

# ST20-34 – Special Interest and Dividends Situations

## Tax Exempt Interest (Form 1099-Int Box 8)

Tax exempt interest is reported on form 1099-INT box 8.

### Federal return

- The full amount of the interest is federally tax exempt
- Enter the amount in TSO 1099-INT box 8
- TSO carries the amount to the federal 1040-line 2a as tax exempt interest

### NJ return

- **NJ taxability varies**
- TSO carries the amount to line 16b – Tax Exempt Interest
- Preparer determines how much is taxable and adjusts in TSO

### How to determine NJ taxability

1. Find in the brokerage statement the interest detail. If the detail is not in the brokerage statement, contact with the broker may be required.
2. Look at each security that makes up the tax-exempt interest to determine if that security is tax exempt in NJ. See NJ document GIT-5 pages 5-7. There is a link from TP4F called NJ Gross Income Tax Publications (GIT-5 etc.2a).

### Entry into TSO

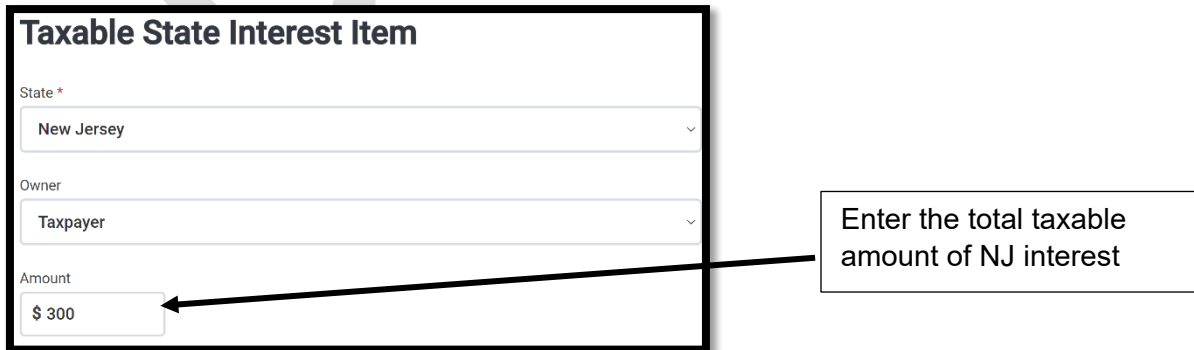
- Enter the amount from the paper Form 1099-INT line 8 into the TSO 1099-INT on line 8
- Using the information in items 1-2 above, determine the NJ taxability of each security
- Total those securities that are not tax exempt in NJ
- Click on “ADD INTEREST ITEMS” button on 1099-INT screen



Taxable State Interest

ADD INTEREST ITEMS

- Complete the state (NJ), owner of the document, and the amount taxable in New Jersey



**Taxable State Interest Item**

State \*  
New Jersey

Owner  
Taxpayer

Amount  
\$ 300

Enter the total taxable amount of NJ interest

- The amount shown in NJ line 16a taxable Interest will be the amount shown above.

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- The difference between the total exempt interest amount Box 8 and the amount entered above will be moved to NJ line 16b tax exempt-interest.

### Example:

Sam and Sally are filing a joint return and they have a 1099-INT that shows \$2,000 of Tax-Exempt Interest (Box-8). A call to the financial institution results in the following information:

- \$200 of the tax-exempt interest was from a New Jersey Turnpike Bond
- \$800 of the tax-exempt interest was from a California Freeway Bond
- \$1,000 of the tax-exempt interest was from a US Post Office Bond

Checking NJ GIT-5 pages 5,6, and 7 we find that the interest from the NJ Turnpike Bond and the US Post Office Bond is tax-exempt in NJ. The California Freeway Bond is not tax-exempt in NJ. The “ADD INTEREST ITEM” screen should read as follows:

### Taxable State Interest Item

State \*

New Jersey

Owner

Joint

Amount

\$ 800

Federal 1040-line 2a (tax-exempt interest) = \$2,000  
NJ 1040-line 16a (Taxable Interest) = \$800  
NJ 1040-line 16b (Tax Exempt Interest) = \$1,200

## Exempt Interest Dividends from Mutual Funds(Form 1099-DIV, Box-11)

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Exempt Interest Dividends are not dividends, but they are tax exempt interest that is reported on the 1099-DIV.

