



Temporary Provisions



Introduction

Some of the provisions contained in this lesson have been commonly referred to as “extenders.” Others are temporary provisions contained in recent legislation. In some instances, these provisions modify only portions of the existing tax law. In those cases, we have included caution statements in the affected lessons redirecting volunteers to explore the temporary modifications in this lesson. The following topics are covered here:

- Child tax credit (CTC) expansion
- Expansion of earned income tax credit (EITC) for taxpayers without qualifying children
- Refundability and enhancement of the child and dependent care credit
- Paycheck Protection Program loans
- Student loan forgiveness
- Business expenses paid to restaurants
- Employer provided educational assistance
- Mortgage insurance premiums deductible as qualified residence interest
- Credit for nonbusiness energy property (residential energy credit)
- Cancellation of debt on a principal residence

Other temporary provisions are included as noted. The recovery rebate credit and the credits for sick and family leave for self-employed individuals were included in the Payments and Miscellaneous Refundable Credits lesson for 2020. They remain in that lesson and are updated for 2021. The 2021 expansion of the premium tax credit (PTC) is covered in the Premium Tax Credit lesson. The deduction for charitable cash contributions by taxpayers who do not itemize is discussed in the Itemized Deductions and Standard Deduction and Tax Computation lessons.

Refer to this lesson, and to the applicable lessons in this publication and tabs in Volunteer Resource Guide for information about the temporary 2021 provisions that follow. In instances where in-depth information was not available when this publication was finalized, a link to the appropriate IRS website is provided. Use those links for the most up-to-date information.

What are the changes to the child tax credit for 2021?

The American Rescue Plan Act (ARPA) of 2021 expands the Child Tax Credit (CTC) for tax year 2021 only. The expanded credit means:

- The amounts of the credit for qualifying children increase for many taxpayers.
- For eligible taxpayers, the credit is fully refundable, which means that taxpayers can benefit from the credit even if they don't have earned income or don't owe any income taxes.
- Taxpayers can receive the credit for qualifying children who turn age 17 (rather than 16) in 2021.
- Eligible taxpayers may receive part of their estimated credit in 2021 before filing their 2021 tax return.

For tax year 2021, families claiming the CTC will receive up to \$3,000 per qualifying child between the ages of 6 and 17 at the end of 2021. They will receive \$3,600 per qualifying child under age 6 at the end of 2021. Under the prior law, the amount of the CTC was up to \$2,000 per qualifying child under the age of 17 at the end of the year.

example

Leonard, a single taxpayer who had a total income of \$24,000, meets all the requirements for an eligible taxpayer to claim the CTC for his two children, Max, age 7 and Tyler, age 3. For 2021, Leonard is eligible for a total CTC in the amount of \$6,600 (\$3,000 for Max and \$3,600 for Tyler)

The maximum credit is available to taxpayers with a modified AGI of:

- \$75,000 or less for singles and married persons filing a separate return,
- \$112,500 or less for heads of household and
- \$150,000 or less for married couples filing a joint return and qualified widows and widowers.

If the taxpayer's modified AGI exceeds these income thresholds, the extra amount above the original \$2,000 credit — either \$1,000 or \$1,600 per child — is reduced by \$50 for every \$1,000 in modified AGI. Also, for eligible taxpayers, the credit is fully refundable for 2021. Before this year, the refundable portion was limited to \$1,400 per child.

Who is eligible for the refundable CTC?

A taxpayer is eligible for the fully refundable CTC if the taxpayer (or the spouse if filing jointly) lived in the United States for more than half of 2021 or is a bona fide resident of Puerto Rico for 2021. If the taxpayer (and spouse if filing jointly) do not meet either of these residency requirements, the taxpayer will still be able to figure and claim a nonrefundable CTC and figure an additional child tax credit instead of the new refundable child tax credit.

example

Juanita and Carlos both lived in the United States for all of 2021. They meet all the requirements for eligible taxpayers to claim the CTC for their three children. The full amount of their CTC is refundable, even if they had no earned income or paid no tax.

What about advance payments of the CTC?

Advance payments of the 2021 CTC were made regularly from July through December to eligible taxpayers who had a main home in the United States for more than half the year. For an eligible taxpayer, the total of the advance payments was 50 percent of the CTC estimated to be allowable for 2021. Advance payments were estimated from information included in eligible taxpayers' 2020 tax returns (or their 2019 returns if the 2020 returns had not been filed and processed when payments were made).

Eligible taxpayers who did not want to receive advance payments of the 2021 Child Tax Credit had the opportunity to decline receiving advance payments. Taxpayers also had the opportunity to update information about changes in their income, filing status or the number of qualifying children.

By the end of January 2022, taxpayers will receive Letter 6419 from the IRS showing the amount of advance payments for 2021. Taxpayers will reconcile the advance payments on their 2021 income tax return and claim any additional credit to which they are entitled. Some taxpayers may be eligible for repayment protection that will excuse them from repaying some or all of the excess amount.

example

Joseph and Carly meet all the requirements (including residency) for eligible taxpayers to claim the CTC for their two children, Peony age 16 and Petunia, age 14 who were enrolled in a post-secondary educational institution at least half-time and for a period of at least five months. Joseph and Carly received a total of \$3,000 in advance CTC payments from July through December 2021. They will claim an additional \$3,000 CTC on their 2021 federal income tax return.

Where can I find answers to additional questions about the CTC?

For up to date information about the CTC and reconciling advance payments, go to <https://www.irs.gov/credits-deductions/advance-child-tax-credit-payments-in-2021>.

What are the changes to EITC for 2021?

For 2021 only, more workers and couples without qualifying children now qualify for the Earned Income Tax Credit (EITC). The maximum credit is nearly tripled for these taxpayers and is, for the first time, made available to both younger workers and senior citizens. In 2021, the maximum EITC for those with no qualifying children is \$1,502, up from \$538 in 2020, and is available to eligible filers with an AGI below \$21,430 (\$27,380 if Married Filing Jointly).

