed by HQ.
- (13) If the taxpayer does not sign agreed before the 90-day letter (Statutory Notice of Deficiency) is ready to be sent, the case will include one Form 5344 for the FICA taxes, penalty, and reference codes, and one final Form 5344 for the income tax and related penalties and reference codes. If the taxpayer signs agreed before the Statutory Notice of Deficiency is ready to be sent, then only one Form 5344 is needed.

Disposal Code and Closure	Posting Delay Codes
DC 04 (agreed) before 90-day letter	All transactions can be entered on one Form 5344. No PDC needed.
DC 04 but IRC 6404(g) applies	Same as above but input PDC 1.
DC 08 (partial assessed)	FICA taxes and related actions will have to be processed on the partial Form 5344, and then the Statutory Notice of Deficiency can be issued.
DC 09 (agreed) after 90-day letter	Income tax and related actions will be processed on the closing Form 5344.
DC 09 (agreed) after 90-day letter and IRC 6404(g) applies	Same as above but input PDC 1.
DC 10 (Default) and DC 13 (Undeliverable)	Follow instructions for DC 09 above.

- (14) The FICA taxes and the related penalties cannot be included on the Statutory Notice of Deficiency. These assessments must be made prior to the issuance of the 90-day letter. Refer to IRM 25.6, Statute of Limitations, for assessment statute of limitations on unreported tips income and IRM 4.23.7.4, Form 4137 Requirements.
- (15) Ensure that the assessments are input timely and properly. Prepare Form 5344 and attach the Form 5344 partial to the outside of the case folder. Attach Form 5344 final closing document to the inside of the case folder. The Examiner may include Form 14980-C, FICA Tax and Penalty, (For Information Only) with the 90-day package. This will inform the taxpayer that the income tax and TICA are both due.

4.19.15.26.3.2
(02-01-2022)

Non-Filers

- (1) Follow the procedures beginning at IRM 4.19.15.45, Non-Filer Program.
- (2) The AIMS database should be created with the following information:

Item	Value
Status	06
Source Code	24
Project Code	The Gaming Industry cases generating from non-Indian Tribal Casinos will have Project Code 0360. Indian Tribal Gaming cases will have Project Code 0916. Food and Industry Non-Gaming cases will have Project Code 0364 and Cosmetology Industry will have Project Code 0672.
Org Code	5XXX
Push Code	036

- (3) After you have verified that the “dummy” TC 150 and TC 420 have posted to Master File, prepare Form 4549 based on all available IRP information and the tip income information in the case file.
- (4) RGS categorization for unreported tip income is: AGI Adjustment/Taxable Earned or Personal Service Income/Unreported Tips from Form 4137. Choose “Primary Taxpayer.” The Filing Status on these cases will be either “Single” or “MFS”. Answer “Yes” to the “Assert FICA Penalty” question. This categorization will generate the preparation of Form 2504 and the proper Transaction Codes on Form 5344.
- (5) Follow the instructions in IRM 25.24.2.8, Balance Due Cases for asserting penalties and IRM 4.19.15.26.3.1 for preparation of Examination Closing, Form 14980-A, Explanation of Tip Income, (Unreported Tip Income) and the tracking sheet.
- (6) Send initial contact letter, Letter 1862, and follow normal procedures for preparation, mail-out and suspense.
- (7) Follow instructions in IRM 4.19.15.26.5, Case Processing-Closing Actions and Other Information, for partial assessment and closing procedures.

4.19.15.26.4
(06-14-2023)

**Case Processing –
Revised Reports and
Responses to 90-day
Letters**

- (1) If the taxpayer replies to the Letter 525/Letter 525-T for TDC cases, or Letter 1862 and a revised report is prepared, issue Letter 692-M/Letter 692-T for TDC cases. Follow normal procedures for mail out and suspense of the letter.

If	Then	And Enter These Amounts
You are issuing the report with Letter 692-M/Letter 692-T for TDC cases.	Annotate the ECID or Form 3198: <ul style="list-style-type: none"> Assess FICA taxes \$ XX.XX (TC 300) Assess FICA Penalty \$XX.XX (TC 310) Assess Delinquency Penalty \$XX.XX (TC 160) (if applicable) Enter Hold Code 4 Change the TC 300 shown on Form 5344 Annotate the ECID or Form 3198	On <ul style="list-style-type: none"> Form 2504 – Total Amount of Tax Form 2504 – IRC 6652(b) Penalty Form 2504 – IRC 6651 Penalty TC 300 entered by RGS less the total amount of tax on Form 2504. (Deficiency shown on Form 4549) TC 160 entered by RGS less the Delinquency Penalty shown on Form 2504

- (2) Ensure that the assessments for FICA tax and related penalties are made before the 90-day letter is issued. Refer to IRM 25.6, Statute of Limitation, on assessment statute of limitation on unreported tips income and IRM 4.23.7.4, Form 4137 Requirements. If you are evaluating a response to a 90 day letter and have reduced the amount of under-reported tip income, update a corrected Form 4549 and Form 2504 , as shown in the table after the next paragraph to ensure that the taxpayer is not over-assessed for FICA taxes and the penalty.

Note: If a taxpayer requests Appeals rights during an examination, the FICA tax and penalty will be assessed prior to transferring to Fresno Appeals function. This is to ensure that the FICA tax and penalty statute are not barred. Any notices generated relating to FICA tax and penalty to the taxpayer should be suppressed. The Examiner/lead and the Clerical unit will review case file to ensure that it is followed and that the case file includes workpapers and Form 14980 with tip unreported income calculations for the taxpayer. The Fresno appeals function will adjust/abate the FICA tax and penalty, if necessary, at the conclusion of their appeals process.

- (3) Send Letter 555 and follow the normal procedures for mail-out and suspense. Keep in mind the restrictions on increasing the assessment and requesting documentation after the statutory notice has been issued. See IRM 4.19.13.14, Statutory Notices.

Direction	Transaction/Reference Code	Amount
Abate FICA taxes	TC 301	Difference between the FICA taxes already assessed, and the amount shown on the corrected Form 2504
Abate FICA Penalty	TC 311	Difference between the FICA penalty already assessed, and the amount shown on the corrected Form 2504.

Direction	Transaction/Reference Code	Amount
Abate Delinquency Penalty (if applicable)	TC 161	Difference between the delinquency penalty already assessed and the amount shown on the corrected Form 2504.
Input	Reference Codes 891 and 898 (for Primary taxpayer)	Difference between the Primary taxpayer's unreported tip income shown on Form 4549 that accompanied the 90 day letter and the Primary taxpayer's unreported tip income shown on your revised report. (Show this amount in brackets.)
Input	Reference Codes 892 and 899 (for Secondary taxpayer)	Difference between the Secondary taxpayer's unreported tip income shown on the Form 4549 that accompanied the 90-day letter and the Secondary taxpayer's unreported tip income shown on your revised report. Show this amount in brackets.

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4.19.15.26.5
(02-01-2022)
**Case Processing –
Closing Actions and
Other Information**

- (1) There are special rules for assessing FICA taxes. FICA tax and the associated penalties may have to be assessed prior to issuing the 90-day letter. Ensure that assessments are input timely and properly. Refer to IRM 4.19.15.26.3.1, Filed Returns – Initial Contact, and IRM 4.19.15.26.4, Case Processing - Revised Reports and Responses to 90-Day Letters.
- (2) Unless otherwise instructed, follow normal closing procedures. Refer to the table to determine the action to take and to IRM 4.4, Audit Information Management System (AIMS) - Validity and Consistency.

If	Then
The taxpayer agrees to the 15/30-day letter.	Input all transaction codes on Form 5344 as printed by RGS. Disregard handwritten notations, except for changes to the TC 310 amount.
The taxpayer does not respond to the 15/30-day letter.	<p>Do a partial assessment, prior to the issuance of the 90-day letter Use AMCLSF and input the following:</p> <ul style="list-style-type: none"> • TC 300 per the examiner's instructions • TC 310 per the examiner's instructions. • TC 160 per the examiner's instructions. This will not occur on all cases. • Reference Codes 891, 892, 898 and 899 as shown on Form 5344. • If partial is input at closing use Posting Delay Code 1. • Hold Code 4 • TC 470 with Closing Code 90 on IDRS using Command Codes REQ77/FRM77 if partial is input prior to 90 day. <p>Prepare the 90-day letter for the income tax deficiency and penalties shown on Form 4549.</p>
The taxpayer agrees to the 90-day letter or the 90-day letter defaults.	<p>Using AMCLSE input:</p> <ul style="list-style-type: none"> • TC 300, TC 350/ Ref. 680, TC 160 per the Form 4549 issued with the 90-day letter. • Input all other transactions and references per Form 5344, if they have not been previously input. • Input Posting Delay Code 1 on the closing assessment.
A revised report and Letter 555 adjusting the tip income were issued after the 90-day letter and the taxpayer agrees or the case defaults.	<p>Do a partial abatement using AMCLSF and input the following:</p> <ul style="list-style-type: none"> • TC 301 per the examiner's instructions. • TC 311 per the examiner's instructions • TC 161 per the examiner's instructions. This will not occur on all cases. • Reference Codes 891, 892, 898 and 899 per the examiner's instructions.
A revised report and Letter 555 adjusting the tip income were issued after the 90-day letter and the taxpayer agrees or the case defaults.	<p>Using AMCLSE input:</p> <ul style="list-style-type: none"> • TC 300, TC350 / Ref. 680, TC 160 per the revised Form 4549 issued with the Letter 555. • Input all other transactions and references per Form 5344, if they have not been previously input.

- (3) Requests for Transfer to an Area Office and Statute Extensions. A case should not be transferred if there are less than 13 months remaining on the statute of limitations. Refer to IRM 4.19.13.16, Transfer to Area Office.

- All Tip program cases that require transfer to Area Office should be routed to the clerical support unit. The support unit will update AIMS and

RGS and route to the following address: Internal Revenue Service -
Attn: PSP M/S 4031 - 600 17th Street - Denver, CO 80202.

- HQ analyst should be informed of the transfer request to the Area Office.
- Refer to IRM 4.19.15.44, Non-Filer Program, for information on the statute of limitations for non-filers and the returns they file in response to the initial contact letter or subsequent letter.
- In cases where the time constraints do not allow for transferring the case, contact the taxpayer, explain the situation, and ask the taxpayer to explain their concerns. Try to resolve the issues via correspondence. If the taxpayer insists on transferring the case, the Statutory Notice has not yet been issued, and there are less than 13 months remaining on the statute of limitations, the statute of limitations must be extended to transfer the case.
- If the taxpayer filed Form 4137 with the tax return, prepare Form 872, Consent to Extend the Time to Assess Tax, and Form SS-10, Consent to Extend the Time to Assess Employment Tax, to extend the statute of limitations on both the income and the FICA taxes. Follow normal procedures for mail out and suspense of the request to extend the statutes. Refer to IRM 25.6.22.5, Preparation of Consent Forms - General Procedures.
- If Form 4137 was not filed with the return, prepare Form 872, Consent to Extend the Time to Assess Tax, for the income tax only.

(4) Other Processing Guidelines

- If the taxpayer states that they disagree with the report and you cannot clearly determine the basis of the disagreement, follow normal procedures for contacting the taxpayer to get clarification.
- If necessary, the unreported tip income, as shown on the original report, can be adjusted. However, do not change the taxpayer's hours, shift, position, or venue unless the taxpayer has provided information from the employer.
- Obtain as much information as possible from the taxpayer and document it in detail on your workpapers.
- Access any additional information that is available from the Tip Match database and other employer driven resources.
- If the taxpayer disagrees with an adjustment that is not related to the tip income use normal procedures to evaluate the information the taxpayer provides.
- Tip diaries must meet specific requirements to be accepted. For information on the specific requirements for a tip diary, see Pub 531, Reporting Tip Income, or section 31.6053-4(a)(2) of the Employment Tax Regulations. Also refer to the SERP Job Aids, Compliance *Tip Diary Evaluation*.
- If the taxpayer states they agree with the adjustment to the tip income but provides information about employee business expenses, the taxpayer may be entitled to, evaluate that information and make the necessary determination based on the information provided.
- If the taxpayer responds to the Letter 1862 with a tax return, review the return for accuracy and process the return as instructed in IRM 4.19.15.45, Non-Filer Program.
- If the taxpayer's response results in a revision to Form 4549 and Form 2504 make sure you make the corresponding changes to the tracking sheet.

- If the taxpayer wishes to have a representative conduct the examination on their behalf, Form 2848 must give the representative authority to handle the income tax and the FICA tax issues.

- (5) If a request is made for printed documentation to be sent to Tax Court or Appeals, follow the instructions below (for clerical only):
1. Request the case file from the CORR team,
 2. Case will be sent to Clerical to have all the requested case documents printed.
 3. Clerical will send case file to Appeals or Tax Court with printed documentation enclosed.
 4. A record should be kept by the Clerical manager.

4.19.15.27
(02-01-2022)
**10 Percent Additional
Tax on Early
Distributions – IRC 72(t)
& IRC 72(q)**

- (1) The 10 percent additional tax is an income tax which is assessed on the Individual Master File and taken into account when the total corrected income tax is determined by the tax examiner. Returns included in this program apply to taxable early distributions from qualified retirement plans, Individual Retirement Arrangements (IRAs), or annuity contracts.
- (2) To encourage taxpayers to save for retirement, Congress enacted an early distributions tax that requires taxpayers to pay an amount equal to 10 percent (or 25 percent of certain SIMPLE IRA distributions, if applicable) of the taxable amount distributed from a retirement plan before they reached the age of 59½. The tax is 10 percent (or 25 percent if applicable) of the amount of early distributions includible in gross income and required to be reported on Line 4b (IRAs, pension and annuities) of Form 1040 for tax years 2018 forward. Lines 15b or 16b of Form 1040 were used prior to tax year 2018.

Note: For taxable year 2018, there are no lines 15b and 16b, this information was reported on line 4b of Form 1040.

The 25 percent additional tax applies to an early distribution from a SIMPLE IRA account that occurs within 2 years from the first contribution made by the employer. Distributions subject to the 25 percent additional tax are reported by the payer on Form 1099-R with a Distribution Code S in Box 7 and are required to be reported on Line 4b of the Form 1040.

- (3) There are a number of exceptions to these additional taxes. Tax examiners will be required to determine if the taxpayer meets one of the exceptions or if the taxpayer simply failed to report the proper amount. See IRM 4.19.15.27.1 (10) for Table A and (12) for Table B, for details regarding exceptions. Generally, the payer (individual or entity who is responsible for preparing Form 1099-R) will not know if a taxpayer is using the distribution for a first time home purchase, qualified medical expenses, qualified higher education expenses, or a qualified birth or adoption distribution. Therefore, the payer will code the Form 1099-R Box 7 as 1 (early distribution, no known exception.)

4.19.15.27.1
(10-16-2024)
Procedural Instructions

- (1) Tax Examiners who work these cases should take the following Basic Income Tax Training lessons: IRA, Pensions, Annuities, and IRA Deductions.
- (2) For more information consult Pub 590-B, Distributions from Individual Retirement Arrangements (IRAs), Pub 575, Pension and Annuity Income, Instructions for Form 5329, Additional Taxes on Qualified Plans (including IRAs) and Other

Tax-Favored Accounts, and Instructions for Form 1099–R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.

- (3) Tax examiners must conduct the following research before contacting the taxpayer to determine if the case should be surveyed and to ensure the audit report is correct.

IDRS Command Codes	If	Then
INOLES to determine taxpayer's age. At time of distribution	59 $\frac{1}{2}$ or older Or 55 or older and meets exception per TABLES A and B	survey, close on AIMS using DC 31
TXMOD to verify if taxpayer amended Form 1040 and reported 10/25 percent additional tax	reported	survey case and close on AIMS using DC 31.
IRPTR a. to verify if payer filed amended Form 1099-R for the distribution(s) that is (are) subject to the 10 percent or 25 percent additional tax, b. to verify that all taxable pension, IRA distributions, or any other taxable income have been reported on the return. Include in income any unreported taxable income determined, and c. to determine if pension or IRA distributions are substantially equal to distributions received in the prior or subsequent tax years. These should be surveyed and closed DC 31 if criteria is met.	Form 1099-R Box 7 Code is: a. 2 (early distribution, exception applies (under 59 $\frac{1}{2}$)) b. 3 (Disability), or c. 4 (Death)	survey, close on AIMS using DC 31.

IDRS Command Codes	If	Then
IRPTR a. to verify if payer filed amended Form 1099-R for the distribution(s) that is (are) subject to the 10 percent or 25 percent additional tax, b. to verify that all taxable pension, IRA distributions, or any other taxable income have been reported on the return. Include in income any unreported taxable income determined, and c. to determine if pension or IRA distributions are substantially equal to distributions received in the prior or subsequent tax years. These should be surveyed and closed DC 31 if criteria is met.	Form 1099-R Box 7 Code is: a. G (Direct Rollover of a distribution to a qualified plan, a Section 403(b) plan, a governmental Section 457(b) plan, or an IRA. This does not include the direct rollover of a designated Roth account distribution.) b. H (Direct Rollover of a designated Roth account distribution to a Roth IRA.) Note: See the instructions to Form 1099-R for Codes G and H.	survey, close on AIMS using DC 31. Note: If the additional tax on early distribution does not apply, consider opening the examination if the amount of unreported income is material
IRPTR to verify Form SSA-1099 has been filed	Confirm the taxpayer is receiving Social Security Disability Income	Survey the case on AIMS using Disposal Code 31.
MFTRA OR RTVUE	Form 1040 Schedule R, Credit for the Elderly or the Disabled: a. Trust Fund field will display DISABILITY.	Survey the case on AIMS using Disposal Code 31.

- (4) 10 percent additional tax cases are opened on AIMS in Project Code 0123, Source Code 06.
- (5) Cases selected using the UCP (Unattended Case Processing) Filter Create Discretionary tool will create in RGS Group B2, pending Status 10, with the Letter 566-S/Letter 566-T for TDC cases, and accompanying Form 886-A. A 100 percent review of these cases is required to identify cases that should be surveyed prior to contacting the taxpayers. Based on the required research shown above, if it is determined the taxpayer meets one of the exceptions and is not liable for the 10 percent additional tax, the case should be surveyed, and letter and forms not issued to the taxpayer. Also, the 10 percent additional tax issue should be reviewed to ensure the tax is only being assessed on applicable distributions and to include any unreported income. Cases which pass review, after any necessary corrections have been made, should be reintroduced to ACE (Automated Correspondence Exam) for subsequent automated processing.
- (6) The case will be suspended for 45 days.
- (7) The Letter 525/Letter 525-T for TDC cases, Form 886-A and Form 4549 (audit report) will be prepared systemically during ACE Create 2 processing. Cases

which fire one of the standard filters during Create 2 processing will reject to RGS Group B2. The audit reports must be randomly reviewed, per ACE procedures in IRM 4.19.20.2.9, Reviews. The standard explanation included in Form 886-A is determined by whether an amount is reported on Line 4b (IRA distributions), and/or Line 5b Pensions, and annuities) of Form 1040 for tax years 2018 forward. Lines 15b and/or 16b on Form 1040, or 11b and/or 12b on Form 1040-A for tax years prior to 2018.

Additional tax of 10 percent due to the early distribution made from your qualified retirement plan.

We are proposing to adjust your tax by 10 percent of the taxable amount of the early distribution made from your qualified retirement plan because you received the distribution before you reached age 59 $\frac{1}{2}$, and the payment did not qualify for one of the following allowable exceptions:

- Payments made from the Plan after you separate from service if you will be at least 55 during the year of payment
- Payments made on account of total and permanent disability
- Payments made in substantially equal periodic amounts over your life or life expectancy (or the joint lives or life expectancies of you and your beneficiary)
- Payments made to a beneficiary after the death of the participant
- Payments of Employee Stock Ownership Plan (ESOP) dividends
- Payments paid directly to the government to satisfy a federal tax levy
- Payments made to an alternate payee under a Qualified Domestic Relations Order (QDRO)
- Payments for medical expenses that do not exceed the amount of your deductible medical expenses (whether or not you itemized deductions)
- For distributions made before January 1, 2016 from a State or local governmental defined benefit pension plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service
- For distributions made after December 31, 2015, payments from a governmental plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service.
- Payments from CSRS and FERS made under a phased retirement annuity
- Payments while you are on active duty, if you were called to duty after September 11, 2001, for more than 179 days.
- Payments made to individuals who receive qualified reservist distributions.
- In-plan Roth rollovers or eligible distributions contributed to another qualified retirement plan or IRA within 60 days.
- Payments made for a qualified birth or adoption distribution.
- For distributions to a victim of domestic abuse, up to the lesser of \$10,000 or 50% of the vested account balance for distributions made after 12/31/23.
- For one distribution per calendar year for personal or family emergency expenses, up to the lesser of \$1,000 or vested account balance over \$1,000, for distributions made after 12/31/23.
- For corrective distributions (and associated earnings) of excess contributions, excess aggregate contributions and excess deferrals, made timely.
- For distributions up to \$22,000 to qualified individuals who sustain economic loss by reason of a federally declared disaster where they live, effective for disasters taking place after January 26, 2021.
- For distributions made from a pension-linked emergency savings account (made after 12/31/2023).
- For distributions made to a terminally ill employee, on or after the date the employee has been certified by a physician as having a terminal illness, effective for distributions made after December 29, 2022.
- For distributions made to a qualified public safety employee from a governmental plan provided that the qualified public safety employee has separated from service during or after the year in which they attained age 50 or 25 years of service under the plan, whichever is earlier. Effective for distributions made after December 29, 2022.
- For distributions made from a plan described in clause (iii), (iv), or (iv) of section 402(c)(8)(B) to an employee who provides firefighting services and who separated from service in or after the year in which they attained age 50 or 25 years of service, whichever is earlier. Effective for distributions made after December 29, 2022.

Additional tax of 10 percent due to the early distribution made from your qualified retirement plan.

If you believe you qualify for one of the exceptions, please provide us with documentation that shows you meet one of the above exceptions. Examples of acceptable documents include:

- corrected Form 1099-R from the issuing entity, or
- a statement from your plan administrator explaining why you meet the exception, or
- a statement from your medical practitioner explaining your disability, or
- copies of cancelled checks or receipts showing when and what qualified expenses were made, or
- a copy of the QDRO (generally part of your divorce decree).

Additional tax of 10 percent due to the early distribution made from your annuity contract.

We are proposing to adjust your tax by 10 percent of the taxable amount of the early distribution made from your annuity contract because you received a distribution before you reached age 59 $\frac{1}{2}$, and the payment did not qualify for one of the following allowable exceptions:

- Payments after the death of the annuity owner
- Payment made on account of total and permanent disability
- Payments made in substantially equal amounts over your life or life expectancy (or the joint lives or life expectancies of you and your beneficiary)
- Payments allocable to an investment in the contract before August 14, 1982
- Payments made under a qualified personal injury settlement
- Payments made under an immediate annuity contract
- Payments made under a deferred annuity contract purchased by your employer upon termination of a qualified plan that is held by your employer until you separate from service
- For distributions up to \$22,000 to qualified individuals who sustain an economic loss by reason of a federally declared disaster where they live. Effective for disasters taking place after January 26, 2021.
- For distributions to a victim of domestic abuse, up to the lesser of \$10,000 or 50% of the vested account balance (for distributions made after 12/31/2023).
- For one distribution per calendar year for personal or family emergency expenses, up to the lesser of \$1,000 or the vested account balance over \$1,000 (made after 12/31/2023).
- The additional tax does not apply to certain excess contributions to an IRA. See section 333 of SECURE 2.0.

If you believe you qualify for one of the exceptions, please provide us with documentation that shows you meet one of the above exceptions. Acceptable documents include:

- corrected Form 1099-R from the issuing entity, or
- a statement from your annuity holder explaining why you meet the exception, or
- a statement from your medical practitioner explaining your disability

- a. Use the following standard explanation if an entry is on Form 1040 Line 15b (IRA distribution taxable amount), but there is no entry on Line 16b (pensions and annuities taxable amount), or if an entry is on Line 11b (IRA distribution taxable amount), but there is no entry on Line 12b (pensions and annuities taxable amount) for Form 1040-A.

Note: For taxable year 2018, there is no line 15b or 16b. The information was entered on line 4b of the Form 1040. Also, for tax year 2018, there is no Form 1040-A.

Additional tax of 10 percent due to the early distribution made from your Individual Retirement Account (IRA).

We are proposing to adjust your tax by 10 percent of the taxable amount of the early distribution made from your Individual Retirement Account (IRA) because you received the distribution before you reached age 59¹/₂, and the payment did not qualify for one of the following allowable exceptions:

- Payments made on account of the total and permanent disability
- Payments made in substantially equal amounts over your life or life expectancy (or joint lives or life expectancies of you and your beneficiary)
- Payments after the death of the IRA owner
- Payments for qualified higher education expenses
- Payments to buy, build, or rebuild a first home
- Payments paid directly to the government to satisfy a federal tax levy
- Payments not exceeding the amount of your deductible medical expenses (whether or not you itemized deductions)
- Payments to unemployed individuals for health insurance premiums
- Payments while you are on active duty if you were called to duty after September 11, 2001, for more than 179 days
- Payments made for a qualified birth or adoption distribution

If you believe you qualify for one of the exceptions, please provide us with documentation that shows you meet one of the above exceptions. Examples of acceptable documents include:

- corrected Form 1099-R from the issuing entity
- a statement from your plan administrator explaining why you meet the exception
- a statement from your medical practitioner explaining your disability, or
- copies of cancelled checks or receipts showing when and what qualifying expenses were made

- b. Use all of the standard explanations (per 7a and 7b above) on Form 886-A if there is an entry on Line 4b (IRAs, pensions, and annuities) of Form 1040 for tax years 2018 forward. For tax years prior to 2018 both Lines 15b (IRA distribution taxable amount) and 16b (pensions and annuities taxable amount) on Form 1040 [Lines 11b (IRA distribution taxable amount) and 12b (pensions and annuities taxable amount) on Form 1040-A].

- (8) Suspend the case for 45 days waiting for taxpayer response to Letter 525/ Letter 525-T for TDC cases. If no reply is received, follow the procedures in IRM 4.19.13.13, No Response Cases.

- (9) Use the following table when reviewing the taxpayer's reply.

If	Then
The taxpayer signs the report or, prior to the mailing of a Statutory Notice of Deficiency, pays the full amount,	Close the case using normal procedures.
The taxpayer submits documentation and you need additional information,	<ol style="list-style-type: none"> 1. If the taxpayer provides a phone number, attempt to call the taxpayer and notate the phone call in your case file. 2. If the attempt to contact the taxpayer is unsuccessful, follow procedures in IRM 4.19.13.11.1, Taxpayer Response – Prior to Status 24 Additional Information Needed.

If	Then
The taxpayer appeals the determination,	Follow relevant procedures in IRM 4.19.13.17, Appeals - Non Docketed Cases.
The taxpayer submits sufficient documentation (refer to tables A and B below) to verify an exception was met,	Close no change using normal procedures.

Note: The IRS has released new and updated publications and forms for individuals who received qualified disaster distributions from retirement plans in 2016 or 2017. The Disaster Tax Relief and Airport and Airway Extension Act of 2017 offered tax-related and other relief to victims of Hurricane or Tropical Storm Harvey, Hurricane Irma, Hurricane Maria, and the California wildfires, that occurred in 2017. In the Tax Cuts and Jobs Act, Congress extended distribution relief to 2016 disasters. New Publication 976, Disaster Relief summarizes various types of tax relief available for individuals and businesses affected by qualifying disasters in 2016 and 2017, including qualified disaster distributions.

- (10) Table A provides the category of payer (IRA, qualified retirement plan, or annuity) and in what tax year the exception is available. Verify that the correct plan applies to the correct exception. For example, a distribution from a 401(k) Plan is not available for the first-time home buyer exception. The exception for distributions made after separation from service after age 55 is not available for an IRA distribution.

Table A

Exceptions to early distribution tax	IRA	Qualified Retirement Plan	Annuity	Tax Year
Payments made on or after the date the plan participant or account holder reached 59¹₂ .	x	x	x	ALL
Payment made to a beneficiary upon death of the plan participant or contract holder.	x	x	x	ALL
Payment made based on total and permanent disability of the recipient.	x	x	x	ALL
Distribution made as a part of a series of substantially equal payments .	x	x	x	ALL
Distribution used for certain higher education expenses .	x	n/a	n/a	Starting 1998
Distributions used for first-time home purchase (Up to \$10,000).	x	n/a	n/a	Starting 1998
Distributions made after separation from service in or after the year the participant reached age 55 .	n/a	x	n/a	Starting 1998

Exceptions to early distribution tax	IRA	Qualified Retirement Plan	Annuity	Tax Year
Distributions made to the extent of deductible medical expenses that can be claimed on Line 4 of <i>Schedule A</i> Form 1040. (Does not apply to annuity contracts or modified endowment contracts.)	x	x	n/a	After 1996
Distributions made to unemployed (at least 12 weeks) individuals for health insurance premiums.	x	n/a	n/a	After 1996
Payments to an alternate payee under a qualified domestic relations order QDRO.	n/a	x	n/a	ALL
Payments made if, as of March 1, 1986 , the plan participant separated from service and began receiving benefits under a written election.	n/a	x	n/a	ALL
Payments made to correct excess deferrals, excess contributions , or excess aggregate contributions.	n/a	x	n/a	ALL
Payments allocable to investment in a deferred annuity contract before August 14, 1982.	n/a	n/a	x	ALL
Payments from an annuity contract under a qualified personal injury settlement.	n/a	n/a	x	ALL
Payments made under a deferred annuity contract purchased by the employer upon the termination of a qualified retirement plan or qualified annuity and that is held by the employer until the participant separates from service.	n/a	n/a	x	ALL
Payments made under an immediate annuity contract.	n/a	n/a	x	ALL
The distribution is due to an IRS levy under Section 6331 of the Internal Revenue Code.	x	x	n/a	Starting in 2000
Distributions to qualified reservists called to active duty for more than 179 days or for an indefinite period.	x	x	n/a	After September 11, 2001
Payments from a federal retirement plan made under a phased retirement annuity program	n/a	n/a	n/a	After 2014

Exceptions to early distribution tax	IRA	Qualified Retirement Plan	Annuity	Tax Year
Payments made after August 17, 2006 and before January 1, 2016, from a State or local governmental defined benefit pension plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service.	n/a	x	n/a	ALL
Payments made after December 31, 2015, from a governmental plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service.	n/a	x	n/a	ALL
Distributions for qualified birth or adoption expenses up to \$5,000 paid during the 1-year period the individual was born or the legal adoption is finalized Note: While qualified birth or adoption distributions may be from a qualified retirement plan, such distributions are not permitted from a defined benefit plan.	x	x	n/a	Starting 2020

(11) The following bullets apply to Table A

- A five percent rate may apply to certain annuity distributions – see IRM 4.19.3.16.3, 10 Percent Tax on Early Distributions From Qualified Retirement Plans/25 Percent Tax on Early Distributions from SIMPLE IRAs, for more information.
- IRAs include Traditional, Roth, and SIMPLE IRAs.
- Qualified Retirement Plans include: 401(a) qualified pension, profit-sharing, and stock bonus plan, including 501(a) tax exempt trust plan, 403(a) qualified employee annuity plan, 403(b) employee annuity contract purchased by a public school or by a 501(c)(3) tax exempt organization, employee stock ownership plan (ESOP), 401(k) qualified cash or deferred arrangement plan, CSRS, FERS, the Federal Thrift Savings Plan, and any tax favored deferred compensation plan that is not an IRA, a SIMPLE IRA or an individual retirement annuity.

