

# EA Exam Preparation 2025

## Part 1: Individuals

VIDEO 4:

### **ADJUSTMENTS AND DEDUCTIONS**

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PRESENTER: TOM NORTON CPA, EA

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## What We'll Study

- Adjustments to income
- Standard deduction
- Itemized deductions
- Qualified Business Income Deduction

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## EA Tax Training

[Free Resources \(irs.gov\)](https://www.irs.gov)

- **Publication 17, *Your Federal Income Tax***
- **Instructions for Forms 1040 and 1040-SR**
- **Schedule A (Form 1040), *Itemized Deductions*, and its instructions**
- **Form 8995-A, *Qualified Business Income Deduction*, and its instructions**
- Form 8995, *Qualified Business Income Deduction Simplified Computation*, and its instructions
- Form 2106, *Employee Business Expenses*, and its instructions
- Publication 529, *Miscellaneous Deductions*

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[Free Resources \(irs.gov\)](https://www.irs.gov)

- Publication 970, *Tax Benefits for Education*
- Publication 502, *Medical and Dental Expenses*
- Publication 530, *Tax Information for Homeowners*
- Publication 936, *Home Mortgage Interest Deduction*
- Publication 1771, *Charitable Contributions—Substantiation and Disclosure Requirements*
- Publication 587, *Business Use of Your Home*
- Publication 547, *Casualties, Disasters, and Thefts*

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## Flow of the Tax Return

START:	Gross income
LESS:	Adjustments to income
EQUALS:	Adjusted gross income (AGI)
LESS:	Deductions (Standard or Itemized, QBI)
EQUALS:	Taxable income
APPLY:	Tax tables/Schedules
EQUALS:	Income tax
LESS:	Credits
PLUS:	Other taxes
EQUALS:	Total tax
LESS:	Payments
EQUALS:	Amount Due/Overpayment (Refund)

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## Adjustments to Income

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Schedule 1 (Form 1040) 2024 Page **2**

**Part II Adjustments to Income**

<b>11</b> Educator expenses		<b>11</b>
<b>12</b> Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106		<b>12</b>
<b>13</b> Health savings account deduction. Attach Form 8889		<b>13</b>
<b>14</b> Moving expenses for members of the Armed Forces. Attach Form 3903		<b>14</b>
<b>15</b> Deductible part of self-employment tax. Attach Schedule SE		<b>15</b>
<b>16</b> Self-employed SEP, SIMPLE, and qualified plans		<b>16</b>
<b>17</b> Self-employed health insurance deduction		<b>17</b>
<b>18</b> Penalty on early withdrawal of savings		<b>18</b>
<b>19a</b> Alimony paid		<b>19a</b>
<b>b</b> Recipient's SSN		
<b>c</b> Date of original divorce or separation agreement (see instructions)		
<b>20</b> IRA deduction		<b>20</b>
<b>21</b> Student loan interest deduction		<b>21</b>
<b>22</b> Reserved for future use		<b>22</b>
<b>23</b> Archer MSA deduction		<b>23</b>
<b>24</b> Other adjustments:		
<b>a</b> Jury duty pay (see instructions)		<b>24a</b>
<b>b</b> Deductible expenses related to income reported on line 8i from the rental of personal property engaged in for profit		<b>24b</b>
<b>c</b> Nontaxable amount of the value of Olympic and Paralympic medals and USOC prize money reported on line 8m		<b>24c</b>
<b>d</b> Reforestation amortization and expenses		<b>24d</b>
<b>e</b> Repayment of supplemental unemployment benefits under the Trade Act of 1974		<b>24e</b>
<b>f</b> Contributions to section 501(c)(18)(D) pension plans		<b>24f</b>
<b>g</b> Contributions by certain chaplains to section 409(b) plans		<b>24g</b>
<b>h</b> Attorney fees and court costs for actions involving certain unlawful discrimination claims (see instructions)		<b>24h</b>
<b>i</b> Attorney fees and court costs you paid in connection with an award from the IRS for information you provided that helped the IRS detect tax law violations		<b>24i</b>
<b>j</b> Housing deduction from Form 2555		<b>24j</b>
<b>k</b> Excess deductions of section 67(e) expenses from Schedule K-1 (Form 1041)		<b>24k</b>
<b>z</b> Other adjustments. List type and amount:		<b>24z</b>
<b>25</b> Total other adjustments. Add lines 24a through 24z		<b>25</b>
<b>26</b> Add lines 11 through 23 and 25. These are your <b>adjustments to income</b> . Enter here and on Form 1040, 1040-SR, or 1040-NR, line 10		<b>26</b>