Another temporary change applies to taxpayers with and without qualifying children. For 2021, they are allowed to choose to figure the EITC using their 2019 earned income, as long as it was higher than their 2021 earned income. In some instances, this option will give them a larger credit.

What are the new temporary age limits for the EITC for taxpayers without qualifying children?

The EITC can be claimed by eligible workers who are at least 19 years of age enrolled in school. Students under age 24 who were enrolled in a post-secondary educational institution at least half-time and for a period of at least five months don't qualify. The minimum age for a qualified former foster youth or a qualified homeless youth is 18 years of age. In the past, the EITC for those with no qualifying children was only available to people ages 25 to 64. The upper age limit is eliminated for 2021.

example

Bailey is 20 years old and not enrolled in school. She earned \$14,250 in 2021. Bailey is a U.S. citizen, has a Social Security number, and lived in the United States all year. Her filing status is Single, and she's not the qualifying child or dependent of any other taxpayer. She had no investment income and is not filing Form 2555. Bailey can claim the EITC on her 2021 federal income tax return.

What is a qualified former foster youth or a qualified homeless youth?

The term 'qualified former foster youth' means an individual who was in foster care on or after the date that he or she turned 14 years old.

The term 'qualified homeless youth' refers to an individual who certifies that he or she is either an unaccompanied youth who is a homeless child or youth, or is unaccompanied, at risk of homelessness, and self-supporting.

An individual who meets either of these definitions and qualifies to claim the EITC without a qualifying child under age 19 must check a box on Form 1040 to certify that they meet these requirements.

Where can I get additional information?

Refer to the Earned Income Credit lesson in this publication for additional rules for claiming the EITC.

What are the changes for the Child and Dependent Care Credit (CDCC) for 2021?

The new law increases the amount of the credit and eligible expenses for child and dependent care, modifies the phase-out of the credit for higher earners and makes it refundable for certain taxpayers.

How much CDCC can a taxpayer claim for 2021?

For 2021, the top credit percentage of qualifying expenses increased from 35% to 50%.

In addition, eligible families can claim qualifying child and dependent care expenses of up to:

- \$8,000 for one qualifying person, up from \$3,000 in prior years, or
- \$16,000 for two or more qualifying persons, up from \$6,000 before 2021.

This means that the maximum credit in 2021 of 50% for one qualifying person's qualifying expenses is \$4,000, or \$8,000 for two or more qualifying persons.

How is the CDCC calculated?

When figuring the credit, employer-provided dependent care benefits, such as those provided through a flexible spending arrangement (FSA), must be subtracted from total eligible expenses first and any remaining expenses may be used in calculating the CDCC. For 2021, the maximum amount of tax-free employer-provided dependent care benefits increased from \$5,000 to \$10,500.

As before, the more a taxpayer earns, the lower the credit percentage. But under the new law, more people will qualify for the new maximum 50% credit rate. That's because the adjusted gross income (AGI) level at which the credit percentage is reduced is raised substantially from \$15,000 to \$125,000.

Above \$125,000, the 50% credit percentage is reduced as income rises, plateauing at a 20% rate for taxpayers with an AGI above \$183,000. The credit percentage level remains at 20% until reaching \$400,000 and is then phased out above that level. It is completely unavailable for any taxpayer with AGI exceeding \$438,000.

example

Rose and Bert have one child, Begonia, age 3. They paid \$9,000 in child care expenses while they worked. Their AGI is \$65,000. Rose earned \$30,000 and Bert earned \$35,000. Rose, Bert and Begonia are all U.S. citizens, have valid SSNs, and lived together in the United States all year. Rose and Bert can claim a maximum of \$8,000 in child care expenses, and qualify for the maximum 50% rate. Their refundable credit for child and dependent care is \$4,000.

What about taxpayers who owe no tax?

For 2021, the child and dependent care credit is fully refundable. This means that an eligible family can get it, even if they owe no federal income tax. To be eligible for refundability, a taxpayer, or spouse if filing jointly, must have had a main home in the United States for more than half of the year.

Where can I get additional information?

Refer to the Credit for Child and Dependent Care Expenses lesson in this publication.



The credit for child and dependent care expenses is refundable if the taxpayer, or spouse if married filing jointly, had a principle place of abode in the United States for more than one-half of 2021.

What other temporary provisions should I be aware of?

Paycheck Protection Plan loans

Revenue Ruling 2021-02 allows deductions for the payments of eligible expenses when such payments would result (or be expected to result) in the forgiveness of a loan (covered loan) under the Paycheck Protection Program (PPP). No deduction is denied, no tax attribute is reduced, and no basis increase is denied by reason of the exclusion from gross income of the forgiveness of an eligible recipient's covered loan.

Student loan forgiveness

An exclusion from gross income is available for student loan forgiveness after 2020 and before 2026 for most forgiven student loans. If eligible for the exclusion, the lender should not issue Form 1099-C.

Business expenses paid to restaurants

There is a temporary exception to the 50% limit on the amount that businesses may deduct for food or beverages. The temporary exception allows a 100% deduction for food or beverages from restaurants. Beginning January 1, 2021, through December 31, 2022, businesses can claim 100% of their food or beverage expenses paid to restaurants as long as the business owner is present when food or beverages are provided and the expense is not lavish or extravagant under the circumstances.

Under the temporary provision, restaurants include businesses that prepare and sell food or beverages to retail customers for immediate on-premises and/or off-premises consumption. However, restaurants do not include businesses that primarily sell pre-packaged goods not for immediate consumption, such as grocery stores and convenience stores. See **Notice 2021-25** for details.

Exclusion for certain employer payments of student loans

Employers may provide a student loan repayment benefit to employees on a tax-free basis. Under the provision, an employer may contribute up to \$5,250 annually toward an employee's student loans, and such payment would be excluded from the employee's income. The \$5,250 cap applies to both the new student loan repayment benefit as well as other educational assistance (e.g., tuition, fees, books) provided by the employer. This provision has been extended through 2025.



Itemized Deductions

What about qualified mortgage insurance premiums?

