PacificCPE

COURSE

32301C

2027 Filing Season: New Tax Law and Income Tax Fundamentals

Stay current with the latest legislative changes and foundational income tax concepts in this opening segment of the 2027 Filing Season Income Tax Update. The course covers recent tax law developments and key updates practitioners need to know heading into filing season, then transitions into a structured review of core income tax principles. Ideal for CPAs and tax professionals who want a solid refresher on fundamentals alongside the most relevant regulatory and legislative changes affecting their clients this year.

CREDIT HOURS 2 | FIELD OF STUDY TAXES | EXAM QUESTIONS 10

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LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Identify the inflation and cost of living adjustments to various federal limits.
- Recognize the applicable optional standard mileage rates.
- Recall the Third Party Network Transaction reporting requirements.
- Recognize the One Big Beautiful Bill Act (OBBBA) provisions affecting various income tax credits.
- Identify the OBBBA provisions affecting various income tax deductions.
- Recall the OBBBA provisions affecting –
  - Charitable contributions,
  - 529 plan account disbursements,
  - Trump Accounts, and
  - Health Savings Accounts.
- Recall the various filing statuses and the change to the gross income limitation for a qualifying relative.
- Identify those items included in a taxpayer's taxable earnings.
- Recognize the tax treatment of interest, dividends, foreign accounts, and trusts.
- Recall the rules governing contributions to and distributions from IRAs.

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Chapter 1: NEW TAX LAW/RECENT UPDATES

Chapter Objective

After completing this chapter, you should be able to:

- Identify the inflation and cost of living adjustments to various federal limits.
- Recognize the applicable optional standard mileage rates.
- Recall the Third Party Network Transaction reporting requirements.
- Recognize the One Big Beautiful Bill Act (OBBBA) provisions affecting various income tax credits.
- Identify the OBBBA provisions affecting various income tax deductions.
- Recall the OBBBA provisions affecting –
    - Charitable contributions,
    - 529 plan account disbursements,
    - Trump Accounts, and
    - Health Savings Accounts.

INTRODUCTION

Federal tax law requires that various limits be adhered to in the preparation of tax returns, and such limits may change from year to year based on an inflation adjustment or on other factors. Included in those changes for 2026 are changes to standard mileage rates, credits, deductions, and various other limits. These and additional changes brought about by recent legislation may affect taxpayers' income tax liability. Chapter 1 will examine these changes occurring in 2026, and will offer some context within which they apply.

ANNUAL INFLATION ADJUSTMENTS

Inflation adjustments are made annually to various limits that affect tax preparation, including adjustments to:

- Certain expenses of elementary and secondary school teachers;
- Interest on education loans;
- Foreign earned income exclusion; and
- Annual exclusion for gifts.

Education Expenses of Elementary and Secondary School Teachers

Education expenses of elementary and secondary teachers may be tax deductible. Deductible expenses, not exceeding the applicable limit, paid or incurred by an eligible educator include expenses in connection with:

- Books;
- Supplies (other than nonathletic supplies for courses in health or physical education);
- Computer equipment, including -
  - Related software,
  - Services, and
  - Other equipment; and
- Supplementary materials.

For 2026, the OBBBA has enhanced the above-the-line deduction for qualified education expenses of elementary and secondary school teachers by increasing the deduction allowed under §162 to $350. In addition, the OBBBA, for tax years after 2025:

- Allows qualified educator expenses in excess of $350 above-the-line deductible as a 2 percent miscellaneous itemized deduction not subject to the 2 percent floor;
- Allows athletic supplies for courses of instruction in health or physical education;
- Adds interscholastic sports administrators and coaches as eligible educators; and
- Broadens the criteria for eligible expenses criteria from being limited to "in the classroom" to "as part of instructional activity."

Interest on Education Loans

Student loan interest is interest paid by a taxpayer during the year on a qualified student loan. It includes both required interest payments and voluntary interest payments.

If the taxpayer paid $600 or more of interest on a qualified student loan during the year, the taxpayer will receive a Form 1098-E, *Student Loan Interest Statement*, from the entity to which the taxpayer paid the student loan interest.