Schedule 1 (Form 1040) 2024

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## Educator Expenses

- Deduct up to \$300 of eligible expenses
  - If MFJ and both are teachers, can deduct up to \$300 each, for a total of \$600
- Must be a K-12 teacher, instructor, counselor, principal, or aide who worked in a school for at least 900 hours
- Unreimbursed ordinary and necessary expenses for:
  - Professional development courses, or
  - Books, supplies, equipment and other materials used in classroom
  - Includes personal protective equipment, disinfectant, and other supplies to prevent spread of coronavirus
- Does not include expenses for home schooling
- Does not include expenses for non-athletic supplies in health or phys ed

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## Certain Business Expenses for...

- Deduct business expenses for:
  - National Guard and reserve members who traveled more than 100 miles from home to perform their service
  - Expenses for qualifying performing artists
  - Fee-basis state or local government officials
- See Form 2106

## HSA/MSA Deduction

- **HSA Deduction:** For contributions to your health savings account that were not:
  - Made by your employer
  - Pre-tax deductions from your paycheck
- **Archer MSA Deduction:** This is a medical savings account set up by small employers or the self-employed to pay for medical expenses, similar to an HSA. No new plans can be set up.
  - Contributions to an existing Archer MSA are deductible

## Self-Employed Health Insurance

- You may be able to deduct the amount you paid for health insurance for yourself, your spouse, and your dependents.
- Must be self-employed and not be eligible for subsidized health insurance from your or your spouse's employer.
  - May be eligible in some months and not others
- Must have a profit (or wages) from the business to cover the deduction

## Alimony Paid

- Alimony payments made under a divorce or separation agreement entered into prior to 1/1/2019, can be deducted
  - Does not apply if the agreement was amended in 2019 or later and expressly provides that alimony will not be included in your former spouse's income

## Retirement Plan Deductions

- **SEP, SIMPLE, and Qualified Plans:** If you were self-employed or a partner, you may be able to take this deduction
  - Will cover in depth in Specialized Returns and Topics video
- **IRA Deduction:** If you made contributions to a traditional IRA for 2024, you may be able to take an IRA deduction.
  - Will cover in depth in Retirement Plans video

## Student Loan Interest

- Student loan interest is deductible up to \$2,500 if all the following apply:
  - You paid interest on a qualifying loan
  - You're not filing MFS
  - You aren't claimed as a dependent on someone else's return
- The deduction phases out between \$80,000 and \$95,000 of AGI if you're Single, HOH or QSS, and between \$165,000 and \$195,000 if MFJ.

## Student Loan Interest

- A qualifying loan is one you took out to pay qualifying higher education expenses for you, your spouse, your dependent, or someone who could have been your dependent except they earned more than \$5,050, filed MFJ, or because you or your spouse could be claimed as a dependent.
- Proceeds must have been used for tuition, fee, room and board, etc. for education in a degree, certificate or similar program at an eligible educational institution (most colleges, universities, and certain vocational schools).

## Certain Attorney Fees

- Attorney fees and court costs for actions involving certain unlawful discrimination claims, but only to the extent of gross income from such actions.
- Attorney fees and court costs you paid in connection with an award from the IRS for information you provided that helped the IRS detect tax law violations, up to the amount of the award includible in your income. (Whistleblower awards).



## Other Adjustments To Income

- **Self-Employment Tax:** You can generally deduct one half of your self-employment tax
  - This represents the "employer's share" of SS and Medicare
- **Moving Expenses:** You can deduct moving expenses if you are a member of the Armed Forces on active duty and due to military order you move because of a permanent change of station.
  - Moving expenses for others are not allowed
- **Penalty on Early Withdrawal of Savings:** Any penalty will be shown on a 1099-INT or 1099-OID you receive.

## Other Adjustments To Income

- **Jury Duty Pay:** If your employer continued to pay you while you were on jury duty, and you handed the jury duty pay over to your employer as a result, you can deduct it here.
- **Olympic Medals:** The nontaxable amount of the value of Olympic and Paralympic medals and USOC prize money reported as Other income can be deducted.
- **Reforestation Expenses:** Certain reforestation amortization and expenses can be deducted.

