CAVARMA

NCBankers

rma CAROLINAS-VIRGINIAS

COMMERCIAL LENDING SCHOOL

Personal Tax Returns

Agenda

Develop a better understanding of the structure of tax returns

- Develop a systematic approach to reviewing a tax return
- Recognize fluctuations from year to year
- Learn to ask relevant questions
- Distinguish tax returns from financial statements

What is True Cash Flow?

Is it Cash?

- Depreciation is what we typically think of as a non-cash item; Personal returns include some depreciation
- Other non-cash items on a Personal Tax Return:
    - Standard and Other Deductions
    - Tax Credits
    - Taxable Benefits

Is it Recurring?

- Can the bank count on this income for 5-30 years for loan repayment?
- Consider large amounts of interest and dividend income
- Capital Gains are often non-recurring (inheritance, stock options, gambling winnings)
- Are wages always recurring?

Is it Consistent?

- Can the bank rely on computed cash flow for 5-30 years for loan repayment?
- Review trends of interest, dividends, and capital gains
- Is business pass through income steady year-over-year?
- Is retirement income fixed and is there adequate balances to maintain distributions?

What is True Cash Flow?

Capital Gains

Purchase 1 share of Berkshire Hathaway Class A for	$750,000
Sell 1 share of Berkshire Hathaway Class A for	$800,000
Gross Profit	$ 50,000
Capital Gain that is taxable	$ 50,000

Short Term Capital Gain tax rate (<1 year) is taxpayers marginal tax rate ranging from 10% to 37% (2025)

Long Term Capital Gain tax rate (> 1 year) is 0%, 15%, or 20% depending on your taxable income (2025)

Presume a 20% Long Term Capital Gain tax of	$ 10,000

What is the effective cash flow of this transaction?

Is it recurring and consistent?

Capital Losses

Purchase 100 shares of Tesla ($450) for	$45,000
Sell 100 shares of Tesla ($250) for	$25,000
Gross Loss	($15,000)
Capital Loss that reduces tax	$15,000

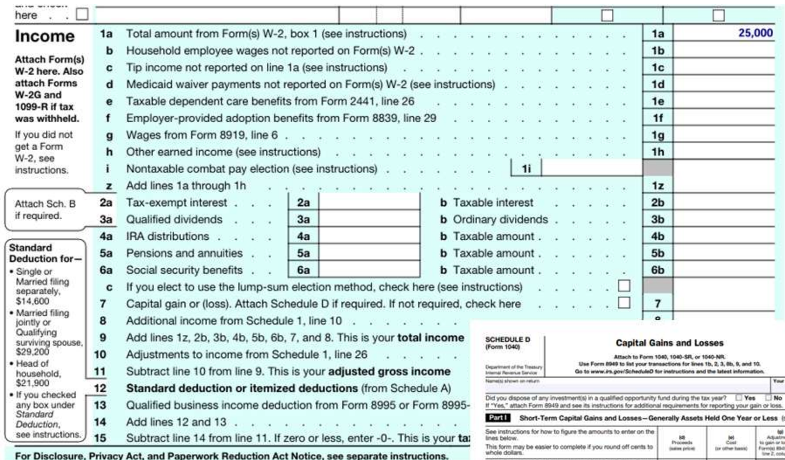
Capital Losses can offset similar Capital Gains in the same year; Short Term can offset Short Term and Long Term can offset Long Term

If Capital Losses outstrip Capital Gains, a taxpayer is limited to $3,000 in Capital Losses that may offset ordinary income

What is the effective cash flow of this transaction?

Is it recurring and consistent?

Capital Gains within a Tax Return



here . . ☐

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

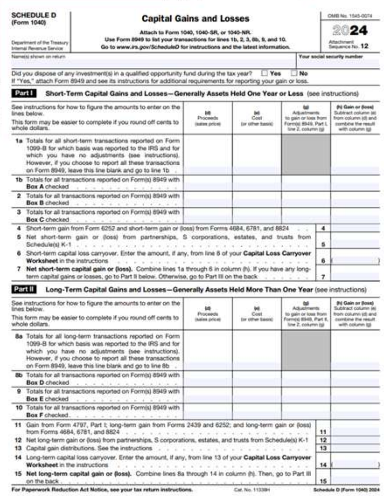
If you did not get a Form W-2, see instructions.

