

STUDENT TEXT
For Use in Preparing Tax Year 2003 Returns

VOLUNTEER ASSISTOR'S GUIDE



FOR USE IN IRS VOLUNTEER PROGRAMS

VITA Volunteer Income Tax Assistance

TCE Tax Counseling for the Elderly

To get the most up to date tax products and information visit our World Wide Web site at: www.irs.gov



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IRS VOLUNTEERS

The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.



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Confidentiality Statement:

All tax information you receive from taxpayers in your VOLUNTEER capacity is strictly confidential and should not, under any circumstances, be disclosed to unauthorized individuals.

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Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1-800-THE-LOST (1-800-843-5678)** if you recognize a child.



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

WAGE AND INVESTMENT DIVISION

NOV 07 2003

WELCOME, VOLUNTEERS!

Through the assistance of trained volunteers from the Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs, the Internal Revenue Service and its partners across the nation and abroad are able to offer free tax help to taxpayers having low-to-moderate income. As a volunteer, you will help prepare tax returns for a taxpayer segment which often includes seniors, disabled persons, people with limited English proficiency, and others who cannot afford professional tax assistance.

This publication will help you to acquire the skills to prepare basic tax returns. There are two tracks to certification – the Wage Earner and the Pension Earner. The Wage Earner track covers issues working individuals and families customarily face. The Pension Earner track contains more complex issues, those generally encountered by retired people and senior citizens. These tracks allow instructors to train volunteers in specific tax issues encountered at the volunteer sites. For instance, a TCE class might certify their volunteers on the Pension Earner track that does not include training on the Earned Income Tax Credit (EITC). If the instructor or the site coordinator anticipates that taxpayers coming into the site will be eligible for the EITC, he/she can also teach, test, and certify volunteers on the EITC chapter, a portion of the Wage Earner track.

I urge you to electronically file (*e-file*) the returns you prepare. Electronic filing (*e-filing*) uses automation to quickly check for errors or missing information. Consequently, *e-filed* returns have a higher accuracy rate than paper prepared returns. As technology changes the face of filing taxes, we recognize that it will impact every aspect of volunteer training. In fact, the 2003 edition of our volunteer training materials employs a new integrated training feature that bridges the gap between paper-based training of the past and web-based training of the future. We are working to make this training as convenient and versatile as possible.

In performing this service to your fellow taxpayers, I appreciate your steps to safeguard the personal and sensitive documents or files that you may encounter. Preserving the privacy of those persons you assist is key to the preservation of the integrity embedded in the VITA/TCE Programs.

I welcome your comments and recommendations about our training material. Your instructor or site coordinator can take your suggestions or you can write to us at the following address:

Internal Revenue Service
Stakeholder Partnerships, Education and Communication
SE:W:CAR:SPEC:PPD:E, Stop 45-W1
401 W. Peachtree Street, NW
Atlanta, GA 30308

Thank you in advance for your willingness to volunteer your own time to provide this much needed service to your neighbors and your community.

Sincerely,

Mark E. Pursley
Director, Stakeholder Partnerships,
Education and Communication

Important Tax Law Changes for 2003

Exemption amount increased. The amount each taxpayer can deduct for each exemption has increased from \$3,000 to \$3,050.

Standard deduction amount increased. The standard deduction (for taxpayers that do not itemize deductions on Schedule A (Form 1040)) is higher in 2003 than it was in 2002. In addition, the standard deduction for married taxpayers filing jointly is twice the amount for single filing status.

Married filing jointly & Qualifying Widow(er)	\$9,500
Head of Household	\$7,000
Single	\$4,750
Married Filing separately	\$4,750

Increase in 10% tax bracket. The 10% tax bracket has been increased from \$6,000 to \$7,000 (\$12,000 to \$14,000) for joint filers.

Increase in 15% bracket for married filing jointly status. The 15% tax bracket has been increased to twice that of single filers.

Marginal tax rates reduced. The rates are reduced to 25%, 28%, 33%, and 35% retroactively effective January 1, 2003.

Capital gains rate reduced. The rate has reduced from 20% to 15% (from 10% to 5% for taxpayers in the 10 and 15 percent brackets) effective on or after May 6, 2003 through December 31, 2008. In 2008, the capital gains rate will drop to 0% for lower-income tax taxpayers. The lower rates will apply to both regular tax and alternative minimum tax.

Certain dividends taxed at capital gains rates. The same rates apply to both foreign and domestic companies' dividends. Lower-income taxpayers will pay 5% on dividends paid between January 1, 2003 and December 31, 2007 and 0% in 2008. Taxpayers in tax brackets above 15 % would pay 15 % on dividends paid between January 1, 2003 and December 31, 2008.

Standard mileage rate. The standard mileage rate for the cost of operating a car in 2003 is 36 cents a mile for all business miles. The 2003 rate for use of a vehicle for medical care and moving expenses is 12 cents a mile.

Household employer's income reporting requirement. In 2003, household employers are required to issue a Form W-2 to employees whose earnings are \$1400 or more.

Lifetime learning credit. Beginning in 2003, the amount of the qualified tuition and related expenses you may take into account in figuring your lifetime learning credit increases from \$5,000 to \$10,000. The credit will equal 20% of qualified expenses, with the maximum credit being \$2,000.

Student loan interest deduction. Beginning in 2003, the modified adjusted gross income ranges for phasing out the student loan interest deduction may be adjusted annual for inflation.

Child tax credit increased. The child tax credit has been increased to \$1,000 for 2003. An early refund of the 2003 Child Tax Credit was issued to eligible taxpayers who claimed the child tax credit on their 2002 tax return and had a qualifying child that was born after 1986. Taxpayers that received the “early refund” Advance Child Tax Credit payment must include the amount received when calculating the 2003 Child Tax Credit.

Earned Income Credit (EIC) Limits: For 2003, the investment, earned income, and adjustment gross income for the EIC are:

Investment income is \$2,600 or less.

Total earned income must be at least \$1 but less than:

- \$33,692 (\$34,692 if married filing jointly) and more than one qualifying child.
- \$29,666 (\$30,666 if married filing jointly) and one qualifying child.
- \$11,230 (\$12,230 if married filing jointly) and no qualifying child.

Adjusted gross income less than:

- \$33,692 (\$34,692 if married filing jointly) and more than one qualifying child.
- \$29,666 (\$30,666 if married filing jointly) and one qualifying child.
- \$11,230 (\$12,230 if married filing jointly) and no qualifying child.

Child and dependent care credit. Significant changes to the child and dependent care credit take effect in 2003.

The credit amount can be as much as 35% (previously 30%) of qualifying expenses.

The maximum adjusted gross income amount that qualifies for the highest rate increases to \$15,000 (previously \$10,000).

The limit on the amount of qualifying expenses increases to \$3,000 for one qualifying individual and \$6,000 for two or more qualifying individuals.

The amount of income that is treated as having been earned by a spouse who is either a full-time student or not able to care for himself or herself increases. This amount increases to \$250 a month if there is one qualifying individual and \$500 a month if there are two or more qualifying individuals.

Tax benefit for adoption. The adoption credit and the exclusion from income of benefits under an adoption assistance program for the adoption of a child with special needs is \$10,160 regardless of the amount of qualified adoption expenses. The modified adjusted gross income limit will be adjusted annually for inflation.

Traditional Individual Retirement Account (IRA) income limits. The amount of income taxpayers can have and not be affected by the deduction phase-out increases. The amounts vary depending on filing status and impacts taxpayers that have a traditional IRA and are covered by a retirement plan at work. For further information go to www.irs.gov.

Deemed IRAs. For plan years beginning after 2002, a qualified employer plan (retirement plan) can maintain a separate account or annuity under the Plan (a deemed IRA) to receive voluntary employee contributions. An employee’s account can be treated as a **traditional IRA** or a **Roth IRA**.

The Health Coverage Tax Credit (HCTC). The HCTC was introduced by the Trade Act of 2002 to assist certain taxpayers. Potentially eligible taxpayers receive a HCTC Program Kit in the mail. This credit is primarily available to workers who have lost

their jobs due to the effects of international trade and taxpayers over age 55 who receive benefits from the Pension Benefit Guaranty Corporation. Calculation of the credit is outside of the scope of the volunteer programs. For further information go to www.irs.gov

Increase in Alternative Minimum Tax Exemption. Increased to \$40,250 for single and head of household taxpayers; \$58,000 for Married Filing Jointly and Qualified Widow(er)s; and \$29,000 for Married Filing Separately taxpayers.

STUDENT NOTES

INTRODUCTION AND ADMINISTRATIVE GUIDELINES

Welcome to the Internal Revenue Service's (IRS) Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs! These volunteer programs are very important to the IRS, our partners and the community. As an IRS volunteer you provide a tremendous service to the American public and to your community. You are about to embark on a very challenging and rewarding task as an important player in tax administration.

Every year thousands of volunteers assist millions of taxpayers with their federal return. The people receiving your assistance need it the most. They are those with low to moderate incomes, individuals with disabilities, limited English proficient, and elderly taxpayers. Thank you for your hard work and dedication!

This section highlights important changes to the VITA and TCE programs.

VITA/TCE Site Identification Number: We will capture all of our statistics from internal reports. Each paper or electronically filed return should be identified with the appropriate "Site Identification Number". This will ensure that all volunteer prepared returns are correctly counted once received by the Internal Revenue Service.

Site Identification Number (Site IDN). Your site IDN is an 8-digit number preceded by the "letter P" that must be entered on all returns (Forms 1040, 1040A, and 1040EZ) you prepare—both paper and electronic. Your site coordinator provides this number along with other necessary guidelines for completing the return.

The Site identification number should appear in the "Paid Preparer's Use Only" section of the return and will be discussed in detail in Lesson 6, Finishing the Return.

EVALUATION PROCESS

A new procedure is in place for student evaluation of the VITA/TCE training and course material. Beginning with training for filing season 2004, a new evaluation form is included in your training materials. It is a scannable form designed for IRS employees but we believe it provides the questions we need to evaluate both your training and our course materials. Your instructor will give you specific instructions on completing the form. If you are taking this course self-study, please contact your local IRS SPEC office or your site manager for details. Your instructor will also give you information on how to complete this form on the internet and transmit directly to the vendor who will compile the evaluations

OTHER IMPORTANT ADMINISTRATIVE INFORMATION

Social Security Cards: One of the primary reasons for the rejection of a return or a delay in processing a return is an incorrect SSN. It is important, therefore, that you check the accuracy of each SSN, as well as the spelling of the name associated with the number.

e-file: Each year the IRS contracts with a software developer to provide tax return preparation software. All returns prepared using the software should be electronically filed. The only exception is when a return is transmitted electronically to the IRS and you experience unworkable rejects.

SCOPE AND SEQUENCE

Most taxpayers are either wage earners or pension earners. Therefore, we have organized this training material in three modules: basic, wage earner, and pension earner. There are instances where a site serves both wage earners and pension earners. Your instructor has worked closely with the coordinator(s) at the site where you will assist taxpayers to determine which lessons you should learn.

Basic Module

All volunteers must complete the following lessons:

Introduction

Lesson 1—Getting Started

Lesson 2—Income

Lesson 3—Adjustments

Lesson 4—Standard Deduction and Itemized Deductions

Lesson 5—Credit for Qualified Retirement Savings Contributions, Mortgage Interest, and Foreign Tax Credit

Lesson 6—Finishing the Return

Wage Earner Module

Volunteers who will be assisting wage earners need to complete the following lessons:

Lesson 7—Credit for Child and Dependent Care

Lesson 8—Education Credits

Lesson 9—Earned Income Tax Credit

Lesson 10—Child Tax Credit

Pension Earner Module

Volunteers who will be assisting pension earners are required to complete the following lessons.

Lesson 11—Sale of Stock

Lesson 12—Sale of Home

Lesson 13—Pensions

Lesson 14—Credit for Elderly or Disabled

Those who are taking this training with the expectation of becoming instructors themselves must learn all lessons.

The sequence of lessons generally follows the order of topics on the tax returns which you will complete at the volunteer site. In a few instances, this does not parallel the order of the tax form itself. For example, while the entity section (taxpayer's name, address, and social security number) appears first on the form, it is covered in the lesson on finishing the return since it is one of the last things to do when completing the return. (Have you ever tried to peel off one of the stick-on labels after you have found an error on the return?)

It is very important for you to assist only with returns and supporting schedules and forms for which you have been trained. If you go beyond your training, you risk making errors and causing difficulties for those you wish to help. Refer taxpayers with difficult returns, or with portions of returns that are beyond the scope of your training to a paid professional tax preparer.

There are separate training materials available for the following categories of taxpayers:

Publication 678FS—Foreign Students and Scholars

Publication 678M—Military/International Student Text

Publication 678PR—Tax Issues for Puerto Rico

As a volunteer, you are not allowed to charge for your services. This includes taxpayer return preparation advice and return preparation. You may at times need to remind taxpayers that the assistance that you are providing is **FREE**. Do not solicit or accept donations on behalf of the VITA or TCE sponsor, or any other individual or organization, while providing assistance in this program.

Assisting taxpayers includes helping to make sure they are aware of their rights. Publication 1, *Your Rights as a Taxpayer*, is available free, from the IRS. Taxpayers can help ensure that they receive fair treatment in tax matters when they are aware of their rights.

Testing

All volunteers must take the applicable test to show that they can complete returns accurately. You may use this text and all reference materials to complete the test. Volunteers who do not pass the test may take the appropriate retest. Instructions on taking and grading the test are in the Test and Retest Booklets.

Proof Copies of Forms

Forms imprinted in this publication were current as of the “draft” date shown on each form. Final forms may be found at www.irs.gov and may have supplemental changes. **Be sure to compare the final forms with those in this publication and make sure you understand processing changes (if any) before helping taxpayers with their returns.**

Exercises and Exhibits

It is important that you take the time to complete the exercises to achieve the objectives in each lesson. Studies have shown that long-term retention of information increases dramatically if you put pencil to paper in responding to questions and problems. The Volunteer Assistor's Guide is your learning tool and you may mark it up in any way you wish.

Note: Answers to all exercises are available at the end of the lesson.

Each exercise is separated from the rest of the text by a border design. Write out your answer to each exercise, and then check it immediately against the answer provided. If your answer is different, work the problem again. If you need additional reinforcement, review any parts of the text that apply.

The exercises are designed to give you practice, to emphasize what we think is important, and to help you complete your training successfully.

The coursebook contains a large number of exhibits of the various tax forms and schedules. These exhibits are numbered starting at the beginning of each lesson. Many of the exercises contain exhibits of blank forms, or part of the form, that you must complete.

Lesson Features

Introduction

There is a brief **Introduction and Objectives** section to each lesson. This will give you an overview of the topic to be covered, as well as an idea of how you will most likely be asked to apply the information when helping taxpayers. The objectives will clearly define the key points for mastery of the topic. They not only help you focus your reading, but also help you check for understanding.

"Summing Up This Section, Segment or Lesson"

This boxed feature appears at the end of each lesson. It provides you with a summary of the main points covered in the lesson. Used together, the lesson summaries provide a comprehensive overview of the course content.

Sidebar Features

Sidebar features appear in the outer margins (left and right) of the text. These boxed features emphasize important points presented in the lesson, or provide additional, related information. **Potential Pitfalls** point out commonly made errors and indicate ways to avoid these errors. **Alert!** identifies pending legislation, tax law changes, or tax forms changes that were expected, but not enacted or in final form when this publication went to print. As a volunteer please confirm that you have the latest information on the tax law and forms before assisting your clients.

ALERT—**CONFIDENTIALITY
AND INTEGRITY**

All tax information you receive from taxpayers in your VOLUNTEER capacity is strictly confidential and should not, under any circumstances, be disclosed to unauthorized individuals. See your site coordinator for additional information.

Taxpayers come to you for help. To provide appropriate assistance, you will be asking very personal questions about the taxpayers and their families, their sources of income, and their expenses. Taxpayers will give this information only if they trust and have confidence in you. **To maintain the taxpayer's trust and confidence, DO NOT disclose any personal tax information you learn as a result of the assistance you provide.**

Taxpayers can be amazingly frank about their personal lives. When taxpayers share extremely personal information with you, this creates a responsibility for you not to discuss the information with other taxpayers or fellow volunteers. Never use a taxpayer's name in the presence of other taxpayers.

However, volunteers may discuss tax situations with other taxpayers and volunteers. For example, a volunteer may refer to a situation (not a taxpayer) and ask or give advice about the appropriate tax treatment for that specific situation.

The VITA and TCE Programs offer free tax assistance. You cannot accept payment nor any type of gratuity for preparing a federal tax return or for other tax-related assistance that you provide. If you accept payment for preparing a tax return, you are considered a "paid preparer." Paid preparers are legally liable under federal law for the returns they prepare; volunteers are not.

An important aspect of integrity for volunteer assistors is declining to prepare a tax return when there is a question about the validity of the information supplied by a taxpayer. Some individuals may attempt to defraud the government by filing false tax returns.

Volunteers who are not comfortable with the information provided by a taxpayer because of any reason, should discuss their concerns with their Site Coordinator or other individual in charge of the site.

QUALITY OF SERVICE

The goal of the TCE and VITA Programs is to provide high quality service. The following list suggests some ways to ensure that each return is prepared correctly:

- Where possible prepare the return using electronic filing software.
- Use a calculator to check your math (paper returns).
- Refer to your Publication 17, other IRS publications and job aids for help with complicated topics.
- Use the checklists and worksheets provided.
- Consult with other, more experienced, volunteers.
- Call the Volunteer Hotline (described later in this lesson).

Volunteer Hotline

There is a toll-free hotline available for VITA and TCE volunteer use only. This hotline is a source of tax information for volunteers. When you use the hotline, identify yourself as a VITA or TCE volunteer.

The hotline number is 1-800-829-8482 (829-VITA). **Do not give this number to taxpayers.** This service is generally available between February 1 and April 15th.

Do not use this hotline to order forms or schedules. Instead, contact your IRS Territory Manager.

EFFECTIVE INTERVIEWING

To complete accurate returns, you must ask certain questions about the taxpayers and their families. It is important to set the appropriate climate to obtain this information.

It is also important to be sensitive to the needs of all taxpayers you assist, especially those with disabilities. All references to taxpayers with disabilities should reflect the individuality, equality and dignity of the person.

Refrain from using such terms as “handicapped, physically or mentally challenged, differently challenged”. It would be better to use:

Person(s) with a disability;

Persons who are blind; persons who are visually impaired;

Persons who are deaf; persons who are hearing impaired or hard of hearing;

Persons who use a wheelchair;

Persons who are physically disabled; or, persons with mental retardation.

Steps to Effective Interviewing:

1. Make necessary introductions and engage in small talk.
2. Preface what will take place during the interview.
3. Share your intentions and any hopeful results/benefits for the taxpayer.
4. Allow the taxpayer to share any expectations, needs, and/or concerns.
5. Respond with active listening skills.
 - A. Create a “safe” climate.
 - B. Remember your nonverbal listening clues.
 - C. Listen, then respond by:
 1. restating,
 2. paraphrasing, (and/or)
 3. encouraging
6. Ask the first key tax question, creating an awareness about why the tax information is needed.
 - A. Make no assumptions.
 - B. Ask no leading questions.
 - C. Ask, “What have you brought with you today?”
7. Continue to ask questions. Define any terms that may be unfamiliar to the taxpayer.
8. Check your own comfort level.
9. Respond to any misunderstandings.
10. Continue with effective questioning and active listening.
11. Overcome any communication barriers.
 - A. Stay on track. (“I hear you.”/repeat question)
 - B. Allow adequate response time.
 - C. Avoid making assumptions.
 - D. Deal with taxpayers.
 1. Silent (“tell me more about...”)
 2. Upset (paraphrase)
 - E. Concentrate.
12. Indicate the taxpayer’s next steps. Inform the taxpayer about the VITA/TCE Programs and stress the benefits of accurate recordkeeping.
 - A. Express confidence in having completed an accurate tax return.
 - B. Part cordially.

Use these questions and answers to provide quick and accurate information to taxpayers who have administrative questions.

1. What is the CHIP Program?

The Children's Health Insurance Program (CHIP) is designed to help millions of children of working families obtain affordable and much-needed health insurance. CHIP informational materials are available at IRS Tax Assistance Centers and Volunteer Income Tax Assistance (VITA) sites. CHIP information (i.e. brochures, flyers) should be provided to VITA sites prior to the filing season. Volunteers at VITA site locations are not expected to answer any questions pertaining to this program, just to make information available to taxpayers visiting their sites.

2. How can I direct someone to their closest AARP sponsored Tax-Aide Site?

AARP Tax-Aide operates a toll-free nationwide number to help people find their closest Tax-Aide Site. The number is 1-888-227-7669. The information is also available on the AARP web page. The address is www.aarp.org/taxaide.

3. What if a taxpayer or dependent does not have a social security number?

Social security numbers are required for all taxpayers and dependents. Taxpayers who do not have a social security number must apply for one by using Form SS-5, *Application for a Social Security Card*. This form is available from the Social Security Administration and U.S. Citizens must show proof of age, identity, and citizenship when they apply for a social security number. Individuals who are age 18 or older must apply at the Social Security Administration office in person rather than by mail.

4. Who needs an Individual Taxpayer Identification (ITIN) Number?

An ITIN is available for certain resident and nonresident aliens, their spouses, and their dependents who are not eligible for a SSN. To obtain an ITIN, you must complete, sign, and submit IRS Form W-7, Application for IRS Individual Taxpayer Identification Number to the Internal Revenue Service with proper documentation to support your status.

5. What if the taxpayer needs an IRS form or publication?

Most IRS offices and many post offices and libraries have IRS forms that taxpayers may take or photocopy. They also have the instruction booklets for specific forms and publications. Remind the taxpayer that forms can also be ordered by calling the IRS on 1-800-829-3676 (1-800-TAX FORM) or from a fax machine dial (703) 487-4160.

IRS offers tax products and information on the Internet. The IRS Internet site provides instant access to federal income tax forms, instructions, publications, and information on free tax assistance programs, electronic tax filing, and more 24 hours a day. Current and prior year federal tax products and information are available for downloading.

By Internet:

1. World Wide Web – www.irs.gov
2. FTP – [ftp.irs.ustreas.gov](ftp://ftp.irs.ustreas.gov)
3. Telnet – [iris.irs.ustreas.gov](telnet://iris.irs.ustreas.gov)

6. What if the taxpayers move?

Taxpayers should use Form 8822, *Change of Address*, to notify the IRS of any change of address. If the taxpayers plan to move after sending the return and before a refund is received, they should notify their old post office and the IRS of their new address. (See item #4 for information on how to order Form 8822.)

7. Which address should taxpayers use, their street address or their post office box?

If the post office delivers mail to the post office box rather than to a street address, enter the P.O. box number on the line for the present home address.

8. What if the taxpayer needs a copy of a prior year return?

To obtain a copy of a prior-year return, taxpayers should complete Form 4506, *Request for Copy or Transcript of Tax Form*, and mail it, with the required fee, to the Internal Revenue Service Submission Processing Center where the return was filed. As an alternative, a transcript of a prior-year return may be obtained, also using Form 4506. There is no charge for the transcript. A transcript shows most line items from the original return, including accompanying forms and schedules.

9. What if the taxpayer wants to make a voluntary contribution to reduce the public debt?

Voluntary contributions to reduce the public debt should be made payable to “Bureau of the Public Debt.” The contribution may be sent in the tax return envelope. If the taxpayer is making a payment of tax due, as well as a contribution, there should be two checks or money orders in the tax-return envelope—one to pay the tax due and one to make the voluntary contribution. Voluntary contributions to reduce the public debt are considered charitable contributions and may be entered as an itemized deduction on Schedule A of Form 1040 in the year paid.

10. How long should taxpayers keep their tax returns?

Taxpayers should keep a copy of the tax return, worksheets used, and records of all items appearing on it (such as 1099 forms) until the statute of limitations runs out for that return. Usually, this is 3 years from the date the return was due or filed, or 2 years from the date the tax was paid, whichever is later. They should keep forms W-2 until the Social Security Administration has recorded the earnings reflected on the forms. Keep property records (including those on a home) as long as they are needed to figure the basis of the original or replacement property. Closing statements for a home should be kept until the home is sold. Brokerage statements showing the purchase price of stock should be kept until the stock is sold. Also, contributions to nondeductible IRAs should be kept until all IRA funds are withdrawn. Calculations determining the nontaxable portion of pension income should be kept until all of the pension income is taxable. For additional recordkeeping information, see Publication 552, *Recordkeeping for Individuals*.

11. What is On-Line filing?

On-line filing allows a taxpayer to file their tax return from home through an Internet Web site or third-party transmitter. Information about filing from home is included in many commercial tax preparation software packages. Also, many software companies offer tax preparation and electronic filing software that can be downloaded from the Web; or they provide the option for individuals to prepare their returns while logged on to the Internet.

All that is needed is a personal computer (PC), software and a modem to send the return data. On-line filing accommodates the same basic forms and schedules as electronic filing. The taxpayer is responsible for sending their signature document (Form 8453-OL) accompanying paper documents to IRS after they receive notification from the Internet on-line provider or transmitter that their return has been accepted by IRS. If IRS rejects the return, the taxpayer will either have to correct the information and retransmit the return or print it and send it as a paper return to IRS. Credit card and direct debit payment options are available for balance due returns.

12. Are there any publications or forms that can assist a taxpayer that owes prior year taxes or previously had their refund offset to satisfy another's debt?

IRS offers various publications and forms that are specific to these issues.

The IRS Collection Process, Publication 594, explains a taxpayer's right and responsibility regarding payment of federal taxes. Installment Agreement Request, Form 9465, gives the taxpayer the option to pay a balance due through monthly installment payments.

Innocent Spouse Relief, Publication 971, addresses how one spouse may request relief from past taxes due solely based on the other spouse's debt. Request for Innocent Spouse Relief, Form 8857, explains various forms of relief and who may qualify.

Injured Spouse Claim and Allocation, Form 8379, allows a taxpayer to request relief from their spouse's past due federal debts including back child support and past due taxes. An injured spouse can get a refund for his or her share of the overpayment that would be used to pay the past due amount.

Additional information on these topics can be obtained by contacting the IRS at 1-800-829-1040, accessing their web page at www.irs.gov, or by visiting a Tax Assistance Center in your area.

13. Your Civil Rights Are Protected

Publication 4053, explains that under no circumstances will the Internal Revenue Service tolerate discrimination by its employees, grantees, contractors, and/or subcontractors. These provisions extend to VITA and TCE Programs. Publication 4053 or other IRS Civil Rights information should be displayed or made available to all taxpayers.

WHERE IS THE TOPIC?

The following pages show forms 1040EZ, 1040A, and 1040. For a discussion about what to put on a line, turn to the lesson in this text that is shown in the circle.

FORM 1040EZ

Form
1040EZ

Department of the Treasury—Internal Revenue Service
**Income Tax Return for Single and
Joint Filers With No Dependents 2003**

OMB No. 1545-0675

Label
(See page 14.)
**Use the IRS
label.**
Otherwise,
please print
or type.

L A B E L H E R E	Your first name and initial	Last name	(6)
	If a joint return, spouse's first name and initial	Last name	
	Home address (number and street). If you have a P.O. box, see page 14.	Apt. no.	
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 14.		

Your social security number
.....
.....
.....

Spouse's social security number
.....
.....
.....

**Presidential
Election
Campaign**
(page 14)

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if a joint return, want \$3 to go to this fund?

▲ Important! ▲
You **must** enter your
SSN(s) above.

You Spouse
 Yes No Yes No

Income
**Attach
Form(s) W-2
here.**
Enclose, but
do not attach,
any payment.

1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1	(2)	
2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2	(2)	
3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3	(2)	
4 Add lines 1, 2, and 3. This is your adjusted gross income .	4		
5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from No. If single , enter \$7,800. <input type="checkbox"/> worksheet on back. <input type="checkbox"/> If married filing jointly , enter \$15,600. See back for explanation.	5	(5)	
6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6		

Note. You
must check
Yes or No.

**Payments
and tax**

7 Federal income tax withheld from box 2 of your Form(s) W-2.	7	(6)	
8 Earned income credit (EIC).	8	(9)	
9 Add lines 7 and 8. These are your total payments .	9	(6)	
10 Tax. Use the amount on line 6 above to find your tax in the tax table on pages 25–29 of the booklet. Then, enter the tax from the table on this line.	10	(4)	

Refund

Have it directly
deposited! See
page 21 and fill
in 11b, 11c,
and 11d.

11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	11a	(6)	
b Routing number	<input type="text"/>	c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	(6)
d Account number	<input type="text"/>		

**Amount
you owe**

12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.	12		
---	----	--	--

**Third party
designee**

Do you want to allow another person to discuss this return with the IRS (see page 22)? **Yes**. Complete the following. **No**

Designee's name Phone no. Personal identification number (PIN)

**Sign
here**

Joint return?
See page 13.
Keep a copy
for your
records.

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number
(6)			()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

**Paid
preparer's
use only**

Preparer's signature	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
(6)			Enter Site Identification Number
Firm's name (or yours if self-employed), address, and ZIP code	EIN	Phone no.	()

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 24.

Cat. No. 11329W

Form **1040EZ** (2003)

FORM 1040A

Form **1040A** Department of the Treasury—Internal Revenue Service **U.S. Individual Income Tax Return 2003** IRS Use Only—Do not write or staple in this space.

Label
(See page 21.)

Use the IRS label.
Otherwise, please print or type.

L A B E L H E R E	Your first name and initial	Last name	⑥
	If a joint return, spouse's first name and initial	Last name	
	Home address (number and street). If you have a P.O. box, see page 22.		Apt. no.
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 22.		

OMB No. 1545-0085

Your social security number _____

Spouse's social security number _____

▲ Important! ▲
You **must** enter your SSN(s) above.

Presidential Election Campaign
(See page 22.)

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if filing a joint return, want \$3 to go to this fund? . . . ▶

You Yes No Spouse Yes No

Filing status
Check only one box.

- ① **Single**
- Married filing jointly** (even if only one had income)
- Married filing separately.** Enter spouse's SSN above and full name here. ▶
- Head of household** (with qualifying person). (See page 23.)
If the qualifying person is a child but not your dependent, enter this child's name here. ▶
- Qualifying widow(er) with dependent child** (See page 24.)

Exemptions

①
If more than six dependents, see page 24.

6a **Yourself.** If your parent (or someone else) can claim you as a dependent on his or her tax return, **do not** check box 6a.

b **Spouse**

c Dependents:

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>

d Total number of exemptions claimed. Add numbers on lines above

Income

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

If you did not get a W-2, see page 27.
Enclose, but do not attach, any payment.

7 Wages, salaries, tips, etc. Attach Form(s) W-2.	7	②
8a Taxable interest. Attach Schedule 1 if required.	8a	②
b Tax-exempt interest. Do not include on line 8a.	8b	②
9a Ordinary dividends. Attach Schedule 1 if required.	9a	
b Qualified dividends (see page XX).	9b	②
10a Capital gain distributions (see page 27).	10a	②
b Post-May 5 capital gain distributions (see page 27).	10b	
11a IRA distributions.	11a	⑬
11b Taxable amount (see page 27).	11b	
12a Pensions and annuities.	12a	⑬
12b Taxable amount (see page 28).	12b	
13 Unemployment compensation and Alaska Permanent Fund dividends.	13	②
14a Social security benefits.	14a	⑬
14b Taxable amount (see page 30).	14b	
15 Add lines 7 through 14b (far right column). This is your total income .	15	
16 Educator expenses (see page 30).	16	
17 IRA deduction (see page 30).	17	③
18 Student loan interest deduction (see page 33).	18	
19 Tuition and fees deduction (see page 33).	19	
20 Add lines 16 through 19. These are your total adjustments .	20	
21 Subtract line 20 from line 15. This is your adjusted gross income .	21	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 57. Cat. No. 11327A Form **1040A** (2003)

FORM 1040A

Form 1040A (2003)

Page **2**

Tax, credits, and payments	22	Enter the amount from line 21 (adjusted gross income).	22	
Standard Deduction for— • People who checked any box on line 23a or 23b or who can be claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000	23a	Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes checked <input type="checkbox"/> 23a 4 if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind }		
	b	If you are married filing separately and your spouse itemizes deductions, see page 34 and check here <input type="checkbox"/> 23b		
	24	Enter your standard deduction (see left margin).	24	
	25	Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25	
	26	Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26	
	27	Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income .	27	
	28	Tax , including any alternative minimum tax (see page 35).	28	4
	29	Credit for child and dependent care expenses. Attach Schedule 2.	29	7
	30	Credit for the elderly or the disabled. Attach Schedule 3.	30	14
	31	Education credits. Attach Form 8863.	31	8
	32	Retirement savings contributions credit. Attach Form 8880.	32	5
	33	Child tax credit (see page 38).	33	10
	34	Adoption credit. Attach Form 8839.	34	5
	35	Add lines 29 through 34. These are your total credits .	35	
	36	Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36	
	37	Advance earned income credit payments from Form(s) W-2.	37	9
	38	Add lines 36 and 37. This is your total tax .	38	
	39	Federal income tax withheld from Forms W-2 and 1099.	39	6
	40	2003 estimated tax payments and amount applied from 2002 return.	40	6
If you have a qualifying child, attach Schedule EIC.	41	Earned income credit (EIC) .	41	9
	42	Additional child tax credit. Attach Form 8812.	42	10
	43	Add lines 39 through 42. These are your total payments .	43	6
Refund	44	If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44	6
	45a	Amount of line 44 you want refunded to you .	45a	6
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	b	Routing number <input style="width:150px;" type="text"/>	c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
	d	Account number <input style="width:300px;" type="text"/>		6
	46	Amount of line 44 you want applied to your 2004 estimated tax .	46	6
Amount you owe	47	Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53.	47	6
	48	Estimated tax penalty (see page 53).	48	
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes . Complete the following. <input type="checkbox"/> No			
	Designee's name <input style="width:200px;" type="text"/>	Phone no. <input style="width:50px;" type="text"/> (<input style="width:20px;" type="text"/>)	Personal identification number (PIN) <input style="width:50px;" type="text"/>	
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.			
	Joint return? See page 22. Keep a copy for your records.	Your signature <input style="width:150px;" type="text"/> 6	Date <input style="width:50px;" type="text"/>	Your occupation <input style="width:150px;" type="text"/>
	Spouse's signature. If a joint return, both must sign. <input style="width:150px;" type="text"/>	Date <input style="width:50px;" type="text"/>	Spouse's occupation <input style="width:150px;" type="text"/>	
Paid preparer's use only	Preparer's signature <input style="width:150px;" type="text"/> 6	Date <input style="width:50px;" type="text"/>	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN <input style="width:50px;" type="text"/>
	Firm's name (or yours if self-employed), address, and ZIP code <input style="width:200px;" type="text"/>	EIN <input style="width:50px;" type="text"/>	Phone no. (<input style="width:20px;" type="text"/>)	Enter Site Identification Number <input style="width:50px;" type="text"/>

Printed on recycled paper

Form **1040A** (2003)

FORM 1040

Form **1040**

Department of the Treasury—Internal Revenue Service
U.S. Individual Income Tax Return 2003

IRS Use Only—Do not write or staple in this space.

Label

(See instructions on page 21.)

Use the IRS label. Otherwise, please print or type.

L
A
B
E
L

H
E
R
E

For the year Jan. 1–Dec. 31, 2003, or other tax year beginning _____, 2003, ending _____, 20

Your first name and initial _____ Last name **6**

If a joint return, spouse's first name and initial _____ Last name _____

Home address (number and street). If you have a P.O. box, see page 21. _____ Apt. no. _____

City, town or post office, state, and ZIP code. If you have a foreign address, see page 21. _____

OMB No. 1545-0074

Your social security number _____

Spouse's social security number _____

▲ Important! ▲
You must enter your SSN(s) above.

Presidential Election Campaign
(See page 21.)

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if filing a joint return, want \$3 to go to this fund? . . . ▶ **You** Yes No **Spouse** Yes No

Filing Status

Check only **1** one box.

- 1 Single
- 2 Married filing jointly (even if only one had income)
- 3 Married filing separately. Enter spouse's SSN above and full name here. ▶
- 4 Head of household (with qualifying person). (See page 21.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
- 5 Qualifying widow(er) with dependent child. (See page 21.)

Exemptions

1

If more than five dependents, see page 22.

6a **Yourself.** If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a

b **Spouse**

c **Dependents:**

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 22)
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>

d Total number of exemptions claimed _____

No. of boxes checked on 6a and 6b _____

No. of children on 6c who:
• lived with you _____
• did not live with you due to divorce or separation (see page 22) _____

Dependents on 6c not entered above _____

Add numbers on lines above ▶

Income

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

If you did not get a W-2, see page 23.

Enclose, but do not attach, any payment. Also, please use **Form 1040-V.**

7	Wages, salaries, tips, etc. Attach Form(s) W-2	7	2	
8a	Taxable interest. Attach Schedule B if required	8a		2
b	Tax-exempt interest. Do not include on line 8a	8b		
9a	Ordinary dividends. Attach Schedule B if required	9a	2	
b	Qualified dividends (see page 25)	9b		
10	Taxable refunds, credits, or offsets of state and local income taxes (see page 25)	10	2	
11	Alimony received	11		
12	Business income or (loss). Attach Schedule C or C-EZ	12	2	
13a	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ <input type="checkbox"/>	13a		
b	If box on 13a is checked, enter post-May 5 capital gain distributions	13b		
14	Other gains or (losses). Attach Form 4797	14		
15a	IRA distributions	15a	13	
b	Taxable amount (see page 25)	15b		
16a	Pensions and annuities	16a		
b	Taxable amount (see page 25)	16b		
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17		
18	Farm income or (loss). Attach Schedule F	18		
19	Unemployment compensation	19	2	
20a	Social security benefits	20a	13	
b	Taxable amount (see page 27)	20b		
21	Other income. List type and amount (see page 29)	21	2	
22	Add the amounts in the far right column for lines 7 through 21. This is your total income ▶	22		

Adjusted Gross Income

23	Educator expenses (see page 29)	23	3	
24	IRA deduction (see page 29)	24	3	3
25	Student loan interest deduction (see page 31)	25	3	
26	Tuition and fees deduction (see page 32)	26		
27	Moving expenses. Attach Form 3903	27	3	
28	One-half of self-employment tax. Attach Schedule SE	28		
29	Self-employed health insurance deduction (see page 33)	29		
30	Self-employed SEP, SIMPLE, and qualified plans	30		
31	Penalty on early withdrawal of savings	31		
32a	Alimony paid b Recipient's SSN ▶	32a		
33	Add lines 23 through 32a	33		
34	Subtract line 33 from line 22. This is your adjusted gross income ▶	34		

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 76.

Cat. No. 11320B

Form **1040** (2003)

Tax and Credits

Standard Deduction for—

• People who checked any box on line 36a or 36b or who can be claimed as a dependent, see page 34.

• All others:
Single or Married filing separately, \$4,750

Married filing jointly or Qualifying widow(er), \$9,500

Head of household, \$7,000

35	Amount from line 34 (adjusted gross income)		35	
36a	Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind. <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind. Total boxes checked ▶ 36a			
b	If you are married filing separately and your spouse itemizes deductions, or you were a dual-status alien, see page 34 and check here ▶ 36b <input type="checkbox"/>			4
37	Itemized deductions (from Schedule A) or your standard deduction (see left margin)		37	
38	Subtract line 37 from line 35		38	
39	If line 35 is \$104,625 or less, multiply \$3,050 by the total number of exemptions claimed on line 6d. If line 35 is over \$104,625, see the worksheet on page 35		39	
40	Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-		40	4
41	Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972		41	4
42	Alternative minimum tax (see page 37). Attach Form 6251		42	
43	Add lines 41 and 42		43	
44	Foreign tax credit. Attach Form 1116 if required	44	45	5
45	Credit for child and dependent care expenses. Attach Form 2441	45	46	7
46	Credit for the elderly or the disabled. Attach Schedule R	46	47	14
47	Education credits. Attach Form 8863	47	48	8
48	Retirement savings contributions credit. Attach Form 8880	48	49	5
49	Child tax credit (see page 39)	49	50	10
50	Adoption credit. Attach Form 8839	50	51	
51	Credits from: a <input type="checkbox"/> Form 8396 b <input type="checkbox"/> Form 8859	51	52	
52	Other credits. Check applicable box(es): a <input type="checkbox"/> Form 3800 b <input type="checkbox"/> Form 8801 c <input type="checkbox"/> Specify	52	53	
53	Add lines 44 through 52. These are your total credits	53	54	
54	Subtract line 53 from line 43. If line 53 is more than line 43, enter -0-	54	55	2

Other Taxes

55	Self-employment tax. Attach Schedule SE	55	56	2
56	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	56	57	13
57	Tax on qualified plans, including IRAs, and other tax-favored accounts. Attach Form 5329 if required	57	58	
58	Advance earned income credit payments from Form(s) W-2	58	59	
59	Household employment taxes. Attach Schedule H	59	60	
60	Add lines 54 through 59. This is your total tax	60		

Payments

If you have a qualifying child, attach Schedule EIC.

61	Federal income tax withheld from Forms W-2 and 1099	61	62	6
62	2003 estimated tax payments and amount applied from 2002 return	62	63	6
63	Earned income credit (EIC)	63	64	9
64	Excess social security and tier 1 RRTA tax withheld (see page 56)	64	65	10
65	Additional child tax credit. Attach Form 8812	65	66	
66	Amount paid with request for extension to file (see page 56)	66	67	
67	Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885	67	68	
68	Add lines 61 through 67. These are your total payments	68		

Refund

Direct deposit? See page 56 and fill in 70b, 70c, and 70d.

69	If line 68 is more than line 60, subtract line 60 from line 68. This is the amount you overpaid	69	70a	6
70a	Amount of line 69 you want refunded to you	70a	71	
b	Routing number	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
d	Account number			6
71	Amount of line 69 you want applied to your 2004 estimated tax	71		

Amount You Owe

72	Amount you owe. Subtract line 68 from line 60. For details on how to pay, see page 57	72		
73	Estimated tax penalty (see page 57)	73		

Third Party Designee

Do you want to allow another person to discuss this return with the IRS (see page 58)? **Yes.** Complete the following. **No**

Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶
--------------------------	------------------------	---

Sign Here

Joint return? See page 21. Keep a copy for your records.

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature ▶ 6	Date	Your occupation	Daytime phone number ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid Preparer's Use Only

Preparer's signature ▶ 6	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Enter Site Identification Number	
	Phone no. ()		

Each year the Internal Revenue Service contracts with a tax preparation software vendor to provide free software to our volunteers. This year you will find TaxWise hints integrated throughout the text. They will be at the end of each lesson just before “Summing Up This Lesson” or “Summing Up This Section.”

▶▶ SUMMING UP THIS SECTION ◀◀

- ▶ Remember that the information used to prepare an individual's income tax return must be treated as confidential.
- ▶ Use the steps for effective interviewing.

INTRODUCTION AND OBJECTIVES

In this lesson you will learn what you need to know when you begin to prepare an individual's federal income tax return. Please note that two of the objectives concern the importance of insuring that the taxpayer's (or dependent's) name and social security number (SSN) match IRS records.

Every U.S. Federal tax return that is filed must have each person identified by a number. Each person refers to the taxpayer, the taxpayer's spouse if the taxpayer is married, and any dependent claimed on the return. The identifying number will be a social security number for those persons who qualify to be issued one. All others must have an individual taxpayer identification number (ITIN).

After completing this lesson you should be able to:

- Explain the importance of requiring a social security card for the tax preparation.
- Determine which taxpayers need an Individual Taxpayer Identification Number (ITIN)
- Use the 5 tests for a qualifying dependent.
- Apply the requirements for each of the five filing statuses.
- Select the correct filing status.
- Determine who must file.
- Determine who should file.
- Select the appropriate tax form to use.

SOCIAL SECURITY NUMBER

It is extremely important that each person use the correct social security number. The most accurate information is usually located on the taxpayer's original social security card. Each year hundreds of thousands of returns are delayed in processing or credit/deductions disallowed because names and social security numbers do not match Social Security Administration (SSA) records. To prevent processing delays in paper returns and rejected electronically filed returns, volunteers must check the accuracy of each Social Security number, as well as the spelling of the name associated with the number. If a tax-

POTENTIAL PITFALLS



Canadians have a number that is like a social security number, but it is for their old age pension. Do not use this number on a U.S. tax return. Canadians often have both a U.S. and Canadian Social Security Number.

payer does not have a valid SSN, direct them to Form SS-5, Social Security Number Application. This form should be submitted to the nearest Social Security Administration Office. Explain to him/her that they **must** have a number before you can assist them with filing the tax return.

To do this volunteers should ask for one of the following documents for each individual on the return.

- Social Security Card (original or copy)
- SSA 1099 benefit statements
- SSA letter

Note: Driver's licenses and passport may not depict the name or number as it appears on SSA records.

INDIVIDUAL TAXPAYER IDENTIFICATION NUMBERS

Important Note: ITIN information will be provided as a separate supplement. For additional information see your instructor or IRS coordinator.

SUMMING UP THIS LESSON

- All taxpayers and dependents listed on a tax return must have an identification number.
- An Identification Number can be either a SSN or an ITIN.
- Use caution when completing the entity section of the tax return.

PERSONAL AND DEPENDENCY EXEMPTIONS

After completing this section, you will be able to:

- **Define** *personal exemption*.
- **Define** *dependency exemption*.
- **Use** the five tests to determine a qualifying dependent.

There are two kinds of exemptions: personal and dependency. While both exemptions are worth the same amount, different rules apply to each type.

Personal exemptions are allowed to the taxpayer and to the taxpayer's spouse.

Dependency exemptions are allowed to the taxpayer for qualifying dependents who meet five specific tests.

The taxpayer can usually deduct the **exemption amount** (\$3,050 for 2003) when figuring taxable income.

The Taxpayer

The taxpayer can claim a personal exemption for himself or herself unless the taxpayer is eligible to be claimed as a dependent on another person's return. If this is true, the taxpayer cannot claim an exemption for himself or herself, even if the other taxpayer does not actually claim the dependency exemption.

The Spouse

Generally, if the taxpayer's spouse is claimed as a dependent on another person's return, the taxpayer cannot claim the spouse's exemption on his or her return. (One spouse is never considered the dependent of the other.)

To claim an exemption for a spouse, the taxpayers must be married by December 31, the last day of the year. If the taxpayer files a separate return, he or she can claim the exemption for his or her spouse only if his or her spouse had no gross income (defined later) and was not the dependent of another taxpayer. This is true even if the other taxpayer does not actually claim the taxpayer's spouse's exemption. If a taxpayer is divorced or legally separated at the end of the tax year, he or she cannot claim his or her (former) spouse's exemption.

If the taxpayer's spouse died during the year and the taxpayer did not remarry by December 31, the taxpayer can generally claim the personal exemption for the deceased spouse. This exemption can be claimed only if the taxpayer was not divorced or legally separated from his or her spouse on the date of the death and would have been able to claim the exemption under regular circumstances.

ALERT



For 2003 the exemption amount increased to \$3,050.

DEPENDENCY EXEMPTIONS

A **dependent** is a person, other than the taxpayer or spouse, who entitles the taxpayer to claim a dependency exemption. A taxpayer can claim a dependency exemption only if **all five** of the following dependency tests are met.

1. Member of Household or Relationship
2. Citizen or Resident
3. Joint Return
4. Gross Income
5. Support

1. The Member of Household or Relationship Test

To meet this test, the person must either:

- A. Live with the taxpayer for the entire year as a member of his or her household, or
- B. Be related to the taxpayer in one of the ways listed later, under *Relatives who do not have to live with the taxpayer*.

Note:

A person away on temporary absences is considered to live and be a member of the household the entire year. Temporary absences include attending school, taking vacations, hospital stays due to illness, and military service. In addition, the relationship must not violate local law.

Relatives who do not have to live with the taxpayer

A person related to the taxpayer in any of the following ways does not have to live with the taxpayer the entire year as a member of his or her household to meet this test.

- Child, grandchild, great grandchild, etc. (A legally adopted child is considered the taxpayer's child)
- Stepchild
- Brother, sister, half brother, half sister, stepbrother, stepsister
- Parent, grandparent, or other direct ancestor, but not foster parent
- Stepmother or stepfather
- Brother or sister of your father or mother
- Son or daughter of your brother or sister
- Father-in-law, mother-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law

If a child was born alive during the year and meets the dependency tests, the taxpayer can take the exemption, even if the child lived only for a moment. No exemption is allowed for a stillborn child. State or local laws determine if a child was born alive or stillborn.

A legally adopted child is considered to be the taxpayer's child. If an adoption is finalized and the child begins living with the taxpayer on or before December 31, member of the household test is met.

If a foster child has lived with the taxpayer for the entire year (except for temporary absences) and the taxpayer cares for the child as his or her own, the child is treated as the taxpayer's own child.

A person who died during the year and was a member of the taxpayer's household until death meets the member of household test.

A cousin must live with the taxpayer for the entire year (except for temporary absences) to meet the member of household test. A cousin *does not* meet the relationship test.

2. Citizen or Resident Test

To meet this test, a person must be for some part of the year:

- a U.S. citizen or resident, or
- a resident of Canada or Mexico.

Children usually are citizens or residents of the country of their parents. A child born in a foreign country can be recognized as a U.S. citizen for tax purposes if either parent is a U.S. citizen.

If a taxpayer (who is a U.S. citizen) legally adopts a child who is not a U.S. citizen or resident, and the other dependency tests are met, the taxpayer can take the exemption if the taxpayer's home is the child's main home and the child is a member of the household for the entire tax year.

3. Joint Return Test

To meet this test, generally, the taxpayer's dependent cannot file a joint return. However, the joint return test does not apply if a joint return is filed by the dependent and his or her spouse ***merely as a claim for refund*** and no tax liability would exist for either spouse on separate returns.

4. The Gross Income Test

A taxpayer cannot take an exemption for a person whose gross income equals or exceeds the **exemption amount**. The exemption amount for 2003 is \$3,050.

Gross income is all *taxable* income in the form of money, goods, property, and services. It includes all unemployment compensation and certain scholarships. It does not include welfare benefits or nontaxable social security benefits.

There are two exceptions to the gross income test. The gross income test does not apply if:

- the taxpayer's child is under 19 years of age at the end of the year, or
- the taxpayer's child is under 24 years of age at the end of the year and is a full-time student

To be considered a student, the taxpayer's child must attend school full-time for some part of each of five calendar months of the year. The five months need not be consecutive in order to qualify. School generally does not include night schools, on-the-job training courses, or correspondence schools.

5. The Support Test

The support test requires that the taxpayer provide more than half of a person's total support for the entire year in order to claim that person as a dependent.

There are two exceptions to the support test:

- Multiple support, and
- Children of divorced or separated parents

(Both of these exceptions will be covered later in this section.)

To determine if the taxpayer provided more than half of the dependent's support, compare the amount that the taxpayer contributed to the person's support with the entire amount of support the person received from all sources. (Exhibit 1 provides a worksheet for figuring whether the taxpayer provided more than half of a dependent's support.)

State benefit payments like welfare, food stamps, and housing are considered support provided by the state, not by the parent, regardless of how the parent actually spends the funds.

Support provided for the dependent includes support paid from these sources: amounts withdrawn from savings; borrowed amounts, such as student loans and car loans; and tax-exempt income, including social security benefits, life insurance proceeds, nontaxable pensions, gifts, and tax-exempt interest.

Only the amount of a dependent's own funds that is actually spent on support is counted. Scholarships received by fulltime students are not included in total support.

Do not include in support any amounts that are:

- paid from a dependent's own funds for income and social security taxes,
- paid as life insurance premiums, or
- not spent, but saved or invested.

Total support items include food, clothing, shelter at fair rental value, education, medical and dental care, recreation, and transportation. Some support items, like food and rent, benefit more than one member of a household. Divide the value of these support items among the number of household members that benefit. Capital items like furniture, appliances, or autos should be included in support if the items are solely for the dependent's own use or benefit.

Example 1

Alexis, age 20, lived all year with her parents and younger sister in an apartment. Alexis earned \$4,000 from her part-time job. She saved \$1,000 for college and \$500 was withheld for income and social security taxes. Alexis spent the remaining \$2,500 on clothing, transportation, and recreation.

Alexis provided \$2,500 of her own support. The college savings will not be counted as support until the money is spent. The funds used to pay income and social security tax are not considered to be support.

In order for Alexis' parents to claim her as a dependent, they must provide additional support of more than \$2,500. Included in support items are one-fourth of the family's rent, utilities, grocery bills, and any additional amounts paid for Alexis' medical expenses and education.

Funds Belonging to the Person You Supported	
1) Total funds belonging to the person you supported, including income received (taxable and nontaxable) and amounts borrowed during the year, plus the amount in savings and other accounts at the beginning of the year	\$
2) Amount used for support	\$
3) Amount used for other purposes	\$
4) Amount in savings and other accounts at end of the year	\$
(The total of lines 2, 3, and 4 should equal line 1)	\$
Expenses for Entire Household (where the person you supported lived)	
5) Lodging (Complete item a or b)	
a) Rent paid	\$
b) If not rented, show fair rental value of home. If the person you supported owned the home, include this amount in line 19.	\$
6) Food	\$
7) Utilities (heat, light, water, etc. not included in line 5a or 5b)	\$
8) Repairs (not included in line 5a or 5b)	\$
9) Other. Do not include expenses of maintaining home, such as mortgage interest, real estate taxes, and insurance.	\$
10) Total household expenses (Add lines 5 through 9)	\$
11) Total number of persons who lived in household	
Expenses for the Person You Supported	
12) Each person's part of household expenses (line 10 divided by line 11)	\$
13) Clothing	\$
14) Education	\$
15) Medical, dental	\$
16) Travel, recreation	\$
17) Other (specify)	\$
18) Total cost of support for the year (Add lines 12 through 17)	\$
Did You Provide More Than Half?	
19) Amount the person provided for own support (line 2, plus line 5b if the person you supported owned the home)	\$
20) Amount others provided for the person's support. Include amounts provided by state, local, and other welfare societies or agencies. Do not include any amounts included on line 1.	\$
21) Amount you provided for the person's support (line 18 minus lines 19 and 20)	\$
22) 50% of line 18	\$
<p>Is line 21 more than line 22?</p> <p>Yes. You meet the support test for the person. If the other exemption tests are met, you may claim an exemption for the person.</p> <p>No. You do not meet the support test for the person. You cannot claim an exemption for the person unless you can do so under a multiple support agreement. See <i>Multiple Support</i>, later.</p>	

Multiple Support

Sometimes, no one person provides more than half of an individual's support, but two or more persons together do. In this situation, anyone who separately provides over 10 percent of the person's total support and meets the other tests can claim the exemption for the dependent. Nonetheless, only one person can claim the exemption. All other persons who provided more than 10 percent of the support and who meet the other tests must sign a written statement agreeing not to claim the exemption for that year. **Form 2120, Multiple Support Declaration**, is used to identify each of the others not claiming the exemption. The person who claims the exemption attaches Form(s) 2120 to his or her current year's tax return and must keep for his records the signed statement from the person agreeing not to claim the exemption.

Example 2

Henry E. and Harold S. Rust each provide more than 10 percent of the total support of their mother Margaret S. Rust, but neither provides more than 50 percent. Together, Henry and Harold provide more than 50 percent. They decide that Henry will claim the exemption this year. Exhibit 2 shows the completed Form 2120 that Henry will attach to his return.

Exhibit 2

Henry's Form 2120

Form 2120 (Rev. December 2002) Department of the Treasury Internal Revenue Service	Multiple Support Declaration ▶ Attach to Form 1040 or Form 1040A.	OMB No. 1545-0071 Attachment Sequence No. 114
Name(s) shown on return Henry E. Rust		Your social security number 000 00 4877
During the calendar year , the eligible persons listed below each paid over 10% of the support of: Margaret S. Rust <small style="text-align: center;">Name of person supported</small>		
I have a signed statement from each eligible person waiving his or her right to claim this person as a dependent for any tax year that began in the above calendar year.		
Harold S. Rust Eligible person's name 123 Main Street, Springfield, VA 22140 Address (number, street, apt. no., city, state, and ZIP code)		000 00 2780 Social security number
Eligible person's name Address (number, street, apt. no., city, state, and ZIP code)		Social security number
Eligible person's name Address (number, street, apt. no., city, state, and ZIP code)		Social security number
Eligible person's name Address (number, street, apt. no., city, state, and ZIP code)		Social security number

Children of Divorced or Separated Parents

The parent who has custody of the child for the greater part of the year (the custodial parent) will generally be considered as having provided over half of the child's support ***if all of the following conditions are met.***

- The child received over half of his or her total support from one or both parents.
- The parents are divorced, legally separated, separated under a written separation agreement, or have lived apart at all times during the last six months of the calendar year.
- The child was in the custody of one or both parents for more than half of the calendar year.

The custodial parent ***will not*** be considered as having provided over half of the child's support if any of the following conditions exist.

- Over half of the support of the child is considered to have been received from a third party, such as a relative or friend.
- The custodial parent signed Form 8332, *Release of Claim to Exemption for Child of Divorced or Separated Parents*, or a similar statement, that allows the noncustodial parent to claim the exemption (this statement must be attached to the noncustodial parent's return).
- A decree or agreement that went into effect after 1984 unconditionally states that the noncustodial parent can claim the child as a dependent.
- A qualified pre-1985 agreement provides that the noncustodial parent shall be entitled to the exemption for the child and the noncustodial parent contributed at least \$600 toward the child's support during the tax year, unless the pre-1985 agreement is modified after 1984 to specify that this provision will not apply.

Example 3

Ellen M. and Richard A. Stonehill are divorced. Under the terms of the 1984 divorce, Richard has custody of their two children, Alan R. and Mary E. The divorce decree specifies that Ellen can claim the dependency exemptions. Ellen provided \$1,500 of support for each child. Assuming all other tests are met, Ellen can claim both children as dependents.

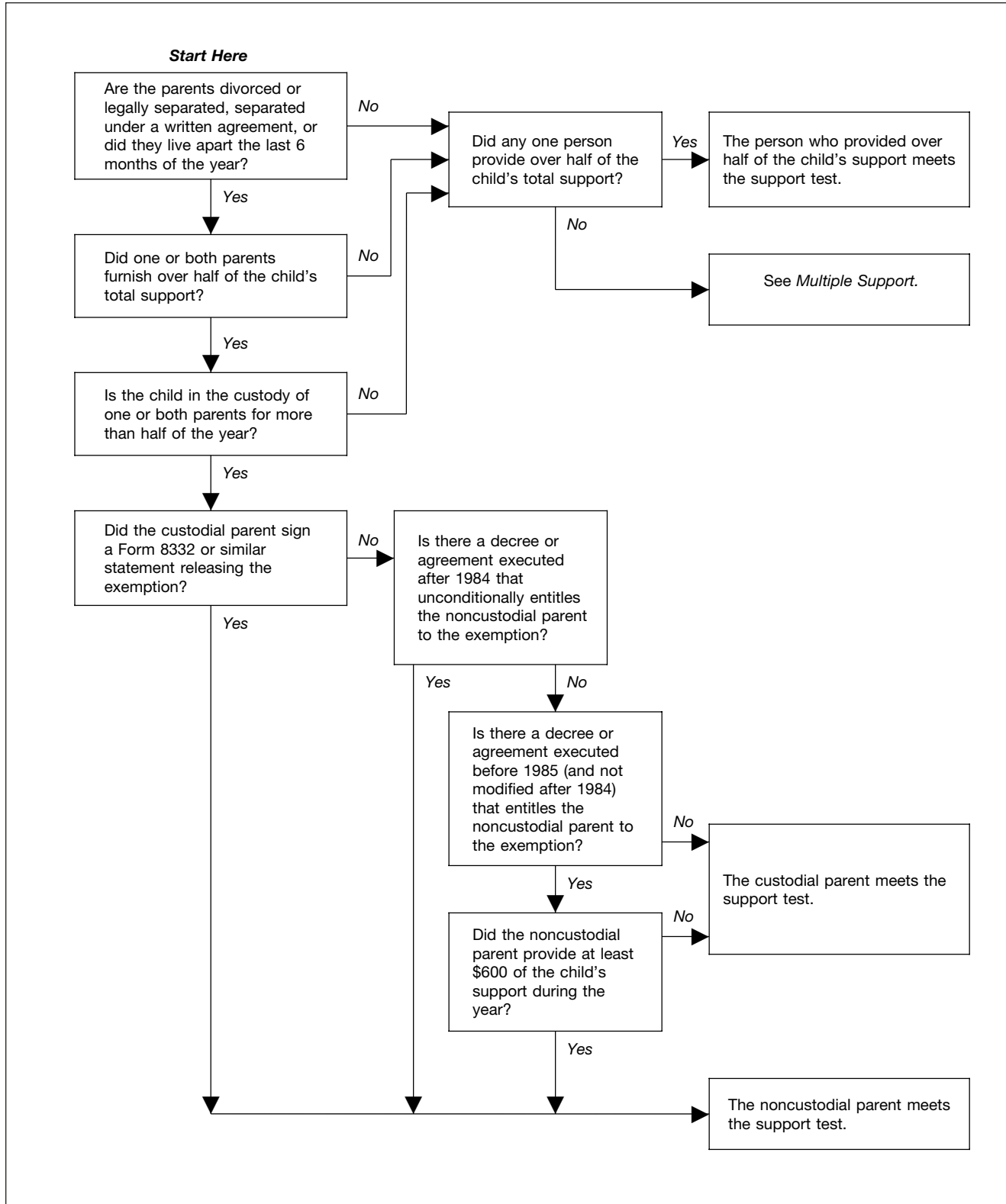
If Ellen had provided only \$500 of support for each child, she could not claim dependency exemptions for the two children. To claim the exemptions, she must provide at least \$600 of support for each child.

If the divorce occurred after 1984 and Richard and Ellen had agreed that Ellen would claim the dependency exemptions for the children, Ellen would attach Form 8332 or a similar statement to her tax return. Exhibit 3 shows a completed Form 8332 for Ellen.

Exhibit 3

Ellen's Form 8332

Form 8332 (Rev. December 2000) Department of the Treasury Internal Revenue Service	Release of Claim to Exemption for Child of Divorced or Separated Parents ▶ Attach to noncustodial parent's return each year exemption is claimed. Caution: Do not use this form if you were never married.	CMB No. 1545-0915 Attachment Sequence No. 115
Name of noncustodial parent claiming exemption <u>Ellen M. Stonehill</u>	Noncustodial parent's social security number (SSN) ▶	<u>000 | 00 | 2338</u>
Part I Release of Claim to Exemption for Current Year		
I agree not to claim an exemption for <u>Alan R. Stonehill and Mary E. Stonehill</u> Name(s) of child (or children)		
for the tax year 20 <u>03</u> .		
<u>Richard A. Stonehill</u> Signature of custodial parent releasing claim to exemption	<u>000 | 00 | 3832</u> Custodial parent's SSN	<u>3/26/2004</u> Date
Note: If you choose not to claim an exemption for this child (or children) for future tax years, also complete Part II.		



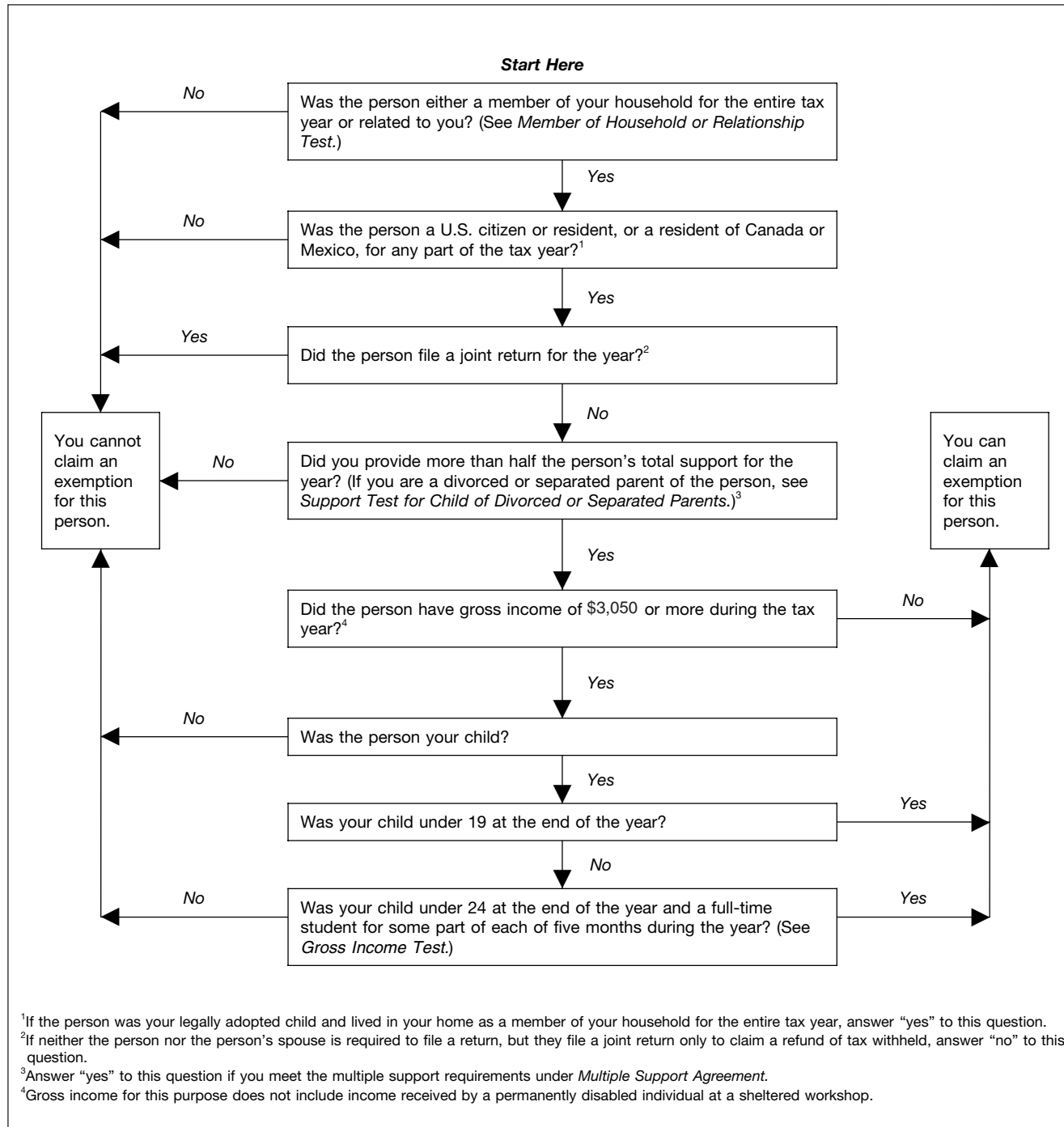
DETERMINING THE NUMBER OF EXEMPTIONS TO CLAIM

When determining the number of exemptions to claim, first look at the personal exemptions and then review each of the tests for dependency exemptions. There are many factors to consider as well as several major exceptions.

REMEMBER: Do not claim an exemption for a person who can be claimed on another return.

Exhibit 5

Can You Claim an Exemption for a Dependent?



COMPLETING THE EXEMPTION SECTION OF FORMS 1040A AND 1040

Exemptions are claimed on lines 6a through 6d. The taxpayer's personal exemption is claimed on line 6a. The personal exemption for the taxpayer's spouse is claimed on line 6b. The total of lines 6a and 6b is entered on the line in the right-hand margin. The dependency exemptions are claimed on line 6c. The columns on line 6c are self-explanatory. In column 3, enter the specific relationship for each dependent: son, daughter, grandson, granddaughter, etc. Column 4 is checked if the taxpayer's dependent is also a qualifying child for the child tax credit (see lesson 10). The line 6c exemptions are totaled on the three right-hand-margin lines that relate to:

- Children who lived with the taxpayer,
- Children who did not live with the taxpayer due to divorce or separation, and
- Other dependents not entered on the lines above.

Line 6d shows the total number of exemptions (See Exhibit 6).

Exhibit 6

Form 1040/1040A, page 1

Exemptions		6a <input checked="" type="checkbox"/> Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a.				No. of boxes checked on 6a and 6b
6b <input checked="" type="checkbox"/> Spouse						2
6c Dependents:		(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)	No. of children on 6c who:	
(1) First name	Last name			• lived with you		
James	Nicholson	000:00:3333	son	<input checked="" type="checkbox"/>	1	
				<input type="checkbox"/>	• did not live with you due to divorce or separation (see page 26)	
				<input type="checkbox"/>	Dependents on 6c not entered above	
				<input type="checkbox"/>	Add numbers on lines above	
d Total number of exemptions claimed.						3

If more than six dependents, see page 24.

If you are claiming Child Tax Credit (CTC), Earned Income Credit, and/or Dependent Care (DC), you must enter the date of birth for qualifying children and “X” the EIC and/or DC box(es). CTC is automatically calculated for you.

▶▶ Summing Up This Section ◀◀

There are two types of exemptions: personal and dependency. Each exemption reduces taxable income by \$3,050 in 2003.

A personal exemption can be claimed for a taxpayer and spouse if neither the taxpayer nor the spouse can be claimed on another taxpayer’s return.

To claim a dependency exemption, the dependent must meet all of 5 tests.

1. The Member of Household or Relationship Test.
2. The Citizen or Resident Test.
3. The Joint Return Test.
4. The Gross Income Test.
5. The Support Test.

There are two exceptions to the gross income test.

- ▶ Taxpayers’ children under age 19.
- ▶ Taxpayers’ children under age 24 who are full-time students.

There are two exceptions to the support test.

- ▶ The multiple-support agreement.
- ▶ Children of divorced or separated parents.

Exercises

1. Janice is 18 years old and a full-time student. She can be claimed as a dependent on her parents' tax return. Janice will file Form 1040EZ to report income from her summer job. How many personal exemptions can Janice claim on her return?

2. Tom Brown supports his wife's uncle, Jim (her mother's brother), who lives in another city. The Browns file a joint return. Can the Browns claim Jim as a dependent if all other tests are met?

3. Ruth filed a joint return with her husband whom she married in November. They claimed two personal exemptions on their return. Ruth had no income; her husband had \$10,600 income. Can Ruth's father, who supported her and paid for the wedding, claim her as a dependent on his return? _____
4. Joe is 65 years old and lives with his son and daughter-in-law. In 2003, Joe's taxable pension income was \$4,700. Can Joe's son and daughter-in-law claim a dependency exemption for Joe if all other tests are met? _____
5. Randy's son, Paul, earned \$4,300 last year. Paul is 18 years old and started college in September 2003. Is the gross income test met? _____
6. Traci's mother received \$3,500 in social security payments and \$600 in interest. Traci paid \$1,500 for her food and \$500 for her medical bills. Her mother paid \$2,400 for lodging, \$300 for recreation, \$150 for clothes, \$100 for transportation, \$400 for life insurance premiums, and \$200 for a television set.
 - A. What is the total support for Traci's mother? _____
 - B. How much did Traci contribute toward her mother's support?

 - C. How much did Traci's mother contribute toward her support?

 - D. Can Traci claim a dependency exemption for her mother?

7. Mrs. Wiley has three children, Mark, Tim, and Mary. Each child contributes toward Mrs. Wiley's support. Mark provides 45 percent, Tim, 35 percent, and Mary, 10 percent.
- A. Which, if any, of her children can claim a dependency exemption for Mrs. Wiley under a multiple-support agreement?

- B. If Mark is to claim the dependency exemption, who must sign a statement waiving his/her right to claim Mrs. Wiley as a dependent? _____
8. Under the terms of Peter's pre-1985 divorce decree, his former wife has custody of their child. The decree states that Peter can claim the exemption. He provided \$700 toward the child's support. Can he claim the exemption? _____

Exercise 1

0

Exercise 2

Yes; Jim is related by blood to Mrs. Brown.

Exercise 3

No, the husband has a filing requirement

Exercise 4

No; His gross income equals or exceeds the exemption amount of \$3,050.

Exercise 5

Yes; Paul is under the age of 19.

Exercise 6

- A. \$5,150 ($\$1,500 + \$500 + \$2,400 + \$300 + \$150 + \$100 + \200) Note that life insurance premiums are not considered support.
- B. \$2,000 ($\$1,500 + \500)
- C. \$3,150 ($\$2,400 + \$300 + \$150 + \$100 + \200) Note that life insurance premiums are not considered support.
- D. No; she did not pass the Gross Income Test.

Exercise 7

- A. Mark or Tim are eligible to claim the exemption. Both provide more than 10 percent of Mrs. Wiley's support. Mary is not eligible since she does not provide more than 10 percent of the support.
- B. Only Tim must sign. Mary is not eligible to take the exemption. Therefore, she does not have to sign a waiver.

Exercise 8

Yes; Peter provided at least \$600 in support.

FILING STATUS

SINGLE

A taxpayer is considered **single** if, on the last day of the year, either of the following is true.

- The taxpayer was never married.
- The taxpayer was legally separated, according to state law, under a decree of divorce or separate maintenance.

A taxpayer can also be considered **single** if the taxpayer was widowed before January 1, 2003, and did not remarry in 2003. However, the taxpayer may be able to use another filing status that will give a lower tax. See *Head of Household* and *Qualifying Widow(er) with Dependent Child*, later.

MARRIED FILING A JOINT RETURN

Taxpayers may use the **married filing jointly** status if they are married. They are considered married if, on the last day of the year, one of the following applies:

- They are married and live together as husband and wife.
- They live together in a common-law marriage recognized in the state where they now live or in the state where the common-law marriage began.
- They are married and live apart but are not legally separated under a decree of divorce or separate maintenance.
- They are separated under an interlocutory (not final) divorce decree.
- The taxpayer's spouse died during the year and the taxpayer has not remarried.

If taxpayers file a joint return, combine the husband's and wife's tax items (for example, income) on the same return. Both the husband and wife must sign the return and both are responsible for any tax owed on that return. Taxpayers can choose the married filing joint status even if only one spouse has income.

Taxpayers filing a joint return generally have a lower tax than their combined tax for any other filing status.

POTENTIAL PITFALLS



A common-law marriage is recognized for federal tax purposes if the marriage is recognized by the state where the taxpayers now live or in the state in which the common-law marriage was entered. Legal advice may be required to determine if a common-law marriage exists.

MARRIED FILING A SEPARATE RETURN

Taxpayers who are married may choose to file separately. The husband and wife report their own incomes and deductions on separate returns. Taxpayers may choose the **married filing separately** status even if one spouse had no income.

If the taxpayers live in a community property state, they must follow state law to determine their separate income. For more information, see Publication 555, *Community Property*.

If a married couple files separately and one spouse itemizes deductions, the other spouse must also itemize deductions because he or she cannot take the standard deduction. See Lesson 4 for more information on itemized deductions.

Taxpayers filing separate returns generally have a higher tax than when filing jointly. Occasionally, however, separate returns may result in a lower tax. If you think this might be the case, compute the tax liability for (a) married filing jointly and (b) married filing separately. Choose the filing status that results in the lower tax.

When a married taxpayer files separately, the taxpayer must show his or her spouse's name and social security number on the return in the label section or line 6a.

HEAD OF HOUSEHOLD

In general, the **head of household** status is for unmarried taxpayers (or those considered unmarried) who pay more than half the cost of keeping up a home for a qualified relative during the year.

Generally, taxpayers who file under the **head of household** filing status have a lower tax than if they file as single. If they qualify, taxpayers should use the head of household status instead of the single status.

Head of Household Qualifications

1. The taxpayer must be unmarried (single, divorced, or legally separated) on the last day of the year

OR

The taxpayer must meet the tests for married persons living apart with dependent children (explained later in this lesson)

AND

2. The taxpayer must have paid more than half the cost of keeping up a home that was the main home for more than half the year (except for temporary absences) of any of the following:

- A. The taxpayer's unmarried child who must have lived with the taxpayer but does not have to have been the taxpayer's dependent,
- B. The taxpayer's foster child who must have lived with the taxpayer and must have been the taxpayer's dependent (To qualify as a dependent, a foster child must live with the taxpayer for the entire tax year.), or
- C. Certain relatives (see the list at the end of this discussion) who lived with the taxpayer and who were the taxpayer's dependents.

EXCEPTION: The taxpayer may claim head of household filing status if the taxpayer's parent is claimed as a dependent, even if the parent does not live with the taxpayer. However, the taxpayer must pay more than half the cost of maintaining the parent's home for the entire year.

- D. The taxpayer's married child—who must have lived with the taxpayer and who must have been the taxpayer's dependent unless:
 - The child is not a dependent because the taxpayer signed a written declaration allowing the noncustodial parent to claim the child as a dependent, or
 - The child is not a dependent because the noncustodial parent provides at least \$600 of support for the child and claims the child as a dependent under a pre-1985 divorce decree or agreement.

“Child” includes:

- Grandchild; stepchild; adopted child

“Relative” includes:

- Parent, grandparent
- Brother, sister, stepbrother, stepsister
- Half brother, half sister
- Stepmother, stepfather
- Mother-in-law, father-in-law
- Brother-in-law, sister-in-law
- Son-in-law, daughter-in-law

AND (if related by blood)

- Uncle, or aunt, nephew, or niece

“Relative” does not include cousins and more distant relatives.

Keeping Up the Home

The taxpayer must pay more than half the cost of keeping up the home. The cost of keeping up a home includes: rent, mortgage interest, real estate taxes, insurance on the home, repairs, utilities, domestic help, and food eaten in the home. Welfare payments are not considered amounts that the taxpayer furnishes to keep up a home.

The home must have been the main home for more than half the year except for temporary absences. Temporary absences include those for school, vacation, illness, business, or military service.

The following chart may help you decide who is eligible to claim head of household filing status.

Exhibit 7

Qualifying Relations for Head of Household		
Relationship to Taxpayer	Must Live with Taxpayer?	Must be Taxpayer's Dependent?
1. Unmarried child, grandchild, or step child	Yes	No
2. Married child, grandchild, or step child	Yes	Yes*
3. Foster child	Yes***	Yes
4. Mother or father	No	Yes
5. Other relatives	Yes**	Yes
Exceptions:		
* The married child does not have to be the taxpayer's dependent if a noncustodial parent claims the child as a dependent under the rules for children of divorced or separated parents.		
** Cousins and more distant relatives do not qualify as "relatives" in determining head of household status.		
NOTE: The taxpayer's home must be the main home of the relative for more than half the year. The relative cannot be a person who files a joint return.		
***The foster child must live with the taxpayer for the entire year.		

Married Persons Living Apart With Dependent Children

Some married taxpayers who live apart from their spouses may be considered unmarried for tax purposes. If so, these taxpayers are permitted to file as head of household and receive the benefit of lower tax amounts.

A married taxpayer can file as head of household if:

1. The taxpayer files a separate return,
2. The taxpayer paid more than half the cost of keeping up his or her home for the year,
3. The taxpayer's spouse did not live in the home during the last six months of the year,
4. The taxpayer's home was the main home of the taxpayer's child, stepchild, or adopted child for more than half of the year or of the taxpayer's foster child for the entire year, and
5. The taxpayer claims the child, stepchild, adopted child, or foster child as a dependent, unless one of the following exceptions for divorced or separated parents applies:
 - the taxpayer signed a statement allowing the noncustodial parent to claim the child as a dependent, or
 - the noncustodial parent provided at least \$600 for the child's support and can claim the dependent under a pre-1985 agreement.

Reporting Head of Household Filing Status

Taxpayers must enter the name of the person who qualifies them for the head of household status. If the person is a dependent, enter the dependent's name on line 6c of the exemption section of the tax return. If the qualifying person is not a dependent, enter the name of the nondependent person on line 4 in the filing status section of the tax return.

Example 4

Samantha is divorced and provided over half the cost of keeping up a home. Her five-year-old daughter, Pam, lived with her for seven months last year. Samantha does not claim Pam as a dependent; her ex-husband does.

Samantha may use head of household status. Samantha must write Pam's name in the space on Form 1040 or 1040A, on line 4.

Exhibit 8

Samantha's Form 1040A, page 1

Filing status	1 <input type="checkbox"/> Single	4 <input checked="" type="checkbox"/> Head of household (with qualifying person). (See page 23.)
	2 <input type="checkbox"/> Married filing jointly (even if only one had income)	If the qualifying person is a child but not your dependent, enter this child's name here. ▶ <u>Pam</u>
	3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here. ▶ _____	5 <input type="checkbox"/> Qualifying widow(er) with dependent child (year spouse died ▶ _____). (See page 24.)
	Check only one box.	

QUALIFYING WIDOW(ER) WITH DEPENDENT CHILD

A widow or widower, with one or more dependent children, may be able to use the **qualifying widow(er) with dependent child** filing status. This filing status yields the lowest tax (the same tax for married filing jointly).

If the taxpayer's spouse died during 2001 or 2002 and the taxpayer did not remarry before the end of 2003, the taxpayer may be able to file as a qualifying widow(er) with dependent child. To qualify, the taxpayer must:

- Have been entitled to file a joint return for the year the spouse died (It does not matter whether or not a joint return was actually filed.),

AND

- Have a child, foster child, adopted child, or stepchild who qualifies as the taxpayer's dependent for the year,

AND

- Have furnished over half the cost of keeping up a home that was the main home of the child for the entire year.

An "adopted child" includes a child placed with the taxpayer by an authorized placement agency for legal adoption.

Social Security survivor benefits received on behalf of the child are considered to be amounts furnished by the child, not by the parent.

In the year a taxpayer's spouse dies, if the taxpayer does not remarry, he or she can use the married filing jointly filing status or married filing separately filing status and can claim an exemption for the deceased spouse. For two years after the year of death, the taxpayer may file as a qualifying widow(er) with dependent child, but may not claim an exemption for the deceased spouse. After the second year following the year of death, the taxpayer can no longer use the qualifying widow(er) filing status. The taxpayer may use either the head of household or single filing status depending on his or her situation then.

The following chart may help you decide which filing status to use for a taxpayer with a qualifying dependent if the spouse is deceased and the taxpayer has not remarried.

Exhibit 9

Filing Status After Death of Spouse		
Tax Year	Filing Status	Exemption for Deceased Spouse?
1. Year of Death	Married (joint)	Yes
	OR	
2. First Year after death	Married (separate)	Yes
	Qualifying widow(er)*	No
3. Second year after death	Qualifying widow(er)*	No
4. After the second year after death	Head of household**	No
	OR	
	Single	No

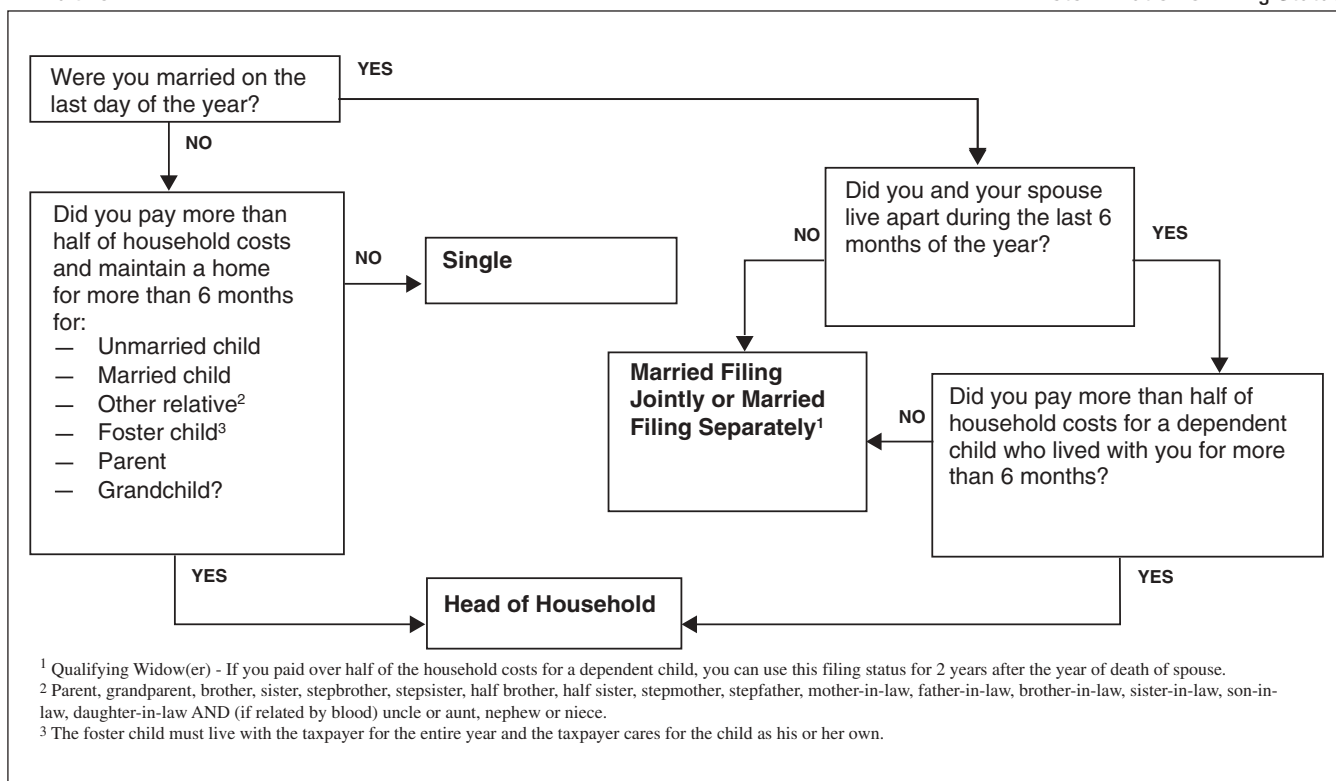
* With a qualifying dependent.
 ** With a qualifying relative.

Taxpayers who use the qualifying widow(er) status must list the year of the spouse’s death on line 5 of Form 1040A or 1040.

You may find the following flowchart helpful in determining the correct filing status.

Exhibit 10

Determination of Filing Status



TaxWise Hints

When using TaxWise to prepare a tax return, you will need to have the Social Security Number of anyone who qualifies the taxpayer for Head of Household filing status and is not the taxpayer's dependent.

For Qualifying Widow(er) filing status, you must enter the year of death of the deceased spouse.

For Married Filing Separate status, you will need the spouse's full name and Social Security number.

▶▶ Summing Up This Section ◀◀

When completing their tax returns, taxpayers can use one of five filing statuses:

Tax Status

(from lowest tax to highest tax)

1. Married filing jointly*
2. Qualifying widow(er) with dependent child*
3. Head of household
4. Single
5. Married filing separately

* Numbers 1 and 2 yield the same (lowest) tax.

Filing status is indicated on lines 1 through 5 of Forms 1040A and 1040. Selecting the correct filing status is one of the most important aspects of completing a tax return because the filing status factors in how much tax will be due. Remember that filing status requirements do not change, regardless of the tax form used. If a taxpayer is qualified to use more than one filing status, choose the one that will result in the lowest tax.

Exercises

9. Carol and Roger were married in 2002. They are not divorced, but lived apart all of 2003. They are not legally separated under a decree of divorce or separate maintenance. They have no children. Can they use the married filing jointly status? _____
10. Martin does not know which filing status to use. You ask if he is married. He answers that he got divorced in December but supported his wife all year and has not remarried. Can Martin and his ex-wife file a joint return? _____
11. Ginger is single and paid more than half the cost of keeping up her home. Her grandmother lived with her all year. Ginger claims her grandmother as a dependent. What is Ginger's filing status? _____
12. Bill is single and lives alone. He paid over half the cost of maintaining a home for his father for the entire year. He claims his father as a dependent. What is Bill's filing status? _____
13. Franklin is single and lives alone. He paid over half the cost of maintaining a separate home for his father. He does not claim his father as a dependent. What is Franklin's filing status?

14. Mrs. Calvin tells you that she is divorced and that her 21-year-old unmarried son lived with her all year. She paid for their rent and food and provided over half of her son's total support. She cannot claim her son as a dependent because he earned \$4,000 and is not a student. Her son used his earnings to pay for his car, clothing, and entertainment. Can Mrs. Calvin file as head of household? _____
15. Kathy lived with her unemployed roommate, Sandra, for the entire year. Kathy had to pay more than half of the cost of keeping up their apartment. Can Kathy file as head of household?

16. Jack has lived apart from his wife for several years. Their children live with his wife but Jack pays over half the children's support. What filing status can Jack use? _____
17. Lily left her husband in August 2003. She took her children with her. She supported the children during all of 2003 and will claim them as dependents. Lily will not file a joint return with her husband. Which filing status should Lily use in 2003? ____
18. Rose and her husband separated in October 2003, but were still married on December 31, 2003. What filing status can she use?

19. Dick's wife died in 2001. Dick has not remarried. Dick provides all of the support for his two dependent children. What will be Dick's filing status for 2004? _____

Exercise 9

Yes

Exercise 10

No

Exercise 11

Head of household

Exercise 12

Head of household

Exercise 13

Single

Exercise 14

Yes

Exercise 15

No; Sandra is not a qualifying person.

Exercise 16

Married filing jointly or married filing separately.

Exercise 17

Married filing separately; she lived with her husband during part of the last six months of 2003.

Exercise 18

Either married filing jointly or married filing separately.

Exercise 19

Head of household; he could claim qualifying widower for 2002 and 2003 only.

WHO MUST FILE—WHO SHOULD FILE

WHO MUST FILE

To decide who must file a tax return, you will need to know the individual's:


- filing status,
 - age,
 - gross income,
- and if:
- special taxes might be owed on different types of income,
 - some of the income is excludable or exempt,
 - the individual can be claimed as a dependent on another's tax return,
 - the individual is blind, or
 - the individual received advance earned income credit payments.

You may not be familiar with some of the terms used on the list. These terms will be explained in later lessons. For now, concentrate on learning how to use the charts and checklists.

How to Use the Charts and Flowcharts

You will use a set of charts to determine who must file. An individual who cannot be claimed as a dependent on another tax-payer's return will use *Chart A—For Most People*. Based on the individual's circumstances, a person who can be claimed as a dependent on another taxpayer's return will use one of the other charts. *Chart C—Other Situations When You Must File* should be reviewed for every individual.

Chart A—For Most People		
If your filing status is...	AND at the end of 2003 you were*	THEN file a return if your gross income** was at least...
Single	Under 65	\$ 7,800
	65 or older	8,950
Married filing jointly***	under 65 (both spouses)	\$15,600
	65 or older (one spouse)	16,550
	65 or older (both spouses)	17,500
Married filing separately	Any age	\$ 3,050***
Head of household (see page 19)	Under age 65	\$10,050
	65 or older	11,200
Qualifying Widow(er) with dependent child (see page 19)	Under 65	\$12,550
	65 or older	13,500
<p>* If you turned age 65 on January 1, 2003, you are considered to be age 65 at the end of 2003</p> <p>** Gross Income means all income you received in the form of money, goods, property, and services that are not exempt from tax including any income from sources outside the United States (even if you may exclude part or all of it). Do not include social security benefits unless you are married filing a separate return and you lived with your spouse at any time in 2003.</p> <p>*** If you did not live with your spouse at the end of 2003 (or on the date your spouse died) and your gross income was at least \$3,050, you must file a return regardless of your age.</p>		

POTENTIAL PITFALLS 

If a checklist or chart indicates that a person must file a return, he or she should do so even if no tax is owed. If a minor child must file a return but cannot do so, the child's parent or guardian must complete and sign a return for the child.

Chart B—For Children and Other Dependents

See the instructions for line 6c that begin on page 21 to find out if someone can claim you as a dependent.

If your parent (or someone else) can claim you as a dependent, use this chart to see if you must file a return.

In this chart, **unearned income** includes taxable interest, ordinary dividends, and capital gain distributions. **Earned income** includes wages, tips, and taxable scholarship and fellowship grants. **Gross income** is the total of your unearned and earned income.



If your gross income was \$3,050 or more, you usually cannot be claimed as a dependent unless you were under age 19 **or** a student and under age 24. For details, see **Test 4—Income** on page 22.

Single dependents. Were you **either** age 65 or older **or** blind?

- No.** You must file a return if **any** of the following apply.
 - Your **unearned income** was over \$750.
 - Your **earned income** was over \$4,750.
 - Your **gross income** was more than the **larger** of—
 - \$750 or
 - Your earned income (up to \$4,500) plus \$250.
- Yes.** You must file a return if **any** of the following apply.
 - Your earned income was over \$1,900 (\$3,050 if 65 or older **and** blind).
 - Your earned income was over \$5,900 (\$7,050 if 65 or older **and** blind).
 - Your gross income was more than—

The larger of:	Plus	This amount:
<ul style="list-style-type: none"> • \$750 or • Your earned income (up to \$4,500) plus \$250. 	}	\$1,150 (\$2,300 if 65 or older and blind)

Married dependents. Were you **either** age 65 or older **or** blind?

- No.** You must file a return if **any** of the following apply.
 - Your unearned income was over \$750.
 - Your earned income was over \$4,750.
 - Your gross income was at least \$5 and your spouse files a separate return and itemizes deductions.
 - Your gross income was more than the **larger** of—
 - \$750 or
 - Your earned income (up to \$4,500) plus \$250.
- Yes.** You must file a return if **any** of the following apply.
 - Your unearned income was over \$1,700 (\$2,650 if 65 or older **and** blind.)
 - Your earned income was over \$5,700 (\$6,650 if 65 or older **and** blind.)
 - Your gross income was at least \$5 and your spouse files a separate return and itemizes deductions.
 - Your gross income was more than—

The larger of:	Plus	This amount:
<ul style="list-style-type: none"> • \$750 or • Your earned income (up to \$4,500) plus \$250. 	}	\$950 (\$1,900 if 65 or older and blind)

DEPENDENTS WHO MUST OR SHOULD FILE A RETURN—CHECKLIST

The dependents listed in the following checklist must or should file a return.

Exhibit 13

Checklist—Children and Other Dependents

- A married dependent with at least \$5 of income whose spouse itemizes deductions on a separate return on Form 1040 must file a return.
- A dependent with at least \$400 of net self-employment income must file a return. (**Self-employment income** is earned income from a trade, business, farming or profession that is not paid by an employer. For example, seamstresses and lawn-care workers who work for themselves (and not for someone else) are considered self-employed.
- A dependent who is not required to file but had income tax withheld should file a return to get a refund.
- A dependent who has to pay a tax, such as the alternative minimum tax, must file a return.

OTHER SITUATIONS

Remember to review the *Chart C—Other Situations When You Must File* chart after you use the other charts.

Chart C — Other Situations When You Must File

You must file a return if any of the four conditions below apply for 2003.

1. You owe any special taxes, such as:
 - Social security and Medicare tax on tips you did not report to your employer,
 - Uncollected social security and Medicare or RRTA tax on tips you reported to your employer or on group-term life insurance,
 - Alternative minimum tax,
 - Recapture taxes (see the instructions for lines 41 and 60 that begin on pages 33 and 40), or
 - Tax on a qualified plan, including an individual retirement arrangement (IRA), or other tax-favored account. But if you are filing a return only because you owe this tax, you can file Form 5329 by itself.
2. You received any advance earned income credit (EIC) payments from your employer. These payments are shown in box 9 of your Form W-2.
3. You had net earnings from self-employment of at least \$400.
4. You had wages of \$108.28 or more from a church or qualified church-controlled organization that is exempt from employer social security and Medicare taxes.

WHO SHOULD FILE A RETURN?

The charts, noted previously in this lesson, may indicate that an individual does not have to file a tax return. However, in three instances, individuals *should* file a return:

- to claim a refund of withheld taxes,
- to claim a earned income credit, and
- to claim the additional child tax credit.

HELPING THOSE WHO DON'T NEED TO FILE

The Reduce Unnecessary Filing Program (RUF) is intended to help certain individuals determine their need to file a federal income tax return. Use Form 9452, *Filing Assistance Program Worksheet*, to help potential unnecessary filers determine whether or not they need to file.

Thank you for helping to save time and effort for your VITA and TCE clients and for helping to reduce the cost to all taxpayers of processing unnecessary returns by helping your clients with Form 9452 and related materials, as needed.

TAXWISE HINT

After completing the tax return refer back to the Main Information screen and select the appropriate tax form.

▶▶ **SUMMING UP THIS SECTION** ◀◀

Use the charts provided in this section to determine who *must* and who *should* file a tax return.

Exercises

20. Emily is married and has one dependent child. She has not lived with her husband since May and is head of household. She is under 65 and not blind. Her gross income from wages is \$15,000. Is she required to file a tax return? _____
21. Larry and Zelda are married but will not file a joint return. Both are under 65 and not blind. Larry's gross income from wages is \$30,150. Zelda's gross income is \$3,500.
- A. Is Larry required to file? _____
- B. Is Zelda required to file? _____



WHO MUST FILE
WHO SHOULD FILE

ANSWERS TO EXERCISES

Exercise 20

Yes

Exercise 21

A. Yes

B. Yes

WHICH FORM TO USE?

FORM 1040EZ

Form 1040EZ is for single and joint filers with no dependents. The form is no longer designed to be read by an optical scanning machine. The form instructions booklet has a worksheet for taxpayers who can be claimed as dependents.

FORM 1040A

Form 1040A is a two-page form. Page 1 of the form shows the filing status, exemptions, income, and adjusted gross income. Page 2 of the form shows the standard deduction, exemption amount, taxable income, tax, credits, payments, amount owed or refund, and signature. Form 1040A may have four schedules. Use **Schedule 1** to report interest and/or dividend income that is more than \$1,500. Use **Schedule 2** to report child and dependent care expenses and to figure the credit. Claim the credit for the elderly or the disabled on **Schedule 3**. This credit is explained in Lesson 14. If the taxpayer can take the earned income credit and has a qualifying child, use **Schedule EIC** to give information about that child. Schedule EIC is discussed and illustrated in Lesson 9.

FORM 1040

Form 1040 is a two-page form. Page 1 of the form shows the filing status, exemptions, income, and adjusted gross income. Page 2 shows the standard deduction or itemized deductions, the exemption amount, taxable income, tax, credits, other taxes, payments, and the amount owed or refund due.



IRS *e-file* offers quick and easy options to traditional paper returns. These options include filing electronically through an authorized tax practitioner, over the telephone, and by personal computer. For those expecting a refund, these options all offer Direct Deposit to a bank account. For those with a balance due, paying is made easier with the option of payment by credit card or a direct debit to their bank account.

Why *e-file*? Because IRS *e-file* makes filing faster and more accurate and gets the taxpayer their refund in half the usual time....even faster with Direct Deposit!

As a volunteer, you should become familiar with these options as there will be occasions when you are called upon to answer questions from taxpayers regarding one or more of them. You may even have the opportunity to volunteer at a VITA or TCE site that has been set up to offer electronic tax filing. If so, you will receive additional specialized training on using return preparation software and on other procedures unique to this type of site.

TeleFile

Eligible 1040EZ filers, single or married filing jointly, who receive a TeleFile tax booklet and have the same address as the previous year, can file their federal income taxes by using a touch tone telephone and dialing a toll-free telephone number found in the tax booklet. (Note: Taxpayers in Georgia, Indiana, Kentucky, Maryland, Oklahoma, Oregon, or West Virginia have the option to TeleFile both their federal **and** state tax returns in the same toll-free telephone call.)

Here's how it works: the taxpayer completes the TeleFile Tax Record found in the booklet before making the call. The call, which prompts the taxpayer through recorded instructions, takes less than ten minutes. The TeleFile system calculates the tax and refund (or balance due) and then files the tax return. If the taxpayer requests Direct Deposit, a refund can be issued in as little as 10 days. **TeleFile is completely paperless; no forms are mailed to IRS, not even W-2s!** The taxpayer "signs" the return with a special Customer Service Number (CSN) provided in the booklet.

TeleFile is available 24 hours a day, seven days a week, through August 15. It is also available to users of TDD/TTY equipment. Credit card and direct debit payment options are available for balance due returns.

Because TeleFile is so easy to use, and because it is completely paperless, its use should be encouraged at every VITA and TCE site that encounters an eligible taxpayer with a TeleFile tax booklet. Even if there is no touch tone telephone available at the site, you should do everything possible to convince the taxpayer to file from home, or wherever a touch tone phone is available.

INTRODUCTION AND OBJECTIVES

In this lesson you will learn to distinguish between taxable and nontaxable income. You will also learn where to report the different types of income. In addition, you will learn to make income entries on Forms 1040EZ, 1040A, and 1040.

This lesson will help you achieve the following objectives.

- Determine what is taxable and nontaxable income.
- Determine where to report income on Forms 1040, 1040A, and 1040EZ.
- Identify who can file Schedule C-EZ.
- Identify who must file Schedule SE.

TAXABLE AND NONTAXABLE INCOME

Taxable income is any income that is subject to tax. It must be reported on a tax return, unless the amount is so small that the individual is not required to file a return.

The following types of income are taxable:

- Wages, salaries, bonuses, and commissions
- Certain fringe benefits
- Tips and other compensation for personal services
- Interest*
- Dividends
- Refunds of state and local taxes**
- Alimony received or separate maintenance payments received
- Business income
- Hobby income (a hobby loss is not deductible)
- Capital gains
- Gain from the sale of property
- Pensions and annuities (part may be nontaxable)
- IRA distributions (part or all may be nontaxable)
- Rents received
- Royalties

- Estate or trust income
- Supplemental unemployment benefits
- Unemployment compensation
- Railroad retirement benefits (part may be taxable)
- Social security benefits (part may be taxable)
- Jury duty pay
- Executors' fees
- Gambling winnings (including lotteries, contests, raffles, etc.)
- Nonqualifying scholarships and fellowships
- Payments for punitive damages and compensatory damages not attributable to physical injuries or sickness
- Certain long-term care benefits. If the taxpayer received copy B of Form 1099-LTC, refer him or her to a paid professional preparer because some of the benefits may be taxable.

*Some interest is not taxable (for example, interest on certain state and local bonds and on qualified Series EE and Series I savings bonds used to pay for higher education expenses).

**Refunds of state and local taxes are taxable only if the taxpayer itemized deductions in the year the taxes were paid and the individual's tax liability was REDUCED because of the deduction.

Nontaxable income is income that is exempt from tax. If a return must be filed, some types of nontaxable income will be shown on the return but will not be added into the amount of income subject to tax.

The following types of income are nontaxable:

- Child support
- Federal income tax refunds
- Certain dividends on life insurance
- Gifts, bequests, and inheritances (may be subject to other taxes)
- Insurance and certain other payments for physical injury and sickness
- Interest on certain Series EE and Series I savings bonds redeemed to pay for qualified higher education expenses
- Interest on certain state and local obligations (municipal bonds)
- Most life insurance proceeds paid upon death (and certain accelerated death benefits or payments received under a life insurance contract on the life of a terminally or chronically ill individual before the individual's death)
- Public assistance payments (certain TANF payments)
- Certain railroad retirement benefits (part may be exempt)
- Social security benefits (part may be exempt)

- Veterans' disability benefits
- Workers' compensation
- Qualified scholarships and fellowships
- Certain dependent care services provided by employer
- Interest on insurance dividends left with VA
- Certain employer-provided educational benefits (up to \$5,250)
- Employer-provided assistance for qualifying adoption expenses. (Refer taxpayers with adoption expenses to a paid professional tax preparer and to Publication 968, *Tax Benefits for Adoption*)
- Restitution payments and excludable interest received by Holocaust victims, their heirs, or their estates, for persecutions are not taxable.
- Certain long-term care benefits. If the taxpayer received copy C of Form 1099-LTC, he or she is not the policyholder. The form is for information only and should be disregarded because none of the benefits are taxable to him or her. If the taxpayer received copy B of Form 1099-LTC, refer him or her to a paid professional preparer because some of the benefits may be taxable.

