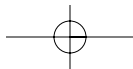
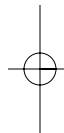
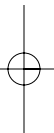
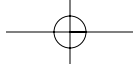


PART I

The Income Tax Return

The five chapters in this part provide basic information on the tax system. They take you through the first steps of filling out a tax return—such as deciding what your filing status is, how many exemptions you can take, and which form to file. They also discuss recordkeeping requirements, IRS e-file (electronic filing), certain penalties, and the two methods used to pay tax during the year: withholding and estimated tax.

- Chapter 1** Filing Information
- Chapter 2** Filing Status
- Chapter 3** Personal Exemptions and Dependents
- Chapter 4** Decedents
- Chapter 5** Tax Withholding and Estimated Tax



1

Filing Information

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Introduction

Unlike the other certainty in life, paying taxes is the one for which you may obtain an extension. Besides explaining when you must file your tax return and what to do if you are unable to get it prepared on time, this chapter provides an introduction to the basic framework within which you file your federal income tax return. It answers a lot of the elementary questions about the procedures and calculations involved in determining your income tax.

This chapter discusses such items as who is required to file and who should file even though he or she is not required to do so. It tells you which forms to use, how

to go about preparing your tax return once you have obtained the correct forms, and where to mail your tax return once it has been completed. In addition, the chapter informs you about the penalties that may be imposed if you do not pay your taxes on time and instructs you on what to do if you discover that a previous tax return is in error. The chapter also explains what the different accounting methods are and which method may be used in preparing your return.

Remember, one of the most important features of this book is Chapter 48, 2003 Federal Tax Forms and Schedules You Can Use.

Important Changes

Who must file. Generally, the amount of income you can receive before you must file a return has been increased. See *Table 1-1*, *Table 1-2*, and *Table 1-3* for the specific amounts.

Mailing your return. You may be mailing your return to a different address this year because the IRS has changed the filing location for several areas. If you received an envelope with your tax package, please use it. Otherwise, see *Where Do I File*, later in this chapter.

Important Reminders

Alternative filing methods. Rather than filing a return on paper, you may be able to file electronically using IRS *e-file*. Create your own personal identification number (PIN) and file a completely paperless tax return. For more information, see *Does My Return Have To Be on Paper*, later.

Change of address. If you change your address, you should notify the IRS. See *Change of Address*, later, under *What Happens After I File*.

4 THE INCOME TAX RETURN

Write in your social security number. You must write your social security number (SSN) in the spaces provided on your tax return. If you file a joint return, write the SSNs in the same order as the names.

Direct Deposit of refund. Instead of getting a paper check, you may be able to have your refund deposited directly into your account at a bank or other financial institution. See *Direct Deposit* under *Refunds*, later.

Alternative payment methods. If you owe additional tax, you may be able to pay electronically. See *How To Pay*, later.

Installment agreement. If you cannot pay the full amount due with your return, you may ask to make monthly installment payments. See *Installment Agreement*, later, under *Amount You Owe*.

Service in combat zone. You are allowed extra time to take care of your tax matters if you are a member of the Armed Forces who served in a combat zone, or if you served in the combat zone in support of the Armed Forces. See *Individuals Serving in Combat Zone*, later, under *When Do I Have To File*.

Adoption taxpayer identification number. If a child has been placed in your home for purposes of legal adoption and you will not be able to get a social security number for the child in time to file your return, you may be able to get an adoption taxpayer identification number (ATIN). For more information, see *Social Security Number*, later.

Taxpayer identification number for aliens. If you or your dependent is a nonresident or resident alien who does not have and is not eligible to get a social security number, file **Form W-7, Application for IRS Individual Taxpayer Identification Number**, with the IRS. For more information, see *Social Security Number*, later.

Third party designee. You can allow the IRS to discuss your tax return with a friend, family member, or any other person you choose by checking the "Yes" box in the *Third party designee* area of your return. For more information, see *Third Party Designee*, later.

