Marquette University
e-Publications@Marquette

Accounting Faculty Research and Publications | Business Administration, College of

3-1-2009

Reduced Income Can Translate into Larger Tax Deductions and Credits

James Trebby
Marquette University, james.trebby@marquette.edu

Originally published in *Practical Tax Strategies*, Volume 82, No. 3 (March 2009).
The published version of the journal article is available here.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

Reduced Income Can Translate into Larger Tax Deductions and Credits

James P. Trebby

Accounting Department, Marquette University

Milwaukee, WI

Abstract:

Income limitations affect eligibility for a variety of tax deductions and credits, making an economic downturn the time for taxpayers to seek out tax savings they could not claim in better financial times.

One trend that increases complexity in the tax law is the greater use of income limitations and phase rules that restrict eligibility for claiming credits and deductions. Thus, taxpayers who incur the "right" kind of expenses may find themselves unable to claim tax incentives because they have too high a level of income. With the present troubled economy, however, many taxpayers will find that their 2008 incomes are lower than in prior years-whether due to job layoffs, lower business profits, smaller bonuses and commissions, or reduced investment income. These individuals could qualify for tax credits and deductions this year for which their previously higher incomes rendered them ineligible. Thus, taxpayers and return preparers should be aware that some individuals will be eligible for tax breaks on their 2008 returns they were unable to claim in prior years. An array of

Practical Tax Strategies, Vol. 82, No. 3 (2009): pg. 167-173. Publisher Link. This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

those tax credits and deductions are discussed below, along with their income limitations.

College Tuition

The Code contains both credits and deductions that are related to college costs.

Education Credits

Two credits, the Hope Scholarship credit and the Lifetime Learning credit, [1] are available to help individuals defray the cost of higher education. The credits, both of which are nonrefundable, are available for qualifying tuition and related expenses incurred by students in the pursuit of undergraduate or graduate degrees, or vocational training. Room, board, and textbooks costs do not qualify for these credits.

The Hope Scholarship credit allows a maximum credit of $1,800 ($3,600 for a Midwestern disaster area student) per year (for both 2008 and 2009). The credit is determined by taking 100% of the first $1,200 of tuition expenses (100% of the first $2,400 for a Midwestern disaster area student) plus 50% of the next $1,200 of tuition expenses (50% of the next $2,400 if a Midwestern disaster area student) for the first two years of postsecondary education.

The Lifetime Learning credit is a maximum of $2,000 ($4,000 for a Midwestern disaster area student). This credit is calculated as 20% (40% if a Midwestern disaster area student) of qualifying expenses up to $10,000 per year, incurred in a year in which the Hope credit is not claimed for a particular student. Thus, the Lifetime Learning credit is useful for individuals who are beyond the first two years of postsecondary education.

Both credits are available for qualified expenses incurred by the taxpayer, the taxpayer's spouse, or the taxpayer's dependent. Married taxpayers must file a joint return to claim either credit. The Hope Scholarship credit is available per eligible student, while the Lifetime Learning credit is calculated on a per-taxpayer basis.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

To be eligible for the Hope Scholarship credit, a student must take at least one-half the fulltime course load for at least one term at a qualifying educational institution. No similar requirement applies, however, for the Lifetime Learning credit. This is beneficial for taxpayers who are seeking new job skills or maintaining existing job skills through continuing education or graduate study.

Both credits are subject to the same income restrictions. For 2008, the credit phases out ratably with modified adjusted gross income (AGI) of $48,000 to $58,000 ($96,000 to $116,000 for married taxpayers filing jointly). For 2009, the credit is phased out with modified AGI in the $50,000 to $60,000 ($100,000 to $120,000 for a joint return) range.

Caveat. As we go to press, the American Recovery and Reinvestment Act of 2009 has modified the Hope Scholarship credit for 2009 and 2010. The changes include an increase in the modified AGI level of the credit phase-out to the $80,000 to $90,000 ($160,000 to $180,000 for joint filers) range, an increase in the maximum annual credit for these years to $2,500 per eligible student, and an expansion of the credit availability to the first four years of post-secondary education.

