To Your Benefit 2002

Understanding Tax Credits and Deductions

A tax primer for service providers

Sponsored by:

Legal Aid Society of Minneapolis

Children's Defense Fund Minnesota

AccountAbility Minnesota

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Introduction

Welcome!

To Your Benefit is an educational program that offers a non-technical overview of tax topics important to low-to-middle income taxpayers including the Earned Income Tax Credit (EITC), the Child Tax Credit, and the Working Family Tax Credit.

Recent changes to the tax code have made it increasingly important for tax filers and service providers to learn more about significant financial benefits available through filing a tax return. Tthe Legal Aid Society of Minneapolis and Children's Defense Fund Minnesota bring you this workshop with support from AccountAbility Minnesota.

Legal Aid Society of Minneapolis

The Legal Aid Society of Minneapolis is a division of Mid-Minnesota Legal Assistance and provides free legal assistance to low-income individuals. The MMLA Tax Project began in July 2000 to assist taxpayers involved in controversies with the Internal Revenue Service. MMLA offers educational workshops for service providers and low-income and non-English speaking taxpayers. The MMLA Tax Project provides legal representation, but does not prepare annual tax returns. *See* page 27 for income guidelines and contact information.

Children's Defense Fund Minnesota

Children's Defense Fund (CDF) Minnesota engages, mobilizes and motivates Minnesotans to consider the well-being of children in all private and public decision making so no child is left behind. Its staff focus includes increasing the number of children covered under health insurance, working to improve policy towards family-friendly initiatives, and providing research on the status of children in our state. CDF Minnesota is a private organization supported by foundations, corporate grants and individuals. CDF Minnesota does not accept government funds. See page 28 for contact information.

AccountAbility Minnesota

AccountAbility Minnesota, a nonprofit organization, has offered free tax assistance to low-income taxpayers for 30 years. AccountAbility Minnesota provides tax services at many Twin Cities and Greater Minnesota locations from February through April each year and throughout the year for taxpayers with special tax concerns. *See* page 27 for income guidelines and contact information.

About this handbook

This handbook is not a comprehensive tax guide or a legal reference. Some important aspects of the tax code may not be included. Please consult a tax practitioner, the Internal Revenue Service or Minnesota Department of Revenue for specific tax information.

Taxable Income

What is taxable income?

Taxable income is any income that the government taxes. In general, most income *earned* from a job or self-employment is taxable, as is interest, dividends, and money received from rental property. Generally, income from public assistance is *not* taxable, nor are gifts and inheritances. As always, there are exceptions. Listed below are the primary categories of taxable and nontaxable income.

Taxable Income	**Nontaxable income**
Wages (Form W-2)	Welfare payments such as MFIP, GA, SSI, and MSA
Interest/dividends/capital gains on savings accounts or other investments (Form 1099-B, 1099-DIV, 1099-INT)	Social Security benefits (unless taxable income exceeds certain income levels)
Income from services as an independent contractor (Form 1099-MISC)	Gain from the sale of primary residence (unless gain is over $250,000)
Income from rental property	Gifts and inheritances
Income from a business	Child support payments
Pension/IRA distributions (if not rolled over to another pension plan or IRA) (Form 1099-R)	Generally, accident, health and life insurance proceeds
Unemployment benefits (Form 1099-G)	
Alimony	
Prizes/Awards	
Certain Scholarships	

Did you know . . . .
Generally, a tax refund is not considered income for public assistance calculations during the month it is received. In the second month after a tax refund is received, the amount of any unspent refund is considered an asset for the purpose of calculating public assistance.

Taxpayers receiving public assistance should keep receipts for items purchased with their refunds.

For more information:
IRS Publication 525

Credits and Deductions

What is a deduction?

A deduction reduces the *income* on which you pay tax.

What is a credit?

A credit reduces, dollar for dollar, the amount of *tax* you pay. Credits can be refundable or non-refundable.

Non-refundable credits
A non-refundable tax credit can reduce tax to zero. Any further credit is lost. The federal Child and Dependent Care Credit is a non-refundable credit. If your tax is $100 and your Child and Dependent Care Credit is $400, the credit would reduce tax to zero; the remaining $300 is lost.

Refundable credits
A refundable credit can reduce your tax below zero and result in a refund. The Earned Income Tax Credit is a refundable credit. If your tax is $100 and your Earned Income Tax Credit is $400, the credit reduces your tax to zero and the additional $300 is refunded. That's why it's called a refundable credit, or sometimes a negative income tax.