(12) Table B details acceptable documentation for exceptions to the early distributions tax. The list is not all inclusive.

Note: Always accept a corrected Form 1099-R. Do not accept Form 5329 submitted after filing as verification.

Table B

If the taxpayer claims one of the following exceptions:	Then acceptable verification is:
Payments made on or after the date the plan participant or account holder reached age 59¹₂ ,	Taxpayer's age verified using IDRS CC INOLES or birth certificate.
Payment made to a beneficiary upon death of an IRA holder or pension plan participant (not applicable to modified endowment contracts),	Date of death verified via IDRS CC INOLES or death certificate, plan beneficiary form or statement from plan administrator.
Payment made based on total and permanent disability ,	Letter from medical practitioner verifying the taxpayer's permanent and total disability.
Distribution made as a part of a series of substantially equal payments ,	<ul style="list-style-type: none"> • Review prior and subsequent year IRP documents, tax returns or RTVUE for amounts distributed and/or reported. • Confirm math is correct by method described in Pub 590-B, Distributions from Individual Retirement Arrangements (IRAs), or Pub 575, Pension and Annuity Income. • Rev. Rul. 2002-62 will affect some distributions made after 2001 if there has been a modification to the series of periodic payments.
Distribution used for certain higher education expenses (tuition, fees, books, supplies, and equipment required by the school for enrollment or attendance of a student). Eligible expenses should be reduced by scholarships and any other tax-free awards. Reminder: The distribution and payments must be within the same tax year.	Verified expenses from Form 1098-T using IDRS CC IRPTR, copies of cancelled checks/money orders and invoices, or statement from school showing dates and payment amounts of higher education expenses. Reminder: Do not accept direct payments from taxpayer to student.

If the taxpayer claims one of the following exceptions:	Then acceptable verification is:
<p>Distributions used for a first-time home purchase, up to \$ 10,000 (this is a lifetime limit). The distribution must be used for this purpose within 120 days after the distribution. Must be principal residence</p> <ul style="list-style-type: none"> Acceptable costs include expenses to acquire, construct or reconstruct a residence, reasonable settlement, financing, or other closing costs, First time homebuyer defined as the taxpayer and, if married, the spouse, as well as any child, grandchild or ancestor of the taxpayer or spouse, who had no ownership interest in a principal residence in the two-year period preceding the date of closing or preceding the date that construction/reconstruction commenced, The 60-day rollover period (see below) for recontributing the distribution to an eligible retirement plan is extended to 120 days if the taxpayer does not close due to delay or cancellation of the purchase or construction of the residence. 	<p>To verify if first-time purchase, use IDRS and research prior years for mortgage interest or real estate tax payments for first time purchase:</p> <ul style="list-style-type: none"> Copies of cancelled checks or money orders, contracts, or closing (settlement) statements showing how the money was used. Letter from financial institution or seller explaining reason for delay or cancellation of closing if applicable.
<p>Distributions made after separation from service in or after the year the participant reached age 55.</p>	<ul style="list-style-type: none"> Use IDRS CC INOLES to verify taxpayer's age Check taxpayer's current and prior years Form W-2 to verify separation from service.
<p>Distributions made to the extent of deductible medical expenses that can be claimed on Line 4 of Form 1040 <i>Schedule A</i>, regardless of whether the taxpayer itemized deductions. (Does not apply to annuity contracts or modified endowment contracts.)</p>	<p>IRM 4.19.15.20, <i>Schedule A</i>, for verification procedures.</p>
<p>Distributions made to individuals unemployed (for at least 12 weeks) for payment for health insurance premiums.</p>	<ul style="list-style-type: none"> Verify unemployment from Form 1099-G or employee records Copies of cancelled checks, money orders for insurance payments or statement of account from insurance agent/company
<p>Paid to an alternate payee under a qualified domestic relations order, QDRO.</p>	<p>Divorce decree or statement from plan administrator.</p>
<p>Payments from an employer plan made if, as of March 1, 1986, the plan participant separated from service and began receiving benefits under a written election.</p>	<p>Statement from plan administrator.</p>
<p>Payments made from employer plans to correct excess wage deferrals, excess contributions, or excess aggregate contributions.</p>	<p>Statement from plan administrator. See Employee Compensation, Retirement Plan Contributions in Pub 575, Pensions and Annuity Income.</p>

If the taxpayer claims one of the following exceptions:	Then acceptable verification is:
Payments from a deferred annuity contract to the extent allocable to investment in the deferred annuity contract before August 14, 1982 .	See Pub 575, Pensions and Annuity Income, for more information and accept statement from plan administrator.
Payments from an annuity contract under a qualified personal injury settlement .	See Pub 575, Pensions and Annuity Income, for more information and accept statement from plan administrator.
Payments made under an immediate annuity contract .	See Pub 575, Pensions and Annuity Income, for more information and accept statement from plan administrator.
Payments made under a deferred annuity contract , purchased by the employer upon the termination of a qualified retirement plan, or a qualified annuity that is held by the employer until the participant separates from service.	See Pub 575, Pensions and Annuity Income, for more information and accept statement from plan administrator.
The distribution is due to an IRS levy of a qualified plan or on an IRA under Section 6331 of the Internal Revenue Code.	Copy of IRS levy showing account levied.
Rollover – This is a tax-free distribution of assets from one eligible retirement plan that is reinvested in another eligible retirement plan or the same plan. The rollover must be completed within 60 days from the date of receipt of the distribution . The amount rolled over is not subject to either the 10 percent or 25 percent additional tax. See Pub 590-B, Distributions from Individual Retirement Arrangements (IRAS), for the frozen deposit exception to this rule.	Statement from administrator of the new plan.
Transfer –If the taxpayer instructs the plan trustee to transfer funds directly to another plan, the transferred amount is not taxable or subject to the early distributions tax.	Statement from plan administrator.
Payments from CSRS and FERS made under a phased retirement annuity program.	Statement from plan administrator.
Permissible withdrawal made from an eligible automatic contribution arrangement (EACA)	Statement from plan administrator.
Payment made by the taxpayer for a qualified birth or adoption distribution	Use IDRS CC TRDBV or RTVUE to verify the name, age and Taxpayer Identification Number of the eligible individual included on the taxpayer's tax return for the tax year in which the distribution is made. See IRC 72(t)(H)(vi)(III) and Q&A, D-2 of Notice 2020-68 on page 567 of IRB 2020-38, for further guidance on qualified birth or adoption distributions.

If the taxpayer claims one of the following exceptions:	Then acceptable verification is:
Payments made after August 17, 2006, and before January 1, 2016 , from a State or local governmental defined benefit pension plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service.	<ul style="list-style-type: none"> • Use IDRS CC INOLES to verify taxpayer's age. • Statement from plan administrator verifying that taxpayer is a public safety employee.
Payments made after December 31, 2015, from a governmental plan to a qualified public safety employee who is at least age 50 at the time the public safety employee separates from service.	<ul style="list-style-type: none"> • Use IDRS CC INOLES to verify taxpayer's age. • Statement from plan administrator verifying that taxpayer is a public safety employee.

(13) **The following bullets apply to Table B**

- The tax on early distributions does not apply to any part of the distribution that is tax free, such as amounts that represent a **return of the taxpayer's cost or amounts rolled over/transferred (see above)** to another retirement plan.
- To avoid the 25 percent additional tax on an early distribution from a SIMPLE IRA Plan, the distribution must be rolled over/transferred into another SIMPLE IRA Plan.
- Certain Roth IRA distributions are not subject to the 10 percent additional tax, see Instructions for Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax Favored Accounts, Page 2 and Pub 590-B, Distributions from Individual Retirement Arrangements (IRAs), for more information.
- Rev. Rul. 2002-62, allows certain taxpayers who began receiving fixed payments from their IRA or retirement plan based on the value of their account at the time they started receiving payments to switch – without penalty – to a method of determining the amount of their periodic payments based on the value of their account as it changes from year to year. If the taxpayer elects to do this, it may result in a lower periodic payment. See Rev. Rul. 2002-62 for more details.
- Rev. Proc. 2003-16 provides guidance for applying to the IRS for a waiver of the 60-day rollover requirement. It also provides for an automatic waiver under certain circumstances. The Procedure is effective for distributions after December 31, 2001. See Rev. Proc. 2003-16 for more information.
- Rev. Proc. 2016-47 provides guidance for waiver of the 60-day rollover requirement from one retirement plan or individual retirement arrangement (IRA) into another plan or IRA by providing a "self-certification procedure" for taxpayers to use in claiming rollover treatment. This revenue procedure is effective on August 24, 2016.

4.19.15.28
(02-01-2022)
**Gambling Issues
(Income and Losses) -
General Casual
Gamblers**

- (1) For tax years prior to 2018, taxpayers report gambling income on Form 1040, Line 21, and gambling losses on Form *1040 Schedule A* Line 28. For tax years 2018, gambling income is reported on *Form 1040 Schedule 1* Line 21, and gambling losses on *1040 Schedule A* Line 16. For tax years 2019 and subsequent, gambling income is reported on Form 1040 Schedule 1, line 8.

Note: The amount of total gambling losses may not exceed the amount of the total gambling income reported on Form 1040. Total gambling losses for a taxable year cannot be netted against total gambling income for a taxable year before the computation of the Adjusted Gross Income on Form 1040. Each item, income or loss, must be reported on the appropriate line or form.

Note: This topic relates solely to casual gamblers. Gamblers in a trade or business of gambling use Schedule C.

- (2) Form W-2G, Certain Gambling Winnings, is a reporting requirement for certain gambling winnings. Gambling winnings are not the same as gambling income. A taxpayer recognizes gambling income (or a gambling loss) at the end of the taxpayer's gambling session (for example, when tokens are redeemed).
- (3) The following table shows examples of documentation taxpayers may provide to support their deduction for gambling losses. This is not an all-inclusive table. For returns with unreported IDRS cc IRPTR gambling winnings, the taxpayer may provide information of gambling losses that offset reportable gambling winnings from gambling income. For example, a taxpayer may show that after receiving the reportable gambling winnings they subsequently continued to gamble and lose the winnings, and ended their gambling session with no gambling income. Use good judgment when evaluating any information the taxpayer provides, including the possible inclusion of additional income.

Note: For residents of the U.S., Courts have applied this concept to non-resident aliens as well. See **Park v. Commissioner, 722 F.3d 384, 406 (D.C. Cir. 2013)**. Note that the use of "session", in determining gambling winnings and losses has historically been limited to a slot machine play.

Gambling documentation - Examples

Documentation or wagering activity	Information provided
Diary of winnings and losses	<ul style="list-style-type: none"> • Date and type of wager or wagering activity. • Name and address or location of the gambling establishment. • Names of other persons present at the gambling establishment. • Amount(s) won or lost.
Canceled checks, credit records, bank withdrawals; copies of casino credit records, copies of casino check cashing records	Location of the gambling establishment; date of the wager.
Keno	Date the keno tickets were validated by the gambling establishment.
Slot machines	A record of the machine number and all winnings by date and time the machine was played.
Table games (twenty-one, blackjack, craps, poker, baccarat, roulette, wheel of fortune, etc.)	<ul style="list-style-type: none"> • The number of the table at which the taxpayer was playing. • Casino credit data indicating whether the credit was issued in the pit or at the cashier's cage.

Documentation or wagering activity	Information provided
Bingo	<ul style="list-style-type: none"> A record of the number of games played, cost of tickets purchased, and amounts collected on winning tickets. Supplemental records include any receipts from the casino, parlor, etc.
Racing (horse, harness, dog, etc.)	<ul style="list-style-type: none"> A record of the races, amounts of wagers, amounts collected on winning tickets and amounts lost on losing tickets. Supplemental records include unredeemed tickets and payment records from the racetrack.
Lotteries	<ul style="list-style-type: none"> A record of ticket purchases, dates, winnings and losses. Supplemental records include unredeemed tickets, payment slips, and winnings statements.

- (4) Taxpayers with whom telephone contact is made should be encouraged to respond in writing with all documentation related to their gambling activities.

4.19.15.28.1
(02-01-2022)

**Initial Contact for
Gambling Income**

- (1) Issue Letter 566-S/Letter 566-T for TDC cases, as the initial contact letter to the taxpayer. Check "Schedule A Itemized Deductions". Identify the issue by typing "Gambling Losses". Identify income as an issue if there is unreported income.

4.19.15.28.2
(12-12-2008)

**Evaluating Gambling
Issue Responses**

- (1) This section provides guidelines to assist in evaluating responses to gambling issues.

4.19.15.28.2.1
(01-01-2015)

**Gambling Losses – IRC
165(d)**

- (1) Carefully examine all documentation of losses for the year of the loss to ensure the losses are for the year related to the win. Notate the workpapers with the amount of losses and income from the documentation.
- (2) Receipts provided to support losses may also include gambling income not included on the return. Carefully review all documentation for income as well as losses. Subsequent reports (except for cases where the statutory notice has been issued) must include the income as well as the losses.
- (3) Examine unredeemed (losing) tickets carefully to ensure that they are for the correct year and that they had not been previously discarded prior to being acquired by the taxpayer.
- (4) Use sound judgment when considering taxpayer replies. Consider all aspects of the case, including the credibility of the taxpayer, additional burden, and the amount of tax when deciding whether to request more documentation.

4.19.15.28.2.2
(01-01-2015)
Gambling Income

- (1) Form 5754, Statement by Person(s) Receiving Gambling Winnings, is completed by the taxpayer and given to the payer of the gambling winnings to ensure that the Form W-2G issued is correctly prepared when the taxpayer receives gambling winnings on behalf of another person or as a member of a group of winners on the same winning ticket.
 - a. A signature is required on Form 5754 only if federal income tax was withheld from the winnings.
 - b. Form 5754 should not be accepted as proof the income was distributed to other taxpayers. If the amount of disputed winnings exceeds \$500, research the accounts of other taxpayers using Command Code IRPTR to determine if a Form W-2G was issued to that payee. If a Form W-2G was issued, then consider this an acceptable explanation.
 - c. If multiple Form W-2G were not issued, correspond with the taxpayer and explain that the gambling income is to be reported by the person to whom the Form W-2G is issued. Advise the taxpayer that a statement from the payer is required in order to accept the Form 5754.
- (2) Follow normal procedures for evaluating the information the taxpayer provides regarding the unreported gambling income. Make all necessary adjustments to gambling losses and income and issue a report, with the appropriate explanations and a cover letter. Refer to the table below for letter sequencing.

4.19.15.28.2.3
(02-01-2022)
Replies – General Processing

- (1) Use the following table when processing replies.

Processing Taxpayer Replies to Letter 566-S/Letter 566-T for TDC cases and Subsequent Letters

If	And	Then
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases, Letter 525/Letter 525-T for TDC cases, Letter 692-M/Letter 692-T for TDC cases. or the Statutory Notice of Deficiency (SNOD) with information to support gambling losses	you are able to determine the taxpayer is entitled to the entire deduction,	close the case “no change.”
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases, or Letter 525/Letter 525-T for TDC cases, with information to support gambling losses	you are able to verify that the taxpayer is entitled to part of the amount claimed,	issue Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases. with Form 4549, allowing the partial amount verified and an appropriate explanation.
The taxpayer replies to Letter 566-S or Letter 525/Letter 525-T for TDC cases, with information to support gambling losses	you are able to determine that the taxpayer is not entitled to any part of the deduction,	issue Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, with Form 4549 and an appropriate explanation.

If	And	Then
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases, Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases with information to support gambling losses	you are able to determine that the amount on <i>Form 1040 Schedule A</i> Line 28 for tax years prior to 2018 or Line 21 for tax years 2018.- For tax years 2019 and subsequent, gambling income is reported on Schedule 1, line 8,	issue Letter 525/Letter 525-T for TDC cases, with Form 4549 and an appropriate explanation.
The taxpayer replies to the SNOD with information to support gambling losses	you are able to verify that the taxpayer is entitled to part of the amount claimed,	issue Letter 555 with a revised Form 4549 and an appropriate explanation to the taxpayer.
The taxpayer replies to the SNOD with verification of their deduction	you are able to determine that the taxpayer is not entitled to any part of the deduction,	issue Letter 555 with the latest Form 4549.
The taxpayer replies to the SNOD with verification of their deduction	you are able to determine that the amount on <i>Form 1040 Schedule A</i> Line 28 for tax years prior to 2018 or Line 21 for tax years 2018. For tax years 2019 and subsequent, gambling income is reported on Schedule 1, line 8,	issue Letter 555 with a revised Form 4549 and an appropriate explanation to the taxpayer. Do not increase the deficiency as shown on the SNOD.

4.19.15.28.2.4
(02-01-2022)

- (1) Take the following action if the taxpayer has not replied to the most recent letter by the normal purge date:

No Response Cases

Latest Letter Issued	Action
Letter 566-S/Letter 566-T for TDC cases,	Prepare Letter 525/525-T for TDC cases, and Form 4549 disallowing the gambling losses and adding the unreported gambling winnings. Use Standard Explanations 1407 and/or 9412.
Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, and the Form 4549 reflects a deficiency	Follow normal procedures to have SNOD issued based on the adjustments shown on Form 4549.
Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, and the Form 4549 reflects an overpayment	Close the case DC 08.
SNOD	Close the case DC 10.

4.19.15.28.3
(01-01-2015)
**Special Gambling
Closing Procedures**

- (1) When closing cases, consideration must be given to the disposition of receipts to the taxpayers. Receipts will not be returned to the taxpayer as a matter of practice. All verification of losses must be retained with the case file. If the verification is not substantial, for example a statement from a casino, it can be retained in the closed case file. If the documentation would be difficult to file, retain the records in a retrievable method for a period of nine months.
- (2) If the IRS and the taxpayer agree on the amount of the losses verified by the documentation, there is no reason to retain the receipts. If the taxpayer requests the return of the receipts, contact the taxpayer by telephone to confirm the taxpayer's request. Explain that there is no longer a tax requirement to retain the receipts. If the taxpayer insists, the tickets must be stamped before they are returned.

Note: When making or receiving phone calls, an IRS employee must follow IRM 21.1.3.2.3, Required Taxpayer Authentication, to ensure that they are speaking to the appropriate taxpayer and to prevent the unauthorized disclosure of tax information.

- (3) If the taxpayer does not address the disposition of unredeemed tickets, retain them for a period of nine months after the case closes.

4.19.15.29
(02-01-2022)
**Health Coverage Tax
Credit – IRC 35**

- (1) **Eligibility:** A taxpayer may elect to take the Health Coverage Tax Credit (HCTC), a refundable credit, if the taxpayer is an eligible individual. An eligible individual is:
 - a. Workers who have been adversely impacted by foreign trade and who are recipients of Trade Adjustment Assistance (TAA), Alternative Trade Adjustment Assistance (ATAA) or Reemployment Trade Adjustment Assistance (RTAA), and
 - b. Pension Benefit Guaranty Corporation (PBGC) pension payees who are at least age 55.
 - c. A qualifying family member (spouses and dependents) can be considered recipients and are eligible to newly receive or continue to receive the HCTC in the event that a related TAA, ATAA, or RTAA recipient or PBGC payee dies or finalizes a divorce with the recipient, if the recipient was a qualifying family member immediately before such event.
 - d. Qualifying family members can receive the HCTC for eligible coverage months up to 24 months from the death or divorce, or until the first coverage month that begins on or after January 1, 2020, whichever comes first.
 - e. Submission Processing (SP) and Accounts Management (AM) correspond with taxpayers claiming HCTC when accounts do not have eligibility coding (under either TIN if a joint return) and taxpayers did not provide proof of eligibility with U.S. Form 1040, Individual Income Tax Return, Form 8453, U.S. Individual Income Tax Transmittal for an IRS e-file Return, or Form 1040-X, Amended U.S. Individual Income Tax Return. Examiners input TC 971 AC 172 when taxpayers respond with eligibility letters from State workforce agencies (SWAs) or PBGC.
- (2) **Qualifying coverage:** Eligible individuals must be covered by qualifying health care insurance to benefit from HCTC, which includes:
 - a. Consolidated Omnibus Budget Reconciliation Act (COBRA) continuation coverage,

- b. Coverage under an employee benefit plan funded by a Voluntary Employees' Beneficiary Association (VEBA) established as a result of bankruptcy proceedings,
 - c. Group health plans available through the employment of the eligible individual's spouse,
 - d. State-based coverage, and
 - e. Individual health insurance which is defined as insurance for medical care offered to individuals other than in connection with a group health plan and does not include Federal or State-based coverage. For tax years prior to 2014, the eligible individual must have been covered under individual health insurance for the 30-day period ending on the date of separation from the employment which qualified the person for TAA/ATAA/RTAA or PBGC benefits. For tax years after 2015, coverage enrolled in through a Health Insurance Marketplace (Exchange) established under the Affordable Care Act (ACA) is not qualifying individual health insurance.
 - f. Qualifying coverage does **not** include; Flexible spending arrangements (FSAs) or similar arrangements; Insurance if substantially all the coverage is for excepted benefits described in IRC 9832(c), such as dental or vision plans, policies covering only a specified disease or illness, and hospitalization insurance. (The examples are not all-inclusive.)
 - g. Taxpayers are required to attach proof of payment for health care insurance to HCTC claims. SP and AM correspond for missing documentation.
- (3) **Other Specified Coverage:** Eligible individuals must not have other specified coverage, defined as:
- a. Subsidized coverage; Coverage under a health plan maintained by a current or former employer of the taxpayer or taxpayer's spouse if the employer pays or incurs at least 50 percent of the cost of the coverage; For ATAA and RTAA recipients only, eligibility for coverage meeting requirements outlined in paragraph (2) above, or enrollment in coverage under an employer-sponsored health plan if the employer pays any of the premiums; Coverage in lieu of a right to receive cash or other benefits under a cafeteria plan as described in IRC 125(d)
 - b. Coverage under Medicare (entitlement under Part A, which generally occurs at age 65, or enrollment under Part B or Part C), Medicaid or the State Children's Health Insurance Program (SCHIP or CHIP), and
 - c. Coverage under the Federal Employees Health Benefits Program (FEHBP) or entitlement to coverage under the U.S. military's TRICARE program (formerly CHAMPUS).
- (4) **Qualifying Family Members:** If an eligible individual has qualifying coverage and does not have other specified coverage (refer to the exception in (c) below), the taxpayer may also claim HCTC for qualifying coverage of qualifying family members (QFMs).
- a. A "qualifying family member" is a person who does not have other specified coverage and; Is the eligible individual's spouse **or**; Is claimed as a dependent on the tax return **unless** the taxpayer is the dependent's non-custodial parent **or**; Could be claimed as a dependent except the taxpayer is the custodial parent who released the right to claim the exemption to the non-custodial parent under the special support test for divorced or separated parents.

- b. If spouses filing separate returns are both eligible individuals during the year, neither will be treated as a qualifying family member.
 - c. If HCTC would be allowed for qualifying coverage of the eligible individual but for Medicare coverage (entitlement under Part A or enrollment under Part B or Part C), the taxpayer may continue to claim HCTC for qualifying coverage of qualifying family members for the first 24 months after the recipient of PBGC or TAA/ATAA/RTAA benefits became covered by Medicare.
 - d. If a qualifying family member is treated as an eligible individual under the terms described in paragraph (1)(d) above, then that person's qualifying family members are limited to those individuals who were qualifying family members immediately preceding the event that conferred provisional eligibility.
- (5) **Other Rules:** Additional considerations apply with respect to HCTC.
- a. HCTC is not allowed if the eligible individual; Was imprisoned under Federal, State or local authority **or**; Could be claimed as a dependent on another taxpayer's return.
 - b. Persons receiving COBRA premium assistance under the American Recovery and Reinvestment Act of 2009 are not treated as eligible individuals or qualifying family members.
 - c. Premiums claimed for HCTC may not be used in determining medical and dental expenses on Schedule A or a self-employed health insurance deduction (SEHID).
 - d. An eligible coverage month is one that begins 90 days after the enactment of the Trade Act of 2002 and before January 1, 2022.
- (6) **HCTC Claims:** HCTC is determined on a month-by-month basis and is computed on Form 8885, Health Coverage Tax Credit.
- a. As of March 2011, HCTC is equal to 72.5 percent of the premiums paid by an eligible individual for qualifying health insurance covering that person and qualifying family members **after** reduction by any distributions from an Archer Medical Savings Account (MSA) or Health Savings Account (HSA). (The credit was 65 percent from December 2002 through April 2009 and 80 percent from May 2009 through February 2011.)
 - b. December 2002 was the first month that HCTC became available with enactment of the Trade Adjustment Assistance Reform Act. Subsequent legislation modified and extended HCTC to December 2013. The Trade Preferences Extension Act of 2015 reinstated the credit, made it retroactive to tax years 2014 and 2015 and extended HCTC through 2019.
 - c. To claim HCTC for tax year 2014, taxpayers must file an amended return with Form 8885 due to the timing of legislation.
 - d. Beginning with tax year 2014, taxpayers must make an irrevocable election to claim HCTC. Generally, the election must be made by the due date (including extensions) for the return. Refer to tax year 2014 - 2016 claims <https://www.irs.gov/pub/irs-irbs/irb17-07.pdf>
 - e. Once HCTC is elected, the Premium Tax Credit (PTC) may not be claimed for the same coverage for that month or any subsequent months that the taxpayer is HCTC eligible for the TY. 1- Taxpayers who previously claimed PTC or who received the benefit of advance PTC (APTC), must file Form 8962, Premium Tax Credit (PTC). No PTC should be claimed for Marketplace coverage subject to the HCTC election. All APTC should still be reported on Form 8962, even for months subject to the

HCTC election. 2- The APTC repayment limitation on form 8962, line 28, may not apply when a taxpayer elects the HCTC for marketplace coverage.

- (7) **Advance (Monthly) HCTC - IRC 7527:** Advanced payments of HCTC became available for the first time in 2003.
- The HCTC Processing Center forwarded payment of 100 percent of the cost of health insurance coverage for a person enrolled in the advance monthly payment option directly to the insurance provider or third-party administrator (TPA). The Center issued invoices to collect the taxpayer's portion. Refer to paragraph (6)(a) above, for the percentage of premiums paid by Department of Treasury.
 - Advance HCTC was not available for tax years 2014 and 2015 due to the timing of extension legislation. It was reinstituted on a limited basis in July of 2016 with the assistance of certain TPAs. Advance monthly HCTC has been available to all qualified applicants since January 1, 2017. Participants will not receive monthly invoices but will remit premium monthly payments with coupons available at www.irs.gov/hctc.
 - Advance monthly HCTC is posted to the tax account of the enrolled participant with TC 971 AC 171. The amount received from the taxpayer for the remaining portion of the premiums is recorded with TC 971 AC 170.
 - Advance monthly HCTC payments are reported to the taxpayer on Form 1099-H, Health Coverage Tax Credit (HCTC) Advance Payments.
- (8) **Resources:** For more information about HCTC, refer to Pub 502, Medical and Dental Expenses (Including the Health Coverage Tax Credit), the instruction for Form 8885, Health Coverage Tax Credit, Notices 2005-50 and 2016-02, and <https://www.irs.gov/credits-deductions/individuals/hctc>, Health Coverage Tax Credit.

4.19.15.29.1
(03-11-2019)
HCTC Case Selection & Classification

- Procedures for HCTC audits are dependent on whether the credit has been posted to the taxpayer's account and the case selection method.
- Returns are categorized as "**processed claims**" if HCTC is posted to the account. TXMOD of a processed claim should include TC 766 with CRN 250 in an amount equal to the HCTC claimed on Form 8885. (Processing errors can occur. Examples of improper HCTC adjustments include TC 291, TC 806 and TC 766 with CRN 336.) Processed claims are generally selected based on criteria established by TS RICS Exam HQ.
- For processing year 2016, processed claims for HCTC will be referred for examination using unallowable programming.
 - SP will post Unallowable (UA) code 89 to a return when one or more of the following conditions exist; There is no TC 971 AC 172, and the taxpayer did not respond to an error notice with proof of eligibility; The taxpayer did not provide proof of payment for health insurance, **and/or** the taxpayer claimed HCTC and Premium Tax Credit (PTC) for the same month(s).
 - Refunds are frozen up to the amount of HCTC claimed with TC 576.
 - Cases are created systemically in source code (SC) 03 and project code (PC) 0505.

