

PASFAA 2021 Virtual Conference Open Forum for Tax Questions

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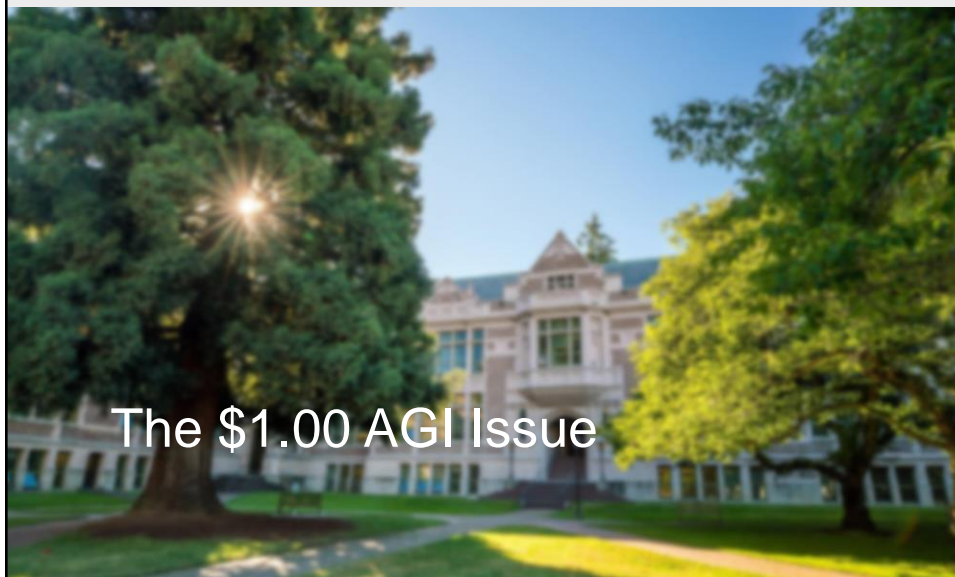
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Sourcing and Distribution

- The information cited in this presentation is based on the following information as available on October 17, 2021
 - IRS publications, forms, and form instructions for tax year 2020
 - The most recent versions of Department of Education publications
 - *The 2022-2023 pdf FAFSA*
 - *The Application and Verification Guide, 2021-2022*
 - *EFC Formula Guide, ISIR Guide, and SAR Comment Codes and Text, etc. for 2022-2023*
 - *Federal Registers, Electronic Announcements, and Dear Colleague Letters*
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 - This conference session was created for and offered by the Pennsylvania Association of Student Financial Aid Administrators (PASFAA)
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What Happened?

- The IRS created a *Child Tax Credit Non-filer Sign-up Tool* in the summer of 2021 to allow 2020 non-filers to provide the IRS with information needed to get advance payments of the 2020 increased child tax credits
 - The IRS created tax year 2020 tax records for these individuals even though they are non-filers, with artificial \$1.00 AGIs
- The \$1.00 AGI tax record will block the creation of an accurate tax record should someone who used the Child Tax Credit Non-filer Sign-up Tool subsequently files an actual return
 - If such a person uses the IRS DRT, the artificial \$1.00 AGI will be imported into the FAFSA
 - The ISIR will be flagged as Automatic Zero EFC eligible (except for independent students without a non-spouse dependent)

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9/30 Electronic Announcement

- (APP-21-19) – IRS Data Retrieval Tool and Potential Inaccurate \$1 Adjusted Gross Income for the 2022–23 FAFSA Form

Free Application for Federal Student Aid (FAFSA®) filers who use the IRS Non-Filer Portal (NFP), subsequently file a 2020 tax return, and then use the IRS DRT to transfer their tax information into the 2022–23 FAFSA form will unknowingly report an incorrect AGI of \$1. This may result in a lower Expected Family Contribution (EFC) and a higher Pell Grant award for students who would not otherwise be eligible.

Note: The new tool was launched after the filing season and has MANY warnings on the landing page and inside the tool to educate taxpayers prior to using the tool. So far, the volumes are low when compared to the number of tax filers who erroneously used the original NFP.