This provision has been extended through 2021. Taxpayers can deduct private mortgage insurance premiums paid during the current tax year on Schedule A in the Interest You Paid section. The insurance must have been in connection with home acquisition debt, and the insurance contract must have been issued after 2006. Volunteers need to be aware that this potential deduction may not be reported on Form 1098. Ask homeowners with a mortgage if they paid mortgage insurance premiums during the tax year. Failure to ask could result in a substantial deduction loss for taxpayers filing Schedule A.



Other itemized deductions are discussed in a later lesson.

What are residential energy credits?

This provision has been extended through 2021. Individuals who purchase qualified energy efficient improvements for their main home may be allowed nonrefundable tax credits. There are two types of residential energy credits:

- Residential energy efficient property credit (Form 5695, Residential Energy Credits, Part I, which is out of scope for the VITA/TCE programs)
- Nonbusiness energy property credit (Form 5695, Part II)
- The adjusted basis of the home is reduced by the residential credit received.



Other credits are discussed in the Miscellaneous Credits lesson.

The IRS provides guidance on what property qualifies for the energy credits. Homeowners generally can rely on manufacturers' certifications that their property qualifies. See the Volunteer Resource Guide, Tab EXT, Legislative Extenders, [irs.gov](https://www.irs.gov), or energystar.gov for more information.

What is the residential energy efficient property credit?

This residential energy credit is claimed on Form 5695, Part I, and is out of scope for the VITA/TCE programs. For awareness only, taxpayers may claim an energy credit for qualified solar electric, solar water heating, small wind energy, and geothermal heat pump property costs. Check for qualifying energy property purchases to determine if the taxpayer should see a professional tax preparer to claim the credit.

What is the nonbusiness energy property credit?

The nonbusiness energy property credit is available for certain qualifying energy efficiency improvements or residential energy property costs. The qualifying items are:

- Biomass stoves
- Heating, ventilating, air-conditioning (HVAC)
- Insulation
- Roofs (metal and asphalt)
- Water heaters (non-solar)
- Windows and doors

The nonbusiness energy property credit is subject to the following limitations:

- The total combined credit limit for all tax years after 2005 is \$500, and the combined credit limit for windows is \$200.
- The maximum credit for residential energy property costs is \$50 for any advanced main air circulating fan; \$150 for any qualified natural gas, propane, or oil furnace, or hot water boiler; and \$300 for any item of energy efficient building property.

It is important to note that:

- The credit is only available for existing homes that are the taxpayer's main home – new construction and rentals do not qualify. The taxpayer must own the home to qualify.
- Amounts provided by subsidized federal, state, or local energy financing do not qualify for the credit.
- The adjusted basis of the home is reduced by the residential credit received.



CAUTION Costs for on-site preparation and installation depend on the type of qualified property. Review the Form 5695 Instructions for more information.



Cancellation of Debt (COD) – Principal Residence

Cancellation of credit card debt is included in the Other Income lesson of this publication for Advanced certification. Exclusion from gross income of qualified principal residence indebtedness has been extended through 2025 on a modified basis.

In Scope for VITA/TCE Programs

Refer to Publication 4731-A, Screening Sheet for Foreclosures/Abandonments and Cancellation of Debt, to ensure that the tax return being prepared is within scope of the VITA/TCE programs. This screening sheet is contained in the Volunteer Resource Guide, Legislative Extenders tab.

- Use Publication 4731-A, Part I for taxpayers with Form 1099-A for a foreclosure or abandonment of their principal residence
- Use Publication 4731-A, Part II for taxpayers with Form 1099-C, or Forms 1099-A and 1099-C resulting from cancellation of debt on a home mortgage loan

Recourse vs. Nonrecourse Debt

There are two types of debts: recourse and nonrecourse. A recourse debt holds the borrower personally liable. All other debt is considered nonrecourse.

In general, recourse debt (loans) allows lenders to collect what is owed for the debt even after they've taken collateral (home, credit cards). Lenders have the right to garnish wages or levy accounts in order to collect what is owed.

A nonrecourse debt (loan) does not allow the lender to pursue anything other than the collateral. For example, if a borrower defaults on a nonrecourse home loan, the bank can only foreclose on the home. The bank generally cannot take further legal action to collect the money owed on the debt. Whether a debt is recourse or nonrecourse may vary from state to state, depending on state law.

If a lender cancels a debt and issues Form 1099-C, the lender will indicate on the form if the borrower was personally liable (recourse) for repayment of the debt.



TIP If property securing the debt was foreclosed on or abandoned, the taxpayer may need to report the disposition (sale) on Form 8949 and Schedule D. This is covered in more detail later in this course.



Generally, if taxpayers abandon property that secures debt for which they are **personally liable**, they do not have a gain or loss until the foreclosure is completed.

If taxpayers abandon property that secures debt for which they are **not personally liable**, the abandonment is treated as a sale or exchange.

For more information on abandonments see Publication 4681, Canceled Debts, Foreclosures, Repossessions, and Abandonments.

Recourse debt holds the borrower personally liable for any amount not satisfied by the surrender of *secured property*.

- If a lender forecloses on property subject to a recourse debt and cancels the portion of the debt in excess of the fair market value (FMV) of the property, the canceled portion of the debt is treated as ordinary income from cancellation of indebtedness. This amount must be included in gross income unless it qualifies for an exception or exclusion.
- In addition to this cancellation of indebtedness income, the taxpayer may realize a gain or loss on the disposition of the property; this amount is generally the difference between the FMV of the property at the time of the foreclosure and the taxpayer's basis in the property.

Nonrecourse debt is satisfied by the surrender of the *secured property* regardless of the FMV at the time of surrender, and the borrower is not personally liable for the debt.