## Other Adjustments To Income

- **Supplemental Unemployment:** Repayment of certain supplemental unemployment benefits can be deducted.
- **Union Pension Plan Contributions:** Contributions to section 501(c)(18)(D) pension plans can be deducted.
- **Chaplain Retirement Contributions:** Contributions by certain chaplains to section 403(b) plans can be deducted.

## Other Adjustments To Income

- **Foreign Housing Deduction:** The foreign housing deduction from Form 2555 is an adjustment to income.
- **Excess Deductions From a Trust:** Excess deductions on termination of a trust found on Form 1041 K-1, Box 11, code A, can be deducted
- **Incorrect Form 1099-K:** If you receive an incorrect Form 1099-K for amounts you did not receive, report them as Other income and then deduct as an adjustment to income

## Adjusted Gross Income

- Gross income (videos 2 and 3), minus
- Adjustments to income, =
- Adjusted Gross Income (AGI)

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## Standard Deduction

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## Standard Deduction

- Most people can choose to either itemize deductions or take the standard deduction
- You can choose whichever method results in the lowest tax by giving you the higher deductions. You can switch back and forth from year to year, depending on your circumstances.

## No Standard Deduction Allowed

- If you file MFS, and your spouse itemizes deductions, you cannot take the standard deduction.
- If you are a nonresident or dual-status alien, you cannot take the standard deduction.
  - If you are married to a US citizen or resident alien, you can elect to be taxed as a US resident, and can then use the standard deduction.
- If you are filing a tax return for a short tax year because of a change in your annual accounting period, you cannot take the standard deduction (rare).

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**Standard Deduction Chart 2024**

<u>Filing Status</u>	<u>Base</u>	<u>Combination Age 65+ and/or Blind*</u>				<u>Increments</u>
		<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	
Single	\$14,600	\$16,550	\$18,500	N/A	N/A	\$1,950
MFS	\$14,600	\$16,150	\$17,700	\$19,250	\$20,800	\$1,550
MFJ	\$29,200	\$30,750	\$32,300	\$33,850	\$35,400	\$1,550
QSS	\$29,200	\$30,750	\$32,300	N/A	N/A	\$1,550
HOH	\$21,900	\$23,850	\$25,800	N/A	N/A	\$1,950

\*Each person who is age 65+ on or before 1/1/2025, counts as 1 point, as does each person who is blind. So a person who is both age 65+ and blind, counts as 2 points.

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**Standard Deduction for Dependents**

- If you (or your spouse) can be claimed as a dependent on someone else's tax return, your standard deduction is limited to the greater of:
  1. \$1,300, or
  2. Earned income plus \$450
    - Up to the amount of your regular standard deduction.
- If age 65+ and/or blind, add \$1,950 for each "point" if Single or HOH, and \$1,550 if MFJ, MFS or QSS.

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## Standard Deduction for Dependents

- **Example:** Joachin is 15, Single, and claimed as a dependent on his parent's tax return. He earned \$3,500 in 2024 working at a fast food restaurant. What is his standard deduction?
- **Answer:** It is the greater of \$1,300 or his earned income plus \$450; therefore, his standard deduction is \$3,950.

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## Disaster Loss

- If you had a qualified disaster loss in a federally declared disaster area (Section 401 of the Stafford Act), you may be entitled to an increased standard deduction.
- The standard deduction is increased by the amount of the loss minus \$500.
- Use Form 4684 to determine the loss.

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## Itemized Deductions

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## Itemized Deductions

- Medical and Dental Expenses
- Taxes
- Interest
- Charitable Contributions
- Casualty and Theft Losses
- Other

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## Medical and Dental Expenses

- You can deduct only the part of your unreimbursed and otherwise undeducted medical expenses that exceed 7.5% of your AGI.
- Can deduct expenses for you, your spouse, and any dependents
  - Also anyone who you could have claimed as a dependent except:
    - They earned \$5,050 or more;
    - They filed a joint return; or
    - You or your spouse can be claimed as a dependent on someone else's tax return
- **Decedent:** You can deduct expenses incurred for a decedent before they died in the year incurred, as long as they are paid within 1 year and 1 day from the date of death.
- Publication 502, *Medical and Dental Expenses*