Education Deduction

A tuition deduction[2] is available for the same types of expenses as qualify for the Hope Scholarship and Lifetime Learning credits. It may not be claimed with respect to an individual for whom one of these tax credits has been taken. This is an above the- line deduction (i.e., a deduction for adjusted gross income), so it is available to those who claim the standard deduction as well for those who itemize deductions. As with the education credits, a married taxpayer may claim the tuition deduction only on a joint return.

The income-based deduction phase-out for the tuition deduction occurs in steps. The maximum credit is $4,000 if the taxpayer's AGI does not exceed $65,000 ($130,000 on a joint return). The maximum credit is $2,000 if a taxpayer's AGI is more than $65,000 but does not exceed $80,000 (more than $130,000 but not more than $160,000 on a joint return). These income limitations are higher than those for the

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

Hope Scholarship or Lifetime Learning credit. Consequently, taxpayers whose incomes render them ineligible for the education credits may still be able to claim a tuition deduction.

Education Loan Interest Deduction

Taxpayers who pay interest on a qualifying student loan may be able to deduct the interest as an above-the-line deduction.[3] The deduction is available only to the extent that the loans are used to pay qualified educational expenses to qualified educational institutions. The deduction is not available for those who are claimed as dependents or for married taxpayers filing separately.

The maximum deduction is $2,500. For 2008, the deduction is phased out for taxpayers with a modified AGI between $55,000 ($115,000 for joint returns) and is completely phased out for taxpayers with modified AGI of $70,000 or more ($145,000 for joint returns). For 2009, the deduction begins to phase-out for taxpayers with modified AGI in excess of $60,000 ($120,000 for joint returns) and is completely phased out for taxpayers with modified AGI of $75,000 or more ($150,000 for joint returns).

Child Tax Credit

Taxpayers may be able to claim a tax credit for each of their qualifying children. To be eligible for the credit, the child must be under age 17 and could be claimed as a dependent on the taxpayer's return.

The maximum credit is $1,000 per child and is scheduled to remain at $1,000 through 2010.[4] The credit is phased out when modified AGI exceeds $110,000 for joint returns, $55,000 for married taxpayers filing separately, and $75,000 for single taxpayers. (The threshold amounts are not indexed for inflation.) A taxpayer's credit eligibility is phased out by $50 for each $1,000 (or part thereof) of AGI that exceeds the applicable threshold amount.

Thus, a $1,000 credit is fully phased out by $19,001 of income above the applicable threshold amount. The more qualifying children the taxpayer has, the larger the taxpayer's potential credit eligibility,

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

and, thus, the more income the taxpayer may have before the taxpayer's total credit eligibility is fully phased out.

Adoption Expenses Credit

Section 23 gives taxpayers a credit for nonrecurring costs directly associated with the adoption of an eligible child (e.g., adoption fees, attorney fees, court costs, transportation costs, and social service review costs). An eligible child must be either:

1. Under age 18 at the time of the adoption.

2. Physically or mentally incapable of caring for himself or herself.

The taxpayer may claim the credit in the year the qualifying expenses were paid or incurred if they were paid or incurred during or *after* the tax year in which the adoption was finalized. For qualifying expenses paid in a tax year *prior* to the year in which the adoption was finalized, the credit must be claimed in the tax year following the tax year in which the expenses were paid or incurred. A married couple must file a joint return.

For 2008, up to $11,650 of costs incurred to adopt an eligible child qualify for the credit. In 2009, the maximum credit is $12,150. The adoption credit begins to phase-out when modified AGI exceeds $174,730 in 2008; eligibility for the credit is completely phased out when modified AG I reaches $214,730. The respective numbers for 2009 are $182,180 and $222,180. The credit is calculated by reducing the allowable credit by a phase-out amount. This amount is the allowable credit multiplied by the ratio of the taxpayer's AG I in excess of $174,300 for 2008 or $182,180 in 2009 to $40,000.