Potential Impact to Student Aid Eligibility for 2022–23 FAFSA cycle

FAFSA filers who use the NFP, prior to filing a 2020 tax return, and then use the IRS DRT to transfer their tax information into the 2022–23 FAFSA will have an incorrect AGI of \$1. This may result in a lower EFC and a higher Pell Grant award for students who would not otherwise be eligible.

As a result of this issue, Financial Aid Administrators are encouraged to identify all instances of \$1 AGIs, for the 2022–23 FAFSA cycle, and follow-up with applicants to resolve as appropriate. Schools should instruct the student and/or parent to obtain a Record of Account from the IRS to verify if the \$1 value is correct and make adjustments to the student's financial aid package as needed.

Important

<https://fsapartners.ed.gov/knowledge-center/library/electronic-announcements/2021-09-30/irs-data-retrieval-tool-and-potential-inaccurate-1-adjusted-gross-income-2022-23-fafsa-form>

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What Does this Mean?

- A \$1.00 AGI imported from the IRS DRT or appearing on a *Tax Return Transcript* is probably incorrect and should be investigated
 - The IRS DRT will place a “No” in the “Did you file a Schedule 1?” field, triggering the Automatic Zero EFC variant *and the related skip logic*
 - The AGI in the “Information from the Return or as Adjusted” section of the Account transcript or **Record of Account** transcript is the correct AGI on the day the transcript is printed
 - If it shows a \$1.00 – then it is correct
 - If it shows a different AGI, then *that AGI is the accurate AGI*
 - **Important** – the Record of Account transcript includes a copy of the tax return transcript *with the unchanged data from the original return*, which will show the \$1.00 AGI in this case

Using The Account Transcript

** INFORMATION FROM THE RETURN OR AS ADJUSTED **

EXEMPTIONS:	
FILING STATUS:	
ADJUSTED GROSS INCOME:	74,092.00
TAXABLE INCOME:	61,540.00
TAX PER RETURN:	9,794.00
SE TAXABLE INCOME	
TAXPAYER:	0.00
SE TAXABLE INCOME	
SPOUSE:	0.00
TOTAL SELF EMPLOYMENT TAX:	0.00

This is the **New** Adjusted Gross Income (AGI)

- You will need a signed copy of Form 1040 and the applicable schedules to correct the other FAFSA data, because the tax transcript will only include information from the artificial \$1.00 AGI tax return

What You'll Need to Do

- Collect the Account Transcript to verify the correct AGI
- Collect a signed copy of the Form 1040 and applicable schedules to update the other data that are imported by the IRS DRT but may not be in the ISIR
- Ask the applicant and their family members to return to the FAFSA and update answers that may be missing
 - Untaxed income
 - Additional financial information
 - Dependent student income and asset information



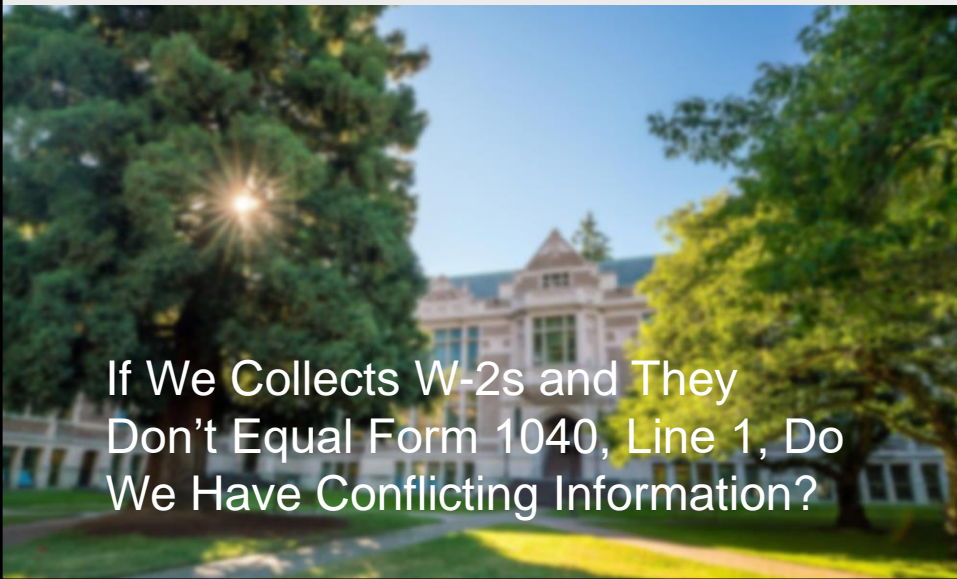
Can We Accept a Preparer's Letter
Restating that a 1040 is Correct?