Did you know . . . .
Many taxpayers have zero taxable income after deductions and exemptions. However, they may be eligible for refundable credits. For this reason it is important for taxpayers with zero taxable income to file a tax return in order to receive the benefits of refundable credits including the Earned Income Tax Credit.

If a taxpayer has not filed a previous year's tax return, most tax credits can be claimed for up to three previous years by filing a return.

If a taxpayer filed an incorrect return, tax credits can still be claimed for up to three years by filing an amended tax return.

Filing Status

What is a filing status?

Filing status is a category of tax filing that determines a taxpayer's:

- Filing requirement
- Standard deduction amount
- Tax rate
- Eligibility for credits and deductions

Primary status options include single, married filing jointly, married filing separately and head of household. The requirements and deduction amounts for each are shown below.

Single

- Standard deduction for 2002 -$4,700.
- Must be considered unmarried on December 31.

Married Filing Jointly

- Standard deduction for 2002 -$7,850.
- Married on or before December 31. If a spouse dies during the year, the taxpayer can claim this status for that year only.
- Generally more financially advantageous than married filing separately.

Married Filing Separately

- Standard deduction for 2002 -$3,925.
- Married on December 31 but choose to file a separate tax return from your spouse.
- Even if otherwise eligible, **cannot** claim the Earned Income Tax Credit, Child and Dependent Care Credit or federal or state education credits.
- If otherwise eligible, **can** claim the Child Tax Credit.

Head of Household

- Standard deduction for 2002 -$6,900
- Considered unmarried **or** did not live with your spouse for at least the last six months of the year.
- Paid for over half the cost of keeping up a home for a relative (child, grandchild, stepchild, parent, brother, sister) who lived in that home for more than half of the year.
- May not file as Head of Household if government assistance, such as MFIP or SSI exceeds earned income. In this case, support of the children is considered to have come from the government, not the taxpayer.
- Further exceptions and complexities of this filing status make it particularly vulnerable to IRS scrutiny, especially if two or more unmarried adults live in the same household. Please consult a tax advisor.

For more information:
IRS Publication 501

Exemptions and Dependents

What is an exemption?

Exemptions (like deductions) reduce taxable income. For 2002, taxpayers receive a $3,000 exemption for themselves and their spouse, and an additional $3,000 for each qualifying dependent.

What is a dependent?

To qualify as a dependent, an individual must:

1. be a relative - child, grandchild, parent, brother, sister (closer than a cousin) -or must live with you as a family member all year,

2. not be claimed as a dependent on another tax return,

3. be a U.S. citizen or resident alien, or a resident of Canada or Mexico,

4. have gross income not greater than $3,000 (unless he or she is the taxpayer’s child under age 19 or a full-time student under age 24), and

5. receive over 1/2 of his or her support from the taxpayer. Under this test, taxpayers who receive government assistance in excess of earned income cannot claim the dependent since support is considered to come from the government not the taxpayer.

Some exceptions apply to children of divorced parents.

Did you know . . .
A resident alien or U.S. citizen may claim an exemption for a spouse who is a nonresident alien and had no income. However, if the spouse has an ITIN and not a Social Security number, he or she cannot claim the Earned Income Tax Credit. ***See*** page 16.

Filing Requirements

What are the filing requirements?

Filing requirements determine the level of income at which an individual is required to file a tax return. Requirements vary with filing status and age, as shown below.

If your filing status is:	And at the end of 2002 you were:	Then file a return if income was at least:
Single	under 65 65 or older	$7,700 $8,800
Married filing jointly	under age 65 (both spouses) 65 or older (one spouse) 65 or older (both spouses)	$13,850 $14,750 $15,650
Married filing separately	any age	$3,000
Head of household	under 65 65 or older	$9,900 $11,000

Caution
Self-employed individuals MUST file a tax return if net income exceeds $400.

Did you know . . . .
Even if a taxpayer is not required to file it is often advantageous to file anyway to claim refunds from excess tax withheld from pay and/or to claim refundable tax credits like the Earned Income Tax Credit.

Form W-4 and Income Tax Withholding

What is a W-4 and how is it used?

Workers must complete a W-4 form when beginning a new job. The W-4 lets the employer know how much state and federal income tax to withhold from each paycheck.

It is rarely appropriate to claim exempt from withholding. Only individuals who expect to have a very low income should consider such an option (for example, students).