- If property that is subject to nonrecourse debt is abandoned, foreclosed upon, subject of a short sale, or repossessed by the lender, the circumstances are treated as a sale of the property by the taxpayer.
- In determining the gain or loss on the disposition of the property, the balance of the nonrecourse debt at the time of the disposition of the property is included in the amount realized (generally the selling price). Since the borrower is not personally liable for the debt, the difference between the FMV of the property and the balance of the loan is *not* included in gross income.

example

Jason lost his home to foreclosure because he could no longer make his mortgage payments. At the time of foreclosure, he owed a balance of \$170,000 to the lender and the FMV of the property was \$140,000.

If Jason is personally liable for the debt (recourse loan), the selling price would be \$140,000. If Jason is not personally liable for the debt (nonrecourse loan), the selling price would be \$170,000.

	Recourse Debt	Nonrecourse Debt
Borrower is...	Personally liable	Not personally liable
Canceled portion of debt is generally...	Treated as ordinary income and included in gross income (unless it qualifies as an exception or exclusion)	Not applicable. Nonrecourse debt is satisfied by the surrender of the secured property regardless of the FMV at the time of surrender.
Gain or loss on disposition of the property	Generally determined by the difference between the FMV of the property and the adjusted basis	The amount realized includes the balance of the nonrecourse debt at the time of the disposition of the property. This is true even if the FMV of the property is less than the outstanding debt.

Exceptions and Exclusions

Some canceled or forgiven debts may be *eliminated* from income by applying exceptions, or *reduced* by applying exclusions to the general rule. **Exceptions are applied before exclusions.**

Exceptions

Exceptions may allow the taxpayer to eliminate the following types of canceled debt from income:

- Amounts otherwise excluded from income (e.g., gifts and bequests)
- Certain student loans, in addition to the general exclusion noted above for tax years 2021 through 2025 (e.g., doctors, nurses, and teachers serving in rural or low-income areas)
- Deductible debt (e.g., home mortgage interest that would have been deductible on Schedule A)
- Price reduced after purchase (e.g., debt on solvent taxpayer's property is reduced by the seller; basis of property must be reduced)

For more information on exceptions, refer to Publication 4681.

Exclusions

There are several exclusions from the general rule for reporting canceled debt as income.

Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness, must be filed with the taxpayer's return to show the amount of the canceled debt excluded.

The exclusions are:

- Discharge of debt through bankruptcy
- Discharge of debt of insolvent taxpayer
- Discharge of qualified farm indebtedness
- Discharge of qualified real property business indebtedness
- Discharge of qualified principal residence indebtedness



The issues involved in exclusions can be complex. Only cancellation of qualified principal residence indebtedness exclusion is within the scope of VITA/TCE.

Discharge of Qualified Principal Residence Indebtedness

Taxpayers may exclude from income certain debt forgiven or canceled on their principal residence. If the canceled debt qualifies for exclusion from gross income, the debtor may be required to reduce tax attributes (certain credits, losses, and basis of assets) by the amount excluded.

If a property was taken by the lender (foreclosure) or given up by the borrower (abandonment), the lender usually sends the taxpayer Form 1099-A, Acquisition or Abandonment of Secured Property. Form 1099-A will have information needed to determine the gain or loss due to the foreclosure or abandonment.

If the debt is canceled, the taxpayer will receive Form 1099-C, Cancellation of Debt. If foreclosure/abandonment and debt cancellation occur in the same calendar year, the lender may issue only Form 1099-C, including the information that would be reported on Form 1099-A.

Qualified Principal Residence Indebtedness

Qualified principal residence indebtedness includes:

- Any debt incurred in acquiring, constructing, or substantially improving a principal residence that is secured by the principal residence
- Any debt *secured by the principal residence resulting from the refinancing of debt* incurred to acquire, construct, or substantially improve a principal residence, but only to the extent that the amount of debt does not exceed the amount of the refinanced indebtedness



A principal residence is generally the home where the taxpayer lives most of the time. A taxpayer can have only one principal residence at a time.

Exclusion Limit

The maximum amount that can be treated as qualified principal residence indebtedness for discharges after 2020 is \$750,000 (\$375,000 in the case of a married individual filing a separate return).

Canceled qualified principal residence indebtedness cannot be excluded from income if the cancellation was for services performed for the lender or on account of any factor not directly related to a decline in the value of the residence or the taxpayer's financial condition.

Criteria for Canceled Principal Residence Debt

Volunteers may assist taxpayers who meet the following requirements:

- The home was never used in a business or as rental property
- The debt was not canceled because the taxpayer filed bankruptcy
- The taxpayer is **not** in bankruptcy when he/she comes to the site for assistance
- Form 1099-C does not include an amount for interest
- The debt must be a mortgage used *only* to buy, build, or substantially improve the taxpayer's primary residence, i.e., this money was not used to pay off credit cards, medical/dental expenses, vacations, etc.
- The mortgage was secured by the taxpayer's primary residence
- The mortgage was not more than \$750,000 (\$375,000 in the case of a married individual filing a separate return)

example

Bob refinanced his personal residence and used the loan proceeds from the equity in his home to build a new master bedroom suite on the main level of his house. This debt is qualified principal residence indebtedness.

example

Tom refinanced his personal residence and used the loan proceeds from the equity in his home to pay off credit cards and buy a car. This debt is **not** qualified principal residence indebtedness.



EXERCISES

Use Publication 4731-A, Part II, to answer the following questions. The answers appear at the end of the lesson.

Question 1: A volunteer with Advanced certification is working with Angie. Angie confirmed that she had to give up her principal residence and produced Form 1099-C for the cancellation of the mortgage loan. Angie explains that she did not file for bankruptcy, even though she experienced hardship due to the loss of income from no longer being able to rent out an upstairs bedroom and bath. Angie also verified that the mortgage loan was used entirely to purchase the home and was secured by the home. Her Form 1099-C lists the amount of debt canceled as \$60,000.

Should the volunteer assist Angie with her return? ☐ Yes ☐ No

Question 2: Fred went to his local VITA site to have his tax return prepared. The volunteer went through Fred's records and noticed Form 1099-C reflecting a canceled debt of \$50,000.

