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TAX in the News

Tax Information for Tax Practitioners

April 10, 2019

FBAR April 15 Filing Reminder—The deadline for filing a Report of Foreign Bank and Financial Accounts (FBAR) is the same as the deadline for filing a federal income tax return: April 15, 2019. The due date is automatically extended to October 15, 2019, for those who cannot file a complete and accurate report by April 15. Generally, the FBAR filing requirement applies to anyone with a foreign bank or financial account with a value exceeding $10,000 *at any time* during 2018. The form must be filed through the BSA E-Filing system.

TAX NEWS

IRS Guidance Explains Interaction of State Tax Refunds with $10,000 SALT Limitation—Starting in 2018, taxpayers who overpay state and local taxes may not have received the full benefit of the overpaid taxes to begin with. Rev. Rul. 2019-11 explains how the tax benefit rule works for taxpayers who receive state and local tax refunds. Four scenarios illustrate how to calculate the amount to include in gross income, given the $10,000 SALT cap and increased standard deduction amount. Page 3

Moving Expense Code "P" Clarification—The 2018 Form W-2 Box 12 code "P" is used *only* to report excludable moving expense reimbursements paid directly to U.S. Armed Forces members who move because of military orders. The IRS advises that the code shouldn't be used for any other purpose, such as to report nontaxable reimbursements made in 2018 for 2017 moves. Page 4

IRS Announces Revised EIN Application Process—Starting May 13, 2019, only responsible parties with tax identification numbers (ITINs or SSNs) may request an Employer Identification Number (EIN). The intent of the change is to improve security and transparency by preventing entities from using their own EINs to obtain other EINs. Page 4

Adjustments to Foreign Housing Expense "Ceiling" for High-Cost Areas—This is the first of two updates on the foreign earned income exclusion. Notice 2019-24 provides adjusted limitation amounts for taxpayers who live and work abroad in 2019 and qualify to exclude or deduct housing expenses. Those that work in high-cost areas may be able to exclude a larger portion of housing expenses because of higher ceilings (upper thresholds) that apply to those areas. Page 4

Foreign Earned Income Exclusion: Waiver of Time Requirements Due to Adverse Conditions—This is the second foreign earned income exclusion update. The IRS periodically lists countries for which the eligibility requirements for the foreign earned income exclusion are waived for U.S. citizens and residents working abroad because adverse conditions prevent them from meeting those requirements. Rev. Proc. 2019-15 adds the Democratic Republic of the Congo, Cuba, Iraq, and Nicaragua to the list of waiver countries for 2018. Page 5

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QUESTION OF THE WEEK

A divorced client has a joint custody agreement with her ex-spouse. The decree states that he has a right to claim the younger child's exemption until she turns 17. Is the client still required to sign an 8332 to relinquish her claim on this child? [Page 6](#)

ORIGINAL INSIGHTS

Tales from the Tax Court: The Wayfair decision changes the standard for sales tax on remote sellers—States now have Supreme Court guidance on when they can require sellers to collect sales tax on internet sales. Full insight. View all insights at www.thetaxinstitute.com/insights/.

IRS GUIDANCE EXPLAINS INTERACTION OF STATE TAX REFUNDS WITH $10,000 SALT LIMITATION

IRS news release IR-2019-59 and Rev. Rul. 2019-11 explain the tax treatment of state and local tax refunds arising in a year when the $10,000 state and local tax "SALT" limitation applies.

The tax benefit rule generally requires a taxpayer to include in gross income in the current year any recovered amount, including a SALT refund, that the taxpayer deducted in a prior tax year. However, the taxpayer must include recovered amounts only to the extent the amounts reduced the taxpayer's tax liability in the prior year.

Starting in 2018, because of the TCJA's $10,000 SALT cap, taxpayers who overpay state and local taxes and receive SALT refunds in 2019 may not have received the full benefit of the overpaid taxes to begin with. Rev. Rul. 2019-11 provides four situations to illustrate the tax treatment of SALT refunds.

Assume in each that the taxpayer is unmarried, uses the single filing status, is under 65, and is not subject to AMT. All taxes were paid in 2018 and all refunds were received in 2019.

Situation 1

Taxpayer A paid $4,000 in local real property taxes and $5,000 in state income taxes for a total SALT deduction of $9,000. A's other deductible expenses were $5,000 and total itemized deductions were $14,000.

A received a $1,500 state income tax refund of overpaid taxes.

If A had paid the correct state income taxes in 2018 ($3,500 instead of $5,000), A's SALT deduction would have been $7,500, and total itemized deductions would have been $12,500, which is a $1,500 difference ($14,000 - $12,500). Thus, A received the full tax benefit of the $1,500 overpayment and must include the entire $1,500 refund in gross income in 2019.

Situation 2

Taxpayer B paid $5,000 in local real property taxes and $7,000 in state income taxes ($12,000 in total) with a SALT deduction limited to $10,000. B's other deductible expenses were $5,000 and total itemized deductions were $15,000.