- d. Manual classification prior to initial contact is required. Change the source code to 20 when additional audit issues are identified. Do not change the project code.
 - e. General UA procedures in IRM 4.19.14.18, Unallowable Code (UA) Program, apply except where contradictory with the above.
- (4) Beginning with filing season 2017, Dependent Database (DDb) filters will be used to identify processed claims for potential audit of HCTC. (Exception: Returns meeting the criteria in paragraph (3)(a) above will continue to be coded with UA 89).
- a. Returns selected via DDb filters will open in SC 06, PC 0505.
 - b. Taxpayers who receive advance monthly HCTC may erroneously claim the same coverage for the same months on Form 8885, Health Coverage
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- compliance strategy.
- c. Additional compliance strategies not involving advance monthly HCTC may include the use of tracking code 7559.
- (5) Returns are worked as “**unprocessed claims**” if HCTC is not posted to the account. Amended returns with increases to HCTC are CII imaged and routed by AM to Exam classifiers if criteria per IRM 21.5.3-3, Examination Criteria (CAT-A) - Credits, is met. (For additional information refer to IRM 21.6.3.4.2.9.1, Health Coverage Tax Credit (HCTC) - Eligibility.
- a. Open AIMS with SC 30 and PC 0505 when an amended return is referred and selected for HCTC.
 - b. General claims procedures in IRM 4.19.16, Claims, apply.
- (6) For processed and unprocessed claims not selected as described above, update AIMS and CEAS/RGS with tracking code 7561 when the scope of an audit is expanded to include HCTC.
- (7) If an HCTC claim is classified for related issues on the return or that are reflected on the tax account, including PTC/APTC, Schedule A medical and dental expenses, a SEHID, or deductions for an Archer MSA and HSA, , refer to:
- a. Pub 974, Premium Tax Credit (PTC),
 - b. IRM 4.19.15.41 , Premium Tax Credit - IRC 36B,
 - c. Pub 502, Medical and Dental Expenses,
 - d. IRM 4.19.15.20, Schedule A,
 - e. Pub 535, Business Expenses,
 - f. IRM 4.19.15.30, Self-Employed Health Insurance Deduction - IRC 162(I), and
 - g. Pub 969, Health Savings Account and Other Tax-Favored Health Plans.
- (8) Examiners must obtain managerial approval in the form of a non-action CEAS note prior to pursuing any large, unusual or questionable items (LUQs) not previously classified on a return.

4.19.15.29.2
(03-11-2019)

**Research for HCTC
Cases**

- (1) Complete research is required when technical employees, other than examiners resolving ACE reject conditions, must take actions to prepare letters and/or review responses. Follow general procedures in IRM 4.19.13.4, Researching Cases, including documenting workpapers for research performed and pertinent information found.

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- (3) Review MeF returns via EUP. Taxpayers may attach PDF files with supporting records. Note the entries on Form 8885, including the months checked.

- (4) Access CII for documents received by AM. Consider a Form 8885 and any related records.

- (5) In IDRS, research the taxpayer's TIN, including a spouse's if applicable, for:

- a. HCTC adjustments (TC 766/767 CRN 250),
- b. HCTC eligibility indicator(s) (TC 971 AC 172),
- c. Coding for advance monthly HCTC (TC 971 AC 170/171),
- d. Age of the taxpayer(s) and qualifying family members,
- e. PBGC-based eligibility per Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts,

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- f. Health insurance coverage and/or premium payment information per: Form 1095-A, Health Insurance Marketplace Statement; Form 1095-B, Health Coverage; Form 1095-C, Employer-Provided Health Insurance Offer and Coverage; Form 1099-H, Health Coverage Tax Credit (HCTC) Advance Payments; Form 1099-SA, Distributions From an HSA, Archer MSA, or Medicare Advantage MSA, **and/or** Form W-2, Wage and Tax Statement.

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4.19.15.29.3
(03-11-2019)

**Initial Contact & No
Response Procedures**

- (1) **Unprocessed Claims - Source Code 30**

- a. Send Letter 566-D for initial taxpayer contact.
- b. Include Form 14749, Health Coverage Tax Credit - Verification of Eligibility and Qualifying Insurance, to request information the taxpayer could provide to verify HCTC claimed and any Forms 886 applicable for HCTC or other classified issues.
- c. Update to Status 10 and suspend the case for 45 days.
- d. Follow IRM 4.19.16.2.4.1, Claims Contact Procedures, if the taxpayer does not respond to Letter 566-D and IRM 4.19.16.2.4.2, Claims Contact Responses, if there is no reply to subsequent letters.

- (2) **Processed Claims - Source Codes 03, 06 and 20**

- a. Disallow HCTC on Form 4549, Income Tax Examination Changes, and send with Letter 525/525-T for TDC cases, for initial contact.
- b. If there are error codes for the Premium Tax Credit (PTC) on the return, include the appropriate adjustments to the PTC and the Advance PTC repayment on Form 4549. Refer to IRM 4.19.15.41.6, Creating the PTC Issue(s), for error code specific instructions.
- c. Include any Forms 886 applicable for HCTC or other classified issues and; Form 14749, Health Coverage Tax Credit - Verification of Eligibility and Qualifying Insurance, if TC 971 AC 172 is not present **or**, Form 14749-A, Health Coverage Tax Credit - Verification of Qualifying Insurance, when an eligibility indicator is posted.

Note: When reviewing accounts for eligibility indicators, ensure TC 971 AC 172 has not been reversed by TC 972 AC 172.

- d. For source codes 03 and 20, follow the additional procedure in IRM 4.19.14.18.5, Processing Reply/NoReply Unallowable Cases.
- e. Update to Status 22 and suspend the case for 45 days.
- f. Follow the instructions in IRM 4.19.13.13, No Response Cases, and IRM 4.19.10.1.7.2, Standard Suspense Periods for Correspondence Examination, if the taxpayer does not reply to the initial contact or subsequent letters.

- (3) **Closures:** Refer to IRM 4.19.15.29.5, Case Closure, when a closure is appropriate after no response from the taxpayer. It details specific actions needed for HCTC and provides references for general closing procedures.

4.19.15.29.4
(03-11-2019)
HCTC Responses

- (1) **General Guidelines:** Follow the steps in the table below to process replies (not all-inclusive).

If	Then
TC 971 AC 172 is not present and the taxpayer did not establish eligibility,	Do not allow HCTC. (Refer to IRM 4.19.15.29(1) for the definition of eligibility. Always ensure a TC 971 AC 172 is not reversed by TC 972 AC 172.)
TC 971 AC 172 is not present and the taxpayer established eligibility for one or more months during the tax year,	Update TXMOD for the return with TC 971 AC 172. Include the TIN of the eligible individual. (For TAA/ATAA/RTAA, do not accept an application or enrollment form in lieu of an eligibility letter from an SWA dated after the eligible months for the year.)
The individual was a PBGC recipient under age 55 as of the first day of the month,	Do not allow premiums paid for anyone's coverage for that month in the HCTC computation. (Age 55 does not apply for a person treated as an eligible individual under the terms in IRM 4.19.15.29(1)(d).)

If	Then
The eligible individual or spouse treated as an eligible individual due to divorce did not have qualifying coverage as of the first day of the month,	Do not allow premiums claimed for anyone's coverage for that month in the HCTC computation.
The eligible individual or spouse treated as an eligible individual due to divorce had other specified coverage as of the first day of the month,	Do not allow premiums claimed for anyone's coverage for that month in the HCTC computation. (Refer to the Medicare exception in IRM 4.19.15.29(4)(c), which conditionally allows HCTC for coverage of qualifying family members.)
An otherwise qualifying family member, including one treated as an eligible individual due to death, had other specified coverage as of the first day of the month,	Do not allow premiums claimed for coverage of the family member for that month in the computation of HCTC.
A qualifying family member, including one treated as an eligible individual due to death, did not have qualifying coverage as of the first day of the month,	Do not allow premiums paid to cover the family member for that month in the HCTC computation.
The taxpayer is the non-custodial parent of a dependent on the return,	Do not allow premiums covering the child of divorced or separated parents in the computation of HCTC for any month.
Health insurance premiums were paid to cover a family member (other than a spouse on the return) who was not claimed as a dependent,	Do not allow premiums paid for the family member's coverage in the computation of HCTC <i>unless</i> the taxpayer is the custodial parent who unconditionally released the right to claim the exemption to the non-custodial parent with Form 8332, Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent, or a divorce decree executed before 2009.
A distribution from an HSA or Archer MSA reported on Form 1099-SA, Distributions From an HSA, Archer MSA, or Medicare Advantage MSA, was not included on Form 8885	Subtract the distribution from allowable premiums and recompute the HCTC.

If	Then
The eligible individual or qualifying family member received COBRA premium assistance under ARRA 2009 as of the first day of the month,	Do not allow premiums paid for any health insurance covering that person for the same month in the HCTC computation. (A 65 percent subsidy was available to eligible workers who lost their jobs between Sept. 1, 2008, and May 31, 2010, for COBRA continuation premiums for themselves and their families for up to 15 months.)
The eligible individual received a 100 percent ARPA COBRA subsidy	Do not allow the HCTC for months the individual received the COBRA subsidy during the period of April 1, 2021 through September 30, 2021.
The taxpayer submits cancelled checks remitted to "U.S. Treasury – HCTC" and/or Form 1099-H to support premium payments on Form 8885,	Do not allow the payments for an end-of-year credit. Inform the taxpayer that the maximum monthly HCTC was allowed for the coverage associated with the advance payment program.
The taxpayer requests a case transfer or meeting with an Appeals Officer,	Follow relevant procedures in IRM 4.19.13.17, Appeals - Non Docketed Cases.
The taxpayer states that supporting records for HCTC were attached to Form 1040 or 8453 or were provided in response to an error notice,	Inform the taxpayer that the information is not readily available and an attempt to obtain it would significantly delay resolution of the audit.
Verified payments for health insurance premiums are not allowable for HCTC but qualify as a Schedule A, Self-employed Health Insurance, HSA, or Archer MSA deduction,	Advise the taxpayer to file an amended return to claim the disallowed premiums as a deduction from income unless a double tax benefit was previously claimed.
HCTC is not allowable, but the taxpayer qualifies for PTC not currently on the tax account,	Allow PTC if the taxpayer previously claimed PTC/APTC and repaid it solely to claim HCTC. Otherwise, advise the taxpayer to file an amended return to claim PTC for the disallowed premiums.

If	Then
For TYs 2014 thru 2015, HCTC is allowable, but the taxpayer claimed PTC based on the same Marketplace coverage,	<p>Disallow PTC claimed for any Marketplace coverage subject to the HCTC election starting with the first month for which the taxpayer elected to claim the HCTC:</p> <ol style="list-style-type: none"> 1. Determine the total amount of PTC for which the taxpayer is eligible and create an issue for Total PTC net credit adjustment to reduce the total PTC claimed on the return. 2. Subtract the recomputed total PTC from the total Advance PTC received and create an Advance PTC repayment net tax adjustment if the result is a positive amount. Reduce the adjustment by any Advance PTC repayment already reported on the return.
HCTC and other classified issues are fully substantiated,	Allow all issues and close the case. (Math verify Form 8885.)

- (2) **Eligibility:** Taxpayers may check too many months on Form 8885 when eligibility was for less than the full tax year. Do not allow premiums claimed for any month if, as of the first day of the month, the eligibility requirement was not met.

- a. Taxpayers whose returns were selected for audit because eligibility indicator TC 971 AC 172 was not present must verify eligibility for all months claimed. Generally, an eligibility letter from an SWA or PBGC is required. If HCTC is claimed based on the special rules in IRM 4.19.15.29, Health Coverage Tax Credit - IRC 35, the taxpayer may need to establish the date of the qualifying event and eligibility of the original recipient of TAA/ATAA/RTAA benefits or PBGC pension payments at that time.
- b. The eligibility months may be determined through internal means when

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- c. Pensions are generally paid to retirees for life. If PBGC issued a Form 1099-R for the tax year prior to the one under audit and the payee taxpayer is the retired employee who was at least age 55 at the start of the AIMS year, then the taxpayer was an eligible individual for the full year under audit or until the date of death, if applicable. (Retirees can be eligible individuals by virtue of PBGC pension payments and not receive

distributions during the tax year. If the retiree elects a lump sum payment, PBGC should continue to transmit eligibility data until the person reaches age 65.)

- d. Similar logic cannot determine TAA/ATAA/RTAA-based eligibility months. The maximum duration of assistance to affected workers varies between 104 and 156 weeks. Benefits may be terminated for lack of program participation, such as attendance for mandatory training, and then subsequently reinstated if the workers reapply. Participants may cease to qualify for assistance due to significant reemployment. (There is an additional grace month for HCTC eligibility after TAA/ATAA/RTAA benefits expire. SWAs include the grace month on HCTC eligibility letters.)

(3) **Qualifying Coverage:** IRC 35 identifies some types of coverage as non-qualifying for HCTC. However, any coverage not specified in IRC 35 as qualifying is not qualifying. Refer to IRM 4.19.15.29, Health Coverage Tax Credit – IRC 35, paragraph (2), for the complete list of qualifying coverage.

- a. Group health plans available through the eligible individual's current employer are not listed coverage and are generally not qualifying for HCTC. If the premiums claimed were for a group plan and the eligible individual was the primary insured, verify that the coverage was COBRA continuation, VEBA-funded due to bankruptcy or an SQP.
- b. VEBAs may fund group coverage for retirees when the employer cannot meet COBRA continuation coverage requirements due to bankruptcy. When VEBAs fund individual health insurance, SQPs or work-related group plans with the spouse as the primary insured, bankruptcy is not a consideration because those coverage types are qualifying in their own right.
- c. There are several types of coverage that a State may elect to designate as qualifying for HCTC, including some employee and retiree group

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- d. FSAs and similar arrangements are listed as non-qualifying coverage. Employee contributions to FSAs are made via pretax payroll deductions.
- e. The tax treatment of employee health benefits may be determined by comparing the deductions on the employee's final leave and earnings statement for the year to the difference between the gross wages on the pay statement and taxable wages in box 1 of Form W-2.
- f. The Office of Chief Counsel has advised that pretax treatment for employee contributions for health care insurance is an arrangement similar to flexible spending (if not actually an FSA) and is therefore not qualifying for HCTC.

(4) **Other Specified Coverage:** Review IRM 4.19.15.29, Health Coverage Tax Credit – IRC 35, paragraph (3), for details about other specified coverage and the consequence for HCTC.

- a. Employers are more likely to pay at least 50 percent of the health insurance costs of a current employee than a former one. The percentage of the amount of premiums paid by the employer may be determined from Form W-2. Employer contributions are identified with code DD in Box 12. The employee's cost of coverage (including dental, vision, and FSC payments) should be itemized in box 14.

- b. If IRC 125 is indicated, verify that the employee's payroll deductions were taxed. If not taxed, the plan meets the condition for other specified coverage. Refer to (3)(b)(1) above to determine the tax treatment.
- (5) **Qualifying Family Members:** Occasionally, examiners must determine the premiums paid for coverage of a nonqualifying family member or beneficiary when one policy covers multiple persons. Counsel provided guidance for the allocation in IRS Notice 2005-50. If the shared policy was enrolled in through a Marketplace, use the guidance in Notice 2016-02 instead.
- (6) **Workpapers:** Follow the general procedures in IRM 4.19.13.6, Workpapers for All Cases, when documenting taxpayer responses. Notate any information still needed and record details about supporting records received, such as:
 - a. The name of the eligible individual, the eligibility type, the eligibility months, and
 - b. The type of coverage, the primary insured and other covered individuals, the dates of coverage, the covered benefits, the employer and/or TPA associated with a group plan, the group name and number if applicable, the insurance provider, the policy number, the cost of premiums by month, and the payment method.
- (7) **Unprocessed Claims:** Consult IRM 4.19.16.2.4.1, Claims Contact Procedures, and IRM 4.19.16.2.4.2, Claims Contact Responses, for the letters and forms to send the taxpayer when considering responses for unprocessed claims.
- (8) **Processed Claims:** Refer to IRM 4.19.13.11, Taxpayer Replies, for the actions to take when all audit issues of a processed claim are not resolved.
- (9) **Closures:** Refer to the next subsection, IRM 4.19.15.29.5, Case Closure, when a closure is appropriate after considering a response. It details specific actions needed for HCTC and provides references for general closing procedures, including those pertaining to agreed cases.

4.19.15.29.5
(01-01-2017)
Case Closure

- (1) **Unprocessed Claims:** Use the instructions in IRM 4.19.16.2.4, Claims Processing in Examination Operation, and IRM 4.19.16.2.4.2, Claims Contact Responses, when closing unprocessed claims if:
 - a. Allowing HCTC, use Credit Reference Number (CRN) 250 with the allowable amount in Block 15 of Form 5344. Send Letter 570 to the taxpayer.
 - b. Disallowing HCTC, and the taxpayer has not waived notification of claim disallowance, provide a detailed explanation on Letter 105-C for a full disallowance or Letter 106-C for a partial one.

Note: When assessing additional tax to deny the HCTC, whether pre-refund or post-refund, deficiency procedures (including letter 3219) must be used.
- (2) **Processed Claims:** Follow procedures in IRM 4.19.13.30, Campus Exam Closing Actions, for processed claims. Also, follow the applicable steps below:

If	And	Then
Allowing any HCTC	TXMOD does not include an unreversed TC 971 AC 172,	<ul style="list-style-type: none"> Input TC 971 AC 172 with the TIN of the eligible individual unless eligibility coding is AP or PN. Input "1" in Block 43 of Form 5344 for a posting delay of one cycle to avoid an unpostable condition.
Allowing all HCTC	Form 5344 does not include changes to tax, income, or other credits,	<ul style="list-style-type: none"> Use DC 02 in Block 13 of Form 5344. Input "no change" Issue Code 61065 in Block 41.
Disallowing some portion of HCTC	TC 766 for HCTC does not include a CRN,	Input CRN 767 with the disallowed amount and a minus sign (-) in Block 15 of Form 5344.
Disallowing some portion of HCTC	TC 766 includes CRN 250,	Input CRN 250 with the disallowed amount and a minus sign (-) in Block 15 of Form 5344.
Disallowing some portion of HCTC	HCTC is posted to the account in any other manner (see above),	<ul style="list-style-type: none"> Consult the work leader for the appropriate reversal code. Use Hold Code 3 in Block 7 of Form 5344 to prevent a notice.
Disallowing some portion of HCTC	A refund is frozen with TC 576 and the taxpayer did not agree to waive statutory notification of claim disallowance,	Issue Letter 105-C. Refer to IRM 4.19.14.18.5, Processing Reply/No Reply Unallowable Cases, for more information.

4.19.15.30
(06-14-2023)
Self-Employed Health Insurance Deduction – IRC 162(l)

- (1) A taxpayer may be able to deduct part or all of the amount paid for health insurance, if the taxpayer is one of the following:
- A self-employed individual and has a net profit for the tax year from a *Schedule C*, Profit or Loss From Business (Sole Proprietorship), Net Profit From Business (Sole Proprietorship) or *Schedule F*, Profit or Loss From Farming
 - A shareholder owning more than two percent of the outstanding stock of an S Corporation (or is considered as owning more than two percent by reason of the attribution rules under IRC 318) with wages reported on Form W-2
 - A partner with net earnings from self-employment reported on Line 14a of Form 1065, U.S. Return of Partnership Income)
 - A self-employed individual that used one of the optional methods to figure net earnings from Self-employment on Schedule SE

Note: A self-employed individual's deduction of health insurance for income tax purposes does not reduce their net earnings from self-employment. (See Section 162(l)(4))

- (2) A taxpayer may be eligible for a section 162(l) deduction and the Premium Tax Credit (PTC) in the same taxable year. Under section 280C(g) of the Internal Revenue Code, a section 162(l) deduction is not allowed for the portion of the premium paid by the PTC. However, a taxpayer must know the section 162(l)

deduction to compute the PTC and the PTC to compute the section 162(l) deduction. See Pub 974 and Rev. Proc. 2014-41 for more information on how taxpayers in this situation compute their section 162(l) deduction and PTC.

- (3) IRC 318 attribution rules include four situations that result in a shareholder's stock in an S corporation being constructively owned by another person:
 - a. An individual will be considered to own the S corporation stock owned by their spouse (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance), children (including legally adopted children), grandchildren and parents;
 - b. A beneficiary or owner of a trust (described in section 1361(c)(2)) will be considered to own the S corporation stock owned by the trust;
 - c. A beneficiary of an estate will be considered to own the S corporation stock owned by the estate; or
 - d. A person with an option to acquire S corporation stock will be considered to own the stock in which they hold the option.
- (4) A self-employed individual or employee-shareholder may claim 100 percent of the amount paid as an adjustment to income.
- (5) In calculating the deductible amount, taxpayers should use the Self-Employed Health Insurance Deduction Worksheet in the *Instructions for Form 1040* which indicates the deduction is the lesser of
 - a. the amount paid for health insurance coverage, or
 - b. net profit or earned income from the business under which the insurance plan is established, minus any deductions claimed on the Form 1040 for one-half of the Self-Employment Tax and any contributions to Self-Employed Simplified Employee Pension Plan (SEP), SIMPLE IRA Plan, and Qualified Plans.
- (6) Taxpayers may receive a Form 1099-MISC, Miscellaneous Income, for self-employed income or Form 1099-NEC, Non-employee compensation. Generally, the taxpayer prepares a *Schedule C* to report this income; however, it may also appear on the "Other Income" line. Ensure the taxpayer has reduced this income by any expenses applicable to the earning of this income to arrive at net income. Taxpayers who are in business as a self-employed writer, inventor, artist, etc., should report their income on *Schedule C*, and apply appropriate expenses to obtain net income.
- (7) For purposes of the deduction, a two percent-plus shareholder's wages from the S Corporation are treated as the shareholder's earned income. No deduction is allowed more than an individual's earned income derived from the trade or business with respect to which the plan providing the health insurance coverage is established.
- (8) For employee-shareholders, the health insurance premiums must be paid in the current year by the corporation and included in the wages (generally shown in Box 14 of the Form W-2) of the employee-shareholder. The amount may include payments for insurance covering the taxpayer, their spouse, and dependents. If the premiums were not included in the employee-shareholder's wages (in Box 1 of the Form W-2), the employee-shareholder may not deduct them.

- (9) The taxpayer may not claim the Health Coverage Tax Credit (for which additional qualifications apply) for the same expenses the taxpayer claimed for the Self-Employed Health Insurance Deduction.

Note: The Health Coverage Tax Credit is not available for months beginning on or after January 1, 2022.

- (10) A taxpayer may not take this deduction for amounts during a calendar month in which the taxpayer participated, or is eligible to participate, in any subsidized health plan maintained by any employer of the taxpayer or of the spouse of , or any dependent, or individual described in subparagraph (d) of paragraph (1) of section 162(l) with respect to, the taxpayer.

4.19.15.30.1
(02-01-2022)

Self-Employed Health Insurance Deduction

- (1) Cases are worked to determine if a taxpayer is:
- Erroneously claiming health insurance payments in excess of earned income or net profits of the business
 - Erroneously claiming health insurance payments because they are unable to itemize
 - Claiming the deduction when they have no self-employment or earned income.
- (2) Procedures are as follows:
- The Initial Contact Letter 566-S/Letter 566-T for TDC cases, will be used to inquire about the income and/or deductions
 - Normal suspense periods will be applied to all letters issued

4.19.15.30.2
(11-04-2019)

Evaluating Responses

- (1) Use the following guidelines when evaluating responses to Self-Employed Health Insurance Deduction:
- Carefully examine all documentation to determine if all or some of the amounts were paid for qualifying insurance. If the taxpayer was eligible to participate in any subsidized health plan maintained by any employer of the taxpayer or of the spouse of, or any dependent, or individual described in subparagraph (D) of paragraph (1) of section 162(l) with respect to, the taxpayer **cannot** deduct premiums for any month in which they are eligible.
 - Determine if the taxpayer had sufficient earned income for the claimed self-employed health insurance deduction. (Note: The deduction is limited to the profit from the business.) Review Form 1099-MISC or other documentation to ensure the taxpayer was self-employed. If the income is unreported, include the additional income in the report and compute self-employment tax, if appropriate.
 - If the taxpayer indicates income is from an S Corporation, review *Schedule K-1*, Partner's Share of Income, Deductions, Credits, etc. and/or other documentation (i.e., Form W-2) to establish if the income and/or wages received and reported were from an S Corporation in which the taxpayer was more than a two percent shareholder.
 - If IDRS information is used to link a taxpayer to a corporation, examiners may use judgment in accepting the taxpayer's statement as verification that they have more than two percent ownership. (The basis for the examiner's judgement must be fully documented on the workpapers.)

- Ensure the taxpayer has reduced earned income by any deduction claimed for one-half of Self-Employment Tax, and a deduction claimed for Self-Employed SEP, SIMPLE, and Qualified Plans (when applying lesser of earned income reduced by these deductions and amount paid).
 - If the taxpayer does not have a Form W-2 from a Subchapter S Corporation, a quick way to determine if the taxpayer is self-employed may be to review the taxpayer's *Schedule SE*, Self-Employment Tax. The amount of income on which they paid Self-employment tax can be used as the amount of income from net self-employment income.
 - Responses involving the concept of material participation generally relate to the allowance of a loss rather than income and are unlikely to be applicable here.
 - Since our taxpayers are "cash basis" taxpayers, all deductible expenses must be incurred by them in the current year. Income must be distributed to them and/or reported by them when earned.
- (2) If the taxpayer filed a joint return, conduct research to determine if both spouses received earned income during the year in question. If both spouses received earned income, request a statement from the taxpayers' employers. The statement(s) must indicate:
- a. If the spouses were eligible to participate in the companies' subsidized health plan(s), and
 - b. The number of months (if any) that the spouses were eligible to participate in the plan.

4.19.15.30.3
(11-04-2019)

Potential Documentation

- (1) Request a copy of the health insurance policy indicating the payment was made for qualifying individuals, i.e., the taxpayer, spouse, or dependents.
- (2) If the insurance premiums were paid by the corporation, verify premiums were included in the taxpayer's wages from the corporation (most generally will appear on Form W-2).
- (3) If premiums were paid by the taxpayer, request cancelled checks, receipts, payroll deductions, etc., to support the deduction.
- (4) The *Schedule K-1*, Partner's Share of Income, Deductions, Credits, etc. and/or IDRS cc BMFOL or cc BMFOLT for the S Corporation may be used to establish the taxpayer is linked to that corporation. Copies of the articles of incorporation, stock certificates or similar documentation may be used to establish whether the taxpayer is a more-than-two percent-shareholder. If the taxpayer indicates they qualify by reason of attribution rules, ask the taxpayer about their relationship to the shareholder. A taxpayer's statement may be sufficient to establish this fact if other issues have been satisfactorily resolved. Workpapers must be documented to support the examiner's determination.
- (5) If the taxpayer is claiming payments for long-term care insurance, request birth certificates if the taxpayer's age cannot be determined from IDRS. See Pub 535, Business Expenses, to determine the aged-based limitations.
- (6) If the taxpayer paid the expenses to the insurance company, cancelled checks, documentation to show payroll deduction, etc., should be adequate to support the deduction.

4.19.15.30.4
(03-11-2019)

**Resources To Assist In
Technical Determination**

(1) Useful tools:

- Pub 502, Medical and Dental Expenses
- Pub 535, Business Expenses.
- IRC 162(l), IRC 1372, IRC 401, IRC 36B and IRC 318.
- If payment is for long-term care insurance, see limitations in Chapter 6 of Pub 535.
- *Instructions for Form 1040, U.S. Individual Income Tax Return* – includes a Self-employed Health Insurance Deduction Worksheet which the taxpayer should complete to determine if there is limit to the deduction amount.

4.19.15.30.5
(02-01-2022)

**Replies – General
Processing**

(1) Use procedures in the following table when processing replies.

Processing Taxpayer Replies to Letter 566-S/ Letter 566-T for TDC cases and Subsequent Letters

If	And	Then
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases,, Letter 525/Letter 525-T for TDC cases, Letter 692-M/Letter 692-T for TDC cases, or the Statutory Notice of Deficiency (SNOD) information to support the deduction	You are able to determine that the taxpayer is entitled to the entire deduction	Close the case “no change”.
The taxpayer replies to Letter 566-S/Letter 566-T for TDC cases, or Letter 525/Letter 525-T for TDC cases, with information to support the deduction	You are able to verify that the taxpayer is entitled to part of the deduction claimed	Issue Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases, with revised Form 4549 and an appropriate explanation.
The taxpayer replies to Letter 566-S/566-T for TDC cases or Letter 525/Letter 525-T for TDC cases, with information to support the deduction	You are able to determine that the taxpayer is not entitled to any part of the deduction	Issue Letter 525/Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases with Form 4549 and an appropriate explanation.
The taxpayer replies to Letter 566-S/566-T for TDC cases, Letter 525/Letter 525-T for TDC cases or Letter 692-M/Letter 692-T for TDC cases with information to support deduction	You are able to determine that the amount belongs on another line on the tax return	Issue Letter 525/Letter 525-T for TDC cases with Form 4549 and an appropriate explanation.

If	And	Then
The taxpayer replies to Letter 566-S/566-T for TDC cases, Letter 525 /Letter 525-T for TDC cases, or Letter 692-M/Letter 692-T for TDC cases with information	Time frame has expired, and information indicates that taxpayer is not entitled or not eligible	Prepare Form 886-A addressing correspondence received and explain disallowance.
The taxpayer replies to the SNOD with information to support deduction	You are able to verify that the taxpayer is entitled to part of the deduction claimed	Issue Letter 555 with a revised Form 4549 and an appropriate explanation to the taxpayer.
The taxpayer replies to the SNOD with verification of their deduction	You are able to determine that the taxpayer is not entitled to any part of the deduction	Issue Letter 555 with the latest Form 4549 and an appropriate explanation to the taxpayer.
The taxpayer replies to the SNOD with verification of their deduction	You are able to determine the deduction amount belongs on another line	Issue Letter 555 with a revised Form 4549 and an appropriate explanation to the taxpayer. Do not increase the deficiency as shown on the SNOD.

4.19.15.31
(02-01-2022)

**Form 1040, Schedule C -
Correspondence
Examination**

- (1) The Form 1040, *Schedule C*, Profit or Loss From Business (Sole Proprietorship), is used to report the profit or loss for a business operating as a sole proprietorship. The nature of the business can be a manufacturer of a product/goods, retail and wholesale sales, or provider of a service. A taxpayer can be involved in more than one business venture. A separate Schedule C is required for each type of business.
- (2) Each type of business has certain characteristics. For example, a manufacturing activity will have costs for materials and labor included in the costs of goods sold. On the other hand, a sales-oriented activity will normally only include the cost of items for resale in their cost of goods; the labor for sales would be included in the wages as an expense of sales. Finally, a service-oriented activity will normally have no cost of goods, unless materials and supplies are sold or charged in the business.
- (3) Because the taxpayers are not accountable to anyone as sole proprietors there are opportunities for them to mix personal and business interests in the pursuit of their trade or business. It is incumbent on the examiner to recognize those instances where personal expenditures are being deducted as business expenses and to make the proper adjustments to the taxpayer's return.
- (4) If the verified expenses are determined to be personal expenses and are deductible on the Schedule A, the examiner should make the proper adjustments to the taxpayer's return.
- (5) To be deductible as a business expense, the expenditure must be reasonable, ordinary and necessary during the course of the business, and be related to the business. The objective of any correspondence examination related to a sole proprietorship is to verify the amount of the expenditures, determine if

they qualify as business expenses, and that they were properly treated on the return. Correspondence examinations are limited in scope to certain line items to determine their deductibility as business expenses.