Using Publication 4731-A, Part II, as a guide, the volunteer learned Fred lost his job and could no longer make his mortgage payments. The bank foreclosed on Fred's home. Due to the housing market slump, the value of Fred's home had declined, and his mortgage balance was more than the fair market value of the home. The bank sold Fred's home and canceled the remaining debt (\$50,000) not covered by the sale price.

Upon further questioning, the volunteer learned Fred had refinanced his home two years ago and used the equity in the home to pay off some credit cards and take a trip to Las Vegas.

Should the volunteer assist Fred with the preparation of his return at the VITA site? ☐ Yes ☐ No

Foreclosures and Capital Gain or Loss

If a taxpayer does not make payments owed on a loan secured by property, the lender may foreclose on the loan or repossess the property. The foreclosure or repossession is treated as a sale from which the taxpayer may realize a gain or loss. This is true even if the taxpayer voluntarily returns the property to the lender.

Figure the gain or loss from a foreclosure or repossession the same way as the gain or loss from a sale. The gain is the difference between the amount realized and the adjusted basis of the transferred property (amount realized minus adjusted basis). The loss is the difference between the adjusted basis in the transferred property and the amount realized (adjusted basis minus amount realized).

When a residence that is security for a mortgage is abandoned or foreclosed upon, the gain or loss must be reported on the return and is subject to the rules for a sale of residence.

Generally, the amount realized on a foreclosure is considered to be the selling price. But this selling price depends, in part, on whether the debt was recourse debt or nonrecourse debt. In addition, the taxpayer may also have ordinary income from the cancellation of debt.

Use the Worksheet for Foreclosures and Repossessions in Publication 4681 to figure the ordinary income from the cancellation of debt and the gain or loss from a foreclosure or repossession.



CAUTION A loss on the sale or disposition of a personal residence is not deductible. A gain may qualify for the Section 121 exclusion (\$250,000 or \$500,000 for Married Filing Jointly taxpayers and some surviving spouses) for a gain on the sale of a principal residence.

Generally, the taxpayer's gain or loss from a foreclosure or abandonment is reported on Form 8949 and Schedule D.

If the taxpayer is personally liable for the debt (recourse debt), and the amount of outstanding debt (mortgage) is more than the home's FMV, the difference is treated as cancellation of debt income.

- If the canceled debt qualifies as excludable from gross income, the exclusion is reported on Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness (And Section 1082 Basis Adjustment)
- Otherwise, the canceled debt is reportable as ordinary income on Form 1040, Schedule 1 and is beyond the scope of VITA/TCE



CAUTION If the canceled debt is reportable on Form 1040, Schedule 1 or the canceled debt is not fully excludable from gross income, the issue is beyond the scope of the VITA/TCE programs.

Form 1099-A, Acquisition or Abandonment of Secured Property

When a personal residence is foreclosed upon, and the lender cancels a portion of the debt, the taxpayer will generally receive Form 1099-A and Form 1099-C. If, in the same calendar year, the debt is canceled in connection with a foreclosure of secured property, the lender has the option of issuing Form 1099-C only.

The filing requirements of Form 1099-A are met by the lender completing the following on Form 1099-C:

- Debt description
- The debtor was personally liable for the repayment of the debt
- Fair market value of property



TIP For more information on determining the basis for sale of residence see the lesson on Income – Capital Gain or Loss, Publication 523, Selling Your Home, or Publication 551, Basis of Assets.

Verify with the taxpayer that the information on Form 1099-A and Form 1099-C is correct. Pay particular attention to the amount of debt forgiven and the fair market value reported. Advise the taxpayer to contact the lender immediately if any of the information is not correct.

Form 1099-A, issued by the lender, reports the outstanding debt and the fair market value of the property. This form provides information needed to determine the amount of any gain or loss due to foreclosure or abandonment. Report the gain or loss on Form 8949 and Schedule D. A loss on the disposition of a personal asset is not deductible.

The sale price (amount realized) is based on whether the taxpayer is personally liable (recourse loan) or not personally liable (nonrecourse loan) for the debt.

- If the taxpayer is personally liable, the sale price is the **lesser** of the balance of the principal mortgage debt outstanding or the fair market value
- If the taxpayer is not personally liable, then the sale price is the full amount of the outstanding debt, as reflected on Form 1099-A
- For both recourse and nonrecourse loans, add any proceeds the taxpayer received from the foreclosure sale to the amount realized

Generally, if there is a loss on the sale of a principal residence or the entire gain is excluded under the Section 121 exclusion (\$250,000 or \$500,000 for Married Filing Jointly and certain surviving spouses), the sale does not have to be reported. However, taxpayers who receive Form 1099-A should report the sale to account for the basis in the property.



CAUTION Failure to report a foreclosure or abandonment transaction on Form 8949 and Schedule D may result in an IRS notice to the taxpayer.

Form 1099-C, Cancellation of Debt

Lenders or creditors are required to issue Form 1099-C if they cancel a debt owed to them of \$600 or more. Generally, an individual taxpayer must include all canceled amounts (even if less than \$600) on the other income line of Form 1040, Schedule 1.

However, under certain circumstances, a taxpayer may not have to include canceled debt in income. For example, if the canceled debt is related to the taxpayer's principal residence, the taxpayer may be able to exclude all or a portion of canceled debt if it is qualified principal residence indebtedness. The amount excluded due to the discharge of qualified principal residence indebtedness is reported on Form 982.

In addition to debtor information, Form 1099-C reports the amount of debt canceled and the date canceled.

If the form has event code A indicating bankruptcy, or if an amount is included for interest, refer the taxpayer to a professional tax preparer.

Form 982 must be filed with the taxpayer's return to report the excluded amount of discharged indebtedness and the reduction of certain tax attributes. Taxpayers excluding discharged debt from qualified principal residence indebtedness must complete only a few lines on Form 982. Refer to the Volunteer Resource Guide, Tab EXT, Legislative Extenders, for details. If the taxpayer kept ownership of the home, the basis adjustment to the principal residence for the excluded canceled debt must be reflected on the form.

