



# 4942

**VITA/TCE Specialty Courses – Cancellation of Debt (COD) and Health Savings Accounts (HSAs)**  
Volunteer Income Tax Assistance (VITA) / Tax Counseling for the Elderly (TCE)

**2011 RETURNS**



Take your VITA/TCE training online at [www.irs.gov](http://www.irs.gov) (keyword: Link & Learn Taxes). Link to the Practice Lab to gain experience using tax software and take the certification test online, with immediate scoring and feedback.

### How to Get Technical Updates?

Updates to the volunteer training materials will be contained in Publication 4491X, VITA/TCE Training Supplement mid-December. To access this publication, in the upper right hand corner of [www.irs.gov](http://www.irs.gov), type in "Pub 4491X" in the search field.

During the tax season, Volunteer Tax Alerts will be issued periodically. Type "volunteer alerts" in the search field to access all tax alerts.



### Volunteer Standards of Conduct VITA/TCE Programs

The mission of the VITA/TCE return preparation programs is to assist eligible taxpayers in satisfying their tax responsibilities by providing free tax return preparation. To establish the greatest degree of public trust, volunteers are required to maintain the highest standards of ethical conduct and provide quality service.

All VITA/TCE volunteers must complete the Volunteer Standards of Conduct Training and sign Form 13615, Volunteer Standards of Conduct Agreement prior to working at a VITA/TCE site. In addition, return preparers, quality reviewers, and VITA/TCE tax law instructors must certify in tax law prior to signing this form. This form is not valid until the site coordinator, sponsoring partner, instructor, or IRS contact confirms the volunteer's identity and signs the form.

As a volunteer participant in the VITA/TCE Programs, I will:

- 1) Follow the Quality Site Requirements (QSR).
- 2) Not accept payment or solicit donations for federal or state tax return preparation.
- 3) Not solicit business from taxpayers I assist or use the knowledge I gained (their information) about them for any direct or indirect personal benefit for me or any other specific individual.
- 4) Not knowingly prepare false returns.
- 5) Not engage in criminal, infamous, dishonest, notoriously disgraceful conduct, or any other conduct deemed to have a negative effect on the VITA/TCE Programs.
- 6) Treat all taxpayers in a professional, courteous, and respectful manner.

Failure to comply with these standards could result in, but is not limited to, the following:

- Removal from the VITA/TCE Programs and inclusion on volunteer registry;
- Deactivation of your Partner's VITA/TCE EFIN (electronic ID number);
- Removal of all IRS products, supplies, loaned equipment, and taxpayer information;
- Termination of the sponsoring organizations partnership with IRS;
- Termination of sponsoring organization grant funds; and
- Subjection to criminal investigations.

Tax Wise® is a copyrighted software program owned by CCH Small Firm Services (CCH). All screen shots that appear throughout the official Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) training materials are used with the permission of CCH. The screen shots used in this publication—or any other screen shots from Tax Wise or its affiliated programs—may not be extracted, copied, or distributed without written approval from the IRS SPEC Office of Education and Product Development.

#### Confidentiality Statement:

All tax information you receive from taxpayers in your VOLUNTEER capacity is strictly confidential and should not, under any circumstances, be disclosed to unauthorized individuals.

All persons, scenarios, and addresses appearing in this product are fictitious. Any resemblance to persons living or dead is purely coincidental.



# VITA/TCE Specialty Courses – Cancellation of Debt (COD) and Health Savings Accounts (HSAs)

## Table of Contents

---

|   |      |
|---|------|
| Cancellation of Debt (COD) Course . . . . .                         | 1-1  |
| COD Practice Scenarios . . . . .                                    | 1-24 |
| COD Qualified Principal Residence Indebtedness Test Questions . . . | 1-42 |
| COD Nonbusiness Credit Card Indebtedness Test Questions . . . . .   | 1-54 |
| COD Retest Questions . . . . .                                      | 1-64 |
| Health Savings Accounts (HSAs) Course . . . . .                     | 2-1  |
| HSA Practice Scenarios . . . . .                                    | 2-21 |
| HSA Test Questions. . . . .   | 2-34 |
| HSA Retest Questions. . . . .                                       | 2-47 |





# Cancellation of Debt (COD)



## Introduction

The Cancellation of Debt course is optional specialty training for volunteers with an Advanced, Military, or International Certification. A separate certification is required for volunteers on cancellation of debt issues. Check with your Site Coordinator to determine whether you should be certified in this topic.

This course will help you recognize when you can help taxpayers who have a canceled debt and when you must refer them elsewhere for help with their tax returns.

## Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Identify the difference between recourse and nonrecourse debt
- Identify the exceptions and exclusions to the general rule for the cancellation of debt income
- Determine when cancellation of debt for principal residence or credit card is within scope for the VITA/TCE program
- Determine the filing requirements for recipients of Form 1099-A and Form 1099-C
- Determine if a taxpayer may exclude from taxable income certain debt forgiven or canceled on a principal residence
- Determine when canceled credit card debt is included in gross income on Form 1040

## Cancellation of Debt – Basics

Cancellation of indebtedness can involve auto loans, credit card debt, medical care, professional services, installment purchases of furniture or other personal property, mortgages, and home equity loans. A debt includes any indebtedness for which a taxpayer is liable or which attaches to the taxpayer's property. Generally, if a debt for which a taxpayer is personally liable is canceled or forgiven, other than as a gift or bequest, the taxpayer must include the canceled amount in income.

### What is in scope for VITA/TCE?

Only two types of cancellation of debt issues are in scope for VITA/TCE:

- Qualified principal residence debt, and
- Nonbusiness credit card debt

For all other cancellation of debt issues, refer the taxpayer to a professional tax preparer.

### What do I need?

- Intake and Interview Sheet
- Publication 4012, Volunteer Resource Guide
- Publication 17
- Publication 4731

### Optional

- Publication 4491-W
- Publication 4681
- Publication 523
- Publication 525
- Publication 544
- Publication 551
- Form 982
- Form 1040 and Instructions
- Form 1099-A and Instructions
- Form 1099-C and Instructions
- Form 8949
- Schedule D and Instructions

## Taxability of Canceled Debt

Taxpayers often question the taxability of canceled debt because they did not receive money in hand. In situations where property is surrendered, such as a foreclosure, taxpayers feel that, by giving up the property, they are relieved from any further obligation. Explain that the benefit to the taxpayer is the relief from personal liability to pay the debt. Information in Publication 17 can assist with the explanation.

Additional resources include:

- Publication 523, Selling Your Home
- Publication 525, Taxable and Nontaxable Income
- Publication 544, Sales and Dispositions of Assets
- Publication 4681, Canceled Debts, Foreclosures, Repossessions, and Abandonments
- Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt

Generally, when debt is canceled, the lender will issue Form 1099-C, Cancellation of Debt, which is then reported by the recipients on their tax return. Exceptions and exclusions to the general rule that canceled debt is included in income are discussed later in this course.

## Recourse vs. Nonrecourse Debt

Debt for which a borrower is personally liable is referred to as recourse debt. All other debt is considered nonrecourse debt. Whether a debt is recourse or nonrecourse may vary from state to state, depending on state law.

If a lender cancels a debt and issues Form 1099-C, the lender will indicate on the form in box 5 if the borrower was personally liable (recourse) for repayment of the debt. The tax impact depends on the type of debt – recourse or nonrecourse.

### TIP

If property securing the debt was foreclosed on or abandoned, the taxpayer may need to report the disposition (sale) on Form 8949 and Schedule D. This is covered in more detail later in this course.

### TIP

Generally, if the taxpayer abandons property that secures debt for which the taxpayer is **personally liable**, the taxpayer does not have gain or loss until the later foreclosure is completed.

If the taxpayer abandons property that secures debt for which the taxpayer is **not personally liable**, the abandonment is treated as a sale or exchange.

For more information on abandonments see Publication 4681.

**Recourse debt** holds the borrower personally liable for any amount not satisfied by the surrender of *secured property*.

- If a lender forecloses on property subject to a recourse debt and cancels the portion of the debt in excess of the fair market value (FMV) of the property, the canceled portion of the debt is treated as ordinary income from cancellation of indebtedness. This amount must be included in gross income unless it qualifies for an exception or exclusion.
- In addition to this cancellation of indebtedness income, the taxpayer may realize a gain or loss on the disposition of the property; this amount is generally the difference between the FMV of the property at the time of the foreclosure and the taxpayer's adjusted basis in the property.

**Nonrecourse debt** is satisfied by the surrender of the *secured property* regardless of the FMV at the time of surrender, and the borrower is not personally liable for the debt.

- If property that is subject to nonrecourse debt is abandoned, foreclosed upon, subject of a short sale, or repossessed by the lender, the circumstances are treated as a sale of the property by the taxpayer.
- In determining the gain or loss on the disposition of the property, the balance of the nonrecourse debt at the time of the disposition of the property is included in the amount realized (generally the selling price). Since the borrower is not personally liable for the debt, the difference between the FMV of the property and the balance of the loan is *not* included in gross income.

|   | <b>Recourse Debt</b>   | <b>Nonrecourse Debt</b>  |
|---|--|--|
| Borrower is...                              | Personally liable  | Not personally liable  |
| Canceled portion of debt is generally...    | Treated as ordinary income and included in gross income (unless it qualifies as an exception or exclusion) | Not applicable. Nonrecourse debt is satisfied by the surrender of the secured property regardless of the FMV at the time of surrender.   |
| Gain or loss on disposition of the property | Generally determined by the difference between the FMV of the property and the adjusted basis              | The amount realized includes the balance of the nonrecourse debt at the time of the disposition of the property. This is true even if the FMV of the property is less than the outstanding debt. |

#### example

Jason lost his home to foreclosure because he could no longer make his mortgage payments. At the time of foreclosure, he owed a balance of \$170,000 to the lender and the FMV of the property was \$140,000.

If Jason is personally liable for the debt (recourse loan), the selling price would be \$140,000.

If Jason is not personally liable for the debt (nonrecourse loan), the selling price would be \$170,000.

## Exceptions and Exclusions

Some canceled or forgiven debts may be *eliminated* from income by applying exceptions, or *reduced* by applying exclusions to the general rule. **Exceptions are applied before exclusions.**

### **Exceptions**

There are several exceptions to the inclusion of canceled debt in income. Exceptions may allow the taxpayer to eliminate the following types of canceled debt from income:

- Amounts otherwise excluded from income (e.g., gifts and bequests)
- Certain student loans (e.g., doctors, nurses, and teachers serving in rural or low-income areas)
- Deductible debt (e.g., home mortgage interest that would have been deductible on Schedule A)
- Price reduced after purchase (e.g., debt on solvent taxpayer's property is reduced by the seller; basis of property must be reduced)

For more information on exceptions, refer to Publication 4681, Canceled Debts, Foreclosures, Repossessions, and Abandonments.

## Exclusions

There are several exclusions from the general rule for reporting canceled debt as income.

Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness, must be filed with the taxpayer's return to show the amount of the canceled debt excluded.

The exclusions are:

- Discharge of debt through bankruptcy
- Discharge of debt of insolvent taxpayer
- Discharge of qualified farm indebtedness
- Discharge of qualified real property business indebtedness
- Discharge of qualified principal residence indebtedness



The issues involved in exclusions can be complex. Only cancellation of qualified principal residence indebtedness is within the scope of VITA/TCE.

## Cancellation of Debt—Principal Residence

---

### Mortgage Forgiveness Debt Relief Act 2007

Under the Mortgage Forgiveness Debt Relief Act of 2007, taxpayers may exclude from income certain debt forgiven or canceled on their principal residence. This exclusion is applicable to the discharge of “qualified principal residence indebtedness.” If the canceled debt qualifies for exclusion from gross income, the debtor may be required to reduce tax attributes (certain credits, losses, and basis of assets) by the amount excluded.

If a property was taken by the lender (foreclosure) or given up by the borrower (abandonment), the lender usually sends the taxpayer Form 1099-A, Acquisition or Abandonment of Secured Property. Form 1099-A will have information needed to determine the gain or loss due to the foreclosure or abandonment.

If the debt is canceled, the taxpayer will receive Form 1099-C, Cancellation of Debt. If foreclosure/abandonment and debt cancellation occur in the same calendar year, the lender may issue only Form 1099-C, including the information otherwise reported on Form 1099-A.

### What is qualified principal residence indebtedness?

Only the exclusion involving cancellation of debt for qualified principal residence indebtedness is within scope for the VITA/TCE program. Qualified principal residence indebtedness includes:

- Any debt incurred in acquiring, constructing, or substantially improving a principal residence and which is secured by the principal residence
- Any debt *secured by the principal residence resulting from the refinancing of debt* incurred to acquire, construct, or substantially improve a principal residence, but only to the extent the amount of the debt does not exceed the amount of the refinanced debt



A principal residence is generally the home where the taxpayer lives most of the time. A taxpayer can have only one principal residence at a time.

### Exclusion Limit

The maximum amount that can be treated as qualified principal residence indebtedness is \$2 million (\$1 million if Married Filing Separately).

Canceled qualified principal residence indebtedness cannot be excluded from income if the cancellation was for services performed for the lender or because of any factor not directly related to a decline in the value of the residence or the taxpayer's financial condition.

## **Applicable Tax Years**

The Mortgage Forgiveness Debt Relief Act of 2007 allows for the exclusion of discharged qualified principal residence indebtedness canceled in 2007, 2008, and 2009.

The Emergency Economic Stabilization Act of 2008 extended the exclusion for tax years 2010 through 2012.

## **Criteria for VITA/TCE Program**

Volunteers may assist taxpayers who meet the following requirements for excluding canceled principal residence debt from income:

- The home was never used in a business or as rental property
- The debt was not canceled because the taxpayer filed bankruptcy (Form 1099-C, box 6 is not checked)
- The taxpayer is **not** in bankruptcy when he/she comes to the site for assistance
- Form 1099-C, box 3 does not include an amount for interest
- The debt must be a mortgage used only to buy, build, or substantially improve the taxpayer's primary residence, i.e., this money was not used to pay off credit cards, medical/dental expenses, vacations, etc.
- The mortgage was secured by the taxpayer's primary residence
- The mortgage was not more than \$2 million (\$1 million if Married Filing Separately)

If the taxpayers do not meet these requirements, they may still qualify for the exclusion. However, the issues may be complex and beyond the scope of VITA/TCE. Such taxpayers should be referred to a professional tax preparer.

Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt, provides step-by-step guidance for the volunteer tax-return preparer to determine if the cancellation of debt is within scope. Part I addresses home mortgage loans. A copy of the screening sheet can be found in the Volunteer Resource Guide (Tab D).

The intake and interview sheet includes a question specifically related to canceled debts and foreclosures. Be sure to ask taxpayers if they underwent foreclosure or if their financial institution canceled a portion of the debt on their home. If so, continue your probing interview guided by Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt, to identify taxpayers with cancellation of debt issues that are within the scope of the VITA/TCE programs.

### **example**

Bob refinanced his personal residence and used the loan proceeds from the equity in his home to build a new master bedroom suite on the main level of his house. This debt is qualified principal residence indebtedness.

### **example**

Tom refinanced his personal residence and used the loan proceeds from the equity in his home to pay off credit cards and buy a car. This debt is not qualified principal residence indebtedness.



## EXERCISES

Use Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt to answer the following questions. The answers appear at the end of the lesson.

**Question 1:** A volunteer with Cancellation of Debt Certification is working with taxpayer Angie. Angie confirmed that she had to give up her principal residence and produced Form 1099-C for the cancellation of the mortgage loan. Angie explains that she did not file for bankruptcy, even though she experienced hardship due to the loss of income from no longer being able to rent out an upstairs bedroom and bath. Angie also verified that the mortgage loan was used entirely to purchase the home and was secured by the home. Her Form 1099-C lists the amount of debt canceled as \$60,000.

Should the volunteer assist Angie with her return?  Yes  No

**Question 2:** Fred went to his local VITA site to have his tax return prepared. The volunteer went through Fred's records and noticed Form 1099-C reflecting a canceled debt of \$50,000.

Using Publication 4731 as a guide, the volunteer learned Fred lost his job and could no longer make his mortgage payments. The bank foreclosed on Fred's home. Due to the housing market slump, the value of Fred's home had declined, and his mortgage balance was more than the fair market value of the home. The bank sold Fred's home and canceled the remaining debt (\$50,000) not covered by the sale price.

Upon further questioning, the volunteer learned Fred had refinanced his home two years ago and used the equity in the home to pay off some credit cards and take a trip to Las Vegas.

Should the volunteer assist Fred with the preparation of his return at the VITA site?  Yes  No

### Tax Issues Outside the Scope of the VITA/TCE Program

If the cancellation of debt issue is not within the scope of the VITA/TCE program, the taxpayer may still qualify to exclude all or part of the discharged debt. In these instances, the volunteer should provide the taxpayer with:

- The resources and possible referrals that are provided in Step 6 of Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt
- A referral based on the taxpayer's need; one of many options includes referring the taxpayer to a professional tax preparer

### IRS References and Tools for Taxpayers with Canceled Mortgage Debt

Some taxpayers may want to research tax topics on their own. Refer them to [www.irs.gov](http://www.irs.gov) for the most up-to-date information on tax issues. To find information on canceled debt, advise the taxpayer to type, "cancellation of debt" in the website's search box.

#### ***Interactive Tax Assistant (ITA)***

Another referral option is the Interactive Tax Assistant (ITA), an online resource that takes the taxpayer through a series of questions and provides responses to questions on a number of tax law topics. To access this interactive tool, advise the taxpayer to go to [www.irs.gov](http://www.irs.gov) and type "ITA" in the website's search box.

One topic covered by ITA is, “Do I Have Cancellation of Debt Income on My Personal Residence?” The ITA application helps taxpayers determine if they have to report income from the cancellation of debt on their principal residence. In order to use this application, the taxpayer will need information about the canceled debt, including the outstanding balance, fair market value of the property, and reason the debt was canceled. Much of this information can be found on Form 1099-C, received from their creditor.

The ITA conducts an interactive interview addressing tax issues for the cancellation of a principal residence. After all the questions are answered, ITA provides a response screen and a simple way to print the entire interview and the final response.

## Foreclosures and Capital Gain or Loss

If a taxpayer does not make payments owed on a loan secured by property, the lender may foreclose on the loan or repossess the property. The foreclosure or repossession is treated as a sale from which the taxpayer may realize gain or loss. This is true even if the taxpayer voluntarily returns the property to the lender.

Figure the gain or loss from a foreclosure or repossession the same way as the gain or loss from a sale. The gain is the difference between the amount realized and the adjusted basis of the transferred property (amount realized minus adjusted basis). The loss is the difference between the adjusted basis in the transferred property and the amount realized (adjusted basis minus amount realized).

When a residence that is security for a mortgage is abandoned or foreclosed upon, the gain or loss that must be reported on the return is subject to the rules for a Sale of Residence.

Generally, the amount realized on a foreclosure is considered to be the selling price. But this selling price depends, in part, on whether the debt was recourse debt or nonrecourse debt. In addition, the taxpayer may also have ordinary income from the cancellation of debt.

Use the Worksheet for Foreclosures and Repossessions in Publication 4681 to figure the ordinary income from the cancellation of debt and the gain or loss from a foreclosure or repossession.

Generally, the taxpayer’s gain or loss from a foreclosure or abandonment is reported on Form 8949 and Schedule D.

If the taxpayer is personally liable for the debt (recourse debt), and the amount of outstanding debt (mortgage) is more than the home’s FMV, the difference is treated as cancellation of debt income.

- If the canceled debt qualifies as excludable from gross income, the exclusion is reported on Form 982
- Otherwise, the canceled debt is reportable as ordinary income on Form 1040, line 21 and is beyond the scope of VITA/TCE

## Form 1099-A

When a personal residence is foreclosed upon, and the lender cancels a portion of the debt, the taxpayer will generally receive Form 1099-A, Acquisition or Abandonment of Secured Property, and Form 1099-C, Cancellation of Debt. If, in the same calendar year, the debt is canceled in connection with a foreclosure of secured property, the lender has the option of issuing Form 1099-C only.



A loss on the sale or disposition of a personal residence is not deductible. A gain may qualify for the Section 121 exclusion (\$250,000 or \$500,000 for Married Filing Jointly taxpayers) for a gain on the sale of a personal residence.



If the canceled debt is reportable on Form 1040, line 21 or the canceled debt is not fully excludable from gross income, the issue is beyond the scope of the VITA/TCE program.

The filing requirements of Form 1099-A are met by the lender completing the following boxes on Form 1099-C:

- Box 4 (debt description)
- Box 5 (if checked, the debtor was personally liable for the repayment of the debt),
- Box 7 (fair market value of property)

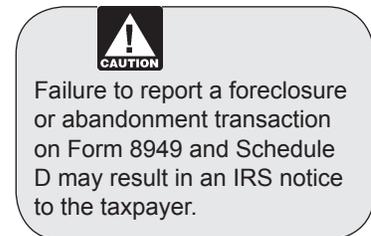
Verify with the taxpayer that the information on Form 1099-A and Form 1099-C is correct. Pay particular attention to the amount of debt forgiven and the fair market value reported. Advise the taxpayer to contact the lender immediately if any of the information is not correct.

Form 1099-A, issued by the lender, reports the outstanding debt and the fair market value of the property. This form provides information needed to determine the amount of any gain or loss due to foreclosure or abandonment. Report the gain or loss from Form 1099-A on Form 8949 and Schedule D.

The sale price (amount realized) is based on whether the taxpayer is personally liable (recourse loan) or not personally liable (nonrecourse loan) for the debt.

- If the taxpayer is personally liable, the sale price is the lesser of the balance of the principal mortgage debt outstanding or the fair market value
- If the taxpayer is not personally liable, then the sale price is the full amount of the outstanding debt, as reflected in Form 1099-A, box 2
- For both recourse and nonrecourse loans, add any proceeds the taxpayer received from the foreclosure sale to the amount realized

Generally, if there is a loss on the sale of a principal residence or the entire gain is excluded under the Section 121 exclusion (\$250,000 or \$500,000 for Married Filing Jointly), the sale does not have to be reported. However, taxpayers who receive Form 1099-A should report the sale to account for the basis in the property.



### ***Gain or Loss Reported on Form 8949 and Schedule D***

**NEW** Schedule D, Capital Gains and Losses: Individual transactions are no longer listed on Schedule D. Subtotal amounts from Form 8949 are carried over to both the short and long-term sections of Schedule D.

Form 8949, Sales and Other Dispositions of Capital Assets: Includes all capital gain and loss transactions. The subtotals from Form 8949 are carried over to Schedule D where gain or loss is calculated in aggregate.

- A checkbox at the top of Form 8949 identifies the type of transaction reported
- Column (b) is for a code used to indicate various adjustments to gain or loss
- Column (g) indicates the amount of the adjustment to gain or loss

Losses on a personal residence are never deductible. Gains (all or part) may be excluded under the rules regarding the sale of a personal residence (Section 121 exclusion).

The following is a sample of some of the more common Form 8949 codes you might use and how to complete columns (b) and (g) of Form 8949. The codes and explanations below are from the **DRAFT** Instructions for Schedule D (and Form 8949). For a complete listing of the **FINAL** codes, see the Instructions for Schedule D (and Form 8949) posted on [www.irs.gov](http://www.irs.gov).

| If...  | Then enter in Form 8949 column (b)... | And...  |
|--|---------------------------------------|---|
| You sold your main home at a gain, must report the sale on Form 8949, and can exclude some or all of the gain from the sale...   | A                                     | Enter the amount of excluded (nontaxable) gain as a negative number (in parentheses) in column (g).   |
| You have a nondeductible loss from the sale or exchange of a capital asset you held for personal use...  | E                                     | Enter the amount of the nondeductible loss as a positive number in column (g).  |
| You have a nondeductible loss other than a loss indicated by code AR, PA, W, or E...   | F                                     | Enter the amount of the nondeductible loss as a positive number in column (g).  |
| You received a Form 1099-B (or substitute statement) and the type of gain or loss indicated in box 8 is incorrect...   | D                                     | Enter -0- in column (g) unless an adjustment is required because of another code. Report the gain or loss in the correct Part of Form 8949. |
| You received a Form 1099-B (or substitute statement), the basis shown in box 3 is incorrect, and the correct basis is higher than the basis shown in box 3 of Form 1099-B (or substitute statement)... | B                                     | Enter the difference between the two amounts as a negative number (in parentheses) in column (g).   |
| You received a Form 1099-B (or substitute statement), the basis shown in box 3 is incorrect, and the correct basis is lower than the basis shown in box 3 of Form 1099-B (or substitute statement)...  | C                                     | Enter the difference between the two amounts as a positive number in column (g).  |
| You have an adjustment not explained above in this column...   | M                                     | Enter the appropriate adjustment in column (g). Attach an explanation.  |

The following examples show three different versions of Form 8949 and Schedule D reporting information from Form 1099-A.

**Example 1: Foreclosure results in loss (nondeductible)**

CORRECTED (if checked)

|  |  |  |   |
|--|--|--|---|
| LENDER'S name, street address, city, state, ZIP code, and telephone no.<br><b>First Home Mortgage<br/>PO Box 12<br/>Your City, State and Your Zip Code</b> |  | OMB No. 1545-0877<br><b>2011</b><br>Form 1099-A  | <b>Acquisition or<br/>Abandonment of<br/>Secured Property</b> |
| LENDER'S federal identification number<br><b>59-7XXXXXX</b>  | BORROWER'S identification number<br><b>383-XX-XXXX</b> | 1 Date of lender's acquisition or knowledge of abandonment<br><b>10/01/2011</b>  | 2 Balance of principal outstanding<br><b>\$ 275,000.00</b>    |
| BORROWER'S name<br><b>Duncan Smith</b>   |  | 3  | 4 Fair market value of property<br><b>\$ 200,000.00</b>       |
| Street address (including apt. no.)<br><b>8000 Pear Lane</b><br>City, state, and ZIP code<br><b>Your City, State and Your Zip Code</b>                     |  | 5 If checked, the borrower was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |   |
| Account number (see instructions)  |  | 6 Description of property<br><b>1000 Anywhere Street<br/>Anywhere Town, State and Zip</b>                                |   |

Form 1099-A (keep for your records) Department of the Treasury - Internal Revenue Service

Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Do not enter name and social security number if shown on other side. Your social security number

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note.** Please round and use whole dollars on this form.  
Check the box below that describes the transactions listed on this page.  
**Caution.** Check only one box. If you have more than one type of transaction, complete a separate Form 8949 for each type.

(A) Long-term gains and losses (Form 1099-B, box 3, shows basis)     (B) Long-term gains and losses (Form 1099-B, box 3, does not show basis)     (C) Long-term gains and losses (Form 1099-B not received)

| 3 (a) Description of property<br>(Example: 100 sh. XYZ Co.)  | (b) Code | (c) Date acquired<br>(Mo., day, yr.) | (d) Date sold<br>(Mo., day, yr.) | (e) Sales price<br>(see instructions) | (f) Cost or other basis<br>(see instructions) | (g) Adjustments to<br>gain or loss |
|--|----------|--------------------------------------|----------------------------------|---------------------------------------|---|------------------------------------|
| <b>Main Home - Form 1099-A Foreclosure</b>   | <b>E</b> | <b>5/15/2002</b>                     | <b>10/01/2011</b>                | <b>\$200,000</b>                      | <b>\$300,000</b>                              | <b>\$100,000</b>                   |
| <b>4 Totals.</b> Add the amounts in columns (e) and (f). Also, combine the amounts in column (g). Enter here and include on Schedule D, line 8 (if box A above is checked), line 9 (if box B above is checked), or line 10 (if box C above is checked) . . . . . ▶ |          |                                      |                                  | <b>4</b>                              | <b>\$200,000</b>                              | <b>\$300,000</b>                   |

Form 8949 (2011)

**7 Net short-term capital gain or (loss).** Combine lines 1 through 6 in column (h) . . . . .

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note:** Please round and use whole dollars on this form.

|  | (e) Sales price from Form(s) 8949, line 4, column (e) | (f) Cost or other basis from Form(s) 8949, line 4, column (f) | (g) Adjustments to gain or loss from Form(s) 8949, line 4, column (g) | (h) Gain or (loss) Combine columns (e), (f), and (g) |
|--|---|---|---|--|
| <b>8</b> Long-term totals from all Forms 8949 with box A checked in Part II . . . . .  |   | ( )   |   |  |
| <b>9</b> Long-term totals from all Forms 8949 with box B checked in Part II . . . . .  |   | ( )   |   |  |
| <b>10</b> Long-term totals from all Forms 8949 with box C checked in Part II . . . . .   | <b>\$200,000</b>                                      | <b>( \$300,000 )</b>  | <b>\$100,000</b>  | <b>\$0</b>   |
| <b>11</b> Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824 . . . . .           |   |   |   | <b>11</b>  |
| <b>12</b> Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1 . . . . .                                     |   |   |   | <b>12</b>  |
| <b>13</b> Capital gain distributions. See the instructions . . . . .   |   |   |   | <b>13</b>  |
| <b>14</b> Long-term capital loss carryover. Enter the amount, if any, from line 13 of your <b>Capital Loss Carryover Worksheet</b> in the instructions . . . . . |   |   |   | <b>14</b> ( )  |
| <b>15</b> <b>Net long-term capital gain or (loss).</b> Combine lines 8 through 14 in column (h). Then go to Part III on the back . . . . .                       |   |   |   | <b>\$0</b>   |

For Paperwork Reduction Act Notice, see your tax return instructions.      Cat. No. 11338H      Schedule D (Form 1040) 2011

**Example 2: Foreclosure results in gain - Section 121 Exclusion applied to total gain**

CORRECTED (if checked)

|  |  |  |   |
|--|--|--|---|
| LENDER'S name, street address, city, state, ZIP code, and telephone no.<br><b>First Home Mortgage<br/>PO Box 12<br/>Your City, State and Your Zip Code</b> |  | OMB No. 1545-0877<br><b>2011</b><br>Form 1099-A  | <b>Acquisition or<br/>Abandonment of<br/>Secured Property</b> |
| LENDER'S federal identification number<br><b>59-7XXXXXX</b>  | BORROWER'S identification number<br><b>383-XX-XXXX</b> | 1 Date of lender's acquisition or knowledge of abandonment<br><b>10/01/2011</b>  | 2 Balance of principal outstanding<br><b>\$ 275,000.00</b>    |
| BORROWER'S name<br><b>Abby Smith</b>   |  | 3  | 4 Fair market value of property<br><b>\$ 200,000.00</b>       |
| Street address (including apt. no.)<br><b>8000 Maple Lane</b><br>City, state, and ZIP code<br><b>Your City, State and Your Zip Code</b>                    |  | 5 If checked, the borrower was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |   |
| Account number (see instructions)  |  | 6 Description of property<br><b>1000 Anywhere Street<br/>Anywhere Town, State and Zip</b>                                |   |

Form 1099-A (keep for your records) Department of the Treasury - Internal Revenue Service

Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Do not enter name and social security number if shown on other side. Your social security number

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note.** Please round and use whole dollars on this form.  
Check the box below that describes the transactions listed on this page.  
**Caution.** Check only one box. If you have more than one type of transaction, complete a separate Form 8949 for each type.