### Federal return

- The full amount of the interest is federally tax exempt
- Enter the amount in TSO 1099-DIV Box 11
- TSO carries the amount to the federal 1040-line 2a (Tax Exempt Interest)

### NJ return

- **NJ taxability varies**
- TSO carries the amount to line 16b (Tax Exempt Interest)
- Preparer determines how much is taxable and adjusts in TSO

### How to determine NJ taxability

1. Look in the brokerage statement for the details of the interest and determine which mutual funds generated the tax-exempt interest.
2. Find in the brokerage statement the table that shows the % of each security in each mutual fund. If the table is not in the brokerage statement, contact with the broker may be required.
3. Look at each fund that makes up the exempt interest dividends and determine if the fund is a NJ qualified investment fund. A NJ qualified investment fund invests 80% or more in securities that are exempt from NJ tax and it is qualified by the State of NJ. Usually, it has New Jersey in the name of the fund.

#### NJ Qualified investment fund (New Jersey in the name)

- Interest from all NJ tax exempt securities are NJ tax exempt in NJ
- Interest from federal debt obligations is tax exempt in NJ
- Interest from other sources is taxable

#### Non-qualified investment fund (New Jersey not in the name)

- Only interest from federal debt obligations is tax-exempt
- **All other interest including interest on NJ tax exempt securities are taxable**

#### 4. How do you determine taxability of Federal and New Jersey Debt Obligations?

- See NJ document GIT-5 pages 5-7. There is a link from TP4F called NJ Gross Income Tax Publications (GIT-5 etc).

### Entry into TSO

- Enter the amount from the paper Form 1099-DIV line 11 into the TSO document on line 11
- Using the rules in items 1-4 above, determine the taxable amount of NJ interest
- There is a link in the TSO 1099-DIV that reads “ADD DIVIDEND ITEMS”.
- Click “ADD DIVIDEND ITEMS”



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- Complete the state (NJ), owner of the document, and the amount taxable in New Jersey


### Taxable State Interest Item

State \*

Owner

Amount

Enter the total taxable amount of NJ interest



- The amount entered above will be moved to NJ line 16a Taxable Interest
- The difference between the exempt interest dividends amount and the amount entered above will be moved to NJ line 16b Tax Exempt Interest.

### Reminders

- Many of our senior taxpayers are eligible for the Retirement/Pension exclusion and Other Retirement Income exclusion that puts them below the NJ filing threshold. If a NJ return is filed for some reason, make all the exempt interest dividends taxable in NJ rather than going through the above process.
- If the interest that makes up the exempt interest dividends is all from non-qualified mutual funds, only the federal debt obligations are tax exempt on the NJ return

### References

- NJ 1040 Instructions
- NJ Tax Publication GIT-5
- NJ Special Handling

### Example

John is filing a Single return and he has a 1099-DIV in a brokerage statement that shows \$200.16 in Exempt Interest Dividends (Box 11). Looking at the interest detail in the brokerage statement we find that the exempt interest came from two mutual funds:

- \$50.16 from Dreyfus NJ Tax-Exempt Fund
- \$150 from Fidelity Municipal Tax-Exempt Fund

Looking further into the brokerage statement the following table was discovered showing the per-cent of each group of securities in the fund:

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	Dreyfus New Jersey Tax-Exempt Fund	Fidelity Municipal Tax-Exempt Fund
Puerto Rico Recovery Bonds	5%	9%
Federal Treasury Bonds	4%	1%
New York Thruway Bonds	8%	40%
New Jersey Turnpike Bonds	81%	45%
Misc	2%	5%

The Dreyfus NJ Tax Exempt Fund appears to be a NJ qualified fund (NJ is in the name). Therefore, all but the New York Thruway Bonds and the Misc. Bonds are tax exempt in NJ

$$50.16 \times (5\% + 4\% + 81\%) = \$45.14 \text{ is tax exempt for NJ}$$

$$50.16 \times (8\% + 2\%) = \$5.02 \text{ is taxable for NJ}$$

The Fidelity Municipal Tax-Exempt Fund does not appear to be a NJ qualified fund. Therefore, only the federal securities which include the Puerto Rico Recovery Bonds, and the Federal Treasury Bonds are tax exempt in NJ. This can be verified in NJ GIT-5.