It is important to claim the correct number of exemptions on the W-4. The more exemptions an employee claims the less tax will be withheld from pay. Generally, an employee should claim one exemption on the W-4 for each exemption allowed on his or her tax return. However, taxpayers may claim more W-4 exemptions if they are eligible for certain tax credits. To make this determination, they should complete the worksheet included with the W-4.

If filing a joint return, married couples should complete the W-4 worksheet together. The spouse with the higher income should claim all exemptions and the other spouse should claim zero exemptions. This way the couple is assured that they will have enough tax withheld from their combined income to avoid a balance due on their tax return.

Caution
Some taxpayers work as independent contractors and have no income tax or FICA tax withheld from their pay.

Independent Contractors should be aware that this type of work will likely result in a large tax liability at the end of the year or a quarterly filing requirement. Please consult a tax advisor.

Did you know . . .
If an individual has both self-employment income and a salaried job, he or she may choose to increase the amount of withholding from the salaried job to cover self-employment tax.

Employees can change their withholding amounts by completing a new W-4 at any time during the year and as many times as they would like.

For more information:
IRS Publication 1779

Social Security and Individual Taxpayer Identification Numbers

What is a Social Security number?

A Social Security number is a 9 digit number issued by the Social Security Administration. The number is used to track workers' earnings over their working life. It also serves as proof of the right to work in the United States.

All taxpayers must have a valid Social Security number (SSN) or an Individual Taxpayer Identification Number (ITIN) to file a tax return. Most U.S. citizens and resident aliens have valid Social Security numbers.

What is an ITIN?

An ITIN is an Individual Taxpayer Identification Number. An ITIN allows an individual who does not have a Social Security number to file a tax return.

Undocumented workers do not have Social Security numbers. Nevertheless they must comply with tax law by filing a tax return in each year they earn income. Indeed it is in their best interest to do so to avoid an IRS inquiry and to possibly qualify for legal status and/or citizenship in the future should the opportunity arise. In order to file, these workers must first apply for an ITIN. **The IRS is prohibited by disclosure laws from disclosing information about tax filers to the Immigration and Naturalization Service (INS).**

Individual Taxpayer Identification Numbers

How to apply for an ITIN

Tax filers should go to an IRS Walk-in office with two original documents included in the following list and complete a form W-7. Forms are also available on the internet in English and Spanish. IRS Walk-in offices are listed on page 26.

Two of the following original documents are required:

- Passport
- Birth Certificate
- Baptismal Certificate
- Marriage Certificate
- Military or voter's registration
- U.S. or foreign driver's license
- State ID card
- Medical card
- Medical records
- School records

More about ITINs

- ITINs are not valid for employment purposes.

- An ITIN allows the personal exemption for the primary filer, spouse and all dependents. Both spouses and all dependents must have either an ITIN or SSN to be listed on the tax return. But remember -to be claimed as a dependent- individuals must be U.S. citizens or residents of North America.

- ITIN filers may claim the Child Tax Credit (with certain requirements) and the Adoption Credit.

- ITIN filers cannot claim the Earned Income Tax Credit (EITC) or Advanced Earned Income Tax Credit. To be eligible for the EITC, the taxpayer and all qualifying children must have valid Social Security numbers. If the taxpayer (and the spouse if they live together during the last six months of the tax year) does not have a valid Social Security number, the EITC will not be allowed.

- An undocumented worker will probably receive W-2s from each job he or she held showing invalid Social Security numbers. Income from these W-2s should be reported on the return -and W-2s attached- so long as all W-2s are for the same individual. The tax filer should use his or her ITIN to file.

Federal Child and Dependent Care Credit

What is the federal Child and Dependent Care Credit?

The Child and Dependent Care Credit is a non-refundable credit available to individuals who pay a caregiver to care for their dependent child or disabled child or adult while they work or look for work.

How much is it worth?

The maximum credit amount is:

- $720 for one qualifying dependent
- $1,440 for two or more qualifying dependents

What are the requirements and limitations?

Expenses must be for qualifying dependents and be work-related. There are no income limitations.

Qualifying dependent

- Child who is under 13 and can be claimed as a dependent or
- Spouse or dependent who is not able to care for himself or herself and
- The individual must live with the taxpayer. For divorced or separated parents, only the custodial spouse is entitled to claim this credit.

Work-Related Expenses

Child and dependent care expenses must be work-related to qualify for the credit. The most common expenses are payments to individual daycare providers or daycare centers. Payments must be paid by the taxpayer. Subsidized amounts are not eligible for the credit. Expenses are considered work-related only if both of the following are true.