(A) Long-term gains and losses (Form 1099-B, box 3, shows basis)     (B) Long-term gains and losses (Form 1099-B, box 3, does not show basis)     (C) Long-term gains and losses (Form 1099-B not received)

| 3 (a) Description of property (Example: 100 sh. XYZ Co.)   | (b) Code | (c) Date acquired (Mo., day, yr.) | (d) Date sold (Mo., day, yr.) | (e) Sales price (see instructions) | (f) Cost or other basis (see instructions) | (g) Adjustments to gain or loss |                   |
|--|----------|-----------------------------------|-------------------------------|------------------------------------|--|---------------------------------|-------------------|
| <b>Main Home - Form 1099-A</b>   | <b>A</b> | <b>5/15/2002</b>                  | <b>10/01/2011</b>             | <b>\$200,000</b>                   | <b>\$125,000</b>                           | <b>(\$75,000)</b>               |                   |
| <b>4 Totals.</b> Add the amounts in columns (e) and (f). Also, combine the amounts in column (g). Enter here and include on Schedule D, line 8 (if box A above is checked), line 9 (if box B above is checked), or line 10 (if box C above is checked) . . . . . |          |                                   |                               | <b>4</b>                           | <b>\$200,000</b>                           | <b>\$125,000</b>                | <b>(\$75,000)</b> |

Form **8949** (2011)

**7 Net short-term capital gain or (loss).** Combine lines 4 through 6 in column (g) . . . . .

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note:** Please round and use whole dollars on this form.

| (e) Sales price from Form(s) 8949, line 4, column (e)  | (f) Cost or other basis from Form(s) 8949, line 4, column (f) | (g) Adjustments to gain or loss from Form(s) 8949, line 4, column (g) | (h) Gain or (loss) Combine columns (e), (f), and (g) |
|--|---|---|--|
| <b>8</b> Long-term totals from all Forms 8949 with box A checked in Part II . . . . .  | ( )   |   |  |
| <b>9</b> Long-term totals from all Forms 8949 with box B checked in Part II . . . . .  | ( )   |   |  |
| <b>10</b> Long-term totals from all Forms 8949 with box C checked in Part II . . . . .   | <b>\$200,000</b>  | <b>(\$125,000)</b>  | <b>(\$75,000)</b>                                    |
| <b>11</b> Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824 . . . . .           |   |   | <b>11</b>  |
| <b>12</b> Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1 . . . . .                                     |   |   | <b>12</b>  |
| <b>13</b> Capital gain distributions. See the instructions . . . . .   |   |   | <b>13</b>  |
| <b>14</b> Long-term capital loss carryover. Enter the amount, if any, from line 13 of your <b>Capital Loss Carryover Worksheet</b> in the instructions . . . . . |   |   | <b>14</b> ( )  |
| <b>15</b> Net long-term capital gain or (loss). Combine lines 8 through 14 in column (h). Then go to Part III on the back . . . . .                              |   |   | <b>15</b> <b>\$0</b>                                 |

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 11338H Schedule D (Form 1040) 2011

**Example 3: Foreclosure results in gain - Section 121 Exclusion applied to part of gain**

CORRECTED (if checked)

|   |  |  |   |
|---|--|--|---|
| LENDER'S name, street address, city, state, ZIP code, and telephone no.<br><b>First Home Mortgage<br/>PO Box 12<br/>Your City, State and Zip Code</b> |  | OMB No. 1545-0877<br><b>2011</b><br>Form 1099-A  | <b>Acquisition or<br/>Abandonment of<br/>Secured Property</b> |
| LENDER'S federal identification number<br><b>59-7XXXXXX</b>   | BORROWER'S identification number<br><b>383-XX-XXXX</b> | 1 Date of lender's acquisition or knowledge of abandonment<br><b>11/30/2011</b>                                | 2 Balance of principal outstanding<br><b>\$ 500,000.00</b>    |
| BORROWER'S name<br><b>Lillie Smith</b>  |  | 3  | 4 Fair market value of property<br><b>\$ 350,000.00</b>       |
| Street address (including apt. no.)<br><b>8000 Pine Lane</b><br>City, state, and ZIP code   |  | 5 If checked, the borrower was personally liable for repayment of the debt <input checked="" type="checkbox"/> |   |
| Account number (see instructions)<br><b>Your City, State and Zip Code</b>   |  | 6 Description of property<br><b>1000 Anywhere Street<br/>Anywhere Town, State and Zip</b>                      |   |

Form 1099-A (keep for your records) Department of the Treasury - Internal Revenue Service

Form 8949 (2011) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Do not enter name and social security number if shown on other side. Your social security number

---

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note.** Please round and use whole dollars on this form.  
Check the box below that describes the transactions listed on this page.  
**Caution.** Check only one box. If you have more than one type of transaction, complete a separate Form 8949 for each type.

(A) Long-term gains and losses (Form 1099-B, box 3, shows basis)     (B) Long-term gains and losses (Form 1099-B, box 3, does not show basis)     (C) Long-term gains and losses (Form 1099-B not received)

| 3 (a) Description of property<br>(Example: 100 sh. XYZ Co.)  | (b) Code | (c) Date acquired<br>(Mo., day, yr.) | (d) Date sold<br>(Mo., day, yr.) | (e) Sales price<br>(see instructions) | (f) Cost or other basis<br>(see instructions) | (g) Adjustments to gain or loss |
|--|----------|--------------------------------------|----------------------------------|---------------------------------------|---|---------------------------------|
| <b>Main Home - Form 1099-A</b>   | <b>A</b> | <b>04/20/1970</b>                    | <b>11/30/2011</b>                | <b>\$350,000</b>                      | <b>\$50,000</b>                               | <b>(\$250,000)</b>              |
| <b>4 Totals.</b> Add the amounts in columns (e) and (f). Also, combine the amounts in column (g). Enter here and include on Schedule D, line 8 (if box A above is checked), line 9 (if box B above is checked), or line 10 (if box C above is checked) |          |                                      |                                  | <b>\$350,000</b>                      | <b>\$50,000</b>                               | <b>(\$250,000)</b>              |

Form 8949 (2011)

**7 Net short-term capital gain or (loss).** Combine lines 4 through 6 in column (g)

---

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note:** Please round and use whole dollars on this form.

| (e) Sales price from Form(s) 8949, line 4, column (e)  | (f) Cost or other basis from Form(s) 8949, line 4, column (f) | (g) Adjustments to gain or loss from Form(s) 8949, line 4, column (g) | (h) Gain or (loss) Combine columns (e), (f), and (g) |
|--|---|---|--|
| <b>8</b> Long-term totals from all Forms 8949 with box A checked in Part II  | ( )   |   |  |
| <b>9</b> Long-term totals from all Forms 8949 with box B checked in Part II  | ( )   |   |  |
| <b>10</b> Long-term totals from all Forms 8949 with box C checked in Part II   | <b>\$350,000</b>  | <b>(\$50,000)</b>   | <b>(\$250,000)</b>                                   |
| <b>11</b> Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824           |   |   | <b>11</b>  |
| <b>12</b> Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1                                     |   |   | <b>12</b>  |
| <b>13</b> Capital gain distributions. See the instructions   |   |   | <b>13</b>  |
| <b>14</b> Long-term capital loss carryover. Enter the amount, if any, from line 13 of your <b>Capital Loss Carryover Worksheet</b> in the instructions |   |   | <b>14</b> ( )  |
| <b>15</b> Net long-term capital gain or (loss). Combine lines 8 through 14 in column (h). Then go to Part III on the back                              |   |   | <b>\$50,000</b>                                      |

For Paperwork Reduction Act Notice, see your tax return instructions.      Cat. No. 11338H      Schedule D (Form 1040) 2011

## Form 1099-C

Lenders or creditors are required to issue Form 1099-C if they cancel a debt owed to them of \$600 or more. Generally, an individual taxpayer must include all canceled amounts (even if less than \$600) on the “Other Income” line of Form 1040.

However, under certain circumstances, a taxpayer may not have to include canceled debt in income. For example, if the canceled debt is related to the taxpayer’s principal residence, the taxpayer may be able to exclude all or a portion of canceled debt if it is “qualified principal residence indebtedness.” The amount excluded due to the “discharge of qualified principal residence indebtedness” is reported on Form 982.

In addition to debtor information, Form 1099-C reports the amount of debt canceled and the date canceled. **If box 6 for bankruptcy is checked, or if an amount is included in box 3 for interest, refer the taxpayer to a professional tax preparer.**

Form 982 must be filed with the taxpayer’s return to report the excluded amount of discharge indebtedness and the reduction of certain tax attributes. Taxpayers excluding discharged debt from “qualified principal residence indebtedness” must complete only a few lines on Form 982; check box 1e and include the amount from Form 1099-C, box 2, on Form 982, line 2. If the taxpayer kept ownership of the home, line 10b must be completed to reflect the basis adjustment to the principal residence for the excluded canceled debt.

### **Coordination with Form 1099-A**

As mentioned earlier, if a personal residence is foreclosed upon, and the debt is canceled in the same year, the taxpayer may receive Form 1099-C *only*. The required filing information from Form 1099-A will be shown in Form 1099-C, boxes 4, 5, and 7.

Generally, the gross foreclosure bid price is considered to be the FMV. For an abandonment or voluntary conveyance in lieu of foreclosure, the FMV is generally the appraised value of the property.

For a recourse loan, the sale price is the lesser of the balance of the principal debt (mortgage) outstanding or fair market value (Form 1099-C, box 7).

### **Mortgage Workouts and Form 1099-C**

Homeowners whose mortgage debt is partly forgiven through a loan modification, or “workout,” which allows them to continue owning their residence, will receive Form 1099-C reporting the debt canceled in box 2. Because the taxpayer kept ownership of the home, there is no gain or loss to be reported.

However, if the canceled debt meets the requirements of “qualified principal residence indebtedness,” Form 982 must be completed to report the amount excluded from gross income and the reduction of tax attributes. Check box 1e on Form 982. The amount from Form 1099-C, box 2, should be entered on line 2. In addition, the amount on line 2 should be entered on line 10b to report the reduction to the basis of the taxpayer’s home.

Taxpayers who are not personally liable for the debt (nonrecourse debt) do not have ordinary income from the cancellation of the debt unless the lender:

- Offered a discount for the early payment of the debt or
- Agreed to a loan modification that resulted in the reduction of the principal balance of the debt

If a lender offers to discount (reduce) the principal balance of a loan that is paid off early, or agrees to a loan modification (“workout”) that includes a reduction in the principal balance of a loan, the amount of the discount or the amount of the principal reduction is *canceled debt* whether or not the taxpayer is personally liable for the debt. The amount of the canceled debt must be included in income unless the exceptions or exclusions discussed earlier apply.

## Case Study – Foreclosure

Frank bought his home on May 14, 2003. His basis in the home was \$200,000. After he lost his job last year, he was not able to make the payments. The bank foreclosed in June 2011, and Frank moved out. At the time of the foreclosure, the fair market value of the home was \$125,000 and the principal balance of the mortgage was \$195,000. All of the debt was incurred to purchase the home. Frank received Form 1099-C for the amount of debt canceled by his bank.

Frank has qualified principal residence indebtedness. His tax return should include Form 8949 and Schedule D to show the basis of the home disposed of through foreclosure, and Form 982 to exclude the debt cancellation from income.

CORRECTED (if checked)

|   |   |  |                                  |   |
|---|---|--|----------------------------------|---|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>FIRST BANK<br/>ANYWHERE USA</b> |   | 1 Date canceled<br><b>JUNE 25, 2011</b>  | OMB No. 1545-1424<br><b>2011</b> | <b>Cancellation<br/>of Debt</b>   |
|   |   | 2 Amount of debt canceled<br><b>\$ 70,000.00</b>   | Form <b>1099-C</b>               |   |
|   |   | 3 Interest if included in box 2<br>\$  |                                  |   |
| CREDITOR'S federal identification number<br><b>XX-XXXXXXX</b>   | DEBTOR'S identification number<br><b>XXX-XX-XXXX</b>  | 4 Debt description<br><b>HOME MORTGAGE LOAN<br/>1111 ANYWHERE STREET<br/>ANYWHERE TOWN, STATE ZIP</b>                  |                                  | <b>Copy B<br/>For Debtor</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |
| DEBTOR'S name<br><b>FRANK LINCOLN</b>   |   | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |                                  |   |
| Street address (including apt. no.)<br><b>ANYWHERE</b>  |   |  |                                  |   |
| City, state, and ZIP code<br><b>CITY, STATE AND ZIP USA</b>   |   |  |                                  |   |
| Account number (see instructions)<br><b>1234567</b>   | 6 Bankruptcy (if checked)<br><input type="checkbox"/> | 7 Fair market value of property<br><b>\$ 125,000.00</b>  |                                  |   |

Form **1099-C** (keep for your records) Department of the Treasury - Internal Revenue Service

Form 8949 (2011) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Do not enter name and social security number if shown on other side. **Frank Lincoln** Your social security number

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

**Note.** Please round and use whole dollars on this form.  
Check the box below that describes the transactions listed on this page.  
**Caution.** Check only one box. If you have more than one type of transaction, complete a separate Form 8949 for each type.

(A) Long-term gains and losses (Form 1099-B, box 3, shows basis)  (B) Long-term gains and losses (Form 1099-B, box 3, does not show basis)  (C) Long-term gains and losses (Form 1099-B not received)

| 3 (a) Description of property<br>(Example: 100 sh. XYZ Co.)  | (b) Code | (c) Date acquired<br>(Mo., day, yr.) | (d) Date sold<br>(Mo., day, yr.) | (e) Sales price<br>(see instructions) | (f) Cost or other basis<br>(see instructions) | (g) Adjustments to<br>gain or loss |
|--|----------|--------------------------------------|----------------------------------|---------------------------------------|---|------------------------------------|
| <b>Main Home Form 1099-A</b>   | <b>E</b> | <b>05/14/2003</b>                    | <b>06/25/2011</b>                | <b>\$125,000</b>                      | <b>\$200,000</b>                              | <b>\$75,000</b>                    |
| <b>4 Totals.</b> Add the amounts in columns (e) and (f). Also, combine the amounts in column (g). Enter here and include on Schedule D, line 8 (if box A above is checked), line 9 (if box B above is checked), or line 10 (if box C above is checked) . . . . . |          |                                      |                                  | <b>4</b>                              | <b>\$125,000</b>                              | <b>\$200,000</b>                   |
|  |          |                                      |                                  |                                       | <b>\$75,000</b>                               |                                    |

Form **8949** (2011)

7 Net short-term capital gain or (loss). Combine lines 1 through 6 in column (h).

**Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year**

| Note: Please round and use whole dollars on this form.  | (e) Sales price from Form(s) 8949, line 4, column (e) | (f) Cost or other basis from Form(s) 8949, line 4, column (f) | (g) Adjustments to gain or loss from Form(s) 8949, line 4, column (g) | (h) Gain or (loss) Combine columns (e), (f), and (g) |
|---|---|---|---|--|
| 8 Long-term totals from all Forms 8949 with box A checked in Part II . . . . .  |   | ( )   |   |  |
| 9 Long-term totals from all Forms 8949 with box B checked in Part II . . . . .  |   | ( )   |   |  |
| 10 Long-term totals from all Forms 8949 with box C checked in Part II . . . . .   | <b>\$125,000</b>                                      | ( <b>\$200,000</b> )  | <b>\$75,000</b>   | <b>\$0</b>   |
| 11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824 . . . . .           |   |   |   | 11   |
| 12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1 . . . . .                                     |   |   |   | 12   |
| 13 Capital gain distributions. See the instructions . . . . .   |   |   |   | 13   |
| 14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your <b>Capital Loss Carryover Worksheet</b> in the instructions . . . . . |   |   |   | 14 ( )   |
| 15 <b>Net long-term capital gain or (loss).</b> Combine lines 8 through 14 in column (h). Then go to Part III on the back . . . . .                       |   |   |   | 15 <b>\$0</b>  |

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 11338H Schedule D (Form 1040) 2011

Form **982**  
(Rev. February 2011)  
Department of the Treasury  
Internal Revenue Service

**Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)**

OMB No. 1545-0046  
Attachment Sequence No. **94**

▶ Attach this form to your income tax return.

Name shown on return: **FRANK LINCOLN** Identifying number: **XXX-XX-XXXX**

**Part I General Information** (see instructions)

- 1 Amount excluded is due to (check applicable box(es)):
  - a Discharge of indebtedness in a title 11 case . . . . .
  - b Discharge of indebtedness to the extent insolvent (not in a title 11 case) . . . . .
  - c Discharge of qualified farm indebtedness . . . . .
  - d Discharge of qualified real property business indebtedness . . . . .
  - e Discharge of qualified principal residence indebtedness . . . . .
- 2 Total amount of discharged indebtedness excluded from gross income . . . . . **2** **\$70,000**
- 3 Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property? . . . . .  Yes  No

**Part II Reduction of Tax Attributes.** You must attach a description of any transactions that result in the reduction in

## Case Study Alternative – Mortgage Workout

If Frank had been able to negotiate a workout with his mortgage lender (reducing the amount he owed on the mortgage and staying in the home), he would not have completed Form 8949 and Schedule D because he had not disposed of the asset.

Assume Frank's lender agreed to reduce his mortgage debt from \$195,000 to \$175,000. The lender issued Frank a Form 1099-C showing \$20,000 of canceled debt. Frank's Form 982 would be similar in that lines 1(e) and 2 would be completed, but the amount of debt forgiven (or his basis in the home, whichever was smaller) would need to be entered on line 10b, and his basis in the home would be decreased by that amount.

|   |  |  |  |  |
|---|--|--|--|--|
| <input type="checkbox"/> CORRECTED (if checked)   |  | <b>2011</b>  |  | <b>Cancellation of Debt</b>  |
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>FIRST BANK ANYWHERE USA</b> |  | 1 Date canceled<br><b>JUNE 25, 2011</b>  | OMB No. 1545-1424<br><b>2011</b>             |  |
|   |  | 2 Amount of debt canceled<br><b>\$ 20,000.00</b>   | Form <b>1099-C</b>                           | <b>Copy B For Debtor</b><br>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported. |
|   |  | 3 Interest if included in box 2<br><b>\$</b>   |  |  |
| CREDITOR'S federal identification number<br><b>XX-XXXXXXX</b>   | DEBTOR'S identification number<br><b>XXX-XX-XXXX</b> | 4 Debt description<br><b>Home Mortgage Loan</b>  |  |  |
| DEBTOR'S name<br><b>FRANK LINCOLN</b>   |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |  |  |
| Street address (including apt. no.)<br><b>ANYWHERE</b>  |  |  |  |  |
| City, state, and ZIP code<br><b>CITY, STATE AND ZIP USA</b>   |  |  |  |  |
| Account number (see instructions)<br><b>1234567</b>   |  | 6 Bankruptcy (if checked)<br><input type="checkbox"/>  | 7 Fair market value of property<br><b>\$</b> |  |
| Form <b>1099-C</b>  |  | (keep for your records)  |  | Department of the Treasury - Internal Revenue Service  |

|   |   |  |
|---|---|--|
| <b>Form 982</b><br>(Rev. February 2011)<br>Department of the Treasury<br>Internal Revenue Service   | <b>Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)</b> | OMB No. 1545-0046                        |
| ▶ Attach this form to your income tax return.   |   | Attachment Sequence No. <b>94</b>        |
| Name shown on return<br><b>FRANK LINCOLN</b>  |   | Identifying number<br><b>XXX-XX-XXXX</b> |
| <b>Part I General Information</b> (see instructions)  |   |  |
| 1 Amount excluded is due to (check applicable box(es)):   |   |  |
| a Discharge of indebtedness in a title 11 case . . . . .  |   | <input type="checkbox"/>                 |
| b Discharge of indebtedness to the extent insolvent (not in a title 11 case) . . . . .  |   | <input type="checkbox"/>                 |
| c Discharge of qualified farm indebtedness . . . . .  |   | <input type="checkbox"/>                 |
| d Discharge of qualified real property business indebtedness . . . . .  |   | <input type="checkbox"/>                 |
| e Discharge of qualified principal residence indebtedness . . . . .   |   | <input checked="" type="checkbox"/>      |
| 2 Total amount of discharged indebtedness excluded from gross income . . . . .  | <b>2</b>  | <b>\$20,000</b>                          |
| 3 Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property? . . . . . <input type="checkbox"/> Yes <input type="checkbox"/> No  |   |  |
| <b>Part II Reduction of Tax Attributes.</b> You must attach a description of any transactions resulting in the reduction in basis under section 1017. See Regulations section 1.1017-1 for basis reduction ordering rules, and, if applicable, required partnership consent statements. (For additional information, see the instructions for Part II.) |   |  |
| Enter amount excluded from gross income:  |   |  |
| 4 For a discharge of qualified real property business indebtedness applied to reduce the basis of depreciable real property . . . . .   | <b>4</b>  |  |
| 5 That you elect under section 108(b)(5) to apply first to reduce the basis (under section 1017) of depreciable property . . . . .  | <b>5</b>  |  |
| 6 Applied to reduce any net operating loss that occurred in the tax year of the discharge or carried over to the tax year of the discharge . . . . .  | <b>6</b>  |  |
| 7 Applied to reduce any general business credit carryover to or from the tax year of the discharge . . . . .  | <b>7</b>  |  |
| 8 Applied to reduce any minimum tax credit as of the beginning of the tax year immediately after the tax year of the discharge . . . . .  | <b>8</b>  |  |
| 9 Applied to reduce any net capital loss for the tax year of the discharge, including any capital loss carryovers to the tax year of the discharge . . . . .  | <b>9</b>  |  |
| 10a Applied to reduce the basis of nondepreciable and depreciable property if not reduced on line 5. DO NOT use in the case of discharge of qualified farm indebtedness . . . . .   | <b>10a</b>  |  |
| b Applied to reduce the basis of your principal residence. Enter amount here ONLY if line 1e is checked . . . . .   | <b>10b</b>  | <b>\$20,000</b>                          |
| 11 For a discharge of qualified farm indebtedness applied to reduce the basis of:   |   |  |
| a Depreciable property used or held for use in a trade or business or for the production of income if not reduced on line 5 . . . . .   |   |  |



## EXERCISES (continued)

**Question 3:** A volunteer with Cancellation of Debt Certification is working with Robert, a taxpayer. The volunteer asks Robert if he underwent foreclosure or had to give up his home during the tax year. Robert confirmed that he did, and produced Form 1099-A. The volunteer asked Robert if he had received Form 1099-C, and Robert replied that he did not. Examining the form, the volunteer noted the balance of principal outstanding was \$234,000. What should the volunteer do next?

- A. Ask the questions on Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt
- B. Ask enough probing questions to determine if Robert had a gain or loss on the foreclosure
- C. Refer Robert to a professional tax preparer
- D. Complete Form 982

**Question 4:** Mary purchased her main home in June 2004 for \$175,000. In 2011, she lost her job and was no longer able to make her mortgage payments. In July, Mary moved out of the home to live with relatives. On July 15, 2011, the bank foreclosed on the home. On November 15, 2011, the bank discontinued its collection activity and canceled the remaining debt. The fair market value at the time of foreclosure was \$100,000 because of the poor housing market, but Mary still owed \$150,000 on the mortgage. None of the loan proceeds were used for any purpose other than to buy, build, or substantially improve the principal residence. Mary never used the home for business or rental purposes and has not filed for bankruptcy. Based on this information, what should the volunteer do?

- A. Refer Mary to another source for tax return preparation
- B. Report a loss of \$50,000 on Schedule D
- C. Report \$50,000 debt canceled on Form 982
- D. Include the debt cancellation amount in income

|   |  |   |  |   |   |
|---|--|---|--|---|---|
| <input type="checkbox"/> CORRECTED (if checked)   |  | OMB No. 1545-0877   |  | <b>2011</b><br>Form <b>1099-A</b>   | <b>Acquisition or Abandonment of Secured Property</b> |
| LENDER'S name, street address, city, state, ZIP code, and telephone no.<br><b>FIRST BANK ANYWHERE USA</b>   |  | 1 Date of lender's acquisition or knowledge of abandonment<br><b>7/15/2011</b>  |  |   |   |
| LENDER'S federal identification number  |  | BORROWER'S identification number  |  | <b>Copy B For Borrower</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction.</small>  |   |
| BORROWER'S name<br><b>MARY</b>  |  | 3 <input type="checkbox"/> If checked, the borrower was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |  |   |   |
| Street address (including apt. no.)<br><b>ANYWHERE</b>  |  | 6 Description of property<br><b>1111 ANYWHERE STREET</b>  |  |   |   |
| City, state, and ZIP code<br><b>CITY, STATE AND ZIP USA</b>   |  |   |  |   |   |
| Account number (see instructions)   |  |   |  |   |   |
| <input type="checkbox"/> CORRECTED (if checked)   |  |   |  |   |   |
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>FIRST BANK ANYWHERE USA</b> |  | 1 Date canceled<br><b>11/15/11</b>  |  | OMB No. 1545-1424   |   |
|   |  | 2 Amount of debt canceled<br><b>\$ 50,000.00</b>  |  | <b>2011</b><br>Form <b>1099-C</b>   |   |
|   |  | 3 Interest if included in box 2<br><b>\$</b>  |  | <b>Copy B For Debtor</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |   |
| CREDITOR'S federal identification number  |  | DEBTOR'S identification number  |  |   |   |
| DEBTOR'S name<br><b>MARY</b>  |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input type="checkbox"/>                                       |  |   |   |
| Street address (including apt. no.)<br><b>ANYWHERE</b>  |  | 6 Bankruptcy (if checked) <input type="checkbox"/>  |  | 7 Fair market value of property<br><b>\$</b>  |   |
| City, state, and ZIP code<br><b>CITY, STATE AND ZIP USA</b>   |  |   |  |   |   |
| Account number (see instructions)<br><b>1234567</b>   |  |   |  |   |   |
| Form <b>1099-C</b> (keep for your records) Department of the Treasury - Internal Revenue Service            |  |   |  |   |   |



## EXERCISES (continued)

**Question 5:** After Tom became ill and could not work full time, he and his wife, Grace, were having difficulty making their mortgage payments. Rather than go through the expense of a foreclosure, the lender agreed to reduce the principal on their loan and refinance it with a better interest rate and lower payments. The principal balance before the November 1, 2011 workout was \$130,000, and the lender reduced the loan to \$110,000. None of the loan proceeds were used for any purpose other than to buy, build, or improve the principal residence. The home has never been used for business or as rental property, and the taxpayers have not filed for bankruptcy.

Based on this information, what should the volunteer do?

- A. Refer Tom and Grace to another source for tax return preparation
- B. Report the reduction in the basis of the home on line 10b of Form 982
- C. Report the \$20,000 as a loss on Schedule D
- D. Include the debt cancellation amount in income

|   |                                |  |                           |   |                             |                                     |  |
|---|--------------------------------|--|---------------------------|---|-----------------------------|-------------------------------------|--|
| <input type="checkbox"/> CORRECTED (if checked)                           |                                | OMB No. 1545-1424  |                           | <b>2011</b>   | <b>Cancellation of Debt</b> |                                     |  |
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no. |                                | 1 Date canceled  | 2 Amount of debt canceled |   |                             | Form <b>1099-C</b>                  |  |
| <b>First Bank<br/>Anywhere USA</b>  |                                | <b>11/01/2011</b>  | <b>\$ 20,000.00</b>       |   |                             |                                     |  |
| CREDITOR'S federal identification number                                  | DEBTOR'S identification number | 3 Interest if included in box 2  |                           | <b>Copy B<br/>For Debtor</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |                             |                                     |  |
| DEBTOR'S name   |                                | 4 Debt description   |                           |   |                             | <input checked="" type="checkbox"/> |  |
| <b>Tom and Grace</b>  |                                | <b>Home Mortgage Loan</b>  |                           |   |                             |                                     |  |
| Street address (including apt. no.)                                       |                                | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . |                           | <b>7 Fair market value of property</b>  |                             |                                     |  |
| <b>Anywhere</b>   |                                | <input checked="" type="checkbox"/>  |                           |   |                             | <b>\$</b>                           |  |
| City, state, and ZIP code   |                                | 6 Bankruptcy (if checked)  |                           |   |                             | <input type="checkbox"/>            |  |
| Account number (see instructions)   |                                | 7 Fair market value of property  |                           | <b>\$</b>   |                             |                                     |  |
| Form <b>1099-C</b>  |                                | (keep for your records)  |                           | Department of the Treasury - Internal Revenue Service   |                             |                                     |  |



## EXERCISES (continued)

**Question 6:** Gene bought his home in 2001. His basis in the home was \$210,000. He lost his job in 2011 and was not able to make the mortgage payments. The bank foreclosed in August 2011 and Gene moved out. At the time of the foreclosure, the fair market value was \$145,000 and the principal balance of the mortgage was \$185,000. All of the debt was incurred to purchase the home, it was never used for business or as a rental, and Gene has not filed for bankruptcy. Gene has a Form 1099-C. Gene is personally liable for repayment of the debt.

