

Western New England University
College of Business
AC 413-01 – Fundamentals of Individual Tax
Fall 2020

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**TERM PROJECT
TAX RETURN AND CLIENT LETTER**

I. PURPOSE

The purposes of this project include giving you practice with preparing a federal income tax return as well as practice with research, writing, and at your own option, teamwork.



II. FACT PATTERN

A. Introduction

Below is the fact pattern. Your goals are to prepare the 2020 federal income tax return and a client letter for your long-time client and friend, Jennifer M. Green.

B. Jennifer's Year-End Status

Jennifer was age 42 and in good health at the end of 2020. Jennifer was a WNE University pharmacy school alumna. She was currently working a good job as a pharmacist with the Big Y grocery chain.

Jennifer took care of her widower father, Leonard Green, age 66. Jennifer, Leonard, and Jennifer's children, discussed in divorce section below, lived with Jennifer in her home throughout all of 2020. Jennifer paid the mortgage payments of \$2,400 per month for the home. Leonard's sole source of income was Social Security benefits totaling \$18,000 per year.

C. Form W-4

During the current year, Big Y paid Jennifer a salary of \$90,000. Big Y withheld from Jennifer's paychecks federal income tax withholdings of \$7,500, and state income tax withholdings of \$3,800.

D. Divorce

On January 1, 2020, Jennifer officially, by a court decree, divorced her now ex-husband Anthony Rivera. Anthony worked as a doctor for Baystate Hospital. The decree awarded Jennifer custody of their three children: Alexandra, Carlita, and Juan Rivera.

The children were in school full-time and were ages 20, 17, and 13, at the end of the 2020, and were properly Jennifer's dependents. The decree ordered Anthony to pay Jennifer child support of \$400 per child (\$1,200 combined) per month. The decree also required Anthony to pay Jennifer monthly alimony of \$500 per month. Anthony was timely on the twelve payments in 2020.

The divorce decree also ordered Anthony to transfer 40 percent of his Traditional 401(k) account balance to Jennifer. On January 15, 2020, immediately before the transfer, Anthony's account had a \$500,000 balance with a zero basis. Therefore, on that same day, Anthony properly transferred \$200,000 to a Traditional 401(k) account for Jennifer.

E. Capital Gains and Losses

On July 13, 2020, Jennifer sold part of her investment in the Vanguard 500 Index Fund Admiral Shares (VFIAX). Jennifer sold the shares for \$11,000. Her basis in the shares was \$2,000. She had purchased the shares at various times five years ago. Additionally, on September 22, 2020, Jennifer sold part of her shares in the Vanguard Energy ETF (VDE). Jennifer sold the shares for \$5,000. Jennifer's basis in the ETFs was \$9,000. Jennifer had purchased the ETFs at various times many years ago.

E. Gift, Insurance, and Inheritance

During the year, Jennifer's Aunt Freida was dying. On August 8, 2020, Aunt Freida gave her engagement ring to Jennifer. The ring had a \$25,000 FMV and a \$5,000 basis. Aunt Freida died shortly afterward. On September 19, 2020, Jennifer received a \$50,000 check from an insurance company for a life insurance policy that Aunt Freida owned. Additionally, on December 20, 2020, Jennifer also received a \$100,000 from an estate attorney as one of the beneficiaries on Aunt Freida's estate.

F. Wagering Winnings and Losses

Jennifer enjoyed playing the slots and the tables at Springfield's MGM Resorts International casino. Jennifer received a Form W-2G from the casino showing line 1 reportable winnings of \$2,500 and line 4 federal income tax withholdings of \$500 for 2020. Upon Jennifer's request, MGM sent to Jennifer her players club card statement. The statement established that Jennifer had gambling losses of \$6,000 for 2020.

D. Jennifer's Personal Expenses

Jennifer's personal expenses during 2020 included the following payments:

- a. Unreimbursed qualified medical expenses for herself and her dependents = \$ 3,600.
- b. Mortgage principal on home = \$ 8,100.
- c. Mortgage interest on home = \$ 12,600.
- d. Property taxes on home = \$ 9,300.
- e. Homeowner's insurance = \$ 2,100.
- f. Sales tax payments for the year = \$2,700.
- g. Charitable contribution by check to WNE University = \$ 2,000.