- They allow the taxpayer (and spouse if married) to work or look for work, and
- Expenses must be to provide care for a qualifying person.

Filing Status

If filing status is Married Filing Separately, taxpayers cannot take the Child and Dependent Care Credit.

How to apply

If filing Form 1040, complete Form 2441.
If filing Form 1040A, complete Schedule 2.

For more information:
IRS Publication 503

Federal Child and Dependent Care Credit

Care providers must be identified

To claim the Child and Dependent Care Credit, all persons or organizations providing child care must be identified on Part I of Form 2441 (Form 1040) or Schedule 2 (Form 1040A). The name, address and Taxpayer ID Number of the daycare provider must be included.

If the daycare provider is an individual, the taxpayer identification number may be his or her Social Security number, Individual Taxpayer Identification Number, or employer identification number. If the care provider is an organization, then it is the employer identification number (EIN).

If the taxpayer receives pre-tax dependent care benefits through work, the amount received (as reported on the W-2) will reduce the eligible expenses for calculation of this credit.

Did you know . . . .
The amount of the credit depends on the taxpayer's income and expenses incurred for dependent care.

A percentage is applied to daycare expenses to determine the credit. The rate depends on income and ranges from 10 to 30 percent. Qualifying expenses are limited to $2,400 for one child and $4,800 with two or more children. The maximum credit for a family with one child is $720 ($2,400 x 30%); for two or more it is $1,440 ($4,800 x 30%).

Minnesota also offers a Child and Dependent Care Credit. ***See*** page 20.

Federal Hope Scholarship and Lifetime Learning Credits

What are the Hope Scholarship and Lifetime Learning Credits?

The Hope Scholarship and Lifetime Learning Credits are non-refundable credits intended to offset post-secondary education expenses.

The Hope Scholarship credit is mainly for first and second year college students. It is available for only two years per eligible student.

The Lifetime Learning credit applies to students of all levels at most post-secondary institutions. It is available for an unlimited number of years.

How much are they worth?

Hope Credit
The Hope Credit is 100% of the first $1,000 in education expenses and 50% of the next $1,000. The maximum credit is therefore $1,500 (100% x $1,000 + 50% x $1,000).

Lifetime Learning Credit
The Lifetime Learning credit is 20% of education expenses up $5,000 of expenses paid. The maximum credit is $1,000 (20% x $5,000).

Federal Hope Scholarship and Lifetime Learning Credits

What are the requirements and limitations?

Income limitations (both credits)

- For Single or Head of Household taxpayers, the credits begin to phase out when Adjusted Gross Income reaches $40,000 and are completely eliminated at $50,000.
- For Married Filing Jointly, the credits begin to phase out at $80,000 and are completely eliminated at $100,000.

Qualifying Expenses (both credits)

Tuition and other fees required for enrollment or attendance at an eligible educational institution. Most universities and colleges, including community colleges, are accredited institutions. Expenses that **do not** qualify: books, room & board, student activities, athletic fees, insurance, equipment, and transportation.

Who is eligible (both credits)

Taxpayer, spouse or dependent. If an individual is a dependent of another, he or she may **not** take the credit even if s/he actually pays for school.

Student enrollment (both credits)

- The student must have been enrolled at an eligible educational institution for at least one academic period during the year.

Hope Credit Only

- The student must have taken at least one-half of the normal full-time workload for his or her course of study for at least one academic period beginning in 2002.
- Student must be enrolled in a program that leads to a degree, certificate, or other recognized credential.

Filing Status

Taxpayers cannot take these credits if filing status is Married Filing Separately.

How to apply

Complete Form 8863 and include with form 1040 or 1040A.

Did you know . . .
The expenses for any student for whom the Hope Credit is claimed are not eligible for the Lifetime Learning Credit.

For more information:
IRS Publication 970

Federal Child Tax Credit

What is the Child Tax Credit?

The Child Tax Credit was new in tax year 1998 and changed significantly in tax year 2001. It applies to taxpayers with dependent children age 16 or younger as of December 31. The Child Tax Credit is a non-refundable credit if the taxpayer can take advantage of the full amount. If not, then the credit may be refundable if the taxpayer's income exceeds $10,000.

How much is it worth?

For 2002, $600 per child.

What are the requirements and limitations?