- (6) Business expenses are the costs of carrying on a trade or business, and they are usually deductible if the business is operated to make a profit. In determining whether a taxpayer is carrying on an activity for profit, nine factors are considered. No one factor alone is decisive. **The issue of whether the taxpayer is carrying on an activity for profit isn't conducive to Correspondence Examination and should not be used to disallow the taxpayer's Schedule C expenses.**
- (7) *Schedule C-4, General Questionnaire*, is sent with Letter 566-S/566-T for TDC cases, Initial Contact Letter, when Schedule C Expenses are being examined to determine the type of business involved, location, records available, ownership and how the business expenses are paid.
- (8) When the taxpayer is being examined for the income reported on Schedule C, Form 11652, Questionnaire- Form 1040 Schedule C (Profit or Loss From Business), will be sent as an enclosure with the Letter 566-S/Letter 566-T for TDC cases, Initial Contact Letter. See IRM 4.19.14.6.3, EITC Schedule C Responses, for guidelines that apply to Schedule C responses for, Project Code 0288.

4.19.15.31.1
(11-04-2019)
Sharing Economy Tax Center

- (1) An emerging area of activity in the past few years, the sharing economy, has changed how people commute, travel, rent vacation accommodations and perform many other activities. Also referred to as the on-demand, gig or access economy, the sharing economy allows individuals and groups to utilize technology advancements to arrange transactions to generate revenue from assets they possess - (such as cars and homes) - or services they provide - (such as household chores or technology services). Although this is a developing area of the economy, there are tax implications for the companies that provide the services and the individuals who perform the services. Refer to *Sharing Economy Tax Center* on irs.gov for guidance on tax issues that may apply to those participating in the sharing economy.

4.19.15.31.2
(02-01-2022)
Schedule C - Car and Truck Expenses

- (1) For a sole proprietorship, the car and truck expenses must be ordinary and necessary, and paid or incurred in the carrying on of a trade or business. A taxpayer may use the standard mileage rate or actual expenses for car and truck expenses, but not both. When using the standard mileage rate, the taxpayer must show by diary, log, or other means how many business miles and total miles were driven in a tax year. If the taxpayer is claiming actual expenses, records must be maintained to establish all the costs associated with the operation and maintenance of the vehicles as well as documentation to support the computation of the business use percentage. In addition, if the business use percentage is not greater than 50 percent there may be limitations imposed on certain expenses. Special rules apply for leased vehicles. Examiners must comment on personal usage of the vehicles in the workpapers. See Pub 463, Travel, Gift, and Car Expenses.
- (2) *Form 886-A Schedule C-5, Car and Truck Expenses*, which includes the Schedule C-5 Car and Truck Expenses questionnaire, is sent with Letter 566-S/566-T to request substantiation documentation for car and truck expenses claimed on Schedule C.

4.19.15.31.3
(02-01-2022)
**Schedule C - Travel
Expenses**

- (1) For a sole proprietorship, the travel expenses must be ordinary and necessary expenses of traveling away from home in the pursuit of a trade or business. In addition, there are specific record keeping requirements for travel, expenses (IRC 274(d)). For all travel expenses, taxpayer must provide information to support the location, dates, business purpose, and who they met with along with the required receipts for the deductions claimed. See Pub 463, Travel Gift and Car Expenses.
- (2) It is imperative that the examiner establish the taxpayer's "tax home" in order to accurately determine the eligibility of the amounts deducted as "away from home" expenses. See Chapter 1 of Pub 463, Travel, Gift, and Car Expenses. The examiner must also determine whether the nature of the travel is temporary (generally, lasting less than one year) or indefinite. If it is determined that a trip qualifies as business travel, all the associated costs (airfare, rail fare, bus fare, lodging, meals, taxis, etc.) are also deductible. However, if the taxpayer is accompanied by a spouse, other family member or relative, the expenses for that person are considered nondeductible personal expenses unless they are performing bona fide business services.
- (3) Special allocations are required if a taxpayer is mixing personal and business activities on any given trip. For tax years prior to 2018, *Form 886-A Schedule C-7, Travel, Meals and Entertainment Expenses*, including on page 2a, Schedule C, Travel, Meals and Entertainment Expense Questionnaire, will be sent to request substantiation documentation for travel, meals and entertainment expenses claimed on Schedule C.

4.19.15.31.3.1
(02-01-2022)
**Schedule C - Meals and
Entertainment Expenses
for TY 2018-2025**

- (1) For expenses paid or incurred after December 2017, the tax law has changed due to the Tax Cuts and Jobs Act (TCJA) of 2017. Traditionally, meals and entertainment expenses have followed the same set of rules. **For expenses after December 31, 2017, meals are now treated differently from entertainment expenses.** For TY 2018-2025, Form 15500, Substantiation Documentation Needed from Taxpayer for Travel and Meal Expenses Claimed on Schedule C, will be sent to request substantiation documentation for travel and meal expenses claimed on Schedule C, and will include on page 2a, Travel and meal Expenses Questionnaire.

Note: TCJA removed substantiation requirements of Treas. Reg. section 1.274-(d) for entertainment and meal expenses (paid or incurred after December 31, 2017), unless the meals are purchased separately from the entertainment or the cost of the meal is stated separately from the cost of the entertainment on the bill, invoice, or receipt. See Treas. Reg. section 1.274-11(b)(1)(ii). However, business travel meals are still subject to the Treas. Reg. section 1.274-(d) substantiation requirements. See Treas. Reg. section 1.274-(d)(1).

- (2) Entertainment includes any activity considered to provide entertainment, amusement, or recreation. Generally, entertainment expenses are non-deductible for expenses paid after December 31, 2017. Facilities used in connection with entertainment and related membership dues (such as country club dues) are also non-deductible. Meal expenses are limited to 50 percent unless an exception applies. (See Pub 463, Travel Gifts and Car Expenses, for a list of exceptions.)

Note: Amounts paid or incurred in tax years 2021 and 2022, for food and beverages provided by a restaurant are 100% deductible. See Treas. Reg. section 1.274-(n)(2)(D) and *Notice 2021-25*.

Note: If food or beverages are provided during or at an entertainment event, and the food and beverages were purchased separately from the entertainment or the cost of the food and beverages was stated separately from the cost of the entertainment on one or more bills, invoices, or receipts, a taxpayer may be able to deduct the separately stated costs as a business meal expense. For more information, see Treas. Reg. section 1.274-11,-12.

- (3) Examples for TY 2018-2025: For each example, assume that the food and beverage expenses are ordinary and necessary expenses under IRC 162(a) paid or incurred during the taxable year in carrying on a trade or business and are not lavish or extravagant under the circumstances. Also assume that the taxpayer and the business contact are not engaged in a trade or business that has any relation to the entertainment activity.

Example: 1. (i) Taxpayer A invites B, a business contact, to a baseball game. A purchases tickets for A and B to attend the game. While at the game, A buys hot dogs and drinks for A and B. (ii) The baseball game is entertainment as defined in Treas. Reg. section 1.274-2(b)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by A. The cost of the hot dogs and drinks, which are purchased separately from the game tickets, is not an entertainment expense and is not subject to the Treas. Reg. section 1.274-(a)(1) disallowance. Therefore, A may deduct 50 percent of the expenses (100 percent for tax years 2021 and 2022) associated with the hot dogs and drinks purchased at the game.

Example: 2. (i) Taxpayer C invites D, a business contact, to a basketball game. C purchases tickets for C and D to attend the game in a suite, where they have access to food and beverages. The cost of the basketball game tickets, as stated on the invoice, includes the food and beverages. (ii) The basketball game is entertainment as defined in Treas. Reg. section 1.274-2(b)(1)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by C. The cost of the food and beverages, which are not purchased separately from the game tickets, is not stated separately on the invoice. Thus, the cost of the food and beverages also is an entertainment expense that is subject to the Treas. Reg. section 1.274-(a)(1) disallowance. Therefore, C cannot deduct any of the expenses associated with the basketball game.

4.19.15.31.4
(03-11-2019)
**Schedule C - Mortgage
Interest**

- (1) Mortgage interest deducted on a Schedule C should be directly related to a business asset. If the taxpayer is using a structure for both business and personal activities, an allocation must be computed to properly reflect the amount attributable to the business. If an adjustment is made to remove a portion of the mortgage interest because it is deemed to be a personal expense, the examiner must consider whether it may still be deductible as an itemized deduction on the Schedule A.
- (2) *Form 886-A Schedule C-3, Interest*, will be sent to request substantiation documentation for interest expenses claimed on Schedule C.

4.19.15.31.5
(02-01-2022)

Schedule C - Legal and Professional Fees

- (1) Amounts paid to attorneys, accountants, appraisers, engineers, etc., for services related to the operation of a business are deductible as business expenses. Amounts paid for wills, estates, divorce and tax preparation fees (except for business returns such as Forms 941 and 940) are personal expenses and should not be deducted as a business expense (however, if they qualify as a personal expense the proper adjustment must be considered). The costs of defending an action in criminal court are not deductible as a business expense unless the charges are attributable to the taxpayer's trade or business, see Pub 529 Miscellaneous Deductions. Expenses incurred before the business commences are considered start-up or getting ready expenses and are not currently deductible (these expenses may be capitalized and amortized if the taxpayer makes a proper election). Illegal payments (bribes, kickbacks, etc.) are not deductible as business expenses. Expenses related to the acquisition of real estate, or a capital asset should be added to the basis of that asset and depreciated. Legal or professional fees incurred in the process of acquiring, creating, or enhancing intangible property should be capitalized and amortized. Fees incurred in defending or perfecting title to real property, tangible personal property, and intangible property, such as a patent should be capitalized and depreciated or amortized. The examiner should seek technical assistance if the issue of capitalization and depreciation is being considered.
- (2) *Form 886-A Schedule C-2*, Legal and Professional Fees, will be sent to request substantiation documentation for legal and professional fees claimed on Schedule C.

4.19.15.31.6
(02-01-2022)

Schedule C - Repairs and Maintenance

- (1) Expenses incurred to repair or maintain equipment and property used in carrying on a trade or business are generally deductible as business expenses. However, if the taxpayer pays or incurs amounts for the improvement of tangible real or personal property, these costs are generally treated as capital expenditures and depreciated over the appropriate recovery period. Amounts are treated as improvements if they are for betterments to tangible property, for replacements of tangible property, or for adapting tangible property to a new or different use. If the taxpayer determines the expenditures are for an improvement, then the taxpayer may still be entitled to a deduction if these expenditures are for the recurring activities that the taxpayer expects to perform to keep the property in an ordinarily efficient operating condition. For example, deductible repairs may include repainting exteriors and interiors of business buildings, repairing broken windowpanes, replacing worn-out minor parts, sealing cracks and leaks, and changing oil or other fluids to maintain business equipment.
- (2) See Treas. Reg. 1.263(a)-3, for additional information on the definition of improvement and exceptions to the improvement rules. Examiners should review receipts and invoices to identify the property that was repaired or improved and to determine the nature of the work done on the property. Examiners should further consider whether these expenditures were for improvements or other capital expenditures. Examiners should seek technical assistance if they are considering an adjustment to capitalize and depreciate any given repair or maintenance expense.
- (3) *Form 886-A - Schedule C - Repairs and Maintenance*, and Schedule C - Repairs and Maintenance Questionnaire, will be sent with Letter 566-S/566-T to request substantiation documentation for repairs and maintenance expenses claimed on Schedule C.

4.19.15.31.7
(06-14-2023)

Schedule C - Insurance

- (1) Generally, the cost of insurance that is ordinary and necessary for a trade, business, or profession is deductible as a business expense.
- (2) Amounts paid for medical and dental insurance and qualified long-term care insurance, may be deducted for the taxpayer, their spouse, and their dependents. See also IRM 4.19.15.30, Self-Employed Health Insurance Deduction – IRC 162(l) for additional information.
- (3) Form 14991, Schedule C-8 Insurance Expense Explanation of Items will be sent to request substantiation of the amount claimed as an Insurance expense on Schedule C.
- (4) For further information regarding insurance as a business deduction, refer to Pub 535, Business Expenses, Chapter 6, and Pub 334, Tax Guide for Small Business, Chapter 8.

4.19.15.31.8
(06-14-2023)

Schedule C - Utilities

- (1) Expenses paid for heat, lights, power, telephone service, water, and sewerage are deductible. However, any part attributed to personal use is not deductible.
- (2) Form 14993, Schedule C-10 Utilities Explanation of Items, will be sent to request substantiation of the amount claimed for utilities, related to the taxpayer's trade or business, on Schedule C.
- (3) Refer to Pub 535.

4.19.15.31.9
(06-14-2023)

Schedule C - Office Expenses

- (1) Form 14992, Schedule C-9 - Office Expenses Explanation of Items, will be sent to request substantiation of the amount claimed for office supplies and postage expenses, related to the taxpayer's trade or business, on Schedule C.

4.19.15.31.10
(06-14-2023)

Excess Business Losses for TY 2021 - TY 2026

- (1) The Tax Cuts and Jobs Act of 2017 limited the amount of losses from the trades or businesses of non-corporate taxpayers that can be claimed each year. For tax years 2018-2028, taxpayers cannot deduct an excess business loss in the current year. However, the excess business loss is treated as a net operating loss (NOL) carryover. Form 461, Limitation on Business Loss, is used by non-corporate taxpayers whose net losses from all of their trades or businesses are more than \$250,000 (\$500,000 for married taxpayers filing a joint return.) See Form 461 for instructions and details.

Note: The limitation established by the Tax Cuts and Jobs Act of 2017 was amended by The Coronavirus Aid, Relief, and Economic Security (CARES) Act. The CARES Act repealed the limitation for tax years 2018, 2019, and 2020. If the taxpayer already filed returns with the limitation, they are able to file an amended return. Pub. L. 117-169, Sec 13903(b)(1) extended the excess business losses to January 1, 2029.

4.19.15.31.11
(11-04-2019)

Schedule C Referrals from the Social Security Administration

- (1) When the Social Security Administration (SSA) determines during an investigation that a taxpayer's self-employment earnings have been omitted or incorrectly reported on Form 1040, the IRS is notified via a Self-Employment Determination Posting Record (SE-DPR).
- (2) These referrals are worked in Project Code (PC) 1502 and include cases that contain questionable Schedule C income and refundable credits. There are three potential issues:

- a. Schedule C
- b. Filing status
- c. Dependents.

- (3) All credits will be worked as statutory issues and adjusted based on changes to the three classified issues.
- (4) Since the focus of a PC 1502 examination is to determine if the taxpayer had self-employment income, Schedule C net profit is questioned. Form 11652, Questionnaire - Form 1040 Schedule C, is sent with the Initial Contact Letter.
- (5) The Earned Income Tax Credit (EITC) is a statutory change only. Based on the facts of the case, consider if a two-year ban is applicable. See IRM 4.19.14.7.1, 2/10 Year Ban - Correspondence Guidelines for Examination Technicians (CET).
- (6) If SSA Form 795, Statement of Claimant or Other Person, SSA Form 7008, Request for Correction of Earnings Record, or similar statement is received from the taxpayer/rep, contact your Campus Fraud Coordinator (CFC) for guidance on a referral to fraud. See IRM 4.19.10.4, Fraud Referrals.
- (7) Subsequent year pick up returns are opened with Tracking Code (TC) 0900. Research the prior and subsequent year patterns and if the same issues are present or a pattern of abuse is noted, strongly consider imposing a 2-year ban or make a referral to your CFC.

4.19.15.31.12
(02-01-2022)

**Project Code 0288,
Questionable Schedule
C with EITC**

- (1) The focus of PC 0288, Questionable Schedule C with EITC, is to determine if the taxpayer had self-employment income. These are single issue cases where only Schedule C net profit is questioned.
- (2) When the taxpayer is being examined for the income reported on Schedule C, Form 11652, Questionnaire - Form 1040 Schedule C (Profit or Loss From Business), will be sent as an enclosure with the Letter 566-S/Letter 566-T for TDC cases, Initial Contact Letter.
- (3) See IRM 4.19.14.6.3, EITC Schedule C Responses, for guidelines that apply to Schedule C responses for PC 0288.
- (4) EITC is a statutory change only for cases in PC 0288. The taxpayer must have earned income to claim EITC. If the decision is made to remove the self-employment income, **applying the 2-year EITC ban needs to be considered based on the facts of the case.** Follow the guidance in IRM 4.19.14.7.1, 2/10-year ban - Correspondence Guidelines for Examination Technicians. Managerial approval is required for all 2/10-year ban cases.

Note: If the PC 0288 case has an AIMS Tracking Code 0649, the EITC 2-year ban was applied at case selection because it is the third year the case has been selected, and the taxpayer has claimed EITC after it was disallowed in two prior years. If the taxpayer responds, make the determination to leave the ban or remove the ban with managerial approval.

- (5) The Consolidated Appropriations Act allows the taxpayer to use Prior Year Earned Income (PYEI), to compute their EITC and ACTC on their 2020 return.
- (6) The American Rescue Plan Act allows the taxpayer to elect to use PYEI, from their 2019 tax return, to compute their EITC on their 2021 return.

(7) Use the table below when evaluating taxpayer's responses regarding PYEI:

Tax year	Mail submitted	Action to take
2020 with tracking code 0900 or 0649	Request to use PYEI to calculate credits	<p>Verify if a reconsideration was completed to reverse the examination results. If yes, update the Per Exam amount in the RGS PYEI credit issues with the allowed PYEI amount. If no reconsideration completed or determination remained unchanged, explain what the taxpayer must provide for resolution</p> <p>Note: If the taxpayer submits information for reconsideration of the 2019 income, evaluate the response and if accepted, both tax years 2019 and 2020 should be adjusted accordingly.</p>
2020 without tracking code 0900 or 0649	Request to use PYEI to calculate credits	Allow the election and make the appropriate adjustments to issues.

4.19.15.32
(02-01-2022)
**Return Preparer
Analysis Tool (RPAT)
Program**

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- (7) Programming has been established through DDb to identify each scheme and related taxpayers so that the examination results can be queried at the HQ level by the Scheme Identification Numbers and Project Codes.

4.19.15.33
(06-14-2023)
**CI Education Credit
Program**

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(3) AIMS Openings:

- Project Code (PC) 0133, Source Code 70
Note: For projects with egregious deductions/credits claimed but not related to a specific preparer use PC 0385.
- An AIMS Tracking Code will be used if applicable.

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(4) Procedures for processing the inventory:

- For Return Preparer Investigations, issue audit letters and follow the examination and closing procedures as specified under PC 0133. See IRM 4.19.15.25, Return Preparer Referrals.
- Document the workpapers, with any statements provided/made by the taxpayer.
- For projects with egregious Sch A and Education credit issues not related to a return preparer investigation, follow the directions specified under PC 0385. Refer to IRM 4.19.15.20, Schedule A . IRM 4.19.15.3, Education Tax Credits - General Requirements and Exam Programs, IRM 20.1, Penalty Handbook, IRM 4.19.13.28, Campus Exam Identity Theft, and other IRM sections as applicable.

- (5) Effective for tax years after 2015, if the taxpayer's claim for AOTC is due to reckless or intentional disregard of rules and regulations, a 2-year ban may apply. If the claim is fraudulent, a 10-year ban may apply. The 2 and 10-year bans do not apply to the Lifetime Learning Credit or the tuition and fees deduction. See IRC 25A(i)(7), and IRM 4.19.14.7.1, 2/10 Year Ban - Correspondence Guidelines for Examination Technicians.

4.19.15.34 (02-01-2022) Child Tax Credit (CTC), Additional Child Tax Credit (ACTC), Refundable Child Tax Credit, and Credit for Other Dependents (ODC)	(1) For specific eligibility requirements, see IRM 4.19.14.12.1, Overview - CTC, ACTC, Refundable CTC and ODC. Note: Information for Individual Taxpayer Identification Number (ITIN) has been moved to IRM 4.19.14.12.5, What is an ITIN?, and IRM 4.19.14.12.8, Date of Attainment.
4.19.15.34.1 (02-01-2022) Programs and Initial Contacts	(2) Additional issues can include the ODC, Earned Income Tax Credit (EITC), American Opportunity Tax Credit (AOTC), Head of Household (HOH) filing status or other related issues. The Project Codes (PCs) are:

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SB/SE Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
0555	Child Tax Credit, Qualifying Child SSN Citizenship Code <> (not) A or B	<p>Taxpayers claimed Child Tax Credit (CTC) for a qualifying child (QC) with a citizenship code that was not an A or B. Citizenship Codes identify the child's citizenship and are located on IDRS CC DDBKD. Values are:</p> <ul style="list-style-type: none"> • A - U.S. Citizen • B - Alien allowed to work • C - Alien not allowed to work • D - Other Alien • E - Alien student • F - Conditionally legalized alien, status not known. 	<p>Issue Letter 566-S or Letter 566-T (for TDC cases) along with Form 14815 Supporting Documents to Prove the Child Tax Credit and Credit for Other Dependents for 2018-2020/Form 14815-A Supporting Documents to Prove the Child Tax Credit and Credit for Other Dependents for 2021.</p>

SB/SE Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
0056	Credit for Other Dependents (ODC)	Taxpayers who claimed the Credit for Other Dependents (ODC) for three or more qualify- ing dependents (QD). ODC QD is an ITIN, filed a return, and/or is a DUPTIN.	Issue Letter 566-S or Letter 566-T (for TDC cases) along with Form 14815 Support- ing Documents to Prove the Child Tax Credit and Credit for Other Depen- dents for 2018- 2020/Form 14815-A Sup- porting Documents to Prove the Child Tax Credit and Credit for Other Dependents for 2021.

TS Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
1179	Additional Child Tax Credit (ACTC)	<ul style="list-style-type: none"> Original returns or claims for refund (Forms 1040-X) claiming Additional Child Tax Credit (ACTC). Taxpayers claimed the credit for individuals who may not be the taxpayer's dependents, may not meet the U.S. citizen or resident requirement, or (for CTC/ACTC after 2017) don't have the required SSN (valid for employment), or citizenship code is not A or B. The return can have other related issues. 	<p>Letter 566-S will be issued via the filer bridge, and claims will be initiated using the Letter 566-D, along with Form 14815, Supporting Documents to Prove the Child tax Credit (CTC) and Credit for Other Dependents (ODC) for 2018-2020/Form 14815-A, Supporting Documents to Prove the Child Tax Credit (CTC) and Credit for Other Dependents (ODC) for 2021</p> <p>Note: For tax years prior to 2018, Form 14800, Child Tax Credit and Additional Child Tax Credit - Explanation of Items, is sent with the ICL. Send Form 886-H-DEP when Form 14800 is used.</p>

TS Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
1334	Refundable Child Tax Credit	<p>Original returns or claims for refund (Forms 1040-X) for tax year 2021 claiming questionable Refundable CTC for individuals who:</p> <ul style="list-style-type: none"> • may not be the taxpayer's dependents, • may not meet the US citizen or resident requirement or don't have the required SSN (valid for employment) or citizenship code is not A or B, • or the taxpayer's principal place of abode may not have been in the U.S. for more than half the year. 	<p>Letter 566-S will be issued via the filer bridge, and claims will be initiated using the Letter 566-D, along with Form 14815-A, Supporting Documents to Prove the Child Tax Credit (CTC) and Credit for Other Dependents (ODC) for 2021</p> <p>Note: Do not use Form 886-H-DEP when Form 14815-A is used.</p>

TS Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
1335	Refundable Child Tax Credit Recertification	<p>Tax year 2021 original returns or claims for refund (Forms 1040-X) claiming refundable Child Tax Credit when subject to ACTC recertification. The credit may have been claimed for individuals who:</p> <ul style="list-style-type: none">• may not be the taxpayer's dependents,• may not meet the U.S. citizen or resident requirement or• don't have the required SSN (valid for employment), or• for taxpayers whose principal place of abode may not have been in the U.S. for more than half the year.	Letter 566-S will be issued via the filer bridge, and claims will be initiated using the "566-D", along with Form 14815-A, Supporting Documents to Prove the Child Tax Credit (CTC) and Credit for Other Dependents (ODC) for 2021

TS Project Codes	Project Code Title	Project Code Descriptions	Initial Contact Letter
1516	Additional Child Tax Credit Recertification (Non-ITIN)	<ul style="list-style-type: none"> Original returns or claims for refund (Forms 1040-X) claiming Additional Child Tax Credit (ACTC) when subject to ACTC recertification. Taxpayers claimed the credit for individuals who may not be the taxpayer's dependents, may not meet the U.S. citizen or resident requirement, or (for CTC/ACTC after 2017) don't have the required SSN (valid for employment), or citizenship code is not A or B. The return can have other related issues. 	<ul style="list-style-type: none"> For 2018-2020 returns, Form 14815, Supporting Documents to Prove the Child Tax Credit (CTC) and Credit for Other Dependents (ODC) for 2018-2020, is sent with the ICL. For 2021 returns, Form 14815-A, Supporting Documents to Prove the Child Tax Credit (CTC) and Credit for Other Dependents (ODC) for 2021, is sent with the ICL. Do not send Form 886-H-DEP when Form 14815 or Form 14815-A is used. For tax years prior to 2018, Form 14800, Child Tax Credit and Additional Child Tax Credit - Explanation of Items, is sent with the ICL. Send Form 886-H-DEP when Form 14800 is used.

- (3) In general, issues are systemically identified and initial contact letters are automated. For manual initiations, after completing research to determine the issues for examination, initiate cases with Letter 566-S/566-T for TDC cases, Initial contact Letter. Use the check boxes to identify the issues in question. If other issues not shown on Form 14815 /Form 14815-A are selected for examination, use additional forms to request needed documentation. Follow the procedures in IRM 4.19.13, General Case Development and Resolution, and IRM 4.19.14.12 , Child Tax Credits.

4.19.15.34.1.1
(10-16-2024)

**Individual Taxpayer
Identification Number
(ITIN) ACTC**

- (2) Additional issues can include the AOTC, HOH filing status, Child and Dependent Care Credit (CDCC), Federal Income Tax Withholding (FITW), and EITC and ACTC claimed for dependents with SSNs or other related issues. The Project Codes (PCs) are:

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PC	Issues
0900	ITIN ACTC and other issues
1518	ITIN ACTC recertification and other issues
1175	ITIN ACTC preparer/promoter scheme

- (3) In general, issues are systemically identified and initial contact letters are automated. For manual initiations, after completing research to determine the issues for examination, initiate PC 0900 and 1518 cases with Letter 566-S/ 566-T for TDC cases, Initial Contact Letter, and initiate PC 1175 cases with Letter 566-B/ Letter 566-J for TDC cases, ICL 30-Day Combo. Use the check boxes to identify the issues in question. Include Form 886-H-ITIN, Dependent-Related Tax Benefits and Credits - Explanation of Items, when requesting documentation for the selected issued. Form 886-H-ITIN (SP) is available in Spanish. If other issues not shown on Form 886-H-ITIN are identified for examination, use additional forms to request needed documentation. PCs 0900 and 1518 can also be used with claims for refund. Follow procedures in IRM 4.19.13, General Case Development and Resolution, IRM 4.19.14.12, Child Tax Credits, and the ITIN-specific guidance in IRM 4.19.15.34.1.1.1, ITIN ACTC - Acceptable Documentation.

4.19.15.34.1.1.1
(02-01-2022)

ITIN ACTC - Acceptable Documentation

- (1) The table below states, in general, what documentation may verify specific requirements for ITIN ACTC cases for tax years prior to 2018. For Additional information regarding acceptable documentation, refer to:
- IRM 4.19.14.6.4, EITC - Filing Status
 - IRM 4.19.14.6.5, EITC - Personal Exemptions and Dependents
 - IRM 4.19.14.12, Child Tax Credits
 - IRM 4.19.15.3, Education Tax Benefits - General Requirements and Exam Programs

Issue	Documents
Child Tax Credit and Additional Child Tax Credit (tax years prior to 2018)	The qualifying child must be a United States (US) citizen, US national or US resident alien. See IRM 4.19.14.12.4, US Resident Alien, and IRM 4.19.14.12.9, Requirements for CTC/ACTC for Tax Years Prior to 2018.
Filing Status	

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Issue	Documents
Federal Income Tax Withheld	
Income	

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Issue	Documents
Education Credit	<p>All verification rules to determine allowable expenses and eligible educational institutions apply. To see if the school is eligible, check the <i>U.S. Department of Education's (USDOE) list of Accredited Schools</i>. Some schools located outside the U.S. also participate in the USDOE's Federal Student Aid programs but are not on the list. If the school is not on the list, the taxpayer must prove the foreign school is an eligible educational institution. An eligible educational institution is an accredited school that offers higher education beyond high school and that is eligible to participate in the student aid program run by the USDOE. For more information refer to IRM 4.19.15.3, Education Tax Benefits - General Requirements and Exam Programs, and Pub 970, Tax Benefits for Education.</p> <p>Note: If an RA taxpayer is married to an NRA spouse, no credit is allowed unless an election to file jointly is made.</p>

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4.19.15.34.2
(05-28-2019)
ITIN and Employment-Related Identity Theft

- (1) IRM 25.23.1.3.1, Identity Theft in Tax Administration, describes employment-related and income-related identity theft. When information from the ITIN taxpayer's examination indicates that another individual's SSN has been used for employment purposes, follow guidance in IRM 25.23.2.4.4, Initial Allegation or Suspicion of Tax-Related Identity Theft - IMF Identity Theft Indicators, paragraph (7), and IRM 25.23.2.8.5, Employment-related Identity Theft - TC 971 AC 525.

4.19.15.35
(01-01-2014)
Conversion of Invalid Form 1120S Cases - Background

- (1) Form 1120-S tax returns filed by a corporation as a Subchapter S Corporation (1120S Corporation) are converted to a Form 1120, Subchapter C Corporation, if the corporation failed to file an election Form 2553, Election by a Small Business Corporation, filed an invalid election, or had its status as a Subchapter S Corporation terminated.
 - a. An 1120S corporation is generally a non-taxable entity whose income flows through via *Schedule K-1*, Partner's Share of Income, Deductions, Credits, etc. to the shareholder to be taxed on the shareholder's return. One tax advantage to an 1120S Shareholder is when the corporation has a loss (subject to loss limitation rules), the shareholder can report that loss on their own return (e.g., Form 1040), reducing the taxable income and tax. When an 1120S corporation is converted to an 1120 corporation, the shareholder can no longer report these flow-through items. For example, if the 1120S corporation had reported a loss, the 1040 shareholder is no longer able to claim that loss on *Schedule E*, Supplemental Income and Loss. The 1120 corporation is not impacted in this example because it has a loss and is unlikely to owe tax.
- (2) If the 1120S return is converted to an 1120 return subsequent to the shareholders filing their own returns, compliance action may be required to make the appropriate changes.