Resolving Discrepant Data

For example, an FAA who notices that a dependent student's parents, who are married and live together, have each filed as head of household (which offers a greater tax deduction than filing as single or married) must ask if that is the right status. Publication 17 explains on pages 23–25 the criteria a person must meet to file as head of household. Resolution of the conflict could be the parents refiling and submitting a copy of the amended return or a reasonable explanation of why there really is no conflict under IRS rules.

- *Resolution of the conflict could be*
 - *The parents refiling and submitting a copy of the amended return*
 - OR**
 - *A **reasonable explanation** of why there is no conflict under IRS rules.*

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If We Collects W-2s and They
Don't Equal Form 1040, Line 1, Do
We Have Conflicting Information?

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What's on Form 1040 – Line 1?

- Earned income *not subject to self-employment taxes*
 - Earned income that is reported to the earner on a W-2
 - Earned income that should have been reported to the earner on a W-2
 - Earned income that would have been reported to the earner on a W-2, had it not been earned at a non-US foreign company or non-governmental organization
 - Tips not reported to the worker's employer
 - Cash tips under \$20
 - Non-cash tips
 - Employee benefit reconciliations
- Taxable scholarships
- Disability pensions

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Non-W-2 Wages

Code	Description	Explanation
HSH	Household Employee Income	Household employees who were under the age of 18 at any point during the year or who earned less than \$2,200 in 2020 do not get W-2s
FEC	Foreign Earned Compensation	Employees of companies with no United State affiliation report their earnings on Form 1040, line 1, but do not have W-2s
No code	UN, World Bank, Other NGOs	United States citizens and residents must report their NGO income on Form 1040, line 1, but may not receive W-2s
*Notice 2014-7	Medicaid Waiver Payments	Caretakers who are paid by Medicaid and provide care in their own home may report their non-taxable wages in line 1 to claim the EIC

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*If a taxpayer receives this kind of income but wants to claim the Earned Income Credit, they report the wages on Form 1040, line 1 and deduct them on Schedule 1, line 8, where they write "Notice 2014-7" and the wages as a negative value

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Statutory Employees

- A statutory employee is someone who
 - Receives a W-2 but pays income tax as a self-employed person
- Their W-2, box 1 wages are reported on Schedule C, line 1, not Form 1040, line 1

Statutory Employee W-2

1 Wages, tips, other compensation 62500.00	2 Federal income tax withheld
3 Social security wages 62500.00	4 Social security tax withheld 3875.00
5 Medicare wages and tips 62500.00	6 Medicare tax withheld 906.25
a Employee's social security no. XXX-XX-7357	b Employer ID number (EIN) 36-4346343
c Employer's name, address, and ZIP code PARENT'S EMPLOYER CURIOUS AND CURIOUSER CURIOUS 1 EMPLOYMENT LN. ANYWHERE, MA 02124	
7 Social security tips	8 Allocated tips
9	10 Dependent care benefits
11 Nonqualified plans	12a
14 Other	12b
	12c
	12d
d Control number	13 Stat Emp. <input checked="" type="checkbox"/> Ret. plan <input type="checkbox"/> Third party <input type="checkbox"/>
e Employee's name PARENT ONE	
f Employee's address and ZIP code 15 HOME AVE. SOMEWHERE, MA 02125	

Note

- Employee will report W-2, box 1 wages on Schedule C, line 1
- They will not file Schedule SE, because they paid social security and Medicare taxes as employees

Social security and Medicare taxes. You must withhold social security and Medicare taxes from the wages of statutory employees if all three of the following conditions apply.