How should the foreclosure and loss be reported?

- A. Report the \$40,000 debt cancellation on Form 982, line 10b
- B. Report the \$40,000 debt cancellation on Form 982, line 2, only
- C. Report the \$40,000 debt cancellation on Form 982, line 2, and the foreclosure on Form 8949 and Schedule D
- D. Report the \$40,000 debt cancellation on Form 1040, line 21

| <input type="checkbox"/> CORRECTED (if checked)                           |                                | OMB No. 1545-1424  |                    | <b>2011</b>   | <b>Cancellation of Debt</b>     |  |  |
|---|--------------------------------|--|--------------------|---|---------------------------------|--|--|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no. |                                | 1 Date canceled  | Form <b>1099-C</b> |   |                                 |  |  |
| <b>First Bank<br/>Anywhere USA</b>  |                                | 2 Amount of debt canceled  | <b>2011</b>        |   | <b>Copy B<br/>For Debtor</b>    |  |  |
|   |                                | 3 Interest if included in box 2  |                    |   |                                 | This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported. |  |
|   |                                | 4 Debt description   |                    |   |                                 |  |  |
| CREDITOR'S federal identification number                                  | DEBTOR'S identification number | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |                    | and the IRS determines that it has not been reported. |                                 |  |  |
| DEBTOR'S name   |                                | 6 Bankruptcy (if checked)  |                    |   | 7 Fair market value of property |  |  |
| Street address (including apt. no.)                                       |                                | <input type="checkbox"/>   |                    |   | <b>\$ 145,000.00</b>            |  |  |
| City, state, and ZIP code   |                                | (keep for your records)  |                    | Department of the Treasury - Internal Revenue Service |                                 |  |  |
| City, State, Zip  |                                | Form <b>1099-C</b>   |                    |   |                                 |  |  |

## Cancellation of Debt – Nonbusiness Credit Card Debt Cancellation

Generally, if a taxpayer receives Form 1099-C for canceled credit card debt and was solvent immediately before the debt was canceled, all the canceled debt will be included on Form 1040, line 21, Other Income. No additional supporting forms or schedules are needed to report canceled credit card debt.

### example

John made a deal with his credit card company to pay \$2,000 on his \$7,000 balance, and the company agreed to take it as payment in full. In January 2012, John received a Form 1099-C from his credit card company reporting \$5,000 in box 2 (the amount of debt canceled). John was solvent (assets greater than liabilities) immediately before the debt was canceled. John would include the entire \$5,000 in income on Form 1040, line 21.

Lenders and creditors are required to issue Form 1099-C if they cancel a debt of \$600 or more. If the debt canceled is less than \$600, some lenders or creditors may send a letter or some other form of notification to the taxpayer. Generally, taxpayers must include all canceled amounts (even if less than \$600) on the Other Income line of Form 1040.

Taxpayers who had nonbusiness credit card debt canceled may be able to exclude the canceled debt from income if the cancellation occurred in a bankruptcy or if the taxpayer was insolvent immediately before the cancellation. These situations are outside the scope of the VITA/TCE program. Refer taxpayers with bankruptcy and insolvency issues to a professional tax preparer.

### Insolvency (Out of Scope for VITA/TCE)

Insolvency is a condition in which the FMV of all assets is less than one's liabilities. The amount or level of insolvency is expressed as a negative net worth.

For purposes of determining insolvency, assets include the value of everything owned (including assets that serve as collateral for debt and exempt assets which are beyond the reach of creditors under the law, such as an interest in a pension plan and the value of a retirement account).

Liabilities are amounts owed, and include:

- The entire amount of recourse debts
- The amount of nonrecourse debt that is not in excess of the FMV of the property that is security for the debt
- The amount of nonrecourse debt in excess of the FMV of the property subject to the nonrecourse debt to the extent nonrecourse debt in excess of the FMV of the property subject to the debt is forgiven

Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt, provides step-by-step guidance for the volunteer tax return preparer to determine if the cancellation of debt is within scope. Part II addresses credit card debt.

### Taxpayer Interview and Tax Law Application

Here is how a volunteer advised Mary regarding her canceled credit card debt.



If the taxpayer had nonbusiness credit card debt canceled, all or part of the debt may be excluded if the cancellation occurred in bankruptcy, or if the taxpayer was insolvent immediately before the cancellation. These situations are beyond the scope of VITA/TCE. If any of these situations apply, refer the taxpayer to a professional tax preparer. See IRS Publication 4681 for more information.

## SAMPLE INTERVIEW

VOLUNTEER SAYS...

MARY RESPONDS...

*I notice you received a 1099-C from a credit card company.*

Yes, I negotiated with them to cancel \$3,000 of my debt.

*Yes, that's indicated in box 2.*

I could only afford to pay them \$1,000, so it really helped me.

*Do you think your debts at the time exceeded your assets?*

I'm not sure, but it's certainly possible.

*If that is the case, some of the canceled debt might not be taxable.*

That sounds like a good thing!

*Yes, but I'm afraid I will not be able to help you with this – VITA/TCE volunteers are not trained to compute the nontaxable portion of canceled credit card debt.*

Oh, I understand.

*I suggest you seek assistance from a professional tax preparer.*

I will, thank you.

|   |  |  |  |
|---|--|--|--|
| <input type="checkbox"/> CORRECTED (if checked)   |  | OMB No. 1545-1424  |  |
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>CREDIT CARD COMPANY<br/>ANYWHERE, USA</b> |  | 1 Date canceled<br><b>06/25/2011</b>   | <div style="font-size: 2em; font-weight: bold;">2011</div> |
| CREDITOR'S federal identification number<br><b>XX-XXXXXXX</b>   |  | 2 Amount of debt canceled<br><b>\$ 3,000.00</b>  |  |
| DEBTOR'S identification number<br><b>XXX-XX-XXXX</b>  |  | 3 Interest if included in box 2<br>\$  |  |
| DEBTOR'S name<br><b>MARY GARDNER</b>  |  | 4 Debt description<br><b>CREDIT CARD DEBT</b>  |  |
| Street address (including apt. no.)<br><b>ANYWHERE</b>  |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/>   |  |
| City, state, and ZIP code<br><b>CITY, STATE ZIP USA</b>   |  | <div style="border: 1px solid black; padding: 5px;"> <b>Copy B<br/>For Debtor</b><br/>                     This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.                 </div> |  |
| Account number (see instructions)<br><b>1234567</b>   |  |  |  |
| Form <b>1099-C</b>  |  | (keep for your records)  |  |
| Department of the Treasury - Internal Revenue Service   |  |  |  |



### EXERCISES (continued)

**Question 7:** Greg was released from his obligation to pay \$5,000 of personal credit card debt. The credit card company sent Form 1099-C showing canceled debt of \$5,000 in box 2. Greg is fairly certain he has more debt than he has assets.

Can the VITA/TCE site provide tax return preparation assistance to Greg?

A. Yes, since the entire \$5,000 in canceled debt is considered income and reported on Form 1040, line 21.

B. No, because it appears Greg is insolvent, which might mean some of the canceled credit card debt would be nontaxable and beyond the scope of the VITA/TCE program.



## EXERCISES (continued)

**Question 8:** Kay was released from her obligation to pay personal credit card debt. She owed \$10,000 to her credit card company, which agreed to accept \$2,500 as payment in full. Before paying the credit card company, it was determined Kay was solvent (assets greater than liabilities) and not in bankruptcy. The credit card company issued Kay a Form 1099-C, reporting \$7,500 in box 2.

Based on the information above, can Kay be assisted at her local VITA/TCE site?  Yes  No

**Question 9:** Review the information in Question 8 about Kay's canceled debt. If the VITA/TCE site is able to assist Kay, what amount would be reported on Kay's Form 1040, line 21?

- A. \$0
- B. \$10,000
- C. \$2,500
- D. \$7,500

## Summary

Cancellation of Debt is an optional specialty course. Check with your Site Coordinator to determine whether you should be certified in this topic.

This course covered cancellation of debt issues that are both within scope and out of scope for the VITA/TCE program.

Cancellation of debt can be complex. VITA/TCE volunteers may assist a taxpayer with issues related to cancellation of debt as long as the taxpayer meets all the criteria for discharge of qualified principal residence indebtedness or if all debt canceled and reported on Form 1099-C was nonbusiness credit card debt.

Under the Mortgage Forgiveness Debt Relief Act of 2007, taxpayers may exclude certain debt forgiven or canceled on their principal residence. This exclusion is applicable to the discharge of "qualified principal residence indebtedness." If the canceled debt qualifies for exclusion from gross income, the debtor may be required to reduce tax attributes (certain credits, losses, and basis of assets) by the amount excluded.

Refer taxpayers who were insolvent immediately before the credit card debt was canceled to a professional tax preparer—all or part of the canceled debt might not be considered taxable income. (An insolvent taxpayer has liabilities that exceed the FMV of all assets.)

VITA/TCE tax preparers with Advanced, Military, or International Certification and who are certified in this module may assist taxpayers with canceled or forgiven mortgage debt issues on a limited basis. Use Publication 4731, Screening Sheet for Form 1099-C, Cancellation of Debt, which provides questions and step-by-step guidance for the volunteer tax-return preparer.

### What situations are out of scope for the VITA/TCE program?

The following are out of scope for this lesson. While this list may not be all inclusive, it is provided for your awareness only.

- Cancellation of debt for issues other than qualified principal residence or nonbusiness credit card
- Cancellation of debt for a principal residence that was used in a business or as rental property
- Cancellation of debt when Form 1099-C, box 3 includes an amount for interest
- Debt was canceled because the taxpayer filed bankruptcy or was insolvent immediately before the cancellation



## EXERCISE ANSWERS

**Answer 1:** No. Because Angie used part of the home as rental property, all the canceled debt may not qualify to be excluded from income. The rules involving mortgage debt exclusions are complex. Angie should be referred to a professional tax preparer.

**Answer 2:** No. Fred's situation is outside the scope of the volunteer program since a portion of his refinanced debt was used for purposes other than to buy, build, or substantially improve his principal residence. Fred should be referred to a professional tax preparer, per the guidance on Publication 4731.

**Answer 3:** B. The volunteer should ask questions to determine if Robert had a gain or loss on the foreclosure. If the taxpayer receives a Form 1099-C, the volunteer would use the screening sheet to determine if the related tax issues are within scope.

**Answer 4:** C. The volunteer would need to complete Form 8949, Schedule D, and Form 982. Although there is a loss, it cannot be deducted. The mortgage debt cancellation is not included in income on the tax return because it is covered by the qualified principal residence indebtedness exclusion on Form 982.

**Answer 5:** B. The volunteer would complete Form 982. The \$20,000 in debt cancellation can be excluded as qualified principal residence indebtedness on Form 982 and is not counted as income on the tax return. In addition to completing Form 982, box 1e and line 2, the volunteer would also need to complete line 10b to report the reduction in the basis of the home. Form 8949 and Schedule D are not required because Tom and Grace did not dispose of the home.

**Answer 6:** C. Form 982, Form 8949, and Schedule D should be completed. When a residence that is security for a mortgage is abandoned or foreclosed upon, it is treated as having been sold. This results in the foreclosure being reported on Form 8949 and Schedule D as sale of home. Failure to file Form 8949 and Schedule D may result in an IRS notice to the taxpayer.

**Answer 7:** B. Greg is fairly certain that he has more debt than he has assets, which means he is insolvent. This situation is beyond the scope of the VITA/TCE program.

**Answer 8:** Yes. Kay was solvent and not in bankruptcy, and the credit card company issued her a Form 1099-C.

**Answer 9:** D. Kay would report \$7,500 on line 21 of her Form 1040.



## Cancellation of Debt – Practice Scenarios

Now that you have completed the Cancellation of Debt course, let's practice. Five practice scenarios are provided to help you apply what you have learned.

Scenarios 1, 2, and 3 involve cancellation of debt issues on the taxpayer's principal residence. The first scenario does not require you to prepare a tax return. For practice using the tax preparation software, review the interview notes and taxpayer documents in order to complete a tax return for scenarios 2 and 3.

Scenarios 4 and 5 involve canceled debt from a credit card. Scenario 4 does not require you to prepare a tax return. For practice using the tax preparation software, review the interview notes and taxpayer documents in order to complete a tax return for scenario 5.

To answer the questions, complete Form 1040 through line 37, and the appropriate forms and schedules.

The Practice Lab on Link & Learn Taxes is available for you to complete the returns using tax preparation software. After you answer the questions, you can check your answers, which are listed at the end of this course.

### Practice Scenario 1 – Mike and Marilyn Albion

Mike and Marilyn owned and lived in their home since 2001. They could not make the mortgage payments, so they moved out of their home in July 2011. In January 2012, they received Form 1099-C from their mortgage company. Box 2 showed canceled debt of \$75,000 and box 5 indicated that they were personally liable for the debt. Their home was never used in a business or as a rental property. The mortgage was used to purchase the home and was secured by the home. They did not file bankruptcy.

#### Scenario Questions

Answers appear at the end of the lesson.

- 1-1 Mike and Marilyn's debt is referred to as nonrecourse debt.  True  False
- 1-2 Mike and Marilyn will not have to report the canceled debt as income because it meets one of the exclusions to the general rule.  True  False
- 1-3 The canceled debt will be reported on:
- A. Form 1040, line 21
  - B. Form 982, line 2
  - C. Form 982, line 10b
  - D. All of the above
- 1-4 VITA/TCE volunteers can assist taxpayers who lose their home during bankruptcy.  True  False

### Practice Scenario 2 – Larry and Donna Rusk

Review the following taxpayer documents.



**Intake/Interview & Quality Review Sheet**

**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |  |   |                          |   |  |  |
|--|--|---|--------------------------|---|--|--|
| 1. Your First Name<br><b>Larry</b>   |  | M. I.                                       | Last Name<br><b>Rusk</b> |   | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No   |  |
| 2. Spouse's First Name<br><b>Donna</b>   |  | M. I.                                       | Last Name<br><b>Rusk</b> |   | Is spouse a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |  |
| 3. Mailing Address<br><b>8899 Lighwood Street</b>  |  | Apt#  | City<br><b>Your City</b> |   | State<br><b>YS</b>   | Zip Code<br><b>Your Zip Code</b>   |
| 4. Contact Information<br>Phone: <b>555-555-5555</b> Cell Phone: E-mail:   |  |   |                          |   |  |  |
| 5. Your Date of Birth<br><b>07/29/1980</b>   |  | 6. Your Job Title<br><b>Teacher</b>         |                          | 7. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No  |  | 8. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No  |
| 9. Spouse's Date of Birth<br><b>01/30/1982</b>   |  | 10. Spouse's Job Title<br><b>Unemployed</b> |                          | 11. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |  | 12. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |  |   |                          |   |  |  |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



|  |  |   |                            |   |                  |   |  |  |  |
|--|--|---|----------------------------|---|------------------|---|--|--|--|
| a Employee's social security number<br><b>381-XX-XXXX</b>  |  | OMB No. 1545-0008   |                            | Safe, accurate,<br>FAST! Use                                |                  |  |  | Visit the IRS website at<br><a href="http://www.irs.gov/efile">www.irs.gov/efile</a> |  |
| b Employer identification number (EIN)<br><b>59-2XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>30,559.00</b>   |                            | 2 Federal income tax withheld<br><b>3,746.35</b>            |                  |   |  |  |  |
| c Employer's name, address, and ZIP code<br><b>OAK TRAIL MIDDLE SCHOOL<br/>200 OAK TRAIL ROAD<br/>YOUR CITY, STATE, ZIP CODE</b> |  | 3 Social security wages<br><b>32,559.00</b>   |                            | 4 Social security tax withheld<br><b>2,018.65</b>           |                  |   |  |  |  |
|  |  | 5 Medicare wages and tips<br><b>32,559.00</b>   |                            | 6 Medicare tax withheld<br><b>472.11</b>                    |                  |   |  |  |  |
|  |  | 7 Social security tips  |                            | 8 Allocated tips  |                  |   |  |  |  |
| d Control number   |  | 9   |                            | 10 Dependent care benefits                                  |                  |   |  |  |  |
| e Employee's first name and initial Last name<br><b>LARRY RUSK<br/>8899 LIGHTWOOD ST.<br/>YOUR CITY, STATE, ZIP CODE</b>         |  | 11 Nonqualified plans   |                            | 12a See instructions for box 12<br><b>D</b> <b>2,000.00</b> |                  |   |  |  |  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/> |                            | 12b   |                  |   |  |  |  |
|  |  | 14 Other  |                            | 12c   |                  |   |  |  |  |
|  |  |   |                            | 12d   |                  |   |  |  |  |
| f Employee's address and ZIP code  |  |   |                            |   |                  |   |  |  |  |
| 15 State Employer's state ID number<br><b>YS 59-2XXXXXX</b>  | 16 State wages, tips, etc.<br><b>30,559.00</b> | 17 State income tax<br><b>1,100.00</b>  | 18 Local wages, tips, etc. | 19 Local income tax   | 20 Locality name |   |  |  |  |

Form **W-2** Wage and Tax Statement **2011** Department of the Treasury—Internal Revenue Service  
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
 This information is being furnished to the Internal Revenue Service.

|  |   |  |                            |   |                  |   |  |  |  |
|--|---|--|----------------------------|---|------------------|---|--|--|--|
| a Employee's social security number<br><b>382-XX-XXXX</b>  |   | OMB No. 1545-0008  |                            | Safe, accurate,<br>FAST! Use                    |                  |  |  | Visit the IRS website at<br><a href="http://www.irs.gov/efile">www.irs.gov/efile</a> |  |
| b Employer identification number (EIN)<br><b>59-3XXXXXX</b>  |   | 1 Wages, tips, other compensation<br><b>5,900.00</b>   |                            | 2 Federal income tax withheld<br><b>590.00</b>  |                  |   |  |  |  |
| c Employer's name, address, and ZIP code<br><b>DAISY DAY CARE<br/>1945 FLOWER RD.<br/>YOUR CITY, STATE and ZIP CODE</b>  |   | 3 Social security wages<br><b>5,900.00</b>   |                            | 4 Social security tax withheld<br><b>365.80</b> |                  |   |  |  |  |
|  |   | 5 Medicare wages and tips<br><b>5,900.00</b>   |                            | 6 Medicare tax withheld<br><b>85.55</b>         |                  |   |  |  |  |
|  |   | 7 Social security tips   |                            | 8 Allocated tips                                |                  |   |  |  |  |
| d Control number   |   | 9  |                            | 10 Dependent care benefits                      |                  |   |  |  |  |
| e Employee's first name and initial Last name<br><b>DONNA RUSK<br/>8899 LIGHTWOOD ST.<br/>YOUR CITY, STATE, ZIP CODE</b> |   | 11 Nonqualified plans  |                            | 12a See instructions for box 12                 |                  |   |  |  |  |
|  |   | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |                            | 12b   |                  |   |  |  |  |
|  |   | 14 Other   |                            | 12c   |                  |   |  |  |  |
|  |   |  |                            | 12d   |                  |   |  |  |  |
| f Employee's address and ZIP code  |   |  |                            |   |                  |   |  |  |  |
| 15 State Employer's state ID number<br><b>YS 59-3XXXXXX</b>  | 16 State wages, tips, etc.<br><b>5,900.00</b> | 17 State income tax  | 18 Local wages, tips, etc. | 19 Local income tax                             | 20 Locality name |   |  |  |  |

Form **W-2** Wage and Tax Statement **2011** Department of the Treasury—Internal Revenue Service  
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
 This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|   |  |  |   |  |
|---|--|--|---|--|
| <b>PAYER'S name, street address, city, state, ZIP code, and telephone no.</b><br><b>GEORGIA STATE UNEMPLOYMENT COMMISSION</b><br><b>456 PEACHTREE ST.</b><br><b>YOUR CITY, STATE and ZIP CODE</b>                           |  | <b>1 Unemployment compensation</b><br><b>\$ 4,500.00</b>                     | OMB No. 1545-0120<br><br><div style="font-size: 2em; font-weight: bold; text-align: center;">2011</div> | <b>Certain Government Payments</b>   |
|   |  | <b>2 State or local income tax refunds, credits, or offsets</b><br><b>\$</b> |   |  |
| <b>PAYER'S federal identification number</b><br><b>53-4XXXXXX</b>   | <b>RECIPIENT'S identification number</b><br><b>382-XX-XXXX</b> | <b>3 Box 2 amount is for tax year</b>  | <b>4 Federal income tax withheld</b><br><b>\$ 0.00</b>  | <b>Copy B For Recipient</b><br><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.</small> |
| <b>RECIPIENT'S name</b><br><br><b>DONNA RUSK</b><br><br><small>Street address (including apt. no.)</small><br><b>8899 LIGHTWOOD ST.</b><br><small>City, state, and ZIP code</small><br><b>YOUR CITY, STATE and ZIP CODE</b> |  | <b>5 ATAA/RTAA payments</b><br><b>\$</b>                                     | <b>6 Taxable grants</b><br><b>\$</b>  |  |
| <small>Account number (see instructions)</small>  |  | <b>7 Agriculture payments</b><br><b>\$</b>                                   | <b>8 If checked, box 2 is trade or business income</b> <input type="checkbox"/>                         |  |
|   |  | <b>9 Market gain</b>   |   |  |
|   |  | <b>10a State</b>   | <b>11 State income tax withheld</b><br><b>\$</b>  |  |

Form **1099-G**
(keep for your records)
Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

|   |   |  |   |                             |
|---|---|--|---|-----------------------------|
| <b>CREDITOR'S name, street address, city, state, ZIP code, and telephone no.</b><br><b>Beacon First National Bank</b><br><b>500 N. Market Street</b><br><b>Your City, State and ZIP Code</b>  |   | <b>1 Date canceled</b><br><b>08/16/2011</b>  | OMB No. 1545-1424<br><br><div style="font-size: 2em; font-weight: bold; text-align: center;">2011</div>   | <b>Cancellation of Debt</b> |
|   |   | <b>2 Amount of debt canceled</b><br><b>\$ 21,000.00</b>  |   |                             |
| <b>CREDITOR'S federal identification number</b><br><b>59-5xxxxxx</b>  | <b>DEBTOR'S identification number</b><br><b>381-XX-XXXX</b> | <b>3 Interest if included in box 2</b><br><b>\$</b>  | <b>Copy B For Debtor</b><br><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |                             |
| <b>DEBTOR'S name</b><br><br><b>Larry and Donna Rusk</b><br><br><small>Street address (including apt. no.)</small><br><b>8899 Lightwood Street</b><br><small>City, state, and ZIP code</small><br><b>Your City, State and ZIP Code</b> |   | <b>4 Debt description</b><br><b>Home Mortgage Loan</b><br><b>415 Cedar Trail</b><br><b>Your City, State and ZIP Code</b> |   |                             |
| <small>Account number (see instructions)</small>  |   | <b>5 If checked, the debtor was personally liable for repayment of the debt</b> <input checked="" type="checkbox"/>      |   |                             |
|   |   | <b>6 Bankruptcy (if checked)</b><br><input type="checkbox"/>   |   |                             |
|   |   | <b>7 Fair market value of property</b><br><b>\$ 112,000.00</b>   |   |                             |

Form **1099-C**
(keep for your records)
Department of the Treasury - Internal Revenue Service

**Interviewer Notes**

- Larry and Donna are married and want to file a joint return.
- Larry is a middle school art teacher.
- Donna lost her job in May 2011 and received unemployment.
- They stopped making their house payments in December 2010, and the bank foreclosed on July 15, 2011. They had owned and lived in the home since June 10, 2000. The cost of the home was \$150,000. The home was never used for business or rental purposes. The balance of the mortgage principal at the time of foreclosure was \$133,000.
- The bank issued a 1099-C for debt canceled.
- They want to have their refund direct deposited: Routing #062005690 Acct. #123876-4.

For practice using the tax preparation software, complete the Rusks' tax return using the Practice Lab on Link & Learn Taxes and answer the following questions.

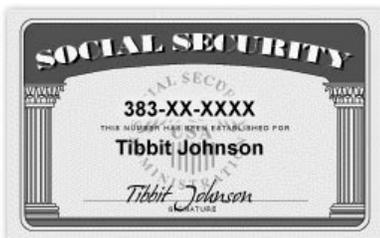
### Scenario Questions

- 2-1** What is the amount of canceled debt excluded from gross income on Form 982, line 2?
- A. \$0
  - B. \$21,000
  - C. \$112,000
  - D. \$133,000
- 2-2** What is the net long-term capital gain or loss shown on Schedule D, line 15?
- A. (\$21,000)
  - B. \$0
  - C. \$17,000
  - D. \$21,000
- 2-3** Which of the following would cause the Rusks' return to be out of scope for VITA/TCE volunteers?
- A. They filed bankruptcy
  - B. They rented out the basement apartment
  - C. They took out a home equity loan and used the proceeds to pay off credit card debt
  - D. All of the above
- 2-4** What is the amount of canceled debt the Rusks will report as income on Form 1040, line 21? \$\_\_\_\_\_
- 2-5** What is the Rusks' total income on Form 1040, line 22?
- A. \$36,459
  - B. \$40,959
  - C. \$50,559
  - D. \$60,959

### Practice Scenario 3 – Tibbit Johnson

---

Review the following taxpayer documents.



**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |                                     |  |  |                                  |
|--|-------------------------------------|--|--|----------------------------------|
| 1. Your First Name<br><b>Tibbit</b>  | M. I.                               | Last Name<br><b>Johnson</b>  | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |                                  |
| 2. Spouse's First Name   | M. I.                               | Last Name  | Is spouse a U.S. Citizen?<br><input type="checkbox"/> Yes <input type="checkbox"/> No          |                                  |
| 3. Mailing Address<br><b>8301 Holly Place</b>  | Apt#                                | City<br><b>Your City</b>   | State<br><b>YS</b>   | Zip Code<br><b>Your Zip Code</b> |
| 4. Contact Information<br>Phone: <b>210-555-5555</b> Cell Phone: E-mail:   |                                     |  |  |                                  |
| 5. Your Date of Birth<br><b>07/13/1949</b>   | 6. Your Job Title<br><b>Retired</b> | Are you:   | 7. Legally Blind<br><input type="checkbox"/> Yes <input checked="" type="checkbox"/> No        |                                  |
|  |                                     | 8. Totally and Permanently Disabled<br><input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |  |                                  |
| 9. Spouse's Date of Birth  | 10. Spouse's Job Title              | Is Spouse:   | 11. Legally Blind<br><input type="checkbox"/> Yes <input type="checkbox"/> No                  |                                  |
|  |                                     | 12. Totally and Permanently Disabled<br><input type="checkbox"/> Yes <input type="checkbox"/> No           |  |                                  |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |                                     |  |  |                                  |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: **2009**

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



CORRECTED (if checked)

|   |  |   |   |   |  |
|---|--|---|---|---|--|
| PAYER'S name, street address, city, state, and ZIP code<br><b>TEACHER'S STATE PENSION FUND<br/>123 OAK STREET<br/>YOUR CITY, STATE and ZIP CODE</b> |  | <b>1</b> Gross distribution<br>\$ <b>20,000.00</b>  | OMB No. 1545-0119<br><b>2011</b>                                    |   | <b>Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.</b>                                     |
|   |  | <b>2a</b> Taxable amount<br>\$ <b>20,000.00</b>   | Form <b>1099-R</b>  |   |  |
| PAYER'S federal identification number<br><b>59-6XXXXXX</b>  |  | RECIPIENT'S identification number<br><b>383-XX-XXXX</b>                                     | <b>2b</b> Taxable amount not determined <input type="checkbox"/>    | Total distribution <input type="checkbox"/>         | <b>Copy B Report this income on your federal tax return. If this form shows federal income tax withheld in box 4, attach this copy to your return.</b> |
| RECIPIENT'S name<br><b>TIBBIT JOHNSON</b>   |  | <b>3</b> Capital gain (included in box 2a)<br>\$  | <b>4</b> Federal income tax withheld<br>\$ <b>1,700.00</b>          |   |  |
| Street address (including apt. no.)<br><b>8201 HOLLY PLACE</b>  |  | <b>5</b> Employee contributions / Designated Roth contributions or insurance premiums<br>\$ | <b>6</b> Net unrealized appreciation in employer's securities<br>\$ |   |  |
| City, state, and ZIP code<br><b>YOUR CITY, STATE and ZIP CODE</b>   |  | <b>7</b> Distribution code(s)<br><b>7</b>   | IRA/SEP/SIMPLE <input type="checkbox"/>                             | <b>8</b> Other<br>\$ %                              | This information is being furnished to the Internal Revenue Service.   |
|   |  | <b>9a</b> Your percentage of total distribution<br>%  | <b>9b</b> Total employee contributions<br>\$                        |   |  |
| <b>10</b> Amount allocable to IRR within 5 years<br>\$  | <b>11</b> 1st year of desig. Roth contrib. | <b>12</b> State tax withheld<br>\$ <b>300.00</b>  | <b>13</b> State/Payer's state no.<br><b>YS 2343235</b>              | <b>14</b> State distribution<br>\$ <b>20,000.00</b> |  |
| Account number (see instructions)   |  | <b>15</b> Local tax withheld<br>\$  | <b>16</b> Name of locality  | <b>17</b> Local distribution<br>\$                  |  |

Form **1099-R**

Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

|   |  |   |  |  |  |
|---|--|---|--|--|--|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>First Home Mortgage<br/>PO Box 12<br/>Your City, State and ZIP Code</b> |  | <b>1</b> Date canceled<br><b>11/13/2011</b>   | OMB No. 1545-1424<br><b>2011</b>                       |  | <b>Cancellation of Debt</b>  |
|   |  | <b>2</b> Amount of debt canceled<br>\$ <b>13,000.00</b>   | Form <b>1099-C</b>                                     |  |  |
| CREDITOR'S federal identification number<br><b>59-7XXXXXX</b>   |  | DEBTOR'S identification number<br><b>383-XX-XXXX</b>  | <b>4</b> Debt description<br><b>Home Mortgage Loan</b> |  | <b>Copy B For Debtor</b><br>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported. |
| DEBTOR'S name<br><b>Tibbit Johnson</b>  |  | <b>5</b> If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |  |  |  |
| Street address (including apt. no.)<br><b>8201 Holly Place</b>  |  | <b>6</b> Bankruptcy (if checked) <input type="checkbox"/>   | <b>7</b> Fair market value of property<br>\$           |  |  |
| City, state, and ZIP code<br><b>Your City, State and ZIP Code</b>   |  |   |  |  |  |
| Account number (see instructions)   |  |   |  |  |  |

Form **1099-C**

(keep for your records)

Department of the Treasury - Internal Revenue Service

## Interview Notes:

- Tibbit Johnson is a retired school teacher and a widower with two adult children. His wife, Sasha, passed away in 2010. At the time of his wife's death, she was employed full-time as a bank teller.
- He has not remarried.
- After the death of his wife, he was struggling to make the mortgage payment on his residence on his teacher's pension alone. In November 2011 he worked out a loan modification agreement with his lender, reducing his monthly payment by \$200, which allowed him to keep his home.
- Tibbit received a Form 1099-R for his teacher's pension and his only other source of income was \$7 in interest on a savings account he had with Teachers Credit Union. He did not receive a Form 1099-INT from the credit union.
- The mortgage breakdown was:
  - Year 1992, mortgage secured to buy the house: \$175,000
  - Year 2000, second mortgage loan to replace the roof and windows: \$25,000
- The home's fair market value (FMV) had fallen to \$160,000 when the mortgage workout with his lender occurred. Tibbit owed \$173,000 on the combined first and second mortgage loans before the mortgage workout with his lender. The lender agreed to refinance the two loans into one and reduce the mortgage principal balance to the current fair market value.
- Tibbit received Form 1099-C reflecting \$13,000 in cancellation of debt. He was solvent at the time the debt was canceled and was not in bankruptcy. The house has never been rented or used for any business purpose.
- Tibbit and Sasha itemized on their joint 2010 return and did not receive a refund on their state return. Tibbit is wondering if he should itemize on his 2011 return.
- Tibbit wants to know if he can still deduct the \$1,200 in mortgage interest. He has no other deductible expenses.
- He would like any refund to be direct deposited into his checking account. Routing #062005690 and Account #123967-3.