4.19.15.35.1
(01-01-2014)
**Identifying the Form
1120S Return to be
Examined**

- (1) Workload Selection and Delivery (WSD) will identify 1120S converted returns with characteristics meeting the Correspondence Examination criteria.
- (2) The identified returns will be further filtered to ensure there has been no subsequent activity which changes the need to examine the return.
- (3) Returns will be placed on AIMS with Project Code 0157 and assigned to a campus.
- (4) A spreadsheet showing the associated shareholder's returns will also be provided.

4.19.15.35.2
(01-01-2016)
**Examining the
Converted Form 1120S
Return and Adjusting
the Shareholders
Returns**

- a. The campus will be sent a spreadsheet identifying the shareholders and the amount of the flow through loss that is no longer includable on the return due to the conversion of the 1120S corporation.
 - b. The campus will issue an initial contact letter (combo) with a report disallowing the flow through loss shown on the spreadsheet.
 - c. If the taxpayer/shareholder does not respond, default procedures will be followed.
 - d. If the taxpayer/shareholder does respond, it will generally be similar to the following: "This business entity has always been treated as an 1120S corporation and every year the shareholders have reported their income from the entity on their individual returns". In their response, the corporation/shareholder might cite certain Revenue Procedures which allow the corporation/shareholder relief in this situation. The corporation/shareholder might cite Rev. Proc. 2003-43, Rev. Proc. 2004-48, Rev. Proc. 2007-62, Rev. Proc. 2013-30, or Rev. Proc. 97-48. If any of these Revenue Procedures are cited, please refer the request to the Entity section of your campus for action. Please ensure that Entity contacts you as soon as a decision is made. Most of the time the corporation/shareholder will contact the IRS before compliance action is taken. If Entity grants relief under any of these Revenue Procedures, the corporate return will be converted back to an 1120S corporation and the shareholder returns will be no-changed.
 - e. If Entity does not grant relief, follow normal closure practices.
- (2) **Gain Returns** - Only the corporation will be examined. The shareholders will be sent a letter advising them to submit an amended return to adjust the gain reported on their individual returns.
- a. The campus will be sent a spreadsheet identifying the corporation and the amount of gain that is now taxable due to the conversion of the 1120S.
 - b. The campus will issue an initial contact letter with a report to the corporation that includes the income previously passed through to the shareholders.
 - c. If the corporation does not respond, default procedures will be followed.
 - d. If the corporation does respond, it will generally be similar to the following, "This business entity has always been treated as an 1120S corporation and every year the shareholders have reported their income from the entity on their individual returns." In their response, the corporation/shareholder might cite certain Revenue Procedures which

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allow the corporation/shareholder relief in this situation. The corporation/shareholder might cite Rev. Proc. 97-48, Rev. Proc. 2003-43, Rev. Proc. 2004-48, or Rev. Proc. 2007-62, Rev. Proc. 2013-30 . If any of these Revenue Procedures are cited, please refer the request to the Entity section of your campus for action. Please ensure that Entity contacts you as soon as a decision is made. Most of the time the corporation/shareholder will contact the IRS before compliance action is taken. If Entity grants relief under any of these Revenue Procedures, the corporate return will be converted back to an 1120S corporation and the shareholder returns will be no-changed.

- e. If Entity does not grant relief, follow normal closure practices.
- f. When the corporate case is ready to close, issue the shareholders a letter notifying them that due to the conversion of the 1120S, the flow through income is no longer includable on their individual returns. Include an amended return (Form 1040-X).

4.19.15.36
(02-01-2022)

Moving Expenses – IRC 217

- (1) Exam cases involving moving expenses are worked under Project Code 0380 and Project Code 0419.
- (2) Issue Letter 566-S/Letter 566-T for TDC cases, with the appropriate box checked. See Form 14978 - Moving Expenses Deduction Supporting Documents, for documents request that may be used for this issue.
- (3) For tax years beginning 2018 through 2025, the deduction of moving expenses is not available for non-military taxpayers.
 - Determine if the taxpayer is a member of the Armed forces on active duty, whose move is due to a military order resulting in a permanent change to the taxpayer's duty station. See IRC 217(k) and (g)
- (4) To be eligible to deduct certain unreimbursed moving expenses, the taxpayer must be an active member of the military, whose move is due to a military order resulting in a permanent change to the member's duty station. Certain moving expenses of a member's spouse or dependent may also be deductible. See Pub 3, Armed Forces' Tax Guide, for details on what moving expenses qualify.

4.19.15.36.1
(03-14-2016)

**Evaluating Responses
Tax Years 2018-2025**

- (1) For tax years 2018 through 2025 the deduction of certain moving expenses is suspended for non-military taxpayers.
- (2) Must be an active member of the military and moving due to a permanent change of station.
- (3) Refer to Form 14978, Moving Expenses Deduction Supporting Documents to request appropriate supporting documentation.

4.19.15.36.2
(02-01-2022)

**Evaluating Responses
Tax Year 2017 and Prior**

- (1) Use the following guidelines when evaluating responses to Moving Expense deductions, for tax years prior to January 1, 2018.

- Determine if the move is job related. The move must be related both in time and in place, to the start of work at the **new job location**.

If	And	Then
The taxpayer provided information to show the move was related to the start of work at a new location	NA	The move was job related. Continue evaluating taxpayer response.
The taxpayer did not provide employer information and was not employed in the prior year, and had no <i>Schedule C</i> , partnership, or Form 1120-S income	The taxpayer has no employment in the year being examined	Disallow the moving expense because the move was not related to the start of work. Issue Letter 525/Letter 525-T for TDC cases, with a report.

4.19.15.36.2.1
(02-01-2022)
Distance Test

- (1) Determine if the taxpayer meets the **distance test**. The **new job location** must be at least 50 miles farther from the taxpayers old home than the old job location was from the taxpayer's old home, for tax years prior to January 1, 2018.
1. Determine the number of miles from the taxpayer's old home to their new workplace.
 2. Determine the number of miles from the taxpayer's old home to their old workplace.
 3. Subtract Step 2 from Step 1. The difference indicates the miles.

If	Then
The number of miles in Step 3 above is less than 50,	Disallow the moving expenses because the distance test was not met. Issue Letter 525/Letter 525-T for TDC cases, and report.
The number of miles in Step 3 above is 50 or more,	The distance test was met. Continue evaluating the taxpayer's response.

4.19.15.36.2.2
(10-16-2024)
Time Test

- (1) Determine if the taxpayer meets the **time test**. If the taxpayer is an employee, they must work full time for at least 39 weeks during the first 12 months after arriving in the general area of the new job location, for tax years prior to January 1, 2018.
- a. The taxpayer may count only full-time work as an employee, not any work as a self-employed person.
 - b. The taxpayer does not have to work for the same employer for all 39 weeks.
 - c. The taxpayer does not have to work 39 weeks in a row.
 - d. The taxpayer must work full time within the same general commuting area for all 39 weeks.

- (2) If the taxpayer is an employee or self-employed, they must work full time for at least 39 weeks during the first 12 months and for a total of at least 78 weeks during the first 24 months after arriving in the general area of the new job location.
 - a. The taxpayer may count any full-time work done either as an employee or as a self-employed person.
 - b. The taxpayer does not have to work for the same employer for all 78 weeks.
 - c. The taxpayer does not have to work 78 weeks in a row.
 - d. The taxpayer must work full time within the same general commuting area for all 78 weeks.
- (3) For tax years prior to January 1, 2018 if the taxpayer does not meet the time test, disallow the expenses and issue Letter 525/Letter 525-T for TDC cases, with a report. If the taxpayer meets the time test, continue evaluating the taxpayer's receipts, cancelled checks, etc., to determine allowable expenses.

Note: There are exceptions for the time test for members of the Armed Forces, and for retirees or survivors who moved to the United States, and in certain other situations.

4.19.15.36.3
(10-16-2024)
Additional Information

- (1) Additional information should be referenced when working moving expense cases. These include:
 - Form 3903, Moving Expenses
 - Pub 3, Armed Forces' Tax Guide
 - Pub 17, Your Federal Income Tax (For Individuals)

4.19.15.37
(02-01-2022)
Multiple Filers

- (1) A multiple filer situation occurs when the same TIN is used for a primary taxpayer on a non-joint return and for a secondary taxpayer on a joint return.
- (2) When this filing situation occurs, Masterfile will post the second return as outlined in IRM 21.6.7.4.5, Multiple Uses of Taxpayer Identification Numbers - TRNS36F (DUPTIN Filing Condition).
- (3) AM (Accounts Management) has contacted the common taxpayer with Letter 31-C, Duplicate Returns Filed; Explanation Requested, requesting information to resolve the situation. Cases not resolved by AM will be routed to Examination Classification.
- (4) When selected for Correspondence Exam, one return will be a joint return and the other return a non-joint return (Single, Head of Household or Married Filing Separate). Both the joint and non-joint returns will be opened in Source Code 04, Project Code 0982. The case file should contain the taxpayer's response to the Letter 31-C issued by AM, if the taxpayer responded, to assist with processing these cases. Cases selected for Correspondence Exam are accounts that could not be resolved by Accounts Management and require deficiency procedures to be followed.
- (5) Married taxpayers may file non-joint returns, such as married filing separately or head of household. If a taxpayer changes their filing status from Married Filing Joint (MFJ) or Married Filing Separate (MFS) to Single (S) or Head of

Household (HOH), the taxpayer **MUST** clearly be eligible, refer to Pub 501, Dependents, Standard Deduction, and Filing Information, and Pub 17, Your Federal Income Tax (For Individuals).

- (6) Cases should be worked together because responses may impact either case; however, if both taxpayers were contacted and there is sufficient documentation to close one of the cases that will have no impact on the other, it should be closed.
- (7) The inventory is centralized in Ogden and Brookhaven.
- (8) For possible return scenarios, refer to IRM 21.6.7.4.5, Multiple Uses of Taxpayer Identification Numbers - TRNS36F (DUPTIN Filing Condition).

4.19.15.37.1
(02-01-2022)
Scenarios and Contact Procedures

- (1) If a joint return is filed and a subsequent non-joint return is received before the due date, the subsequent non-joint return supersedes the joint return. The subsequent non-joint return is the return of record for the filer of the separate return. The correct information for the filer that did not file a superseding return will be determined by examination. Conduct IDRS research to determine which return was filed first. The following table describes the different scenarios that can occur when a return is selected by Classification and explains the appropriate issues to pursue for examination:

If	And	Then
Joint return followed by a non-joint return before the due date	DUP TIN taxpayer indicates they did not sign the joint return or signature was forged	Change FS on the joint return to MFS, remove spousal exemption, spouse's income, and duplicate dependents claimed on the separate return. Also remove all associated credits. Change the FS on the non-joint return when applicable. (ie. non-joint return was filed HOH from same address as the joint return was filed from)

If	And	Then
Joint return followed by a non-joint return before the due date	Taxpayer(s) indicate they were not married (divorce decree) or were never legally married, Invalid Joint election was made.	Change FS on the joint return to Single, remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated credits. Consider changes to non-joint return based on facts and circumstances and determine if issues will be pursued.
Joint return followed by a non-joint return before the due date	DUP TIN taxpayer indicates the joint return is valid	Combine the non-joint return with the joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/ withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.
Joint return followed by a non-joint return before the due date	No response,	Non-joint return is the return of record. Change FS on the joint return to MFS. When applicable, change the FS on the non-joint return to MFS as well. Consider all statutory adjustments that need to be made to the return according to the FS change.

If	And	Then
Non-joint return followed by a joint return before the due date of the return.	DUP TIN taxpayer indicates they did not sign the joint return or signature was forged	Non-joint return is the return of record. Change FS on the Joint return to MFS. When applicable, change the FS on the non-joint return to MFS as well. Consider all statutory adjustments that need to be made to the return according to the FS change.
Non-joint return followed by a joint return before the due date of the return.	Taxpayer(s) indicate they were not married (divorce decree) or were never legally married,	Non-joint return is the return of record. Change FS on the joint return to Single, remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated credits. Consider changes to non-joint return based on facts and circumstances and determine if issues will be pursued.
Non-joint return followed by a Joint return before the due date of the return.	DUP TIN taxpayer indicates the joint return is valid	Combine non-joint return with the joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/ withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.

If	And	Then
Non-joint return followed by a Joint return before the due date of the return.	No response,	Joint return is the return of record. Combine non-joint return with the Joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/ withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.

- (2) If a joint return is filed and a subsequent non-joint return is received after the due date, the subsequent non-joint return does not supersede the joint return. Conduct IDRS research to determine which return was filed first. The following table describes the different scenarios that a return is selected by Classification and explains the appropriate issues to pursue for examination:

If	And	Then
Joint return followed by a non-joint return after the due date	DUP TIN taxpayer indicates did not sign the joint return or signature was forged,	Non-joint return is the return of record. Change FS on the joint return to MFS remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated. When applicable, change the FS on the non-joint return to MFS as well. Consider all statutory adjustments that need to be made to the return(s) according to the FS change(s).

If	And	Then
Joint return followed by a non-joint return after the due date	Taxpayer(s) indicate they were not married (divorce decree) or were never legally married,	Non-joint return is the return of record. Change FS on the joint return to Single, remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated credits.
Joint return followed by a non-joint return after the due date	DUP TIN taxpayer indicates the joint return was valid, but they want to reverse the joint election (amend) to file a non-joint return	Joint return is the return of record. TP cannot elect to file a non-joint return after the due date. Combine non-joint return with the joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/ withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.
Joint return followed by a non-joint return after the due date	No response	Joint return is the return of record. TP cannot elect to file a non-joint return after the due date. Combine non-joint return with the Joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/ withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.

If	And	Then
Non-joint return followed by a joint return after the due date,	DUP TIN taxpayer indicates they did not sign the joint return or signature was forged,	Non-joint return is the return of record. Change FS on the joint return to MFS, remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated. When applicable, change the FS on the non-joint return to MFS as well. Consider all statutory adjustments that need to be made to the return according to the FS change.
Non-joint return followed by a joint return after the due date,	Taxpayer(s) indicate they were not married (divorce decree) or were never legally married,	Non-joint return is the return of record. Change FS on the joint return to Single, remove spousal exemption, spouse's income, and duplicate dependents claimed on the non-joint return. Also remove all associated.
Non-joint return followed by a joint return after the due date,	No response,	Joint return is the return of record. Combine non-joint return with the joint return. Compare the data on the non-joint (FS 1/3/4) return to the joint return to verify income/withholding is reported. Follow Separate to Joint procedures. Non-joint return will be backed out at closing.

- (3) Issue Letter 566-S and identify all applicable issues per the Form 6754, Examination Classification Checksheet.

Note: If combining the non-joint return to the joint return, the ICL should be sent to each taxpayer's address of record.

- (4) If no response to the Letter 566-S or the information submitted is not sufficient to change the determination, issue the appropriate 30-day letter with Form 4549 Income Tax Examination Changes Report to reflect the proposed changes;
 - Issue Letter 545 if proposed change to joint and/or non-joint return is to MFS.
 - Issue Letter 539 if proposed change is to combine non-joint return to the joint return.
 - Issue Letter 525 if proposed change to joint or non-joint return is to Single.

Note: If combining the non-joint return to the joint return, the 30-day letter should be sent to each taxpayer's address of record.

4.19.15.37.2
(02-01-2022)

Non-Joint Return is Valid or Considered the Return of Record - Remove Secondary from Joint Return

- (1) If income reported on the joint return belongs to the non-joint return, remove the income and adjust the tax/credits accordingly.
- (2) If the primary taxpayer on the joint return responds stating the joint return is valid, then request the primary taxpayer provide a notarized statement from the secondary taxpayer. The statement should explain why both returns were filed and indicate the joint filed return is valid.
- (3) If a non-joint return is filed after the due date of the return, and it is determined the joint return was not signed by the non-joint/secondary taxpayer, see IRM 4.19.11.5.9, Unlawful Returns - Joint Filed Returns.
- (4) If the non-joint return filer is not contacted by Exam, retain the two cases together and upon closing, survey the non-joint return using DC (Disposal Code) 32.
- (5) When changing FS to MFS, if one itemizes, both must itemize. Address on both the joint and non-joint returns when applicable.
- (6) If unable to determine entitlement for duplicate dependency exemptions, disallow on both returns until verification of entitlement is received.

4.19.15.37.3
(02-01-2022)

Joint Return is valid or Considered the Return of Record - Combine Non-Joint to the Joint Return

- (1) Disclosure of returns is subject to the disclosure rules under section 6103. If a joint return is filed, both spouses to whom the return relates are entitled to access the return. In the case of a return of an individual, however, only that individual can generally obtain a copy of the return. See IRC 6103(e)(1) and/or IRM 11.3.2.4, Persons Who May Have Access to Returns and Return Information Pursuant to IRC 6103(e).
- (2) Ensure all income reported on the non-joint return is added to the joint return and adjust the tax/credits accordingly.
- (3) Non-joint return will remain in Status 08 until joint return is closed.
- (4) Upon closing the joint return, complete the non-joint back-out using Form 5344. Use Disposal Code 08 on Form 5344 to close/back-out the non-joint return.

Caution: Care must be taken when processing statute year returns to prevent erroneous abatements. The filing of a married filing joint return subsequent to non-joint return(s) may affect the Assessment Statute Expiration Date (ASED). The IRS will have at least one year from the actual filing of a married filing joint return to make an assessment, IRC IRC 6013(b)(4). It is extremely important that you carefully review for the Assessment Statute Expiration Date (ASED), and the Refund Statute Expiration Date (RSED). Refer to IRM 25.6.1, Statute of Limitations Processes and Procedures, for additional information. For Reconsiderations; refer to the following IRMs when Correspondence Exam has combined the non-joint return to the joint return and the non-joint filer provides information after the case has closed, indicating the joint return was not valid:

- IRM 25.15.19.2.4, Joint Returns - Invalidated
- IRM 25.15.19.2.4.2, Determining if Joint Election is Valid, and
- IRM 25.15.19.2.4.3, Joint Election is Invalid

Note: Each situation is different and all scenarios cannot be addressed in the IRM. All accounts should be adjusted based on the facts and knowledge of the case. All decisions, facts, and findings must be clearly documented in the workpapers to support the reasons for the adjustments being made.

Note: To ensure that any warranted adjustments on the joint and non-joint returns are not overlooked, since adjustment to one could have a possible adverse impact to the other, both returns should be closed at the same time. If a phone call is received that can resolve both cases, only then Self-assign both cases and work them at the same time. See IRM 4.19.19.6.1, Self-Assign Procedures. Each taxpayer should be advised of the final outcome.

4.19.15.38
(02-01-2022)
Clean Vehicle Credit

- (1) Section 30D originally was enacted in the Energy Improvement and Extension Act of 2008. The American Recovery and Reinvestment Act 09 2009 amended IRC 30D in certain material respects, effective for vehicles acquired after December 31, 2009. Section 30D was substantially amended as part of the Inflation Reduction Act of 2022.
- (2) The Clean Vehicle Credit is claimed by filing Form 8936, Clean Vehicle Credits, and is reported on *Schedule 3*, for both Form 1040 and Form 1040NR. Prior to tax year 2018, the credit was reported directly on Form 1040, line 54 (or Form 1040NR, line 51).
- (4) Letter 566S will be issued as the ICL and cases will be updated to Status 10. On the Letter 566S/Letter 566-T for TDC cases, list as a check box, Form 8936, Clean Vehicle Credit.

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- (5) Include Form 886-A, Explanation of Items, as shown in IRM 4.19.15.38.2, Taxpayer Explanations for Form 886-A.
- (6) Vehicles must meet certain requirements. Generally, a purchaser can rely on the manufacturer's (or, in the case of a foreign manufacturer, its domestic distributor's) certification to the IRS that a specific make, model, and model year vehicle qualifies for the credit and, if applicable, the amount of the credit for which it qualifies. If, however, the IRS publishes an announcement that the certification for any specific make, model, and model year vehicle has been withdrawn, the purchaser cannot rely on the certification for such a vehicle purchased after the date of publication of the withdrawal announcement.
- (7) If the taxpayer does not provide the manufacturer's verification you may use the following link to verify if the vehicle being claimed qualifies for the credit: *Credits for New Electric Vehicles Purchased in 2022 or Before* / Internal Revenue Service (irs.gov). This link may not be all inclusive.
- (8) The Vehicle Identification Number (VIN) must be verified and must match the make, model, and year of a vehicle approved for the credit. The type of vehicle may be verified by entering the VIN number in the National Highway Traffic Safety Administration (NHTSA) VIN Decoder site at: <https://vpic.nhtsa.dot.gov/decoder/> The VIN number provided by the taxpayer on their original tax return was either incomplete or invalid and can be viewed on IDRS under CC TRDBV. The Form 886-A Sent with the ICL requested the taxpayer provide a copy of their vehicle registration certificate to verify the VIN, make, model and year of the vehicle for which they are claiming the credit.
- (9) The following use of vehicle requirements must also be met:
 - a. Original use of the vehicle began with the taxpayer,
 - b. The vehicle was acquired for personal use or to lease to others, not for resale,
 - c. The taxpayer owns the vehicle (if the vehicle is leased, only the lessor and not the lessee is entitled to the credit),
 - d. The vehicle was placed in service during the tax year, and
 - e. The vehicle is used primarily in the United States.
- (10) The credit is subject to a phase-out (reduction) once the vehicle manufacturer (or, for a foreign manufacturer, its domestic distributor) sells 200,000 vehicles for years prior to 2022. All phased-out credits will be identified on irs.gov. Beginning tax year 2019 two manufacturers will be subject to a phase-out:
 1. *Notice 2018-96* announced the credit phase-out schedule for new qualified plug-in electric drive motor vehicles sold by Tesla, Inc. (2018-52 I.R.B 1061) (**Tesla**. Enter the following percentage if the vehicle was manufactured by Tesla. One hundred percent if you purchased it before January 1, 2019. Fifty percent if you purchased it after December 31, 2018, but before July 1, 2019. Twenty-five percent if you purchased it after June 30, 2019, but before January 1, 2020. The credit is not available for Tesla vehicles purchased after December 31, 2019.)
 2. *Notice 2019-22* announced the credit phase-out schedule for new qualified plug-in electric drive motor vehicles sold by General Motors, LLC. (2109-14 I.R.B. 931) (**General Motors**. Enter the following percentage if the vehicle was manufactured by General Motors. 100 percent if you purchased it before April 1, 2019. 50 percent if you purchased it after March 31, 2019, but before October 1, 2019. 25 percent if you purchased it after

September 30, 2019, but before April 1, 2020. The credit is not available for General Motors vehicles purchased after March 31, 2020.)

4.19.15.38.1
(11-04-2019)

Special Situations and Replies

- (1) Taxpayers may claim the correct amount of credit on the wrong form. Before a credit can be disallowed, the examiner should review all vehicle listings prior to making a determination.
- (2) A credit claimed on an incorrect form should be processed as follows:

If	And	Then
The taxpayer claims a vehicle on Form 8834 or Form 8910 that should have been claimed on Form 8936	The amount claimed is the allowable amount for Form 8936	Allow the credit and No Change the case
The taxpayer claims a vehicle on Form 8834 or Form 8910, that should have been claimed on Form 8936	The amount claimed is not allowable on Form 8936	Disallow the credit

- (3) Processing Taxpayer Replies

If	And	Then
The requested documentation is sent in	It meets the criteria of the credit claimed	Allow the credit and no Change the case.
The bill of sale is sent in without the certification	The certification can be validated through the index to Manufacturers at https://www.irs.gov/businesses/small-businesses-self-employed/a-z-index-for-business	Allow the credit and no Change the case
The bill of sale is sent in without the certification	The certification <i>cannot</i> be validated through the Index to Manufacturers at https://www.irs.gov/businesses/small-businesses-self-employed/a-z-index-for-business	Disallow the credit

If	And	Then
The taxpayer claimed a credit over the maximum for an allowable vehicle	Documentation to support a credit was provided. Verify the allowable amount of the credit at: https://www.irs.gov/businesses/irc-30d-new-qualified-plug-in-electric-drive-motor-vehicle-credit	Revise the report to reflect the correct amount of allowable credit. On the Form 886-A state: "The amount of credit claimed on your original return was over the allowable limit for the vehicle claimed. We have revised your report to reflect the amount of credit you are entitled to."
The taxpayer claimed a credit over the maximum for an allowable vehicle	Valid documentation was not provided	Disallow the credit.
The taxpayer provides a copy of their vehicle registration	The registration matches an allowable vehicle claimed on Form 8936.	Allow the credit and No Change the case.
The taxpayer provides valid VIN	The VIN matches an allowable vehicle claimed on Form 8936. Verify using the NHTSA VIN Decoder at: https://vpic.nhtsa.dot.gov/decoder/Decoder .	Allow the credit and No Change the case
The taxpayer does not provide the requested vehicle registration, valid VIN number, or provide documentation to support the credit.	The claim for the credit is not valid	Disallow the credit

4.19.15.38.2
(12-01-2017)

**Taxpayer Explanations
for Form 886-A**

- (1) **Clean Vehicle Credits - Form 8936 Explanation:** To be allowed the Clean Vehicle Credit you must provide documentation that qualifies you for this credit. Our records indicate:

- a. The Vehicle Identification Number (VIN) you provided on Form 8936 with your Form 1040 was either ineligible or invalid, or

- b. The amount you claimed was over the maximum allowed for your vehicle. The manufacturer of this vehicle may have reached its phased-out limit for this credit. To view the credit amounts allowed for Plug-In Electric Motor Vehicles visit <https://www.irs.gov/businesses/irc-30d-new-qualified-plug-in-electric-drive-motor-vehicle-credit>.

(2) **To verify your claim please provide:**

- a. A copy of your vehicle registration, for the Plug-In Electric Drive Motor Vehicle you purchased.
- b. A copy of the valid sales contract.
- c. The manufacturer's certification, or the domestic distributor's certification if a foreign manufacturer, for each vehicle claimed on the Form 8936.

(3) **In addition to certification, the following requirements must be met to qualify for the credit:**

- a. You are the owner of the vehicle. If the vehicle is leased, only the lessor, and not the lessee, is entitled to the credit.
- b. You placed the vehicle in service during your tax year.
- c. The original use of the vehicle began with you.
- d. You acquired the vehicle for use or to lease to others, and not for resale.
- e. You used the vehicle primarily in the United States.

4.19.15.39
(10-16-2024)

**Math Error Authority on
Clean Vehicle Credit**

- (1) Taxpayers that placed certain clean vehicles (as defined by 26 U.S. Code 30D, 26 U.S. Code 45W, and 26 U.S. Code 25E) into service during the tax year 2023, or any year after through 2032, can claim a non-refundable clean vehicle credit (CVC) on the return for the year in which they placed the clean vehicle in service. The amount of the credit(s) varies depending on whether the vehicle is a new clean vehicle, a qualified commercial clean vehicle, or a previously-owned clean vehicle.
- (2) To ensure only the right vehicles are claimed, the manufacturer enters the qualifying vehicle identification number (VIN) into the Enterprise Data Platform (EDP). The IRS uses this platform to validate the VIN(s) that are claimed on taxpayer returns.
- (3) The IRS has been granted math error authority to adjust taxpayer accounts when there is a VIN mismatch under 26 U.S. IRC 6213 (g)(2)(T)-(V).
- (4) When a VIN mismatch is identified, the return is flagged for review. If the original return reflected a refund, a Refund Held freeze (-R) with TC 971 AC 831 MISC CVC may be placed on the taxpayer's account.

Note: The "MISC CVC" language may sometimes be missing from the TC 971 AC 831.

- (5) Once a return is flagged for a possible mismatch, the account must be reviewed and resolved. In general, accounts will be resolved in one of three ways:
 - the refund released
 - the total amount of the credit is reversed; or
 - the credit is recomputed and reversed in part.

4.19.15.39.1
(10-16-2024)

**Required Accesses and
Case Control**

- (1) Examiners assigned this workstream will require the following IDRS command codes:
 - ADJ54, REQ54
 - REQ77, FRM77
 - ACTON
 - LETER, LPAGE, LETUP, LETED, LLIST, LREVV
 - IMFOL, BMFOL
 - RTVUE, BRTVUE, TRDBV
 - MFREQ
 - TERUP
 - INTST
- (2) Managers of examiners working this program will require IDRS Command Codes RVIEW and QRADD.
- (3) To validate a VIN, examiners will require access to IMF and BMF EUP and Accounts Management System (AMS).
- (4) This inventory is not established on AIMS since there is no examination being conducted. Exam Case Selection will ensure Taxpayer Identification Numbers have a TXMOD control established when delivering this workstream to the campus so that inventory can be monitored through Control D reports.

4.19.15.39.2
(10-16-2024)

CVC Process Overview

- (1) Review assigned accounts and research the EDP to check the validity of the VIN(s) reported on Form 8936, Schedule A in AMS using the VIN Lookup Tool.
- (2) Based on the results of this research, use one of the If/Then tables to resolve the account:
 - All VINs valid
 - All VINs invalid
 - Combination of valid and invalid VINs
- (3) For research showing all VINs valid:

If	Then
<p>The taxpayer's refund is frozen, and there are no other open controls on the account</p>	<ul style="list-style-type: none"> • Input a TC 571 using REQ77 and release the refund • Use CC ACTON to update and close the IRDS control base. • Use activity "CVCgoodref", with C (for closing), and * for current date. • When the TC 971 AC 831 is posted on the tax module, reverse it with a TC 972 using REQ77. <p>Note: If "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p>
<p>The taxpayer's refund is frozen and there are other open controls (e.g., LB&I EPE, IDT, etc.)</p> <ul style="list-style-type: none"> • LB&I/TEGE will have TC 971 AC 831 MISC EPE. In some earlier accounts, there will not be a MISC field. • IDT will be identified with TC 971 AC 152, or TC 971 AC 152. 	<ul style="list-style-type: none"> • Do NOT release the refund with TC 571. • When the TC 971 AC 831 is posted on the tax module, reverse it with a TC972 using REQ77. <p>Note: If "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p> <ul style="list-style-type: none"> • Use CC ACTON to update and close the IRDS control base with activity of "CVC-goodVINS", with C (for closing), and * for current date.

