Detailed Practitioner Checklist Supplement

Seven Shades of Tax

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Part I – Child-Related Federal Tax Credits

A. Child Tax Credit (CTC)

- **Confirm child is under age 17 at year-end and has a valid SSN.**
- **Child must live with taxpayer more than half the year (temporary absences excluded).**
- **Verify Form 8332 is executed if non-custodial parent claims the credit.**
- **Phaseout: Begins at $400,000 (MFJ) / $200,000 (Single).**
- **Refundable portion for 2025 up to $1,700 per qualifying child (subject to OBBBA).**
- **Confirm income documentation: W-2, 1099, or self-employment earnings.**
- **Advise client IRS disregards court orders absent executed Form 8332.**
- **Retain copies of returns, custody schedules, and separation agreement clauses for audit defense.**

B. Child & Dependent Care Credit

- **Child under 13 or disabled dependent qualifies.**
- **Expenses must enable taxpayer to work or seek work.**
- **Provider cannot be spouse, dependent, or child under age 19.**
- **Both spouses must have earned income unless one is disabled or a student.**
- **Calculate credit on Form 2441 attached to Form 1040.**
- **Eligible expenses: up to $3,000 (one child) or $6,000 (two or more).**
- **Percentage 20–35% based on AGI (lower percentage for higher income).**
- **Include clause allocating which parent may claim and how expenses are reimbursed.**
- **Maintain records: receipts, provider tax ID, and payment proof.**

C. Head of Household (HOH)

- **Taxpayer must be unmarried or 'considered unmarried' on December 31.**
- **Must pay more than half the cost of keeping up the home.**
- **Qualifying person must live with taxpayer more than half the year.**
- **Temporary absences for school or medical care do not break residence.**

- **Parents of dependents can qualify even if child lives elsewhere if maintaining parent's home.**
- **Audit red flag: both parents claiming HOH for the same child.**
- **Include clause clarifying which parent will claim HOH and file consistently.**

D. Earned Income Credit (EIC) 💵

- **Taxpayer must have earned income and valid SSN.**
- **Cannot file 'Married Filing Separately.'**
- **Qualifying child: meets age, relationship, residency, and joint return tests.**
- **2025 income thresholds (approx.): $63,398 for MFJ with 3+ children.**
- **Verify tie-breaker rules for separated parents (custodial parent usually qualifies).**
- **Require annual exchange of income documentation to prevent duplicate claims.**
- **Include clause indemnifying against penalties from inconsistent filings.**
- **Keep custody calendars and proof of residency available for audit.**

Part II – The $500,000 Real Estate Trap 🏠

- **Verify ownership and use tests: owned and lived in 2 of the last 5 years.**
- **If one spouse vacates under agreement, ensure 'use by former spouse' counts (§121(d)(3)(B)).**
- **Confirm §1041 transfer: no gain/loss recognized but basis carries over.**
- **If sale within 3 years of transfer, both may claim combined $500,000 exclusion.**
- **Non-occupying spouse after divorce may lose eligibility after 3 years.**
- **Check for business or rental use – allocate basis and gain accordingly.**
- **Confirm exclusion not used in prior 2 years.**
- **Review Form 1040 Schedule D and maintain HUD-1, deed, and occupancy proofs.**
- **Include clause requiring mutual cooperation and sale certification if sold post-divorce.**
- **Caution: Failure to meet both ownership/use tests can result in full taxable gain for one spouse.**

Appendix – Practitioner References 📚

• IRS Forms: 8332, 2441, 1040, Schedule D

• IRS Publications: 501 (Dependents), 503 (Child and Dependent Care), 504 (Divorced or Separated), 523 (Selling Your Home)

• Code Sections: 26 U.S.C. §§ 24, 21, 2(b), 32, 121, 1041

• Cross-reference: One Big Beautiful Bill Act (OBBBA) and SECURE Act 2.0 updates

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