For practice using the tax preparation software, complete Tibbit's tax return using the Practice Lab on Link & Learn Taxes and answer the following questions.

## Scenario Questions

- 3-1** Tibbit's debt is referred to as recourse debt.  True  False
- 3-2** Tibbit's adjusted gross income is \$33,007.  True  False
- 3-3** How should the workout with the mortgage lender be reported on Tibbit's tax return?
- A. Report the \$13,000 debt cancellation on Form 982, line 2 only.
  - B. Report the \$13,000 debt cancellation on Form 982, line 2, and Form 8949 and Schedule D.
  - C. Report the \$13,000 debt cancellation on Form 982, line 2, and on Form 1040, line 21.
  - D. Report the \$13,000 debt cancellation on Form 982, line 2, and line 10b.

## Practice Scenario 4 – Jay Smith

---

Jay incurred \$15,000 in credit card debt. He was unable to pay the monthly payments. In September 2011, the credit card company agreed to accept \$8,000 from Jay as full payment. Jay received a Form 1099-C from the credit card company for \$7,000. He was also personally liable for the payment of the debt. Jay was not insolvent immediately before the cancellation of debt, nor has he filed for bankruptcy.

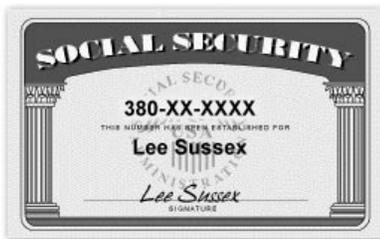
### Scenario Questions

- 4-1 What is the taxable portion of Jay's canceled debt that will be reported on Form 1040? \$\_\_\_\_\_
- 4-2 If the fair market value of Jay's assets were less than his liabilities, this is what is referred to as being solvent.  True  False

## Practice Scenario 5 – Lee Sussex

---

Review the following taxpayer documents.



**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |                                    |                            |  |   |
|--|------------------------------------|----------------------------|--|---|
| 1. Your First Name<br><b>Lee</b>   | M. I.<br><b>M.</b>                 | Last Name<br><b>Sussex</b> | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |   |
| 2. Spouse's First Name   | M. I.                              | Last Name                  | Is spouse a U.S. Citizen?<br><input type="checkbox"/> Yes <input type="checkbox"/> No          |   |
| 3. Mailing Address<br><b>7294 Elm</b>  | Apt#                               | City<br><b>Your City</b>   | State<br><b>YS</b>   | Zip Code<br><b>Your Zip Code</b>                                    |
| 4. Contact Information<br>Phone: <b>510-555-5555</b> Cell Phone: E-mail:   |                                    |                            |  |   |
| 5. Your Date of Birth<br><b>11/29/1985</b>   | 6. Your Job Title<br><b>Editor</b> | Are you:                   | 7. Legally Blind   | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
|  |                                    |                            | 8. Totally and Permanently Disabled  | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 9. Spouse's Date of Birth  | 10. Spouse's Job Title             | Is Spouse:                 | 11. Legally Blind  | <input type="checkbox"/> Yes <input type="checkbox"/> No            |
|  |                                    |                            | 12. Totally and Permanently Disabled   | <input type="checkbox"/> Yes <input type="checkbox"/> No            |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |                                    |                            |  |   |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- **Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.**
- **To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.**

**To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.**

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



|  |  |  |   |
|--|--|--|---|
| a Employee's social security number<br><b>380-XX-XXXX</b>  |  | Safe, accurate,<br>FAST! Use  Visit the IRS website at<br>www.irs.gov/efile |   |
| b Employer identification number (EIN)<br><b>59-0XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>30,000.00</b>  | 2 Federal income tax withheld<br><b>4,081.25</b>  |
| c Employer's name, address, and ZIP code<br><b>WORLD HERALD NEWS<br/>141 PINE STREET<br/>YOUR CITY, STATE and ZIP CODE</b> |  | 3 Social security wages<br><b>32,500.00</b>  | 4 Social security tax withheld<br><b>2,015.00</b> |
|  |  | 5 Medicare wages and tips<br><b>32,500.00</b>  | 6 Medicare tax withheld<br><b>471.25</b>          |
|  |  | 7 Social security tips   | 8 Allocated tips                                  |
| d Control number   |  | 9  | 10 Dependent care benefits                        |
| e Employee's first name and initial Last name<br><b>LEE SUSSEX<br/>7294 ELM<br/>YOUR CITY, STATE and ZIP CODE</b>          |  | 11 Nonqualified plans  |   |
|  |  | 12a See instructions for box 12<br><b>D</b> <b>2,500.00</b>  |   |
|  |  | 12b <input type="checkbox"/> Statutory employee <input checked="" type="checkbox"/> Retirement plan <input type="checkbox"/> Third-party sick pay              |   |
| f Employee's address and ZIP code  |  | 14 Other   |   |
| 15 State Employer's state ID number<br><b>YS 59-0XXXXXX</b>  | 16 State wages, tips, etc.<br><b>30,000.00</b> | 17 State income tax<br><b>1,200.00</b>   | 18 Local wages, tips, etc.                        |
|  |  | 19 Local income tax  | 20 Locality name                                  |

Form **W-2** Wage and Tax Statement **2011** Department of the Treasury—Internal Revenue Service  
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
 This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|  |  |  |  |  |
|--|--|--|--|--|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>CREDIT CARD COMPANY<br/>100 OVERPASS HWY<br/>YOUR CITY, STATE and ZIP CODE</b> |  | 1 Date canceled<br><b>06/01/2011</b>   | OMB No. 1545-1424<br><b>2011</b><br>Form <b>1099-C</b> | <b>Cancellation of Debt</b>  |
|  |  | 2 Amount of debt canceled<br><b>\$ 6,500.00</b>  |  |  |
|  |  | 3 Interest if included in box 2<br><b>\$</b>   |  |  |
| CREDITOR'S federal identification number<br><b>59-1XXXXXX</b>  | DEBTOR'S identification number<br><b>380-XX-XXXX</b> | 4 Debt description<br><b>Credit Card Debt</b>  |  | <b>Copy B For Debtor</b><br>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported. |
| DEBTOR'S name<br><b>LEE SUSSEX</b>   |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |  |  |
| Street address (including apt. no.)<br><b>7294 ELM</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE and ZIP CODE</b>                                    |  | 6 Bankruptcy (if checked)<br><input type="checkbox"/>  | 7 Fair market value of property<br><b>\$</b>           |  |

Form **1099-C** (keep for your records) Department of the Treasury - Internal Revenue Service

## Interview Notes:

- Lee is single with no children.
- She did not itemize last year.
- She received Form 1099-C for the cancellation of her nonbusiness credit card debt.
- Lee was not insolvent at the time the credit card debt was canceled, nor has she filed for bankruptcy.
- She wants her refund to be direct deposited to Routing #062005690, Account # 07131968.

For practice using the tax preparation software, complete Lee's tax return using the Practice Lab on Link & Learn Taxes and answer the following questions.

## Scenario Questions

- 5-1** Lee can exclude from income the entire amount of canceled debt.  True  False
- 5-2** If it were determined Lee was insolvent at the time of the cancellation of debt, could a VITA/TCE volunteer still assist her?  Yes  No
- 5-3** What is Lee's adjusted gross income?
- A. \$30,000
  - B. \$32,500
  - C. \$36,500
  - D. \$39,000

## Answers to Practice Scenarios

- |                   |                   |
|-------------------|-------------------|
| <b>1-1:</b> False | <b>3-1:</b> True  |
| <b>1-2:</b> True  | <b>3-2:</b> False |
| <b>1-3:</b> B     | <b>3-3:</b> D     |
| <b>1-4:</b> False |                   |
|                   | <b>4-1:</b> 7,000 |
| <b>2-1:</b> B     | <b>4-2:</b> False |
| <b>2-2:</b> B     |                   |
| <b>2-3:</b> D     | <b>5-1:</b> False |
| <b>2-4:</b> 0     | <b>5-2:</b> No    |
| <b>2-5:</b> B     | <b>5-3:</b> C     |



# Cancellation of Debt – Qualified Principal Residence Indebtedness Test Questions

## Test Answer Sheet

Name \_\_\_\_\_

Instructions: Volunteers with an Advanced, Military, or International Certification may proceed to a certification for Cancellation of Debt (COD). COD is an optional specialty training and certification test available on Link & Learn Taxes. Volunteers must achieve a minimum of 80% to be certified.

**CAUTION: The Test/Retest scenarios are provided electronically in a PDF format for information purposes only. The questions on the online test may be either from the test or retest. Students should read each question on the online test very carefully before answering.**

### Privacy Act Notice

The Privacy Act of 1974 requires that when we ask for information we tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if we do not receive it, and whether your response is voluntary, required to obtain a benefit, or mandatory.

Our legal right to ask for information is 5 U.S.C. 301.

We are asking for this information to assist us in contacting you relative to your interest and/or participation in the IRS volunteer income tax preparation and outreach programs. The information you provide may be furnished to others who coordinate activities and staffing at volunteer return preparation sites or outreach activities. The information may also be used to establish effective controls, send correspondence and recognize volunteers.

Your response is voluntary. However, if you do not provide the requested information, the IRS may not be able to use your assistance in these programs.

| Question                     | Answer          |
|------------------------------|-----------------|
| <b>COD Scenario 1</b>        |                 |
| 1.                           |                 |
| 2.                           |                 |
| 3.                           |                 |
| <b>COD Scenario 2</b>        |                 |
| 4.                           |                 |
| 5.                           |                 |
| 6.                           |                 |
| <b>COD Scenario 3</b>        |                 |
| 7.                           |                 |
| 8.                           |                 |
| <b>COD Scenario 4</b>        |                 |
| 9.                           |                 |
| 10.                          |                 |
| 11.                          |                 |
| 12.                          |                 |
| <b>COD Scenario 5</b>        |                 |
| 13.                          |                 |
| 14.                          |                 |
| <b>COD Scenario 6</b>        |                 |
| 15.                          |                 |
| 16.                          |                 |
| 17.                          |                 |
| <b>COD Scenario 7</b>        |                 |
| 18.                          |                 |
| 19.                          |                 |
| 20.                          |                 |
| Total Answers Correct: _____ |                 |
| Total Questions:             | 20              |
| <b>Passing Score:</b>        | <b>16 of 20</b> |

## Directions

The first three scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

## COD Scenario 1: Mark and Valerie Smith

---

### Interview Notes

- Mark and Valerie received Form 1099-A reporting the foreclosure on their principal residence in 2011.
- At the time of foreclosure, they owed a balance of \$150,000 to the lender (box 2) and the FMV of the property was \$120,000 (box 4).
- Mark and Valerie had owned and lived in the home since 1999.
- They moved out of their home on August 15, 2011.
- Their residence was never used as a business or as rental property.
- Mark and Valerie have not filed for bankruptcy.
- Mark and Valerie were personally liable for the debt.
- The debt has not been canceled by the creditor.

## COD Scenario 1: Test Questions

---

1. How should Mark and Valerie report the foreclosure on their 2011 Form 1040?
  - a. Report the foreclosure on Form 8949 and Schedule D.
  - b. Report the foreclosure on Form 1040, Schedule A.
  - c. They do not need to report the foreclosure on their tax return.
  - d. Report the foreclosure on Form 982.
2. Since Mark and Valerie have a recourse loan, they will report the sales price of the home on Form 8949 and Schedule D as \$120,000.
  - a. True
  - b. False
3. A lender can use Form 1099-A to report both a foreclosure and cancellation of debt if they occur in the same year.
  - a. True
  - b. False

## COD Scenario 2: Frank and Kathy Howell

---

### Interview Notes

- Frank and Kathy Howell owned and lived in their home since 2000.
- They could not make the mortgage payments and moved out of their home in January 2011.
- In October 2011, they received Form 1099-C from the mortgage company showing they were personally liable for the debt (box 5). Box 2 indicated canceled debt of \$75,000. Box 3 indicated no interest.
- The home was never used in a business or as rental property.
- The original mortgage of \$250,000 was used to purchase and was secured by the home.
- They did not file bankruptcy.

### COD Scenario 2: Test Questions

---

4. Frank and Kathy's canceled mortgage debt is an exclusion to the general rule that cancellation of debt is reported as income on the tax return.
  - a. True
  - b. False
5. Frank and Kathy are personally liable for the debt. Another way of saying they are personally liable is to say they have a \_\_\_\_\_ loan.
  - a. Nonrecourse
  - b. Recourse
  - c. Home equity
  - d. Debt consolidation
6. Exceptions to the general rule for reporting cancellation of debt as income are applied before exclusions.
  - a. True
  - b. False

## COD Scenario 3: Wanda Cobb

---

### Interview Notes

- Wanda owned and lived in her home since 2006.
- In 2008, Wanda lost her high paying job. She started a second career as a middle school teacher in 2010.
- In February 2011, she was struggling to make the mortgage payment on her home. She worked out a loan modification agreement with her lender and was able to reduce her monthly mortgage payment by \$500, allowing her to stay in her home.
- Wanda purchased the home in 2006 for \$400,000. In February 2011, at the time of her mortgage workout, the balance owed on her mortgage was \$350,000. Due to the real estate market in her area, the fair market value (FMV) of her home had declined to less than what she currently owed on the mortgage.
- Wanda's lender issued a Form 1099-C, showing \$40,000 in box 2. Box 3 indicated no interest.
- Form 1099-C, box 5 is checked "yes" indicating that she is personally liable for the loan.
- The home was never used in a business or as rental property.
- The mortgage was used to purchase and was secured by the home.
- Wanda has not filed for bankruptcy.

### COD Scenario 3: Test Questions

---

7. How will Wanda report the Form 1099-C information on her 2011 Form 1040?
  - a. She will report it on Form 982, lines 1e, 2, and 10b.
  - b. She will report the transaction on Form 8949, Schedule D, and Form 982.
  - c. She will report it on Form 982, lines 1e and 2.
  - d. She does not have to report it since there was no foreclosure on her home.
8. The basis of Wanda's home is reduced by \$ \_\_\_\_\_

## COD Scenario 4: John and Mary Bates

---

### Taxpayer Documents

- Completed intake and interview sheet
- Social security cards for John and Mary Bates
- Form W-2 for Mary Bates
- Form 1099-R for John Bates
- Form 1099-A from Statewide Mortgage Company
- Form 1099-C from Statewide Mortgage Company

### Interview Notes

- John and Mary Bates want to file a joint return.
- Mary lost her job in 2010 and they got behind on their mortgage payments.
- Mary started working for a flower shop in 2011 but they still struggled to meet all their financial obligations.
- Their mortgage company foreclosed on their principal residence in May 2011.
- The mortgage was used to purchase the home, and was secured by the home. There was no business or rental use of the property. Their records show the following information:
  - Fair Market Value: \$175,000
  - Purchase date: August 16, 1999
  - Cost basis: \$275,000
  - Mortgage balance at the time of foreclosure: \$225,000
- They did not file for bankruptcy.
- They want to know if they can exclude the canceled debt by the mortgage company under the qualified principal residence indebtedness exclusion.
- John and Mary will not itemize for 2011.
- If they have a refund, they want the check mailed to them.



**Intake/Interview & Quality Review Sheet**

**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |  |  |  |                             |
|--|--|--|--|-----------------------------|
| 1. Your First Name<br><b>JOHN</b>  | M. I.  | Last Name<br><b>BATES</b>  | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No   |                             |
| 2. Spouse's First Name<br><b>MARY</b>  | M. I.  | Last Name<br><b>BATES</b>  | Is spouse a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |                             |
| 3. Mailing Address<br><b>1225 10th STREET</b>  | Apt#   | City<br><b>YOUR CITY</b>   | State<br><b>YS</b>   | Zip Code<br><b>YOUR ZIP</b> |
| 4. Contact Information<br>Phone: <b>YOUR PHONE #</b> Cell Phone: ` E-mail: <b>NONE</b>   |  |  |  |                             |
| 5. Your Date of Birth<br><b>08/19/1968</b>   | 6. Your Job Title<br><b>RETIRED MILITARY</b> | Are you:   | 7. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No             |                             |
|  |  | 8. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No  |  |                             |
| 9. Spouse's Date of Birth<br><b>08/15/1975</b>   | 10. Spouse's Job Title<br><b>FLORIST</b>     | Is Spouse:   | 11. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No            |                             |
|  |  | 12. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |  |                             |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |  |  |  |                             |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?

Single

Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No

Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_

Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



**Section B. For Certified Volunteer Preparer Completion**

**Remember:** You are the link between the taxpayer's information and a correct tax return. Verify the taxpayer's information on pages 1, 2 & 3 is complete. All questions must be discussed with the taxpayer and all "Unsure" responses should be changed to "Yes" or "No".

**Must be completed by Certified Volunteer only if persons are listed in Part II Question 2**

Check if persons are listed in Part II Question 2

- Yes  No 1. Can anyone else claim any of the persons listed in Part II, Question 2, as a dependent on their return? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 2. Were any of the persons listed in Part II, Question 2, totally and permanently disabled? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 3. Did any of the persons listed in Part II, Question 2 provide more than 50% of their own support? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No  N/A 4. Did the taxpayer provide more than half the support for each of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 5. Did the taxpayer pay over half the cost of maintaining a home for any of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_

**Reminders**

Use Publication 4012, *Volunteer Resource Guide* and Publication 17, *Your Federal Income Tax* in making tax law determinations.

**Additional Tax Preparer Notes:**

\_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

**Section C. For Certified Quality Reviewer Completion**

**Confirm each item after reviewing the tax return and verifying that it reflects correct tax law application to the information provided by the taxpayer.**

- 1. Sections A & B of this form are complete.
- 2. Taxpayer's identity, address and phone numbers were verified.
- 3. Names, SSN or ITINs, and dates of birth of taxpayer, spouse and dependents match the supporting documents.
- 4. Filing Status is correctly determined.
- 5. Personal and Dependency Exemptions are entered correctly on the return.
- 6. All information shown on source documents and noted in Section A, Part III is included on the tax return.
- 7. Any Adjustments to Income are correctly reported.
- 8. Standard, Additional or Itemized Deductions are correct.
- 9. All credits are correctly reported.
- 10. Withholding shown on Forms W-2, 1099 and Estimated Tax Payments are correctly reported.
- All tax law issues above have been addressed and necessary changes have been made.
- If direct deposit or debit was elected, checking/saving account and routing information match the supporting documents.
- Correct SIDN and EFIN are shown on the return.

|  |  |  |                            |  |                  |
|--|--|--|----------------------------|--|------------------|
| a Employee's social security number<br><b>384-XX-XXXX</b>  |  | Safe, accurate,<br>FAST! Use   |                            | Visit the IRS website at<br>www.irs.gov/efile    |                  |
| b Employer identification number (EIN)<br><b>38-6XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>17,000.00</b>  |                            | 2 Federal income tax withheld<br><b>1,090.00</b> |                  |
| c Employer's name, address, and ZIP code<br><b>SPRING FLOWER SHOP<br/>5062 HASLET ST.<br/>YOUR CITY, STATE ZIP</b> |  | 3 Social security wages<br><b>17,000.00</b>  |                            | 4 Social security tax withheld<br><b>714.00</b>  |                  |
|  |  | 5 Medicare wages and tips<br><b>17,000.00</b>  |                            | 6 Medicare tax withheld<br><b>247.00</b>         |                  |
|  |  | 7 Social security tips   |                            | 8 Allocated tips                                 |                  |
| d Control number   |  | 9  |                            | 10 Dependent care benefits                       |                  |
| e Employee's first name and initial Last name<br><b>MARY BATES<br/>1225 10TH STREET<br/>YOUR CITY, STATE ZIP</b>   |  | 11 Nonqualified plans  |                            | 12a See instructions for box 12                  |                  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |                            | 12b  |                  |
|  |  | 14 Other   |                            | 12c  |                  |
| f Employee's address and ZIP code  |  |  |                            | 12d  |                  |
| 15 State Employer's state ID number<br><b>YS 38-6XXXXXX</b>  | 16 State wages, tips, etc.<br><b>17,000.00</b> | 17 State income tax<br><b>580.00</b>   | 18 Local wages, tips, etc. | 19 Local income tax                              | 20 Locality name |

Form **W-2** Wage and Tax Statement

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|   |   |   |  |   |  |   |  |
|---|---|---|--|---|--|---|--|
| PAYER'S name, street address, city, state, and ZIP code<br><b>DFAS<br/>PO BOX 8899<br/>YOUR CITY, STATE ZIP</b> |   | 1 Gross distribution<br><b>\$ 11,500.00</b>   |  | OMB No. 1545-0119<br><b>2011</b><br>Form <b>1099-R</b>  |  | Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.<br><br><b>Copy B Report this income on your federal tax return. If this form shows federal income tax withheld in box 4, attach this copy to your return.</b> |  |
| PAYER'S federal identification number<br><b>30-2XXXXXX</b>  |   | 2a Taxable amount<br><b>\$ 11,500.00</b>  |  | 2b Taxable amount not determined <input type="checkbox"/> Total distribution <input type="checkbox"/> |  |   |  |
| RECIPIENT'S name<br><b>JOHN BATES</b>   | RECIPIENT'S identification number<br><b>385-XX-XXXX</b> | 3 Capital gain (included in box 2a)<br>\$   |  | 4 Federal income tax withheld<br><b>\$ 640.00</b>   |  | This information is being furnished to the Internal Revenue Service.  |  |
| Street address (including apt. no.)<br><b>1225 10TH STREET</b>  |   | 5 Employee contributions /Designated Roth contributions or insurance premiums<br>\$ |  | 6 Net unrealized appreciation in employer's securities<br>\$  |  |   |  |
| City, state, and ZIP code<br><b>YOUR CITY, STATE ZIP</b>  |   | 7 Distribution code(s)<br><b>7</b>  |  | 8 Other<br>\$ %   |  |   |  |
| 10 Amount allocable to IRR within 5 years<br>\$   |   | 11 1st year of desig. Roth contrib.   |  | 9a Your percentage of total distribution %  |  | 9b Total employee contributions<br>\$   |  |
| Account number (see instructions)   |   | 12 State tax withheld<br>\$   |  | 13 State/Payer's state no.  |  | 14 State distribution<br>\$   |  |
|   |   | 15 Local tax withheld<br>\$   |  | 16 Name of locality   |  | 17 Local distribution<br>\$   |  |

Form **1099-R**

Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

|   |  |  |  |   |   |
|---|--|--|--|---|---|
| LENDER'S name, street address, city, state, ZIP code, and telephone no.<br><b>STATEWIDE MORTGAGE COMPANY<br/>3434 BROADWAY<br/>YOUR CITY, STATE ZIP</b> |  | OMB No. 1545-0877<br><b>2011</b><br>Form 1099-A  |  | <b>Acquisition or<br/>Abandonment of<br/>Secured Property</b> |   |
| LENDER'S federal identification number<br><b>38-9XXXXXX</b>   | BORROWER'S identification number<br><b>385-XX-XXXX</b> | 1 Date of lender's acquisition or knowledge of abandonment<br><b>May 15, 2011</b>  | 2 Balance of principal outstanding<br><b>\$ 225,000.00</b> |   | <b>Copy B<br/>For Borrower</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |
| BORROWER'S name<br><b>JOHN AND MARY BATES</b>   |  | 3  | 4 Fair market value of property<br><b>\$ 175,000.00</b>    |   |   |
| Street address (including apt. no.)<br><b>1225 10TH STREET</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE ZIP</b>                              |  | 5 If checked, the borrower was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |  |   |   |
| Account number (see instructions)   |  | 6 Description of property<br><b>125 OAK STREET<br/>YOUR CITY, STATE ZIP</b>  |  |   |   |

Form 1099-A

(keep for your records)

Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

|   |  |   |  |                                 |   |
|---|--|---|--|---------------------------------|---|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>STATEWIDE MORTGAGE COMPANY<br/>3434 BROADWAY<br/>YOUR CITY, STATE ZIP</b> |  | OMB No. 1545-1424<br><b>2011</b><br>Form 1099-C   |  | <b>Cancellation<br/>of Debt</b> |   |
| CREDITOR'S federal identification number<br><b>38-9XXXXXX</b>   | DEBTOR'S identification number<br><b>385-XX-XXXX</b> | 1 Date canceled<br><b>MAY 15, 2011</b>  | 2 Amount of debt canceled<br><b>\$ 50,000.00</b> |                                 | <b>Copy B<br/>For Debtor</b><br><small>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.</small> |
| DEBTOR'S name<br><b>JOHN AND MARY BATES</b>   |  | 3 Interest if included in box 2<br><b>\$</b>  |  |                                 |   |
| Street address (including apt. no.)<br><b>1225 10TH STREET</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE ZIP</b>                                |  | 4 Debt description<br><b>HOME MORTGAGE LOAN</b>   |  |                                 |   |
| Account number (see instructions)   |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input type="checkbox"/> |  |                                 |   |
|   |  | 6 Bankruptcy (if checked)<br><input type="checkbox"/>   | 7 Fair market value of property<br><b>\$</b>     |                                 |   |

Form 1099-C

(keep for your records)

Department of the Treasury - Internal Revenue Service

## COD Scenario 4: Test Questions

---

### Directions

Using the interview notes, taxpayer documents, and reference material, prepare John and Mary's tax return through line 22 of Form 1040 including the appropriate forms, schedules or worksheets to answer each of the following questions.

*Note: When using the Link & Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your User ID.*

9. What is the selling price of the home shown on Part II of Form 8949? \$\_\_\_\_\_
10. What is the long-term capital gain (or loss) that is reported on Schedule D?
  - a. (\$100,000)
  - b. \$0
  - c. \$50,000
  - d. \$175,000
11. What is the total amount of canceled debt excluded from gross income on Form 982, Part I, line 2?
  - a. \$0
  - b. \$50,000
  - c. \$175,000
  - d. \$225,000
12. Which of the following would cause John and Mary's return to be out of scope?
  - a. They took out a home equity loan in 2007 to vacation in Peru.
  - b. John and Mary filed for bankruptcy.
  - c. They had an interest amount in box 3 of their Form 1099-C.
  - d. All of the above.



## Cancellation of Debt – Nonbusiness Credit Card Indebtedness Test Questions

---

### Directions

The next two scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

### COD Scenario 5: Cynthia Gilmer

---

#### Interview Notes

- In 2011, Cynthia Gilmer negotiated with her credit card company to pay them \$4,500 on her \$12,000 balance. The company agreed to accept it as payment in full.
- At the end of the year, she received Form 1099-C from the credit card company with \$7,500 in box 2. Box 3 indicated no interest.
- It was determined that she was solvent immediately before the cancellation of debt and she was not in bankruptcy.
- Cynthia was personally liable for the payment of the debt.