First-time Homebuyers Tax Credit

The Housing Assistance Tax Act of 2008 provides a temporary credit for home buyers purchasing a home between 4/9/08 and 7/1/09. The credit is 10% of the purchase price of the home, up to stated maximum. This credit ceiling is $7,500 ($3,750 for married filing separately).[5]

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

An unusual feature of this credit, however, is that it must be repaid in equal installments over 15 years beginning in the second year after the credit is claimed. For example, a taxpayer who claims the maximum credit of $7,500 on his or her 2008 return must begin repaying the credit by including 1/15 of this amount, or $500, as an additional tax beginning on his or her 2010 return. Normally, $500 will be due with each tax return for years 2010 through 2024.

The credit is phased out for married couples filing jointly with modified AGI between $150,000 and $170,000 and for single taxpayers with modified AGI between $75,000 and $95,000.

Caveat. As we go to press, the American Recovery and Reinvestment Act of 2009 has extended the first-time homebuyer credit to residences purchased before 12/1/09. It also increased the maximum credit amount to $8,000 and eliminated the repayment requirement (unless the home is sold or no longer used as a principal residence within three years) for homes purchased after 2008.

Credit for the Elderly and Disabled

The Section 22 credit for the elderly and the permanently and totally disabled is designed to provide tax relief on retirement income for taxpayers who are not receiving substantial benefits from tax-free Social Security payments. To be eligible, the taxpayer must be either:

1. Age 65 or older.

2. Under age 65, retired, and receiving disability income from a public or private employer on account of a permanent and total disability.

The maximum credit is 15% of the qualifying amount. The qualifying amounts are:

1. $7,500 for married taxpayers filing a joint return and both spouses qualify for the credit.

2. $5,000 for married taxpayers filing a joint return and only one spouse qualifies.

3. $5,000 for taxpayers who are single individuals.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

4. $3,750 for married taxpayers (per spouse) filing separate returns if the spouses live apart for the entire tax year. (If the spouses have not lived apart for the entire year, they must file a joint return to claim the credit.)

The credit is reduced by one-half of the excess of the taxpayer's AG lover these thresholds:

1. $10,000 for married taxpayers filing a joint return where either spouse qualifies.

2. $7,500 for a single individual

3. $5,000 (per spouse) for married taxpayers filing separate returns if the spouses live apart for the entire tax year.

The credit is also reduced by amounts the taxpayer receives as pension or disability benefits that are excludable from tax (including payments made under title II of the Social Security Act). Thus, many taxpayers receive sufficient amounts of Social Security benefits or have a high enough AGI base to reduce this credit to zero. The credit is nonrefundable and, therefore, cannot exceed the taxpayer's tax liability.

Interest on Savings Bonds

Section 135 excludes from income interest on Series EE U.S. savings bonds to the extent the bond proceeds do not exceed higher education expenses (i.e., tuition and fees). This exclusion applies only if both of the following requirements are satisfied:

1. The savings bonds are issued after 12/31/89.

2. The savings bonds were issued to an individual who was at least age 24 at the time of the issuance. (Thus, the exclusion is not available for bonds issued in the name of a child.)

For 2008, the exclusion begins to phase-out for modified AGI above $67,100 ($100,650 on a joint return). For 2009, the phase-out begins with modified AGI above $69,950 ($104,900 on a joint return).

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

The phase-out is completed when modified AGI exceeds the threshold amounts by more than $15,000 ($30,000 on a joint return).

Limitation on Itemized Deductions

Section 68 reduces the deductible portion of itemized expenses for taxpayers whose incomes exceed certain thresholds. For 2008, the phase-out of itemized deductions applies to taxpayers whose AGI exceeds $159,950 ($79,975 for married taxpayers filing separately). The 2009 phase-out AGI amounts are $166,800 and $83,400 respectively.

This limitation on itemized deductions is itself being phased-out over a four year period beginning in 2006. (The deduction limitation will no longer exist for tax years beginning after 2009.) Therefore, a two-step computation is needed to determine how much of an affected taxpayer's itemized deductions are phased out.