This chapter discusses:

- Whether you have to file a return,
- Which form to use,
- How to file electronically,
- When, how, and where to file your return,
- What happens if you pay too little or too much tax,
- What records you should keep and how long you should keep them, and
- How you can change a return you have already filed.

Do I Have To File a Return?

You must file a federal income tax return if you are a citizen or resident of the United States or a resident of Puerto Rico and you meet the filing requirements for any of the following categories that apply to you.

- 1) Individuals in general. (There are special rules for surviving spouses, executors, administrators, legal representatives, U.S. citizens and residents living outside the United States, residents of Puerto Rico, and individuals with income from U.S. possessions.)
- 2) Dependents.
- 3) Children under age 14.
- 4) Self-employed persons.
- 5) Aliens.

The filing requirements for each category are explained in this chapter.

The filing requirements apply even if you do not owe tax.

Tip. *Even if you do not have to file a return, it may be to your advantage to do so. See Who Should File, later.*

Caution. *File only one federal income tax return for the year regardless of how many jobs you had, how many Forms W-2 you received, or how many states you lived in during the year.*

Individuals—In General

If you are a U.S. citizen or resident, whether you must file a return depends on three factors:

- 1) Your gross income,
- 2) Your filing status, and
- 3) Your age.

To find out whether you must file, see *Table 1-1*, *Table 1-2*, and *Table 1-3*. Even if no table shows that you must file, you may need to file to get money back. (See *Who Should File*, later.)

Gross income. This includes all income you receive in the form of money, goods, property, and services that is not exempt from tax. It also includes income from sources outside the United States (even if you may exclude all or part of it). Common types of income are discussed in *Part Two* of this publication.

Community income. If you are married and your permanent home is in a community property state, half of any income described by state law as community income may be considered yours. This affects your federal taxes, including whether you must file if you do not file a joint return with your spouse. See Publication 555, *Community Property*, for more information.

Self-employed individuals. If you are self-employed, your gross income includes the amount on line 7 of Schedule C (Form 1040), *Profit or Loss From Business*, line 1 of Schedule C-EZ (Form 1040), *Net Profit From Business*, and line 11 of Schedule F (Form 1040), *Profit or Loss From Farming*. See *Self-Employed Persons*, later, for more information about your filing requirements.

Caution. *If you do not report all of your self-employment income, your social security benefits may be lower when you retire.*

Filing status. Your filing status depends on whether you are single or married and on your family situation. Your filing status is determined on the last day of your tax year, which is December 31 for most taxpayers. See chapter 2 for an explanation of each filing status.

Age. If you are 65 or older at the end of the year, you generally can have a higher amount of gross income than other taxpayers before you must file. See *Table 1-1*. You are considered 65 on the day before your 65th birthday. For example, if your 65th birthday is on January 1, 2004, you are considered 65 for 2003.

Example

You are 65 years old and earned \$11,000 of **taxable income** last year. Your husband, who is 66 years old, received a **pension** of \$6,000, all of which was **taxable income**. You and your husband legally separated on December 28. If you had been living together at the end of the year, you would not have had to file an income tax return, because your combined income was less than \$17,500. But, because you are living apart and your gross income was more than \$8,950, you must file a return.

Surviving Spouses, Executors, Administrators, and Legal Representatives

You must file a final return for a decedent (a person who died) if **both** of the following are true.

- You are the surviving spouse, executor, administrator, or legal representative.
- The decedent met the filing requirements at the date of death.

For more information on rules for filing a decedent's final return, see chapter 4.

U.S. Citizens and Residents Living Outside the United States

If you are a U.S. citizen or resident living outside the United States, you must file a return if you meet the filing requirements. For information on special tax rules that may apply to you, get Publication 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad*. It is available at

Table 1-1. 2003 Filing Requirements for Most Taxpayers

To use this table, first find your marital status at the end of 2003. Then, read across the line that shows your filing status and age at the end of 2003. You must file a return if your gross income was at least the amount shown in the last column.