Example 1

Robert received the following income: wages, interest, child support, alimony, inheritance, workers' compensation, and lottery winnings.

The wages, interest, alimony, and lottery winnings are taxable income and will appear on Robert's tax return.

Child support, inheritance, and workers' compensation are nontaxable income and will not appear on Robert's tax return.

Exercise 1

Indicate whether the income listed is taxable or nontaxable.

Type of Income	Nontaxable	Taxable
1. Wages	_____	_____
2. Dividends from stock	_____	_____
3. Veterans' disability benefits	_____	_____
4. Child Support	_____	_____
5. Credit union dividends	_____	_____
6. Cash bonuses	_____	_____
7. Inheritances	_____	_____
8. Tips	_____	_____
9. Worker's compensation	_____	_____
10. Veteran's life insurance dividends	_____	_____

ALERT



New line added to Forms 1040 and 1040A for qualified dividends.

Qualified dividends are eligible for the capital gains rates.

WHERE TO REPORT INCOME

Taxpayers can report only wages, salaries, tips, unemployment compensation, qualified state tuition program payments, Alaska Permanent Fund dividends, taxable scholarship and fellowship grants, and interest income of \$1,500 or less on Form 1040EZ.

In addition to the types of income that can be reported on Form 1040EZ, ordinary and qualified dividends, capital gains distribution, interest income greater than \$1,500, IRA distributions, pension and annuity income, and taxable social security and equivalent railroad retirement benefits can be reported on Form 1040A.

These and all other types of income can be reported on Form 1040.

EARNED INCOME

Wages and Salaries

The total of wages, salaries, tips, and taxable scholarships and fellowships are reported on Form 1040EZ, line 1, Form 1040A or Form 1040, line 7.

Wages, salaries, and tips are primary examples of earned income received for services performed. Wages and salaries are compensation received. Tips are money and goods received as a gratuity by food servers, maids, porters, etc.

Form W-2. Form W-2, *Wages and Tax Statement*, reports the employee's earned income for the year. Employers should issue Form W-2 to every employee and a copy to the Social Security Administration. Box 1, *Wages, tips, and other compensation*, shows the amount of payments received in cash, goods and services, bonuses, supplemental unemployment benefits, awards, and taxable employee benefits. This amount should be included on the return.

An individual taxpayer or a couple filing jointly might have one or more Forms W-2s from various employers. When the taxpayer and/or spouse receive Forms W-2s from their employers, add the amounts from Box 1 of each Form W-2 and report the total amount on the return.

Generally, if a **household employee** earned less than \$1,400 a year while working in the employer's home, the employer is not required to provide the taxpayer with a Form W-2 but, the income must be included on line 7 (Form 1040A or 1040) or line 1 (Form 1040EZ). However, a Form W-2 is required if the employer withheld federal income taxes.

If a taxpayer does not get a Form W-2, or if the one he or she gets is not correct, the taxpayer will have to contact his or her employer as soon as possible. Only an employer can **issue** a Form W-2 or a Form W-2c.

In the event that the employer prepared an incorrect W-2, a Form W-2c, *Corrected Wage and Tax Statement*, should be issued. Use the W-2c amounts on the return. Be sure to attach the Form W-2c to the taxpayer's return.

All wage, salary, and tip income must be reported on the return, even if the employee did not receive a Form W-2.

If the taxpayer does not receive a Form W-2 by January 31, he or she should first contact the employer and find out if or when the Form W-2 was mailed. If after allowing a reasonable amount of time for the employer to issue or reissue the Form W-2, the Form W-2 still has not been received, he or she should contact the IRS for assistance at 1-800-829-1040, but not before February 15.

If after requesting a Form W-2 from the employer the taxpayer does not receive it by the due date of the return, he or she should file a Form 4852, *Substitute for Form W-2, Wage and Tax Statement or Form 1099-R, Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRA's, Insurance Contracts, Etc.*

The taxpayer should keep a copy of Form 4852 for his or her records and file a copy with the Social Security Administration to ensure proper social security credit.

POTENTIAL PITFALLS



Volunteers should be alert to the following possible indications of fraudulent activity:


- Forms W-2 that are typed, handwritten or have noticeable corrections
- Form W-2 from a firm in the area that is different from other Forms W-2s issued by the same firm
- Suspicious person accompanying the taxpayer and observed on other occasions
- Multiple refunds directed to the same address or P.O. Box
- Employment or earnings, that are a basis for refundable credits, that are not well documented
- Similar returns (e.g. same amount of refund, or same number of dependents, or same number of Forms W-2s)

ALERT



In 2003, household employers are required to issue a Form W-2 to employees whose earnings are \$1,400 or more.

Exhibit 1

a Control number		OMB No. 1545-0008		Safe, accurate, FAST! Use				Visit the IRS Web Site at www.irs.gov .	
b Employer identification number		1 Wages, tips, other compensation		2 Federal income tax withheld					
c Employer's name, address, and ZIP code		3 Social security wages		4 Social security tax withheld					
		5 Medicare wages and tips		6 Medicare tax withheld					
		7 Social security tips		8 Allocated tips					
d Employee's social security number		9 Advance EIC payment		10 Dependent care benefits					
e Employee's first name and initial Last name		11 Nonqualified plans		12a See instructions for box 12					
		13 Statutory employee Retirement plan Third-party sick pay		12b					
		<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12c					
		14 Other		12d					
f Employee's address and ZIP code									
15 State	Employer's state ID number	16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.	19 Local income tax	20 Locality name			
<p>Form W-2 Wage and Tax Statement 2003 Department of the Treasury—Internal Revenue Service</p> <p>Copy B To Be Filed with Employee's FEDERAL Tax Return. This information is being furnished to the Internal Revenue Service.</p>									

Form 1099-MISC. Taxpayers with earnings reported on Form 1099-MISC, Miscellaneous Income, may be considered self-employed. These amounts are reported on Schedule C-EZ or Schedule C. Net losses and profits are reported on line 12 of Form 1040. Self-employment income is discussed later in this lesson.

Some employers misclassify workers as independent contractors and report their earnings on Form 1099-MISC. Taxpayers who believe they have been misclassified should contact the IRS.

<input type="checkbox"/> CORRECTED (if checked)				
PAYER'S name, street address, city, state, ZIP code, and telephone no.		1 Rents	OMB No. 1545-0115 2003 Form 1099-MISC	Miscellaneous Income
		\$		
		2 Royalties		
		\$	4 Federal income tax withheld	Copy B For Recipient
		3 Other income	\$	
PAYER'S Federal identification number	RECIPIENT'S identification number	5 Fishing boat proceeds	6 Medical and health care payments	This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
		\$	\$	
RECIPIENT'S name		7 Nonemployee compensation	8 Substitute payments in lieu of dividends or interest	
		\$	\$	
Street address (including apt. no.)		9 Payer made direct sales of \$5,000 or more of consumer products to a buyer (recipient) for resale <input type="checkbox"/>	10 Crop insurance proceeds	
		\$	\$	
City, state, and ZIP code		11	12	
Account number (optional)		13 Excess golden parachute payments	14 Gross proceeds paid to an attorney	
		\$	\$	
15		16 State tax withheld	17 State/Payer's state no.	18 State income
		\$		\$
		\$		\$
Form 1099-MISC		(keep for your records)		Department of the Treasury - Internal Revenue Service

Tip Income

All tip income is taxable. Individuals who receive **\$20 or more per month in tips** while working one job must report their tip income to their employer. Tips that are reported to employers are included with wages on Form W-2, box 1. If the taxpayer received tip income of \$20 or more in a month and did not report all of those tips to the employer, he or she must report the social security and Medicare taxes on the unreported tips as additional tax on Form 1040. Form 4137, *Social Security and Medicare Tax on Unreported Tip Income*, should be used to compute and report the additional tax.

Individuals who receive **less than \$20 per month in tips** while working one job do not have to report their tip income to their employer. Additionally, noncash tips (for example, tickets or passes) do not have to be reported to the employer. Tips of less than \$20 per month or noncash tips are not subject to social security and Medicare taxes. However, this tip income is subject to federal income taxes and must be reported on line 7 of Form 1040 or Form 1040A, or line 1 of Form 1040EZ.

POTENTIAL PITFALLS

If the taxpayer fails to report tip income as required to the employer, the taxpayer may be subject to a penalty equal to 50% of the social security and Medicare taxes owed on unreported tips.

POTENTIAL PITFALLS



The following individuals cannot file Form 1040EZ or 1040A; they must file Form 1040:

(1) Individuals who received \$20 or more in tips in any month while working for one employer and who did not report the full amount to the employer. (These tips are subject to social security and Medicare tax.) (2)

Taxpayers whose Form W-2 has an amount entered in box 8, *Allocated tips*, that they must report as income. For more information, see Publication 531, *Reporting Tip Income*.

Allocated tips are tips an employer assigns to an employee. They are in addition to the tips the employee reported to the employer. The taxpayer may have allocated tips if he or she worked in a restaurant, cocktail lounge, or similar business that must allocate tips to employees.

Allocated tips are shown separately in box 8 of Form W-2. They are not included in the amount in box 1. The taxpayer must report allocated tips on his or her tax return unless either of the following exceptions applies.

- 1) The taxpayer kept a daily tip record, or other evidence that is as credible and as reliable as a daily tip record, as required. (See Pub. 531, Reporting Tip Income).
- 2) The taxpayer's tip record is incomplete, but it shows that his or her actual tips were more than the tips reported to his or her employer plus the allocated tips.

If either exception applies, report actual tips on the return. Do not report the allocated tips.

If the taxpayer is required to report allocated tips on the return, the amount on Form W-2, box 8, should be added to the amount in box 1. The total is reported on line 7 of Form 1040. Allocated tips cannot be reported on Form 1040EZ or 1040A, and are subject to social security and Medicare taxes. Form 4137 should be used to compute and report the additional tax.

The taxpayer should keep a copy for his or her records and file a copy with the local Social Security Administration to ensure proper social security credit.

Example 2

Fred works as a repairman during the week and as a barber on alternate Saturdays. His tips are less than \$20 in any month and he does not report them to his employer. The amounts from box 1 on his Forms W-2 show income of \$23,500 (repairman) and \$1,950 (barber). His unreported tip income was \$200.

Fred will report \$25,650 on Form 1040A, line 7. This is the total of his Form W-2, box 1 income and his unreported tip income (\$23,500 plus \$1,950 plus \$200).

If Fred reported his tip income to his employer, the tips would be included in box 1 of the Form W-2. The amount in box 1 of that Form W-2 would be \$2,150 (\$1,950 plus \$200). Fred would still enter \$25,650 on line 7 (\$23,500 plus \$2,150).

Scholarships and Fellowships

Some scholarships and fellowships may be partially taxable. If the taxpayer received a Form W-2 for the scholarship or fellowship, add the amount in box 1 to any other box 1 amounts. Enter the total on line 1, Form 1040EZ, or line 7, Form 1040A or 1040.

Even if the taxpayer did not receive a Form W-2 for the scholarship or fellowship, the taxable portion of the scholarship or fellowship must be reported. Add the taxable portion to other Form W-2, box 1 amounts and unreported tip income. Enter the total on line 7 (Form 1040 or 1040A) or line 1 (Form 1040EZ). Write "SCH" and the amount not reported on Form W-2 in the space to the left of line 7 or line 1, whichever applies.

Exercise 2

- A.** Mike worked two jobs. He was a quality inspector during the week and a bartender on the weekends. He reported all of his tip income (\$3,000) to his employer. His Forms W-2, box 1, showed income of \$21,000 (quality inspector) and \$8,250 (bartender). What amount will Mike report on his Form 1040A, line 7? _____
- B.** John works as a food server in an expensive restaurant. He tells you that he did not report his tip income of \$18,100 to his employer. Can John file Form 1040A? _____
- C.** Randy had several employers during the tax year. On February 3, 2004, he comes into the VITA site to have his return prepared. He tells you that he has not received the Form W-2 for XYZ Inc. What should you tell Randy? _____

INTEREST INCOME

Money earns interest when it:

- is deposited in accounts in banks, savings and loans, credit unions,
- is used to buy certificates of deposit or bonds, or
- is lent to another person or business.

Interest income is considered unearned income. Money, not a person, is working to earn the income.

TAXABLE INTEREST INCOME

Savings Accounts

Interest is reported in the year that it is credited to the taxpayer's account and is available for withdrawal by the taxpayer. The taxpayer should report all interest received during the year, even if the interest is not entered in the taxpayer's passbook.

POTENTIAL PITFALLS



Some savings and loans, credit unions, cooperative banks, and mutual savings banks call their distributions "dividends." These "dividends" are really interest and are reported as interest. True dividends are different and will be discussed later in this lesson.

U.S. Savings Bonds

Interest on U.S. savings bonds is earned in one of two ways.

- Some bonds are issued at a “discount” and the interest earned equals the increase in the bond’s value over a period of time.
- Some bonds pay interest at stated intervals of time.

Series EE and Series I Bonds. Series EE bonds are the most common type. They are issued at a discount; this means that the purchase price is less than the face value (the amount shown on the bond). The interest is the difference between the purchase price and the amount received when the bonds are redeemed (cashed in).

Series I bonds were first offered in 1998. They are issued at face value with a maturity period of 30 years. Interest on these bonds is paid when the bond is redeemed.

Taxpayers can choose one of two ways to report interest income from these bonds.

- Report the increase in value when the bond is cashed in or when the bond matures, whichever is earlier.
- Report the increase in the bond’s value each year.

Generally, taxpayers must use the same method for all Series EE and Series I bonds they own.

If a U.S. savings bond is issued in the names of co-owners, such as the taxpayer and child, or the taxpayer and spouse, interest on the bond is generally taxable to the co-owner who purchased the bond. To determine who is responsible for paying the tax on a bond see the table below.

Exhibit 3

Who Pays Tax on U.S. Savings Bond Interest	
IF...	THEN tax on the bond interest must be paid by...
You use your funds to buy a bond in your name and the name of another person as co-owners.	You.
You buy a bond in the name of another person, who is the sole owner of the bond.	The person for whom you bought the bond.
You and another person buy a bond as co-owners, each contributing part of the purchase price.	Both you and the other co-owner, in proportion to the amount each paid for the bond.
You and your spouse, who live in a community property state, buy a bond that is community property.	You and your spouse. If you file separate returns, both you and your spouse generally pay tax on one-half.

Example 3

Barbara owns a \$500 U.S. Series EE savings bond. She paid \$250 for the bond. When the bond matures, Barbara will receive \$500. At the end of the first year, the bond was worth \$265.

Barbara can report interest income in one of two ways.

- She can report \$250 of interest income when the bond matures. This is the difference between the \$500 value at maturity and the \$250 she paid for the bond. Barbara would report interest income only once, at maturity.
- She can report \$15 of interest income at the end of the first year. This is the increase in value at the end of the year (\$265 minus \$250). Barbara would report interest income each year until maturity.

Excludable Interest on U.S. Savings Bonds. Taxpayers may be able to exclude from income all or part of the interest received from certain qualified U.S. savings bonds. The taxpayer must have paid for qualified higher education expenses the same year the bonds are cashed. The bonds must be either Series EE bonds issued after 1989 or Series I bonds in the taxpayer's name or, if married, the taxpayer's name or spouse's name. The individual in whose name the bonds were issued must be 24 years of age or older before the bonds were issued. The taxpayer cannot file married filing separately.

Qualified higher education expenses include tuition and fees paid to an eligible educational institution for the bond owner, the bond owner's spouse, or the bond owner's dependent for whom the bond owner claims an exemption. An eligible educational institution is any college, university, vocational school, or other postsecondary educational institution eligible to participate in a student aid program administered by the Department of Education.

Qualified expenses include any **contribution** to a qualified state tuition program or to a Coverdell ESA. (For more information, see Publication 970, *Tax Benefits for Higher Education*).

Use Form 8815, *Exclusion of Interest From Series EE and I U.S. Savings Bonds Issued After 1989 (For Filers with Qualified Higher Education Expenses)*, to report the exclusion of interest income. The excludable amount is transferred from Form 8815 to Part I, line 3 of Schedule 1 (Form 1040A) or to Schedule B (Form 1040).

Series HH Bonds. The interest on these bonds is paid twice a year. Report the interest on these bonds in the year in which it is received.

Other U.S. Obligations. Interest on other U.S. obligations, such as U.S. Treasury notes and bonds, is fully taxable when received.

Savings Certificates, Money Market Certificates, and Other Deferred Interest Accounts

Interest that is paid at fixed intervals of one year or less is included in taxable income when it is received or when the taxpayer could receive it (that is, when it is credited to the account, even if it is not withdrawn) without paying a substantial penalty. If an account matures in one year or less and provides a single interest payment at maturity, include the interest in taxable income when the account matures and the interest is received.

Example 4

Duane has a six-month certificate of deposit (CD) that matures in January 2004. He will receive \$75 in interest income.

Duane will report the interest income on the certificate of deposit on his 2004 tax return. It matures in one year or less with a single interest payment at maturity.

Certificates of Deposit with Maturities of Over One Year

If interest on a CD is deferred for more than one year, the taxpayer must include a part of the interest in income each year. The taxpayer should receive Form 1099-INT stating the amount to report.

Example 5

Deborah has a two-year CD that pays interest every three months. She bought the CD on March 1, 2003. It matures on February 29, 2005.

For 2003, Deborah reports the interest income earned from March through December. For 2004, she will report 12 months of interest. For 2005, she will report two months of interest.

Original Issue Discount. Long-term obligations that pay no interest before maturity are considered to be issued at a discount.

Original Issue Discount (OID) is the amount by which the principal amount (redemption price at maturity) of a long-term debt instrument, such as a bond or note, exceeds its issue price. Taxpayers generally report a portion of the OID each year until the obligation matures.

Example 6

Roger purchased a \$1,000 U.S. Treasury Zero Coupon Bond for \$350. When the bond matures, Roger will receive \$1,000. He will receive no interest income until the bond matures many years later.

The difference between the redemption amount (\$1,000) and the issue price (\$350) is the OID (\$650). Each year until maturity, Roger must recognize part of the OID as taxable interest income.

Interest on Insurance Proceeds

Life insurance proceeds include interest. Taxpayers can receive life insurance policy benefits paid upon the death of the insured either in a lump sum or in installments. Generally, if the payments are received in installments, the portion that is interest must be included in the taxpayer's income. However, if the insured individual died before October 23, 1986, and was the taxpayer's spouse, the first \$1,000 of interest income received each year is not taxed if the payments are received in installments. This exclusion does not apply if proceeds are left on deposit with the insurance company and only interest is paid.

Life insurance dividends generally are not taxable. These dividends may be used to reduce life insurance premiums due, purchase additional paid-up insurance, or earn interest. In general, the interest earned on life insurance dividends is taxable when it is credited to the taxpayer's account.

Interest on insurance dividends that have been left on deposit with the Department of Veterans Affairs (VA) is **not** taxable. Do not include this interest in taxable income.

COVERDELL ESA

Contributions to a Coverdell ESA are not deductible. Amounts in the ESA grow (tax deferred) until they are distributed. Generally, if the beneficiary has qualified education expenses that are greater than the distribution during the year, then no tax is due.

If the taxpayer received Form 1099-Q, showing a distribution from a Coverdell ESA, ask the taxpayer if the funds were used for qualified education expenses. Coverdell ESA qualified education expenses include elementary, secondary, and postsecondary (higher) education expenses.

If the entire amount of the distribution was spent on qualified elementary and secondary expenses, the distribution is tax-free. Tax-free distributions are not reported. If the taxpayer paid for qualified higher (postsecondary) education expenses, the taxpayer may be eligible for the Hope Credit or Lifetime Learning Credit, which may be more beneficial.

Refer the taxpayer/beneficiary to a paid professional tax preparer and/or Publication 970, *Tax Benefits for Higher Education*, if:

- The funds were not used for qualified education expenses.
- The distribution is more than the amount spent for qualified expenses.

ALERT



Starting in 2003, Coverdell ESA distributions are no longer reported on Form 1099-R. They are reported on Form 1099-Q.

- Part or all of the distribution is taxable and earnings must be computed.
- The taxpayer/beneficiary received other education benefits such as a distribution from a Qualified Tuition Program, employer provided educational assistance, or a scholarship, or used U.S. Savings Bonds to pay for qualified education expenses.
- If any amount needs to be reported, report it on Form 1040, line 21. Additional tax may be due. Use Part II of Form 5329, *Additional Taxes on Qualified Plans (including IRAs) and Other Tax Favored Accounts*, to figure any additional tax.

TAX-EXEMPT INTEREST

Certain types of interest are exempt from federal income tax. Bonds issued by the following entities generally pay **tax-exempt interest**:

- State and political subdivisions (county or city),
- District of Columbia, and
- U.S. possessions and political subdivisions.

Examples of tax-exempt bonds are those issued by:

- Port authorities
- Toll-road commissions
- Utility service authorities
- Community redevelopment agencies
- Qualified volunteer fire departments
- Amounts indicated on broker statements as tax-exempt interest or dividends

Although tax-exempt interest is not taxable, the taxpayer must report all tax-exempt interest on Form 1040, 1040A or 1040EZ.

Form 1099-INT

Interest income is reported to the taxpayer on Form 1099-INT, *Interest Income*. A copy of Form 1099-INT is also sent to the IRS.

Box 1 shows taxable interest income from various institutions.

Some taxpayers withdraw funds from a time deposit before the maturity date of the account and, therefore, incur an interest penalty. The early withdrawal penalty is reported on Form 1099-INT in box 2. Report the total interest earned, shown in box 1 of Form 1099-INT, on line 8a of Form 1040. Do not subtract the penalty from the total interest. The early withdrawal penalty is an adjustment to income and is entered on line 31 of Form 1040.

Box 3 shows U.S. savings bond and Treasury obligations interest. Be sure to ask the taxpayer about this interest income. The amount shown on Form 1099-INT may be too high if the taxpayer was not the original owner of the bond or if the taxpayer has reported the interest income each year as it was earned.

Some Forms 1099-INT will have entries in box 4 indicating that federal income tax has been withheld from the interest paid. Be sure to include the amount shown in box 4 with other tax withheld on Form 1040A, line 39, or Form 1040, line 61.

Exhibit 4

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0112		2003 Interest Income
PAYER'S name, street address, city, state, ZIP code, and telephone no.		Payer's RTN (optional)		
PAYER'S Federal identification number		RECIPIENT'S identification number		Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
RECIPIENT'S name		1 Interest income not included in box 3 \$		
Street address (including apt. no.)		2 Early withdrawal penalty \$		
City, state, and ZIP code		3 Interest on U.S. Savings Bonds and Treas. obligations \$		
Account number (optional)		4 Federal income tax withheld \$		
		5 Investment expenses \$		
		6 Foreign tax paid \$		
		7 Foreign country or U.S. possession		
Form 1099-INT		(keep for your records)		Department of the Treasury - Internal Revenue Service

Form 1099-OID

Form 1099-OID, *Original Issue Discount*, reports the amount of Original Issue Discount income that a taxpayer should report as income for the year. A copy of Form 1099-OID is also sent to the IRS.

Box 1 shows the amount of interest (OID) for the year if the taxpayer bought the obligation at its original issue and held the issue all year.

Box 2 shows regular interest paid on the obligation other than the OID income.

Reporting Interest Income

If the taxpayer is a **1040EZ** filer, taxable interest income is reported on line 2. 1040EZ filers should report tax-exempt interest by writing “TEI” and the amount of tax-exempt interest on line 2 as shown in the example below. Do not include tax-exempt interest in the *Dollars/Cents* portion of line 2. If the taxpayer’s interest income is more than \$1500, he or she cannot file a Form 1040EZ.

Example 7

Jennifer received taxable interest income of \$65 and tax-exempt interest income of \$23. She would report her interest income on Form 1040EZ as shown in the exhibit below.

Exhibit 5		Jennifer's 1040EZ	
Income Attach Form(s) W-2 here. Enclose, but do not attach, any payment. Note. You must check	1	Total wages, salaries, and tips. This should be shown in box 1 of your W-2 form(s). Attach your W-2 form(s).	1
	2	Taxable interest. If the total is over \$400, you cannot use Form 1040EZ. TEI=\$23.00	2 6 5 0 0
	3	Unemployment compensation, qualified state tuition program earnings, and Alaska Permanent Fund dividends (see page 14).	3
	4	Add lines 1, 2, and 3. This is your adjusted gross income .	4
	5	Can your parents (or someone else) claim you on their return? Yes. Enter amount from No. If single, enter 7,450.00.	

Taxpayers who file **Forms 1040A or 1040**, report taxable interest income on line 8a and tax-exempt interest on line 8b.

If the taxpayer files Forms 1040A or 1040 and:

- Has interest income of more than \$1500,
- Wants to claim an exclusion for savings bond interest in the same year that he or she paid for qualified higher education expenses, or
- Receives a Form 1099-INT for tax-exempt interest,

Schedule 1, Part I (1040A) or Schedule B, Part I (1040) must be completed, before making an entry on line 8a or 8b.

If the tax-exempt interest is shown on a Form 1099-INT, and a Schedule 1 or B must be filed, the taxpayer must include tax-exempt interest on Schedule 1 or B. It should be reported on line 1 but it should not be included in the total on line 2. Instead, under the last entry on line 1, a subtotal of all interest listed should be made. Below the subtotal, the taxpayer should write “Tax-exempt interest” and show the amount. Subtract it from the subtotal and the result should be entered on line 2.

On Schedule 1 or Schedule B, Part I, list the interest payers’ names and the various amounts received for each form, even if there are two or more forms from the same source.

Exercise 3

A. Randy and Ann have three Forms 1099-INT: Epping National Bank, \$62; Epping Credit Union, \$178; and Brenton Savings and Loan, \$760.

1. How much interest income will be reported on Schedule 1 (Form 1040A)? _____

2. How much interest income will be reported on Form 1040A, line 8a? _____

B. Catherine received \$398 interest income this year. She files Form 1040EZ. How much interest income is reported on her return, and where is it reported? _____

C. Emily and Andrew file a joint return on Form 1040. They have the following interest income: City Savings and Loan (joint), \$320; Third National Bank (Andrew), \$100; U.S. Series HH Savings Bonds (joint), \$45; and Welder's Credit Union (Emily), \$30. _____

How much interest is reported on their Form 1040, and where is it reported? _____

DIVIDEND INCOME AND OTHER CORPORATE DISTRIBUTIONS

Dividends are payments made by corporations to shareholders. Dividends can also be paid through partnerships, estates, or trusts.

There are several types of corporate distributions, including ordinary and qualified dividends, capital gain distributions, nontaxable distributions, stock dividends, and others. Most dividends are paid in cash. Some dividends, however, are paid in property, services, or additional shares of stock. Only **ordinary and qualified dividends** can be reported on Form 1040A. Any other dividends or distributions received are reported on Form 1040. Taxpayers with dividend income may not use Form 1040EZ. Other types of dividends and distributions include the following:

- Dividend reinvestment — Through **dividend reinvestment**, instead of receiving cash (a dividend check), some stockholders ask the corporation to use their dividends to purchase more shares of the corporation's stock. The shareholders "reinvest" their dividends. The dividend is taxable at the time it would be paid if it were in cash.
- Capital gain distributions — Mutual funds (regulated investment companies) and real estate investment trusts (REITs) pass capital gains to their investors in the form of **capital gain distributions**. Capital gain distributions are treated as long-term capital gains, regardless of how long the taxpayer holds the shares. See Lesson 11, *Sale of Stock*, for more information on capital gains.

ALERT



In 2003, line 9b is added to Forms 1040 and 1040A for qualified dividends.

- Return of capital — A **return of capital** represents a return of part of the taxpayer's investment in the stock of the company. A return of capital reduces the basis of the stock and is not taxed until the taxpayer's basis in the stock is fully recovered. Any return of capital in excess of basis is treated as a capital gain and is reported on Schedule D, *Capital Gains and Losses*.
- Stock dividends — **Stock dividends** increase the taxpayer's number of shares in the company. Generally, stock dividends are not taxable.

Other types of nontaxable dividends are:

- Exempt-interest dividends paid by mutual funds (This interest is listed on Form 1040, line 8b.)
- Dividends on insurance policies, as long as they do not exceed the total of all net premiums paid by the taxpayer
- Dividends on veterans' insurance
- Certain patronage dividends

Reporting Dividends and Capital Gain Distributions

The payer reports dividends and certain other distributions on **Form 1099-DIV**, *Dividends and Distributions*.

Ordinary dividends are reported in box 1a of Form 1099-DIV. Add the amounts in box 1a from all the Forms 1099-DIV the taxpayer received. If the total is:

- \$1500 or less, enter the total on line 9a of Form 1040A or 1040.
- over \$1500, complete Schedule 1 (Form 1040A), Part II, or Schedule B (Form 1040), Part II. Transfer the result to line 9a of Form 1040A or 1040.

On Schedule 1 or Schedule B enter the payer's name and the amount received for each Form 1099-DIV even if the same corporation used separate forms to report more than one distribution. If the taxpayer has a substitute Form 1099-DIV from a brokerage firm, it may show a total for dividends received. Enter the brokerage firm as the payer of the dividends and enter the total dividend amount. Do not list the dividends individually.

Some taxpayers receive dividend income from shares that the husband and wife own jointly. If they file a joint return, enter the total dividend in the appropriate place on the return. If they file separate tax returns, divide the dividend by two. Report half on the husband's return and half on the wife's return.

Capital gain distributions occur when a mutual fund (regulated investment company) sells assets for more than their cost, and the realized capital gain is distributed to the fund's shareholders. This should not be confused with a capital gain that occurs when the owner of a mutual fund or a capital asset sells shares in the fund

ALERT



In 2003, Line 1 of Form 1099-DIV was changed to Line 1a—Ordinary dividends and Line 1b—Qualified dividends.

or the asset for more than the cost and realizes a capital gain. For more information on capital gains and losses, see Lesson 11, *Sale of Stock*.

Payers report capital gain distributions in box 2a of Form 1099-DIV. Taxpayers can report capital gain distributions directly on Form 1040A or Form 1040 if:

- The only amounts the taxpayer has to report on Schedule D are capital gain distributions (box 2a),
- The taxpayer does not have any Post-May 5 capital gain distributions (box 2b), qualified 5-year gain (box 2c) unrecaptured section 1250 gain (box 2d), or section 1202 gain (box 2e), and
- If the taxpayer files Form 4952, *Investment Interest Expense Deduction*, the amount on line 4e of Form 4952 is not more than zero.

Exhibit 6

<input type="checkbox"/> CORRECTED (if checked)				OMB No. 1545-0110	
PAYER'S name, street address, city, state, ZIP code, and telephone no.		1a Total ordinary dividends		2003	Dividends and Distributions
		\$			
		1b Qualified dividends		Form 1099-DIV	
		\$			
		2a Total capital gain distr.		2b Post-May 5 capital gain distr.	Copy B For Recipient
		\$		\$	
PAYER'S Federal identification number	RECIPIENT'S identification number	2c Qualified 5-year gain		2d Unrecap. Sec. 1250 gain	
		\$		\$	
RECIPIENT'S name		2e Section 1202 gain		2f Collectibles (28%) gain	This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
		\$		\$	
Street address (including apt. no.)		3 Nontaxable distributions		4 Federal income tax withheld	
		\$		\$	
City, state, and ZIP code				5 Investment expenses	
				\$	
Account number (optional)		6 Foreign tax paid		7 Foreign country or U.S. possession	
		\$		\$	
		8 Cash liquidation distributions		9 Noncash liquidation distributions	
		\$		\$	
Form 1099-DIV		(keep for your records)		Department of the Treasury - Internal Revenue Service	

If the taxpayer does not meet the requirements to report the capital gain distribution directly on Form 1040A or Form 1040, a Schedule D, *Capital Gains and Losses* must be filed. If a Schedule D is not required, the capital gain distributions can be reported directly on line 13a of Form 1040, or line 10 of Form 1040A. Capital gain distributions are not reported on Form 1040EZ.

If capital gain distributions are reported directly on Form 1040 or Form 1040A:

- Check the box next to line 13a, Form 1040 and
- Use the Capital Gain Tax Worksheet from either the Form 1040A or 1040 instruction booklet to compute tax.

The volunteer should be careful not to ignore other boxes on the Form 1099-DIV.

- Box 2c, *Qualified 5-year gain*. If the taxpayer has an entry in box 2c, see Lesson 11 for the proper treatment of the gain.
- Box 4, *Federal income tax withheld*. Be sure to include this amount on line 39 of Form 1040A or line 61 of Form 1040.
- Box 5, *Investment expenses*. If the taxpayer files Form 1040 and itemizes deductions on Schedule A, report the amount from box 5 as a miscellaneous itemized deduction subject to the 2%-of-adjusted-gross-income limit. (See *Itemized Deductions* in Lesson 4.)
- Box 6, *Foreign tax paid*. If the taxpayer has an entry in box 6, see Lesson 5 for the proper treatment of the tax. The taxpayer may be able to claim the Foreign Tax Credit.

A capital gain distribution is reported on a Schedule D when the taxpayer has more than capital gain distributions to report, for example when boxes 2b, 2d, 2e, 3, 8, or 9 have entries, or when the taxpayer has sold a capital asset. Capital gain distributions are always treated as long-term capital gains, regardless of how long the taxpayer holds the shares, and are reported on line 13, column (f) of the Schedule D. If the taxpayer has an entry in box 2b or 2c, then that number is reported on line 13 column (g).

POTENTIAL PITFALLS



If the state or local income tax refund reflects any deductions, credits, or payments for years other than 2002, refer the taxpayer to a paid professional tax preparer.

STATE AND LOCAL TAX REFUNDS

Taxpayers who receive a refund of state or local taxes may receive a Form 1099-G, *Certain Government Payments*. If the taxpayer claimed the standard deduction on the 2002 return and received a refund of 2002 state or local tax, the taxpayer does not have to include the refund in taxable income for tax year 2003. However, if the taxpayer itemized deductions **and** received a state or local tax refund, the taxpayer may have to include part or all of the refund in taxable income in 2003. Use the *State and Local Income Tax Refund Worksheet—Line 10* in the Form 1040 instruction booklet to determine what part, if any, of the refund is taxable. Enter the taxable portion of state and local refunds on Form 1040, line 10.

Exhibit 7

<input type="checkbox"/> CORRECTED (if checked)			
PAYER'S name, street address, city, state, ZIP code, and telephone no.		1 Unemployment compensation	OMB No. 1545-0120 2003 Form 1099-G
		\$	
PAYER'S Federal identification number		2 State or local income tax refunds, credits, or offsets	Form 1099-G
		\$	
RECIPIENT'S name	RECIPIENT'S identification number	3 Box 2 amount is for tax year	4 Federal income tax withheld
Street address (including apt. no.)		5	\$
City, state, and ZIP code		7 Agriculture payments	6 Taxable grants
Account number (optional)		\$	\$
			8 Box 2 is trade or business income <input type="checkbox"/>

Certain Government Payments

Copy B For Recipient

This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.

Form **1099-G** (keep for your records) Department of the Treasury - Internal Revenue Service

ALIMONY RECEIVED

Alimony or separate maintenance payments made under a court decree are taxable income to the person receiving them. They are reported on Form 1040, line 11. The person making the payments deducts them on Form 1040, line 32a, as an adjustment to gross income.

Child support payments are not alimony. The person making the payments cannot deduct them. The person receiving child support payments does not have to include them in income.

INCOME FROM BUSINESS (OPTIONAL TOPIC)

Business income or loss is reported first on Schedule C (Form 1040), *Profit or Loss From Business*, or Schedule C-EZ, *Net Profit From Business*, and then transferred to Form 1040, line 12.

Taxpayers who must file a Schedule C should see a paid professional tax preparer.

VITA and TCE volunteers who have received training on this topic, at the discretion of the site coordinator, may assist self-employed individuals who qualify to use Schedule C-EZ.

Who Can Use Schedule C-EZ

A taxpayer can use Schedule C-EZ only if he or she:

- Had business expenses of \$2,500 or less,
- Uses the cash method of accounting,
- Did not have an inventory at any time during the year,
- Did not have a net loss from his or her business,
- Had only one business as a sole proprietor,

POTENTIAL PITFALLS



Many taxpayers erroneously report amounts from Form 1099-MISC, Miscellaneous Income, with wages or other income. This income should instead be reported on Schedule C or C-EZ and on Schedule SE, Self-Employment Tax. If the income is reported incorrectly, IRS may later issue a notice of proposed tax increase for the self-employment income and tax.

- Had no employees during the year,
- Is not required to file Form 4562, *Depreciation and Amortization*, for this business (See the instructions for Schedule C, line 13, to find out if the taxpayer must file.),
- Does not deduct expenses for business use of his or her home, and
- Does not have prior year unallowed passive activity losses from this business.

Completing Schedule C-EZ

Schedule C-EZ has three parts:

Part I: General Information

Part II: Figure Your Net Profit

Part III: Information on Your Vehicle

Part I: General Information

Part I is used to determine whether or not the taxpayer is eligible to use this form instead of Schedule C for reporting self-employment income. If all the criteria are met, the taxpayer then completes Part I.

Line B, Principal Business Code, is determined by looking at the code list in the *Instructions for Schedule C, Profit or Loss From Business*.

Line D, Employer ID Number, is a number that the Internal Revenue Service supplies to businesses and other professional activities. If the taxpayer does not have one, the space should be left blank. The taxpayer cannot use the taxpayer's social security number.

Part II: Figure Your Net Profit

Gross receipts are all receipts from a trade or business including income reported on a Form 1099-MISC, *Miscellaneous Income*. All items of taxable income actually or constructively received during the year are included. Gross receipts are entered on line 1.

Total expenses include the total amount of all deductible business expenses actually paid during the year. Examples of these expenses include advertising, car and truck expenses, commissions, insurance, interest, legal and professional services and fees, office expense, rent or lease expense, repairs and maintenance, supplies, taxes, travel, 50% of business meals and entertainment, and utilities (including telephone). Total expenses of \$2,500 or less are entered on line 2.

If the taxpayer uses his or her car or truck for business purposes, he or she can deduct expenses related to using the car or truck. To determine the amount of car and truck expenses that can be deducted, the taxpayer must use either the:

- Standard Mileage Rate, or
- Actual Car Expenses.

Standard Mileage Rate. If the taxpayer can and does choose to use the standard mileage rate, business miles are multiplied by the applicable mileage rate and added to the deductible parking and tolls. Car expenses using the standard mileage rate are computed as follows:

$$\begin{array}{l} \text{Business miles incurred during the year} \times \mathbf{36\text{¢}} \text{ per mile} \\ + \text{ Parking and tolls incurred while on business } \end{array}$$

Actual Car Expenses. If the taxpayer chooses to use the actual car expenses, only the business portion of the expenses is deductible. Deductible expenses under the actual method are computed as follows:

1. Compute the percentage of business use:

$$\frac{\text{Business miles}}{\text{Total miles}} = \% \text{ of business use}$$

2. Determine the deductible expenses:

$$\begin{array}{l} (\% \text{ of business use} \times \text{total actual expenses}) \\ + \text{ Parking and tolls incurred while on business } \end{array}$$

NOTE: If taxpayers depreciate their car or truck, or their total expenses are more than \$2,500, they cannot use Schedule C-EZ and should be referred to a paid professional tax preparer.

Subtracting line 2 from line 1 and entering the net amount on line 3 determine net profit or loss.


If line 3 shows a profit, transfer this amount to Form 1040, line 12, and to Schedule SE, line 2 (except statutory employees). Attach Schedule C-EZ to Form 1040 in the correct sequence.

If line 3 is zero, show zero amount on Form 1040, line 12.

If line 3 shows a loss, the taxpayer cannot use Schedule C-EZ and should be referred to a paid professional tax preparer.

Part III: Information on Your Vehicle

Part III should be completed if the taxpayer is claiming car and truck expenses in Part II.

ALERT 
The 2003 rate for business use of your vehicle is 36 cents a mile.

SCHEDULE C-EZ (Form 1040) Department of the Treasury Internal Revenue Service	Net Profit From Business (Sole Proprietorship) ▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B. ▶ Attach to Form 1040 or 1041. ▶ See instructions on back.	OMB No. 1545-0074 <div style="font-size: 2em; font-weight: bold; text-align: center;">2003</div> Attachment Sequence No. 09A
Name of proprietor		Social security number (SSN)

Part I General Information

You May Use Schedule C-EZ Instead of Schedule C Only If You:

- Had business expenses of \$2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-4 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service	B Enter code from pages C-7, 8, & 9 ▶ | | | | | | | | | |
C Business name. If no separate business name, leave blank.	D Employer ID number (EIN), if any | | | | | | | | | |
E Business address (including suite or room no.). Address not required if same as on Form 1040, page 1. City, town or post office, state, and ZIP code	

Part II Figure Your Net Profit

1 Gross receipts. Caution. If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employees in the instructions for Schedule C, line 1, on page C-3 and check here <input type="checkbox"/>	1		
2 Total expenses (see instructions). If more than \$2,500, you must use Schedule C	2		
3 Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12 , and also on Schedule SE, line 2 . (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)	3		

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶/...../.....

5 Of the total number of miles you drove your vehicle during 2003, enter the number of miles you used your vehicle for:

a Business **b** Commuting **c** Other

6 Do you (or your spouse) have another vehicle available for personal use? **Yes** **No**

7 Was your vehicle available for personal use during off-duty hours? **Yes** **No**

8a Do you have evidence to support your deduction? **Yes** **No**

b If "Yes," is the evidence written? **Yes** **No**

Self-Employment Tax

Self-employment tax is a social security tax for persons who work for themselves. It is similar to the social security tax and Medicare tax withheld from employees' wages.

Special exemptions from self-employment tax may apply to members of the clergy, members of certain religious sects, and certain nonclergy church employees.

The tax is computed on Schedule SE and transferred to the Form 1040 to be added to other taxes owed. The Schedule SE is attached to the Form 1040.

Who Must File Schedule SE

A taxpayer must file Schedule SE if he or she has:

- Net earnings from self-employment of \$400 or more, other than church employee income (line 4 of Short Schedule SE),

OR

- Church employee income of \$108.28 or more (line 5a of Long Schedule SE).

Exception: If the only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner AND the taxpayer has filed Form 4361, Application for Exemption From Self-Employment Tax for Use by Ministers, Members of Religious Orders and Christian Science Practitioners, and has received IRS approval not to be taxed on these earnings, he or she does not have to file Schedule SE. Instead, write "Exempt—Form 4361" on Form 1040, line 55.

Most taxpayers will need to complete only Section A of Schedule SE, also known as the Short Schedule SE. Follow the chart on the form to determine whether the taxpayer qualifies to file the short form. Anyone who does not qualify and who must file the long form should be referred to a paid professional tax preparer.

If the taxpayer qualifies for the short form, enter the net profit from Schedule C-EZ, line 3, on lines 2 and 3 of the Schedule SE.

Follow the instructions on the form to determine net earnings from self-employment on line 4 and the self-employment tax on line 5.

Enter the amount from line 5 on Form 1040, line 55.

Deduction of Self-Employment Tax

Self-employed people may claim an adjustment to income of one-half of the social security and Medicare taxes they pay.

Enter the amount from Schedule SE, line 6, on Form 1040, line 28 as an adjustment to income.

SCHEDULE SE
(Form 1040)

Department of the Treasury
Internal Revenue Service

Self-Employment Tax

▶ **Attach to Form 1040.** ▶ **See Instructions for Schedule SE (Form 1040).**

OMB No. 1545-0074

2003

Attachment
Sequence No. **17**

Name of person with **self-employment** income (as shown on Form 1040)

Social security number of person
with **self-employment** income ▶

Who Must File Schedule SE

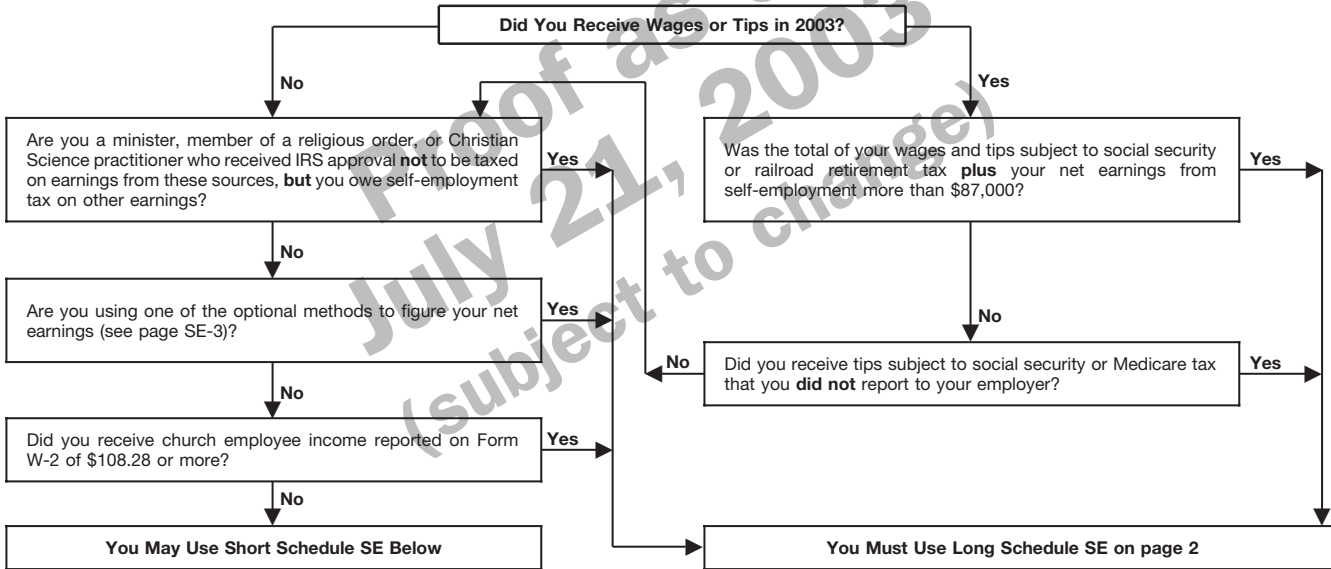
You must file Schedule SE if:

- You had net earnings from self-employment from **other than** church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of \$400 or more **or**
- You had church employee income of \$108.28 or more. Income from services you performed as a minister or a member of a religious order **is not** church employee income (see page SE-1).

Note. Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE (see page SE-3).

Exception. If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner **and** you filed Form 4361 and received IRS approval not to be taxed on those earnings, **do not** file Schedule SE. Instead, write "Exempt-Form 4361" on Form 1040, line 55.

May I Use Short Schedule SE or Must I Use Long Schedule SE?



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

1	Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a			
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report			
3	Combine lines 1 and 2			
4	Net earnings from self-employment. Multiply line 3 by 92.35% (.9235). If less than \$400, do not file this schedule; you do not owe self-employment tax ▶			
5	Self-employment tax. If the amount on line 4 is: • \$87,000 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 55. • More than \$87,000, multiply line 4 by 2.9% (.029). Then, add \$10,788.00 to the result. Enter the total here and on Form 1040, line 55.			
6	Deduction for one-half of self-employment tax. Multiply line 5 by 50% (.5). Enter the result here and on Form 1040, line 28			

CAPITAL GAINS AND LOSSES

Both the sale of stock and the sale of a home are reported on Form 1040, line 13a. The amount entered on Form 1040, line 13a, is transferred from Schedule D (Form 1040), *Capital Gains and Losses*. See Lessons 11 and 12 for more information about these types of sales.

SALE OF BUSINESS PROPERTY

The sale or involuntary conversion of business property is reported on Form 1040, line 14. If taxpayers are reporting the sale of business property, they should be referred to a paid professional tax preparer.

PENSION AND ANNUITY INCOME

Generally, payers of pension and annuity income send Form 1099-R to the recipients. The total pension or annuity income is reported on Form 1040A, line 12a, or Form 1040, line 16a; the taxable portion is reported on line 12b (1040A) or 16b (1040). If all of the pension or annuity is taxable, make an entry on line 12b or 16b only.

For more information on pension and annuity income, see Lesson 13, *Pensions*.

RENTS, ROYALTIES, PARTNERSHIPS, ESTATES, AND TRUSTS

Income from rental property, royalties, partnerships, estates, and/or trusts is reported on Form 1040, line 17. Refer any taxpayer who receives income from these sources to a paid professional tax preparer.

FARM INCOME

Farm income is reported on Form 1040, line 18. Advise taxpayers with farm income to see a paid professional tax preparer.

UNEMPLOYMENT COMPENSATION

Unemployment compensation includes benefits to unemployed individuals that a state or the District of Columbia paid from the Federal Unemployment Trust Fund. It is reported to the recipient on Form 1099-G, *Certain Government Payments*. All unemployment compensation is taxable. Transfer the amount in (See Exhibit 7) box 1 of Form 1099-G to line 3 of Form 1040EZ, line 13 of Form 1040A, or line 19 of Form 1040.

Supplemental benefits provided from an employer's fund to which the employee did not contribute are sometimes thought of as unemployment benefits also. They are reported to the employee on Form W-2. Include them on line 7 of Form 1040A or 1040, or on line 1 of Form 1040EZ.

POTENTIAL PITFALLS



Form 1099-R reports pension income, not earned income. Form 1099-R amounts are not included on line 7 of Form 1040. They are reported on Form 1040A, lines 12a and 12b or Form 1040, lines 16a and 16b. You will learn how to report pensions in Lesson 13, *Pensions*..

TaxWise Hints

- When entering income for the taxpayer you have the following three choices:

Go to Line 7 and click F9 ([Link](#)),

Click the right mouse and select “Link” or

Click on add form and select “W-2”.

- All the information entered into TaxWise should be exactly what is on the W-2.

Note: TaxWise automatically rounds numbers.

- When an entry is made for Alimony paid, TaxWise requires the Social Security Number of the spouse receiving the alimony.
- Form 4852, Substitute for Form W-2, Wage and Tax Statement or Form 1099-R, Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRA's, Insurance Contracts, etc. is available and can be completed in TaxWise.

▶▶ **SUMMING UP THIS LESSON** ◀◀

Form 1040EZ can be used to report only income from wages, salaries, tips, qualified tuition program earnings, Alaska Permanent Fund dividends, taxable scholarships and fellowship grants, interest of \$1500 or less, and unemployment compensation.

You can report several types of income on Form 1040A:

- ▶ Wages, salaries, tips, scholarships and fellowship grants, qualified tuition program payments, and Alaska Permanent Fund dividends
- ▶ Interest income
- ▶ Dividend income
- ▶ Capital gain distributions
- ▶ Unemployment compensation

Use Form 1040A, Schedule 1, or Form 1040, Schedule B, to report:

- ▶ Interest and/or dividend income over \$1500 and
- ▶ Interest from Series I and/or Series EE savings bonds, issued after 1989, that is excluded from taxable income.

Report any early withdrawal penalties on Form 1040, line 31, as an adjustment to income. Do not subtract penalties from interest income.

Report capital gain distributions directly on Form 1040, line 13a or Form 1040A, line 10, if the taxpayer is not required to file Schedule D.

State and local tax refunds are included in taxable income if:

- ▶ the taxpayer itemized deductions AND
- ▶ received a tax benefit by including the state and local tax in itemized deductions.

Alimony and separate maintenance payments are taxable income of the person receiving these payments. The person paying these payments can subtract them as an adjustment to income.

▶▶ **SUMMING UP THIS LESSON** ◀◀

(continued)

Business income or loss is generally beyond the scope of VITA or TCE. However, in some cases, trained volunteers may help self-employed taxpayers who qualify to use Schedule C-EZ.

Taxpayers with net self-employment income of \$400 or more must complete Schedule SE to compute self-employment tax.

Some nontaxable income is reported but is not included in taxable income:

- ▶ Tax-exempt interest
- ▶ Nontaxable portion of IRA distributions, including rollovers

Other income, such as prizes, awards, lottery winnings, and jury duty pay, is reported on line 21 of Form 1040, including the amount and description.

Volunteers should refer taxpayers with any of the following items to paid professional tax preparers:

- ▶ Sales of business property
- ▶ Income from rental property, royalties, partnerships, estates, or trusts
- ▶ Farm income

Exercise 1

1. Taxable
2. Taxable
3. Nontaxable
4. Nontaxable
5. Taxable
6. Taxable
7. Nontaxable
8. Taxable
9. Nontaxable
10. Nontaxable

Exercise 2

- (A) Mike will report \$29,250 on line 7. The tip income is included in the \$8,250.
- (B) No; John must file Form 1040 to pay social security and Medicare tax on his tip income.
- (C) Randy should be advised to contact the employer and request that a Form W-2 be issued or reissued. If after waiting a reasonable amount of time, it still has not been received, Randy should contact the IRS (but not before February 15th).

Exercise 3

- (A) 1. None
2. \$1,000
- (B) \$398 is reported on line 2 of Form 1040EZ.
- (C) \$495 is reported on line 8a of Form 1040.

STUDENT NOTES

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about adjustments to income. There are six adjustments covered in this lesson. They are educators expenses, traditional IRA deductions, student loan interest deduction, tuition and fees deduction, penalty on early withdrawal of savings, and alimony payments. Lesson 2 discusses an additional adjustment to income covered in the VITA/TCE training — one-half of self employment tax.

The remaining adjustments — moving expenses; self-employed health insurance deduction; and self-employed SEP, SIMPLE, and qualified plans — are not covered in traditional VITA/TCE training. Taxpayers who need assistance with these adjustments should be referred to a paid professional tax preparer.

After completing this lesson you should be able to:

- Calculate and accurately report adjustments to income.
- Identify which IRA contributions are within the scope of the VITA/TCE program.
- Identify contribution limits for IRAs.

ADJUSTMENTS TO INCOME

Adjustments are subtractions from total income. Total income minus adjustments results in **adjusted gross income (AGI)**, an important number for tax purposes. Adjusted gross income is used to figure some limitations. In addition, it is used to figure income tax in some states.

Taxpayers cannot take any adjustments to income on Form 1040EZ. On Form 1040EZ total income and adjusted gross income are the same. Form 1040A filers can take adjustments for educator expenses, contributions to a traditional IRA, the student loan interest deduction, and tuition and fees payments. Form 1040 filers can take any of the adjustments for which they are eligible.

DEDUCTION FOR EDUCATOR EXPENSES

If the taxpayer is an eligible educator, he or she can deduct as an adjustment to income up to \$250 in qualified expenses. The taxpayer can deduct these expenses even if he or she does not itemize deductions on Schedule A (Form 1040). This adjustment to income is for expenses paid or incurred in 2003. If both the taxpayer and spouse are eligible educators and choose to file a joint tax return, they may deduct up to \$500 (\$250 each) of qualified expenses. Prior to 2002 these expenses were deductible only as miscellaneous itemized deductions.

Eligible educator

The taxpayer is an eligible educator if, for the tax year, he or she is a kindergarten through grade 12 teacher, instructor, counselor, principal, or aide, and he or she works at least 900 hours during a school year in a school that provides elementary or secondary education as determined under state law.

Qualified expenses

Qualified expenses are the *unreimbursed expenses* paid or incurred for books, supplies, computer equipment (including related software and services), other equipment and supplementary materials that the taxpayer uses in his or her classroom. For courses in health and physical education, expenses for supplies are qualified expenses only if they are related to athletics.

To be deductible as an adjustment to income, the qualified expenses must be more than the following amounts for the tax year:

- The interest on qualified U.S. savings bonds that the taxpayer excluded from income because he or she paid qualified higher education expenses.
- Any distributions from a qualified tuition program that the taxpayer excluded from income, or
- Any tax-free withdrawals by the taxpayer from a Coverdell education savings account.

The educator expense can be claimed on Form 1040, line 23 or Form 1040A, line 16.

Example 1

Joe and Mary will file a joint return for 2003. Joe is a high school math teacher and incurred \$500 in qualified unreimbursed expenses. Mary is a grade school principal and incurred \$200 in qualified unreimbursed expenses. Both Joe and Mary meet the definition of eligible educators. They will claim \$450 (\$250 for Joe and \$200 for Mary) on Form 1040, line 23.

INDIVIDUAL RETIREMENT ARRANGEMENTS

An **Individual Retirement Arrangement (IRA)** is a tax-sheltered savings plan set up by the taxpayer, generally for retirement income. This lesson discusses only **traditional IRAs** (IRAs other than Roth IRAs, SIMPLE IRAs, or Coverdell education savings accounts (ESAs)). Contributions to the nontraditional IRAs are not deductible as adjustments to income.

Information on nontraditional IRAs can be found in Publication 590, *Individual Retirement Arrangements (IRAs)*.

Contributions to a traditional IRA can be either deductible or nondeductible. Earnings and gains on the contributions are not taxed until withdrawn from the traditional IRA account.

Example 2

Anna contributed a total of \$2,500 over the last two years to her traditional IRA account. During 2003 she earned \$140 of interest on her traditional IRA. All of the interest was added to her traditional IRA savings account.

Anna will not have to pay tax on the interest until she withdraws it from her traditional IRA account.

Contributions

Anyone under 70 1/2 years of age (at the end of the tax year) who has taxable compensation can contribute to a traditional IRA. If both the taxpayer and spouse have compensation and both are under age 70 1/2, each can set up an IRA. However, they cannot participate in the same IRA — they must have separate accounts.

Compensation includes wages, salaries, commissions, tips, bonuses, professional fees, and earnings from self-employment. Alimony or separate maintenance payments that are included in total income are also compensation for traditional IRA purposes. Compensation **does not include** interest, rents, dividends, pension and annuity income, deferred compensation received, or income you can exclude.

General Contribution Limits

The most that can be contributed for any year to a traditional IRA is the lesser of:

- \$3,000 (\$3,500 if age 50 or older), or
- Compensation that is includible in gross income for the year.

If a taxpayer has more than one traditional IRA, the taxpayer must combine all of the traditional IRAs and treat them as one when figuring the amount that can be contributed for the year.

Example 3

Dan, a college student, working part time earned \$1,500 in 2003. His IRA contributions for 2003 are limited to \$1,500 (the lesser of \$3,000 or compensation includible in income for the year).

Example 4

George has three traditional IRA accounts. During 2003 he contributed \$1,000 to each. His total IRA contributions for 2003 will be \$3,000.

ALERT

Deemed IRAs are new for tax year 2003.

Deemed IRAs

Beginning in 2003, employers who provide qualified employer retirement plans can maintain a separate account or annuity under the plan to receive voluntary employee contributions. This separate account is referred to as a deemed IRA. A deemed IRA can be a traditional IRA or a Roth IRA, and the same limits apply whether they are deemed or not. If a taxpayer has both a regular IRA and a deemed IRA, the taxpayer can divide contributions between them in any manner, but total contributions to both cannot exceed the \$3,000/\$3,500 limit.

Spousal IRA limit

If taxpayers file a joint return and one spouse's compensation is less than that of the other spouse's compensation, the most that can be contributed for that spouse is the lesser of:

- 1) \$3,000 (\$3,500 if age 50 or older), or
- 2) The total compensation includible in the gross income of both spouses for the year, reduced by:
 - a) IRA contributions for the spouse with the greater compensation,
 - b) Any contribution for the year to a Roth IRA for the spouse with the greater compensation.

The total combined contributions to both traditional IRAs cannot exceed the lesser of:

- \$6,000 (\$7,000 if both individuals are age 50 or older), or
- The total taxable compensation of both spouses.

Example 5

Kristen, a full time student with no taxable compensation, marries Jeremy during the year. Neither will be 50 by the end of the year. For the year, Jeremy has taxable compensation of \$30,000. He will contribute \$3,000 to a traditional IRA. If he and Kristen file a joint return, each can contribute \$3,000. This is because Kristen, who has no compensation, can add Jeremy's compensation, reduced by his IRA contribution ($\$30,000 - \$3,000 = \$27,000$) to her own compensation (0) to figure her maximum contribution. In her case, \$3,000 is her contribution limit, because \$3,000 is less than \$27,000 (her compensation for purposes of the figuring the spousal IRA).

Example 6

Tom and Darcy are married and both are 53. They both work and each has a traditional IRA. Tom earned \$1,800 and Darcy earned \$48,000 in 2003. Because of the spousal IRA limit rule, even though Tom earned less than \$3,500, they can contribute up to \$3,500 in each of their IRAs if they file a joint return. If they file separate returns, the amount that can be contributed to Tom's IRA is limited to \$1,800 (his taxable compensation).

Excess Contributions

Generally, an excess contribution is the amount contributed to a traditional IRA that is more than the lesser of the:

- 1) Taxable compensation for the year, or
- 2) \$3,000 (\$3,500 if age 50 or older).

This limit applies whether the contributions are deductible or nondeductible. Contributions made in the year the taxpayer reaches age 70 1/2 and any later year are also excess contributions.

In general, if the excess contribution for a year and any earnings on it are not withdrawn by the due date of the tax return (including extensions), the taxpayer is subject to an additional 6% tax. The additional 6% tax must be paid each year on the excess amounts that remain in the traditional IRA at the end of the tax year. The tax cannot be more than 6% of the value of the IRA as of the end of the tax year. The excise tax is figured on Form 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*.

A taxpayer who has taxable compensation, but can no longer contribute to a traditional IRA because of age (70 1/2 years or older) may continue to contribute to a spouse's traditional IRA until the year in which the spouse reaches 70 1/2.

Example 7

Eldridge is a 73-year-old attorney. He earned \$12,000 during the year.

Eldridge had compensation for traditional IRA purposes but he cannot make an IRA contribution because he is 70 1/2 or older. If Eldridge files a joint return with his spouse who is 68 years old, he can still contribute up to \$3,500 to his spouse's IRA.

Exercise 1

- A. Liz receives alimony which is included in her total income. All of her other income is from interest and dividends. Can Liz make a traditional IRA contribution? Explain. _____
- B. David is 73 and works part time in a hardware store. David's wife, Mary, does not work outside of the home. Mary is 68. Can David make a traditional IRA contribution for Mary? Explain _____
- C. Carla receives all her income from a rental property, interest income, and dividends. Can Carla make a traditional IRA contribution? Explain. _____
- D. Joy is 62 years old. Most of her income comes from a pension. However, Joy did earn \$1,250 doing consumer testing. How much can Joy contribute to a traditional IRA? Explain. _____

Deductible IRA Contributions

Generally, you can deduct the lesser of the contributions to your traditional IRA for the year or the general limit (or the spousal IRA limit, if it applies).

The actual deductible amount for a traditional IRA depends on the following:

- Whether or not the taxpayer or taxpayer's spouse is covered by a retirement plan set up by an employer for any part of the year,
- The taxpayer's **modified adjusted gross income**, and
- The taxpayer's filing status.

Modified Adjusted Gross Income

Generally, **modified adjusted gross income** is the adjusted gross income without consideration of certain deductions. The modified adjusted gross income (MAGI) can be figured as follows:

AGI (Form 1040 Line 34) plus

- IRA deduction
- Student loan interest deduction
- Tuition and fees deduction
- Foreign earned income exclusion
- Foreign housing exclusion or deduction
- Exclusion of qualified savings bond interest shown on Form 8815

- Exclusion of employer-paid adoption expenses shown on Form 8839.

Not covered by an employer retirement plan.

A taxpayer whose filing status is single, head of household, or qualifying widow(er), and who is not covered by an employer retirement plan, can take a full traditional IRA deduction of either his or her taxable compensation or \$3,000 (whichever amount is smaller). The \$3,000 amount is increased to \$3,500 if the taxpayer is age 50 or older.

Example 8

Cyril is single and 40 years of age. His modified adjusted gross income is \$50,000. He is not covered by a retirement plan at work. Cyril's traditional IRA contribution of \$3,000 is deductible.

Married taxpayers who file separate returns for a taxable year and who live apart at all times during the taxable year are treated as single and can take a full IRA deduction, if not covered by an employer plan. This is true even if the other spouse is covered by an employer retirement plan.

Married taxpayers who file jointly or separately may each be able to take the full IRA deduction of \$3,000 (\$3,500 if age 50 or older) or taxable compensation (whichever amount is smaller), if they had taxable compensation and both were not covered by an employer retirement plan. The total deduction for a joint return cannot exceed \$6,000 (\$7,000 if both individuals are age 50 or older). ***When determining the allowable deduction each spouse figures the deduction separately.***

Covered by an employer retirement plan.

If the taxpayer is covered by a retirement plan at work, the traditional IRA deduction will be reduced or eliminated, as shown in **Table 1**, depending on filing status and modified AGI.

NOTE: If Box 13, Retirement Plan, on Form W-2 is checked, the taxpayer is covered by an employer retirement plan. If taxpayers do not agree with the Form W-2 they must contact their employer. Volunteers cannot make a determination on whether or not a taxpayer is covered by an employer retirement plan. Refer taxpayers with questions on their employer retirement plans to their employer or Publication 590, Individual Retirement Arrangements (IRAs).

Table 1.
Traditional IRA Deduction Phaseout Chart
(If taxpayer is covered by an employer retirement plan)

Filing Status	Allowable traditional IRA deduction is...		
	reduced if modified AGI is:		zero when modified AGI is:
	at least	but less than	
Single or Head of household	\$40,000	\$50,000	\$50,000 or more
Married filing jointly or Qualifying widow(er)	\$60,000	\$70,000	\$70,000 or more
Married filing separately ¹	\$0.01	\$10,000	\$10,000 or more

¹If the taxpayer did not live with his or her spouse at any time during the year, his or her filing status is considered Single for this purpose.

ALERT 

For 2003, the MAGI limits increased for taxpayers covered by an employer retirement plan.

Example 9

Emily, 36 years old, is single. Her modified AGI was \$49,500. She is covered by a retirement plan at work. Emily's \$3,000 traditional IRA contribution will be reduced or modified on her tax return because her modified AGI is between \$40,000 and \$50,000.

If either the taxpayer or the taxpayer's spouse is covered by an employer retirement plan, he or she may be entitled to only a partial deduction or no deduction at all, depending on filing status and modified adjusted gross income, as shown in **Table 2**.

Table 2.
Traditional IRA Deduction Phaseout Chart
(If taxpayer is not covered, but the spouse is)


Filing Status	Allowable traditional IRA deduction is...		
	reduced if modified AGI is:		zero when modified AGI is:
	more than	but less than	
Married filing jointly or Qualifying widow(er)	\$150,000	\$160,000	\$160,000 or more
Married filing separately ¹	\$0.01	\$10,000	\$10,000 or more

¹The taxpayer is entitled to the full deduction if he or she did not live with their spouse at any time during the year.

Example 10

David and Ruth are filing a joint return. David earned \$72,000 and is covered by his employer’s retirement plan. Ruth, age 32, is a homemaker, and has no compensation. David, age 36, contributed \$2,800 to his traditional IRA and \$3,000 to a traditional IRA for Ruth.

Because David is covered by his employer’s retirement plan, the modified AGI limits apply (Table 1). Based on Table 1, David is not allowed a deduction for his traditional IRA contributions. Because David made traditional IRA contributions for Ruth, they can take a deduction on the tax return for her IRA contributions. Ruth is not covered by an employer’s retirement plan. Their compensation for IRA purposes is \$72,000 and their modified AGI is not more than \$150,000 (see Table 2).

POTENTIAL PITFALLS 

When determining the allowable deduction, each spouse figures the deduction separately.

Example 11

Assume still that David earned \$72,000 and is covered by his employer's retirement plan. Assume too that Ruth is employed; she earned \$66,000 and she is not covered by her employer's retirement plan. David cannot deduct his traditional IRA contribution, but Ruth can deduct hers. The modified AGI limits that apply to David are shown in Table 1. Table 2 modified AGI limits apply to Ruth's deduction. Her deduction would not be reduced unless the couple's modified AGI was more than \$150,000. It would not be eliminated unless their modified AGI was \$160,000 or more.

Exercise 2

- A.** Angela and Joe are married and file a joint return. Joe, age 23, is covered by a retirement plan at work, but Angela, age 25, is not. Joe earned \$25,000 and Angela earned \$20,000; their modified AGI is \$45,000. Is any portion of Angela's traditional IRA contribution deductible, and why? _____

- B.** Annette, age 26, is single. She earned \$23,000, and her modified AGI is \$24,500. She made a \$500 contribution to a traditional IRA. Annette is covered by a retirement plan at work. Is any portion of her contribution deductible, and why? _____

- C.** Richard and Lynn are married and lived together during the year. They file separate returns. Richard is covered by a retirement plan at work. Lynn is not covered by a retirement plan at work. Richard, age 40, earned \$17,000 and contributed \$1,400 to a traditional IRA. Lynn, age 33, worked part-time and earned \$4,500. She contributed \$1,000 to a traditional IRA. Can Richard or Lynn deduct any of the IRA contributions, and why? _____

When to Deduct Traditional IRS Contributions

Individuals may deduct traditional IRA contributions on their 2003 tax return if the contributions are made in 2003 or by April 15, 2004. Taxpayers may not deduct on their 2003 tax return contributions made in 2003 which were deducted on the 2002 tax return. The contributions do not have to be made before the return is filed. However, if the taxpayer deducts traditional IRA contributions on the 2003 tax return but does not make the traditional IRA contributions by April 15, 2004, for the exact amount deducted, the taxpayer must file an amended tax return.

Using the Worksheet and Reporting the Deduction

Use the IRA Deduction Worksheet in the Form 1040A or Form 1040 instructions booklet to figure the traditional IRA deduction.

The traditional IRA deduction is reported on Form 1040A, line 17 or Form 1040, line 24. On joint returns when both spouses are making deductible traditional IRA contributions, enter the total contribution.

Example 12

Nick and Susan file a joint return. Both work, and Nick, age 27, was covered by a retirement plan, but Susan, age 25, was not. Nick earned \$12,300 and Susan earned \$10,990. Their total income (Form 1040, line 22) is \$23,400. Nick and Susan each contributed \$500 to a traditional IRA.

The completed worksheet is shown in Exhibit 1. The information for Nick is shown in the column for *Your IRA*. The information for Susan is shown in the column for *Spouse's IRA*.

IRA Deduction Worksheet—Line 24

Keep for Your Records

Before you begin:

- ✓ Complete Form 1040, lines 27 through 32a, if they apply to you.
- ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
- ✓ Be sure you have read the list beginning on page 28.



		Your IRA	Spouse's IRA																
<p>1a. Were you covered by a retirement plan (see page 30)?</p> <p>1b. If married filing jointly, was your spouse covered by a retirement plan?</p> <p>Next. If you checked "No" on line 1a (and "No" on line 1b if married filing jointly), skip lines 2 through 6; enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7a (and 7b if applicable), and go to line 8. Otherwise, go to line 2.</p> <p>2. Enter the amount shown below that applies to you.</p> <ul style="list-style-type: none"> • Single, head of household, or married filing separately and you lived apart from your spouse for all of 2003, enter \$50,000 • Qualifying widow(er), enter \$70,000 • Married filing jointly, enter \$70,000 in both columns. But if you checked "No" on either line 1a or 1b, enter \$160,000 for the person who was not covered by a plan • Married filing separately and you lived with your spouse at any time in 2003, enter \$10,000 <p>3. Enter the amount from Form 1040, line 22</p> <p>4. Enter the total of the amounts from Form 1040, lines 23, 27 through 32a, plus any amount you entered on the dotted line next to line 33</p> <p>5. Subtract line 4 from line 3. Enter the result in both columns</p> <p>6. Is the amount on line 5 less than the amount on line 2?</p> <p><input type="checkbox"/> No. None of your IRA contributions are deductible. For details on nondeductible IRA contributions, see Form 8606.</p> <p><input checked="" type="checkbox"/> Yes. Subtract line 5 from line 2 in each column. If the result is \$10,000 or more, enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7 for that column and go to line 8. Otherwise, go to line 7.</p> <p>7. Multiply lines 6a and 6b by 30% (.30) (or by 35% (.35) in the column for the IRA of an individual who is age 50 or older at the end of 2003). If the result is not a multiple of \$10, increase it to the next multiple of \$10 (for example, increase \$490.30 to \$500). If the result is \$200 or more, enter the result. But if it is less than \$200, enter \$200</p> <p>8. Enter your wages, and your spouse's if filing jointly, and other earned income from Form 1040, minus any deductions on Form 1040, lines 28 and 30. Do not reduce wages by any loss from self-employment.</p>	<p>1a. <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>1b. <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; border-bottom: 1px solid black; text-align: center;">2a. 70,000</td> <td style="width: 50%; border-bottom: 1px solid black; text-align: center;">2b. 160,000</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">3. 23,400</td> <td style="border-bottom: 1px solid black; text-align: center;">3. 23,400</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">4. 0</td> <td style="border-bottom: 1px solid black; text-align: center;">4. 0</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">5a. 23,400</td> <td style="border-bottom: 1px solid black; text-align: center;">5b. 23,400</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">6a. 46,600</td> <td style="border-bottom: 1px solid black; text-align: center;">6b. 136,600</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">7a. 3,000</td> <td style="border-bottom: 1px solid black; text-align: center;">7b. 3,000</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">8. 23,400</td> <td style="border-bottom: 1px solid black; text-align: center;">8. 23,400</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">9a. 500</td> <td style="border-bottom: 1px solid black; text-align: center;">9b. 500</td> </tr> <tr> <td style="border-bottom: 1px solid black; text-align: center;">10a. 500</td> <td style="border-bottom: 1px solid black; text-align: center;">10b. 500</td> </tr> </table>	2a. 70,000	2b. 160,000	3. 23,400	3. 23,400	4. 0	4. 0	5a. 23,400	5b. 23,400	6a. 46,600	6b. 136,600	7a. 3,000	7b. 3,000	8. 23,400	8. 23,400	9a. 500	9b. 500	10a. 500	10b. 500
2a. 70,000	2b. 160,000																		
3. 23,400	3. 23,400																		
4. 0	4. 0																		
5a. 23,400	5b. 23,400																		
6a. 46,600	6b. 136,600																		
7a. 3,000	7b. 3,000																		
8. 23,400	8. 23,400																		
9a. 500	9b. 500																		
10a. 500	10b. 500																		



If married filing jointly and line 8 is less than \$6,000 (\$6,500 if one spouse is age 50 or older at the end of 2003; \$7,000 if both spouses are age 50 or older at the end of 2003), **stop here** and see Pub. 590 to figure your IRA deduction.

Nondeductible IRA Contributions

Although the deductible amount of traditional IRA contributions can be reduced or eliminated because of the modified adjusted gross income limitation, a taxpayer can make nondeductible contributions to new or existing traditional IRAs. Earnings and gains on these contributions are not taxed until they are distributed to the taxpayer.

The total traditional IRA contribution, whether deductible or nondeductible, cannot be more than the taxpayer's taxable compensation or \$3,000 (\$3,500 if age 50 or older), whichever amount is smaller.

Taxpayers must complete Form 8606, *Nondeductible IRAs*, for each year that nondeductible contributions are made.

If taxpayers do not report nondeductible contributions, all of the contributions to a traditional IRA will be treated as deductible. This means all distributions will be taxed unless the taxpayer can show, with satisfactory evidence, that nondeductible contributions were made.

Example 13

Rachel, age 35, is single and wants to contribute the maximum amount possible to her traditional IRA. She is covered by her employer's retirement plan and her total income, Form 1040A Line 15, is \$41,000. Her total basis in traditional IRAs from line 14 of her 2002 Form 8606 is \$10,000. The completed IRA Deduction Worksheet and Form 8606 are shown in Exhibits 2 and 3.

IRA Deduction Worksheet—Line 24

Keep for Your Records

- Before you begin:**
- ✓ Complete Form 1040, lines 27 through 32a, if they apply to you.
 - ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
 - ✓ Be sure you have read the list beginning on page 28.



		Your IRA	Spouse's IRA
<p>1a. Were you covered by a retirement plan (see page 30)?</p> <p>1b. If married filing jointly, was your spouse covered by a retirement plan?</p> <p>Next. If you checked "No" on line 1a (and "No" on line 1b if married filing jointly), skip lines 2 through 6; enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7a (and 7b if applicable), and go to line 8. Otherwise, go to line 2.</p> <p>2. Enter the amount shown below that applies to you.</p> <ul style="list-style-type: none"> • Single, head of household, or married filing separately and you lived apart from your spouse for all of 2003, enter \$50,000 • Qualifying widow(er), enter \$70,000 • Married filing jointly, enter \$70,000 in both columns. But if you checked "No" on either line 1a or 1b, enter \$160,000 for the person who was not covered by a plan • Married filing separately and you lived with your spouse at any time in 2003, enter \$10,000 <p>3. Enter the amount from Form 1040, line 22</p> <p>4. Enter the total of the amounts from Form 1040, lines 23, 27 through 32a, plus any amount you entered on the dotted line next to line 33</p> <p>5. Subtract line 4 from line 3. Enter the result in both columns</p> <p>6. Is the amount on line 5 less than the amount on line 2?</p> <p><input type="checkbox"/> No. None of your IRA contributions are deductible. For details on nondeductible IRA contributions, see Form 8606.</p> <p><input type="checkbox"/> Yes. Subtract line 5 from line 2 in each column. If the result is \$10,000 or more, enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7 for that column and go to line 8. Otherwise, go to line 7.</p> <p>7. Multiply lines 6a and 6b by 30% (.30) (or by 35% (.35) in the column for the IRA of an individual who is age 50 or older at the end of 2003). If the result is not a multiple of \$10, increase it to the next multiple of \$10 (for example, increase \$490.30 to \$500). If the result is \$200 or more, enter the result. But if it is less than \$200, enter \$200</p> <p>8. Enter your wages, and your spouse's if filing jointly, and other earned income from Form 1040, minus any deductions on Form 1040, lines 28 and 30. Do not reduce wages by any loss from self-employment.</p>	<p>1a. <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>1b. <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>2a. 50,000</p> <p>2b.</p> <p>3. 41,000</p> <p>4. 0</p> <p>5a. 41,000</p> <p>5b.</p> <p>6a. 9,000</p> <p>6b.</p> <p>7a. 2,700</p> <p>7b.</p> <p>8. 41,000</p>		
<p> CAUTION If married filing jointly and line 8 is less than \$6,000 (\$6,500 if one spouse is age 50 or older at the end of 2003; \$7,000 if both spouses are age 50 or older at the end of 2003), stop here and see Pub. 590 to figure your IRA deduction.</p>			
<p>9. Enter traditional IRA contributions made, or that will be made by April 15, 2004, for 2003 to your IRA on line 9a and to your spouse's IRA on line 9b</p> <p>10. On line 10a, enter the smallest of line 7a, 8, or 9a. On line 10b, enter the smallest of line 7b, 8, or 9b. This is the most you can deduct. Add the amounts on lines 10a and 10b and enter the total on Form 1040, line 24. Or, if you want, you may deduct a smaller amount and treat the rest as a nondeductible contribution (see Form 8606)</p>	<p>9a. 3,000</p> <p>9b.</p> <p>10a. 2,700</p> <p>10b.</p>		

<p>Form 8606</p> <p>Department of the Treasury Internal Revenue Service</p>	<p>Nondeductible IRAs</p> <p>▶ See separate instructions.</p> <p>▶ Attach to Form 1040, Form 1040A, or Form 1040NR.</p>	<p>OMB No. 1545-1007</p> <p style="font-size: 2em; font-weight: bold;">2003</p> <p>Attachment Sequence No. 48</p>
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Name. If married, file a separate form for each spouse required to file Form 8606. See page 5 of the instructions.

Rachel Green

Your social security number
000 00 6220

<p>Fill in Your Address Only if You Are Filing This Form by Itself and Not With Your Tax Return</p>	<p>Home address (number and street, or P.O. box if mail is not delivered to your home)</p>	<p>Apt. no.</p>
<p>City, town or post office, state, and ZIP code</p>		

Part I Nondeductible Contributions to Traditional IRAs and Distributions From Traditional, SEP, and SIMPLE IRAs

Complete this part only if:

- You made nondeductible contributions to a traditional IRA for 2003,
- You took distributions from a traditional, SEP, or SIMPLE IRA in 2003 (other than a rollover, conversion, recharacterization, or return of certain contributions) **and** you made nondeductible contributions to a traditional IRA in 2003 or an earlier year, **or**
- You converted part, but not all, of your traditional, SEP, and SIMPLE IRAs to Roth IRAs in 2003 (excluding any portion you recharacterized) **and** you made nondeductible contributions to a traditional IRA in 2003 or an earlier year.

<p>1 Enter your nondeductible contributions to traditional IRAs for 2003, including those made for 2003 from January 1, 2004, through April 15, 2004 (see page 5 of the instructions)</p>	1	300					
<p>2 Enter your total basis in traditional IRAs (see page 6 of the instructions)</p>	2	10,000					
<p>3 Add lines 1 and 2</p>	3	10,300					
<table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width:35%; padding: 5px;"> <p>In 2003, did you take a distribution from traditional, SEP, or SIMPLE IRAs or make a Roth IRA conversion?</p> </td> <td style="width:10%; padding: 5px;"> <p>No —————▶ Enter the amount from line 3 on line 14. Do not complete the rest of Part I.</p> </td> </tr> <tr> <td style="padding: 5px;"> <p>—————▶ Yes —————▶ Go to line 4.</p> </td> <td></td> </tr> </table>	<p>In 2003, did you take a distribution from traditional, SEP, or SIMPLE IRAs or make a Roth IRA conversion?</p>	<p>No —————▶ Enter the amount from line 3 on line 14. Do not complete the rest of Part I.</p>	<p>—————▶ Yes —————▶ Go to line 4.</p>				
<p>In 2003, did you take a distribution from traditional, SEP, or SIMPLE IRAs or make a Roth IRA conversion?</p>	<p>No —————▶ Enter the amount from line 3 on line 14. Do not complete the rest of Part I.</p>						
<p>—————▶ Yes —————▶ Go to line 4.</p>							
<p>4 Enter those contributions included on line 1 that were made from January 1, 2004, through April 15, 2004</p>	4						
<p>5 Subtract line 4 from line 3</p>	5						
<p>6 Enter the value of all your traditional, SEP, and SIMPLE IRAs as of December 31, 2003, plus any outstanding rollovers (see page 6 of the instructions)</p>	6						
<p>7 Enter your distributions from traditional, SEP, and SIMPLE IRAs in 2003. Do not include rollovers, conversions to a Roth IRA, certain returned contributions, or recharacterizations of traditional IRA contributions (see page 6 of the instructions)</p>	7						
<p>8 Enter the net amount you converted from traditional, SEP, and SIMPLE IRAs to Roth IRAs in 2003. Do not include amounts converted that you later recharacterized (see page 7 of the instructions). Also enter this amount on line 16</p>	8						
<p>9 Add lines 6, 7, and 8</p>	9						
<p>10 Divide line 5 by line 9. Enter the result as a decimal rounded to at least 3 places. If the result is 1.000 or more, enter "1.000"</p>	10	×					
<p>11 Multiply line 8 by line 10. This is the nontaxable portion of the amount you converted to Roth IRAs. Also enter this amount on line 17</p>	11						
<p>12 Multiply line 7 by line 10. This is the nontaxable portion of your distributions that you did not convert to a Roth IRA</p>	12						
<p>13 Add lines 11 and 12. This is the nontaxable portion of all your distributions</p>	13						
<p>14 Subtract line 13 from line 3. This is your total basis in traditional IRAs for 2003 and earlier years</p>	14	10,300					
<p>15 Taxable amount. Subtract line 12 from line 7. Also include this amount on Form 1040, line 15b; Form 1040A, line 11b; or Form 1040NR, line 16b</p>	15						

Note: You may be subject to an additional 10% tax on the amount on line 15 if you were under age 59½ at the time of the distribution (see page 7 of the instructions).

Exercise 3

Bill and Kathy are both employed and each earned \$15,000 in 2003. Both Bill and Kathy are age 32. Bill was covered by an employer retirement plan but Kathy was not. In July 2003, Bill contributed \$1,200 to his 2003 traditional IRA. In February 2004, he contributed \$800 to his 2003 traditional IRA. Kathy contributed \$400 to her 2003 traditional IRA. They file a joint return. Their total income on line 22 is \$30,000. They have no other adjustments to income.

Complete their IRA deduction worksheet (Exhibit 4).

Additional Taxes and Penalties

Taxpayers are generally subject to additional taxes and penalties for:

- Contributing more to a traditional IRA than is allowed,
- Making traditional IRA withdrawals before age 59 1/2, and
- Not withdrawing enough traditional IRA funds after age 70 1/2.
- Investing in collectibles
- Prohibited transactions, such as borrowing money from one's own IRA or selling property to it.

There are penalties for overstating the amount of nondeductible contributions and for failure to file Form 8606, if required.

Credit for Qualified Retirement Savings Contribution

Refer to Lesson 5 to determine if a taxpayer is also eligible to receive the credit for qualified retirement savings contributions based on their contributions to an IRA.

IRA Deduction Worksheet—Line 24

Keep for Your Records

Before you begin:

- ✓ Complete Form 1040, lines 27 through 32a, if they apply to you.
- ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
- ✓ Be sure you have read the list beginning on page 28.



	Your IRA	Spouse's IRA
1a. Were you covered by a retirement plan (see page 30)?	1a. <input type="checkbox"/> Yes <input type="checkbox"/> No	
1b. If married filing jointly, was your spouse covered by a retirement plan?		1b. <input type="checkbox"/> Yes <input type="checkbox"/> No
<p>Next. If you checked "No" on line 1a (and "No" on line 1b if married filing jointly), skip lines 2 through 6; enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7a (and 7b if applicable), and go to line 8. Otherwise, go to line 2.</p>		
2. Enter the amount shown below that applies to you.		
<ul style="list-style-type: none"> • Single, head of household, or married filing separately and you lived apart from your spouse for all of 2003, enter \$50,000 • Qualifying widow(er), enter \$70,000 • Married filing jointly, enter \$70,000 in both columns. But if you checked "No" on either line 1a or 1b, enter \$160,000 for the person who was not covered by a plan • Married filing separately and you lived with your spouse at any time in 2003, enter \$10,000 	2a. _____	2b. _____
3. Enter the amount from Form 1040, line 22.	3. _____	
4. Enter the total of the amounts from Form 1040, lines 23, 27 through 32a, plus any amount you entered on the dotted line next to line 33	4. _____	
5. Subtract line 4 from line 3. Enter the result in both columns	5a. _____	5b. _____
6. Is the amount on line 5 less than the amount on line 2?		
<input type="checkbox"/> No. None of your IRA contributions are deductible. For details on nondeductible IRA contributions, see Form 8606.		
<input type="checkbox"/> Yes. Subtract line 5 from line 2 in each column. If the result is \$10,000 or more, enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7 for that column and go to line 8. Otherwise, go to line 7	6a. _____	6b. _____
7. Multiply lines 6a and 6b by 30% (.30) (or by 35% (.35) in the column for the IRA of an individual who is age 50 or older at the end of 2003). If the result is not a multiple of \$10, increase it to the next multiple of \$10 (for example, increase \$490.30 to \$500). If the result is \$200 or more, enter the result. But if it is less than \$200, enter \$200	7a. _____	7b. _____
8. Enter your wages, and your spouse's if filing jointly, and other earned income from Form 1040, minus any deductions on Form 1040, lines 28 and 30. Do not reduce wages by any loss from self-employment	8. _____	
<div style="border: 1px solid black; padding: 5px; margin: 5px 0;"> <p>If married filing jointly and line 8 is less than \$6,000 (\$6,500 if one spouse is age 50 or older at the end of 2003; \$7,000 if both spouses are age 50 or older at the end of 2003), stop here and see Pub. 590 to figure your IRA deduction.</p> </div>		
9. Enter traditional IRA contributions made, or that will be made by April 15, 2004, for 2003 to your IRA on line 9a and to your spouse's IRA on line 9b	9a. _____	9b. _____
10. On line 10a, enter the smallest of line 7a, 8, or 9a. On line 10b, enter the smallest of line 7b, 8, or 9b. This is the most you can deduct. Add the amounts on lines 10a and 10b and enter the total on Form 1040, line 24. Or, if you want, you may deduct a smaller amount and treat the rest as a nondeductible contribution (see Form 8606)	10a. _____	10b. _____

If a taxpayer paid interest on a student loan in 2003, he or she may be able to deduct up to \$2,500 of the interest paid.

If the taxpayer paid \$600 or more in interest to a single lender, the taxpayer should receive a statement from the lender showing the amount of interest paid. This information will assist you in completing the student loan interest deduction.

Qualified Student Loan Interest

Generally, student loan interest is the interest paid during the year on a loan for qualified higher education expenses that were:

1. For the taxpayer, the taxpayer's spouse, or a person who was the taxpayer's dependent when the loan was obtained.
2. Paid within a reasonable period of time before or after obtaining the loan, and
3. For an eligible student.

Interest can be the interest paid during the life of the loan (voluntary and required interest payments), loan origination fees, capitalized interest, interest on revolving lines of credit, and interest on refinanced student loans.

Interest does not include interest on any of the following:

1. A loan from a related person.
2. A loan from a qualified employer plan.
3. A loan for which the taxpayer is not legally liable.

Who Can Claim the Deduction

Generally, a taxpayer can claim the deduction if all the following requirements are met:

1. Taxpayer cannot use married filing separately filing status.
2. Taxpayer cannot be claimed as a dependent on someone else's return.
3. The interest is on a loan to pay tuition and other qualified higher education expenses for the taxpayer, the taxpayer's spouse, or someone whom the taxpayer can claim as a dependent, when the loan was taken out.
4. The education expenses were paid or incurred within a reasonable period of time before or after the loan was taken out.
5. The person for whom the expenses were paid or incurred was an eligible student.

Qualified Higher Education Expenses

Generally, qualified higher education expenses include tuition and fees; room and board; books, supplies and equipment; and other necessary expenses.

These costs must be reduced by the following:

1. Employer provided educational assistance benefits.
2. Tax-free withdrawals from a Coverdell ESA.
3. Tax-free withdrawals from a qualified tuition program.
4. U.S. savings bond interest excluded from income because it is used to pay qualified higher education expenses.
5. Certain scholarships.
6. Veteran's educational assistance benefits.
7. Any other nontaxable payments (other than gifts, bequests, or inheritances) received for educational expenses.

Eligible educational institution

An eligible educational institution is any college, university, vocational school or other postsecondary educational institution eligible to participate in a student aid program administered by the Department of Education. It includes virtually all accredited public, nonprofit, and privately owned profit-making postsecondary institutions.

For the student loan interest deduction only, an eligible educational institution also includes an institution conducting an internship or residency program leading to a degree or certificate from an institution of higher education, hospital, or health care facility that offers postgraduate training.

If a taxpayer does not know if the educational institution is an eligible institution, the taxpayer should contact the school.

Eligible student

An eligible student is a student who is enrolled at least half-time in a program leading to a degree, certificate, or other recognized educational credential.

The standard for what is half the normal full-time work load is determined by each eligible educational institution.

Deduction Limits

The student loan interest deduction is generally the smaller of \$2,500 or the interest payments paid in 2003.

This amount may be gradually reduced (phased out) or eliminated based on the taxpayer's filing status and modified adjusted gross income (MAGI). Table 3 depicts when the limits apply.

Table 3

Limit on Student Loan Interest Deduction		
If your filing status is	AND your modified AGI is	THEN...
Single, head of household, or qualifying widow(er)	\$50,000 or less	You can deduct all your interest, up to \$2,500
	More than \$50,000, but less than \$65,000	Your deduction is limited
	\$65,000 or more	You cannot claim this deduction.
Married filing jointly	\$100,000 or less	You can deduct all your interest up to \$2,500
	More than \$100,000, but less than \$130,000	Your deduction is limited
	\$130,000 or more	You cannot claim this deduction.

Figuring the Deduction

Use the Student Loan Interest Deduction worksheet found in the Form 1040 or Form 1040A instructions to figure the deduction.

Claiming the Deduction

The student loan interest deduction is entered on Form 1040, line 25, or Form 1040A, line 18.

Example 14

During 2003, Rick paid \$2,650 in qualified interest on his student loan. His total income, Form 1040, line 22, is \$35,000. He has no other adjustments to his income. His completed student loan interest deduction worksheet, Exhibit 5, shows Rick is entitled to \$2,500. Although his MAGI falls within the income limits, he is only entitled to a maximum \$2,500 deduction.

Student Loan Interest Deduction Worksheet—Line 25

Keep for Your Records

- Before you begin:**
- ✓ Complete Form 1040, lines 27 through 32a, if they apply to you.
 - ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32).
 - ✓ See the instructions for line 25 that begin on this page.
 - ✓ Be sure you have read the **Exception** above to see if you can use this worksheet instead of Pub. 970 to figure your deduction.



<p>1. Enter the total interest you paid in 2003 on qualified student loans (defined above). Do not enter more than \$2,500</p>		1. <u>2,500</u>
<p>2. Enter the amount from Form 1040, line 22</p>	2. <u>35,000</u>	
<p>3. Enter the total of the amounts from Form 1040, lines 23, 24, 27 through 32a, plus any amount you entered on the dotted line next to line 33</p>	3. <u>0</u>	
<p>4. Subtract line 3 from line 2</p>	4. <u>35,000</u>	
<p>5. Enter the amount shown below for your filing status.</p> <ul style="list-style-type: none"> • Single, head of household, or qualifying widow(er)—\$50,000 • Married filing jointly—\$100,000 	5. <u>50,000</u>	
<p>6. Is the amount on line 4 more than the amount on line 5?</p> <p><input type="checkbox"/> No. Skip lines 6 and 7, enter -0- on line 8, and go to line 9.</p> <p><input type="checkbox"/> Yes. Subtract line 5 from line 4</p>	6. _____	
<p>7. Divide line 6 by \$15,000 (\$30,000 if married filing jointly). Enter the result as a decimal (rounded to at least three places). If the result is 1.000 or more, enter 1.000</p>	7. <u>.0</u>	
<p>8. Multiply line 1 by line 7</p>	8. <u>0</u>	
<p>9. Student loan interest deduction. Subtract line 8 from line 1. Enter the result here and on Form 1040, line 25. Do not include this amount in figuring any other deduction on your return (such as on Schedule A, C, E, etc.)</p>	9. <u>2,500</u>	

Taxpayers can deduct an amount equal to the qualified tuition and related expenses paid during the tax year as an adjustment to income. The adjustment is reported on Form 1040, line 26, or Form 1040A, line 19.

To claim the deduction the taxpayer must have incurred ***qualified expenses*** for an ***eligible student*** to attend an ***eligible educational institution*** during the tax year. In addition, the taxpayer must include on the tax return the name and taxpayer identification number of the qualified student.

Qualified Expenses

Qualified tuition and related expenses include tuition and fees required for enrollment or attendance at an eligible educational institution and generally include fees for:

- Course-related books, supplies and equipment, and

The fees must be paid to the institution as a condition of enrollment or attendance.

Qualified tuition and related expenses do not include the cost of:

- Insurance,
- Medical expenses (including student health fees),
- Room and board,
- Student activities.
- Transportation or similar personal, living or family expenses, even if the fees must be paid to the institution as a condition of enrollment or attendance.
- Athletic fees.
- Other expenses unrelated to an individual's academic course of instruction.

Eligible Student

The deduction can be claimed for the taxpayer, the taxpayer's spouse (if filing a joint return) and any dependent (for whom the taxpayer claims a dependency exemption).

Married taxpayers that file as married filing separately cannot take the deduction.

An individual who is the dependent of another taxpayer cannot claim the deduction.

Eligible Educational Institution

An eligible educational institution is generally any accredited public, nonprofit, or private postsecondary institution eligible to participate in the student aid programs administered by the

Department of Education. It includes virtually all accredited, public, nonprofit, and privately owned profit-making post secondary institutions.

If the taxpayer does not know if the educational institution is an eligible institution, he or she should contact the school.

Deduction Amount

The deduction amount is determined by the taxpayer's filing status and adjusted gross income. Table 4 depicts when the income limitations apply.

The total amount of qualified tuition and related expenses are reduced by:

- Distributions from qualified state tuition programs
- Distributions from Coverdell ESAs
- Interest from savings bonds used for higher education expenses

Table 4 Limit on Tuition and Fees Deduction

IF your filing status is...	AND your modified AGI is...	THEN...
Single, Head of Household, or Qualifying widow(er)	Equal to or less than \$65,000	You can deduct all of your qualified tuition and fees up to \$3,000.
	More than \$65,000	You cannot claim the credit
Married filing jointly	Equal to or less than \$130,000	You can deduct all of your qualified tuition and fees up to \$3,000
	More than \$130,000	You cannot claim the credit.
Married filing separately	Any amount	You cannot claim the credit.

Modified adjusted gross income for purposes of the deduction for qualified tuition and related fees is adjusted gross income before the deduction for qualified tuition and related fees and after adding back the following:

- Foreign earned income exclusion,
- Foreign housing exclusion or deduction,
- Exclusion of income for bona fide residents of Guam, Puerto Rico, American Samoa, or the Northern Mariana Islands.

Figuring the Deduction



Use the Tuition and Fees Deduction worksheet found in the Form 1040 or Form 1040A instructions to figure the modified adjusted gross income and the resulting deduction amount.

Example 15

Luis and Priscilla file a joint return for 2003. Their 1040 line 22 total income is \$49,620. In 2003, Priscilla paid \$1,300 for classes taken at the local university. She had allowable IRA deductions of \$1,500. Their allowable tuition and fees deduction is \$1,300, shown in Exhibit 6.

Exhibit 6

Luis and Priscilla's Tuition and Fees Deduction Worksheet

Tuition and Fees Deduction Worksheet—Line 26		<i>Keep for Your Records</i>
Before you begin:		
✓	Complete Form 1040, lines 27 through 32a, if they apply to you.	
✓	Figure any amount to be entered on the dotted line next to line 33 (see page 32).	
✓	See the instructions for line 26 above.	
✓	Be sure you have read the Exception above to see if you can use this worksheet instead of Pub. 970 to figure your deduction.	
1.	Enter amount from Form 1040, line 22	1. 49,620
2.	Enter the total of the amounts from Form 1040, lines 23 through 25, 27 through 32a, plus any amount you entered on the dotted line next to line 33	2. 1,500
3.	Subtract line 2 from line 1. If the result is more than \$65,000 (\$130,000 if married filing jointly),  You cannot take the deduction for tuition and fees	3. 48,120
4.	Tuition and fees deduction. Enter the total qualified tuition and fees (defined above) you paid in 2003. Do not enter more than \$3,000. Also, enter this amount on Form 1040, line 26. Do not include this amount in figuring any other deduction on your return (such as on Schedule A, C, E, etc.)	4. 1,300

No Double Benefits

A taxpayer cannot:

- Deduct qualified tuition and related expenses if the same expense is deductible on a different line of the return.
- Claim the Hope credit or the lifetime learning credit for an individual in the same year as a deduction for qualified tuition and related expenses are claimed.
- Claim a credit based on expenses paid with a tax-free scholarship, grant, or an employer-provided educational assistance.

ONE-HALF OF SELF-EMPLOYMENT TAX

Report on Form 1040, line 28, the adjustment for one-half of self-employment tax from Schedule SE. This subject was covered in Lesson 2, for volunteers who will be helping self-employed taxpayers.

PENALTY ON EARLY WITHDRAWAL OF SAVINGS

Depositors may withdraw funds from ordinary savings accounts any time they wish. However, if they withdraw funds from a time deposit (such as a certificate of deposit) before the maturity date, a penalty is charged. Form 1099-INT reports the interest earned as well as any early withdrawal penalties.

As you learned in Lesson 2, taxpayers must report the total amount of interest earned. They cannot subtract the early withdrawal penalty from the interest earned and report the difference. The early withdrawal penalty can be claimed as an adjustment only on Form 1040, line 31. The entire penalty is deducted, even if it is greater than the interest income.

Example 16

Arlene has one Form W-2 and one Form 1099-INT and no other income. Her Form 1099-INT shows both interest income and an early withdrawal penalty. Arlene does not pay alimony, and she did not make a contribution to a traditional IRA. She will not itemize deductions, and she cannot claim any tax credits. Normally, she would be able to file Form 1040A.

However, Arlene must file Form 1040 to claim the adjustment for the penalty on early withdrawal of savings.

ALIMONY PAID

As you learned in Lesson 2, alimony and separate maintenance payments are taxable to the person receiving these payments. The person paying the alimony or separate maintenance can claim it as an adjustment to income. This adjustment can be claimed only on Form 1040. The amount paid during the year and the recipient's social security number are entered on line 32a and 32b, respectively. Claim the adjustment only for amounts paid during the tax year.

Child support is not the same as alimony or separate maintenance payments. Child support is not taxable to the recipient and cannot be claimed as an adjustment by the payer.

JURY DUTY PAY GIVEN TO EMPLOYER

As you learned in Lesson 2, *Income*, jury duty pay received by taxpayers is included in other income on line 21 of Form 1040.

Some employees receive their regular wages from their employers when they are serving on a jury instead of working at their jobs. Often the jury duty pay the employees receive is turned over to their employers. The amount given to the employer may be claimed as an adjustment to income. On the dotted line next to line 33, write "jury pay" and the amount. Include jury duty pay with the adjustments claimed on lines 23 through 32a.

OTHER ADJUSTMENTS

The other adjustments that can be claimed on Form 1040 are beyond the scope of the VITA/TCE Program. Taxpayers who have adjustments that aren't discussed in this lesson should be advised to seek paid professional tax assistance.

TOTAL ADJUSTMENTS AND ADJUSTED GROSS INCOME

Add all adjustments and enter the total on Form 1040A, line 20, or Form 1040, line 33. Subtract the total adjustments from total income on Form 1040A, line 15, or Form 1040, line 22. Enter the result on Form 1040A, line 21, or Form 1040, line 34. This is **adjusted gross income** and is often referred to as "**AGI**." Adjusted gross income is used to compute some limitations, such as the medical and dental deduction on Schedule A and the credit for child and dependent care expenses.

TAXWISE HINTS

TaxWise will quickly complete any worksheets needed to determine adjustments to income.

There is one worksheet for educator expenses, student loan interest deduction, and tuition and fees deduction. You can link to this form from Form 1040, lines 23, 25, or 26.

Link to the Deductible and Non-deductible IRA Worksheet from Form 1040, line 24. Once the IRA contribution is input for the taxpayer (and spouse if married), TaxWise will complete the Form 8606, if necessary, and input the entry on Form 1040, line 24.

One half the self employment tax will be entered automatically when completing Schedule C or C-EZ.

The penalty on withdrawal from savings should be entered by linking to the Interest Received Worksheet. This worksheet is a link from Schedule B.

TaxWise breaks out the remaining adjustments. Simply input the appropriate amount.