1. The first step involves calculating the littlest of (a) 3% of the amount by which the taxpayer's AGI exceeds the applicable income thresholds or (b) 80% of itemized deductions that are affected by the limit.

2. The second step requires multiplying the itemized deduction reduction that would apply in the first step by ⅓ as (for both 2008 and 2009).

This deduction limitation applies to only the following itemized deductions:

1. Taxes.

2. Home mortgage interest, including points.

3. Charitable contributions.

4. Miscellaneous itemized expenses subject to the 2%-of-AGI deduction floor.

Thus, medical and dental expenses, investment interest expense, nonbusiness casualty and theft losses, and gambling losses are *not* subject to the limitation.

Practical Tax Strategies, Vol. 82, No. 3 (2009): pg. 167-173. Publisher Link. This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

Personal and Dependency Exemptions

The personal and dependency exemption deduction is $3,500 in 2008 ($3,650 in 2009). A of personal and dependency exemptions6 begins when AGI exceeds the following amounts:

- For 2008, $239,950 for joint returns and surviving spouses; $199,950 for heads of households; $159,950 for single taxpayers; and $119,975 for married individuals filing separate returns.
- For 2009, the respective AGI amounts that trigger the phase-out are $250,200, $208,500, $166,800, and $125,100.

The exemption phase-out is calculated by a two-step formula:

1. First, calculate a phase-out amount of 2% for each $2,500 (or fraction thereof) by which the taxpayer's AGI exceeds the applicable threshold amount. This phase-out percentage cannot exceed 100%.

2. Then multiply the amount determined in the first step by ⅓ (for both 2008 and 2009).

Deductible IRA Contributions

Taxpayers may contribute up to $5,000 ($6,000 if at least age 50) to an IRA in 2008 or 2009. Section 219(g) places income restrictions on a taxpayer's ability to deduct contributions to a traditional IRA if the individual (or, if married, his or her spouse) is an active participant in an employer-sponsored retirement plan. If the taxpayer (and, if married, his or her spouse) participate in an employer-sponsored plan, the traditional IRA deduction is phased out proportionately between the following AGI ranges:

- For unmarried taxpayers, $53,000 to $63,000 in 2008 ($55,000 to $65,000 for 2009).
- For married taxpayers filing a joint return, $85,000 to $105,000 in 2008 ($89,000 to $109,000 for 2009).

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

- For married taxpayers who file separate returns $0 to $10,000 for both 2008 and 2009.

If the taxpayer is not an active participant in an employer-sponsored retirement plan, but the taxpayer's spouse does participate in such a plan, the deduction phases out for the taxpayer in a higher income range: $159,000 to $169,000 in 2008 ($166,000 to $176,000 in 2009).

Alternative Minimum Tax (AMT) Exemption

Late in 2008, Congress approved a long-expected patch for the AMT. The patch increases the AMT exemption, which is essentially a standard deduction for taxpayers affected by the AMT. Under the new law, the exemption amounts are: $46,200 for single and head of household taxpayers, $69,950 for married taxpayers filing jointly, and $34,975 for married taxpayers filing separately. This "patch" is a one-year fix only, which means that Congress will likely have to address this issue again in 2009.

The exemption is phased out, however, at the rate of 25% of AMT taxable income above $150,000 for married taxpayers filing jointly, $112,500 for single and head of household taxpayers, and $75,000 for married taxpayers filing separately. These thresholds are not indexed for inflation, which is one reason why more people (whom Congress never initially intended) owe the AMT each year.

Earned Income Credit

The earned income credit7 is intended to provide tax equity to the working poor and encourages economically disadvantaged individuals to join the workforce. This credit is a refundable credit. Refundable credits are paid to the taxpayer even if the credit exceeds the taxpayer's tax liability.

The computation of the credit is somewhat complex. The credit is (1) a percentage of earned income amounts, up to a specified ceiling, (2) reduced by a phase-out percentage of adjusted gross income (or earned income, if greater) in excess of a phase-out amount.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

The credit percentages and earned income amount ceilings in 2008 are as follows:

- No qualifying children, 7.65% and $5,720 ($5,970 in 2009).
- One qualifying child, 34% and $8,580 ($8,950 in 2009).
- Two or more qualifying children, 40% and $12,060 ($12,570 in 2009).