## Medical and Dental Expenses

- You can deduct standard medical care, such as expenses for:
  - Prescription medicines or insulin
  - Doctors, dentists, chiropractors, eye doctors, acupuncturists, occupational and physical therapists, psychologists, etc.
  - Medical exams, procedures, X-rays, laboratory services
  - Diagnostic tests, including for pregnancy and blood sugar
  - Hospital care
  - Nursing help
  - Qualified long-term care services
  - Medical aids such as eyeglasses, contacts, hearing aids, braces, crutches, wheelchairs, guide dogs, etc.
  - Smoking cessation programs and treatments
  - Weight loss program as treatment for a specific disease (including obesity) diagnosed by a doctor
  - Breast pumps and supplies
  - Ambulance services and transportation to get medical care
  - Lodging (but not meals) while away from home to receive medical care, up to \$50 per eligible person.
  - Personal protective equipment for preventing the spread of Coronavirus.



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## Health Insurance Premiums

- You can deduct premiums for health/dental/vision insurance, but only for the portion for which you did not get a deduction elsewhere (e.g. self-employed health insurance deduction, or pre-tax amounts through your employer).
- Can deduct Medicare Parts B and D premiums
- Can also deduct a limited amount of long-term care insurance (decreased from 2023).
  - 40 or under                 \$470
  - 41-50                         \$880
  - 51-60                         \$1,760
  - 61-70                         \$4,710
  - 71 or older                 \$5,880

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## Nondeductible Medical Expenses

- Examples of items you **cannot** deduct:
  - Diet food
  - Cosmetic surgery
  - Life insurance
  - Medicare tax
  - Nursing care for a healthy baby
  - Nonprescription medicine (other than insulin)
  - Illegal drugs or procedures
  - Imported drugs not FDA approved
  - Travel to rest or de-stress

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## Medical Expenses- Example

▪ **Example:** John has AGI of \$30,000. He works part-time, with no health insurance benefits, making \$20,000, and is also self-employed in his own business, making \$10,000. He pays health and dental insurance premiums of \$12,000, for which he gets an adjustment to income of \$10,000 for self-employed health insurance. He has other out-of-pocket medical costs of \$5,000. John can treat \$2,000 of the insurance premiums, and the other \$5,000 of out-of-pocket expenses, as deductible medical expenses, for a total of \$7,000; however, he can only deduct the amount that exceeds 7.5% of his AGI ( $\$30,000 \times 7.5\% = \$2,250$ ), making his deductible medical and dental expense amount \$4,750 ( $\$7,000 - \$2,250$ ).

## Taxes You Paid

- State and local income taxes
  - Includes mandatory contributions to state unemployment, workers compensation, and similar funds.
  - Includes taxes paid to a US possession.
- As an alternative to state and local income tax, you can elect to deduct state and local sales tax instead.
  - Either actual taxes paid (receipts), or
  - Tables and worksheets in the instructions to Schedule A

## Taxes You Paid

- Real property taxes
  - If you sold your home, your settlement statement may include taxes paid
  - Cannot deduct foreign property taxes
  - Do not include special assessments, or assessments for items like trash service, lawn service, etc.
- Personal property taxes based on value
- Your total taxes paid deduction, from all sources and types, cannot exceed **\$10,000**.

## Taxes You Cannot Deduct

- Federal income and excise taxes
- Social security, Medicare, federal unemployment, and railroad retirement taxes
- Customs duties
- Federal estate and gift taxes
- Certain state and local taxes such as driver's license and marriage fees, tax on gasoline, car inspections, special assessments.
- Foreign personal or real property taxes (but you can deduct foreign income tax, though you may want to take a credit instead).

## Home Mortgage Interest

- A mortgage is any loan secured by your main home or second home, regardless of how the loan is labeled. It includes first and second mortgages, home equity loans, and refinanced mortgages.
- A "home" can be a house, condominium, cooperative, mobile home, boat, or similar property. It must provide basic living accommodations including sleeping space, toilet, and cooking facilities.

## Mortgage Interest Deduction

- Can deduct interest on up to two homes: Your main home and one other
- Can change the second home year to year
- Look for Form 1098, *Mortgage Interest Statement*
- Closing statement when buying or building
- Publication 936, *Home Mortgage Interest Deduction*

## Limits on Mortgage Interest

- Limit for loan proceeds not used to buy, build, or substantially improve your home. If the proceeds were used for anything else, they are not deductible as home mortgage interest.
- If the proceeds were used for business or investment purposes, the interest may be deductible as a business or investment expense.
- If you refinance a loan where the original loan was used to buy, build, or substantially improve your home, the new loan still qualifies.
  - But if you refinanced for more than the old loan balance and used the extra cash for another purpose (such as paying off credit cards), the additional loan amount does not qualify.