If	Then
The taxpayer's account has a balance due or has a zero-balance due	<ul style="list-style-type: none">Reverse the TC 971 AC 831 if posted on the tax module, with a TC972 using REQ77. Note: If "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.Use CC ACTON to update and close the IRDS control base with activity of "CVC-goodVINS", with C (for closing), and * for current date.

(4) For research showing all VINs invalid:

If	Then
The taxpayer's refund is frozen and there are no other open controls on the account	<ul style="list-style-type: none">• Remove the full credit using ADJ54 and Hold Code 3• Issue Letter 474C to inform the taxpayer of the change.• When the TC 971 AC 831 is posted on the tax module, reverse it with a TC972 using REQ77. <p>Note: if "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p> <p>Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly.</p> <p>Reminder: If the adjustment places the taxpayer in a balance due status, you will need to calculate the interest out 21 days using CC INTST (after the adjustment) to provide that information in the Letter 474C, paragraph 9.</p>

If	Then
<p>The taxpayer's refund is frozen and there are other open controls (e.g., LB&I EPE, IDT, etc.)</p> <ul style="list-style-type: none"> • LB&I/TEGE will have TC 971 AC 831 MISC EPE. In some earlier accounts, there will not be a MISC field. • IDT will be identified with TC 971 AC 152, or TC 971 AC 152. 	<ul style="list-style-type: none"> • Remove the full credit using ADJ54 and Hold Code 2 • Issue Letter 474C to inform the taxpayer of the change. • When the TC 971 AC 831 is posted on the tax module, reverse it with a TC972 using REQ77. <p>Note: if "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p> <p>Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly.</p> <p>Reminder: If the adjustment places the taxpayer in a balance due status, you will need to calculate the interest out 21 days using CC INTST (after the adjustment) to provide that information in the Letter 474C, paragraph 9.</p>

If	Then
<p>The taxpayer's account has a balance due or has a zero balance due with or without other open controls (e.g., LB&I EPE, IDT, etc.)</p> <ul style="list-style-type: none"> • LB&I/TEGE will have TC 971 AC 831 MISC EPE. In some earlier accounts, there will not be a MISC field. • IDT will be identified with TC 971 AC 152, or TC 971 AC 152. 	<ul style="list-style-type: none"> • Remove the full credit using ADJ54 and Hold Code 0 • Issue Letter 474C to inform the taxpayer of the change. • Reverse the TC 971 AC 831 if posted on the tax module, with a TC972 using REQ77. <p>Note: If "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p> <p>Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly.</p>

(5) For research showing all a combination of valid and invalid VINs:

If	Then
<p>The taxpayer's refund is frozen and there are no other open controls on the account</p>	<ul style="list-style-type: none"> • Compute the amount of credit not allowed Caution: If the invalid VIN(s) does not impact the amount of the credit, ADJ54 is required to input a TC 290 \$0. • Adjust the account accordingly using ADJ54 and Hold Code 3 Caution: If the adjustment places the taxpayer in a balance due status, use a Hold Code 0 instead of Hold Code 2. • Issue Letter 474C to inform the taxpayer of the change. • When the TC 971 AC 831 is posted on the tax module, reverse it with a TC972 using REQ77. Note: if "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972. Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly. Reminder: If the adjustment places the taxpayer in a balance due status, you will need to calculate the interest out 21 days using CC INTST (after the adjustment) to provide that information in the Letter 474C, paragraph 9.

If	Then
<p>The taxpayer's refund is frozen and there are other open controls (e.g., LB&I EPE, IDT, etc.)</p> <ul style="list-style-type: none"> • LB&I/TEGE will have TC 971 AC 831 MISC EPE. In some earlier accounts, there will not be a MISC field. • IDT will be identified with TC 971 AC 152, or TC 971 AC 152. 	<ul style="list-style-type: none"> • Compute the amount of credit not allowed Caution: If the invalid VIN(s) does not impact the amount of the credit, ADJ54 is required to input a TC 290 \$0. • Adjust the account accordingly using ADJ54 and Hold Code 2 Caution: If the adjustment places the taxpayer in a balance due status, use a Hold Code 0 instead of Hold Code 2. • Issue Letter 474C to inform the taxpayer of the change. • When the TC 971 AC 831 is posted on the tax module, reverse it with a TC972 using REQ77. Note: if "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972. Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly. Reminder: If the adjustment places the taxpayer in a balance due status, you will need to calculate the interest out 21 days using CC INTST (after the adjustment) to provide that information in the Letter 474C, paragraph 9.

If	Then
<p>The taxpayer's account has a balance due or has a zero balance due with or without other open controls (e.g., LB&I EPE, IDT, etc.)</p> <ul style="list-style-type: none"> LB&I/TEGE will have TC 971 AC 831 MISC EPE. In some earlier accounts, there will not be a MISC field. IDT will be identified with TC 971 AC 152, or TC 971 AC 152. 	<ul style="list-style-type: none"> Compute the amount of credit not allowed Caution: If the invalid VIN(s) does not impact the amount of the credit, ADJ54 is required to input a TC 290 \$0. Adjust the account accordingly using ADJ54 and Hold Code 0 Issue Letter 474C to inform the taxpayer of the change. Reverse the TC 971 AC 831 if posted on the tax module, with a TC972 using REQ77. <p>Note: If "MISC CVC" is on the posted TC 971 AC 831, include "CVC" in the MISC field for the TC 972.</p> <p>Caution: If disallowing the CVC credit has any impact on other credits claimed by the taxpayer, address them accordingly.</p>

4.19.15.39.3
(10-16-2024)

Mismatch CVC with an A freeze

- (1) Follow the chart below when using math error authority on CVC Mismatch VIN cases that have an A Freeze present on the account:

If	Then
the TC 976/977 is a true duplicate of the original return, still claiming the SAME vehicle, and research shows the VIN is invalid with no other changes being made to the return	<p>follow normal Math Error procedure, input TC290 assessment, issue Letter 474C, input TC971 AC010 to reset the A freeze.</p> <p>Note: If research shows VIN is valid, release the refund and do not adjust.</p>
the TC 976/977 is not a true duplicate of the original return, and is now claiming an additional vehicle with an invalid VIN	<p>follow normal Math Error procedure, input TC290 assessment to remove the credit for the first vehicle, and issue Letter 474C. Input 971 010 to set the A freeze so AM can formally disallow the claim for the second invalid claimed Vehicle.</p>

If	Then
the TC 976/977 is not a true duplicate of the original return, and does not change/address the VIN claimed on the original return	follow normal Math Error procedure, input TC290 assessment using Hold Code 2, issue 474C letter, input TC 971 AC 010 to set the A freeze so AM can work the claim.

4.19.15.39.4
(10-16-2024)

CVC Special Conditions

- (1) If an account has a -V Freeze, indicating Bankruptcy, see IRM 21.5.6.4.44, -V Freeze for guidance.
- (2) If an account has a -W Freeze, indicating other types of litigation, see IRM 21.5.6.4.46, -W Freeze for guidance.
- (3) If the TC 150 has an Unpostable Code 126 Reason Code 0, do not take any action. RIVO/RICS will resolve the unpostable and address any other issues present on the account. Close the open Exam TXMOD control.

4.19.15.40
(10-16-2024)

Residential Energy Credits

- (1) There are two types of residential energy credits:
 - Energy Efficient Home Improvement Credit, IRC Section 25C, previously known as the Non-business Energy Property Credit (prior to amendment by the Inflation Reduction Act of 2022) and
 - Residential Clean Energy Credit, IRC Section 25D, previously known as the Residential Energy Efficient Property Credit (prior to amendment by the Inflation Reduction Act of 2022)
- (2) The Residential Energy Efficient Property Credit was renamed by IRA to the Residential Clean Energy Credit. Section 13302 of the IRA amended the eligibility for the credit and amounts available under IRC Section 25C for property placed in service after December 31, 2022, and extended the credit through December 31, 2032.
- (3) The Non-business Energy Property Credit was renamed by the Inflation Reduction Act of 2022 (IRA) to the Energy Efficient Home Improvement Credit. Section 13301 of the IRA amended the eligibility for the credit and amounts available under IRC Section 25D for tax years beginning after 2022 and extended the credit through December 31, 2034.
- (4) Under law prior to the IRA, the Non-business Energy Property Credit and the Residential Energy Efficient Property Credit have been available since 2005 and have been revised and/or extended many times. Section 141 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 extended the Non-business Property Energy Credit through December 31, 2021. The Taxpayer Certainty and Disaster Tax Relief Act of 2020 later extended this same treatment to qualified biomass fuel property expenditures through 2023. The Non-business energy Property credit expired at the end of 2017. Section 148 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 is now part of the Residential Energy Efficiency Property Credit rather than the Non-business Energy Property Credit. This subsection is provided for the inclusion of qualified biomass fuel property expenditures paid or incurred in taxable years after 2020 as part of the Residential Energy Efficient Property Credit. Section

148 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 extended the Residential Energy Efficient Property Credit for property placed in service through 2023 and modified the applicable percentages. The Protecting Americans from Tax Hikes (PATH) Act of 2015 amended the Residential Energy Efficient Property Credit to extend the credit for qualified solar electric property and qualified solar water heating property at specified applicable percentages as described in the statute through 2021. The Bipartisan Budget Act (BBA) of 2018 later extended this same treatment to fuel cell property, small wind property, and geothermal heat pump property through 2021. The Consolidated Appropriations Act, 2021 extends the credit to qualified biomass fuel property and extends the residential energy efficient property credit rate to property placed in service in 2021 and 2022. It also disallows the non-business energy property credit for a stove using biomass fuel and extends the balance of nonbusiness energy property credit to property placed in service in 2021.

- (5) These cases will open in Project Code 1046.
- (6) Tracking Code 6203 will be used for credits claimed when there is no indication of home ownership (It must be noted that home ownership is not required for the Residential Clean Energy Credit). No tracking code will be used for other cases.
- (7) Residential Energy Credits are non-refundable.
- (8) The following apply to all residential energy credits:
 - Taxpayers can rely on manufacturer's certification in writing that a product is a qualifying product for the credit.
 - For credit purposes, costs are treated as being paid when the original installation of the item is completed, or in the case of costs connected with the construction or reconstruction of the taxpayer's home, when the taxpayer's original use of the constructed or reconstructed home begins. Taxpayers cannot claim the Nonbusiness Energy Property Credit for property installed on a newly constructed home.
 - If a subsidy was provided by any public utility for the purchase or installation of an energy conservation product, the cost must be reduced by the amount of the subsidy before computing the credit. This rule also applies if a third party such as a contractor receives the subsidy on the taxpayer's behalf.
- (9) For specific information on each credit, refer to:
 - IRM 4.19.15.40.1, Energy Efficient Home Improvement Credit and Residential Clean Energy Credit
 - IRM 4.19.15.40.2, Initial Contact Letter
 - IRM 4.19.15.40.3, Taxpayer Replies
 - Form 5695, Residential Energy Credits
 - IRC 25C, Energy Efficient Home Improvement Credit
 - IRC 25D, for Residential Clean Energy Credit
 - Protecting Americans from Tax Hikes (PATH) Act of 2015
 - Bipartisan Budget Act (BBA) of 2018
 - The Consolidated Appropriations Act, 2021
 - The Inflation Reduction Act of 2022
 - *Technical Communication Document (TCD)*, 0172 in the numeric index
 - *Interactive Tax Law Assistant (ITLA)*

4.19.15.40.1
(10-16-2024)

**Energy Efficient Home
Improvement Credit and
Residential Clean
Energy Credit**

- (1) The Form 5695 which is used to compute the Residential Energy Credits, is divided into two parts:
1. Part I: For tax years 2021 and earlier, the Residential Energy Efficient Property Credit and for tax years 2022 and later, the Residential Clean Energy Credit.
 2. Part II: For tax years 2021 and earlier, the Nonbusiness Energy Property Credit and for tax years 2022 and later, the Energy Efficient Home Improvement Credit.

(2) The information below is related to Part II of Form 5695:

- a. For detailed information refer to IRC 25C, Energy Efficient Home Improvement Credit and *Notice 2013-70*.
- b. The two types of Non-business Energy Property Credits are Qualified Energy Efficiency Improvements and the Residential Energy Property Costs.
- c. Allows for improving energy efficiency of an existing home (not for new construction) and is available for costs related to new qualified items (such as high efficiency) installed on or in connection with your main home in the United States. Qualified items include; heating and cooling systems, water heaters, windows, skylights, doors (meeting certain energy requirements), insulation, and certain metal or asphalt roofs (for tax years 2022 and earlier).

Note: Credit does not apply to any property placed in service after December 31, 2032.

- d. For tax years 2022 and earlier, qualifying expenses must be for the taxpayer's main home, owned by the taxpayer in the United States. These expenses may include a house, houseboat, mobile home, cooperative apartment, or condominium.
- e. Enter total costs on Part II of Form 5695 for tax year 2012 and forward. For tax year 2011 and prior, enter on Part I.
- f. The sum of amounts that can be claimed is 10% of the amount paid for qualified energy efficiency improvements installed during the year and costs for residential energy property costs paid or incurred during the year.
- g. For tax year 2011 through 2022, the credit is limited to an overall lifetime credit limit of \$500 (\$200 for windows). Other credit limitations include: \$50 for any advanced main air circulating fan; \$150 for any qualified natural gas, propane, or oil furnace or hot water boiler; \$300 for any item of energy-efficient building property.

Note: Does not cover the installation/labor costs for insulation, windows, doors and roofs.

Caution: Any amounts paid using subsidized energy financing cannot be used to figure this credit.

- h. Applicable for tax years 2023 through 2032, the IRA eliminated the annual lifetime limitation and replaced it with an annual aggregate limitation of up to \$3,200. The IRA also placed annual limitations on specific properties within the annual aggregate limitation. Unless noted, the credit is allowed for a main home and for other dwellings used as a home. The maximum credit you can claim each year is \$1,200 for energy property costs and certain energy efficient home improvements; with limits on

doors (\$250 per door and \$500 total), windows (\$600) and home energy audits (\$150), and \$2,000 per year for qualified heat pumps, biomass stoves or biomass boilers.

- i. Unless noted, the credit is allowed for a main home and for other dwellings used as a home.
- j. Cannot carryforward unused credits.

(3) The information below is related to Part I of Form 5695:

- a. For detailed information refer to IRC 25D, Residential Clean Energy Credit.
- b. Refer to *Notice 2013-70*.
- c. Allowed for qualified expenses for adding qualified properties to an existing or newly constructed home in the United States. This includes, solar electric, solar water heating, small wind energy, geothermal heat pump, biomass fuel (for tax years after 2020 and before 2023), battery storage technology (for tax years after 2022), and fuel cell (limited to \$1,667 for each half kilowatt of capacity)

Note: Costs for swimming pools, hot tubs, or any other energy storage medium is not eligible for the credit.

- d. Can be permitted for more than one home (home ownership is not a requirement) however, home must be in the United States and used as a residence during the year
- e. Enter total costs on Part I of Form 5695 for tax year 2012 and forward. For tax year 2011 and prior, enter on Part II
- f. Generally, credit is limited as follows: 30% of total cost when property placed in service date range after December 31, 2016, and before January 1, 2020 or service date range December 31, 2021 and before January 1, 2033; 26% of total cost when property placed in service date range after December 31, 2019, and before January 1, 2022 or service date range after December 31, 2032 and before January 1, 2034; 22% of total cost when property placed in service date range after December 31, 2033 and before January 1, 2035
- g. Qualified fuel cell property credit is limited to \$500 per one-half kilowatt of capacity of the property
- h. Can carryforward unused credits

(4) If the Residential Energy Credit is claimed in addition to Child Tax Credit/Credit for Other Dependents, Mortgage Interest Credit, or Adoption Credit, then the taxpayer must compute these credits before completing the carryforward section of Form 5695.

(5) See *Instructions for Form 5695* for detailed information regarding joint ownership, married taxpayers with more than one home and joint occupancy rules.

4.19.15.40.2
(02-01-2022)
Initial Contact Letter

- (1) For the initial contact, Letter 566-S/Letter 566-T for TDC cases, along with Form 886-A is issued to the taxpayers and the cases are updated to Status 10 on AIMS.
- (2) The issue to create in RGS is energy credit.
- (3) The credit is calculated on Form 5695.

- (4) For information on the order in which non-refundable credits are applied, refer to Form 5695.
- (5) To figure the credit when there is joint ownership of the energy property, joint occupancy of the home, or for married taxpayers with more than one home, refer to the instructions for Form 5695.
- (6) For additional information regarding appropriate, supporting documentation requests, refer to the *Exam Project Code Search Tool* for Project Code 1046.

4.19.15.40.3

- (1) Evaluating taxpayer replies

(01-01-2014)

Taxpayer Replies

If	And	Conclusion
Taxpayer submits proof of purchase; proof of payment; documentation such as a manufacturer's certification proving that the product taxpayer purchased qualifies for the credit; proof of home ownership, if applicable; and proof that the home was their main home, if applicable	the amounts claimed on the original return are correct	No change the case.
Taxpayer submits proof of purchase; proof of payment; documentation such as a manufacturer's certification proving that the product taxpayer purchased qualifies for the credit; proof of home ownership, if applicable; and proof that the home was their main home, if applicable	the amounts claimed on the original return are higher than the maximum amount of credit	Revise the report to reflect the correct amount of allowable credit. On Form 886-A, state: "The amount of credit claimed on your original return was over the allowable limit for the credit. We have revised our report to reflect the amount of credit you are entitled to." Refer to IRM 4.19.13.11.1, Taxpayer Responses – Prior to Status 24.
Taxpayer submits only one required piece of information, without the other requested information	you were able to contact the taxpayer by phone	If the taxpayer faxes in the missing information and substantiates entitlement of the credit; no change the case. If the taxpayer is unable to fax in the requested documentation, see below for information on proceeding to the next stage of the examination. Refer to IRM 4.19.13.11.1, Taxpayer Responses – Prior to Status 24.

If	And	Conclusion
Taxpayer submits only one required piece of information, without the other requested information	you were unable to contact the taxpayer by phone	Proceed to the next stage of the examination. On Form 886-A make sure to thank the taxpayer for their correspondence and request the missing information. Make sure to state exactly what information is needed to allow the credit. Refer to IRM 4.19.13.9.11.1, Taxpayer Responses – Prior to Status 24.

4.19.15.41
(03-11-2019)

**Premium Tax Credit -
IRC 36B**

- (1) The premium tax credit (PTC) is a refundable tax credit designed to help eligible individuals and families with low or moderate income afford health insurance purchased through the Health Insurance Marketplace, also known as the Exchange, beginning in 2014. Taxpayers can choose to have an estimate of their PTC paid in advance (called advance payments of the PTC, Advance credit payments, APTC) to their insurance companies to lower what they pay for their monthly premiums, or they can forgo advance credit payments and get all of the benefit of the PTC when they file their tax return for the year. If a taxpayer chooses advance payments of the PTC the taxpayer must reconcile the amount paid in advance with the actual PTC computed when filing their tax return.
- (2) The Health Insurance Marketplace is where taxpayers will find information about private health insurance options, purchase health insurance, and obtain help with premiums and out-of-pocket costs if eligible. The Department of Health and Human Services (HHS) administers the requirements for the Marketplace and the health plans offered. More information about the Marketplace may be found at HealthCare.gov.
- (3) There are 4 categories or “metal levels” of coverage in the Marketplace. Plans in each category pay different amounts of the total costs of an average person’s care. The categories have nothing to do with the quality or amount of care provided. The plans are:

Plan Type	The Health Plan Pays (on average)	The Taxpayers Pays
Bronze	60 percent	40 percent
Silver	70 percent	30 percent
Gold	80 percent	20 percent
Platinum	90 percent	10 percent

Note: Individuals may also enroll in catastrophic coverage plans, which pay less than 60 percent of the total average cost of care on average. They’re available only to people who are under 30 years old or have a hardship exemption. PTC is not allowed for coverage under a catastrophic plan.

- (4) The Marketplace will estimate the amount of the premium tax credit that a taxpayer may be able to claim for the tax year, using information provided about family size, projected household income, whether the members of the family enrolled in coverage are eligible for employer coverage or government-sponsored coverage, and other information. This estimated credit is the maximum amount of advance credit payments for which the taxpayer is eligible. Based upon that estimate, the taxpayer may decide to have all, some, or none of the estimated credit paid directly to the insurance company to be applied to the monthly premiums. If a taxpayer receives the benefit of advance payments of the premium tax credit, the taxpayer must reconcile the amount of the advance credit payments with the allowable amount of the premium tax credit for the year.
- (5) Form 8962, Premium Tax Credit (PTC), is used to claim the credit and to reconcile advance credit payments with allowable amount of PTC for the year. Taxpayers who had excess advance credit payments must treat the excess amount as an additional tax, subject to limitations based on the taxpayer's household income. If the allowable amount of PTC for the year is greater than the advance credit payments, the net PTC reduces tax liability or results in a refund.
- (6) Taxpayers who purchased health insurance through the Marketplace for themselves, a spouse or a dependent will receive a Form 1095-A, Health Insurance Marketplace Statement, to assist in completing Form 8962. The Form 1095-A includes the monthly premium for the plan enrolled in, the monthly premium for the taxpayer's applicable benchmark plan and the advance credit payments made for the taxpayer.
- (7) For further details about the Premium Tax Credit, see Pub 17, Your Federal Income Tax, Pub 974, Premium Tax Credit, and the instructions for Form 8962. Additional information may also be found on the Affordable Care Act Resource page located on SERP, and at www.irs.gov/uac/Affordable-Care-Act-Tax-Provisions-for-Individuals-and-Families.

4.19.15.41.1
(06-14-2023)
**Premium Tax Credit
Eligibility**

- (1) The taxpayer is eligible for a premium tax credit for a taxable year if they meet all of the following:
 - a. The taxpayer, the taxpayer's spouse if a joint return is filed, or a dependent of the taxpayer must have been enrolled in a qualified health plan offered through the Marketplace for one or more months in which they are not eligible for other health insurance such as employer or government-sponsored coverage, that has minimum essential coverage,
 - b. The taxpayer must have paid their share of the plan premiums for one or more of the months by the taxpayer's tax return due date (not including extensions),
 - c. The taxpayer must be an applicable taxpayer. An applicable taxpayer is a taxpayer with household income of at least 100 percent* but not more than 400 percent of the federal poverty line for the taxpayer's family size, who uses a filing status other than married filing separately** and cannot be claimed as a dependent by another person.

Note: *There are two exceptions for taxpayers below 100 percent of the FPL (see instructions for Form 8962). **An abused or abandoned spouse who cannot file jointly because of the abandonment or abuse may still be an applicable taxpayer.

Note: There are three provisions of the American Rescue Plan Act of 2021 that temporarily modify Premium Tax Credit (PTC) eligibility: **Section 9661:** For tax years 2021 and 2022, eliminates the requirement that household income not exceed 400 percent of the federal poverty line for the taxpayer's family size in order for the taxpayer to be eligible for the PTC. The tables for determining the taxpayer's contribution to their health care coverage are also modified, increasing the amount of the credit. **Section 9662:** For tax year 2020 only, eliminated the requirement to repay excess Advanced Premium Tax Credit (APTC). **Section 9663:** For tax years 2021 only, allows the maximum credit available to any taxpayer who received or was approved to receive unemployment compensation during the tax year, regardless of their household income.

- d. The taxpayer, spouse, or dependent must be a U.S. citizen, or lawfully present in the U.S.
- e. The taxpayer, spouse, or dependent must not be incarcerated.

(2) Filing Status

- a. Taxpayers who file a married filing separate tax return, will not be eligible for the premium tax credit, unless they meet the criteria in IRC 1.36B-2(b)(2)(ii) of the Income Tax Regulations, which allows certain victims of domestic abuse and spousal abandonment to claim the credit, using the married filing separate filing status. This relief from the joint filing requirement may be used for no more than three consecutive years.

Note: Victims of domestic abuse or spousal abandonment will check the box on the line about Part 1 of Form 8962, Premium Tax Credit. If the taxpayer has marked the box above Part I for the married filing separately exception, edit "1" to the right of the checkbox in the right margin per IRM 3.11.3.66(8).

4.19.15.41.2
(06-14-2023)
Common Terms

- (1) Household Income is the sum of the modified adjusted gross income (MAGI) of the taxpayer, the MAGI of the taxpayer's spouse, if married, and either filing a joint return or filing a separate return and claiming a personal exemption for the spouse, and the MAGI of all the dependents of the taxpayer required to file a tax return because their income is above the filing threshold.

Note: The Tax Cuts and Jobs Act amended IRC 151 by reducing the personal exemption amount to zero for taxable years beginning after 12/31/2017 and before 01/01/2026. IRS *Notice 2018-84, 2018-45 I.R.B. 768* provides interim guidance in relation to how the personal exemption deduction is applied for purposes of interpreting the regulatory provisions governing eligibility for the Premium Tax Credit.

Note: Under *Notice 2018-84*, for purposes of claiming the Premium Tax Credit, a taxpayer is considered to have claimed a personal exemption deduction for themselves if the taxpayer files an income tax return for the year, and a taxpayer is considered to have claimed a personal exemption deduction for an individual other than the taxpayer if the taxpayer is allowed a personal exemption for the individual (taking into account IRC 151(d)(5)(B)) and lists the

individual's name and TIN on the Form 1040, U.S. Individual Income Tax Return or Form 1040-NR, U.S. Nonresident Alien Tax Return the taxpayer files for the year.

- (2) Modified Adjusted Gross Income (MAGI) is the adjusted gross income shown on the return plus:
- a. Excluded foreign earned income
 - b. Foreign earned income housing cost exclusion
 - c. Tax-exempt interest,
 - d. Non-taxable social security benefits
 - e. Non-taxable railroad retirement benefits

Note: Modified adjusted gross income does not include Supplemental Security Income (SSI).

- (3) To be eligible for a PTC, a taxpayer must have household income of at least 100 percent and, except for tax years 2021 and 2022, not more than 400 percent of the Federal Poverty Line (FPL) for the taxpayer's family size (although there are 2 exceptions for taxpayers below 100 percent of the FPL). For 2013, for residents of one of the 48 contiguous states or Washington, D.C., a few examples of the federal poverty levels are:
- a. \$11,490 (100 percent) up to \$45,960 (400 percent) for one individual
 - b. \$15,510 (100 percent) up to \$62,040 (400 percent) for a family of two
 - c. \$23,550 (100 percent) up to \$94,200 (400 percent) for a family of four
- (4) The federal poverty line or FPL is an income amount considered poverty level for the year, for the size of the family. The Department of Health and Human Services (HHS) determines the federal poverty line amounts annually. HHS provides three federal poverty lines: one for residents of the 48 contiguous states and D.C., one for Alaska residents and one for Hawaii residents. For purposes of the premium tax credit, eligibility for a certain year is based on the most recently published set of federal poverty guidelines at the time of the first day of the annual enrollment period for coverage during that year. As a result, the premium tax credit for 2014 is based on the 2013 FPL. The premium tax credit for 2015 is based on the 2014 FPL. Current FPLs and updated information can be found on the HHS website and in the instructions for Form 8962, Premium Tax Credit (PTC) under line 4.

4.19.15.41.3
(03-11-2019)
PTC Project Codes

- (1) The following table provides an overview of the Non-EITC single-issue Premium Tax Credit (PTC) programs worked in Exam:

PTC Program worked in Exam

Project Code	Project Code Title	Project Code Description	Initial Contact Letter
1300	Premium Tax Credit Pre-Refund	Non-EITC examination questions taxpayer eligibility for PTC for the year. Refund is held on taxpayer's account.	CP 06 or LTR 566-S/ LTR 566-T for TDC cases, with Form 14950

Project Code	Project Code Title	Project Code Description	Initial Contact Letter
1310	Premium Tax Credit Post Refund	Non-EITC examination questions taxpayer eligibility for PTC for the year. Refund is not held on taxpayer's account.	CP 06A or LTR 566-S/LTR 566-T for TDC cases, with Form 14950
1322	Premium Tax Credit (Non-EITC)	This examination includes the PTC, questionable W-2s (income) and credits. Note: There are different types of QRP cases identified by various source codes. See IRM 4.19.14.9.2, QRP Source Code and Project Codes	LTR 566-S/LTR 566-T for TDC cases, or 566B/566-J for TDC cases, with Form 4549, Income Tax Examination Changes with Form 14950
1321	Premium Tax Credit SLCSP	This examination includes the Second Lowest Cost Silver Plan (SLCSP) for the Premium Tax Credit	LTR 566-S/LTR 566-T for TDC cases, with form 14950

- (2) Tracking Code 8071 will be used to identify Discretionary cases that also have PTC issues. The Discretionary cases that are in other project codes with this tracking code will reject from ACE automation. The examiner will need to manually add the PTC issue and reintroduce the cases into the ACE automation process.

4.19.15.41.4
(02-26-2015)
Case Selection

- (1) When a Premium Tax Credit (PTC) return is filed, Submission Processing (SP) will compare the return information against the information from the Federal and State Health Exchanges. If the information on the return does not match the information from the exchanges, SP will correspond with the taxpayer to obtain the information needed to process the return.
- (2) If the taxpayer does not respond, SP will input error codes on the return. Nine error codes will be worked in Exam. (Four error codes apply to single-issue examinations.) Please refer to IRM 4.19.14.8.4, Premium Tax Credit (PTC), for a description of the error code conditions.
- (3) After SP inputs the error codes, the returns will be available in Dependent Database (DDb) for case selections.
- (4) DDb will generate flags which will be used to strengthen the selection criteria in conjunction with the error codes. There are 11 flags that will be used. Refer to IRM 4.19.14.8.3, Premium Tax Credit (PTC), for a description of the flags.
- (5) The overall priorities for selecting pre-refund cases are as follows:

1. Returns with an error code and a flag
 2. Returns with an error code
 3. No error code, which includes special processing code (SPC) 4, aging reason code (ARC) 7 or 8 and computed zero values
- (6) Cases will *not* be selected for returns only meeting the flags criteria unless there is an indication the data matching was not completed.