- The service contract states or implies that substantially all the services are to be performed personally by them.
- They don't have a substantial investment in the equipment and property used to perform the services (other than an investment in facilities for transportation, such as a car or truck).
- The services are performed on a continuing basis for the same payer.

Income tax. Don't withhold federal income tax from the wages of statutory employees.

Statutory Employee Schedule C

Part I Income			
1	Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on Form W-2 and the "Statutory employees" box on that form was checked <input checked="" type="checkbox"/>	1	62,500
2	Returns and allowances	2	
3	Subtract line 2 from line 1	3	62,500
4	Cost of goods sold (from line 42)	4	0
5	Gross profit. Subtract line 4 from line 3	5	62,500
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	0
7	Gross income. Add lines 5 and 6	7	62,500
Part II Expenses. Enter expenses for business use of your home only on line 30.			
8	Advertising	8	
9	Car and truck expenses (see instructions)	9	0
10	Commissions and fees	10	
11	Contract labor (see instructions)	11	
12	Depreciation	12	
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13	0
14	Employee benefit programs (other than on line 19)	14	
15	Insurance (other than health)	15	
16	Interest (see instructions)	16	
16a	Mortgage (paid to banks, etc.)	16a	
16b	Other	16b	
17	Legal and professional services	17	
18	Office expense (see instructions)	18	300
19	Pension and profit-sharing plans	19	
20	Rent or lease (see instructions)	20	
20a	Vehicles, machinery, and equipment	20a	0
20b	Other business property	20b	
21	Repairs and maintenance	21	400
22	Supplies (not included in Part III)	22	1,650
23	Taxes and licenses	23	
24	Travel and meals:	24	
24a	Travel	24a	0
24b	Deductible meals (see instructions)	24b	0
25	Utilities	25	
26	Wages (less employment credits)	26	
27a	Other expenses (from line 4b)	27a	3,680
27b	Reserved for future use	27b	
28	Total expenses before expenses for business use of home. Add lines 8 through 27a	28	6,030
29	Tentative profit or (loss). Subtract line 28 from line 7	29	56,470
30	Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method. See instructions. Simplified method filers only: Enter the total square footage of: (a) your home: 2,500 and (b) the part of your home used for business: 300. Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30	30	1,500
31	Net profit or (loss). Subtract line 30 from line 29	31	54,970

Note (pointing to line 1): W-2, box 1

Schedule 1, line 3 FAFSA

Not to Schedule SE

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Form 1099-NEC – Box 1

- Formerly Form 1099-MISC, box 7
- Used by companies that have determined that a person working for them is a contractor, not an employee
 - If the worker agrees that they are self-employed (not an employee), they report their income on Schedule C, line 1
 - If the worker feels they should have been paid as an employee
 1. They report their Form 1099-NEC, box 1 income on Form 1040, line 1
 2. They file Form 8919 with their tax return to calculate their FICA taxes owed, and report their tax on Schedule 2, line 5, which ends up on Form 1040, line 23 (and 24)
 3. They file Form SS-8 directly with the IRS (it is not part of Form 1040 and supporting schedules) so the IRS can investigate the employer and attempt to get the employer to pay the employer's share of the FICA taxes

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Do You Have Conflicting Information?

- Issue – You have a 1099-NEC, and the taxpayer has reported the income on Form 1040, line 1
 - But – they did not file Form 8919
 - **Robert's opinion**
 - It's up to the IRS to determine if the taxpayer was an employee or self-employed, not you
 - If you get a signed statement from the employee that they considered themselves employees and that's why they put the income on Form 1040, line 1, you have a reasonable explanation of why the **FAFSA data from the tax return is correct and does not need to be changed**
 - Form 8919 will not change any FAFSA item as the lowest numbered line on Form 1040 that it impacts is line 23
 - Without this signed statement, the tax return is incorrect – if the person is self employed, their AGI and Income Tax for 2020 are incorrect because of the deduction for ½ the self-employment tax

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Thank You!

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