Income limitations

Married Filing Joint
- begins to phase out at $110,000
- completely eliminated at $120,000

Single or Head of Household
- begins to phase out at $75,000
- completely eliminated at $85,000

Married Filing Separately
- begins to phase out at $55,000
- completely eliminated at $60,000

Qualifying Children
- Must be a dependent (*See* page 5)
- Under age 17 as of December 31
- Must be a son, daughter, adopted child, grandchild, stepchild, brother, sister, stepbrother, stepsister, a descendant of any such individual who the taxpayer cares for as the taxpayer's own child, or eligible foster child (*See* page 17)
- Must be a U.S. citizen or resident alien

How to apply

The Child Tax Credit is calculated on a worksheet found in the 1040A or 1040 instruction booklet. Fill in the appropriate line on Form 1040A or Form 1040. If a taxpayer is not able to take full advantage of the non-refundable credit, and their income was over $10,000, then they may also need to fill out form 8812.

Federal Earned Income Tax Credit

What is the Earned Income Tax Credit?

The Earned Income Tax Credit is a refundable credit available to people who have earned income below a certain amount and meet other eligibility criteria. In the tax year 2001, over $310,456,000 was claimed in EITC by Minnesota taxpayers.

How much is it worth?

For 2002, the EITC can be as much as $2,506 for taxpayers with one qualifying child; $4,140 for taxpayers with two or more qualifying children; and up to $376 for taxpayers without a qualifying child.

Income limitations

Tax filers are eligible for the EITC if their earned income from either a job or self-employment does not exceed:

- $29,201 with one qualifying child (or $30,201 if married filing jointly)
- $33,178 with more than one qualifying child (or $34,178 if married filing jointly)
- $11,060 with no qualifying child (or $12,060 if married filing jointly). If you have no qualifying children, you must be at least 25, but under age 65 as of December 31.

Qualifying Children

Qualifying children include all of the following:

- Son, daughter, adopted child, grandchild, stepchild, brother, sister, stepfather, or stepsister, a descendant of any such individual who the taxpayer cares for as the taxpayer's own child, or eligible foster child.

See page 17 for the definition of an eligible foster child

- Must be under 19 years or, if a full-time student, under 24 and any age if totally and permanently disabled.
- Must have lived with tax filer for *more than half* of the year in the United States.

Taxpayer I.D. number

The taxpayer, spouse and qualifying children must have valid Social Security numbers to claim the EITC. If the taxpayer or spouse is filing with an ITIN, the credit cannot be claimed.

Filing status

Taxpayers filing Married Filing Separately cannot claim EITC.

Investment Income

Investment income including interest and dividends cannot exceed $2,550.

Citizenship and foreign income

To claim the EITC, a taxpayer must be a U.S. citizen or resident alien for all of 2002 and cannot have earned income from a foreign country.

Federal Earned Income Tax Credit

How to apply

With a qualifying child, complete schedule EIC. This schedule requires the children's name, birth date, Social Security number, and the number of months the child lived with the taxpayer during the year.

The calculation of the credit can be completed on the worksheet found in the IRS instruction book. The completed worksheet should not be included with the return.

Eligible Foster Child

An eligible foster child is a child placed by an authorized placement agency. The foster child must live with the taxpayer for over six months of the year and meet age requirements. Prior to 2002, a foster child must have lived with the taxpayer for the entire year.

The new definition is more restrictive than in years prior to tax year 2000 when an adult could claim a distantly related or an unrelated child for EITC if he or she cared for the child as if s/he was his or her own. The most common situations occurred when two unmarried adults lived together and cared for a child related to only one of the adults or where the taxpayer may be taking care of younger cousins or more distantly related relatives. Under the new law, the unrelated person cannot claim the child for EITC purposes.

Tiebreaker Rule:

If a child meets the definition of a qualifying child for more than one taxpayer, and only one of those taxpayers is their parent, then the parent is the only person who can claim the credit.

If a child meets the definition of a qualifying child for more than one taxpayer, and more than one of those taxpayers is their parent, then the parent who lived with the child the longest is the only person who can claim the credit.

If a child meets the definition of a qualifying child for more than one taxpayer, and more than one of those taxpayers is their parent, and they lived with each parent for the same amount of time (must be over 6 months of the year), then the parent with the highest income is the only person who can claim the credit.

For more information:
IRS Publication 596

Federal Advanced Earned Income Tax Credit

What is the Advanced Earned Income Tax Credit?

The Advanced Earned Income Tax Credit is advanced payments of estimated Earned Income Tax Credit. The payments are received as an addition to the employee's paycheck each pay period throughout the calendar year.

Who qualifies?