Thus, the maximum credits in 2008 are as follows:

- No qualifying children, $438 ($457 in 2009).
- One qualifying child, $2,917 ($3,043 in 2009).
- Two or more qualifying children, $4,824 ($5,028 in 2009).

The phase-out percentage and phase-out amounts for 2008 are as follows:

- No qualifying children, 7.65% and $7,160 ($7,470 in 2009); phase-out amount of $10,160 ($10,590 in 2009) for joint return filers.
- One qualifying child, 15.98% and $15,740 ($16,420 in 2009); phase-out amount of $18,740 ($19,540 in 2009) for joint return filers.
- Two or more qualifying children, 21.06% and $15,740 (16,420 in 2009); phase-out amount of $18,740 ($19,540 in 2009) for joint return filers.

The credit is completed phased out for 2008 when earned income (or AGI, if higher) reaches these levels:

- No qualifying children, $12,880 ($13,440 in 2009); $15,880 ($16,560 in 2009) for joint return filers.
- One qualifying child, $33,995 ($35,463 in 2009); $36,995 ($38,583 in 2009) for joint return filers.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

- Two or more qualifying children, $38,646 ($40,295 in 2009); $41,646 ($43,415 for joint return filers.

Economic Stimulus Payments

More than 124 million households received the one-time economic stimulus payment in 2008, which was based on 2007 tax return information. The payment is not taxable, and does not reduce a taxpayer's 2008 refund or increase his or her tax liability for 2008. Taxpayers are eligible if they have a valid Social Security number (SSN), cannot be claimed as a dependent on a tax return, and have either an income tax liability or "qualifying income" of at least $3,000. Qualifying income includes any amount of earned income and certain benefits from Social Security, Veterans Affairs, or Railroad Retirement. Both taxpayers listed on a married filing jointly return must have a valid SSN to receive the payment. (There is an exception for members of the military who file a joint return.)

The amount of the stimulus payment depends on the information contained on the tax return. Eligible individuals received between $300 and $600. Those who filed a joint return received between $600 and $1,200. Those with children (the child must be eligible under the child tax credit rules) received an additional $300 for each qualifying child.

Both the basic component and the additional amounts for qualifying children begin to phase-out for individuals with AGI over $75,000 and married couples who file a joint return with AGI over $150,000. The combined payment is reduced by 5% of the income above the AGI thresholds.

For 2008, a recovery rebate credit is available for those who did not receive the full economic stimulus payment in 2008 and whose circumstances may have changed, making them eligible for some or all of the unpaid portion. Basically speaking, taxpayers are entitled to the credit based on their 2008 income, reduced by the stimulus payment they already received based on their 2007 income. Taxpayers who fall into the following categories may be eligible to receive the recovery rebate credit this year:

1. Individuals who did not receive an economic stimulus payment.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

2. Those who received less than the maximum economic stimulus payment in 2008 because their qualifying or gross income was too high or too low.

3. Families who gained an additional qualifying child in 2008.

4. Individuals who could be claimed as a dependent on someone else's tax return in 2007, but who cannot be claimed as a dependent on another return in 2008.

5. Individuals who did not have a valid SSN number in 2007 but received one in 2008.

Unlike the stimulus payments distributed last year, the recovery rebate credit will be included in a taxpayer's tax refund for 2008 and will not be issued as a separate payment.

Conclusion

A variety of tax deductions and credits have income-based restrictions or limitations. By being aware of these rules, taxpayers and return preparers can better focus on the types of tax benefits a taxpayer may be eligible to claim. AGI is generally the starting point for applying income limitations, but the AGI figure may be modified for purposes of calculating a particular deduction or credit, and the modifications can vary among the Code sections.

A taxpayer whose income declined significantly from prior years may be eligible for additional tax breaks even though the taxpayer made the same expenditures in 2008 as were made in the prior years. Thus, a prior year's tax return can be a good starting point for mapping out this year's return preparation task, but it should not be used blindly as a template.