B received a $750 state income tax refund of overpaid taxes.

If B had paid the correct state income taxes in 2018 ($6,250 instead of $7,000), B's SALT deduction would still have been limited to $10,000 and total itemized deductions would remain at $15,000. B received no tax benefit from the $750 overpayment and is not required to include any of the $750 refund in gross income in 2019.

Situation 3

Taxpayer C paid $5,000 in local real property taxes and $6,000 in state income taxes ($11,000 in total) with a SALT deduction limited to $10,000. C's other deductible expenses were $5,000 and total itemized deductions were $15,000.

C received a $1,500 state income tax refund of overpaid taxes.

If C had paid the correct state income taxes in 2018 ($4,500 instead of $6,000) C's SALT deduction would have been $9,500 and total itemized deductions would have been $14,500, a difference of $500 ($15,000 - $14,500). C received a tax benefit of $500 and must include $500, not the full $1,500 refund, in gross income.

Situation 4

Taxpayer D paid $4,250 local real property taxes and $6,000 state income taxes ($10,250 in total) for a SALT deduction limited to $10,000. D's other deductible expenses were $2,500 and total itemized deductions were $12,500.

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D received a $1,000 state income tax refund of overpaid taxes.

If D had paid the correct state income taxes in 2018 ($5,000 instead of $6,000) D's SALT deduction would have been $9,250 and total itemized deductions would have been $11,500, which is less than the $12,000 standard deduction. D received a tax benefit of $500, the difference between total itemized deductions and the standard deduction. D is required to include $500 of the state tax refund in gross income.

Summary

If a taxpayer received a state tax benefit from deducting state and local taxes in a prior year and recovers all or a portion of the taxes in the current year, the taxpayer must include in gross income the *lesser* of:

1. The difference between total itemized deductions and itemized deductions that would have been claimed had the taxpayer paid the proper amount of state and local income tax, or
2. The difference between total itemized deductions and the applicable standard deduction amount for the prior year.

Rev. Rul. 2019-11 discusses recoveries of state and local income tax, but the same principles apply to recoveries of state and local real or personal property tax.

MOVING EXPENSE CODE "P" CLARIFICATION

An IRS information release explains that the 2018 Form W-2 Box 12 code "P" is to be used only for 2018 excludable moving expense reimbursements paid directly to a member of the U.S. Armed Forces who moves per a military order and incident to a permanent change of station.

The code is not to be used for any other purpose. For instance, some employers have reported nontaxable reimbursements made in 2018 for 2017 moves. Employers who have used the code incorrectly should inform their employees to disregard the amount and omit the code P from Form W-2 information for tax return preparation. However, employers do not need to file corrected forms with the SSA or IRS or furnish them to employees.

IRS ANNOUNCES REVISED EIN APPLICATION PROCESS

IRS news release IR-2019-58 announces a change to the process of requesting an Employer Identification Number (EIN). An EIN is a nine-digit number assigned to sole proprietors, corporations, partnerships, estates, trusts, and other entities for tax purposes.

Starting May 13, 2019, only responsible parties with tax identification numbers (ITINs or SSNs) may request an EIN. Generally, the responsible party is the individual who owns or controls the entity. The change means that entities will not be able to use their own EINs to obtain additional EINs. The change provides greater security to the process and improve transparency by requiring individuals to be the responsible party.

Individuals obtain an EIN by completing a paper or online Form SS-4, *Application for Employer Identification Number*. Form SS-4 instructions provide a detailed explanation of who should be the responsible party for various entities. Tax professionals may continue to act as third-party designees and complete the EIN application for entities.

ADJUSTMENTS TO FOREIGN HOUSING EXPENSE "CEILING" FOR HIGH-COST AREAS

The Treasury Department and IRS have issued Notice 2019-24 providing adjustments to the limitation on housing expenses for purposes of the §911 housing cost exclusion for specific locations in 2019.

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Foreign housing costs

U.S. citizens and residents who live and work abroad are eligible to exclude portions of their foreign earned income and housing costs under IRC §911. To calculate the foreign housing exclusion amount, the taxpayer needs to consider both a “floor” and a “ceiling.” The excludable amount is the amount by which the housing expenses (up to the ceiling) exceed the base housing amount (floor).

The ceiling (upper threshold) on excludable housing costs is 30 percent of the maximum foreign earned income exclusion for the year. For tax year 2019, the ceiling on excludable housing costs is $31,770 ($105,900 exclusion × 30%).

The floor, called the “base housing amount,” is 16 percent of the maximum foreign earned income exclusion for the year. For tax year 2019, the base housing amount is therefore $16,944 ($105,900 exclusion × 16%). Only housing costs in *excess* of this base amount are excludable. A taxpayer with qualified housing expenses equal to or less than the amount many not exclude any of the housing costs. Putting the two concepts together, the maximum housing cost an eligible individual may exclude from income in 2019 is $14,826 ($31,770 ceiling – $16,944 floor).