The taxpayer must:

- have at least one qualifying child
- expect total family income to be less than $29,000
- expect to be eligible for the Earned Income Tax Credit
- be a U.S. citizen or resident alien for the entire year

How to apply

Complete a Form W-5 and submit it to the employer. Each paycheck will be increased by a *portion* of the anticipated credit. Employers cannot pay more than $1,457 to one taxpayer in AEITC during 2002. This amount will increase slightly for 2003.

Form W-5 expires at the end of each year. A new W-5 must be completed each year to continue receiving payments.

Caution
Taxpayers are required to file a tax return for any year in which they receive AEITC payments. It is possible that a taxpayer's AEITC payments will exceed actual EITC for which he or she qualifies. In this case, the taxpayer may owe the IRS at year's end. This may occur if circumstances change which impact the taxpayer's eligibility. (For example, a child moves out of the house after only four months into the year.)

Federal Saver's Tax Credit

What is the Saver's Tax Credit?

This is a new tax credit for 2002.

Some contributions to retirement plans or Individual Retirement Accounts (IRA's) are not taxable and are not used to calculate the EITC or the Child Tax Credit.

In addition, the Saver's Tax Credit reduces or eliminates the income tax a taxpayer may owe, and encourages taxpayers to contribute to retirement plans or IRA's. A taxpayer can receive a tax credit of up to 50 percent of a maximum $2,000 contribution.

For example, if a taxpayer makes a $1,000 contribution to their retirement plan, their taxable income is reduced by $1,000. They may also claim a $500 credit.

Who is eligible?

- must be at least 18 years of age
- must not be a full time student
- must not be claimed as a dependent on someone else's tax return

Income limitations:

A taxpayer's adjusted gross income must be no higher than:

- $50,000 if married filing jointly
- $37,000 if filing as head of household
- $25,000 if filing single, or married filing separately

Example:

Paul and Laura are married, with two children and earned $24,000 in 2002. Normally, they would owe income tax of $415 and qualify for an EITC of $2,143 in 2002. But they made a $1,000 contribution to Paul's retirement plan at work. This reduced their taxable income to $23,000 and lowered their income tax to $315. The tax will be eliminated by the Saver's Tax Credit, which is worth up to 50 percent of their $1,000 retirement contribution. Also, under new EITC rules in 2002, they will figure their EITC based on $23,000 in taxable earnings. This boosts their EITC to $2,354. By making a $1,000 retirement contribution, Paul and Laura get a tax benefit of $626 (elimination of $415 income tax, plus $211 more from the EITC).

Minnesota Child and Dependent Care Credit

What is the Minnesota Child and Dependent Care Credit?

The Minnesota Child and Dependent Care Credit is a refundable credit available to taxpayers who pay for care of their dependent child under age 13 or disabled older child or adult dependent while they work or look for work.

How much is it worth?

Amounts vary based on income. The maximum credits are the same as the federal credit:

- $720 for one qualifying dependent
- $1,440 for two or more dependents

The state child care credit cannot exceed the allowable federal child care credit. For example, if the federal child care credit is $400 and the calculated Minnesota child care credit is $1,440, the allowable Minnesota child care credit is $400.

What are the requirements and limitations?

Work-related expenses and qualifying dependents

Rules for work-related expenses and qualifying dependents are the same as those for the federal Child and Dependent Care Credit. *See* page 10.

Income limitation

You are eligible if your 2002 household income is less than $32,250. *See* definition of Household Income on page 24. This varies from the federal credit which has no income limit.

How to apply

The Minnesota Child and Dependent Care Credit is applied for on Form M-1CD and attached to Form M-1.

Did you know . . .
The Minnesota Child and Dependent Care Credit is refundable. The federal Child and Dependent Care Credit is non-refundable. As a result, a taxpayer with zero taxable income could not receive the federal credit, but may still claim the Minnesota Child and Dependent Care Credit. In this case, the federal Form 2441 or Schedule 2 must be completed (even though it will not be included with the federal return) and attached to the state return.

Attention new parents
The state gives a special bonus to families with babies born in 2002. Married couples who file a joint return are entitled to this credit even if they paid no daycare expenses. Consult a tax advisor.

Minnesota Working Family Credit

What is the Minnesota Working Family Credit?

The Minnesota Working Family Credit is the Minnesota counterpart to the federal Earned Income Tax Credit. It is a refundable credit based on earned income and number of qualifying children. There is a small credit for childless taxpayers.

How much is it worth?

For 2002, the maximum credit is $750 for a family with one child, $1,447 for a family with two or more children, and $94 for adults without children.

What are the requirements and limitations?