Beginning in 2026, the maximum deductible interest on qualified education loans is $2,500. The income limit phaseout begins for taxpayers with a modified adjusted gross income (MAGI) of $85,000 ($175,000 for MFJ) and is completely phased out for taxpayers with a MAGI of $100,000 ($205,000 for MFJ) or more.

Amounts Included as Interest

The amounts considered interest, for purposes of the student loan interest deduction, include simple interest on the loan and—provided all other applicable requirements are met—the following items:

- Loan origination fee, i.e., the one-time fee charged by the lender when the loan is made. If loan origination fees are not included in the amount reported on the taxpayer's Form 1098–E, the taxpayer can use any reasonable method to allocate the loan origination fees over the term of the loan;
- Capitalized interest, i.e., unpaid interest added by the lender to the outstanding principal balance;
- Interest on revolving lines of credit if the borrower uses the line of credit only to pay qualified education expenses;
- Interest on refinanced student loans. However, if the taxpayer refinances a qualified student loan for more than the original loan amount and uses the additional amount for any purpose other than qualified education expenses, the taxpayer *cannot deduct any* interest paid on the refinanced loan; and
- Voluntary interest payments, i.e., payments made on a qualified student loan during a period when interest payments are not required.

Foreign Earned Income Exclusion

Foreign earned income is the earned income a qualified individual receives from sources within a foreign country for services performed during the taxable year. The term "qualified individual," for purposes of the **Foreign Earned Income Exclusion**, means an individual whose tax home is in a foreign country and who is:

- A citizen of the United States who has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or
- A citizen or resident of the United States who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period.

For taxable years beginning in 2026, the foreign earned income exclusion amount is $132,900.

Earnings Excluded in Foreign Earned Income

The foreign earned income for a qualified individual excludes amounts:

- Received as a pension or annuity,
- Paid by the United States or an agency thereof to an employee of the United States or an agency thereof,
- Included in gross income by reason of:
  - Taxability of beneficiary of nonexempt trust, or
  - Relating to taxability of beneficiary under a nonqualified annuity, or
- Received after the close of the taxable year following the taxable year in which the services to which the amounts are attributable are performed.

Limitation on Foreign Earned Income

In cases involving a qualifying taxpayer who has earned income in any year from working in a foreign country and also from working in the United States, the taxpayer's foreign earned income that may be excluded can be determined by dividing the workdays he or she worked in the foreign country by the number of workdays in the year. The result is then applied to the taxpayer's total earned income.

For example, suppose Sally, a qualified taxpayer, has a 2026 income of $125,000, partly from work in a foreign country and partly from work done in the United States. Sally works a five-day week and has a four-week annual vacation. In addition to her work in the foreign country, she worked six weeks in the United States.

To calculate the part of Sally's $125,000 income that is eligible for exclusion, we need to begin by determining the percentage of the year she worked in the foreign country and then apply that percentage to her salary. To do that, you will need to divide the number of workdays spent working in the foreign country by the total number of workdays in the year. Since the year has 52 weeks and four of those weeks are vacation weeks, 48 weeks—240 days, in other words—are spent at work each year (48 x 5 = 240). Since Sally worked six weeks (30 days) in the United States during the year, she worked 210 days in the foreign country (240 – 30 = 210). The percentage of time Sally worked in a foreign country is determined by dividing 210, the days she worked in the foreign country, by 240, i.e., the number of workdays in the year. The result is 87.5% (210 ÷ 240 = .875). By multiplying Sally's $125,000 income by 87.5%, we can see that her foreign income is $109,375 ($125,000 x .875 = $109,375).

If both spouses work abroad and each meets either the bona fide residence test or the physical presence test, they can each choose the foreign earned income exclusion. They both don't need to meet the same test. Together, they can exclude as much as $265,800 in 2026.

Annual Exclusion for Gifts

A gift is considered to be any transfer to an individual, either directly or indirectly, where full consideration (measured in money or money's worth) is not received in return. The general rule is that any gift is a taxable gift. However, there are many exceptions to this rule. Generally, the following gifts are not taxable gifts:

1. Gifts valued at not more than the annual gift tax exclusion;
2. Tuition or medical expenses paid by the taxpayer for another;
3. Gifts to a spouse who is a U.S. citizen; and
4. Gifts to a political organization.