4.19.15.41.5
(06-14-2023)
**Research and Initial
Report Writing**

- (1) **For fully automated cases, the PTC is disallowed in full or the advance payments of PTC are being treated as repayment. The PTC issue is created by ACE processing and includes the case types listed below:**
- Combination EITC/PTC cases with PTC EC 190, 191 or 195.
 - Single issue non-EITC PTC cases with PTC EC 190, 191 or 195.
- (2) **Partially automated cases will be routed to RGS Group B2. ACE will create the case and all issues with the exception of the PTC and/or APTC repayment issue. Examiners will perform the relevant research, create the PTC and/or APTC Repayment issue, and generate the Examination Report Form 4549. The RAR report (Form 4549 and accompanying forms) will be printed and mailed by the campus at the appropriate time. The cases can then be reintroduced to ACE Group B0 for Aging and Closing. The following types of cases will be partially automated:**
- Any currently automated (EITC or non-EITC) project codes with a PTC EC 193, 194, 196, 197, 198 or 199.
 - Any currently automated (EITC or non-EITC) project codes with multiple PTC error codes.
 - Any currently automated non-EITC project codes with tracking code 8071.
- (3) **Manual Cases-** Manually created cases will set up in ACE Group B1. Examiners will perform the relevant research, create the PTC and/or APTC Repayment issue, along with other relevant issues and generate the Examination Report Form 4549. The Letter 566-S/566-T for TDC cases, 566B/566-J for TDC cases, Form 4549 and accompanying forms will be printed and mailed by the campus. The cases can then be reintroduced to ACE Group B0 for Aging and Closing.
- (4) PTC allowed on the original return posts as a Transaction Code (TC) 766 with credit reference number (CRN) 262. Excess APTC Repayment is included in the total tax. Posted PTC associated data can be viewed in the posted return section of CC TXMOD or CC IMFOLR. The data elements are:

PTC Data Elements

Data Element	Term
Total Premium Tax Credit	TOTAL PTC
Advance Premium Tax Credit	TOTAL APTC
Excess Advance Payment Above Limitation	LIMIT AMT
Excess APTC Repayment	APTC TX LIAB

Note: Note: The PTC which posts as TC 766 CRN 262 is the Reconciled Premium Tax Credit which is the Total PTC minus the Advance PTC. For additional credit reference numbers that relate to the adjustment of PTC data, refer to IRM 21.6.3.4.2.12.7, Adjusting the Account.

- (5) **Federal Poverty Line** - The Department of Health and Human Services (HHS) determines the federal poverty line amounts annually. A taxpayer who receives excess advance payments must treat the excess amount as additional tax, subject to limitations based on the household percentage of FPL; limitations do not apply in all circumstances.

Note: The American Rescue Plan Act of 2021, enacted on March 11, 2021, suspended the repayment of excess advanced premium tax credit (APTC) amounts for tax year 2020 only. See the IRS website, *More details about changes for taxpayers who received advance payments of the 2020 Premium Tax Credit* for more information. Do not assess the Excess APTC Repayment for tax year 2020 for examination cases.

- (6) The repayment limitation for advance payments are revised yearly and are shown in the *Instructions for Form 8962 - Premium Tax Credit (PTC)* under Table 5, Repayment Limitation. The taxpayer's liability is the smaller of the excess advance payment or repayment limitation. There is no limitation if the taxpayer's household income is 400 percent or more of the FPL.

(7) **FPL Percentages Not Eligible for PTC -**

- **Household Income Below 100 percent of the FPL;** If the household income is less than 100 percent of the Federal poverty line and the taxpayer does not meet the requirements for **Estimated household income at least 100 percent of the Federal poverty line or Alien lawfully present in the United States**, the taxpayer is not eligible to Claim the PTC. Please refer to *Instructions for Form 8962 - Premium Tax Credit (PTC)*, page 8, for additional information regarding the exceptions.
- **Household Income Above 400 percent of the FPL;** If the household income is greater than 400 percent of the FPL, for tax years other than 2021 and 2022, the taxpayer cannot take the PTC. The taxpayer must repay all APTC paid for individuals in the tax family.

Note: The American Rescue Plan Act of 2021 and the Inflation Reduction Act of 2022 temporarily modified Premium Tax Credit (PTC) eligibility for tax years 2021 through 2025. 1) The requirement that the household income not exceed 400 percent of the Federal poverty line is eliminated for these years. 2) For tax year 2020 only, the requirement to repay excess Advanced Premium Tax Credit is eliminated. 3) For tax year 2021 only, any taxpayer who received or was approved to receive unemployment compensation during the tax year, regardless of their household income, is allowed the maximum credit available.

4.19.15.41.6
(06-14-2023)
Creating the PTC Issue(s)

- (1) For cases assigned to ACE Group B2 or B1, examiners will have to create the PTC issue based on the assigned Error Code(s) and/or Flags.
- (2) Prior to creating the PTC issue, ensure that all other issues that might affect the PTC have been addressed:

- Research IDRS CC IRPTL to ensure that all income has been properly reported on return. Create issues to address any unreported or mis-reported income in the General Income section under Special Applications in RGS. Be sure to include income from both spouses on jointly filed returns. Refer to IRM 4.19.11.4.3.2, Issues Appropriate for Taxpayer Services versus SB/SE, for guidance on the types of unreported income that should be addressed.
 - If the case has multiple EITC/PTC issues, ensure that all of the issues that pertain to Filing Status and Dependent Exemptions are properly created.
- (3) Research IDRS CC DLITE to determine the Error Code (EC)(s) and/or Flags that apply to the case. Refer to IRM 4.19.14.8.4, Premium Tax Credit (PTC), for a description of the Error Code of Flag conditions.

Note: When Error Codes are present they may also be viewed on: 1) IDRS CC RTVUE Definer 1, 2) IDRS CC TRDBV CODES screen, 3) RGS in the Pre-audit comments of the Batch History Issue

Issue Determination

IF	AND	THEN
Error Codes and Flags exist on DLITE	NA	Follow the steps in paragraphs 4 –9 and 11 -12 to create the appropriate PTC issues in RGS based on the Error Codes
Only Flags exist on DLITE	There is an indication that data matching was not completed: SPC 4 (CC RTVUE) Definer R1 or ARC 7 or 8 (CC AMDIS)	Follow the steps in paragraphs 10 -12 to create the PTC issue in RGS based on the Flags only

- (4) When ACA Verification System (AVS) data is available at the time the taxpayer's return is processed, the data from that system is displayed on IDRS CC RTVUE screens B1 and B2. This data will be used to determine the Per Exam amounts on the PTC issues in RGS.

RTVUE fields used in creation of PTC Issues

RTVUE Definer	Field Name	Description
B1	AVS EXPOSURE AMT	Discrepancy in the PTC calculated by AVS. This will include any increase to the repayment of Advance PTC
B1	AVS RECONCILED PTC	This number will generally be the same as the amount of PTC that is posted to the tax module. (TC 766 CRN 262)

RTVUE Definer	Field Name	Description
B2	PREM CMPTR AMT	The policy premium amounts per AVS. Note: There will be a yearly amount (row Y) and amounts for each month. These amounts are compared to the corresponding entries on F 8962 Part 2 to identify discrepancies.
B2	SLCP CMPTR AMT	The SLCSP premium amounts per AVS (see Note above)
B2	MAX APTC CMP	Advance PTC paid per AVS (see Note above)
B2	CNTRB CMPTR AMT	Taxpayer's monthly contribution.

(5) There are two IMF Codes in RGS for creating PTC issues:

- IMF Code 62002 - Premium Tax Credit (PTC)
- IMF Code 62003 – Excess Advance PTC (APTC) Repayment

(6) Use IMF Code 62003 when creating the issue associated with PTC Error Code 190 (as described below.) For all other PTC Error Codes and Flags use IMF Code 62002. As always, when creating multiple issues in RGS with the same IMF Code you must give each issue a unique name. Give each issue a name that is descriptive of the associated issue categorization.

Note: The American Rescue Plan Act of 2021, enacted on March 11, 2021, suspended the repayment of excess advanced premium tax credit (APTC) amounts for tax year 2020 only.

(7) The following Error Codes will result in a full disallowance of the PTC and full repayment of any Advance PTC. These issues will normally be created systematically by ACE on the initial 30-day report:

Error Codes resulting in full disallowance of PTC

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount	Standard Paragraph Number
190	APTC repayment-net tax adj	Form 1040 Line 46, Form 1040-A Line 29, or for 2018 on <i>Schedule 5</i> of Form 1040	Per Return Amount + AVS EXPOSURE AMT (from IDRS CC RTVUE Definer B1)	8703
191	Net PTC-net credit adj	AVS RECON-CILED PTC (from	0	8704

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount	Standard Paragraph Number
195	Net PTC-net credit adj	IDRS CC RTVUE Definer B1)	0	8707

Caution: The APTC repayment net adjustment cannot be used to create the issue for EC 190 if the taxpayer has provided a response (i.e. Form 8962). EC 190 will require adjustments to specific lines of Form 8962.

(8) These instructions provide guidelines for adjusting specific lines on Form 8962. The taxpayer's Form 8962 entries may be viewed on the following:

- IDRS CC RTVUE Definer PT and P2
- IDRS CC TRDBV 8962 screen
- RGS Return Setup Form 8962 tab
- RTF F-8962 section (viewable in RGS)

(9) Follow the steps below to create the RGS PTC issue. Multiple error conditions may result for some of the Error Codes listed below.

Error codes that potentially affect multiple entries on Form 8962

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount	Standard Paragraph Number
190 with response (i.e. Form 8962)	Create issues for each entry on F-8962 Columns A, B, & F, lines 12-23 that do not match the corresponding entries on IDRS CC RTVUE B2	See Table in paragraph 9	See Table in paragraph 9	Provide appropriate explanation based results of Form 8962
193 with no other error	Net PTC-net credit adj	AVS Reconciled PTC (from IDRS CC RTVUE Definer B1)	0	8705
193 with any of the following ECs: 197, 198, 199	Do NOT create an issue for Net PTC - net credit adj. Create the issues for the additional ECs as described in para 8	See table in para 9	See Table in para 9	8705 (Include this paragraph on each associated issue.)

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount	Standard Paragraph Number
194 (may be accompanied by ECs 197, 198, and/or 199)	Create issues for each entry on F-8962 Columns A,B & F, lines 12-23 that do not match the corresponding entries on IDRS CC RTVUE B2	See Table in para 9	See Table in para 9	8706
196 (This EC indicates that the TP incorrectly used the annual calculation – Form 8962, Line 11 – instead of the monthly calculation – Form 8962, Lines 12-23)	Create issues for each month that has a non-zero entry in the first, second or fifth column on IDRS CC RTVUE B2	PTC-calculation method-Monthly = 0:(Important: Enter zero as the Per Return Amount for each issue. Do NOT try to divide the TP's entries on Line 11 between the various months.)	PTC-calculation method-Monthly = 1: See Table in para 9 for appropriate fields to use from IDRS CC RTVUE Definer B2	8706

- (10) The following Error Codes indicate that the taxpayer's entries on specific lines on Part 2 of Form 8962 do not match the values provided by the AVS. The radio buttons on the RGS Return Setup F-8962 tab will indicate whether the taxpayer is using the annual or monthly method to calculate the PTC. If the taxpayer is using the monthly method, you will need to create an issue for each month where the taxpayer's entry does not match the corresponding AVS. You do not need to create an issue for any month in which the taxpayer's Form 8962 entry matches the AVS value.

Note: If you are creating monthly issues in association with Error Code 196 (see above) you will have to create an entry for each month for which there is a non-zero AVS value.

Error codes pertaining to entries on Part 2 of Form 8962

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount (research IDRS CC RTVUE Definer B2)	Standard Paragraph
197 (TP used annual calculation)	PTC-annual premium amount	Form 8962 Column A Line 11	PREM COMPTR AMT line Y	8708

Error Code	RGS Issue Categorization	Per Return Amount	Per Exam Amount (research IDRS CC RTVUE Definer B2)	Standard Paragraph
197 (TP used monthly calculation)	PTC-monthly premium amount-(month) Note: Create an issue for each month for which the amount from F-8962 does not match the corresponding amount from IDRS CC RTVUE B2.	Form 8962 Column A Lines 12 – 23 (or 0 if creating this issue in association with EC 196)	PREM COMPTR AMT lines J - D	8708 (Input paragraph on each monthly issue created*)
198 (TP used annual calculation)	PTC-annual premium SLCSP amount	Form 8962 Column B Line 11	SLCP CMPTR AMT line Y	8708
198 (TP used monthly calculation)	PTC-monthly prem SLCSP-(month) See Note above.	Form 8962 Column B Lines 12 – 23 (or 0 if creating this issue in association with EC 196)	SLCP CMPTR AMT lines J - D	8708 (Input paragraph on each monthly issue created*)
199 (TP used annual calculation)	PTC-annual advance	Form 8962 Column F Line 11	MAX APTC CMP line Y	8708
199 (TP used monthly calculation)	PTC-monthly advance-(month) See Note above	Form 8962 Column F Lines 12 – 23 (or 0 if creating this issue in association with EC 196)	MAX APTC CMP lines J - D	8708 (Input paragraph on each monthly issue created*)

Note: Standard paragraph 8708 must be input on at least one monthly adjustment. For the remaining monthly adjustments, you may use a custom paragraph. The custom paragraph may consist of a single character such as a period (.). This will allow the paragraph to appear only once on the form instead of multiple times which may cause confusion. A generic paragraph such as 9426 can also be used.

- (11) Use the following table to create the PTC issue based on the PTC Flags.
(**IMPORTANT:** This table should only be used if AVS data is unavailable, and it is not possible to determine whether there are any PTC error conditions associated with the return).

PTC Flag	RGS Issue Categorization	Per Return Amount	Per Exam Amount	Standard Paragraph Number
PTC - SLCSP Flag	Net PTC-net credit adj	AVS RECON-CILED PTC (from IDRS CC RTVUE Definer B1) (TC 766 CRN 262 amount on IDRS CC IMFOLT if no RTVUE Definer B1)	0	8715
PTC Flag # 1 - 11	Net PTC - net credit adj	AVS RECON-CILED PTC (from IDRS CC RTVUE Definer B1) (TC 766 CRN 262 amount on IDRS CC IMFOLT if no RTVUE Definer B1)	0	8716

- (12) Run a tax computation in RGS. RGS will generate statutory issues for the change to the Net PTC (Form 8962, Line 26) and the Excess Advance PTC as needed.
- (13) Generate the Form 4549 Examination report including the tax computation report for Form 8962 and save to Case File Documents. If this is the initial report, print and mail the report per local procedures and move the case file to ACE Group B0 for Aging and Closing. Include Form 14950 Premium Tax Credit Verification, with the mail packet.

4.19.15.41.7
(06-14-2023)

Evaluating Responses

- (1) Taxpayers must provide verification to show they are eligible to claim the Premium Tax Credit (PTC). The taxpayer must have purchased health insurance through a Health Insurance Marketplace. If the health insurance was not purchased through a Marketplace, then the taxpayer is not eligible for PTC and does not need to send us any documentation.

IF	THEN acceptable documentation is:
Taxpayer needs to verify names of the individuals they are claiming for PTC	Insurance enrollment forms, invoices, statements from the insurance provider, or Form 1095-A
Taxpayer Form 8962 is incorrect or is missing (not attached to tax return)	Completed or corrected Form 8962 Note: You will need to calculate the PTC using AMS PTC calculator or create issues in RGS corresponding to the Form 1095-A. Refer to IRM 4.19.15.41.6 , Creating the PTC Issue(s).

IF	THEN acceptable documentation is:
Information is needed to support the allocation of the PTC in Part 4 of the Form 8962	Statement from the insurance provider which shows: <ul style="list-style-type: none"> • Policy number • Social security number • Start and stop months • Percentage of allocation Note: You will need to calculate the PTC using AMS PTC calculator or create issues in RGS corresponding to the taxpayer's entries on Form 8962. Refer to IRM 4.19.15.41.6 Creating the PTC Issue(s).
Information is needed to support the alternative calculation for marriage in Part 5 of the Form 8962	Taxpayer's date of marriage. (marriage certificate)
Proof of payment for the health premium is needed	<ul style="list-style-type: none"> • Cancelled checks (both sides) • Paid receipts • Certificate or insurance coverage • Credit card statements • Bank statements

Note: Taxpayers may send in Form 1095-A or Form 1095-B which can be used to verify items on the Form 8962

Caution: A Form 1095-A marked as Void means the form is no longer valid. The taxpayer is not liable for any APTC originally reported on the Form, nor are they eligible for any credit for data originally reported. A Form 8962 does not have to be submitted to update the account.

Reminder: In 2015, Oregon state-run Marketplace transitioned to Federal. Oregon state-run Marketplace systems did not allow for the electronic transmission of corrected Forms 1095-A for Tax Year 2014 return data when updated information was received from the health care providers. If working a PTC-related return from a taxpayer that participated in the Oregon State Marketplace coverage, and the information the taxpayer provides cannot be verified on BOE or CC IRPOL, advise the taxpayer that they will need to request an official statement from Oregon along with the corrected Form 1095-A that verifies the information reported on their return. Refer taxpayers with questions to the Oregon Marketplace at: **1-855-268-3767 (TTY 711)** or e-mail address: **Info.Marketplace@oregon.gov**.

(2) Judgment must be used based on the facts and circumstances in each case to make a substantially correct determination. Workpapers must contain determinations, facts, and circumstances pertaining to the cases.

Note: The American Rescue Plan Act of 2021, enacted on March 11, 2021, suspended the repayment of excess advanced premium tax credit (APTC) amounts for tax year 2020 only. See *IRS suspends requirement to repay excess advance payments of the 2020 premium tax credit* for more information. Starting with RGS 23.0, for tax year 2020 if the taxpayer's return data in the

RGS Return Setup includes an Excess APTC Repayment, the Variance Report will show a “true” variance for the amount of the Excess APTC Repayment. This results in an adjustment on Form 5344 to correct the tax to abate the Excess APTC Repayment. Do not assess the Excess APTC Repayment for tax year 2020 for examination cases.

Note: If the taxpayer’s Second Lowest Cost Silver Plan (SLCSP) premium on their Form 1095-A is incorrect, the taxpayer is directed not to request a corrected form. The taxpayer must use the Health coverage tax tool located on the HealthCare.gov web page at: <https://www.healthcare.gov/tax-tool/#/>, to determine their correct SLCSP premium. The printed copy from this web page may be accepted if the information provided is reasonable. Examiners may also use the Health coverage tax tool to validate the information provided.

- (3) A taxpayer (TP1) must allocate policy amounts (enrollment premiums, applicable SLCSP premiums and/or APTC) with another taxpayer (TP2), for example, TP1 and TP2 are former spouses, if (1) the same policy covers one or more individuals claimed on TP1’s return and one or more individuals claimed on TP2’s return, and (2) the Form 1095-A for the policy lists one or more individuals in TP1’s family and one or more individuals in TP2’s family. The taxpayers generally may agree on any allocation percentage from zero through one hundred percent (for example, they may agree to allocate 40 percent of the policy amounts to TP1 and 60 percent to TP2), but that same percentage must be used for all of the policy amounts being allocated (that is, if they choose 40/60, then 40/60 must be used for all policy amounts being allocated). Also, if the taxpayers do not agree on an allocation percentage, the default allocation percentage for a particular taxpayer is generally equal to the number of individuals enrolled in the policy and claimed as a personal exemption deduction on the taxpayer’s return, divided by the total number of individuals enrolled in the same policy (Allocation Situation 4 in the Form 8962 instructions). Finally, if policy amounts are being allocated because the taxpayers are still married to each other but using either the married filing separately or the head-of-household filing status (Allocation Situation 2 in the Form 8962 instructions), the enrollment premiums and the APTC must be divided equally between the taxpayers (50/50 allocation), and the applicable SLCSP premiums are not allocated (each taxpayer computes their own applicable SLCSP premiums if allowed a PTC for the year).

Example: Charlie and Sam have 5 children and divorced in 2014. For 2016, Sam and the five children enroll in the same Marketplace policy and Charlie enrolls in their employer’s coverage. A Form 1095-A for the policy is sent to Sam. However, Charlie claims two of the children on their 2016 return and Sam claims the other three on their 2016 return. Charlie and Sam must allocate the policy amounts for the policy on which Sam and the five children enrolled. They can agree on the percentage to be allocated to Charlie and the percentage to be allocated to Sam. If they do not agree, the enrollment premiums, the SLCSP premiums, and APTC would be allocated as follows:

1. Charlie checks the yes box on line 9 of Part II of F-8962. In Part IV, Charlie enters the appropriate information, including Sam’s SSN in column b and inputs **0.33** in columns (e), (f) and (g) (Charlie is claiming 2 individuals on the policy and a total of 6 are enrolled).

2. Sam checks the yes box on line 9 of Part II of F-8962. In Part IV, Sam enters the appropriate information, including Charlie's SSN in column b and inputs **0.67** in columns (e), (f) and (g) (Sam is claiming 4 individuals on the policy and a total of 6 are enrolled).

Any other allocation percentage is acceptable as long as both taxpayers agree.

If the taxpayers must allocate but have not agreed on the percentage or have not reported an allocation, use the default allocation when

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Reminder: Only exemptions claimed for individuals enrolled in the Marketplace are used in the calculation. For instance, if Charlie also claimed an exemption for their mother who is Medicare eligible, this would not affect the calculation. Similarly, the calculation would not be affected if Charlie was enrolled in a separate Marketplace policy.

Note: In the case of married taxpayers with a shared policy electing to file separately, the amounts must be allocated as follows:

If	Then
Both taxpayers are filing Married Filing Separate (FS 3)	50 percent of any APTC received must be allocated to each return, regardless of the number of exemptions claimed on either return
One taxpayer meets the requirements for filing Head of Household (FS 4)	50 percent of the APTC is allocated to each return. 50 percent of the enrollment premiums are allocated to the taxpayer filing FS 4. The SLCSP premiums are not allocated. The taxpayer filing FS 4 calculates the SLCSP premiums that are appropriate based on their tax family and reports this in Part II of Form 8962 and reports 0.5 in columns (e) and (g) of Part IV.
Both taxpayers meet the requirements for filing Head of Household (FS 4)	50 percent of the APTC and enrollment premiums are allocated to each return. The SLCSP premiums are not allocated. The taxpayers calculate the SLCSP premiums that are appropriate based on their tax family and report this in Part II of Form 8962. They report 0.5 in columns (e) and (g) of Part IV.

Reminder: Identify the shared policy in the workpapers. When communicating the basis for the adjustment to the taxpayer(s) adhere to the disclosure guidelines discussed below.

- (4) Third party data of another taxpayer (for example, Form 1095-A data found on the Coverage Data Repository(CDR)) may sometimes be needed to calculate the taxpayer's PTC. If requested by the taxpayer, you may provide the following information as long as the information is directly related to or directly affects the resolution of the taxpayers' filing\reporting requirements:

- Recipient's name
- Premium amount
- SLCSP amount
- APTC amount

Note: Only information about who received health insurance and amounts should be disclosed if the taxpayer specifically requests assistance. Never provide recipients' SSN or address. If there is a discrepancy between the information the taxpayer provides and the data on CC RTVUE or CDR, use the Form 1095-A to verify SLCSP, APTC and Premiums. The Form 1095-A data is accessible via CC IRPOL or through Business Objects. Refer to IRM 2.3.86, Command Code IRPOL, for guidance using CC IRPOL.

4.19.15.41.8
(01-01-2017)

Closing Procedures

- (1) See IRM 4.19.13.30, Campus Exam Closing Actions, paragraph (1), for closing procedures.

4.19.15.42
(10-16-2024)

General Business Credit

- (1) The General Business Credit exists as an incentive for businesses to engage in certain types of activities beneficial to the economy or public at large. The General Business Credit for a taxable year is the sum of the business credit carryforwards, the current year business credit, and the business credit carrybacks. It is not a single credit, instead it represents a compilation of specific tax credits. Each credit is tallied on its separate form first, then carried over to the Form 3800, General Business Credit. The credit was reported on Form 1040, line 54 until tax year 2018 when it was moved to Schedule 3, reported on line 12b of Form 1040 in 2018 and on line 13b in 2019. Beginning in 2020, the General Business Credit is reported on line 6a of Schedule 3 and on line 20 of Form 1040 .
- (2) In general, General Business Credits that are not used in a current year may be carried back to the preceding year, and then carried forward for up to 20 years. The marginal oil and gas well production credit may be carried back five years and carried forward 24 years. The applicable credits listed in section 6417(b) may be carried back 3 years and carried forward 22 years. It is possible that the credit being claimed on the return under examination is a carryforward or carryback of unused credits from another tax year. If this is the case, the taxpayer must submit a computation of how the carry forward was computed, and they must provide the Schedule K-1 or appropriate credit source form from the originating year. See Instructions for Form 3800 for further details.
- (3) General Business Credit is a non-refundable credit worked under PC 0420. Cases are identified through the Discretionary Examination Business Rules (DEBR) program as claiming General Business Credit with no apparent

business indicators. The return did not contain a Schedule C, E or F and IRP does not show a Schedule K-1 on file. The cases are started with ICL 566-S/566-T for TDC cases, including Form 14981, General Business Credit - Request for Supporting Documentation, requesting documentation to verify the business association to the Form 3800.

- (4) To qualify for a General Business Credit the taxpayer must be in a trade or business. Examples of a business are:
- A corporation whose stock is not publicly traded
 - A partnership or
 - A sole proprietorship.
- (5) A Pass-through entity is also referred to as a Flow-through entity. Examples are:
- S Corporation
 - Cooperative
 - Partnership
 - Estate or
 - Trust

Note: Prior to 2023, if the credit is from a pass-through entity, the entity's employer identification number must be entered on Form 3800, Part III column (d). Beginning in 2023, if the credit is from a pass-through entity, the entity's employer identification number must be entered on Form 3800, Part III column (d), Part IV column (d), Part V column (c), or Part VI column (d), as applicable.

#

- (7) The taxpayer was asked to provide:
- A complete copy of the Schedule K-1 received from the flow-through entity. The Schedule K-1 must include the entity's name and EIN, the taxpayers name and SSN, and the "Credits" line amount from the Schedule. If they are claiming the credit for more than one flow-through entity, a Schedule K-1 must be provided for each one.
 - If the amount claimed was for a carryforward from a prior year, they must include the Schedule K-1 received from the originating tax year, and a computation of how the carryforward was computed.
 - If they are claiming the credit as the owner of a business, they must provide the appropriate business schedule C, E, or F and the complete credit source form(s) that was used to calculate the credit(s) claimed on the Form 3800.
- (8) If the taxpayer is claiming the credit as the patron of a subchapter T cooperative corporation, ask the taxpayer to provide the Form 1099-PATR and the complete credit source form(s) that was used to calculate the credit(s) claimed by the patron on Form 3800.

4.19.15.42.1
(02-01-2022)
Evaluating Responses

- (1) If the taxpayer submits a Schedule K-1 in response to our inquiry, we will need to ascertain its validity. In order to validate the K-1, there must be a corresponding return filed by the Flow-Through Entity (FTE). If the entity has properly filed a return and the information on the Schedule K-1 matches the information shown on the taxpayer's Form 3800, the credit should be allowed. If the FTE has not filed a return, do not accept the Schedule K-1, and disallow any credit claimed. IDRS can be used to validate the filing of the proper return by the FTE. Command Code BMFOLT will show returns filed by the entity under their EIN.
- (2) If the taxpayer states that the credit is from a business owned by the taxpayer, further documentation will be required. This includes a copy of the applicable credit source form as well as a copy of the appropriate business schedule (Schedule C, E or F). If the taxpayer does not validate the business, disallow the credit, and instruct the taxpayer to file an amended return with all appropriate credit source forms and business schedules.
- (3) Taxpayers may reply stating the credit claimed was not a General Business Credit but is a personal credit that was incorrectly claimed on Form 3800. The Form 3800 credit will be disallowed, and the taxpayer must file the correct form to claim their credit directly on Schedule 3 of Form 1040 . If the form is received by exam, then certify the tax law requirements for the new credit claimed have been met. Refer to specific form requirements in other areas of the IRM. These credits may include but are not limited to:
 - Form 5695, Residential Energy Credit
 - Form 8396, Mortgage Interest Credit
 - Form 8396, Part III and Part IV, Clean Vehicle Credits

Note: The Tax Cut and Jobs Act repealed the corporate alternative minimum tax for tax years beginning after 2017. As a result, corporations will enter zero in Part II line 14 of Form 3800.

Note: The Inflation Reduction Act of 2022 reinstated the alternative minimum tax for applicable corporations as defined in IRC 59(k).

4.19.15.43
(06-14-2023)
**Unemployment
Compensation Exclusion
(UCE)**

- (1) Cases selected for tax year 2020 only, where taxpayers excluded Unemployment Compensation over the allowable income threshold amounts, up to \$10,200 (\$20,400 for Married Filing Jointly) if they had less than \$150,000 in MAGI.
- (2) This income threshold applies to all filing statuses.
- (3) This inventory will be worked under project code 0567.
- (4) This inventory is centralized in Brookhaven and Ogden.

4.19.15.43.1
(06-14-2023)
Initial Contact Letter

- (1) Issue Letter 566-B with Form 4549.
- (2) Use RGS standard paragraph 1458, "We have made an adjustment to your income to include all taxable unemployment compensation you received. Based on the American Rescue Plan of 2021, unemployment compensation of up to \$10,200 for individuals (for married filing joint returns, this exclusion is up to \$10,200 per spouse), is only excludable from taxable income when adjusted

gross income (AGI) is less than \$150,000 (for all filing statuses).” Refer to IRM 4.10.10, Examination of Returns, Standard Paragraphs and Explanation of Adjustments.

- (3) Update CEAS and AIMS to status 22. See IRM 4.19.10.1.7.2, Standard Suspense Periods for Correspondence Examination, for appropriate timeframe.

Note: No documentation will be solicited from the taxpayer and therefore, will not be updated to status 10.

4.19.15.43.2
(06-14-2023)
Taxpayer Replies

- (1) Follow procedures in IRM 4.19.13.11.2, Evaluating Taxpayer Responses.

4.19.15.43.3
(06-14-2023)
Case Closure

- (1) Follow procedures in IRM 4.19.13.30, Campus Exam Closing Actions.