Coordination with Form 1099-A

As mentioned earlier, if a personal residence is foreclosed upon, and the debt is canceled in the same year, the taxpayer may receive Form 1099-C *only*. The required filing information from Form 1099-A will be shown on Form 1099-C.

Generally, the gross foreclosure bid price is considered to be the FMV. For an abandonment or voluntary conveyance in lieu of foreclosure, the FMV is generally the appraised value of the property.

For a recourse loan, the sale price is the **lesser** of the balance of the principal debt (mortgage) outstanding or fair market value.

Mortgage Workouts and Form 1099-C

Homeowners whose mortgage debt is partly forgiven through a loan modification, or workout, which allows them to continue owning their residence, will receive Form 1099-C reporting the amount of debt discharged. Because the taxpayer kept ownership of the home, there is no gain or loss to be reported.

However, if the canceled debt meets the requirements of qualified principal residence indebtedness, Form 982 must be completed to report the amount excluded from gross income and the reduction of tax attributes. See Publication 4012, Tab EXT, Legislative Extenders, Entering Forgiveness of Qualified Principal Residence Indebtedness, for directions on completing Form 982.

Taxpayers who are not personally liable for the debt (nonrecourse debt) do not have ordinary income from the cancellation of the debt unless the lender:

- Offered a discount for the early payment of the debt or
- Agreed to a loan modification that resulted in the reduction of the principal balance of the debt

If a lender offers to discount (reduce) the principal balance of a loan that is paid off early, or agrees to a loan modification (workout) that includes a reduction in the principal balance of a loan, the amount of the discount or the amount of the principal reduction is *canceled debt* whether or not the taxpayer is personally liable for the debt. The amount of the canceled debt must be included in income unless the exceptions or exclusions discussed earlier apply.

Gain or Loss Reported on Form 8949 and Schedule D

Form 8949, Sales and Other Dispositions of Capital Assets, includes all capital gain and loss transactions. The subtotals from Form 8949 are carried over to Schedule D, Capital Gains and Losses, where gain or loss is calculated in aggregate.

Losses on a personal residence are never deductible. Gains (all or part) may be excluded under the rules regarding the sale of a personal residence (Section 121 exclusion).

For more information on how to report the gain or losses, see the Volunteer Resource Guide, Tab D, Capital Gains or Losses Sale of Main Home.

Case Study – Reporting a Foreclosure and Canceled Debt



The following case studies are only examples of how the mentioned issues and forms can look and be reported. The dates and years of the forms are not relevant for these case studies.

Frank bought his home on May 14, 2017. His basis in the home was \$200,000. After he lost his job last year, he was not able to make the payments. The bank foreclosed in June of the current tax year, and Frank moved out. At the time of the foreclosure, the fair market value of the home was \$125,000 and the principal balance of the mortgage was \$195,000. All of the debt was incurred to purchase the home. Frank received Form 1099-C for the amount of debt canceled by his bank.

Frank has qualified principal residence indebtedness. His tax return should include Form 8949 and Schedule D to show the basis of the home disposed of through foreclosure, and Form 982 to exclude the debt cancellation from income.

☐ CORRECTED (if checked)

CREDITOR'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no. FIRST BANK ANYWHERE USA		1 Date of identifiable event 6/25/20XX 2 Amount of debt discharged \$ 70,000.00 3 Interest if included in box 2 \$	OMB No. 1545-1424 20XX Form 1099-C	Cancellation of Debt	
CREDITOR'S federal identification number XX-XXXXXXX	DEBTOR'S identification number XXX-XX-XXXX	4 Debt description HOME MORTGAGE LOAN 1111 ANYWHERE STREET ANYWHERE TOWN, STATE ZIP		Copy B For Debtor This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.	
DEBTOR'S name FRANK LINCOLN Street address (including apt. no.) ANYWHERE City or town, state or province, country, and ZIP or foreign postal code CITY, STATE ZIP USA		5 If checked, the debtor was personally liable for repayment of the debt ☒			
Account number (see instructions) 1234567		6 Identifiable event code	7 Fair market value of property \$ 125,000.00		
Form 1099-C		(keep for your records)		www.irs.gov/form1099c	Department of the Treasury - Internal Revenue Service

Form 8949

Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Name and SSN or taxpayer identification no. not required if shown on other side
FRANK LINCOLN

Social security number or taxpayer identification number
XXX-XX-XXXX

Before you check Box D, E, or F below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either may show your basis (usually your cost) even if your broker did not report it to the IRS. Brokers must report basis to the IRS for most stock you bought in 2011 or later (and for certain debt instruments you bought in 2014 or later).

Part II Long-Term. Transactions involving capital assets you held more than 1 year are long term. For short-term transactions, see page 1.

Note. You may aggregate all long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the total directly on Schedule D, line 8a; you are not required to report these transactions on Form 8949 (see instructions).

You must check Box D, E, or F below. Check only one box. If more than one box applies for your long-term transactions, complete a separate Form 8949, page 2, for each applicable box. If you have more long-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- ☐ (D) Long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- ☐ (E) Long-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- ☒ (F) Long-term transactions not reported to you on Form 1099-B

1	(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the Note below and see Column (e) in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions.		(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
						(f) Code(s) from instructions	(g) Amount of adjustment	
	Main Home Form 1099-A	05/14/17	06/25/XX	\$ 125,000	\$ 200,000	L	\$ 75,000	\$ 0

2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, line 8b (if Box D above is checked), line 9 (if Box E above is checked), or line 10 (if Box F above is checked) ▶

\$ 125,000 \$ 200,000 \$ 75,000 \$ 0

Note. If you checked Box D above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See Column (g) in the separate instructions for how to figure the amount of the adjustment.

Form **8949**

term capital gains or losses, go to Part II below. Otherwise, go to Part III on the back.

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

See instructions for how to figure the amounts to enter on the lines below.

This form may be easier to complete if you round off cents to whole dollars.