▶▶ SUMMING UP THIS LESSON ◀◀

- An adjustment is an amount subtracted from total income. The result is adjusted gross income.
- Adjustments covered in the VITA program are:
 - ▶ Educator expenses
 - ▶ Contributions to a traditional IRA
 - ▶ Student loan interest deduction
 - ▶ Tuition and fees paid
 - ▶ One-half of self-employment tax paid (volunteers trained to prepare Schedule C-EZ and SE can assist taxpayers claiming this adjustment)
 - ▶ Penalty on early withdrawal of savings
 - ▶ Alimony paid
 - ▶ Jury duty pay given to employer
- The adjustments for traditional IRA contributions, student loan interest deduction, tuition and fees deduction, and educator expenses deduction can be claimed either on Form 1040A or Form 1040. The other adjustments can be claimed on Form 1040 only.
- Persons 70 1/2 years of age or older by the end of the tax year cannot make traditional IRA contributions for that tax year.
- Traditional IRA contributions generally cannot be more than the taxpayer's taxable compensation or \$3,000 (\$3,500 if age 50 or older), whichever amount is smaller.
- Individuals who are not covered by retirement plans at work may make deductible IRA contributions regardless of their modified adjusted gross income. Taxpayers who are covered by retirement plans at work may deduct all, part, or none of their traditional IRA contributions depending on their modified adjusted gross income and filing status.
- Taxpayers may be subject to additional tax for contributing more to a traditional IRA than is allowed, making traditional IRA withdrawals before age 59 1/2, and not withdrawing enough traditional IRA funds after 70 1/2.

Exercise 1

- (A) Yes; alimony is considered compensation for traditional IRA purposes.
- (B) Yes; But only if they file a joint return.
- (C) No; Carla has no compensation for traditional IRA purposes.
- (D) \$1,250; The lessor of taxable compensation or \$13,500.

Exercise 2

- (A) Yes; all of her contribution up to \$3,000 is deductible because their combined modified adjusted gross income is not more than \$150,000.
- (B) Yes; all of it is deductible because her modified adjusted gross income is less than \$40,000.
- (C) Richard may not deduct any of his contribution because his modified adjusted gross income is at least \$10,000. Lynn will be able to deduct a portion of her IRA contribution because she is not covered by an employer-sponsored retirement plan and her income is less than \$10,000.

Exercise 3

Bill and Kathy's IRA Deductions Worksheet

IRA Deduction Worksheet—Line 24

Keep for Your Records

- Before you begin:**
- ✓ Complete Form 1040, lines 27 through 32a, if they apply to you.
 - ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
 - ✓ Be sure you have read the list beginning on page 28.



	Your IRA	Spouse's IRA
1a. Were you covered by a retirement plan (see page 30)?	1a. <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	
1b. If married filing jointly, was your spouse covered by a retirement plan?		1b. <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
<p>Next. If you checked "No" on line 1a (and "No" on line 1b if married filing jointly), skip lines 2 through 6; enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7a (and 7b if applicable), and go to line 8. Otherwise, go to line 2.</p>		
2. Enter the amount shown below that applies to you.		
<ul style="list-style-type: none"> • Single, head of household, or married filing separately and you lived apart from your spouse for all of 2003, enter \$50,000 • Qualifying widow(er), enter \$70,000 • Married filing jointly, enter \$70,000 in both columns. But if you checked "No" on either line 1a or 1b, enter \$160,000 for the person who was not covered by a plan • Married filing separately and you lived with your spouse at any time in 2003, enter \$10,000 	2a. <u>70,000</u>	2b. <u>160,000</u>
3. Enter the amount from Form 1040, line 22.	3. <u>30,000</u>	
4. Enter the total of the amounts from Form 1040, lines 23, 27 through 32a, plus any amount you entered on the dotted line next to line 33.	4. <u>0</u>	
5. Subtract line 4 from line 3. Enter the result in both columns.	5a. <u>30,000</u>	5b. <u>30,000</u>
6. Is the amount on line 5 less than the amount on line 2?		
<input type="checkbox"/> No. None of your IRA contributions are deductible. For details on nondeductible IRA contributions, see Form 8606.		
<input type="checkbox"/> Yes. Subtract line 5 from line 2 in each column. If the result is \$10,000 or more, enter \$3,000 (\$3,500 if age 50 or older at the end of 2003) on line 7 for that column and go to line 8. Otherwise, go to line 7.	6a. <u>40,000</u>	6b. <u>130,000</u>
7. Multiply lines 6a and 6b by 30% (.30) (or by 35% (.35) in the column for the IRA of an individual who is age 50 or older at the end of 2003). If the result is not a multiple of \$10, increase it to the next multiple of \$10 (for example, increase \$490.30 to \$500). If the result is \$200 or more, enter the result. But if it is less than \$200, enter \$200.	7a. <u>3,000</u>	7b. <u>3,000</u>
8. Enter your wages, and your spouse's if filing jointly, and other earned income from Form 1040, minus any deductions on Form 1040, lines 28 and 30. Do not reduce wages by any loss from self-employment.	8. <u>30,000</u>	
<div style="border: 1px solid black; padding: 5px; display: inline-block;"> <p>If married filing jointly and line 8 is less than \$6,000 (\$6,500 if one spouse is age 50 or older at the end of 2003; \$7,000 if both spouses are age 50 or older at the end of 2003), stop here and see Pub. 590 to figure your IRA deduction.</p> </div>		
9. Enter traditional IRA contributions made, or that will be made by April 15, 2004, for 2003 to your IRA on line 9a and to your spouse's IRA on line 9b.	9a. <u>2,000</u>	9b. <u>400</u>
10. On line 10a, enter the smallest of line 7a, 8, or 9a. On line 10b, enter the smallest of line 7b, 8, or 9b. This is the most you can deduct. Add the amounts on lines 10a and 10b and enter the total on Form 1040, line 24. Or, if you want, you may deduct a smaller amount and treat the rest as a nondeductible contribution (see Form 8606).	10a. <u>2,000</u>	10b. <u>400</u>

STUDENT NOTES

Lined writing area for student notes.

STANDARD AND ITEMIZED DEDUCTIONS, AND TAX COMPUTATION

Lesson 4

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about the standard deduction, itemized deductions and tax computations. You will learn which expenses can be included in itemized deductions. You will also learn when the taxpayer will use the tax tables and the Capital Gains Worksheet to compute their total tax.

After completing this lesson you should be able to:

- Identify the correct standard deduction.
- Calculate and accurately report itemized deductions on Schedule A.
- Identify the miscellaneous deductions reported on Schedule A, line 27.
- Review the Capital Gain Tax Worksheet.
- Explain the process to calculate and report tax liability.

STANDARD DEDUCTION

The **standard deduction** depends on:

- the taxpayer's filing status,
- whether the taxpayer (or the taxpayer's spouse) is 65 or older and/or blind, and
- whether the taxpayer can be claimed as a dependent on another taxpayer's return.

Based on the taxpayer's situation, you will figure the standard deduction by using one of the following:

- Standard deduction amount for the appropriate filing status from the appropriate tax form,
- *Standard Deduction Chart for People Age 65 or Older or Blind*, or
- *Standard Deduction Worksheet for Dependents*.

ALERT



In 2003, the basic standard deduction for married taxpayers filing jointly and qualifying widow(er)s has increased to \$9,500 (double that of single filers).

The standard deduction for married filing separately has increased to \$4,750 (one half of that for married filing jointly).

Example 1

Bob is 55 years old and is married to Janice, age 50. If they are filing a joint return and neither is blind, they can enter \$9,500 on either Form 1040 or Form 1040A for their standard deduction amount.

Example 2

John is 73 years old, blind, and files a single tax return. To find his standard deduction, use the *Standard Deduction Chart for People Age 65 or Older or Blind*. His standard deduction is \$7,050.

PERSONAL EXEMPTION IN CONNECTION WITH STANDARD DEDUCTION ON FORM 1040EZ

If the taxpayer (or his or her spouse, if married filing a joint return) can be claimed as a dependent on another taxpayer's return, check the *Yes* box on line 5 of the Form 1040EZ. To fill in the amount on line 5 for this taxpayer, you must then turn the form over and complete the worksheet (Exhibit 1 shows a blank worksheet from Form 1040EZ, page 2).

If the taxpayer (or his or her spouse, if filing a joint return) cannot be claimed as a dependent on another taxpayer's return, check the *No* box on line 5. Enter on line 5 the amount shown below that applies to the taxpayer (and spouse, if married filing jointly).

A. Single, enter \$7,800. This is the total of the taxpayer's standard deduction (\$4,750) and personal exemption (\$3,050).

Exhibit 1

Form 1040EZ, Page 2

Worksheet for dependents who checked "Yes" on line 5

(keep a copy for your records)

Use this worksheet to figure the amount to enter on line 5 if someone can claim you (or your spouse if married filing jointly) as a dependent, even if that person chooses not to do so. To find out if someone can claim you as a dependent, use TeleTax topic 354 (see page 8).

- A. Amount, if any, from line 1 on front _____
+ 250.00 Enter total ► **A.** _____
- B. Minimum standard deduction _____ **B.** 750.00
- C. Enter the **larger** of line A or line B here _____ **C.** _____
- D. Maximum standard deduction. If **single**, enter \$4,750; if **married filing jointly**, enter \$9,500 _____ **D.** _____
- E. Enter the **smaller** of line C or line D here. This is your standard deduction _____ **E.** _____
- F. Exemption amount.
 - If single, enter -0-.
 - If married filing jointly and—
 - both you and your spouse can be claimed as dependents, enter -0-.
 - only one of you can be claimed as a dependent, enter \$3,050.} **F.** _____
- G. Add lines E and F. Enter the total here and on line 5 on the front _____ **G.** _____

If you checked "No" on line 5 because no one can claim you (or your spouse if married filing jointly) as a dependent, enter on line 5 the amount shown below that applies to you.

- Single, enter \$7,800. This is the total of your standard deduction (\$4,750) and your exemption (\$3,050).
- Married filing jointly, enter \$15,600. This is the total of your standard deduction (\$9,500), your exemption (\$3,050), and your spouse's exemption (\$3,050).

- B.** Married, enter \$15,600. This is the total of the taxpayer's and spouse's standard deduction (\$9,500), exemption for the taxpayer (\$3,050), and exemption for the taxpayer's spouse (\$3,050).

POTENTIAL PITFALLS



Entering an incorrect standard deduction amount is a frequently made error on tax returns. Take care to report the correct standard deduction amount.

Exercise 1

- A.** James is 37 years old. He has two children who live with him and he files as head of household. What is James' standard deduction? _____
- B.** Malcom is 37 years old. He was divorced in 2003. He is blind and has no dependent children. What is Malcom's standard deduction? _____
- C.** Carl is 67 years old and married to Sue, who is 59 years old. Neither is blind. If they file a joint return, what is their standard deduction? _____
- D.** If they are filing separate returns, what is Carl's standard deduction? _____
- E.** If they are filing separate returns, what is Sue's standard deduction? _____
- F.** Shirley is 15 years old and is claimed as a dependent on her parents' tax return. She earned \$1,500 during the summer and deposited it all into her savings account, where she earned \$40 in interest. What is her standard deduction? _____

ITEMIZED DEDUCTIONS

Taxpayers can either claim the standard deduction or itemize their deductions. Both the standard deduction and itemized deductions reduce adjusted gross income. Most taxpayers choose the larger of their itemized deductions or the standard deduction. However, there are some exceptions:

- A married taxpayer filing a separate return cannot claim the standard deduction if the taxpayer's spouse itemizes deductions, and
- Nonresident aliens cannot claim the standard deduction.

When itemizing, you should complete the taxpayer's return through line 36 of Form 1040. Then figure itemized deductions on Schedule A.

POTENTIAL PITFALLS



Explain to taxpayers that they can only deduct expenses in the year they are paid. They cannot deduct expenses that are owed but not paid.

ALERT



The standard mileage rate for operating a vehicle for medical transportation is 12 cents a mile.

Medical and Dental Expenses

Claim medical and dental expenses paid in 2003 on lines 1 through 4 of Schedule A. Include expenses incurred for:

- the taxpayer and spouse,
- dependents claimed on the return, and
- others who could have been claimed as dependents except that they had gross income of \$3,050 or more, or they filed a joint return.

If a child of divorced or separated parents is claimed as a dependent on either parent's return, each parent may deduct the medical expenses that he or she pays for the child.

Deductible expenses include:

- Prescription medicines and drugs (including insulin)
- Medical, dental, and nursing care, including amounts paid for unreimbursed qualified long-term care services
- Medical and hospital insurance premiums, including amounts paid for eligible long-term care (subject to certain limitations based on the insured person's age — see Exhibit 2, next page.)
- Prescription eyeglasses, hearing aids, crutches, wheelchairs, braces, and guide dogs
- Transportation for medical care at 12 cents a mile, or actual out-of-pocket expenses, plus parking fees and tolls
- Certain lodging expenses
- Certain home improvements made for medical care purposes or to make the home suitable for a disabled person
- Medicare A premiums for persons not enrolled in Social Security
- Medicare B
- Certain weight-loss programs to treat disease diagnosed by a physician, including obesity
- Unreimbursed costs of smoking-cessation programs, including the cost of prescription drugs designed to alleviate nicotine withdrawal
- Expenses for admission and transportation to a medical conference relating to the chronic disease of a dependent (if the costs are primarily for and essential to the medical care of the dependent).

Total medical and dental expenses must exceed 7.5 percent of a taxpayer's adjusted gross income (Form 1040, line 35) for Schedule A deduction.

Nondeductible expenses include:

- Medical expenses paid from a medical savings account (MSA).
[Refer taxpayers with MSAs to Publication 969, *Medical Savings Accounts (MSAs)*, Publication 502, *Medical and Dental Expenses*, and a paid professional tax preparer.]
- Payroll tax paid for Medicare A
- Life insurance policy premiums
- Babysitting, child care, and nursing care for a healthy baby
- Illegal drugs
- Nonprescription drugs or medicines
- The cost of purchasing diet food items
- Nonprescription nicotine gum and patches designed to stop smoking
- Funeral, burial, or cremation costs
- Unnecessary cosmetic surgery (surgery that does not correct a congenital abnormality or an abnormality caused by injury or disease)
- Income protection policies, including nursing home policy premiums, if the policy ensures a maximum out-of-pocket expense per day
- Meals and lodging while attending a medical conference relating to the chronic disease of a dependent.

Eligible Long-Term Care Premiums

Exhibit 2

IF the person was, at the end of 2003, age . . .	THEN the most you may deduct is . . .
40 or under	\$250
41-50	\$470
51-60	\$940
61-70	\$2,510
71 or older	\$3,130

These figures should always be checked against the figures in the instructions for the Form 1040, Schedule A.

Exercise 2

Sam and Paula Ferris file a joint return. Sam's social security number is 000-00-8612. Their adjusted gross income is \$40,000. They paid the following medical bills:

Unreimbursed doctor's bills	\$ 500
Unreimbursed orthodontist bill for braces	1,200
Hospital insurance premiums	300
Life insurance premiums	500
Unreimbursed prescription medicines	100
Vitamins	70
Hospital bill (before deducting \$1,000) reimbursed by insurance company)	2,000
Smoking cessation program	150

Complete the *Medical and Dental Expenses* section of Schedule A for the Ferris family.

Exhibit 3

Schedule A

SCHEDULES A&B (Form 1040) <small>Department of the Treasury Internal Revenue Service</small>	Schedule A—Itemized Deductions (Schedule B is on back) ▶ Attach to Form 1040. ▶ See Instructions for Schedules A and B (Form 1040).	<small>OMB No. 1545-0074</small> <div style="font-size: 2em; font-weight: bold;">2003</div> <small>Attachment Sequence No. 07</small>																								
Name(s) shown on Form 1040		Your social security number																								
Medical and Dental Expenses	Caution. Do not include expenses reimbursed or paid by others. 1 Medical and dental expenses (see page A-2) 2 Enter amount from Form 1040, line 35 2 3 Multiply line 2 by 7.5% (.075) 4 Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 15%; border: 1px solid black; background-color: #cccccc;">1</td> <td style="width: 15%; border: 1px solid black;"> </td> <td style="width: 15%; border: 1px solid black;"> </td> <td style="width: 15%; border: 1px solid black;"> </td> <td style="width: 15%; border: 1px solid black;"> </td> <td style="width: 15%; border: 1px solid black;"> </td> </tr> <tr> <td style="border: 1px solid black; background-color: #cccccc;">2</td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> </tr> <tr> <td style="border: 1px solid black; background-color: #cccccc;">3</td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> </tr> <tr> <td style="border: 1px solid black; background-color: #cccccc;">4</td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> <td style="border: 1px solid black;"> </td> </tr> </table>	1						2						3						4					
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Taxes

To be deductible, a tax must be imposed on and paid by the taxpayer. Taxpayers **cannot** deduct:

- a tax that they do not owe, but pay for someone else,
- a tax that they owe, but someone else pays, or
- a tax that was not paid in 2003.

Report deductible taxes on lines 5 through 9 of Schedule A.

State, Local, and Foreign Income Taxes — Taxpayers can deduct income taxes paid to a state or local government or to a foreign government or tax any of its subdivisions. These taxes include tax withheld, estimated tax payments, and taxes paid in 2003 for an earlier year.

Real Estate Taxes — State, local, or foreign taxes on real property, such as the taxpayer's house or land, are deductible. Real estate taxes are deductible when paid. If the taxes are paid with a mortgage payment and held in escrow, do not deduct the taxes until they are paid by the bank or mortgage lender.

Assessments to pave a street or install lighting or a sewer generally are not deductible.

Personal Property Tax — Taxes that state and local governments charge on the value of personal property are deductible. A portion of the cost of personal vehicle registration may fall in this category.

Nondeductible Taxes — Many federal, state, and local government taxes are not deductible. The following taxes are not deductible:

- General sales tax
- Federal taxes—income tax, social security (FICA), Medicare, railroad retirement tax, gift tax, and excise taxes or customs duties
- Hunting licenses and dog licenses
- Water and sewer taxes
- Taxes on alcoholic beverages, cigarettes, and tobacco
- State, local, and federal taxes on gasoline, diesel, and other motor fuels used in a nonbusiness vehicle
- Utility taxes — telephone, gas, electricity, etc.

Interest

Interest is the amount that is paid in order to borrow money. Only taxpayers who are legally liable for the debt can deduct the interest in the year it is paid or accrued. Interest expenses are reported on lines 10 through 14 of Schedule A.

Home Mortgage Interest — The amount of mortgage interest that a taxpayer can deduct depends on the:

- date of the loan,
- amount of the loan, and
- use of the proceeds of the loan.

If the mortgage debt was incurred on or before October 13, 1987, and was secured by a main or second home, the interest on that debt is fully deductible, regardless of the amount of the loan or the use of the loan proceeds.

If the mortgage debt was incurred after October 13, 1987, and was secured by a main or second home, the interest is fully deductible if:

- the loans plus any grandfathered debt do not exceed \$1 million (\$500,000 if married filing separate returns), and
- the proceeds were used to buy, build, or improve the home or homes.

SPECIAL POPULATIONS



Members of the clergy and military personnel can deduct real estate taxes even if they receive a housing allowance that is excluded from income. Also, they can deduct allowable mortgage interest even if the interest was paid from a nontaxable housing allowance.

In addition to loans used to buy, build, or improve a main or second home, taxpayers can deduct interest on other loans secured by a main or second home, regardless of the use of the proceeds, if:

- the total of these loans does not exceed \$100,000 (\$50,000 if married filing separate returns), and
- the total amount of the secured debt is not more than the home's fair market value minus any outstanding acquisition debt and any grandfathered debt on the home.

Points. Certain charges paid by a borrower and/or a seller to a lender to secure a loan are called points. They are also called loan origination fees (including VA and FHA loan origination fees), maximum loan charges, premium charges, loan discount, or discount points.

Points paid only for the use of money are considered prepaid interest. This interest, even if it qualifies as home mortgage interest, must be spread over the life of the mortgage and is considered paid and deductible over that period unless it meets the following exception.

Exception. A taxpayer may fully deduct points in the year he or she pays them only if all of the following conditions apply.

- The taxpayer itemizes deductions.
- The taxpayer's loan is secured by his or her main home. (The main home is the one the taxpayer lives in most of the time.)
- Paying points is an established business practice in the area where the loan was made.
- The points paid were not more than the points generally charged in that area.
- The taxpayer uses the cash method of accounting. (The cash method means that the taxpayer reports income in the year received and deducts expenses in the year paid.)
- The points were not paid in place of amounts that ordinarily are stated separately on the settlement statement, such as appraisal fees, inspection fees, title fees, attorney fees, and property taxes.
- The taxpayer uses his or her loan to buy or build his or her main home.
- The points were computed as a percentage of the principal amount of the mortgage.
- The amount is clearly shown on the settlement statement (such as Form HUD-1) as points charged for the mortgage.
- The points may be shown as paid from either the taxpayer's or the seller's funds.

- The funds the taxpayer provided at or before closing, plus any points the seller paid, were at least as much as the points charged. The funds the taxpayer provided do not have to have been applied to the points. They can include a down payment, an escrow deposit, earnest money, and other funds the taxpayer paid at or before closing for any purpose. The taxpayer cannot have borrowed these funds from his or her lender or mortgage broker.

Charges by the lender for specific services, such as appraisal fees, preparation costs, VA funding fees, or notary fees, may be called points. However, these charges are not considered interest and are not deductible.

Points paid by the seller are deductible as interest by the buyer.

Points paid to refinance a mortgage are generally not deductible in full in the year the taxpayer paid them (unless they are paid in connection with the improvement of a main home and the first seven statements, discussed earlier under Exception, are true).

Points paid in excess of those generally charged in the area and points paid to refinance a mortgage can be deducted over the life of the mortgage. Deduct points reported to the taxpayer on Form 1098 on line 10 of Schedule A (Form 1040). Deduct points not reported to the taxpayer on Form 1098 on line 12 of Schedule A (Form 1040).

Investment Interest. Interest that is paid on money borrowed to buy or carry property held for investment is called **investment interest**. Taxpayers with investment interest expense that exceeds investment income (interest and ordinary dividend income) should see a paid professional tax preparer.

Interest that cannot be deducted. Interest that cannot be deducted includes:

- Interest on car loans where the car is used for personal use and other personal loans,
- Credit investigation fees,
- Loan fees; aid for services necessary to get a loan,
- Interest on a debt the taxpayer is not legally liable to pay, and
- Finance charges on credit card purchases of personal items.

POTENTIAL PITFALLS



Personal interest cannot be claimed as an itemized deduction. Personal interest includes interest on car loans, credit card balances, and installment plan loans that are incurred for personal use or for personal expenses.

Exercise 3

John and Shannon file a joint return. During the year, they paid the bank \$2,180 of interest on their home mortgage that was reported to them on Form 1098 (all qualified), \$400 in credit card interest, \$300 on installment loan, and \$2,000 on a car loan. Complete the *Interest You Paid* section of Schedule A for John and Shannon.

Exhibit 4

Schedule A

Interest You Paid (See page A-3.) Note. Personal interest is not deductible.	10	Home mortgage interest and points reported to you on Form 1098	10				
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ▶					

	12	Points not reported to you on Form 1098. See page A-3 for special rules	12				
	13	Investment interest. Attach Form 4952 if required. (See page A-3.)	13				
	14	Add lines 10 through 13				14	

Contributions

Taxpayers can deduct contributions to organizations that are:

- Organized and operated exclusively for religious, charitable, educational, scientific, or literary purposes,
- Organizations that work to prevent cruelty to children or animals, and
- Organizations that foster national or international amateur sports competition if they do not provide athletic facilities or equipment.

To be deductible, contributions must be made to an organization, not an individual. *Qualifying organizations* include:

- Churches, synagogues, temples, mosques, Salvation Army, Red Cross, CARE, United Way, Boy Scouts, Girl Scouts, World Wildlife Fund, etc.,
- Fraternal orders (if used for the purposes listed above),
- Nonprofit schools and hospitals,
- Nonprofit medical research organizations,
- Veterans' groups and certain cultural groups, and
- Federal, state, and local governments (if the gifts are exclusively for public purposes).

Nonqualifying organizations include:

- Business organizations, such as the Chamber of Commerce,
- Civic leagues and associations,

- Political organizations and candidates,
- Social clubs,
- Foreign organizations,
- Homeowners' associations, and
- Communist organizations.

Deductible items include:

- Money gifts,
- Dues, fees, and assessments paid to qualified organizations above the value of the benefits received (not country clubs or other social organizations),
- Fair market value of used clothing, furniture,
- Cost and upkeep of uniforms that have no general use but must be worn while performing donated services,
- Unreimbursed transportation expenses that relate directly to the services the taxpayer gave the qualified organization, including bus fare, parking fees, tolls, and either the actual cost of gas and oil or a standard mileage charge of 14 cents per mile, and
- The part of a contribution above the fair market value for items such as merchandise and tickets to charity balls or sporting events.

Nondeductible items include:

- Cost of raffle, bingo, or lottery tickets,
- Tuition,
- Value of a person's time or service,
- Blood donated to a blood bank or the Red Cross,
- Car depreciation, insurance, general repairs, or maintenance,
- Direct contributions to an individual,
- Sickness or burial expenses for members of a fraternal society, and
- The part of a contribution that personally benefits the taxpayer (such as the fair market value of the meal eaten at a charity dinner).

Report cash and check contributions on Schedule A, line 15.

Contributions other than cash or check are entered on line 16.

Taxpayers with noncash contributions exceeding \$500 should see a paid professional tax preparer.

The taxpayer must keep records to prove the amount of the cash and noncash contributions he or she makes during the year.

**POTENTIAL
PITFALLS**



If the taxpayer makes a contribution to a qualifying organization that is more than \$75 and is partly for goods or services, the qualifying organization must give the taxpayer a written statement. For more information, see Publication 526, *Charitable Contributions*.

A taxpayer can claim a deduction for any single contribution of \$250 or more **only** if he or she has a written acknowledgment of the contribution from the qualifying organization. You do not have to see the written acknowledgement, but you should ask the taxpayer if they have one.

Exercise 4

Rose contributed \$600 to St. Martin’s Church (church gave letter verifying amount). \$32 to the Girl Scouts, and \$40 to a family whose house burned. She purchased \$50 worth of lottery tickets and spent \$100 playing bingo at her church. She donated used furniture with a fair market value of \$200 to Goodwill.

Complete the *Gifts to Charity* section of Schedule A for Rose.

Exhibit 5

Schedule A

Gifts to Charity	15	Gifts by cash or check. If you made any gift of \$250 or more, see page A-4	15			18	
	16	Other than by cash or check. If any gift of \$250 or more, see page A-4. You must attach Form 8283 if over \$500	16			18	
	17	Carryover from prior year	17			18	
	18	Add lines 15 through 17				18	

Casualty and Theft Losses

A casualty occurs when property is damaged as a result of a sudden, unexpected, or unusual event such as fire, storm, shipwreck, flood, earthquake, or automobile accident. Theft is the unlawful taking and removing of money or property with the intent to deprive the owner of it. Theft does not include the mere disappearance of money or property.

A casualty or theft may result in a gain if the insurance proceeds or other reimbursements exceed the adjusted basis of destroyed or stolen property.

Usually, however, a casualty or theft results in a loss. Part of a casualty or theft loss may be deductible if the taxpayer can prove that the casualty or theft occurred to property that the taxpayer owned. The taxpayer must also prove the dollar amount of the loss.

Miscellaneous Itemized Deductions

Certain employee expenses, expenses of producing income, and other qualifying expenses are reported as miscellaneous itemized deductions on Schedule A. Miscellaneous itemized deductions that exceed 2% of adjusted gross income are deductible. There are some miscellaneous itemized deductions that are deductible, regardless of a taxpayer’s adjusted gross income.

Examples of deductions that are subject to the 2% limit and that are reported on lines 20 through 26 of Schedule A are:

- Union dues and fees,
- Professional society dues,
- Uniforms not adaptable to general use,
- Small tools and supplies,
- Professional books, magazines, journals,
- Employment-related educational expenses,
- Expenses of looking for a new job,
- Investment counsel fees,
- Investment expenses,
- Tax counsel and assistance,
- Fees paid to an IRA custodian, and
- Safe deposit box rental for investment documents.
- Unrecovered after-tax pension contributions (see Lesson 13).

Examples of deductions that are not subject to the 2% limit and that are reported on line 27 of Schedule A are:

- Gambling losses to the extent of gambling winnings, and
- Work-related expenses for an individual with a disability, such as attendant-care services at the individual's place of work, that are necessary for the person to work.

Nondeductible expenses include:

- Burial or funeral expenses,
- Wedding expenses,
- Fees and licenses, such as car and marriage licenses and dog tags,
- Fines and penalties, such as parking tickets,
- Home repairs, insurance, and rent,
- Illegal bribes and kickbacks,
- Insurance premiums (except medical insurance premiums),
- Losses from the sale of a taxpayer's home, furniture, or personal car,
- Lost or misplaced cash or property,
- Personal legal expenses, and
- Commuting expenses to and from work.

Exercise 5

Robert is a janitor. His adjusted gross income is \$20,000. He wants to deduct the following items on his tax return:

2003 income tax preparation fee	\$ 100
Safe deposit box rental (used to keep bonds)	75
Life insurance premiums	300
Investment expenses	70
Loss on sale of personal home	800
Investment journals and newsletters	250
Investment advisory fees	200
Attorney fees for preparation of will	100

Complete Robert's Schedule A, line 20 through 26.

Exhibit 6

Schedule A

Job Expenses and Most Other Miscellaneous Deductions (See page A-5 for expenses to deduct here.)	20	Unreimbursed employee expenses—job travel, union dues, job education, etc. You must attach Form 2106 or 2106-EZ if required. (See page A-5.) ▶					
		20					
	21	Tax preparation fees	21				
	22	Other expenses—investment, safe deposit box, etc. List type and amount ▶	22				
	23	Add lines 20 through 22	23				
	24	Enter amount from Form 1040, line 35 | 24 |	24				
	25	Multiply line 24 by 2% (.02)	25				
26	Subtract line 25 from line 23. If line 25 is more than line 23, enter -0-	26					

TOTAL ITEMIZED DEDUCTIONS

Schedule A, line 28, is *Total Itemized Deductions*. It is the sum of lines 4, 9, 14, 18, 19, 26, and 27.

Compare the amount on line 28 to the standard deduction, and enter the larger of the two on Form 1040, line 38.

Exercise 6

Seth A. and Karen Yale's adjusted gross income is \$28,000. Seth's social security number is 000-00-1039. They gave you a list of their itemized deductions. They received no insurance reimbursement for medical expenses. They purchased their home in 1989, and a commercial mortgage company holds the mortgage. They have not refinanced the mortgage or increased the principal balance since they bought their home. They are both under age 65 and not blind. Neither can be claimed as a dependent by another taxpayer.

Unreimbursed medical expenses:

Medical insurance premiums	\$480
Hospital	600
Doctors and dentists	820
Vitamins	75
Prescription drugs	300
Insulin	120

Taxes:

State income tax	\$1,200
Federal income tax	2,400
Real estate tax	780

Interest:

Interest on mortgage (reported on Form 1098)	\$4,500
Car loan	900
Credit cards	102

Contributions:

Church (gave Yales' letter verifying this amount)	\$850
Bingo costs	60
American Cancer Society	130
Canned goods donated to a food drive	15
Fair market value of donated used clothing	60

Miscellaneous:

Union dues	\$90
IRA custodial fee	10
Traffic fine	70
Investment expenses	20

Complete Seth and Karen's Schedule A.

SCHEDULES A&B
(Form 1040)

Schedule A—Itemized Deductions

OMB No. 1545-0074

2003

Attachment
Sequence No. **07**

Department of the Treasury
Internal Revenue Service

(Schedule B is on back)

▶ **Attach to Form 1040.** ▶ See Instructions for Schedules A and B (Form 1040).

Name(s) shown on Form 1040

Your social security number

Medical and Dental Expenses

Caution. Do not include expenses reimbursed or paid by others.

- 1** Medical and dental expenses (see page A-2)
- 2** Enter amount from Form 1040, line 35 | **2** |
- 3** Multiply line 2 by 7.5% (.075)
- 4** Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-

Taxes You Paid

(See page A-2.)

- 5** State and local income taxes
- 6** Real estate taxes (see page A-2)
- 7** Personal property taxes
- 8** Other taxes. List type and amount ▶
- 9** Add lines 5 through 8

Interest You Paid

(See page A-3.)

- 10** Home mortgage interest and points reported to you on Form 1098
- 11** Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ▶

Note. Personal interest is not deductible.

- 12** Points not reported to you on Form 1098. See page A-3 for special rules
- 13** Investment interest. Attach Form 4952 if required. (See page A-3.)
- 14** Add lines 10 through 13

Gifts to Charity

If you made a gift and got a benefit for it, see page A-4.

- 15** Gifts by cash or check. If you made any gift of \$250 or more, see page A-4
- 16** Other than by cash or check. If any gift of \$250 or more, see page A-4. You **must** attach Form 8283 if over \$500
- 17** Carryover from prior year
- 18** Add lines 15 through 17

Casualty and Theft Losses

- 19** Casualty or theft loss(es). Attach Form 4684. (See page A-5.)

Job Expenses and Most Other Miscellaneous Deductions

(See page A-5 for expenses to deduct here.)

- 20** Unreimbursed employee expenses—job travel, union dues, job education, etc. You **must** attach Form 2106 or 2106-EZ if required. (See page A-5.) ▶
- 21** Tax preparation fees
- 22** Other expenses—investment, safe deposit box, etc. List type and amount ▶
- 23** Add lines 20 through 22
- 24** Enter amount from Form 1040, line 35 | **24** |
- 25** Multiply line 24 by 2% (.02)
- 26** Subtract line 25 from line 23. If line 25 is more than line 23, enter -0-

Other Miscellaneous Deductions

- 27** Other—from list on page A-6. List type and amount ▶

Total Itemized Deductions

- 28** Is Form 1040, line 35, over \$139,500 (over \$69,750 if married filing separately)?
 - No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 27. Also, enter this amount on Form 1040, line 37. } ▶
 - Yes.** Your deduction may be limited. See page A-6 for the amount to enter. }

TAXABLE INCOME COMPUTATION

Once you have determined the standard deduction, compare it to the total itemized deductions. In most cases, you will enter the larger of the two amounts on Form 1040, line 37. Subtract line 37 from line 35 and enter the result on line 38. Then subtract the exemption deduction (line 39) to compute the taxable income.

If the taxpayer has capital gain distributions that are reported directly on Form 1040 or Form 1040A, the taxpayer should use the Capital Gain Tax Worksheet to determine if the tax is less.

The taxpayer should:

- Check the box next to line 13a, Form 1040 and
- Use the Capital Gain Tax Worksheet (Exhibit 8) from either the Form 1040A or 1040 instruction booklet to compute tax.

Example 3

Marjorie is a single taxpayer with taxable income of \$46,250. She files Form 1040 and does not have to file a Schedule D. In 2003, she received capital gain distributions of \$798 from XYZ Investments. Marjorie pays less tax by using Capital Gain Tax Worksheet (Exhibit 8).

Qualified Dividends and Capital Gain Tax Worksheet—Line 41

Keep for Your Records

Before you begin: ✓ Be sure you do not have to file Schedule D (see the instructions for Form 1040, line 13a, that begin on page 23).
 ✓ Be sure you checked the box on line 13a of Form 1040.



1. Enter the amount from Form 1040, line 40	1.	46,250	
2. Enter the amount from Form 1040, line 9b	2.	0	
3. Enter the amount from Form 1040, line 13a	3.	798	
4. Add lines 2 and 3	4.	798	
5. If you are claiming investment interest expense on Form 4952, enter the amount from line 4g; otherwise enter -0-	5.	0	
6. Subtract line 5 from line 4. If zero or less, enter -0-	6.	798	
7. Subtract line 6 from line 1. If zero or less, enter -0-	7.	45,452	
8. Enter the smaller of: • The amount on line 1 or • \$56,800 if married filing jointly or qualifying widow(er), \$28,400 if single or married filing separately, or \$38,050 if head of household.	8.	28,400	
9. Is the amount on line 7 equal to or more than the amount on line 8? <input type="checkbox"/> Yes. Skip lines 9 through 15; go to line 16 and check the "No" box. <input type="checkbox"/> No. Enter the amount from line 7	9.		
10. Subtract line 9 from line 8	10.		
11. Add Form 1040, line 13b, and line 2 above	11.		
12. Enter the smaller of line 10 or line 11	12.		
13. Multiply line 12 by 5% (.05)	13.		
14. Subtract line 12 from line 10. If zero, go to line 16	14.		
15. Multiply line 14 by 10% (.10)	15.		
16. Are the amounts on lines 6 and 10 the same? <input type="checkbox"/> Yes. Skip lines 16 through 25; go to line 26. <input type="checkbox"/> No. Enter the smaller of line 1 or line 6	16.	798	
17. Enter the amount from line 10 (if line 10 is blank, enter -0-)	17.	0	
18. Subtract line 17 from line 16	18.	798	
19. Add Form 1040, line 13b, and line 2 above	19.	0	
20. Enter the amount from line 12 (if line 12 is blank, enter -0-)	20.	0	
21. Subtract line 20 from line 19	21.	0	
22. Enter the smaller of line 18 or line 21	22.	0	
23. Multiply line 22 by 15% (.15)	23.	0	
24. Subtract line 22 from line 18. If zero, go to line 26	24.	798	
25. Multiply line 24 by 20% (.20)	25.	160	
26. Figure the tax on the amount on line 7. Use the Tax Table or Tax Rate Schedules, whichever applies	26.	8,179	
27. Add lines 13, 15, 23, 25, and 26	27.	8,339	
28. Figure the tax on the amount on line 1. Use the Tax Table or Tax Rate Schedules, whichever applies	28.	8,379	
29. Tax on all taxable income. Enter the smaller of line 27 or line 28 here and on Form 1040, line 41	29.	8,339	

FINDING THE TAX

Taxpayers with taxable income of less than \$100,000 use the Tax Table to find their tax. However, children under 14 years of age who have more than \$1,500 of investment income (interest, dividends, etc.) might not be able to use the Tax Table. Their income might have to be taxed at the parents' tax rate. These taxpayers should be referred to a paid professional tax preparer.

The Tax Table is in the back of this book. The tax is based on the person's filing status and taxable income. To find the tax, use the **taxable income** from the tax forms (1040EZ, line 6; 1040A, line 27; and 1040, line 40), and:

- locate the income bracket for the taxable income,
- read across that line until you reach the column for the appropriate filing status, and
- find the amount where the taxable income and filing status meet. This is the tax liability.

If the taxable income is the same as the ending amount in an income bracket, go to the next bracket to find the tax.

Qualifying widows(ers) use the married filing jointly column.

Enter the tax on Form 1040EZ, line 10, Form 1040A, line 28, or Form 1040, line 41.

Double check the amount entered. **Common errors** include:

- Using the wrong standard deduction,
- Incorrectly figuring the exemption amount,
- Using an amount other than taxable income to find the tax,
- Picking up the wrong number from the Tax Table, and
- Transposing the numbers when entering the tax amount.

TAXWISE HINT

If a taxpayer wants to determine whether the standard or itemized deduction is best for him or her, input Schedule A information. TaxWise will automatically select the deduction that is more beneficial.

▶▶ SUMMING UP THIS LESSON ◀◀

Both the standard deduction (or total itemized deductions, if greater) and exemption amounts are subtracted from adjusted gross income to arrive at taxable income.

The standard deduction depends upon:

- ▶ filing status,
- ▶ age, eyesight, and
- ▶ whether the taxpayer can be claimed as a dependent on another taxpayer's return.

Determine the standard deduction by using the:

- ▶ Standard Deduction amount for the appropriate filing status from the appropriate tax form,
- ▶ *Standard Deduction Chart for People Age 65 or Older or Blind*, or
- ▶ *Standard Deduction Worksheet for Dependents*

Itemized deductions are specifically allowed by law. Claim itemized deductions on Schedule A (Form 1040).

Itemized deductions include:

- ▶ Medical and dental expenses
- ▶ Taxes paid
- ▶ Home mortgage and certain investment interest paid
- ▶ Charitable contributions
- ▶ Casualty and theft losses
- ▶ Miscellaneous itemized deductions.

Medical and dental expenses that exceed 7.5 percent of adjusted gross income are deductible.

To be deductible as a charitable contribution, a donation of \$250 or more must be acknowledged in writing by the charitable organization that received the donation.

Most miscellaneous itemized deductions that exceed 2% of adjusted gross income are deductible. However, there are certain miscellaneous itemized deductions that are fully deductible, regardless of gross income.

If deducted investment interest expense exceeds investment income, refer the taxpayer to a paid professional tax preparer.

If you are uncertain whether an expense qualifies as a deduction, do not guess. Refer the taxpayer to a paid professional tax preparer.

▶▶ **SUMMING UP THIS LESSON** ◀◀
(continued)

Most taxpayers compare their total itemized deductions to their standard deduction and enter the larger amount on Form 1040, line 37.

Do not use the Tax Table for taxpayers with taxable income of \$100,000 or more

Common errors include:

- ▶ Using the wrong standard deduction,
- ▶ Incorrectly figuring the exemption amount,
- ▶ Using an amount other than taxable income to find the tax,
- ▶ Picking up the wrong number from the Tax Table, and
- ▶ Transposing the numbers when entering the tax amount.

STUDENT NOTES

STANDARD AND ITEMIZED DEDUCTIONS AND TAX COMPUTATION

ANSWERS TO EXERCISES

Exercise 1

- (A) \$7,000
- (B) \$5,900
- (C) \$10,450
- (D) \$5,700
- (E) \$4,750
- (F) \$1,750

Exercise 2

Sam and Paula's Schedule A

SCHEDULES A&B (Form 1040) <small>Department of the Treasury Internal Revenue Service</small>	Schedule A—Itemized Deductions (Schedule B is on back) ▶ Attach to Form 1040. ▶ See Instructions for Schedules A and B (Form 1040).	<small>OMB No. 1545-0074</small> <div style="font-size: 2em; font-weight: bold;">2003</div> <small>Attachment Sequence No. 07</small>																		
Name(s) shown on Form 1040 <p style="text-align: center;">Sam and Paula Fordham</p>		Your social security number <p style="text-align: center;">000 00 8612</p>																		
Medical and Dental Expenses	Caution. Do not include expenses reimbursed or paid by others. 1 Medical and dental expenses (see page A-2) 2 Enter amount from Form 1040, line 35 2 40,000 3 Multiply line 2 by 7.5% (.075). 4 Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%; text-align: center;">1</td> <td style="width: 40%; text-align: center;">3,250</td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> </tr> <tr> <td style="text-align: center;">3</td> <td style="text-align: center;">3,000</td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td style="text-align: center;">4</td> <td></td> <td></td> <td></td> <td style="text-align: center;">250</td> <td></td> </tr> </table>	1	3,250					3	3,000					4				250	
1	3,250																			
3	3,000																			
4				250																

Exercise 3

John and Shanon's Schedule A

	9	Add lines 5 through 8		9																												
Interest You Paid <small>(See page A-3.)</small> Note. Personal interest is not deductible.	10 Home mortgage interest and points reported to you on Form 1098 11 Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ▶ ----- ----- 12 Points not reported to you on Form 1098. See page A-3 for special rules 13 Investment interest. Attach Form 4952 if required. (See page A-3.) 14 Add lines 10 through 13	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%; text-align: center;">10</td> <td style="width: 40%; text-align: center;">2,180</td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> <td style="width: 10%;"></td> </tr> <tr> <td style="text-align: center;">11</td> <td></td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td style="text-align: center;">12</td> <td></td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td style="text-align: center;">13</td> <td></td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td style="text-align: center;">14</td> <td></td> <td></td> <td></td> <td style="text-align: center;">2,180</td> <td></td> </tr> </table>	10	2,180					11						12						13						14				2,180	
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STANDARD AND ITEMIZED DEDUCTIONS AND TAX COMPUTATION

ANSWERS TO EXERCISES

Exercise 4

Line 15 \$632

Line 16 \$200

Line 18 \$832

Exercise 5

Robert's Schedule A

Job Expenses and Most Other Miscellaneous Deductions (See page A-5 for expenses to deduct here.)	20	Unreimbursed employee expenses—job travel, union dues, job education, etc. You must attach Form 2106 or 2106-EZ if required. (See page A-5.) ▶				
	21	Tax preparation fees	100			
	22	Other expenses—investment, safe deposit box, etc. List type and amount ▶	595			
	23	Add lines 20 through 22	695			
	24	Enter amount from Form 1040, line 35 | 24 | 20,000 |				
	25	Multiply line 24 by 2% (.02)	400			
	26	Subtract line 25 from line 23. If line 25 is more than line 23, enter -0-				295

STANDARD AND ITEMIZED DEDUCTIONS AND TAX COMPUTATION

ANSWERS TO EXERCISES

Exercise 6

Schedule A

SCHEDULES A&B (Form 1040)		Schedule A—Itemized Deductions (Schedule B is on back)		OMB No. 1545-0074	
Department of the Treasury Internal Revenue Service		▶ Attach to Form 1040. ▶ See Instructions for Schedules A and B (Form 1040).		2003 Attachment Sequence No. 07	
Name(s) shown on Form 1040 Seth and Karen Yale				Your social security number 000 00 1039	
Medical and Dental Expenses	1	Medical and dental expenses (see page A-2)	2,320		
	2	Enter amount from Form 1040, line 35 | 2 | 28,000 |			
	3	Multiply line 2 by 7.5% (.075)	2,100		
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-		4	220
Taxes You Paid (See page A-2.)	5	State and local income taxes	1,200		
	6	Real estate taxes (see page A-2)	780		
	7	Personal property taxes			
	8	Other taxes. List type and amount ▶			
	9	Add lines 5 through 8		9	1,980
Interest You Paid (See page A-3.)	10	Home mortgage interest and points reported to you on Form 1098	4,500		
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ▶			
	12	Points not reported to you on Form 1098. See page A-3 for special rules			
Note. Personal interest is not deductible.	13	Investment interest. Attach Form 4952 if required. (See page A-3.)			
	14	Add lines 10 through 13		14	4,500
Gifts to Charity If you made a gift and got a benefit for it, see page A-4.	15	Gifts by cash or check. If you made any gift of \$250 or more, see page A-4	980		
	16	Other than by cash or check. If any gift of \$250 or more, see page A-4. You must attach Form 8283 if over \$500	75		
	17	Carryover from prior year			
	18	Add lines 15 through 17		18	1,055
Casualty and Theft Losses	19	Casualty or theft loss(es). Attach Form 4684. (See page A-5.)		19	
Job Expenses and Most Other Miscellaneous Deductions (See page A-5 for expenses to deduct here.)	20	Unreimbursed employee expenses—job travel, union dues, job education, etc. You must attach Form 2106 or 2106-EZ if required. (See page A-5.) ▶	90		
	21	Tax preparation fees			
	22	Other expenses—investment, safe deposit box, etc. List type and amount ▶	30		
	23	Add lines 20 through 22	120		
	24	Enter amount from Form 1040, line 35 | 24 | 20,000 |			
	25	Multiply line 24 by 2% (.02)	560		
	26	Subtract line 25 from line 23. If line 25 is more than line 23, enter -0-		26	0
Other Miscellaneous Deductions	27	Other—from list on page A-6. List type and amount ▶		27	
Total Itemized Deductions	28	Is Form 1040, line 35, over \$139,500 (over \$69,750 if married filing separately)?			
		<input type="checkbox"/> No. Your deduction is not limited. Add the amounts in the far right column for lines 4 through 27. Also, enter this amount on Form 1040, line 37. <input type="checkbox"/> Yes. Your deduction may be limited. See page A-6 for the amount to enter.		28	

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 11330X

Schedule A (Form 1040) 2003

STUDENT NOTES

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about three “miscellaneous credits”. The mortgage interest credit, the foreign tax credit and the credit for qualified retirement savings are covered in this lesson.

After completing this lesson you should be able to:

- Calculate the credit for qualified retirement savings contributions by using Form 8880.
- Accurately report the foreign tax credit if Form 1116 is not required.
- Be aware of the mortgage interest credit.

CREDITS

A credit is a dollar-for-dollar reduction of the taxpayer’s tax liability. A **refundable** credit can be greater than the tax. Taxpayers not only can have their tax reduced to zero; they can also receive a “refund” of excess credit. A **nonrefundable credit** can also be greater than the tax, but the nonrefundable credit can only reduce the tax to zero. Therefore, taxpayers will not receive a refund for any excess nonrefundable credit. All of the credits discussed in this lesson are non-refundable.

CREDIT FOR QUALIFIED RETIREMENT SAVINGS CONTRIBUTIONS

If the taxpayer contributed to a retirement plan or an IRA, he or she may be eligible for the credit for qualified retirement savings contributions credit. The amount of the saver's credit is determined by the taxpayer's filing status, adjusted gross income, and his or her qualified contributions.

The credit is reported on line 48 of Form 1040, or line 32 of Form 1040A.

To be eligible for the saver's credit, the taxpayer:

- Must be age 18 or older by the end of the tax year,
- Cannot be claimed on another person's tax return, and
- Cannot be a full-time student.

A **full-time student** is anyone who attends school full-time for some part of each of five calendar months of the year. The five months need not be consecutive. An individual is a full-time student if he or she is enrolled for the number of hours or courses the school considers as full-time attendance.

FIGURING THE CREDIT

The credit for qualified retirement savings contributions is figured by multiplying the **credit rate** by the lessor of the:

- Maximum allowable contribution (\$2,000) or
- Eligible contributions.

The credit rate is determined by using the following table.

IF your filing status is...	AND your adjusted gross income is...	THEN your credit rate is...
Married filing jointly	Less than \$30,001	50%
	Between \$30,001 and \$32,500	20%
	Between \$32,501 and \$50,000	10%
	Over \$50,000	0
Head of Household	Less than \$22,501	50%
	Between \$22,501 and \$24,375	20%
	Between \$24,376 and \$37,500	10%
	Over \$37,500	0

Single, Married filing separately, or qualifying widow(er)	Less than \$15,001	50%
	Between \$15,001 and \$16,250	20%
	Between \$16,251 and \$25,000	10%
	Over \$25,000	0

Adjusted gross income is determined without regards to:

- The foreign income exclusion
- The foreign housing exclusion or deduction
- Income from sources within Guam, American Samoa, and the Northern Mariana Islands
- Income from Puerto Rico

Eligible contributions are determined by reducing the taxpayer's **qualified retirement savings contributions** by the following distributions that were received during the **testing period**.

- Any distribution, that is included in the taxpayer's gross income, from a qualified retirement plan, or from an eligible deferred compensation plan.
- Any distribution from a Roth IRA that is not a qualified rollover contribution.

If the distributions received by the taxpayer are for loans or for excess IRA contributions returned before the due date of the return, they are not used to reduce the taxpayer's qualified retirement savings contributions.

Qualified retirement savings contributions are contributions made to a traditional or Roth IRA and salary reduction contributions to a 401(k) plan (including a SIMPLE 401(k)), a tax-sheltered annuity (403(b)) plan, an eligible deferred compensation plan of a state or local government (457(b)) plan, a SIMPLE IRA plan, or a salary reduction SEP.

Qualified retirement savings contributions also include voluntary after-tax employee contributions to a tax-qualified retirement plan or a tax-sheltered annuity (403(b)) plan. For purposes of the credit, an employee contribution will be voluntary as long as it is not required as a condition of employment.

The **testing period** includes:

- The tax year,
- The two preceding tax years, and
- The period between the end of the tax year and the due date of the return (including extensions).

Example 1

Terry contributes \$3,000 to a 401(k) plan during 2003. In 2002, Terry withdrew \$500 from his IRA. In 2003, he withdrew \$900 from his IRA. Neither of these withdrawals were rolled over. In 2003, Terry's adjusted gross income was \$23,000 and his filing status was head of household. Based on these facts, Terry would figure his saver's credit as follows:

(Qualified retirement contributions – withdrawals) x credit rate
(per table)

$$(\$3,000 - \$1,400) \times .20$$

$$\$1,600 \times .20 = \$320 \text{ saver's credit}$$

The credit is figured on **Form 8880**, *Credit for Qualified Retirement Savings Contributions*.

Married filing jointly. If the taxpayer is married filing a joint return, he or she and his or her spouse may both use the credit. Both the taxpayer and spouse are eligible for a credit of the maximum annual contribution amount of \$2,000.

If the taxpayers file a joint return, the qualified contribution is reduced by the taxable distributions received by the taxpayer or the taxpayer's spouse if the taxpayers filed jointly for both:

- the year a distribution was made, and
- the year the credit is claimed.

Exercise 1

Jason is 22 and earned \$30,000 in 2003. He is single and contributed \$3,000 to his 401(k) plan at work. Is Jason eligible for the credit for qualified retirement savings contributions?

Exercise 2

Martha Barnard (000-00-0088) is 32 and files as Head of Household. Her only income is wages of \$26,819. This year, she was able to contribute \$1,000 to her employer's 401(k) plan. She did not put any money in an IRA. Use Exhibit 1 to complete Sally's Form 8880 through line 10.

Form **8880**

Department of the Treasury
Internal Revenue Service

Credit for Qualified Retirement Savings Contributions

▶ Attach to Form 1040 or Form 1040A.

OMB No. 1545-1805

2003

Attachment
Sequence No. **129**

Name(s) shown on return

Your social security number



You **cannot** claim this credit if **either** of the following applies.

- The amount on Form 1040, line 35, or Form 1040A, line 22, is more than \$25,000 (\$37,500 if head of household, \$50,000 if married filing jointly).
- The person(s) who made the qualified contribution or elective deferral **(a)** was born after January 1, 1986, **(b)** is claimed as a dependent on someone else's 2003 tax return, or **(c)** was a **student** in 2003 (see instructions).

	(a) You	(b) Your spouse
1 Traditional and Roth IRA contributions for 2003. Do not include rollover contributions		
2 Elective deferrals to a 401(k) or other qualified employer plan, voluntary employee contributions, and 501(c)(18) plan contributions for 2003 (see instructions)		
3 Add lines 1 and 2		
4 Certain distributions received after 2000 and before the due date (including extensions) of your 2003 tax return (see instructions). If married filing jointly, include both spouses' amounts in both columns. See instructions for an exception		
5 Subtract line 4 from line 3. If zero or less, enter -0-		
6 In each column, enter the smaller of line 5 or \$2,000		
7 Add the amounts on line 6. If zero, stop ; you cannot claim the credit		
8 Enter the amount from Form 1040, line 35*, or Form 1040A, line 22		

9 Enter the applicable decimal amount shown below:

If line 8 is—		And your filing status is—		
Over—	But not over—	Married filing jointly	Head of household	Single, Married filing separately, or Qualifying widow(er)
Enter on line 9—				
---	\$15,000	.5	.5	.5
\$15,000	\$16,250	.5	.5	.2
\$16,250	\$22,500	.5	.5	.1
\$22,500	\$24,375	.5	.2	.1
\$24,375	\$25,000	.5	.1	.1
\$25,000	\$30,000	.5	.1	.0
\$30,000	\$32,500	.2	.1	.0
\$32,500	\$37,500	.1	.1	.0
\$37,500	\$50,000	.1	.0	.0
\$50,000	---	.0	.0	.0

Note: If line 9 is zero, **stop**; you cannot claim the credit.

10 Multiply line 7 by line 9		
11 Enter the amount from Form 1040, line 43, or Form 1040A, line 28		
12 Enter the total of your credits from Form 1040, lines 44 through 47, or Form 1040A, lines 29 through 31		
13 Subtract line 12 from line 11. If zero, stop ; you cannot take the credit		
14 Credit for qualified retirement savings contributions. Enter the smaller of line 10 or line 13 here and on Form 1040, line 48, or Form 1040A, line 32		

MORTGAGE INTEREST CREDIT

Taxpayers who hold qualified mortgage credit certificates under a qualified state or local government program may claim a credit for mortgage interest paid. The certificate must be for the taxpayer's main home. If the interest is paid to certain related parties (such as relatives), the credit cannot be claimed.

The credit is figured on Form 8396, *Mortgage Interest Credit*. Include the amount of the credit on Form 1040, line 52. Also, check box a on line 52 for Form 8396.

Any mortgage interest credit that the taxpayer cannot use in 2003 can be carried forward for up to three tax years. Figure the carry-forward credit in Part II of Form 8396.

Reduce the mortgage interest deduction claimed on Schedule A, Form 1040, by the amount shown on line 3 of Form 8396.

Caution: If the taxpayer was issued (and used) a qualified mortgage credit certificate after 1990 for a home, the taxpayer may have to recapture (repay) all or part of the benefit if the taxpayer sells that home within 9 years. The recapture is figured on Form 8828, *Recapture of Federal Mortgage Subsidy*.

If the taxpayer paid income, war profits, or excess profits taxes to any:

- Foreign country,
- U.S. possession, or
- Any political subdivision, or agency or instrumentality of the country or possession, he or she may be able to take a **Foreign Tax Credit** (FTC) for taxes paid.

To determine if the tax paid is eligible for the foreign tax credit, the taxpayer **may** need to consult a paid professional preparer.

Generally, to claim the FTC, a taxpayer is required to file Form 1116, *Foreign Tax Credit (Individual, Estate, Trust, or Nonresident Alien Individual)*; however, the taxpayer does not have to file Form 1116 to take the credit if he or she meets all of the following requirements.

- All of the taxpayer's gross foreign source income is from interest and dividends that are reported on Form 1099-INT, or Form 1099-DIV (or substitute statement)
- If the taxpayer has dividend income from shares of stock, he or she held those shares for at least 16 days.
- The taxpayer is not filing Form 4563, *Exclusion of Income for Bona Fide Residents of American Samoa*, or excluding income from sources within Puerto Rico.
- The total of the taxpayer's foreign taxes is less than or equal to \$300 (\$600 if married filing jointly).
- All of the taxpayer's foreign taxes were:
 - Legally owed and not eligible for a refund, and
 - Paid to countries that are recognized by the United States and do not support terrorism.

For additional information, see *the Instructions for Form 1116*.

If the taxpayer meets all of the requirements listed above, enter the foreign tax credit on line 45 of Form 1040. Form 1116 is not required.

Example 2

Tabitha received a 1099-DIV that shows \$219 of foreign taxes (box 6) in 2003. According to Tabitha she paid no other foreign taxes. She can claim the \$219 on line 44 of Form 1040.

Exercise 3

Clyde comes to your site seeking help with his foreign tax credit. He is single and his 1099-DIVs show a total of \$423 of foreign tax. Does Clyde need Form 1116 to claim his credit?

Exercise 1

No; Jason is not eligible for the credit because his income exceeds the threshold limit.

Exercise 2

See the completed Form 8880 on the next page.

Exercise 3

Yes, Clyde needs to complete a Form 1116 since his foreign taxes exceed \$300. Clyde will need to seek the assistance of a paid professional preparer.

Name(s) shown on return

MARTHA BARNARD

Your social security number

000 00 0088



You **cannot** claim this credit if **either** of the following applies.

- The amount on Form 1040, line 35, or Form 1040A, line 22, is more than \$25,000 (\$37,500 if head of household, \$50,000 if married filing jointly).
- The person(s) who made the qualified contribution or elective deferral **(a)** was born after January 1, 1986, **(b)** is claimed as a dependent on someone else's 2003 tax return, or **(c)** was a **student** in 2003 (see instructions).

	(a) You	(b) Your spouse																																																																	
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Note: If line 9 is zero, **stop**; you cannot claim the credit.

*See Pub. 590 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

STUDENT NOTES

Lined area for student notes.

FINISHING THE RETURN

Lesson 6

INTRODUCTION AND OBJECTIVES

In this lesson you will learn how to report federal income tax payments and figure the overpayment or balance due. You will also learn how to determine if estimated taxes should be paid. Additionally, you will learn how to finish the return and have the taxpayer sign the return.

After completing this lesson you should be able to:

- Calculate and report federal income tax withheld from all sources.
- Calculate and report estimated tax payments.
- Calculate the refund or amount due.
- Determine if estimated taxes should be paid.
- Determine if changes to the taxpayer's W-4 or W-4P should be suggested.

Please pay close attention to the section about identifying the returns that you work on. It is critical for you to enter the correct site identification number in the preparer's signature section of the return. The number goes in the designated area on the forms with the pre-printed "P" followed by 8 digits or in the PTIN/SSN field of the return.

This lesson will provide detailed information on how to finish the tax return. The following checklist is provided as a quick reference of the steps needed to finish the return.

CHECKLIST FOR FINISHING THE RETURN

Withholdings, Payments and Other Credits:

- Add all Federal Income Tax Withholding from Form W-2, box 2, and include on return.
- Add all Federal Income Tax Withholding from box 4 of Forms 1099R, 1099INT, 1099DIV and 1099G. Include in the payments section of the return.
- Include all estimated tax payments in the payment section.

POTENTIAL PITFALLS



Form W-2, box 4, shows social security tax withheld and box 6 shows Medicare tax withheld. These are not the same as federal income tax withheld. Do not report the amounts in box 4 and box 6 as federal income tax withheld.

POTENTIAL PITFALLS



When a taxpayer worked for more than one employer during the year, add up the amounts shown in box 4 of all Forms W-2. If the total in box 4 of all forms exceeds \$5,263.80 the taxpayers should claim a refund of excess social security tax withheld. Use the worksheet in Pub. 505, *Tax Withholding and Estimated Tax* to compute the refund.

- Include the amount of last year's refund that was applied to this year in the payment section. Note: If you need assistance with how to do this with TaxWise®, ask your site coordinator or computer specialist.
- Calculate all of the refundable credits (covered in later lessons) that the taxpayer is entitled to and include them in the payments section of the return. Using TaxWise® software will help you determine what credits that the taxpayer is entitled to.
- Add all payments together and enter them on the total payments line. TaxWise® will do this step for you.
- Subtract the total payments from the total tax. TaxWise® will also complete this step for you.
- Record the account number and the routing number for taxpayers who want their refund direct deposited. Note: TaxWise® will ask you for this information on the Main Information screen and on the tax form. This is to help ensure that you have keyed in the correct information. Complete the line to apply part of the refund to next year, if the taxpayer wishes to use this option.

Paying Taxes or Adjusting Withholding Taxes if Balance Due:

- Explain the payment option (check, credit card, direct debit and installment agreement) to a taxpayer who owes money.
- Inform the taxpayer about the identifying information to include on payments made by check.
- Explain that interest and penalties continue to accrue on the unpaid balance even if the taxpayer has a valid installment agreement.
- Explain estimated taxes to taxpayers who expect to owe tax in 2004.
- Assist the taxpayer with completing form 1040ES for 2004. TaxWise® can do this for you. It will even print the vouchers for the payments.
- Provide the taxpayer with the mailing address for the estimated payments. (Some sites provide unstamped envelopes for the taxpayers.)
- Encourage taxpayers to consider adjusting their withholding (on Form W-4 or W-4P) if they have a large refund or owe more than \$1,000 on the return.

Advance Earned Income Tax Credit (AEIC):

- Inform taxpayers about the Advance Earned Income Credit, if they were eligible for EIC this year and have at least one qualifying child. Be prepared to give the taxpayer a Form W-5, if they request it.

Name, Address, and Taxpayer Identification Section of Return:

- Complete the name and address section of the tax return. Use the taxpayer's label (if available) on a return prepared by hand. For computer generated returns, this section will be completed based on the information you entered in the Main Information section of the TaxWise® software.
- Make sure that you include the Taxpayer Identification Number for all taxpayers and dependents listed on the return. Note: If you are using TaxWise®, you will get an error when you run diagnostics if you have not included the identifying number. TaxWise® also has a diagnostic feature that helps you check the accuracy of the identifying number by comparing it to a database of information from the Social Security Administration. This does not guarantee that the name and social security number match. You should always try to look at the actual Social Security cards if possible.
- Mark the Presidential Election Campaign Box for the taxpayer. Note: If the taxpayer has a total tax of zero, the presidential campaign box should be marked no.

Return Assembly and Copy:

- Assemble the return. If filing a paper return for the taxpayer, forms should be in the order of the sequence number in the upper right corner. Procedures on assembling electronic returns may vary from site to site. Please ask your site coordinator for this information.
- Retain a copy of all electronic returns. Remember that you are not allowed to retain copies of the tax returns at your site past the end of the filing season. The retained copies should be forwarded to your local IRS territory office, where they will be retained until the end of the calendar year (as prescribed by the electronic filing regulations).

Site Identification Number on Forms 1040, 1040A, & 1040EZ

Congress annually asks the IRS to provide the number of returns that were filed by volunteer tax assistance sites. For statistical purposes, the IRS requests that all Federal returns be identified with a Site Identification Number. The Site Identification Number is entered in the Paid Preparer's section of the tax return. The Internal Revenue Service Submission Processing Center will count each return processed using this data.

More about this topic is covered later in this lesson.

On Site Quality Review:

- Submit the completed return to the quality reviewer at your site. Note: Not all sites have enough volunteers to have a designated quality reviewer. In this case, ask another volunteer to review the form you prepared. Using TaxWise® is not a substitute for quality review.

Signing the Return and Third Party Designation:

- Mark the area where the taxpayer should sign the return and/or Form 8453. Publication 3189 will contain additional information on how to use the PIN program to sign electronic returns.
- Complete the third party designation section of the return if the taxpayer wishes to allow someone else to discuss the return with the IRS. (**You can't designate yourself.**)

Taxpayer Question:

- Ask the taxpayer if they have any additional questions.

Where to Mail Paper Returns:

- Tell the taxpayer where to mail the return (if filing by paper). Electronically filed returns are automatically transmitted to the correct IRS Processing Center. Paper tax returns must be mailed in by the taxpayer to the IRS processing Center for the area (state) where the taxpayer resides. Each tax package contains a pre-addressed envelope for a particular area based on the last address filed with the IRS. If the taxpayer has moved or does not have a pre-addressed envelope the address and other mailing information is located in the individual federal tax package and in your Quick Reference Guide, Publication 1977. On-site. Some sites provide unstamped pre-addressed envelope for their taxpayers. (You might be able to get the envelopes donated from a local office supply store. Your site receptionist could address the envelopes or you could print computer labels to use on them.)

PAYMENTS

The federal government has a pay-as-you-earn tax system. The information for the payments section of the return has three sources: federal income tax withholdings, estimated tax payments, and refundable credits.

Income tax withheld can appear on:

- Form W-2, *Wage and Tax Statement*, in box 2
- Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, in box 4
- Form 1099-INT, *Interest Income*, in box 4

- Form 1099-DIV, *Dividends and Distributions*, in box 4
- Form W-2G, *Certain Gambling Winnings*, in box 2
- Form 1099-G, *Certain Government and Qualified State Tuition Program Payments*, box 4
- SSA-1099, Social Security Benefits
- RRB-1099, Railroad Retirement Benefits Tier 1
- RRB-1099R, Railroad Retirement Benefits Tier 2
- Form 1099B, Proceeds from Broker and Barter Exchange Transactions


Example 1

Kamica has one Form W-2 (Exhibit 1).

The entry on line 7, Form 1040EZ, line 39, Form 1040A, or line 62, Form 1040, is \$988.

Exhibit 1

Kamica's Form W-2

a Control number		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number 10-0864213			1 Wages, tips, other compensation 12,350.00		2 Federal income tax withheld 988.00		
c Employer's name, address, and ZIP code XYZ Associates 2112 Third Street Tampa, FL 33621			3 Social security wages 12,350.00		4 Social security tax withheld 765.70		
			5 Medicare wages and tips 12,350.00		6 Medicare tax withheld 179.08		
			7 Social security tips		8 Allocated tips		
d Employee's social security number			9 Advance EIC payment		10 Dependent care benefits		
e Employee's first name and initial Last name Kamica A. Howard 134 Dawes Blvd. Tampa, FL 33621			11 Nonqualified plans		12a See instructions for box 12		
			13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12b		
			14 Other		12c		
					12d		
f Employee's address and ZIP code							
15 State	Employer's state ID number	16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.	19 Local income tax	20 Locality name	

Form **W-2** Wage and Tax Statement
 Copy B To Be Filed with Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

2003
(Rev. February 2003)

Department of the Treasury—Internal Revenue Service

Example 2

Lucas has a Form 1099-INT (Exhibit 2), a Form 1099-R (Exhibit 3), and a Form 1099-DIV (Exhibit 4). His total income tax withheld is entered on line 39, Form 1040A. It is \$1,247.

Exhibit 2

Lucas's Form 1099-INT

PAYER'S name, street address, city, state, ZIP code, and telephone no.		Payer's RTN (optional)	OMB No. 1545-0112
Second Federal Bank 210 Miller Avenue Denver, CO 86011			2003 Interest Income
PAYER'S Federal identification number 10-4213597		RECIPIENT'S identification number 000-00-4213	Form 1099-INT
RECIPIENT'S name Lucas B. George		1 Interest income not included in box 3 \$ 935.00	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
Street address (including apt. no.) 1360 Shannon Avenue		2 Early withdrawal penalty \$	
City, state, and ZIP code Denver, CO 86011		3 Interest on U.S. Savings Bonds and Treas. obligations \$	
Account number (optional)		4 Federal income tax withheld \$ 187.00	
		5 Investment expenses \$	
		6 Foreign tax paid \$	7 Foreign country or U.S. possession

Form **1099-INT** (keep for your records) Department of the Treasury - Internal Revenue Service

Exhibit 3

Lucas's Form 1099-R

PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution		OMB No. 1545-0119
APEX Triangles 213 Hickory Meadows Denver, CO 86011		\$ 12,000.00		2003
		2a Taxable amount \$		Form 1099-R
		2b Taxable amount not determined <input type="checkbox"/>		Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return.
		Total distribution <input type="checkbox"/>		
PAYER'S Federal identification number 10-9753124	RECIPIENT'S identification number 000-00-4213	3 Capital gain (included in box 2a) \$		4 Federal income tax withheld \$ 960.00
RECIPIENT'S name Lucas B. George		5 Employee contributions or insurance premiums \$		6 Net unrealized appreciation in employer's securities \$
Street address (including apt. no.) 1360 Shannon Ave.		7 Distribution code	IRA/SEP/SIMPLE <input type="checkbox"/>	8 Other \$ %
City, state, and ZIP code Denver, CO 86011		9a Your percentage of total distribution %		9b Total employee contributions \$
Account number (optional)		10 State tax withheld \$	11 State/Payer's state no.	12 State distribution \$
		13 Local tax withheld \$	14 Name of locality	15 Local distribution \$

Form **1099-R** Department of the Treasury - Internal Revenue Service

<input type="checkbox"/> CORRECTED (if checked)			OMB No. 1545-0110		2003	Dividends and Distributions	
PAYER'S name, street address, city, state, ZIP code, and telephone no. Denver Sheet Metal 214 16th Street Denver, CO 86013		1 Ordinary dividends	\$ 500.00	Form 1099-DIV			
		2a Total capital gain distr.	\$				
		2b 28% rate gain	\$				
PAYER'S Federal identification number 10-2846731	RECIPIENT'S identification number 000-00-4213	2c Qualified 5-year gain	\$	2d Unrecap. sec. 1250 gain	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.		
RECIPIENT'S name Lucas B. George Street address (including apt. no.) 1360 Shannon Avenue City, state, and ZIP code Denver, CO 86011		2e Section 1202 gain	\$	3 Nontaxable distributions			\$
		4 Federal income tax withheld	\$ 100.00	5 Investment expenses			\$
		6 Foreign tax paid	\$	7 Foreign country or U.S. possession			
Account number (optional)		8 Cash liquidation distr.	\$	9 Noncash liquidation distr.			\$
Form 1099-DIV		(keep for your records)		Department of the Treasury - Internal Revenue Service			

Estimated Tax Payments

Add all estimated tax payments made by the taxpayer for the year. Be sure to include:

- Payment made from last year's overpayment (see last year's tax return.)
- Quarterly payments made using the Form 1040ES, including the one made in January of the current tax year.

Record total estimated tax payments on Line 40 of Form 1040A or Line 63 of Form 1040.


Refundable Credits

Make sure that any refundable credits you have calculated are entered on the proper lines. The Earned Income Credit is reported on line 8 of the Form 1040 EZ, Line 41 of the Form 1040A, and Line 64 of the Form 1040. Any refundable Child Tax Credit is reported on Line 42 of the Form 1040A and Line 66 of the Form 1040. If excess Social Security deductions were made because of multiple employers, that amount is shown on Line 65 of the Form 1040.

Total Payments

Add the total of withholdings, estimated tax payments made, and refundable credits together. Enter this total on Line 9 of the Form 1040EZ, Line 43 of the Form 1040A, or Line 69 of the Form 1040.

FIGURING THE OVERPAYMENT OR THE TAX DUE

ALERT 

You must reduce the 2003 child tax credit by any advance payment that the taxpayer received in 2003.

Overpayments

If there has been more tax payments made than the amount of tax liability (line 10, Form 1040EZ, line 38, Form 1040A, or line 61, Form 1040), this is considered an overpayment. A taxpayer may wish to have a portion of the overpayment applied to next year's taxes. If so, then enter the amount to be applied to the following year on line 46 of the Form 1040A or line 72 of the Form 1040. Subtract this amount from the total overpayment and enter the remainder on line 45a of the Form 1040A or line 71a of the Form 1040.

Only a total refund can be entered on the Form 1040EZ, line 12a. Any overpayment on Form 1040EZ must be refunded; It cannot be applied to next year's taxes.

Example 3

Exhibit 5 shows Form 1040A, lines 28 through 46, for Ron his tax due. His total tax is \$3,491. His total payments are \$5,000. Ron overpaid and wants \$900 to be applied to his 2004 estimated tax. Note that line 45a plus line 46 equals the amount on line 44.

Exhibit 5

Form 1040A, page 2

28	Tax , including any alternative minimum tax (see page 35).	28	3,491.00
29	Credit for child and dependent care expenses. Attach Schedule 2.	29	
30	Credit for the elderly or the disabled. Attach Schedule 3.	30	
31	Education credits. Attach Form 8863.	31	
32	Retirement savings contributions credit. Attach Form 8880.	32	
33	Child tax credit (see page 38).	33	
34	Adoption credit. Attach Form 8839.	34	
35	Add lines 29 through 34. These are your total credits .	35	0.00
36	Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36	3,491.00
37	Advance earned income credit payments from Form(s) W-2.	37	
38	Add lines 36 and 37. This is your total tax .	▶ 38	3,491.00
39	Federal income tax withheld from Forms W-2 and 1099.	39	2,600.00
40	2003 estimated tax payments and amount applied from 2002 return.	40	2,400.00
41	Earned income credit (EIC) .	41	
42	Additional child tax credit. Attach Form 8812.	42	
43	Add lines 39 through 42. These are your total payments .	▶ 43	5,000.00
44	If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44	1,509.00
45a	Amount of line 44 you want refunded to you .	▶ 45a	609.00
▶ b	Routing number <input type="text"/>	▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
▶ d	Account number <input type="text"/>		
46	Amount of line 44 you want applied to your 2004 estimated tax .	46	900.00
47	Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53.	▶ 47	0.00
48	Estimated tax penalty (see page 53).	48	

Refunds

If the taxpayer wants an overpayment refunded, advise that a check should be mailed within 6-8 weeks after the return is filed. Remind the taxpayer of the availability to have the refund deposited directly into a financial account, such as a bank account.

Direct Deposit

Instead of getting a paper check, taxpayers may choose to have their refund deposited directly into their account at a bank or other financial institution such as a mutual fund, brokerage firm, or credit union.

Note. Taxpayers should check with their financial institution to make sure their direct deposit will be accepted and to get the correct routing and account number.

Exhibit 6 shows the general location of the routing and account number on a sample check. The routing number must be nine digits (the first two digits must begin with 01 through 12 or 21 through 32, otherwise the direct deposit will be rejected and a check sent instead). The account number can be up to 17 characters (both numbers and letters). It can include hyphens but not spaces or special symbols. The number should be entered from left to right with any unused boxes left blank.

Exhibit 6

The diagram shows a check with the following details:

- Payor: LERON BROWN, RENA BROWN, 123 Main Street, Anyplace, CA 10000
- Payee: PAY TO THE ORDER OF
- Bank: ANYPLACE BANK, Anyplace, NY 10000
- Routing number (line 70b): 250250025
- Account number (line 70d): 202020 86 1234
- Check number: 1234
- Microprint MICR line: @250250025 @202020 86 1234
- Check number in top right: 1234
- Check number in bottom right: 15-00000000

Annotations in the diagram:

- A circle around the routing number is labeled "Routing number (line 70b)".
- A circle around the account number is labeled "Account number (line 70d)".
- An oval around the check number in the bottom right is labeled "Do not include the check number".
- A diagonal watermark "SAMPLE" is visible across the center of the check.

Tax Due

If there are less tax payments than the amount of tax liability, then there is tax due to be paid with the return. When this happens, remind the taxpayer to make the check or money order payable to the "United States Treasury." Taxpayers can also pay by credit card or by authorizing a direct debit from their checking or savings account on the date they choose (anytime up to April 15, 2004). Encourage a 1040 filer to voluntarily send Form 1040-V, *Payment Voucher*, with his or her payment. The instructions for completing the voucher appear on the 1040-V. The taxpayer should write his or her name, address, social security number, daytime telephone number, and "2003 Form 1040 (or 1040A or 1040EZ, whichever applies)"

on the check or money order. The payment and Form 1040-V should be enclosed, but not attached to the tax return. Taxpayers should not mail cash with their returns.

To help IRS process the payment, the taxpayer should enter the amount on the right side of the check like this: \$XXX.XX. Do not use dashes or lines (for example, do not enter “\$XXX—” or “\$XXX^{XX}/₁₀₀”).

Electronic Payment Options

If the taxpayer owes an amount on his or her return, he/she can make the payment electronically. To pay by credit card, the taxpayer must use one of the service providers listed in the instructions for Forms 1040, 1040A, or 1040EZ. The taxpayer can also pay by authorizing a direct debit out of his/her checking or savings account by April 15, 2004.

If the taxpayer cannot pay the full amount owed shown on his/her return, the taxpayer may ask permission to make monthly installment payments. To ask for an installment agreement, the taxpayer should file Form 9465, *Installment Agreement Request*, with the tax return.

Estimated Tax Penalty. If line 10, Form 1040EZ, line 47, Form 1040A, or line 73, Form 1040, is \$1,000 or more and it is more than 10 percent of the tax shown on the return, or if the taxpayer underpaid his or her 2003 estimated tax liability, the taxpayer can owe a penalty for underpayment of estimated tax. If so, report the penalty on line 48 for Form 1040A or line 74 of Form 1040. Line 47 or line 73 should include the amount owed with the return plus the penalty reported on line 48 of Form 1040A or line 74 of Form 1040, respectively.

Because the Form 2210, *Underpayment of Estimated Tax by Individuals, Estates, and Trusts*, used to compute estimated tax penalty is complicated, the IRS encourages taxpayers to let the IRS figure the penalty for them. The IRS will figure the penalty for underpayment of estimated tax and, if a penalty is owed, the taxpayer will be sent a bill. If taxpayers want the IRS to figure the penalty for them, the taxpayers should leave the penalty line on their return blank and **should not** complete Form 2210. As long as the taxpayer files the return by April 15, 2004, the IRS will not charge interest on the penalty if the bill is paid by the date specified on the bill.

FIGURING ESTIMATED TAX FOR NEXT YEAR

Estimated tax is the amount a taxpayer expects to owe for the year after deducting any tax credits or federal income tax withheld. In other words, it is the amount the taxpayer anticipates will be owed on his or her 2004 federal income tax return.

If a taxpayer is an employee, the taxpayer's employer generally must withhold income, Medicare, and social security taxes on the wages paid. Also, most payers of taxable pensions withhold income tax and pay it to the government. However, a taxpayer may receive many types of taxable income that are not subject to having tax withheld.

A taxpayer who receives interest, dividends, alimony, unemployment compensation, rent, gains from the sale of assets, prizes, or awards, generally will have no income tax withheld on the payments. As a result, the taxpayer may find that he or she owes estimated tax. Most self-employed taxpayers will also find they are required to pay estimated tax.

Who Must Pay Estimated Tax

Estimated tax payments are required if certain conditions are met. Generally a taxpayer must make payments of estimated tax if:

1. He or she expects to owe \$1,000 or more in tax for 2004 after subtracting federal income tax withheld and credits from taxable income,

AND

2. He or she expects the 2004 tax withheld and credits to be less than the smaller of:
 - a) 90 percent of the tax to be shown on his or her 2004 tax return, or
 - b) 100 percent of the tax shown on his or her 2003 tax return. The return must cover all 12 months.

POTENTIAL PITFALLS



When figuring estimated tax, be sure to include all taxes, such as tax on lump-sum distributions and self-employment tax.

Married taxpayers can pay estimated tax either separately or jointly. How they pay their estimated tax will not affect their choice of filing a joint return or separate returns for the year. Joint estimated tax payments may be divided between the spouses if they later choose to file separate returns.

Example 4

Jayne is single and retired. She works part time as an usher in a movie theater. She estimates her 2004 income will be \$16,421, which includes \$3,500 of interest income from which there will be no tax withheld. Jayne calculates that she expects to owe \$1,008 (after taking into account her expected tax withheld and credits). Jayne meets condition 1 (mentioned earlier) and may have to pay estimated tax. Further checking tells Jayne that her expected 2004 tax withheld will be less than 100 percent of the tax shown on her 2003 return and less than 90 percent of the tax she will show on her 2004 tax return. Since Jayne also meets condition 2 (mentioned earlier), she is required to pay estimated tax.

Limit on the use of prior year's tax. Married taxpayers with joint AGI exceeding \$150,000 or \$75,000 if married filing separately cannot use 100% of their 2003 tax to figure their 2004 estimated tax payments.

For more information, see Publication 505, *Tax Withholding and Estimated Tax*.

How to Figure Estimated Tax

Estimated tax is paid by using Form 1040-ES, *Estimated Tax For Individuals*. Form 1040-ES also contains a worksheet that can be used in figuring a taxpayer's estimated tax. The taxpayer should keep the worksheet for his or her records.

To figure the estimated tax, the taxpayer must first figure his or her expected adjusted gross income, taxable income, taxes, and credits for 2004. All available facts that will affect those items during the year must be taken into account. Use the 2003 tax return as a starting point for estimating 2004 income, deductions, and credits. However, be careful to make adjustments both for anticipated changes in the taxpayer's situation and for recent changes in the tax law.

Form 1040-ES contains both the 2004 Tax Rate Schedules and the 2004 standard deduction and exemption amounts. Be sure to use the 2004 figures when figuring the estimated tax.

When to Pay Estimated Tax

For estimated tax purposes, the year is divided into four payment periods. Each period has a specific due date.

Date taxpayer receives income	Due date of first installment	No. of payments
January 1– March 31	April 15, 2004	4
April – May 31	June 16, 2004	3
June 1 – August 31	September 15, 2004	2
September 1 – December 31	January 17, 2005	1

POTENTIAL PITFALLS



Advise the taxpayer to use the pre-addressed envelopes that came with his or her Form 1040-ES package, or mail payment vouchers to the address shown in the Form-ES instructions for the place where he or she lives. *Do not* use the address shown in the Form 1040 or Form 1040A instructions.

Most of the taxpayers that you assist will pay their estimated tax in four equal installments. However, a taxpayer does not have to make estimated tax payments until he or she has income on which tax is owed. If a taxpayer receives income after one or more of the payment periods have passed, he or she will begin making payments during the period when the income is received.

The minimum payment due during the period when the income is received is one-fourth of the total estimated tax for the year, generally, plus an additional fourth of the yearly total for each period which has already passed. The balance of the estimated tax will be paid during the remaining periods (one-fourth of the yearly total for each remaining period).

The taxpayer also has the option of paying all the estimated tax at once. Instead of paying by installments, he or she may choose to pay the entire amount by the due date of the period during which the income is received.

Some taxpayers choose to pay all of their estimated tax with the first payment, April 15, 2004. It alleviates the need for them to remember to make the remaining payments.

Also, a taxpayer can apply all or part of an overpayment from his or her 2003 Form 1040 or Form 1040A to the estimated tax for 2004. The overpayment amount to be credited is entered on Form 1040, line 72, or Form 1040A, line 46. All of the credit can be applied to the first payment or it can be spread out among any or all of the payments.

If any due date falls on a Saturday, Sunday, or legal holiday, the payment is due on the next business day.

If a taxpayer files his or her 2004 Form 1040 or Form 1040A by January 31, 2005, and pays the entire amount of tax owed at that time, he or she is not required to make the estimated tax payment that would be due on January 18, 2005.

How Much Estimated Tax to Pay

The computed estimated tax is based on expected income and deductions and should take into account all facts known at the time the estimate is made. If the taxpayer is unsure about the accuracy of the estimate, he or she may want to pay more than the required minimum 90 percent of the 2003 estimated tax. Taxpayers who do not pay enough tax by the due date of each payment period may be charged a penalty, even if the filed 2004 return shows a refund. Generally, the simplest and safest procedure is to make sure that the total of tax withheld plus the amount of estimated tax for each payment period during 2004 is at least one-fourth of the tax shown on the 2003 return. For more information, see Publication 505.

How to Pay Estimated Tax

Estimated tax payments can be sent electronically to the IRS by direct debit payment from the taxpayer's checking or savings account, by credit card, or can be sent along with a payment voucher from Form 1040-ES. Each voucher is inscribed with its due date. Be sure to use the correct voucher for each payment. For more information on electronic filing and payments, see Form 1040-ES instructions.

If the taxpayer paid estimated tax in 2003, he or she should have received a Form 1040-ES package containing preprinted vouchers. These vouchers show the taxpayer's preprinted name, address, and social security number. To use them, simply enter the amount of the payment on the appropriate line. If a taxpayer does not have the preprinted forms, use a set of blank vouchers from Form 1040-ES and enter the information on the appropriate lines. Advise the taxpayer to write his or her social security number and "2004 Form 1040-ES" on the check or money order (payable to the "United States Treasury") when paying estimated tax.

FORM W-4 AND W-4P

An employer withholds tax based on wages paid and information the employee provides on Form W-4, *Employee's Withholding Allowance Certificate*. The employee uses his or her expected income, deductions, adjustments to income, and credits to figure the total withholding allowances to claim on Form W-4. In addition, an employee can claim extra allowances in certain situations.

A taxpayer who receives distributions from a pension, an annuity, an IRA, a stock bonus plan, or certain deferred compensation plans should use Form W-4P, *Withholding Certificate for Pension or Annuity Payments*, to notify the payer whether, and how much, income tax should be withheld.

Income, deductions, and credits should be estimated carefully. Taxpayers who do not have enough federal income tax withheld can be subject to interest and penalties. Taxpayers who have a very large refund or who owe should consider adjusting their withholding.

Some taxpayers want their withholding to be high enough to ensure that they receive a tax refund. They do not want to pay an additional amount when filing their tax return. If a taxpayer wishes, it is legal to claim fewer allowances than he or she is allowed. More tax than required will be withheld each pay period and, at the end of the year, the taxpayer should be eligible for a refund of overpaid taxes.

Forms W-4 and W-4P also contain:

- Instructions
- *Personal Allowances Worksheet*
- *Deductions and Adjustments Worksheet*
- *Two-Earner / Two-Job, Multiple Pension / More Than One Income Worksheets*
- Tables

The worksheets incorporate the number of allowances, adjustments, deductions, and credits that the employee expects on his or her 2004 income tax return. Some or all of these additional worksheets will then be used by the employee in completing the allowance certificate.

If an employee has a working spouse or income from two jobs, only one set of Form W-4 Worksheets should be completed. Complete the Form W-4 Worksheets using the combined expected income (from all sources and for both spouses if filing a joint return), adjustments, deductions, and exemptions. The number of total allowances from this Form W-4 can then be divided among all jobs. Withholding will usually be the most accurate when an employee claims zero allowances on all jobs except for the highest paying one. Reminder: A separate Form W-4 is needed for each job.

Certain events can occur during the year that can change an employee's marital status, exemptions, allowances, deductions or credits. When this happens, the employee may have to change his or her withholding allowances by submitting a new Form W-4 to the employer. The original Form W-4 remains in effect until the employee changes it.

For more information on withholding, refer to Publication 919, *How Do I Adjust My Tax Withholding?*

W-5, Advance Earned Income Credit (AEIC)

At this time, you as the preparer have the opportunity and the means to assist the taxpayer with the Form W-5, *Earned Income Credit Advance Payment Certificate*. The amount of the AEIC pay-

ments are based on wages by payroll cycle. Only persons with at least one qualifying child can get AEIC payments. If the taxpayer qualifies for the Earned Income Credit for 2003 refer them to Publication 596, *Earned Income Credit* or Form W-5 for additional information.

Completing and Assembling the Return

After all the decisions have been made regarding payments, overpayments, and estimated taxes, you should complete the taxpayer identification section, assemble the return, and submit it for quality review. When the review is completed, have the taxpayer sign the return and provide instructions on where and when to send it to the IRS. These steps are provided below.

Taxpayer Identification Section

This section is completed after the rest of the return. Often, this saves time because after you begin preparing Form 1040A, you may discover that Form 1040EZ or Form 1040 is more appropriate. If this happens, you will not have to complete the taxpayer identification section twice.

Taxpayers who filed returns last year probably received a forms package by mail this year. The package includes a preaddressed label which shows the name and address of the taxpayer(s).

Peel the label off and place it in the address area of the return. Mark through any errors on the label, and print the correct information on the label. Be sure to enter the social security number(s) (or Taxpayer Identification Number (ITIN) to the right of the label area.

If a taxpayer did not receive a forms package or does not have a pre-addressed label, PRINT the required information. Enter the taxpayer's name and social security number (or ITIN) on the first line. If married taxpayers are filing a joint return, enter one spouse's complete name and social security number (or ITIN) on the first line and the other spouse's complete name and social security number (or ITIN) on the second line. Be sure that each taxpayer's name and social security number (or ITIN) appear on one line, separate from the spouse's information. If you enter the husband's name and the wife's social security number (or ITIN) on the same line, there can be a considerable delay in processing the return.

Enter the address where any refund or notices should be sent. If the post office delivers mail to a post office box rather than to a street address, enter the P.O. box number on the line for the home address.

The Presidential Election Campaign Fund appears in the name and address area of Forms 1040EZ, 1040A, or 1040. Check *Yes* if the taxpayer wishes to have \$3 go to the Presidential Election

Campaign Fund. Otherwise, check *No*. Checking *Yes* will not change the tax or reduce the refund. On a joint return, each taxpayer chooses whether or not §3 should go to the fund.

POTENTIAL PITFALLS



Using the pre-addressed label reduces processing time. However, to protect the taxpayer's privacy, the peel-off label that he or she received in the mail with the tax return booklet does not have his or her SSN (or that of his or her spouse if filing a joint return) printed on it. Therefore, *be sure* the taxpayer's SSN (and spouse's, if applicable) is entered in the space provided on the tax form (1040, 1040A, or 1040EZ).

Further, if the taxpayer filed a joint return for 2002 and is filing a joint return for 2003 with the same spouse, *be sure* the taxpayer's and spouse's names and SSNs are entered in the same order as on the 2002 tax return.

Assembling the Return

Make sure that all forms, schedules, and attachments show the taxpayer's name and social security number. List the names in the same order that they appear on the front of the return and use the first social security (or ITIN) number that appears on the front of the return.

Attach forms and schedules behind Form 1040 according to the attachment sequence number shown in the upper right corner of the form or schedule. Items without an attachment sequence number should be placed at the end. For Form 1040A, attach any forms or schedules in order by number with Schedule EIC last.

Attach Form(s) W-2 to the left margin of the return. If any Form 1099 shows federal income tax withheld, include that amount in the payments section of the return.

When any Form 1099 shows federal income tax withheld, attach a copy to the return, along with any Form(s) W-2.

IDENTIFYING RETURNS

- If taxpayers ask about the site identification number designation at the bottom of the return in the paid preparer's section, explain that this is entered for statistical purposes. Inform the taxpayers that the site identification number does not affect the likelihood of an IRS examination (audit) of the return.
- If you prepare over 50 percent of the tax return and you are reasonably sure that the return will be filed as you prepared it, enter the site identification number at the bottom of the return in the Paid Preparer Section in the PTIN/SSN field.
- Most sites will have forms preprinted with the site identification number format entered in the Paid Preparer Section of the return. You must enter the number that has been assigned by the Territory Office for that site.
- If you do not have forms with the pre-printed site identification number format, print the appropriate site identification number for that site in the Paid Preparer Section of the return.

SITE IDENTIFICATION NUMBER

The Internal Revenue Service (IRS) will capture statistical information using the Individual Master File Report (IMF Report) and the Electronic Tax Administration (ETA) report. Based on this change, it is very important that **all returns** prepared by a volunteer tax preparation site be identified as VITA or TCE prepared.

The following procedures must be used when returns are prepared in a VITA or TCE site.

- The site identification number should be entered in the Preparer Section of the return. (See Exhibit 7).
- The following procedures must be followed when returns are prepared in a VITA or TCE site.

1. Paper Returns

- All sites will enter the letter P followed by an 8 digit site identification number that is provided by the territory office. Sites should use the overprint form with the bold P format indicated in the Paid Preparer Section. Each of the numbers represent a certain area determined by the territory office. For instance, the fifth digit of the number will be 1 for VITA, 2 for Military VITA, 3 for Co-located site, 4 for TCE and 5 for AARP.
- If you use a return without the bold P format for the number enter the assigned number in the space provided in the Paid Preparer section of the return. Forms 1040EZ, 1040A, and 1040 with the bold “P” format is available from IRS and will be ordered by each site coordinator.

2. Electronically Filed Returns

- E-file administrators will set up computers to default to the proper location on the return where the number will already be entered. Ensure the default number has been entered for the site you are working.

Exhibit 7 illustrates a site identification number entered on three tax forms.

Refund	11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund . ▶ 11a		
Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.	▶ b Routing number	<input type="text"/>	▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
	▶ d Account number	<input type="text"/>	
Amount you owe	12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22. ▶ 12		
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 22)? <input type="checkbox"/> Yes . Complete the following. <input type="checkbox"/> No		
	Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶ <input type="text"/>
Sign here	Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.		
Joint return? See page 13. Keep a copy for your records.	Your signature	Date	Your occupation
	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation
			Daytime phone number ()
Paid preparer's use only	Preparer's signature ▶	Date	Site Identification Number ▶
	Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Preparer's SSN or PTIN P10-05-1234
		Phone no. ()	
For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 24.		Cat. No. 11329W	Form 1040EZ (2003)

Refund	44 If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid . ▶ 44		
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	45a Amount of line 44 you want refunded to you . ▶ 45a		
	▶ b Routing number	<input type="text"/>	▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
	▶ d Account number	<input type="text"/>	
	46 Amount of line 44 you want applied to your 2004 estimated tax . ▶ 46		
Amount you owe	47 Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53. ▶ 47		
	48 Estimated tax penalty (see page 53). ▶ 48		
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes . Complete the following. <input type="checkbox"/> No		
	Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶ <input type="text"/>
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.		
Joint return? See page 22. Keep a copy for your records.	Your signature	Date	Your occupation
	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation
			Daytime phone number ()
Paid preparer's use only	Preparer's signature ▶	Date	Site Identification Number ▶
	Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Preparer's SSN or PTIN P10-05-1234
		Phone no. ()	
♻️ Printed on recycled paper		Form 1040A (2003)	

Refund	69	If line 68 is more than line 60, subtract line 60 from line 68. This is the amount you overpaid	69	
	70a	Amount of line 69 you want refunded to you	70a	
Direct deposit?	b	Routing number	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
See page 56 and fill in 70b, 70c, and 70d.	d	Account number		
	71	Amount of line 69 you want applied to your 2004 estimated tax	71	
Amount You Owe	72	Amount you owe. Subtract line 68 from line 60. For details on how to pay, see page 57	72	
	73	Estimated tax penalty (see page 57)	73	
Third Party Designee	Do you want to allow another person to discuss this return with the IRS (see page 58)? <input type="checkbox"/> Yes. Complete the following. <input type="checkbox"/> No			
	Designee's name	Phone no.	Personal identification number (PIN)	
Sign Here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.			
Joint return? See page 21. Keep a copy for your records.	Your signature	Date	Your occupation	Daytime phone number
	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	
Paid Preparer's Use Only	Preparer's signature	Date	Site Identification Number	Preparer's SSN or PTIN
	Firm's name (or yours if self-employed), address, and ZIP code	EIN		P10-05-1234
		Phone no.	()	

Form **1040** (2003)

QUALITY SERVICE

The goal of the TCE and VITA Programs is to provide high quality service.

On-Site Quality Review Program

Every site should have a quality review program. Properly reviewed returns will help prevent taxpayers from receiving an error notice from the IRS. At larger sites, an experienced volunteer should be designated as the quality reviewer. At small sites, volunteers may review each other's work. A Quality Review Checklist, like the one shown below, may be used for this purpose.

Quality Review Checklist

Entity

- Are the name, address, and **social security number** correct for each taxpayer on the return?
- Is the social security number(s) or ITIN(s) entered to the right of the label area?
- Is the Presidential Election Campaign Fund box(es) checked?
- Is the filing status correct? Is the box checked?
- Are the exemptions and dependents checked, listed, and added correctly?
- Are dependents' social security numbers or ITINs entered?

Income

- Are income items correctly transferred from Form W-2, Form 1099-INT, Form 1099-DIV, Form 1099-G, Form 1099-R, and Form SSA-1099 (or RRB-1099), for example?
- Is tax-exempt interest income reported? Is "TEI" written to the left of line 2 on Form 1040EZ?
- Is the taxable portion of social security benefits, IRA distributions, pensions, and/or annuity income correctly figured?
- Are there IRA withdrawals to report?
- Is there any other income to report (lottery, fees, etc.)?
- If the taxpayer paid alimony, is the recipient's social security number entered?

Tax and Credits

- Are all appropriate boxes on line 37a, Form 1040 or line 23a, Form 1040A or line 5, Form 1040EZ checked?
- Is the standard deduction correct? Complete worksheet if taxpayer is someone else's dependent.
- Is the tax correct?
- Is the taxpayer eligible to claim the credit for child and dependent care expenses, child tax credit, education credits, adoption credit, or credit for the elderly or the disabled?

Payments

- Does the tax withheld agree with the total of amounts shown on all Forms W-2, 1099-INT, 1099-DIV, and 1099-R?
- Are the estimated tax payments correct?
- Is the taxpayer eligible to claim the earned income credit?
- Is the overpayment or the amount owed correct? Does the taxpayer want any part of the refund applied to next year's estimated tax? Does the taxpayer want the refund or any part directly deposited?

Quality Review Checklist
(continued)

Other

- Did you use a calculator to check your math?
- Are all Forms W-2 and 1099 (showing tax withheld), as well as schedules and forms, attached to the return?
- Is the appropriate site identification number entered?
- Did the taxpayer(s) sign, date, and fill in his/her occupation on the return?
- Is the taxpayer eligible to claim the Earned income credit? Advanced earned income credit?

Signature Section

Make sure the taxpayer signs and dates the return before mailing. An unsigned return cannot be processed and may be sent back to the taxpayer. On a joint return, both spouses must sign, even if only one spouse had income. Also, make sure the occupation(s) of the taxpayer (or of both spouses, if married filing jointly) is entered.

If a taxpayer died before filing a return for 2003, the taxpayer's spouse or personal representative may have to file and sign a return for that taxpayer. A personal representative can be an executor, administrator, or anyone who is in charge of the deceased taxpayer's property. If the deceased taxpayer did not have to file a return but had tax withheld, a return must be filed to get a refund. The person who files the return should enter "DECEASED," the deceased taxpayer's name, and the date of death across the top of the return.

If the taxpayer's spouse died in 2003 and the taxpayer did not remarry in 2003, the taxpayer can file a joint return. (The taxpayer can also file a joint return if his or her spouse dies in 2004 before filing a 2003 return.) A joint return should show the taxpayer's spouse's 2003 income before death and the taxpayer's income for all of 2003. The taxpayer should enter "Filing as surviving spouse" in the area where the taxpayer signs the return. If someone else is the personal representative, he or she must also sign.

The surviving spouse or personal representative should promptly notify all payers of income, including financial institutions, of the taxpayer's death. This will ensure the proper reporting of income earned by the taxpayer's estate or heirs. A deceased taxpayer's social security number should not be used for tax years after the year of death, except for estate tax return purposes.

Third-Party Designee

If the taxpayer wants to allow a friend, family member, or any other person he or she chooses to discuss his or her 2003 tax return with the IRS, the taxpayer should check the “Yes” box in the “Third party designee” area of the return. Also, the taxpayer should enter the designee’s name, phone number, and any five numbers the designee chooses as his or her personal identification number (PIN).

If the taxpayer checks the “Yes” box, he or she, and his or her spouse if filing a joint return, is authorizing the IRS to call the designee to answer any questions that may arise during the processing of the return. The taxpayer is also authorizing the designee to:

- Give the IRS any information that is missing from the return,
- Call the IRS for information about the processing of the return or the status of the taxpayer’s refund or payment(s), and
- Respond to certain IRS notices that the taxpayer has shared with the designee about math errors, offsets, and return preparation. The notices will not be sent to the designee.

The taxpayer is not authorizing the designee to receive any refund check, bind the taxpayer to anything (including any additional tax liability), or otherwise represent the taxpayer before the IRS. If the taxpayer wants to expand the designee’s authorization, he or she should see Publication 947, *Practice Before the IRS and Power of Attorney*.

The authorization cannot be revoked. However, the authorization will automatically end no later than the due date (without regard to extensions) for filing the taxpayer’s 2004 tax return. This is April 15, 2005, for most people.

As a volunteer preparer you may not be designated as a “Third Party Designee.”

Ending the Interview

Make sure the taxpayer keeps a copy of all Forms W-2 and 1099 with a copy of the tax return. Advise the taxpayer to keep these copies for at least three years. As the volunteer assistor, you should not keep a copy of the return.

If an envelope has been provided for the taxpayer’s records place the copies into it. **Advise the taxpayer to bring the tax return and records back next year.**

VOLUNTEER ASSISTANCE WORKSHEET

The Volunteer Assistance Worksheet is currently under revision and was not available at publication date. Your local Stakeholder Partnerships, Education and Communication (SPEC) office will provide you with the revised Volunteer Assistance Worksheet when you attend training along with the training module that explains the new worksheet and reporting requirements.

Exercise 1

- A.** Helen paid \$500 in estimated tax to the United States Treasury. Where is this reported on Form 1040A? _____

- B.** Shirley paid \$200, the amount owed on last year's income tax return. Is this the \$200 an estimated tax payment for this year's income tax return? _____
- C.** Elmer wants his refund deposited in his checking account. What information should you enter on line 45b of Form 1040A? _____

- D.** Jennifer had tax withheld from her wages on Form W-2. She also had some withholding on her Form 1099-R. Can these items be combined and listed on one line on her tax return? _____

Exercise 2

Look at the completed Form 1040EZ shown in Exhibit 8 and identify at least 3 areas that have not been properly completed.

Form
1040EZ

Department of the Treasury—Internal Revenue Service
**Income Tax Return for Single and
Joint Filers With No Dependents 2003**

OMB No. 1545-0675

Label
(See page 14.)
Use the IRS label.
Otherwise, please print or type.

Your first name and initial Jorge	Last name Mendez
If a joint return, spouse's first name and initial Lucinda	Last name Mendez
Home address (number and street). If you have a P.O. box, see page 14. 1040 Main Street	
City, town or post office, state, and ZIP code. If you have a foreign address, see page 14. Anywhere USA 99999	

Your social security number
123 45 6789
Spouse's social security number

▲ Important! ▲
You **must** enter your SSN(s) above.

Presidential Election Campaign (page 14)

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if a joint return, want \$3 to go to this fund?