## Limits on Mortgage Interest

- Limits on dollar amount of mortgage:
  - For loans taken out before December 15, 2017, you can deduct interest on up to \$1,000,000 (\$500,000 MFS) of that debt.
    - Loans taken out on or before October 13, 1987, or loans which refinanced such a mortgage, are generally not limited
  - For loans taken out after December 15, 2017, you can deduct interest on up to \$750,000 (\$375,000 MFS) of that debt.
    - You can still use the \$1,000,000 limit if you had a contract on the home on December 15, 2017, for closing by January 1, 2018, and the home was actually purchased before April 1, 2018

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## Points

- The general rule is that loan points are not deductible in the year paid. Instead, they are deducted ratably over the term of the loan (e.g. 1/30<sup>th</sup> per year for a 30-year mortgage).
- However, if you meet certain criteria when buying or building a home (the home mortgage qualifies, the points are based on a percentage of the loan and are reasonable, your cash out of pocket is at least as much as the points, etc.), you can deduct them in the year paid.
- You can also deduct points on a mortgage loan used for home improvements, if you meet similar criteria.

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## Investment Interest

- Investment interest is interest on a loan used to generate taxable investment income.
  - Does not include interest allocable to passive activities
  - Does not include interest allocable to tax-exempt securities
- Use Form 4952 to determine the deduction.

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## Charitable Contributions

- You can deduct gifts to qualified charitable organizations
  - Religious, charitable, educational, scientific, or literary in purpose, or work to prevent cruelty to children or animals.
  - Organization must have applied for and received tax exempt status from the IRS, or have other not-for-profit status, such as a governmental entity
- Contributions can be in cash, property, or out-of-pocket expenses you paid to do volunteer work.
  - Charitable mileage = \$.14 per mile
- Must itemize deductions. "Above the line" charitable contribution deduction of \$300 (\$600 MFJ) expired at the end of 2021.

## Nondeductible Contributions

- If you receive a tax credit for the contribution
- Amounts paid to a college or university for the right to purchase tickets to athletic events
- Travel expenses while away from home, unless there was no significant element of personal pleasure or vacation
- Political contributions
- Dues, fees or bills paid to country clubs, lodges, fraternal orders, etc.

## Nondeductible Contributions

- Cost of raffle, bingo, or lottery tickets (though may be gambling losses).
- Value of your time or services
- Value of blood given
- Transfer of a future interest in tangible personal property
- Gifts to individuals and groups that are operated for personal benefit
- Gifts to foreign organizations (with exceptions for some Canadian, Israeli and Mexican charities)

## Nondeductible Contributions

- Gifts to organizations engaged in political activities that are of direct financial interest to your trade or business.
- Gifts to lobbying groups
- Gifts to civic leagues, social and sports clubs, labor unions, and chambers of commerce
- Value of benefits received in connection with a contribution
- Cost of tuition (may be eligible for an education credit)



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## Charitable Contribution Rules

- If you make a gift and received something in return, such as food, entertainment, or merchandise, you only deduct the amount that is greater than the value of the benefit received.
  - Doesn't apply to certain membership benefits received for an annual payment of \$75 or less, or to items of token benefit.
- Gifts of \$250 or more: Must have a contemporaneous written acknowledgement from the organization showing what you donated and whether or not you received anything in return.
  - For gifts of \$250 or more all at one time. Does not apply to multiple gifts given over time that add up to \$250 or more.

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## Charitable Contribution Limits

- Cash contributions are limited to 60% of AGI for 2024
- Noncash contributions are limited to 50% of AGI minus your cash contributions
- Gifts of capital gain property cannot exceed 30% of AGI
- Amounts that exceed the limits can be carried over for up to 5 future years
- There are other limits as well. See Publication 526.

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## Contributions of Property

- Contributions of property under \$250 total to one organization
  - Written receipt with the description of the property, date, name of organization, etc.
  - If not practical (e.g. drop-off site) then your own records, including detailed description, value and how you determined the value
- Contributions of property of \$250 to \$500
  - Written receipt with the description of the property and a description and value of anything you received in return.