### COD Scenario 5: Test Questions

---

13. What is the taxable portion of Cynthia's cancellation of debt shown in the Income section of Form 1040? \$\_\_\_\_\_
14. Which forms and/or schedules will Cynthia need to attach to Form 1040 to report the cancellation of debt income?
  - a. No additional forms or schedules are needed
  - b. Form 982
  - c. Form 8949 and Schedule D
  - d. Form 8949, Schedule D, and Form 982

## COD Scenario 6: James Baxter

---

### Interview Notes

- James Baxter borrowed \$4,000 on his bank credit card in 2009 to go to Italy.
- After paying \$1,000 of the bank credit card debt, James lost his job and was unable to pay the balance of \$3,000. The debt was canceled by the bank credit card company in 2011 and they issued a Form 1099-C indicating no interest in box 3.
- James also had a letter from a department store stating that it had canceled his store credit card debt of \$400. The amount canceled did not include interest.
- Immediately before the debt was canceled, James was solvent.
- James was personally liable for the debt.
- James has not filed for bankruptcy.

### COD Scenario 6: Test Questions

---

- 15.** What is the taxable amount of canceled debt from the bank credit card reported in the Income section of Form 1040?
- a. \$1,000
  - b. \$3,000
  - c. \$3,400
  - d. \$4,000
- 16.** Is James required to file Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082, Basis Adjustment), with his 2011 Form 1040?
- a. Yes
  - b. No
- 17.** James is not required to report the \$400 of canceled credit card debt because he did not receive a Form 1099-C from the department store.
- a. True
  - b. False

## COD Scenario 7: Debbie and Jeff Yamhill

---

### Taxpayer Documents

- Social security cards for Debbie and Jeff Yamhill
- Completed intake and interview sheet
- Form W-2 for Debbie Yamhill
- Form W-2 for Jeff Yamhill
- Form 1099-C from National Credit Card Co.

### Interview Notes

- Debbie and Jeff Yamhill want to file a joint tax return.
- They have no dependents.
- Debbie and Jeff settled their \$9,000 personal credit card debt by paying \$5,000. They received a Form 1099-C.
- It was determined that Debbie and Jeff were solvent at the time the credit card debt was canceled, and they have not filed for bankruptcy.
- Debbie and Jeff will not itemize for 2011.
- If they are due a refund, they would like it direct deposited into their checking account:
  - Routing number: 111993776
  - Account number: 43243



**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |  |                                      |  |   |
|--|--|--------------------------------------|--|---|
| 1. Your First Name<br><b>DEBBIE</b>  | M. I.                                    | Last Name<br><b>YAMHILL</b>          | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No   |   |
| 2. Spouse's First Name<br><b>JEFF</b>  | M. I.                                    | Last Name<br><b>YAMHILL</b>          | Is spouse a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |   |
| 3. Mailing Address<br><b>6140 ROSA STREET</b>  | Apt#                                     | City<br><b>YOUR CITY</b>             | State<br><b>YS</b>   | Zip Code<br><b>YOUR ZIP</b>   |
| 4. Contact Information<br>Phone: <b>YOUR PHONE #</b> Cell Phone: ` E-mail: <b>NONE</b>   |  |                                      |  |   |
| 5. Your Date of Birth<br><b>08/29/1982</b>   | 6. Your Job Title<br><b>CLERK</b>        | Are you:                             | 7. Legally Blind   | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
|  |  | 8. Totally and Permanently Disabled  |  | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 9. Spouse's Date of Birth<br><b>07/19/1980</b>   | 10. Spouse's Job Title<br><b>MANAGER</b> | Is Spouse:                           | 11. Legally Blind  | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
|  |  | 12. Totally and Permanently Disabled |  | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |  |                                      |  |   |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter,<br>son, mother,<br>sister, none) | Number<br>of months<br>lived in<br>your home<br>in 2011 | US Citizen or<br>resident of the<br>US, Canada or<br>Mexico in 2011<br>(yes/no) | Marital<br>Status<br>as of<br>12/31/11<br>(S/M) | Full-<br>time<br>student<br>in 2011<br>(yes/no) | Received<br>less than<br>\$3700<br>income<br>in 2011<br>(yes/no) |
|--|-----------------------------|---|---|---|---|---|--|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)   | (g)   | (h)  |
|  |                             |   |   |   |   |   |  |
|  |                             |   |   |   |   |   |  |
|  |                             |   |   |   |   |   |  |
|  |                             |   |   |   |   |   |  |
|  |                             |   |   |   |   |   |  |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. xx-xxxx)

2



**Section B. For Certified Volunteer Preparer Completion**

**Remember:** You are the link between the taxpayer's information and a correct tax return. Verify the taxpayer's information on pages 1, 2 & 3 is complete. All questions must be discussed with the taxpayer and all "Unsure" responses should be changed to "Yes" or "No".

**Must be completed by Certified Volunteer only if persons are listed in Part II Question 2**

Check if persons are listed in Part II Question 2

- Yes  No 1. Can anyone else claim any of the persons listed in Part II, Question 2, as a dependent on their return? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 2. Were any of the persons listed in Part II, Question 2, totally and permanently disabled? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 3. Did any of the persons listed in Part II, Question 2 provide more than 50% of their own support? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No  N/A 4. Did the taxpayer provide more than half the support for each of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 5. Did the taxpayer pay over half the cost of maintaining a home for any of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_

**Reminders**

Use Publication 4012, *Volunteer Resource Guide* and Publication 17, *Your Federal Income Tax* in making tax law determinations.

**Additional Tax Preparer Notes:**

\_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

**Section C. For Certified Quality Reviewer Completion**

**Confirm each item after reviewing the tax return and verifying that it reflects correct tax law application to the information provided by the taxpayer.**

- 1. Sections A & B of this form are complete.
- 2. Taxpayer's identity, address and phone numbers were verified.
- 3. Names, SSN or ITINs, and dates of birth of taxpayer, spouse and dependents match the supporting documents.
- 4. Filing Status is correctly determined.
- 5. Personal and Dependency Exemptions are entered correctly on the return.
- 6. All information shown on source documents and noted in Section A, Part III is included on the tax return.
- 7. Any Adjustments to Income are correctly reported.
- 8. Standard, Additional or Itemized Deductions are correct.
- 9. All credits are correctly reported.
- 10. Withholding shown on Forms W-2, 1099 and Estimated Tax Payments are correctly reported.
- All tax law issues above have been addressed and necessary changes have been made.
- If direct deposit or debit was elected, checking/saving account and routing information match the supporting documents.
- Correct SIDN and EFIN are shown on the return.

|  |  |  |  |  |  |   |  |   |  |                     |  |                  |  |
|--|--|--|--|--|--|---|--|---|--|---------------------|--|------------------|--|
| a Employee's social security number<br><b>597-XX-XXXX</b>  |  | OMB No. 1545-0008  |  | Safe, accurate,<br>FAST! Use                     |  |  |  | Visit the IRS website at<br>www.irs.gov/efile |  |                     |  |                  |  |
| b Employer identification number (EIN)<br><b>59-9XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>20,000.00</b>  |  | 2 Federal income tax withheld<br><b>2,777.00</b> |  |   |  |   |  |                     |  |                  |  |
| c Employer's name, address, and ZIP code<br><b>BEXAR FINANCIAL COMPANY<br/>1200 ALAMO ST.<br/>YOUR CITY, STATE ZIP</b>     |  | 3 Social security wages<br><b>20,000.00</b>  |  | 4 Social security tax withheld<br><b>840.00</b>  |  |   |  |   |  |                     |  |                  |  |
|  |  | 5 Medicare wages and tips<br><b>20,000.00</b>  |  | 6 Medicare tax withheld<br><b>290.00</b>         |  |   |  |   |  |                     |  |                  |  |
|  |  | 7 Social security tips   |  | 8 Allocated tips                                 |  |   |  |   |  |                     |  |                  |  |
| d Control number   |  | 9  |  | 10 Dependent care benefits                       |  |   |  |   |  |                     |  |                  |  |
| e Employee's first name and initial Last name Suff.<br><b>DEBBIE YAMHILL<br/>6140 ROSA STREET<br/>YOUR CITY, STATE ZIP</b> |  | 11 Nonqualified plans  |  | 12a See instructions for box 12                  |  |   |  |   |  |                     |  |                  |  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |  | 12b  |  |   |  |   |  |                     |  |                  |  |
|  |  | 14 Other   |  | 12c  |  |   |  |   |  |                     |  |                  |  |
|  |  |  |  | 12d  |  |   |  |   |  |                     |  |                  |  |
| f Employee's address and ZIP code  |  | 15 State Employer's state ID number<br><b>YS 59-9XXXXXX</b>  |  | 16 State wages, tips, etc.<br><b>20,000.00</b>   |  | 17 State income tax<br><b>533.00</b>  |  | 18 Local wages, tips, etc.                    |  | 19 Local income tax |  | 20 Locality name |  |

Form **W-2 Wage and Tax Statement**

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

|  |  |  |  |  |  |   |  |   |  |                     |  |                  |  |
|--|--|--|--|--|--|---|--|---|--|---------------------|--|------------------|--|
| a Employee's social security number<br><b>598-XX-XXXX</b>  |  | OMB No. 1545-0008  |  | Safe, accurate,<br>FAST! Use                     |  |  |  | Visit the IRS website at<br>www.irs.gov/efile |  |                     |  |                  |  |
| b Employer identification number (EIN)<br><b>59-3XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>16,500.00</b>  |  | 2 Federal income tax withheld<br><b>1,650.00</b> |  |   |  |   |  |                     |  |                  |  |
| c Employer's name, address, and ZIP code<br><b>DAYLILLY RESTAURANT<br/>3200 BROADWAY<br/>YOUR CITY, STATE ZIP</b>        |  | 3 Social security wages<br><b>16,500.00</b>  |  | 4 Social security tax withheld<br><b>693.00</b>  |  |   |  |   |  |                     |  |                  |  |
|  |  | 5 Medicare wages and tips<br><b>16,500.00</b>  |  | 6 Medicare tax withheld<br><b>239.00</b>         |  |   |  |   |  |                     |  |                  |  |
|  |  | 7 Social security tips   |  | 8 Allocated tips                                 |  |   |  |   |  |                     |  |                  |  |
| d Control number   |  | 9  |  | 10 Dependent care benefits                       |  |   |  |   |  |                     |  |                  |  |
| e Employee's first name and initial Last name Suff.<br><b>JEFF YAMHILL<br/>6140 ROSA STREET<br/>YOUR CITY, STATE ZIP</b> |  | 11 Nonqualified plans  |  | 12a See instructions for box 12                  |  |   |  |   |  |                     |  |                  |  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |  | 12b  |  |   |  |   |  |                     |  |                  |  |
|  |  | 14 Other   |  | 12c  |  |   |  |   |  |                     |  |                  |  |
|  |  |  |  | 12d  |  |   |  |   |  |                     |  |                  |  |
| f Employee's address and ZIP code  |  | 15 State Employer's state ID number<br><b>YS 59-3XXXXXX</b>  |  | 16 State wages, tips, etc.<br><b>16,500.00</b>   |  | 17 State income tax<br><b>275.00</b>  |  | 18 Local wages, tips, etc.                    |  | 19 Local income tax |  | 20 Locality name |  |

Form **W-2 Wage and Tax Statement**

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|  |  |  |                                  |  |
|--|--|--|----------------------------------|--|
| CREDITOR'S name, street address, city, state, ZIP code, and telephone no.<br><b>NATIONAL CREDIT CARD CO.<br/>110 THIRD STREET<br/>YOUR CITY, STATE ZIP</b> |  | 1 Date canceled<br><b>11/29/11</b>   | OMB No. 1545-1424<br><b>2011</b> | <b>Cancellation of Debt</b>  |
|  |  | 2 Amount of debt canceled<br><b>\$ 4,000.00</b>  | Form <b>1099-C</b>               |  |
|  |  | 3 Interest if included in box 2<br>\$  |                                  |  |
| CREDITOR'S federal identification number<br><b>38-8XXXXXX</b>  | DEBTOR'S identification number<br><b>597-XX-XXXX</b> | 4 Debt description<br><b>CREDIT CARD DEBT</b>  |                                  | <b>Copy B<br/>For Debtor</b><br>This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported. |
| DEBTOR'S name<br><b>DEBBIE AND JEFF YAMHILL</b>  |  | 5 If checked, the debtor was personally liable for repayment of the debt . . . . . <input checked="" type="checkbox"/> |                                  |  |
| Street address (including apt. no.)<br><b>6140 ROSA STREET</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE ZIP</b>                                 |  | 7 Fair market value of property<br>\$  |                                  |  |
| Account number (see instructions)  |  | 6 Bankruptcy (if checked)<br><input type="checkbox"/>  |                                  |  |

Form **1099-C**

(keep for your records)

Department of the Treasury - Internal Revenue Service

## COD Scenario 7: Test Questions

---

### Directions

Using the interview notes, taxpayer documents, and reference material, prepare Debbie and Jeff's tax return through line 37 of Form 1040 including the appropriate forms, schedules or worksheets to answer each of the following questions.

*Note: When using the Link & Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your User ID.*

18. On which schedule or form is the excluded portion of their canceled credit card debt reported?
  - a. Debbie and Jeff cannot exclude the debt. No additional schedule or form is filed with Form 1040.
  - b. Schedule A
  - c. Schedule D
  - d. Form 982
  
19. If the Yamhills were insolvent immediately before their non-business credit card debt was canceled, \_\_\_\_\_
  - a. part or all of the canceled debt may be excluded from income.
  - b. their return would be out of scope for the volunteer program.
  - c. the volunteer should prepare their tax return.
  - d. part or all of the canceled debt may be excluded from income, and their return would be out of scope for the volunteer program. (Both answers A & B.)
  
20. What is the Yamhills' adjusted gross income?
  - a. \$35,500
  - b. \$40,500
  - c. \$41,500
  - d. \$45,000



# Cancellation of Debt – Retest Questions

## Retest Answer Sheet

Name \_\_\_\_\_

Instructions: Volunteers with an Advanced, Military, or International Certification may proceed to a certification for Cancellation of Debt (COD). COD is an optional specialty training and certification test available on Link & Learn Taxes. Volunteers must achieve a minimum of 80% to be certified.

**CAUTION: The Test/Retest scenarios are provided electronically in a PDF format for information purposes only. The questions on the online test may be either from the test or retest. Students should read each question on the online test very carefully before answering.**

### Privacy Act Notice

The Privacy Act of 1974 requires that when we ask for information we tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if we do not receive it, and whether your response is voluntary, required to obtain a benefit, or mandatory.

Our legal right to ask for information is 5 U.S.C. 301.

We are asking for this information to assist us in contacting you relative to your interest and/or participation in the IRS volunteer income tax preparation and outreach programs. The information you provide may be furnished to others who coordinate activities and staffing at volunteer return preparation sites or outreach activities. The information may also be used to establish effective controls, send correspondence and recognize volunteers.

Your response is voluntary. However, if you do not provide the requested information, the IRS may not be able to use your assistance in these programs.

| Question                     | Answer          |
|------------------------------|-----------------|
| <b>COD Scenario 1</b>        |                 |
| 1.                           |                 |
| 2.                           |                 |
| 3.                           |                 |
| <b>COD Scenario 2</b>        |                 |
| 4.                           |                 |
| 5.                           |                 |
| 6.                           |                 |
| <b>COD Scenario 3</b>        |                 |
| 7.                           |                 |
| 8.                           |                 |
| <b>COD Scenario 4</b>        |                 |
| 9.                           |                 |
| 10.                          |                 |
| 11.                          |                 |
| 12.                          |                 |
| <b>COD Scenario 5</b>        |                 |
| 13.                          |                 |
| 14.                          |                 |
| <b>COD Scenario 6</b>        |                 |
| 15.                          |                 |
| 16.                          |                 |
| 17.                          |                 |
| <b>COD Scenario 7</b>        |                 |
| 18.                          |                 |
| 19.                          |                 |
| 20.                          |                 |
| Total Answers Correct: _____ |                 |
| Total Questions:             | 20              |
| <b>Passing Score:</b>        | <b>16 of 20</b> |

## Directions

The first three scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

### COD Scenario 1: Mark and Valerie Smith

---

#### Interview Notes

- Mark and Valerie received Form 1099-A reporting the foreclosure on their principal residence in 2011.
- At the time of foreclosure, they owed a balance of \$150,000 to the lender (box 2) and the FMV of the property was \$120,000 (box 4).
- Mark and Valerie had owned and lived in the home since 1999.
- They moved out of their home on August 15, 2011.
- Their residence was never used as a business or as rental property.
- Mark and Valerie have not filed for bankruptcy.
- Mark and Valerie were personally liable for the debt.
- The debt has not been canceled by the creditor.

### COD Scenario 1: Retest Questions

---

1. Mark and Valerie should report the foreclosure of their home on Form 8949 and Schedule D.
  - a. True
  - b. False
2. If Mark and Valerie had a nonrecourse loan, they would report the sales price of the home on Form 8949 and Schedule D as \$150,000.
  - a. True
  - b. False
3. Can the lender report both a foreclosure and cancellation of debt on Form 1099-C if they occur in the same year?
  - a. Yes
  - b. No

## COD Scenario 2: Frank and Kathy Howell

---

### Interview Notes

- Frank and Kathy Howell owned and lived in their home since 2000.
- They could not make the mortgage payments and moved out of their home in January 2011.
- In October 2011, they received Form 1099-C from the mortgage company showing they were personally liable for the debt (box 5). Box 2 indicated canceled debt of \$75,000. Box 3 indicated no interest.
- The home was never used in a business or as rental property.
- The original mortgage of \$250,000 was used to purchase and was secured by the home.
- They did not file bankruptcy.

### COD Scenario 2: Retest Questions

---

4. Which of the following is **not** an exception to the general rule that cancellation of debt is income to the taxpayer?
  - a. Gifts
  - b. Insolvency
  - c. Deductible debt
  - d. Certain student loans
5. If Frank and Kathy were personally liable for the debt, their loan would be a recourse loan.
  - a. True
  - b. False
6. Which of the following is an exclusion to the general rule that cancellation of debt is income to the taxpayer?
  - a. Discharge of debt of an insolvent taxpayer
  - b. Discharge of debt through bankruptcy
  - c. Discharge of qualified principal residence indebtedness
  - d. All of the above

## COD Scenario 3: Wanda Cobb

---

### Interview Notes

- Wanda owned and lived in her home since 2006.
- In 2008, Wanda lost her high paying job. She started a second career as a middle school teacher in 2010.
- In February 2011, she was struggling to make the mortgage payment on her home. She worked out a loan modification agreement with her lender and was able to reduce her monthly mortgage payment by \$500, allowing her to stay in her home.
- Wanda purchased the home in 2006 for \$400,000. In February 2011, at the time of her mortgage workout, the balance owed on her mortgage was \$350,000. Due to the real estate market in her area, the fair market value (FMV) of her home had declined to less than what she currently owed on the mortgage.
- Wanda's lender issued a Form 1099-C, showing \$40,000 in box 2. Box 3 indicated no interest.
- Form 1099-C, box 5 is checked "yes" indicating that she is personally liable for the loan.
- The home was never used in a business or as rental property.
- The mortgage was used to purchase and was secured by the home.
- Wanda has not filed for bankruptcy.

### COD Scenario 3: Retest Questions

---

7. Line \_\_\_ of Form 982 is used to report the reduction in basis of Wanda's home.
  - a. 1e
  - b. 2
  - c. 10a
  - d. 10b
8. What is the amount reported on Form 982, line 2? \$\_\_\_\_\_

## COD Scenario 4: Retest Questions

---

### Directions

Refer to the scenario information for John and Mary Bates beginning on page 1-46.

Using the interview notes, taxpayer documents, and reference material, prepare John and Mary's tax return through line 22 of Form 1040 including the appropriate forms, schedules or worksheets to answer each of the following questions.

*Note: When using the Link & Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your User ID.*

9. What is the selling price of the home shown on Part II of Form 8949?
  - a. \$50,000
  - b. \$175,000
  - c. \$225,000
  - d. \$275,000
  
10. What is the long-term capital gain (or loss) that is reported on Schedule D? \$\_\_\_\_\_
  
11. What is the total amount of canceled debt John and Mary can exclude from gross income on Form 982, Part I, line 2? \$\_\_\_\_\_
  
12. John and Mary's return would be out of scope for the VITA/TCE program if:
  - a. They used the proceeds from a home equity loan to pay off their credit card debt
  - b. They had someone rent an apartment in their basement
  - c. They filed for bankruptcy
  - d. All of the above

## Directions

The next two scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

## COD Scenario 5: Cynthia Gilmer

---

### Interview Notes

- In 2011, Cynthia Gilmer negotiated with her credit card company to pay them \$4,500 on her \$12,000 balance. The company agreed to accept it as payment in full.
- At the end of the year, she received Form 1099-C from the credit card company with \$7,500 in box 2. Box 3 indicated no interest.
- It was determined that she was solvent immediately before the cancellation of debt and she was not in bankruptcy.
- Cynthia was personally liable for the payment of the debt.

## COD Scenario 5: Retest Questions

---

13. What taxable amount of canceled debt, if any, is included in the Income section of Form 1040?
  - a. \$0
  - b. \$4,500
  - c. \$7,500
  - d. \$12,000
14. Cynthia will need to attach Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness, to her 2011 Form 1040.
  - a. True
  - b. False

## COD Scenario 6: James Baxter

---

### Interview Notes

- James Baxter borrowed \$4,000 on his bank credit card in 2009 to go to Italy.
- After paying \$1,000 of the bank credit card debt, James lost his job and was unable to pay the balance of \$3,000. The debt was canceled by the bank credit card company in 2011 and they issued a Form 1099-C indicating no interest in box 3.
- James also had a letter from a department store stating that it had canceled his store credit card debt of \$400. The amount canceled did not include interest.
- Immediately before the debt was canceled, James was solvent.
- James was personally liable for the debt.
- James has not filed for bankruptcy.

### COD Scenario 6: Retest Questions

---

15. What is the taxable amount of canceled debt from the bank credit card reported in the Income section of Form 1040? \$\_\_\_\_\_.
16. How much should be reported on Form 982 as discharged indebtedness excluded from gross income?
  - a. \$3,000
  - b. \$3,400
  - c. \$4,000
  - d. Nothing, Form 982 is not required
17. James is still required to report the \$400 of canceled credit card debt even if the department store credit card company fails to send a Form 1099-C.
  - a. True
  - b. False

## COD Scenario 7: Retest Questions

---

### Directions

Refer to the scenario information for Debbie and Jeff Yamhill beginning on page 1-56.

Using the interview notes, taxpayer documents, and reference material, prepare Debbie and Jeff's tax return through line 37 of Form 1040 including the appropriate forms, schedules or worksheets to answer each of the following questions.

*Note: When using the Link & Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your User ID.*

18. Debbie and Jeff should not file Form 982 with their 2011 Form 1040.
  - a. True
  - b. False
  
19. In general, if the Yamhills were solvent immediately before their non-business credit card debt was canceled, \_\_\_\_\_
  - a. the entire amount of canceled debt would be reported on Form 1040, line 21.
  - b. the volunteer would have to exclude part of the canceled debt from income.
  - c. the return would be in scope for the volunteer program.
  - d. the entire amount of canceled debt would be reported on Form 1040, line 21, and the return would be in scope for the volunteer program. (Both answers A and C.)
  
20. What is the Yamhills' adjusted gross income on their 2011 Form 1040?  
\$\_\_\_\_\_





# Health Savings Accounts (HSAs)



## Introduction

**NEW** Health Savings Accounts (HSAs) is now an optional course for volunteers with Intermediate certification or higher. Check with your Site Coordinator to determine if you should seek certification in this topic.

This course was developed to help volunteers assist taxpayers who have an HSA. HSAs allow individuals with high-deductible health insurance to use tax-deductible contributions to pay qualified medical expenses. The course covers **HSA eligibility, contributions, and distributions**. In addition, it covers **reporting HSA activity on Form 8889, Health Savings Accounts**.

## Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Define an HSA and other tax-favored arrangements
- Determine eligibility to contribute to an HSA
- Calculate the limits on contributions to an HSA
- Identify information documents, Forms 5498-SA, W-2 and 1099-SA, used in reporting contributions and distributions
- Determine when and how to report HSA contributions on Form 8889 and calculate the tax deduction, if any
- Determine when and how to report HSA distributions on Form 8889
- Explain the effects of losing HSA eligibility

## What is out of scope for VITA/TCE?

Some aspects of HSAs are complex and are out of scope for VITA/TCE. Refer taxpayers with these issues to a professional tax preparer:

- Excess contributions to an HSA that are not withdrawn in a timely fashion
- Qualified HSA funding distributions from an IRA
- Qualified HSA distributions from a health Flexible Spending Arrangement (FSA) or a Health Reimbursement Arrangement (HRA)
- Death of an HSA holder
- Form 8889, Part III, Income and Additional Tax for Failure to Maintain HDHP Coverage
- Deemed distributions from an HSA due to prohibited transactions, such as using an HSA as a security for a loan

For more information, see Publication 969, Health Savings Accounts and Other Tax-Favored Health Plans.

### What do I need?

- Intake and Interview Sheet
- Publication 17
- Publication 502
- Publication 969
- Publication 4885, HSA Screening Sheet
- Form 1040
- Form 8889 and Instructions
- Form 5498-SA and Instructions
- Form 1099-SA and Instructions
- Form W-2 and Instructions
- Optional:**
- Form 1040 Instructions

## The Background on HSAs

---

Congress authorized the creation of health savings accounts (HSAs) in 2003. An HSA is a tax-favored medical savings account available to taxpayers. HSAs enable taxpayers to pay for current medical expenses and save for future qualified medical expenses on a tax-free basis.

HSAs are owned by individuals, but contributions may be made by an employer or any other person. Amounts in an HSA may be accumulated over the years or distributed on a tax-free basis to pay for or reimburse qualified medical expenses.

As the number of HSAs continues to increase, having this training available for volunteers will be a benefit to the program.

### TIP

HSAs are similar to Individual Retirement Accounts (IRAs). Qualified taxpayers can make contributions to a designated account that may be deductible, and there are rules related to distributions.

### Intake/Interview Process

Use the interview techniques and tools discussed in the Screening and Interviewing lesson. Use Form 13614-C, Intake/Interview & Quality Review Sheet to determine if the taxpayer had HSA contributions or distributions, addressed in Question 1 of the Life Events section. The intake and interview sheet is a starting point for a comprehensive interaction with the taxpayer. This interaction, along with the source documents provided by the taxpayer, will help you prepare an accurate return.

Form 5498-SA is used to report HSA contributions and Form 1099-SA is used to report HSA distributions. These information documents are issued by the HSA trustee to taxpayers who have HSA contributions or distributions, for use in tax return preparation.

Confirm each item on the intake and interview sheet to make sure you and the taxpayer have considered all the necessary information. If items are incorrect or incomplete, revisit the issue and make corrections to the return, as needed.

### HSA Helpful Hints and HSA Screening Sheet

The HSA Helpful Hints document was developed to provide an at-a-glance summary of the HSA topic. Publication 4885, HSA Screening Sheet, was developed to help volunteers determine if the HSA issue was within the scope of the volunteer program. Use these references if HSA questions arise during the interview with the taxpayer.

The HSA Helpful Hints and the HSA Screening Sheet are included in Publication 4012, the Volunteer Resource Guide (Tab E). You can download and print a copy of Publication 4885, HSA Screening Sheet, from [www.irs.gov](http://www.irs.gov).

### New Legislation and HSAs

The Affordable Care Act (ACA) was passed in March 2010.

The IRS's role is to administer the various **tax** provisions included in the new law. The Department of Health and Human Services (HHS) has the lead in all health insurance and health care policy provisions of the new legislation.

**NEW** The Affordable Care Act made the following changes to HSAs:

- Beginning in 2011, taxpayers must have a prescription for over-the-counter medicine in order to pay for over-the-counter medicine with a distribution from a health savings account (HSA) and have that distribution be tax-free. *This change does not apply to insulin.*
- The additional tax increased. For HSA purposes, the additional tax on distributions not used for qualified medical expenses is increased to 20%. This applies to distributions after 2010.

These changes are covered in detail in the course.

## Types of Tax-Favored Arrangements

---

### What are tax-favored arrangements?

Various programs are designed to give individuals tax advantages to offset health care costs. This section provides general definitions of other tax-favored arrangements. These definitions will help you distinguish the **differences** in these programs and help with your overall understanding of tax-favored arrangements. While these programs may have features similar to an HSA, it is important to know they are different.

Types of tax-favored arrangements are:

- Archer Medical Savings Accounts
- Medicare Advantage MSAs
- Health Reimbursement Arrangements
- Flexible Spending Arrangements

### ***Archer Medical Savings Accounts (MSAs)***

The Archer MSA represents the first generation of HSAs. MSA contributions may be received from either an eligible individual or his or her employer but not in the same tax year. Contributions by the individual are taken as an adjustment to income and are deductible whether or not the individual itemizes deductions. Employer contributions are not included in taxable income. As long as distributions from an MSA are used to pay qualified medical expenses, they are not taxed. But MSA eligibility is restricted to employees of small employers and the self-employed, which rules out participation for many taxpayers.

### ***Medicare Advantage MSAs***

A Medicare Advantage MSA is an Archer MSA designated by Medicare to be used solely to pay the qualified expenses of the account holder who is enrolled in Medicare. Contributions can only be made by Medicare. The contributions are not included in the individual's income. Distributions from a Medicare Advantage MSA that are used to pay qualified medical expenses are not taxed.

### ***Health Reimbursement Arrangements (HRAs)***

An HRA must receive contributions from the employer only. Employees may not contribute. Contributions are not includible in income. Reimbursements from an HRA that are used to pay qualified medical expenses are not taxed.



Refer taxpayers with an Archer Medical Savings Account, Medicare Advantage MSA, or a Health Reimbursement Arrangement to a professional tax preparer. These topics are out of scope and the information is provided for your awareness only.