You **Spouse**
 Yes No Yes No

Income
Attach Form(s) W-2 here.
Enclose, but do not attach, any payment.

1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1	14,900	00
2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2	2	00
3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3		
4 Add lines 1, 2, and 3. This is your adjusted gross income .	4		
5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from <input type="checkbox"/> worksheet on back. No. If single , enter \$7,800. If married filing jointly , enter \$15,600. See back for explanation.	5		
6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6	14,900	00

Note. You must check Yes or No.

Payments and tax

7 Federal income tax withheld from box 2 of your Form(s) W-2.	7	1,700	00
8 Earned income credit (EIC).	8		
9 Add lines 7 and 8. These are your total payments .	9	1,700	00
10 Tax. Use the amount on line 6 above to find your tax in the tax table on pages 25–29 of the booklet. Then, enter the tax from the table on this line.	10	1,490	00

Refund
Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.

11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	11a	2	00
b Routing number <input type="text"/>	c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings		
d Account number <input type="text"/>			

Amount you owe

12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.	12		
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Third party designee

Do you want to allow another person to discuss this return with the IRS (see page 22)? **Yes**. Complete the following. **No**

Designee's name <input type="text"/>	Phone no. <input type="text"/> (<input type="text"/>) <input type="text"/>	Personal identification number (PIN) <input type="text"/>
--------------------------------------	--	---

Sign here

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.

Joint return? See page 13. Keep a copy for your records.

Your signature Lucinda Mendez	Date 1/23/04	Your occupation	Daytime phone number () () ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid preparer's use only

Preparer's signature	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code	EIN	Phone no. () () ()	

▶▶ SUMMING UP THIS LESSON ◀◀

The information for the payment section of the return comes from these sources:

- ▶ Federal income tax withheld by the employer, and
- ▶ Forms 1099, and
- ▶ Estimated tax payments paid by the taxpayer (not reported on Form 1040EZ), and
- ▶ Refundable credits.

If the amount owed is \$1,000 or more, the taxpayer may have to pay an estimated tax penalty. If there is an overpayment, the taxpayer can take one of the following courses of action:

- ▶ Receive a complete refund,
- ▶ Apply the overpayment to the next year's estimated tax, or
- ▶ Receive a partial refund and apply the remainder of the overpayment to the next year's estimated tax.

Estimated tax payments must be made if a taxpayer:

- ▶ Expects to owe \$1,000 or more in tax for 2003 after subtracting income tax withheld and credits,

AND

- ▶ Expects his or her 2004 tax withheld and credits to be less than the smaller of: 90 percent of the tax to be shown on his or her 2004 tax return or, generally, 100 percent of the tax shown on his or her 2003 tax return.

Withholding allowances for employees are reported on Form W-4. Allowances for pension or annuity recipients are reported on Form W-4P. They are figured by taking into account:

- ▶ Expected income
- ▶ Deductions
- ▶ Credits
- ▶ Adjustments to income

▶▶ **SUMMING UP THIS LESSON** ◀◀
(continued)

To finish the return:

- ▶ Consider the taxpayer's possible eligibility for Advance Earned Income Credit.
- ▶ Complete the taxpayer's identification section after you have finished the rest of the return.
- ▶ Enter the site identification number in the paid preparer's section.
- ▶ Assemble the return correctly, attaching any Forms W-2 and Forms 1099 showing federal income tax withholding.
- ▶ Check each return for completeness and accuracy.
- ▶ Submit each return for on-site quality review.
- ▶ Have the taxpayer(s) sign and date the return.

Answers to Exercise 1

- (A) Line 40
- (B) No
- (C) The routing number for his bank account, and type of account.
- (D) Yes

Answers to Exercise 2

- Wife's SSN is missing
- Presidential Election Campaign is not marked
- Husband's signature is missing
- The Site Identification Number is missing in the preparer's SSN/PTIN section of the form.
- Line 4 is blank
- Line 5 is blank
- Line 6 is incorrect
- Line 11a is incorrect
- Occupations are missing
- Spouse's signature is missing

STUDENT NOTES

CREDIT FOR CHILD AND DEPENDENT CARE EXPENSES

Lesson 7

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about the credit for child and dependent care expenses. This nonrefundable credit is one of the most commonly used credits. The requirements for claiming the credit are the same regardless of the form used. In fact, Form 2441 (used with Form 1040) and Schedule 2 (used with Form 1040A) are virtually identical. In order to qualify for this credit, the taxpayer must satisfy all six tests of eligibility.

Some taxpayers receive employer provided dependent care benefits. Dependent care benefits include amounts the employer paid directly to the taxpayer or to the care provider. These benefits can also include the fair market value of care in a day care facility provided or sponsored by the employer. The taxpayer's salary may have been reduced to pay for these benefits. The employer provided benefits will be reported on Form W-2, Box 10.

After completing this lesson you should be able to:

- Determine who is eligible for the child and dependent care credit.
- Calculate the credit, the exclusion and report the expenses on the correct form.

QUALIFYING PERSON TEST

The child and dependent care expenses must be for at least one qualifying person.

A qualifying person is:

- A child who was under the age of 13 when the care was provided and for whom a dependency exemption can be claimed. Special rules apply, however, if the parents are divorced or separated. (See next page).
- A dependent who was physically or mentally not able to care for himself or herself and for whom a dependency exemption can be claimed (or could be claimed except the person had \$3,050 or more of gross income).
- A spouse who was physically or mentally not able to care for himself or herself.

Example 1

Jim paid someone to care for his wife, Janet. Janet is physically unable to care for herself. Jim also paid to have someone prepare meals for his 12-year-old daughter, Jill. Both Janet and Jill are qualifying persons for the credit.

Example 2

Bob and Rhonda paid child care expenses for their son, Ronnie. Ronnie turned 13 on July 15. Ronnie is a qualifying person until he reached the age of 13.

Children of Divorced or Separated Parents Exception

If the taxpayer is the custodial parent, he or she can treat the child as a qualifying person for the credit even if he or she cannot claim the child's dependency exemption. If the taxpayer **is not** the custodial parent, he or she cannot treat the child as a qualifying person for the credit even if he or she can claim the child's dependency exemption.

This exception applies only if **all** the following are true:

- One or both parents had custody of the child for more than half the year.
- One or both parents provided more than half of the child's support for the year.
- Either
 1. The custodial parent signed Form 8332, Release of Claim to Exemption for Child of Divorced or Separated Parents, or a similar statement, agreeing not to claim the child's exemption for the year, or
 2. The noncustodial parent provided at least \$600 for the child's support and can claim the child's exemption under a pre-1985 decree of divorce or separate maintenance, or written agreement.

Example 3

Amanda is divorced and has custody of her 8-year-old daughter, Carrie. Amanda signed Form 8332 to allow her ex-spouse to claim the dependency exemption for Carrie. In order to work, Amanda paid child care expenses for Carrie. Carrie is a qualifying person for the credit. Amanda can claim the credit for child and dependent care expenses. The ex-spouse cannot claim the credit.

KEEPING UP A HOME TEST

To claim the credit, the taxpayer must pay more than half the cost of keeping up a home for himself or herself and one or more qualifying persons. The cost of keeping up a home normally includes property taxes, mortgage interest, rent, utility charges, home repairs, insurance on the home, and food eaten in the home. Public assistance benefits are funds provided by the state not by the taxpayer.

EARNED INCOME TEST

The taxpayer (and spouse if married) must have earned income during the year. Earned income includes wages, salaries, tips, other taxable employee compensation, net earnings from self-employment, strike benefits, and disability pay reported as wages.

A spouse is treated as having earned income for any month he or she is a full-time student or physically or mentally not able to care for himself or herself. Only one spouse can be **treated** as having earned income in any one month.

A full-time student is defined as enrolled and attending a school for the number of hours or classes the school considers full-time. The taxpayer (or spouse) must be a student for some part of five calendar months during the year.

WORK-RELATED EXPENSE TEST

Child and dependent care expenses must be work related to qualify for the credit. Expenses are considered work related only if both of the following are true:

1. The expenses allow the taxpayer (and spouse if married) to work or look for work and
2. The expenses are for a qualifying person's care.

A spouse is treated as working during any month he or she is a full-time student or is physically or mentally not able to care for himself or herself.

To be work related, the expenses must be to provide care for a qualifying person. Expenses are for the care of a qualifying person only if their main purpose is the person's well being and protection.

Expenses for care do not include amounts paid for food, clothing, education, and entertainment. However, small amounts paid for these items can be included if they are incident to and cannot be separated from the cost of care.

Education. Expenses to attend first grade or a higher grade are not expenses for care.

Camp. The cost of sending a child to an overnight camp is not considered a work-related expense.

Payments to relatives. Do not count amounts paid to:

1. A dependent for whom the taxpayer (or spouse if married) can claim as an exemption, or
2. The taxpayer's child who is under age 19 at the end of the year, even if he or she is not the taxpayer's dependent

JOINT RETURN TEST

Generally, a married couple must file a joint return to take the credit. However, if the taxpayer is legally separated or living apart from his or her spouse, the taxpayer may be able to file a separate return and still take the credit.

If the taxpayer's filing status is married filing separately and all of the following apply, the taxpayer is considered unmarried for purposes of figuring the credit:

1. The taxpayer lived apart from his or her spouse during the last six months of the year, and
2. The qualifying person lived in the taxpayer's home for more than half of the year, and
3. The taxpayer provided over half the cost of keeping up the home, and
4. The taxpayer met the other five tests for eligibility to take the credit.

PROVIDER IDENTIFICATION TEST

The taxpayer must provide the care provider's name, address, and taxpayer identification number. If the taxpayer is unable to provide this information or if the information is incorrect, he or she must show they used due diligence to obtain the information.

Due Diligence. The taxpayer can show due diligence by getting and keeping any of the following documents:

1. Form W-10, Dependent Care Provider's Identification and Certification.
2. Copy of the provider's social security card.
3. Copy of the provider's driver's license if it includes the social security number.
4. A copy of the provider's Form W-4 if the provider is the taxpayer's household employee.
5. A copy of the statement furnished by the taxpayer's employer if the provider is a dependent care plan.
6. A letter or invoice from the provider if it shows the name, address, and taxpayer identification number (EIN or SSN).

Provider Refusal. If the care provider refuses to give the taxpayer the identifying information, report whatever information is available, enter “see page 2” for the missing information, and provide a statement at the bottom of page 2 of Form 2441 or Schedule 2.

LIMIT ON EXPENSES

The amount of expenses eligible for the credit is limited to the lowest of the following amounts for the year.

- The lower paid spouse’s earned income (in the case of married taxpayers).
- The single taxpayer’s earned income.
- The actual expenses paid.
- The overall limit of \$3,000 for one qualifying person or \$6,000 for two or more qualifying persons.

Example 4

Mark earned \$14,000. His wife, Evelyn, earned \$5,600. Day care expenses for their three-year-old daughter were \$2,200. The maximum amount of qualifying child care expenses is \$2,200. This is the lowest of:

- The lower paid spouse’s earnings (\$5,600),
- The amount actually paid (\$2,200), and
- The overall limit for one qualifying person (\$3,000).

Some taxpayers receive dependent care benefits from their employers. If so, the overall limit of \$3,000/\$6,000 is reduced, dollar for dollar, by any reimbursement excluded from the taxpayer’s income. The amount of dependent care benefits received is shown in box 10 of Form W-2.

Example 5

Geraldine has one dependent child, Donald, who is 6 years old. She paid \$2,900 in qualified expenses. Box 10 of Geraldine’s Form W-2 shows she received \$1,400 during the year from her employer’s dependent care assistance program. Because she received dependent care benefits, Part III of Form 2441 must be completed before completing Part II.

Nonworking Spouse

Married taxpayers usually must both work in order to claim the credit. However, if a spouse is either a full-time student during any five months of the year, or is not capable of caring for himself or herself for some period during the year, a credit can still be claimed. To figure the credit, the earned income for each month the spouse is either a full-time student or disabled is considered to be at least:

ALERT



Beginning in 2003, the maximum expenses for the credit increased to \$3,000 for one qualifying person and \$6,000 for two or more qualifying persons.

ALERT



Beginning in 2003, the amount of earned income for the nonworking spouse increased to \$250 with one qualifying person and \$500 for two or more qualifying persons.

- \$250 with one qualifying person in the home, or
- \$500 with two or more qualifying persons in the home.

Example 6

Janice worked full time. Her husband, Ken, was a full-time student from January through May. Their son, Jason, was in daycare while Ken attended school. Ken's earned income for the time he attended school is considered to be \$1,250 (5 months \times \$250).

Exercise 1

- A. Karen earned \$18,000. She paid \$3,200 for child care expenses for her four-year-old daughter, Crystal. What is the maximum amount of child care expenses Karen can claim? _____
- B. Andrea is married to Bill. They have a seven-year-old son, Charles. Charles lived with Andrea for the entire year. Andrea paid all the expenses of keeping up the home for herself and Charles. Andrea also paid for before-school and after-school child care. Her total child care expenses were \$1,800. Bill left the area 18 months ago. He did not live with Andrea at all during 2003, but he did send \$1,200 in child support. Andrea and Bill will file separate returns. Andrea signed Form 8332 to allow Bill to claim the dependency exemption for Charles. Who can claim the credit for child and dependent care expenses? _____
- C. Ellen is divorced. She has custody of her 12-year-old daughter, Terri. Terri takes care of herself after school. In the summer, Ellen spends \$2,000 to send Terri to a two week long overnight camp. Are the camp expenses qualified expenses for the credit for child and dependent care credit? _____

The credit is a percentage of qualifying expenses. For taxpayers with adjusted gross incomes of \$15,000 or less, the credit is 35 percent of qualifying expenses. As adjusted gross income increases, the percentage decreases. The lowest percentage is 20 percent for an AGI equal to or greater than \$43,000. There is no upper limitation on income for this credit. The tables on Schedule 2 (Form 1040A) and on Form 2441 show the percentage for each adjusted gross income bracket. After the credit is figured using Form 2441 or Schedule 2, it is reported on Form 1040, line 45, or Form 1040A, line 29.

Example 7

David A. and Edith B. Fullerton are married and file a joint return. Last year, they paid \$3,500 for the care of their son, Jonathan. The payment was made to Karen's Kiddie Care, 456 Chapman Avenue, Wilmington, DE 19850 (EIN 00-0009101). The \$3,500 payment includes a \$1,000 dependent care benefit Edith received from her employer. Edith earned \$18,979 and David earned \$22,450 last year. Their adjusted gross income is \$39,429 and their tax liability is \$2,492.

Exhibits 1 and 2 show the completed Form 2441 (Form 1040) for David and Edith.

ALERT

Beginning in 2003, the credit percentages increased and the maximum AGI amount that qualifies for the highest percentage increased to \$15,000.

Form **2441**
 Department of the Treasury
 Internal Revenue Service

Child and Dependent Care Expenses

OMB No. 1545-0068
2003
 Attachment
 Sequence No. **21**

▶ Attach to Form 1040.
 ▶ See separate instructions.

Name(s) shown on Form 1040: **David A. and Edith B. Fullerton**
 Your social security number: **000 00 2935**

Before you begin: You need to understand the following terms. See **Definitions** on page 1 of the instructions.

- **Dependent Care Benefits**
- **Qualifying Person(s)**
- **Qualified Expenses**
- **Earned Income**

Part I **Persons or Organizations Who Provided the Care**—You must complete this part.
 (If you need more space, use the bottom of page 2.)

1	(a) Care provider's name	(b) Address (number, street, apt. no., city, state, and ZIP code)	(c) Identifying number (SSN or EIN)	(d) Amount paid (see instructions)
	Karen's Kiddie Car	456 Chapman Ave Wilmington DE 19850	00-0009101	3,500

Did you receive dependent care benefits?

No → Complete only Part II below.

Yes → Complete Part III on the back next.

Caution. If the care was provided in your home, you may owe employment taxes. See the instructions for Form 1040, line 59.

Part II **Credit for Child and Dependent Care Expenses**

2 Information about your **qualifying person(s)**. If you have more than two qualifying persons, see the instructions.

(a) Qualifying person's name		(b) Qualifying person's social security number	(c) Qualified expenses you incurred and paid in 2003 for the person listed in column (a)
First	Last		
Jonathan	Fullerton	000 00 2194	2,500

3 Add the amounts in column (c) of line 2. Do not enter more than \$3,000 for one qualifying person or \$6,000 for two or more persons. If you completed Part III, enter the amount from line 26	3		2,000																																																												
4 Enter your earned income	4		22,450																																																												
5 If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions); all others , enter the amount from line 4	5		18,979																																																												
6 Enter the smallest of line 3, 4, or 5	6		2,000																																																												
7 Enter the amount from Form 1040, line 35 7 39,429																																																															
8 Enter on line 8 the decimal amount shown below that applies to the amount on line 7																																																															
<table style="width: 100%; border-collapse: collapse;"> <tr> <th colspan="3" style="text-align: left;">If line 7 is:</th> <th colspan="3" style="text-align: left;">If line 7 is:</th> </tr> <tr> <th style="text-align: left;">Over</th> <th style="text-align: left;">But not over</th> <th style="text-align: left;">Decimal amount is</th> <th style="text-align: left;">Over</th> <th style="text-align: left;">But not over</th> <th style="text-align: left;">Decimal amount is</th> </tr> <tr> <td>\$0—15,000</td> <td></td> <td>.35</td> <td>\$29,000—31,000</td> <td></td> <td>.27</td> </tr> <tr> <td>15,000—17,000</td> <td></td> <td>.34</td> <td>31,000—33,000</td> <td></td> <td>.26</td> </tr> <tr> <td>17,000—19,000</td> <td></td> <td>.33</td> <td>33,000—35,000</td> <td></td> <td>.25</td> </tr> <tr> <td>19,000—21,000</td> <td></td> <td>.32</td> <td>35,000—37,000</td> <td></td> <td>.24</td> </tr> <tr> <td>21,000—23,000</td> <td></td> <td>.31</td> <td>37,000—39,000</td> <td></td> <td>.23</td> </tr> <tr> <td>23,000—25,000</td> <td></td> <td>.30</td> <td>39,000—41,000</td> <td></td> <td>.22</td> </tr> <tr> <td>25,000—27,000</td> <td></td> <td>.29</td> <td>41,000—43,000</td> <td></td> <td>.21</td> </tr> <tr> <td>27,000—29,000</td> <td></td> <td>.28</td> <td>43,000—No limit</td> <td></td> <td>.20</td> </tr> </table>	If line 7 is:			If line 7 is:			Over	But not over	Decimal amount is	Over	But not over	Decimal amount is	\$0—15,000		.35	\$29,000—31,000		.27	15,000—17,000		.34	31,000—33,000		.26	17,000—19,000		.33	33,000—35,000		.25	19,000—21,000		.32	35,000—37,000		.24	21,000—23,000		.31	37,000—39,000		.23	23,000—25,000		.30	39,000—41,000		.22	25,000—27,000		.29	41,000—43,000		.21	27,000—29,000		.28	43,000—No limit		.20	8		× .22
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9 Multiply line 6 by the decimal amount on line 8. If you paid 2002 expenses in 2003, see the instructions	9		440																																																												
10 Enter the amount from Form 1040, line 43, minus any amount on Form 1040, line 44	10		2,492																																																												
11 Credit for child and dependent care expenses. Enter the smaller of line 9 or line 10 here and on Form 1040, line 45	11		440																																																												

Part III Dependent Care Benefits

12	Enter the total amount of dependent care benefits you received for 2003. This amount should be shown in box 10 of your W-2 form(s). Do not include amounts that were reported to you as wages in box 1 of Form(s) W-2	12	1,000
13	Enter the amount forfeited, if any (see the instructions)	13	0
14	Subtract line 13 from line 12	14	1,000
15	Enter the total amount of qualified expenses incurred in 2003 for the care of the qualifying person(s)	15	3,500
16	Enter the smaller of line 14 or 15	16	1,000
17	Enter your earned income	17	22,450
18	Enter the amount shown below that applies to you. <ul style="list-style-type: none"> • If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions for line 5). • If married filing separately, see the instructions for the amount to enter. • All others, enter the amount from line 17. 	18	18,979
19	Enter the smallest of line 16, 17, or 18	19	1,000
20	Excluded benefits. Enter here the smaller of the following: <ul style="list-style-type: none"> • The amount from line 19 or • \$5,000 (\$2,500 if married filing separately and you were required to enter your spouse's earned income on line 18). 	20	1,000
21	Taxable benefits. Subtract line 20 from line 14. Also, include this amount on Form 1040, line 7. On the dotted line next to line 7, enter "DCB"	21	0

To claim the child and dependent care credit, complete lines 22–26 below.

22	Enter \$3,000 (\$6,000 if two or more qualifying persons)	22	3,000
23	Enter the amount from line 20	23	1,000
24	Subtract line 23 from line 22. If zero or less, stop . You cannot take the credit. Exception. If you paid 2002 expenses in 2003, see the instructions for line 9	24	2,000
25	Complete line 2 on the front of this form. Do not include in column (c) any benefits shown on line 20 above. Then, add the amounts in column (c) and enter the total here	25	2,500
26	Enter the smaller of line 24 or 25. Also, enter this amount on line 3 on the front of this form and complete lines 4–11	26	2,000

Exercise 2

Sam L. (000-00-9832) and Sue D. Windham are married and will file a joint return. They have two dependent children whom they send to day care to allow both parents to work. Sam's earned income is \$18,500 and Sue's earned income is \$19,350. Their AGI (Form 1040, line 35) is \$37,850 and their tax liability (Form 1040, line 43) is \$1,723.

During 2003, they paid The Learning Center day care (496 Irvine Road, Newark, NJ 07102, EIN 11-0007965) \$5,450 to care for their children. The Windhams paid \$2,950 of the total and Sue's employer paid \$2,500 under a dependent care benefits program. The \$2,500 is in Box 10 of Sue's Form W-2.

The children and the amounts paid for day care are as follows:

Doug	SSN 000-00-2387	\$3,000	\$1,250 dependent care benefit
Sally	SSN 000-00-4923	\$2,450	\$1,250 dependent care benefit

Complete their Form 1040, Form 2441 (Exhibits 3 and 4).

TAXWISE HINTS

Use the flow charts in Publication 4012, VITA/TCE Resource Guide, to determine credit eligibility. For each qualifying child, check the "DC" box on the Main Information Sheet, Dependents/Non-dependents box. TaxWise will add a Form 2441 or Schedule 2 to the forms tree. Complete all entries annotated in red. TaxWise will then calculate any exclusion amounts, calculate the credit, complete the form and insert the credit amount on Form 1040 or Form 1040A.

▶▶ SUMMING UP THIS LESSON ◀◀

The Credit for Child and Dependent Care Expenses is a non-refundable credit which allows a taxpayer to reduce their tax liability for a portion of the expenses.

Beginning in 2003, the maximum expense amount increased to \$3,000 for one qualifying person and \$6,000 for two or more qualifying persons.

The maximum credit rate increased from 30% to 35%.

A taxpayer must satisfy the six tests to qualify for the credit. The tests are the qualifying person test; the keeping up a home test; the earned income test; the work-related expense test; the joint return test; and the provider identification test.

The credit is calculated and reported on Form 2441 (Form 1040) or Schedule 2 (Form 1040A).

Form 2441 Department of the Treasury Internal Revenue Service	Child and Dependent Care Expenses ▶ Attach to Form 1040. ▶ See separate instructions.	OMB No. 1545-0068 2003 Attachment Sequence No. 21																																																								
Name(s) shown on Form 1040		Your social security number																																																								
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<p>Part I Persons or Organizations Who Provided the Care—You must complete this part. (If you need more space, use the bottom of page 2.)</p>																																																										
1	(a) Care provider's name	(b) Address (number, street, apt. no., city, state, and ZIP code)	(c) Identifying number (SSN or EIN)	(d) Amount paid (see instructions)																																																						
<table border="1" style="margin: auto;"> <tr> <td style="padding: 5px;">Did you receive dependent care benefits?</td> <td style="padding: 5px;">No</td> <td style="padding: 5px;">▶ Complete only Part II below.</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">Yes</td> <td style="padding: 5px;">▶ Complete Part III on the back next.</td> </tr> </table>					Did you receive dependent care benefits?	No	▶ Complete only Part II below.		Yes	▶ Complete Part III on the back next.																																																
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11	Credit for child and dependent care expenses. Enter the smaller of line 9 or line 10 here and on Form 1040, line 45			11																																																						
<p>For Paperwork Reduction Act Notice, see page 3 of the instructions. Cat. No. 11862M Form 2441 (2003)</p>																																																										

Part III Dependent Care Benefits

12 Enter the total amount of dependent care benefits you received for 2003. This amount should be shown in box 10 of your W-2 form(s). Do not include amounts that were reported to you as wages in box 1 of Form(s) W-2	12		
13 Enter the amount forfeited, if any (see the instructions)	13		
14 Subtract line 13 from line 12	14		
15 Enter the total amount of qualified expenses incurred in 2003 for the care of the qualifying person(s)	15		
16 Enter the smaller of line 14 or 15	16		
17 Enter your earned income	17		
18 Enter the amount shown below that applies to you. <ul style="list-style-type: none"> • If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions for line 5). • If married filing separately, see the instructions for the amount to enter. • All others, enter the amount from line 17. 	18		
19 Enter the smallest of line 16, 17, or 18	19		
20 Excluded benefits. Enter here the smaller of the following: <ul style="list-style-type: none"> • The amount from line 19 or • \$5,000 (\$2,500 if married filing separately and you were required to enter your spouse's earned income on line 18). 	20		
21 Taxable benefits. Subtract line 20 from line 14. Also, include this amount on Form 1040, line 7. On the dotted line next to line 7, enter "DCB"	21		

Proof as of July 21, 2003 (subject to change)

To claim the child and dependent care credit, complete lines 22–26 below.

22 Enter \$3,000 (\$6,000 if two or more qualifying persons)	22		
23 Enter the amount from line 20	23		
24 Subtract line 23 from line 22. If zero or less, stop . You cannot take the credit. Exception. If you paid 2002 expenses in 2003, see the instructions for line 9	24		
25 Complete line 2 on the front of this form. Do not include in column (c) any benefits shown on line 20 above. Then, add the amounts in column (c) and enter the total here	25		
26 Enter the smaller of line 24 or 25. Also, enter this amount on line 3 on the front of this form and complete lines 4–11	26		

Exercise 1

- (A) \$3,000, which is the lowest of: earned income (\$18,000); the amount actually paid (\$3,200); and the limit of one qualifying person (\$3,000).
- (B) Andrea. Even though she is filing a separate tax return, she is eligible for the credit because she signed a Form 8332 to allow her husband to claim the dependency exemption..
- (C) No.

CREDIT FOR CHILD AND DEPENDENT CARE EXPENSES

ANSWERS TO EXERCISES

Lesson 7

Exhibit 5 Exercise 2

The Windham's Form 2441, page 1

Form 2441 Department of the Treasury Internal Revenue Service	Child and Dependent Care Expenses ▶ Attach to Form 1040. ▶ See separate instructions.	OMB No. 1545-0068 2003 Attachment Sequence No. 21																																																								
Name(s) shown on Form 1040 Sam L. and Sue D. Windham		Your social security number 000 00 9832																																																								
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<p>Part I Persons or Organizations Who Provided the Care—You must complete this part. (If you need more space, use the bottom of page 2.)</p>																																																										
1	(a) Care provider's name The Learning Cente	(b) Address (number, street, apt. no., city, state, and ZIP code) 496 Irvine Rd Newark NJ 07102	(c) Identifying number (SSN or EIN) 11-0007965	(d) Amount paid (see instructions) 5,450																																																						
Did you receive dependent care benefits? <div style="display: flex; justify-content: space-around; margin-top: 5px;"> <div style="border: 1px solid black; padding: 2px;">No</div> <div style="border: 1px solid black; padding: 2px;">Yes</div> </div>																																																										
Complete only Part II below. Complete Part III on the back next.																																																										
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<p>2 Information about your qualifying person(s). If you have more than two qualifying persons, see the instructions.</p>																																																										
	(a) Qualifying person's name First Last	(b) Qualifying person's social security number	(c) Qualified expenses you incurred and paid in 2003 for the person listed in column (a)																																																							
	Doug	Windham	000 00 2387	1,750																																																						
	Sally	Windham	000 00 4923	1,200																																																						
3	Add the amounts in column (c) of line 2. Do not enter more than \$3,000 for one qualifying person or \$6,000 for two or more persons. If you completed Part III, enter the amount from line 26			2,950																																																						
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5	If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions); all others , enter the amount from line 4			19,350																																																						
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7	Enter the amount from Form 1040, line 35			37,850																																																						
8	Enter on line 8 the decimal amount shown below that applies to the amount on line 7			× .23																																																						
If line 7 is: <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 15%;">Over</th> <th style="width: 15%;">But not over</th> <th style="width: 15%;">Decimal amount is</th> <th style="width: 15%;">Over</th> <th style="width: 15%;">But not over</th> <th style="width: 15%;">Decimal amount is</th> </tr> </thead> <tbody> <tr> <td>\$0—15,000</td> <td></td> <td>.35</td> <td>\$29,000—31,000</td> <td></td> <td>.27</td> </tr> <tr> <td>15,000—17,000</td> <td></td> <td>.34</td> <td>31,000—33,000</td> <td></td> <td>.26</td> </tr> <tr> <td>17,000—19,000</td> <td></td> <td>.33</td> <td>33,000—35,000</td> <td></td> <td>.25</td> </tr> <tr> <td>19,000—21,000</td> <td></td> <td>.32</td> <td>35,000—37,000</td> <td></td> <td>.24</td> </tr> <tr> <td>21,000—23,000</td> <td></td> <td>.31</td> <td>37,000—39,000</td> <td></td> <td>.23</td> </tr> <tr> <td>23,000—25,000</td> <td></td> <td>.30</td> <td>39,000—41,000</td> <td></td> <td>.22</td> </tr> <tr> <td>25,000—27,000</td> <td></td> <td>.29</td> <td>41,000—43,000</td> <td></td> <td>.21</td> </tr> <tr> <td>27,000—29,000</td> <td></td> <td>.28</td> <td>43,000—No limit</td> <td></td> <td>.20</td> </tr> </tbody> </table>					Over	But not over	Decimal amount is	Over	But not over	Decimal amount is	\$0—15,000		.35	\$29,000—31,000		.27	15,000—17,000		.34	31,000—33,000		.26	17,000—19,000		.33	33,000—35,000		.25	19,000—21,000		.32	35,000—37,000		.24	21,000—23,000		.31	37,000—39,000		.23	23,000—25,000		.30	39,000—41,000		.22	25,000—27,000		.29	41,000—43,000		.21	27,000—29,000		.28	43,000—No limit		.20
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9	Multiply line 6 by the decimal amount on line 8. If you paid 2002 expenses in 2003, see the instructions			679																																																						
10	Enter the amount from Form 1040, line 43, minus any amount on Form 1040, line 44			1,723																																																						
11	Credit for child and dependent care expenses. Enter the smaller of line 9 or line 10 here and on Form 1040, line 45			679																																																						
<p>For Paperwork Reduction Act Notice, see page 3 of the instructions. Cat. No. 11862M Form 2441 (2003)</p>																																																										

CREDIT FOR CHILD AND DEPENDENT CARE EXPENSES

ANSWERS TO EXERCISES

Lesson 7

Exhibit 6 Exercise 2

The Windham's Form 2441, page 2

Form 2441 (2003)

Page 2

Part III Dependent Care Benefits

12	Enter the total amount of dependent care benefits you received for 2003. This amount should be shown in box 10 of your W-2 form(s). Do not include amounts that were reported to you as wages in box 1 of Form(s) W-2	12	2,500
13	Enter the amount forfeited, if any (see the instructions)	13	0
14	Subtract line 13 from line 12	14	2,500
15	Enter the total amount of qualified expenses incurred in 2003 for the care of the qualifying person(s)	15	5,450
16	Enter the smaller of line 14 or 15	16	2,500
17	Enter your earned income	17	18,500
18	Enter the amount shown below that applies to you. <ul style="list-style-type: none"> • If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions for line 5). • If married filing separately, see the instructions for the amount to enter. • All others, enter the amount from line 17. 	18	19,350
19	Enter the smallest of line 16, 17, or 18	19	2,500
20	Excluded benefits. Enter here the smaller of the following: <ul style="list-style-type: none"> • The amount from line 19 or • \$5,000 (\$2,500 if married filing separately and you were required to enter your spouse's earned income on line 18). 	20	2,500
21	Taxable benefits. Subtract line 20 from line 14. Also, include this amount on Form 1040, line 7. On the dotted line next to line 7, enter "DCB"	21	0

To claim the child and dependent care credit, complete lines 22-26 below.

22	Enter \$3,000 (\$6,000 if two or more qualifying persons)	22	6,000
23	Enter the amount from line 20	23	2,500
24	Subtract line 23 from line 22. If zero or less, stop . You cannot take the credit. Exception. If you paid 2002 expenses in 2003, see the instructions for line 9	24	3,500
25	Complete line 2 on the front of this form. Do not include in column (c) any benefits shown on line 20 above. Then, add the amounts in column (c) and enter the total here	25	2,950
26	Enter the smaller of line 24 or 25. Also, enter this amount on line 3 on the front of this form and complete lines 4-11	26	2,950

Printed on recycled paper

Form 2441 (2003)

STUDENT NOTES

INTRODUCTION AND OBJECTIVES

For tax year 2003, there are nine different tax benefits for higher education. Some of these benefits are not taxed (i.e., Coverdell education savings account, qualified tuition program, early IRA withdrawals, employer provided educational assistance and education savings bond program). The student loan interest deduction and tuition and fees deduction were covered in Lesson 3, Adjustments. In this lesson you will learn about the two education credits: Hope credit and the lifetime learning credit.

After completing this lesson, you should be able to:

- Calculate the Hope credit on Form 8863.
- Calculate the lifetime learning credit on Form 8863.

GENERAL REQUIREMENTS

Taxpayers can claim the **Hope Scholarship Credit** (Hope credit) and the **Lifetime Learning Credit** for higher education expenses paid in 2003 for an eligible student. Both credits are **nonrefundable** and can be claimed on either Form 1040 or Form 1040A. These two credits are also called **education credits**.

To claim either of the education credits the taxpayer must:

- File using any filing status other than married filing separately,
- Meet all of the general requirements,
- Meet all of the specific requirements for the individual credit, and
- Meet the income limits.

The general requirements provide that the taxpayer must have incurred **qualified expenses** for an **eligible student** to attend **an eligible educational institution** during the tax year.

Qualified Expenses

The Hope credit and the lifetime learning credit are based on qualified tuition and related expenses the taxpayer pays for himself or herself, the taxpayer's spouse, or dependents the taxpayer claims on his or her tax return.

Qualified tuition and related expenses are tuition and fees required for enrollment or attendance at an eligible educational institution and generally **include fees for**:

- Course-related books, supplies and equipment, and
- Student activities.

The fees must be paid **to the institution** as a condition of enrollment or attendance.

Qualified tuition and related expenses **do not include** the cost of:

- Insurance,
- Medical expenses (including student health fees),
- Room and board,
- Transportation or similar personal, living, or family expenses, **even if** the fees must be paid to the institution as a condition of enrollment or attendance.

When considering qualified tuition and related expenses for the Hope credit, the cost of courses for athletics, sports, games, hobbies or noncredit courses are not used unless the course is part of the student's degree program. However, when computing the qualified tuition and related expenses for the lifetime learning credit, these types of expenses are includible if the course was taken to acquire or improve the job skills of the student.

If a taxpayer **prepaid** qualified tuition and related expenses for an academic period that begins in the first three months of the following year, he or she can use the prepaid amount in figuring the credit.

Example 1

Thomas pays \$1,500 in December 2003 for qualified tuition for the winter semester that begins in January 2004. He can use the \$1,500 paid in December of 2003 to compute his credit for 2003.

Payments with borrowed funds.

Taxpayers can claim the Hope credit and lifetime learning credit for qualified tuition and related expenses paid with the proceeds of a loan. Use the expenses to figure the credit for the year in which the expenses are paid, not the year in which the loan is repaid.

Eligible Student

The taxpayer, the taxpayer's spouse, or the taxpayer's dependent (for whom the taxpayer claims a dependency exemption) can be an eligible student.

In addition, for the Hope credit, the student must be:

- Enrolled in a program that leads to a degree, certificate or other recognized educational credential.
- Taking at least one-half of the normal full-time workload for his or her course of study for at least one academic period beginning during the calendar year.
- Enrolled for one of the first two years of his or her postsecondary education.
- Free of any felony conviction for possessing or distributing a controlled substance.

WHO CAN CLAIM EXPENSES?

The taxpayer must claim a dependent exemption for the eligible student in order to claim an education credit. Either the taxpayer or the dependent, but not both, can claim an education credit for that dependent's higher education expenses.

If the taxpayer...	Then only...
Claims an exemption on the tax return for a dependent who is an eligible student	The taxpayer can claim the Hope or lifetime learning credit based on that student's expenses. The student cannot claim the credit.
Does not claim an exemption for a dependent who is an eligible student (even if entitled to the exemption)	The student can claim the Hope or lifetime learning credit. The taxpayer cannot claim the student's expenses.

If someone other than the taxpayer, the taxpayer's spouse, or the dependent (such as a relative or former spouse) makes a payment directly to the eligible educational institution to pay for qualified tuition and related expenses, the student is treated as receiving the payment from the other person. The student is considered to have paid the qualified tuition and related expenses to the eligible institution. If the taxpayer claims an exemption for the student, the taxpayer is considered to have paid the expenses. If the taxpayer does not claim a dependent exemption for the student, the student may claim the credit.

Example 2

Mary Birch paid her grandson, Todd's, tuition for 2003 directly to the university. For purposes of claiming the Hope credit, her grandson is treated as receiving the money as a gift and in turn paying his qualified tuition and related expenses himself. Unless an exemption for Todd is claimed on someone else's return, only Todd can use the payment to claim the Hope credit. If Todd's parents claim his exemption, they may be able to use the expenses to claim the Hope credit. If anyone else claims an exemption for Todd, Todd cannot claim a Hope credit.

Eligible Educational Institution

An eligible educational institution is generally any accredited public, nonprofit, or proprietary (private) postsecondary institution eligible to participate in the student aid programs administered by the Department of Education. Most universities and colleges, including community colleges, meet these requirements.

Income Requirements

The Hope credit and the lifetime learning credit are phased out (gradually reduced) if the taxpayer's modified AGI is over \$41,000 (over \$83,000 if married filing jointly). If a taxpayer's modified AGI is \$51,000 or more (\$103,000 or more if married filing jointly), no credit is allowed. Education credits are not allowed to persons who are married filing separately.

Modified Adjusted Gross Income (MAGI)

For most taxpayers, modified adjusted gross income (MAGI) is adjusted gross income (AGI) as figured on their federal income tax return. MAGI when using Form 1040A is the AGI on line 22 of that form. MAGI when using Form 1040 is the AGI on line 35 of that form, modified by adding back any:

- 1) Foreign earned income exclusion
- 2) Foreign housing exclusion
- 3) Exclusion of income for bona fide residents of America Samoa, and
- 4) Exclusion of income from Puerto Rico.

A Hope credit can be claimed for *each* eligible student that is claimed on the taxpayer's return.

Credit Amounts

The Hope credit is figured on Form 8863, *Education Credits (Hope and Lifetime Learning Credits)*. The maximum Hope credit is \$1,500 *per student* for each of the first two taxable years of his or her postsecondary education. For each eligible student who qualifies for the Hope credit:

- If the expenses are \$1,000 or less, the credit is the amount of the expenses,
- If the expenses are \$2,000 or more, the credit is \$1,500, and
- If the expenses are between \$1,000 and \$2,000, the credit is \$1,000 plus one-half of the expenses over \$1,000. For example, if the expenses are \$1,500, the credit is \$1,250 (\$1,000 plus one-half of \$500).

Example 3

Sue and Ted paid \$7,000 in qualified tuition and fees for their daughter to attend the local university. They determined it would be more beneficial for them to take the Hope Credit rather than the Tuition and Fees Deduction. Their Form 8863 is shown in Exhibit 1.

Form **8863**
Department of the Treasury
Internal Revenue Service

Education Credits
(Hope and Lifetime Learning Credits)

▶ See instructions.
▶ Attach to Form 1040 or Form 1040A.

OMB No. 1545-1618

2003
Attachment
Sequence No. **50**

Name(s) shown on return

Sue and Ted Green

Your social security number

000 00 9876

Caution: You **cannot** take both an education credit and the tuition and fees deduction (Form 1040, line 26, or Form 1040A, line 19) for the **same student** in the same year.

Part I Hope Credit. Caution: You cannot take the Hope credit for more than **2** tax years for the **same student**.

1	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions). Do not enter more than \$2,000 for each student.	(d) Enter the smaller of the amount in column (c) or \$1,000	(e) Subtract column (d) from column (c)	(f) Enter one-half of the amount in column (e)
	Mary Green	000 00 1234	2,000	1,000	1,000	500
2	Add the amounts in columns (d) and (f)			2	1,000	500
3	Tentative Hope credit. Add the amounts on line 2, columns (d) and (f). If you are claiming the lifetime learning credit for another student, go to Part II; otherwise, go to Part III ▶			3	1,500	

Part II Lifetime Learning Credit

4	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions)
Caution: You cannot take the Hope credit and the lifetime learning credit for the same student in the same year.			
5	Add the amounts on line 4, column (c), and enter the total		5
6	Enter the smaller of line 5 or \$10,000		6
7	Tentative lifetime learning credit. Multiply line 6 by 20% (.20) and go to Part III ▶		7

Part III Allowable Education Credits

8	Tentative education credits. Add lines 3 and 7	8	1,500
9	Enter: \$103,000 if married filing jointly; \$51,000 if single, head of household, or qualifying widow(er)	9	103,000
10	Enter the amount from Form 1040, line 35 *, or Form 1040A, line 22	10	35,000
11	Subtract line 10 from line 9. If zero or less, stop ; you cannot take any education credits	11	68,000
12	Enter: \$20,000 if married filing jointly; \$10,000 if single, head of household, or qualifying widow(er)	12	20,000
13	If line 11 is equal to or more than line 12, enter the amount from line 8 on line 14 and go to line 15. If line 11 is less than line 12, divide line 11 by line 12. Enter the result as a decimal (rounded to at least three places)	13	×
14	Multiply line 8 by line 13 ▶	14	1,500
15	Enter the amount from Form 1040, line 43, or Form 1040A, line 28	15	3,349
16	Enter the total, if any, of your credits from Form 1040, lines 44 through 46, or Form 1040A, lines 29 and 30	16	0
17	Subtract line 16 from line 15. If zero or less, stop ; you cannot take any education credits ▶	17	3,349
18	Education credits. Enter the smaller of line 14 or line 17 here and on Form 1040, line 47, or Form 1040A, line 31 ▶	18	1,500

*See Pub. 970 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

The lifetime learning credit is based on the total qualified education expenses paid by the taxpayer and not on the number of eligible students. Education expenses are qualified for the lifetime learning credit if they are:

- For courses taken as part of a postsecondary degree program, or
- For courses that are not part of a postsecondary degree program, but that are taken to improve or acquire job skills.

Example 4

Samantha, a professional photographer, enrolls in an advanced photography course at a local community college. Although the course is not part of a degree program, she enrolls in it to improve her job skills. The course fee paid by Samantha is considered qualified tuition for the purpose of claiming the lifetime learning credit.

Example 5

Cleve, an engineer, plans to vacation in Europe next year. In preparation for the trip, he enrolls in a noncredit photography class at a local community college. Because Cleve is not taking the course as part of a degree program or to acquire or improve his job skills, the cost of the course is not a qualifying expense for claiming the lifetime learning credit.

Credit amounts

The lifetime learning credit is also figured on Form 8863. The maximum amount of the credit is \$2,000 per taxpayer for all eligible students. The credit amount is figured by multiplying total qualified educational expenses, up to \$10,000, by 20%.

Example 6

Judy Green is single and took a course at the local college to recertify her to teach in public schools. Her qualified tuition expenses were \$500. She chooses to take the lifetime learning credit rather than the Tuition and Fees Deduction. Her completed Form 8863 is shown in Exhibit 2.

ALERT

The maximum lifetime learning credit increased from \$1,000 to \$2,000 for 2003.

Form **8863**
 Department of the Treasury
 Internal Revenue Service

Education Credits
(Hope and Lifetime Learning Credits)

▶ See instructions.
 ▶ Attach to Form 1040 or Form 1040A.

OMB No. 1545-1618

2003

Attachment
 Sequence No. **50**

Name(s) shown on return

Judy Green

Your social security number

000 00 2586

Caution: You **cannot** take both an education credit and the tuition and fees deduction (Form 1040, line 26, or Form 1040A, line 19) for the **same student** in the same year.

Part I Hope Credit. Caution: You cannot take the Hope credit for more than **2** tax years for the **same student**.

1	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions). Do not enter more than \$2,000 for each student.	(d) Enter the smaller of the amount in column (c) or \$1,000	(e) Subtract column (d) from column (c)	(f) Enter one-half of the amount in column (e)	
2	Add the amounts in columns (d) and (f)			2			
3	Tentative Hope credit. Add the amounts on line 2, columns (d) and (f). If you are claiming the lifetime learning credit for another student, go to Part II; otherwise, go to Part III ▶					3	

Part II Lifetime Learning Credit

4	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions)
	Judy Green	000 00 2586	500
5	Add the amounts on line 4, column (c), and enter the total		5 500
6	Enter the smaller of line 5 or \$10,000		6 500
7	Tentative lifetime learning credit. Multiply line 6 by 20% (.20) and go to Part III ▶		7 100

Part III Allowable Education Credits

8	Tentative education credits. Add lines 3 and 7		8 100
9	Enter: \$103,000 if married filing jointly; \$51,000 if single, head of household, or qualifying widow(er)	9 51,000	
10	Enter the amount from Form 1040, line 35 *, or Form 1040A, line 22	10 29,524	
11	Subtract line 10 from line 9. If zero or less, stop ; you cannot take any education credits	11 21,476	
12	Enter: \$20,000 if married filing jointly; \$10,000 if single, head of household, or qualifying widow(er)	12 10,000	
13	If line 11 is equal to or more than line 12, enter the amount from line 8 on line 14 and go to line 15. If line 11 is less than line 12, divide line 11 by line 12. Enter the result as a decimal (rounded to at least three places)	13 × .	
14	Multiply line 8 by line 13	14 100	
15	Enter the amount from Form 1040, line 43, or Form 1040A, line 28	15 1,701	
16	Enter the total, if any, of your credits from Form 1040, lines 44 through 46, or Form 1040A, lines 29 and 30	16 0	
17	Subtract line 16 from line 15. If zero or less, stop ; you cannot take any education credits	17 1,701	
18	Education credits. Enter the smaller of line 14 or line 17 here and on Form 1040, line 47, or Form 1040A, line 31	18 100	

*See Pub. 970 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

A taxpayer cannot:

- Deduct higher education expenses and claim a credit based on those same expenses,
- Claim a Hope credit and a lifetime learning credit based on the same qualified education expenses, or
- Claim a credit based on expenses paid with tax-free scholarship, grant, employer-provided educational assistance or a distribution from a Coverdell ESA.

However, a taxpayer can claim a credit based on expenses paid with the eligible student's earnings, loans, gifts, inheritances, or personal savings.

An eligible student cannot claim an education credit if he or she is claimed as a dependent on another taxpayer's tax return. Any amounts paid by the student are considered paid by the taxpayer who claims the student as a dependent.

The following table summarizes the differences between the credits.

Table: Comparison of Education Credits

Lifetime Learning Credit	Hope Scholarship Credit
per taxpayer credit	per eligible student credit
\$2,000 limit per taxpayer	\$1,500 limit per eligible student
available for an unlimited number of years	available ONLY for the first two years of postsecondary education
credit available for courses taken as part of a postsecondary degree program or to acquire or improve job skills (including non-credit courses and graduate level work)	must be pursuing a degree or other educational credential
available for one or more courses	must take at least 1/2 of the normal full-time workload for one academic period
no other restrictions	felony drug conviction restriction

Adjustments to Qualified Expenses

Tax-free educational assistance can include the following:

- Scholarships,
- Pell grants,
- Employer-provided educational assistance,
- Veteran's educational assistance, and

- Any other nontaxable payments (other than gifts, bequests, or inheritances) received for education expenses.

If the taxpayer paid qualified tuition expenses with these tax-free funds, a credit cannot be claimed for these amounts. Qualified expenses must be reduced by the amount of any tax-free educational assistance received.

Example 3

In 2003, Jackie paid \$3,000 for tuition and \$5,000 for room and board at her local university. To help pay these costs, she was awarded a \$2,000 scholarship and a \$4,000 student loan.

The scholarship is a qualified scholarship that is excludable from Jackie's income. For purposes of the education credit, she must first use the scholarship to reduce her tuition (her only qualified expense). The student loan is not considered tax-free educational assistance so she does not use it to reduce the qualified expenses. Therefore, Jackie is treated as having paid only \$1,000 in qualified expenses (\$3,000 tuition - \$2,000 scholarship).

Refunds. Qualified tuition and related expenses do not include expenses for which the taxpayer received a refund. If the refund or tax-free assistance is received in the same year in which the expenses were paid or in the following year before the tax return is filed, reduce the qualified expenses by the amount received and figure the education credits using the reduced amount of qualified expenses.

If the refund or tax-free assistance is received after the tax return is filed for the year in which the expenses were paid, figure the amount by which the education credits would have been reduced if the refund or tax-free assistance had been received in the year for which the education credits were claimed. Include that amount as an additional tax for the year the refund or tax-free assistance was received. Enter the amount and "ECR" on line 42.

Example 4

Sally paid \$2,250 tuition on December 26, 2002, for her daughter who began college on January 16, 2003. She filed her 2002 tax return on February 12, 2003, and claimed a Hope credit of \$1,500. After Sally filed her return, her daughter dropped two courses but maintained one-half of a full-time workload. Sally received a refund of \$750. She must refigure her 2002 Hope credit using \$1,500 of qualified expenses instead of \$2,250. The refigured credit is \$1,250. She must include the difference of \$250 on line 41 of her 2003 Form 1040 and annotate next to the line: \$250 ECR.

Exercise 1

Bruce (SSN 000-00-9541) and Toni Green are married and file a joint tax return. For 2003, their modified AGI (\$65,500) is the same as their AGI. They completed Form 1040 through line 44. Their tax amount on Line 43 is \$6,203. Toni is attending the local community college part time to earn credits toward an associate degree in nursing. She paid \$2,500 in tuition and fees. Their son, Ben, is a full time freshman at the state university. Bruce and Toni paid \$8,000 in tuition and fees for Ben in 2003. They choose to take the lifetime learning credit for Toni and the Hope credit for Ben. They will claim no other credits. Toni's SSN is 000-00-4651. Ben's SSN is 000-00-3945. Complete their Form 8863.

TAXWISE HINTS

To input qualified tuition expenses and prepare a Form 8863 using TaxWise, select Form 8863, enter the student's name in either the Hope credit section or the lifetime learning credit section and complete all the entries annotated in red. TaxWise will automatically complete the form and carry the mathematical calculations to the Form 1040.

►► SUMMING UP THIS LESSON ◀◀

The maximum credit amount for the lifetime learning credit for tax year 2003 increased to \$2,000.

The Hope and lifetime learning credits are nonrefundable credits that allow a taxpayer to claim all or a portion of qualified tuition and related expenses paid for post-secondary education.

Generally, a taxpayer can claim the Hope or lifetime learning credit if they pay qualified tuition and related expenses of higher education for an eligible student who is either the taxpayer, the taxpayer's spouse, or a dependent whom the taxpayer can claim an exemption on his or her tax return.

A taxpayer cannot:

- ▶ Deduct higher education expenses on his or her tax return and also claim a Hope or lifetime learning credit based on those same expenses,
- ▶ Claim a Hope credit and a lifetime learning credit based on the same qualified education expenses, or
- ▶ Claim a credit based on expenses paid with tax-free scholarship, grant, or employer-provided educational assistance.

The Hope and lifetime learning credits are claimed on Form 8863 which can be filed with either Form 1040 or Form 1040A.

Form **8863**
 Department of the Treasury
 Internal Revenue Service
 Name(s) shown on return

Education Credits
(Hope and Lifetime Learning Credits)
 ▶ See instructions.
 ▶ Attach to Form 1040 or Form 1040A.

OMB No. 1545-1618
2003
 Attachment
 Sequence No. **50**

Your social security number

Caution: You **cannot** take both an education credit and the tuition and fees deduction (Form 1040, line 26, or Form 1040A, line 19) for the **same student** in the same year.

Part I Hope Credit. Caution: You cannot take the Hope credit for more than **2** tax years for the **same student**.

1	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions). Do not enter more than \$2,000 for each student).	(d) Enter the smaller of the amount in column (c) or \$1,000	(e) Subtract column (d) from column (c)	(f) Enter one-half of the amount in column (e)
2	Add the amounts in columns (d) and (f)					2
3	Tentative Hope credit. Add the amounts on line 2, columns (d) and (f). If you are claiming the lifetime learning credit for another student, go to Part II; otherwise, go to Part III ▶					3

Part II Lifetime Learning Credit

4	(a) Student's name (as shown on page 1 of your tax return) First name Last name	(b) Student's social security number (as shown on page 1 of your tax return)	(c) Qualified expenses (see instructions)
5	Add the amounts on line 4, column (c), and enter the total		5
6	Enter the smaller of line 5 or \$10,000		6
7	Tentative lifetime learning credit. Multiply line 6 by 20% (.20) and go to Part III ▶		7

Part III Allowable Education Credits

8	Tentative education credits. Add lines 3 and 7		8
9	Enter: \$103,000 if married filing jointly; \$51,000 if single, head of household, or qualifying widow(er)		
10	Enter the amount from Form 1040, line 35 *, or Form 1040A, line 22		
11	Subtract line 10 from line 9. If zero or less, stop ; you cannot take any education credits		
12	Enter: \$20,000 if married filing jointly; \$10,000 if single, head of household, or qualifying widow(er)		
13	If line 11 is equal to or more than line 12, enter the amount from line 8 on line 14 and go to line 15. If line 11 is less than line 12, divide line 11 by line 12. Enter the result as a decimal (rounded to at least three places)		
14	Multiply line 8 by line 13 ▶		
15	Enter the amount from Form 1040, line 43, or Form 1040A, line 28		
16	Enter the total, if any, of your credits from Form 1040, lines 44 through 46, or Form 1040A, lines 29 and 30		
17	Subtract line 16 from line 15. If zero or less, stop ; you cannot take any education credits ▶		
18	Education credits. Enter the smaller of line 14 or line 17 here and on Form 1040, line 47, or Form 1040A, line 31 ▶		

*See Pub. 970 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

For Paperwork Reduction Act Notice, see page 3.

Cat. No. 25379M

Form **8863** (2003)

Exercise 1

Bruce and Toni's Form 8863

<p>Form 8863</p> <p>Department of the Treasury Internal Revenue Service</p>	<p>Education Credits (Hope and Lifetime Learning Credits)</p> <p>▶ See instructions. ▶ Attach to Form 1040 or Form 1040A.</p>	<p>OMB No. 1545-1618</p> <p>2003 Attachment Sequence No. 50</p>					
Name(s) shown on return Bruce and Toni Green		Your social security number 000 00 9541					
<p>Caution: You <i>cannot</i> take both an education credit and the tuition and fees deduction (Form 1040, line 26, or Form 1040A, line 19) for the same student in the same year.</p>							
<p>Part I Hope Credit. Caution: You <i>cannot</i> take the Hope credit for more than 2 tax years for the same student.</p>							
1	<p>(a) Student's name (as shown on page 1 of your tax return)</p> <p>First name Last name</p>	<p>(b) Student's social security number (as shown on page 1 of your tax return)</p>	<p>(c) Qualified expenses (see instructions). Do not enter more than \$2,000 for each student.</p>	<p>(d) Enter the smaller of the amount in column (c) or \$1,000</p>	<p>(e) Subtract column (d) from column (c)</p>	<p>(f) Enter one-half of the amount in column (e)</p>	
	Ben Green	000 00 3945	2,000	1,000	1,000	500	
2	Add the amounts in columns (d) and (f)					500	
3	Tentative Hope credit. Add the amounts on line 2, columns (d) and (f). If you are claiming the lifetime learning credit for another student, go to Part II; otherwise, go to Part III ▶					3	1,500
<p>Part II Lifetime Learning Credit</p>							
4	<p>(a) Student's name (as shown on page 1 of your tax return)</p> <p>First name Last name</p>	<p>(b) Student's social security number (as shown on page 1 of your tax return)</p>	<p>(c) Qualified expenses (see instructions)</p>				
	Toni Green	000 00 4651	2,500				
5	Add the amounts on line 4, column (c), and enter the total					5	2,500
6	Enter the smaller of line 5 or \$10,000					6	2,500
7	Tentative lifetime learning credit. Multiply line 6 by 20% (.20) and go to Part III ▶					7	500
<p>Part III Allowable Education Credits</p>							
8	Tentative education credits. Add lines 3 and 7					8	2,000
9	Enter: \$103,000 if married filing jointly; \$51,000 if single, head of household, or qualifying widow(er)					9	103,000
10	Enter the amount from Form 1040, line 35 *, or Form 1040A, line 22					10	65,500
11	Subtract line 10 from line 9. If zero or less, stop ; you cannot take any education credits					11	37,500
12	Enter: \$20,000 if married filing jointly; \$10,000 if single, head of household, or qualifying widow(er)					12	20,000
13	If line 11 is equal to or more than line 12, enter the amount from line 8 on line 14 and go to line 15. If line 11 is less than line 12, divide line 11 by line 12. Enter the result as a decimal (rounded to at least three places)					13	×
14	Multiply line 8 by line 13 ▶					14	2,000
15	Enter the amount from Form 1040, line 43, or Form 1040A, line 28					15	6,203
16	Enter the total, if any, of your credits from Form 1040, lines 44 through 46, or Form 1040A, lines 29 and 30					16	0
17	Subtract line 16 from line 15. If zero or less, stop ; you cannot take any education credits ▶					17	6,203
18	Education credits. Enter the smaller of line 14 or line 17 here and on Form 1040, line 47, or Form 1040A, line 31 ▶					18	2,000
<p>*See Pub. 970 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.</p>							

For Paperwork Reduction Act Notice, see page 3.

Cat. No. 25379M

Form **8863** (2003)

STUDENT NOTES

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about the earned income tax credit. This is a refundable credit, and taxpayers must file a tax return to receive the credit.

After completing this lesson you should be able to:

- Use the EITC rules to determine which taxpayers are eligible for the earned income tax credit.
- Calculate and report the credit using the EIC worksheet.
- Explain the benefits of the Advanced Earned Income Credit (AEIC).
- Report the AEIC on the tax return.

GENERAL REQUIREMENTS

Some taxpayers are able to claim the earned income credit. This is a refundable credit, and eligible taxpayers can receive a refund of this credit even if they owe no tax and had no income tax withheld.

All taxpayers (and spouses, if filing a joint return) must meet the general requirements to claim the credit. Other requirements apply depending on whether or not the taxpayer has a qualifying child (defined later).

Generally, to claim the earned income tax credit, a taxpayer must:

- Have earned income during the year,
- Not have investment income of more than \$2,600.
Investment income includes taxable interest and dividends, tax exempt interest, capital gain net income, net income from rents and royalties not derived from a trade or business, and net income from passive activities,
- Use any filing status except married filing a separate return,
- Have a tax return that covers a 12-month period. This does not apply if a short period return is filed because of an individual's death,
- Show on the tax return the SSN of the taxpayer (and spouse if filing a joint return). See identification numbers, later.
- Not be the qualifying child of another person,
- Not exclude from gross income any income earned in foreign countries, or deduct or exclude a foreign housing amount (File Form 2555 or Form 2555-EZ), and
- Not be a nonresident alien. Nonresident aliens may qualify for the credit only if they are married to a U.S. citizen or resident **and** their filing status is married filing jointly.

POTENTIAL PITFALLS



If the taxpayer's filing status is married filing separately, the taxpayer cannot claim the earned income credit.

Table 9-1. Earned Income Credit in a Nutshell

Part A Rules for Everyone	Part B Rules If You Have a Qualifying Child	Part C Rules If You Do Not Have a Qualifying Child
Rule 1. You must have a valid social security number.	Rule 7. Your child must meet the relationship, age, and residency tests.	Rule 10. You must be at least age 25 but under age 65.
Rule 2. Your filing status cannot be “Married filing separately.”	Rule 8. Your qualifying child cannot be used by more than one person to claim the EIC.	Rule 11. You cannot be the dependent of another person.
Rule 3. You must be a U.S. citizen or resident alien all year.	Rule 9. You cannot be a qualifying child of another person.	Rule 12. You cannot be a qualifying child of another person.
Rule 4. You cannot file Form 2555 or Form 2555–EZ (relating to foreign earned income).		Rule 13. You must have lived in the United States more than half the year.
Rule 5. Your investment income must be \$2,600 or less.		
Rule 6. You must have earned income.		
Part D		
Figuring and Claiming the EIC		
<p>Rule 14. Your earned income must be less than:</p> <ul style="list-style-type: none"> • \$33,692 (\$34,692 for married filing jointly) if you have more than one qualifying child, • \$29,666 (\$30,666 for married filing jointly) if you have one qualifying child, or • \$11,230 (\$12,230 for married filing jointly) if you do not have a qualifying child 		
<p>Rule 15. Your AGI must be less than:</p> <ul style="list-style-type: none"> • \$33,692 (\$34,692 for married filing jointly) if you have more than one qualifying child, • \$29,666 (\$30,666 for married filing jointly) if you have one qualifying child, or • \$11,230 (\$12,230 for married filing jointly) if you do not have a qualifying child 		

Identification Numbers

To claim the EIC, the taxpayer (and spouse if filing a joint return) must have a valid Social Security number (SSN) issued by the Social Security Administration (SSA). Any qualifying child listed on Schedule EIC must also have a valid SSN. If a social security card has a legend that says **“Not valid for employment”** and the number was issued so that the taxpayer (or spouse or qualifying child) could receive a federally funded benefit, the taxpayer cannot claim the EIC. An example of a federally funded benefit is Medicaid.

Individual Taxpayer Identification Numbers (ITINs) and Adoption Taxpayer Identification Numbers (ATINs) cannot be used when claiming the EIC.

If a taxpayer has a social security card that contains the legend “valid for work only with INS authorization,” the taxpayer may claim the credit, assuming he or she meets the other requirements.

Taxpayers With One or More Qualifying Children

If the taxpayer has a qualifying child (defined later), the following additional requirements apply.

- The taxpayer's earned income and adjusted gross income must each be less than:
 - a) \$29,666 (\$30,666 if married filing jointly) if he or she has one qualifying child, or
 - b) \$33,692 (\$34,692 if married filing jointly) if he or she has more than one qualifying child,
- The taxpayer must show on Schedule EIC the name, age, and SSN for each qualifying child listed (see *Identification Numbers*, earlier).

Taxpayers With No Qualifying Child

If the taxpayer does not have a qualifying child, the following additional requirements apply.

- The taxpayer's earned income and adjusted gross income must each be less than \$11,230 (\$12,230 if married filing jointly).
- The taxpayer (or the taxpayer's spouse, if filing a joint return) must be at least age 25 but under age 65 at the end of the year.
- Neither the taxpayer (nor the taxpayer's spouse if filing jointly) can be eligible to be claimed as a dependent on another person's return.
- The principal place of abode of the taxpayer (and the taxpayer's spouse, if filing jointly) must be in the United States for more than half the year.

Earned Income

Earned income is wages, salaries, tips and other employee compensation, but only if the amounts are includible in gross income; plus net earnings from self-employment. Table 1 provides examples of what to include and not to include as earned income in computing the earned income credit.

Amounts received for work performed while an inmate in a penal institution are not considered earned income for purposes of the earned income credit. Enter "PRI" and the amount of the income earned while an inmate next to line 7 (Form 1040 or 1040A) or line 1 (Form 1040 EZ). This income is still considered taxable for purposes of determining the taxpayer's federal income tax.

If the taxpayer was a household employee who did not receive a Form W-2 because he or she was paid less than \$1,300, the income must still be included on line 7 (Form 1040A or 1040) or line 1 (Form 1040EZ). Enter "HSH" and the amount not reported on Form W-2 next to line 7 (Form 1040A or 1040) or Line 1 (Form 1040EZ).

Table 9-2. Examples of Earned Income for the Earned Income Credit

Earned Income	
Includes	Does not include
<p>Taxable wages, salaries, and tips</p> <p>Union strike benefits</p> <p>Taxable long-term disability benefits received prior to minimum retirement age</p> <p>Net earnings from self-employment</p> <p>Gross income of a statutory employee</p>	<p>Interest and dividends</p> <p>Social Security and railroad retirement benefits</p> <p>Welfare benefits</p> <p>Workfare payments</p> <p>Pensions or annuities</p> <p>Veteran’s benefits (including VA rehabilitation payments)</p> <p>Workers’ compensation benefits</p> <p>Alimony</p> <p>Child Support</p> <p>Nontaxable foster care payments</p> <p>Unemployment compensation</p> <p>Taxable scholarship or fellowship grants that are not reported on Form W-2</p> <p>Earnings for work performed while an inmate at a penal institution</p> <p>Salary deferrals (for example, under a 401(k) or 403(b) plan or the Federal Thrift Savings Plan)</p> <p>Combat zone excluded pay (box 12, code Q of Form W-2)</p> <p>Basic housing and subsistence allowances for the U.S. Military (box 12, code Q of Form W-2)</p> <p>The value of meals or lodging provided by an employer for the convenience of the employer</p> <p>Housing allowance or rental value of a parsonage for the clergy</p> <p>Excludable dependent care benefits (line 18 of either Form 2441, Form 1040, or Schedule 2, Form 1040A)</p> <p>Salary reductions such as under a cafeteria plan</p> <p>Excludable employer provided educational assistance benefits (may be shown in box 13 of Form W-2)</p> <p>Anything else of value received from someone for services performed, if it is not currently taxable</p>

For purposes of the earned income credit, a taxpayer has a qualifying child, if the child meets three tests.

- Relationship Test
- Residency Test, and
- Age Test

Relationship Test

To meet the relationship test, the qualifying child must be the taxpayer's:

1. Son, daughter, stepson, stepdaughter or a descendant of the taxpayer's son, daughter, stepson, or stepdaughter.
2. Brother, sister, stepbrother, stepsister or a descendant of the taxpayer's brother, sister, stepbrother or stepsister. The taxpayer must care for any of these children as his or her own child. A descendant must be lineal descendant.
3. Eligible foster child.

An **eligible foster child** is a child placed with the taxpayer by an authorized placement agency and whom the taxpayer cares for as his or her own child. An authorized placement agency is an agency of a state or political subdivision of a state, including a court, or tax-exempt organization licensed by the state.

An adopted child (and a child placed with the taxpayer for adoption) is treated as a child by blood.

Residency Test

To meet the residency test, the child must live with the taxpayer in the United States for more than half of the tax year. If a child fails to meet the residency test because the child was born or died during the year, the child is considered to meet the test if the child lived with the taxpayer while the child was alive. The taxpayer does not need to have a home. It is sufficient if the taxpayer and child live together in a series of homeless shelters.

Age Test

To meet the age test, the child must be:

- Under age 19 at the end of the year,
- A full-time student under age 24 at the end of year, or
- Permanently and totally disabled at any time during the tax year, regardless of age.

A **married taxpayer** can be a qualifying child of the taxpayer if he or she can be claimed as a dependent by the taxpayer.

Qualifying Child of More Than One Taxpayer

If a child is a qualifying child of more than one taxpayer, the taxpayers may choose which of them will claim the credit on the basis of that child. If two or more children are qualifying children of the same taxpayers (not filing a joint return together), the taxpayers may agree that one will claim the credit on the basis of one child and the other will claim the credit on the basis of the other child.

Example 1

Jane (age 30) is unmarried. In 2003, Jane lived with her four children and her mother, Linda. Provided they each meet the eligibility and income requirements, Jane may claim the EIC based on one or two of the children, and Linda may claim the EIC based on the other two children not claimed by Jane.

If two or more taxpayers actually claim the credit on the basis of the same qualifying child, the statute determines which of them is entitled to the credit on the basis of that child. This is the tie-breaker rule. The taxpayer who is entitled to the credit is —

- The parent, if one taxpayer is a parent of the child.
- The parent the child lived with longest during the tax year, if both taxpayers are parents of the child and they do not file a joint return together.
- The parent with the higher AGI, if both taxpayers are parents of the child, the child lived with both parents for the same length of time during the tax year, and they do not file a joint return together.
- The taxpayer with the higher AGI, if neither is a parent of the child.

Example 2

John (age 26) is unmarried. In 2003, John and his daughter, Lynn, lived with John's father, Paul. John's sole income was wages of \$19,000. Paul's sole income was wages of \$12,000.

Lynn is a qualifying child of both John and Paul. John and Paul agree that Paul will claim the EIC on the basis of Lynn, because Paul's credit would be more than John's. If John later decides to claim the credit, under the tie-breaker rule, Paul will lose the credit he claimed.

Example 3

Ralph is single and has two qualifying children. He earned \$23,247 in taxable wages and his adjusted gross income is \$26,928.

Ralph can claim the earned income credit because his earned income and adjusted gross income are each less than \$33,692.

Example 4

Maureen has \$23,050 in earned income; her adjusted gross income is \$23,175. Her filing status is single. Maureen's 20-year-old daughter, Angie, lived with her for eight months of the year. Angie is not married and is a full-time college student.

Maureen can claim the earned income credit because she has a qualifying child and her earned income and adjusted gross income are under \$29,666.

DISALLOWED EARNED INCOME CREDIT

If a taxpayer's earned income credit was disallowed in for any year after 1996 as a result of the deficiency procedures, he or she cannot claim the credit again unless *Form 8862, Information To Claim Earned Income Credit After Disallowance*, is attached to the return. If the credit is claimed without attaching Form 8862, it will be automatically denied, under the math error procedures.

A deficiency procedure occurs when the IRS questions the taxpayer's eligibility for the earned income credit for reasons other than a mathematical or clerical error. If the credit was disallowed in the earlier year because of a mathematical or clerical error, Form 8862 should not be completed. For more information on deficiency procedures, see Publication 596.

A taxpayer who is determined to have claimed the EIC due to reckless or intentional disregard of rules or regulations is ineligible to claim the EIC for a subsequent period of 2 years.

A taxpayer who is determined to have fraudulently claimed the EIC is ineligible to claim the EIC for a subsequent period of 10 years.

CERTIFICATION — EARNED INCOME CREDIT

The Internal Revenue Service will execute a pilot initiative during the 2004 Filing Season with the balanced goal of providing better service and improving the integrity of the administration of the Earned Income Tax Credit. A part of this initiative was an EITC certification component. The twin objectives of the certification process are to 1) reduce overpayments and 2) improve participation of eligible EITC customers

If a taxpayer has received correspondence regarding EITC certification, offer to review the information with the customer. If the taxpayer has received a determination letter, please complete the return, relative to the EITC, as directed. Please note if the customer's situation has altered since receiving a determination letter the qualifying rules still apply. The customer interview is a critical part of completing a correct return.

Exercise 1

Determine if the taxpayers in this exercise can claim the earned income credit. If they cannot, explain why.

- A.** Sharon has an eligible foster child, Eric. Eric is 12 years old and began living with Sharon in August 2003. Sharon's earned income and her adjusted gross income are \$14,275. Can Sharon claim the earned income credit? _____
- _____
- B.** Doug and Donna are married and live together. Their combined earned income is \$22,222. Doug reports adjusted gross income of \$10,728 on his separate tax return, and Donna reports adjusted gross income of \$11,514 on her separate return. Sam, their four-year-old son, lives with Doug and Donna. Can Doug and/or Donna claim the earned income credit? _____
- C.** Randy and Cara were married and lived together until August when they divorced. Randy and Cara have two children, Jimmy, age seven, and Anna, age five. The children lived with both of their parents until August, then they lived with their mother. Randy's earned income and adjusted gross income are \$19,251. Cara's earned income is \$14,751, and her adjusted gross income is \$15,362. Can Randy and/or Cara claim the earned income credit? _____
- D.** Benjamin, age 26, lives alone, is single, and earns \$8,250. His adjusted gross income is \$8,950. Can Benjamin claim the earned income credit? _____
- E.** Melanie is 18 years old and married. Melanie's husband is overseas, and she lives with her mother, Susan. Susan's earned income is \$18,431, and her adjusted gross income is \$18,453. Susan cannot claim Melanie as a dependent. Can Susan claim the earned income credit? _____
- F.** Circle the items that are considered earned income for earned income credit purposes.
1. Wages
 2. Housing allowance for a member of the clergy
 3. Social security benefits
 4. Interest income
 5. Unemployment compensation
 6. Tip income
 7. Dividend income
 8. Military subsistence allowances

The earned income credit is computed on the Earned Income Credit (EIC) Worksheet. Before completing the EIC Worksheet, **you must** complete the steps in the EIC instructions line 63 of Form 1040; line 41 of Form 1040A; or line 8 of Form 1040EZ.

Completing the steps will help you determine whether or not the taxpayer is eligible to take the credit. If the taxpayer can claim the earned income credit, complete the EIC Worksheet. If the taxpayer is not eligible to claim the credit but appears to be based on income limitations, write “No” next to line 8 of 1040EZ; line 41 of 1040A; or line 63 of 1040. **The steps and the EIC Worksheets are included in the 1040, 1040A, and 1040EZ instructions.**

There are two versions (A and B) of the EIC Worksheet for Form 1040 filers. If the taxpayer was self-employed or reported income and expenses on Schedule C or C-EZ as a statutory employee, he or she must use the EIC Worksheet B to figure his or her credit amount. Complete the EIC Worksheet to determine the amount of the earned income credit the taxpayer can claim. The EIC Worksheet should not be attached to the return; the taxpayer should keep it with his or her tax records.

Using the Earned Income Credit Table

The Earned Income Credit (EIC) Table is used to determine the amount of the credit. The tables are found in the instructions for Forms 1040EZ, 1040A, or 1040.

When using the earned income credit table to determine the credit, read down the columns labeled *At least . . . But less than* and find the line that includes the amount you are instructed to look up from the EIC Worksheet. Read across to the column that includes the number of qualifying children of the taxpayer and filing status. Enter the earned income credit from that column on the EIC Worksheet.

Example 5

Roger’s filing status is head of household and he has two qualifying children. The amount shown on lines 1 and 3 of his Form 1040A EIC Worksheet is \$19,300.

Roger’s earned income credit from the EIC Table is \$3,026.

Exercise 2

- A.** Alex and Cheryl have two qualifying children. Their filing status is married filing jointly. The amount shown on lines 1 and 3 of their EIC Worksheet is \$19,866.

What is the earned income credit from the EIC Table? _____

- B.** Roxanne is divorced. She lives with her infant daughter. The amount shown on lines 1 and 3 of her EIC Worksheet is \$17,750.

What is the earned income credit from the EIC Table? _____

POTENTIAL PITFALLS



Errors are easily made when using the earned income credit table. To ensure that you have entered the correct amount on the tax form, look up the credit twice—once before you enter the credit on the form and once after you have entered it on the form.

Completing Schedule EIC

Qualifying Child Information

Schedule EIC, *Earned Income Credit*, contains only information about qualifying children. Only taxpayers who have a qualifying child must fill out the schedule and attach it to Form 1040A or Form 1040.

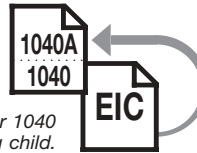
Example 6

Ronald Evans (SSN 000-00-9840) is single. His son, Harry (SSN 000-00-9849), was born in 1981. Harry lived with Ronald during all of 2003. Harry is a full-time student. Harry is not married and is a qualifying child of his father. He is not a qualifying child of his mother. However, Harry's mother claims him as a dependent on her tax return.

Exhibit 1 shows the Schedule EIC.

SCHEDULE EIC
(Form 1040A or 1040)

Earned Income Credit
Qualifying Child Information



OMB No. 1545-0074

2003

Attachment
Sequence No. **43**

Department of the Treasury
Internal Revenue Service

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.

Name(s) shown on return

RONALD EVANS

Your social security number

000 : 00 : 9840

Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that
(a) you can take the EIC and (b) you have a qualifying child.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.

Qualifying Child Information

Child 1

Child 2

1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	First name	Last name	First name	Last name
		HARRY	EVANS	
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.	000	00	9849	

Next, if the child was born after 1984, go to line 4. Otherwise, continue.

3 If the child was born before 1985— a Was the child under age 24 at the end of 2003 and a student?	<input checked="" type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>
	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.
4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)	SON			
5 Number of months child lived with you in the United States during 2003 • If the child lived with you for more than half of 2003 but less than 7 months, enter "7". • If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12".	12 months <i>Do not enter more than 12 months.</i>		_____ months <i>Do not enter more than 12 months.</i>	



You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.

For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2003

Exercise 3

Sam U. and Robin O. Bell are married and file a joint return. Sam's social security number is 000-00-4797 and Robin's is 000-00-4798. They have a child, Jennifer S. Bell (SSN 000-00-1987) who was born in 1996. Jennifer lived with her parents for the entire year. Form 1040A, line 7 shows that the Bells had wages of \$21,211, line 8a shows \$39 of taxable interest income, and line 21 shows the Bells' adjusted gross income of \$21,250.

Complete the EIC Worksheet and Schedule EIC.

POTENTIAL PITFALLS



Remember that the amount of the earned income credit depends on the taxpayer's income, number of qualifying children, and filing status. Be sure to use the correct column from the EIC Table.

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet that applies to you **or** let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

- If, in 2003:
 - 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
 - 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
 - No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* **No.** You cannot take the credit.
- Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* **No.** You cannot take the credit. Put "No" to the left of the entry space for line 41.
- Is your filing status married filing separately?

Yes. You cannot take the credit. **No.** *Continue*
- Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*

Step 2 Investment Income

- Add the amounts from Form 1040A:

Line 8a _____
 Line 8b + _____
 Line 9a + _____
 Line 10a + _____

Investment Income =

- Is your investment income more than \$2,600?

Yes. You cannot take the credit. **No.** *Continue*
- Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.* **No.** *Go to Step 4 on page 40.*

(Continued on page 40)

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)


AND

who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* ↘
You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Do you have at least one child who meets the above conditions to be your qualifying child?


Yes. *Go to question 3.* **No.** *Skip question 3; go to Step 4, question 2.*

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?


Yes. *See Qualifying Child of More Than One Person on page 42.* **No.** This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. *Skip Step 4; go to Step 5 on page 41.*

Step 4 Filers Without a Qualifying Child


1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* ↘
You cannot take the credit. Put "No" to the left of the entry space for line 41.


2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?

Yes.  **No.** *Continue* ↘
You cannot take the credit.

3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. *Continue* ↘ **No.**  You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. *Go to Step 5 on page 41.* **No.**  You cannot take the credit. Put "No" to the left of the entry space for line 41.

(Continued on page 41)

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 _____

Subtract, if included on line 7, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put "PRI" and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

Earned Income =

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.** **STOP**

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See *Credit Figured by the IRS* below.
 No. Go to the *worksheet on page 43.*

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put "EIC" to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to "Time Lived With You" Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child's home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.


Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

(Continued on page 42)

Earned Income Credit (EIC) Worksheet—Line 41


Keep for Your Records 

Part 1

All Filers

1. Enter your earned income from Step 5 on page 43. 1

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here. 2

If line 2 is zero,  You cannot take the credit. Put “No” to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22. 3

4. Are the amounts on lines 3 and 1 the same?
 Yes. Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered “No” on Line 4

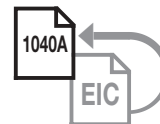
5. If you have:
 • No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?
 • 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?
 Yes. Leave line 5 blank; enter the amount from line 2 on line 6.
 No. Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here. 5
 Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

Part 3

Your Earned Income Credit

6. This is your earned income credit. 6
 Enter this amount on Form 1040A, line 41.

Reminder—
 ✓ If you have a qualifying child, complete and attach Schedule EIC.



If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.

Complete this Form

Exhibit 6

Form 1040A (2003)

Page 2

Tax, credits, and payments	22	Enter the amount from line 21 (adjusted gross income).	22	
Standard Deduction for— • People who checked any box on line 23a or 23b or who can be claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000	23a	Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind } checked ▶ 23a <input type="checkbox"/>		
	b	If you are married filing separately and your spouse itemizes deductions, see page 34 and check here ▶ 23b <input type="checkbox"/>		
	24	Enter your standard deduction (see left margin).	24	
	25	Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25	
	26	Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26	
	27	Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income . ▶ 27	27	
	28	Tax, including any alternative minimum tax (see page 35).	28	
	29	Credit for child and dependent care expenses. Attach Schedule 2.	29	
	30	Credit for the elderly or the disabled. Attach Schedule 3.	30	
	31	Education credits. Attach Form 8863.	31	
32	Retirement savings contributions credit. Attach Form 8880.	32		
33	Child tax credit (see page 38).	33		
34	Adoption credit. Attach Form 8839.	34		
35	Add lines 29 through 34. These are your total credits .	35		
36	Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36		
37	Advance earned income credit payments from Form(s) W-2.	37		
38	Add lines 36 and 37. This is your total tax . ▶ 38	38		
39	Federal income tax withheld from Forms W-2 and 1099.	39		
40	2003 estimated tax payments and amount applied from 2002 return.	40		
41	Earned income credit (EIC) .	41		
42	Additional child tax credit. Attach Form 8812.	42		
43	Add lines 39 through 42. These are your total payments . ▶ 43	43		
Refund	44	If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44	
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	45a	Amount of line 44 you want refunded to you . ▶ 45a		
	b	Routing number <input type="text"/> ▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings		
d	Account number <input type="text"/>			
46	Amount of line 44 you want applied to your 2004 estimated tax .	46		
Amount you owe	47	Amount you owe. Subtract line 43 from line 38. For details on how to pay, see page 53. ▶ 47		
48	Estimated tax penalty (see page 53).	48		
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes . Complete the following. <input type="checkbox"/> No			
	Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶	<input type="text"/>
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.			
Joint return? See page 22. Keep a copy for your records.	Your signature	Date	Your occupation	Daytime phone number ()
	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	<input style="background-color: #cccccc;" type="text"/>
Paid preparer's use only	Preparer's signature ▶	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
	Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Phone no. ()	

Printed on recycled paper

Form 1040A (2003)

Complete this Form

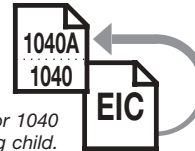
Exhibit 7

SCHEDULE EIC
(Form 1040A or 1040)

Department of the Treasury
Internal Revenue Service

Earned Income Credit
Qualifying Child Information

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.



OMB No. 1545-0074

2003

Attachment
Sequence No. **43**

Name(s) shown on return

Your social security number

Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that
(a) you can take the EIC and (b) you have a qualifying child.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.

Qualifying Child Information

Child 1

Child 2

1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	Child 1		Child 2	
	First name	Last name	First name	Last name
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.				
Next, if the child was born after 1984, go to line 4. Otherwise, continue.				
3 If the child was born before 1985—				
a Was the child under age 24 at the end of 2003 and a student?	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>
b Was the child permanently and totally disabled during any part of 2003?	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.
4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)				
5 Number of months child lived with you in the United States during 2003				
• If the child lived with you for more than half of 2003 but less than 7 months, enter "7".				
• If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12".	_____ months <i>Do not enter more than 12 months.</i>		_____ months <i>Do not enter more than 12 months.</i>	



You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.

For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2003

ADVANCE EARNED INCOME CREDIT PAYMENTS

An employee who expects to qualify for the earned income credit (EIC) and to have at least one qualifying child for 2004 can choose to get a portion of the credit in advance throughout the year (based on one qualifying child) by giving a filled out Form W-5, *Earned Income Credit Advance Payment Certificate*, to his or her employer. Taxpayers receive only a portion of the credit through advance payments, so the eligibility questions and the EIC Worksheet must be completed when the tax return is prepared to determine the full amount of the credit the taxpayer is entitled to receive.

If the employee chooses to receive the EIC in advance, the employer will include advance payments of the credit in the employee's regular paychecks during the year. Employees who receive advance earned income credit payments **must** file a tax return even if they are not otherwise required to file.

Advance earned income credit payments are reported in box 9 of Form W-2. Enter this amount on Form 1040A, line 37, or Form 1040, line 58.

Exercise 4

Kyle B. Evans is a single parent. He claims his daughter, Julie, as a dependent on his tax return. Kyle's social security number is 000-00-2442. Julie was born in November 2001. Her social security number is 000-00-4104. Kyle's earned income was \$18,751, and his total income and adjusted gross income were \$19,223. He received \$550 in advance earned income credit payments.

- A. Complete Kyle's eligibility questions and EIC Worksheet.
- B. What entries would you make on Schedule EIC?

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet that applies to you **or** let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

1. If, in 2003:
 - 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
 - 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
 - No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* → **No.** You cannot take the credit.
2. Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* → **No.** You cannot take the credit. Put "No" to the left of the entry space for line 41.
3. Is your filing status married filing separately?

Yes. You cannot take the credit. **No.** *Continue* →
4. Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*

Step 2 Investment Income

1. Add the amounts from Form 1040A:

Line 8a _____
 Line 8b + _____
 Line 9a + _____
 Line 10a + _____

Investment Income =

2. Is your investment income more than \$2,600?

Yes.

No. *Continue* →

You cannot take the credit.

3. Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.*

No. *Go to Step 4 on page 40.*

(Continued on page 40)

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)

AND

who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Do you have at least one child who meets the above conditions to be your qualifying child?


Yes. *Go to question 3.* **No.** *Skip question 3; go to Step 4, question 2.*

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?

Yes. *See Qualifying Child of More Than One Person on page 42.* **No.** This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. *Skip Step 4; go to Step 5 on page 41.*


Step 4 Filers Without a Qualifying Child

1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?

Yes.  **No.** *Continue* →

You cannot take the credit.

3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. *Continue* → **No.** 

You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. *Go to Step 5 on page 41.* **No.** 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

(Continued on page 41)

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 _____

Subtract, if included on line 7, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put “PRI” and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put “DFC” and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

Earned Income =

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.**

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See *Credit Figured by the IRS* below. **No.** Go to the worksheet on page 43.

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put “EIC” to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to “Time Lived With You” Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child’s home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.


Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

(Continued on page 42)

Earned Income Credit (EIC) Worksheet—Line 41

Keep for Your Records 

Part 1


All Filers

1. Enter your earned income from Step 5 on page 43.

1	
---	--

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

2	
---	--

If line 2 is zero,  You cannot take the credit. Put “No” to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22.

3	
---	--

4. Are the amounts on lines 3 and 1 the same?
 Yes. Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered “No” on Line 4

5. If you have:
 • No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?
 • 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?
 Yes. Leave line 5 blank; enter the amount from line 2 on line 6.
 No. Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

5	
---	--

 Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

Part 3

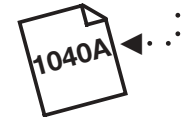
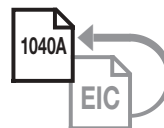
Your Earned Income Credit

6. **This is your earned income credit.**

6	
---	--

 Enter this amount on Form 1040A, line 41.

Reminder—
 ✓ If you have a qualifying child, complete and attach Schedule EIC.



If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.

Complete this Form

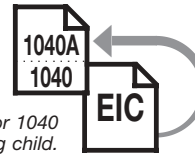
Exhibit 12

SCHEDULE EIC
(Form 1040A or 1040)

Department of the Treasury
Internal Revenue Service

Earned Income Credit
Qualifying Child Information

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.



OMB No. 1545-0074

2003

Attachment
Sequence No. **43**

Name(s) shown on return

Your social security number

Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that (a) you can take the EIC and (b) you have a qualifying child.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.

Qualifying Child Information

Child 1

Child 2

1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	Child 1		Child 2	
	First name	Last name	First name	Last name
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.				

Next, if the child was born after 1984, go to line 4. Otherwise, continue.

3 If the child was born before 1985				
a Was the child under age 24 at the end of 2003 and a student?	<input type="checkbox"/> Yes. Go to line 4.	<input type="checkbox"/> No. Continue	<input type="checkbox"/> Yes. Go to line 4.	<input type="checkbox"/> No. Continue
b Was the child permanently and totally disabled during any part of 2003?	<input type="checkbox"/> Yes. Continue	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. Continue	<input type="checkbox"/> No. The child is not a qualifying child.
4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)				
5 Number of months child lived with you in the United States during 2003				
• If the child lived with you for more than half of 2003 but less than 7 months, enter "7". • If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12".	_____ months Do not enter more than 12 months.		_____ months Do not enter more than 12 months.	



You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.

For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2003

▶▶ **SUMMING UP THIS LESSON** ◀◀

- ▶ The earned income credit can be claimed on Form 1040EZ, Form 1040A or Form 1040.

Exercise 1

- (A) No; to be a qualifying child, the child must live with the taxpayer more than half of the year.
- (B) Neither Donna nor Doug can claim the credit; in order to claim the earned income credit, married taxpayers living together must file a joint return.
- (C) Jimmy and Anna are qualifying children of both Randy and Cara. Randy and Cara can choose which of them will claim the credit based on each child. One can claim the credit on the basis of two children, or each can claim the credit on the basis of one child. If both claim the credit on the basis of the same child or both children, Cara will be entitled to the credit because each child lived with her for the longer period of time during the year.
- (D) Yes. He is between 25 and 65; his earned income is less than \$11,230; he cannot be claimed as a dependent and he is not a qualifying child of another person.
- (E) No; to be a qualifying child, a married child must generally be eligible to be claimed as a dependent by the taxpayer.
- (F) Numbers 1 and 6 should be circled.

Exercise 2

- (A) \$3,120
- (B) \$1,900

EARNED INCOME CREDIT

Lesson 9

ANSWERS TO EXERCISES

Exercise 3

Bell's EIC Worksheet

Earned Income Credit (EIC) Worksheet—Line 41

Keep for Your Records



Part 1


All Filers

1. Enter your earned income from Step 5 on page 43.

1	21,211
---	--------

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

2	1,509
---	-------

If line 2 is zero,  You cannot take the credit. Put "No" to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22.

3	21,250
---	--------

4. Are the amounts on lines 3 and 1 the same?

Yes. Skip line 5; enter the amount from line 2 on line 6.

No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. If you have:

• No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?

• 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?

Yes. Leave line 5 blank; enter the amount from line 2 on line 6.

No. Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

5	\$1,501
---	---------

Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

Part 3

Your Earned Income Credit

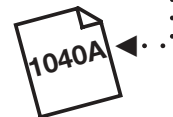
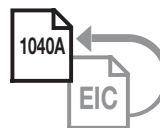
6. This is your earned income credit.

6	\$1,501
---	---------

Enter this amount on Form 1040A, line 41.

Reminder—

- ✓ If you have a qualifying child, complete and attach Schedule EIC.



If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.

Exercise 3

Bell's Eligibility Questions, page 1

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:


- Follow the steps below.
- Complete the worksheet that applies to you **or** let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.





If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

1. If, in 2003:
 - 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
 - 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
 - No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* → **No.**  You cannot take the credit.
2. Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* → **No.**  You cannot take the credit. Put "No" to the left of the entry space for line 41.
3. Is your filing status married filing separately?

Yes.  **No.** *Continue* →

You cannot take the credit.
4. Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*


Step 2 Investment Income

1. Add the amounts from Form 1040A:

Line 8a		\$39
Line 8b	+	0
Line 9a	+	0
Line 10a	+	0

Investment Income = **\$39**

2. Is your investment income more than \$2,600?

Yes.  **No.** *Continue* →

You cannot take the credit.
3. Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.* **No.** *Go to Step 4 on page 40.*

EARNED INCOME CREDIT

Lesson 9

ANSWERS TO EXERCISES

Exercise 3

Bell's Eligibility Questions, page 2

Form 1040A—Line 41

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)

AND

who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes. 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

No. Continue

2. Do you have at least one child who meets the above conditions to be your qualifying child?

Yes. Go to question 3.

No. Skip question 3; go to Step 4, question 2.

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?

Yes. See *Qualifying Child of More Than One Person* on page 42.

No. This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. Skip Step 4; go to Step 5 on page 41.

Step 4 Filers Without a Qualifying Child

1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes. 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

No. Continue

2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?

Yes. 

You cannot take the credit.

No. Continue

3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. Continue

No. 

You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. Go to Step 5 on page 41.

No. 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

Exercise 3

Bell's Eligibility Questions, page 3

Form 1040A—Line 41

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 21,211

Subtract, if included on line 7, any:


- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put "PRI" and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

0

Earned Income = 21,211

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.** 

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See Credit Figured by the IRS below. **No.** Go to the worksheet on page 43.

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put "EIC" to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to "Time Lived With You" Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child's home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

(Continued on page 42)

EARNED INCOME CREDIT

ANSWERS TO EXERCISES

Lesson 9

Exercise 3

Bell's Schedule EIC, page 1

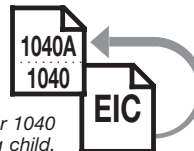
SCHEDULE EIC
(Form 1040A or 1040)

Department of the Treasury
Internal Revenue Service

Earned Income Credit

Qualifying Child Information

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.



OMB No. 1545-0074

2003

Attachment
Sequence No. **43**

Name(s) shown on return

Sam U. and Robin O. Bell

Your social security number

000 00 4797

Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that
(a) you can take the EIC and (b) you have a qualifying child.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.

Qualifying Child Information

Child 1

Child 2

	First name	Last name	First name	Last name
1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	Jennifer	Bell		
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.	000	00	1987	
Next , if the child was born after 1984, go to line 4. Otherwise, continue.				
3 If the child was born before 1985— a Was the child under age 24 at the end of 2003 and a student?	<input type="checkbox"/> Yes. Go to line 4.	<input type="checkbox"/> No. Continue	<input type="checkbox"/> Yes. Go to line 4.	<input type="checkbox"/> No. Continue
b Was the child permanently and totally disabled during any part of 2003?	<input type="checkbox"/> Yes. Continue	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. Continue	<input type="checkbox"/> No. The child is not a qualifying child.
4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)	Daughter			
5 Number of months child lived with you in the United States during 2003 • If the child lived with you for more than half of 2003 but less than 7 months, enter "7". • If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12".	12 months Do not enter more than 12 months.		_____ months Do not enter more than 12 months.	



You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.

For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2003

EARNED INCOME CREDIT

ANSWERS TO EXERCISES

Lesson 9

Exercise 3

Bell's Schedule EIC, page 2

claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000	28	Tax, including any alternative minimum tax (see page 35).	28		
	29	Credit for child and dependent care expenses. Attach Schedule 2.	29		
	30	Credit for the elderly or the disabled. Attach Schedule 3.	30		
	31	Education credits. Attach Form 8863.	31		
	32	Retirement savings contributions credit. Attach Form 8880.	32		
	33	Child tax credit (see page 38).	33		
	34	Adoption credit. Attach Form 8839.	34		
	35	Add lines 29 through 34. These are your total credits .	35	0	00
	36	Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36	0	00
	37	Advance earned income credit payments from Form(s) W-2.	37		
	38	Add lines 36 and 37. This is your total tax .	▶ 38	0	00
	39	Federal income tax withheld from Forms W-2 and 1099.	39		
	40	2003 estimated tax payments and amount applied from 2002 return.	40		
If you have a qualifying child, attach Schedule EIC.	41	Earned income credit (EIC).	41	1,501	00
	42	Additional child tax credit. Attach Form 8812.	42		
	43	Add lines 39 through 42. These are your total payments .	▶ 43	1,501	00

Exercise 4

- (A) See Kyle's completed steps and the EIC worksheet.
 (B) See Kyle's Schedule EIC.

EARNED INCOME CREDIT

Lesson 9

ANSWERS TO EXERCISES

Kyle's EIC Eligibility Questions, page 1

Exercise 4(D)

Form 1040A—Line 41

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet that applies to you or let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

1. If, in 2003:


- 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
- 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
- No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* →


No.  You cannot take the credit.

2. Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* →

No.  You cannot take the credit. Put "No" to the left of the entry space for line 41.

3. Is your filing status married filing separately?

Yes.  You cannot take the credit.

No. *Continue* →

4. Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*

Step 2 Investment Income

1. Add the amounts from Form 1040A:

Line 8a		0
Line 8b	+	0
Line 9a	+	0
Line 10a	+	0

Investment Income =

2. Is your investment income more than \$2,600?

Yes. 

No. *Continue* →

You cannot take the credit.

3. Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.*

No. *Go to Step 4 on page 40.*

Exercise 4(D)

Kyle's EIC Eligibility Questions, page 2

Form 1040A—Line 41

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)

AND


who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes. 

No. *Continue* 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Do you have at least one child who meets the above conditions to be your qualifying child?

Yes. *Go to question 3.* **No.** *Skip question 3; go to Step 4, question 2.*

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?


Yes. *See Qualifying Child of More Than One Person on page 42.*

No. This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. *Skip Step 4; go to Step 5 on page 41.*

Step 4 Filers Without a Qualifying Child

1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes. 

No. *Continue* 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?

Yes. 

No. *Continue* 

You cannot take the credit.


3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. *Continue* 

No. 

You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. *Go to Step 5 on page 41.* **No.** 

You cannot take the credit. Put "No" to the left of the entry space for line 41.

EARNED INCOME CREDIT

Lesson 9

ANSWERS TO EXERCISES

Kyle's EIC Eligibility Questions, page 3

Exercise 4(D)

Form 1040A—Line 41

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 18,751

Subtract, if included on line 7, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put "PRI" and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

0

Earned Income = 18,751

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.** 

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

- Yes.** See Credit Figured by the IRS below.
- No.** Go to the worksheet on page 43.

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put "EIC" to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to "Time Lived With You" Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child's home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

(Continued on page 42)

EARNED INCOME CREDIT

ANSWERS TO EXERCISES

Lesson 9

Exercise 4(D)

Kyle's EIC Worksheet

Earned Income Credit (EIC) Worksheet—Line 41

Keep for Your Records



Part 1


All Filers

1. Enter your earned income from Step 5 on page 43.

1	18,751
---	--------

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

2	1,740
---	-------

If line 2 is zero,  You cannot take the credit. Put "No" to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22.

3	19,223
---	--------

4. Are the amounts on lines 3 and 1 the same?

Yes. Skip line 5; enter the amount from line 2 on line 6.

No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. If you have:

• No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?

• 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?

Yes. Leave line 5 blank; enter the amount from line 2 on line 6.

No. Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

5	1,668
---	-------

Part 3

Your Earned Income Credit

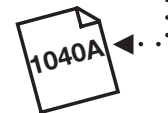
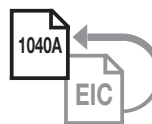
6. This is your earned income credit.

6	1,668
---	-------

Enter this amount on Form 1040A, line 41.

Reminder—

- ✓ If you have a qualifying child, complete and attach Schedule EIC.



If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.



EARNED INCOME CREDIT

Lesson 9

ANSWERS TO EXERCISES

Exercise 4(D)

Evan's Schedule EIC

<p>SCHEDULE EIC (Form 1040A or 1040)</p> <p>Department of the Treasury Internal Revenue Service</p>	<p>Earned Income Credit Qualifying Child Information</p> <p><i>Complete and attach to Form 1040A or 1040 only if you have a qualifying child.</i></p>		<p>OMB No. 1545-0074</p> <p>2003</p> <p>Attachment Sequence No. 43</p>																
Name(s) shown on return Kyle B. Evans		Your social security number 000 00 2442																	
<p>Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that (a) you can take the EIC and (b) you have a qualifying child.</p> <ul style="list-style-type: none"> • If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details. • It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child. • Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213. 																			
																			
<p>Qualifying Child Information</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 40%;"></th> <th style="width: 20%; text-align: center;">Child 1</th> <th style="width: 20%;"></th> <th style="width: 20%; text-align: center;">Child 2</th> </tr> <tr> <td></td> <td style="text-align: center;">First name</td> <td style="text-align: center;">Last name</td> <td style="text-align: center;">First name Last name</td> </tr> </thead> <tbody> <tr> <td>1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.</td> <td style="text-align: center;">Julie</td> <td style="text-align: center;">Evans</td> <td></td> </tr> <tr> <td>2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.</td> <td style="text-align: center;">000 00 4104</td> <td></td> <td></td> </tr> </tbody> </table> <p>Next, if the child was born after 1984, go to line 4. Otherwise, continue.</p>					Child 1		Child 2		First name	Last name	First name Last name	1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	Julie	Evans		2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.	000 00 4104		
	Child 1		Child 2																
	First name	Last name	First name Last name																
1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.	Julie	Evans																	
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.	000 00 4104																		
<p>3 If the child was born before 1985—</p> <p>a Was the child under age 24 at the end of 2003 and a student?</p> <table style="width: 100%;"> <tr> <td style="width: 25%; text-align: center;"><input type="checkbox"/> Yes. <i>Go to line 4.</i></td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> No. <i>Continue</i></td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> Yes. <i>Go to line 4.</i></td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> No. <i>Continue</i></td> </tr> </table> <p>b Was the child permanently and totally disabled during any part of 2003?</p> <table style="width: 100%;"> <tr> <td style="width: 25%; text-align: center;"><input type="checkbox"/> Yes. <i>Continue</i></td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> No. The child is not a qualifying child.</td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> Yes. <i>Continue</i></td> <td style="width: 25%; text-align: center;"><input type="checkbox"/> No. The child is not a qualifying child.</td> </tr> </table>				<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.								
<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>																
<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.																
<p>4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)</p> <p style="text-align: center;">Daughter</p>																			
<p>5 Number of months child lived with you in the United States during 2003</p> <ul style="list-style-type: none"> • If the child lived with you for more than half of 2003 but less than 7 months, enter "7". • If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12". <table style="width: 100%;"> <tr> <td style="width: 50%; text-align: center;">12 months <i>Do not enter more than 12 months.</i></td> <td style="width: 50%; text-align: center;">_____ months <i>Do not enter more than 12 months.</i></td> </tr> </table>				12 months <i>Do not enter more than 12 months.</i>	_____ months <i>Do not enter more than 12 months.</i>														
12 months <i>Do not enter more than 12 months.</i>	_____ months <i>Do not enter more than 12 months.</i>																		
<p>TIP You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.</p>																			
For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.		Cat. No. 13339M	Schedule EIC (Form 1040A or 1040) 2003																

INTRODUCTION AND OBJECTIVES

In this lesson you will learn about the child tax credit. This credit is unique because it can be both nonrefundable and refundable. This lesson will discuss who qualifies for the credit and how to calculate the credit.

After completing this lesson you should be able to:

- Explain the advance child tax credit and determine who received the advance payment.
- Calculate the child tax credit using the child tax credit worksheet.
- Calculate the additional child tax credit by using form 8812.

ADVANCE CHILD TAX CREDIT PAYMENTS

The Jobs and Growth Tax Relief Reconciliation Act of 2003 raised the Child Tax Credit to a maximum of \$1,000 per child from \$600 per child, beginning in 2003. The Act also provided for immediate tax relief by directing the Treasury to send this increase to taxpayers last summer. Eligible taxpayers could receive up to \$400 for each child claimed on their 2002 returns as an advance payment of their 2003 Child Tax Credit.