Attach Sch. B if required.

Standard Deduction for—
- Single or Married filing separately, $14,600
- Married filing jointly or Qualifying surviving spouse, $29,200
- Head of household, $21,900
- If you checked any box under *Standard Deduction*, see instructions.

1a	Total amount from Form(s) W-2, box 1 (see instructions)			1a	25,000
b	Household employee wages not reported on Form(s) W-2			1b	
c	Tip income not reported on line 1a (see instructions)			1c	
d	Medicaid waiver payments not reported on Form(s) W-2 (see instructions)			1d	
e	Taxable dependent care benefits from Form 2441, line 26			1e	
f	Employer-provided adoption benefits from Form 8839, line 29			1f	
g	Wages from Form 8919, line 6			1g	
h	Other earned income (see instructions)			1h	
i	Nontaxable combat pay election (see instructions)	1i			
z	Add lines 1a through 1h			1z	
2a	Tax-exempt interest	2a	b Taxable interest	2b	
3a	Qualified dividends	3a	b Ordinary dividends	3b	
4a	IRA distributions	4a	b Taxable amount	4b	
5a	Pensions and annuities	5a	b Taxable amount	5b	
6a	Social security benefits	6a	b Taxable amount	6b	
c	If you elect to use the lump-sum election method, check here (see instructions) ☐				
7	Capital gain or (loss). Attach Schedule D if required. If not required, check here ☐			7	
8	Additional income from Schedule 1, line 10			8	
9	Add lines 1z, 2b, 3b, 4b, 5b, 6b, 7, and 8. This is your **total income**				
10	Adjustments to income from Schedule 1, line 26				
11	Subtract line 10 from line 9. This is your **adjusted gross income**				
12	**Standard deduction or itemized deductions** (from Schedule A)				
13	Qualified business income deduction from Form 8995 or Form 8995-				
14	Add lines 12 and 13				
15	Subtract line 14 from line 11. If zero or less, enter -0-. This is your ta				

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions.



SCHEDULE D (Form 1040)
Department of the Treasury Internal Revenue Service

Capital Gains and Losses

Attach to Form 1040, 1040-SR, or 1040-NR.
Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.
Go to www.irs.gov/ScheduleD for instructions and the latest information.

OMB No. 1545-0074
2024
Attachment Sequence No. 12

Name(s) shown on return | Your social security number

Did you dispose of any investment(s) in a qualified opportunity fund during the tax year? ☐ Yes ☐ No
If "Yes," attach Form 8949 and see its instructions for additional requirements for reporting your gain or loss.

Part I **Short-Term Capital Gains and Losses—Generally Assets Held One Year or Less** (see instructions)

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 I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-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 1b				
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked				
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked				
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked				

4	Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824	4	
5	Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	5	
6	Short-term capital loss carryover. Enter the amount, if any, from line 8 of your **Capital Loss Carryover Worksheet** in the instructions	6	( )
7	**Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the back	7	

Part II **Long-Term Capital Gains and Losses—Generally Assets Held More Than One Year** (see instructions)

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				

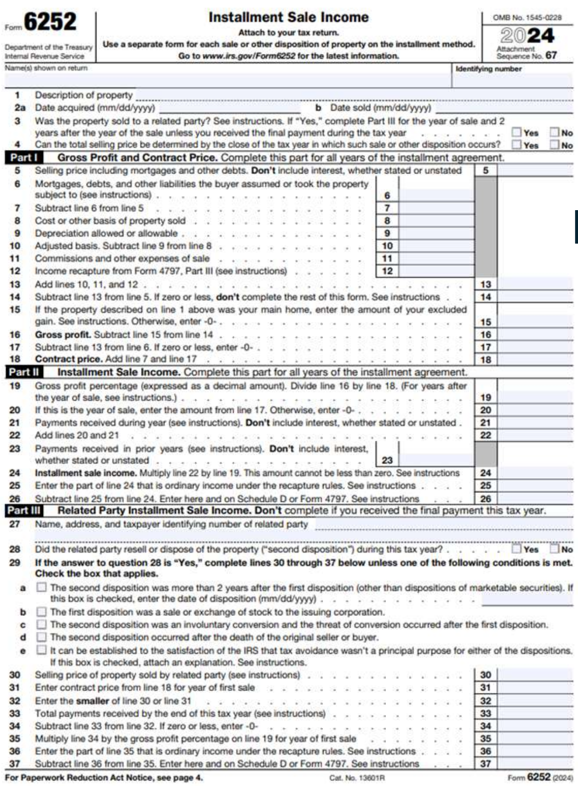
11	Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824	11	
12	Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	12	
13	Capital gain distributions. See the instructions	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	