### ***Flexible Spending Arrangements (FSAs)***

A health Flexible Spending Arrangement (FSA) allows an employee to be reimbursed for medical expenses. An FSA is usually funded through a voluntary salary reduction agreement with the employer. No employment tax or federal income tax is deducted from an employee's contribution. The employer may also contribute. The FSA is not a health plan but only a means of reimbursing the FSA participant for qualified medical expenses. Unused funds will be lost if not spent by the end of the qualifying period. Do not confuse FSAs with HSAs; FSA activity is not reported on an individual tax return.

## What is an HSA?

An HSA is the newest of all tax-favored medical savings plans. An HSA is a tax-exempt trust or custodial account that a taxpayer sets up with a qualified HSA trustee. Distributions from an HSA are nontaxable if the funds are used for qualified medical expenses. A taxpayer must be an eligible individual to qualify for an HSA.

No permission or authorization from the IRS is necessary to establish an HSA. To set up an HSA a taxpayer will need to work with a trustee. A qualified HSA trustee can be a bank, an insurance company, or anyone already approved by the IRS to be a trustee of individual retirement arrangements (IRAs) or Archer MSAs. The HSA can be established through a trustee that is different from the taxpayer's health plan provider.

An HSA is created by:

- Enrolling in a High-Deductible Health Plan (HDHP) and then
- Opening a tax-exempt trust or custodial account, with a qualified HSA trustee, to pay for qualified medical expenses

## HSA Benefits

There are several benefits from having an HSA including the following:

- The taxpayer can claim a tax deduction for contributions made by the taxpayer or someone other than an employer, even if the taxpayer does not itemize deductions on Form 1040.
- Contributions to an HSA by an employer may be excluded from gross income; this includes contributions made through a Section 125 cafeteria plan.
- The contributions remain in the account from year to year until the taxpayer uses them.
- The interest and other earnings on the assets in the account are tax-free.
- Distributions may be tax-free if used to pay unreimbursed qualified medical expenses.
- An HSA is portable, so it stays with taxpayers even if they change employers or leave the work force.



### EXERCISES

Answers are at the end of the lesson.

**Question 1:** Does an HSA stay with the taxpayer even if the taxpayer changes employers?

Yes  No

**Question 2:** Which of the following statements is false?

- A. Taxpayers' contributions to an HSA are tax deductible.
- B. Interest earned on an HSA is tax-free if used for unreimbursed qualified medical expenses.
- C. Taxpayers pay taxes on HSA earnings when they take distributions for unreimbursed qualified medical expenses.
- D. Unused funds and interest are carried over, without limit, from year to year.

## Individuals Who Qualify for an HSA

To be an **eligible individual** and qualify for an HSA, taxpayers must meet the following requirements:

- Be covered by a high-deductible health plan (HDHP) on the first day of the month
- Not be covered by other health insurance (see Publication 969 for exceptions)
- Not be enrolled in Medicare (the individual can be HSA-eligible for the months before being covered by Medicare)
- Not be eligible to be claimed as a dependent on someone else's tax return (see Caution)

### **Rules for Married Individuals**

In the case of married individuals, each spouse who is an eligible individual who wants to have an HSA must open a separate HSA. Married couples cannot have a joint HSA, but distributions can be used to cover the qualified expenses of the other spouse.

## High-Deductible Health Plan

Taxpayers must be covered by a high-deductible health plan (HDHP) to take advantage of HSAs. An HDHP generally costs less than traditional health care coverage. These cost savings can then be put into the HSA.

An HDHP is health coverage with a:

- Higher annual deductible than typical health plans and
- Maximum limit on the sum of the annual deductible and out-of-pocket medical expenses that the taxpayer must pay for covered expenses. Out-of-pocket expenses include co-payments and other amounts but do not include premiums.

The IRS has ruled that an HDHP can cover certain types of **preventive care** without a deductible, or with a deductible that is less than the annual deductible applicable to all other services. Generally, preventive care services do not include any service, benefit, or medication to treat an existing illness, injury, or condition. In situations where the treatment is incidental or ancillary to a preventive care service or screening, the treatment may fall within the safe-harbor for preventive care. See IRS Notice 2004-50, Internal Revenue Bulletin 2004-33, available on [www.irs.gov](http://www.irs.gov), for details on these situations.

If an HDHP has a deductible for preventive care expenses, those expenses, up to the deductible, are qualified medical expenses for HSA purposes. If the HDHP has no deductible for these preventive services, the plan – not the HSA – covers the expenses.



If another taxpayer is entitled to claim an exemption for the individual, the individual cannot claim a deduction for an HSA contribution. This is true even if the other person does not actually claim the exemption.



An employee covered by an HDHP and a health FSA or an HRA that pays or reimburses qualified medical expenses generally cannot make contributions to an HSA.



In addition to preventive care, the high deductible requirements are not necessary for dental or vision coverage.

## HDHP Deductible Limits

There are limits for annual deductible and out-of-pocket expenses for HDHPs.

| HDHP Deductible Limits for 2011                            |                    |                 |
|--|--------------------|-----------------|
|  | Self-Only Coverage | Family Coverage |
| Minimum Annual Deductible                                  | \$1,200            | \$2,400         |
| Maximum Annual Deductible and Other Out-of-Pocket Expenses | \$5,950            | \$11,900        |

For more information, refer to Publication 969.



### EXERCISES (continued)

**Question 3:** An HDHP must have a minimum and maximum annual deductible along with other out-of-pocket expenses.

For 2011 what are the limits for self-only coverage for minimum annual deductible and maximum annual deductible and other out-of-pocket expenses for HDHPs?

- A. \$1,150 and \$5,800
- B. \$1,200 and \$5,950
- C. \$2,400 and \$11,900

**Question 4:** Frank is retired and has no other health coverage except for Medicare. He would like to open an HSA to cover his additional medical expenses. He's been shopping for high-deductible health plans. Provided he gets an HDHP, is he eligible for an HSA?  Yes  No

**Question 5:** Bill and Ann are married. They are both self-employed, and each is enrolled in a self-only HDHP. Can Bill and Ann set up a joint HSA?  Yes  No

**Question 6:** John is 18 years old and a full-time student. He also works and is covered under his employer's HDHP (self-only). John's parents are eligible to claim him as a dependency exemption on their tax return, but they choose not to claim him. Does John qualify for an HSA?  Yes  No

## Contributions to HSAs

Any eligible individual can contribute to an HSA. For an employee's HSA, the employee, employer, or both may contribute to the employee's HSA in the same year. For an HSA established by a self-employed (or unemployed) individual, the individual can contribute.

Family members or any other person may also contribute on behalf of an eligible individual. Contributions to an HSA must be made in cash. Contributions of stock or property are not allowed.

### Employer Contributions

Taxpayers must reduce the amount they, or any other person, can contribute to their HSA by the amount of any contributions made by the taxpayer's employer that are excludable from income. This includes amounts contributed to the taxpayer's account by the employer through a cafeteria plan.



## EXERCISES (continued)

**Question 7:** Arnold has a high-deductible health plan with an HSA with his company. His mother contributed to his HSA as a gift on his 40th birthday. Is this an allowable contribution?  Yes  No

### HSA Limits on Contributions

The amount that can be contributed to an HSA depends on the type of HDHP coverage, the taxpayer's age, the date the taxpayer became an eligible individual, and the date the taxpayer ceases to be an eligible individual.

For 2011, if the taxpayer has self-only HDHP coverage, the contribution limit is \$3,050. If the taxpayer has family HDHP coverage, the contribution is limited to \$6,150.

Employer contributions (including an employee's contribution through a cafeteria plan) are allowed to be made to an employee's HSA. Generally, employer contributions are excludable from an employee's income. *Taxpayers must reduce the amount that they or any other person can contribute to their HSA by the amount of any employer contributions that are excludable from income.* For example, if the employer contributed \$1,000 to a taxpayer's HSA who had a self-only HDHP, the remaining contribution limit would be \$2,050.

Eligible individuals who are 55 or older by the end of the tax year can increase their contribution limit up to \$1,000 a year for 2011. For example, an eligible individual who is 55 or older with self-only coverage can contribute up to \$4,050. This extra amount is the catch-up contribution allowed for HSAs.

The table below provides the 2011 HSA contribution limits established by the IRS. Remember these are maximum allowable contribution amounts. Confirm with the taxpayer the amounts actually contributed to the HSA.

| 2011 HSA Contribution Limits   |                    |                 |
|--|--------------------|-----------------|
|  | Self-Only Coverage | Family Coverage |
| Annual Contribution Limit  | \$3,050            | \$6,150         |
| Catch-up Contribution (55 or older)*   | \$1,000            | \$1,000         |
| *Spouses 55 or older each make the additional contribution to their own HSA. |                    |                 |



Taxpayers with excess contributions (contributions over the limits) must withdraw the excess to avoid an additional tax. If the excess was not timely withdrawn, refer the taxpayer to a professional tax preparer. Review Form 8889 Instructions, line 13 and Publication 969 for details.



## EXERCISES (continued)

**Question 8:** What is the maximum amount an eligible taxpayer under age 55 can contribute if the taxpayer has a self-only HDHP?

- A. \$4,050
- B. \$1,000
- C. \$3,050
- D. \$6,150

**Question 9:** Marie is 56 years old. She wants to contribute as much as she can to her HSA. She had self-only coverage for the entire year of 2011. What is the maximum amount that Marie can contribute to her HSA?

- A. \$4,050
- B. \$1,000
- C. \$3,050
- D. \$6,150

### Rules for Married People

The rules for married people apply only if both spouses are eligible individuals. If either spouse has family HDHP coverage and the family contribution limit of \$6,150 applies, both spouses are treated as having family HDHP coverage. If each spouse has family coverage under a separate plan, the contribution limit remains at \$6,150.

If **both** spouses are 55 or older and not enrolled in Medicare:

- Each spouse is entitled to increase his or her contribution limit with an additional contribution.
- Their maximum total contributions under family HDHP coverage cannot be more than \$8,150 ( $\$6,150 + [\$1,000 \times 2] = \$8,150$ ). This rule applies regardless of whether each spouse's family coverage covers the other spouse.
- The contribution limit is divided between the spouses by agreement. If there is no agreement, the contribution limit is split equally between the spouses.
- Any additional contribution for age 55 or over must be made by each spouse to his or her own HSA.

#### example

For 2011, Mr. Auburn and his wife are both eligible individuals. They each have family coverage under separate HDHPs. Mr. Auburn is 58 years old and Mrs. Auburn is 53. Mr. and Mrs. Auburn can split the family contribution limit (\$6,150) equally, or they can agree on a different division. If they split it equally, Mr. Auburn can contribute \$4,075 to an HSA (one-half the maximum contribution for family coverage  $\$3,075 + \$1,000$  additional contribution), and Mrs. Auburn can contribute \$3,075 to an HSA.



**Tax Software Hint:** A manual calculation will be needed for Forms 8889 line 6 for a married couple with separate HSAs. The manual calculation is based upon equal amounts or the amounts agreed upon by the taxpayers. Remember the additional contributions for 55 or over must go into the HSA belonging to the person who meets the age requirement.

## Case Study

Harry and Wilma are married and both are 45 years old. Harry and Wilma are otherwise eligible individuals. Harry has self-only HDHP coverage, and Wilma has an HDHP with family coverage for Wilma and their two children. In 2011, their combined family contribution limit is \$6,150. Harry and Wilma can split the family contribution limit (\$6,150) equally or they can agree on a different division.

If Harry and Wilma each have family coverage HDHPs, the contribution limit for their HSAs would still be \$6,150. They could split this equally or agree on a different division.



### EXERCISES (continued)

**Question 10:** The HSA contribution limit is \$7,150 for a married couple when both spouses have family HDHP coverage and one spouse is age 55 or older.  True  False

## Contribution Rule Limits

While most taxpayers may not contribute the maximum amount allowed to their HSA, you may need to explain these limits to taxpayers. The amount that can be contributed to an HSA depends on the:

- Type of HDHP coverage (self-only or family coverage)
- Taxpayer's age
- Date the taxpayer became an eligible individual, *and*
- Date the taxpayer ceases to become an eligible individual.

If the taxpayer is an eligible individual on the first day of every month with the same coverage for the entire year, the full contribution amount is allowed.

If the taxpayer was not an eligible individual for the entire year or changed his or her coverage during the year, the contribution limit is the greater of the:

- **Last-month rule** (also known as the full contribution rule). Maximum annual HSA contribution is based on the first day of the last month of the person's taxable year (December 1 for most taxpayers) plus catch-up contributions. The taxpayer is considered to have been an eligible individual for the entire year. The taxpayer is treated as enrolled in the same HDHP coverage for the entire year. A testing period (covered later in this lesson) applies to this rule.

OR

- **Sum of the monthly contribution limits rule** (use Line 3 Limitation Chart and Worksheet in Form 8889 Instructions). This is the amount determined separately for each month based on eligibility and HDHP coverage on the first day of each month plus catch-up contributions.

A taxpayer who cannot use the last-month rule **must** use the sum of the monthly contribution limits rule to determine the maximum HSA contribution.



**Tax Software Hint:** The Line 3 Limitation Worksheet is at the bottom of Form 8889, page 1. You will also need the Instructions for Form 8889. To view the instructions, click anywhere on the form to access the help feature.

## Last-Month Rule

A taxpayer may contribute the full amount to an HSA using the last-month rule if the taxpayer was an eligible individual on the first day of the last month of the tax year (December 1 for most taxpayers).

If the taxpayer does not qualify to contribute the full amount for the year, the contribution is determined by using the sum of the monthly contribution limits rule.

### **Full Contribution for Last-Month Rule**

The last-month rule allows eligible individuals to make a full contribution for the year even if they were not an eligible individual for the entire year. They can make the full contribution for the year if:

- They are eligible individuals on the first day of last month of their taxable year. For most people this would be December 1, **and**
- They remain eligible individuals during the testing period. The testing period runs (for calendar taxpayers) from December 1 of the current year through December 31 of the following year.

#### example

Chris, age 53, became an eligible individual on December 1, 2011. He has family HDHP coverage on that date. He fully expects to meet the testing period by remaining eligible through December 31, 2012. Under the last-month rule, he can contribute up to \$6,150 for the 2011 tax year.

## Sum of the Monthly Contribution Limits

Under the sum of the monthly contribution limits rule, the maximum contribution is determined monthly based on eligibility and HDHP coverage on the first day of each month. For this purpose, the monthly limit is 1/12 of the annual contribution limit, as calculated on the Limitation Chart and worksheet.

For more information, refer to the Limitation Chart and Worksheet in the instructions for Form 8889.

#### example

Maria, age 48, was an eligible individual with self-only HDHP coverage. She was covered from January through September. She was not an eligible individual for the remaining months of October, November, and December 2011. Her maximum contribution allowed is \$2,287.50 [(\$3,050 x 9) divided by 12].

## Case Study

Erika, age 39, had self-only HDHP coverage on January 1, 2011. She changed to family HDHP coverage on August 1, 2011. Erika lost HDHP coverage as of October 31, 2011. She will use the Line 3 Limitation Chart and Worksheet in Form 8889 Instructions to determine her HSA contribution limit. See Erika's completed Line 3 Limitation Chart and Worksheet on the next page.

### Specific Instructions

**Name and social security number (SSN).** Enter your name(s) as shown on your tax return and the SSN of the HSA beneficiary. If married filing jointly and both you and your spouse have HSAs, complete a separate Form 8889 for each of you.

### Part I—HSA Contributions and Deductions

Use Part I to figure:

- Your HSA deduction,
- Any excess contributions you made (or those made on your behalf), and
- Any excess contributions made by an employer (see *Excess Employer Contributions* beginning on page 5).

### Figuring Your HSA Deduction

The maximum amount that can be contributed to your HSA depends on the type of HDHP coverage you have. If you have self-only coverage, your maximum contribution is \$3,050. If you have family coverage, your maximum contribution is \$6,150.

**Note.** If you are age 55 or older at the end of 2011, you can make an additional contribution of \$1,000.

Your maximum contribution is reduced by any employer contributions to your HSA, any contributions made to your Archer MSA, and any qualified HSA funding distributions.

You can make deductible contributions to your HSA even if your employer made contributions. However, if you (or someone on your behalf) made contributions in addition to any employer contributions and qualified HSA funding distributions, you may have to pay an additional tax. See *Excess Contributions You Make* on page 5.

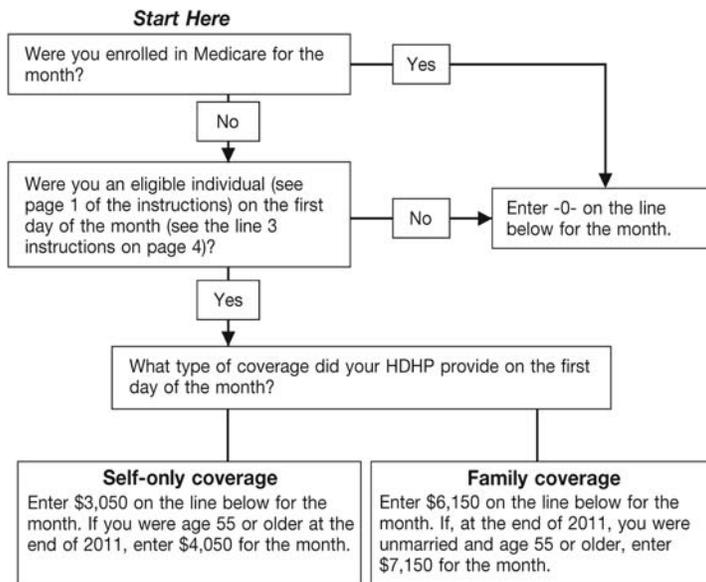
You cannot deduct any contributions for any month in which you were enrolled in Medicare. Also, you cannot deduct contributions if you can be claimed as a dependent on someone else's 2011 tax return.

### Line 3 Limitation Chart and Worksheet

Before you begin: See the instructions for line 3 on page 4.

Go through this chart for each month of 2011.

(Keep for your records)



| Month in 2011  | Amount from chart above |
|--|-------------------------|
| January . . . . .  | \$3,050.00              |
| February . . . . .   | \$3,050.00              |
| March . . . . .  | \$3,050.00              |
| April . . . . .  | \$3,050.00              |
| May . . . . .  | \$3,050.00              |
| June . . . . .   | \$3,050.00              |
| July . . . . .   | \$3,050.00              |
| August . . . . .   | \$6,150.00              |
| September . . . . .  | \$6,150.00              |
| October . . . . .  | \$6,150.00              |
| November . . . . .   | \$0                     |
| December . . . . .   | \$0                     |
| <b>Total for all months . . . . .</b>  | <b>\$39,800.00</b>      |
| <b>Limitation.</b> Divide the total by 12. Enter here and on line 3. . . . . | <b>\$3,316.67</b>       |



## EXERCISES (continued)

**Question 11:** From January through June 2011, Peggy, age 30, participated in her employer's HDHP (with self-only coverage) and made monthly contributions to her HSA. Peggy was laid off in July and remained unemployed and without health insurance for the remainder of 2011. When completing Form 8889, line 3, Peggy will enter \$3,050.  True  False

## HSA Contribution Timeframe

The taxpayers can make contributions to their HSA for 2011 by April 17, 2012. If they were not eligible individuals for the entire year in 2011, they can still make contributions up by April 17, 2012, for the months they were eligible individuals.

Employers can also make 2011 HSA contributions for their employees by April 17, 2012. The employer must notify the taxpayer and the trustee that the HSA contribution is for 2011. The contribution will be reported on the taxpayer's 2011 Form W-2.

## HSA Rollovers or Transfers

### Rollover Contributions

Generally, a rollover is a tax-free distribution to the taxpayer of cash or other assets from one HSA that the taxpayer contributes to another HSA. The contribution to the second HSA is called a rollover contribution. These contributions:

- Are not included in taxpayers' income
- Are not deductible
- Do not reduce taxpayers' contribution limit

Taxpayers can also roll over amounts from Archer MSAs into an HSA. They do not have to be eligible individuals to make a rollover contribution from their existing HSA to a new HSA.



Remember, Archer MSAs are out of scope for VITA/TCE. Refer taxpayers who have issues that involve Archer MSA to a professional tax preparer. The following are also out of scope:

- Qualified HSA funding distributions made from traditional IRAs or Roth IRAs
- Qualified HSA distributions from a health FSA or HRA that is transferred to an HSA

Rollovers are not subject to annual contribution limits and a rollover contribution is not always cash; for example, it could be a Certificate of Deposit (CD). The taxpayer must roll over the amount within 60 days after the date of receipt, and may only make one rollover contribution to an HSA during a one-year period.

See Publication 969 for more information on rollover contributions.

### example

Mary became unemployed in 2011. She was required by her previous employer to move her HSA. She rolled over the amount within 60 days to a new HSA.

**TIP**

If the taxpayers have their HSA funds transferred directly into another HSA in a trustee-to-trustee transfer, this is not considered a rollover. There is no limit on the number of these transfers. Do not include the amount transferred in income, deduct it as a contribution or include it as a distribution on Form 8889, line 14a.

**EXERCISES** (continued)

**Question 12:** Doris moved to a new job. She asked the HSA trustee to transfer her funds into the new HSA. Is this allowable?  Yes  No

## Distributions from an HSA

---

### Distributions for Qualified Medical Expenses

Generally, taxpayers will pay medical expenses during the year without being reimbursed by the HDHP until the plan's annual deductible is reached. When the taxpayer pays these medical expenses that are not reimbursed by the HDHP, the taxpayer can request a distribution from the HSA trustee. The taxpayer can receive tax-free distributions from an HSA to pay or be reimbursed for qualified medical expenses incurred after the taxpayer establishes the HSA.

Qualified medical expenses are expenses that *generally* would qualify for the medical and dental expenses deduction. Examples include unreimbursed expenses for doctors, dentists, and hospitals. See Publication 502, Medical and Dental Expenses, for more information.

Taxpayers must keep records to show that HSA distributions were used to pay or reimburse qualified medical expenses, that these expenses had not been paid or reimbursed from another source, and the medical expense had not been taken as an itemized deduction in any year. For recordkeeping requirements on HSA distributions see Publication 969, Distributions from an HSA. Taxpayers are not required to take annual distributions from their HSA.



Expenses incurred before establishing an HSA are not qualified medical expenses. If a taxpayer is considered to be an eligible individual for the entire year under the last-month rule, only those expenses incurred after actually establishing the HSA are qualified expenses.

#### example

Laura established an HSA in July 2011. She incurred medical expenses in May 2011 and wants to pay those from her HSA. The expenses incurred in May before she established her HSA are not qualified medical expenses for purposes of her HSA.

### Over-the-counter and Prescription Medicines

**NEW** For 2011, over-the-counter medicines or drugs without a prescription, except for insulin, are no longer qualified medical expenses for HSA purposes. For HSA purposes, a medicine or drug will be a qualified medical expense only if the medicine or drug:

- Requires a prescription
- Is available without a prescription (an over-the-counter medicine or drug) and the taxpayer gets a prescription for it, or
- Is insulin



This applies to amounts paid after 2010. However, it does not apply to amounts paid in 2011 for medicines or drugs purchased before January 1, 2011.

example

Vikki purchased \$300 of over-the-counter medicine without a prescription on December 29, 2010. This qualifies as an HSA medical expense, even if she received an HSA distribution for the reimbursement in 2011. If Vikki buys more over-the-counter medicine without a prescription in April 2011, it will not qualify as a medical expense for HSA purposes. The new rules apply to over-the-counter medicines without a prescription, purchased after December 31, 2010.

**TIP**

Preventive services, not reimbursed by the HDHP, can be paid from an HSA.



**EXERCISES** (continued)

**Question 13:** Mariah purchased over-the-counter medicine (without a prescription) in June 2011. Can she request funds from her HSA to pay for this?  Yes  No

**Qualified Insurance Premiums for HSA Purposes**

Qualified insurance premiums for HSA purposes are different than premiums that qualify as a medical expense on Schedule A.

A taxpayer cannot treat insurance premiums as qualified medical expenses **unless** the premiums are for:

- Long-term care insurance based on the following premium limits (also shown in the Instructions for Schedule A, Itemized Deductions)
  - Age 40 or less: \$340
  - More than age 40 but not more than 50: \$640
  - More than age 50 but not more than 60: \$1,270
  - More than age 60 but not more than 70: \$3,390
  - More than age 70: \$4,240
- Health care continuation coverage, such as coverage under COBRA
- Health care coverage while receiving unemployment compensation
- Medicare and other health care coverage if the taxpayer was 65 or older (other than premiums for a Medicare supplemental policy, such as Medigap)



**EXERCISES** (continued)

**Question 14:** Johnnie, who is 49 years old, wants to use funds from her HSA to pay her long-term care insurance premiums. She can use HSA funds to pay a portion of her long-term care insurance premiums.  
 True  False

## Whose medical expenses qualify?

Qualified medical expenses are those incurred by the following persons:

- The taxpayer and spouse
- All dependents claimed on the tax return
- Any other person who could have been claimed as a dependent on the taxpayer's return except that:
  - The person filed a joint return
  - The person had gross income of \$3,700 or more, or
  - The taxpayer or spouse (if filing jointly) could be claimed as a dependent on someone else's 2011 tax return



Taxpayers cannot deduct qualified medical expenses as an itemized deduction on Form 1040, Schedule A, that are equal to the tax-free distribution from their HSAs. Since the medical expenses have been paid from HSA funds, the taxpayers cannot include the same expenses on Schedule A.



A child of parents who are divorced, separated, or living apart for the last six months of the calendar year is treated as the dependent of both parents whether or not the custodial parent releases the claim to the child's exemption.



Even taxpayers who have a self-only HDHP may use the money in their HSA to pay the unreimbursed medical expenses for their spouse or other family members (as described previously).

## Out of Scope HSA Distributions

The following are out of scope for the VITA/TCE program. The information is provided for awareness purposes only. Taxpayers with these issues should be referred to a professional tax preparer.

- Deemed distributions from HSAs:
  - Engaging in prohibited transactions; see Publication 969 for details
  - Using an HSA as security for a loan

Also, a taxpayer cannot claim the health coverage tax credit for premiums paid with a tax-free distribution from an HSA. As stated in the Payments lesson, Form 8885, Health Coverage Tax Credit, is out of scope for the VITA/TCE program.

## Reporting Contributions and Distributions

---

### Form 8889, Health Savings Accounts (HSAs)

A taxpayer must file Form 8889 with Form 1040 if the taxpayer (or spouse if filing a joint return) had any activity in an HSA. This is true even if only the taxpayer's employer or the spouse's employer made contributions to the HSA.

Taxpayers who are filing jointly and who each have separate HSAs will each complete a separate Form 8889. Married taxpayers cannot have a joint HSA.

Ask taxpayers during the interview process if their HDHP coverage is "self-only" or "family," and check the corresponding box on Form 8889, line 1.

### Form 8889, Part I

Form 8889, Part 1, is used to report all HSA contributions and to compute the allowable HSA deduction. This includes contributions made by April 17, 2012, that are designated for 2011. Contributions made by an employer are also shown in Part I, but are not included in the deductible amount.

An HSA may receive contributions from an eligible individual or any other person, including an employer or a family member, on behalf of an eligible individual.



**Tax Software Hint:** The entry of code W and the amount in box 12 of Form W-2 will generate Form 8889 with employer contributions reflected on line 9. After all other entries have been completed on Part I, the HSA deduction will be carried from Form 8889 to line 25 in the Adjusted Gross Income section of Form 1040.

### Form 5498-SA

Form 5498-SA shows the amount contributed during the year for any HSA, Archer MSA, or Medicare Advantage MSA. Generally, contributions made by the taxpayer or someone other than the taxpayer's employer are deductible on the taxpayer's tax return. In addition to being included on Form 5498-SA, employer contributions will also be shown on Form W-2, box 12, with code W. Contributions made by an employer are not included in the income of the taxpayer. Contributions to an employee's account by an employer using the amount of an employee's salary reduction through a cafeteria plan (also known as a "125 plan") are treated as employer contributions. HSA contribution limits are reduced by employer contributions.

Excess contributions will be included in income and are also subject to a 6% excise tax. Excess contributions that are not withdrawn in a timely fashion are out of scope for the VITA/TCE program. Refer taxpayers in this situation to a professional tax preparer.

**TIP**

Form 5498-SA is issued by the HSA Trustee showing the amount of HSA contributions.

**CAUTION**

Taxpayers may not receive Form 5498-SA before April 17, but they should have the information regarding contributions to their HSA.

#### 2011 HSA Contribution Limits

|                                      | Self-Only Coverage | Family Coverage |
|--------------------------------------|--------------------|-----------------|
| Annual Contribution Limit            | \$3,050            | \$6,150         |
| Catch-up Contribution (55 or older)* | \$1,000            | \$1,000         |

\*If a spouse is 55 or older, a second HSA must be established and a second contribution of \$1,000 could be made to that account.



### EXERCISES (continued)

**Question 15:** Audrey has HDHP coverage for herself only. She contributed \$2,000 to her HSA. Her employer also contributed \$1,000 to her HSA. Using Form 8889, what is her HSA deduction?

- A. \$1,000
- B. \$2,000
- C. \$3,000

**Question 16:** Form 8889, Part I, is used to report HSA contributions made by \_\_\_\_\_.

- A. An employer
- B. A taxpayer
- C. A person on behalf of the taxpayer
- D. All of the above

**Question 17:** Employer contributions to an HSA will be included in the taxpayer's HSA deduction on Form 1040, line 25.  True  False

## Form 8889, Part II

Form 1099-SA, Distributions from an HSA, Archer MSA, or Medicare Advantage MSA, reports distributions to a taxpayer. Box 5 will indicate whether the distribution is from an HSA, Archer MSA, or a Medicare Advantage MSA. The code in Form 1099-SA, box 3, identifies the distribution the taxpayer received. Code 1 is a normal distribution. Refer to Form 1099-SA for an explanation of the other codes.