The IRS used 2002 tax year data to determine who was issued the advance payment. Generally:

- Taxpayers must have claimed the Child Tax Credit on the 2002 tax return.
- Taxpayers must have used Form 1040 or Form 1040A, or filed electronically.
- The child must have been born after 1986.

There were no actions required of the Taxpayers to receive the advance payment. The IRS automatically sent notices to eligible taxpayers. The IRS notice was followed a few days later by the advance payment check. Both the notice and the check were mailed to the address listed on the taxpayer's 2002 tax return. Anyone who had moved since the filing of the 2002 return should have notified the U.S. Postal Service of the new address, and the notice and check were forwarded.

ALERT



Beginning in 2003, the Child Tax Credit increased to \$1,000 per qualifying child.

The advance payment checks were mailed July 25th, August 1st, and August 8th to taxpayers who filed their returns by April 15th. The checks were issued based on the last two digits of the Social Security number listed first on the 2002 tax return. Taxpayers whose last two digits are the lowest received their checks first.

Taxpayers who received filing extensions still got the advance payment checks if they were eligible. They were mailed between four to six weeks after the IRS received their 2002 tax return.

If the taxpayer received the advance Child Tax Credit payment, he or she must include the amount received on the Child Tax Credit Worksheet when calculating the 2003 Child Tax Credit.

The IRS established a new service at *www.irs.gov: Where's My Advance Child Tax Credit?* This new service provides on-line advance child tax credit payment information. The information includes the amount of a taxpayer's advance payment, the check mailing date, and any offsets to outstanding liabilities.

Since the taxpayers must figure their advance payments into their calculations for their 2003 child tax credit, *Where's My Advance Child Tax Credit?* information will be available through April 15, 2004.

ALERT



Beginning in 2003, the Child Tax Credit increased to \$1,000 per child.

CHILD TAX CREDIT

A taxpayer can claim a child tax credit for each of the taxpayer's qualifying children. The maximum child tax credit is \$1000 per child for 2003. The credit can be claimed on either Form 1040 or 1040A.

Qualifying child

To qualify, the child must be:

- Under age 17 at the end of 2003,
- A citizen or resident of the United States,
- The taxpayer's dependent, and
- The taxpayer's:
 - Son or daughter,
 - Stepson or stepdaughter, adopted child,
 - Grandchild, or
 - Eligible foster child

The taxpayer must provide the name and identification number (usually a social security number) of each qualifying child on his or her tax return.

Limits on credit

The amount of a taxpayer's child tax credit depends on the taxpayer's modified adjusted gross income (modified AGI) and the taxpayer's filing status.

Modified AGI

The credit begins to phase out if the taxpayer's modified AGI is above a certain amount (**Table 1**). For most taxpayers, modified AGI is generally the same as AGI. For 2003, AGI is shown on line 21 of Form 1040A and on line 34 of Form 1040.

Table 1: <i>Child Tax Credit</i> Threshold Modified AGI Amounts for Claiming Child Tax Credit	
Filing Status	Amount
Married filing jointly	\$110,000
Qualifying widow(er)	75,000
Head of household	75,000
Single	75,000
Married filing separately	55,000

Before you can figure a taxpayer's credit amount for the year, you must have the taxpayer answer certain questions (Exhibit 1) to see if you must use the worksheet in Publication 972, *Child Tax Credit*. These questions are in the tax form instructions. If you do not need to use Publication 972, you can use the shorter *Child Tax Credit Worksheet* in the form instructions.

Example 1

Bill and Mary Allen have two dependent children under age 17. The children are qualifying children for purposes of claiming the child tax credit. Bill and Mary have modified AGI of \$34,000. They received an \$800 advance child tax credit payment last summer. Their tax on line 43 for 2003 is \$4,503. Bill and Mary need to answer questions to determine if they must use Publication 972 (Exhibit 1). The completed Child Tax Credit Worksheet (Exhibit 2) shows that their credit is \$1,200, after considering the advance child tax credit payment. Their modified AGI is less than the phaseout amount for their filing status (\$110,000).

Form 1040—Line 49

Line 49—Child Tax Credit

What Is the Child Tax Credit?

This credit is for people who have a qualifying child as defined below. It is in addition to the credit for child and dependent care expenses on Form 1040, line 45, and the earned income credit on Form 1040, line 63.

Three Steps To Take the Child Tax Credit!

- Step 1.** Make sure you have a qualifying child for the child tax credit. See **Qualifying Child for Child Tax Credit** below.
- Step 2.** Make sure you checked the box in column (4) of line 6c on Form 1040 for each qualifying child.
- Step 3.** Answer the questions on this page to see if you may use the worksheet on page 39 to figure your credit or if you must use Pub. 972, Child Tax Credit. If you need Pub. 972, see page 9.

Qualifying Child for Child Tax Credit

A qualifying child for purposes of the child tax credit is a child who:

- Is claimed as your dependent on line 6c, **and**
- Was **under age 17** at the end of 2003, **and**
- Is your (a) son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild); (b) brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew), whom you cared for as you would your own child; or (c) foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child), **and**
- Is a U.S. citizen or resident alien.

Note. The above requirements are not the same as the requirements to be a qualifying child for the earned income credit.

An **adopted child** is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

A **grandchild** is any descendant of your son, daughter, adopted child, or stepchild and includes your great-grandchild, great-great-grandchild, etc.

Questions

Who Must Use Pub. 972



1. Are you excluding income from Puerto Rico **or** are you filing any of the following forms?
 - Form 2555 or 2555-EZ (relating to foreign earned income)
 - Form 4563 (exclusion of income for residents of American Samoa)

No. *Continue* **Yes.** You must use Pub. 972 to figure your credit.

2. Is the amount on Form 1040, line 35, more than the amount shown below for your filing status?
 - Married filing jointly – \$110,000
 - Single, head of household, or qualifying widow(er) – \$75,000
 - Married filing separately – \$55,000

No. *Continue* **Yes.** You must use Pub. 972 to figure your credit.

3. Are you claiming any of the following credits?
 - Adoption credit, Form 8839 (see the instructions for Form 1040, line 50, on page 40)
 - Mortgage interest credit, Form 8396 (see the instructions for Form 1040, line 51, on page 40)
 - District of Columbia first-time homebuyer credit, Form 8859

No. Use the worksheet on page 39 to figure your child tax credit. **Yes.** You must use Pub. 972 to figure your child tax credit. You will also need the form(s) listed above for any credit(s) you are claiming.

Need more information or forms? See page 7.

Child Tax Credit Worksheet—Line 49

Keep for Your Records

Before you begin: If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



- To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2003 and meet the other requirements listed on page 38.
- **Do not** use this worksheet if you answered “Yes” to question 1, 2, or 3 on page 38. Instead, use Pub. 972.

1. Number of qualifying children: 2 X \$1,000. Enter the result. 1 | \$2,000

2. Enter the amount, if any, of your advance child tax credit (before offset). 2 | \$800

3. Is line 1 less than or equal to line 2?
 Yes. You cannot take this credit. If line 2 is more than line 1, you do not have to pay back the difference.
 No. Subtract line 2 from line 1. 3 | \$1,200

4. Enter the amount from Form 1040, line 43. 4 | \$4,503

5. Enter the total of the amounts from Form 1040, lines 44 through 48. 5 | \$0

6. Are the amounts on lines 4 and 5 the same?
 Yes. You cannot take this credit because there is no tax to reduce. However, you may be able to take the **additional child tax credit**. See the **TIP** below.
 No. Subtract line 5 from line 4. 6 | \$4,503

7. Is the amount on line 3 more than the amount on line 6?
 Yes. Enter the amount from line 6. Also, you may be able to take the **additional child tax credit**. See the **TIP** below.
 No. Enter the amount from line 3. 7 | \$1,200

} **This is your child tax credit.**
Enter this amount on Form 1040, line 49.



You may be able to take the **additional child tax credit** on Form 1040, line 65, if you answered “Yes” on line 6 or line 7 above.

- First, complete your Form 1040 through line 64.
- Then, use Form 8812 to figure any additional child tax credit.

Draft as of 08/27/2003

ADDITIONAL CHILD TAX CREDIT

The child tax credit is a nonrefundable credit that gives eligible taxpayers \$1000 for each qualifying child. If a taxpayer's tax liability is less than the allowable nonrefundable child tax credit, the taxpayer may be eligible to claim the **refundable additional child tax credit**.

The additional child tax credit was expanded to include **all** taxpayers who have **earned income**, regardless of the number of qualifying children. This extended the refundable part of the child tax credit to families who have less than three qualified children.

Before figuring additional child tax credit, figure the taxpayer's:

- Unused nonrefundable child tax credit amount,
- Total Social Security and Medicare taxes withheld (Form W-2, *Wage and Tax Statement*, boxes 4 and 6),
- Earned income credit amount,
- Total taxable earned income (back of Form 8812), and
- For 1040 filers, one-half of self-employment tax paid, Form 1040, line 29.

The taxpayer will need to seek the assistance of a paid professional tax preparer if he or she has:

- Excess social security and RRTA tax withheld (more than one employer and gross income in excess of \$84,900) or
- Social Security and Medicare tax on **unreported** tip income.

Taxpayers must use **Form 8812**, *Additional Child Tax Credit*, to claim the additional child tax credit. This credit is based on 10% of the taxpayer's taxable earned income in excess of \$10,500.

Form 8812 explains step-by-step how to compute the additional child tax credit. The form allows a taxpayer who can use both rules to claim the larger additional child tax credit. That is, taxpayers with three or more children can continue to claim a refundable additional tax credit, under the rules that applied in prior years, if that amount is greater than the refundable credit based on the taxpayer's earned income in excess of \$10,500.

Example 2

Maureen Langston is filing Form 1040. Her filing status is head of household for 2003. She has five dependent children, all of whom are qualifying children for purposes of the child tax credit. Maureen received a \$2,000 advance child tax credit payment check in August 2003. Maureen's earned income (and adjusted gross income) is \$26,375, her tax is \$149, Social Security/Medicare taxes are \$2,018, and the earned income credit is \$1,433. Based on this information, Maureen's child tax credit is \$149 (Exhibit 4) and her additional child tax credit is \$1,588. Exhibits 5 and 6 illustrate how Maureen's additional child tax credit was figured.

POTENTIAL PITFALLS



When figuring the additional child tax credit, you must use the back of Form 8812 to determine taxable earned income (line 4).

Form 1040—Line 49

Line 49—Child Tax Credit

What Is the Child Tax Credit?

This credit is for people who have a qualifying child as defined below. It is in addition to the credit for child and dependent care expenses on Form 1040, line 45, and the earned income credit on Form 1040, line 63.

Three Steps To Take the Child Tax Credit!

- Step 1.** Make sure you have a qualifying child for the child tax credit. See **Qualifying Child for Child Tax Credit** below.
- Step 2.** Make sure you checked the box in column (4) of line 6c on Form 1040 for each qualifying child.
- Step 3.** Answer the questions on this page to see if you may use the worksheet on page 39 to figure your credit or if you must use Pub. 972, Child Tax Credit. If you need Pub. 972, see page 9.

Qualifying Child for Child Tax Credit

A qualifying child for purposes of the child tax credit is a child who:

- Is claimed as your dependent on line 6c, **and**
- Was **under age 17** at the end of 2003, **and**
- Is your **(a)** son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild); **(b)** brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew), whom you cared for as you would your own child; or **(c)** foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child), **and**
- Is a U.S. citizen or resident alien.

Note. The above requirements are not the same as the requirements to be a qualifying child for the earned income credit.

An **adopted child** is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

A **grandchild** is any descendant of your son, daughter, adopted child, or stepchild and includes your great-grandchild, great-great-grandchild, etc.

Questions

Who Must Use Pub. 972



1. Are you excluding income from Puerto Rico **or** are you filing any of the following forms?
 - Form 2555 or 2555-EZ (relating to foreign earned income)
 - Form 4563 (exclusion of income for residents of American Samoa)

No. *Continue*

Yes. You must use Pub. 972 to figure your credit.

2. Is the amount on Form 1040, line 35, more than the amount shown below for your filing status?
 - Married filing jointly – \$110,000
 - Single, head of household, or qualifying widow(er) – \$75,000
 - Married filing separately – \$55,000

No. *Continue*

Yes. You must use Pub. 972 to figure your credit.

3. Are you claiming any of the following credits?
 - Adoption credit, Form 8839 (see the instructions for Form 1040, line 50, on page 40)
 - Mortgage interest credit, Form 8396 (see the instructions for Form 1040, line 51, on page 40)
 - District of Columbia first-time homebuyer credit, Form 8859

No. Use the worksheet on page 39 to figure your child tax credit.

Yes. You must use Pub. 972 to figure your child tax credit. You will also need the form(s) listed above for any credit(s) you are claiming.

Need more information or forms? See page 7.

Child Tax Credit Worksheet—Line 49

Keep for Your Records

Before you begin:

✓ If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



- To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2003 and meet the other requirements listed on page 38.
- **Do not** use this worksheet if you answered “Yes” to question 1, 2, or 3 on page 38. Instead, use Pub. 972.

1. Number of qualifying children: 5 X \$1,000. Enter the result. 1 \$5,000

2. Enter the amount, if any, of your advance child tax credit (before offset). 2 \$2,000

3. Is line 1 less than or equal to line 2?
 Yes. You cannot take this credit. If line 2 is more than line 1, you do not have to pay back the difference.
 No. Subtract line 2 from line 1. 3 \$3,000

4. Enter the amount from Form 1040, line 43. 4 \$149

5. Enter the total of the amounts from Form 1040, lines 44 through 48. 5 \$0

6. Are the amounts on lines 4 and 5 the same?
 Yes. You cannot take this credit because there is no tax to reduce. However, you may be able to take the **additional child tax credit**. See the **TIP** below.
 No. Subtract line 5 from line 4. 6 \$149

7. Is the amount on line 3 more than the amount on line 6?
 Yes. Enter the amount from line 6. Also, you may be able to take the **additional child tax credit**. See the **TIP** below.
 No. Enter the amount from line 3. 7 \$149
} This is your child tax credit.
Enter this amount on Form 1040, line 49.



You may be able to take the **additional child tax credit** on Form 1040, line 65, if you answered “Yes” on line 6 or line 7 above.

- First, complete your Form 1040 through line 64.
- Then, use Form 8812 to figure any additional child tax credit.

Form 8812 Department of the Treasury Internal Revenue Service	<h2 style="margin:0;">Additional Child Tax Credit</h2> <p style="font-size: small; margin: 5px 0;">Complete and attach to Form 1040 or Form 1040A.</p>		OMB No. 1545-1620 <h1 style="margin: 0;">2003</h1> Attachment Sequence No. 47
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Name(s) shown on return Maureen Langston Your social security number
000 : 00 : 9999

Part I All Filers

1 Enter the amount from line 3 of your Child Tax Credit Worksheet on page 40 of the Form 1040 instructions or page 39 of the Form 1040A instructions. If you used Pub. 972, enter the amount from line 10 of the worksheet on page 3 of the publication	1	\$3,000	
2 Enter the amount from Form 1040, line 49, or Form 1040A, line 33	2	\$149	
3 Subtract line 2 from line 1. If zero, stop ; you cannot take this credit	3	\$2,851	
4 Enter your total taxable earned income. See the instructions on back	4	\$26,375	
5 Is the amount on line 4 more than \$10,500? <input type="checkbox"/> No. Leave line 5 blank and enter -0- on line 6. <input checked="" type="checkbox"/> Yes. Subtract \$10,500 from the amount on line 4. Enter the result	5	\$15,875	
6 Multiply the amount on line 5 by 10% (.10) and enter the result Next. Do you have three or more qualifying children? <input type="checkbox"/> No. If line 6 is zero, stop ; you cannot take this credit. Otherwise, skip Part II and enter the smaller of line 3 or line 6 on line 13. <input checked="" type="checkbox"/> Yes. If line 6 is equal to or more than line 3, skip Part II and enter the amount from line 3 on line 13. Otherwise, go to line 7.	6	\$1,588	

Part II Certain Filers Who Have Three or More Qualifying Children

7 Enter the total of the withheld social security and Medicare taxes from Form(s) W-2, boxes 4 and 6. If married filing jointly, include your spouse's amounts with yours. If you worked for a railroad, see the instructions on back	7	\$2,018	
8 1040 filers: Enter the total of the amounts from Form 1040, lines 28 and 56, plus any uncollected social security and Medicare or tier 1 RRTA taxes included on line 60. 1040A filers: Enter -0-.	8	\$0	
9 Add lines 7 and 8	9	\$2,018	
10 1040 filers: Enter the total of the amounts from Form 1040, lines 63 and 64. 1040A filers: Enter the total of the amount from Form 1040A, line 41, plus any excess social security and tier 1 RRTA taxes withheld that you entered to the left of line 43 (see the instructions on back).	10	\$1,433	
11 Subtract line 10 from line 9. If zero or less, enter -0-	11	\$585	
12 Enter the larger of line 6 or line 11 here Next, enter the smaller of line 3 or line 12 on line 13.	12	\$1,588	

Part III Your Additional Child Tax Credit

13 This is your additional child tax credit	13	\$1,588	
--	----	---------	--

Enter this amount on Form 1040, line 65, or Form 1040A, line 42.

Instructions

Purpose of Form

Use Form 8812 to figure your additional child tax credit.



The additional child tax credit may give you a refund even if you do not owe any tax.

Who Should Use Form 8812

First, complete the Child Tax Credit Worksheet that applies to you. See the instructions for Form 1040, line 49, or Form 1040A, line 33. If you meet the condition given in the **TIP** at the end of your Child Tax Credit Worksheet, use Form 8812 to see if you can take the additional child tax credit.

Effect of Credit on Welfare Benefits

Any refund you receive as a result of taking the additional child tax credit will not be used to determine if you are eligible for the following programs, or how much you can receive from them.

- Temporary Assistance for Needy Families (TANF).
- Medicaid and supplemental security income (SSI).
- Food stamps and low-income housing.

Taxable Earned Income

1. Did you, or your spouse if filing a joint return, have net earnings from self-employment and use either optional method to figure those net earnings?

- No.** Go to question 2.
- Yes.** Use Pub. 972 to figure the amount to enter on Form 8812, line 4.

2. Are you claiming the earned income credit (EIC) on Form 1040, line 63, or Form 1040A, line 41?

- Yes.** Use the following chart to find the amount to enter on Form 8812, line 4.

IF you are filing Form...	AND you completed...	THEN enter on Form 8812, line 4, the amount from...
1040	Worksheet B on page 48 of your 1040 instructions	Worksheet B, line 4b.*
	Step 5 on page 45 of your 1040 instructions (but not Worksheet B)	Step 5, Earned Income
1040A	Step 5 on page 43 of your 1040A instructions	Step 5, Earned Income

* If you were a member of the clergy, subtract the following from the amount on line 4b: (a) the rental value of a home or the nontaxable portion of an allowance for a home furnished to you (including payments for utilities) and (b) the value of meals and lodging provided to you, your spouse, and your dependents for your employer's convenience.

- No.** **1040 filers:** Go to question 3.
1040A filers: Skip question 3 and go to question 4.

3. Were you, or your spouse if filing a joint return, self-employed, or are you filing Schedule SE because you were a member of the clergy or you had church employee income, or are you filing Schedule C or C-EZ as a statutory employee?

- No.** Go to question 4.
- Yes.** Use Pub. 972 to figure the amount to enter on Form 8812, line 4.

4. Does the amount on line 7 of Form 1040 or Form 1040A include any of the following amounts?

- Taxable scholarship or fellowship grants not reported on a W-2 form.
 - Amounts paid to an inmate in a penal institution for work (put "PRI" and the amount paid in the space next to line 7 of Form 1040 or 1040A).
 - Amounts received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount received in the space next to line 7 of Form 1040 or 1040A). This amount may be reported in box 11 of your W-2 form. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.
 - Amounts from Form 2555, line 41, or Form 2555-EZ, line 18.
- No.** Enter the amount from line 7 of Form 1040 or Form 1040A on Form 8812, line 4.
- Yes.** Subtract the total of those amounts from the amount on line 7 of Form 1040 or Form 1040A. (If an amount is included in more than one of the above categories, include it only once in figuring the total amount to subtract.) Enter the result on Form 8812, line 4.

Railroad Employees

If you worked for a railroad, include the following taxes in the total on Form 8812, line 7.

- Tier 1 tax withheld from your pay. This tax should be shown in box 14 of your W-2 form(s) and identified as "Tier 1 tax."
- If you were an employee representative, 50% of the total tier 1 tax and tier 1 Medicare tax you paid for 2003.

1040A Filers

If you, or your spouse if filing a joint return, had more than one employer for 2003 and total wages of over \$87,000, figure any excess social security and tier 1 railroad retirement (RTA) taxes withheld. See the instructions for Form 1040A, line 43. Include any excess on Form 8812, line 10.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Internal Revenue Code section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is: **Recordkeeping**, 6 min.; **Learning about the law or the form**, 5 min.; **Preparing the form**, 28 min.; **Copying, assembling, and sending the form to the IRS**, 20 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. See the Instructions for Form 1040 or Form 1040A.



Exercise 1

Emily and Victor (SSN-000-00-4410) Howard are married taxpayers with four children. They file married filing jointly for 2003 on Form 1040A. All of their children are qualifying for purposes of the child tax credit. The Howards received a \$1,600 advance child tax credit payment in August 2003. Their adjusted gross income is \$31,467, of which \$18,467 is taxable earned income and \$13,000 is unemployment compensation. The Howards' taxable income is \$3,667, Social Security/Medicare taxes are \$1,413, and the earned income credit is \$569. They have no other credits entered in lines 29-32. Based on the facts given, figure the Howards:

- A. Child tax credit
- B. Additional child tax credit.

Exhibit 7

Complete this Form.

Line 33—Child Tax Credit

What Is the Child Tax Credit?

This credit is for people who have a qualifying child as defined below. It is in addition to the credit for child and dependent care expenses on Form 1040A, line 29, and the earned income credit on Form 1040A, line 41.

Three Steps To Take the Child Tax Credit!

- Step 1.** Make sure you have a qualifying child for the child tax credit. See **Qualifying Child for Child Tax Credit** below.
- Step 2.** Make sure you checked the box in column (4) of line 6c on Form 1040A for each qualifying child.
- Step 3.** Answer the questions on this page to see if you may use the worksheet on page 37 to figure your credit or if you must use Pub. 972, Child Tax Credit. If you need Pub. 972, see page 7.

Qualifying Child for Child Tax Credit. A qualifying child for purposes of the child tax credit is a child who:

- Is claimed as your dependent on line 6c, **and**
- Was **under age 17** at the end of 2003, **and**
- Is your **(a)** son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild); **(b)** brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew), whom you cared for as you would your own child; or **(c)** a foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child), **and**
- Is a U.S. citizen or resident alien.

Note. The above requirements are not the same as the requirements to be a qualifying child for the earned income credit.

An **adopted child** is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.


A **grandchild** is any descendant of your son, daughter, adopted child, or stepchild and includes your great-grandchild, great-great-grandchild, etc.


Questions

Who Must Use Pub. 972



1. Is the amount on Form 1040A, line 22, more than the amount shown below for your filing status?
 - Married filing jointly – \$110,000
 - Single, head of household, or qualifying widow(er) – \$75,000
 - Married filing separately – \$55,000

No. *Continue* 

Yes.  You must use Pub. 972 to figure your credit.
2. Are you claiming the adoption credit on Form 8839 (see the instructions for Form 1040A, line 34, on page 38)?
 - No.** Use the worksheet on page 37 to figure your child tax credit.
 - Yes.** You must use Pub. 972 to figure your child tax credit. You will also need Form 8839.

Child Tax Credit Worksheet—Line 33

Keep for Your Records

Before you begin: ✓ If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



If you received Notice 1319, have it available. The notice shows the amount of your advance payment (before offset). If you do not have Notice 1319, you can check the amount of your advance payment (before offset) on the IRS website at www.irs.gov. You will need to enter your SSN, your 2002 filing status, and the total number of exemptions you claimed on line 6d of your 2002 Form 1040 or Form 1040A.



- To be a qualifying child for the child tax credit, the child must be under age 17 at the end of 2003 and meet the other requirements listed on page 38.
Do not use this worksheet if you answered "Yes" to question 1 or 2 on page 38. Instead, use Pub. 972.

1. Number of qualifying children: _____ x \$1,000. Enter the result.
2. Enter the amount, if any, of your advance child tax credit (before offset).
3. Is line 1 less than or equal to line 2?
4. Enter the amount from Form 1040A, line 28.
5. Add the amounts from Form 1040A, lines 29 through 32.
6. Are the amounts on lines 4 and 5 the same?
7. Is the amount on line 3 more than the amount on line 6? This is your child tax credit.



You may be able to take the additional child tax credit on Form 1040A, line 42, if you answered "Yes" on line 6 or line 7 above.

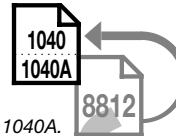
- First, complete your Form 1040A through line 41.
Then, use Form 8812 to figure any additional child tax credit.



Enter this amount on Form 1040A, line 33.

Form **8812**

Additional Child Tax Credit



OMB No. 1545-1620

2003

Attachment Sequence No. **47**

Department of the Treasury
Internal Revenue Service

Complete and attach to Form 1040 or Form 1040A.

Name(s) shown on return

Your social security number

Part I All Filers

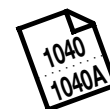
1	Enter the amount from line 3 of your Child Tax Credit Worksheet on page 40 of the Form 1040 instructions or page 39 of the Form 1040A instructions. If you used Pub. 972, enter the amount from line 10 of the worksheet on page 3 of the publication				1
2	Enter the amount from Form 1040, line 49, or Form 1040A, line 33				2
3	Subtract line 2 from line 1. If zero, stop ; you cannot take this credit				3
4	Enter your total taxable earned income. See the instructions on back				4
5	Is the amount on line 4 more than \$10,500? <input type="checkbox"/> No. Leave line 5 blank and enter -0- on line 6. <input type="checkbox"/> Yes. Subtract \$10,500 from the amount on line 4. Enter the result				5
6	Multiply the amount on line 5 by 10% (.10) and enter the result Next. Do you have three or more qualifying children? <input type="checkbox"/> No. If line 6 is zero, stop ; you cannot take this credit. Otherwise, skip Part II and enter the smaller of line 3 or line 6 on line 13. <input type="checkbox"/> Yes. If line 6 is equal to or more than line 3, skip Part II and enter the amount from line 3 on line 13. Otherwise, go to line 7.				6

Part II Certain Filers Who Have Three or More Qualifying Children

7	Enter the total of the withheld social security and Medicare taxes from Form(s) W-2, boxes 4 and 6. If married filing jointly, include your spouse's amounts with yours. If you worked for a railroad, see the instructions on back				
8	1040 filers: Enter the total of the amounts from Form 1040, lines 28 and 56, plus any uncollected social security and Medicare or tier 1 RRTA taxes included on line 60. 1040A filers: Enter -0-.				
9	Add lines 7 and 8				
10	1040 filers: Enter the total of the amounts from Form 1040, lines 63 and 64. 1040A filers: Enter the total of the amount from Form 1040A, line 41, plus any excess social security and tier 1 RRTA taxes withheld that you entered to the left of line 43 (see the instructions on back).				
11	Subtract line 10 from line 9. If zero or less, enter -0-				11
12	Enter the larger of line 6 or line 11 here Next , enter the smaller of line 3 or line 12 on line 13.				12

Part III Your Additional Child Tax Credit

13	This is your additional child tax credit				13
----	--	--	--	--	----



Enter this amount on Form 1040, line 65, or Form 1040A, line 42.

For Paperwork Reduction Act Notice, see back of form.

Cat. No. 10644E

Form **8812** (2003)

Instructions

Purpose of Form

Use Form 8812 to figure your additional child tax credit.



The additional child tax credit may give you a refund even if you do not owe any tax.

Who Should Use Form 8812

First, complete the Child Tax Credit Worksheet that applies to you. See the instructions for Form 1040, line 49, or Form 1040A, line 33. If you meet the condition given in the **TIP** at the end of your Child Tax Credit Worksheet, use Form 8812 to see if you can take the additional child tax credit.

Effect of Credit on Welfare Benefits

Any refund you receive as a result of taking the additional child tax credit will not be used to determine if you are eligible for the following programs, or how much you can receive from them.

- Temporary Assistance for Needy Families (TANF).
- Medicaid and supplemental security income (SSI).
- Food stamps and low-income housing.

Taxable Earned Income

1. Did you, or your spouse if filing a joint return, have net earnings from self-employment and use either optional method to figure those net earnings?

- No.** Go to question 2.
- Yes.** Use Pub. 972 to figure the amount to enter on Form 8812, line 4.

2. Are you claiming the earned income credit (EIC) on Form 1040, line 63, or Form 1040A, line 41?

- Yes.** Use the following chart to find the amount to enter on Form 8812, line 4.

IF you are filing Form...	AND you completed...	THEN enter on Form 8812, line 4, the amount from...
1040	Worksheet B on page 48 of your 1040 instructions	Worksheet B, line 4b.*
	Step 5 on page 45 of your 1040 instructions (but not Worksheet B)	Step 5, Earned Income
1040A	Step 5 on page 43 of your 1040A instructions	Step 5, Earned Income

* If you were a member of the clergy, subtract the following from the amount on line 4b: (a) the rental value of a home or the nontaxable portion of an allowance for a home furnished to you (including payments for utilities) and (b) the value of meals and lodging provided to you, your spouse, and your dependents for your employer's convenience.

- No. 1040 filers:** Go to question 3.
1040A filers: Skip question 3 and go to question 4.

3. Were you, or your spouse if filing a joint return, self-employed, or are you filing Schedule SE because you were a member of the clergy or you had church employee income, or are you filing Schedule C or C-EZ as a statutory employee?

- No.** Go to question 4.
- Yes.** Use Pub. 972 to figure the amount to enter on Form 8812, line 4.

4. Does the amount on line 7 of Form 1040 or Form 1040A include any of the following amounts?

- Taxable scholarship or fellowship grants not reported on a W-2 form.
 - Amounts paid to an inmate in a penal institution for work (put "PRI" and the amount paid in the space next to line 7 of Form 1040 or 1040A).
 - Amounts received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount received in the space next to line 7 of Form 1040 or 1040A). This amount may be reported in box 11 of your W-2 form. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.
 - Amounts from Form 2555, line 41, or Form 2555-EZ, line 18.
- No.** Enter the amount from line 7 of Form 1040 or Form 1040A on Form 8812, line 4.
- Yes.** Subtract the total of those amounts from the amount on line 7 of Form 1040 or Form 1040A. (If an amount is included in more than one of the above categories, include it only once in figuring the total amount to subtract.) Enter the result on Form 8812, line 4.

Railroad Employees

If you worked for a railroad, include the following taxes in the total on Form 8812, line 7.

- Tier 1 tax withheld from your pay. This tax should be shown in box 14 of your W-2 form(s) and identified as "Tier 1 tax."
- If you were an employee representative, 50% of the total tier 1 tax and tier 1 Medicare tax you paid for 2003.

1040A Filers

If you, or your spouse if filing a joint return, had more than one employer for 2003 and total wages of over \$87,000, figure any excess social security and tier 1 railroad retirement (RRTA) taxes withheld. See the instructions for Form 1040A, line 43. Include any excess on Form 8812, line 10.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Internal Revenue Code section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is: **Recordkeeping**, 6 min.; **Learning about the law or the form**, 5 min.; **Preparing the form**, 28 min.; **Copying, assembling, and sending the form to the IRS**, 20 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. See the Instructions for Form 1040 or Form 1040A.

Line 33—Child Tax Credit

What Is the Child Tax Credit?

This credit is for people who have a qualifying child as defined in the instructions for line 6c, column (4), that begin on page 25. It is in addition to the credit for child and dependent care expenses on Form 1040A, line 33, and the earned income credit on Form 1040A, line 50.


Three Steps To Take the Child Tax Credit!

- Step 1.** Make sure you have a qualifying child for the child tax credit. See the instructions for line 6c, column (4), that begin on page 25.
- Step 2.** Make sure you checked the box in column (4) of line 6c on Form 1040A for each qualifying child.
- Step 3.** Answer the questions on this page to see if you may use the worksheet on page 39 to figure your credit or if you must use Pub. 972, Child Tax Credit. If you need Pub. 972, see page 9.

Questions

Who Must Use Pub. 972



1. Is the amount on Form 1040A, line 22, more than the amount shown below for your filing status?
- Married filing jointly – \$110,000
 - Single, head of household, or qualifying widow(er) – \$75,000
 - Married filing separately – \$55,000
- No.** Continue ↘ **Yes.**  You must use Pub. 972 to figure your credit.
2. Are you claiming the adoption credit on Form 8839 (see the instructions for Form 1040A, line 34, on page 40)?
- No.** Use the worksheet on page 39 to figure your child tax credit. **Yes.** You must use Pub. 972 to figure your child tax credit. You will also need Form 8839.

Exercise 1(A)

The Howard's Child Tax Worksheet.

Form 1040A—Line 33

Child Tax Credit Worksheet—Line 33

Keep for Your Records

Before you begin: ✓ If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



If you received Notice 1319, have it available. The notice shows the amount of your advance payment (before offset). If you do not have Notice 1319, you can check the amount of your advance payment (before offset) on the IRS website at www.irs.gov. You will need to enter your SSN, your 2002 filing status, and the total number of exemptions you claimed on line 6d of your 2002 Form 1040 or Form 1040A.



- To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2003 and meet the other requirements listed on page 38.
- **Do not** use this worksheet if you answered “Yes” to question 1 or 2 on page 38. Instead, use Pub. 972.

<p>1. Number of qualifying children: <u>4</u> × \$1,000. Enter the result.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">1</td> <td>\$4,000</td> </tr> </table>	1	\$4,000
1	\$4,000		
<p>2. Enter the amount, if any, of your advance child tax credit (before offset).</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">2</td> <td>\$1,600</td> </tr> </table>	2	\$1,600
2	\$1,600		
<p>3. Is line 1 less than or equal to line 2? <input type="checkbox"/> Yes. You cannot take this credit. If line 2 is more than line 1, you do not have to pay back the difference.</p> <p><input checked="" type="checkbox"/> No. Subtract line 2 from line 1.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">3</td> <td>\$2,400</td> </tr> </table>	3	\$2,400
3	\$2,400		
<p>4. Enter the amount from Form 1040A, line 28.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">4</td> <td>\$368</td> </tr> </table>	4	\$368
4	\$368		
<p>5. Add the amounts from Form 1040A, lines 29 through 32.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">5</td> <td>\$0</td> </tr> </table>	5	\$0
5	\$0		
<p>6. Are the amounts on lines 4 and 5 the same? <input type="checkbox"/> Yes. You cannot take this credit because there is no tax to reduce. However, you may be able to take the additional child tax credit. See the TIP below.</p> <p><input checked="" type="checkbox"/> No. Subtract line 5 from line 4.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">6</td> <td>\$368</td> </tr> </table>	6	\$368
6	\$368		
<p>7. Is the amount on line 3 more than the amount on line 6? <input checked="" type="checkbox"/> Yes. Enter the amount from line 6. Also, you may be able to take the additional child tax credit. See the TIP below. <input type="checkbox"/> No. Enter the amount from line 3.</p>	<table border="1" style="width: 100%; text-align: center;"> <tr> <td style="width: 30px;">7</td> <td>\$368</td> </tr> </table> <p><i>Enter this amount on Form 1040A, line 33.</i></p>	7	\$368
7	\$368		

This is your child tax credit.



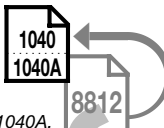
You may be able to take the **additional child tax credit** on Form 1040A, line 42, if you answered “Yes” on line 6 or line 7 above.

- First, complete your Form 1040A through line 41.
- Then, use Form 8812 to figure any additional child tax credit.



Exercise 1(B)

The Howard's Additional Child Tax Credit

Form 8812 Department of the Treasury Internal Revenue Service	<h2 style="margin: 0;">Additional Child Tax Credit</h2> <p style="font-size: small; margin: 5px 0;">Complete and attach to Form 1040 or Form 1040A.</p>		OMB No. 1545-1620 <h2 style="margin: 0;">2003</h2> Attachment Sequence No. 47
Name(s) shown on return <p style="text-align: center; font-weight: bold;">Emily and Victor Howard</p>		Your social security number <p style="text-align: center; font-weight: bold;">000 : 00 : 4410</p>	
Part I All Filers			
1 Enter the amount from line 3 of your Child Tax Credit Worksheet on page 40 of the Form 1040 instructions or page 39 of the Form 1040A instructions. If you used Pub. 972, enter the amount from line 10 of the worksheet on page 3 of the publication	1	\$2,400	
2 Enter the amount from Form 1040, line 49, or Form 1040A, line 33	2	\$368	
3 Subtract line 2 from line 1. If zero, stop ; you cannot take this credit	3	\$2,032	
4 Enter your total taxable earned income. See the instructions on back	4	\$18,467	
5 Is the amount on line 4 more than \$10,500? <input type="checkbox"/> No. Leave line 5 blank and enter -0- on line 6. <input checked="" type="checkbox"/> Yes. Subtract \$10,500 from the amount on line 4. Enter the result	5	\$7,967	
6 Multiply the amount on line 5 by 10% (.10) and enter the result Next. Do you have three or more qualifying children? <input type="checkbox"/> No. If line 6 is zero, stop ; you cannot take this credit. Otherwise, skip Part II and enter the smaller of line 3 or line 6 on line 13. <input checked="" type="checkbox"/> Yes. If line 6 is equal to or more than line 3, skip Part II and enter the amount from line 3 on line 13. Otherwise, go to line 7.	6	\$797	
Part II Certain Filers Who Have Three or More Qualifying Children			
7 Enter the total of the withheld social security and Medicare taxes from Form(s) W-2, boxes 4 and 6. If married filing jointly, include your spouse's amounts with yours. If you worked for a railroad, see the instructions on back	7	\$1,413	
8 1040 filers: Enter the total of the amounts from Form 1040, lines 28 and 56, plus any uncollected social security and Medicare or tier 1 RRTA taxes included on line 60. 1040A filers: Enter -0-.	8	\$0	
9 Add lines 7 and 8	9	\$1,413	
10 1040 filers: Enter the total of the amounts from Form 1040, lines 63 and 64. 1040A filers: Enter the total of the amount from Form 1040A, line 41, plus any excess social security and tier 1 RRTA taxes withheld that you entered to the left of line 43 (see the instructions on back).	10	\$569	
11 Subtract line 10 from line 9. If zero or less, enter -0-	11	\$844	
12 Enter the larger of line 6 or line 11 here Next, enter the smaller of line 3 or line 12 on line 13.	12	\$844	
Part III Your Additional Child Tax Credit			
13 This is your additional child tax credit	13	\$844	
		Enter this amount on Form 1040, line 65, or Form 1040A, line 42.	

STUDENT NOTES

WAGE EARNER COMPREHENSIVE PROBLEMS

INTRODUCTION


In this section, you will complete tax returns for several common wage earner scenarios often encountered at volunteer assistance sites. This will be valuable practice as you prepare to help taxpayers. Although answers to each of the problems are shown at the end of this section, you should try to complete the blank forms for each problem before referring to its answers.

After completing this section, you will be able to:

- accurately complete a basic tax return.

PROBLEM 1

John Marshall, a sophomore in college, wants help with preparing his tax return. He tells you he is 19 years old (born May 28, 1984). Although he lives in the dorm at college, his parents can claim him as a dependent on their tax return. He does not wish to contribute to the presidential campaign fund. If he receives a refund he would like it direct deposited into his checking account (account number xxxxxxxxxxxxxx, routing number xxxxxxxxxxxx). John does not want to name a third party designee. His address and SSN are correct on his Form W-2 and Form 1099-INT.

a Control number 3456781		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number xxx-xx-xxxx				1 Wages, tips, other compensation \$2,694.00		2 Federal income tax withheld \$94.00	
c Employer's name, address, and ZIP code Norfolk Trading Company 819 Ferris St. Your City, State, Zip Code				3 Social security wages \$2,694.00		4 Social security tax withheld \$39.00	
				5 Medicare wages and tips \$2,694.00		6 Medicare tax withheld	
				7 Social security tips		8 Allocated tips	
d Employee's social security number xxx-xx-xxxx				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name John Marshall 878 Hudson Ave Your City, State, Zip Code				11 Nonqualified plans		12a See instructions for box 12	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c 12d	
f Employee's address and ZIP code				15 State Employer's state ID number xxx-xx-xxxx		16 State wages, tips, etc. \$2,694.00	
		17 State income tax \$52.00		18 Local wages, tips, etc.		19 Local income tax	
						20 Locality name	

Form **W-2** Wage and Tax Statement

2003

Department of the Treasury—Internal Revenue Service

Copy B To Be Filed with Employee's FEDERAL Tax Return.
This information is being furnished to the Internal Revenue Service.

WAGE EARNER COMPREHENSIVE PROBLEMS

CORRECTED (if checked)

PAYER'S name, street address, city, state, ZIP code, and telephone no. First Bank 2940 N. Second St. Your City, State, Zip Code		Payer's RTN (optional)	OMB No. 1545-0112 2003 Form 1099-INT	Interest Income
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	1 Interest income not included in box 3 \$ 50.00		
RECIPIENT'S name John Marshall Street address (including apt. no.) 878 Hudson Ave. City, state, and ZIP code Your City, State, Zip Code		2 Early withdrawal penalty \$	3 Interest on U.S. Savings Bonds and Treas. obligations \$	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
Account number (optional)		4 Federal income tax withheld \$	5 Investment expenses \$	
		6 Foreign tax paid \$	7 Foreign country or U.S. possession	
Form 1099-INT		(keep for your records)		Department of the Treasury - Internal Revenue Service

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040EZ, front

Form
1040EZ

Department of the Treasury—Internal Revenue Service
**Income Tax Return for Single and
Joint Filers With No Dependents 2003**

OMB No. 1545-0675

Label

(See page 14.)
Use the IRS label.
Otherwise, please print or type.

Presidential Election Campaign
(page 14) ▶

Your first name and initial	Last name
If a joint return, spouse's first name and initial	Last name
Home address (number and street). If you have a P.O. box, see page 14.	Apt. no.
City, town or post office, state, and ZIP code. If you have a foreign address, see page 14.	

Your social security number

Spouse's social security number

▲ Important! ▲

You **must** enter your SSN(s) above.

You Spouse
 Yes No Yes No

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if a joint return, want \$3 to go to this fund? ▶

Income

Attach Form(s) W-2 here.
Enclose, but do not attach, any payment.

Note. You must check Yes or No.

1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1
2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2
3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3
4 Add lines 1, 2, and 3. This is your adjusted gross income .	4
5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from No. If single , enter \$7,800. <input type="checkbox"/> worksheet on back. <input type="checkbox"/> If married filing jointly , enter \$15,600. See back for explanation.	5
6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	▶ 6

Payments and tax

7 Federal income tax withheld from box 2 of your Form(s) W-2.	7
8 Earned income credit (EIC).	8
9 Add lines 7 and 8. These are your total payments .	▶ 9
10 Tax. Use the amount on line 6 above to find your tax in the tax table on pages 25–29 of the booklet. Then, enter the tax from the table on this line.	10

Refund

Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.

11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	▶ 11a
▶ b Routing number <input type="text"/>	▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
▶ d Account number <input type="text"/>	

Amount you owe

12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.	▶ 12
---	------

Third party designee

Do you want to allow another person to discuss this return with the IRS (see page 22)? **Yes**. Complete the following. **No**

Designee's name ▶ Phone no. ▶ () Personal identification number (PIN) ▶

Sign here

Joint return? See page 13.
Keep a copy for your records.

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid preparer's use only

Preparer's signature ▶	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Phone no. ()	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 24.

Cat. No. 11329W

Form **1040EZ** (2003)

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040EZ, page 2

Form 1040EZ (2003)

Page 2

Use this form if

- Your filing status is single or married filing jointly.
- You (and your spouse if married filing jointly) were born after January 1, 1939, and were not blind at the end of 2003.
- You do not claim any dependents.
- Your taxable income (line 6) is less than \$50,000.
- You do not claim a deduction for educator expenses, the student loan interest deduction, or the tuition and fees deduction.
- You do not claim an education credit, the retirement savings contributions credit, or the health insurance credit for eligible recipients.
- You had **only** wages, salaries, tips, taxable scholarship or fellowship grants, unemployment compensation, or Alaska Permanent Fund dividends, and your taxable interest was not over \$1,500. **But** if you earned tips, including allocated tips, that are not included in box 5 and box 7 of your W-2, you may not be able to use Form 1040EZ (see page 15). If you are planning to use Form 1040EZ for a child who received Alaska Permanent Fund dividends, see page 16.
- You did not receive any advance earned income credit payments.

If you are not sure about your filing status, see page 13. If you have questions about dependents, use TeleTax topic 354 (see page 8). If you **cannot use this form**, use TeleTax topic 352 (see page 8).

Filing in your return

For tips on how to avoid common mistakes, see page 23.

If you received a scholarship or fellowship grant or tax-exempt interest income, such as on municipal bonds, see the booklet before filling in the form. Also, see the booklet if you received a Form 1099-INT showing Federal income tax withheld or if Federal income tax was withheld from your unemployment compensation or Alaska Permanent Fund dividends.

Remember, you must report all wages, salaries, and tips even if you do not get a Form W-2 from your employer. You must also report all your taxable interest, including interest from banks, savings and loans, credit unions, etc., even if you do not get a Form 1099-INT.

Worksheet for dependents who checked "Yes" on line 5

(keep a copy for your records)

Use this worksheet to figure the amount to enter on line 5 if someone can claim you (or your spouse if married filing jointly) as a dependent, even if that person chooses not to do so. To find out if someone can claim you as a dependent, use TeleTax topic 354 (see page 8).

- A. Amount, if any, from line 1 on front _____
+ 250.00 Enter total ► A. _____
- B. Minimum standard deduction B. 750.00
- C. Enter the **larger** of line A or line B here C. _____
- D. Maximum standard deduction. If **single**, enter \$4,750; if **married filing jointly**, enter \$9,500 D. _____
- E. Enter the **smaller** of line C or line D here. This is your standard deduction E. _____
- F. Exemption amount. } F. _____
- If single, enter -0-.
 - If married filing jointly and—
 - both you and your spouse can be claimed as dependents, enter -0-.
 - only one of you can be claimed as a dependent, enter \$3,050.
- G. Add lines E and F. Enter the total here and on line 5 on the front . . . G. _____

If you checked "No" on line 5 because no one can claim you (or your spouse if married filing jointly) as a dependent, enter on line 5 the amount shown below that applies to you.

- Single, enter \$7,800. This is the total of your standard deduction (\$4,750) and your exemption (\$3,050).
- Married filing jointly, enter \$15,600. This is the total of your standard deduction (\$9,500), your exemption (\$3,050), and your spouse's exemption (\$3,050).


Mailing return

Mail your return by **April 15, 2004**. Use the envelope that came with your booklet. If you do not have that envelope or if you moved during the year, see the back cover for the address to use.

WAGE EARNER COMPREHENSIVE PROBLEMS

PROBLEM 2

Melody York is 34 years old (born August 31, 1969) and single. Melody was laid off from her job as a clerk in September and received unemployment compensation for the remainder of the year. She would like to contribute to the Presidential campaign fund. If she receives a refund, she would like it direct deposited into her savings account (account number xxxxxxxxxxxx; routing transit number xxxxxxxxxx). Melody does not want to name a third party designee. Her address and SSN are correct as shown on her Form W-2 and Form 1099-G.

a Control number 258963		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number xxx-xx-xxxx				1 Wages, tips, other compensation \$6,923.12		2 Federal income tax withheld \$261.00	
c Employer's name, address, and ZIP code Miller Industries 975 Parks Blvd Your City, State, Zip Code				3 Social security wages \$6,923.12		4 Social security tax withheld \$429.00	
				5 Medicare wages and tips \$6,923.12		6 Medicare tax withheld \$100.00	
				7 Social security tips		8 Allocated tips	
d Employee's social security number xxx-xx-xxxx				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name Melody York 17 North 9th Avenue Your City, State, Zip Code				11 Nonqualified plans		12a See instructions for box 12	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code							
15 State Employer's state ID number xxx-xx-xxxx		16 State wages, tips, etc. \$6,923.12		17 State income tax \$68.36		18 Local wages, tips, etc.	
						19 Local income tax	
						20 Locality name	


Form **W-2** Wage and Tax Statement

2003

Department of the Treasury—Internal Revenue Service

Copy B To Be Filed with Employee's FEDERAL Tax Return.
This information is being furnished to the Internal Revenue Service.

WAGE EARNER COMPREHENSIVE PROBLEMS

<input type="checkbox"/> CORRECTED (if checked)					
PAYER'S name, street address, city, state, ZIP code, and telephone no. Department of Employment Security 4010 West Third St. Your City, State, Zipcode		1 Unemployment compensation \$ 3,240.00	OMB No. 1545-0120 2003	Certain Government Payments	
		2 State or local income tax refunds, credits, or offsets \$	Form 1099-G		
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	3 Box 2 amount is for tax year	4 Federal income tax withheld \$ 0.00	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.	
RECIPIENT'S name Melody York Street address (including apt. no.) 17th North 9th Avenue City, state, and ZIP code Your City, State, Zip Code		5 	6 Taxable grants \$		
Account number (optional)		7 Agriculture payments \$	8 Box 2 is trade or business income <input type="checkbox"/>		
Form 1099-G		(keep for your records)		Department of the Treasury - Internal Revenue Service	

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040EZ, front

Form
1040EZ

Department of the Treasury—Internal Revenue Service

Income Tax Return for Single and Joint Filers With No Dependents 2003

OMB No. 1545-0675

Label

(See page 14.)

Use the IRS label.

Otherwise, please print or type.

Presidential Election Campaign (page 14)

L A B E L H E R E	Your first name and initial	Last name
	If a joint return, spouse's first name and initial	Last name
	Home address (number and street). If you have a P.O. box, see page 14.	Apt. no.
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 14.	

Your social security number

Spouse's social security number

▲ Important! ▲
You **must** enter your SSN(s) above.

Note. Checking "Yes" will not change your tax or reduce your refund.

Do you, or your spouse if a joint return, want \$3 to go to this fund?

You Spouse
 Yes No Yes No

Income

Attach Form(s) W-2 here.
Enclose, but do not attach, any payment.

Note. You must check Yes or No.

1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1
2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2
3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3
4 Add lines 1, 2, and 3. This is your adjusted gross income .	4
5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from worksheet on back. <input type="checkbox"/> No. If single , enter \$7,800. If married filing jointly , enter \$15,600. See back for explanation. <input type="checkbox"/>	5
6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6

Payments and tax

7 Federal income tax withheld from box 2 of your Form(s) W-2.	7
8 Earned income credit (EIC).	8
9 Add lines 7 and 8. These are your total payments .	9
10 Tax. Use the amount on line 6 above to find your tax in the tax table on pages 25–29 of the booklet. Then, enter the tax from the table on this line.	10

Refund

Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.

11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	11a
b Routing number	<input type="text"/>
c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
d Account number	<input type="text"/>

Amount you owe

12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.	12
---	----

Third party designee

Do you want to allow another person to discuss this return with the IRS (see page 22)? **Yes.** Complete the following. **No**

Designee's name	Phone no. ()	Personal identification number (PIN)
-----------------	---------------	--------------------------------------

Sign here

Joint return? See page 13. Keep a copy for your records.

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid preparer's use only

Preparer's signature	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code	EIN	Phone no. ()	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 24.

Cat. No. 11329W

Form **1040EZ** (2003)

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040EZ, page 2

Form 1040EZ (2003)

Page **2**

Use this form if

- Your filing status is single or married filing jointly.
- You (and your spouse if married filing jointly) were born after January 1, 1939, and were not blind at the end of 2003.
- You do not claim any dependents.
- Your taxable income (line 6) is less than \$50,000.
- You do not claim a deduction for educator expenses, the student loan interest deduction, or the tuition and fees deduction.
- You do not claim an education credit, the retirement savings contributions credit, or the health insurance credit for eligible recipients.
- You had **only** wages, salaries, tips, taxable scholarship or fellowship grants, unemployment compensation, or Alaska Permanent Fund dividends, and your taxable interest was not over \$1,500. **But** if you earned tips, including allocated tips, that are not included in box 5 and box 7 of your W-2, you may not be able to use Form 1040EZ (see page 15). If you are planning to use Form 1040EZ for a child who received Alaska Permanent Fund dividends, see page 16.
- You did not receive any advance earned income credit payments.

If you are not sure about your filing status, see page 13. If you have questions about dependents, use TeleTax topic 354 (see page 8). If you **cannot use this form**, use TeleTax topic 352 (see page 8).

Filling in your return

For tips on how to avoid common mistakes, see page 23.

If you received a scholarship or fellowship grant or tax-exempt interest income, such as on municipal bonds, see the booklet before filling in the form. Also, see the booklet if you received a Form 1099-INT showing Federal income tax withheld or if Federal income tax was withheld from your unemployment compensation or Alaska Permanent Fund dividends.

Remember, you must report all wages, salaries, and tips even if you do not get a Form W-2 from your employer. You must also report all your taxable interest, including interest from banks, savings and loans, credit unions, etc., even if you do not get a Form 1099-INT.

Worksheet for dependents who checked "Yes" on line 5

(keep a copy for your records)

Use this worksheet to figure the amount to enter on line 5 if someone can claim you (or your spouse if married filing jointly) as a dependent, even if that person chooses not to do so. To find out if someone can claim you as a dependent, use TeleTax topic 354 (see page 8).

- A. Amount, if any, from line 1 on front
- + 250.00 Enter total ► A.
- B. Minimum standard deduction B. 750.00
- C. Enter the **larger** of line A or line B here C.
- D. Maximum standard deduction. If **single**, enter \$4,750; if **married filing jointly**, enter \$9,500 D.
- E. Enter the **smaller** of line C or line D here. This is your standard deduction E.
- F. Exemption amount.
 - If single, enter -0-.
 - If married filing jointly and—
 - both you and your spouse can be claimed as dependents, enter -0-.
 - only one of you can be claimed as a dependent, enter \$3,050.
- } F.
- G. Add lines E and F. Enter the total here and on line 5 on the front G.

If you checked "No" on line 5 because no one can claim you (or your spouse if married filing jointly) as a dependent, enter on line 5 the amount shown below that applies to you.

- Single, enter \$7,800. This is the total of your standard deduction (\$4,750) and your exemption (\$3,050).
- Married filing jointly, enter \$15,600. This is the total of your standard deduction (\$9,500), your exemption (\$3,050), and your spouse's exemption (\$3,050).

Mailing return

Mail your return by **April 15, 2004**. Use the envelope that came with your booklet. If you do not have that envelope or if you moved during the year, see the back cover for the address to use.

Line 8 Earned Income Credit (EIC)

What Is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.



If you have a qualifying child (see the next column on this page), you may be able to take the credit, but you must use Schedule EIC and Form 1040A or 1040 to do so. For details, see Pub. 596.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet on page 19 **or** let the IRS figure the credit for you.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

- Is the amount on Form 1040EZ, line 4, less than \$11,230 (\$12,230 if married filing jointly)?
 - Yes.** *Continue* →
 - No.** You cannot take the credit.
- Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 18)?
 - Yes.** *Continue* →
 - No.** You cannot take the credit. Enter "No" in the space to the left of line 8.
- Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?
 - Yes.** You cannot take the credit.
 - No.** *Continue* →
- Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?
 - Yes.** *Go to question 5.*
 - No.** You cannot take the credit.

- Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 18 before you answer.
 - Yes.** *Continue* →
 - No.** You cannot take the credit. Enter "No" in the space to the left of line 8.

- Look at the qualifying child conditions below. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?
 - Yes.** You cannot take the credit. Enter "No" in the space to the left of line 8.
 - No.** *Go to Step 2* → on page 18.

A **qualifying child** is a child who is your—

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as your own child)

AND

was at the end of 2003...
Under age 19

or

under age 24 and a student

or

any age and permanently and totally disabled

AND

who...

Either lived with you in the United States for more than half of 2003 **or** was born or died in 2003 and your home was the child's home for the entire time he or she was alive in 2003.

Note. Special rules apply if the child was married or also meets the conditions to be a qualifying child of another person (other than your spouse if filing a joint return). For details, use TeleTax topic 601 (see page 8) or see Pub. 596.

WAGE EARNER COMPREHENSIVE PROBLEMS

Form 1040EZ, Earned Income Credit Worksheet, page 2

Form 1040EZ—Line 8

Step 2 Earned Income

1. Figure earned income:

Form 1040EZ, line 1 _____

Subtract, if included in line 1, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2
- Amount paid to an inmate in a penal institution for work (enter "PRI" in the space to the left of line 1 on Form 1040EZ)
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (enter "DFC" and the amount subtracted in the space to the left of line 1 on Form 1040EZ). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

Earned Income =

2. Is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 3. No. 

You cannot take the credit.

Step 3 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See Credit Figured by the IRS on this page. No. Go to the worksheet on page 19.

Definitions and Special Rules

(listed in alphabetical order)

Credit Figured by the IRS To have the IRS figure the credit for you:

1. Enter "EIC" in the space to the left of line 8 on Form 1040EZ.
2. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- The only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

Members of the Military. If you were on extended active duty outside the United States, your home is considered to be in the United States during that duty period. Extended active duty is military duty ordered for an indefinite period or for a period of more than 90 days. Once you begin serving extended active duty, you are considered to be on extended active duty even if you serve fewer than 90 days.

Social Security Number (SSN). For purposes of taking the EIC, a valid SSN is a number issued by the Social Security Administration unless "Not Valid for Employment" is printed on the social security card and the number was issued solely to apply for or receive a Federally funded benefit.

To find out how to get an SSN, see page 14. If you will not have an SSN by April 15, 2004, see What if You Cannot File on Time? on page 11.

Welfare Benefits, Effect of Credit on. Any refund you receive as a result of taking the EIC will not be used to determine if you are eligible for the following programs or how much you can receive from them. But if the refund you receive because of the EIC is not spent within a certain period of time, it may count as an asset (or resource) and affect your eligibility.

- Temporary Assistance for Needy Families (TANF).
- Medicaid and supplemental security income (SSI).
- Food stamps and low-income housing.

(Continued on page 19)

Need more information or forms? See page 7.

- 16 -

Earned Income Credit (EIC) Worksheet—Line 8

Keep for Your Records



Part 1


All Filers

1. Enter your earned income from Step 2 on page 18.

1	
---	--

2. Look up the amount on line 1 above in the EIC Table on page 20 to find the credit. Be sure you use the correct column for your filing status. Enter the credit here.

2	
---	--

If line 2 is zero,  You cannot take the credit.
Enter "No" in the space to the left of line 8.

3. Enter the amount from Form 1040EZ, line 4.

3	
---	--

4. Are the amounts on lines 3 and 1 the same?

- Yes.** Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. Is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?

Yes. Leave line 5 blank; enter the amount from line 2 on line 6.

No. Look up the amount on line 3 in the EIC Table on page 20 to find the credit. Be sure you use the correct column for your filing status. Enter the credit here.

5	
---	--

Look at the amounts on lines 5 and 2.
Then, enter the **smaller** amount on line 6.

Part 3

Your Earned Income Credit

6. This is your earned income credit.

6	
---	--

Enter this amount on
Form 1040EZ, line 8.



If your EIC for a year after 1996 was reduced or disallowed, see page 18 to find out if you must file Form 8862 to take the credit for 2003.

WAGE EARNER COMPREHENSIVE PROBLEMS


PROBLEM 3

Marvin Simmons is 55 (born on December 4, 1948). His grandson, Eric (SSN xxx-xx-xxxx; born on March 10, 1993), has lived with him for the last two years. Marvin pays the total cost of keeping up a home for himself and his grandson and provides all the support for Eric. Eric is a qualifying child for EIC purposes.

Marvin paid \$978 in child care expenses to allow him to work. The provider information is as follows:

Joy Day Care
 9192 East Huron St.
 Your City, State, Zip Code
 EIN: xx-xxxxxxx

He does not want to contribute to the presidential election fund and if he is due a refund, he would like a direct deposit to his checking account (account xxxxxxxxxxxxxx; routing transit number xxxxxxxxxxxx). His address and SSN are correct on his Form W-2. Marvin received the \$400 advance child tax credit payment. He does not want to designate a third party. Marvin is a mechanic.

a Control number 3495127		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number xxx-xx-xxxx				1 Wages, tips, other compensation \$24,952.00		2 Federal income tax withheld \$1,964.00	
c Employer's name, address, and ZIP code Endicott Motors 473 Endicott Lane Your City, State, Zip Code				3 Social security wages \$24,952.00		4 Social security tax withheld \$1,547.00	
				5 Medicare wages and tips \$24,952.00		6 Medicare tax withheld \$362.00	
				7 Social security tips		8 Allocated tips	
d Employee's social security number				9 Advance EIC payment \$600.00		10 Dependent care benefits	
e Employee's first name and initial Last name Marvin Simmons 9701 Austin Rd Your City, State, Zip Code				11 Nonqualified plans		12a See instructions for box 12	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code				15 State Employer's state ID number xxx-xx-xxxx		16 State wages, tips, etc. \$24,952.00	
				17 State income tax \$875.00		18 Local wages, tips, etc.	
				19 Local income tax		20 Locality name	

Form **W-2** Wage and Tax Statement **2003** Department of the Treasury—Internal Revenue Service

Copy B To Be Filed with Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040A, front

Form 1040A	Department of the Treasury—Internal Revenue Service U.S. Individual Income Tax Return	2003	IRS Use Only—Do not write or staple in this space.
Label (See page 21.) Use the IRS label. Otherwise, please print or type.	Your first name and initial	Last name	OMB No. 1545-0085
	If a joint return, spouse's first name and initial	Last name	Your social security number
	Home address (number and street). If you have a P.O. box, see page 22.	Apt. no.	Spouse's social security number
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 22.		▲ Important! ▲ You must enter your SSN(s) above.
Presidential Election Campaign (See page 22.)		Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if filing a joint return, want \$3 to go to this fund?	
		You	Spouse
		<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
Filing status Check only one box.	1 <input type="checkbox"/> Single 2 <input type="checkbox"/> Married filing jointly (even if only one had income) 3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here.		
		4 <input type="checkbox"/> Head of household (with qualifying person). (See page 23.) If the qualifying person is a child but not your dependent, enter this child's name here.	
		5 <input type="checkbox"/> Qualifying widow(er) with dependent child (See page 24.)	
Exemptions	6a <input type="checkbox"/> Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a.		No. of boxes checked on 6a and 6b
		b <input type="checkbox"/> Spouse	
		c Dependents:	
If more than six dependents, see page 24.	(1) First name	Last name	(2) Dependent's social security number
		(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)
		<input type="checkbox"/>	<input type="checkbox"/>
		<input type="checkbox"/>	<input type="checkbox"/>
		<input type="checkbox"/>	<input type="checkbox"/>
		<input type="checkbox"/>	<input type="checkbox"/>
		No. of children on 6c who:	
		• lived with you	
		• did not live with you due to divorce or separation (see page 26)	
		Dependents on 6c not entered above	
		Add numbers on lines above	
		d Total number of exemptions claimed.	
Income	7 Wages, salaries, tips, etc. Attach Form(s) W-2. 7		
		8a Taxable interest. Attach Schedule 1 if required. 8a	
		b Tax-exempt interest. Do not include on line 8a. 8b	
		9a Ordinary dividends. Attach Schedule 1 if required. 9a	
		b Qualified dividends (see page XX). 9b	
		10a Capital gain distributions (see page 27). 10a	
		b Post-May 5 capital gain distributions (see page 27). 10b	
		11a IRA distributions. 11a	11b Taxable amount (see page 27). 11b
		12a Pensions and annuities. 12a	12b Taxable amount (see page 28). 12b
		13 Unemployment compensation and Alaska Permanent Fund dividends. 13	
		14a Social security benefits. 14a	14b Taxable amount (see page 30). 14b
		15 Add lines 7 through 14b (far right column). This is your total income . 15	
Adjusted gross income	16 Educator expenses (see page 30). 16		
		17 IRA deduction (see page 30). 17	
		18 Student loan interest deduction (see page 33). 18	
		19 Tuition and fees deduction (see page 33). 19	
		20 Add lines 16 through 19. These are your total adjustments . 20	
		21 Subtract line 20 from line 15. This is your adjusted gross income . 21	
For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 57.			
		Cat. No. 11327A	Form 1040A (2003)

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Form 1040A, page 2

Form 1040A (2003)

Page 2

Tax, credits, and payments	22	Enter the amount from line 21 (adjusted gross income).	22	
	23a	Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind } checked ▶ 23a <input type="checkbox"/>		
	b	If you are married filing separately and your spouse itemizes deductions, see page 34 and check here ▶ 23b <input type="checkbox"/>		
	24	Enter your standard deduction (see left margin).	24	
	25	Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25	
	26	Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26	
	27	Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income .	▶ 27	
	28	Tax , including any alternative minimum tax (see page 35).	28	
	29	Credit for child and dependent care expenses. Attach Schedule 2.	29	
	30	Credit for the elderly or the disabled. Attach Schedule 3.	30	
	31	Education credits. Attach Form 8863.	31	
	32	Retirement savings contributions credit. Attach Form 8880.	32	
	33	Child tax credit (see page 38).	33	
	34	Adoption credit. Attach Form 8839.	34	
	35	Add lines 29 through 34. These are your total credits .	35	
	36	Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36	
	37	Advance earned income credit payments from Form(s) W-2.	37	
	38	Add lines 36 and 37. This is your total tax .	▶ 38	
	39	Federal income tax withheld from Forms W-2 and 1099.	39	
	40	2003 estimated tax payments and amount applied from 2002 return.	40	
	41	Earned income credit (EIC) .	41	
	42	Additional child tax credit. Attach Form 8812.	42	
	43	Add lines 39 through 42. These are your total payments .	▶ 43	
	Refund	44 If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44	
	45a	Amount of line 44 you want refunded to you .	▶ 45a	
	b	Routing number <input type="text"/> ▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings		
	d	Account number <input type="text"/>		
	46	Amount of line 44 you want applied to your 2004 estimated tax .	46	
	Amount you owe	47 Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53.	▶ 47	
	48	Estimated tax penalty (see page 53).	48	

Third party designee Do you want to allow another person to discuss this return with the IRS (see page 54)? **Yes**. Complete the following. **No**

Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶ <input type="text"/>
-------------------	-----------------	---

Sign here Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid preparer's use only

Preparer's signature ▶	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN		
	Phone no. ()		

Printed on recycled paper

Form 1040A (2003)

WAGE EARNER COMPREHENSIVE PROBLEMS

Complete this form

Schedule 2, page 1

Schedule 2
(Form 1040A)

Department of the Treasury—Internal Revenue Service

Child and Dependent Care Expenses for Form 1040A Filers

2003

OMB No. 1545-0085

Name(s) shown on Form 1040A

Your social security number

Before you begin: You need to understand the following terms. See **Definitions** on page 1 of the separate instructions.

- **Dependent Care Benefits**
- **Qualifying Person(s)**
- **Qualified Expenses**
- **Earned Income**

Part I

Persons or organizations who provided the care

1	(a) Care provider's name	(b) Address (number, street, apt. no., city, state, and ZIP code)	(c) Identifying number (SSN or EIN)	(d) Amount paid (see instructions)

(If you need more space, use the bottom of page 2.)

You must complete this part.

Did you receive dependent care benefits?	No	Yes	Complete only Part II below. Complete Part III on the back next.
--	----	-----	---

Caution. If the care was provided in your home, you may owe employment taxes. If you do, you must use Form 1040. See **Schedule H** and its instructions for details.

Part II

Credit for child and dependent care expenses

2 Information about your **qualifying person(s)**. If you have more than two qualifying persons, see the instructions.

3	(a) Qualifying person's name		(b) Qualifying person's social security number	(c) Qualified expenses you incurred and paid in 2003 for the person listed in column (a)
	First	Last		

3 Add the amounts in column (c) of line 2. **Do not** enter more than \$3,000 for one qualifying person or \$6,000 for two or more persons. If you completed Part III, enter the amount from line 26. 3

4 Enter your **earned income**. 4

5 If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions); **all others**, enter the amount from line 4. 5

6 Enter the **smallest** of line 3, 4, or 5. 6

7 Enter the amount from Form 1040A, line 22. 7

8 Enter on line 8 the decimal amount shown below that applies to the amount on line 7.

If line 7 is:			If line 7 is:				
Over	But not over	Decimal amount is	Over	But not over	Decimal amount is		
\$0—15,000		.35	\$29,000—31,000		.27		
15,000—17,000		.34	31,000—33,000		.26		
17,000—19,000		.33	33,000—35,000		.25		
19,000—21,000		.32	35,000—37,000		.24		
21,000—23,000		.31	37,000—39,000		.23		
23,000—25,000		.30	39,000—41,000		.22		
25,000—27,000		.29	41,000—43,000		.21		
27,000—29,000		.28	43,000—No limit		.20	8	×

9 Multiply **line 6** by the decimal amount on line 8. If you paid 2002 expenses in 2003, see the instructions. 9

10 Enter the amount from Form 1040A, line 28. 10

11 **Credit for child and dependent care expenses.** Enter the **smaller** of line 9 or line 10 here and on Form 1040A, line 29. 11

For Paperwork Reduction Act Notice, see Form 1040A instructions.

Cat. No. 107491

Schedule 2 (Form 1040A) 2003

WAGE EARNER COMPREHENSIVE PROBLEMS

Form 1040A Child Tax Credit Worksheet

Child Tax Credit Worksheet—Line 33

Keep for Your Records

Before you begin: ✓ If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



If you received Notice 1319, have it available. The notice shows the amount of your advance payment (before offset). If you do not have Notice 1319, you can check the amount of your advance payment (before offset) on the IRS website at www.irs.gov. You will need to enter your SSN, your 2002 filing status, and the total number of exemptions you claimed on line 6d of your 2002 Form 1040 or Form 1040A.



- To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2003 and meet the other requirements listed on page 38.
- Do not** use this worksheet if you answered “Yes” to question 1 or 2 on page 38. Instead, use Pub. 972.

1. Number of qualifying children: _____ × \$1,000.
Enter the result.

1	
---	--

2. Enter the amount, if any, of your advance child tax credit (before offset).

2	
---	--

3. Is line 1 less than or equal to line 2?

Yes.

You cannot take this credit. If line 2 is more than line 1, you do not have to pay back the difference.

No. Subtract line 2 from line 1.

3	
---	--

4. Enter the amount from Form 1040A, line 28.

4	
---	--

5. Add the amounts from Form 1040A, lines 29 through 32.

5	
---	--

6. Are the amounts on lines 4 and 5 the same?

Yes.

You cannot take this credit because there is no tax to reduce. However, you may be able to take the **additional child tax credit**. See the **TIP** below.

No. Subtract line 5 from line 4.

6	
---	--

7. Is the amount on line 3 more than the amount on line 6?

Yes. Enter the amount from line 6. Also, you may be able to take the **additional child tax credit**. See the **TIP** below.

No. Enter the amount from line 3.

This is your child tax credit.

7	
---	--

Enter this amount on Form 1040A, line 33.



You may be able to take the **additional child tax credit** on Form 1040A, line 42, if you answered “Yes” on line 6 or line 7 above.



- First, complete your Form 1040A through line 41.
- Then, use Form 8812 to figure any additional child tax credit.

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet that applies to you **or** let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

- If, in 2003:
 - 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
 - 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
 - No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* **No.** You cannot take the credit.
- Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* **No.** You cannot take the credit. Put "No" to the left of the entry space for line 41.
- Is your filing status married filing separately?

Yes. You cannot take the credit. **No.** *Continue*
- Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*

Step 2 Investment Income

- Add the amounts from Form 1040A:

Line 8a _____
 Line 8b + _____
 Line 9a + _____
 Line 10a + _____

Investment Income =

- Is your investment income more than \$2,600?

Yes. You cannot take the credit. **No.** *Continue*
- Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.* **No.** *Go to Step 4 on page 40.*

WAGE EARNER COMPREHENSIVE PROBLEMS

Form 1040A EIC Worksheet, Page 2

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)

AND

who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Do you have at least one child who meets the above conditions to be your qualifying child?

Yes. *Go to question 3.* **No.** *Skip question 3; go to Step 4, question 2.*

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?

Yes. *See Qualifying Child of More Than One Person on page 42.* **No.** This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. *Skip Step 4; go to Step 5 on page 41.*

Step 4 Filers Without a Qualifying Child

1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →


You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?


Yes.  **No.** *Continue* →

You cannot take the credit.

3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. *Continue* → **No.**  You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. *Go to Step 5 on page 41.* **No.**  You cannot take the credit. Put "No" to the left of the entry space for line 41.

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 _____


Subtract, if included on line 7, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put "PRI" and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

Earned Income =

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.** 

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See Credit Figured by the IRS below. **No.** Go to the worksheet on page 43.

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put "EIC" to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to "Time Lived With You" Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child's home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

WAGE EARNER COMPREHENSIVE PROBLEMS

Form 1040A EIC Worksheet

Earned Income Credit (EIC) Worksheet—Line 41

Keep for Your Records



Part 1


All Filers

1. Enter your earned income from Step 5 on page 43.

1

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

2

If line 2 is zero,  You cannot take the credit. Put "No" to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22.

3

4. Are the amounts on lines 3 and 1 the same?

- Yes.** Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. If you have:

- No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?
- 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?

Yes. Leave line 5 blank; enter the amount from line 2 on line 6.

No. Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

5

Part 3

Your Earned Income Credit

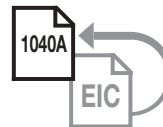
6. This is your earned income credit.

6

Enter this amount on Form 1040A, line 41.

Reminder—

- ✓ If you have a qualifying child, complete and attach Schedule EIC.



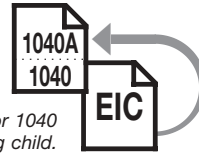
If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.

WAGE EARNER COMPREHENSIVE PROBLEMS

Schedule EIC

SCHEDULE EIC
(Form 1040A or 1040)

Earned Income Credit
Qualifying Child Information



OMB No. 1545-0074

2003

Attachment Sequence No. **43**

Department of the Treasury
Internal Revenue Service

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.

Name(s) shown on return

Your social security number

Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that (a) you can take the EIC and (b) you have a qualifying child.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.

Qualifying Child Information

Child 1

Child 2

1 Child's name	Child 1		Child 2	
	First name	Last name	First name	Last name
If you have more than two qualifying children, you only have to list two to get the maximum credit.				
2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.				
Next, if the child was born after 1984, go to line 4. Otherwise, continue.				
3 If the child was born before 1985—				
a Was the child under age 24 at the end of 2003 and a student?	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>	<input type="checkbox"/> Yes. <i>Go to line 4.</i>	<input type="checkbox"/> No. <i>Continue</i>
b Was the child permanently and totally disabled during any part of 2003?	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.	<input type="checkbox"/> Yes. <i>Continue</i>	<input type="checkbox"/> No. The child is not a qualifying child.
4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)				
5 Number of months child lived with you in the United States during 2003				
<ul style="list-style-type: none"> • If the child lived with you for more than half of 2003 but less than 7 months, enter "7". • If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12". 	_____ months <i>Do not enter more than 12 months.</i>		_____ months <i>Do not enter more than 12 months.</i>	



You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.

For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2003

Comprehensive Problems

CW-21

WAGE EARNER

WAGE EARNER COMPREHENSIVE PROBLEMS

Comprehensive Problem 1

Department of the Treasury—Internal Revenue Service Form 1040EZ Income Tax Return for Single and Joint Filers With No Dependents 2003		OMB No. 1545-0675																									
Label (See page 14.) Use the IRS label. Otherwise, please print or type. Presidential Election Campaign (page 14)	Your first name and initial John	Last name Marshall	Your social security number XXX-XX-XXXX																								
	If a joint return, spouse's first name and initial	Last name	Spouse's social security number																								
	Home address (number and street). If you have a P.O. box, see page 14. 878 Hudson Ave		Apt. no.																								
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 14. Your City, State, Zip Code		▲ Important! ▲ You must enter your SSN(s) above.																								
Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if a joint return, want \$3 to go to this fund?			You Spouse <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No <input type="checkbox"/> Yes <input type="checkbox"/> No																								
Income Attach Form(s) W-2 here. Enclose, but do not attach, any payment.	<table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width: 5%;">1</td> <td style="width: 75%;">Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.</td> <td style="width: 10%; text-align: center;">1</td> <td style="width: 10%; text-align: right;">2,694.00</td> </tr> <tr> <td>2</td> <td>Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.</td> <td style="text-align: center;">2</td> <td style="text-align: right;">50.00</td> </tr> <tr> <td>3</td> <td>Unemployment compensation and Alaska Permanent Fund dividends (see page 16).</td> <td style="text-align: center;">3</td> <td></td> </tr> <tr> <td>4</td> <td>Add lines 1, 2, and 3. This is your adjusted gross income.</td> <td style="text-align: center;">4</td> <td style="text-align: right;">2,744.00</td> </tr> <tr> <td>5</td> <td>Can your parents (or someone else) claim you on their return? Yes. Enter amount from worksheet on back. <input checked="" type="checkbox"/> No. If single, enter \$7,800. <input type="checkbox"/> If married filing jointly, enter \$15,600. See back for explanation. <input type="checkbox"/></td> <td style="text-align: center;">5</td> <td style="text-align: right;">2,944.00</td> </tr> <tr> <td>6</td> <td>Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income.</td> <td style="text-align: center;">6</td> <td style="text-align: right;">0.00</td> </tr> </table>		1	Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1	2,694.00	2	Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2	50.00	3	Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3		4	Add lines 1, 2, and 3. This is your adjusted gross income .	4	2,744.00	5	Can your parents (or someone else) claim you on their return? Yes. Enter amount from worksheet on back. <input checked="" type="checkbox"/> No. If single , enter \$7,800. <input type="checkbox"/> If married filing jointly , enter \$15,600. See back for explanation. <input type="checkbox"/>	5	2,944.00	6	Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6	0.00	
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Refund Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.	11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .		11a 94.00																								
▶ b Routing number XXXXX XXXX		▶ c Type: <input checked="" type="checkbox"/> Checking <input type="checkbox"/> Savings																									
▶ d Account number XXXXX XXXX																											
Amount you owe	12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.		12																								
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 22)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No																										
Designee's name		Phone no. ()	Personal identification number (PIN)																								
Sign here Joint return? See page 13. Keep a copy for your records.	Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.																										
Your signature		Date	Your occupation clerk																								
Spouse's signature. If a joint return, both must sign.		Date	Daytime phone number ()																								
Paid preparer's use only	Preparer's signature	Date	Preparer's SSN or PTIN PXX-XX-XXXX																								
Firm's name (or yours if self-employed), address, and ZIP code		EIN																									
		Phone no. ()																									
For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 24.			Cat. No. 11329W Form 1040EZ (2003)																								

Comprehensive Problem 1

Form 1040EZ (2003)

Page **2**

Use this form if

- Your filing status is single or married filing jointly.
 - You (and your spouse if married filing jointly) were born after January 1, 1939, and were not blind at the end of 2003.
 - You do not claim any dependents.
 - Your taxable income (line 6) is less than \$50,000.
 - You do not claim a deduction for educator expenses, the student loan interest deduction, or the tuition and fees deduction.
 - You do not claim an education credit, the retirement savings contributions credit, or the health insurance credit for eligible recipients.
 - You had **only** wages, salaries, tips, taxable scholarship or fellowship grants, unemployment compensation, or Alaska Permanent Fund dividends, and your taxable interest was not over \$1,500. **But** if you earned tips, including allocated tips, that are not included in box 5 and box 7 of your W-2, you may not be able to use Form 1040EZ (see page 15). If you are planning to use Form 1040EZ for a child who received Alaska Permanent Fund dividends, see page 16.
 - You did not receive any advance earned income credit payments.
- If you are not sure about your filing status, see page 13. If you have questions about dependents, use TeleTax topic 354 (see page 8). If you **cannot use this form**, use TeleTax topic 352 (see page 8).

Filling in your return

For tips on how to avoid common mistakes, see page 23.

If you received a scholarship or fellowship grant or tax-exempt interest income, such as on municipal bonds, see the booklet before filling in the form. Also, see the booklet if you received a Form 1099-INT showing Federal income tax withheld or if Federal income tax was withheld from your unemployment compensation or Alaska Permanent Fund dividends.

Remember, you must report all wages, salaries, and tips even if you do not get a Form W-2 from your employer. You must also report all your taxable interest, including interest from banks, savings and loans, credit unions, etc., even if you do not get a Form 1099-INT.

Worksheet for dependents who checked "Yes" on line 5

(keep a copy for your records)

Use this worksheet to figure the amount to enter on line 5 if someone can claim you (or your spouse if married filing jointly) as a dependent, even if that person chooses not to do so. To find out if someone can claim you as a dependent, use TeleTax topic 354 (see page 8).

A. Amount, if any, from line 1 on front	<u>2694</u>		
	+ <u>250.00</u>	Enter total ▶	A. <u>2944</u>
B. Minimum standard deduction			B. <u>750.00</u>
C. Enter the larger of line A or line B here			C. <u>2944</u>
D. Maximum standard deduction. If single , enter \$4,750; if married filing jointly , enter \$9,500			D. <u>4750</u>
E. Enter the smaller of line C or line D here. This is your standard deduction			E. <u>2944</u>
F. Exemption amount.			F. <u>0</u>
• If single, enter -0-.			
• If married filing jointly and— —both you and your spouse can be claimed as dependents, enter -0-. —only one of you can be claimed as a dependent, enter \$3,050.			
G. Add lines E and F. Enter the total here and on line 5 on the front			G. <u>2944</u>

If you checked "No" on line 5 because no one can claim you (or your spouse if married filing jointly) as a dependent, enter on line 5 the amount shown below that applies to you.

- Single, enter \$7,800. This is the total of your standard deduction (\$4,750) and your exemption (\$3,050).
- Married filing jointly, enter \$15,600. This is the total of your standard deduction (\$9,500), your exemption (\$3,050), and your spouse's exemption (\$3,050).

Mailing return

Mail your return by **April 15, 2004**. Use the envelope that came with your booklet. If you do not have that envelope or if you moved during the year, see the back cover for the address to use.

WAGE EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Comprehensive Problem 2

Form 1040EZ	Department of the Treasury—Internal Revenue Service Income Tax Return for Single and Joint Filers With No Dependents 2003	OMB No. 1545-0675																								
Label (See page 14.) Use the IRS label. Otherwise, please print or type. Presidential Election Campaign (page 14)	<table style="width:100%; border-collapse: collapse;"> <tr> <td style="width:35%; border-bottom: 1px solid black;">Your first name and initial Melody</td> <td style="width:35%; border-bottom: 1px solid black;">Last name York</td> <td style="width:30%; border-bottom: 1px solid black;">Your social security number XXX XX XXXX</td> </tr> <tr> <td style="border-bottom: 1px solid black;">If a joint return, spouse's first name and initial</td> <td style="border-bottom: 1px solid black;">Last name</td> <td style="border-bottom: 1px solid black;">Spouse's social security number</td> </tr> <tr> <td colspan="2" style="border-bottom: 1px solid black;">Home address (number and street). If you have a P.O. box, see page 14. 17 North 9th Avenue</td> <td style="border-bottom: 1px solid black;">Apt. no.</td> </tr> <tr> <td colspan="3" style="border-bottom: 1px solid black;">City, town or post office, state, and ZIP code. If you have a foreign address, see page 14. Your City, State, Zip Code</td> </tr> </table>	Your first name and initial Melody	Last name York	Your social security number XXX XX XXXX	If a joint return, spouse's first name and initial	Last name	Spouse's social security number	Home address (number and street). If you have a P.O. box, see page 14. 17 North 9th Avenue		Apt. no.	City, town or post office, state, and ZIP code. If you have a foreign address, see page 14. Your City, State, Zip Code			<p>▲ Important! ▲ You must enter your SSN(s) above.</p> <p>You Spouse <input type="checkbox"/> Yes <input type="checkbox"/> No <input type="checkbox"/> Yes <input type="checkbox"/> No</p>												
Your first name and initial Melody	Last name York	Your social security number XXX XX XXXX																								
If a joint return, spouse's first name and initial	Last name	Spouse's social security number																								
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<p>Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if a joint return, want \$3 to go to this fund? <input type="checkbox"/> Yes <input type="checkbox"/> No</p>																										
Income Attach Form(s) W-2 here. Enclose, but do not attach, any payment. Note. You must check Yes or No.	<table style="width:100%; border-collapse: collapse;"> <tr> <td style="width:65%; border-bottom: 1px solid black;">1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.</td> <td style="width:5%; text-align: center; border-bottom: 1px solid black;">1</td> <td style="width:15%; text-align: right; border-bottom: 1px solid black;">6,923</td> <td style="width:15%; text-align: right; border-bottom: 1px solid black;">00</td> </tr> <tr> <td style="border-bottom: 1px solid black;">2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.</td> <td style="text-align: center; border-bottom: 1px solid black;">2</td> <td style="border-bottom: 1px solid black;"></td> <td style="border-bottom: 1px solid black;"></td> </tr> <tr> <td style="border-bottom: 1px solid black;">3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).</td> <td style="text-align: center; border-bottom: 1px solid black;">3</td> <td style="text-align: right; border-bottom: 1px solid black;">3,240</td> <td style="text-align: right; border-bottom: 1px solid black;">00</td> </tr> <tr> <td style="border-bottom: 1px solid black;">4 Add lines 1, 2, and 3. This is your adjusted gross income.</td> <td style="text-align: center; border-bottom: 1px solid black;">4</td> <td style="text-align: right; border-bottom: 1px solid black;">10,163</td> <td style="text-align: right; border-bottom: 1px solid black;">00</td> </tr> <tr> <td style="border-bottom: 1px solid black;">5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from worksheet on back. <input type="checkbox"/> No. If single, enter \$7,800. If married filing jointly, enter \$15,600. See back for explanation. <input checked="" type="checkbox"/></td> <td style="text-align: center; border-bottom: 1px solid black;">5</td> <td style="text-align: right; border-bottom: 1px solid black;">7,800</td> <td style="text-align: right; border-bottom: 1px solid black;">00</td> </tr> <tr> <td style="border-bottom: 1px solid black;">6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income.</td> <td style="text-align: center; border-bottom: 1px solid black;">6</td> <td style="text-align: right; border-bottom: 1px solid black;">2,363</td> <td style="text-align: right; border-bottom: 1px solid black;">00</td> </tr> </table>	1 Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1	6,923	00	2 Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2			3 Unemployment compensation and Alaska Permanent Fund dividends (see page 16).	3	3,240	00	4 Add lines 1, 2, and 3. This is your adjusted gross income .	4	10,163	00	5 Can your parents (or someone else) claim you on their return? Yes. Enter amount from worksheet on back. <input type="checkbox"/> No. If single , enter \$7,800. If married filing jointly , enter \$15,600. See back for explanation. <input checked="" type="checkbox"/>	5	7,800	00	6 Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6	2,363	00	
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Refund Have it directly deposited! See page 21 and fill in 11b, 11c, and 11d.	<table style="width:100%; border-collapse: collapse;"> <tr> <td style="width:65%; border-bottom: 1px solid black;">11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund.</td> <td style="width:5%; text-align: center; border-bottom: 1px solid black;">11a</td> <td style="width:15%; text-align: right; border-bottom: 1px solid black;">106</td> <td style="width:15%; text-align: right; border-bottom: 1px solid black;">00</td> </tr> <tr> <td style="border-bottom: 1px solid black;">b Routing number <input type="checkbox"/> XXXXX XXXX c Type: <input type="checkbox"/> Checking <input checked="" type="checkbox"/> Savings</td> <td colspan="3"></td> </tr> <tr> <td style="border-bottom: 1px solid black;">d Account number <input type="checkbox"/> XXXXX XXXX XXXX</td> <td colspan="3"></td> </tr> </table>	11a If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	11a	106	00	b Routing number <input type="checkbox"/> XXXXX XXXX c Type: <input type="checkbox"/> Checking <input checked="" type="checkbox"/> Savings				d Account number <input type="checkbox"/> XXXXX XXXX XXXX																
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Amount you owe	<table style="width:100%; border-collapse: collapse;"> <tr> <td style="width:65%; border-bottom: 1px solid black;">12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe. For details on how to pay, see page 22.</td> <td style="width:5%; text-align: center; border-bottom: 1px solid black;">12</td> <td style="width:15%; border-bottom: 1px solid black;"></td> <td style="width:15%; border-bottom: 1px solid black;"></td> </tr> </table>	12 If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 22.	12																							
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Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 22)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No																									
Sign here Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge. Your signature _____ Date _____ Your occupation _____ Daytime phone number _____ Spouse's signature. If a joint return, both must sign. _____ Date _____ Spouse's occupation _____	Designee's name _____ Phone no. () _____ Personal identification number (PIN) _____ Preparer's signature _____ Date _____ Check if self-employed <input type="checkbox"/> Preparer's SSN or PTIN PXX-XX-XXXX Firm's name (or yours if self-employed), address, and ZIP code _____ EIN _____ Phone no. () _____																									
Paid preparer's use only	Preparer's signature _____ Date _____ Check if self-employed <input type="checkbox"/> Preparer's SSN or PTIN PXX-XX-XXXX Firm's name (or yours if self-employed), address, and ZIP code _____ EIN _____ Phone no. () _____																									

Line 8 Earned Income Credit (EIC)

What Is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.



If you have a qualifying child (see the next column on this page), you may be able to take the credit, but you must use Schedule EIC and Form 1040A or 1040 to do so. For details, see Pub. 596.

To Take the EIC:

- Follow the steps below.
- Complete the worksheet on page 19 **or** let the IRS figure the credit for you.



If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

- Is the amount on Form 1040EZ, line 4, less than \$11,230 (\$12,230 if married filing jointly)?
 Yes. *Continue* **No.** You cannot take the credit.
- Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 18)?
 Yes. *Continue* **No.** You cannot take the credit. Enter "No" in the space to the left of line 8.
- Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?
 Yes. You cannot take the credit. **No.** *Continue*
- Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?
 Yes. *Go to question 5.* **No.** You cannot take the credit.

- Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 18 before you answer.
 Yes. *Continue* **No.** You cannot take the credit. Enter "No" in the space to the left of line 8.

- Look at the qualifying child conditions below. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?
 Yes. You cannot take the credit. Enter "No" in the space to the left of line 8. **No.** *Go to Step 2* on page 18.

A **qualifying child** is a child who is your—

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendent of any of them (for example, your niece or nephew) whom you cared for as your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as your own child)

AND

was at the end of 2003...

Under age 19

or

under age 24 and a student

or

any age and permanently and totally disabled

AND

who...

Either lived with you in the United States for more than half of 2003 **or** was born or died in 2003 and your home was the child's home for the entire time he or she was alive in 2003.

Note. Special rules apply if the child was married or also meets the conditions to be a qualifying child of another person (other than your spouse if filing a joint return). For details, use TeleTax topic 601 (see page 8) or see Pub. 596.

Form 1040EZ, Earned Income Credit Worksheet, line 8, page 2

Form 1040EZ—Line 8

Step 2 Earned Income

1. Figure earned income:

Form 1040EZ, line 1 6,923

Subtract, if included in line 1, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2
- Amount paid to an inmate in a penal institution for work (enter "PRI" in the space to the left of line 1 on Form 1040EZ)
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (enter "DFC" and the amount subtracted in the space to the left of line 1 on Form 1040EZ). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

0

Earned Income = 6,923

2. Is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 3. **No.** 

You cannot take the credit.

Step 3 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See *Credit Figured by the IRS on this page.* **No.** Go to the worksheet on page 19.

Definitions and Special Rules

(listed in alphabetical order)

Credit Figured by the IRS To have the IRS figure the credit for you:

1. Enter "EIC" in the space to the left of line 8 on Form 1040EZ.
2. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- The only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

Members of the Military. If you were on extended active duty outside the United States, your home is considered to be in the United States during that duty period. Extended active duty is military duty ordered for an indefinite period or for a period of more than 90 days. Once you begin serving extended active duty, you are considered to be on extended active duty even if you serve fewer than 90 days.

Social Security Number (SSN). For purposes of taking the EIC, a valid SSN is a number issued by the Social Security Administration unless "Not Valid for Employment" is printed on the social security card and the number was issued solely to apply for or receive a Federally funded benefit.

To find out how to get an SSN, see page 14. If you will not have an SSN by April 15, 2004, see What if You Cannot File on Time? on page 11.

Welfare Benefits, Effect of Credit on. Any refund you receive as a result of taking the EIC will not be used to determine if you are eligible for the following programs or how much you can receive from them. But if the refund you receive because of the EIC is not spent within a certain period of time, it may count as an asset (or resource) and affect your eligibility.

- Temporary Assistance for Needy Families (TANF).
- Medicaid and supplemental security income (SSI).
- Food stamps and low-income housing.

Draft as of 08/27/2003

Form 1040EZ, Earned Income Credit Worksheet, line 8, page 3

Form 1040EZ—Line 8

Earned Income Credit (EIC) Worksheet—Line 8

Keep for Your Records



Part 1

All Filers

1. Enter your earned income from Step 2 on page 18.

1	6,923
---	-------

2. Look up the amount on line 1 above in the EIC Table on page 20 to find the credit. Be sure you use the correct column for your filing status. Enter the credit here.

2	329
---	-----

If line 2 is zero, You cannot take the credit. Enter "No" in the space to the left of line 8.

3. Enter the amount from Form 1040EZ, line 4.

3	10,163
---	--------

4. Are the amounts on lines 3 and 1 the same?
 Yes. Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. Is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?
 Yes. Leave line 5 blank; enter the amount from line 2 on line 6.
 No. Look up the amount on line 3 in the EIC Table on page 20 to find the credit. Be sure you use the correct column for your filing status. Enter the credit here.

5	81
---	----

Look at the amounts on lines 5 and 2. Then, enter the smaller amount on line 6.

Part 3

Your Earned Income Credit

6. This is your earned income credit.

6	81
---	----

Enter this amount on Form 1040EZ, line 8.



If your EIC for a year after 1996 was reduced or disallowed, see page 18 to find out if you must file Form 8862 to take the credit for 2003.

WAGE EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Comprehensive Problem 3

Form 1040A U.S. Individual Income Tax Return (99) 2003

Department of the Treasury—Internal Revenue Service

OMB No. 1545-0085

Your first name and initial: Marvin Last name: Simmons

If a joint return, spouse's first name and initial: Last name:

Home address (number and street). If you have a P.O. box, see page 22. 9701 Austin Rd Apt. no.:

City, town or post office, state, and ZIP code. If you have a foreign address, see page 22. Your City, State, Zip Code:

Your social security number: xxx : xx : xxxxx

Spouse's social security number:

Important! You must enter your SSN(s) above.

Presidential Election Campaign Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if filing a joint return, want \$3 to go to this fund? Yes No Yes No

Filing status Check only one box.

1 Single

2 Married filing jointly (even if only one had income)

3 Married filing separately. Enter spouse's SSN above and full name here. ▶

4 Head of household (with qualifying person). (See page 23.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶

5 Qualifying widow(er) with dependent child (See page 24.)

Exemptions

6a Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a.

b Spouse

c Dependents:

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)	No. of boxes checked on 6a and 6b	No. of children on 6c who:
Eric	Simmons	xxx : xx : xxxxx	Grandson	<input checked="" type="checkbox"/>	1	1
				<input type="checkbox"/>		• did not live with you due to divorce or separation (see page 26)
				<input type="checkbox"/>		
				<input type="checkbox"/>		
				<input type="checkbox"/>		
				<input type="checkbox"/>		

d Total number of exemptions claimed. 2

Income

Line	Description	Amount
7	Wages, salaries, tips, etc. Attach Form(s) W-2.	24,952.00
8a	Taxable interest. Attach Schedule 1 if required.	
8b	Tax-exempt interest. Do not include on line 8a.	
9a	Ordinary dividends. Attach Schedule 1 if required.	
9b	Qualified dividends (see page XX).	
10a	Capital gain distributions (see page 27).	
10b	Post-May 5 capital gain distributions (see page 27).	
11a	IRA distributions.	
11b	Taxable amount (see page 27).	
12a	Pensions and annuities.	
12b	Taxable amount (see page 28).	
13	Unemployment compensation and Alaska Permanent Fund dividends.	
14a	Social security benefits.	
14b	Taxable amount (see page 30).	
15	Add lines 7 through 14b (far right column). This is your total income.	24,952.00
16	Educator expenses (see page 30).	
17	IRA deduction (see page 30).	
18	Student loan interest deduction (see page 33).	
19	Tuition and fees deduction (see page 33).	
20	Add lines 16 through 19. These are your total adjustments.	0.00
21	Subtract line 20 from line 15. This is your adjusted gross income.	24,952.00

Adjusted gross income

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 57. Cat. No. 11327A Form 1040A (2003)

Comprehensive Problem 3

Form 1040A (2003)		Page 2
Tax, credits, and payments	22 Enter the amount from line 21 (adjusted gross income).	22 24,952 | 00
Standard Deduction for— • People who checked any box on line 23a or 23b or who can be claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000	23a Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind } checked ▶ 23a <input type="checkbox"/>	
	b If you are married filing separately and your spouse itemizes deductions, see page 34 and check here ▶ 23b <input type="checkbox"/>	
	24 Enter your standard deduction (see left margin).	24 7,000 | 00
	25 Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25 17,952 | 00
	26 Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26 6,100 | 00
	27 Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income .	▶ 27 11,852 | 00
	28 Tax , including any alternative minimum tax (see page 35).	28 1,281 | 00
	29 Credit for child and dependent care expenses. Attach Schedule 2.	29 293 | 00
	30 Credit for the elderly or the disabled. Attach Schedule 3.	30
	31 Education credits. Attach Form 8863.	31
32 Retirement savings contributions credit. Attach Form 8880.	32	
33 Child tax credit (see page 38).	33 600 | 00	
34 Adoption credit. Attach Form 8839.	34	
35 Add lines 29 through 34. These are your total credits .	35 893 | 00	
36 Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36 388 | 00	
37 Advance earned income credit payments from Form(s) W-2.	37 600 | 00	
38 Add lines 36 and 37. This is your total tax .	▶ 38 988 | 00	
39 Federal income tax withheld from Forms W-2 and 1099.	39 1,964 | 00	
40 2003 estimated tax payments and amount applied from 2002 return.	40	
41 Earned income credit (EIC) .	41 750 | 00	
42 Additional child tax credit. Attach Form 8812.	42	
43 Add lines 39 through 42. These are your total payments .	▶ 43 2,714 | 00	
Refund	44 If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44 1,726 | 00
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	45a Amount of line 44 you want refunded to you .	▶ 45a 1,726 | 00
	b Routing number <input type="text" value="x x x x x x x x x x"/> c Type: <input checked="" type="checkbox"/> Checking <input type="checkbox"/> Savings	
	d Account number <input type="text" value="x x x x x x x x x x x x x x x x"/>	
	46 Amount of line 44 you want applied to your 2004 estimated tax .	46
Amount you owe	47 Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53.	▶ 47
	48 Estimated tax penalty (see page 53).	48
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No	
	Designee's name ▶ _____	Phone no. ▶ () _____
		Personal identification number (PIN) ▶ <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/>
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.	
Joint return? See page 22. Keep a copy for your records.	Your signature	Date / / Your occupation mechanic
	Spouse's signature. If a joint return, both must sign.	Date / / Spouse's occupation
		Daytime phone number () _____
Paid preparer's use only	Preparer's signature ▶ _____	Date / /
	Firm's name (or yours if self-employed), address, and ZIP code ▶ _____	Check if self-employed <input type="checkbox"/>
		Preparer's SSN or PTIN Pxx-xx-xxxx
		EIN _____
		Phone no. () _____



WAGE EARNER COMPREHENSIVE

PROBLEMS

ANSWERS TO PROBLEMS

Comprehensive Problems

Schedule 2 (Form 1040A)

Department of the Treasury—Internal Revenue Service
**Child and Dependent Care
Expenses for Form 1040A Filers**

2003

OMB No. 1545-0085

Name(s) shown on Form 1040A

Marvin Simmons

Your social security number

XXX : XX : XXXX

Before you begin: You need to understand the following terms. See **Definitions** on page 1 of the separate instructions.

• **Dependent Care Benefits** • **Qualifying Person(s)** • **Qualified Expenses** • **Earned Income**

Part I

Persons or organizations who provided the care

1	(a) Care provider's name	(b) Address (number, street, apt. no., city, state, and ZIP code)	(c) Identifying number (SSN or EIN)	(d) Amount paid (see instructions)
	Joy Day Care	9192 East Huron Your City, State, Zip Code	XX-XXXXXXXX	978

(If you need more space, use the bottom of page 2.)

You must complete this part.

Did you receive dependent care benefits?

No

Complete only Part II below.

Yes

Complete Part III on the back next.

Caution. If the care was provided in your home, you may owe employment taxes. If you do, you must use Form 1040. See **Schedule H** and its instructions for details.

Part II

Credit for child and dependent care expenses

2 Information about your **qualifying person(s)**. If you have more than two qualifying persons, see the instructions.

(a) Qualifying person's name	(b) Qualifying person's social security number	(c) Qualified expenses you incurred and paid in 2003 for the person listed in column (a)
First Last		
Eric Simmons	XXX : XX : XXXX	978
3 Add the amounts in column (c) of line 2. Do not enter more than \$3,000 for one qualifying person or \$6,000 for two or more persons. If you completed Part III, enter the amount from line 26.		3 978
4 Enter your earned income .		4 24,952
5 If married filing jointly, enter your spouse's earned income (if your spouse was a student or was disabled, see the instructions); all others , enter the amount from line 4.		5 24,952
6 Enter the smallest of line 3, 4, or 5.		6 978
7 Enter the amount from Form 1040A, line 22.		7 24,952
8 Enter on line 8 the decimal amount shown below that applies to the amount on line 7.		
If line 7 is:		
Over	But not over	Decimal amount is
\$0—15,000		.35
15,000—17,000		.34
17,000—19,000		.33
19,000—21,000		.32
21,000—23,000		.31
23,000—25,000		.30
25,000—27,000		.29
27,000—29,000		.28
If line 7 is:		
Over	But not over	Decimal amount is
\$29,000—31,000		.27
31,000—33,000		.26
33,000—35,000		.25
35,000—37,000		.24
37,000—39,000		.23
39,000—41,000		.22
41,000—43,000		.21
43,000—No limit		.20
		8 × .30
9 Multiply line 6 by the decimal amount on line 8. If you paid 2002 expenses in 2003, see the instructions.		9 293
10 Enter the amount from Form 1040A, line 28.		10 1,281
11 Credit for child and dependent care expenses. Enter the smaller of line 9 or line 10 here and on Form 1040A, line 29.		11 293

For Paperwork Reduction Act Notice, see Form 1040A instructions.

Cat. No. 10749I

Schedule 2 (Form 1040A) 2003

Child Tax Credit Worksheet—Line 33

Keep for Your Records

Before you begin: ✓ If you received (before offset) an advance payment of the child tax credit and you filed a joint return for 2002, you and your spouse are each considered to have received one-half of the payment.