	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b.				
8b Totals for all transactions reported on Form(s) 8949 with Box D checked.				
9 Totals for all transactions reported on Form(s) 8949 with Box E checked.				
10 Totals for all transactions reported on Form(s) 8949 with Box F checked.	\$125,000	\$200,000	\$75,000	\$0
11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824.				11
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1.				12
13 Capital gain distributions. See the instructions.				13
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your Capital Loss Carryover Worksheet in the instructions.				14 ()
15 Net long-term capital gain or (loss). Combine lines 8a through 14 in column (h). Then go to Part III on the back.				15 \$0

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 11338H

Schedule D (Form 1040)

Form **982**
(Rev. July 20XX)
Department of the Treasury
Internal Revenue Service

Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)

▶ Attach this form to your income tax return.

▶ Information about Form 982 and its instructions is at www.irs.gov/form982.

OMB No. 1545-0046

Attachment
Sequence No. **94**

Name shown on return

FRANK LINCOLN

Identifying number

XXX-XX-XXXX

Part I General Information (see instructions)

- 1** Amount excluded is due to (check applicable box(es)):
- a** Discharge of indebtedness in a title 11 case ☐
 - b** Discharge of indebtedness to the extent insolvent (not in a title 11 case) ☐
 - c** Discharge of qualified farm indebtedness ☐
 - d** Discharge of qualified real property business indebtedness ☐
 - e** Discharge of qualified principal residence indebtedness ☒
- 2** Total amount of discharged indebtedness excluded from gross income **2** **\$70,000**
- 3** Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property? ☐ Yes ☐ No

Part II Reduction of Tax Attributes. You must attach a description of any transactions resulting in the reduction in

Case Study Alternative – Mortgage Workout

If Frank had been able to negotiate a workout with his mortgage lender (reducing the amount he owed on the mortgage and staying in the home), he would not have completed Form 8949 and Schedule D because he had not disposed of the asset.

Assume Frank's lender agreed to reduce his mortgage debt from \$195,000 to \$175,000. The lender issued Frank a Form 1099-C showing \$20,000 of canceled debt. Frank's Form 982 would be completed, but the amount of debt forgiven (or his basis in the home, whichever was smaller) would need to be entered on the form, and his basis in the home would be decreased by that amount.

☐ CORRECTED (if checked)

CREDITOR'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no. FIRST BANK ANYWHERE USA		1 Date of identifiable event 6/25/20XX 2 Amount of debt discharged \$ 20,000.00 3 Interest if included in box 2 \$	OMB No. 1545-1424 20XX Form 1099-C	Cancellation of Debt
CREDITOR'S federal identification number XX-XXXXXXX	DEBTOR'S identification number XXX-XX-XXXX	4 Debt description HOME MORTGAGE LOAN 1111 ANYWHERE STREET ANYWHERE TOWN, STATE ZIP 5 If checked, the debtor was personally liable for repayment of the debt ☒		Copy B For Debtor This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.
DEBTOR'S name FRANK LINCOLN Street address (including apt. no.) ANYWHERE City or town, state or province, country, and ZIP or foreign postal code CITY, STATE ZIP USA		6 Identifiable event code \$		
Account number (see instructions) 1234567		7 Fair market value of property \$		

Form **1099-C**
(keep for your records)
www.irs.gov/form1099c
Department of the Treasury - Internal Revenue Service

Form 982 (Rev. July 20XX) Department of the Treasury Internal Revenue Service	Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment) ▶ Attach this form to your income tax return. ▶ Information about Form 982 and its instructions is at www.irs.gov/form982 .	OMB No. 1545-0046 Attachment Sequence No. 94
Name shown on return FRANK LINCOLN		Identifying number XXX-XX-XXXX
Part I General Information (see instructions)		
1 Amount excluded is due to (check applicable box(es)): a Discharge of indebtedness in a title 11 case b Discharge of indebtedness to the extent insolvent (not in a title 11 case) c Discharge of qualified farm indebtedness d Discharge of qualified real property business indebtedness e Discharge of qualified principal residence indebtedness ☐ ☐ ☐ ☐ ☒		
2 Total amount of discharged indebtedness excluded from gross income		2 \$20,000
3 Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property? ☐ Yes ☐ No		
Part II Reduction of Tax Attributes. You must attach a description of any transactions resulting in the reduction in basis under section 1017. See Regulations section 1.1017-1 for basis reduction ordering rules, and, if applicable, required partnership consent statements. (For additional information, see the instructions for Part II.)		
Enter amount excluded from gross income:		
4 For a discharge of qualified real property business indebtedness applied to reduce the basis of depreciable real property		4
5 That you elect under section 108(b)(5) to apply first to reduce the basis (under section 1017) of depreciable property		5
6 Applied to reduce any net operating loss that occurred in the tax year of the discharge or carried over to the tax year of the discharge		6
7 Applied to reduce any general business credit carryover to or from the tax year of the discharge		7
8 Applied to reduce any minimum tax credit as of the beginning of the tax year immediately after the tax year of the discharge		8
9 Applied to reduce any net capital loss for the tax year of the discharge, including any capital loss carryovers to the tax year of the discharge		9
10a Applied to reduce the basis of nondepreciable and depreciable property if not reduced on line 5. <i>DO NOT use in the case of discharge of qualified farm indebtedness</i>		10a
b Applied to reduce the basis of your principal residence. <i>Enter amount here ONLY if line 1e is checked</i>		10b \$20,000
11 For a discharge of qualified farm indebtedness applied to reduce the basis of: a Depreciable property used or held for use in a trade or business or for the production of income if not reduced on line 5		



EXERCISES (continued)

Question 3: A volunteer with Advanced certification is working with Robert. Following up to a “yes” answer on the Intake & Interview Sheet, the volunteer asks Robert if he underwent foreclosure or had to give up his home during the tax year. Robert confirmed that he did, and produced Form 1099-A. The volunteer asked Robert if he had received Form 1099-C, and Robert replied that he did not. Examining the form, the volunteer noted the balance of principal outstanding was \$234,000. What should the volunteer do next?