4.19.15.44
(06-14-2023)
**Schedule E - Passive
Activity Loss (PAL) -
\$25,000 Special
Allowance Cases PC
0396**

- (1) For rental real estate with active participation, a special allowance up to \$25,000 in net losses is currently deductible under IRC 469(i). In general, the special allowance begins to be phased out when Modified Adjusted Gross Income (MAGI) exceeds \$100,000 and is completely phased out when MAGI exceeds \$150,000. Losses may be carried forward until there is passive income or an entire disposition of the rental activity in a fully taxable disposition to an unrelated party.
- (2) **For single or married filing joint taxpayers (MFJ)**, for every dollar of Modified Adjusted Gross Income (MAGI) exceeding \$100,000, the \$25,000 offset for rental real estate is reduced by 50 cents. If MAGI exceeds \$150,000, then taxpayers are allowed none of the \$25,000 offset. See IRC 469(i)(3).
- (3) **Special rules apply to married taxpayers filing separately IRC 469(i)(5)**, if the taxpayers lived with their spouse at any time during the year, they do not get any deduction. If they lived apart the special allowance is \$12,500. If MAGI exceeds \$50,000, the \$12,500 offset for rental real estate is reduced by 50 cents for every dollar of excess MAGI. The entire allowance is phased out at \$75,000.
- (4) Refer to *Project Code 0396 - Passive Activity Loss Project* and Pub 925, Passive Activity and At-Risk Rules for more information.

4.19.15.44.1
(06-14-2023)
**Items to Consider when
evaluating Responses**

- (1) If filing status MFS and taxpayer lived with their spouse, disallow the deduction.
- (2) If Form 8582, Passive Activity Loss Limitations, does not contain rental losses on lines 1b or 1c, disallow the deduction.
- (3) Verify the activity is the rental of real estate. Rental of non-real property is not eligible for the special allowance.
- (4) Royalty income is portfolio income and should not be included on Form 8582.
- (5) If MAGI is greater than \$150,000 and no passive income is reported on Form 8582, disallow the deduction.

- (6) If Married Filing Separate and the taxpayer and spouse lived apart, the special allowance is limited to \$12,500. If MAGI is greater than \$75,000, no special allowance deduction allowed.
- (7) Compute the MAGI using the *Modified AGI tab* on the Passive Activity Examination Tool, for Form 1040, using the corrected AGI.
- (8) IF MAGI is greater than \$100,000 but less than \$150,000, compute the limitation to calculate the special allowance deduction.
- (9) The difference between the total calculated loss and allowable loss is the suspended loss.

Note: If there is a suspended loss, a separate issue is needed in RGS.

4.19.15.45
(10-16-2024)
Non-Filer Program

- (1) The IRS's effort to identify non-compliant taxpayers and design methods to encourage compliance is directly aligned with the National Non-Filer Strategy. The Non-Filer program, also known as SFR (Substitute for Return), and its automated version, Automated Substitute for Return (ASFR) (worked in Collections) were developed to contact taxpayers who have not filed tax returns voluntarily and for whom income information is available to substantiate a significant income tax liability.
- (2) Internal Revenue Code IRC 6212 authorizes the IRS to send a notice of deficiency whenever a deficiency is determined, including the deficiency of a taxpayer who appears to have a filing requirement but does not comply by voluntarily filing a tax return.
- (3) This IRM section contains information specific to Non-Filer Exam program guidance. This subsection is to be used in conjunction with other applicable examination guidance contained in other IRMs listed below. This list is not all inclusive.
 - IRM 4.19.13, General Case Development and Resolution
 - IRM 25.1.2.3, Indicators of Fraud
 - IRM 4.19.13.28, Campus Exam Identity Theft
 - IRM 4.19.13.33, Campus Exam Return Preparer Misconduct
 - IRM 20.1.1.3, Criteria Relief from Penalties
 - IRM 5.18.1.9.2.3.11, Freedom of Information Request
 - IRM 25.6, Statute of Limitations
 - IRM 4.19.20.2.4, B2 ACE Create/Tax Computation/Manual Review of Reports
 - IRM 4.8.9.9.2.1, Mandatory Area Counsel Review
 - IRM 4.19.13.22 , Bankruptcy Procedures - Tax Examiner Instructions
 - IRM 25.16, Disaster Assistance and Emergency Relief
 - IRM 4.19.13.9, Power of Attorney and Other Third-Party Authorizations

4.19.15.45.1
(06-14-2023)
**Letter 2269C -
Preliminary Contact with
taxpayer**

- (1) Exam Case Selection will systemically issue Letter 2269-C, Delinquent Individual Return, requesting the taxpayer to file a return within 30 days.
- (2) Cases will be opened on AIMS in status 08 with push code 036. This will post TC 150 on the module and update ENMOD to Single or Married Filing Separate.
- (3) Cases will be established in EGC (Examination Group Code) 5065.

- (4) Case action will be suspended for 45 days from Letter 2269C issuance awaiting a taxpayer response. Cases will remain in AIMS Status 08 during this suspense period.

Note: If the taxpayer files a return during this 45 day period, the case meets Non-Filer Reject criteria and will be processed according to IRM 4.19.15.45.10.1, Non-Filer Rejects, or Closure based on Fact of Filing DC 37 or DC01.

- (5) If no response from the taxpayer after the 45 day suspense period, ECS will systemically establish the case(s) on the Report Generation System (RGS). Letter 1862, Initial Contact Letter - SFR Program and , IRC 6020(b), Certification are issued to the taxpayer through automation or manually. Form 13496 is kept in the administrative file only. Do not send to the taxpayer.

Note: If a case is updated on AIMS from Status 08 during the 45 day suspense period from when the Letter 2269C was issued, the campus is required to manually start the case. Once manually started, it can be placed into ACE (B0) for automated processing. However, cases should remain in AIMS Status 08 during the delinquent return notification process to the extent possible to avoid manual starts in the campus.

4.19.15.45.2
(06-14-2023)
**Non-Filer Source and
Project Codes**

- (1) Source Code 24, Substitute for Return, and 25, Non-Filer Strategic Initiative-High Income Non-Filer are used for Non-Filer program work. Do not update from Source Code 25 to another Source Code or to Source Code 25 from another Source Code.
- (2) Source Code 24 with Project Code 0277 will be used for initiating additional Non-Filer cases identified during the course of working other programs.
- (3) Project Code 0277 is used for Non-Filer inventory.

Note: Tracking code 0911 with Project Code 0277 identifies a case as part of the Refund Hold Program.

4.19.15.45.3
(06-14-2023)
**Initial Contact Letter
1862**

- (1) Letter 1862, Initial Contact Letter SFR Program is the notification letter issued by Correspondence Exam after the preliminary contact with the taxpayer is made. Refer to IRM 4.19.15.45.1 , Letter 2269C - Preliminary Contact with taxpayer. Letter 1862 and Form 4549, Report of Income Tax Examination Changes, will be mailed and the case will be updated to Status 22.
- (2) Complete Form 13496, IRC 6020(b), Certification to maintain with the case.

4.19.15.45.4
(10-16-2024)
Manual Reports

- (1) There will be instances when a Non-Filer case rejects from ACE processing. If these cases cannot be corrected and re-introduced into batch, then a manual report must be prepared.
- (2) See IRM 4.19.13.4, **Report Generation Software (RGS) System**, for guidance for creating the examination report, including categorization of issues.
- (3) Completion of Substitute for Return (SFR):
- a. Include any income reported on behalf of the taxpayer by employers, banks, and other payers (W2, 1099, etc.).

- b. Any stock basis identified on the IRP documents will be allowed as an offset against the corresponding proceeds from the sale of that stock.
- c. No expenses/deductions (except the standard deduction) shall be allowed for the taxpayer, including mortgage interest, points, or the Qualified Business Income Deduction (QBID), unless the taxpayer files an original return. Please note that this list is not all inclusive.
- d. Allow the taxpayer any applicable federal tax withholding or estimated tax payments.

4.19.15.45.5
(06-14-2023)
IRC 6020(b) Certification

- (1) IRC 6020(b) provides that the return is prima facie good and sufficient for all legal purposes, however despite this language, for most purposes of the IRC, the 6020(b) return is not treated as a return filed by the taxpayer. For example, be aware of the following:
 - a. The amount shown as tax on an IRC 6020(b) return must be assessed under the deficiency procedures.
 - b. An IRC 6020(b) return does not start the statute of limitations on assessment.
 - c. An IRC 6020(b) return does not stop the Failure to File (FTF) Penalty.
 - d. An IRC 6020(b) return prepared using the Married Filing Separate (MFS) filing status will not prevent taxpayers from electing a Joint filing status under IRC 6013(b).
- (2) IRC 6020(b) pertains to individual income tax returns. Such returns may be automatically generated by the Campus or manually prepared with reports of proposed tax adjustments.
- (3) When the taxpayer has not filed an individual income tax return, the IRS needs to create a valid IRC 6020(b) return to apply the Failure to Pay (FTP) Penalty.
- (4) The Tax Court does not consider a mere assessment of tax or FTP penalty to constitute a "return" under the provisions of IRC 6651(a) (2) and will not sustain the penalty. Therefore, to sustain a FTP penalty on a taxpayer who has not filed a return, the IRS must, IN ALL CASES, properly process an IRC 6020(b) return according to the following Form 13496 Certification procedures or have the taxpayer sign an appropriate return.

4.19.15.45.6
(06-14-2023)
Form 13496 Certification Procedures

- (1) There are two different processes for certifying a valid IMF IRC 6020(b) return. The first is the Report Generation Software (RGS)/Automated Correspondence Exam (ACE) procedure, and the other is paper Form 13496, IRC 6020(b) Certification.
- (2) Electronic Form 13496 - The RGS/ACE IRC 6020(b) Certification and attached documents are generated systemically. Under Exam RGS/ACE procedures, the data that constitutes a valid return under IRC 6020(b) includes computation of the taxpayer's tax liability for the tax period in question and a completed Electronic Certification form with the electronic signature of the delegated IRS employee.
- (3) Paper Form 13496 Procedures - Form 13496 **MUST** be completed with a live signature if not generated systemically through RGS/ACE and **MUST** be dated on or after the date the 30-day letter (or revised 30-day letter) is signed and dated such that the date of the certification is identical to, or later than, the 30-day letter. The completed Form 13496 **MUST**:

- a. Identify the taxpayer by name and taxpayer identification number.
 - b. Contain sufficient information from which to compute the taxpayer's liability, Form 4549, Report of Income Tax Examination Changes (or the equivalent such as Form 4549-A with all schedules) and Form 886-A, Explanation of Items, or the equivalent.
 - c. Purports to be a valid IRC 6020(b) return.
 - d. Be properly signed and dated.
- (4) Form 13496 may not be prepared or dated after the date of the 90-day letter.
 - (5) Whenever the examiner revises a report of proposed adjustments that increases the total tax liability of the taxpayer (without regard to whether the revised report is reissued to the taxpayer), a re-certification is required on another Form 13496 dated on (or after) the same day as the revised report.
 - (6) When the report of proposed adjustments involves more than one tax year, create a separate Form 13496 for each year and attach each one to a photocopy of the report for each year.

4.19.15.45.7
(06-14-2023)
Non-Filer Penalties

- (1) An SFR IRC 6020(b) return must be prepared before penalties can be considered.
- (2) Penalties to be considered if no return is filed and the case is closed through deficiency procedures are:
 - a. Failure to File Penalty (FTF) IRC 6651(a)(1),
 - b. Failure to Pay Penalty (FTP) IRC 6651(a)(2), and
 - c. Estimated Tax Penalty IRC 6654 or IRC 6655.

Note: When using guidance in Special Processing for Non-Filer case, penalties to be considered on secured delinquent returns and IRC 6020(a) returns are same as above along with:

 - Fraudulent Failure to File IRC 6651(f). The burden of proof is on the Government to establish fraud. Refer to IRM 4.19.10.4, Fraud Referrals, for examples of Fraud Indicators and on how to refer returns to the Campus/Exam Fraud Coordinator.
 - Accuracy Penalty IRC 6662(a).

4.19.15.45.8
(06-14-2023)
Taxpayer Replies

- (1) Taxpayer replies include telephone inquiries, filed returns and written correspondence. The reply may be in response to a 30-day or 90-day (SNOD) letter. Follow IRM 4.19.13.11, Taxpayer Replies.
- (2) Update correspondence to the appropriate reply status per IRM 4.19.13.12, Monitoring Overage Replies.

Note: Even though a Non-filer return does not meet Policy Statement P-21-3 criteria for Interim Letter purposes, it is still considered correspondence and must be updated to Status 54, with the earliest IRS received date upon receipt of the return in Exam, unless the case is in Status 24. When in status 24, update the correspondence date to reflect the earliest IRS received date.

4.19.15.45.8.1
(06-14-2023)

**Common
Correspondence and
Telephone Inquiries**

- (1) The table below provides a list of common taxpayer replies to Non-Filer cases and guidance for resolution.

IF	THEN
Taxpayer needs more time to file a return	Consideration will be given on a case-by-case basis dependent on the taxpayers' need for the additional time. Extensions past 30 days should not be given. See IRM 4.19.13.11.6, Taxpayer Requests Additional Time to Respond.
Taxpayer filed as the secondary on a Joint return with their spouse	<ul style="list-style-type: none"> Research IDRS for fact of filing. If Joint return was filed, close case using Disposal Code 38. Send Letter 4391, Non-Examined Non-Filer. If there is no record of the filed return, issue next appropriate letter and request a signed copy be faxed, mailed or uploaded through the Document Upload Tool (DUT).
Taxpayer states they are not required to file	Verify through research and/or additional contact with the taxpayer reason(s) why they are not required to file. If verified, close case using the appropriate disposal code.
Taxpayer requests copy of income information	<p>Send sanitized IRP info (IRPTRW).</p> <p>Note: If the taxpayer is requesting spousal IRP information to file a joint return to resolve the Non-Filer compliance issue, ensure proper authority has been granted by spouse.</p>
Taxpayer wants to know how to get blank prior year forms and tax tables	Refer taxpayer to IRS website, <i>Forms, Instructions & Publications</i> .

IF	THEN
Taxpayer states that they did not receive income reported on the IRP payer document	<ul style="list-style-type: none"> Request the taxpayer secure a corrected payer document to reflect the amount they actually received or a statement from the payer to verify the amount An attempt may be made to verify IRP information through a third party contact. See IRM 25.27.1, Third-Party Contact Program. If the third party cannot be located, has ceased to operate, has not retained records from which verification can be derived, or other circumstances suggest that the IRP payer information is not reliable or accurate, remove the income from the Non-Filer deficiency proposal report. Note: If removing the income reduces the total income below the level for filing a return, close the case using Disposal Code 39 and issue Letter 4391, Non-Examined Non-Filer. If the payer information can be verified, notify taxpayer and proceed with Non-Filer case.
Taxpayer indicates they previously submitted their return	Research IDRS for fact of filing. If verified, close case using Disposal Code 37 and issue Letter 4391, Non-Examined Non-Filer.

4.19.15.45.9
(06-14-2023)
Return Validation

- (1) Delinquent returns can be received directly in the operation (in paper or digital format), posted to Master File as a duplicate return (TC 976/977), or available on TRDBV. Regardless of how the return is received, it must be verified that it is a valid, processable return.

Note: Generally, TRDBV should be considered a valid return.

Caution: Returns identified on TRDBV must be researched as indicated in IRM 4.19.15.45.9.1, Return Validation with Taxpayer Protection Program (TPP) involvement.

- (2) If the return is posted to an account has a TC 976/977 and the return is on CIS, follow guidance in IRM 4.19.15.45.10.
- (3) A taxpayer is not considered to have filed a tax return which begins the period of limitations on assessment (ASED) until the taxpayer files a valid tax return. An unsigned return is not considered a valid tax return.
- (4) If signature is missing, at least one attempt must be made to contact the taxpayer by telephone to obtain a signed return. If attempted telephone contact was not successful, document the attempt in the workpaper and send Letter 143-C, Request for Signature, see IRM 3.12.279.8, Contacting Taxpayers for Additional Information.
- (5) If no reply is received to the Letter 143-C, send the return back to the taxpayer stating the return is not acceptable due to the missing signature and that the substitute for return process will continue. Maintain a copy of page 1 and 2 of the taxpayer's return before returning and associate with the Non-Filer case in Files. Proceed with the Non-filer case putting the case back into ACE if applicable following IRM 4.19.20.2, Automated Correspondence Exam Overview (ACE).
- (6) If the requested information is received, the return is processed with a "Return Processable Date (RPD)" reflecting the date the information was received. This date is also known as the "Correspondence Received Date (CRD)". The CRD is used to calculate interest the IRS owes on refunds.

4.19.15.45.9.1
(10-16-2024)
**Return Validation with
Taxpayer Protection
Program (TPP)
involvement**

- (1) The Taxpayer Protection Program (TPP) is responsible for identifying potential identity theft cases that are scored by a set of identity theft models in the Dependent Database (DDb); selected through filters in the Return Review Program (RRP) system; or manually selected by Return Integrity Verification Operations (RIVO). For more information, see IRM 25.25.6, Taxpayer Protection Program. Refer to the chart below for actions to take when there is TPP involvement:

If	and	then
<ul style="list-style-type: none"> Unreversed TC 971 AC 124 present on IMFOLT/TXMOD and no other markers below, or TC 971 AC 506 MISC>WI PRP DDB present on ENMOD, or TC 971 AC 111 MISC>DLN must match TC 971 AC 124 MISC>DLN with MFT 32 <p>Note: Cases will not have an MFT 32 if RIVO archived/deleted shown on TRDBV. Check TXMOD for UNP 126 RC 0 to see if GUF VOIDED/DELETED</p>	no response from the taxpayer	<p>continue the examination since the return has been deemed invalid. Do not set an ASED.</p> <p>Caution: Employees should always review AMS to check for notes where the taxpayer may have authenticated their identity, but the return was never processed. If notes confirm authentication was completed, the return must be processed.</p>

If	and	then
<ul style="list-style-type: none"> Unreversed TC 971 AC 124 present on IMFOLT/TXMOD and no other markers below, or TC 971 AC 506 MISC>WI PRP DDB present on ENMOD, or TC 971 AC 111 MISC>DLN must match TC 971 AC 124 MISC>DLN with MFT 32 <p>Note: Cases will not have an MFT 32 if RIVO archived/deleted shown on TRDBV. Check TXMOD for UNP 126 RC 0 to see if GUF VOIDED/DELETED</p>	response received from the taxpayer	follow guidance in IRM 25.25.6.2.3, Exam/Collection/Compliance Office Employees – Procedures for Cases with Taxpayer Protection Program (TPP) Involvement.
TRDBV with no TC 971 AC 124, TPP indicators on the account	with or without a taxpayer response	consider TRDBV a valid signed return. Put a -A freeze on the account and forward the TRDBV print to AM for processing. Follow guidance in IRM 4.19.15.44.10, Non-Filer Closures

4.19.15.45.10
(06-14-2023)
Non-Filer Closures

- (1) IRM 4.19.13.30, Campus Exam Closing Actions, should be followed unless the case meets exceptions and/or needs additional actions specific to Non-Filer cases as described in this subsection.

4.19.15.45.10.1
(10-16-2024)
Non-Filer Rejects, or Closure Based on Fact of Filing DC 37 or DC01

- (1) For started cases in Bankruptcy, Docketed Appeals or returns within 180 days of the ASER, do not route the return to AM and follow procedures in IRM 4.19.15.45.11, Special Processing for Non-Filer Cases.
- (2) If AIMS is Status 08 or below with a TC 97X posting, close AIMS DC 37. No closing letter required.

Note: HQ may provide a listing identifying TC97X posting/NFR cases in EGC 5065. If closing per the listing, do not order the returns and close the case immediately.

- (3) If AIMS is status 08 or below, Exam secures a return, and there is no TC 97X posted, write "NFR" across the top of the return and forward to the AM site where the taxpayer would have filed. Ensure to post the -A freeze using REQ77 with an action code 010.
- (4) If AIMS status is above 08 and less than 90 and Exam secures a return, no TC 97X posted, close case DC 01 and issue Correspondex Letter 0086C to the taxpayer(s). Select an open paragraph and input the following information:
We have received your Form 1040 U.S. Individual Income Tax Return dated XX/XX/XXXX. It has been forwarded to the appropriate office for processing. If you have any questions, please call 1-800-829-1040. Write "NFR" across the top of the return and route to the AM IMF site where the taxpayer would have originally filed their timely return.
- (5) If AIMS status is above 08 and less than 90 with a TC 97X posted on the account, close case DC 01. Returns will be worked in the Individual Masterfile (IMF) AM site of the posted TC 97X.
- (6) A -A freeze must always be present on an account where AM will be processing a secured delinquent return. To close the Examination the -A freeze must temporarily be removed. Take the appropriate actions:
 - a. If -A freeze is already on the account, post a TC 290 to remove it. Place the -A freeze back on the account after AIMS closure using REQ77 with action code 010.
 - b. If no -A freeze is on the account and the return is being sent to AM to be processed, after AIMS closure input a -A freeze using REQ77 with action code 010.
 - c. Monitor the case to ensure the -A freeze posts and route to AM after it does.
- (7) Other actions that must be taken when closing DC 37 or DC 01:
 - Update the ASER when a delinquent return is secured by Exam.
 - Use appropriate hold code to ensure payments on the account do not result in an erroneous refund. See IRM 4.4.12, AIMS Procedures and Processing Instructions, for hold code information.

4.19.15.45.10.2

(06-14-2023)

**Taxpayer Previously
Filed or Filed with
Spouse DC 37 or DC 38**

- (1) Telephone call or correspondence from taxpayer states they previously filed a return and research verifies their claim:
 - a. Close the case DC 37.
 - b. Send Letter 4391, Non-Examined Non-Filer.
- (2) Telephone call or correspondence from taxpayer states they filed as secondary on a joint return with spouse and research verified the claim:
 - a. Close the case DC 38.
 - b. Send Letter 4391, Non-Examined Non-Filer.

4.19.15.45.10.3

(06-14-2023)

**Taxpayer Verifies
Income Does Not Belong
to Them DC 39**

- (1) If after contacting the taxpayer correspondence is received and the taxpayer provides verification that the income does not belong to them.
 - a. Close the case DC 39.
 - b. Send Letter 4391, Non-Examined Non-Filer.

4.19.15.45.10.4
(06-14-2023)

**Taxpayer Deceased with
No Estate or Estate
Closed DC 39**

- a. Close the case DC 39.
- b. Send Letter 4391, Non-Examined Non-Filer.

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4.19.15.45.10.5
(06-14-2023)

**Taxpayer Due a Refund
DC 41**

- (1) If prior to or after contacting the taxpayer correspondence is received or research shows the taxpayer is due a refund:
 - a. Close the case DC41.
 - b. Send Letter 2469-C, ASFR Possible Refund Letter.

4.19.15.45.10.6
(06-14-2023)

**Agreed - Signed Form
4549 DC 04 or 09**

- (1) Taxpayer submits signed Form 4549:
 - a. If pre-90 day letter/prior to Status 24, close the case DC 04.
Note: For additional closing instructions, see IRM 4.19.13.30 , Campus Exam Closing Actions.
 - b. If post-90 day letter/after in Status 24, close the case DC 09.
 - c. Update name, address, and filing status as appropriate.
 - d. Resolve any credit balances if RSED is expired.
 - e. Use Priority Code 9. The 30-Day Interest Free period will not be allowed if there is a Push Code 036 on AMDISA and Priority Code 3 or 9 is used.
 - f. Update the activity code after the examination is completed based on the new income figure. Refer to Document 6036, Examination Division Reporting System Codes Booklet, for applicable activity code.

4.19.15.45.11
(10-16-2024)

**Exam Return Processing
for Non-Filer Cases**

- (1) When a return is secured in Exam and is within 180 days of the ASSED, or the taxpayer has petitioned Tax Court (Docketed Appeals) or is in litigation for Bankruptcy, do not route to AM for processing. The return will be processed by Exam following the procedures outlined in this section.
- (2) All secured returns must be screened based on criteria outlined in IRM 21.5.2.4.23.6 , Discriminant Function (DIF) SCORE or CLASSIFICATION "Send Returns(s) to Examination for Review. Follow the steps below based on the outcome of screening the return:
 - a. If a secured return is within 180 days of the ASSED, and does not meet DIF Score or Classification criteria, accept and process the return as agreed, using the appropriate disposal code. If the return does meet criteria, continue the audit by following procedures in IRM 4.19.15.45.11.3 , Partial Assessments.
 - b. If a secured return is in Bankruptcy, and does not meet DIF Score or Classification criteria, accept and process the return as agreed, using the appropriate disposal code. If the return does meet criteria, continue the audit by following procedures in IRM 4.19.15.45.11.3, Partial Assessments and also refer to IRM 4.19.13.22, Bankruptcy Procedures - Tax Examiner Instructions.
 - c. For Docketed Appeal cases, procedures in coordination with Appeals must be followed to resolve the case. For more information refer to IRM 4.19.13.18, Appeals - Docketed Cases.

4.19.15.45.11.1
(06-14-2023)

**Entity, Filing Status, and
Dependent Verification**

- (1) The following Entity information on the taxpayer's return must be verified:
 - a. Name of the primary taxpayer is for the correct Non-Filer tax period and matches the SSN.
 - b. Spouse's name matches the SSN shown on the return and the spouse has not already filed.
 - c. Dependent(s) name(s) matches SSN shown on the return and dependent(s) is not being claimed on someone else's return.

Note: If the dependent's SSN is not valid, then the following credits cannot be allowed: Dependent exemptions, Child Tax Credit, Child Care Credit, and the Earned Income Credit.
 - d. Verify the taxpayer's correct address. If the address is different on the secured return from Master File verify the correct address with the taxpayer.
 - e. Update Entity information as appropriate.

4.19.15.45.11.2
(06-14-2023)

Math Errors

- (1) Returns must be reviewed for math errors. See IRM 5.18.1.9.2.3.21, Math Errors for guidance.
- (2) Document workpapers with math error(s) identified and actions taken to resolve them.
- (3) Include math error adjustment(s) with other examination issues on the examination report with an explanation on Form 886.
- (4) For returns that meet DIF screening criteria, follow guidance in IRM 4.19.15.45.11.3, Partial Assessments, to continue the examination process.

4.19.15.45.11.3
(06-14-2023)

Partial Assessments

- (1) Anytime a valid original return is received and additional issues are being pursued, a partial assessment per the original return filing must be made and the ASED established. A subsequent report will be created reflecting amounts per the original return assessment and unresolved issues.
- (2) Do NOT resolve credit balances on partial assessments until final case closure.
- (3) Update filing status and name line, if applicable, and Assessment Statute Expiration Date (ASED) as appropriate.
- (4) When applicable, update the activity code after the examination is completed based on the new income amount.

4.19.15.45.11.4
(06-14-2023)

**Contact After Partial
Assessment**

- (1) If the Non-Filer SNOD has already been issued and the taxpayer's filing status per the secured return is Joint, a new SNOD must be issued in the Joint name to allow the spouse the same deficiency rights the Non-Filer taxpayer received prior to making the assessment per the corrected report. It is not necessary to wait until the Non-Filer SNOD has expired before issuing a Joint SNOD or to rescind the previous Non-Filer SNOD.

4.19.15.45.12
(06-14-2023)

International Returns

- (1) Returns that appear to be international, such as returns with international addresses, or returns that contain Form 2555, Foreign Earned Income will be treated the same as any other Non-Filer case. They will no longer be transferred to Philadelphia Exam Classification.

4.19.15.45.13
(06-14-2023)

Refund Hold (RH) Cases

- (1) Refund Hold (RH) inventory occurs when the IRS holds individual income tax refunds and credit elects when a current or prior year refund return is filed and the taxpayer's account has at least one unfiled tax return within the five years prior to the current tax year. The refund is used to offset any balance due on the delinquent return(s). If there is no balance due, or an amount remains after offsetting, the refund is released to the taxpayer. If after initial contact, the delinquent return(s) are not filed, a Statutory Notice of Deficiency may be issued. Once issued, the refund can be transferred to the tax year of the proposed deficiency(ies). It will remain there until a return is filed or the IRS imposes the proposed assessment after the appropriate suspense period.
- (2) Refer to multifunctional IRM 25.12.1, Processing Refund Hold Program Inventory, for specific information.
- (3) Each functional area that is assigned a RH case is responsible for monitoring its cases and ensuring disposition of the case is expeditious and timely.
- (4) IRC 6611(e) provides that there is no interest if an overpayment is refunded within 45 days after the due date of the return, or in the case of a late filed return, within 45 days after the return is filed. If, however, the refund is not made within the 45 day period, interest must be paid from the date of overpayment. Thus, it is imperative RH cases be processed expeditiously and monitored for the most expeditious resolution possible to prevent additional cost to the IRS while processing these cases.

4.19.15.45.13.1
(06-14-2023)

Refund Hold Inventory

- (1) RH account information is passed from Master File to IDRS for processing and analysis. A Control D report, LE62740Z, is created weekly to alert Examination Operations of the RH cases in their inventory.
- (2) SB/SE Headquarters will provide each SB/SE Examination Operation a filtered Control D report of RH cases at least twice a month.
- (3) See IRM 25.12.1.2, How to Identify Delinquent Return Refund Hold, for details on identifying refund holds. Tracking code 0911 is used to track SB/SE Refund Hold cases in Correspondence Exam.
- (4) Each Examination Operation is responsible for weekly review of the report to identify cases assigned to their functional area and determining whether the refund should be released or applied to a proposed liability.
 - a. See IRM 25.12.1.1(5), Program Controls, for conditions in which a refund will be released.
 - b. If after initial contact, the delinquent return(s) are not filed, a Statutory Notice of Deficiency may be issued. Once issued, the refund can be transferred to the tax year of the proposed deficiency(ies). It will remain there until a return is filed or the IRS imposes the proposed assessment after the appropriate suspense period. All efforts to expedite RH case processing should be made. However, if the assessment cannot be made prior to the systemic release, see note below, the refund must be transferred to the tax year of the proposed deficiency to avoid premature release. Extensions to extend the refund hold period should be very limited.

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4.19.15.45.13.2
(06-14-2023)
**Refund Hold
Coordinator**

- (1) Compliance Services Examination Operations must designate functional Refund Hold Coordinators (RHC). See IRM 25.12.1.1.3, Roles and Responsibilities. Primary responsibilities are:
- a. Communicate to Headquarters Policy/Program Analyst with the responsibility for the Refund Hold Program any systemic or technical problems or issues identified during case processing.
 - b. Review and take action on all cases listed on the LE62740 CSEO weekly listings and ensure timely movement of cases including timely release or transfer of refunds
 - c. Contact the Office of Appeals or Area Counsel to determine the status and history of a RH case in Appeals or Litigation. In coordination with these offices, make a decision immediately whether to release the freeze.