If you received Notice 1319, have it available. The notice shows the amount of your advance payment (before offset). If you do not have Notice 1319, you can check the amount of your advance payment (before offset) on the IRS website at www.irs.gov. You will need to enter your SSN, your 2002 filing status, and the total number of exemptions you claimed on line 6d of your 2002 Form 1040 or Form 1040A.



- To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2003 and meet the other requirements listed on page 38.
- **Do not** use this worksheet if you answered “Yes” to question 1 or 2 on page 38. Instead, use Pub. 972.

1. Number of qualifying children: 1 × \$1,000.

1	1000
---	------

Enter the result.

2. Enter the amount, if any, of your advance child tax credit (before offset).

2	400
---	-----

3. Is line 1 less than or equal to line 2?

Yes.

You cannot take this credit. If line 2 is more than line 1, you do not have to pay back the difference.

No. Subtract line 2 from line 1.

3	600
---	-----

4. Enter the amount from Form 1040A, line 28.

4	1281
---	------

5. Add the amounts from Form 1040A, lines 29 through 32.

5	293
---	-----

6. Are the amounts on lines 4 and 5 the same?

Yes.

You cannot take this credit because there is no tax to reduce. However, you may be able to take the **additional child tax credit**. See the **TIP** below.

No. Subtract line 5 from line 4.

6	988
---	-----

7. Is the amount on line 3 more than the amount on line 6?

Yes. Enter the amount from line 6. Also, you may be able to take the **additional child tax credit**. See the **TIP** below.

This is your child tax credit.

No. Enter the amount from line 3.

7	600
---	-----

Enter this amount on Form 1040A, line 33.



You may be able to take the **additional child tax credit** on Form 1040A, line 42, if you answered “Yes” on line 6 or line 7 above.



- First, complete your Form 1040A through line 41.
- Then, use Form 8812 to figure any additional child tax credit.

Form 1040A, Earned Income Credit Worksheet, line 41, page 1

Line 41— Earned Income Credit (EIC)

What is the EIC?

The EIC is a credit for certain people who work. The credit may give you a refund even if you do not owe any tax.

To Take the EIC:


- Follow the steps below.
- Complete the worksheet that applies to you **or** let the IRS figure the credit for you.
- If you have a qualifying child, complete and attached Schedule EIC.





If you take the EIC even though you are not eligible and it is determined that your error is due to reckless or intentional disregard of the EIC rules, you will not be allowed to take the credit for 2 years even if you are otherwise eligible to do so. If you fraudulently take the EIC, you will not be allowed to take the credit for 10 years. You may also have to pay penalties.

Step 1 All Filers

1. If, in 2003:
 - 2 children lived with you, is the amount on Form 1040A, line 22, less than \$33,692 (\$34,692 if married filing jointly)?
 - 1 child lived with you, is the amount on Form 1040A, line 22, less than \$29,666 (\$30,666 if married filing jointly)?
 - No children live with you, is the amount on Form 1040A, line 22, less than \$11,230 (\$12,230 if married filing jointly)?

Yes. *Continue* → **No.**  You cannot take the credit.
2. Do you, and your spouse if filing a joint return, have a social security number that allows you to work or is valid for EIC purposes (see page 42)?

Yes. *Continue* → **No.**  You cannot take the credit. Put "No" to the left of the entry space for line 41.
3. Is your filing status married filing separately?

Yes.  You cannot take the credit. **No.** *Continue* →
4. Were you a nonresident alien for any part of 2003?

Yes. *See Nonresident aliens on page 42.* **No.** *Go to Step 2.*


Step 2 Investment Income

1. Add the amounts from Form 1040A:

Line 8a _____
Line 8b + _____
Line 9a + _____
Line 10a + _____

Investment Income =

2. Is your investment income more than \$2,600?

Yes.  **No.** *Continue* →
You cannot take the credit.

3. Did a child live with you in 2003?

Yes. *Go to Step 3 on page 40.* **No.** *Go to Step 4 on page 40.*

Form 1040A, Earned Income Credit Worksheet, line 41, page 2

Form 1040A—Line 41

Step 3 Qualifying Child

A qualifying child is a child who is your...

Son, daughter, adopted child, stepchild, or a descendant of any of them (for example, your grandchild)

or

Brother, sister, stepbrother, stepsister, or a descendant of any of them (for example, your niece or nephew) whom you cared for as you would your own child

or

Foster child (any child placed with you by an authorized placement agency whom you cared for as you would your own child)

AND

was at the end of 2003...

Under age 19

or

Under age 24 and a student (see page 42)

or

Any age and permanently and totally disabled (see page 42)


AND

who...

Lived with you in the United States for more than half of 2003. If the child did not live with you for the required time, see Exception to "Time Lived With You" Condition on page 41.

Note. If the child was married, see page 42.

1. Look at the qualifying child conditions above. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →

You cannot take the credit. Put "No" to the left of the entry space for line 41.

2. Do you have at least one child who meets the above conditions to be your qualifying child?


Yes. *Go to question 3.* **No.** *Skip question 3; go to Step 4, question 2.*

3. Does the child meet the conditions to be a qualifying child of any other person (other than your spouse if filing a joint return) for 2003?


Yes. *See Qualifying Child of More Than One Person on page 42.* **No.** This child is your qualifying child. The child must have a valid social security number as defined on page 42 unless the child was born and died in 2003. *Skip Step 4; go to Step 5 on page 41.*

Step 4 Filers Without a Qualifying Child


1. Look at the qualifying child conditions in Step 3. Could you, or your spouse if filing a joint return, be a qualifying child of another person in 2003?

Yes.  **No.** *Continue* →
You cannot take the credit. Put "No" to the left of the entry space for line 41.


2. Can you, or your spouse if filing a joint return, be claimed as a dependent on someone else's 2003 tax return?

Yes.  **No.** *Continue* →
You cannot take the credit.

3. Were you, or your spouse if filing a joint return, at least age 25 but under age 65 at the end of 2003?

Yes. *Continue* → **No.**  You cannot take the credit.

4. Was your home, and your spouse's if filing a joint return, in the United States for more than half of 2003? Members of the military stationed outside the United States, see page 42 before you answer.

Yes. *Go to Step 5 on page 41.* **No.**  You cannot take the credit. Put "No" to the left of the entry space for line 41.

WAGE EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Form 1040A, Earned Income Credit Worksheet, line 41, page 3

Step 5 Earned Income

1. Figure earned income:

Form 1040, line 7 24,952

Subtract, if included on line 7, any:

- Taxable scholarship or fellowship grant not reported on a Form W-2.
- Amount paid to an inmate in a penal institution for work (put "PRI" and the amount subtracted to the left of the entry space for line 7 of Form 1040A).
- Amount received as a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan (put "DFC" and the amount subtracted to the left of the entry space for line 7 of Form 1040A). This amount may be shown in box 11 of your Form W-2. If you received such an amount but box 11 is blank, contact your employer for the amount received as a pension or annuity.

Earned Income = 24,952

2. If you have:

- 2 or more qualifying children, is your earned income less than \$33,692 (\$34,692 if married filing jointly)?
- 1 qualifying child, is your earned income less than \$29,666 (\$30,666 if married filing jointly)?
- No qualifying children, is your earned income less than \$11,230 (\$12,230 if married filing jointly)?

Yes. Go to Step 6. **No.** 

You cannot take the credit.

Step 6 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?

Yes. See Credit Figured by the IRS below. **No.** Go to the worksheet on page 43.

Definitions and Special Rules

(listed in alphabetical order)

Adopted Child. An adopted child is always treated as your own child. An adopted child includes a child placed with you by an authorized placement agency for legal adoption even if the adoption is not final. An authorized placement agency includes any person or court authorized by state law to place children for legal adoption.

Credit Figured by the IRS. To have the IRS figure the credit for you:

1. Put "EIC" to the left of the entry space for line 41 of Form 1040A.
2. If you have a qualifying child, complete and attach Schedule EIC. If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, Who Must File, below.

Exception to "Time Lived With You" Condition. A child is considered to have lived with you for all of 2003 if the child was born or died in 2003 and your home was this child's home for the entire time he or she was alive in 2003. Temporary absences, such as for school, vacation, medical care, or detention in a juvenile facility, count as time lived at home. If your child is presumed to have been kidnapped by someone who is not a family member, see Pub. 596 to find out if that child is a qualifying child for the EIC. To get Pub. 596, see page 7. If you were in the military stationed outside the United States, see Members of the Military on page 42.

Form 8862, Who Must File. You must file Form 8862 if your EIC for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But you do not have to file Form 8862 if either of the following applies.

- After your EIC was reduced or disallowed in an earlier year (a) you filed Form 8862 (or other documents) and your EIC was then allowed and (b) your EIC has not been reduced or disallowed again for any reason other than a math or clerical error.
- You are taking the EIC without a qualifying child and the only reason your EIC was reduced or disallowed in the earlier year was because it was determined that a child listed on Schedule EIC was not your qualifying child.

Also, do not file Form 8862 or take the credit if it was determined that your error was due to reckless or intentional disregard of the EIC rules or fraud.

Earned Income Credit (EIC) Worksheet—Line 41

Keep for Your Records



Part 1


All Filers

1. Enter your earned income from Step 5 on page 43.

1	24,952
---	--------

2. Look up the amount on line 1 above in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

2	750
---	-----

If line 2 is zero,  You cannot take the credit. Put "No" to the left of the entry space for line 41.

3. Enter the amount from Form 1040A, line 22.

3	24,952
---	--------

4. Are the amounts on lines 3 and 1 the same?

- Yes.** Skip line 5; enter the amount from line 2 on line 6.
 No. Go to line 5.

Part 2

Filers Who Answered "No" on Line 4

5. If you have:
- No qualifying children, is the amount on line 3 less than \$6,250 (\$7,250 if married filing jointly)?
 - 1 or more qualifying children, is the amount on line 3 less than \$13,750 (\$14,750 if married filing jointly)?
- Yes.** Leave line 5 blank; enter the amount from line 2 on line 6.

- No.** Look up the amount on line 3 in the EIC Table on pages 46–51 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

5	
---	--

Look at the amounts on lines 5 and 2. Then, enter the **smaller** amount on line 6.

Part 3

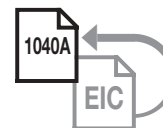
Your Earned Income Credit

6. This is your earned income credit.

6	750
---	-----

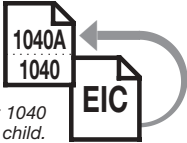


Enter this amount on Form 1040A, line 41.

- Reminder—**
- ✓ If you have a qualifying child, complete and attach Schedule EIC.



If your EIC for a year after 1996 was reduced or disallowed, see page 43 to find out if you must file Form 8862 to take the credit for 2003.

Schedule EIC

<p>SCHEDULE EIC (Form 1040A or 1040)</p> <p>Department of the Treasury Internal Revenue Service</p> <p>Name(s) shown on return</p>	<p>Earned Income Credit Qualifying Child Information</p> <p>Complete and attach to Form 1040A or 1040 only if you have a qualifying child.</p>	<p>OMB No. 1545-0074</p> <p>2003</p> <p>Attachment Sequence No. 43</p>	
<p>Marvin Simmons</p>		<p>Your social security number XXX | XX | XXXX</p>	
<p>Before you begin: See the instructions for Form 1040A, line 41, or Form 1040, line 63, to make sure that (a) you can take the EIC and (b) you have a qualifying child.</p>			
<p> If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See back of schedule for details.</p> <p>It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.</p> <p>Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.</p>			
<p>Qualifying Child Information</p>			
		<p>Child 1</p>	<p>Child 2</p>
<p>1 Child's name If you have more than two qualifying children, you only have to list two to get the maximum credit.</p>	<p>First name Eric</p>	<p>Last name Simmons</p>	<p>First name</p> <p>Last name</p>
<p>2 Child's SSN The child must have an SSN as defined on page 44 of the Form 1040A instructions or page 46 of the Form 1040 instructions unless the child was born and died in 2003. If your child was born and died in 2003 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate.</p>	<p>XXX | XX | XXXX</p>	<p>XXX | XX | XXXX</p>	<p>XXX | XX | XXXX</p>
<p>Next, if the child was born after 1984, go to line 4. Otherwise, continue.</p>			
<p>3 If the child was born before 1985—</p>	<p><input type="checkbox"/> Yes. <i>Go to line 4.</i></p>	<p><input type="checkbox"/> No. <i>Continue</i></p>	<p><input type="checkbox"/> Yes. <i>Go to line 4.</i></p> <p><input type="checkbox"/> No. <i>Continue</i></p>
<p>a Was the child under age 24 at the end of 2003 and a student?</p>	<p><input type="checkbox"/> Yes. <i>Continue</i></p>	<p><input type="checkbox"/> No. The child is not a qualifying child.</p>	<p><input type="checkbox"/> Yes. <i>Continue</i></p> <p><input type="checkbox"/> No. The child is not a qualifying child.</p>
<p>b Was the child permanently and totally disabled during any part of 2003?</p>			
<p>4 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)</p>	<p>Grandchild</p>		
<p>5 Number of months child lived with you in the United States during 2003</p> <p>• If the child lived with you for more than half of 2003 but less than 7 months, enter "7".</p> <p>• If the child was born or died in 2003 and your home was the child's home for the entire time he or she was alive during 2003, enter "12".</p>	<p style="text-align: center;">12 months <i>Do not enter more than 12 months.</i></p>	<p style="text-align: center;">_____ months <i>Do not enter more than 12 months.</i></p>	<p style="text-align: center;">_____ months <i>Do not enter more than 12 months.</i></p>
<p> You may also be able to take the additional child tax credit if your child (a) was under age 17 at the end of 2003, (b) is claimed as your dependent on line 6c of Form 1040A or Form 1040, and (c) is a U.S. citizen or resident alien. For more details, see the instructions for line 42 of Form 1040A or line 65 of Form 1040.</p>			
<p>For Paperwork Reduction Act Notice, see Form 1040A or 1040 instructions.</p>		<p>Cat. No. 13339M</p>	<p>Schedule EIC (Form 1040A or 1040) 2003</p>

OBJECTIVES

After completing this lesson you should be able to:

- Identify the items that affect the basis of a stock.
- Determine if a stock's holding period is long term or short term.
- Determine when and how to report commissions from sale of stock on Schedule D.
- Calculate the amount of the qualified 5-year gain (On transactions concluded before May 6, 2003.).
- Calculate the taxable gain or deductible loss using Schedule D.
- Calculate the tax liability using Part IV of Schedule D.
- Calculate the amount of capital loss carryover using the capital loss carryover worksheet.

What You Will Need

In order for you to complete Schedule D, the taxpayer will need to show you his or her records, including information returns he or she receives that are also forwarded to IRS.

- Form 1099-B, *Proceeds From Broker and Barter Exchange Transactions*, which the broker gives the taxpayer to report the sale price of stock.
- The taxpayer's records of his or her basis in the stock sold. Basis is explained in this lesson.
- The taxpayer's records of the date he or she originally acquired the stock.
- Form 1099-DIV, *Dividends and Distributions*, if the taxpayer received capital gain distributions (for example, from a mutual fund).
- The taxpayer's *Capital Loss Carryover Worksheet* from last year's Schedule D instructions if the taxpayer is carrying over a loss to 2003.

The Internal Revenue Service (IRS) receives copies of Form 1099-B from the broker and copies of Form 1099-DIV from the payer. The taxpayer should not file these items with the return, but keep them with his or her records.

The Jobs and Growth Tax Relief Reconciliation Act of 2003 reduced the 10% and 20% capital gains rates to 5% and 15% for capital gains realized on or after May 6, 2003. For tax year 2003 only the Schedule D will have a column (G) which requires an entry for capital gains transactions after May 5, 2003. The net effect of this law is that taxpayers may have two different tax rates for capital gains transactions in 2003. The key to successful completion of the form and calculation of the correct tax is to follow the Schedule D line requests for information very carefully.

Capital Asset

A **capital asset** is any asset held either for personal use or for investment. Thus, all your items of personal property, such as your home and car, are capital assets. Property held for investment includes stocks and bonds. Property used in a trade or business, such as inventory or machinery, is not a capital asset.

In this lesson, corporate stock is the only capital asset discussed. **Capital gain distributions** are also discussed. They are recognized when the entity (such as a mutual fund) that owned a capital asset disposes of it and passes gain through to its shareholders. The discussion of capital gain distributions in this lesson supplements what you previously learned in Lesson 2.

Capital Gains Distribution (Only)

The Schedule D generally is not needed for taxpayers who received capital gain distributions from mutual funds but did not sell any shares of stock and do not have any Forms 1099-B as explained in Lesson 2, Income. Instead, report the total capital gain distribution on Form 1040, line 13a, or on Form 1040A, line 10a. If the taxpayer must file Form 1040, remember to check the box next to line 13 of Form 1040 to indicate that Schedule D is not required. If the taxpayer sold stocks, he or she must file Form 1040 and cannot report capital gain distributions on Form 1040A.

Basis

The **basis** of property is usually its cost. Certain additional costs relating to its purchase are included in the basis of a capital asset. An example of an expense to include in the basis of stock is the commission or fee paid to a broker when stock is purchased.

If the taxpayer is not able to provide his or her basis in the property, the IRS will deem it to be zero. The taxpayer should make every effort to determine the basis. Refer taxpayers to their stockbroker or financial planner for assistance in determining basis. Once the taxpayer has the basis, volunteers may assist in preparing the tax return.

Adjusted Basis

Events after purchase can require adjustments to the basis of stock. The term **adjusted basis** refers to the basis after changes are made. For example, when a stock dividend or stock split is declared, the stockholder receives additional shares of stock. Some of the basis from the original stock is then allocated to the new stock. This change reduces the basis per share of the original shares.

Example 1

Fran paid \$1,100 for 100 shares of ABC, Inc. stock (including the broker's commission of \$25). Fran received 10 additional shares of ABC stock as a tax-free stock dividend. Her \$1,100 basis must be spread over 110 shares (100 original shares plus the 10-share stock dividend). Her basis per share decreases from \$11 to \$10 per share.

Holding Period

Long-term or short-term. Capital gains and losses are classified as either "long-term" or "short-term," depending on how long the taxpayer owned the stock. Stock held for more than one year (12 months) has a long-term holding period. Stock held for one year or less has a short-term holding period.

Example 2

Loretta bought stock on January 11, 2002 (trade date). Her holding period began the next day, January 12. If she sells that stock on January 11, 2003, she will not have owned them for more than a year. The holding period will be short-term. However, if she sells the stock on January 12, 2003, or later, the holding period will be long-term.

Blocks. Frequently, a taxpayer owns shares of stock that were bought on different dates or for different prices. That is, the individual owns more than one block of stock. Each block may differ from the others in its holding period (long-term or short-term), its basis (amount paid for the stock), or both.

In directing a broker to sell stock, the taxpayer may specify which block, or part of a block, to sell. Specification can make a difference in determining the holding period or basis of the stock sold, giving the taxpayer an element of control and versatility in handling an investment. To be valid, any such specification must be made before or at the time of sale. It cannot be made after the sale. If the taxpayer does not identify the specific block at the time of sale, shares sold are treated as coming from the earliest block purchased.

TAX TIPS



To find out how long the taxpayer has held the stocks, begin counting on the day *after the day* he or she bought the shares of stock and include the day the shares were sold. This sale trade date is part of the holding period.

POTENTIAL PITFALLS

Stock splits and stock dividends do not occur often. However, do not assume that they never happen. Ask taxpayers if they received any additional shares from a stock split or stock dividend.

Example 3

In 1996, Tina bought 100 shares of Acme Corporation stock for \$2,000. In 1997 she bought another 100 shares of Acme for \$2,300. In 2003, Tina sold 100 shares of Acme for \$3,000.

The adjusted basis of the shares sold is \$2,000. However, if Tina had told her broker to sell the 100 shares bought in 1997, the adjusted basis of the shares sold would have been \$2,300, reducing her profit (and any taxable amount) on the sale.

Tax-free stock dividends and stock splits. Stock acquired in a tax-free stock dividend or stock split has the same holding period as the original stock owned. Thus, if the original stock has a long-term holding period, stock received in a tax-free stock dividend also has a long-term holding period. Similarly, if the original stock has a holding period of three months, the new stock immediately has a three-month holding period.

Example 4

On February 18, 1999, Wallace bought 500 shares of XYZ Corporation stock for \$1,500, including his broker's commission. XYZ distributed a two-percent stock dividend on April 6, 2003. On April 9, 2003, Wallace sold all his XYZ stock for \$2,030. He has a long-term capital gain of \$530 on the sale of his stock. Although he owned the 10 shares he received as a tax-free stock dividend for only three days, all the stock has a long-term holding period.

Taxable dividends. There are several types of taxable dividends, as discussed in Lesson 2. A taxpayer who participates in a dividend reinvestment plan (one type of taxable dividend) will use the dividends to purchase more shares of the stock. The stocks acquired (including fractional shares) through the dividend reinvestment plan are added to the taxpayer's basis at fair market value on the date of distribution. Thus, the new shares of stock do not always have the same holding period as the original stock. If the taxpayer does not know their basis refer them to their stockbroker or financial planner.

Demutualization

Some taxpayers have been informed by their insurance company that the company has been demutualized. When this happens the policy holder receives either a block of stock or the cash equivalent of company stock. The holding period for such stock is the length of time the policy has been in effect, usually many years. The basis for this stock is zero. The taxpayer must report all of the proceeds as a capital gain, usually long term.

POTENTIAL PITFALLS



Shares from a stock dividend may or may not have the same holding period as the original shares.

Wash Sales

Generally, a **wash sale** occurs when stock is sold and, within 30 days before or after the sale, substantially identical stock is bought. A loss on a wash sale is not deductible, and special rules relate to the basis of the replacement stock. However, a gain on a wash sale must be reported. Any taxpayer with a wash sale should be referred to a paid professional tax preparer.

Sales Price, Form 1099-B, and Adjusted Basis

The stockbroker reports **sales price** to the Internal Revenue Service in box 2 of Form 1099-B, *Proceeds From Broker and Barter Exchange Transactions* (see Exhibit 1). Some brokers do not subtract commissions and fees; they report the **gross proceeds** as the sales price. Other brokers do subtract commissions and fees, reporting the **gross proceeds less commissions** (referred to as **net proceeds** in this lesson) as the sales price. The broker checks the appropriate square at the right of box 2 to indicate whether the gross or net proceeds were reported to IRS.

If Form 1099-B reports gross proceeds, add the sales broker's commissions and fees to the basis. If Form 1099-B reports net proceeds, the broker already subtracted the commissions and fees the seller paid. Do not adjust the basis further.

Exhibit 1

Form 1099-B

7979		<input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0715		2003 Form 1099-B	Proceeds From Broker and Barter Exchange Transactions
PAYER'S name, street address, city, state, ZIP code, and telephone no.		1a Date of sale		Reported to IRS <input type="checkbox"/> Gross proceeds				2 Stocks, bonds, etc. $	☐ Gross proceeds less commissions and option premiums
		1b CUSIP no.					
PAYER'S Federal identification number	RECIPIENT'S identification number	3 Bartering \$		4 Federal income tax withheld \$		Copy A For Internal Revenue Service Center File with Form 1096. For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G.	
RECIPIENT'S name		5 Description		Regulated Futures Contracts			
Street address (including apt. no.)		6a Profit or (loss) realized in 2003 \$		6b Post-5/5/2003 profit or (loss) realized \$			
City, state, and ZIP code		7 Unrealized profit or (loss) on open contracts—12/31/2002 \$		8 Unrealized profit or (loss) on open contracts—12/31/2003 \$			
Account number (optional)	2nd TIN not. <input type="checkbox"/>	9a Aggregate profit or (loss) \$		9b Post-5/5/2003 aggregate profit or (loss) \$			

Form 1099-B Cat. No. 14411V Department of the Treasury - Internal Revenue Service

Do Not Cut or Separate Forms on This Page — Do Not Cut or Separate Forms on This Page

Example 5

George sold stock for \$2,300. He paid his broker a commission of \$35 on the sale and received net proceeds of \$2,265. If his broker reported the gross proceeds, box 2 of Form 1099-B would show \$2,300, and the box next to gross proceeds would be checked. If his broker reported the net proceeds, box 2 of Form 1099-B would show \$2,265, and the box next to gross proceeds less commissions would be checked.

As a general rule, you will need the following information from Form 1099-B:

Information You Will Need From Form 1099-B	
IF Form 1099-B shows information in:	THEN report it on:
Box 1a , Date of sale	Schedule D, column (c), of either Part I, line 1, or Part II, line 8
Box 2 , Sales price reported to Internal Revenue Service whether gross or net proceeds were reported	Schedule D, column (d), of either Part I, line 1, or Part II, (line 8
Box 4 , Federal income tax withheld	Form 1040, line 61
Box 5 , Description of the property sold	Schedule D, column (a) in either Part I, line 1, or Part II, line 8

If there are entries in box 3 or in boxes 6 through 9 of Form 1099-B, refer the taxpayer to a paid professional tax preparer.

Form 1099-B does **not** include the date the taxpayer bought the stock or what he or she paid for it. The taxpayer will need to provide you with this information.

Some brokers do not issue standard Forms 1099-B. Instead they issue a statement, sometimes titled “A 1099 Consolidated Statement,” which shows stock sales and other types of distributions such as dividends and interest. Exhibit 2 is an example of such a statement.

Exhibit 2

A 1099 Consolidated Statement

Payer		Account Number 7764366		SS# 000-00-7026	
KING INVESTMENTS 555 CENTER STREET NEW YORK, NY 10022		Paul J. Birch Susan L. Birch 123 Green Street Claremont, VA 91711			
1099-INT Interest Income 2003					
Interest income not included in box 3	Early withdrawal penalty	US Savings Bonds and other US Treasury interest	Federal income tax withheld	Foreign tax paid	Foreign country or US possession
Box 1 \$378.00	Box 2	Box 3 \$100.00	Box 4	Box 5	Box 6
1099-DIV Dividends & Distributions 2003					
Ordinary dividends	Capital gain distributions	28% rate gain	Unrecaptured sec. 1250 gain	Section 1202 gain	Non-taxable distributions
Box 1 \$559.00	Box 2a \$179.00	Box 2b	Box 2c	Box 2d	Box 3
Investment expenses	Foreign tax paid	Foreign country or US possession	Liquidation distributions—cash	Liquidation distributions—non-cash	Box 4
Box 35	Box 6 \$25.00	Box 7	Box 8	Box 9	
1099-B Proceeds from Broker and Barter Exchange Transactions 2003					
Reference number	Trade date (Box 1a)	CUSIP number (Box 1b)	Quantity Description (Box 5)	Price	Gross proceeds less commissions (Box 2)
145367	7/17/03	765298	200 shrs ABC Corp.	\$16.75	\$3,299.90
239863	10/23/03	927651	300 shrs XYZ Markets, Inc.	\$83.65	\$25,000.20
Totals					\$28,300.10
1099-R Distributions from IRAs 2003					
Gross distribution (Box 1)	Taxable amount (Box 2a)	Taxable amount not determined	(Box 2b) Total Distribution	Federal Income tax withheld (Box 4)	Distribution Code (Box 7)
\$2,000	\$2,000			\$0.00	7-Normal Distribution
					IRA/SEP/SIMPLE Yes

Qualified 5-Year Gain Applies to transactions prior to May 6, 2003

In 2001, the capital gains rate on qualified property held for more than five years was lowered to 18% (8% for lower income taxpayers). These reduced rates continue to apply to sales of qualified property before May 6, 2003. Sales after May 5, 2003, will be taxed using the reduced tax rates introduced earlier in this lesson. The schedule D has been redesigned to accommodate the multiple tax rates that could apply for 2003. You should exercise caution when completing the Schedule D.

Exhibit 3

2003 Qualified 5-year Worksheet

Qualified 5-Year Gain Worksheet—Line 35

Keep for Your Records



1. Enter the total of all gains that you reported on line 8, column (f), of Schedules D and D-1 from property held more than 5 years and disposed of before May 6, 2003. Do not reduce these gains by any losses	1.	
2. Enter the total of all gains from property held more than 5 years and disposed of before May 6, 2003, from Form 4797, Part I, but only if Form 4797, line 7, column (g), is more than zero. Do not reduce these gains by any losses	2.	
3. Enter the total of all capital gains from property held more than 5 years and disposed of before May 6, 2003, from Form 4684, line 4, but only if Form 4684, line 15, is more than zero. Do not reduce these gains by any losses	3.	
4. Enter the total of all capital gains from property held more than 5 years and disposed of before May 6, 2003, from Form 6252; Form 6781, Part II; and Form 8824. Do not reduce these gains by any losses	4.	
5. Enter the total of any qualified 5-year gain reported to you on:		
<ul style="list-style-type: none"> • Form 1099-DIV, box 2c; • Form 2439, box 1c; and • Schedule K-1 from a partnership, S corporation, estate, or trust (do not include gains from section 1231 property; take them into account on line 2 above, but only if Form 4797, line 7, column (g), is more than zero).	}	. . . . . 5.
6. Add lines 1 through 5	6.	
7. Enter the part, if any, of the gain on line 6 that is:		
<ul style="list-style-type: none"> • Attributable to 28% rate gain or • Included on line 6, 10, 11, or 12 of the Unrecaptured Section 1250 Gain Worksheet on page D-7.	}	. . . . . 7.
8. Qualified 5-year gain. Subtract line 7 from line 6. Enter the result here and on Schedule D, line 35	8.	

Exercise 1

For the following situations, determine the adjusted basis of the stock sold, whether the holding period is long-term or short-term, and how the sales price is reported.

- A.** On May 11, 2000, Morris bought 1,000 shares of ZZZ Corporation stock for \$5,000, plus a \$100 commission. On February 14, 2003, he sold 500 shares for \$3,300 and paid a \$45 commission. The broker reported net proceeds on the sale.
1. What is the adjusted basis of the stock sold? _____

 2. Is the holding period long term or short term? _____

 3. What amount is reported to the Internal Revenue Service in box 2 of Form 1099-B? _____

- B.** In the case of Morris, above, assume that he bought 500 more shares of ZZZ stock on October 6, 2002, for \$3,500, plus a \$50 commission. At the time of the sale, he told the broker to sell the stock he had bought in 2002.
1. What is the adjusted basis of the stock sold? _____
 2. Is the holding period long term or short term? _____

- C.** On November 30, 2000, Janice bought 100 shares of ABC Corporation stock for \$9,965, plus a \$35 commission. On January 5, 2003, the stock split two-for-one, and she then held a total of 200 shares. On March 6, 2003, she sold 100 shares for \$6,470 and paid a \$30 commission. Her broker reported net proceeds.
1. What is the adjusted basis of the stock sold? _____
 2. Is the holding period long term or short term? _____

 3. What amount is reported to the Internal Revenue Service in box 2 of Form 1099-B? _____

REPORTING GAIN OR LOSS ON SCHEDULE D

Use Schedule D (Form 1040), *Capital Gains and Losses*, to report gain or loss on the sale of stock. Figure gain or loss by subtracting the adjusted basis of stock sold from its sales price. If the sales price is greater, the taxpayer has gain on the sale. By contrast, if the adjusted basis is greater than the sales price, the taxpayer has a loss on the sale. To denote a loss, place the number in parentheses. The taxpayer should receive Form 1099-B, reporting each sale of stock.

Also use Schedule D to report capital gain distributions that the taxpayer has in addition to any sales of stock. Enter the capital gain distributions on Schedule D, Part II, line 13. They are reported to the taxpayer on Form 1099-DIV, *Dividends and Distributions*, box 2a.

Any distributions that are qualified 5-year gain will be reported to the taxpayer in box 2c and used to complete the Qualified 5-year gain Worksheet in the Schedule D instructions.

If the taxpayer had capital gain distributions, but did not sell stock, he or she may not have to use Schedule D. Instead, report the capital gain distributions as explained in Lesson 2, Income.

Schedule D is divided into four parts. They are:

- Part I, *Short-Term Capital Gains and Losses*. For assets held one year or less.
- Part II, *Long-Term Capital Gains and Losses*. For assets held more than one year. Part II shows all long-term gains and losses and identifies the part subject to the 28% tax rate. The 28% rate applies to section 1202 gain from the sale or exchange of qualified small business stock and to collectibles.
- Part III, *Taxable Gain or Deductible Loss*.
- Part IV, *Tax Computation Using Maximum Capital Gains Rates*. You should have no trouble with Part IV if you take your time and do as the form says for each line. Using Part IV, rather than the Tax Table or Tax Rate Schedules, may result in lower tax.

Parts I and II: Short-Term and Long-Term Capital Gains and Losses

Report transactions in Parts I and II as follows:

To Report Capital Gain or Loss in Part I or II, Schedule D		
	Short-Term	Long-Term
Show the first four sales on:	Part I, Line 1, Schedule D	Part II, line 8, Schedule D
For additional sales, use:	Part I, line 1, Schedule D-1	Part II, line 8, Schedule D-1
And transfer the total sales amount:	From Part I, line 2, Schedule D-1	From Part II, line 9, Schedule D-1
	Onto Part I, line 2, Schedule D	Onto Part II, line 9, Schedule D

Add the sales price amounts in column (d), lines 1 and 2 of Part I. Enter the result on line 3. Then add the amounts in column (d), lines 8 and 9 of Part II. Enter the result on line 10. The total of line 3 plus line 10 must equal the total from box 2 of all the taxpayer's Forms 1099-B. If they do not agree, the taxpayer should attach a statement to the return to explain the difference.

The Internal Revenue Service will compare the amounts reported on all of a taxpayer's Forms 1099-B with the sum of the amounts reported on lines 3 and 10 of Schedule D. If the numbers do not agree and the taxpayer did not explain the difference, IRS will contact the taxpayer.

Example 6

On November 13, 2002, Mary Lou bought 500 shares of XEN, Inc. stock for \$20 a share (\$10,000 total), plus a \$50 commission. On February 26, 2003, she sold the stock for \$8,090 and paid selling expenses of \$40. The Form 1099-B from her broker reported a sales price of \$8,090 (gross proceeds). Part I of Mary Lou's completed Schedule D appears in Exhibit 3.

Mary Lou has a short-term capital loss. Notice that Mary Lou shows the loss in column (f) of line 1 with no entry in column (g) because the transaction was completed before May 6, 2003. She completes Part I by entering the net short-term loss on line 7. This example shows that:

- Her broker reported gross proceeds on Form 1099-B. The amount shown in column (d) is \$8,090 (because selling expenses have not been subtracted), and
- She works those expenses into the computation as an adjustment to basis, column (e)—and the result in column (f) reflects her true gain or loss.

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less						
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1 500 sh. XEN	11/13/02	2/26/03	8,090.00	10,090.00	(2,000.00)	
2 Enter your short-term totals, if any, from Schedule D-1, line 2	2					
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)	3		8,090.00			
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 2002 Capital Loss Carryover Worksheet	6				()	
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero	7a				()	
b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)	7b				(2,000.00)	

Example 7

Exhibit 4 shows the three long-term transactions that Tess is reporting on Schedule D, Part II, for 2003. On August 21, 1999, she bought 200 shares of XYZ Company for \$1,500. On October 1, 2000, she bought 500 shares of TUV, Inc., for \$8,000, and on November 18, 2000, she bought 2,000 shares of QRS, Inc., for \$5,000. Each amount includes the commission.

On January 10, 2003, Tess sold the stock in XYZ and TUV. The Form 1099-B from her broker reported gross proceeds of \$1,875 for the XYZ stock, and \$6,000 for TUV. Tess paid commissions of \$35 for selling the XYZ shares, and \$40 for selling TUV. On May 27, 2003, Tess sold the QRS stock for \$10,000. She paid a \$50 commission. Her broker reported net proceeds of \$9,950 on Form 1099-B.

This example shows how to:

- Report basis when Form 1099-B shows gross proceeds (XYZ and TUV—basis includes commissions on the sale, as well as prior adjusted basis), in contrast to when it shows net proceeds (QRS—basis does not include commissions on the sale, but only the prior adjusted basis).
- Net gains and losses in column (f).

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8							
200 sh. XYZ	8/21/99	1/10/03	1,875 00	1,535 00	340 00		
500 sh. TUV	10/1/00	1/10/03	6,000 00	8,040 00	(2,040 00)		
2,000 sh. QRS	11/18/00	5/27/03	9,950 00	5,000 00	4,950 00	4,950 00	
9 Enter your long-term totals, if any, from Schedule D-1, line 9							
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)			17,825 00				
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							
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1							
13 Capital gain distributions. See page D-1 of the instructions							
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet					()		
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-						4,950 00	
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.					3,250 00		

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, **do not** include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

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Cat. No. 11338H

Schedule D (Form 1040) 2003

Exercise 2

For each of the following situations, figure the gain or loss on the sale of stock and indicate whether the gain or loss will be long term or short term.

A. On March 15, 2002, Bill bought 1,000 shares of stock for \$15,000, including commission. On March 15, 2003, he sold 600 shares of the stock for \$7,800, net proceeds on Form 1099-B.

1. Will Bill report a gain or a loss? _____
2. How much is the gain or loss? _____
3. Is the holding period long term or short term? _____

B. On January 7, 2001, Margo bought stock for \$1,500, plus a \$25 commission. On July 15, 2003, she sold the stock for \$2,000 and paid a \$25 commission. Her Form 1099-B shows the gross proceeds of \$2,000 as the sales price.

1. Will Margo report a gain or a loss? _____
2. How much is the gain or loss? _____
3. Is the holding period long term or short term? _____

Reporting Capital Gain Distributions From Form 1099-DIV on Schedule D

If the taxpayer received Form 1099-DIV, *Dividends and Distributions*, see whether an amount is shown in box 2a and box 2c.

- If capital gain distributions from Form 1099-DIV are the only capital gains or losses the taxpayer had for the year, the taxpayer may be able to report them directly on Form 1040A or Form 1040, as explained in Lesson 2, *Income*.
- If the taxpayer also sold stock reported on Form 1099-B, report the total capital gain distributions from Form 1099-DIV on line 13, column (f), of Schedule D. For transactions completed after May 5, 2003, include the gain or loss in Column G also.

Example 8

Alec received a Form 1099-DIV. Box 2a which shows he received a total capital gain distribution of \$170. Alec also received a Form 1099-B that shows a net sales price of \$1,200 on the sale of 600 shares of ABC Group, Inc. He bought the stock on February 19, 2000, and sold it on August 25, 2003. His basis in ABC, including commission, is \$1,455. Alec's Form 1099-DIV, and Part II of his Schedule D, are shown in Exhibits 5 and 6. In this example, the capital gain distribution must be shown on Schedule D because Alec also sold stock in 2003 that must be reported on Schedule D.

Exhibit 6

Alec's Form 1099-DIV

9191 <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0110		2003 Form 1099-DIV	Dividends and Distributions
PAYER'S name, street address, city, state, ZIP code, and telephone no. MIG INC. 4321 Main Street Anytown, VA 00012		1a Total ordinary dividends \$	1b Qualified dividends \$		
PAYER'S Federal identification number 00-0000123		RECIPIENT'S identification number 000-00-0128		2a Total capital gain distr. \$ 170.00	2b Post-May 5 capital gain distr. \$
PAYER'S name Alec Green		2c Qualified 5-year gain \$	2d Unrecap. Sec. 1250 gain \$	Copy A For Internal Revenue Service Center File with Form 1096. For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G.	
Street address (including apt. no.) 1234 A Street		2e Section 1202 gain \$	2f Collectibles (28%) gain \$		
City, state, and ZIP code Anytown, VA 00013		3 Nontaxable distributions \$	4 Federal income tax withheld \$	5 Investment expenses \$	
Account number (optional)		6 Foreign tax paid \$	7 Foreign country or U.S. possession		
2nd TIN not. <input type="checkbox"/>		8 Cash liquidation distributions \$	9 Noncash liquidation distributions \$		
Form 1099-DIV		Cat. No. 14415N		Department of the Treasury - Internal Revenue Service	
Do Not Cut or Separate Forms on This Page			Do Not Cut or Separate Forms on This Page		

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year									
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)		(e) Cost or other basis (see page D-5 of the instructions)		(f) Gain or (loss) for the entire year Subtract (e) from (d)		(g) Post-May 5 gain or (loss)* (see below)
8 600 sh. ABC	2/19/00	8/25/03	1,200	00	1,455	00	(255)	00	(255.00)
9	Enter your long-term totals, if any, from Schedule D-1, line 9		9						
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)		10	1,200	00				
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 page D-1 of the instructions		13			170	00		
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet		14			()			
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-		15						
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.		16			(85)	00		

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

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After Completing Parts I and II of Schedule D

Double-check your entries on Schedule D up to this point.

- Check that the sales price amount from each Form 1099-B agrees with the amount entered in column (d) of either line 1 or line 8.
- Check that all entries in column (d), lines 1 and 2, add up to the amount on line 3.
- Check that all entries in column (d), lines 8 and 9, add up to the amount on line 10.
- Check that line 3, added to line 10, agrees with the total sales price reported on all of the taxpayer's Forms 1099-B.
- Check that the amount on line 13, column (f), is the same as the total from all the taxpayer's Forms 1099-DIV, box 2a.
- Check Column G of both line 1 or 8 to detail sales, exchanges or conversions completed after May 5, 2003 have been recorded.

Exercise 3

This exercise will give you practice with Schedule D. Use the following information to complete Parts I and II of Jane's Schedule D.

Jane sold five stocks during 2003. Her broker reported net proceeds as sales price.

Stock	Purchase Date	Date Sold	Net Sales Price	Adjusted Basis
500 sh LSR	1/21/02	1/4/03	\$ 4,000	\$9,000
250 sh BGI	3/11/02	2/12/03	10,000	2,500
75 sh ABC	1/22/01	1/29/03	2,000	7,500
400 sh XYZ	12/3/99	3/6/03	15,000	10,000
100 sh DEF	4/2/99	10/16/03	1,200	2,000

Jane also owns shares in a mutual fund that sent her a Form 1099-DIV. It reported \$1,200 paid to her in total capital gain distributions for the year.

Exhibit 8

Complete Parts I and II of Jane's Schedule D.

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
1							
2 Enter your short-term totals, if any, from Schedule D-1, line 2							
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)							
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824							
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1							
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 2002 Capital Loss Carryover Worksheet					()		
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero						()	
b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)							
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8							
9 Enter your long-term totals, if any, from Schedule D-1, line 9							
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)							
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							
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1							
13 Capital gain distributions. See page D-1 of the instructions							
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet					()		
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-							
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f)							

Next: Go to Part III on the back.

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, **do not** include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

Part III: Summary of Parts I and II

Combine the amounts from line 7b (net short-term capital gain or loss) and line 16 (net long-term capital gain or loss). Enter the result on line 17a in Part III. This combined number may be a gain or a loss.

- If the line 17a amount is a gain, also enter it on line 13a of Form 1040, and go to line 17b.
- If the line 17a amount is a loss, complete line 18 of Schedule D. Line 18 ensures that no more than the maximum allowable capital loss is deducted on Form 1040. The line 18 amount is limited to the smaller of:
 - The loss from line 17a or
 - \$3,000 (\$1,500 for a married taxpayer filing separately).

Also enter this amount on line 13a of Form 1040. Because it is a loss, be sure to put parentheses around the number when you enter it on Form 1040.

Part IV: Tax Computation Using the Maximum Capital Gains Rates

The law limits tax rates on net long-term capital gains. To obtain the lowest rate, taxpayers with long-term capital gains must go to Part IV of Schedule D to figure their tax. To determine whether you need Part IV, complete Form 1040 through line 40, Taxable Income. Then go to Part IV of Schedule D if:

- Both lines 16 and 17a of Schedule D are gains, and
- Form 1040, line 40, is more than zero.

Example 9

Edmund's tax return shows:

Filing status: Form 1040, line 1 box checked, single.

Amount from: Form 1040, line 40: \$65,001

 Schedule D, line 7b: (5,000)

 Schedule D, line 16: 16,000

 Schedule D, line 17a: 11,000

 (Transferred to Form 1040, line 13a.)

There is capital gain on Schedule D, lines 16 and 17a, and Form 1040, line 40, is more than zero.

Exhibits 9 and 10 show Edmund's Schedule D, Parts III and IV, and his Form 1040, lines 13a and 41. His tax is \$12,516. Without Schedule D, his tax from the Tax Table would be \$13,066. Using Schedule D saved Edmund \$1,100.

Part III Taxable Gain or Deductible Loss

17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below	17a	11,000	00
b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40 Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040.	17b		
18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions) Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040.	18	()

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19 Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6	19		
20 Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions	20		

If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.

21 Enter your taxable income from Form 1040, line 40	21	65,001	00
22 Enter the smaller of line 16 or line 17a, but not less than zero	22	11,000	00
23 Enter your qualified dividends from Form 1040, line 9b	23		
24 Add lines 22 and 23	24	11,000	00
25 Amount from line 4g of Form 4952 (investment interest expense)	25		
26 Subtract line 25 from line 24. If zero or less, enter -0-	26	11,000	00
27 Subtract line 26 from line 21. If zero or less, enter -0-	27	54,001	00
28 Enter the smaller of line 21 or: • \$56,800 if married filing jointly or qualifying widow(er); • \$28,400 if single or married filing separately; or • \$38,050 if head of household	28	28,400	00
If line 27 is more than line 28, skip lines 29–39 and go to line 40.			
29 Enter the amount from line 27	29		
30 Subtract line 29 from line 28. If zero or less, go to line 40	30		
31 Add lines 17b and 23*	31		
32 Enter the smaller of line 30 or line 31	32		
33 Multiply line 32 by 5% (.05)	33		
If lines 30 and 32 are the same, skip lines 34–39 and go to line 40.			
34 Subtract line 32 from line 30	34		
35 Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8	35		
36 Enter the smaller of line 34 or line 35	36		
37 Multiply line 36 by 8% (.08)	37		
38 Subtract line 36 from line 34	38		
39 Multiply line 38 by 10% (.10)	39		
If lines 26 and 30 are the same, skip lines 40–49 and go to line 50.			
40 Enter the smaller of line 21 or line 26	40	11,000	00
41 Enter the amount from line 30 (if line 30 is blank, enter -0-)	41		
42 Subtract line 41 from line 40	42	11,000	00
43 Add lines 17b and 23*	43		
44 Enter the amount from line 32 (if line 32 is blank, enter -0-)	44		
45 Subtract line 44 from line 43	45		
46 Enter the smaller of line 42 or line 45	46		
47 Multiply line 46 by 15% (.15)	47		
48 Subtract line 46 from line 42	48	11,000	00
49 Multiply line 48 by 20% (.20)	49	2,200	00
50 Figure the tax on the amount on line 27 . Use the Tax Table or Tax Rate Schedules, whichever applies	50	10,316	00
51 Add lines 33, 37, 39, 47, 49, and 50	51	12,516	00
52 Figure the tax on the amount on line 21 . Use the Tax Table or Tax Rate Schedules, whichever applies	52	13,066	00
53 Tax on all taxable income. Enter the smaller of line 51 or line 52 here and on Form 1040, line 41	53	12,516	00

*If line 25 is more than zero, see Lines 31 and 43 on page D-9 for the amount to enter. Printed on recycled paper Schedule D (Form 1040) 2003

Exhibit 10

Edmund's Form 1040, Lines 13a and 41.

12	Business income or (loss). Attach Schedule C or C-EZ	12		
13a	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13a	11,000	00
b	If box on 13a is checked, enter post-May 5 capital gain distributions 13b			
40	Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-	40		
41	Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972	41	12,516	00

Exercise 4

Melvin sold the following stocks during 2003. His broker reported net sales proceeds on Form 1099-B.

Stock	Purchase Date	Date Sold	Net Sales Price	Adjusted Basis
50 sh ABC	3/15/02	7/26/03	\$ 4,000	\$5,000
200 sh MLG	5/10/02	6/7/03	1,200	1,000
150 sh XYZ	4/17/02	3/8/03	5,500	6,000
300 sh MLS	1/13/98	6/19/03	6,000	3,000

Melvin also had shares in a mutual fund. The fund sent him a Form 1099-DIV that showed he received \$1,500 in total capital gain distributions. His taxable income (line 40, Form 1040) was \$67,001. His filing status is single.

Use the information given to complete Melvin's Schedule D.
 What amounts would be shown on his:

(A) 1. Form 1040, line 13? _____
 2. Form 1040, line 41? _____

SCHEDULE D (Form 1040) Department of the Treasury Internal Revenue Service	Capital Gains and Losses ▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040). ▶ Use Schedule D-1 to list additional transactions for lines 1 and 8.	OMB No. 1545-0074 <div style="font-size: 2em; font-weight: bold;">2003</div> Attachment Sequence No. 12
Name(s) shown on Form 1040		Your social security number xxx xx xxxx

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1						
2	Enter your short-term totals, if any, from Schedule D-1, line 2			2		
3	Total short-term sales price amounts. Add lines 1 and 2 in column (d)			3		
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 2002 Capital Loss Carryover Worksheet				6	()
7a	Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero				7a	()
7b	Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)				7b	

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
8						
9	Enter your long-term totals, if any, from Schedule D-1, line 9			9		
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)			10		
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 page D-1 of the instructions				13	
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet				14	()
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-				15	
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f)				16	

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

Part III Taxable Gain or Deductible Loss

17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below

b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40 .

- Next:** • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete **Part IV** below (unless Form 1040, line 40, is zero).
 • Otherwise, skip the rest of Schedule D and complete Form 1040.

18 If line 17a is a loss, enter here and on Form 1040, line 13a, the **smaller** of **(a)** that loss or **(b)** (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)

- Next:** • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete **Part IV** below (but skip lines 19 and 20).
 • Otherwise, skip **Part IV** below and complete the rest of Form 1040.

17a		
17b		
18	()

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19 Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6

20 Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions

19		
20		

If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.

21 Enter your taxable income from Form 1040, line 40

22 Enter the **smaller** of line 16 or line 17a, but not less than zero

23 Enter your qualified dividends from Form 1040, line 9b

24 Add lines 22 and 23

25 Amount from line 4g of Form 4952 (investment interest expense)

26 Subtract line 25 from line 24. If zero or less, enter -0-

27 Subtract line 26 from line 21. If zero or less, enter -0-

28 Enter the **smaller** of line 21 or:

- \$56,800 if married filing jointly or qualifying widow(er);
- \$28,400 if single or married filing separately; or
- \$38,050 if head of household

If line 27 is more than line 28, skip lines 29–39 and go to line 40.

29 Enter the amount from line 27

30 Subtract line 29 from line 28. If zero or less, go to line 40

31 Add lines 17b and 23*

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

33 Multiply line 32 by 5% (.05)

If lines 30 and 32 are the same, skip lines 34–39 and go to line 40.

34 Subtract line 32 from line 30

35 Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8

36 Enter the **smaller** of line 34 or line 35

37 Multiply line 36 by 8% (.08)

38 Subtract line 36 from line 34

39 Multiply line 38 by 10% (.10)

If lines 26 and 30 are the same, skip lines 40–49 and go to line 50.

40 Enter the **smaller** of line 21 or line 26

41 Enter the amount from line 30 (if line 30 is blank, enter -0-)

42 Subtract line 41 from line 40

43 Add lines 17b and 23*

44 Enter the amount from line 32 (if line 32 is blank, enter -0-)

45 Subtract line 44 from line 43

46 Enter the **smaller** of line 42 or line 45

47 Multiply line 46 by 15% (.15)

48 Subtract line 46 from line 42

49 Multiply line 48 by 20% (.20)

50 Figure the tax on the amount on line 27. Use the Tax Table or Tax Rate Schedules, whichever applies

51 Add lines 33, 37, 39, 47, 49, and 50

52 Figure the tax on the amount on line 21. Use the Tax Table or Tax Rate Schedules, whichever applies

53 **Tax on all taxable income.** Enter the **smaller** of line 51 or line 52 here and on Form 1040, line 41

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*If line 25 is more than zero, see Lines 31 and 43 on page D-9 for the amount to enter. Printed on recycled paper **Schedule D (Form 1040) 2003**

Capital Loss Carryovers

Use the *Capital Loss Carryover Worksheet* in the Schedule D instructions to figure how much capital loss the taxpayer can carry from 2003 to 2004. As you learned earlier, a taxpayer cannot take net losses of more than \$3,000 (\$1,500 for married taxpayers filing separately) in figuring taxable income. The allowable loss for the year is also referred to as the deduction limit.

Unused losses are not gone forever. Rather, they are carried over to the next year. The carryover losses are combined with the gains and losses that actually occur in that next year. Unused losses are recycled this way, year after year, until they are all deducted. There is no limit on how many times a loss can be carried over during the taxpayer's life.

Unused losses keep their short-term or long-term classification when they are carried over. If the taxpayer has a short-term capital loss carryover from 2002, enter it on line 6, Part I, Schedule D. Enter it on line 14, Part II, if it is long-term.

NOTE: If a capital loss is limited and the remainder must be carried forward to 2004, remind the Taxpayer to bring a copy of the 2003 return for 2004 return preparation.

Example 10

Andrew sold two stocks in 2003, as summarized here.

Stock	Purchase Date	Date Sold	Net Sales Price	Adjusted Basis
200 sh FFF	5/8/02	1/6/03	\$ 4,000	\$ 3,025
50 sh WWW	11/6/00	3/12/03	8,700	11,000

Andrew's 2002 return showed the following capital loss carryovers to 2003: a \$4,200 short-term loss (line 8 of the 2002 *Capital Loss Carryover Worksheet*) and a \$240 long-term loss (line 13 of the 2002 worksheet). His 2003 Form 1040, line 40, shows \$55,825.

Andrew's Schedule D, Parts I through III, his 2003 Form 1040, line 13a, and his 2002 *Capital Loss Carryover Worksheet* appear below as Exhibits 13 through 16. This example shows how to:

- Report a capital loss carryover from 2002 and work it into the computation on Schedule D as if it had resulted from a 2003 sale. This example shows both a short-term loss (reported on Schedule D, Part I, line 6) and a long-term loss (reported on Schedule D, Part II, line 14).

TAX TIPS

★★★★★★★

It is easy to double check the carryover from 2003 to 2004. Take as much as possible of the \$3,000 (or \$1,500) deduction from short-term capital losses first. Then take any remaining amount of the \$3,000 (or \$1,500) from long-term capital losses. What is left is the carryover to 2004.

- Combine a short-term capital loss and a long-term capital loss and apply the deduction limit (\$3,000 for Andrew). Andrew reports the combined long-term and short-term loss on Schedule D, Part III, line 17. Line 18 applies Andrew's deduction limit, his allowable loss for the year.
- Show the allowable loss for the year (\$3,000 for Andrew) in the Income section of Form 1040.
- Use the *Capital Loss Carryover Worksheet* to apply the \$3,000 deduction limit against the short-term loss first and figure the capital loss carryover to 2004. In this case, the carryover is a short-term loss of \$225 (line 8 of the worksheet) and a long-term loss of \$2,540 (line 13 of the worksheet).

**SCHEDULE D
(Form 1040)**

Department of the Treasury
Internal Revenue Service

Capital Gains and Losses

▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040).
▶ Use Schedule D-1 to list additional transactions for lines 1 and 8.

OMB No. 1545-0074

2003

Attachment
Sequence No. **12**

Name(s) shown on Form 1040

Your social security number

XXX XX XXXX

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1 200 sh. FFF	5/8/02	1/6/03	4,000:00	3,025:00	975:00	
2 Enter your short-term totals, if any, from Schedule D-1, line 2			2			
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)			3 4,000:00			
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 2002 Capital Loss Carryover Worksheet					6 (4,200:00)	
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero					7a	()
b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)					7b (3,225:00)	

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
8 50 sh. WWW	11/6/00	3/12/03	8,700:00	11,000:00	(2,300:00)	
9 Enter your long-term totals, if any, from Schedule D-1, line 9			9			
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)			10 8,700:00			
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 page D-1 of the instructions					13	
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet					14 (240:00)	
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-					15	
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.					16 (2,540:00)	

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, **do not** include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

Schedule D (Form 1040) 2003		Page 2						
Part III Taxable Gain or Deductible Loss								
<p>17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below</p> <p>b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40</p> <p>Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero).</p> <p>• Otherwise, skip the rest of Schedule D and complete Form 1040.</p> <p>18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)</p> <p>Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20).</p> <p>• Otherwise, skip Part IV below and complete the rest of Form 1040.</p>	<table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="text-align: center;">17a</td> <td style="text-align: right;">(5,765.00)</td> </tr> <tr> <td style="text-align: center;">17b</td> <td></td> </tr> <tr> <td style="text-align: center;">18</td> <td style="text-align: right;">(3,000.00)</td> </tr> </table>	17a	(5,765.00)	17b		18	(3,000.00)	
17a	(5,765.00)							
17b								
18	(3,000.00)							

Exhibit 15

Andrew's Form 1040, line 13a

<p>13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/></p>	<p>13a</p>	<p>(3,000.00)</p>
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Exhibit 16

Andrew's Capital Loss Carryover Worksheet

Capital Loss Carryover Worksheet—Line 18

Use this worksheet to figure your capital loss carryovers from 2003 to 2004 if Schedule D, line 18, is a loss and (a) that loss is a smaller loss than the loss on Schedule D, line 17a, or (b) Form 1040, line 38, is a loss. Otherwise, you do not have any carryovers.

1. Enter the amount from Form 1040, line 38. If a loss, enclose the amount in parentheses	1. _____
2. Enter the loss from Schedule D, line 18, as a positive amount	2. _____
3. Combine lines 1 and 2. If zero or less, enter -0-	3. _____
4. Enter the smaller of line 2 or line 3	4. _____
If line 7b of Schedule D is a loss, go to line 5; otherwise, enter -0- on line 5 and go to line 9.	
5. Enter the loss from Schedule D, line 7b, as a positive amount	5. _____
6. Enter any gain from Schedule D, line 16	6. _____
7. Add lines 4 and 6	7. _____
8. Short-term capital loss carryover to 2004. Subtract line 7 from line 5. If zero or less, enter -0-	8. _____
If line 16 of Schedule D is a loss, go to line 9; otherwise, skip lines 9 through 13.	
9. Enter the loss from Schedule D, line 16, as a positive amount	9. _____
10. Enter any gain from Schedule D, line 7b	10. _____
11. Subtract line 5 from line 4. If zero or less, enter -0-	11. _____
12. Add lines 10 and 11	12. _____
13. Long-term capital loss carryover to 2004. Subtract line 12 from line 9. If zero or less, enter -0-	13. _____

Exercise 5

This exercise and the next one review the concepts covered in this lesson. They will measure your ability to apply what you have learned.

Matthew has a Form 1099-B from Broker One, who reported gross proceeds:

Stock	Date Sold	Sales Price
100 sh MNO	2/8/03	\$5,050
500 sh ZYX	8/7/03	5,250

Broker One reported sales commissions to Matthew separately. They were:

MNO: \$50 ZYX; \$200

Matthew also has a Form 1099-B from Broker Two, who reported net proceeds:

Stock	Date Sold	Sales Price
200 sh BCA	8/7/03	\$4,000
300 sh JKL	8/7/03	5,910

Matthew gave you the following information about the stocks he sold:

- He paid \$6,940, plus a \$60 commission, to buy the MNO stock on February 9, 2002.
- He bought the ZYX on March 11, 2000, for \$5,200, plus a \$100 commission.
- He paid \$3,900, plus a \$50 commission, to buy the BCA stock on January 29, 2003.
- He bought the JKL on June 26, 2001, for \$6,300, plus a \$30 commission.

Matthew's filing status is head of household. His Form 1040, line 40, shows \$55,282. When you look at Matthew's Form 1040 and Capital Loss Carryover Worksheet from 2002, you see that he has a \$450 short-term loss and a \$325 long-term loss that he can carry over to his 2003 return.

Use this information to complete Matthew's Schedule D, Parts I, II, and III, and his Form 1040, line 13a, for 2003. Also complete the *Capital Loss Carryover Worksheet* to figure how much capital loss he can carry over to 2004.

SCHEDULE D (Form 1040) Department of the Treasury Internal Revenue Service	Capital Gains and Losses ▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040). ▶ Use Schedule D-1 to list additional transactions for lines 1 and 8.	OMB No. 1545-0074 2003 Attachment Sequence No. 12				
Name(s) shown on Form 1040		Your social security number xxx xx xxxx				
Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less						
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1						
2 Enter your short-term totals, if any, from Schedule D-1, line 2						
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)						
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824						
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1						
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 2002 Capital Loss Carryover Worksheet						
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero						
b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)						
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year						
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
8						
9 Enter your long-term totals, if any, from Schedule D-1, line 9						
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)						
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						
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1						
13 Capital gain distributions. See page D-1 of the instructions						
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet						
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-						
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f)						
Next: Go to Part III on the back.						
*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).						
For Paperwork Reduction Act Notice, see Form 1040 instructions.			Cat. No. 11338H		Schedule D (Form 1040) 2003	

Exhibit 18

(B) Complete this form.

Schedule D, Part III

Schedule D (Form 1040) 2003		Page 2									
Part III Taxable Gain or Deductible Loss											
<p>17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below</p> <p>b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40 . Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040.</p> <p>18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions) Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040.</p>	<table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width: 20px; text-align: center;">17a</td> <td style="width: 40px;"></td> <td style="width: 40px;"></td> </tr> <tr> <td style="text-align: center;">17b</td> <td></td> <td></td> </tr> <tr> <td style="text-align: center;">18</td> <td style="text-align: center;">(</td> <td style="text-align: center;">)</td> </tr> </table>	17a			17b			18	()	
17a											
17b											
18	()									

Exhibit 19

(C) Complete this line on Matthew’s Form 1040.

Form 1040, line 13a

13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13a	
--	------------	--

Exhibit 20

(D) Complete this worksheet.

Capital Loss Carryover Worksheet

Capital Loss Carryover Worksheet—Line 18

Use this worksheet to figure your capital loss carryovers from 2003 to 2004 if Schedule D, line 18, is a loss and (a) that loss is a smaller loss than the loss on Schedule D, line 17a, or (b) Form 1040, line 38, is a loss. Otherwise, you do not have any carryovers.

1. Enter the amount from Form 1040, line 38. If a loss, enclose the amount in parentheses	1.	
2. Enter the loss from Schedule D, line 18, as a positive amount	2.	
3. Combine lines 1 and 2. If zero or less, enter -0-	3.	
4. Enter the smaller of line 2 or line 3	4.	
If line 7b of Schedule D is a loss, go to line 5; otherwise, enter -0- on line 5 and go to line 9.		
5. Enter the loss from Schedule D, line 7b, as a positive amount	5.	
6. Enter any gain from Schedule D, line 16	6.	
7. Add lines 4 and 6	7.	
8. Short-term capital loss carryover to 2004. Subtract line 7 from line 5. If zero or less, enter -0-	8.	
If line 16 of Schedule D is a loss, go to line 9; otherwise, skip lines 9 through 13.		
9. Enter the loss from Schedule D, line 16, as a positive amount	9.	
10. Enter any gain from Schedule D, line 7b	10.	
11. Subtract line 5 from line 4. If zero or less, enter -0-	11.	
12. Add lines 10 and 11	12.	
13. Long-term capital loss carryover to 2004. Subtract line 12 from line 9. If zero or less, enter -0-	13.	

Exercise 6

Katherine has two Forms 1099-B. They show:

From Broker No. 1 (gross proceeds reported):

Stock	Date Sold	Sales Price
100 sh LMN	4/20/03	\$3,000
50 sh PQR	4/17/03	2,600
500 OLE	6/17/03	7,800

Expenses for selling the stock through Broker No. 1 (reported to Katherine separately from Form 1099-B) were:

On the sale of: LMN stock: \$175 PQR stock: \$105 OLE: \$590

From Broker No. 2 (net proceeds reported):

Stock	Date Sold	Sales Price
75 sh ABC	1/24/03	\$2,500
125 sh XYZ	3/22/03	6,000

Katherine gave you the following information about these stocks:

- She bought 100 shares of LMN stock on March 6, 2000, for \$12.50 a share (\$1,250), plus a 10% broker's commission (\$125).
- She bought 200 shares of PQR stock on January 8, 2003, for \$14 a share (\$2,800), plus a 10% broker's commission (\$280).
- Katherine bought OLE stock on two dates. On November 27, 2000, she bought 800 shares for \$10 a share (\$8,000), plus 10% broker's commission (\$800). On March 6, 2002, she bought 600 more shares for \$18 a share (\$10,800), plus a 10% broker's commission (\$1,080). When Katherine sold 500 shares of OLE in 2002, she did not specify which block they came from.
- Katherine bought 100 shares of ABC on October 15, 1999, for \$72 a share (\$7,200), plus a 5% broker's commission (\$360). On May 8, 2000, the stock split two-for-one, so Katherine owned 200 shares after the split.
- She bought 125 shares of XYZ stock on October 26, 2002, for \$74 a share (\$9,250), plus a broker's commission of \$250.

Katherine also gave you a Form 1099-DIV from the Acme Mutual Fund. It showed \$1,050 in total capital gain distributions. From Katherine's tax return and worksheets for last year (2002), you found she has a \$150 long-term capital loss carryover from 2002 to 2003.

Complete Katherine's Schedule D, Parts I through IV, and her Form 1040, lines 13 and 42. She is single, and her taxable income shown on line 40 of her Form 1040 is \$61,221.

(A) Complete this form.

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less						
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1						
2	Enter your short-term totals, if any, from Schedule D-1, line 2		2			
3	Total short-term sales price amounts. Add lines 1 and 2 in column (d)		3			
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 2002 Capital Loss Carryover Worksheet			6	()	
7a	Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero			7a		()
7b	b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)			7b		
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year						
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
8						
9	Enter your long-term totals, if any, from Schedule D-1, line 9		9			
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)		10			
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 page D-1 of the instructions			13		
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet			14	()	
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-			15		
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.			16		

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, **do not** include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

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Part III Taxable Gain or Deductible Loss

17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below

17a		
17b		

b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40.
Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete **Part IV** below (unless Form 1040, line 40, is zero).
 • Otherwise, skip the rest of Schedule D and complete Form 1040.

18 If line 17a is a loss, enter here and on Form 1040, line 13a, the **smaller** of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)

18	()	
-----------	-----	--

Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete **Part IV** below (but skip lines 19 and 20).
 • Otherwise, skip **Part IV** below and complete the rest of Form 1040.

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19 Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6

19		
20		

20 Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions

If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.

21 Enter your taxable income from Form 1040, line 40

21		
-----------	--	--

22 Enter the **smaller** of line 16 or line 17a, but not less than zero

22		
-----------	--	--

23 Enter your qualified dividends from Form 1040, line 9b

23		
-----------	--	--

24 Add lines 22 and 23

24		
-----------	--	--

25 Amount from line 4g of Form 4952 (investment interest expense)

25		
-----------	--	--

26 Subtract line 25 from line 24. If zero or less, enter -0-

26		
-----------	--	--

27 Subtract line 26 from line 21. If zero or less, enter -0-

27		
-----------	--	--

28 Enter the **smaller** of line 21 or:

- \$56,800 if married filing jointly or qualifying widow(er);
- \$28,400 if single or married filing separately; or
- \$38,050 if head of household

28		
-----------	--	--

If line 27 is more than line 28, skip lines 29-39 and go to line 40.

29 Enter the amount from line 27

29		
-----------	--	--

30 Subtract line 29 from line 28. If zero or less, go to line 40

30		
-----------	--	--

31 Add lines 17b and 23*

31		
-----------	--	--

32		
-----------	--	--

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

33 Multiply line 32 by 5% (.05)

33		
-----------	--	--

If lines 30 and 32 are the same, skip lines 34-39 and go to line 40.

34 Subtract line 32 from line 30

34		
-----------	--	--

35 Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8

35		
-----------	--	--

36		
-----------	--	--

36 Enter the **smaller** of line 34 or line 35

37 Multiply line 36 by 8% (.08)

37		
-----------	--	--

38 Subtract line 36 from line 34

38		
-----------	--	--

39 Multiply line 38 by 10% (.10)

39		
-----------	--	--

If lines 26 and 30 are the same, skip lines 40-49 and go to line 50.

40 Enter the **smaller** of line 21 or line 26

40		
-----------	--	--

41 Enter the amount from line 30 (if line 30 is blank, enter -0-)

41		
-----------	--	--

42 Subtract line 41 from line 40

42		
-----------	--	--

43 Add lines 17b and 23*

43		
-----------	--	--

44		
-----------	--	--

44 Enter the amount from line 32 (if line 32 is blank, enter -0-)

45 Subtract line 44 from line 43

45		
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46		
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46 Enter the **smaller** of line 42 or line 45

47 Multiply line 46 by 15% (.15)

47		
-----------	--	--

48 Subtract line 46 from line 42

48		
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49 Multiply line 48 by 20% (.20)

49		
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50 Figure the tax on the amount on line 27. Use the Tax Table or Tax Rate Schedules, whichever applies

50		
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51 Add lines 33, 37, 39, 47, 49, and 50

51		
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52 Figure the tax on the amount on line 21. Use the Tax Table or Tax Rate Schedules, whichever applies

52		
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53 Tax on all taxable income. Enter the **smaller** of line 51 or line 52 here and on Form 1040, line 41

53		
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*If line 25 is more than zero, see Lines 31 and 43 on page D-9 for the amount to enter. Printed on recycled paper Schedule D (Form 1040) 2003

13a	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13a		
40	Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-	40		
41	Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972	41		

▶▶ **Summing Up This Lesson** ◀◀

To figure and properly report a taxpayer's gain or loss on a sale of stock, you need to know:

1. Sales price (reported to the taxpayer and to the IRS on Form 1099-B),
2. Adjusted basis, and
3. Holding period.

To determine gain or loss, subtract adjusted basis from sales price. The holding period determines whether the gain or loss is long-term or short-term. Long-term capital gains are generally taxed at lower rates than short-term capital gains. In 2003, capital gains will be subject to different tax rates depending on the date of the sale. Transactions completed after May 5, 2003 will be taxed at a different rate than transactions completed before May 6, 2003.

Use Schedule D, Parts I through IV, to figure capital gain or loss and the correct tax. Be sure the total sales price you report on line 3 plus line 10 of Schedule D is the same as the total sales price from all the taxpayer's Forms 1099-B, box 2.

Include capital gain distributions (reported to the taxpayer and to IRS on Form 1099-DIV) in the computation of long-term capital gains. Show them on Schedule D, Part II, line 13. Report capital gains distributions directly on Form 1040, line 13a (or on Form 1040A, line 10), if a Schedule D is not required to be completed for the gain or loss on a sale of stock.

A taxpayer can deduct up to \$3,000 (\$1,500 for a married taxpayer filing separately) in net capital loss for the year. The taxpayer can carry over any remaining loss to the next year. If the taxpayer has a carryover loss from 2002, include it on Schedule D, Part I, line 6, or Part II, line 14. The *Capital Loss Carryover Worksheet*, in the Schedule D instructions, can help you figure the carryover amount for 2004.

Report capital gain or loss on Form 1040, line 13a.

Exercise 1

A. 1. \$2,550. $[(\$5,000 + \$100) \div 1,000] \times 500 = \$2,550$

2. Long-term.

3. \$3,255. $\$3,300 - \$45 = \$3,255$

B. 1. \$3,550. $\$3,500 + \$50 = \$3,550$

2. Short-term.

C. 1. \$5,000. $[(\$9,965 + \$35) \div 200] \times 100 = \$5,000$

2. Long-term.

3. \$6,440. $\$6,470 - \$30 = \$6,440$

Exercise 2

A. 1. Loss.

2. \$1,200. $\$7,800 - [(\$15,000 \div 1,000) \times 600] = (\$1,200)$

3. Short-term.

B. 1. Gain.

2. \$450. $\$2,000 - (\$1,500 + \$25 + \$25) = \$450$

3. Long-term.

Exercise 3

Jane's Schedule D, Parts I and II

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
1	500 sh. LSR	1/12/02	1/4/03	4,000.00	9,000.00	(5,000.00)	
	250 sh. BGI	3/11/02	2/12/03	10,000.00	2,500.00	7,500.00	
2	Enter your short-term totals, if any, from Schedule D-1, line 2			2			
3	Total short-term sales price amounts. Add lines 1 and 2 in column (d)			3	14,000.00		
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 2002 Capital Loss Carryover Worksheet			6	()		
7a	Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero			7a		()	
7b	Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)			7b	2,500.00		
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8	75 sh. ABC	1/22/01	1/29/03	2,000.00	7,500.00	(5,500.00)	
	400 sh. XYZ	12/3/99	3/6/03	15,000.00	10,000.00	5,000.00	
	100 sh. DEF	4/2/99	1/16/03	1,200.00	2,000.00	(800.00)	
9	Enter your long-term totals, if any, from Schedule D-1, line 9			9			
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)			10	18,200.00		
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 page D-1 of the instructions			13	1,200.00		
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet			14	()		
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-			15			
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.			16	(100.00)		

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

Exercise 4

- (A) 1. Form 1040, line 13: \$3,200
 2. Form 1040, line 41: \$12,766
- (B) Melvin's Schedule D, Page 1

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
1 50 sh. ABC	3/15/03	7/26/03	4,000.00	5,000.00	(1,000.00)	(1,000.00)	
200 sh. MLG	5/10/03	6/7/03	1,200.00	1,000.00	200.00	200.00	
2 Enter your short-term totals, if any, from Schedule D-1, line 2			2				
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)			3	5,200.00			
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 2002 Capital Loss Carryover Worksheet					6	()	
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero					7a		()
b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)					7b	(800.00)	
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8 150 sh. XYZ	4/17/00	3/8/03	5,500.00	6,000.00	(500.00)	(500.00)	
300 sh. MLS	1/13/98	6/19/03	6,000.00	3,000.00	3,000.00	3,000.00	
9 Enter your long-term totals, if any, from Schedule D-1, line 9			9				
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)			10	11,500.00			
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 page D-1 of the instructions					13	1,500.00	
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet					14	()	
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-					15		3,000.00
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.					16	4,000.00	

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

(C) Melvin's Schedule D, Page 2

Schedule D (Form 1040) 2003

Page **2**

Part III Taxable Gain or Deductible Loss

17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below	17a	3,200	00
b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40. Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040.	17b		
18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)	18 ()
Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040.			

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19 Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6	19		
20 Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions	20		
If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.			
21 Enter your taxable income from Form 1040, line 40	21	67,001	00
22 Enter the smaller of line 16 or line 17a, but not less than zero	22	3,200	00
23 Enter your qualified dividends from Form 1040, line 9b	23		
24 Add lines 22 and 23	24	3,200	00
25 Amount from line 4g of Form 4952 (investment interest expense)	25	0	00
26 Subtract line 25 from line 24. If zero or less, enter -0-	26	3,200	00
27 Subtract line 26 from line 21. If zero or less, enter -0-	27	63,801	00
28 Enter the smaller of line 21 or: • \$56,800 if married filing jointly or qualifying widow(er); • \$28,400 if single or married filing separately; or • \$38,050 if head of household	28	28,400	00
If line 27 is more than line 28, skip lines 29-39 and go to line 40.			
29 Enter the amount from line 27	29	63,801	00
30 Subtract line 29 from line 28. If zero or less, go to line 40	30	0	00
31 Add lines 17b and 23*	31		
32 Enter the smaller of line 30 or line 31	32		
33 Multiply line 32 by 5% (.05)	33		
If lines 30 and 32 are the same, skip lines 34-39 and go to line 40.			
34 Subtract line 32 from line 30	34		
35 Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8	35		
36 Enter the smaller of line 34 or line 35	36		
37 Multiply line 36 by 8% (.08)	37		
38 Subtract line 36 from line 34	38		
39 Multiply line 38 by 10% (.10)	39		
If lines 26 and 30 are the same, skip lines 40-49 and go to line 50.			
40 Enter the smaller of line 21 or line 26	40	3,200	00
41 Enter the amount from line 30 (if line 30 is blank, enter -0-)	41	0	00
42 Subtract line 41 from line 40	42	3,200	00
43 Add lines 17b and 23*	43		
44 Enter the amount from line 32 (if line 32 is blank, enter -0-)	44		
45 Subtract line 44 from line 43	45		
46 Enter the smaller of line 42 or line 45	46		
47 Multiply line 46 by 15% (.15)	47		
48 Subtract line 46 from line 42	48	3,200	00
49 Multiply line 48 by 20% (.20)	49	640	00
50 Figure the tax on the amount on line 27 . Use the Tax Table or Tax Rate Schedules, whichever applies	50		
51 Add lines 33, 37, 39, 47, 49, and 50	51	12,766	00
52 Figure the tax on the amount on line 21 . Use the Tax Table or Tax Rate Schedules, whichever applies	52	13,406	00
53 Tax on all taxable income. Enter the smaller of line 51 or line 52 here and on Form 1040, line 41	53	12,766	00

*If line 25 is more than zero, see **Lines 31 and 43** on page D-9 for the amount to enter. Printed on recycled paper **Schedule D (Form 1040) 2003**

Exercise 5

(A) Matthew's Schedule D, Parts I and II

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
1	100 sh. MNO	2/9/02	2/8/03	5,050 00	7,050 00	(2000 00)	
	200 sh. BCA	1/29/03	8/7/03	4,000 00	3,950 00	50 00	
2	Enter your short-term totals, if any, from Schedule D-1, line 2			2			
3	Total short-term sales price amounts. Add lines 1 and 2 in column (d)			3	9,050 00		
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 2002 Capital Loss Carryover Worksheet			6	(450 00)		
7a	Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero			7a		()	
7b	Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)			7b	(2,400 00)		
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8	500 sh. ZYX	3/11/00	8/7/03	5,250 00	5,500 00	(250 00)	(250 00)
	300 sh. JKL	6/26/01	8/7/03	5,910 00	6,330 00	(420 00)	(420 00)
9	Enter your long-term totals, if any, from Schedule D-1, line 9			9			
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)			10	11,160 00		
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 page D-1 of the instructions			13			
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet			14	(325 00)		
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-			15		(660 00)	
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f)			16	(995 00)		
Next: Go to Part III on the back.							
*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).							
For Paperwork Reduction Act Notice, see Form 1040 instructions.				Cat. No. 11338H		Schedule D (Form 1040) 2003	

(B) Matthew's Schedule D, Part III

Schedule D (Form 1040) 2003		Page 2								
Part III Taxable Gain or Deductible Loss										
<p>17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below</p> <p>b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40</p> <p>Next:</p> <ul style="list-style-type: none"> • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040. <p>18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)</p> <p>Next:</p> <ul style="list-style-type: none"> • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040. 	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%;">17a</td> <td style="width: 70%; text-align: right;">(3,395</td> <td style="width: 20%; text-align: right;">00)</td> </tr> <tr> <td>17b</td> <td></td> <td></td> </tr> <tr> <td>18</td> <td style="text-align: right;">(3,000</td> <td style="text-align: right;">00)</td> </tr> </table>	17a	(3,395	00)	17b			18	(3,000	00)
17a	(3,395	00)								
17b										
18	(3,000	00)								

(C) Matthew's Form 1040, Line 13a

<p>13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/></p>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%;">13a</td> <td style="width: 70%; text-align: right;">(3,000</td> <td style="width: 20%; text-align: right;">00)</td> </tr> </table>	13a	(3,000	00)
13a	(3,000	00)		

(D) Matthew's Capital Loss Carryover Worksheet

Capital Loss Carryover Worksheet—Line 18

Use this worksheet to figure your capital loss carryovers from 2003 to 2004 if Schedule D, line 18, is a loss and (a) that loss is a smaller loss than the loss on Schedule D, line 17a, or (b) Form 1040, line 38, is a loss. Otherwise, you do not have any carryovers.

1. Enter the amount from Form 1040, line 38. If a loss, enclose the amount in parentheses	1. _____
2. Enter the loss from Schedule D, line 18, as a positive amount	2. _____
3. Combine lines 1 and 2. If zero or less, enter -0-	3. _____
4. Enter the smaller of line 2 or line 3	4. _____
If line 7b of Schedule D is a loss, go to line 5; otherwise, enter -0- on line 5 and go to line 9.	
5. Enter the loss from Schedule D, line 7b, as a positive amount	5. _____
6. Enter any gain from Schedule D, line 16	6. _____
7. Add lines 4 and 6	7. _____
8. Short-term capital loss carryover to 2004. Subtract line 7 from line 5. If zero or less, enter -0-	8. _____
If line 16 of Schedule D is a loss, go to line 9; otherwise, skip lines 9 through 13.	
9. Enter the loss from Schedule D, line 16, as a positive amount	9. _____
10. Enter any gain from Schedule D, line 7b	10. _____
11. Subtract line 5 from line 4. If zero or less, enter -0-	11. _____
12. Add lines 10 and 11	12. _____
13. Long-term capital loss carryover to 2004. Subtract line 12 from line 9. If zero or less, enter -0-	13. _____

Exercise 6

Basis Computations:

LMN:

100 shares bought at \$12.50	=	\$1,250
Commission on purchase	=	125
Commission on sale	=	<u>+ 175</u>
Adjusted basis, LMN sold	=	<u>\$1,550</u>

PQR:

200 shares bought at \$14	=	\$2,800
Commission on purchase	=	<u>+ 280</u>
Total paid for purchase	=	3,080
Divided by number of shares bought		<u>÷ 200</u>
Per share basis after purchase	=	15.40
Times number of shares sold		x 50
	=	770
Commission on sale	=	<u>+ 105</u>
Adjusted basis, PQR sold		<u>\$ 875</u>

OLE: Katherine did not specify which block of stock to sell; the stocks sold are assumed to be from the block purchased first.

800 shares bought at \$10	=	\$8,000
Commission on purchase	=	<u>+ 800</u>
Total paid for purchase	=	8,800
Divided by number of shares bought		<u>÷ 800</u>
Per share basis after purchase	=	11
Times number of shares sold		<u>x 500</u>
	=	5,500
Commission on sale	=	<u>+ 590</u>
Adjusted basis, OLE sold		<u>\$6,090</u>

ABC:

100 shares bought at \$72	=	\$7,200
Commission on purchase	=	<u>+ 360</u>
Total paid for purchase	=	7,560
Divided by number of shares Katherine held after the two-for-one split		<u>÷ 200</u>
Per share basis after the split	=	37.80
Times number of shares sold	=	<u>x 75</u>
Adjusted basis, ABC sold	=	<u><u>\$2,835</u></u>

XYZ:

125 shares bought at \$74	=	\$9,250
Commission on purchase	=	<u>+ 250</u>
Adjusted basis, XYZ sold	=	<u><u>\$9,500</u></u>

Exercise 6

(A) Katherine's Schedule D, Parts I and II

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
1	50 sh. PQR	1/8/03	4/17/03	2,600:00	875:00	1,725:00	
	125 sh. XYZ	10/26/02	3/22/03	6,000:00	9,500:00	(3,500:00)	
2	Enter your short-term totals, if any, from Schedule D-1, line 2		2				
3	Total short-term sales price amounts. Add lines 1 and 2 in column (d)		3	8,600:00			
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 2002 Capital Loss Carryover Worksheet		6		()		
7a	Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero		7a			()	
7b	Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)		7b		1,775:00		
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year							
(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)	
8	100 sh. LMN	3/6/00	4/20/03	3,000:00	1,550:00	1,450:00	
	500 sh. OLE	11/27/00	6/17/03	7,800:00	6,090:00	1,710:00	
	75 sh. ABC	10/15/99	1/24/03	2,500:00	2,835:00	(335:00)	
9	Enter your long-term totals, if any, from Schedule D-1, line 9		9				
10	Total long-term sales price amounts. Add lines 8 and 9 in column (d)		10	13,300:00			
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 page D-1 of the instructions		13		1,050:00		
14	Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet		14		(150:00)		
15	Combine lines 8 through 13 in column (g). If zero or less, enter -0-		15			(150:00)	
16	Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on the back.		16		3,725:00		

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11338H Schedule D (Form 1040) 2003

(B) Katherine's Schedule D, Parts III and IV

Schedule D (Form 1040) 2003

Page **2**

Part III Taxable Gain or Deductible Loss

17a	Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below	17a	1,950	00
b	Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40.	17b		
	Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040.			
18	If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)	18 ()
	Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040.			

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19	Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6	19		
20	Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions	20		
	If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.			
21	Enter your taxable income from Form 1040, line 40	21	61,221	00
22	Enter the smaller of line 16 or line 17a, but not less than zero	22	1,950	00
23	Enter your qualified dividends from Form 1040, line 9b	23		
24	Add lines 22 and 23	24	1,950	00
25	Amount from line 4g of Form 4952 (investment interest expense)	25	0	00
26	Subtract line 25 from line 24. If zero or less, enter -0-	26	1,950	00
27	Subtract line 26 from line 21. If zero or less, enter -0-	27	59,271	00
28	Enter the smaller of line 21 or: • \$56,800 if married filing jointly or qualifying widow(er); • \$28,400 if single or married filing separately; or • \$38,050 if head of household	28	28,400	00
	If line 27 is more than line 28, skip lines 29-39 and go to line 40.			
29	Enter the amount from line 27	29		
30	Subtract line 29 from line 28. If zero or less, go to line 40	30		
31	Add lines 17b and 23*	31		
32	Enter the smaller of line 30 or line 31	32		
33	Multiply line 32 by 5% (.05)	33		
	If lines 30 and 32 are the same, skip lines 34-39 and go to line 40.			
34	Subtract line 32 from line 30	34		
35	Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8	35		
36	Enter the smaller of line 34 or line 35	36		
37	Multiply line 36 by 8% (.08)	37		
38	Subtract line 36 from line 34	38		
39	Multiply line 38 by 10% (.10)	39		
	If lines 26 and 30 are the same, skip lines 40-49 and go to line 50.			
40	Enter the smaller of line 21 or line 26	40	1,950	00
41	Enter the amount from line 30 (if line 30 is blank, enter -0-)	41	0	00
42	Subtract line 41 from line 40	42	1,950	00
43	Add lines 17b and 23*	43		
44	Enter the amount from line 32 (if line 32 is blank, enter -0-)	44		
45	Subtract line 44 from line 43	45		
46	Enter the smaller of line 42 or line 45	46		
47	Multiply line 46 by 15% (.15)	47		
48	Subtract line 46 from line 42	48	1,950	00
49	Multiply line 48 by 20% (.20)	49	390	00
50	Figure the tax on the amount on line 27. Use the Tax Table or Tax Rate Schedules, whichever applies	50	11,629	00
51	Add lines 33, 37, 39, 47, 49, and 50	51	12,019	00
52	Figure the tax on the amount on line 21. Use the Tax Table or Tax Rate Schedules, whichever applies	52	12,116	00
53	Tax on all taxable income. Enter the smaller of line 51 or line 52 here and on Form 1040, line 41	53	12,019	00

*If line 25 is more than zero, see Lines 31 and 43 on page D-9 for the amount to enter. Printed on recycled paper Schedule D (Form 1040) 2003

(C) Katherine's Form 1040, lines 13 and 42

13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13a	1,950	00
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41 Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972	41	12,019	00
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STUDENT NOTES

INTRODUCTION AND OBJECTIVES

Introduction

This lesson generally discusses the tax rules that apply when a taxpayer sells his or her **main home** in 2003. The taxpayer's **main home** is the one in which he or she lives most of the time.

A taxpayer does not need to report the sale of his or her main home on his or her tax return if the gain on the sale is less than or equal to an **exclusion amount** (discussed later). Generally, if the taxpayer meets the **ownership and use tests** (discussed later), he or she can exclude any gain from income up to \$250,000 (\$500,000, if married filing jointly).

This lesson does not cover the sale of a main home used as rental property or partially for business.

Objective

At the end of this lesson you will be able to determine the amount of gain a taxpayer may exclude if a primary residence is sold.

MAIN HOME

Only the gain from the sale of the taxpayer's main home is eligible for the rules discussed in this lesson. If a home that is not the taxpayer's main home is sold during the year, the gain generally will have to be reported as income. Any gain that must be reported as income is taxable gain and is reported on Schedule D (Form 1040), *Capital Gains and Losses*. Therefore, a clear understanding of what is, and what is not, an individual's main home is very important.

A **main home** is where the taxpayer lives most of the time. The home does not necessarily have to be a house. A houseboat, a mobile home, a cooperative apartment, or a condominium (house or apartment) may also qualify as a main home. Taxpayers cannot choose which home to designate as their main home. Facts and circumstances determine which home is the main home.

POTENTIAL PITFALLS



A taxpayer's main home is not necessarily a home that is owned by the taxpayer. A rental home may be a main home..

If a taxpayer has more than one home, it is necessary to determine which home he or she lives in most of the time. In many, if not most cases, the taxpayer owns a single home in which he or she lives all the time.

It may seem easy to evaluate this situation, since it is not necessary to determine which home is the main home. However, you must be sure that the owner of a single home also meets the requirement of living in the home most of the time. If not, it cannot be considered the main home.

Never assume that the house sold during the year was the taxpayer's main home, even if the house was the only one owned by the taxpayer. Be sure to check that the house was, in fact, the individual's main home.

Example 1

Lucille owns a home in a Colorado ski area (the ski home). She stays at the ski home most weekends and spends the entire months of December, January, and February there. When she is not at the ski home, she lives in a four-room apartment that she rents in Denver. For over half the year, she lives in Denver. Lucille's main home is her rental apartment in Denver, because she lives there most of the time. This is so even though she does not own the apartment in Denver.

POTENTIAL PITFALLS



If there is a loss on the sale of a taxpayer's main home, the taxpayer cannot deduct it on his or her tax return.

GAIN ON SALE OF MAIN HOME

To figure the gain (or loss) on the sale of the taxpayer's main home, you must know the **selling price**, the **amount realized**, and the **adjusted basis**.

Selling price

The selling price is the total amount the taxpayer (seller) received for his or her main home. It includes money, all notes, mortgages, or other debts taken over by the buyer as part of the sale, and the fair market value of any other property or services that the seller received.

Form 1099-S

If the taxpayer received Form 1099-S, *Proceeds From Real Estate Transactions*, box 1 shows the date of sale (closing) and box 2 shows the **gross proceeds** received from the sale of his or her main home. (Exhibit 1 shows a blank Form 1099-S.) If the taxpayer can exclude the entire gain from a sale in 2003, the person responsible for closing the sale (for example, a real estate broker or settlement agent) generally will not have to report it on Form 1099-S.

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0997		2003 Proceeds From Real Estate Transactions Form 1099-S
FILER'S name, street address, city, state, ZIP code, and telephone no.		1 Date of closing	2 Gross proceeds	
FILER'S Federal identification number	TRANSFEROR'S identification number	3 Address or legal description		Copy B For Transferor This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this item is required to be reported and the IRS determines that it has not been reported.
TRANSFEROR'S name		4 Transferor received or will receive property or services as part of the consideration (if checked) <input type="checkbox"/>		
Street address (including apt. no.)		5 Buyer's part of real estate tax		
City, state, and ZIP code		\$		
Account number (optional)				
Form 1099-S		(keep for your records)		Department of the Treasury - Internal Revenue Service

Amount realized

The amount realized is the selling price minus **selling expenses**.

Selling expenses

Selling expenses include commissions, advertising fees, legal fees, and loan charges paid by the seller, such as points (points were discussed in lesson 4).

Adjusted basis

While the taxpayer owned his or her main home, he or she may have made adjustments (increases or decreases) to the **basis**. This adjusted basis is used to figure gain or loss on the sale of the taxpayer's main home. For information on how to figure the home's adjusted basis, see *Basis* in Publication 523.

Amount of gain (or loss)

When you know the amount realized and the home's adjusted basis, you can figure the taxpayer's **gain or loss**. If the amount realized is more than the adjusted basis, the difference is a gain and the taxpayer may be able to exclude all or part of it. If the amount realized is less than the adjusted basis, the difference is a loss. ***A loss on the sale of the taxpayer's main home cannot be deducted.***

POTENTIAL PITFALLS



A taxpayer cannot exclude the part of any depreciation allowed or allowable for the business use of his or her home.

Refer a taxpayer who used his or her main home for business to a paid professional tax preparer.

AMOUNT OF EXCLUSION

A single homeowner can generally exclude up to \$250,000 of gain from the sale of a main home. A married couple can exclude up to \$500,000 if they meet all of the following conditions.

1. They filed a joint return.
2. Either spouse or both meet the ownership test.
3. Both individuals meet the use test.
4. Neither individual excluded gain in the 2 years before the current sale of the home (not counting any sales before May 7, 1997).

For married individuals filing jointly who do not qualify for the \$500,000 exclusion of gain on the sale of a home because they do not satisfy the two-year ownership test, two-year use test, and the prohibition on any other sale or exchange of a residence within the last two years, the limit on the amount of excludable gain should be calculated separately for each spouse. In that case, the maximum exclusion for the couple is equal to the sum of the exclusions to which the spouses would otherwise be entitled if they had not been married.

OWNERSHIP AND USE TESTS

The **exclusion** is allowed each time a taxpayer sells or exchanges his or her main home, but generally no more than once every 2 years. To be eligible, the property must have been:

1. Owned by the taxpayer for a combined period of at least 2 years out of a 5-year period ending on the date of sale (the ownership test).
2. Lived in as the taxpayer's main home for at least 2 years of that 5-year period (the use test).

Period of ownership and use

The required 2 years of ownership and use do not have to be continuous. The taxpayer meets the tests if the taxpayer can show that he or she owned and lived in the property as his or her main home for either 24 full months or 730 days during the 5-year period. Short temporary absences, even if the property is rented during those absences, are counted as periods of use.

Ownership and use tests can be met during different 2-year periods. However, a taxpayer must meet both tests during the 5-year period ending on the date of the sale.

Example 2

In 1995, Helen Jones lived in a rented apartment. The apartment building was later changed to a condominium, and she bought her apartment on December 1, 2000. In 2001, Helen became ill and on April 14 of that year she moved in to her daughter's home. On July 10, 2003, while still living in her daughter's home, she sold her apartment.

Helen can exclude all the gain on the sale of her apartment because she met the ownership and use tests. Her 5-year period is from July 11, 1998, to July 10, 2003, the date she sold the apartment. She owned her apartment from December 1, 2000, to July 10, 2003 (over 2 years). She lived in the apartment from July 11, 1998 (the beginning of the 5-year period), to April 14, 2001 (over 2 years).

Reduced Exclusion

If the property was owned and used as a main home for less than 2 years, a taxpayer may be able to claim a reduced exclusion. If this situation applies to a taxpayer, use the worksheet in Publication 523 to figure how to claim the reduced exclusion.

Example 3

Amanda, who is single, bought her first home in August 2001. In December 2002, the company she worked for notified her that she would be transferred to another town by the end of 2003. She continued to live in the home until June 2003, when she sold it at a gain and moved to the new town. Amanda owned and lived in the home less than 2 years, so she does not meet the ownership and use tests. However, she qualifies to exclude the gain because she sold the home due to a change in place of employment.

Exercise 1

John is single and sold his home in July 2003, for \$300,000. The amount he realized from the sale was \$297,500. His adjusted basis in the home was \$255,500. Assuming he meets the ownership and use tests,

- a. What is the amount of the gain?
- b. What is his exclusion amount?

Exercise 2

Tim owns two homes. One residence is located in St. Louis where he works and the other is located in a resort area approximately 100 miles away. Tim lives in his St. Louis home during the week (Monday through Friday) and travels to his weekend home for Saturday and Sunday. His office allows him to work from home so approximately 5 months of the year he works from his weekend home. Which home is his main home?

TAXWISE HINTS

If a gain on the sale of a main home must be reported on the taxpayer's Form 1040. Link to a Schedule D, enter the description of property, and complete the remaining entries annotated in red. The software will calculate the gain and carry the calculation to the Form 1040.

▶▶ SUMMING UP THIS LESSON ◀◀

In this lesson you have learned about the simplified rules that apply to homeowners who sell or exchange their principal residence. For more information on the tax rules that apply on the sale of a main home, see Publication 523.

- Exercise 1a. \$42,000 (\$297,500 minus \$255,500)
1b. \$42,000
- Exercise 2. His main home is the St. Louis residence.

STUDENT NOTES

INTRODUCTION

In this lesson, you will learn about *Pensions and Annuities*.

Pensions and annuities provide cash payments, usually after a person has retired. The payments may be for life or for a fixed period of time. They may begin at retirement or at a specific age.

OBJECTIVES

After completing this lesson, you should be able to:

- Identify different types of Retirement Income
- Determine the taxable portion of the Retirement Income
- Report Retirement Income on the Tax Return
- Explain when a Minimum Distribution is required
- Determine when an adjustment to withholding should be made

DEFINITIONS

A **pension** is generally a series of definitely determinable payments made to an employee or survivor (the beneficiary of a deceased employee's pension) after the employee retires from work. Payments are made regularly and are for past services with an employer. A pension is fully or partially taxable depending on whether the employee contributed to the pension plan. The total amount of the pension will usually depend on how long the taxpayer worked for the company and how much the taxpayer earned over the years.

Employee contributions that are "after-tax" contributions are amounts that the employer usually deducts from wages and deposits them into the pension fund on behalf of the employee. Each year, the employee pays tax on the amount that he or she contributed that year. The employee's contributions are included in his or her Form W-2. Employee contributions are often referred to as the cost of the pension or as the investment in the annuity contract.

Employee contributions that are “before-tax” include amounts deposited to a 401(K) or 403(b) program. Each year, the employee pays income tax on the salary after the “before-tax” contributions have been deducted.

A **disability pension** is generally paid to a taxpayer who retires because of a disability before the minimum retirement age (set by the employer). The disability pension is considered regular pension income when the taxpayer reaches the minimum retirement age.

An **annuity** is a series of payments under a contract from an insurance company, a trust company, or an individual. Annuity payments are made at regular intervals over a period of more than one full year.

An **Individual Retirement Arrangement (IRA)** is a personal savings plan that provides tax advantages for setting money aside for retirement.

Social Security Benefits are payments made under Title II of the Social Security Act. They include old-age, survivors, disability insurance, and some workers’ compensation benefits. Social security benefits are reported to the taxpayer on Form SSA-1099, *Social Security Benefit Statement*.

Railroad Retirement Benefits (RRB) are based on the number of months that the taxpayer was working in a job that was covered by the Railroad Retirement Act. The RRA has two components. Tier 1 is the equivalent of Social Security Benefits and Tier 2 is like an employer’s pension plan.

There are several other types of pension plans, including 403(b), Keogh, SEP and SIMPLE. Payments from any of these types of plans should be reported to the taxpayer on Form 1099R. You will use this form to prepare the tax return. It is not necessary for you to understand all of the contribution rules associated with the many types of pension plans.

TAKING A LOOK AT THE FORMS

Retirement income may be reported on Form 1099R, Form SSA-1099, Form RRB-1099 or Form RRB-1099-R. Disability income may be reported on Form W-2 or Form 1099R. It is very important to enter all of the required information from these forms when using tax preparation software. This allows the software to do its job and help you with the calculations.

Form 1099-R

The **Form 1099-R** (as seen in Exhibit 1) is used by payers to report distributions from Pensions, Annuities, Retirement or Profit Sharing plans, IRAs, Insurance Contracts etc. While it is important to review all of the boxes on the form, you will be most concerned about the entries in Boxes 1, 2a, 2b, 4, 5, 7 and the little box that indicates whether this is an IRA/SEP/SIMPLE payment.

Exhibit 1

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0119		2003 Form 1099-R	Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution \$	2b Taxable amount not determined <input type="checkbox"/>		
PAYER'S Federal identification number		2a Taxable amount \$			
RECIPIENT'S identification number		3 Capital gain (included in box 2a) \$	4 Federal income tax withheld \$		Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return.
RECIPIENT'S name		5 Employee contributions or insurance premiums \$	6 Net unrealized appreciation in employer's securities \$		
Street address (including apt. no.)		7 Distribution code(s)	IRA/SEP/SIMPLE <input type="checkbox"/>	8 Other \$ %	
City, state, and ZIP code		9a Your percentage of total distribution %	9b Total employee contributions \$		This information is being furnished to the Internal Revenue Service.
Account number (optional)		10 State tax withheld \$	11 State/Payer's state no.	12 State distribution \$	
		13 Local tax withheld \$	14 Name of locality	15 Local distribution \$	

Form **1099-R**

Department of the Treasury - Internal Revenue Service

Some 1099-R forms may not look like the one above. Some payer's receive permission to customize the form. In all cases, the box numbers will remain the same.

Exhibit 2 is the instructions for the recipient of the Form 1099-R. While these instructions can be found on the back of copies B and C of the Form 1099-R, the print is small and may be difficult to read. Therefore, we are duplicating the information here in a larger print.

Instructions for Recipient

Generally, distributions from pensions, annuities, profit-sharing and retirement plans (including section 457 state and local government plans), IRAs, insurance contracts, etc., are reported to recipients on Form 1099-R.

Qualified plans. If your annuity starting date is after 1997, you must use the simplified method to figure your taxable amount if your payer did not show the taxable amount in box 2a. See **Pub. 575**, Pension and Annuity Income.

IRAs. For distributions from a traditional individual retirement arrangement (IRA), simplified employee pension (SEP), or savings incentive match plan for employees (SIMPLE), generally the payer is not required to compute the taxable amount. Therefore, the amounts in boxes 1 and 2a will be the same most of the time. See the Form 1040 or 1040A instructions to determine the taxable amount. If you are at least age 70½, you must take minimum distributions from your IRA (other than a Roth IRA). If you do not, you may be subject to a 50% excise tax on the amount that should have been distributed. See **Pub. 590**, Individual Retirement Arrangements (IRAs), and **Pub. 560**, Retirement Plans for Small Business (SEP, SIMPLE, and Qualified Plans), for more information on IRAs.

Roth IRAs. For distributions from a Roth IRA, generally the payer is not required to compute the taxable amount. You must compute any taxable amount on **Form 8606**, Nondeductible IRAs. An amount shown in box 2a may be taxable earnings on an excess contribution.

Loans treated as distributions. If you borrow money from a qualified plan, tax-sheltered annuity, or government plan, you may have to treat the loan as a distribution and include all or part of the amount borrowed in your income. There are exceptions to this rule. If your loan is taxable, Code L will be shown in box 7. See **Pub. 575**.

Box 1. Shows the total amount you received this year. The amount may have been a direct rollover, a transfer or conversion to a Roth IRA, a recharacterized IRA contribution; or you may have received it as periodic payments, as nonperiodic payments, or as a total distribution. Report the amount on Form 1040 or 1040A on the line for "IRA distributions" or "Pensions and annuities" (or the line for "Taxable amount"), and on Form 8606, whichever applies. However, if this is a lump-sum distribution, report it on **Form 4972**, Tax on

Lump-Sum Distribution. If you have not reached minimum retirement age, report your disability payments on the line for "Wages, salaries, tips, etc." Also report on that line corrective distributions of excess deferrals, excess contributions, or excess aggregate contributions.

If a life insurance, annuity, or endowment contract was transferred tax free to another trustee or contract issuer, an amount will be shown in this box and Code 6 will be shown in box 7. You need not report this on your tax return.

Box 2a. This part of the distribution is generally taxable. If there is no entry in this box, the payer may not have all the facts needed to figure the taxable amount. In that case, the first box in box 2b should be checked. You may want to get one of the following publications from the IRS to help you figure the taxable amount:

Pub. 560, **Pub. 571**, Tax-Sheltered Annuity Plans (403(b) Plans) for Employees of Public Schools and Certain Tax-Exempt Organizations, **Pub. 575**, **Pub. 590**, **Pub. 721**, Tax Guide to U.S. Civil Service Retirement Benefits, or **Pub. 939**, General Rule for Pensions and Annuities. For an IRA distribution, see **IRAs** and **Roth IRAs** above. For a direct rollover, zero should be shown, and you must enter zero (-0-) on the "Taxable amount" line of your tax return.