## Contributions of Property

- Contributions of property of \$500 to \$5,000
  - Must file Form 8283 and provide a more detailed description, when acquired, cost, condition, whether donee has certified it for a related use to its charitable purpose, et. al.
- Contributions of property of over \$5,000
  - Must file Form 8283, and have a written appraisal from a qualified appraiser.

## Special Rules for Certain Property

- Clothing and Household Items
  - Must be in good used condition or better, unless have an appraisal for \$500 or more
  - Household items include furniture and furnishings, electronics, appliances, linens and other similar items
  - Does not include food, paintings, antiques, and other objects of art, jewelry and gems, or collections

## Special Rules for Certain Property

- Cars, Boats, and Airplanes
  - If more than \$500, you deduct the smaller of:
    - The gross proceeds of the sale of the vehicle by the organization, or
    - The vehicle's FMV on the date of contribution
    - Attach copy B of 1098-C you receive from the organization
  - If less than \$500, you can deduct the smaller of \$500 or the FMV on the date of contribution. If more than \$250, must have statement from the organization as with any other property donation.

## Special Rules for Certain Property

- Taxidermy Property
  - Deduction limited to basis or FMV, whichever is less
- Property Subject to a Debt
  - Reduce the amount of the FMV of the donation by the amount of any debt the charitable organization assumes
  - Reduce the donation by any interest deduction you take on the debt after the donation
  - For a bond, reduce the FMV for any allowable deduction for interest to buy or carry the bond for any period before the donation, and the interest, including bond discount, receivable on the bond that is attributable to any period before the contribution, and that isn't includible in your income.

## Determining Fair Market Value

- FMV is the price at which property would change hands between a willing buyer and a willing seller, neither having to buy or sell, and both having reasonable knowledge of all the relevant facts.
- Used clothing and personal items: The FMV is usually far less than the price you paid. Claim the amount buyers actually pay in used clothing stores, such as thrift shops.

## Determining Fair Market Value

- If the FMV of a donated item is less than your basis, you can deduct only the FMV, and get no deduction for a loss on the donation.
- If the FMV is higher than your basis, then for:
  - Ordinary income property: Deduct only your basis
  - Capital gains property: Generally, you can use the FMV of the property (there are exceptions)

## Casualty and Theft Losses

- For 2018 to 2025, can only deduct losses of personal-use property from fire, storm, shipwreck, or other casualty, or theft, if the loss is attributable to a federally declared disaster.
- Even then, must deduct \$100 from each loss, and then add up the remaining amount of all your losses, and deduct only the amount that exceeds 10% of AGI.
- For losses of income producing property, see Other Itemized Deductions.

## Casualty and Theft Losses

▪ **Example:** Terry lives in a federally declared disaster area due to a flood. She had a car destroyed that was not covered by insurance and was valued at \$2,000. She also had \$500 of items stolen by looters. Her AGI is \$30,000. First, she reduces each loss by \$100, leaving a \$1,900 loss on the car, and a \$400 theft loss, for a total of \$2,300. Since 10% of her AGI is \$3,000, none of the casualty and theft losses are deductible.

## Losses You Cannot Deduct

- Money or property misplaced or lost
- Breakage of china, glassware, furniture, and similar items, under normal conditions
- Progressive damage to property (buildings, clothes, trees, etc.) caused by termites, moths, other insects, or disease.
- A decline in market value of stock, caused by disclosure of accounting or other illegal misconduct by the officers or directors of the corporation that issues the stock, that was acquired on the open market for investment.

## Gain Realized on Main Home

- If you lose your main home in a disaster (in a federally declared disaster area), and realize a gain upon reimbursement (i.e. reimbursement is greater than basis) of the home or its contents, you may not have to pay tax on all or part of the gain.
  - Also applies to renters
- Any gain on reimbursement for unscheduled personal property does not have to be recognized.

## Gain Realized on Main Home

- Any additional insurance proceeds you receive for the home or its contents are treated as received for a single item of property, and any replacement property you purchase to replace lost items are treated as a single replacement property. Therefore, you can choose to recognize gain only to the extent the insurance proceeds exceed the total replacement costs.
- If you choose to postpone the gain, the period in which you need to replace the property is 4 years after the end of the first tax year in which any part of the gain is realized.