Form 8889, Part II, is used by taxpayers to report distributions from an HSA. Taxpayers receive tax-free distributions from an HSA to pay or be reimbursed for qualified medical expenses. The taxpayer will have to tell you what types of expenses were paid or reimbursed with the distribution.

If distributions are received for reasons other than qualified medical expenses, the amount withdrawn will be included in income and reported on Form 1040, line 21. **NEW** Beginning in 2011, the additional tax for HSA distributions not used for qualified medical expenses increased to 20%. This tax is computed on Form 8889 and reported on Form 1040, line 60.

Taxpayers do not have to make distributions from their HSA each year.



**Tax Software Hint:** Amounts entered on Form 8889 are automatically carried over to the applicable lines of Form 1040. The amount of HSA distributions not used for qualified medical expenses will carry over to line 21. On the line for "Type," enter HSA. If you have more than one item to enter on line 21, see the Volunteer Resource Guide, (Tab 2), How/Where to Enter Income, for guidance.

### Unreimbursed Medical Expenses

If unreimbursed qualified medical expenses were paid with the distribution, the taxpayer does not pay tax on the distribution, but it is reported on Form 8889, Part II, line 14a; the unreimbursed qualified medical expenses are reported on line 15. If the taxpayer does not use the distribution for qualified medical expenses, it must be included in income and the taxpayer must pay tax on the distribution.

HSA distributions included in income (line 16) are subject to an additional 20% tax unless the account beneficiary:

- Dies
- Becomes disabled (see Form 8889 Instructions, page 2)
- Turns age 65



## EXERCISES (continued)

**Question 18:** Vikki incurred \$3,000 of unreimbursed qualified medical expenses. She received a \$2,000 distribution from her HSA to pay for these medical expenses. Using Form 8889, determine Vikki's taxable HSA distribution.

- A. \$0
- B. \$2,000
- C. \$3,000
- D. \$5,000

**Question 19:** Joe paid \$4,000 in unreimbursed qualified medical expenses. He received an HSA distribution of \$4,000. Where is this reported on his tax return?

- A. Form 8889, Part II, line 14a
- B. Form 8889, Part II, line 15
- C. Does not need to be reported
- D. Both A and B

**Question 20:** Assume Joe paid \$3,000 in unreimbursed qualified medical expenses and received an HSA distribution of \$4,000. What amount is reported on Form 8889, Part II, line 15?

- A. \$4,000
- B. \$3,000
- C. \$1,000
- D. \$0

### Form 8889, Part III

There are consequences when a taxpayer fails to maintain HDHP coverage. Form 8889, Part III, Income and Additional Tax for Failure to Maintain HDHP Coverage, is used to figure amounts that must be reported on Form 1040 for failure to be an eligible individual during the testing period for:

- A qualified HSA distribution (see Form 8889 Instructions, page 2)
- Last-month rule (see Form 8889 Instructions, page 1)
- A qualified HSA funding distribution (see Form 8889 Instructions, page 5)

See the discussions on the pages indicated and refer affected taxpayers to a professional tax preparer. This information is provided for your awareness. Form 8889, Part III, is out of scope for the VITA/TCE program.

## Summary

---

Health savings accounts (HSAs) are the newest of all tax-favored medical savings accounts. An HSA is a tax-exempt trust or custodial account that a taxpayer sets up with a qualified HSA trustee to pay for or reimburse certain medical expenses a taxpayer incurs.

### Eligibility

A taxpayer must be an **eligible individual** to qualify for an HSA. See specific qualifications outlined earlier.

A high-deductible health plan (HDHP) is health coverage with:

- A higher annual deductible than typical health plans, and
- A maximum limit on the sum of the annual deductible and out-of-pocket medical expenses that the taxpayer must pay for covered expenses. Out-of-pocket expenses include co-payments and other amounts, but do not include most premiums.

An HSA is created by:

- Enrolling in an HDHP, and
- Establishing the HSA

### Contributions, Distributions, and Form 8889

The amount the taxpayer or any other person can contribute to the taxpayer's HSA depends on the type of HDHP coverage, the taxpayer's age, the date the taxpayer became an eligible individual, and the date the taxpayer is no longer an eligible individual. In addition, the contribution limit for an HSA is reduced by employer contributions.

HSAs enable taxpayers to pay for current medical expenses and save for future qualified medical expenses on a tax-free basis. The following forms are used to report HSA activities:

- Form 5498-SA to report contributions to a taxpayer's HSA. Employer contributions will also be shown in Form W-2, box 12 – may include employee contributions under a Section 125 Cafeteria Plan (pretax dollars).
- Form 1099-SA to report HSA distributions for the year.
- Form 8889, Health Savings Accounts, Part I, to report contributions and calculate the HSA deduction.
- Form 8889, Health Saving Accounts, Part II, to report HSA distributions and report qualified medical expenses. Amounts that are taxable are calculated, and the 20% additional tax is also shown here.
- Form 8889, Health Savings Accounts, Part III, is Income and Additional Tax for Failure to Maintain HDHP Coverage. This part of the form is out of scope. Refer taxpayers with these issues to a professional tax preparer.

Funds in an HSA can remain in the account from year to year until the taxpayer uses them. Interest or other earnings on the assets in the account are tax-free.

Taxpayers can receive tax-free distributions from their HSA to pay or be reimbursed for qualified medical expenses that are incurred after establishing the HSA.

Qualified medical expenses are those expenses that would generally qualify for the medical and dental expense deduction on Schedule A of Form 1040.

There are recordkeeping requirements for HSA distributions. See Publication 969 for additional information.



## EXERCISE ANSWERS

**Answer 1:** Yes. An HSA is portable, so it stays with the taxpayer even if the taxpayer changes employers or leaves the work force.

**Answer 2:** C. With an HSA, distributions for unreimbursed qualified medical expenses are tax-free.

**Answer 3:** B. The minimum annual deductible is \$1,200, and the maximum annual deductible and other out-of-pocket expense is \$5,950.

**Answer 4:** No. To set up and contribute to an HSA, an individual must not be enrolled in Medicare.

**Answer 5:** No. Spouses cannot have a joint HSA. Each spouse who is an eligible individual must open a separate HSA.

**Answer 6:** No. Any person eligible to be claimed as an exemption by another individual does not qualify for an HSA. This is true even if the person is not actually claimed.

**Answer 7:** Yes. Family members or any other person may also contribute on behalf of an eligible individual.

**Answer 8:** C. The annual contribution limit for an eligible individual under age 55 is \$3,050.

**Answer 9:** A. The annual contribution limit for an eligible individual over age 55 is \$4,050.

**Answer 10:** True. The contribution limit is \$7,150 for a married couple when both spouses have family HDHP coverage and one spouse is age 55 or older.

**Answer 11:** False. Peggy was not an eligible person all year, so the Line 3 Limitation Worksheet must be completed to determine the amount to enter on Line 3.

**Answer 12:** Yes. This is allowed because Doris transferred her HSA funds directly into another HSA in a trustee-to-trustee transfer. This is not considered a rollover; there is no limit on the number of these transfers.

**Answer 13:** No. Nonprescription medicines (other than insulin) do not qualify for HSA purposes. See Publication 969 for more information.

**Answer 14:** True. Qualifying long-term care insurance premiums are limited, based on age. A taxpayer cannot treat insurance premiums as qualified medical expenses unless the premiums are for long-term care insurance, health care continuation coverage (such as coverage under COBRA), health care coverage while receiving unemployment compensation, or Medicare and other health care coverage if the taxpayer is 65 or older (other than premiums for a Medicare supplemental policy, such as Medigap). For more information see Publication 969.

**Answer 15:** B. Employer contributions are not deductible.

**Answer 16:** D. Form 8889, Part I, is used to report contributions made by taxpayers, contributions made by any other person on behalf of the taxpayer, and the contributions made by the taxpayer's employer.

**Answer 17:** False. Only contributions made by the taxpayer or by any other person, other than the employer, can be included in the taxpayer's HSA deduction on Form 1040, line 25.

**Answer 18:** A. If the HSA distribution is for qualified medical expenses it is tax-free. If the distribution is more than the amount of qualified expenses, the difference is then taxable income.

**Answer 19:** D. Total distributions are reported on Form 8889, Part II, line 14a, and unreimbursed qualified medical expenses are reported on Form 8889, Part II, line 15.

**Answer 20:** B. The unreimbursed qualified medical expenses of \$3,000 are reported on line 15.



## Health Savings Accounts – Practice Scenarios

---

Three practice scenarios are provided to help you apply what you have learned in the Health Savings Accounts course.

The first scenario does not require you to prepare a tax return. The next two scenarios require you to review the interview notes and taxpayer documents in order to complete the practice exercise. In order to answer the questions, you need to complete Form 1040 through line 37, and the appropriate forms and schedules.

The Practice Lab on Link & Learn Taxes is available for you to complete the returns using tax preparation software. After you answer the questions, you can check your answers, which are listed on the last page of the HSA course.

### Practice Scenario 1 – Lucy Hildago

---

This scenario does not require you to prepare a tax return. Review Form 8889 and use your resource materials and the interview notes to answer the questions below.

#### Interview Notes

- Lucy is a single mother, age 35. Lucy's 2-year-old daughter, Carmen, lives with her.
- Lucy is enrolled in an HDHP with family coverage and had the same coverage for all of 2011. She established an HSA two years ago.
- Lucy put \$1,200 of her own money in the HSA. She also tells you that her grandmother deposited \$3,000 in that account for her during 2011.
- Lucy's Form W-2 shows \$1,020 in box 12 with code W. She has Form 5498-SA showing \$5,220 in box 2.

#### Scenario Questions

- 1-1** Lucy can identify the employer's HSA contribution by the information in box 12 on her Form W-2.
- A. True
  - B. False
- 1-2** What amount will be entered on Form 8889, line 2?
- A. \$1,200
  - B. \$3,000
  - C. \$4,200
  - D. \$5,220
- 1-3** After completing Form 8889, Part I, what is Lucy's HSA deduction?
- A. \$3,000
  - B. \$4,200
  - C. \$5,130
  - D. \$5,220

### Practice Scenario 2 – Andrew Noble

---

Use the taxpayer documents and interview notes to complete this practice exercise. Complete Form 1040 through line 37, and the appropriate forms and schedules, to answer the questions.

For practice using the tax preparation software, complete this scenario using the Practice Lab on Link & Learn Taxes.

**Intake/Interview & Quality Review Sheet**

**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |  |                                     |                           |  |  |   |
|--|--|-------------------------------------|---------------------------|--|--|---|
| 1. Your First Name<br><b>ANDREW</b>  |  | M. I.<br><b>T</b>                   | Last Name<br><b>NOBLE</b> |  | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |   |
| 2. Spouse's First Name   |  | M. I.                               | Last Name                 |  | Is spouse a U.S. Citizen?<br><input type="checkbox"/> Yes <input type="checkbox"/> No          |   |
| 3. Mailing Address<br><b>1244 E STATE STREET</b>   |  |                                     | Apt#                      | City<br><b>YOUR CITY</b>   | State<br><b>YS</b>   | Zip Code<br><b>YOUR ZIP CODE</b>  |
| 4. Contact Information<br>Phone: <b>502-555-XXXX</b> Cell Phone: E-mail:   |  |                                     |                           |  |  |   |
| 5. Your Date of Birth<br><b>03/03/1951</b>   |  | 6. Your Job Title<br><b>MANAGER</b> |                           | 7. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |  | 8. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 9. Spouse's Date of Birth  |  | 10. Spouse's Job Title              |                           | 11. Legally Blind <input type="checkbox"/> Yes <input type="checkbox"/> No           |  | 12. Totally and Permanently Disabled <input type="checkbox"/> Yes <input type="checkbox"/> No           |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |  |                                     |                           |  |  |   |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

- | <b>Yes</b>                          | <b>No</b>                           | <b>Unsure</b>            |   |
|-------------------------------------|-------------------------------------|--------------------------|---|
| <input checked="" type="checkbox"/> | <input type="checkbox"/>            | <input type="checkbox"/> | 1. Wages or Salary? (Form W-2)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 2. Tip Income?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 3. Scholarships? (Forms W-2, 1098-T)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)        |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 5. Refund of state/local income taxes? (Form 1099-G)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 6. Alimony Income?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)              |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B) |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)             |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 11. Unemployment Compensation? (Form 1099-G)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)                                 |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 13. Income (or loss) from Rental Property?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: _____ (Forms W-2 G, 1099-MISC)  |

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

- | <b>Yes</b>                          | <b>No</b>                           | <b>Unsure</b>            |   |
|-------------------------------------|-------------------------------------|--------------------------|---|
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 1. Alimony: If yes, do you have the recipient's SSN? <input type="checkbox"/> Yes <input type="checkbox"/> No   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 2. Contributions to a retirement account? <input type="checkbox"/> IRA <input type="checkbox"/> Roth IRA <input type="checkbox"/> 401K <input type="checkbox"/> Other |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?   |
| <input checked="" type="checkbox"/> | <input type="checkbox"/>            | <input type="checkbox"/> | 5. Medical expenses (including health insurance premiums)?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 6. Home mortgage interest? (Form 1098)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 8. Charitable contributions?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 9. Child/dependent care expenses, such as day-care?   |

**Part V. Life Events – In 2011 Did you (or your spouse):**

- | <b>Yes</b>                          | <b>No</b>                           | <b>Unsure</b>            |   |
|-------------------------------------|-------------------------------------|--------------------------|---|
| <input checked="" type="checkbox"/> | <input type="checkbox"/>            | <input type="checkbox"/> | 1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C) |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 3. Buy, sell or have a foreclosure of your home? (Form 1099-A)                                      |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? _____    |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 6. Live in an area that was affected by a natural disaster? If yes, where? _____                    |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 7. Receive the First Time Homebuyers Credit in 2008?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 8. Pay any student loan interest? (Form 1098-E)   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? _____  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 10. Attend school as a full time student? (Form 1098-T)   |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 11. Adopt a child?  |
| <input type="checkbox"/>            | <input checked="" type="checkbox"/> | <input type="checkbox"/> | 12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?   |

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. xx-xxxx)

2



CORRECTED (if checked)

|   |  |   |  |   |
|---|--|---|--|---|
| TRUSTEE'S name, street address, city, state, and ZIP code<br><b>STATE BANK<br/>123 MAIN ST<br/>YOUR CITY, STATE ZIP</b> |  | 1 Employee or self-employed person's Archer MSA contributions made in 2011 and 2012 for 2011<br>\$<br><b>\$ 3,500.00</b>                        | OMB No. 1545-1518<br><b>2011</b><br>Form <b>5498-SA</b>                  | <b>HSA, Archer MSA, or Medicare Advantage MSA Information</b> |
| TRUSTEE'S federal identification number<br><b>56-4XXXXXX</b>  | PARTICIPANT'S social security number<br><b>560-XX-XXXX</b> | 3 Total HSA or Archer MSA contributions made in 2012 for 2011<br><b>\$ 0.00</b>   | 5 Fair market value of HSA, Archer MSA, or MA MSA<br><b>\$ 14,650.00</b> |   |
| PARTICIPANT'S name<br><b>ANDREW T. NOBLE<br/>1244 E STATE ST.<br/>YOUR CITY, STATE ZIP</b>                              |  | 4 Rollover contributions<br>\$  |  |   |
| Account number (see instructions)   |  | 6 HSA <input checked="" type="checkbox"/><br>Archer MSA <input type="checkbox"/><br>MA <input type="checkbox"/><br>MSA <input type="checkbox"/> |  |   |

**Copy B  
For  
Participant**

The information in boxes 1 through 6 is being furnished to the Internal Revenue Service.

Form **5498-SA**

(keep for your records)

Department of the Treasury - Internal Revenue Service

|  |                            |  |                     |   |                     |   |  |
|--|----------------------------|--|---------------------|---|---------------------|---|--|
| a Employee's social security number<br><b>560-XX-XXXX</b>  |                            | OMB No. 1545-0008  |                     | Safe, accurate, FAST! Use  |                     | Visit the IRS website at <a href="http://www.irs.gov/efile">www.irs.gov/efile</a> |  |
| b Employer identification number (EIN)<br><b>56-2XXXXXX</b>  |                            | 1 Wages, tips, other compensation<br><b>28,625.00</b>  |                     | 2 Federal income tax withheld<br><b>2,175.00</b>  |                     |   |  |
| c Employer's name, address, and ZIP code<br><b>PORTER INDUSTRIES<br/>123 CENTRAL AVE<br/>LOUISVILLE, KY 40202</b>          |                            | 3 Social security wages<br><b>28,625.00</b>  |                     | 4 Social security tax withheld<br><b>1,202.25</b>   |                     |   |  |
|  |                            | 5 Medicare wages and tips<br><b>28,625.00</b>  |                     | 6 Medicare tax withheld<br><b>415.06</b>  |                     |   |  |
|  |                            | 7 Social security tips   |                     | 8 Allocated tips  |                     |   |  |
| d Control number   |                            | 9  |                     | 10 Dependent care benefits  |                     |   |  |
| e Employee's first name and initial Last name Suff.<br><b>ANDREW T. NOBLE<br/>1244 E STATE ST<br/>YOUR CITY, STATE ZIP</b> |                            | 11 Nonqualified plans  |                     | 12a See instructions for box 12   |                     |   |  |
|  |                            | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |                     | 12b   |                     |   |  |
|  |                            | 14 Other   |                     | 12c   |                     |   |  |
|  |                            |  |                     | 12d   |                     |   |  |
| f Employee's address and ZIP code  |                            |  |                     |   |                     |   |  |
| 15 State   | Employer's state ID number | 16 State wages, tips, etc.   | 17 State income tax | 18 Local wages, tips, etc.  | 19 Local income tax | 20 Locality name  |  |
| <b>KY</b>  | <b>53-0XXXXXX</b>          | <b>28,625.00</b>   | <b>1,025.00</b>     |   |                     |   |  |

Form **W-2 Wage and Tax Statement**

**2011**

Department of the Treasury—Internal Revenue Service

**Copy B—To Be Filed With Employee's FEDERAL Tax Return.**  
This information is being furnished to the Internal Revenue Service.

## Interview Notes:

- Andrew is 60 years old.
- Andrew was not on Medicare at any time in 2011.
- Andrew was enrolled the entire year of 2011 in an HDHP with self-only coverage.
- During 2011, Andrew contributed \$3,500 to his HSA.
- Andrew took a distribution from his HSA to pay the following unreimbursed expenses:
  - Urgent care bill: \$375
  - Hospital bill: \$1,200
  - Prescription medicine: \$578
  - Dental bills for routine exams: \$168
  - Nonprescription medication: \$79

## Scenario Questions

- 2-1** What is the amount of Andrew's HSA deduction on Form 1040, line 25?
- A. \$3,050
  - B. \$3,500
  - C. \$4,050
  - D. \$6,150
- 2-2** Did Andrew make an excess contribution to his HSA?
- A. Yes. The contribution is over the \$3,050 limit for self-only HDHP coverage.
  - B. No. Andrew can make catch up contributions because he is 55 or older.
- 2-3** Is the urgent care bill a qualified medical expense for HSA purposes?
- A. Yes
  - B. No
- 2-4** What is the total unreimbursed qualified medical expenses reported on Form 8889, Part II, line 15?
- A. \$1,946
  - B. \$2,025
  - C. \$2,321
  - D. \$2,400

## Practice Scenario 3 – James and Diana Calhoun

---

Use the taxpayer documents and interview notes to complete this practice exercise. Complete Form 1040 through line 37, and the appropriate forms and schedules, to answer the questions.

For practice using the tax preparation software, complete this scenario using the Practice Lab on Link & Learn Taxes.

**Intake/Interview & Quality Review Sheet**

**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |  |  |  |   |
|--|--|--|--|---|
| 1. Your First Name<br><b>JAMES</b>   | M. I.<br><b>P</b>                      | Last Name<br><b>CALHOUN</b>  | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No   |   |
| 2. Spouse's First Name<br><b>DIANA</b>   | M. I.<br><b>G</b>                      | Last Name<br><b>CALHOUN</b>  | Is spouse a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |   |
| 3. Mailing Address<br><b>1679 ROBERTS ST</b>   |  | Apt#   | City<br><b>YOUR CITY</b>   | State<br><b>YS</b> Zip Code<br><b>YOUR ZIP CODE</b>                                   |
| 4. Contact Information<br>Phone: Cell Phone: E-mail:   |  |  |  |   |
| 5. Your Date of Birth<br><b>06/04/1964</b>   | 6. Your Job Title<br><b>ACCOUNTANT</b> | Are you:   |  | 7. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No  |
|  |  | 8. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No  |  |   |
| 9. Spouse's Date of Birth<br><b>12/04/1963</b>   | 10. Spouse's Job Title<br><b>NURSE</b> | Is Spouse:   |  | 11. Legally Blind <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
|  |  | 12. Totally and Permanently Disabled <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |  |   |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |  |  |  |   |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?
- Single
- Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No
- Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_
- Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: \_\_\_\_\_ (Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



|  |  |  |                            |   |                  |
|--|--|--|----------------------------|---|------------------|
| a Employee's social security number<br><b>520-XX-XXXX</b>  |  | Safe, accurate,<br>FAST! Use                          |                            | Visit the IRS website at<br>www.irs.gov/efile     |                  |
| b Employer identification number (EIN)<br><b>53-0XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>27,418.00</b>  |                            | 2 Federal income tax withheld<br><b>2,175.00</b>  |                  |
| c Employer's name, address, and ZIP code<br><b>PATTERSON FOODS INC<br/>1106 WILSON WAY<br/>INDIANAPOLIS, IN 46205</b>            |  | 3 Social security wages<br><b>27,418.00</b>  |                            | 4 Social security tax withheld<br><b>1,152.00</b> |                  |
|  |  | 5 Medicare wages and tips<br><b>27,418.00</b>  |                            | 6 Medicare tax withheld<br><b>398.00</b>          |                  |
|  |  | 7 Social security tips   |                            | 8 Allocated tips                                  |                  |
| d Control number   |  | 9  |                            | 10 Dependent care benefits                        |                  |
| e Employee's first name and initial Last name Suff.<br><br><b>JAMES P. CALHOUN<br/>1679 ROBERTS ST<br/>YOUR CITY, STATE, ZIP</b> |  | 11 Nonqualified plans  |                            | 12a See instructions for box 12                   |                  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |                            | 12b   |                  |
|  |  | 14 Other   |                            | 12c   |                  |
|  |  |  |                            | 12d   |                  |
| f Employee's address and ZIP code  |  |  |                            |   |                  |
| 15 State Employer's state ID number<br><b>IN 53-0XXXXXX</b>  | 16 State wages, tips, etc.<br><b>27,418.00</b> | 17 State income tax<br><b>1,025.00</b>   | 18 Local wages, tips, etc. | 19 Local income tax                               | 20 Locality name |

Form **W-2** Wage and Tax Statement

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

|  |  |  |                            |  |                  |
|--|--|--|----------------------------|--|------------------|
| a Employee's social security number<br><b>521-XX-XXXX</b>  |  | Safe, accurate,<br>FAST! Use                        |                            | Visit the IRS website at<br>www.irs.gov/efile        |                  |
| b Employer identification number (EIN)<br><b>53-1XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>15,327.54</b>  |                            | 2 Federal income tax withheld<br><b>1,033.57</b>     |                  |
| c Employer's name, address, and ZIP code<br><b>HARRIMAN EMERGENCY CLINIC<br/>1250 OHIO BLVD<br/>INDIANAPOLIS, IN 46205</b>       |  | 3 Social security wages<br><b>15,327.54</b>  |                            | 4 Social security tax withheld<br><b>643.76</b>      |                  |
|  |  | 5 Medicare wages and tips<br><b>15,327.54</b>  |                            | 6 Medicare tax withheld<br><b>222.25</b>             |                  |
|  |  | 7 Social security tips   |                            | 8 Allocated tips                                     |                  |
| d Control number   |  | 9  |                            | 10 Dependent care benefits                           |                  |
| e Employee's first name and initial Last name Suff.<br><br><b>DIANA G. CALHOUN<br/>1679 ROBERTS ST<br/>YOUR CITY, STATE, ZIP</b> |  | 11 Nonqualified plans  |                            | 12a See instructions for box 12<br><b>W 1,000.00</b> |                  |
|  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> |                            | 12b  |                  |
|  |  | 14 Other   |                            | 12c  |                  |
|  |  |  |                            | 12d  |                  |
| f Employee's address and ZIP code  |  |  |                            |  |                  |
| 15 State Employer's state ID number<br><b>IN 53-1XXXXXX</b>  | 16 State wages, tips, etc.<br><b>15,327.54</b> | 17 State income tax<br><b>89.06</b>  | 18 Local wages, tips, etc. | 19 Local income tax                                  | 20 Locality name |

Form **W-2** Wage and Tax Statement

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|  |  |  |   |   |
|--|--|--|---|---|
| TRUSTEE'S name, street address, city, state, and ZIP code<br><b>USA TRUST BANK<br/>123 MAIN ST<br/>YOUR CITY, STATE, ZIP</b> |  | 1 Employee or self-employed person's Archer MSA contributions made in 2011 and 2012 for 2011<br>\$<br><b>\$ 3,000.00</b> | OMB No. 1545-1518<br><b>2011</b><br>Form <b>5498-SA</b> | <b>HSA, Archer MSA, or Medicare Advantage MSA Information</b> |
| TRUSTEE'S federal identification number<br><b>53-2XXXXXX</b>   | PARTICIPANT'S social security number<br><b>521-XX-XXXX</b> | 3 Total HSA or Archer MSA contributions made in 2012 for 2011<br>\$ <b>0.00</b>  | <b>Copy B<br/>For Participant</b>                       |   |
| PARTICIPANT'S name<br><b>DIANA CALHOUN<br/>1679 ROBERTS ST<br/>YOUR CITY, STATE, ZIP</b>                                     |  | 4 Rollover contributions<br>\$   |   |   |
| Account number (see instructions)  |  | 6 HSA <input checked="" type="checkbox"/><br>Archer MSA <input type="checkbox"/><br>MA MSA <input type="checkbox"/>      |   |   |

The information in boxes 1 through 6 is being furnished to the Internal Revenue Service.

Form **5498-SA**

(keep for your records)

Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

|   |   |   |   |   |                                 |
|---|---|---|---|---|---------------------------------|
| TRUSTEE'S/PAYER'S name, street address, city, state, and ZIP code<br><b>JACKSON BANK &amp; TRUST<br/>14907 S.W. GRAND ST<br/>INDIANAPOLIS, IN 46205</b>                   |   |   | OMB No. 1545-1517<br><b>2011</b><br>Form <b>1099-SA</b> | <b>Distributions From an HSA, Archer MSA, or Medicare Advantage MSA</b> |                                 |
| PAYER'S federal identification number<br><b>54-2XXXXXX</b>  | RECIPIENT'S identification number<br><b>521-XX-XXXX</b> | 1 Gross distribution<br>\$ <b>1,900.00</b>  | 2 Earnings on excess cont.<br>\$                        |   | <b>Copy B<br/>For Recipient</b> |
| RECIPIENT'S name<br><b>DIANA G. CALHOUN</b><br>Street address (including apt. no.)<br><b>1679 ROBERTS ST</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE, ZIP</b> |   | 3 Distribution code<br><b>1</b>   | 4 FMV on date of death<br>\$                            |   |                                 |
| Account number (see instructions)   |   | 5 HSA <input checked="" type="checkbox"/><br>Archer MSA <input type="checkbox"/><br>MA MSA <input type="checkbox"/> |   |   |                                 |

This information is being furnished to the Internal Revenue Service.

Form **1099-SA**

(keep for your records)

Department of the Treasury - Internal Revenue Service

## Interview Notes

- James and Diana want to file a joint tax return.
- James works as an accountant and Diana is a nurse. They have no children.
- Diana Calhoun is enrolled in an HDHP with family coverage. She has an HSA through her employer. As part of her benefit program, the employer contributed \$1,000 to her HSA during 2011. In addition, Diana made a contribution of \$2,000.
- Diana received a distribution from her HSA of \$1,900.
- James and Diana did not itemize last year and do not plan to itemize this year.
- Diana checked the unsure box on Part III, question 14 on the intake and interview sheet, since she is not sure she has to include the HSA distribution in her income.
- Medical bills for James:
  - Over-the-counter medication (no prescription): \$400
  - Unreimbursed doctor bills: \$300
  - Unreimbursed expense for eyeglasses (needed for medical reasons): \$425
  - Unreimbursed prescription drugs: \$657
- Medical bills for Diana:
  - HDHP insurance premium: \$1,500
  - Unreimbursed doctor bills: \$195
  - Unreimbursed prescription drugs: \$128
  - Unreimbursed lab work (routine blood tests): \$250

## Scenario Questions

- 3-1** The HSA deduction on the Calhouns' tax return (Form 1040, line 25) is:
- A. \$0
  - B. \$1,000
  - C. \$2,000
  - D. \$3,000
- 3-2** What is the Calhouns' Adjusted Gross Income as shown on Form 1040?
- A. \$39,746
  - B. \$40,746
  - C. \$42,746
  - D. \$44,646
- 3-3** What is the total of unreimbursed qualified medical expenses on Form 8889, Part II, line 15?
- A. \$1,955
  - B. \$2,355
  - C. \$3,455
  - D. \$3,855
- 3-4** Did the Calhouns receive distributions in excess of their unreimbursed, qualified medical expenses?
- A. Yes
  - B. No

## Answers to Practice Scenarios

1-1: A

1-2: C

1-3: B

2-1: B

2-2: B

2-3: A

2-4: C

3-1: C

3-2: B

3-3: A

3-4: B



# Health Savings Accounts – Test Questions

## Test Answer Sheet

Name \_\_\_\_\_

Instructions: Volunteers with an Intermediate certification or higher may proceed to a certification for Health Savings Accounts (HSA). HSA is an optional specialty training and certification test available on Link & Learn Taxes. Volunteers must achieve a minimum of 80% to be certified.

