



Individual Income Tax: Income Part 2

Course #3112D

Taxes

2 Credit Hours

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INDIVIDUAL INCOME TAX: INCOME PART 2

This course covers various types of income and discusses which ones are taxed and which ones are not. Types of income discussed include: rental income, retirement benefit and pensions, annuities, and others

LEARNING ASSIGNMENTS AND OBJECTIVES

As a result of studying each assignment, you should be able to meet the objectives listed below each individual assignment.

SUBJECTS

Rental Income and Expenses
Retirement Plans, Pensions, and Annuities

Study the course materials from pages 1 to 67

Complete the review questions at the end of each chapter

Answer the exam questions 1 to 10

Objectives:

- Recognize the proper treatment of rental property income and expenses for tax purposes.
- Identify various requirements regarding retirement plan taxation.
- Identify the taxability of various types of other income.

NOTICE

All references to IRS forms and line numbers throughout this course are based on prior year or draft forms available from the IRS in late 2022. There is a possibility some of these references will change.

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EXAM OUTLINE

- **TEST FORMAT:** The final exam for this course consists of 10 multiple-choice questions and is based specifically on the information covered in the course materials.
- **ACCESS FINAL EXAM:** Log in to your account and click Take Exam. A copy of the final exam is provided at the end of these course materials for your convenience, however you must submit your answers online to receive credit for the course.
- **LICENSE RENEWAL INFORMATION:** This course qualifies for **2** CPE hours.
- **PROCESSING:** You will receive the score for your final exam immediately after it is submitted. A score of 70% or better is required to pass.
- **CERTIFICATE OF COMPLETION:** Will be available in your account to view online or print. If you do not pass an exam, it can be retaken free of charge.

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CHAPTER 1: RENTAL INCOME AND EXPENSES

Chapter Objective

After completing this chapter, you should be able to:

- Recognize the proper treatment of rental property income and expenses for tax purposes.

I. INTRODUCTION

This chapter discusses rental income and expenses. It covers the following topics.

- Personal use of dwelling unit (including vacation home).
- Depreciation.
- Limits on rental losses.

II. RENTAL INCOME

In most cases, you must include in your gross income all amounts you receive as rent. Rental income is any payment you receive for the use or occupation of property. It is not limited to amounts you receive as normal rent payments.

When to report. If you are a cash basis taxpayer, report rental income on your return for the year you actually or constructively receive it, regardless of when it was earned. You constructively receive income when it is made available to you, for example, by being credited to your bank account. If you are an accrual basis taxpayer, you generally report income when you earn it, rather than when you receive it.

Advance rent. Advance rent is any amount you receive before the period that it covers. Include advance rent in your rental income in the year you receive it regardless of the period covered or the method of accounting you use.

Example



You sign a 10-year lease to rent your property. In the first year, you receive \$5,000 for the first year's rent and \$5,000 as rent for the last year of the lease. You must include \$10,000 in your income in the first year.

Security deposits. Do not include a security deposit in your income when you receive it if you plan to return it to your tenant at the end of the lease. But if you keep part or all of the security deposit during any year because your tenant does not live up to the terms of the lease, include the amount you keep in your income in that year.

If an amount called a security deposit is to be used as a final payment of rent, it is advance rent. Include it in your income when you receive it.

Payment for canceling a lease. If your tenant pays you to cancel a lease, the amount you receive is rent. Include the payment in your income in the year you receive it regardless of your method of accounting.

Expenses paid by tenant. If your tenant pays any of your expenses, those payments are rental income. You must include them in your income. You can deduct the expenses if they are deductible rental expenses. See *Rental Expenses*, later, for more information.

Property or services. If you receive property or services, instead of money, as rent, include the fair market value of the property or services in your rental income.

If the services are provided at an agreed upon or specified price, that price is the fair market value unless there is evidence to the contrary.

Rental of property also used as a home. If you rent property that you also use as your home and you rent it fewer than 15 days during the tax year, do not include the rent you receive in your income and do not deduct rental expenses. However, you can deduct on Schedule A (Form 1040) the interest, taxes, and casualty and theft losses that are allowed for nonrental property. See *Personal Use of Dwelling Unit (Including Vacation Home)*, later.

Part interest. If you own a part interest in rental property, you must report your part of the rental income from the property.

III. RENTAL EXPENSES

This part discusses repairs and certain other expenses of renting property that you ordinarily can deduct from your rental income. It includes information on the expenses you can deduct if you rent part of your property, or if you change your property to rental use. Depreciation, which you can also deduct from your rental income, is discussed later.

When to deduct. If you are a cash-basis taxpayer, you generally deduct your rental expenses in the year you pay them.

Vacant rental property. If you hold property for rental purposes, you may be able to deduct your ordinary and necessary expenses (including depreciation) for managing, conserving, or maintaining the property while the property is vacant. However, you cannot deduct any loss of rental income for the period the property is vacant.

Vacant while listed for sale. If you sell property you held for rental purposes, you can deduct the ordinary and necessary expenses for managing, conserving, or maintaining the property until it is sold. If the property is not held out and available for rent while listed for sale, the expenses are not deductible rental expenses.

Pre-rental expenses. You can deduct your ordinary and necessary expenses for managing, conserving, or maintaining rental property from the time you make it available for rent.

Personal use of rental property. If you sometimes use your rental property for personal purposes, you must divide your expenses between rental and personal use. Also, your rental expense deductions may be limited. See *Personal Use of Dwelling Unit (Including Vacation Home)*, later.

Part interest. If you own a part interest in rental property, you can deduct expenses that you paid according to your percentage of ownership.

Uncollected rent. If you are a cash-basis taxpayer, you do not deduct uncollected rent. Because you do not include it in your income, it is not deductible.

Depreciation. You can begin to depreciate rental property when it is ready and available for rent. See *Placed-in Service Date* under *Depreciation*, later.

REPAIRS AND IMPROVEMENTS

Generally, an expense for repairing or maintaining your rental property may be deducted if you are not required to capitalize the expense.

Improvements. You must capitalize any expense you pay to improve your rental property. An expense is for an improvement if it results in a betterment to your property, restores your property, or adapts your property to a new or different use.

Betterments. Expenses that may result in a betterment to your property include expenses for fixing a pre-existing defect or condition, enlarging or expanding your property, or increasing the capacity, strength, or quality of your property.

Restoration. Expenses that may be for restoration include expenses for replacing a substantial structural part of your property, repairing damage to your property after you properly adjusted the basis of your property as a result of a casualty loss, or rebuilding your property to a like-new condition.

Adaptation. Expenses that may be for adaptation include expenses for altering your property to a use that is not consistent with the intended ordinary use of your property when you began renting the property.

Safe harbor for routine maintenance. If you determine that your cost was for an improvement to a building or equipment, you still may be able to deduct your cost under the routine maintenance safe harbor.

Note



Separate the costs of repairs and improvements, and keep accurate records. You will need to know the cost of improvements when you sell or depreciate your property. The expenses you capitalize for improving your property generally can be depreciated as if the improvement were separate property.