Adjustments to the “ceiling”

The Secretary is authorized to adjust the ceiling based on geographic differences in housing costs relative to the U.S. Notice 2019-24 provides a *Table of Adjusted Limitations* for high housing cost areas for 2019. For example, the ceiling in Seoul, South Korea is $57,600 and the maximum excludable housing cost is $40,656 ($57,600 - $16,944).

Taxpayers in high-cost locations during 2018 may elect to apply the limitations set forth in the 2019 Table of Adjusted Limitations instead of the 2018 table in Notice 2018-44. The How to Use High Cost Table for §911 Housing Costs Quick Reference Card explains how to apply the Table of Limitations for 2019.

FOREIGN EARNED INCOME EXCLUSION—WAIVER OF TIME REQUIREMENTS DUE TO ADVERSE CONDITIONS

A U.S. citizen or resident alien who lives and works abroad may be eligible to exclude some or all foreign earnings from U.S. taxation. The IRS periodically lists countries for which the eligibility requirements for the foreign earned income exclusion under §911(d)(1) are waived because adverse conditions prevented individuals from meeting those requirements.

Under §911(d)(4), an individual who is required to leave one of the listed countries because of war, civil unrest, or other similar adverse conditions will be treated as a qualified individual if he or she establishes a reasonable expectation of meeting the bona fide residence test or physical presence test, but for the adverse conditions.

In Rev. Proc. 2019-15, the waiver applies to qualified individuals who left the following countries on or after the dates indicated:

- Democratic Republic of the Congo (December 14, 2018)
- Cuba (January 4, 2018)
- Iraq (September 28, 2018)
- Nicaragua (July 6, 2018)

To be eligible for relief under §911(d)(4), the taxpayer must have established residency or have been physically present in the foreign country *prior to* the date shown above. For example, an individual who first established residency in the Congo *after* December 14, 2018, would not be eligible for relief under §911(d)(4).

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Form 2555, *Foreign Earned Income Exclusion*, is used to calculate and claim the exclusion. See "What are the countries for which an exception to the bona fide residence or physical presence test for the foreign earned income exclusion is allowed because of civil unrest?" in the Tax Research Center's Tax Knowledge Base. Also, The Quick Reference Card Form 2555-Adverse Conditions in a Foreign Country is a listing of countries for which the adverse conditions waiver has applied in recent years.

QUESTION OF THE WEEK

Q. My client is divorced and has a joint custody agreement with her ex-spouse for their two children. The children live with her in her home for more than half the year (they stay with their father for some holiday weekends, vacations, etc.). Their decree states that he has a right to the younger child's exemption until she turns 17. The decree was signed in 2011. Does the client need to sign an 8332 in order to relinquish her claim for this child?

A. Yes, your client must sign Form 8332, *Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent* if she wants her ex-spouse to claim the child. Without the exemption release, the child's father may not claim her. The tax law does not *require* her to release the exemption, but she should consult her attorney if she doesn't wish to do so.

Even though their decree states they have joint custody, your client *is* the custodial parent. Under the regulations (Reg. §1.152-4(d)), for tax purposes, the custodial parent is "the parent with whom the child resides for the greater number of nights during the calendar year, and the noncustodial parent is the parent who is not the custodial parent." In this situation, the children clearly reside with your client the greater number of nights during the year.

Under the rules for divorced and separated parents (§152(e)), the custodial parent must sign a written declaration "in such manner and form as the Secretary may by regulations prescribe" that she will not claim the child as a dependent. The noncustodial parent must attach the declaration to his return. The regulations (Reg. §1.152-4(e)(3)(ii)) state that Form 8332 is the appropriate form for the release.

Form 8332 is not expressly required by the regulations, but any alternative written declaration must contain all information in the form to accomplish the release:

- The child's name
- The year or years of the release
- An explicit statement that the custodial parent will not claim the child for the stated years
- The custodial parent's signature, SSN, and the date
- The noncustodial parent's name and SSN

Also, the only purpose of the alternative declaration must be for the exemption release.

For most parents, Form 8332 is the best way to effect the release and it is very difficult to produce a satisfactory alternative. Before 2009, the IRS did accept divorce decrees if several requirements were met. One of these was the unconditional release of the child's exemption. Since most decrees include a condition, such as the payment of support, few divorce decrees were acceptable. Decrees executed in 2009 or later may not be used as an alternative declaration, regardless of the language in the decree.

TCJA and the exemption release

Although the exemption amount is $0 for tax years 2018 through 2025, the release allows the noncustodial parent to claim the child tax credit, additional child tax credit, and the credit for other dependents as applicable. The release does not apply to the EITC, child and dependent care credit, or head of household filing status. See "Written declaration" on page 11 of IRS Pub. 504, *Divorced or Separated Individuals*.