III. FEDERAL INCOME TAX RETURN

Upload for your entire team one Form 1040, U.S. Individual Income Tax Return and supporting schedules for 2020. Upload the tax return to Kodiak as one single document, not schedule by schedule. Complete all the pertinent information on the forms, e.g., principal business code on Schedule C.

A. At a minimum, include the following forms:

- Form 1040, U.S. Individual Income Tax Return, and accompanying numbered schedules.
- Schedule 1, Additional Income and Adjustments to Income
- Schedule 3. Additional Credits and Payments
- Schedule A, Itemized Deductions

B. Simplifying the Return

To make this project easier for you, disregard the Alternative Minimum Tax. Also, do not prepare the State income tax return. Do not compute any underpayment of income tax penalty even if it would apply. Do not prepare anyone else's tax return.

IV. CLIENT LETTER

A. Overview

Upload one client letter from your entire team. Begin with a warm opening and end with friendly closing. Jennifer is, after all, a friend and a client that your firm wants to retain.

B. Required Topics

The client letter must explain to Jennifer the amounts, tax consequences, for each of the following topics. Include the pertinent Internal Revenue Code sections.

1. Divorce: Child support, alimony, and property settlement (Anthony's transfer to Jennifer).
2. Capital gains and losses.
3. Gifts, insurance, and inheritance.
4. Wagering winnings and losses
5. Itemized versus standard deduction. For the itemized deduction, explain the allowable individual components.
6. Child tax credit

C. One Additional Required Topic – 401(k) to IRA

As noted above, Jennifer's ex-husband, Anthony, transferred to Jennifer part of his 401(k) account. Jennifer asked you about a Roth IRA. Explain in the client letter the pros, cons, and tax consequences if Jennifer were to convert the funds to a Roth IRA. Tell her whether there are any restrictions or limitations applicable to her on this type of conversion. Explain to Jennifer what is your recommendation regarding a conversion to Roth, good idea or bad, and crucially, explain why. Regardless of your recommendation, suppose Jennifer did decide to convert the funds. Explain whether you'd then recommend that Jennifer convert all of the funds in one year, or a series of smaller conversions over multiple years. Explain the difference in tax consequences of the two alternatives regarding years.

VI. RESEARCH, FOOTNOTES, BIBLIOGRAPHY

Each student must show proficiency in research by providing a minimum of *three* quality sources from separate authorities. More than one reference from the same source or Code section count as only one source. Quality sources will merit a higher grade than

quick Internet grabs. Students can provide more than three sources for a better grade in research. Three's just the minimum.

Document the sources using footnotes, not endnotes. Do not use APA or MPL format. Use instead Harvard's Bluebook, which is the format that the legal and accounting professions widely prefer. Don't stress over minute details of the Bluebook. The main objective is to simply aim for footnotes that fully identify each source. Likewise, don't solely provide a URL. A quality footnote should also include, to the extent available, the author, date, title, and publication name. The goal of footnotes is to enable the reader to assess the timeliness and quality of each source, and to find the source if reader desired further investigation.

Include at the end of the client letter include a bibliography. The bibliography should list each student's name and then the sources that the student provided. List only sources that the client letter cited. The sources in descending order of authority, and alphabetical or numeric order within each category. To save time, usually students can usually simply copy and paste the citations from their footnotes.

VIII. WRITING

Use the writing quality that a professional would wield. To prevent the letters from becoming too long, and too burdensome, for the text of the letter, **the word limit is 2,399 words**. Words in the footnotes and the bibliography do not count toward the limit, but to help minimize the work, students shouldn't add too many words there either. Students working in teams may add 200 words for each teammate beyond one. For example, a team of four people would have a limit of 2,999 words. Reserve enough time at the end for editing. Ignore good writing at one's own peril.

VII. GRADING RUBRIC – Quality of:

Tax Return

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| • TR | 30 % |
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Client Letter

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| • Explanation and Analysis | 50 % |
| • Research, Footnotes & Bibliography | 10 % |
| • Writing | 10 % |

Total	<u>100 %</u>
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