- A. Ask the questions on Publication 4731-A
- B. Ask enough probing questions to determine if Robert had a gain or loss on the foreclosure
- C. Refer Robert to a professional tax preparer
- D. Complete Form 982

Question 4: Mary purchased her main home in June 2004 for \$175,000. She lost her job and was no longer able to make her mortgage payments during the current year. In July of the current tax year, Mary moved out of the home to live with relatives. On July 15, the bank foreclosed on the home. On November 15, the bank discontinued its collection activity and canceled the remaining debt. The fair market value at the time of foreclosure was \$100,000 because of the poor housing market, but Mary still owed \$150,000 on the mortgage. None of the loan proceeds were used for any purpose other than to buy, build, or substantially improve the principal residence. Mary never used the home for business or rental purposes and has not filed for bankruptcy. Based on this information, what should the volunteer do?

- A. Refer Mary to another source for tax return preparation
- B. Report a loss of \$50,000 on Schedule D
- C. Report \$50,000 debt canceled on Form 982
- D. Include the debt cancellation amount in income

Question 5: After Tom became ill and could not work full time, he and his wife, Grace, were having difficulty making their mortgage payments. Rather than go through the expense of a foreclosure, the lender agreed to reduce the principal on their loan and refinance it with a better interest rate and lower payments. The principal balance before November 1 of the current tax year workout was \$130,000, and the lender reduced the loan to \$110,000. None of the loan proceeds were used for any purpose other than to buy, build, or substantially improve the principal residence. The home has never been used for business or as rental property, and the taxpayers have not filed for bankruptcy.

Based on this information, what should the volunteer do?

- A. Refer Tom and Grace to another source for tax return preparation
- B. Report the reduction in the basis of the home on line 10b of Form 982
- C. Report the \$20,000 as a loss on Schedule D
- D. Include the debt cancellation amount in income



EXERCISES (continued)

Question 6: Gene bought his home in 2003. His basis in the home was \$210,000. He lost his job in January of the current tax year and was not able to make the mortgage payments. The bank foreclosed in August and Gene moved out. At the time of the foreclosure, the fair market value was \$145,000 and the principal balance of the mortgage was \$185,000. All of the debt was incurred to purchase the home, it was never used for business or as a rental property, and Gene has not filed for bankruptcy. Gene has a Form 1099-C. Gene is personally liable for repayment of the debt.

How should the foreclosure and loss be reported?

- A. Report the \$40,000 debt cancellation on Form 982, line 10b
- B. Report the \$40,000 debt cancellation on Form 982, line 2, only
- C. Report the \$40,000 debt cancellation on Form 982, line 2, and the foreclosure on Form 8949 and Schedule D
- D. Report the \$40,000 debt cancellation on Form 1040

Summary

This lesson included the following temporary changes; other changes are detailed in other lessons.

2021 Changes to Credits

There are temporary changes for 2021 to the child and dependent care credit, earned income tax credit, and child tax credit.

Itemized Deductions

Taxpayers may be able to deduct qualified mortgage insurance premiums.

Nonbusiness Energy Property Credit

Taxpayers who make certain energy-efficient improvements to their main home may be eligible for this credit (Form 5695, Part II). The limit for this credit is \$500 total for all tax years after 2005.

Cancellation of Debt (COD) – Principal Residence

Cancellation of debt can be complex. VITA/TCE volunteers may assist a taxpayer with issues related to cancellation of debt as long as the taxpayer meets all the criteria for discharge of qualified principal residence indebtedness.

Taxpayers who go through a foreclosure or abandonment of their principal residence receive Form 1099-A, Acquisition or Abandonment of Secured Property. Form 1099-A will have information needed to determine the gain or loss due to the foreclosure or abandonment.

If the debt on the principal residence is canceled, the taxpayer will receive Form 1099-C, Cancellation of Debt. If foreclosure/abandonment and debt cancellation occur in the same calendar year, the lender may issue only Form 1099-C, including the information that would be reported on Form 1099-A.

What situations are out of scope for the VITA/TCE programs?

The following are out of scope for this lesson. While this list may not be all inclusive, it is provided for your awareness only.

- Residential energy-efficient property credit (Form 5695, Part I)
- Cancellation of debt on a residence other than a qualified principal residence
- Cancellation of debt for a principal residence that was used in a business or as rental property
- Cancellation of debt when Form 1099-C includes an amount for interest
- Cancellation of debt was because the taxpayer filed bankruptcy or was insolvent immediately before the debt was canceled



EXERCISE ANSWERS

Answer 1: No. Because Angie used part of the home as rental property, all the canceled debt may not qualify to be excluded from income. The rules involving mortgage debt exclusions are complex. Angie should be referred to a professional tax preparer.

Answer 2: No. Fred's situation is outside the scope of the volunteer program since a portion of his refinanced debt was used for purposes other than to buy, build, or substantially improve his principal residence. Fred should be referred to a professional tax preparer, per the guidance in Publication 4731-A.

Answer 3: A. The volunteer should use Publication 4731-A, Part I to determine if Robert had a gain or loss on the foreclosure. If the taxpayer receives a Form 1099-C, the volunteer would use the screening sheet to determine if the related tax issues are within scope.

Answer 4: C. The volunteer would need to complete Form 8949, Schedule D, and Form 982. Although there is a loss, it cannot be deducted. The mortgage debt cancellation is not included in income on the tax return because it is covered by the qualified principal residence indebtedness exclusion on Form 982.

Answer 5: B. The volunteer would complete Form 982 and report the reduction in the basis of the home. The \$20,000 in debt cancellation can be excluded as qualified principal residence indebtedness on Form 982 and is not counted as income on the tax return. Form 8949 and Schedule D are not required because Tom and Grace did not dispose of the home.

Answer 6: C. Form 982, Form 8949, and Schedule D should be completed. When a residence that is security for a mortgage is abandoned or foreclosed upon, it is treated as having been sold. This results in the foreclosure being reported on Form 8949 and Schedule D as sale of home. Failure to file Form 8949 and Schedule D may result in an IRS notice to the taxpayer.