Gift tax rates and estate tax rates are the same. Therefore, a gift in excess of the annual gift tax exclusion will generally incur gift tax liability that may be paid by the donor at the time of the gift or will otherwise reduce the unified credit applicable upon the taxpayer-donor's death. The annual gift tax exclusion amount in 2026 is $19,000, which means that a taxpayer may give assets away equal to $19,000 to any donee without incurring gift taxes. In addition, if a spouse joins in the gift (a split gift), the annual gift tax exclusion is doubled.

The annual gift tax exclusion for gifts to non-U.S. citizen spouses in 2026 increased to $194,000 (from $190,000 in 2025).

Note

Gifts made to a U.S. citizen spouse are not taxable in any amount, whether made during the spouse's lifetime or at death.

STANDARD MILEAGE RATES

The standard mileage rates enable a taxpayer using a vehicle for specified purposes to deduct vehicle expenses on a per-mile basis rather than deducting actual car expenses that are incurred during the year. The rates vary, depending on the purpose of the transportation.

Accordingly, the standard mileage rates differ from one another depending on whether the vehicle is used for:

- Business purposes;
- Charitable purposes; or
- Obtaining medical care or moving.

Rather than using the optional standard mileage rates, however, a taxpayer may choose to take a deduction based on the actual costs of using the vehicle.

Business Use of a Taxpayer's Personal Vehicle

The 2026 standard mileage rate applicable to eligible business use of a vehicle is 72.5¢ per mile, up from 70¢ in 2025. In order for such expenses to be deductible, they must have been:

- Paid or incurred during the tax year;
- For the purpose of carrying on the taxpayer's trade or business; and
- Ordinary and necessary.

Provided the vehicle expenses meeting these three criteria are not reimbursed, the deductible personal vehicle expenses include those incurred while traveling:

- Between workplaces;
- To meet with a business customer;
- To attend a business meeting located away from the taxpayer's regular workplace; or
- From the taxpayer's home to a temporary place of work.

In addition to using the standard mileage rate, a taxpayer may also deduct any business-related parking fees and tolls paid while engaging in deductible business travel. However, parking fees paid by a taxpayer to park his or her vehicle at the usual place of business are considered commuting expenses and are not deductible.

Personal Vehicle Use for Charitable Purposes

A taxpayer may deduct as a charitable contribution any unreimbursed out-of-pocket expenses, such as the cost of gas and oil, directly related to the use of a personal vehicle in providing services to a charitable organization. Alternatively, a taxpayer may use the standard mileage rate applicable to the use of a personal vehicle for charitable purposes. The standard mileage rate applicable to a taxpayer's use of a personal vehicle for charitable purposes is based on statute and remains unchanged at 14¢ per mile. The taxpayer may also deduct parking fees and tolls, regardless of whether the actual expenses or standard mileage rate is used.

A related issue involves a taxpayer's travel expenses incurred in providing services to a charity. Thus, in addition, a taxpayer may generally claim a charitable contribution deduction for travel expenses necessarily incurred while away from home performing services for a charitable organization. In order to claim a charitable deduction for such travel expenses, however, certain criteria must be met. Pursuant to federal regulations, in order to take a charitable contribution deduction for such travel expenses:

- There must be no significant element of personal pleasure, recreation, or vacation in the travel; and
- The taxpayer must be on duty in a genuine and substantial sense throughout the trip. (A taxpayer having only nominal duties in connection with the trip or who has no duties for a significant part of it would not be permitted to deduct the travel expenses.)

Use of a Taxpayer's Personal Vehicle to Obtain Medical Care

A taxpayer may also deduct medical and dental expenses to the extent they exceed the applicable percentage of his or her adjusted gross income (AGI). The vehicle expenses a taxpayer may include as medical and dental expenses are the amounts paid for transportation to obtain medical care for the taxpayer, a spouse, or a dependent. A taxpayer may also include as medical and dental expenses those transportation costs incurred:

- By a parent who must accompany a child needing medical care;