Qualifications for the Minnesota credit are the same as the federal Earned Income Tax Credit. *See* page 16.

How to apply

Complete Form M-1WFC and attach it to Form M-1. The calculation of the credit is based on information from the federal EITC worksheet and the Working Family Credit tables found in the M-1 instructions.

Did you now . . .
Part-year residents must adjust the credit based on the portion of the year spent in Minnesota. See the M-1NR requirements for part-year residents and nonresidents.

Taxpayers disqualified from the federal Earned Income Tax Credit due to fraud may still qualify for the Minnesota Working Family Credit.

If a taxpayer fails a federal EITC audit, the IRS will notify Minnesota and a WFTC audit will likely follow.

Minnesota K-12 Education Credit

What is the Minnesota K-12 Education Credit?

The Minnesota K-12 Education Credit is a refundable credit available for low-income families that paid certain educational expenses for their children. For 2002, this credit has been reduced from 100% of eligible expenses to 75% of eligible expenses.

How much is it worth?
The maximum credit is $1,000 per child and $2,000 per family.

What are the requirements and limitations?

Income ceiling
The credit begins to phase out when household income reaches $33,500 and is completely eliminated at $37,500.

Qualifying children
A qualifying child need not be a dependent, but must meet the definition of a qualifying child under the Earned Income Tax Credit. *See* page 16.

Qualifying schools
Your child must be attending public, private, or home school and be in grades K-12.

Qualifying expenses
The following expenses qualify for the credit. Private school tuition does not qualify for the credit, however, it does qualify for the subtraction. *See* page 23.

- Tutoring
- Academic books and materials
- Fees paid to others for transportation
- Music lessons
- After school enrichment programs
- Home computer hardware or educational software (limit: $200)
- Academic summer camp
- Purchase or rental of long-life equipment such as calculators or musical instruments

Filing status
You cannot claim this credit if you file Married Filing Separately.

How to apply
Complete schedule M-1ED and attach to M-1. Keep all receipts for 2002 educational expenses.
This credit is heavily audited.

Minnesota K-12 Education Subtraction

What is the Minnesota Education Subtraction?

The education subtraction, like a deduction, allows parents to deduct from their taxable income certain expenses paid for K-12 education for their dependents.

How much is it worth?

The maximum subtraction for students in grades K-6 is $1,625. For students in grades 7-12 it is $2,500. There is no family limit. Therefore, if a parent pays 8.5% tax on income, the maximum tax savings would be $138 for a K-6 student or $212.50 for a 7-12 student.

What are the requirements and limitations?

Income ceilings

Families at all income levels are entitled to a subtraction.

Qualifying child

Same as Earned Income Tax Credit. *See* page 16.

Qualifying expenses

All expenses eligible for the credit are also eligible for the subtraction. See page 22 for a list of qualifying expenses. In addition, private school tuition qualifies for the subtraction.

How to apply

Simply subtract your education expenses from income on Form M-1. Keep all receipts for 2002 education expenses.

How do the credit and subtraction work together?

If education expenses exceed the family limit for the credit, the excess can be applied to the subtraction. Tax filers can then add this excess to any private school tuition paid -which does not qualify for the credit, but does qualify for the subtraction-and subtract the total. The 25% of expenses not refunded by the credit cannot be used for the subtraction.

What are the differences between the credit and the subtraction?

Household income must be below $37,500 for the credit. There is no income limit for the subtraction.

All education expenses that qualify for the credit also qualify for the subtraction. Private school tuition does not qualify for the credit, but does qualify for the subtraction.

The credit has a $2,000 family limit. There is a per child limit for the subtraction, but no family limit.

Minnesota Property Tax Refund

What is the Minnesota Property Tax Refund?

The Property Tax Refund is a refund of overpayment of property taxes based on income and property taxes paid and is available to homeowners and renters. The refund is applied for annually on the yellow Property Tax Refund Return M-1PR.

How much is it worth?

Refund amounts decline as income increases. Refund amounts also decline as property taxes or rent decline.

- Renters maximum refund: $1,190
- Homeowners maximum refund: $1,450

What are the requirements and limitations?

Total household income must be less than:

- $43,250 for renters
- $80,180 for homeowners

The taxpayer also must:

- Not be claimed as a dependent on someone else's current tax return
- Have been a full or part year resident of Minnesota
- Have paid rent or property taxes on their principal place of residence or home

What documentation is needed?

Renters need to obtain their 2002 CRP from their landlord. Homeowners need their Statement of Property Taxes Payable for 2003 from their county office. The statement should be mailed in March 2003.