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## Gain Realized on Main Home

- **Example:** George and Carla lost their home and all its contents in a tornado in a federally declared disaster area in 2024. They received insurance proceeds of \$200,000 for the home, \$25,000 for unscheduled personal property, \$5,000 for jewelry, and \$10,000 for a stamp collection. They do not have to pay tax on the \$25,000. The jewelry and stamp collection were scheduled property. If George and Carla spend \$215,000 or more on a new home before 2029, they do not have to recognize any gain. The gain is postponed until they sell their new house.

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## Other Itemized Deductions

- Amortizable premium on taxable bonds.
- Casualty and theft losses from income-producing property.
- Excess deductions of an estate or trust.
- Federal estate tax on income in respect of a decedent.
- Gambling losses up to the amount of gambling winnings.
- Home office
- Impairment-related work expenses of persons with disabilities.
- Losses from Ponzi-type investment schemes (see Pub. 547 for more information).
- Repayments of more than \$3,000 under a claim of right.
- Unlawful discrimination claims.
- Unrecovered investment in an annuity.

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## Amortizable Premium on Taxable Bonds

- In general, if the amount you pay for a bond is greater than its stated principal amount, the excess is bond premium. You can elect to amortize the premium on taxable bonds.
- The amortization of the premium is generally an offset to interest income rather than a separate deduction.
- For certain bonds, such as those acquired prior to October 23, 1986, you can deduct the premium instead.

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## Fines or Penalties

- In general, fines or penalties are not deductible. For example parking tickets, tax penalties, and penalties deducted from teachers' paychecks after an illegal strike.
- However, certain amounts can be in the following situations:
  - Certain amounts that constitute restitution.
  - Certain amounts paid to come into compliance with the law.
  - Amounts paid as the result of certain court orders in which no government or specified nongovernmental agency is a party.
  - Amounts paid or incurred for taxes due (the tax itself, not the penalty).
- For restitution or to come into compliance, the amounts must be specifically identified in the settlement agreement.
- Cannot deduct reimbursement to the government for the costs of any investigation or litigation.

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## Gambling Losses

- You must report the full amount of your gambling winnings for the year on Schedule 1.
- You can deduct your gambling losses for the year on Schedule A, but only up to the amount of your winnings.
  - Losses include the winnings, plus expenses, such as travel, incurred.
- You **cannot** simply reduce your gambling winnings by your gambling losses and report the difference.
- You must keep records, such as a gambling diary, of your wins and losses.
- If you're a professional gambler, can report on Schedule C and deduct all losses.

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## Home Office Deduction

- Use part of your home regularly and exclusively for business
  - For example, an extra room used to run your business
- Must be your principal place of business, or the only place where administrative or management activities can be performed
- Can be owner or renter
- Cannot be as an employee

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## Home Office Deduction

- Two methods:
  - **Simplified method:** \$5 per square foot for the area used regularly and exclusively for business, with a maximum of 300 feet. So the maximum deduction is \$1,500.
  - **Regular method:** The deductions are based on the percentage of the home devoted to business use. Usually based on square feet used for business divided by total square feet of living space. Deduct that percentage of mortgage interest, insurance, utilities, repairs, maintenance, depreciation, and rent.

## Loss from Ponzi Scheme

- Losses from a Ponzi-type investment scheme are deductible as theft losses of income-producing property in the year the loss was discovered.
- Use Form 4684 to figure the deductible loss.

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## Repayments Under Claim of Right

- If you included income of \$3,000 or more in a previous year because you thought you had an unrestricted right to the income, and then have to pay it back, you can take a deduction for the amount paid back.

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## Not Deductible

- Charitable contributions for non-itemizers
  - Previously could deduct \$300 (\$600 MFJ) of cash contributions even if did not itemize.
- Mortgage insurance premiums are no longer deductible.
- Miscellaneous itemized deductions subject to the 2%-of-AGI floor are no longer deductible.

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## Qualified Business Income Deduction

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## Qualified Business Income Deduction

- Business owners may be eligible for a deduction of 20% of their Qualified Business Income, plus 20% of their real estate investment trust (REIT) dividends and publicly traded partnership (PTP) income.
- This is called a Qualified Business Income Deduction (QBID) or Section 199A deduction.
- Available regardless of whether you itemize deductions or take the standard deduction.