Notes

1. Section 25A.
2. Section 222.
3. Section 221.
4. Section 24.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

5. Section 36.

6. Section 151 (d)(3).

7. Section 32.

Appendix

Other Income-Related Restrictions

Some tax deductions have restrictions that are based on income, but do not take the form of deduction phase-outs. Here are some examples:

Medical expenses. The medical expense deduction in Section 213 is not subject to an income ceiling, but it is restricted by a percentage-of-AGI deduction floor. Taxpayers who pay medical and dental expenses (which are not reimbursed by insurance) for themselves, their spouse, or their dependents may claim an itemized deduction for the amount of the cost that exceeds 7.50/0 of the taxpayer's AGI Thus, the lower one's income, the less medical expense needed to produce a tax benefit. Taxpayers who have experienced a drop in income in 2008 may find themselves eligible to claim a tax benefit for a level of medical expenses for which no deduction would be available were their income higher.

Miscellaneous itemized deductions. Section 67 imposes a 2%-of-AGI deduction floor on miscellaneous itemized deductions. This category includes unreimbursed employee business expenses (including union and professional association dues). Expenses related to investment property, tax return preparation costs, and hobby expenses to the extent of hobby income. As with medical expenses, a taxpayer whose income has declined in 2008 needs less of these expenses to overcome the deduction floor.

Charitable contributions. If the qualifying charitable contributions for the year total 20% or less of the contribution base (a form of modified AGI), they are fully deductible under Section 170. If the qualifying contributions are more than 20% of contribution base, the deduction may be limited to either 20%, 30%, or 50% of the taxpayer's contribution base, depending on the type of property contributed and the type of organization to which the property is

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

donated. In any event, the maximum charitable contribution for the year may not exceed 50% of the taxpayer's contribution base. Excess contributions may be carried forward to future years. Consequently, the higher one's income, the greater is the maximum charitable contribution deduction that may be claimed in a particular year.

In general, the 50% limit applies to contributions to certain types of public charities. A 30%of- AGI ceiling applies to contributions of cash and ordinary income property to private nonoperation foundations that are not 50% organizations. Finally, a 20% ceiling applies to contributions of appreciated long-term capital gain property to private nonoperation foundations that are not 50% organizations.

Carolyn is a professional poker player whose sole occupation is gambling. While she is good at this line of work, she does have some bad years, and this is one of them. Over the course of year, she has $100,000 of gambling winnings, but $110,000 of wagering losses-producing a $10,000 net loss from wagering. She also has $12,000 of business expenses, consisting mainly of bills racked up on transportation, lodging, and food on overnight trips to poker tournaments. Fortunately, Carolyn has investments to help her make ends meet, and they threw off $40,000 of income for the year.

Can Carolyn deduct her business expenses even though she has a net loss from wagering?

Solution: Yes. AM 2008-013 (IRS Generic Legal Advice on Professional Gambler's Wagering Losses and Business Expenses).

Rationale: Section 165(d) restricts the deduction of wagering losses to the taxpayer's wagering gains for the year, but this does not restrict the deduction of other business expenses incurred by a professional gambler. Thus, when Carolyn reports her $100,000 of wagering gains as gross receipts, she may deduct only $100,000 of wagering losses to offset those gains. She may also, however, deduct the $12,000 of business expenses without regard to Section 165(d). This produces a $12,000 business loss from gambling that can be used to offset her investment income.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.

***NOT THE PUBLISHED VERSION;* this is the author's final, peer-reviewed manuscript.** The published version may be accessed by following the link in the citation at the bottom of the page.

If Carolyn had no investment income, she would have a $12,000 net operating loss, which could be carried back or forward to another year under Section 172(b). In contrast, her $10,000 of net losses from wagering may not be carried over to another year.

 This article is © Thomson Reuters and permission has been granted for this version to appear in e-Publications@Marquette. Thomson Reuters does not grant permission for this article to be further copied/distributed or hosted elsewhere without the express permission from Thomson Reuters.