What is household income?

Household income has a specific meaning for purposes of the Property Tax Refund. It is also used to determine eligibility for the Minnesota Child and Dependent Care Credit and the Minnesota K-12 Education Credit.

Generally, household income includes income from both taxable or nontaxable sources. Government assistance including MFIP, SSI, and MSA are all included in household income, as are Social Security benefits. Also included are contributions to pension and IRAs which are subtracted from income on a federal tax return. The value of food stamps, assistance that goes directly to children, child support, and federal tax refunds are not included in household income.

For the property tax refund, a dependent may be claimed even if they receive more support from the government than the taxpayer (such as MFIP or SSI).

Did you know . . .
The property tax refund can only be claimed for up to one year after the filing deadline. For 2002, the filing deadline is August 15, 2003.

Documentation

Documents required to complete tax returns

Bring the following items to your tax preparer. If Married Filing Jointly, bring applicable items for both spouses.

Last year's tax return is helpful and highly recommended but is usually not mandatory.

Year-end statements that show income received including:

- W-2s from all jobs.
- 1099s for income from work as an independent contractor.
- 1099s for bank interest, dividends, tax refunds, gambling winnings, etc.
- 1099s for Social Security payments, pension or IRA distributions
- Income from unemployment compensation
- Statements that show nontaxable income including MFIP, SSI, and MSA. Income from these sources is not taxable, however, the amounts are used in the calculation of several tax credits and refunds.

See list of taxable and nontaxable income sources on page 2.

Year-end statements for homeowners

- Mortgage interest payments
- Real estate taxes paid-often found on mortgage statements
- State income taxes paid during the year from W-2s and last year's tax return

Amounts of certain expenses including:

- Educational expenses, (keep all receipts for your records) 1098-E, and 1098-T
- Self-employed individuals need a record of business expenses including car mileage and information about car make and model
- Charitable contributions

Taxpayer's and children's Social Security numbers or ITINs and birthdates

- Bring Social Security cards if available

Minnesota Property Tax Refund requires:

- Renters -CRP from landlord
- Homeowners -Statement of Property Taxes payable in 2003
- County benefits statement if taxpayer(s) received MFIP

IRS and Minnesota Department of Revenue Information

Internal Revenue Service

Tax Information	1-800-829-1040
Automated refund info	1-800-829-4477
Tax Forms or Pubs	1-800-829-3676
Taxpayer Advocate	1-877-777-4778

Metro Area Walk-in Offices

Federal Courts Building
Room 385
316 North Robert Street
St. Paul, MN 55101

Towle Building
Skyway -Room 275
330 Second Avenue South
Minneapolis, MN 55401

2001 Killebrew Drive
Room 239
Bloomington, MN

Web site

www.irs.gov

Taxpayer Education Department

EITC Coordinator 651-312-7636

Call to request:
- Translated EITC information
- A tax information session at your agency

Minnesota Department of Revenue

Individual Income Tax	651-296-3781
Tax forms	651-296-9118
Free tax clinic locations	651-297-3724
Taxpayer Advocate	651-296-0992
TDD	612-297-2196
Collection/bills	651-296-3457
Practitioners hotline	651-297-2499

The Department of Revenue no longer has toll free numbers.

Web site

www.taxes.state.mn.us

AccountAbility Minnesota and Legal Aid Society of Minneapolis

AccountAbility Minnesota

2314 University Avenue
Suite 12
St. Paul, MN 55114

General Information	651-287-0187
Fax	651-287-0190

Web site: www.accountabilitymn.org

Free Assistance Income Guidelines

Family Size	Income
Single	$25,000
Family	$35,000

Legal Aid Society of Minneapolis

430 First Avenue North
Suite 300
Minneapolis, MN 55401

General Information	612-332-1441
Intake	612-334-5970
Fax	612-334-5755

Free Assistance Income Guidelines

187.50% of Federal Poverty Guidelines

Children's Defense Fund Minnesota

200 West University Avenue, Suite 210
St. Paul, MN 55013

General Information: 651-227-6121

Fax: 651-227-2553

web site: www.cdf-mn.org

Volunteer Income Tax Assistance (VITA)

Volunteers provide free tax preparation assistance to low income families and individual taxpayers during the filing season. To find a local site contact:

First Call For Help: 1-800-543-7709

MN Department of Revenue:651-297-3724

A taxpayer may also go to a local IRS walk-in site to have their taxes prepared. To find a local office, look in the blue section of the phone book.