If this is a total distribution from a qualified plan (other than an IRA or tax-sheltered annuity) and you were born before January 2, 1936 (or you are the beneficiary of someone born before January 2, 1936), you may be eligible for the 10-year tax option. See the **Instructions for Form 4972** for more information.

Box 2b. If the first box is checked, the payer was unable to determine the taxable amount, and box 2a should be blank. However, if this is a traditional IRA, SEP, or SIMPLE distribution, then see **IRAs** above. If the second box is checked, the distribution was a total distribution that closed out your account.

Box 3. If you received a lump-sum distribution from a qualified plan and were born before January 2, 1936 (or you are the beneficiary of someone born before January 2, 1936), you may be able to elect to treat this amount as a capital gain on Form 4972 (not on Schedule D (Form 1040)). See the Instructions for Form 4972. For a charitable gift annuity, report as a long-term capital gain on Schedule D (Form 1040).

(Continued on the back of Copy C.)

Instructions for Recipient (Continued)

Box 4. This is the amount of Federal income tax withheld. **Include this on your income tax return as tax withheld, and if box 4 shows an amount (other than zero), attach Copy B to your return.** Generally, if you will receive payments next year that are not eligible rollover distributions, you can change your withholding or elect not to have income tax withheld by giving the payer **Form W-4P**, Withholding Certificate for Pension or Annuity Payments.

Box 5. Generally, this shows the employee's investment in the contract (after-tax contributions), if any, recovered tax free this year; the part of premiums paid on commercial annuities or insurance contracts recovered tax free; or the nontaxable part of a charitable gift annuity. This box does not show any IRA contributions.

Box 6. If you received a lump-sum distribution from a qualified plan that includes securities of the employer's company, the net unrealized appreciation (NUA) (any increase in value of such securities while in the trust) is taxed only when you sell the securities unless you choose to include it in your gross income this year. See Pub. 575 and the Instructions for Form 4972. If you did not receive a lump-sum distribution, the amount shown is the NUA attributable to employee contributions, which is not taxed until you sell the securities.

Box 7. The following codes identify the distribution you received. **1**—Early distribution, no known exception (in most cases, under age 59½). See **Form 5329**, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts. For a rollover to a traditional IRA of the entire taxable part of the distribution, do not file Form 5329. See the Form 1040/1040A instructions. **2**—Early distribution, exception applies (under age 59½)*. **3**—Disability*. **4**—Death*. **5**—Prohibited transaction. **6**—Section 1035 exchange (a tax-free exchange of life insurance, annuity, or endowment contracts). **7**—Normal distribution. **8**—Excess contributions plus earnings/excess deferrals (and/or earnings) taxable in 2003. **9**—Cost of current life insurance protection (premiums paid by a trustee or custodian for current insurance protection, taxable to you currently). **A**—May be eligible for 10-year tax option. See Form 4972. **D**—Excess contributions plus earnings/excess deferrals taxable in 2001. **E**—Excess annual additions under section 415 and certain excess amounts under section 403(b) plans. Report on Form 1040/1040A on the line for taxable pension or annuity income*. **F**—Charitable gift

annuity. **G**—Direct rollover to a qualified plan, a tax-sheltered annuity, a governmental 457(b) plan, or an IRA. May also include a transfer from a conduit IRA to a qualified plan*. **J**—Early distribution from a Roth IRA, no known exception (in most cases, under age 59½). Report on Forms 1040 and 8606 and see Form 5329. **L**—Loans treated as distributions. **N**—Recharacterized IRA contribution made for 2003 and recharacterized in 2003. Report on 2003 Form 1040/1040A and Form 8606, if applicable. **P**—Excess contributions plus earnings/excess deferrals taxable in 2002. **Q**—Roth IRA qualified distribution. You are age 59½ or over and meet the 5-year holding period for a Roth IRA. See the Form 1040/1040A instructions*. **R**—Recharacterized IRA contribution made for 2002 and recharacterized in 2003. Report on 2002 Form 1040/1040A and Form 8606, if applicable. **S**—Early distribution from a SIMPLE IRA in first 2 years, no known exception (under age 59½). May be subject to an additional 25% tax. See Form 5329. **T**—Roth IRA distribution, exception applies. You are either age 59½ or over or an exception (code 3 or 4) applies. See the Form 1040/1040A instructions.

If the IRA/SEP/SIMPLE box is checked, you have received a traditional IRA, SEP, or SIMPLE distribution.

Box 8. If you received an annuity contract as part of a distribution, the value of the contract is shown. It is not taxable when you receive it and should not be included in boxes 1 and 2a. When you receive periodic payments from the annuity contract, they are taxable at that time. If the distribution is made to more than one person, the percentage of the annuity contract distributed to you is also shown. You will need this information if you use the 10-year tax option (Form 4972).

Box 9a. If a total distribution was made to more than one person, the percentage you received is shown.

Box 9b. For a life annuity from a qualified plan or from a tax-sheltered annuity (with after-tax contributions), an amount may be shown for the employee's total investment in the contract. It is used to compute the taxable part of the distribution. See Pub. 575.

Boxes 10–15. If state or local income tax was withheld from the distribution, these boxes may be completed. Boxes 12 and 15 may show the part of the distribution subject to state and/or local tax.

*You are not required to file Form 5329.

Exercise 1

Alisha received a Form 1099R for 2003. In box 7 of the form there is a number 7. What does this mean? _____

Form SSA-1099

Every person who received Social Security Benefits will receive a Form SSA-1099. Sometimes the taxpayer does not bring this form with them because they didn't think that their Social Security is taxable. You need to know how much is in box 5 of the Form SSA-1099 to correctly calculate the taxpayers return. You may need to ask the taxpayer to go home and get the form. If the taxpayer did not receive the form or has misplaced it, they can get a printout of benefits from the local Social Security office. The amount in box 5 should be entered in the tax software program, even if the benefits aren't taxable (we will explain later how to determine if the benefits are taxable). This is a critical step to calculating the correct tax.

Exhibit 3

FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT		
2003 • PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME. • SEE THE REVERSE FOR MORE INFORMATION.		
Box 1. Name		Box 2. Beneficiary's Social Security Number
Box 3. Benefits Paid in 2001	Box 4. Benefits Repaid to SSA in 2001	Box 5. Net Benefits for 2001 (Box 3 minus Box 4)
DESCRIPTION OF AMOUNT IN BOX 3		DESCRIPTION OF AMOUNT IN BOX 4
		Box 6. Voluntary Federal Income Tax Withholding
		Box 7. Address
		Box 8. Claim Number (Use this number if you need to contact SSA.)
Form SSA-1099-SM (1-2003)		DO NOT RETURN THIS FORM TO SSA OR IRS

Exercise 2

Ralph comes to your site to get help with his taxes. You ask him if he received Social Security benefits. He tells you that he gets the benefits but that they have never been taxable so he didn't bring that information with him. Can you accurately complete his return without the information? _____

Forms RRB-1099 and Form RRB-1099R

Benefits paid under the Railroad Retirement Act fall into two categories. These categories are treated differently for income tax purposes.

The first category is the amount of tier 1 railroad retirement benefits that equals the social security benefit that a railroad employee or beneficiary would have been entitled to receive under the social security system. This part of the tier 1 benefit is called the "social security equivalent benefit" and is treated for tax purposes like social security benefits. It is shown on the **BLUE** part of the Form RRB-1099, *Payments by the Railroad Retirement Board*. (An example of this form is contained in Publication 915, *Social Security and Tier 1 Railroad Retirement Benefits*.) Use the amount from box 5 of Form RRB-1099 to complete the Social Security worksheet.

The second category contains the rest of the tier 1 benefits, called the "non-social security equivalent benefit," any tier 2 benefits, vested dual benefits, and supplemental annuity benefits. This category of benefits, shown on the **GREEN** part of the Form RRB-1099-R, *Annuities or Pensions by the Railroad Retirement Board*, is treated as an amount received from a qualified employer plan. Vested dual benefits and supplemental annuity benefits are fully taxable pensions. Publication 575, *Pension and Annuity Income* shows an example of this form and explains the items shown on the form.

Exercise 3

Jacob is a retired railroad switchyard operator. He receives Railroad Retirement Benefits. What Railroad Retirement forms does he need to bring with him when he gets his taxes done?

DETERMINING THE TAXABLE PORTION OF THE RETIREMENT INCOME

To make the correct determinations about the taxability of the taxpayer's retirement income, you may need to ask the taxpayer several questions. Be considerate when probing for the information you need to complete the return.

If the taxpayer cannot provide the required information, suggest that the former employer or annuity administrator be contacted. You may want to give the taxpayer a written list of questions that should be answered by the employer.

Pensions In General

Generally, if the taxpayer did not pay any part of the cost of his or her employee pension or annuity and his or her employer did not withhold part of the cost from his or her pay while he or she worked, the amounts received each year are fully taxable.

Example 1

Delilah worked for a software development company for 20 years. She retired in 2003 and she receives a monthly pension of \$1,348. She never contributed to the pension plan while she was working, her employer made all of the contributions. Her pension is fully taxable.

Exercise 4

Dotty worked for the local tire plant for 32 years. She retired in June of 2003 and she receives a monthly pension of \$1,679 (she received 6 payments in 2003). Dotty never contributed to the pension plan. Her employer made all of the contributions. How much of her pension is taxable? _____

If the taxpayer made contributions to a pension plan with "before tax" dollars, then the entire distribution will be taxable. The contribution that the taxpayer made was with money that had not been taxed. This is common in 401(K) and Thrift Savings plans.

If the taxpayer paid part of the cost of the annuity or pension with "after tax" dollars, he or she is not taxed on the part of the annuity or pension he or she receives that represents a return of his or her cost. Generally, this amount will be clearly stated on the Form 1099R. See the next section for more information on determining the taxable portion of an annuity or pension.

Example 2

Joseph retired in 2003 after working 30 years for a construction company. Each week, he contributed to the Carpenter's Pension Plan. Every year, he paid tax on the gross amount of his salary. His pension contributions were made with dollars that had already been taxed. Joseph's pension payments will be partially taxable.

Partially Taxable Pensions and Annuities Other Than IRAs

General Rule

The General Rule is one of the two methods used to figure the tax-free part of each pension/annuity payment. It is based on the ratio of the investment in the contract to the total expected return.

Most taxpayers who retire after 1996 can no longer use the General Rule. Unless the exception applies, retirees must use the Simplified Method for annuity payments from a qualified plan.

The General Rule must be used if the pension or annuity payment is from a nonqualified plan (for example, a private annuity, a purchased commercial annuity, or a nonqualified employee plan).

The calculation of the taxable portion of a payment under the General Rule is outside of the scope of the volunteer program. However, if the exclusion percentage has already been computed, you can assist the taxpayer with the return.

If you need more information, please see Publication 939, *General Rule for Pensions and Annuities*.


Simplified Method

Under the Simplified Method, the tax-free portion of each pension/annuity payment is figured by dividing the taxpayer's cost in the contract by the total number of expected monthly payments. For a pension/annuity that is payable for the life of the taxpayer (and his or her beneficiary), the number of expected months is based on the age of the taxpayer and is determined from a table.

Example 3

James retired from a manufacturing plant in 2003. While he was working at the plant, his employer withheld money from each paycheck and sent it to the Engineer's Pension Fund. James will receive a monthly pension payment for the rest of his life. James will use the table at the bottom of the Simplified Method worksheet to determine the number of expected monthly payments.

To determine the taxable portion of a pension or annuity, you will use the Simplified General Rule Worksheet (see Exhibit 4). Once figured, the monthly exclusion amount remains the same even when the pension income increases.

Before you begin: ✓ If you are the beneficiary of a deceased employee or former employee who died **before** August 21, 1996, see Pub. 939 to find out if you are entitled to a death benefit exclusion of up to \$5,000. If you are, include the exclusion in the amount entered on line 2 below. 

Note. If you had more than one partially taxable pension or annuity, figure the taxable part of each separately. Enter the total of the taxable parts on Form 1040, line 16b. Enter the total pension or annuity payments received in 2003 on Form 1040, line 16a.

1. Enter the total pension or annuity payments received in 2003. Also, enter this amount on Form 1040, line 16a . . .	1.	_____
2. Enter your cost in the plan at the annuity starting date	2.	_____
3. Enter the appropriate number from Table 1 below. But if your annuity starting date was after 1997 and the payments are for your life and that of your beneficiary, enter the appropriate number from Table 2 below	3.	_____
4. Divide line 2 by the number on line 3	4.	_____
5. Multiply line 4 by the number of months for which this year's payments were made. If your annuity starting date was before 1987 , skip lines 6 and 7 and enter this amount on line 8. Otherwise, go to line 6	5.	_____
6. Enter the amount, if any, recovered tax free in years after 1986	6.	_____
7. Subtract line 6 from line 2	7.	_____
8. Enter the smaller of line 5 or line 7	8.	_____
9. Taxable amount. Subtract line 8 from line 1. Enter the result, but not less than zero. Also, enter this amount on Form 1040, line 16b. If your Form 1099-R shows a larger amount, use the amount on this line instead of the amount from Form 1099-R	9.	_____

Table 1 for Line 3 Above

IF the age at annuity starting date (see page 26) was . . .	AND your annuity starting date was—	
	before November 19, 1996, enter on line 3 . . .	after November 18, 1996, enter on line 3 . . .
55 or under	300	360
56–60	260	310
61–65	240	260
66–70	170	210
71 or older	120	160

Table 2 for Line 3 Above

IF the combined ages at annuity starting date (see page 26) were . . .	THEN enter on line 3 . . .
110 or under	410
111–120	360
121–130	310
131–140	260
141 or older	210

For pensions starting after December 31, 1986, the taxpayer will exclude the nontaxable pension amount until the pension cost is recovered. Once the pension cost is recovered, the entire pension income is taxable.

Example 4

Peter, age 65, receives retirement benefits under a joint and survivor annuity, to be paid over the joint lives of Peter and his wife, Mary, age 62. Peter's annuity starting date is January 1, 2003.

He contributed \$31,000 to a qualified plan and did not receive any distributions before the annuity starting date. Peter receives monthly payments of \$1,200 and his tax-free monthly amount is \$100. Mary will receive monthly survivor benefits of \$600 upon her husband's death.

See Exhibit 5 for a completed Simplified Method Worksheet for Peter.

Exhibit 5

Simplified Method Worksheet from Peter and Mary

Before you begin: ✓ If you are the beneficiary of a deceased employee or former employee who died **before** August 21, 1996, see Pub. 939 to find out if you are entitled to a death benefit exclusion of up to \$5,000. If you are, include the exclusion in the amount entered on line 2 below.



Note. If you had more than one partially taxable pension or annuity, figure the taxable part of each separately. Enter the total of the taxable parts on Form 1040, line 16b. Enter the total pension or annuity payments received in 2003 on Form 1040, line 16a.

1. Enter the total pension or annuity payments received in 2003. Also, enter this amount on Form 1040, line 16a . . .	1.	14,400
2. Enter your cost in the plan at the annuity starting date	2.	31,000
3. Enter the appropriate number from Table 1 below. But if your annuity starting date was after 1997 and the payments are for your life and that of your beneficiary, enter the appropriate number from Table 2 below	3.	310
4. Divide line 2 by the number on line 3	4.	100
5. Multiply line 4 by the number of months for which this year's payments were made. If your annuity starting date was before 1987 , skip lines 6 and 7 and enter this amount on line 8. Otherwise, go to line 6	5.	1,200
6. Enter the amount, if any, recovered tax free in years after 1986	6.	
7. Subtract line 6 from line 2	7.	1,200
8. Enter the smaller of line 5 or line 7	8.	1,200
9. Taxable amount. Subtract line 8 from line 1. Enter the result, but not less than zero. Also, enter this amount on Form 1040, line 16b. If your Form 1099-R shows a larger amount, use the amount on this line instead of the amount from Form 1099-R	9.	13,200

Table 1 for Line 3 Above

IF the age at annuity starting date (see page 26) was . . .	AND your annuity starting date was—	
	before November 19, 1996, enter on line 3 . . .	after November 18, 1996, enter on line 3 . . .
55 or under	300	360
56–60	260	310
61–65	240	260
66–70	170	210
71 or older	120	160

Table 2 for Line 3 Above

IF the combined ages at annuity starting date (see page 26) were . . .	THEN enter on line 3 . . .
110 or under	410
111–120	360
121–130	310
131–140	260
141 or older	210

We use the Simplified Method for Peter because his annuity starting date is after November 18, 1986, and the payments are from a qualified plan. In addition, because his annuity starting date is after December 31, 1997, and his annuity is payable over the lives of more than one annuitant, you must combine his age with his wife's age in completing line 3 of the worksheet.

After Peter has excluded a total of \$31,000 the rest of his retirement benefits will be fully taxable.

Because this is a joint and survivor annuity, if Peter dies before recovering all of the pension cost, his wife will also exclude \$100 from her \$600 monthly payment until the pension cost is fully recovered. If she dies before recovering all of the pension cost, the remaining unrecovered cost will be deducted on her final income tax return as a miscellaneous itemized deduction on Schedule A (Form 1040) (not subject to the 2-percent of adjusted-gross-income limitation).

Exercise 5

George, age 65, began receiving pension income under a joint and survivor annuity. George's annuity starting date is January 1, 2003. George had contributed \$26,000 to a qualified plan and had received no distribution before 2003. George is to receive a monthly retirement benefit of \$1,000 and his wife, age 66, is to receive a monthly survivor benefit of \$500 upon George's death. Complete the Simplified Method Worksheet for George.

Before you begin: ✓ If you are the beneficiary of a deceased employee or former employee who died **before** August 21, 1996, see Pub. 939 to find out if you are entitled to a death benefit exclusion of up to \$5,000. If you are, include the exclusion in the amount entered on line 2 below.



Note. If you had more than one partially taxable pension or annuity, figure the taxable part of each separately. Enter the total of the taxable parts on Form 1040, line 16b. Enter the total pension or annuity payments received in 2003 on Form 1040, line 16a.

1. Enter the total pension or annuity payments received in 2003. Also, enter this amount on Form 1040, line 16a . . .	1.	<input type="text"/>
2. Enter your cost in the plan at the annuity starting date	2.	<input type="text"/>
3. Enter the appropriate number from Table 1 below. But if your annuity starting date was after 1997 and the payments are for your life and that of your beneficiary, enter the appropriate number from Table 2 below	3.	<input type="text"/>
4. Divide line 2 by the number on line 3	4.	<input type="text"/>
5. Multiply line 4 by the number of months for which this year's payments were made. If your annuity starting date was before 1987, skip lines 6 and 7 and enter this amount on line 8. Otherwise, go to line 6	5.	<input type="text"/>
6. Enter the amount, if any, recovered tax free in years after 1986	6.	<input type="text"/>
7. Subtract line 6 from line 2	7.	<input type="text"/>
8. Enter the smaller of line 5 or line 7	8.	<input type="text"/>
9. Taxable amount. Subtract line 8 from line 1. Enter the result, but not less than zero. Also, enter this amount on Form 1040, line 16b. If your Form 1099-R shows a larger amount, use the amount on this line instead of the amount from Form 1099-R	9.	<input type="text"/>

Table 1 for Line 3 Above

IF the age at annuity starting date (see page 26) was . . .	AND your annuity starting date was—	
	before November 19, 1996, enter on line 3 . . .	after November 18, 1996, enter on line 3 . . .
55 or under	300	360
56–60	260	310
61–65	240	260
66–70	170	210
71 or older	120	160

Table 2 for Line 3 Above

IF the combined ages at annuity starting date (see page 26) were . . .	THEN enter on line 3 . . .
110 or under	410
111–120	360
121–130	310
131–140	260
141 or older	210

Exercise 6

Gustav retired in 2003 at the age of 63. He has never been married. He paid in to his pension with after tax dollars, so part of his pension payments will not be taxable. How many months of life expectancy will you use when you determine the taxable portion of his pension? _____

Individual Retirement Arrangement

A taxpayer establishes an **individual retirement arrangement (IRA)** and makes **contributions** to it through a bank, credit union, brokerage, or other entity approved by the IRS. Earnings and gains generally accumulate tax free until they are withdrawn as taxable, non-taxable or partly taxable **distributions**.

There are four kinds of IRAs, each of which offer tax advantages.

Traditional IRA

If the taxpayer made **nondeductible** contributions into the IRA, he or she need not pay income tax on those contributions again when receiving them later as part of a distribution from the traditional IRA.

If the taxpayer made nondeductible contributions to a traditional IRA he or she has a cost basis (investment in the contract) equal to the amount of those contributions. The nondeductible contributions are not taxed when they are distributed. They are a return of investment.

Form 8606, *Nondeductible IRAs*, must be completed and attached to the return if the taxpayer received a distribution from a traditional IRA and he or she has ever made a nondeductible contribution to any traditional IRAs.

The taxpayer cannot withdraw only nondeductible contributions from a traditional IRA; if there have been any earnings or gains on contributions or deductible contributions have been made to any traditional IRA, part of each distribution will be taxable.

Example 5

Tyrone contributed \$500 a year to a traditional IRA. Each year he deducted his traditional IRA contribution from his income. This year he received his first distribution from the traditional IRA. It is fully taxable. Tyrone will pay income tax on the distributions he receives which represent the contributions he made and deducted as well as the money the contributions have earned over the years.

Example 6

Dorothy contributed \$750 a year to a traditional IRA. She did not qualify to deduct her contributions from her income. This year she received her first distribution from the traditional IRA. She will pay income tax only on the part of the distribution from the traditional IRA that represents earnings on the contributions. She will use Form 8606, *Nondeductible IRAs* to determine the taxable portion of her distribution.

Savings Incentive Match Plans for Employees (SIMPLE) IRA

Some employers offer their employees, including a self employed individual, the chance to contribute part of their pay to an IRA as part of a SIMPLE plan. The employer is also generally required to make contributions on behalf of eligible employees. The employee is not currently taxed on his or her contributions when they are paid into the IRA. Distributions from a SIMPLE IRA are generally fully taxable.

Simplified Employee Pension (SEP) IRA

Some employers offer their employees the chance to take part in a SEP. Self employed people also can establish a SEP-IRA for themselves. Generally, SEP-IRA contributions are not included in an employee's income when paid into the IRA. Distributions are generally fully taxable when the employee receives them in later years.

Roth IRA

Contributions to a Roth IRA are not deductible. Distributions from a Roth IRA are tax free if they meet certain conditions, even if they represent earnings that accumulated in the Roth IRA. For the distribution of earnings to be excluded from income, the following requirements must be met:

1. The distribution is made after the 5-year period beginning with the first taxable year for which a contribution was made to a Roth IRA set up for the taxpayer's benefit, and
2. The distribution is:
 - a) Made on or after age 59 1/2,
 - b) made because the taxpayer was disabled,
 - c) made to a beneficiary or to an estate, or
 - d) to pay certain qualified first-time homebuyer amounts.

Social Security Benefits

Social security benefits are reported to the taxpayer on Form SSA-1099, *Social Security Benefit Statement*. Part of the social security benefits or Part of the social security equivalent portion of tier 1 railroad retirement benefits a taxpayer receives may be taxable. The taxable amount, if any, depends upon the rest of the taxpayer's income and filing status.

Generally, if Social Security benefits were the taxpayers only source of income, the benefits are not taxable and the taxpayer probably does not need to file a federal income tax return. If the taxpayer received Social Security benefits plus other income, the answer to how much, if any, is taxable can be found by completing the Social Security Benefits Worksheet.

The *Social Security Benefits Worksheet* is found in the instruction booklets for Forms 1040 and 1040A. The worksheet is also available on tax software packages. If you are using Taxwise you will not

need to complete the worksheet. The software will calculate the taxable portion of the benefits. The worksheet is used to figure the taxable portion of benefits received. Some of the benefits received are taxable if total income, plus one-half of the benefits received, is more than certain **base amounts**. The current base income amounts are:

- \$32,000 if married and filing a joint return
- \$25,000 if taxpayer is filing as single, head of household, or qualifying widow(er) with dependent child
- \$25,000 if married but filing separately, and the taxpayer **did not** live with his or her spouse at any time during 2003
- \$0 if married filing separately, and the taxpayer **did** live with his or her spouse at any time during 2003

The taxable amount of benefits received is figured using the worksheet provided in the instruction booklets for Forms 1040 and 1040A. The amount in box 5, Net benefits for 2003, is entered on a worksheet to figure if any of the benefits are taxable. Net benefits are the gross benefits less any repayments made by the taxpayer in the tax year. Make sure you enter only the amount from box 5 of Form SSA-1099 on line 1 of the worksheet or on the tax preparation software.

Example 7

Ray and Susan are married and file a joint Form 1040. Ray is retired and receives a fully taxable pension of \$12,000 (Form 1040, line 16b). Ray received a \$3,000 short-term capital gain from the sale of stock.

Ray also receives social security benefits. His Form SSA-1099 is shown in Exhibit 7. Susan worked and earned wages of \$21,000 (Form 1040, line 7) in 2003. She also contributed \$560 to her traditional IRA (Form 1040, line 23). Susan is not covered at work by a pension plan.

Ray and Susan's completed *Social Security Benefits Worksheet* is shown in Exhibit 8.

FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT

2003 • PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME.
 • SEE THE REVERSE FOR MORE INFORMATION.

Box 1. Name Ray Maple	Box 2. Beneficiary's Social Security Number xxx-xx-xxxx
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Box 3. Benefits Paid in 2003 \$7,056.00	Box 4. Benefits Repaid to SSA in 2003	Box 5. Net Benefits for 2003 (Box 3 minus Box 4) \$7,056.00
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DESCRIPTION OF AMOUNT IN BOX 3	DESCRIPTION OF AMOUNT IN BOX 4
<p style="font-size: 2em; opacity: 0.5; transform: rotate(-30deg);">Draft as of 09/01/2003</p>	Box 6. Voluntary Federal Income Tax Withholding
	Box 7. Address 123 Ash Street Your Town, IL 00000
	Box 8. Claim Number (Use this number if you need to contact SSA.)

Form SSA-1099-SM (1-2004)

DO NOT RETURN THIS FORM TO SSA OR IRS



Before you begin:

- ✓ Complete Form 1040, lines 21, 23, 24, and 27 through 32a, if they apply to you.
- ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
- ✓ If you are married filing separately and you **lived apart** from your spouse for all of 2003, enter "D" to the right of the word "benefits" on line 20a.
- ✓ Be sure you have read the **Exception** on page 26 to see if you can use this worksheet instead of a publication to find out if any of your benefits are taxable.

1. Enter the total amount from box 5 of all your Forms SSA-1099 and Forms RRB-1099	1.	7,056	
2. Enter one-half of line 1	2.		3,528
3. Enter the total of the amounts from Form 1040, lines 7, 8a, 9a, 10 through 12, 13a, 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099	3.		36,000
4. Enter the amount, if any, from Form 1040, line 8b	4.		
5. Add lines 2, 3, and 4.	5.		39,528
6. Enter the total of the amounts from Form 1040, lines 23, 24, and 27 through 32a, plus any amount you entered on the dotted line next to line 33	6.		560
7. Is the amount on line 6 less than the amount on line 5? <input type="checkbox"/> No. None of your social security benefits are taxable. <input checked="" type="checkbox"/> Yes. Subtract line 6 from line 5	7.		38,968
8. If you are: <input checked="" type="checkbox"/> Married filing jointly, enter \$32,000 <input type="checkbox"/> Single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003, enter \$25,000 <input type="checkbox"/> Married filing separately and you lived with your spouse at any time in 2003, skip lines 8 through 15; multiply line 7 by 85% (.85) and enter the result on line 16. Then go to line 17	8.		32,000
9. Is the amount on line 8 less than the amount on line 7? <input type="checkbox"/> No. None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. But if you are married filing separately and you lived apart from your spouse for all of 2003, enter -0- on line 20b. Be sure you entered "D" to the right of the word "benefits" on line 20a. <input checked="" type="checkbox"/> Yes. Subtract line 8 from line 7	9.		6,968
10. Enter: \$12,000 if married filing jointly; \$9,000 if single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003	10.		12,000
11. Subtract line 10 from line 9. If zero or less, enter -0-	11.		0
12. Enter the smaller of line 9 or line 10	12.		6,968
13. Enter one-half of line 12	13.		3,484
14. Enter the smaller of line 2 or line 13	14.		3,484
15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0-	15.		0
16. Add lines 14 and 15	16.		3,484
17. Multiply line 1 by 85% (.85)	17.		5,998
18. Taxable social security benefits. Enter the smaller of line 16 or line 17	18.		3,484
<input type="checkbox"/> Enter the amount from line 1 above on Form 1040, line 20a. <input checked="" type="checkbox"/> Enter the amount from line 18 above on Form 1040, line 20b.			



If part of your benefits are taxable for 2003 **and** they include benefits paid in 2003 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

Exercise 7

Jules and Olga are both over 65 and they both received Social Security benefits. They will file a joint return. They had \$2,093 of tax-exempt interest income. Do you need to include this amount on the Social Security benefits worksheet ? _____

Example 8

Anne and her son, Tony, both receive survivor social security benefits. Anne receives a benefit check for \$400 each month.

A portion of these benefits belongs to Tony. He was sent a Form SSA-1099, which showed \$1,800 of net benefits received. Tony also had \$4,000 income from a summer job and some interest income. When you prepare his tax return, you would complete a *Social Security Benefits Worksheet* for Tony to figure if any of his social security benefits are taxable.

When you complete Anne's tax return, you would include only the \$3,000 of her social security benefits on her worksheet to figure if any of her benefits are taxable.

Exercise 8

Antoinette's husband was killed by a drunk driver. He was only 34 and he left behind three young children in addition to his wife. Each of the three kids will receive Social Security benefits until they turn 18. Antoinette does not receive a survivor's benefit for herself. Since Antoinette will claim the children on her return, should she include the children's Social Security benefits on her return? _____

If the taxpayer files a joint return, you must combine the income and benefits of both spouses when completing the worksheet. Even if the spouse received no social security benefits, include the spouse's other income when completing the worksheet. If both spouses received benefits, combine both their benefits and income, and complete only one worksheet.

Example 9

Wanda and Dan are both retired and they file a joint return. Wanda received a Form SSA-1099 with an amount of \$4,300 appearing in box 5. Dan retired from the railroad, and box 5 of his Form RRB-1099 shows an amount of \$6,800. Wanda and Dan will use benefits of \$11,100 and only one worksheet to figure if any of their benefits are taxable.

Disability Pension Income

Generally, a taxpayer who retires on disability must include all of his or her disability payments in income. Disability payments are taxed as wages until the taxpayer reaches the minimum retirement age set by the employer. After the taxpayer reaches the minimum retirement age, disability payments are treated as pension income. Minimum retirement age is generally the earliest age at which the taxpayer may receive a pension whether or not disabled.

(Some taxpayers with retirement income may be eligible for the credit for the elderly or the disabled. See Lesson 14 for more information.)

REPORTING THE RETIREMENT INCOME

Reporting Pension Income

Total pension income is entered on Form 1040, line 16a, or Form 1040A, line 12a. The taxable part is entered on Form 1040, line 16b, or on Form 1040A, line 12b. If the pension is fully taxable, enter it on Form 1040, line 16b, or Form 1040A, line 12b and leave Form 1040, line 16a, or Form 1040A, line 12a, blank. Social Security benefits and IRA distributions are not reported on the pension line of the tax return. Later in this lesson, you will learn where to report these payments. If the taxpayer has more than one pension or annuity that is not fully taxable, figure the taxable part of each separately. Enter only totals on the proper lines of Form 1040 and Form 1040A. If you are using tax preparation software, the totals will be computed for you and placed on the appropriate lines, if you correctly enter all of the information from the 1099 forms.

When the taxpayer has more than one pension or annuity, and you are preparing the return by hand, use a separate piece of paper as a worksheet to group together detailed information. Only the summary information is entered on Form 1040 or Form 1040A. The worksheet should be kept for future reference.

Be sure to add the amounts shown on all Forms 1099-R as federal income tax withheld and enter the total on Form 1040, line 62, or on Form 1040A, line 39. The omission of pension withholding is a frequent error that results in an incorrect amount owed or refunded (and an unhappy taxpayer).

Exercise 9

Verna comes to you for help with her tax return. She tells you that she worked for 17 years in a factory and then she worked for 22 years in a state job. She opens up a big brown envelope and takes out many pieces of paper. After you help her sort through the papers, you determine that she had the following income:

- Form 1099INT for Interest on her savings - \$3,951
- Form 1099INT for Interest on her checking - \$504
- Form 1099INT for Interest on her CDs - \$1,832
- Form 1099R for Pension from her Factory employer - \$2,637 (fully taxable)
- Form 1099R for IRA distribution - \$1,030 (fully taxable)
- Form 1099R for Pension from her state employer - \$17,044 (she has been getting this for several years and she shows you the simplified general rule worksheet that indicates that \$219 of each monthly payment is non-taxable).
- Form SSA1099 with an amount of \$3,692 in box 5.

She also had receipts for medical bills, prescriptions, real estate taxes and contributions. They totaled \$3,904.

What amount should you enter on lines 12 a and 12b of Verna's form 1040A? _____

DISABILITY REPORTING

An employer may report disability income on Form W-2, *Wage and Tax Statement*. However, an employer may also report disability income on Form 1099-R, *Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.* Enter disability income reported on Form W-2 on line 7 of either Form 1040 or Form 1040A.

If the employer reports disability income on Form 1099-R, Box 2a shows the taxable amount. Check to see if Box 7 (Distribution Code) shows the code number 3 (Disability). If Box 7 indicates that the taxpayer is receiving disability payments, then determine if the taxpayer has reached the minimum retirement age.

1. Until the taxpayer reaches the minimum retirement age, report the disability income as wages on line 7 of Form 1040 or Form 1040A.

2. After the taxpayer has reached the minimum retirement age, report the disability income as a taxable pension. If the disability payments are partially taxable, use lines 16a and 16b (Form 1040) or lines 12a and 12b (Form 1040A). If the payments are fully taxable, enter the taxable amount on line 16b or line 12b; do not make an entry on line 16a or line 12a.

Exercise 10

Annie Jo is 47 years old and she tells you that she has retired on disability from her job. She used to load cargo for a tractor-trailer company, but a large box fell on her and left her paralyzed. She receives a monthly payment from her former employer's pension plan. She has not reached the minimum retirement age set by her company's pension plan. Where should you report her disability income? _____

Reporting Social Security Benefits

Report taxable social security benefits on Form 1040, line 20b, or Form 1040A, line 14b. Complete the other income and adjustment items on page 1 of Form 1040 or Form 1040A before you use the *Social Security Benefits Worksheet*. Then complete the other lines of the worksheet to figure if any of the benefits are taxable.

If the worksheet shows that no benefits are taxable, leave the line blank for social security benefits on Form 1040 or Form 1040A. Then total page 1 and complete the remainder of the tax return. If you determine that any benefits are taxable, complete line 20 of Form 1040 or line 14 of Form 1040A.

Enter the social security benefits received on Form 1040, line 20a, and enter the taxable portion (from line 18 of the worksheet) on line 20b. On Form 1040A, enter the benefits received on line 14a, and enter the taxable portion of benefits on line 14b.

The taxable portion of social security benefits is never more than 85 percent of the net benefits the taxpayer has received. In many cases, the taxable portion is less than 50 percent.

Exercise 11

Hank comes to your site for some help with his tax return. He is really upset because his neighbor told him that he would have to pay tax on all of his Social Security benefits this year. After talking to Hank, you learn that his wife died in 2002 and that he decided to sell his farm and move into senior housing in 2003. The sale of the farm created \$31,896 of taxable income for Hank. His neighbor told him that with that much income, the entire \$11,724 of his Social Security benefits would be taxable. What is the maximum taxable amount of Hank's benefits? _____

Reporting IRA Distributions

IRA distributions are reported on Form 1099-R, *Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*

Traditional IRA, SIMPLE IRA, or SEP-IRA: Box 7 of Form 1099-R shows "7" as the distribution code for a normal distribution, and the box "IRA/SEP/SIMPLE" is checked. Ask the taxpayer whether he or she deducted all traditional IRA contributions from income in the year they were made. If so, the entire distribution is taxable. Report it on Form 1040A, lines 11a and 11b, or on Form 1040, lines 15a and 15b. Distributions from a SIMPLE IRA and from a SEP-IRA are generally fully taxable.

Exercise 12

Steve and Sally need you to help them with their taxes. They have done most of the work, but they are not sure what to put on lines 11a, 11b, 12a and 12b of their Form 1040A. You look at the 1099R forms that they have brought with them and you make the following observations:

- ABC Pension - fully taxable - \$4,382
- XYZ Pension - partially taxable - Gross amount = \$9,202, Taxable portion = \$7,834
- Sally's IRA withdrawal - fully taxable - \$3,809
- Steve's IRA withdrawal - partially taxable - Gross amount = \$4,800, Taxable amount \$4,193

What amount should Steve and Sally put on:

Line 11a _____
Line 11b _____
Line 12a _____
Line 12b _____

Premature Distributions

Most distributions (both periodic and lump-sum) from qualified retirement plans made before the taxpayer has reached age 59 1/2 are subject to an additional tax of 10%. The tax applies to the taxable portion of the distribution or payment. Certain early distributions are exempted for the early distribution tax. If the distribution code in box 7 of Form 1099R is 2, 3, or 4, the taxpayer does not have to pay the additional tax. If the Form 1099R shows a code 1 in box 7 you may need to complete Form 5329 to determine the additional tax on the distribution. However, if the taxpayer does not meet one of the exceptions to the additional tax (as noted on Form 5329), you can just enter 10% of the distribution on line 57 of Form 1040.

Lump-sum Distributions

A **lump-sum distribution** is the distribution or payment within one tax year of an employee's entire balance (less deductible voluntary employee contributions and certain amounts forfeited or subject to forfeiture) from all qualified pension, stock bonus, or profit-sharing plans that the employer maintains. To qualify as a lump-sum distribution, the payment must have been made:

- Because the plan participant died, or
- After the participant reached age 59 1/2, or
- Because the participant (not including a self-employed individual) separated from service with the employer, or
- After the participant, if a self-employed individual, becomes totally and permanently disabled.

Lump-sum distributions are reported on Form 1099-R like any other pension distribution. Some lump-sum distributions qualify for special tax treatments. Code A in box 7 of the 1099-R indicates that it is a lump-sum distribution and it qualifies for special tax treatments such as:

- Distributions allocable to pre-1974 participation being taxed at a special rate (there will be an amount in box 3 of Form 1099-R) (The part after 1973 is ordinary income)
- Ten-year tax option of the distributions
- Tax-free rollover of the distribution into an Individual Retirement Arrangement (IRA).

Minimum Distributions

Taxpayers are required to receive **minimum distributions** from qualified employee retirement plans, qualified annuity plans, deferred compensation plans, tax-sheltered annuity plans and Individual Retirement Arrangements (IRAs) other than Roth IRAs.

Distributions must begin by April 1 of the calendar year that follows the calendar year in which the taxpayer reaches age 70 1/2 or retires, if later. (For IRAs, it does not matter whether the taxpayer is employed. Distributions must begin by April 1 of the year following the calendar year in which the taxpayer reaches age 70 1/2.) Required distributions for later years must be made by December 31 of that year.

IMPORTANT! If the taxpayer does not receive the minimum distribution, an excise tax may be imposed. The tax is 50 percent of the difference between the minimum distribution and the amount actually distributed for the tax year.

Exercise 13

Helen turned 71 on March 17, 2004. She retired in 1998. She has never taken any distribution from her traditional IRA accounts. She is asking for your help, because she knows that she will have to take a distribution from the IRA this year. The bank where she has her IRA told her that she needs to take a minimum distribution of \$1,479 per year. What does Helen need to do?

- a) Helen only needs to take a distribution of \$1,479 by 12-31-04.
- b) Helen needs to take a distribution of at least \$1,479 by 4-1-04 and at least another \$1,479 by 12-31-04.
- c) Helen needs to take a distribution of \$2,958 by 12-31-04.
- d) Helen does not need to take any distributions until 2005.

Lump-Sum Benefit Payments

Some taxpayers may have received a **lump-sum benefit payment** in 2003. This payment could be for both the current tax year and the prior tax year. The lump-sum payment will be included in box 3 of the Form SSA-1099 or Form RRB-1099 that the taxpayer receives.

The form will also show the year, or years, of the payment. When figuring the taxable portion of social security benefits, two options are available for lump-sum benefit payments. The first option allows the taxpayer to report the whole payment in 2003, the year it was received. When the taxpayer chooses this option, complete the *Social Security Benefits Worksheet* as usual by including the entire lump-sum payment on line 1.

The taxpayer also has the option of treating the payment as received in the earlier year or years. This is done by figuring whether any part of these benefits is taxable, based on the earlier

year's income. Any part that is taxable is then added to any taxable benefits for the current year (2003) and included on Form 1040, line 20b.

If the taxpayer chooses to spread the payments back to earlier years, only 2003 income will be adjusted. The taxpayer does not file amended returns for the earlier years. However, a special procedure **must** be used to figure the taxable portion of the benefits assigned to the earlier years. If the taxpayer wants to use this option, refer him or her to a paid professional tax preparer or to IRS Publication 915, *Social Security and Equivalent Railroad Retirement Benefits*.

IRAs Withdrawal of Excess Contributions

If the taxpayer withdraws excess contributions and any earnings by the due date of the return, he or she will not be subject to an additional 6% tax on the excess contribution. The withdrawal must be completed by the due date of the tax return for that year, including extensions.

The withdrawn excess contribution is not included in the taxpayer's gross income if both of the following conditions are met. 1) No deduction was allowed for the excess contribution. 2) All interest or other income earned on the excess contribution is withdrawn. However, the taxpayer must include in his or her gross income the interest or other income that was earned on the excess contribution. Report it on the return for the year in which the excess contribution was made.

The withdrawal of interest or other income may be subject to an additional 10% tax on early withdrawals. Taxpayers will receive Form 1099-R indicating the amount of the withdrawal. If the excess contribution was made in a previous tax year, the form will indicate the year in which the earnings are taxable.

In general, a taxpayer must include all withdrawals from his or her traditional IRA in gross income. However, if the total contributions to an IRA (other than rollover contributions for the year) are \$3,000 or less (\$3,500 or less if taxpayer is age 50 or older), and there are no employer contributions for the year, the taxpayer can withdraw any excess contribution after the due date for filing the tax return for that year, including extensions, and not include the amount withdrawn in his or her gross income.

This applies only to the part of the excess for which the taxpayer did not take a deduction. For more information on excess contributions, see Publication 590.

Pension Withholding and Estimated Tax Payments

Income tax is normally withheld from the taxable part of a pension or annuity. At the taxpayer's request, the payer of the pension or annuity can adjust the withholding amount or stop the withholding completely. Generally, Form W-4P is used to request a change in withholding on a pension. The taxpayer should complete the form

and send it to the payer of the pension. The taxpayer can request withholding from their Social Security benefits by completing Form W-4V, Voluntary Withholding Request, and filing it with the Social Security Administration.

A taxpayer who chooses not to have tax withheld may have to pay estimated tax. For more information about estimated tax or withholding, see Lesson 7 and Publication 505, *Tax Withholding and Estimated Tax*. Failure to have enough federal income tax paid in throughout the year can result in an estimated tax penalty. Also, it can result in a large amount of tax due when the return is filed. If the taxpayer owes more than \$1,000 on the tax return, you should discuss their withholding and estimated tax options with them.

Exercise 14

FaithMae comes to your site to get her 2003 tax return done. When you finish her return, you explain to her that she owes \$985. You tell her that she needs to pay this amount by April 15, 2004. She says that she will pay the amount, but she wants to know if there is some way to have more tax withheld from her pension so that she doesn't owe so much at the end of the year. What form should she complete to increase the withholding from her pension? Who does she give the form to? _____

Health Coverage Tax Credit

The following information is provided for awareness only. You are not expected to calculate this new credit.

The Health Coverage Tax Credit (HCTC) is a federal tax credit that was established to assist the following groups of people:

1. Workers who lose their jobs due to the effects of international trade. The worker must be eligible for either certain Trade Adjustment Assistance benefits or Alternative Trade Adjustment Assistance.
2. People who receive benefits from the Pension Benefit Guaranty Corporation (PBGC) and are at least 55 years old.

Taxpayers who are potentially eligible for this credit will be notified by mail. Shortly after the mailing, the HCTC Customer Contact Center will mail the taxpayer a packet describing the program and eligibility requirements.

For additional information on this topic, you can visit the IRS website at: www.irs.gov.

▶▶ SUMMING UP THIS LESSON ◀◀

Pensions or annuities may have a tax-free portion if the taxpayer made after-tax contributions to the plan.

To determine the taxable portion of the annuity payments of a taxpayer, use:

- a.** The Simplified Method if the taxpayer's annuity starting date is after November 18, 1996, and annuity payments are from a qualified plan. For annuity starting dates after 1997, use the annuitant's age (or combined ages if more than one annuitant) at the annuity starting date of the taxpayer(s).
- b.** The General Rule for annuity payments from a nonqualified plan and for certain retirees age 75 or older.
 - ▶ Total pension or annuity income and taxable pension or annuity income are entered on Form 1040, lines 16a and 16b, or Form 1040A, lines 12a and 12b.
 - ▶ Social security – Nontaxable or taxable To determine taxable portion of social security payments received by a taxpayer, use: Social Security Benefits Worksheet.
 - ▶ Total social security income and taxable portion are entered on Form 1040, lines 20a and 20b, or Form 1040A, lines 14a and 14b.
 - ▶ Federal income tax on pension, annuity and social security income can be withheld by the payer, or the taxpayer may choose to pay estimated tax.

Answers to Exercises

Exercise 1

The distribution was a “normal distribution”.

Exercise 2

No

Exercise 3

Form RRB-1099 and Form RRB 1099-R.

Exercise 4

All of it. \$10,074

Exercise 5

Before you begin: ✓ If you are the beneficiary of a deceased employee or former employee who died **before** August 21, 1996, see Pub. 939 to find out if you are entitled to a death benefit exclusion of up to \$5,000. If you are, include the exclusion in the amount entered on line 2 below.



Note. If you had more than one partially taxable pension or annuity, figure the taxable part of each separately. Enter the total of the taxable parts on Form 1040, line 16b. Enter the total pension or annuity payments received in 2003 on Form 1040, line 16a.

1. Enter the total pension or annuity payments received in 2003. Also, enter this amount on Form 1040, line 16a . . .	1.	<u>12,000</u>
2. Enter your cost in the plan at the annuity starting date	2.	<u>26,000</u>
3. Enter the appropriate number from Table 1 below. But if your annuity starting date was after 1997 and the payments are for your life and that of your beneficiary, enter the appropriate number from Table 2 below	3.	<u>260</u>
4. Divide line 2 by the number on line 3	4.	<u>100</u>
5. Multiply line 4 by the number of months for which this year's payments were made. If your annuity starting date was before 1987 , skip lines 6 and 7 and enter this amount on line 8. Otherwise, go to line 6	5.	<u>1,200</u>
6. Enter the amount, if any, recovered tax free in years after 1986	6.	
7. Subtract line 6 from line 2	7.	<u>1,200</u>
8. Enter the smaller of line 5 or line 7	8.	<u>1,200</u>
9. Taxable amount. Subtract line 8 from line 1. Enter the result, but not less than zero. Also, enter this amount on Form 1040, line 16b. If your Form 1099-R shows a larger amount, use the amount on this line instead of the amount from Form 1099-R	9.	<u>10,800</u>

Table 1 for Line 3 Above

IF the age at annuity starting date (see page 26) was . . .	AND your annuity starting date was—	
	before November 19, 1996, enter on line 3 . . .	after November 18, 1996, enter on line 3 . . .
55 or under	300	360
56–60	260	310
61–65	240	260
66–70	170	210
71 or older	120	160

Table 2 for Line 3 Above

IF the combined ages at annuity starting date (see page 26) were . . .	THEN enter on line 3 . . .
110 or under	410
111–120	360
121–130	310
131–140	260
141 or older	210

Exercise 6

260 months

Exercise 7

Yes

Exercise 8

No

Exercise 9

Line 12a \$19,681

Line 12b \$17,053

Exercise 10

Line 7 - Wages

Exercise 11

\$9,965.40 85%

Exercise 12

Line 11a \$8,609

Line 11b \$8,002

Line 12a \$13,584

Line 12b \$12,216

Exercise 13

B

Exercise 14

Form W-4P

Give to the payer of the pension.

STUDENT NOTES

Lined area for student notes.

INTRODUCTION AND OBJECTIVES

Although few taxpayers will qualify for this credit, we still get questions about who qualifies for the credit. Even if a taxpayer meets the basic qualifications, he or she may not have a credit due to the income limits on their nontaxable social security, veterans benefits, or other excludable pension, annuity, or disability benefit.

In this lesson, you will learn about the credit for the elderly or the disabled. After completing this lesson you should be able to:

- Determine who is a qualified individual for the “credit for the elderly or disabled”
- Apply the income limits to the qualified individual
- Calculate the credit

WHO IS A QUALIFIED INDIVIDUAL FOR THE “CREDIT FOR THE ELDERLY OR THE DISABLED”?

Elderly individuals and individuals who are permanently and totally disabled may be able to claim a special credit on their tax returns if they are a U.S. citizen or resident.

To be eligible for the credit, an individual must be:

- At least 65 years old by the end of the year, or
- Under age 65, retired on permanent and total disability by the end of the year and did not reach mandatory retirement age before this year. They must also have received taxable disability income for this year.

Although physician statements are no longer required to be attached to the return, they must be completed and kept with the taxpayer’s records.

Certain work offered at qualified locations to persons with disabilities or with mental retardation is considered sheltered employment. Because a person has accepted sheltered employment is not proof of the person’s ability to engage in substantial gainful activity.

Exhibit 1 helps to determine if the taxpayer is a qualified individual for this credit.

Income Limits

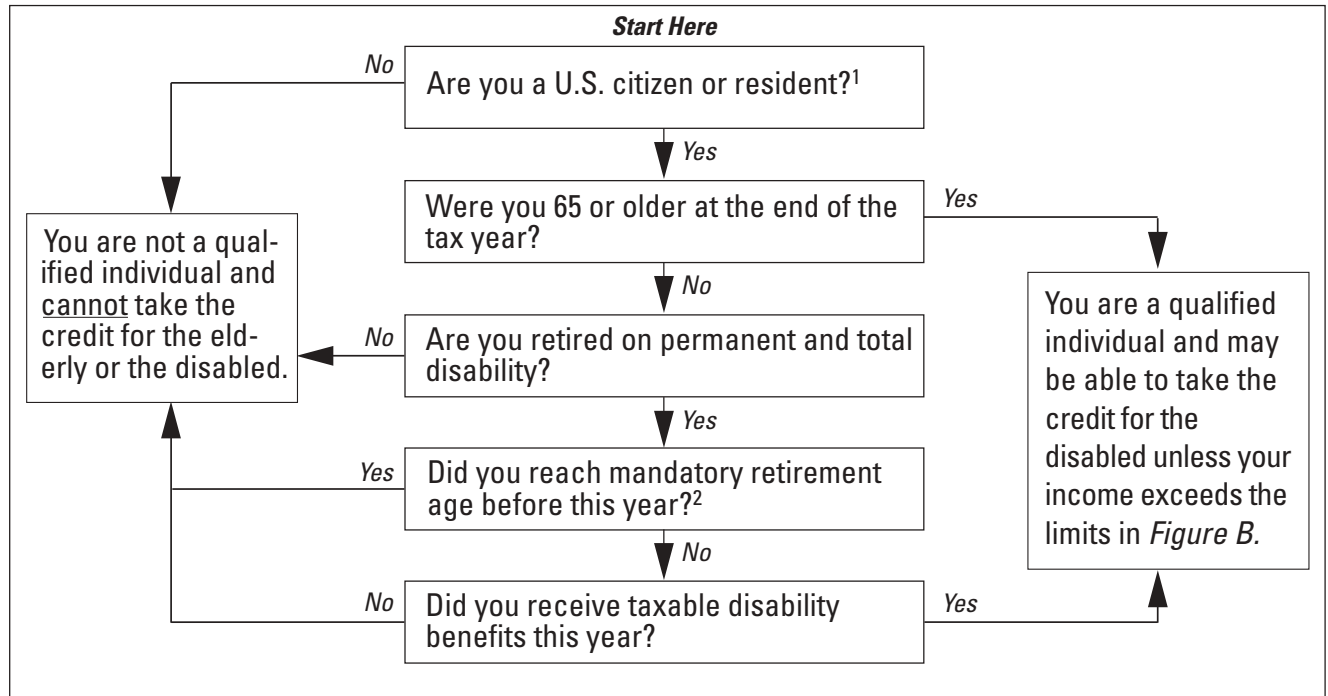
Taxpayers cannot exceed the income limits for their filing status (see **Exhibit 2**).

CALCULATE THE CREDIT

If the taxpayer is a qualified individual and meets the income limits, complete a Schedule 3 for 1040A filers or a Schedule R for 1040 filers. Schedule R (Form 1040) and Schedule 3 (Form 1040A) are nearly identical.

Example 1

John (000-00-9850) and Sarah Hillsdale are married and file a joint return. Their respective ages are 66 and 68. They received nontaxable social security benefits of \$4,500 in 2003. They had adjusted gross income (line 35, Form 1040) of \$13,000. Parts I and III of the Schedule R will be completed and the schedule attached to their Form 1040 for 2003. (Part II need not be completed since both are age 65 or older.) See Exhibits 3 and 4.



¹ If you were a nonresident alien at any time during the tax year and were married to a U.S. citizen or resident at the end of the tax year, see U.S. citizen or resident under *Qualified individual*. If you and your spouse both choose to be treated as U.S. residents, answer yes to this question.

² Mandatory retirement age is the age set by your employer at which you would have been required to retire, had you not become disabled.

Exhibit 2

Even if you qualify (see Figure A), you CANNOT take the credit if:

Your filing status is	AND your adjusted gross income (AGI)* is equal to or more than	OR your nontaxable social security or other nontaxable pension(s) is equal to or more than
Single, Head of household, or Qualifying widow(er) with dependent child	\$17,500	\$5,000
Married filing a joint return and both spouses qualify in <i>Figure A</i>	\$25,000	\$7,500
Married filing a joint return and only one spouse qualifies in <i>Figure A</i>	\$20,000	\$5,000
Married filing a separate return and you did not live with your spouse at any time during the year	\$12,500	\$3,750

*AGI is the amount on Form 1040A, line 21, or Form 1040, line 35.

**Schedule R
(Form 1040)**

Credit for the Elderly or the Disabled

OMB No. 1545-0074

2003

Attachment
Sequence No. **16**

Department of the Treasury
Internal Revenue Service (99)

▶ Attach to Form 1040. ▶ See instructions for Schedule R (Form 1040).

Name(s) shown on Form 1040

Your social security number

John and Sarah Hillsdale

000 00 9850

You may be able to take this credit and reduce your tax if by the end of 2003*:

- You were age 65 or older **or**
- You were under age 65, you retired on **permanent and total** disability, and you received taxable disability income.

If you were born on January 1, 1939, you are considered to be age 65 at the end of 2003. But you must also meet other tests. See page R-1.

TIP In most cases, the IRS can figure the credit for you. See page R-1.

Part I Check the Box for Your Filing Status and Age

If your filing status is: **And by the end of 2003:** **Check only one box:**

- Single,
Head of household, or
Qualifying widow(er)
- 1 You were 65 or older 1
 - 2 You were under 65 and you retired on permanent and total disability 2

- 3 Both spouses were 65 or older. 3
- 4 Both spouses were under 65, but only one spouse retired on permanent and total disability 4

- Married filing jointly
- 5 Both spouses were under 65, and both retired on permanent and total disability 5
 - 6 One spouse was 65 or older, and the other spouse was under 65 and retired on permanent and total disability 6
 - 7 One spouse was 65 or older, and the other spouse was under 65 and **not** retired on permanent and total disability. 7

- Married filing separately
- 8 You were 65 or older and you lived apart from your spouse for all of 2003 8
 - 9 You were under 65, you retired on permanent and total disability, and you lived apart from your spouse for all of 2003 9

Did you check box 1, 3, 7, or 8?

Yes → Skip Part II and complete Part III on back.

No → Complete Parts II and III.

Part II Statement of Permanent and Total Disability (Complete **only** if you checked box 2, 4, 5, 6, or 9 above.)

If: 1 You filed a physician's statement for this disability for 1983 or an earlier year, or you filed or got a statement for tax years after 1983 and your physician signed line B on the statement, **and**

2 Due to your continued disabled condition, you were unable to engage in any substantial gainful activity in 2003, check this box

- If you checked this box, you do not have to get another statement for 2003.
- If you **did not** check this box, have your physician complete the statement on page R-4. You **must** keep the statement for your records.

Part III Figure Your Credit

10 If you checked (in Part I):		Enter:			
Box 1, 2, 4, or 7		\$5,000	}	10	7,500 00
Box 3, 5, or 6		\$7,500			
Box 8 or 9		\$3,750			
Did you check box 2, 4, 5, 6, or 9 in Part I?		Yes →	You must complete line 11.		
		No →	Enter the amount from line 10 on line 12 and go to line 13.		
11 If you checked (in Part I):					
<ul style="list-style-type: none"> Box 6, add \$5,000 to the taxable disability income of the spouse who was under age 65. Enter the total. Box 2, 4, or 9, enter your taxable disability income. Box 5, add your taxable disability income to your spouse's taxable disability income. Enter the total. 			11		
TIP For more details on what to include on line 11, see page R-3.					
12 If you completed line 11, enter the smaller of line 10 or line 11; all others , enter the amount from line 10				12	7,500 00
13 Enter the following pensions, annuities, or disability income that you (and your spouse if filing a joint return) received in 2003.					
a Nontaxable part of social security benefits and Nontaxable part of railroad retirement benefits treated as social security (see page R-3).		13a	4,500 00		
b Nontaxable veterans' pensions and Any other pension, annuity, or disability benefit that is excluded from income under any other provision of law (see page R-3).		13b			
c Add lines 13a and 13b. (Even though these income items are not taxable, they must be included here to figure your credit.) If you did not receive any of the types of nontaxable income listed on line 13a or 13b, enter -0- on line 13c		13c	4,500 00		
14 Enter the amount from Form 1040, line 35		14	13,000 00		
15 If you checked (in Part I):		Enter:			
Box 1 or 2		\$7,500	}	15	10,000 00
Box 3, 4, 5, 6, or 7		\$10,000			
Box 8 or 9		\$5,000			
16 Subtract line 15 from line 14. If zero or less, enter -0-		16	3,000 00		
17 Enter one-half of line 16		17	1,500 00		
18 Add lines 13c and 17		18			6,000 00
19 Subtract line 18 from line 12. If zero or less, stop ; you cannot take the credit. Otherwise, go to line 20		19			1,500 00
20 Multiply line 19 by 15% (.15)		20			225 00
21 Enter the amount from Form 1040, line 43		21			
22 Add the amounts from Form 1040, lines 44 and 45, and enter the total		22			
23 Subtract line 22 from line 21		23			0 00
24 Credit for the elderly or the disabled. Enter the smaller of line 20 or line 23 here and on Form 1040, line 46		24			225 00

The credit for the elderly will be calculated automatically. The software will check age, income, and filing status to determine eligibility. However, it is extremely important to input Social Security Benefit income even if you know it is not taxable. Without this information the software may incorrectly calculate the credit.

▶▶ SUMMING UP THIS LESSON ◀◀

- ▶ The credit for the elderly or disabled is a nonrefundable credit which allows a taxpayer to reduce their liability.
- ▶ Due to the income limitations, very few taxpayers are eligible to receive this credit.
- ▶ The credit is based on filing status, age, and income.
- ▶ The credit is calculated and reported on Form 1040, Schedule R, or Form 1040A, Schedule 3.

PENSION EARNER COMPREHENSIVE PROBLEMS

INTRODUCTION

In this section, you will complete tax returns for several common pension earner scenarios often encountered at volunteer assistance sites. This will be valuable practice as you prepare to help taxpayers. Although answers to each of the problems are shown at the end of this section, you should try to complete the blank forms for each problem before referring to its answers.

After completing this section, you will be able to:

- accurately complete a basic tax return with some advanced topics.

PROBLEM 1

Stuart Morehouse (born July 2, 1935) and Donna Morehouse (born December 28, 1950) are married and will file a joint tax return. Neither one wishes to contribute to the presidential campaign fund.


Stuart is retired and received a pension from his former employer as well as social security benefits.

Donna is a secretary and received a Form W-2. She made a \$900 payment to her 2003 traditional IRA on January 15, 2004. Stuart and Donna do not want to name a third party designee.

If they are entitled to a refund they would like the check mailed to them. Their address and social security numbers are correct on their income statements.

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Form W-2, First Bank of Hillsdale

a Control number 8162834		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number XX-XXXXXXX				1 Wages, tips, other compensation \$18,526.00		2 Federal income tax withheld \$2,423.00	
c Employer's name, address, and ZIP code First Bank of Hillsdale 1000 Main St. Your City, State, Zip Code				3 Social security wages \$18,526.00		4 Social security tax withheld \$1,149.00	
				5 Medicare wages and tips \$18,526.00		6 Medicare tax withheld \$269.00	
				7 Social security tips		8 Allocated tips	
d Employee's social security number				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name Donna Morehouse 10923 Fullerton Your City, State, Zip Code				11 Nonqualified plans		12a See instructions for box 12	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code							
15 State Employer's state ID number XX-XXXXXXX		16 State wages, tips, etc. \$18,526.00		17 State income tax \$984.00		18 Local wages, tips, etc.	
						19 Local income tax	
						20 Locality name	

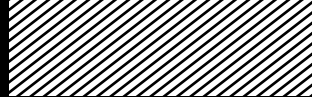
Form **W-2** Wage and Tax Statement

2003

Department of the Treasury—Internal Revenue Service

Copy B To Be Filed with Employee's FEDERAL Tax Return.
This information is being furnished to the Internal Revenue Service.

PENSION EARNER COMPREHENSIVE PROBLEMS



Form 1099, Social Security Benefit Statement

FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT			
2003 • PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME. • SEE THE REVERSE FOR MORE INFORMATION.			
Box 1. Name Stuart Morehouse		Box 2. Beneficiary's Social Security Number xxx-xx-xxxx	
Box 3. Benefits Paid in 2003 10,499	Box 4. Benefits Repaid to SSA in 2003	Box 5. Net Benefits for 2003 (Box 3 minus Box 4) 10,499	
DESCRIPTION OF AMOUNT IN BOX 3		DESCRIPTION OF AMOUNT IN BOX 4	
(Large empty area for description of amounts)		Box 6. Voluntary Federal Income Tax Withholding	
		Box 7. Address 10923 Fullerton Your City, State, Zip Code	
		Box 8. Claim Number (Use this number if you need to contact SSA.)	
Form SSA-1099-SM (1-2004)		DO NOT RETURN THIS FORM TO SSA OR IRS	

Draft as of 09/01/2003

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Form 1099-R, AB Industries

<input type="checkbox"/> CORRECTED (if checked)				
PAYER'S name, street address, city, state, and ZIP code AB Industries 346 North 3rd Terrace Your City, State, Zip Code		1 Gross distribution \$ 13,567.00	OMB No. 1545-0119 2003 Form 1099-R	Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return. This information is being furnished to the Internal Revenue Service.
		2a Taxable amount \$ 13,567.00			2b Taxable amount not determined ☐ Total distribution ☐
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	3 Capital gain (included in box 2a) \$	4 Federal income tax withheld \$ 1,357.00	
RECIPIENT'S name Stuart Morehouse Street address (including apt. no.) 10923 Fullerton City, state, and ZIP code Your City, State, Zip Code		5 Employee contributions or insurance premiums \$	6 Net unrealized appreciation in employer's securities \$	
		7 Distribution code(s) 7	8 Other \$ %	
		9a Your percentage of total distribution %	9b Total employee contributions \$	
Account number (optional)	10 State tax withheld \$ \$	11 State/Payer's state no. \$	12 State distribution \$ \$	
	13 Local tax withheld \$ \$	14 Name of locality	15 Local distribution \$ \$	

Form 1099-R

Department of the Treasury - Internal Revenue Service

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Form 1099-INT, Fisk Bank

<input type="checkbox"/> CORRECTED (if checked)				2003		Interest Income
PAYER'S name, street address, city, state, ZIP code, and telephone no. Fisk Bank 4010 North Second St. Your City, State, Zip Code		Payer's RTN (optional)		OMB No. 1545-0112 Form 1099-INT		
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	1 Interest income not included in box 3 \$ 235.00		Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.		
RECIPIENT'S name Stuart Morehouse Street address (including apt. no.) 10923 Fullerton City, state, and ZIP code Your City, State, Zip Code		2 Early withdrawal penalty \$	3 Interest on U.S. Savings Bonds and Treas. obligations \$			
Account number (optional)		4 Federal income tax withheld \$	5 Investment expenses \$			
		6 Foreign tax paid \$	7 Foreign country or U.S. possession			
Form 1099-INT		(keep for your records)		Department of the Treasury - Internal Revenue Service		

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Form 1040A, page 1

Form **1040A** Department of the Treasury—Internal Revenue Service **U.S. Individual Income Tax Return 2003** IRS Use Only—Do not write or staple in this space.

Label
(See page 21.)

L A B E L H E R E	Your first name and initial	Last name		
	If a joint return, spouse's first name and initial	Last name		
	Home address (number and street). If you have a P.O. box, see page 22.		Apt. no.	
	City, town or post office, state, and ZIP code. If you have a foreign address, see page 22.			

OMB No. 1545-0085

Your social security number

Spouse's social security number

Use the IRS label.
Otherwise, please print or type.

▲ Important! ▲
You **must** enter your SSN(s) above.

Presidential Election Campaign
(See page 22.)

Note. Checking "Yes" will not change your tax or reduce your refund.
Do you, or your spouse if filing a joint return, want \$3 to go to this fund? . . .

You Yes No Spouse Yes No

Filing status
Check only one box.

- 1 Single
- 2 Married filing jointly (even if only one had income)
- 3 Married filing separately. Enter spouse's SSN above and full name here. ▶
- 4 Head of household (with qualifying person). (See page 23.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
- 5 Qualifying widow(er) with dependent child (See page 24.)

Exemptions

6a **Yourself.** If your parent (or someone else) can claim you as a dependent on his or her tax return, **do not** check box 6a.

No. of boxes checked on 6a and 6b _____

b **Spouse**

c **Dependents:**

If more than six dependents, see page 24.

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>

No. of children on 6c who:
• lived with you _____

• did not live with you due to divorce or separation (see page 26) _____

Dependents on 6c not entered above _____

Add numbers on lines above

d Total number of exemptions claimed.

Income

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

If you did not get a W-2, see page 27.

Enclose, but do not attach, any payment.

7 Wages, salaries, tips, etc. Attach Form(s) W-2.	7	
8a Taxable interest. Attach Schedule 1 if required.	8a	
b Tax-exempt interest. Do not include on line 8a.	8b	
9a Ordinary dividends. Attach Schedule 1 if required.	9a	
b Qualified dividends (see page XX).	9b	
10a Capital gain distributions (see page 27).	10a	
b Post-May 5 capital gain distributions (see page 27).	10b	
11a IRA distributions.	11a	11b Taxable amount (see page 27).
		11b
12a Pensions and annuities.	12a	12b Taxable amount (see page 28).
		12b
13 Unemployment compensation and Alaska Permanent Fund dividends.	13	
14a Social security benefits.	14a	14b Taxable amount (see page 30).
		14b
15 Add lines 7 through 14b (far right column). This is your total income .	▶ 15	
Adjusted gross income		
16 Educator expenses (see page 30).	16	
17 IRA deduction (see page 30).	17	
18 Student loan interest deduction (see page 33).	18	
19 Tuition and fees deduction (see page 33).	19	
20 Add lines 16 through 19. These are your total adjustments .	20	
21 Subtract line 20 from line 15. This is your adjusted gross income .	▶ 21	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 57. Cat. No. 11327A Form **1040A** (2003)

PENSION EARNER COMPREHENSIVE PROBLEMS

Form 1040A (2003)		Page 2		
Tax, credits, and payments Standard Deduction for— <ul style="list-style-type: none"> • People who checked any box on line 23a or 23b or who can be claimed as a dependent, see page 34. • All others: <ul style="list-style-type: none"> Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000 	22 Enter the amount from line 21 (adjusted gross income).	22		
	23a Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind } checked ▶ 23a <input type="checkbox"/>	b If you are married filing separately and your spouse itemizes deductions, see page 34 and check here ▶ 23b <input type="checkbox"/>		
	24 Enter your standard deduction (see left margin).	24		
	25 Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25		
	26 Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26		
	27 Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income . ▶ 27	27		
	28 Tax , including any alternative minimum tax (see page 35).	28		
	29 Credit for child and dependent care expenses. Attach Schedule 2.	29		
	30 Credit for the elderly or the disabled. Attach Schedule 3.	30		
	31 Education credits. Attach Form 8863.	31		
	32 Retirement savings contributions credit. Attach Form 8880.	32		
	33 Child tax credit (see page 38).	33		
	34 Adoption credit. Attach Form 8839.	34		
	35 Add lines 29 through 34. These are your total credits .	35		
	36 Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36		
	37 Advance earned income credit payments from Form(s) W-2.	37		
	38 Add lines 36 and 37. This is your total tax . ▶ 38	38		
	39 Federal income tax withheld from Forms W-2 and 1099.	39		
	40 2003 estimated tax payments and amount applied from 2002 return.	40		
	41 Earned income credit (EIC) .	41		
42 Additional child tax credit. Attach Form 8812.	42			
43 Add lines 39 through 42. These are your total payments . ▶ 43	43			
Refund	44 If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44		
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	45a Amount of line 44 you want refunded to you . ▶ 45a	45a		
	▶ b Routing number <input type="text"/> ▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings			
	▶ d Account number <input type="text"/>			
	46 Amount of line 44 you want applied to your 2004 estimated tax .	46		
Amount you owe	47 Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53. ▶ 47	47		
	48 Estimated tax penalty (see page 53).	48		
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes . Complete the following. <input type="checkbox"/> No			
	Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶ <input type="text"/>	
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.			
Joint return? See page 22. Keep a copy for your records.	Your signature	Date	Your occupation	
	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	
Paid preparer's use only	Preparer's signature ▶	Date	Check if self-employed <input type="checkbox"/>	
	Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Preparer's SSN or PTIN	
		Phone no. ()		

PENSION EARNER COMPREHENSIVE PROBLEMS

Form 1040A, Social Security Benefits Worksheet

Before you begin:

- ✓ Complete Form 1040A, lines 16 and 17, if they apply to you.
- ✓ If you are married filing separately and you **lived apart** from your spouse for all of 2003, enter "D" to the right of the word "benefits" on line 14a.
- ✓ Be sure you have read the **Exception** on page 27 to see if you can use this worksheet instead of a publication to find out if any of your benefits are taxable.



<p>1. Enter the total amount from box 5 of all your Forms SSA-1099 and Forms RRB-1099 1. <input style="width: 100px;" type="text"/></p> <p>2. Enter one-half of line 1 2. <input style="width: 100px;" type="text"/></p> <p>3. Enter the total of the amounts from Form 1040A, lines 7, 8a, 9a, 10a, 11b, 12b, and 13 3. <input style="width: 100px;" type="text"/></p> <p>4. Enter the amount, if any, from Form 1040A, line 8b 4. <input style="width: 100px;" type="text"/></p> <p>5. Add lines 2, 3, and 4 5. <input style="width: 100px;" type="text"/></p> <p>6. Enter the total of the amounts from Form 1040A, lines 16 and 17 6. <input style="width: 100px;" type="text"/></p> <p>7. Is the amount on line 6 less than the amount on line 5?</p> <p><input type="checkbox"/> No. None of your social security benefits are taxable.</p> <p><input type="checkbox"/> Yes. Subtract line 6 from line 5 7. <input style="width: 100px;" type="text"/></p> <p>8. If:</p> <ul style="list-style-type: none"> • Married filing jointly, enter \$32,000. • Single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003, enter \$25,000. • Married filing separately and you lived with your spouse at any time in 2003, skip lines 8 through 15; multiply line 7 by 85% (.85) and enter the result on line 16. Then go to line 17. <p style="text-align: right; margin-right: 20px;">} 8. <input style="width: 100px;" type="text"/></p> <p>9. Is the amount on line 8 less than the amount on line 7?</p> <p><input type="checkbox"/> No. None of your social security benefits are taxable. You do not have to enter any amount on line 14a or 14b of Form 1040A. But if you are married filing separately and you lived apart from your spouse for all of 2003, enter -0- on line 14b. Be sure you entered "D" to the right of the word "benefits" on line 14a.</p> <p><input type="checkbox"/> Yes. Subtract line 8 from line 7 9. <input style="width: 100px;" type="text"/></p> <p>10. Enter: \$12,000 if married filing jointly; \$9,000 if single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003 10. <input style="width: 100px;" type="text"/></p> <p>11. Subtract line 10 from line 9. If zero or less, enter -0- 11. <input style="width: 100px;" type="text"/></p> <p>12. Enter the smaller of line 9 or line 10 12. <input style="width: 100px;" type="text"/></p> <p>13. Enter one-half of line 12 13. <input style="width: 100px;" type="text"/></p> <p>14. Enter the smaller of line 2 or line 13 14. <input style="width: 100px;" type="text"/></p> <p>15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0- 15. <input style="width: 100px;" type="text"/></p> <p>16. Add lines 14 and 15 16. <input style="width: 100px;" type="text"/></p> <p>17. Multiply line 1 by 85% (.85) 17. <input style="width: 100px;" type="text"/></p> <p>18. Taxable social security benefits. Enter the smaller of line 16 or line 17 18. <input style="width: 100px;" type="text"/></p> <ul style="list-style-type: none"> • Enter the amount from line 1 above on Form 1040A, line 14a. • Enter the amount from line 18 above on Form 1040A, line 14b.
--



If part of your benefits are taxable for 2003 **and** they include benefits paid in 2003 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

PENSION EARNER COMPREHENSIVE PROBLEMS

PROBLEM 2

Jay Lehigh (born February 10, 1930) and Sandra Lehigh (November 27, 1935) are married and will file a joint return. They both wish to contribute to the presidential election campaign. Jay's social security number and address are correct as shown on his income statements. Sandra's social security number is xxx-xx-xxxx. Jay and Sandra do not want to name a third party designee.

Jay is retired, receives a pension from his former employer, and receives social security benefits.

Sandra is a housewife. She provided day care for her 3 grandchildren. The state paid her for this service and issued her a Form 1099-MISC. She incurred no expenses.

Jay and Sandra sold some stock in 2003 and provided the following information: The principal business code for child care is 624410.

Company	# of Shares	Purchase Date	Per Share Basis	Sale Date	Per Share Sales Price
ABC Inc	100	12/01/1985	24.00	07/15/2003	51.24
XYZ Inc	200	12/20/1987	28.50	11/14/2003	53.98

2003 Form 1099-R, CD Associates

PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution		OMB No. 1545-0119		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
CD Associates 345 East 100th St. Your City, State, Zip Code		\$ 18,945.00		2003		
		2a Taxable amount		Form 1099-R		Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return.
		\$ 18,945.00		2b Taxable amount not determined <input type="checkbox"/> Total distribution <input type="checkbox"/>		
PAYER'S Federal identification number	RECIPIENT'S identification number	3 Capital gain (included in box 2a)		4 Federal income tax withheld		This information is being furnished to the Internal Revenue Service.
xx-xxxxxxx	xxx-xx-xxxx	\$		\$ 1,895.00		
RECIPIENT'S name		5 Employee contributions or insurance premiums		6 Net unrealized appreciation in employer's securities		
Jay Lehigh		\$		\$		
Street address (including apt. no.)		7 Distribution code(s)		8 Other		
99 Danville Ave		7		\$ %		
City, state, and ZIP code		9a Your percentage of total distribution %		9b Total employee contributions \$		
Your City, State, Zip Code						
Account number (optional)		10 State tax withheld		11 State/Payer's state no.		12 State distribution
		\$				\$
		\$				\$
		13 Local tax withheld		14 Name of locality		15 Local distribution
		\$				\$
		\$				\$

Form 1099-R

Department of the Treasury - Internal Revenue Service

Comprehensive Problems

CP-9

PENSION EARNER

PENSION EARNER COMPREHENSIVE PROBLEMS

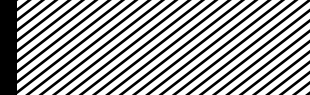
Form 1099, Social Security Benefit Statement

FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT		
2003 : PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME. : SEE THE REVERSE FOR MORE INFORMATION.		
Box 1. Name Jay Lehigh	Box 2. Beneficiary's Social Security Number XXX-XX-XXXX	
Box 3. Benefits Paid in 2003 \$14,263.00	Box 4. Benefits Repaid to SSA in 2003	Box 5. Net Benefits for 2003 (Box 3 minus Box 4) \$14,263.00
DESCRIPTION OF AMOUNT IN BOX 3		DESCRIPTION OF AMOUNT IN BOX 4
		Box 6. Voluntary Federal Income Tax Withholding
		Box 7. Address 99 Danville Your City, State, Zip Code
		Box 8. Claim Number (Use this number if you need to contact SSA.)

Form SSA-1099-SM (1-2004) **DO NOT RETURN THIS FORM TO SSA OR IRS**

Draft as of
09/01/2003

PENSION EARNER COMPREHENSIVE PROBLEMS



Reserved for Form 1099-MISC

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0115		Miscellaneous Income
PAYER'S name, street address, city, state, ZIP code, and telephone no. Division of Social Services 1000 N. 16th St. Your City, State, Zip Code		1 Rents \$	2 Royalties \$		2003
		3 Other income \$	4 Federal income tax withheld \$	Form 1099-MISC
		5 Fishing boat proceeds \$	6 Medical and health care payments \$	Copy B For Recipient
PAYER'S Federal identification number XX-XXXXXXX	RECIPIENT'S identification number XXX-XX-XXXX	7 Nonemployee compensation \$ 6,000.00	8 Substitute payments in lieu of dividends or interest \$	This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
RECIPIENT'S name Sandra Lehigh		9 Payer made direct sales of \$5,000 or more of consumer products to a buyer (recipient) for resale <input type="checkbox"/>	10 Crop insurance proceeds \$	
Street address (including apt. no.) 99 Danville Ave		11	12	
City, state, and ZIP code Your City, State, Zip Code		13 Excess golden parachute payments \$	14 Gross proceeds paid to an attorney \$	
Account number (optional)		15	16 State tax withheld \$	17 State/Payer's state no.
		18 State income \$	\$	\$

Form **1099-MISC**

(keep for your records)

Department of the Treasury - Internal Revenue Service

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Form 1040, page 1

Form 1040	Department of the Treasury—Internal Revenue Service U.S. Individual Income Tax Return 2003	IRS Use Only—Do not write or staple in this space. OMB No. 1545-0074																																																																		
Label (See instructions on page 21.) Use the IRS label. Otherwise, please print or type. Presidential Election Campaign (See page 21.)	For the year Jan. 1–Dec. 31, 2003, or other tax year beginning _____, 2003, ending _____, 20																																																																			
	Your first name and initial _____ Last name _____	Your social security number _____																																																																		
	If a joint return, spouse's first name and initial _____ Last name _____	Spouse's social security number _____																																																																		
	Home address (number and street). If you have a P.O. box, see page 21. Apt. no. _____ City, town or post office, state, and ZIP code. If you have a foreign address, see page 21.																																																																			
Filing Status Check only one box.	Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if filing a joint return, want \$3 to go to this fund?																																																																			
	You <input type="checkbox"/> Yes <input type="checkbox"/> No Spouse <input type="checkbox"/> Yes <input type="checkbox"/> No																																																																			
Exemptions If more than five dependents, see page 22.	1 <input type="checkbox"/> Single 2 <input type="checkbox"/> Married filing jointly (even if only one had income) 3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here.																																																																			
	4 <input type="checkbox"/> Head of household (with qualifying person). (See page 21.) If the qualifying person is a child but not your dependent, enter this child's name here. 5 <input type="checkbox"/> Qualifying widow(er) with dependent child. (See page 21.)																																																																			
	6a <input type="checkbox"/> Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a. b <input type="checkbox"/> Spouse c Dependents: <table border="1" style="width:100%; border-collapse: collapse;"> <thead> <tr> <th style="width:30%;">(1) First name</th> <th style="width:30%;">Last name</th> <th style="width:15%;">(2) Dependent's social security number</th> <th style="width:15%;">(3) Dependent's relationship to you</th> <th style="width:10%;">(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 22)</th> </tr> </thead> <tbody> <tr><td> </td><td> </td><td> </td><td> </td><td><input type="checkbox"/></td></tr> <tr><td> </td><td> </td><td> </td><td> </td><td><input type="checkbox"/></td></tr> <tr><td> </td><td> </td><td> </td><td> </td><td><input type="checkbox"/></td></tr> <tr><td> </td><td> </td><td> </td><td> </td><td><input type="checkbox"/></td></tr> <tr><td> </td><td> </td><td> </td><td> </td><td><input type="checkbox"/></td></tr> </tbody> </table> d Total number of exemptions claimed _____		(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 22)					<input type="checkbox"/>					<input type="checkbox"/>					<input type="checkbox"/>					<input type="checkbox"/>					<input type="checkbox"/>																																				
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Income Attach Forms W-2 and W-2G here. Also attach Form(s) 1099-R if tax was withheld. If you did not get a W-2, see page 23. Enclose, but do not attach, any payment. Also, please use Form 1040-V.	<table border="1" style="width:100%; border-collapse: collapse;"> <tr><td>7 Wages, salaries, tips, etc. Attach Form(s) W-2</td><td>7</td><td> </td></tr> <tr><td>8a Taxable interest. Attach Schedule B if required</td><td>8a</td><td> </td></tr> <tr><td>b Tax-exempt interest. Do not include on line 8a</td><td>8b</td><td> </td></tr> <tr><td>9a Ordinary dividends. Attach Schedule B if required</td><td>9a</td><td> </td></tr> <tr><td>b Qualified dividends (see page 25)</td><td>9b</td><td> </td></tr> <tr><td>10 Taxable refunds, credits, or offsets of state and local income taxes (see page 25)</td><td>10</td><td> </td></tr> <tr><td>11 Alimony received</td><td>11</td><td> </td></tr> <tr><td>12 Business income or (loss). Attach Schedule C or C-EZ</td><td>12</td><td> </td></tr> <tr><td>13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/></td><td>13a</td><td> </td></tr> <tr><td>b If box on 13a is checked, enter post-May 5 capital gain distributions</td><td>13b</td><td> </td></tr> <tr><td>14 Other gains or (losses). Attach Form 4797</td><td>14</td><td> </td></tr> <tr><td>15a IRA distributions</td><td>15a</td><td> </td></tr> <tr><td>b Taxable amount (see page 25)</td><td>15b</td><td> </td></tr> <tr><td>16a Pensions and annuities</td><td>16a</td><td> </td></tr> <tr><td>b Taxable amount (see page 25)</td><td>16b</td><td> </td></tr> <tr><td>17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E</td><td>17</td><td> </td></tr> <tr><td>18 Farm income or (loss). Attach Schedule F</td><td>18</td><td> </td></tr> <tr><td>19 Unemployment compensation</td><td>19</td><td> </td></tr> <tr><td>20a Social security benefits</td><td>20a</td><td> </td></tr> <tr><td>b Taxable amount (see page 27)</td><td>20b</td><td> </td></tr> <tr><td>21 Other income. List type and amount (see page 29)</td><td>21</td><td> </td></tr> <tr><td>22 Add the amounts in the far right column for lines 7 through 21. This is your total income</td><td>22</td><td> </td></tr> </table>		7 Wages, salaries, tips, etc. Attach Form(s) W-2	7		8a Taxable interest. Attach Schedule B if required	8a		b Tax-exempt interest. Do not include on line 8a	8b		9a Ordinary dividends. Attach Schedule B if required	9a		b Qualified dividends (see page 25)	9b		10 Taxable refunds, credits, or offsets of state and local income taxes (see page 25)	10		11 Alimony received	11		12 Business income or (loss). Attach Schedule C or C-EZ	12		13a Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13a		b If box on 13a is checked, enter post-May 5 capital gain distributions	13b		14 Other gains or (losses). Attach Form 4797	14		15a IRA distributions	15a		b Taxable amount (see page 25)	15b		16a Pensions and annuities	16a		b Taxable amount (see page 25)	16b		17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17		18 Farm income or (loss). Attach Schedule F	18		19 Unemployment compensation	19		20a Social security benefits	20a		b Taxable amount (see page 27)	20b		21 Other income. List type and amount (see page 29)	21		22 Add the amounts in the far right column for lines 7 through 21. This is your total income	22	
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Cat. No. 11320B		Form 1040 (2003)																																																																		

PENSION EARNER COMPREHENSIVE PROBLEMS

Form 1040 (2003)		Page 2				
<p>Tax and Credits</p> <p>Standard Deduction for—</p> <ul style="list-style-type: none"> • People who checked any box on line 36a or 36b or who can be claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000 	<p>35 Amount from line 34 (adjusted gross income)</p> <p>36a Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind. } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind. } checked ▶ 36a <input type="checkbox"/></p> <p>b If you are married filing separately and your spouse itemizes deductions, or you were a dual-status alien, see page 34 and check here ▶ 36b <input type="checkbox"/></p> <p>37 Itemized deductions (from Schedule A) or your standard deduction (see left margin)</p> <p>38 Subtract line 37 from line 35</p> <p>39 If line 35 is \$104,625 or less, multiply \$3,050 by the total number of exemptions claimed on line 6d. If line 35 is over \$104,625, see the worksheet on page 35</p> <p>40 Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-</p> <p>41 Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972</p> <p>42 Alternative minimum tax (see page 37). Attach Form 6251</p> <p>43 Add lines 41 and 42 ▶</p> <p>44 Foreign tax credit. Attach Form 1116 if required 44</p> <p>45 Credit for child and dependent care expenses. Attach Form 2441 45</p> <p>46 Credit for the elderly or the disabled. Attach Schedule R 46</p> <p>47 Education credits. Attach Form 8863 47</p> <p>48 Retirement savings contributions credit. Attach Form 8880 48</p> <p>49 Child tax credit (see page 39) 49</p> <p>50 Adoption credit. Attach Form 8839 50</p> <p>51 Credits from: a <input type="checkbox"/> Form 8396 b <input type="checkbox"/> Form 8859 51</p> <p>52 Other credits. Check applicable box(es): a <input type="checkbox"/> Form 3800 b <input type="checkbox"/> Form 8801 c <input type="checkbox"/> Specify 52</p> <p>53 Add lines 44 through 52. These are your total credits 53</p> <p>54 Subtract line 53 from line 43. If line 53 is more than line 43, enter -0- ▶</p>	<p>35</p> <p>37</p> <p>38</p> <p>39</p> <p>40</p> <p>41</p> <p>42</p> <p>43</p> <p>44</p> <p>45</p> <p>46</p> <p>47</p> <p>48</p> <p>49</p> <p>50</p> <p>51</p> <p>52</p> <p>53</p> <p>54</p>				
	<p>Other Taxes</p>	<p>55 Self-employment tax. Attach Schedule SE</p> <p>56 Social security and Medicare tax on tip income not reported to employer. Attach Form 4137</p> <p>57 Tax on qualified plans, including IRAs, and other tax-favored accounts. Attach Form 5329 if required</p> <p>58 Advance earned income credit payments from Form(s) W-2</p> <p>59 Household employment taxes. Attach Schedule H</p> <p>60 Add lines 54 through 59. This is your total tax ▶</p>	<p>55</p> <p>56</p> <p>57</p> <p>58</p> <p>59</p> <p>60</p>			
		<p>Payments</p> <p>If you have a qualifying child, attach Schedule EIC.</p>	<p>61 Federal income tax withheld from Forms W-2 and 1099 61</p> <p>62 2003 estimated tax payments and amount applied from 2002 return 62</p> <p>63 Earned income credit (EIC) 63</p> <p>64 Excess social security and tier 1 RRTA tax withheld (see page 56) 64</p> <p>65 Additional child tax credit. Attach Form 8812 65</p> <p>66 Amount paid with request for extension to file (see page 56) 66</p> <p>67 Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885 67</p> <p>68 Add lines 61 through 67. These are your total payments ▶</p>	<p>61</p> <p>62</p> <p>63</p> <p>64</p> <p>65</p> <p>66</p> <p>67</p> <p>68</p>		
			<p>Refund</p> <p>Direct deposit? See page 56 and fill in 70b, 70c, and 70d.</p>	<p>69 If line 68 is more than line 60, subtract line 60 from line 68. This is the amount you overpaid 69</p> <p>70a Amount of line 69 you want refunded to you ▶ 70a</p> <p>b Routing number <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> ▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings</p> <p>d Account number <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/></p> <p>71 Amount of line 69 you want applied to your 2004 estimated tax ▶ 71</p>	<p>69</p> <p>70a</p> <p>71</p>	
				<p>72 Amount you owe. Subtract line 68 from line 60. For details on how to pay, see page 57 ▶</p> <p>73 Estimated tax penalty (see page 57) 73</p>	<p>72</p> <p>73</p>	
				<p>Third Party Designee</p> <p>Designee's name <input type="text"/> Phone no. <input type="text"/> (<input type="text"/>) Personal identification number (PIN) <input type="text"/></p> <p>Sign Here</p> <p>Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.</p> <p>Your signature <input type="text"/> Date <input type="text"/> Your occupation <input type="text"/> Daytime phone number (<input type="text"/>)</p> <p>Spouse's signature. If a joint return, both must sign. <input type="text"/> Date <input type="text"/> Spouse's occupation <input type="text"/></p> <p>Paid Preparer's Use Only</p> <p>Preparer's signature <input type="text"/> Date <input type="text"/> Check if self-employed <input type="checkbox"/></p> <p>Firm's name (or yours if self-employed), address, and ZIP code <input type="text"/> EIN <input type="text"/></p> <p>Phone no. (<input type="text"/>) <input type="text"/></p>	<p>Do you want to allow another person to discuss this return with the IRS (see page 58)? <input type="checkbox"/> Yes. Complete the following. <input type="checkbox"/> No</p>	<p>72</p> <p>73</p>
					<p>72</p> <p>73</p>	

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Schedule C-EZ

**SCHEDULE C-EZ
(Form 1040)**

Department of the Treasury
Internal Revenue Service

Net Profit From Business
(Sole Proprietorship)

► Partnerships, joint ventures, etc., must file Form 1065 or 1065-B.
► Attach to Form 1040 or 1041. ► See instructions on back.

OMB No. 1545-0074

2003

Attachment
Sequence No. **09A**

Name of proprietor

Social security number (SSN)

Part I General Information

**You May Use
Schedule C-EZ
Instead of
Schedule C
Only If You:**

- Had business expenses of \$2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file Form 4562, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-4 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service

B Enter code from pages C-7, 8, & 9

C Business name. If no separate business name, leave blank.

D Employer ID number (EIN), if any

E Business address (including suite or room no.). Address not required if same as on Form 1040, page 1.

City, town or post office, state, and ZIP code

Part II Figure Your Net Profit

<p>1 Gross receipts. Caution. If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employees in the instructions for Schedule C, line 1, on page C-3 and check here <input type="checkbox"/></p>	1			
<p>2 Total expenses (see instructions). If more than \$2,500, you must use Schedule C</p>	2			
<p>3 Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12, and also on Schedule SE, line 2. (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)</p>	3			

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

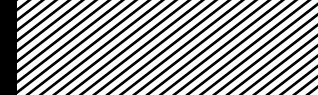
- 4** When did you place your vehicle in service for business purposes? (month, day, year) ►/...../.....
- 5** Of the total number of miles you drove your vehicle during 2003, enter the number of miles you used your vehicle for:
- a** Business **b** Commuting **c** Other
- 6** Do you (or your spouse) have another vehicle available for personal use? **Yes** **No**
- 7** Was your vehicle available for personal use during off-duty hours? **Yes** **No**
- 8a** Do you have evidence to support your deduction? **Yes** **No**
- b** If "Yes," is the evidence written? **Yes** **No**

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 14374D

Schedule C-EZ (Form 1040) 2003

PENSION EARNER COMPREHENSIVE PROBLEMS



2003 Form 1040 Schedule SE

SCHEDULE SE (Form 1040) <small>Department of the Treasury Internal Revenue Service</small>	Self-Employment Tax ▶ Attach to Form 1040. ▶ See Instructions for Schedule SE (Form 1040).	OMB No. 1545-0074 2003 Attachment Sequence No. 17
Name of person with self-employment income (as shown on Form 1040)		Social security number of person with self-employment income ▶

Who Must File Schedule SE

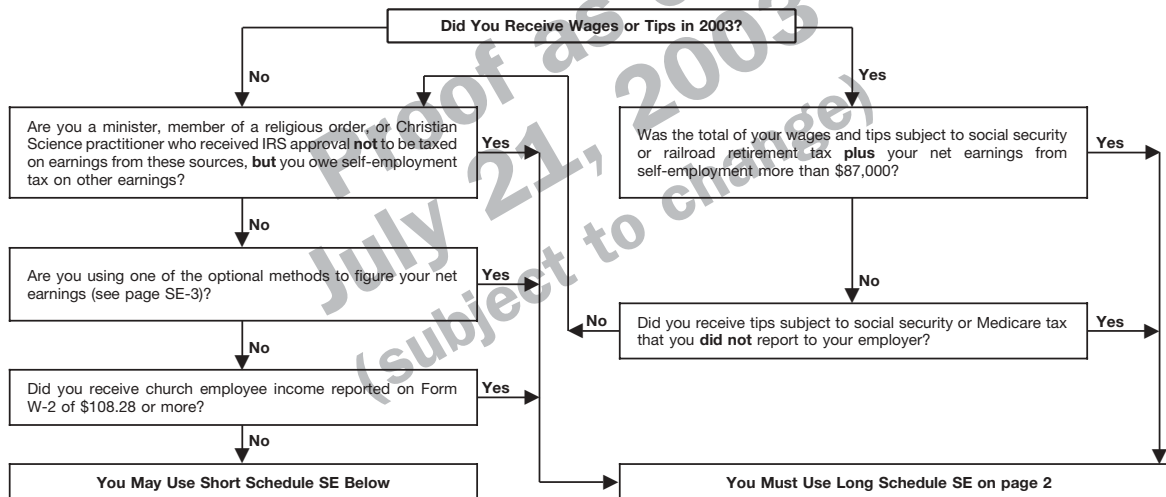
You must file Schedule SE if:

- You had net earnings from self-employment from **other than** church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of \$400 or more **or**
- You had church employee income of \$108.28 or more. Income from services you performed as a minister or a member of a religious order **is not** church employee income (see page SE-1).

Note. Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE (see page SE-3).

Exception. If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner **and** you filed Form 4361 and received IRS approval not to be taxed on those earnings, **do not** file Schedule SE. Instead, write "Exempt-Form 4361" on Form 1040, line 55.

May I Use Short Schedule SE or Must I Use Long Schedule SE?



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

<p>1 Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a</p> <p>2 Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report</p> <p>3 Combine lines 1 and 2</p> <p>4 Net earnings from self-employment. Multiply line 3 by 92.35% (.9235). If less than \$400, do not file this schedule; you do not owe self-employment tax ▶</p> <p>5 Self-employment tax. If the amount on line 4 is:</p> <ul style="list-style-type: none"> • \$87,000 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 55. • More than \$87,000, multiply line 4 by 2.9% (.029). Then, add \$10,788.00 to the result. Enter the total here and on Form 1040, line 55. <p>6 Deduction for one-half of self-employment tax. Multiply line 5 by 50% (.5). Enter the result here and on Form 1040, line 28</p>	<table border="1" style="width:100%; border-collapse: collapse;"> <tr><td style="text-align: center;">1</td><td style="width: 40px;"></td><td style="width: 40px;"></td></tr> <tr><td style="text-align: center;">2</td><td></td><td></td></tr> <tr><td style="text-align: center;">3</td><td></td><td></td></tr> <tr><td style="text-align: center;">4</td><td></td><td></td></tr> <tr><td style="text-align: center;">5</td><td></td><td></td></tr> <tr><td style="text-align: center;">6</td><td></td><td></td></tr> </table>	1			2			3			4			5			6		
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PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Schedule D, page 1

SCHEDULE D (Form 1040) <small>Department of the Treasury Internal Revenue Service</small>	Capital Gains and Losses ▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040). ▶ Use Schedule D-1 to list additional transactions for lines 1 and 8.	OMB No. 1545-0074 <div style="text-align: center; font-size: 24pt; font-weight: bold;">2003</div> Attachment Sequence No. 12				
Name(s) shown on Form 1040		Your social security number xxx : xx : xxxx				
Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less						
(a) Description of property <small>(Example: 100 sh. XYZ Co.)</small>	(b) Date acquired <small>(Mo., day, yr.)</small>	(c) Date sold <small>(Mo., day, yr.)</small>	(d) Sales price <small>(see page D-5 of the instructions)</small>	(e) Cost or other basis <small>(see page D-5 of the instructions)</small>	(f) Gain or (loss) for the entire year <small>Subtract (e) from (d)</small>	(g) Post-May 5 gain or (loss)* <small>(see below)</small>
1						
2 Enter your short-term totals, if any, from Schedule D-1, line 2		2				
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)		3				
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 2002 Capital Loss Carryover Worksheet		6	()			
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero		7a				()
7b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)		7b				
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year						
(a) Description of property <small>(Example: 100 sh. XYZ Co.)</small>	(b) Date acquired <small>(Mo., day, yr.)</small>	(c) Date sold <small>(Mo., day, yr.)</small>	(d) Sales price <small>(see page D-5 of the instructions)</small>	(e) Cost or other basis <small>(see page D-5 of the instructions)</small>	(f) Gain or (loss) for the entire year <small>Subtract (e) from (d)</small>	(g) Post-May 5 gain or (loss)* <small>(see below)</small>
8						
9 Enter your long-term totals, if any, from Schedule D-1, line 9		9				
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)		10				
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 page D-1 of the instructions		13				
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet		14	()			
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-		15				
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f). Next: Go to Part III on the back.		16				
<small>*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).</small>						
For Paperwork Reduction Act Notice, see Form 1040 instructions.			Cat. No. 11338H		Schedule D (Form 1040) 2003	

PENSION EARNER COMPREHENSIVE PROBLEMS

Schedule D (Form 1040) 2003

Page **2**

Part III Taxable Gain or Deductible Loss

- 17a** Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below
- b** Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40. **Next:** • If both lines 16 and 17a of Schedule D are gains **or** you have qualified dividends on Form 1040, line 9b, complete **Part IV** below (unless Form 1040, line 40, is zero).
• Otherwise, skip the rest of Schedule D and complete Form 1040.
- 18** If line 17a is a loss, enter here and on Form 1040, line 13a, the **smaller** of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions) **Next:** • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete **Part IV** below (but skip lines 19 and 20).
• Otherwise, skip **Part IV** below and complete the rest of Form 1040.

17a		
17b		
18	()

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

- 19** Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6
- 20** Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions

19		
20		

If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.

- 21** Enter your taxable income from Form 1040, line 40
- 22** Enter the **smaller** of line 16 or line 17a, but not less than zero
- 23** Enter your qualified dividends from Form 1040, line 9b
- 24** Add lines 22 and 23
- 25** Amount from line 4g of Form 4952 (investment interest expense)
- 26** Subtract line 25 from line 24. If zero or less, enter -0-
- 27** Subtract line 26 from line 21. If zero or less, enter -0-
- 28** Enter the **smaller** of line 21 **or:**
• \$56,800 if married filing jointly or qualifying widow(er);
• \$28,400 if single or married filing separately; or
• \$38,050 if head of household
- If line 27 is more than line 28, skip lines 29-39 and go to line 40.
- 29** Enter the amount from line 27
- 30** Subtract line 29 from line 28. If zero or less, go to line 40
- 31** Add lines 17b and 23*
- 32** Enter the **smaller** of line 30 or line 31
- 33** Multiply line 32 by 5% (.05)
- If lines 30 and 32 are the same, skip lines 34-39 and go to line 40.
- 34** Subtract line 32 from line 30
- 35** Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8
- 36** Enter the **smaller** of line 34 or line 35
- 37** Multiply line 36 by 8% (.08)
- 38** Subtract line 36 from line 34
- 39** Multiply line 38 by 10% (.10)
- If lines 26 and 30 are the same, skip lines 40-49 and go to line 50.
- 40** Enter the **smaller** of line 21 or line 26
- 41** Enter the amount from line 30 (if line 30 is blank, enter -0-)
- 42** Subtract line 41 from line 40
- 43** Add lines 17b and 23*
- 44** Enter the amount from line 32 (if line 32 is blank, enter -0-)
- 45** Subtract line 44 from line 43
- 46** Enter the **smaller** of line 42 or line 45
- 47** Multiply line 46 by 15% (.15)
- 48** Subtract line 46 from line 42
- 49** Multiply line 48 by 20% (.20)
- 50** Figure the tax on the amount on line 27. Use the Tax Table or Tax Rate Schedules, whichever applies
- 51** Add lines 33, 37, 39, 47, 49, and 50
- 52** Figure the tax on the amount on line 21. Use the Tax Table or Tax Rate Schedules, whichever applies
- 53** **Tax on all taxable income.** Enter the **smaller** of line 51 or line 52 here and on Form 1040, line 41

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*If line 25 is more than zero, see Lines 31 and 43 on page D-9 for the amount to enter. Printed on recycled paper Schedule D (Form 1040) 2003

PENSION EARNER COMPREHENSIVE PROBLEMS

2003 Social Security Benefits Worksheet

Before you begin:

- ✓ Complete Form 1040, lines 21, 23, 24, and 27 through 32a, if they apply to you.
- ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
- ✓ If you are married filing separately and you **lived apart** from your spouse for all of 2003, enter "D" to the right of the word "benefits" on line 20a.
- ✓ Be sure you have read the **Exception** on page 26 to see if you can use this worksheet instead of a publication to find out if any of your benefits are taxable.