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 11338H **Schedule D (Form 1040) 2024**

The sum of all Capital Gains is found on Line 7 of Page 1 of the taxpayer's 1040

Details of these transaction are found in Schedule D (with additional detail included as Statements if necessary)

Installment Sales



Form **6252** Department of the Treasury Internal Revenue Service

Installment Sale Income

Attach to your tax return.

Use a separate form for each sale or other disposition of property on the installment method.

Go to *www.irs.gov/Form6252* for the latest information.

OMB No. 1545-0228 2024 Attachment Sequence No. 67

Name(s) shown on return | **Identifying number**

1 Description of property

2a Date acquired (mm/dd/yyyy) **b** Date sold (mm/dd/yyyy)

3 Was the property sold to a related party? See instructions. If "Yes," complete Part III for the year of sale and 2 years after the year of the sale unless you received the final payment during the tax year ☐ **Yes** ☐ **No**

4 Can the total selling price be determined by the close of the tax year in which such sale or other disposition occurs? ☐ **Yes** ☐ **No**

Part I Gross Profit and Contract Price. Complete this part for all years of the installment agreement.

5 Selling price including mortgages and other debts. **Don't** include interest, whether stated or unstated — 5

6 Mortgages, debts, and other liabilities the buyer assumed or took the property subject to (see instructions) — 6

7 Subtract line 6 from line 5 — 7

8 Cost or other basis of property sold — 8

9 Depreciation allowed or allowable — 9

10 Adjusted basis. Subtract line 9 from line 8 — 10

11 Commissions and other expenses of sale — 11

12 Income recapture from Form 4797, Part III (see instructions) — 12

13 Add lines 10, 11, and 12 — 13

14 Subtract line 13 from line 5. If zero or less, **don't** complete the rest of this form. See instructions — 14

15 If the property described on line 1 above was your main home, enter the amount of your excluded gain. See instructions. Otherwise, enter -0- — 15

16 **Gross profit.** Subtract line 15 from line 14 — 16

17 Subtract line 13 from line 6. If zero or less, enter -0- — 17

18 **Contract price.** Add line 7 and line 17 — 18

Part II Installment Sale Income. Complete this part for all years of the installment agreement.

19 Gross profit percentage (expressed as a decimal amount). Divide line 16 by line 18. (For years after the year of sale, see instructions.) — 19

20 If this is the year of sale, enter the amount from line 17. Otherwise, enter -0- — 20

21 Payments received during year (see instructions). **Don't** include interest, whether stated or unstated — 21

22 Add lines 20 and 21 — 22

23 Payments received in prior years (see instructions). **Don't** include interest, whether stated or unstated — 23

24 **Installment sale income.** Multiply line 22 by line 19. This amount cannot be less than zero. See instructions — 24

25 Enter the part of line 24 that is ordinary income under the recapture rules. See instructions — 25

26 Subtract line 25 from line 24. Enter here and on Schedule D or Form 4797. See instructions — 26

Part III Related Party Installment Sale Income. Don't complete if you received the final payment this tax year.

27 Name, address, and taxpayer identifying number of related party

28 Did the related party resell or dispose of the property ("second disposition") during this tax year? ☐ **Yes** ☐ **No**

29 **If the answer to question 28 is "Yes," complete lines 30 through 37 below unless one of the following conditions is met. Check the box that applies.**

a ☐ The second disposition was more than 2 years after the first disposition (other than dispositions of marketable securities). If this box is checked, enter the date of disposition (mm/dd/yyyy)

b ☐ The first disposition was a sale or exchange of stock to the issuing corporation.

c ☐ The second disposition was an involuntary conversion and the threat of conversion occurred after the first disposition.

d ☐ The second disposition occurred after the death of the original seller or buyer.

e ☐ It can be established to the satisfaction of the IRS that tax avoidance wasn't a principal purpose for either of the dispositions. If this box is checked, attach an explanation. See instructions.