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## Qualified Business Income Deduction

▪ The deduction has two components:

1. **QBI Component.** The component equals 20% of QBI from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust, or estate. This component is subject to limitations based on the taxpayer's taxable income and type of business, amount of W-2 wages paid by the business, and other factors.
2. **REIT/PTP Component.** This component equals 20% of qualified REIT dividends and PTP income. It does not have the limitations of the QBI component, though depending on the taxpayer's taxable income, the amount of PTP income that qualifies may be limited depending on the type of the PTP's trade or business.

## Qualified Business Income (QBI)

- QBI is, essentially, the net business income from any domestic trade or business, including income from partnerships, S corporations, sole proprietorships, and certain trusts.
  - Does not include investment income, such as capital gains, interest, and dividends, or wages or similar amounts received for services performed.
  - Does include the deductible part of self-employment tax, self-employed health insurance, and deductions for contributions to qualified retirement plans (e.g. SEP, SIMPLE and qualified plan deductions).

## Qualified Business Income (QBI)

- Solely for purposes of the QBID, many rental real estate activities will qualify as QBI.
  - Keep separate books and records for each rental enterprise.
  - 250 or more hours of rental services performed in 3 of last 5 years (or every year if less than 4 years of existence).
  - Keep contemporaneous records of work performed, hours, dates, etc.
- Rental or licensing of tangible or intangible property that does not rise to the level of a trade or business under section 162 will nevertheless qualify for the QBID if the rental or licensing of property is to a commonly controlled trade or business.

## QBI Limitations

- If total taxable income is at or below \$191,950 (\$383,900 MFJ), then no limitation.
- For taxable income over that amount, the type of business matters.
  - Specified Service Trade or Business (SSTB)
  - Non-SSTB

## QBI Limitations- SSTB

- Specified Service Trade or Business (SSTB)
  - Law, medicine, accounting, actuarial services, consulting, financial services, professional athletes, performing artists, et. al.
- If SSTB, then:
  - S, HOH, QSS, MFS: QBID phased out between \$191,950 and \$241,950 of TI
  - S, HOH, QSS, MFS: No QBID over \$241,950 of TI
  - MFJ QBID phased out between \$383,900 and \$483,900 of TI
  - MFJ No QBID over \$483,900 of TI

## QBI Limitations- Non-SSTB

- For Non-SSTB, no limitation below \$241,950 (\$483,900 MFJ) of taxable income.
- For S, HOH, QSS, or MFS with TI over \$241,950, or MFJ with TI over \$483,900, the QBID is limited to the greater of:
  - 50% of your share of W-2 wages paid out in the business, or
  - 25% of your share of W-2 wages paid out in the business, plus 2.5% of the unadjusted basis immediately after acquisition (UBIA) of qualified property
  - Qualified property is depreciable property used in the trade or business which is not yet fully depreciated.



## REIT/PTP Component

- The second component, which gets added to the first, is for 20% of the dividends received from a real estate investment trust (REIT), and 20% of income received from a publicly traded partnership (PTP).
- The PTP component is limited if generated by an SSTB, following the similar rules/limits.

## Calculation of the QBID

- Add together the QBI component and the REIT/PTP component.
- The total cannot be more than 20% of taxable income minus capital gain.

## QBID Example

▪ **Example:** Hannibal and Clarice (MFJ) have taxable income of \$350,000, including capital gains of \$40,000. Their Schedule C construction business generates QBI of \$290,000. They also own several REITs, which generated \$50,000 of dividends for them.

Their QBID is calculated as follows:

- QBI component:  $\$290,000 \times 20\% = \$58,000$
- REIT/PTP component:  $\$50,000 \times 20\% = \$10,000$
- Tentative QBID =  $\$68,000$

Their taxable income minus capital gains is \$310,000. 20% of that is \$62,000. So their QBID is limited to \$62,000.

## QBID Recap

- 20% of combined QBI component and REIT/PTP component.
- The total cannot be more than 20% of taxable income minus capital gain.
- Limited at higher income levels.
- More limited for SSTBs than non-SSTBs.

## Taxable Income

- Gross income (videos 2 and 3), minus
- Adjustments to income, =
- Adjusted Gross Income (AGI), minus
- Standard deduction or Itemized deduction, minus
- Qualified Business Income Deduction, =
- Taxable Income (TI)

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**End of Video 4. See you in Video 5!**

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