

Need for Extra Cash, Tax Implications of Dipping Into Savings Top 2013 List of Taxpayer Dilemmas

April 11, 2013 9:00 AM ET

Top Five Taxpayer Questions Range From Canceled Debt to Military Residency Issues

KANSAS CITY, MO -- (Marketwired) -- 04/11/13 -- To get the pulse of how taxpayers see their financial situations, all one has to do is step inside one of the 11,000 [H&R Block](#) (NYSE: HRB) offices or scroll through the help section on its [At Home](#) solution. As the 2013 tax season comes to a close, The Tax Institute at H&R Block unveils some of the top taxpayer questions.

In prior years, unemployment, foreclosures and dependent care questions from the sandwich generation dominated the question queue. This year, the questions are about military residency, canceled debt and hardship distributions from retirement savings. This shows taxpayers are still seeking ways to save money, but also may have had to tap into savings.

"We are hearing about complicated topics on our digital product's help line and via the questions being asked at the tax desk," said Kathy Pickering, executive director of The Tax Institute at H&R Block. "We often say people's lives and their taxes intersect, and the proof is in this list. These tax topics are about some of the bigger life changes."

The following questions (and answers) are among the top searched by taxpayers and H&R Block tax professionals.

Q1. I am in the military and stationed in a different state than where I usually live. What state tax returns do I need to file?

While this may seem really complicated, the simple rule is taxpayers file where they "live" and not necessarily where they are "stationed." If the only reason a military member lives in a particular state is due to active duty status, then the original "home" state should be used for filing purposes. A military spouse may be eligible for the same tax treatment as the service member. Because individual situations vary, it's best to consult a tax professional to be sure.

Q2. I negotiated with my credit card company to cancel my debt. How do I know if I am eligible to exclude that from my income?

Income from the cancelation of personal credit card debt is not excludable income. Generally, when a debt is canceled, that amount must be reported as income on a tax return. Sometimes when the canceled debt is taxable income, taxpayers can exclude that income and reduce other tax attributes, such as a capital loss carryforward.

Exceptions that allow taxpayers to not claim canceled debt as income include debt canceled as a result of insolvency or bankruptcy. Through 2013, the Mortgage Debt Relief Act makes some taxpayers eligible to exclude canceled debt from foreclosures.

Q3. Do I owe penalties if I took a hardship distribution from my 401(k)?

Unless a penalty exception is explicitly stated in tax code, financial hardship is not an exception to the penalty. Generally, there is a 10-percent early distribution penalty when money is withdrawn from a 401(k) before the holder is 59 1/2. Following are some exceptions to this penalty:

- When the distribution is made to beneficiaries after the account holder's death
- When the distribution is because of total and permanent disability
- When the distribution will pay for tax-deductible medical expenses.

Q4. Who is responsible for paying a deceased taxpayer's taxes?

The deceased taxpayer's estate is responsible for paying the taxes and the executor of the estate is responsible for making sure a tax return is filed. Federal taxes due generally must be paid before all other estate debts. If the executor pays other debts first and there isn't enough money left to pay the taxes, the executor could become personally responsible for the taxes.

Q5. If I take online classes, can I claim education tax breaks? What if I used money from a trust to pay the tuition?

Students who take online courses from an eligible educational institution and meet the other eligibility requirements may qualify to claim education tax breaks. An eligible institution is any college, university, vocational school or other post-secondary educational institution eligible to participate in a student-aid program administered by the Department of Education. Individual institutions should be able to tell students if they are eligible institutions.

If tuition is paid with money from a trust, education tax breaks can be claimed as long as the other eligibility qualifications are met.

"Taxes really aren't a one-time, annual event," Pickering said. "Deaths in the family, moves due to job changes and financial hardships happen all year and impact the tax return. Knowing the tax impact of these events when they occur can help save stress and possibly money."

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About The Tax Institute at H&R Block

[The Tax Institute at H&R Block](#) is the go-to source for objective insights on federal and state tax laws affecting the individual. It provides nonpartisan information and analysis on the real world implications of tax policies and proposals to policymakers, journalists, experts and tax preparers. The Institute's experts include CPAs, Enrolled Agents, tax attorneys and former IRS agents. Building off more than 10 years of research and analysis from a specialized tax research group at H&R Block, the company launched The Tax Institute in 2007.

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Source: H & R Block