1. Enter the total amount from box 5 of all your Forms SSA-1099 and Forms RRB-1099	1.	<input type="text"/>
2. Enter one-half of line 1	2.	<input type="text"/>
3. Enter the total of the amounts from Form 1040, lines 7, 8a, 9a, 10 through 12, 13a, 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099	3.	<input type="text"/>
4. Enter the amount, if any, from Form 1040, line 8b	4.	<input type="text"/>
5. Add lines 2, 3, and 4.	5.	<input type="text"/>
6. Enter the total of the amounts from Form 1040, lines 23, 24, and 27 through 32a, plus any amount you entered on the dotted line next to line 33	6.	<input type="text"/>
7. Is the amount on line 6 less than the amount on line 5? <input type="checkbox"/> No. None of your social security benefits are taxable. <input type="checkbox"/> Yes. Subtract line 6 from line 5	7.	<input type="text"/>
8. If you are: <ul style="list-style-type: none"> • Married filing jointly, enter \$32,000 • Single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003, enter \$25,000 • Married filing separately and you lived with your spouse at any time in 2003, skip lines 8 through 15; multiply line 7 by 85% (.85) and enter the result on line 16. Then go to line 17 	8.	<input type="text"/>
9. Is the amount on line 8 less than the amount on line 7? <input type="checkbox"/> No. None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. But if you are married filing separately and you lived apart from your spouse for all of 2003, enter -0- on line 20b. Be sure you entered "D" to the right of the word "benefits" on line 20a. <input type="checkbox"/> Yes. Subtract line 8 from line 7	9.	<input type="text"/>
10. Enter: \$12,000 if married filing jointly; \$9,000 if single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003	10.	<input type="text"/>
11. Subtract line 10 from line 9. If zero or less, enter -0-	11.	<input type="text"/>
12. Enter the smaller of line 9 or line 10.	12.	<input type="text"/>
13. Enter one-half of line 12	13.	<input type="text"/>
14. Enter the smaller of line 2 or line 13	14.	<input type="text"/>
15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0-	15.	<input type="text"/>
16. Add lines 14 and 15	16.	<input type="text"/>
17. Multiply line 1 by 85% (.85)	17.	<input type="text"/>
18. Taxable social security benefits. Enter the smaller of line 16 or line 17	18.	<input type="text"/>
<ul style="list-style-type: none"> • Enter the amount from line 1 above on Form 1040, line 20a. • Enter the amount from line 18 above on Form 1040, line 20b. 		



If part of your benefits are taxable for 2003 **and** they include benefits paid in 2003 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Comprehensive Problem 1

2003 Form 1040A, page 1

Form 1040A		Department of the Treasury—Internal Revenue Service		U.S. Individual Income Tax Return (99) 2003		IRS Use Only—Do not write or staple in this space.	
Label (See page 21.) Use the IRS label. Otherwise, please print or type.	LABEL HERE	Your first name and initial		Last name		OMB No. 1545-0085	
		Stuart		Morehouse		Your social security number xxx :xx :xxxx	
		If a joint return, spouse's first name and initial		Last name		Spouse's social security number xxx :xx :xxxx	
		Donna		Morehouse			
Home address (number and street). If you have a P.O. box, see page 22.		Apt. no.		▲ Important! ▲ You must enter your SSN(s) above.			
10923 Fullerton							
City, town or post office, state, and ZIP code. If you have a foreign address, see page 22.		Your City, State, Zip Code					
Presidential Election Campaign (See page 22.)		Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if filing a joint return, want \$3 to go to this fund?		You <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No		Spouse <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	
Filing status Check only one box.		1 <input type="checkbox"/> Single 2 <input checked="" type="checkbox"/> Married filing jointly (even if only one had income) 3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here.		4 <input type="checkbox"/> Head of household (with qualifying person). (See page 23.) If the qualifying person is a child but not your dependent, enter this child's name here.			
		5 <input type="checkbox"/> Qualifying widow(er) with dependent child (See page 24.)					
Exemptions		6a <input checked="" type="checkbox"/> Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a.		No. of boxes checked on 6a and 6b 2			
		b <input checked="" type="checkbox"/> Spouse		No. of children on 6c who: • lived with you			
		c Dependents:		(4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 25)		• did not live with you due to divorce or separation (see page 26)	
If more than six dependents, see page 24.		(1) First name Last name (2) Dependent's social security number (3) Dependent's relationship to you		(4) <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		Dependents on 6c not entered above	
				Add numbers on lines above		2	
		d Total number of exemptions claimed.					
Income		7 Wages, salaries, tips, etc. Attach Form(s) W-2.		7		18,526 00	
Attach Form(s) W-2 here. Also attach Form(s) 1099-R if tax was withheld.		8a Taxable interest. Attach Schedule 1 if required.		8a		235 00	
		b Tax-exempt interest. Do not include on line 8a.		8b			
		9a Ordinary dividends. Attach Schedule 1 if required.		9a			
		b Qualified dividends (see page XX).		9b			
		10a Capital gain distributions (see page 27).		10a			
		b Post-May 5 capital gain distributions (see page 27).		10b			
If you did not get a W-2, see page 27.		11a IRA distributions.		11a		11b Taxable amount (see page 27).	
		12a Pensions and annuities.		12a		12b Taxable amount (see page 28).	
Enclose, but do not attach, any payment.						12b 13,567 00	
		13 Unemployment compensation and Alaska Permanent Fund dividends.		13			
		14a Social security benefits.		14a 10,499.00		14b Taxable amount (see page 30).	
						14b 2,339 00	
		15 Add lines 7 through 14b (far right column). This is your total income.		15		34,667 00	
Adjusted gross income		16 Educator expenses (see page 30).		16			
		17 IRA deduction (see page 30).		17 900		00	
		18 Student loan interest deduction (see page 33).		18			
		19 Tuition and fees deduction (see page 33).		19			
		20 Add lines 16 through 19. These are your total adjustments.		20		900 00	
		21 Subtract line 20 from line 15. This is your adjusted gross income.		21		33,767 00	
For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 57. Cat. No. 11327A Form 1040A (2003)							

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Form 1040A, page 2

Form 1040A (2003)		Page 2
Tax, credits, and payments	22 Enter the amount from line 21 (adjusted gross income).	22 33,767 00
Standard Deduction for— • People who checked any box on line 23a or 23b or who can be claimed as a dependent, see page 34. • All others: Single or Married filing separately, \$4,750 Married filing jointly or Qualifying widow(er), \$9,500 Head of household, \$7,000	23a Check if: <input checked="" type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind } Total boxes checked ▶ 23a 1	
	b If you are married filing separately and your spouse itemizes deductions, see page 34 and check here ▶ 23b <input type="checkbox"/>	
	24 Enter your standard deduction (see left margin).	24 10,450 00
	25 Subtract line 24 from line 22. If line 24 is more than line 22, enter -0-.	25 23,317 00
	26 Multiply \$3,050 by the total number of exemptions claimed on line 6d.	26 6,100 00
	27 Subtract line 26 from line 25. If line 26 is more than line 25, enter -0-. This is your taxable income .	27 17,217 00
	28 Tax , including any alternative minimum tax (see page 35).	28 1,884 00
	29 Credit for child and dependent care expenses. Attach Schedule 2.	29
	30 Credit for the elderly or the disabled. Attach Schedule 3.	30
	31 Education credits. Attach Form 8863.	31
32 Retirement savings contributions credit. Attach Form 8880.	32	
33 Child tax credit (see page 38).	33	
34 Adoption credit. Attach Form 8839.	34	
35 Add lines 29 through 34. These are your total credits .	35 0 00	
36 Subtract line 35 from line 28. If line 35 is more than line 28, enter -0-.	36 1,884 00	
37 Advance earned income credit payments from Form(s) W-2.	37	
38 Add lines 36 and 37. This is your total tax .	38 1,884 00	
39 Federal income tax withheld from Forms W-2 and 1099.	39 3,780 00	
40 2003 estimated tax payments and amount applied from 2002 return.	40	
41 Earned income credit (EIC) .	41	
42 Additional child tax credit. Attach Form 8812.	42	
43 Add lines 39 through 42. These are your total payments .	43 3,780 00	
Refund 44 If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you overpaid .	44 1,896 00	
Direct deposit? See page 52 and fill in 45b, 45c, and 45d.	45a Amount of line 44 you want refunded to you .	45a 1,896 00
	b Routing number 	c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
	d Account number 	
	46 Amount of line 44 you want applied to your 2004 estimated tax .	46
Amount you owe	47 Amount you owe . Subtract line 43 from line 38. For details on how to pay, see page 53.	47
	48 Estimated tax penalty (see page 53).	48
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 54)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No	
	Designee's name ▶ _____	Phone no. ▶ () _____
		Personal identification number (PIN) ▶
Sign here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based on all information of which the preparer has any knowledge.	
Joint return? See page 22. Keep a copy for your records.	Your signature ▶ _____	Date / / _____
	Spouse's signature. If a joint return, both must sign.	Your occupation Retired
		Spouse's occupation Secretary
		Daytime phone number () _____
Paid preparer's use only	Preparer's signature ▶ _____	Date / / _____
	Firm's name (or yours if self-employed), address, and ZIP code ▶ _____	Check if self-employed <input type="checkbox"/>
		Preparer's SSN or PTIN Pxx-xx-xxxx
		EIN _____
		Phone no. () _____



Form 1040A (2003)

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Social Security Benefits Worksheet

Social Security Benefits Worksheet—Lines 20a and 20b

Keep for Your Records

- Before you begin:**
- ✓ Complete Form 1040, lines 21, 23, 24, and 27 through 32a, if they apply to you.
 - ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
 - ✓ If you are married filing separately and you **lived apart** from your spouse for all of 2003, enter "D" to the right of the word "benefits" on line 20a.
 - ✓ Be sure you have read the **Exception** on page 26 to see if you can use this worksheet instead of a publication to find out if any of your benefits are taxable.



1. Enter the total amount from box 5 of all your Forms SSA-1099 and Forms RRB-1099	1.	10,499
2. Enter one-half of line 1	2.	5,250
3. Enter the total of the amounts from Form 1040, lines 7, 8a, 9a, 10 through 12, 13a, 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099	3.	32,328
4. Enter the amount, if any, from Form 1040, line 8b	4.	0
5. Add lines 2, 3, and 4	5.	37,578
6. Enter the total of the amounts from Form 1040, lines 23, 24, and 27 through 32a, plus any amount you entered on the dotted line next to line 33	6.	900
7. Is the amount on line 6 less than the amount on line 5? <input type="checkbox"/> No. None of your social security benefits are taxable. <input checked="" type="checkbox"/> Yes. Subtract line 6 from line 5	7.	36,678
8. If you are: <input checked="" type="checkbox"/> Married filing jointly, enter \$32,000 <input type="checkbox"/> Single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003, enter \$25,000 <input type="checkbox"/> Married filing separately and you lived with your spouse at any time in 2003, skip lines 8 through 15; multiply line 7 by 85% (.85) and enter the result on line 16. Then go to line 17	8.	32,000
9. Is the amount on line 8 less than the amount on line 7? <input type="checkbox"/> No. None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. But if you are married filing separately and you lived apart from your spouse for all of 2003, enter -0- on line 20b. Be sure you entered "D" to the right of the word "benefits" on line 20a. <input checked="" type="checkbox"/> Yes. Subtract line 8 from line 7	9.	4,678
10. Enter: \$12,000 if married filing jointly; \$9,000 if single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003	10.	12,000
11. Subtract line 10 from line 9. If zero or less, enter -0-	11.	0
12. Enter the smaller of line 9 or line 10	12.	4,678
13. Enter one-half of line 12	13.	2,339
14. Enter the smaller of line 2 or line 13	14.	2,339
15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0-	15.	0
16. Add lines 14 and 15	16.	2,339
17. Multiply line 1 by 85% (.85)	17.	8,924
18. Taxable social security benefits. Enter the smaller of line 16 or line 17	18.	2,339

• Enter the amount from line 1 above on Form 1040, line 20a.
 • Enter the amount from line 18 above on Form 1040, line 20b.



If part of your benefits are taxable for 2003 **and** they include benefits paid in 2003 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Comprehensive Problem 2

2003 Form 1040, page 1

Form 1040	Department of the Treasury—Internal Revenue Service U.S. Individual Income Tax Return 2003	(99) IRS Use Only—Do not write or staple in this space.																																																																																								
Label (See instructions on page 21.) Use the IRS label. Otherwise, please print or type. Presidential Election Campaign (See page 21.)	For the year Jan. 1–Dec. 31, 2003, or other tax year beginning _____, 2003, ending _____, 20 OMB No. 1545-0074	Your social security number XXX XX XXXX																																																																																								
	Your first name and initial Jay	Last name Lehigh	Spouse's social security number XXX XX XXXX																																																																																							
	If a joint return, spouse's first name and initial Sandra	Last name Lehigh	Home address (number and street). If you have a P.O. box, see page 21. 99 Danville																																																																																							
	Home address (number and street). If you have a P.O. box, see page 21. 99 Danville	Apt. no. City, town or post office, state, and ZIP code. If you have a foreign address, see page 21. Your City, State Zip Code	Important! You must enter your SSN(s) above.																																																																																							
Filing Status Check only one box.	Note. Checking "Yes" will not change your tax or reduce your refund. Do you, or your spouse if filing a joint return, want \$3 to go to this fund?	You <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No Spouse <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No																																																																																								
Exemptions If more than five dependents, see page 22.	1 <input type="checkbox"/> Single 2 <input checked="" type="checkbox"/> Married filing jointly (even if only one had income) 3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here. 4 <input type="checkbox"/> Head of household (with qualifying person). (See page 21.) If the qualifying person is a child but not your dependent, enter this child's name here. 5 <input type="checkbox"/> Qualifying widow(er) with dependent child. (See page 21.)	No. of boxes checked on 6a and 6b: 2 No. of children on 6c who: • lived with you _____ • did not live with you due to divorce or separation (see page 22) _____ Dependents on 6c not entered above _____ Add numbers on lines above: 2																																																																																								
Income Attach Forms W-2 and W-2G here. Also attach Form(s) 1099-R if tax was withheld. If you did not get a W-2, see page 23. Enclose, but do not attach, any payment. Also, please use Form 1040-V.	6a <input checked="" type="checkbox"/> Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a. b <input checked="" type="checkbox"/> Spouse c Dependents: (1) First name Last name (2) Dependent's social security number (3) Dependent's relationship to you (4) <input checked="" type="checkbox"/> if qualifying child for child tax credit (see page 22) d Total number of exemptions claimed	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="width: 5%;">7</td><td style="width: 75%;">Wages, salaries, tips, etc. Attach Form(s) W-2</td><td style="width: 10%;"></td><td style="width: 10%;"></td></tr> <tr><td>8a</td><td>Taxable interest. Attach Schedule B if required</td><td></td><td></td></tr> <tr><td>8b</td><td>Tax-exempt interest. Do not include on line 8a</td><td></td><td></td></tr> <tr><td>9a</td><td>Ordinary dividends. Attach Schedule B if required</td><td></td><td></td></tr> <tr><td>9b</td><td>Qualified dividends (see page 25)</td><td></td><td></td></tr> <tr><td>10</td><td>Taxable refunds, credits, or offsets of state and local income taxes (see page 25)</td><td></td><td></td></tr> <tr><td>11</td><td>Alimony received</td><td></td><td></td></tr> <tr><td>12</td><td>Business income or (loss). Attach Schedule C or C-EZ</td><td style="text-align: right;">6,000</td><td style="text-align: right;">00</td></tr> <tr><td>13a</td><td>Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/></td><td style="text-align: right;">7,820</td><td style="text-align: right;">00</td></tr> <tr><td>13b</td><td>If box on 13a is checked, enter post-May 5 capital gain distributions</td><td></td><td></td></tr> <tr><td>14</td><td>Other gains or (losses). Attach Form 4797</td><td></td><td></td></tr> <tr><td>15a</td><td>IRA distributions</td><td></td><td></td></tr> <tr><td>15b</td><td>Taxable amount (see page 25)</td><td></td><td></td></tr> <tr><td>16a</td><td>Pensions and annuities</td><td></td><td></td></tr> <tr><td>16b</td><td>Taxable amount (see page 25)</td><td style="text-align: right;">18,945</td><td style="text-align: right;">00</td></tr> <tr><td>17</td><td>Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E</td><td></td><td></td></tr> <tr><td>18</td><td>Farm income or (loss). Attach Schedule F</td><td></td><td></td></tr> <tr><td>19</td><td>Unemployment compensation</td><td></td><td></td></tr> <tr><td>20a</td><td>Social security benefits</td><td style="text-align: right;">14,263</td><td style="text-align: right;">00</td></tr> <tr><td>20b</td><td>Taxable amount (see page 27)</td><td style="text-align: right;">3,737</td><td style="text-align: right;">00</td></tr> <tr><td>21</td><td>Other income. List type and amount (see page 29)</td><td></td><td></td></tr> <tr><td>22</td><td>Add the amounts in the far right column for lines 7 through 21. This is your total income</td><td style="text-align: right;">36,502</td><td style="text-align: right;">00</td></tr> </table>	7	Wages, salaries, tips, etc. Attach Form(s) W-2			8a	Taxable interest. Attach Schedule B if required			8b	Tax-exempt interest. Do not include on line 8a			9a	Ordinary dividends. Attach Schedule B if required			9b	Qualified dividends (see page 25)			10	Taxable refunds, credits, or offsets of state and local income taxes (see page 25)			11	Alimony received			12	Business income or (loss). Attach Schedule C or C-EZ	6,000	00	13a	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	7,820	00	13b	If box on 13a is checked, enter post-May 5 capital gain distributions			14	Other gains or (losses). Attach Form 4797			15a	IRA distributions			15b	Taxable amount (see page 25)			16a	Pensions and annuities			16b	Taxable amount (see page 25)	18,945	00	17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E			18	Farm income or (loss). Attach Schedule F			19	Unemployment compensation			20a	Social security benefits	14,263	00	20b	Taxable amount (see page 27)	3,737	00	21	Other income. List type and amount (see page 29)			22	Add the amounts in the far right column for lines 7 through 21. This is your total income	36,502	00
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Adjusted Gross Income	23 Educator expenses (see page 29) 24 IRA deduction (see page 29) 25 Student loan interest deduction (see page 31) 26 Tuition and fees deduction (see page 32) 27 Moving expenses. Attach Form 3903 28 One-half of self-employment tax. Attach Schedule SE 29 Self-employed health insurance deduction (see page 33) 30 Self-employed SEP, SIMPLE, and qualified plans 31 Penalty on early withdrawal of savings 32a Alimony paid b Recipient's SSN 33 Add lines 23 through 32a 34 Subtract line 33 from line 22. This is your adjusted gross income	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="width: 5%;">23</td><td style="width: 75%;">Educator expenses (see page 29)</td><td style="width: 10%;"></td><td style="width: 10%;"></td></tr> <tr><td>24</td><td>IRA deduction (see page 29)</td><td></td><td></td></tr> <tr><td>25</td><td>Student loan interest deduction (see page 31)</td><td></td><td></td></tr> <tr><td>26</td><td>Tuition and fees deduction (see page 32)</td><td></td><td></td></tr> <tr><td>27</td><td>Moving expenses. Attach Form 3903</td><td></td><td></td></tr> <tr><td>28</td><td>One-half of self-employment tax. Attach Schedule SE</td><td style="text-align: right;">424</td><td style="text-align: right;">00</td></tr> <tr><td>29</td><td>Self-employed health insurance deduction (see page 33)</td><td></td><td></td></tr> <tr><td>30</td><td>Self-employed SEP, SIMPLE, and qualified plans</td><td></td><td></td></tr> <tr><td>31</td><td>Penalty on early withdrawal of savings</td><td></td><td></td></tr> <tr><td>32a</td><td>Alimony paid b Recipient's SSN</td><td></td><td></td></tr> <tr><td>33</td><td>Add lines 23 through 32a</td><td style="text-align: right;">424</td><td style="text-align: right;">00</td></tr> <tr><td>34</td><td>Subtract line 33 from line 22. This is your adjusted gross income</td><td style="text-align: right;">36,078</td><td style="text-align: right;">00</td></tr> </table>	23	Educator expenses (see page 29)			24	IRA deduction (see page 29)			25	Student loan interest deduction (see page 31)			26	Tuition and fees deduction (see page 32)			27	Moving expenses. Attach Form 3903			28	One-half of self-employment tax. Attach Schedule SE	424	00	29	Self-employed health insurance deduction (see page 33)			30	Self-employed SEP, SIMPLE, and qualified plans			31	Penalty on early withdrawal of savings			32a	Alimony paid b Recipient's SSN			33	Add lines 23 through 32a	424	00	34	Subtract line 33 from line 22. This is your adjusted gross income	36,078	00																																								
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For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 76.

Cat. No. 11320B

Form 1040 (2003)

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Form 1040, page 2

Form 1040 (2003)		Page 2	
Tax and Credits		35	36,078 00
35 Amount from line 34 (adjusted gross income)			
36a Check <input checked="" type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind. } Total boxes checked <input checked="" type="checkbox"/> 36a <input type="checkbox"/> 2			
if: <input checked="" type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind. }			
b If you are married filing separately and your spouse itemizes deductions, or you were a dual-status alien, see page 34 and check here <input type="checkbox"/> 36b <input type="checkbox"/>			
37 Itemized deductions (from Schedule A) or your standard deduction (see left margin)		37	11,400 00
38 Subtract line 37 from line 35		38	24,678 00
39 If line 35 is \$104,625 or less, multiply \$3,050 by the total number of exemptions claimed on line 6d. If line 35 is over \$104,625, see the worksheet on page 35		39	6,100 00
40 Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-		40	18,578 00
41 Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972		41	2,086 00
42 Alternative minimum tax (see page 37). Attach Form 6251		42	
43 Add lines 41 and 42		43	2,086 00
44 Foreign tax credit. Attach Form 1116 if required		44	
45 Credit for child and dependent care expenses. Attach Form 2441		45	
46 Credit for the elderly or the disabled. Attach Schedule R		46	
47 Education credits. Attach Form 8863		47	
48 Retirement savings contributions credit. Attach Form 8880		48	
49 Child tax credit (see page 39)		49	
50 Adoption credit. Attach Form 8839		50	
51 Credits from: a <input type="checkbox"/> Form 8396 b <input type="checkbox"/> Form 8859		51	
52 Other credits. Check applicable box(es): a <input type="checkbox"/> Form 3800 b <input type="checkbox"/> Form 8801 c <input type="checkbox"/> Specify		52	
53 Add lines 44 through 52. These are your total credits		53	0 00
54 Subtract line 53 from line 43. If line 53 is more than line 43, enter -0-		54	2086 00
Other Taxes		55	848 00
55 Self-employment tax. Attach Schedule SE			
56 Social security and Medicare tax on tip income not reported to employer. Attach Form 4137		56	
57 Tax on qualified plans, including IRAs, and other tax-favored accounts. Attach Form 5329 if required		57	
58 Advance earned income credit payments from Form(s) W-2		58	
59 Household employment taxes. Attach Schedule H		59	
60 Add lines 54 through 59. This is your total tax		60	2934 00
Payments		61	1,895 00
61 Federal income tax withheld from Forms W-2 and 1099			
62 2003 estimated tax payments and amount applied from 2002 return		62	
63 Earned income credit (EIC)		63	
64 Excess social security and tier 1 RRTA tax withheld (see page 56)		64	
65 Additional child tax credit. Attach Form 8812		65	
66 Amount paid with request for extension to file (see page 56)		66	
67 Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885		67	
68 Add lines 61 through 67. These are your total payments		68	1,895 00
Refund		69	
69 If line 68 is more than line 60, subtract line 60 from line 68. This is the amount you overpaid			
70a Amount of line 69 you want refunded to you		70a	
Direct deposit? See page 56 and fill in 70b, 70c, and 70d.			
b Routing number			
c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings			
d Account number			
71 Amount of line 69 you want applied to your 2004 estimated tax		71	
Amount You Owe		72	1,039 00
72 Amount you owe. Subtract line 68 from line 60. For details on how to pay, see page 57			
73 Estimated tax penalty (see page 57)		73	
Do you want to allow another person to discuss this return with the IRS (see page 58)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No			
Third Party Designee		Designee's name <input type="text"/> Phone no. <input type="text"/> () Personal identification number (PIN) <input type="text"/>	
Sign Here			
Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.			
Your signature		Date / /	Your occupation
Spouse's signature. If a joint return, both must sign.		Date / /	Spouse's occupation
Daytime phone number ()		Preparer's SSN or PTIN XXX-XX-XXXX	
Paid Preparer's Use Only		Preparer's signature <input type="text"/> Date / / Check if self-employed <input type="checkbox"/>	
Firm's name (or yours if self-employed), address, and ZIP code <input type="text"/>		EIN <input type="text"/> Phone no. ()	

Form 1040 (2003)

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Schedule C-EZ, page 1

**SCHEDULE C-EZ
(Form 1040)**

Department of the Treasury
Internal Revenue Service
Name of proprietor

Net Profit From Business (Sole Proprietorship)

► Partnerships, joint ventures, etc., must file Form 1065 or 1065-B.
► Attach to Form 1040 or 1041. ► See instructions on back.

OMB No. 1545-0074

2003

Attachment
Sequence No. **09A**

Sandra Leigh

Social security number (SSN)

xxx xx xxxx

Part I General Information

**You May Use
Schedule C-EZ
Instead of
Schedule C
Only If You:**

- Had business expenses of \$2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-4 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service
Day Care

B Enter code from pages C-7, 8, & 9

6 2 4 4 1 0

C Business name. If no separate business name, leave blank.

D Employer ID number (EIN), if any

E Business address (including suite or room no.). Address not required if same as on Form 1040, page 1.

City, town or post office, state, and ZIP code

Part II Figure Your Net Profit

1 Gross receipts. Caution. If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employees in the instructions for Schedule C, line 1, on page C-3 and check here	<input type="checkbox"/>	1	6,000
2 Total expenses (see instructions). If more than \$2,500, you must use Schedule C		2	
3 Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12 , and also on Schedule SE, line 2 . (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)		3	6,000

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

- 4** When did you place your vehicle in service for business purposes? (month, day, year) ► / /
- 5** Of the total number of miles you drove your vehicle during 2003, enter the number of miles you used your vehicle for:
- a** Business **b** Commuting **c** Other
- 6** Do you (or your spouse) have another vehicle available for personal use? **Yes** **No**
- 7** Was your vehicle available for personal use during off-duty hours? **Yes** **No**
- 8a** Do you have evidence to support your deduction? **Yes** **No**
- b** If "Yes," is the evidence written? **Yes** **No**

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 14374D

Schedule C-EZ (Form 1040) 2003

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Schedule SE

SCHEDULE SE
(Form 1040)

Department of the Treasury
Internal Revenue Service

Self-Employment Tax

▶ Attach to Form 1040. ▶ See Instructions for Schedule SE (Form 1040).

OMB No. 1545-0074

2003

Attachment
Sequence No. **17**

Name of person with self-employment income (as shown on Form 1040)

Sandra Leigh

Social security number of person with self-employment income ▶

xxx : xx : xxxx

Who Must File Schedule SE

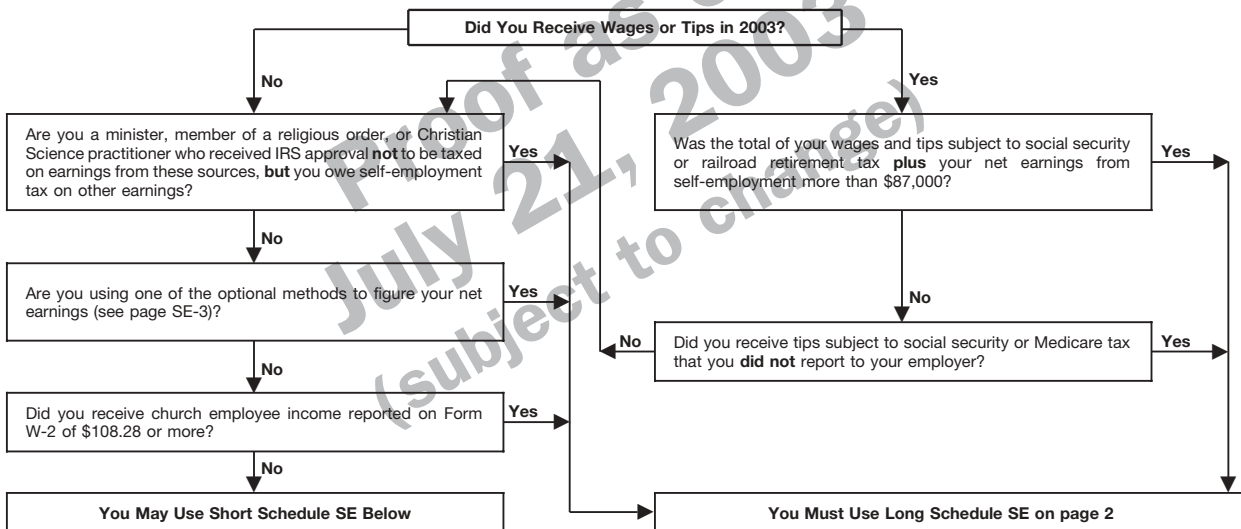
You must file Schedule SE if:

- You had net earnings from self-employment from **other than** church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of \$400 or more **or**
- You had church employee income of \$108.28 or more. Income from services you performed as a minister or a member of a religious order **is not** church employee income (see page SE-1).

Note. Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE (see page SE-3).

Exception. If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner **and** you filed Form 4361 and received IRS approval not to be taxed on those earnings, **do not** file Schedule SE. Instead, write "Exempt-Form 4361" on Form 1040, line 55.

May I Use Short Schedule SE or Must I Use Long Schedule SE?



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

1	Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a	1		
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report	2	6,000	00
3	Combine lines 1 and 2	3	6,000	00
4	Net earnings from self-employment. Multiply line 3 by 92.35% (.9235). If less than \$400, do not file this schedule; you do not owe self-employment tax ▶	4	5,541	00
5	Self-employment tax. If the amount on line 4 is: <ul style="list-style-type: none"> • \$87,000 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 55. • More than \$87,000, multiply line 4 by 2.9% (.029). Then, add \$10,788.00 to the result. Enter the total here and on Form 1040, line 55. 	5	848	00
6	Deduction for one-half of self-employment tax. Multiply line 5 by 50% (.5). Enter the result here and on Form 1040, line 28	6	424	00

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 11358Z

Schedule SE (Form 1040) 2003

Comprehensive
Problems

CP-25

PENSION EARNER

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

2003 Schedule D, page 1

**SCHEDULE D
(Form 1040)**

Department of the Treasury
Internal Revenue Service

Capital Gains and Losses

▶ **Attach to Form 1040.** ▶ **See Instructions for Schedule D (Form 1040).**
▶ **Use Schedule D-1 to list additional transactions for lines 1 and 8.**

OMB No. 1545-0074

2003

Attachment
Sequence No. **12**

Name(s) shown on Form 1040

Your social security number

Jay and Sandra Lehigh

xxx | xx | xxxx

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
1						
2 Enter your short-term totals, if any, from Schedule D-1, line 2						
3 Total short-term sales price amounts. Add lines 1 and 2 in column (d)						
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824						
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1						
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 2002 Capital Loss Carryover Worksheet					()	
7a Combine lines 1 through 5 in column (g). If the result is a loss, enter the result. Otherwise, enter -0-. Do not enter more than zero						()
7b Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)						

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5 of the instructions)	(e) Cost or other basis (see page D-5 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)	(g) Post-May 5 gain or (loss)* (see below)
8						
100 sh. ABC Inc	12/01/85	07/15/03	5,124 00	2,400 00	2,724 00	2,724 00
200 sh. XYZ Inc	12/20/87	11/14/03	10,796 00	5,700 00	5,096 00	5,096 00
9 Enter your long-term totals, if any, from Schedule D-1, line 9						
10 Total long-term sales price amounts. Add lines 8 and 9 in column (d)			105 22			
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						
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1						
13 Capital gain distributions. See page D-1 of the instructions						
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your 2002 Capital Loss Carryover Worksheet					()	
15 Combine lines 8 through 13 in column (g). If zero or less, enter -0-						7,820 00
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f)					7,820 00	

*Include in column (g) all gains and losses from column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, "collectibles gains and losses" (as defined on page D-6 of the instructions) or eligible gain on qualified small business stock (see page D-4 of the instructions).

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 11338H

Schedule D (Form 1040) 2003

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Schedule D (Form 1040) 2003

Page **2**

Part III Taxable Gain or Deductible Loss

17a Combine lines 7b and 16 and enter the result. If a loss, enter -0- on line 17b and go to line 18. If a gain, enter the gain on Form 1040, line 13a, and go to line 17b below	17a	7,820	00
b Combine lines 7a and 15. If zero or less, enter -0-. Then complete Form 1040 through line 40	17b	7,820	00
Next: • If both lines 16 and 17a of Schedule D are gains or you have qualified dividends on Form 1040, line 9b, complete Part IV below (unless Form 1040, line 40, is zero). • Otherwise, skip the rest of Schedule D and complete Form 1040.			
18 If line 17a is a loss, enter here and on Form 1040, line 13a, the smaller of (a) that loss or (b) (\$3,000) (or, if married filing separately, (\$1,500)) (see page D-6 of the instructions)	18	()
Next: • If you have qualified dividends on Form 1040, line 9b, complete Form 1040 through line 40, and then complete Part IV below (but skip lines 19 and 20). • Otherwise, skip Part IV below and complete the rest of Form 1040.			

Part IV Tax Computation Using Maximum Capital Gains Rates

If line 16 or line 17a is zero or less, skip lines 19 and 20 and go to line 21. Otherwise, go to line 19.

19 Enter your unrecaptured section 1250 gain, if any, from line 18 of the worksheet on page D-6	19		
20 Enter your 28% rate gain, if any, from line 7 of the worksheet on page D-9 of the instructions	20		
If lines 19 and 20 are zero, go to line 21. Otherwise, complete the worksheet on page D-10 of the instructions to figure the amount to enter on lines 35 and 53 below, and skip all other lines below.			
21 Enter your taxable income from Form 1040, line 40	21	18,578	00
22 Enter the smaller of line 16 or line 17a, but not less than zero	22	7,820	00
23 Enter your qualified dividends from Form 1040, line 9b	23		
24 Add lines 22 and 23	24	7,820	00
25 Amount from line 4g of Form 4952 (investment interest expense)	25		
26 Subtract line 25 from line 24. If zero or less, enter -0-	26	7,820	00
27 Subtract line 26 from line 21. If zero or less, enter -0-	27	10,758	00
28 Enter the smaller of line 21 or: • \$56,800 if married filing jointly or qualifying widow(er); • \$28,400 if single or married filing separately; or • \$38,050 if head of household	28	18,578	00
If line 27 is more than line 28, skip lines 29–39 and go to line 40.			
29 Enter the amount from line 27	29	10,758	00
30 Subtract line 29 from line 28. If zero or less, go to line 40	30	7,820	00
31 Add lines 17b and 23*	31	7,820	00
32 Enter the smaller of line 30 or line 31	32	7,820	00
33 Multiply line 32 by 5% (.05)	33	391	00
If lines 30 and 32 are the same, skip lines 34–39 and go to line 40.			
34 Subtract line 32 from line 30	34		
35 Enter your qualified 5-year gain, if any, from line 8 of the worksheet on page D-8	35		
36 Enter the smaller of line 34 or line 35	36		
37 Multiply line 36 by 8% (.08)	37		
38 Subtract line 36 from line 34	38		
39 Multiply line 38 by 10% (.10)	39		
If lines 26 and 30 are the same, skip lines 40–49 and go to line 50.			
40 Enter the smaller of line 21 or line 26	40		
41 Enter the amount from line 30 (if line 30 is blank, enter -0-)	41		
42 Subtract line 41 from line 40	42		
43 Add lines 17b and 23*	43		
44 Enter the amount from line 32 (if line 32 is blank, enter -0-)	44		
45 Subtract line 44 from line 43	45		
46 Enter the smaller of line 42 or line 45	46		
47 Multiply line 46 by 15% (.15)	47		
48 Subtract line 46 from line 42	48		
49 Multiply line 48 by 20% (.20)	49		
50 Figure the tax on the amount on line 27 . Use the Tax Table or Tax Rate Schedules, whichever applies	50	1,078	00
51 Add lines 33, 37, 39, 47, 49, and 50	51	1,469	00
52 Figure the tax on the amount on line 21 . Use the Tax Table or Tax Rate Schedules, whichever applies	52	2,086	00
53 Tax on all taxable income. Enter the smaller of line 51 or line 52 here and on Form 1040, line 41	53	1,469	00

*If line 25 is more than zero, see **Lines 31 and 43** on page D-9 for the amount to enter. Printed on recycled paper **Schedule D (Form 1040) 2003**

PENSION EARNER COMPREHENSIVE PROBLEMS

ANSWERS TO PROBLEMS

Social Security Benefits Worksheet.

- Before you begin:**
- ✓ Complete Form 1040, lines 21, 23, 24, and 27 through 32a, if they apply to you.
 - ✓ Figure any amount to be entered on the dotted line next to line 33 (see page 32.)
 - ✓ If you are married filing separately and you **lived apart** from your spouse for all of 2003, enter "D" to the right of the word "benefits" on line 20a.
 - ✓ Be sure you have read the **Exception** on page 26 to see if you can use this worksheet instead of a publication to find out if any of your benefits are taxable.



1. Enter the total amount from box 5 of all your Forms SSA-1099 and Forms RRB-1099	1.	14,263			
2. Enter one-half of line 1	2.	7,132			
3. Enter the total of the amounts from Form 1040, lines 7, 8a, 9a, 10 through 12, 13a, 14, 15b, 16b, 17 through 19, and 21. Do not include amounts from box 5 of Forms SSA-1099 or RRB-1099	3.	32,765			
4. Enter the amount, if any, from Form 1040, line 8b	4.	0			
5. Add lines 2, 3, and 4	5.	39,897			
6. Enter the total of the amounts from Form 1040, lines 23, 24, and 27 through 32a, plus any amount you entered on the dotted line next to line 33	6.	424			
7. Is the amount on line 6 less than the amount on line 5? <input type="checkbox"/> No. STOP None of your social security benefits are taxable. <input checked="" type="checkbox"/> Yes. Subtract line 6 from line 5	7.	39,473			
8. If you are: <ul style="list-style-type: none"> • Married filing jointly, enter \$32,000 • Single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003, enter \$25,000 • Married filing separately and you lived with your spouse at any time in 2003, skip lines 8 through 15; multiply line 7 by 85% (.85) and enter the result on line 16. Then go to line 17 	8.	32,000			
9. Is the amount on line 8 less than the amount on line 7? <input type="checkbox"/> No. STOP None of your social security benefits are taxable. You do not have to enter any amounts on lines 20a or 20b of Form 1040. But if you are married filing separately and you lived apart from your spouse for all of 2003, enter -0- on line 20b. Be sure you entered "D" to the right of the word "benefits" on line 20a. <input checked="" type="checkbox"/> Yes. Subtract line 8 from line 7	9.	7,473			
10. Enter: \$12,000 if married filing jointly; \$9,000 if single, head of household, qualifying widow(er), or married filing separately and you lived apart from your spouse for all of 2003	10.	12,000			
11. Subtract line 10 from line 9. If zero or less, enter -0-	11.	0			
12. Enter the smaller of line 9 or line 10	12.	7,473			
13. Enter one-half of line 12	13.	3,737			
14. Enter the smaller of line 2 or line 13	14.	3,737			
15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0-	15.	0			
16. Add lines 14 and 15	16.	3,737			
17. Multiply line 1 by 85% (.85)	17.	12,124			
18. Taxable social security benefits. Enter the smaller of line 16 or line 17	18.	3,737			
<ul style="list-style-type: none"> • Enter the amount from line 1 above on Form 1040, line 20a. • Enter the amount from line 18 above on Form 1040, line 20b. 					



If part of your benefits are taxable for 2003 **and** they include benefits paid in 2003 that were for an earlier year, you may be able to reduce the taxable amount. See Pub. 915 for details.

MODULE 1

Objectives

After completing this module you should be able to:

- Open and create a new tax return.
- Complete the main information sheet for this module in TaxWise.
- Identify and enter pertinent taxpayer information into the return.
- Determine the qualifications for the single filing status.
- Define wages and input a Form W-2 using the software.
- Determine taxable and non-taxable interest income and input applicable information from Form 1099-INT.
- Identify Unemployment Compensation and input a Form 1099-G.
- Define the Educators Expense adjustment and input applicable information for the calculation of the adjustment.
- Define the qualifications for the “Student Loan Interest” adjustment and input applicable information for the calculation of the adjustment.
- Know the qualifications for an IRA contribution and input applicable information.
- Define early withdrawal penalty.
- Identify who qualifies for the “Credit for Qualified Retirement Savings Contribution” and input applicable information.
- Identify proper procedures for finishing the return.

Taxpayer Profile

Taxpayer Name	James Fairmont
TP SSN	XXX-XX-XXXX
Spouse Name	
SP SSN	
Street Address	76 Fisk Ave
City, State, Zip	Your City State and Zip Code
Phone Number	(412) 555-1212
Date of birth TP	03/10/1979
Date of birth Spouse	
Occupation TP	3 rd Grade Teacher
SP	
Blind? TP	No
SP	
Donate to Presidential Fund?	
TP	No
SP	
Filing Status	Single
Can be claimed as dependent by someone else? TP	No
SP	
State Return Info (Yes or No)	No
Direct Deposit	Yes
Bank Routing Number	112200001
Account number	987123

Other considerations:

He tells you he spent \$537.26 on classroom supplies.


This is his first year teaching, he started in August, and worked 640 hours.

He is repaying a student loan and received a statement from his loan institution showing he paid \$235.87 in interest.

He made a traditional IRA contribution of \$450.


Documents taxpayer gives you:

Form W-2 Kathy's Restaurant

a Control number 123456		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number XX-XXXXXXX				1 Wages, tips, other compensation \$2,226.15		2 Federal income tax withheld \$203.12	
c Employer's name, address, and ZIP code Kathy's Restaurant 10 Franklin St. Your City, State, and Zip Code				3 Social security wages \$2,226.15		4 Social security tax withheld \$139.02	
				5 Medicare wages and tips \$2,226.15		6 Medicare tax withheld \$32.38	
				7 Social security tips		8 Allocated tips	
d Employee's social security number				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name James Fairmont 76 Fisk Ave. Your City, State, and Zip Code				11 Nonqualified plans		12a See instructions for box 12	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code							
15 State Employer's state ID number XX-XXXXXXX		16 State wages, tips, etc. \$2,226.15		17 State income tax \$160.34		18 Local wages, tips, etc.	
						19 Local income tax	
						20 Locality name	


Form **W-2** Wage and Tax Statement **2003** Department of the Treasury—Internal Revenue Service
 Copy B To Be Filed with Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

Form W-2 Sunshine School District

a Control number 123456		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number XX-XXXXXXX				1 Wages, tips, other compensation \$6,432.67		2 Federal income tax withheld \$432.28	
c Employer's name, address, and ZIP code Sunshine School District 45 North Third Street Your City, State, and Zip Code				3 Social security wages \$0.00		4 Social security tax withheld \$0.00	
				5 Medicare wages and tips \$6,432.67		6 Medicare tax withheld \$93.23	
				7 Social security tips		8 Allocated tips	
d Employee's social security number				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name James Fairmont 76 Fisk Ave. Your City, State, and Zip Code				11 Nonqualified plans		12a See instructions for box 12 \$435.87	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code							
15 State Employer's state ID number XX-XXXXXXX		16 State wages, tips, etc. \$6,432.67		17 State income tax \$795.43		18 Local wages, tips, etc.	
						19 Local income tax	
						20 Locality name	

Form **W-2** Wage and Tax Statement **2003** Department of the Treasury—Internal Revenue Service
 Copy B To Be Filed with Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

PAYER'S name, street address, city, state, ZIP code, and telephone no. Division of Employment Security 290 West 4th St. Your City, State and Zip Code		1 Unemployment compensation \$ 1,340.00	OMB No. 1545-0120 2003 Form 1099-G	Certain Government Payments
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	2 State or local income tax refunds, credits, or offsets \$	3 Box 2 amount is for tax year	
RECIPIENT'S name James Fairmont Street address (including apt. no.) 76 Fisk Ave City, state, and ZIP code Your City, State, and Zip Code Account number (optional)		5 	4 Federal income tax withheld \$ 80.98	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
		6 Taxable grants \$	7 Agriculture payments \$	
		8 Box 2 is trade or business income <input type="checkbox"/>		

Form **1099-G** (keep for your records) Department of the Treasury - Internal Revenue Service

CORRECTED (if checked)

PAYER'S name, street address, city, state, ZIP code, and telephone no. First Bank 99 W. 48th St. Your City, State, Zip Code		Payer's RTN (optional)	OMB No. 1545-0112 2003 Form 1099-INT	Interest Income
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	1 Interest income not included in box 3 \$ 147.48	2 Early withdrawal penalty \$ 19.68	
RECIPIENT'S name James Fairmont Street address (including apt. no.) 76 Fisk Ave City, state, and ZIP code Your City, State, Zip Code Account number (optional)		3 Interest on U.S. Savings Bonds and Treas. obligations \$	4 Federal income tax withheld \$	Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
		5 Investment expenses \$	6 Foreign tax paid \$	
		7 Foreign country or U.S. possession		

Form **1099-INT** (keep for your records) Department of the Treasury - Internal Revenue Service

Module 2**Objectives**

After completing this module you should be able to:

- Create a new tax return by completing the main information sheet for this module in TaxWise.
- Determine the qualifications for head of household and married filing separately filing status.
- Use the 5 tests for dependents, to determine dependency status.
- Determine who is eligible for the credit for child and dependent care expenses.
- Use the EIC eligibility requirements, to determine an EIC qualifying child.
- Determine who is eligible for the child tax credit.
- Input applicable information from Form 1099-DIV.
- Determine who can use Schedule C-EZ and complete Schedule C-EZ and Schedule SE.
- Complete Form 2441.
- Complete the Child Tax Credit Worksheet.
- Complete the EIC Worksheet
- Explain the benefits of AEIC and review where AEIC is reported on Form 1040 or Form 1040A.
- Identify proper procedures for finishing the return.

Taxpayer Profile

Taxpayer Name	Betsy Curry
TP SSN	XXX-XX-XXXX
Spouse Name	
SP SSN	
Street Address	614 Howard Ave
City, State, Zip	Your City State and Zip Code
Phone Number	402-555-1212
Date of birth TP	08/23/1969
Date of birth Spouse	
Occupation TP	Executive Assistant
SP	
Blind? TP	No
SP	
Donate to Presidential Fund?	
TP	Yes
SP	
Filing status	Head of Household
Can be claimed as dependent by someone else? TP	No
SP	
State Return Info (Yes or No)	No
Direct Deposit	
Bank Routing Number	XXXXXXXXXX
Account number	XXXXXXX

Other Members of Household

Name	Date of Birth	SSN or ITIN	Relationship	Citizenship	# of Months in Home
Mary Curry	07/21/1994	xxx-xx-xxxx	Daughter	U.S.	12
James Curry	08/24/1997	xxx-xx-xxxx	Son	U.S.	12

Other considerations:

Mary is divorced and keeps up a main home for herself and her children.

She provides 100% of her children's support.

Both children lived with her for the entire year.


Betsy has a small word processing business (Code: 561900) which she runs out of her home. Her gross income was \$4,850. Her total expenses for materials were \$363 and she has written records for

1,200 business miles and 9,000 other miles on her only car. Her car was put into business use on January 1, 2002. Her business takes up only a very small area in her home and she uses her computer mainly for personal use. She elects to take the standard mileage rate.

Betsy's neighbor, Mary King, cares for her two children after school. Betsy paid \$1,750 for each child during 2003. Mary's SSN is xxx-xx-xxxx and her address is 628 Howard Ave., Your City, State, and Zip Code.

Documents taxpayer gives you:

Form W-2, State of Nebraska

a Control number 123456		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS Web Site at www.irs.gov .	
b Employer identification number XX-XXXXXXX		1 Wages, tips, other compensation \$14,834.56		2 Federal income tax withheld \$1,739.86			
c Employer's name, address, and ZIP code State of Nebraska 1345 South 10th Street Omaha, Nebraska 68104		3 Social security wages \$17,834.56		4 Social security tax withheld \$1,106.00			
		5 Medicare wages and tips \$17,834.56		6 Medicare tax withheld \$259.00			
		7 Social security tips		8 Allocated tips			
d Employee's social security number XXX-XX-XXXX		9 Advance EIC payment \$1,000.00		10 Dependent care benefits \$1,000.00			
e Employee's first name and initial Last name Betsy Curry 7614 Howard Ave. Your City, State, Zip Code		11 Nonqualified plans		12a See instructions for box 12 \$2,000.00			
		13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b			
		14 Other		12c			
				12d			
f Employee's address and ZIP code							
15 State Employer's state ID number XX-XXXXXXX	16 State wages, tips, etc. \$14,834.56	17 State income tax	18 Local wages, tips, etc.	19 Local income tax	20 Locality name		

Form **W-2** Wage and Tax Statement

2003

Department of the Treasury—Internal Revenue Service

Copy B To Be Filed with Employee's FEDERAL Tax Return.
This information is being furnished to the Internal Revenue Service.

CORRECTED (if checked)

PAYER'S name, street address, city, state, ZIP code, and telephone no. ABC Corporation 3333 North Tenth Street Your City, State, Zip Code		1a Total ordinary dividends \$ 54.00	OMB No. 1545-0110 2003	Dividends and Distributions
		1b Qualified dividends \$	Form 1099-DIV	
		2a Total capital gain distr. \$	2b Post-May 5 capital gain distr. \$	Copy B For Recipient
PAYER'S Federal identification number XX-XXXXXXX	RECIPIENT'S identification number XXX-XX-XXXX	2c Qualified 5-year gain \$	2d Unrecap. Sec. 1250 gain \$	
RECIPIENT'S name Betsy Curry		2e Section 1202 gain \$	2f Collectibles (28%) gain \$	This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
Street address (including apt. no.) 614 Howard Ave.		3 Nontaxable distributions \$	4 Federal income tax withheld \$	
City, state, and ZIP code Your City, State, Zip Code		5 Investment expenses \$	6 Foreign tax paid \$	
Account number (optional)		7 Foreign country or U.S. possession	8 Cash liquidation distributions \$	
		9 Noncash liquidation distributions \$		

Form **1099-DIV**

(keep for your records)

Department of the Treasury - Internal Revenue Service

Module 3**Objectives**

After completing this module you should be able to:

- Create a new tax return by completing the main information sheet for this module in TaxWise.
- Determine the qualifications for married filing jointly and qualifying widower filing status.
- Determine basis and capital gain/loss on sale of stock.
- Determine if IRA distributions are taxable, nontaxable, or partly taxable and calculate the taxable portion.
- Determine if retirement income is taxable and calculate the taxable portion.
- Distinguish between taxable and nontaxable social security benefits and calculate the taxable portion.
- Identify how other types of income are reported.
- Determine the qualifications for the tuition and fees deduction.
- Determine the qualifications for the education credits.
- Determine the most advantageous method for reporting tuition and fees.
- Determine which items are allowed when itemizing deductions.
- Know where to report estimated tax payments.
- Determine if the estimated tax penalty applies.

Taxpayer Profile

Taxpayer Name	Don Hillsdale
TP SSN	XXX-XX-XXXX
Spouse Name	Sarah Wilson
SP SSN	xxx-xx-xxxx
Street Address	129 Pembroke Ave.
City, State, Zip	Your City, State, Zip Code
Phone Number	402-555-1212
Date of birth TP	03/12/1932
Date of birth Spouse	12/21/1940
Occupation TP	Retired
SP	Housewife
Blind? TP	No
SP	No
Donate to Presidential Fund?	
TP	Yes
SP	No
Filing Status	MFJ
Can be claimed as dependent by someone else? TP	No
SP	No
State Return Info (Yes or No)	
Direct Deposit	
Bank Routing Number	XXXXXXXXXX
Account number	XXXXXXXXXXXXXXXXXX

Other Members of Household

Name	Date of Birth	SSN or ITIN	Relationship	Citizenship	# of Months in Home
Betty Wilson	05/23/1983	xxx-xx-xxxx	Granddaughter	U.S.	12

Other considerations:

- Don paid \$1,350 for tuition and fees to the local college for his granddaughter's education. She is a junior and a full-time student.
- Don and Sarah's previous year tax liability was \$2,011.

- Sarah provided the following information on the sale of stock.

Company	# of Shares	Purchase Date	Per Share Basis	Sale Date	Per Share Sale Price
ABC Co.	100	05/28/1985	48.00	05/30/2003	55.00
XYZ Co.	100	11/05/2002	32.00	04/10/2003	49.00

- Don and Sarah had the following expenses for the year:

Medical insurance	\$2,250
Medical travel	500 miles
Dental bills	\$275
New glasses	\$165
Prescription drugs	\$1,263
Over the counter medication	\$120
Church donations	\$1,000
Donation to neighbor whose house burnt	\$100
Other charities (cash)	\$82
Clothing to Salvation Army	\$327
Home mortgage interest	\$3,175
City real estate tax	\$550
County real estate tax	\$1,721
Car license fee	\$35
Personal property tax	\$817
Gambling losses	\$1,500

- Don made the following estimated tax payments:

04/12/2003	\$200
06/15/2003	\$200
09/10/2003	\$200
01/15/2004	\$200

- Don and Sarah had \$200 of their previous year's tax refund applied to this year's taxes.

Documents taxpayer gives you:

Form 1099-R, Emerson Utility

<input type="checkbox"/> CORRECTED (if checked)				OMB No. 1545-0119		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return.
PAYER'S name, street address, city, state, and ZIP code Emerson Utilities 555 East 10th St. Your City, State, Zip Code		1 Gross distribution \$ 31,562.00	2003 Form 1099-R		2a Taxable amount \$ 31,562.00	
		2b Taxable amount not determined <input type="checkbox"/>			Total distribution <input type="checkbox"/>	
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	3 Capital gain (included in box 2a) \$	4 Federal income tax withheld \$ 1,250.00		This information is being furnished to the Internal Revenue Service.	
RECIPIENT'S name Don Hillsdale Street address (including apt. no.) 129 Pembroke Ave City, state, and ZIP code Your City, State Zip Code		5 Employee contributions or insurance premiums \$	6 Net unrealized appreciation in employer's securities \$			
		7 Distribution code(s) 7	IRA/SEP/SIMPLE <input type="checkbox"/>	8 Other \$ %		9a Your percentage of total distribution %	9b Total employee contributions $
Account number (optional)		10 State tax withheld \$	11 State/Payer's state no.	12 State distribution \$		
		13 Local tax withheld \$	14 Name of locality	15 Local distribution \$		

Form **1099-R** Department of the Treasury - Internal Revenue Service

Form 1099-R, First Security

<input type="checkbox"/> CORRECTED (if checked)				OMB No. 1545-0119		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. Copy B Report this income on your Federal tax return. If this form shows Federal income tax withheld in box 4, attach this copy to your return.
PAYER'S name, street address, city, state, and ZIP code First Security 895 West Whittier Your City, State, Zip Code		1 Gross distribution \$ 2,252.00	2003 Form 1099-R		2a Taxable amount \$ 2,252.00	
		2b Taxable amount not determined <input type="checkbox"/>			Total distribution <input type="checkbox"/>	
PAYER'S Federal identification number xx-xxxxxxx	RECIPIENT'S identification number xxx-xx-xxxx	3 Capital gain (included in box 2a) \$	4 Federal income tax withheld \$ 225.00		This information is being furnished to the Internal Revenue Service.	
RECIPIENT'S name Don Hillsdale Street address (including apt. no.) 129 Pembroke Ave City, state, and ZIP code Your City, State Zip Code		5 Employee contributions or insurance premiums \$	6 Net unrealized appreciation in employer's securities \$			
		7 Distribution code(s) 7	IRA/SEP/SIMPLE <input checked="" type="checkbox"/>	8 Other \$ %		9a Your percentage of total distribution %	9b Total employee contributions $
Account number (optional)		10 State tax withheld \$	11 State/Payer's state no.	12 State distribution \$		
		13 Local tax withheld \$	14 Name of locality	15 Local distribution \$		

Form **1099-R** Department of the Treasury - Internal Revenue Service

3232		<input type="checkbox"/> CORRECTED		OMB No. 1545-0238	
PAYER'S name ABC Casino Street address 2233 N. 33rd St. City, state, and ZIP code Your City, State, Zip Code Federal identification number Telephone number		1 Gross winnings \$1,500.00	2 Federal income tax withheld		2003 Form W-2G Certain Gambling Winnings For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G. File with Form 1096.
		3 Type of wager Slots	4 Date won 3 : 31 : 2003		
		5 Transaction	6 Race		
		7 Winnings from identical wagers	8 Cashier		
WINNER'S name Sarah Wilson Street address (including apt. no.) 129 Pembroke Ave City, state, and ZIP code Your City, State, Zip Code		9 Winner's taxpayer identification no. XXX-XX-XXXX	10 Window		Copy A For Internal Revenue Service Center
		11 First I.D.	12 Second I.D.		
		13 State/Payer's state identification no.	14 State income tax withheld		
Under penalties of perjury, I declare that, to the best of my knowledge and belief, the name, address, and taxpayer identification number that I have furnished correctly identify me as the recipient of this payment and any payments from identical wagers, and that no other person is entitled to any part of these payments.					
Signature ►				Date ►	
Form W-2G		Cat. No. 10138V		Department of the Treasury - Internal Revenue Service	

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0110		
PAYER'S name, street address, city, state, ZIP code, and telephone no. ABC Securities 3333 North Tenth Street Your City, State, Zip Code		1a Total ordinary dividends \$	2003 Form 1099-DIV	Dividends and Distributions
		1b Qualified dividends \$		
PAYER'S Federal identification number XX-XXXXXXX		2a Total capital gain distr. \$ 1,236.00	2b Post-May 5 capital gain distr. \$ 1,000.00	Copy B For Recipient
		2c Qualified 5-year gain \$ 236.00	2d Unrecap. Sec. 1250 gain \$	
RECIPIENT'S name Sarah Wilson Street address (including apt. no.) 129 Pembroke Ave. City, state, and ZIP code Your City, State, Zip Code		2e Section 1202 gain \$	2f Collectibles (28%) gain \$	This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.
		3 Nontaxable distributions \$	4 Federal income tax withheld \$ 124.00	
Account number (optional)		5 Investment expenses \$	6 Foreign tax paid \$	
		7 Foreign country or U.S. possession	8 Cash liquidation distributions \$	
		9 Noncash liquidation distributions \$		
Form 1099-DIV (keep for your records) Department of the Treasury - Internal Revenue Service				

FORM SSA-1099 – SOCIAL SECURITY BENEFIT STATEMENT

2003 : PART OF YOUR SOCIAL SECURITY BENEFITS SHOWN IN BOX 5 MAY BE TAXABLE INCOME.
 : SEE THE REVERSE FOR MORE INFORMATION.

Box 1. Name Don Hillsdale		Box 2. Beneficiary's Social Security Number xxx-xx-xxxx	
Box 3. Benefits Paid in 2003 12,240.00	Box 4. Benefits Repaid to SSA in 2003	Box 5. Net Benefits for 2003 (Box 3 minus Box 4) 12,240.00	
DESCRIPTION OF AMOUNT IN BOX 3		DESCRIPTION OF AMOUNT IN BOX 4	
		Box 6. Voluntary Federal Income Tax Withholding 0	
		Box 7. Address 129 Pembroke Ave Your City, State, Zip Code	
		Box 8. Claim Number (Use this number if you need to contact SSA.)	

Form SSA-1099-SM (1-2004)

DO NOT RETURN THIS FORM TO SSA OR IRS

Module 4**Wage Earner Objectives**

After completing this module you should be able to:

- Identify when Individual Taxpayer Identification Numbers are required.
- Define multiple support as it applies to dependent exemptions.
- Determine when and how tip income is reported.
- Determine when scholarship and fellowship grants are taxable.
- Determine when state and local tax refunds are taxable.
- Distinguish between alimony and child support and identify where to report the receipt of alimony.
- Identify where alimony payments are reported.
- Identify where jury duty payments returned to an employer are reported.
- Explain foreign tax credit and mortgage interest credit.

Pension Earner Objectives

After completing this module you should be able to:

- Determine when a gain from the sale of a home is reported.
- Determine when Coverdell ESAs are taxable.
- Determine the qualifications for the credit for the elderly and disabled.

STUDENT NOTES

STUDENT NOTES

Lined writing area for student notes.

STUDENT NOTES

STUDENT NOTES

Lined writing area for student notes.

STUDENT NOTES

2003 Earned Income Credit (EIC) Table

Caution. This is not a tax table.

1. To find your credit, read down the "At least - But less than" columns and find the line that includes the amount you were told to look up from your EIC Worksheet.

2. Then, go to the column that includes your filing status and the number of qualifying children you have. Enter the credit from that column on your EIC Worksheet.

Example. If your filing status is single, you have one qualifying child, and the amount you are looking up from your EIC Worksheet is \$2,455, you would enter \$842.

If the amount you are looking up from the worksheet is—		And your filing status is—		
		No children	One child	Two children
At least	But less than	Your credit is—		
2,400	2,450	186	825	970
2,450	2,500	189	842	990

If the amount you are looking up from the worksheet is—		And your filing status is—						If the amount you are looking up from the worksheet is—		And your filing status is—					
		Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—					Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—		
At least	But less than	No children	One child	Two children	No children	One child	Two children	At least	But less than	No children	One child	Two children	No children	One child	Two children
\$1	\$50	\$2	\$9	\$10	\$2	\$9	\$10	3,000	3,050	231	1,029	1,210	231	1,029	1,210
50	100	6	26	30	6	26	30	3,050	3,100	235	1,046	1,230	235	1,046	1,230
100	150	10	43	50	10	43	50	3,100	3,150	239	1,063	1,250	239	1,063	1,250
150	200	13	60	70	13	60	70	3,150	3,200	243	1,080	1,270	243	1,080	1,270
200	250	17	77	90	17	77	90	3,200	3,250	247	1,097	1,290	247	1,097	1,290
250	300	21	94	110	21	94	110	3,250	3,300	251	1,114	1,310	251	1,114	1,310
300	350	25	111	130	25	111	130	3,300	3,350	254	1,131	1,330	254	1,131	1,330
350	400	29	128	150	29	128	150	3,350	3,400	258	1,148	1,350	258	1,148	1,350
400	450	33	145	170	33	145	170	3,400	3,450	262	1,165	1,370	262	1,165	1,370
450	500	36	162	190	36	162	190	3,450	3,500	266	1,182	1,390	266	1,182	1,390
500	550	40	179	210	40	179	210	3,500	3,550	270	1,199	1,410	270	1,199	1,410
550	600	44	196	230	44	196	230	3,550	3,600	273	1,216	1,430	273	1,216	1,430
600	650	48	213	250	48	213	250	3,600	3,650	277	1,233	1,450	277	1,233	1,450
650	700	52	230	270	52	230	270	3,650	3,700	281	1,250	1,470	281	1,250	1,470
700	750	55	247	290	55	247	290	3,700	3,750	285	1,267	1,490	285	1,267	1,490
750	800	59	264	310	59	264	310	3,750	3,800	289	1,284	1,510	289	1,284	1,510
800	850	63	281	330	63	281	330	3,800	3,850	293	1,301	1,530	293	1,301	1,530
850	900	67	298	350	67	298	350	3,850	3,900	296	1,318	1,550	296	1,318	1,550
900	950	71	315	370	71	315	370	3,900	3,950	300	1,335	1,570	300	1,335	1,570
950	1,000	75	332	390	75	332	390	3,950	4,000	304	1,352	1,590	304	1,352	1,590
1,000	1,050	78	349	410	78	349	410	4,000	4,050	308	1,369	1,610	308	1,369	1,610
1,050	1,100	82	366	430	82	366	430	4,050	4,100	312	1,386	1,630	312	1,386	1,630
1,100	1,150	86	383	450	86	383	450	4,100	4,150	316	1,403	1,650	316	1,403	1,650
1,150	1,200	90	400	470	90	400	470	4,150	4,200	319	1,420	1,670	319	1,420	1,670
1,200	1,250	94	417	490	94	417	490	4,200	4,250	323	1,437	1,690	323	1,437	1,690
1,250	1,300	98	434	510	98	434	510	4,250	4,300	327	1,454	1,710	327	1,454	1,710
1,300	1,350	101	451	530	101	451	530	4,300	4,350	331	1,471	1,730	331	1,471	1,730
1,350	1,400	105	468	550	105	468	550	4,350	4,400	335	1,488	1,750	335	1,488	1,750
1,400	1,450	109	485	570	109	485	570	4,400	4,450	339	1,505	1,770	339	1,505	1,770
1,450	1,500	113	502	590	113	502	590	4,450	4,500	342	1,522	1,790	342	1,522	1,790
1,500	1,550	117	519	610	117	519	610	4,500	4,550	346	1,539	1,810	346	1,539	1,810
1,550	1,600	120	536	630	120	536	630	4,550	4,600	350	1,556	1,830	350	1,556	1,830
1,600	1,650	124	553	650	124	553	650	4,600	4,650	354	1,573	1,850	354	1,573	1,850
1,650	1,700	128	570	670	128	570	670	4,650	4,700	358	1,590	1,870	358	1,590	1,870
1,700	1,750	132	587	690	132	587	690	4,700	4,750	361	1,607	1,890	361	1,607	1,890
1,750	1,800	136	604	710	136	604	710	4,750	4,800	365	1,624	1,910	365	1,624	1,910
1,800	1,850	140	621	730	140	621	730	4,800	4,850	369	1,641	1,930	369	1,641	1,930
1,850	1,900	143	638	750	143	638	750	4,850	4,900	373	1,658	1,950	373	1,658	1,950
1,900	1,950	147	655	770	147	655	770	4,900	4,950	377	1,675	1,970	377	1,675	1,970
1,950	2,000	151	672	790	151	672	790	4,950	5,000	382	1,692	1,990	382	1,692	1,990
2,000	2,050	155	689	810	155	689	810	5,000	5,050	382	1,709	2,010	382	1,709	2,010
2,050	2,100	159	706	830	159	706	830	5,050	5,100	382	1,726	2,030	382	1,726	2,030
2,100	2,150	163	723	850	163	723	850	5,100	5,150	382	1,743	2,050	382	1,743	2,050
2,150	2,200	166	740	870	166	740	870	5,150	5,200	382	1,760	2,070	382	1,760	2,070
2,200	2,250	170	757	890	170	757	890	5,200	5,250	382	1,777	2,090	382	1,777	2,090
2,250	2,300	174	774	910	174	774	910	5,250	5,300	382	1,794	2,110	382	1,794	2,110
2,300	2,350	178	791	930	178	791	930	5,300	5,350	382	1,811	2,130	382	1,811	2,130
2,350	2,400	182	808	950	182	808	950	5,350	5,400	382	1,828	2,150	382	1,828	2,150
2,400	2,450	186	825	970	186	825	970	5,400	5,450	382	1,845	2,170	382	1,845	2,170
2,450	2,500	189	842	990	189	842	990	5,450	5,500	382	1,862	2,190	382	1,862	2,190
2,500	2,550	193	859	1,010	193	859	1,010	5,500	5,550	382	1,879	2,210	382	1,879	2,210
2,550	2,600	197	876	1,030	197	876	1,030	5,550	5,600	382	1,896	2,230	382	1,896	2,230
2,600	2,650	201	893	1,050	201	893	1,050	5,600	5,650	382	1,913	2,250	382	1,913	2,250
2,650	2,700	205	910	1,070	205	910	1,070	5,650	5,700	382	1,930	2,270	382	1,930	2,270
2,700	2,750	208	927	1,090	208	927	1,090	5,700	5,750	382	1,947	2,290	382	1,947	2,290
2,750	2,800	212	944	1,110	212	944	1,110	5,750	5,800	382	1,964	2,310	382	1,964	2,310
2,800	2,850	216	961	1,130	216	961	1,130	5,800	5,850	382	1,981	2,330	382	1,981	2,330
2,850	2,900	220	978	1,150	220	978	1,150	5,850	5,900	382	1,998	2,350	382	1,998	2,350
2,900	2,950	224	995	1,170	224	995	1,170	5,900	5,950	382	2,015	2,370	382	2,015	2,370
2,950	3,000	228	1,012	1,190	228	1,012	1,190	5,950	6,000	382	2,032	2,390	382	2,032	2,390

(Continued on page 51)

2003 Earned Income Credit (EIC) Table—Continued

(Caution. This is not a tax table.)

If the amount you are looking up from the worksheet is—		And your filing status is—						If the amount you are looking up from the worksheet is—		And your filing status is—					
		Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—					Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—		
		No children	One child	Two children	No children	One child	Two children			No children	One child	Two children	No children	One child	Two children
At least	But less than	Your credit is—			Your credit is—			At least	But less than	Your credit is—			Your credit is—		
6,000	6,050	382	2,049	2,410	382	2,049	2,410	9,500	9,550	130	2,547	3,810	207	2,547	3,810
6,050	6,100	382	2,066	2,430	382	2,066	2,430	9,550	9,600	127	2,547	3,830	203	2,547	3,830
6,100	6,150	382	2,083	2,450	382	2,083	2,450	9,600	9,650	123	2,547	3,850	199	2,547	3,850
6,150	6,200	382	2,100	2,470	382	2,100	2,470	9,650	9,700	119	2,547	3,870	195	2,547	3,870
6,200	6,250	382	2,117	2,490	382	2,117	2,490	9,700	9,750	115	2,547	3,890	192	2,547	3,890
6,250	6,300	379	2,134	2,510	382	2,134	2,510	9,750	9,800	111	2,547	3,910	188	2,547	3,910
6,300	6,350	375	2,151	2,530	382	2,151	2,530	9,800	9,850	107	2,547	3,930	184	2,547	3,930
6,350	6,400	371	2,168	2,550	382	2,168	2,550	9,850	9,900	104	2,547	3,950	180	2,547	3,950
6,400	6,450	368	2,185	2,570	382	2,185	2,570	9,900	9,950	100	2,547	3,970	176	2,547	3,970
6,450	6,500	364	2,202	2,590	382	2,202	2,590	9,950	10,000	96	2,547	3,990	173	2,547	3,990
6,500	6,550	360	2,219	2,610	382	2,219	2,610	10,000	10,050	92	2,547	4,010	169	2,547	4,010
6,550	6,600	356	2,236	2,630	382	2,236	2,630	10,050	10,100	88	2,547	4,030	165	2,547	4,030
6,600	6,650	352	2,253	2,650	382	2,253	2,650	10,100	10,150	85	2,547	4,050	161	2,547	4,050
6,650	6,700	348	2,270	2,670	382	2,270	2,670	10,150	10,200	81	2,547	4,070	157	2,547	4,070
6,700	6,750	345	2,287	2,690	382	2,287	2,690	10,200	10,250	77	2,547	4,090	153	2,547	4,090
6,750	6,800	341	2,304	2,710	382	2,304	2,710	10,250	10,300	73	2,547	4,110	150	2,547	4,110
6,800	6,850	337	2,321	2,730	382	2,321	2,730	10,300	10,350	69	2,547	4,130	146	2,547	4,130
6,850	6,900	333	2,338	2,750	382	2,338	2,750	10,350	10,400	65	2,547	4,150	142	2,547	4,150
6,900	6,950	329	2,355	2,770	382	2,355	2,770	10,400	10,450	62	2,547	4,170	138	2,547	4,170
6,950	7,000	326	2,372	2,790	382	2,372	2,790	10,450	10,500	58	2,547	4,190	134	2,547	4,190
7,000	7,050	322	2,389	2,810	382	2,389	2,810	10,500	10,550	54	2,547	4,204	130	2,547	4,204
7,050	7,100	318	2,406	2,830	382	2,406	2,830	10,550	10,600	50	2,547	4,204	127	2,547	4,204
7,100	7,150	314	2,423	2,850	382	2,423	2,850	10,600	10,650	46	2,547	4,204	123	2,547	4,204
7,150	7,200	310	2,440	2,870	382	2,440	2,870	10,650	10,700	42	2,547	4,204	119	2,547	4,204
7,200	7,250	306	2,457	2,890	382	2,457	2,890	10,700	10,750	39	2,547	4,204	115	2,547	4,204
7,250	7,300	303	2,474	2,910	379	2,474	2,910	10,750	10,800	35	2,547	4,204	111	2,547	4,204
7,300	7,350	299	2,491	2,930	375	2,491	2,930	10,800	10,850	31	2,547	4,204	107	2,547	4,204
7,350	7,400	295	2,508	2,950	371	2,508	2,950	10,850	10,900	27	2,547	4,204	104	2,547	4,204
7,400	7,450	291	2,525	2,970	368	2,525	2,970	10,900	10,950	23	2,547	4,204	100	2,547	4,204
7,450	7,500	287	2,542	2,990	364	2,542	2,990	10,950	11,000	20	2,547	4,204	96	2,547	4,204
7,500	7,550	283	2,547	3,010	360	2,547	3,010	11,000	11,050	16	2,547	4,204	92	2,547	4,204
7,550	7,600	280	2,547	3,030	356	2,547	3,030	11,050	11,100	12	2,547	4,204	88	2,547	4,204
7,600	7,650	276	2,547	3,050	352	2,547	3,050	11,100	11,150	8	2,547	4,204	85	2,547	4,204
7,650	7,700	272	2,547	3,070	348	2,547	3,070	11,150	11,200	4	2,547	4,204	81	2,547	4,204
7,700	7,750	268	2,547	3,090	345	2,547	3,090	11,200	11,250	*	2,547	4,204	77	2,547	4,204
7,750	7,800	264	2,547	3,110	341	2,547	3,110	11,250	11,300	0	2,547	4,204	73	2,547	4,204
7,800	7,850	260	2,547	3,130	337	2,547	3,130	11,300	11,350	0	2,547	4,204	69	2,547	4,204
7,850	7,900	257	2,547	3,150	333	2,547	3,150	11,350	11,400	0	2,547	4,204	65	2,547	4,204
7,900	7,950	253	2,547	3,170	329	2,547	3,170	11,400	11,450	0	2,547	4,204	62	2,547	4,204
7,950	8,000	249	2,547	3,190	326	2,547	3,190	11,450	11,500	0	2,547	4,204	58	2,547	4,204
8,000	8,050	245	2,547	3,210	322	2,547	3,210	11,500	11,550	0	2,547	4,204	54	2,547	4,204
8,050	8,100	241	2,547	3,230	318	2,547	3,230	11,550	11,600	0	2,547	4,204	50	2,547	4,204
8,100	8,150	238	2,547	3,250	314	2,547	3,250	11,600	11,650	0	2,547	4,204	46	2,547	4,204
8,150	8,200	234	2,547	3,270	310	2,547	3,270	11,650	11,700	0	2,547	4,204	42	2,547	4,204
8,200	8,250	230	2,547	3,290	306	2,547	3,290	11,700	11,750	0	2,547	4,204	39	2,547	4,204
8,250	8,300	226	2,547	3,310	303	2,547	3,310	11,750	11,800	0	2,547	4,204	35	2,547	4,204
8,300	8,350	222	2,547	3,330	299	2,547	3,330	11,800	11,850	0	2,547	4,204	31	2,547	4,204
8,350	8,400	218	2,547	3,350	295	2,547	3,350	11,850	11,900	0	2,547	4,204	27	2,547	4,204
8,400	8,450	215	2,547	3,370	291	2,547	3,370	11,900	11,950	0	2,547	4,204	23	2,547	4,204
8,450	8,500	211	2,547	3,390	287	2,547	3,390	11,950	12,000	0	2,547	4,204	20	2,547	4,204
8,500	8,550	207	2,547	3,410	283	2,547	3,410	12,000	12,050	0	2,547	4,204	16	2,547	4,204
8,550	8,600	203	2,547	3,430	280	2,547	3,430	12,050	12,100	0	2,547	4,204	12	2,547	4,204
8,600	8,650	199	2,547	3,450	276	2,547	3,450	12,100	12,150	0	2,547	4,204	8	2,547	4,204
8,650	8,700	195	2,547	3,470	272	2,547	3,470	12,150	12,200	0	2,547	4,204	4	2,547	4,204
8,700	8,750	192	2,547	3,490	268	2,547	3,490	12,200	12,250	0	2,547	4,204	*	2,547	4,204
8,750	8,800	188	2,547	3,510	264	2,547	3,510	12,250	13,750	0	2,547	4,204	0	2,547	4,204
8,800	8,850	184	2,547	3,530	260	2,547	3,530	13,750	13,800	0	2,539	4,195	0	2,547	4,204
8,850	8,900	180	2,547	3,550	257	2,547	3,550	13,800	13,850	0	2,531	4,184	0	2,547	4,204
8,900	8,950	176	2,547	3,570	253	2,547	3,570	13,850	13,900	0	2,523	4,173	0	2,547	4,204
8,950	9,000	173	2,547	3,590	249	2,547	3,590	13,900	13,950	0	2,515	4,163	0	2,547	4,204
9,000	9,050	169	2,547	3,610	245	2,547	3,610	13,950	14,000	0	2,507	4,152	0	2,547	4,204
9,050	9,100	165	2,547	3,630	241	2,547	3,630	14,000	14,050	0	2,499	4,142	0	2,547	4,204
9,100	9,150	161	2,547	3,650	238	2,547	3,650	14,050	14,100	0	2,491	4,131	0	2,547	4,204
9,150	9,200	157	2,547	3,670	234	2,547	3,670	14,100	14,150	0	2,483	4,121	0	2,547	4,204
9,200	9,250	153	2,547	3,690	230	2,547	3,690	14,150	14,200	0	2,475	4,110	0	2,547	4,204
9,250	9,300	150	2,547	3,710	226	2,547	3,710	14,200	14,250	0	2,467	4,100	0	2,547	4,204
9,300	9,350	146	2,547	3,730	222	2,547	3,730	14,250	14,300	0	2,460	4,089	0	2,547	4,204
9,350	9,400	142	2,547	3,750	218	2,547	3,750	14,300	14,350	0	2,452	4,079	0	2,547	4,204
9,400															

2003 Earned Income Credit (EIC) Table—Continued (Caution. This is not a tax table.)

If the amount you are looking up from the worksheet is—		And your filing status is—						If the amount you are looking up from the worksheet is—		And your filing status is—					
		Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—					Single, head of household, or qualifying widow(er) and you have—			Married filing jointly and you have—		
		No children	One child	Two children	No children	One child	Two children			No children	One child	Two children	No children	One child	Two children
At least	But less than	Your credit is—			Your credit is—			At least	But less than	Your credit is—			Your credit is—		
28,450	28,500	0	190	1,099	0	350	1,309	31,950	32,000	0	0	362	0	0	572
28,500	28,550	0	182	1,088	0	342	1,299	32,000	32,050	0	0	351	0	0	562
28,550	28,600	0	174	1,078	0	334	1,288	32,050	32,100	0	0	341	0	0	551
28,600	28,650	0	166	1,067	0	326	1,278	32,100	32,150	0	0	330	0	0	541
28,650	28,700	0	158	1,057	0	318	1,267	32,150	32,200	0	0	319	0	0	530
28,700	28,750	0	150	1,046	0	310	1,257	32,200	32,250	0	0	309	0	0	520
28,750	28,800	0	142	1,036	0	302	1,246	32,250	32,300	0	0	298	0	0	509
28,800	28,850	0	134	1,025	0	294	1,236	32,300	32,350	0	0	288	0	0	498
28,850	28,900	0	126	1,014	0	286	1,225	32,350	32,400	0	0	277	0	0	488
28,900	28,950	0	118	1,004	0	278	1,215	32,400	32,450	0	0	267	0	0	477
28,950	29,000	0	110	993	0	270	1,204	32,450	32,500	0	0	256	0	0	467
29,000	29,050	0	102	983	0	262	1,193	32,500	32,550	0	0	246	0	0	456
29,050	29,100	0	94	972	0	254	1,183	32,550	32,600	0	0	235	0	0	446
29,100	29,150	0	86	962	0	246	1,172	32,600	32,650	0	0	225	0	0	435
29,150	29,200	0	78	951	0	238	1,162	32,650	32,700	0	0	214	0	0	425
29,200	29,250	0	70	941	0	230	1,151	32,700	32,750	0	0	204	0	0	414
29,250	29,300	0	63	930	0	222	1,141	32,750	32,800	0	0	193	0	0	404
29,300	29,350	0	55	920	0	214	1,130	32,800	32,850	0	0	183	0	0	393
29,350	29,400	0	47	909	0	206	1,120	32,850	32,900	0	0	172	0	0	383
29,400	29,450	0	39	899	0	198	1,109	32,900	32,950	0	0	162	0	0	372
29,450	29,500	0	31	888	0	190	1,099	32,950	33,000	0	0	151	0	0	362
29,500	29,550	0	23	878	0	182	1,088	33,000	33,050	0	0	140	0	0	351
29,550	29,600	0	15	867	0	174	1,078	33,050	33,100	0	0	130	0	0	341
29,600	29,650	0	7	857	0	166	1,067	33,100	33,150	0	0	119	0	0	330
29,650	29,700	0	**	846	0	158	1,057	33,150	33,200	0	0	109	0	0	319
29,700	29,750	0	0	835	0	150	1,046	33,200	33,250	0	0	98	0	0	309
29,750	29,800	0	0	825	0	142	1,036	33,250	33,300	0	0	88	0	0	298
29,800	29,850	0	0	814	0	134	1,025	33,300	33,350	0	0	77	0	0	288
29,850	29,900	0	0	804	0	126	1,014	33,350	33,400	0	0	67	0	0	277
29,900	29,950	0	0	793	0	118	1,004	33,400	33,450	0	0	56	0	0	267
29,950	30,000	0	0	783	0	110	993	33,450	33,500	0	0	46	0	0	256
30,000	30,050	0	0	772	0	102	983	33,500	33,550	0	0	35	0	0	246
30,050	30,100	0	0	762	0	94	972	33,550	33,600	0	0	25	0	0	235
30,100	30,150	0	0	751	0	86	962	33,600	33,650	0	0	14	0	0	225
30,150	30,200	0	0	741	0	78	951	33,650	33,700	0	0	***	0	0	214
30,200	30,250	0	0	730	0	70	941	33,700	33,750	0	0	0	0	0	204
30,250	30,300	0	0	720	0	63	930	33,750	33,800	0	0	0	0	0	193
30,300	30,350	0	0	709	0	55	920	33,800	33,850	0	0	0	0	0	183
30,350	30,400	0	0	699	0	47	909	33,850	33,900	0	0	0	0	0	172
30,400	30,450	0	0	688	0	39	899	33,900	33,950	0	0	0	0	0	162
30,450	30,500	0	0	678	0	31	888	33,950	34,000	0	0	0	0	0	151
30,500	30,550	0	0	667	0	23	878	34,000	34,050	0	0	0	0	0	140
30,550	30,600	0	0	656	0	15	867	34,050	34,100	0	0	0	0	0	130
30,600	30,650	0	0	646	0	7	857	34,100	34,150	0	0	0	0	0	119
30,650	30,700	0	0	635	0	**	846	34,150	34,200	0	0	0	0	0	109
30,700	30,750	0	0	625	0	0	835	34,200	34,250	0	0	0	0	0	98
30,750	30,800	0	0	614	0	0	825	34,250	34,300	0	0	0	0	0	88
30,800	30,850	0	0	604	0	0	814	34,300	34,350	0	0	0	0	0	77
30,850	30,900	0	0	593	0	0	804	34,350	34,400	0	0	0	0	0	67
30,900	30,950	0	0	583	0	0	793	34,400	34,450	0	0	0	0	0	56
30,950	31,000	0	0	572	0	0	783	34,450	34,500	0	0	0	0	0	46
31,000	31,050	0	0	562	0	0	772	34,500	34,550	0	0	0	0	0	35
31,050	31,100	0	0	551	0	0	762	34,550	34,600	0	0	0	0	0	25
31,100	31,150	0	0	541	0	0	751	34,600	34,650	0	0	0	0	0	14
31,150	31,200	0	0	530	0	0	741	34,650	34,692	0	0	0	0	0	4
31,200	31,250	0	0	520	0	0	730	34,692 or more		0	0	0	0	0	0
31,250	31,300	0	0	509	0	0	720								
31,300	31,350	0	0	498	0	0	709								
31,350	31,400	0	0	488	0	0	699								
31,400	31,450	0	0	477	0	0	688								
31,450	31,500	0	0	467	0	0	678								
31,500	31,550	0	0	456	0	0	667								
31,550	31,600	0	0	446	0	0	656								
31,600	31,650	0	0	435	0	0	646								
31,650	31,700	0	0	425	0	0	635								
31,700	31,750	0	0	414	0	0	625								
31,750	31,800	0	0	404	0	0	614								
31,800	31,850	0	0	393	0	0	604								
31,850	31,900	0	0	383	0	0	593								
31,900	31,950	0	0	372	0	0	583								

**If the amount you are looking up from the worksheet is at least \$29,650 (\$30,650 if married filing jointly) but less than \$29,666 (\$30,666 if married filing jointly), your credit is \$1. Otherwise, you cannot take the credit.

***If the amount you are looking up from the worksheet is at least \$33,650 but less than \$33,692, your credit is \$4. Otherwise, you cannot take the credit.

STUDENT NOTES

If line 40 (taxable income) is—	And you are—					If line 40 (taxable income) is—	And you are—					If line 40 (taxable income) is—	And you are—							
	At least	But less than	Single	Married filing jointly *	Married filing sepa- rately		Head of a house- hold	At least	But less than	Single	Married filing jointly *		Married filing sepa- rately	Head of a house- hold	At least	But less than	Single	Married filing jointly *	Married filing sepa- rately	Head of a house- hold
14,000						17,000						20,000								
14,000	14,050	1,754	1,404	1,754	1,604	17,000	17,050	2,204	1,854	2,204	2,054	20,000	20,050	2,654	2,304	2,654	2,504			
15,000						18,000						21,000								
15,000	15,050	1,904	1,554	1,904	1,754	18,000	18,050	2,354	2,004	2,354	2,204	21,000	21,050	2,804	2,454	2,804	2,654			
16,000						19,000						22,000								
16,000	16,050	2,054	1,704	2,054	1,904	19,000	19,050	2,504	2,154	2,504	2,354	22,000	22,050	2,954	2,604	2,954	2,804			

* This column must also be used by a qualifying widow(er).

(Continued on page 66)

2003 Tax Table—Continued

If line 40 (taxable income) is—		And you are—				If line 40 (taxable income) is—		And you are—				If line 40 (taxable income) is—		And you are—			
		Single	Married filing jointly *	Married filing separately	Head of a household			Single	Married filing jointly *	Married filing separately	Head of a household			Single	Married filing jointly *	Married filing separately	Head of a household
		Your tax is—						Your tax is—						Your tax is—			
23,000		26,000				29,000											
23,000	23,050	3,104	2,754	3,104	2,954	26,000	26,050	3,554	3,204	3,554	3,404	29,000	29,050	4,066	3,654	4,066	3,854
24,000		27,000				30,000											
24,000	24,050	3,254	2,904	3,254	3,104	27,000	27,050	3,704	3,354	3,704	3,554	30,000	30,050	4,316	3,804	4,316	4,004
25,000		28,000				31,000											
25,000	25,050	3,404	3,054	3,404	3,254	28,000	28,050	3,854	3,504	3,854	3,704	31,000	31,050	4,566	3,954	4,566	4,154
26,000		29,000				32,000											
26,000	26,050	3,554	3,204	3,554	3,404	29,000	29,050	4,066	3,654	4,066	3,854	32,000	32,050	4,816	4,204	4,816	4,392

* This column must also be used by a qualifying widow(er).

(Continued on page 67)

2003 Tax Table—Continued

If line 40 (taxable income) is—		And you are—				If line 40 (taxable income) is—		And you are—				If line 40 (taxable income) is—		And you are—					
		Single	Married filing jointly *	Married filing sepa- rately	Head of a house- hold			Single	Married filing jointly *	Married filing sepa- rately	Head of a house- hold			Single	Married filing jointly *	Married filing sepa- rately	Head of a house- hold		
At least	But less than	Your tax is—				Your tax is—				Your tax is—									
41,000		44,000				47,000				42,000		45,000				48,000			
41,000	41,050	7,066	5,454	7,066	5,951	44,000	44,050	7,816	5,904	7,816	6,701	47,000	47,050	8,566	6,354	8,566	7,451		
41,050	41,100	7,079	5,461	7,079	5,964	44,050	44,100	7,829	5,911	7,829	6,714	47,050	47,100	8,579	6,361	8,579	7,464		
41,100	41,150	7,091	5,469	7,091	5,976	44,100	44,150	7,841	5,919	7,841	6,726	47,100	47,150	8,591	6,369	8,591	7,476		
41,150	41,200	7,104	5,476	7,104	5,989	44,150	44,200	7,854	5,926	7,854	6,739	47,150	47,200	8,604	6,376	8,604	7,489		
41,200	41,250	7,116	5,484	7,116	6,001	44,200	44,250	7,866	5,934	7,866	6,751	47,200	47,250	8,616	6,384	8,616	7,501		
41,250	41,300	7,129	5,491	7,129	6,014	44,250	44,300	7,879	5,941	7,879	6,764	47,250	47,300	8,629	6,391	8,629	7,514		
41,300	41,350	7,141	5,499	7,141	6,026	44,300	44,350	7,891	5,949	7,891	6,776	47,300	47,350	8,641	6,399	8,641	7,526		
41,350	41,400	7,154	5,506	7,154	6,039	44,350	44,400	7,904	5,956	7,904	6,789	47,350	47,400	8,654	6,406	8,654	7,539		
41,400	41,450	7,166	5,514	7,166	6,051	44,400	44,450	7,916	5,964	7,916	6,801	47,400	47,450	8,666	6,414	8,666	7,551		
41,450	41,500	7,179	5,521	7,179	6,064	44,450	44,500	7,929	5,971	7,929	6,814	47,450	47,500	8,679	6,421	8,679	7,564		
41,500	41,550	7,191	5,529	7,191	6,076	44,500	44,550	7,941	5,979	7,941	6,826	47,500	47,550	8,691	6,429	8,691	7,576		
41,550	41,600	7,204	5,536	7,204	6,089	44,550	44,600	7,954	5,986	7,954	6,839	47,550	47,600	8,704	6,436	8,704	7,589		
41,600	41,650	7,216	5,544	7,216	6,101	44,600	44,650	7,966	5,994	7,966	6,851	47,600	47,650	8,716	6,444	8,716	7,601		
41,650	41,700	7,229	5,551	7,229	6,114	44,650	44,700	7,979	6,001	7,979	6,864	47,650	47,700	8,729	6,451	8,729	7,614		
41,700	41,750	7,241	5,559	7,241	6,126	44,700	44,750	7,991	6,009	7,991	6,876	47,700	47,750	8,741	6,459	8,741	7,626		
41,750	41,800	7,254	5,566	7,254	6,139	44,750	44,800	8,004	6,016	8,004	6,889	47,750	47,800	8,754	6,466	8,754	7,639		
41,800	41,850	7,266	5,574	7,266	6,151	44,800	44,850	8,016	6,024	8,016	6,901	47,800	47,850	8,766	6,474	8,766	7,651		
41,850	41,900	7,279	5,581	7,279	6,164	44,850	44,900	8,029	6,031	8,029	6,914	47,850	47,900	8,779	6,481	8,779	7,664		
41,900	41,950	7,291	5,589	7,291	6,176	44,900	44,950	8,041	6,039	8,041	6,926	47,900	47,950	8,791	6,489	8,791	7,676		
41,950	42,000	7,304	5,596	7,304	6,189	44,950	45,000	8,054	6,046	8,054	6,939	47,950	48,000	8,804	6,496	8,804	7,689		
43,000		46,000				49,000				42,800		45,800				48,800			
43,000	43,050	7,566	5,754	7,566	6,451	46,000	46,050	8,316	6,204	8,316	7,201	49,000	49,050	9,066	6,654	9,066	7,951		
43,050	43,100	7,579	5,761	7,579	6,464	46,050	46,100	8,329	6,211	8,329	7,214	49,050	49,100	9,079	6,661	9,079	7,964		
43,100	43,150	7,591	5,769	7,591	6,476	46,100	46,150	8,341	6,219	8,341	7,226	49,100	49,150	9,091	6,669	9,091	7,976		
43,150	43,200	7,604	5,776	7,604	6,489	46,150	46,200	8,354	6,226	8,354	7,239	49,150	49,200	9,104	6,676	9,104	7,989		
43,200	43,250	7,616	5,784	7,616	6,501	46,200	46,250	8,366	6,234	8,366	7,251	49,200	49,250	9,116	6,684	9,116	8,001		
43,250	43,300	7,629	5,791	7,629	6,514	46,250	46,300	8,379	6,241	8,379	7,264	49,250	49,300	9,129	6,691	9,129	8,014		
43,300	43,350	7,641	5,799	7,641	6,526	46,300	46,350	8,391	6,249	8,391	7,276	49,300	49,350	9,141	6,699	9,141	8,026		
43,350	43,400	7,654	5,806	7,654	6,539	46,350	46,400	8,404	6,256	8,404	7,289	49,350	49,400	9,154	6,706	9,154	8,039		
43,400	43,450	7,666	5,814	7,666	6,551	46,400	46,450	8,416	6,264	8,416	7,301	49,400	49,450	9,166	6,714	9,166	8,051		
43,450	43,500	7,679	5,821	7,679	6,564	46,450	46,500	8,429	6,271	8,429	7,314	49,450	49,500	9,179	6,721	9,179	8,064		
43,500	43,550	7,691	5,829	7,691	6,576	46,500	46,550	8,441	6,279	8,441	7,326	49,500	49,550	9,191	6,729	9,191	8,076		
43,550	43,600	7,704	5,836	7,704	6,589	46,550	46,600	8,454	6,286	8,454	7,339	49,550	49,600	9,204	6,736	9,204	8,089		
43,600	43,650	7,716	5,844	7,716	6,601	46,600	46,650	8,466	6,294	8,466	7,351	49,600	49,650	9,216	6,744	9,216	8,101		
43,650	43,700	7,729	5,851	7,729	6,614	46,650	46,700	8,479	6,301	8,479	7,364	49,650	49,700	9,229	6,751	9,229	8,114		
43,700	43,750	7,741	5,859	7,741	6,626	46,700	46,750	8,491	6,309	8,491	7,376	49,700	49,750	9,241	6,759	9,241	8,126		
43,750	43,800	7,754	5,866	7,754	6,639	46,750	46,800	8,504	6,316	8,504	7,389	49,750	49,800	9,254	6,766	9,254	8,139		
43,800	43,850	7,766	5,874	7,766	6,651	46,800	46,850	8,516	6,324	8,516	7,401	49,800	49,850	9,266	6,774	9,266	8,151		
43,850	43,900	7,779	5,881	7,779	6,664	46,850	46,900	8,529	6,331	8,529	7,414	49,850	49,900	9,279	6,781	9,279	8,164		
43,900	43,950	7,791	5,889	7,791	6,676	46,900	46,950	8,541	6,339	8,541	7,426	49,900	49,950	9,291	6,789	9,291	8,176		
43,950	44,000	7,804	5,896	7,804	6,689	46,950	47,000	8,554	6,346	8,554	7,439	49,950	50,000	9,304	6,796	9,304	8,189		

* This column must also be used by a qualifying widow(er).

(Continued on page 69)

2003 Tax Table—Continued

If line 40 (taxable income) is—		And you are—				If line 40 (taxable income) is—		And you are—							
		Single	Married filing jointly *	Married filing separately	Head of a household			Single	Married filing jointly *	Married filing separately	Head of a household				
At least	But less than	Your tax is—				At least	But less than	Your tax is—							
95,000					98,000										
95,000	95,050	21,353	17,376	22,081	19,451	98,000	98,050	22,193	18,126	23,071	20,201				
95,050	95,100	21,367	17,389	22,098	19,464	98,050	98,100	22,207	18,139	23,088	20,214				
95,100	95,150	21,381	17,401	22,114	19,476	98,100	98,150	22,221	18,151	23,104	20,226				
95,150	95,200	21,395	17,414	22,131	19,489	98,150	98,200	22,235	18,164	23,121	20,239				
95,200	95,250	21,409	17,426	22,147	19,501	98,200	98,250	22,249	18,176	23,137	20,251				
95,250	95,300	21,423	17,439	22,164	19,514	98,250	98,300	22,263	18,189	23,154	20,265				
95,300	95,350	21,437	17,451	22,180	19,526	98,300	98,350	22,277	18,201	23,170	20,279				
95,350	95,400	21,451	17,464	22,197	19,539	98,350	98,400	22,291	18,214	23,187	20,293				
95,400	95,450	21,465	17,476	22,213	19,551	98,400	98,450	22,305	18,226	23,203	20,307				
95,450	95,500	21,479	17,489	22,230	19,564	98,450	98,500	22,319	18,239	23,220	20,321				
95,500	95,550	21,493	17,501	22,246	19,576	98,500	98,550	22,333	18,251	23,236	20,335				
95,550	95,600	21,507	17,514	22,263	19,589	98,550	98,600	22,347	18,264	23,253	20,349				
95,600	95,650	21,521	17,526	22,279	19,601	98,600	98,650	22,361	18,276	23,269	20,363				
95,650	95,700	21,535	17,539	22,296	19,614	98,650	98,700	22,375	18,289	23,286	20,377				
95,700	95,750	21,549	17,551	22,312	19,626	98,700	98,750	22,389	18,301	23,302	20,391				
95,750	95,800	21,563	17,564	22,329	19,639	98,750	98,800	22,403	18,314	23,319	20,405				
95,800	95,850	21,577	17,576	22,345	19,651	98,800	98,850	22,417	18,326	23,335	20,419				
95,850	95,900	21,591	17,589	22,362	19,664	98,850	98,900	22,431	18,339	23,352	20,433				
95,900	95,950	21,605	17,601	22,378	19,676	98,900	98,950	22,445	18,351	23,368	20,447				
95,950	96,000	21,619	17,614	22,395	19,689	98,950	99,000	22,459	18,364	23,385	20,461				
96,000					99,000										
96,000	96,050	21,633	17,626	22,411	19,701	99,000	99,050	22,473	18,376	23,401	20,475				
96,050	96,100	21,647	17,639	22,428	19,714	99,050	99,100	22,487	18,389	23,418	20,489				
96,100	96,150	21,661	17,651	22,444	19,726	99,100	99,150	22,501	18,401	23,434	20,503				
96,150	96,200	21,675	17,664	22,461	19,739	99,150	99,200	22,515	18,414	23,451	20,517				
96,200	96,250	21,689	17,676	22,477	19,751	99,200	99,250	22,529	18,426	23,467	20,531				
96,250	96,300	21,703	17,689	22,494	19,764	99,250	99,300	22,543	18,439	23,484	20,545				
96,300	96,350	21,717	17,701	22,510	19,776	99,300	99,350	22,557	18,451	23,500	20,559				
96,350	96,400	21,731	17,714	22,527	19,789	99,350	99,400	22,571	18,464	23,517	20,573				
96,400	96,450	21,745	17,726	22,543	19,801	99,400	99,450	22,585	18,476	23,533	20,587				
96,450	96,500	21,759	17,739	22,560	19,814	99,450	99,500	22,599	18,489	23,550	20,601				
96,500	96,550	21,773	17,751	22,576	19,826	99,500	99,550	22,613	18,501	23,566	20,615				
96,550	96,600	21,787	17,764	22,593	19,839	99,550	99,600	22,627	18,514	23,583	20,629				
96,600	96,650	21,801	17,776	22,609	19,851	99,600	99,650	22,641	18,526	23,599	20,643				
96,650	96,700	21,815	17,789	22,626	19,864	99,650	99,700	22,655	18,539	23,616	20,657				
96,700	96,750	21,829	17,801	22,642	19,876	99,700	99,750	22,669	18,551	23,632	20,671				
96,750	96,800	21,843	17,814	22,659	19,889	99,750	99,800	22,683	18,564	23,649	20,685				
96,800	96,850	21,857	17,826	22,675	19,901	99,800	99,850	22,697	18,576	23,665	20,699				
96,850	96,900	21,871	17,839	22,692	19,914	99,850	99,900	22,711	18,589	23,682	20,713				
96,900	96,950	21,885	17,851	22,708	19,926	99,900	99,950	22,725	18,601	23,698	20,727				
96,950	97,000	21,899	17,864	22,725	19,939	99,950	100,000	22,739	18,614	23,715	20,741				
97,000										<div style="border: 1px solid black; border-radius: 50%; padding: 20px; width: fit-content; margin: 0 auto;"> <p>\$100,000 or over — use the Tax Rate Schedules on page 75</p> </div>					
97,000	97,050	21,913	17,876	22,741	19,951										
97,050	97,100	21,927	17,889	22,758	19,964										
97,100	97,150	21,941	17,901	22,774	19,976										
97,150	97,200	21,955	17,914	22,791	19,989										
97,200	97,250	21,969	17,926	22,807	20,001										
97,250	97,300	21,983	17,939	22,824	20,014										
97,300	97,350	21,997	17,951	22,840	20,026										
97,350	97,400	22,011	17,964	22,857	20,039										
97,400	97,450	22,025	17,976	22,873	20,051										
97,450	97,500	22,039	17,989	22,890	20,064										
97,500	97,550	22,053	18,001	22,906	20,076										
97,550	97,600	22,067	18,014	22,923	20,089										
97,600	97,650	22,081	18,026	22,939	20,101										
97,650	97,700	22,095	18,039	22,956	20,114										
97,700	97,750	22,109	18,051	22,972	20,126										
97,750	97,800	22,123	18,064	22,989	20,139										
97,800	97,850	22,137	18,076	23,005	20,151										
97,850	97,900	22,151	18,089	23,022	20,164										
97,900	97,950	22,165	18,101	23,038	20,176										
97,950	98,000	22,179	18,114	23,055	20,189										

* This column must also be used by a qualifying widow(er).

2003 Tax Rate Schedules



Use **only** if your taxable income (Form 1040, line 40) is \$100,000 or more. If less, use the **Tax Table**. Even though you cannot use the Tax Rate Schedules below if your taxable income is less than \$100,000, all levels of taxable income are shown so taxpayers can see the tax rate that applies to each level.

Schedule X—Use if your filing status is **Single**

If the amount on Form 1040, line 40, is: Over—	But not over—	Enter on Form 1040, line 41	of the amount over—
\$0	\$7,000	..... 10%	\$0
7,000	28,400	\$700.00 + 15%	7,000
28,400	68,800	3,910.00 + 25%	28,400
68,800	143,500	14,010.00 + 28%	68,800
143,500	311,950	34,926.00 + 33%	143,500
311,950	.....	90,514.50 + 35%	311,950

Schedule Y-1—Use if your filing status is **Married filing jointly** or **Qualifying widow(er)**

If the amount on Form 1040, line 40, is: Over—	But not over—	Enter on Form 1040, line 41	of the amount over—
\$0	\$14,000	..... 10%	\$0
14,000	56,800	\$1,400.00 + 15%	14,000
56,800	114,650	7,820.00 + 25%	56,800
114,650	174,700	22,282.50 + 28%	114,650
174,700	311,950	39,096.50 + 33%	174,700
311,950	.....	84,389.00 + 35%	311,950

Schedule Y-2—Use if your filing status is **Married filing separately**

If the amount on Form 1040, line 40, is: Over—	But not over—	Enter on Form 1040, line 41	of the amount over—
\$0	\$7,000	..... 10%	\$0
7,000	28,400	\$700.00 + 15%	7,000
28,400	57,325	3,910.00 + 25%	28,400
57,325	87,350	11,141.25 + 28%	57,325
87,350	155,975	19,548.25 + 33%	87,350
155,975	.....	42,194.50 + 35%	155,975

Schedule Z—Use if your filing status is **Head of household**

If the amount on Form 1040, line 40, is: Over—	But not over—	Enter on Form 1040, line 41	of the amount over—
\$0	\$10,000	..... 10%	\$0
10,000	38,050	\$1,000.00 + 15%	10,000
38,050	98,250	5,207.50 + 25%	38,050
98,250	159,100	20,257.50 + 28%	98,250
159,100	311,950	37,295.50 + 33%	159,100
311,950	87,736.00 + 35%	311,950

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STUDENT NOTES

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