$$\$150.00 \times (9\% + 1\%) = \$15.00 \text{ is tax exempt for NJ}$$

$$\$150.00 \times (40\% + 45\% + 5\%) = \$135.00 \text{ is taxable for NJ}$$

The total NJ taxable amount =  $\$5.02 + \$135.00 = \$140.02$

The "ADD DIVIDENDS ITEMS" screen should look like the following:

### Taxable State Interest Item

State \*

New Jersey

Owner

Taxpayer

Amount

\$ 140.02

### 1099-INT Boxes 10,11,12,13

Market discount bonds are bought below face value. Market discount is the difference between the bond's redemption price and cost. The taxpayer has the option to accrue the market discount over the period the taxpayer owns the bond.

- This accrued market discount is reported in box 10 of the 1099-INT.

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Bond premium bonds are bought above the face value. Bond premium is an additional amount paid over the total amount payable at maturity. Bond premiums paid are part of the bond's basis.

- The taxpayer has the **option** to amortize bond premium when the bond yields taxable interest.
  - The taxable interest is reduced by the bond premium
  - The basis of the bond is reduced by the bond premium deducted
- The taxpayer **must** amortize bond premium when bonds yield tax exempt interest
  - Tax-exempt interest is reduced by the tax-exempt bond premium (not visible on Schedule B)
  - Basis of the bond is reduced by the bond premium deducted

Entry into TSO – See Pub 4012-page D-9

- Box 10 – Enter value as you see it. Accrued market discount entered in box 10 will automatically be added to the interest in Box 1 and carried to Schedule B and the 1040.

### Example

1099-INT – Box 1 = 1000, Box 10=50

Schedule B

SCHEDULE B (Form 1040)		Interest and Ordinary Dividends		OMB No. 1545-0074
Department of the Treasury Internal Revenue Service (99)		▶ Go to <a href="http://www.irs.gov/ScheduleB">www.irs.gov/ScheduleB</a> for instructions and the latest information. ▶ Attach to Form 1040 or 1040-SR.		2020 Attachment Sequence No. 08
Name(s) shown on return JOE & JANE TAX		Your social security number XXX-XX-4321		
<b>Part I</b>	<b>1</b>	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see the instructions and list this interest first. Also, show that buyer's social security number and address ▶		<b>Amount</b>
<b>Interest</b>		ABC		1050
(See instructions and the instructions for Forms 1040 and 1040-SR, line 2b.)				
<b>Note:</b> If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.				
			<b>1</b>	
	<b>2</b>	Add the amounts on line 1 . . . . .	<b>2</b>	1050
	<b>3</b>	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815. . . . .	<b>3</b>	
	<b>4</b>	Subtract line 3 from line 2. Enter the result here and on Form 1040 or 1040-SR, line 2b . . . . .	<b>4</b>	1050

- Box 11 – Enter the value as you see it. If the box 11 amount is greater than the box 1 amount, the return is OUT OF SCOPE. The amortized bond premium entered in Box 11 will be carried to Schedule B as a negative adjustment.

### Example

1099-INT – Box 1 = 250, Box 11 = 25

Schedule B

# ST20-34 – Special Interest and Dividends Situations

SCHEDULE B (Form 1040)		Interest and Ordinary Dividends		OMB No. 1545-0074
Department of the Treasury Internal Revenue Service (99)		▶ Go to <a href="http://www.irs.gov/ScheduleB">www.irs.gov/ScheduleB</a> for instructions and the latest information. ▶ Attach to Form 1040.		Attachment Sequence No. <b>08</b>
Name(s) shown on return <b>TAXPAYER DOE</b>			Your social security number <b>100-00-0000</b>	
<b>Part I</b> <b>Interest</b> <small>(See instructions and the instructions for Form 1040, line 2b.)</small>  <b>Note:</b> If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.	<b>1</b>	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see the instructions and list this interest first. Also, show that buyer's social security number and address <b>BOND ISSUER</b>		<b>Amount</b>
				250
		<b>INTEREST SUBTOTAL</b>		250
		<b>ABP ADJUSTMENT</b>		-25
	<b>2</b>	Add the amounts on line 1 . . . . .	<b>2</b>	225
	<b>3</b>	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815 . . . . .	<b>3</b>	
	<b>4</b>	Subtract line 3 from line 2. Enter the result here and on Form 1040, line 2b . . ▶	<b>4</b>	225

- Box 12 – Enter the value as you see it. The amortized bond premium on Treasury Obligations entered in Box 12 will be carried to Schedule B as a negative adjustment.