**CAUTION: The Test scenarios are provided electronically in a PDF format for information purposes only. The questions on the online test may be either from the test or retest. Students should read each question on the online test very carefully before answering.**

### Privacy Act Notice

The Privacy Act of 1974 requires that when we ask for information we tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if we do not receive it, and whether your response is voluntary, required to obtain a benefit, or mandatory.

Our legal right to ask for information is 5 U.S.C. 301.

We are asking for this information to assist us in contacting you relative to your interest and/or participation in the IRS volunteer income tax preparation and outreach programs. The information you provide may be furnished to others who coordinate activities and staffing at volunteer return preparation sites or outreach activities. The information may also be used to establish effective controls, send correspondence and recognize volunteers.

Your response is voluntary. However, if you do not provide the requested information, the IRS may not be able to use your assistance in these programs.

Question                      Answer

### HSA Scenario 1

|    |  |
|----|--|
| 1. |  |
| 2. |  |
| 3. |  |

### HSA Scenario 2

|    |  |
|----|--|
| 4. |  |
| 5. |  |

### HSA Scenario 3

|    |  |
|----|--|
| 6. |  |
| 7. |  |
| 8. |  |

### HSA Scenario 4

|     |  |
|-----|--|
| 9.  |  |
| 10. |  |
| 11. |  |

### HSA Scenario 5

|     |  |
|-----|--|
| 12. |  |
| 13. |  |
| 14. |  |
| 15. |  |

Total Answers Correct: \_\_\_\_\_

Total Questions:                      15

**Passing Score:                      12 of 15**

## Directions

The first four scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

## HSA Scenario 1: Jason Grant

---

### Interview Notes

- Jason Grant is single and 46 years old.
- Jason works as an office manager and his Form W-2 shows wages of \$48,000.
- Jason participated in his employer's self-only coverage High Deductible Health Plan (HDHP) all year.
- Jason does not have any other health coverage.
- Jason has had an HSA for three years.
- Jason's employer contributed \$1,000 in 2011 to his HSA.
- In 2011, Jason contributed \$1,500 to his HSA.
- Jason is a U.S. citizen and has a valid social security number.

## HSA Scenario 1: Test Questions

---

1. Jason is an eligible individual for HSA purposes because:
  - a. He cannot be claimed as a dependent on someone else's return.
  - b. He has an HDHP and is not on Medicare.
  - c. He does not have any other health coverage.
  - d. All the above.
2. How much can Jason take as an HSA deduction on Form 1040?
  - a. \$0
  - b. \$1,000
  - c. \$1,500
  - d. \$2,500
3. As a volunteer, where would you find the employer contributions made to Jason's HSA?
  - a. Form 1099-SA
  - b. Form W-2, box 12, code W
  - c. Form 1099-MISC, box 3
  - d. No form is required; the employee needs to keep records

## HSA Scenario 2: Sidney and Mary Allen

---

### Interview Notes

- Sidney and Mary Allen are married and will file a joint return.
- Sidney is 60 years old, and Mary is 53 years old.
- Both were enrolled in self-only coverage High Deductible Health Plans (HDHPs) through their employers for the entire year of 2011.
- Sidney and Mary each have an HSA.
- Both have contributed the maximum amounts to their HSAs in 2011.
- Sidney and Mary are both U.S. citizens and have valid social security numbers.

### HSA Scenario 2: Test Questions

---

4. What is the maximum amount of contributions to their HSAs?
  - a. Sidney – \$3,050; Mary – \$3,050
  - b. Sidney – \$4,050; Mary – \$3,050
  - c. \$6,150
  - d. \$11,900
5. Sidney and Mary will each need to complete a separate Form 8889 when filing their joint return.
  - a. True
  - b. False

## HSA Scenario 3: Penny Cook

---

### Interview Notes

- Penny Cook is 35 years old.
- Penny is single and has no dependents.
- In 2011, she had earnings from her job of \$43,000.
- Penny has participated in her employer's self-only HDHP coverage all year.
- Penny has had an HSA for the past three years, including all of 2011.
- Penny contributed the maximum amount allowed to her HSA in 2011.
- In 2011, Penny took funds from her HSA to pay the following expenses:
  - Eyeglasses (needed for medical reasons)—\$250
  - Over-the-counter medication for a skin condition (no prescription from a doctor)—\$120
  - Co-payments for doctor office visits—\$80
  - Dental checkup—\$75
  - Swimming lessons—\$112
- Penny is a U.S. citizen and has a valid social security number.

### HSA Scenario 3: Test Questions

---

6. What is the amount of Penny's HSA contribution reported on Form 8889, line 2?
  - a. \$3,000
  - b. \$3,050
  - c. \$5,950
  - d. \$6,150
  
7. What is the amount of **total** distributions reported on Form 8889, line 14a?
  - a. \$515
  - b. \$525
  - c. \$562
  - d. \$637
  
8. What is the amount of unreimbursed qualified medical expenses reported on Form 8889, line 15?
  - a. \$405
  - b. \$517
  - c. \$525
  - d. \$637

## HSA Scenario 4: Charles and Hazel Rowan

---

### Interview Notes

- Charles, age 42, and Hazel, age 40, are married and will file a joint return.
- They have two children, Jessica and Robert, whom they will claim as dependents on their joint return.
- Hazel's cousin, George (age 30), came to live with them in August 2011. George's gross income was \$4,000. Hazel and Charles did not provide over one-half of George's support for the year but did pay \$500 of George's medical bills in October 2011.
- Charles was enrolled all of 2011 in an HDHP with family coverage.
- Charles has had an HSA for five years.
- In 2011, Charles made regular contributions to his HSA totaling \$2,500.
- In 2011, Charles took funds from his HSA to pay numerous medical expenses including:
  - \$100 for over-the-counter allergy medicine for their daughter, Jessica (no prescription from doctor)
  - \$200 in co-payments for office visits to the pediatrician for Jessica and Robert
  - \$150 to purchase Hazel's contact lenses (needed for medical reasons)
  - \$1,000 for long-term care insurance for Charles
- Charles, Hazel, Jessica, Robert, and cousin George are all U.S. citizens and have valid social security numbers.

### HSA Scenario 4: Test Questions

---

9. The amount of Charles' HSA deduction on Form 1040 is:
  - a. \$1,500
  - b. \$2,500
  - c. \$3,050
  - d. \$6,150
10. For HSA purposes, Charles can include qualified medical expenses for which of the following people?
  - a. Charles and Hazel
  - b. Jessica and Robert
  - c. Charles, Hazel, Jessica, and Robert
  - d. Charles, Hazel, Jessica, Robert, and George

11. On his 2011 Form 8889, Charles can include the \$100 paid for Jessica's nonprescription allergy medicine as a qualifying medical expense for HSA purposes.
- a. True
  - b. False

## HSA Scenario 5: Thomas Franklin

---

### Taxpayer Documents

- Social security cards for Thomas Franklin and James Franklin
- Completed intake and interview sheet
- Form W-2 for Thomas Franklin
- Form 1099-SA, Distributions from an HSA, Archer MSA, or Medicare Advantage MSA

### Interview Notes

- Thomas Franklin, age 44, is a single parent raising his 17-year-old son, James.
- Thomas qualifies to file as Head of Household.
- For the last three years, Thomas has had family health coverage through a High Deductible Health Plan (HDHP) from his employer.
- Thomas has had an HSA for several years.
- In 2011, he contributed \$2,000 to his HSA.
- Thomas' mother helped him out and contributed \$3,000 to his HSA in 2011.
- Thomas' employer also contributed \$500 to his HSA in 2011.
- Thomas paid the following expenses in 2011 using money from his HSA:
  - \$575 for doctor visits for Thomas
  - \$250 for prescription medicine for Thomas
  - \$300 for doctor visits for James
  - \$100 for toiletries for the family



**Intake/Interview & Quality Review Sheet**

**Section A. You should complete Pages 1-3**

Thank you for allowing us to prepare your tax return. You are responsible for the information on your return so please provide complete and accurate information to the certified tax preparer. If you have any questions please ask your preparer.

**You will need your:**

- Tax information such as Forms W-2, 1099, 1098.
- Social security cards or ITIN letters for you and all persons on your tax return.
- Proof of Identity (such as a valid drivers license or other government issued picture ID).

**Part I. Your Personal Information**

|  |                                     |                                      |  |   |
|--|-------------------------------------|--------------------------------------|--|---|
| 1. Your First Name<br><b>THOMAS</b>  | M. I.<br><b>B</b>                   | Last Name<br><b>FRANKLIN</b>         | Are you a U.S. Citizen?<br><input checked="" type="checkbox"/> Yes <input type="checkbox"/> No |   |
| 2. Spouse's First Name   | M. I.                               | Last Name                            | Is spouse a U.S. Citizen?<br><input type="checkbox"/> Yes <input type="checkbox"/> No          |   |
| 3. Mailing Address<br><b>65421 SW 17TH ST</b>  | Apt#                                | City<br><b>YOUR CITY</b>             | State<br><b>YS</b>   | Zip Code<br><b>YOUR ZIP</b>   |
| 4. Contact Information<br>Phone: <b>YOUR PHONE #</b> Cell Phone: E-mail: <b>NONE</b>   |                                     |                                      |  |   |
| 5. Your Date of Birth<br><b>05/20/1967</b>   | 6. Your Job Title<br><b>MANAGER</b> | Are you:                             | 7. Legally Blind   | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
|  |                                     | 8. Totally and Permanently Disabled  |  | <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No |
| 9. Spouse's Date of Birth  | 10. Spouse's Job Title              | Is Spouse:                           | 11. Legally Blind  | <input type="checkbox"/> Yes <input type="checkbox"/> No            |
|  |                                     | 12. Totally and Permanently Disabled |  | <input type="checkbox"/> Yes <input type="checkbox"/> No            |
| 13. Can anyone claim you or your spouse on their tax return? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Unsure |                                     |                                      |  |   |

**Part II. Marital Status and Household Information**

1. As of December 31, 2011, were you?

Single

Married: Did you live with your spouse during any part of the last six months of 2011?  Yes  No

Divorced or Legally Separated: Date of final decree or separate maintenance agreement: \_\_\_\_\_

Widowed: Year of spouse's death: \_\_\_\_\_

2. List names below of everyone who lived in your home in 2011 (other than you or spouse). Also list anyone who lived outside of your home that you supported during 2011. If additional space is needed please check here  and list on page 3.

| Name (first, last)<br>Do not enter your name or spouse's name below. | Date of Birth<br>(mm/dd/yy) | Relationship to you<br>(e.g. daughter, son, mother, sister, none) | Number of months lived in your home in 2011 | US Citizen or resident of the US, Canada or Mexico in 2011 (yes/no) | Marital Status as of 12/31/11 (S/M) | Full-time student in 2011 (yes/no) | Received less than \$3700 income in 2011 (yes/no) |
|--|-----------------------------|---|---|---|-------------------------------------|------------------------------------|---|
| (a)  | (b)                         | (c)   | (d)   | (e)   | (f)                                 | (g)                                | (h)   |
| <b>JAMES FRANKLIN</b>  | <b>1/18/1994</b>            | <b>SON</b>  | <b>12</b>                                   | <b>YES</b>  | <b>S</b>                            | <b>YES</b>                         | <b>YES</b>  |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |
|  |                             |   |   |   |                                     |                                    |   |

- Volunteers assisting with preparing your return are trained to provide high quality service and uphold the highest ethical standards.
- To report unethical behavior to IRS, email us at [wi.voltax@irs.gov](mailto:wi.voltax@irs.gov) or call toll free 1-877-330-1205.

To check the status of your REFUND visit "Where's My Refund?" on [www.irs.gov](http://www.irs.gov) or call 1-800-829-1954 for assistance.

**Section A. Please complete – check Yes, No or Unsure to all questions below. Please ask if you need help.**

**Part III. Income – In 2011, did you (or your spouse) receive:**

**Yes No Unsure**

1. Wages or Salary? (Form W-2)
2. Tip Income?
3. Scholarships? (Forms W-2, 1098-T)
4. Interest/Dividends from: checking/savings accounts, bonds, CDs, brokerage? (Forms 1099-INT, 1099-DIV)
5. Refund of state/local income taxes? (Form 1099-G)
6. Alimony Income?
7. Self-Employment payments (such as cash received for services, small business)? (Form 1099-MISC)
8. Income (or loss) from the sale of Stocks, Bonds or Real Estate (including your home)? (Forms 1099-S, 1099-B)
9. Disability Income (such as payments from insurance or workers compensation)? (Forms 1099-R, W-2)
10. Distributions from Pensions, Annuities, and/or IRA? (Form 1099-R)
11. Unemployment Compensation? (Form 1099-G)
12. Social Security or Railroad Retirement Benefits? (Forms SSA-1099, RRB-1099)
13. Income (or loss) from Rental Property?
14. Other Income: (gambling, lottery, prizes, awards, jury duty, etc.) Specify: HSA DISTRIBUTION  
(Forms W-2 G, 1099-MISC)

**Part IV. Expenses – In 2011 Did you (or your spouse) pay:**

**Yes No Unsure**

1. Alimony: If yes, do you have the recipient's SSN?  Yes  No
2. Contributions to a retirement account?  IRA  Roth IRA  401K  Other
3. Educational expenses paid for yourself, spouse or dependents, such as tuitions, books, fees, etc.? (Form 1098-T)
4. Unreimbursed employee business expenses (such as teacher supplies, uniforms or mileage)?
5. Medical expenses (including health insurance premiums)?
6. Home mortgage interest? (Form 1098)
7. Real estate taxes for your home or personal property taxes for your vehicle? (Form 1098)
8. Charitable contributions?
9. Child/dependent care expenses, such as day-care?

**Part V. Life Events – In 2011 Did you (or your spouse):**

**Yes No Unsure**

1. Have a Health Savings Account? (Forms 5498-SA, 1099-SA)
2. Have debt from a mortgage or credit card canceled/forgiven by a commercial lender? (Form 1099-C)
3. Buy, sell or have a foreclosure of your home? (Form 1099-A)
4. Have Earned Income Credit (EIC) disallowed in a prior year? If yes, for which tax year? \_\_\_\_\_
5. Purchase and install energy efficient home items (such as windows, furnace, insulation, etc.)?
6. Live in an area that was affected by a natural disaster? If yes, where? \_\_\_\_\_
7. Receive the First Time Homebuyers Credit in 2008?
8. Pay any student loan interest? (Form 1098-E)
9. Make estimated tax payments or apply last year's refund to your 2011 tax? If so how much? \_\_\_\_\_
10. Attend school as a full time student? (Form 1098-T)
11. Adopt a child?
12. File a 2010 federal tax return containing a "capital loss carryover" on Form 1040 Schedule D?

**Presidential Election Campaign Fund:** (If you check a box, your tax or refund will not change.)

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund  You  Spouse

Catalog Number 52121E

Form **13614-C** (Rev. XX-XXXX)

2



**Section B. For Certified Volunteer Preparer Completion**

**Remember:** You are the link between the taxpayer's information and a correct tax return. Verify the taxpayer's information on pages 1, 2 & 3 is complete. All questions must be discussed with the taxpayer and all "Unsure" responses should be changed to "Yes" or "No".

**Must be completed by Certified Volunteer only if persons are listed in Part II Question 2**

Check if persons are listed in Part II Question 2

- Yes  No 1. Can anyone else claim any of the persons listed in Part II, Question 2, as a dependent on their return? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 2. Were any of the persons listed in Part II, Question 2, totally and permanently disabled? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 3. Did any of the persons listed in Part II, Question 2 provide more than 50% of their own support? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No  N/A 4. Did the taxpayer provide more than half the support for each of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_
- Yes  No 5. Did the taxpayer pay over half the cost of maintaining a home for any of the persons in Part II, Question 2? **If yes, which ones:**  
\_\_\_\_\_

**Reminders**

Use Publication 4012, *Volunteer Resource Guide* and Publication 17, *Your Federal Income Tax* in making tax law determinations.

**Additional Tax Preparer Notes:**

\_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

**Section C. For Certified Quality Reviewer Completion**

**Confirm each item after reviewing the tax return and verifying that it reflects correct tax law application to the information provided by the taxpayer.**

- 1. Sections A & B of this form are complete.
- 2. Taxpayer's identity, address and phone numbers were verified.
- 3. Names, SSN or ITINs, and dates of birth of taxpayer, spouse and dependents match the supporting documents.
- 4. Filing Status is correctly determined.
- 5. Personal and Dependency Exemptions are entered correctly on the return.
- 6. All information shown on source documents and noted in Section A, Part III is included on the tax return.
- 7. Any Adjustments to Income are correctly reported.
- 8. Standard, Additional or Itemized Deductions are correct.
- 9. All credits are correctly reported.
- 10. Withholding shown on Forms W-2, 1099 and Estimated Tax Payments are correctly reported.
- All tax law issues above have been addressed and necessary changes have been made.
- If direct deposit or debit was elected, checking/saving account and routing information match the supporting documents.
- Correct SIDN and EFIN are shown on the return.

|  |  |  |   |   |                     |
|--|--|--|---|---|---------------------|
| a Employee's social security number<br><b>441-XX-XXXX</b>  |  | Safe, accurate,<br>FAST! Use                          |   | Visit the IRS website at<br>www.irs.gov/efile |                     |
| b Employer identification number (EIN)<br><b>44-1XXXXXX</b>  |  | 1 Wages, tips, other compensation<br><b>29,922.00</b>  | 2 Federal income tax withheld<br><b>1,279.00</b>          |   |                     |
| c Employer's name, address, and ZIP code<br><b>WILLIAMS MANUFACTURING<br/>2520 AUSTIN BLVD<br/>YOUR CITY, STATE ZIP</b>      |  | 3 Social security wages<br><b>29,922.00</b>  | 4 Social security tax withheld<br><b>1,257.00</b>         |   |                     |
|  |  | 5 Medicare wages and tips<br><b>29,922.00</b>  | 6 Medicare tax withheld<br><b>434.00</b>                  |   |                     |
|  |  | 7 Social security tips   | 8 Allocated tips  |   |                     |
| d Control number   |  | 9  | 10 Dependent care benefits                                |   |                     |
| e Employee's first name and initial Last name<br><b>THOMAS B. FRANKLIN<br/>65421 SW 17TH STREET<br/>YOUR CITY, STATE ZIP</b> |  | Suff. 11 Nonqualified plans  | 12a See instructions for box 12<br><b>W</b> <b>500.00</b> |   |                     |
| f Employee's address and ZIP code  |  | 13 Statutory employee Retirement plan Third-party sick pay<br><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> | 12b   |   |                     |
|  |  | 14 Other   | 12c   |   |                     |
| 15 State Employer's state ID number<br><b>YS 44-1XXXXXX</b>  |  | 16 State wages, tips, etc.<br><b>29,922.00</b>   | 17 State income tax<br><b>421.00</b>                      | 18 Local wages, tips, etc.                    | 19 Local income tax |
|  |  |  |   | 20 Locality name                              |                     |

Form **W-2** Wage and Tax Statement

**2011**

Department of the Treasury—Internal Revenue Service

Copy B—To Be Filed With Employee's FEDERAL Tax Return.  
This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

|   |   |   |                                  |   |  |
|---|---|---|----------------------------------|---|--|
| TRUSTEE'S/PAYER'S name, street address, city, state, and ZIP code<br><b>HEALTHCARE TRUSTEE OF AMERICA<br/>123 MAIN STREET<br/>YOUR CITY, STATE ZIP</b>                          |   | OMB No. 1545-1517<br><b>2011</b><br>Form <b>1099-SA</b>   |                                  | <b>Distributions From an HSA, Archer MSA, or Medicare Advantage MSA</b>                                 |  |
| PAYER'S federal identification number<br><b>44-4XXXXXX</b>  | RECIPIENT'S identification number<br><b>441-XX-XXXX</b> | 1 Gross distribution<br><b>\$ 1,225.00</b>  | 2 Earnings on excess cont.<br>\$ | <b>Copy B For Recipient</b><br><br>This information is being furnished to the Internal Revenue Service. |  |
| RECIPIENT'S name<br><b>THOMAS B. FRANKLIN</b><br>Street address (including apt. no.)<br><b>65421 SW 17TH STREET</b><br>City, state, and ZIP code<br><b>YOUR CITY, STATE ZIP</b> |   | 3 Distribution code<br><b>1</b>   | 4 FMV on date of death<br>\$     |   |  |
| Account number (see instructions)   |   | 5 HSA <input checked="" type="checkbox"/><br>Archer MSA <input type="checkbox"/><br>MA <input type="checkbox"/><br>MSA <input type="checkbox"/> |                                  |   |  |

Form **1099-SA**

(keep for your records)

Department of the Treasury - Internal Revenue Service

## HSA Scenario 5: Test Questions

---

### Directions

Use the interview notes, taxpayer documents, and reference materials needed for this scenario. **Please complete Form 1040 through line 61**, and the appropriate forms, schedules, or worksheets to answer each of the following questions.

*Note: When using the Link and Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your User ID.*

12. What is the amount of Thomas Franklin's health savings account deduction on Form 1040, page 1?
  - a. \$2,000
  - b. \$4,500
  - c. \$5,000
  - d. \$5,500
  
13. What is Thomas Franklin's adjusted gross income (AGI) on Form 1040?
  - a. \$24,922
  - b. \$25,022
  - c. \$25,522
  - d. \$30,022
  
14. What is the amount of unreimbursed qualified medical expenses reported on Form 8889, line 15?
  - a. \$0
  - b. \$500
  - c. \$675
  - d. \$1,125
  
15. What is the amount of additional tax reported on Form 1040, line 60?
  - a. \$10
  - b. \$20
  - c. \$123
  - d. \$245



# Health Savings Accounts – Retest Questions

## Retest Answer Sheet

Name \_\_\_\_\_

Instructions: Volunteers with an Intermediate certification or higher may proceed to a certification for Health Savings Accounts (HSA). HSA is an optional specialty training and certification test available on Link & Learn Taxes. Volunteers must achieve a minimum of 80% to be certified.

**CAUTION: The Test scenarios are provided electronically in a PDF format for information purposes only. The questions on the online test may be either from the test or retest. Students should read each question on the online test very carefully before answering.**

### Privacy Act Notice

The Privacy Act of 1974 requires that when we ask for information we tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if we do not receive it, and whether your response is voluntary, required to obtain a benefit, or mandatory.

Our legal right to ask for information is 5 U.S.C. 301.

We are asking for this information to assist us in contacting you relative to your interest and/or participation in the IRS volunteer income tax preparation and outreach programs. The information you provide may be furnished to others who coordinate activities and staffing at volunteer return preparation sites or outreach activities. The information may also be used to establish effective controls, send correspondence and recognize volunteers.

Your response is voluntary. However, if you do not provide the requested information, the IRS may not be able to use your assistance in these programs.

| Question                     | Answer          |
|------------------------------|-----------------|
| <b>HSA Scenario 1</b>        |                 |
| 1.                           |                 |
| 2.                           |                 |
| 3.                           |                 |
| <b>HSA Scenario 2</b>        |                 |
| 4.                           |                 |
| 5.                           |                 |
| <b>HSA Scenario 3</b>        |                 |
| 6.                           |                 |
| 7.                           |                 |
| 8.                           |                 |
| <b>HSA Scenario 4</b>        |                 |
| 9.                           |                 |
| 10.                          |                 |
| 11.                          |                 |
| <b>HSA Scenario 5</b>        |                 |
| 12.                          |                 |
| 13.                          |                 |
| 14.                          |                 |
| 15.                          |                 |
| Total Answers Correct: _____ |                 |
| Total Questions:             | 15              |
| <b>Passing Score:</b>        | <b>12 of 15</b> |

## Directions

These first four scenarios do not require you to prepare a tax return. Read the interview notes for each scenario carefully and use your training and resource materials to answer the questions after each scenario.

## HSA Scenario 1: Jason Grant

---

### Interview Notes

- Jason Grant is single and 46 years old.
- Jason works as an office manager and his Form W-2 shows wages of \$48,000.
- Jason participated in his employer's self-only coverage High Deductible Health Plan (HDHP) all year.
- Jason does not have any other health coverage.
- Jason has had an HSA for three years.
- Jason's employer contributed \$1,000 in 2011 to his HSA.
- In 2011, Jason contributed \$1,500 to his HSA.
- Jason is a U.S. citizen and has a valid social security number.

## HSA Scenario 1: Retest Questions

---

1. Based on the information provided, Jason is an eligible individual for HSA purposes.
  - a. True
  - b. False
2. Jason's HSA deduction on Form 1040, line 25 is \_\_\_\_\_.
3. The employer contributions to Jason's HSA are reported on Form 1099-MISC.
  - a. True
  - b. False

## HSA Scenario 2: Sidney and Mary Allen

---

### Interview Notes

- Sidney and Mary Allen are married and will file a joint return.
- Sidney is 60 years old, and Mary is 53 years old.
- Both were enrolled in self-only coverage High Deductible Health Plans (HDHPs) through their employers for the entire year of 2011.
- Sidney and Mary each have an HSA.
- Both have contributed the maximum amounts to their HSAs in 2011.
- Sidney and Mary are both U.S. citizens and have valid social security numbers.

### HSA Scenario 2: Retest Questions

---

4. Sidney can contribute a maximum of \$4,050 to his HSA and Mary can contribute a maximum of \$3,050 to her HSA for 2011.
  - a. True
  - b. False
5. Which form or schedule will Sidney and Mary each use to calculate their HSA deductions?
  - a. Schedule A
  - b. Form 8853
  - c. Form 8889
  - d. Form W-2

## HSA Scenario 3: Penny Cook

---

### Interview Notes

- Penny Cook is 35 years old.
- Penny is single and has no dependents.
- In 2011, she had earnings from her job of \$43,000.
- Penny has participated in her employer's self-only HDHP coverage all year.
- Penny has had an HSA for the past three years, including all of 2011.
- Penny contributed the maximum amount allowed to her HSA in 2011.
- In 2011, Penny took funds from her HSA to pay the following expenses:
  - Eyeglasses (needed for medical reasons)—\$250
  - Over-the-counter medication for a skin condition (no prescription from a doctor)—\$120
  - Co-payments for doctor office visits—\$80
  - Dental checkup—\$75
  - Swimming lessons—\$112
- Penny is a U.S. citizen and has a valid social security number.

### HSA Scenario 3: Retest Questions

---

6. Penny's HSA deduction on Form 8889, line 13 is \$\_\_\_\_\_.
7. The amount of **total** distributions reported on Penny's Form 8889, line 14a is \_\_\_\_\_.
8. Which item is not included on Form 8889, line 15?
  - a. Dental checkup – \$75
  - b. Eyeglasses needed for medical reasons – \$250
  - c. Co-payments for doctor office visits – \$80
  - d. Over-the-counter medicine for a skin condition (no doctor's prescription) – \$120

## HSA Scenario 4: Charles and Hazel Rowan

---

### Interview Notes

- Charles, age 42, and Hazel, age 40, are married and will file a joint return.
- They have two children, Jessica and Robert, whom they will claim as dependents on their joint return.
- Hazel's cousin, George (age 30), came to live with them in August 2011. George's gross income was \$4,000. Hazel and Charles did not provide over one-half of George's support for the year but did pay \$500 of George's medical bills in October 2011.
- Charles was enrolled all of 2011 in an HDHP with family coverage.
- Charles has had an HSA for five years.
- In 2011, Charles made regular contributions to his HSA totaling \$2,500.
- In 2011, Charles took funds from his HSA to pay numerous medical expenses including:
  - \$100 for over-the-counter allergy medicine for their daughter, Jessica (no prescription from doctor)
  - \$200 in co-payments for office visits to the pediatrician for Jessica and Robert
  - \$150 to purchase Hazel's contact lenses (needed for medical reasons)
  - \$1,000 for long-term care insurance for Charles
- Charles, Hazel, Jessica, Robert, and cousin George are all U.S. citizens and have valid social security numbers.

### HSA Scenario 4: Retest Questions

---

9. Charles' HSA deduction amount on Form 1040 is \$6,150.
  - a. True
  - b. False
  
10. The \$500 that Charles paid for cousin George's medical bill is a qualified medical expense for HSA purposes.
  - a. True
  - b. False
  
11. For HSA purposes, what is the total amount of qualified medical expenses paid by Charles?
  - a. \$350
  - b. \$990
  - c. \$1,350
  - d. \$1,450

## HSA Scenario 5: Retest Questions

---

### Directions

Refer to the scenario information for Thomas Franklin beginning on page 2-40. Use the interview notes, taxpayer documents, and reference materials needed for this scenario. **Please complete Form 1040 through line 61**, and the appropriate forms, schedules, or worksheets to answer each of the following questions.

*Note: When using the Link and Learn Taxes Practice Lab, complete the social security numbers and employer identification numbers by replacing the Xs with your user ID.*

12. The amount shown on Form 1040, line 25, comes from Form 8889, line 13.
  - a. True
  - b. False
  
13. Thomas Franklin's adjusted gross income (AGI) is \$\_\_\_\_\_.
  
14. The expenses reported on Form 8889, line 15, should be:
  - a. Qualified medical expenses
  - b. Reimbursed qualified medical expenses
  - c. Unreimbursed qualified medical expenses
  - d. Unreimbursed qualified medical expenses in excess of 7.5% of Adjusted Gross Income (AGI)
  
15. What is the percentage of the additional tax that Thomas must pay on the HSA distribution that was not used for unreimbursed qualified medical expenses?
  - a. 5%
  - b. 10%
  - c. 20%
  - d. 50%