30 Selling price of property sold by related party (see instructions) — 30

31 Enter contract price from line 18 for year of first sale — 31

32 Enter the **smaller** of line 30 or line 31 — 32

33 Total payments received by the end of this tax year (see instructions) — 33

34 Subtract line 33 from line 32. If zero or less, enter -0- — 34

35 Multiply line 34 by the gross profit percentage on line 19 for year of first sale — 35

36 Enter the part of line 35 that is ordinary income under the recapture rules. See instructions — 36

37 Subtract line 36 from line 35. Enter here and on Schedule D or Form 4797. See instructions — 37

For Paperwork Reduction Act Notice, see page 4. Cat. No. 13601R Form **6252** (2024)

Installment Sales

Taxpayers receive three types of income from Installment Sales

- Taxable Principal (Schedule D, Form 6252)
- Non-Taxable Principal (Form 6252)
- Interest Income (Schedule B)

Considerations:

- Years left on note compared to your loan?
- Payment history (how do you know)?
- Amount of down payment?
- Who is the note from?

Recommend you obtain the following documents:

- Promissory Note
- Deed of Trust
- Assignment and Acknowledgement
- Contact the Obligee

Rental Properties – Active vs. Passive

Active and Passive Income Rules are applied to Real Estate and Pass Through Business Income

- *Passive Losses* are not available to offset *Active Income*

Example – A medical professional's rental property losses are not available to offset wage income

- Rental real estate by IRS definition is considered Passive Income or Passive Loss
- Unused Passive Losses can be carried forward to offset future Passive Income
- Small Investor Exception:
    - Must be active in rental activity
    - Must have 10% or more ownership
    - MAGI must be under $100,000 (phases out up to $150,000)

Active Income	Passive Income
• Wages, Interest Dividends • Income from Partnerships and S-Corps	• Income from Partnerships and S-Corps • Rental Real Estate

Active Losses	Passive Losses
• Losses from Partnerships and S-Corps	• Losses from Partnerships and S-Corps • Rental Real Estate

	Passive Income and Loss		Nonpassive Income and Loss		
	(g) Passive loss allowed (attach Form 8582 if required)	(h) Passive income from Schedule K-1	(i) Nonpassive loss allowed (see Schedule K-1)	(j) Section 179 expense deduction from Form 4562	(k) Nonpassive income from Schedule K-1
A					
B					
C					
D					
29a Totals					
b Totals					
30 Add columns (h) and (k) of line 29a				30	
31 Add columns (g), (i), and (j) of line 29b				31	( )
32 **Total partnership and S corporation income or (loss).** Combine lines 30 and 31				32	

CAVARMA COMMERCIAL LENDING SCHOOL

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In Class Case Study

- Peter and Bunny Gammons

Peter and Bunny Gammons

Background:
- Peter works as a farm equipment sales representative.
- Bunny works as a nurse at a local hospital and also owns a sole proprietorship consulting business.
- The couple wishes to discuss a loan to purchase some equipment they have been renting for the sole proprietorship business.
- The Gammons are large landowners; they sold timber rights on their land to Weyerhaeuser for $1.2 million and have a 10-year contract with Weyerhaeuser that will pay them $120,000 per year.
- A few years ago, they sold a parcel of land to Joseph Clark for $250,000.
- The Gammons took a note back on the land sale and are being paid in equal installments of $38,955 per year (principal and interest) over 15 years.
- In December, the Gammons donated half of their IBM stock to their church.
- The Gammons also own a rental house.

What is there recurring source of cash flow using the following

The case will include the following:
- Personal 1040 – U.S. Individual Income Tax Return
- Schedule 1 – Additional Income and Adjustments to Income
- Schedule 2 – Additional Taxes
- Schedule A – Itemized Deductions
- Schedule B – Interest and Ordinary Dividends
- Schedule C – Profit or Loss From Business (Sole Proprietorship)
- Schedule D – Capital Gains and Losses
- Form 6252 – Installment Sale Income
- Schedule E – Supplemental Income and Loss (Rental Property)
- Form 4562 – Depreciation and Amortization
- Form 8283 – Noncash Charitable Contributions
- Form 4797 – Sales of Business Property

Case Studies

- Cooper
- Rubble