### NJ Adjustment

Since the total interest on the Treasury Obligation is reduced the amount that is subtracted for NJ must also be reduced by the same adjustment.

### **Example**

1099-INT – Box 3=250, Box 12=25  
Schedule B

# ST20-34 – Special Interest and Dividends Situations

SCHEDULE B (Form 1040)		Interest and Ordinary Dividends		OMB No. 1545-0074
Department of the Treasury Internal Revenue Service (99)		▶ Go to <a href="http://www.irs.gov/ScheduleB">www.irs.gov/ScheduleB</a> for instructions and the latest information. ▶ Attach to Form 1040.		Attachment Sequence No. <b>08</b>
Name(s) shown on return <b>TAXPAYER DOE</b>			Your social security number <b>100-00-0000</b>	
<b>Part I</b> <b>Interest</b> (See instructions and the instructions for Form 1040, line 2b.)  <b>Note:</b> If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.	<b>1</b>	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see the instructions and list this interest first. Also, show that buyer's social security number and address <b>US T NOTE</b>		<b>Amount</b> <b>250</b>
		<b>INTEREST SUBTOTAL</b>		<b>250</b>
		<b>ABP ADJUSTMENT</b>		<b>-25</b>
	<b>2</b>	Add the amounts on line 1 . . . . .	<b>2</b>	<b>225</b>
	<b>3</b>	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815 . . . . .	<b>3</b>	
	<b>4</b>	Subtract line 3 from line 2. Enter the result here and on Form 1040, line 2b . . ▶	<b>4</b>	<b>225</b>

### NJ Adjustment

In TSO Interest Screen the “Amount of interest on US Savings Bonds and Treasury Obligations that you want to subtract from your state return” should be changed from 250 to 225.

- Box 13 – Enter the amount in box 13. Due to a bug in TSO, manually reduce the amount of tax-exempt interest in Box 8 by the amount in Box 13. There is no adjustment to Schedule B since tax exempt interest is not shown on Schedule B. There will be an adjustment made to the 1040 Line 2a.

### NJ adjustment

If all the tax-exempt interest was tax exempt in NJ, no action required.

If some of the tax-exempt interest was not tax exempt in NJ, you must determine which security had the amortized bond premium. If it was a NJ tax-exempt one, no action required. If it was a NJ taxable one, the “Add Interest Items” amount should be reduced by the Box 13 amount.



## ST20-34 – Special Interest and Dividends Situations

**Example** 1099-INT – Box 8=1200, Box 13=200  
TSO Interest Screen  
Before Adjustment

Tax Exempt Interest (Box 8)	\$ 1200
Specified Private Activity Bond (Box 9)	\$
Market Discount (Box 10)	\$
Bond Premium (Box 11)	\$
Bond Premium on Treasury Obligations (Box 12)	\$
Bond Premium on Tax-exempt bond (Box 13)	\$ 200

After Adjustment

Tax Exempt Interest (Box 8)	\$ 1000
Specified Private Activity Bond (Box 9)	\$
Market Discount (Box 10)	\$
Bond Premium (Box 11)	\$
Bond Premium on Treasury Obligations (Box 12)	\$
Bond Premium on Tax-exempt bond (Box 13)	\$ 200

NJ Adjustment: Let's assume two bonds made up the exempt interest. One was a NJ tax exempt bond with \$600 of exempt interest and the other a NJ taxable bond with \$600 of exempt interest.

1. The NJ tax-exempt bond had the amortized \$200 bond premium.
  - o By adjusting box 8 to \$1000, the total tax-exempt interest going to the federal 1040-line 2a and the NJ 1040 line 16b are reduced to \$1,000. No further action required.
2. The NJ taxable bond had the amortized \$200 bond premium.
  - o The total tax-exempt amount going to the federal 1040-line 2a is reduced By \$200 to \$1,000. The amount that goes into "Add Interest Items" must be adjusted by \$200 from \$600 to \$400.