

# IRS Difficulty of Care Payments

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## Difficulty of Care Payments IRS Notice 2014-7

If you provide care to an individual who has a physical, mental, or emotional handicap, the difficulty of care payments you receive are generally excluded from income. Review the information below to determine how to report these payments, if necessary, on your tax return.

According to the IRS website Certain Medicaid Waiver Payments May Be Excludable From Income:

On January 3, 2014, the IRS issued Notice 2014-7 addressing the income tax treatment of certain payments to an individual care provider under a state Home and Community-Based Services Waiver (Medicaid waiver) program. The notice provides that the IRS will treat "qualified Medicaid waiver payments" as difficulty of care payments excludable from gross income under § 131 of the Internal Revenue Code. For purposes of the notice, qualified Medicaid waiver payments are payments by a state, a political subdivision of a state, or a certified Medicaid provider under a Medicaid waiver program to an individual care provider for nonmedical support services provided under a plan of care to an individual (whether related or unrelated) living in the individual care provider's home.

**Exception:** Difficulty of care payments are **not** excludable to the extent that the payments are for more than 10 qualified foster individuals who have not attained age 19 or 5 qualified foster individuals who have attained age 19.

### Form 1099-MISC, Box 3:

Generally, amounts reported to you in Box 3 of Form 1099-MISC are reported on Form 1040, Line 21 as other income. However, if you choose to apply the Notice to payments received in 2016, you would not include the payments on Line 21. If you are filing electronically, do not report the Form 1099-MISC. If you file a paper return, write "Notice 2014-7" to the left of Line 21.

### **Form 1099-MISC, Box 7:**

Generally, amounts reported to you in Box 7 of Form 1099-MISC are reported on Schedule C as business income. If you choose to apply the Notice to payments received in 2016, you will enter the income on Schedule C through the Form 1099-MISC, but will also report the excludable amount as a Schedule C expense.

To enter the Form 1099-MISC, Box 7 income on Schedule C:

1. From within your TaxAct® return (Online or Desktop), click on the **Federal** tab. On smaller devices, click the menu icon in the upper left-hand corner, then select **Federal**
2. Click **Form 1099-MISC** to expand the category and then click **7-Nonemployee compensation**
3. Select **Schedule C, Profit or Loss from Business** and then click **Continue**. Note, if you have already created a Schedule C, click **Add** to create a new copy of the form or click **Review** to review a form already created. If not, the program will proceed with the interview questions for you to enter or review the appropriate information.

Once you have entered the Form 1099-MISC income, the program will bring you through additional screens to complete the Schedule C. To enter the excludable amount as an expense, continue to the screen titled **Business Income - Expenses**, and click **Yes**. Continue to the screen titled **Business Income - Expenses** with an entry field for **Qualified Medicaid waiver payments exclusion (Notice 2014-7)**. Enter the excluded amount on this screen.

### **Form W-2:**

Generally, amounts reported to you in Box 1 of Form W-2 are reported on Form 1040, Line 7 as wages. If you choose to apply the Notice to payments received in 2016, you will enter the income in the Wages and Salaries section of the Federal Q&A, but will also report the excludable amount as a negative adjustment on Form 1040, Line 21.

To enter the Form W-2:

1. From within your TaxAct return (Online or Desktop), click on the **Federal** tab. On smaller devices, click the menu icon in the upper left-hand corner, then select **Federal**
2. Click **Wages and Salaries** to expand the category and then click **Wage income reported on Form W-2**
3. Click **Add** to create a new copy of the form or click **Review** to review a form already created
4. Click **Quick Entry** or **Step-by-Step Guidance**
  - a. If you select **Quick Entry**, fill in the form to match your paper copy of Form W-2 and be sure to scroll down to answer questions.
  - b. If you select **Step-by-Step Guidance**, the program will proceed with the interview questions for you to enter or review the appropriate information.

To enter the adjustment on Form 1040, Line 21:

1. Click on the **Federal** tab. On smaller devices, click the menu icon in the upper left-hand corner, then select **Federal**

2. Click **Other Income** to expand the category and then click **Prizes, awards and other miscellaneous income**
3. On the screen titled **Miscellaneous - Amounts Received**, enter the excluded amount in the field for **Medicaid waiver payments to care provider**.

When you print your return, the text **See Attached** will print to the left of Line 21 on the Form 1040. An attached sheet will print with the return titled **Other Income - Supporting Details for Form 1040, Line 21** which will print both the description and amount that was entered.

**Additional Information:**

- Please understand, the Notice 2014-7 exclusion only applies to income tax. It does not address when these payments are subject to FICA tax (i.e. Social Security and Medicare taxes). The IRS has not yet provided guidance on this matter.
- Generally the payor should not issue a Form W-2 or 1099-MISC if they know the difficulty of care payments are excludable from your income. If you receive a Form W-2 or 1099-MISC reporting excludable difficulty of care payments, notify the payor that you are choosing to exclude the payments from your gross income. They should file and issue a corrected Form 1099-MISC or Form W-2c. Otherwise, use the information above to report the income and exclusion.
- The IRS is allowing taxpayers who received and reported payments in prior years to amend those prior year returns in order to exclude the income based on the new rules outlined in Notice 2014-7. Generally, for a credit or refund, you must file Form 1040X within 3 years (including extensions) after the date you filed your original return or within 2 years after the date you paid the tax, whichever is later.

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**Audit Assistant**

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