Gross income means all income you received in the form of money, goods, property, and services that is not exempt from tax, including any income from sources outside the United States (even if you may exclude part or all of it).

When using this table, do not include social security benefits as gross income unless you are married filing a separate return and lived with your spouse at any time in 2003. (If you must include the benefits, see chapter 12 for the amount to include.)

Also, see *Table 1-2* and *Table 1-3* for other situations when you must file a return.

Marital Status	Filing Status	Age*	Gross Income
Single (including divorced and legally separated)	Single	under 65 65 or older	\$ 7,800 \$ 8,950
	Head of household	under 65 65 or older	\$10,050 \$11,200
Married, with a child in your home, living apart from your spouse during the last 6 months of 2003	Head of household	under 65 65 or older	\$10,050 \$11,200
		Married, joint return	under 65 (both spouses) 65 or older (one spouse) 65 or older (both spouses)
Married, living with your spouse at the end of 2003 (or on the date your spouse died)	Married, separate return	any age	\$ 3,050
	Married, joint or separate return	any age	\$ 3,050
Married, not living with your spouse at end of 2003 (or on the date your spouse died)	Single	under 65 65 or older	\$ 7,800 \$ 8,950
	Head of household	under 65 65 or older	\$10,050 \$11,200
	Qualifying widow(er) with dependent child	under 65 65 or older	\$12,550 \$13,500

*If your 65th birthday is on January 1, 2004, you are considered to be age 65 at the end of 2003.

most U.S. embassies and consulates. Also see *How To Get Tax Help* in the back of this publication.

Explanation

For more information about U.S. citizens living abroad, see Chapter 42, *U.S. Citizens Working Abroad: Tax Treatment of Foreign Earned Income*.

Residents of Puerto Rico

Generally, if you are a U.S. citizen and a resident of Puerto Rico, you must file a U.S. income tax return if you meet the filing requirements. This is in addition to any legal requirement you may have to file an income tax return for Puerto Rico.

If you are a resident of Puerto Rico for the entire year, gross income does not include income from sources within Puerto Rico, except for amounts received as an employee of the United States or a U.S. agency. If you receive income from Puerto Rican sources that is not subject to U.S. tax, you must reduce your standard deduction. As a result, the amount of income you must have before you are required to file a U.S. income tax return is lower than the applicable amount in *Table 1-1* or *Table 1-2*. For more information, see *U.S. taxation* and its discussion, *Standard deduction*, under *The Commonwealth of Puerto Rico* in Publication 570, *Tax Guide for Individuals With Income From U.S. Possessions*.

Individuals With Income From U.S. Possessions

If you had income from Guam, the Commonwealth of the Northern Mariana Islands, American Samoa, or the Virgin Islands, special rules

may apply when determining whether you must file a U.S. federal income tax return. In addition, you may have to file a return with the individual island government. See Publication 570 for more information.

Dependents

If you are a dependent (one who meets the dependency tests in chapter 3), see *Table 1-2* to find whether you must file a return. You also must file if your situation is described in *Table 1-3*.

Responsibility of parent. Generally, a child is responsible for filing his or her own tax return and for paying any tax on the return. But if a dependent child who must file an income tax return cannot file it for any reason, such as age, then a parent, guardian, or other legally responsible person must file it for the child. If the child cannot sign the return, the parent or guardian must sign the child's name followed by the words "By (your signature), parent for minor child."

Child's earnings. Amounts a child earns by performing services are his or her gross income. This is true even if under local law the child's parents have the right to the earnings and may actually have received them. If the child does not pay the tax due on this income, the parent is liable for the tax.

Explanation

For more details about **dependents**, see Chapter 3, *Personal Exemptions and Dependents*.

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Table 1-2. 2003 Filing Requirements for Dependents

See chapter 3 to find out if someone can claim you as a dependent.

<p>If your parents (or someone else) can claim you as a dependent, and any of the situations below apply to you, you must file a return. (See <i>Table 1-3</i> for other situations when you must file.)</p> <p>In this table, earned income includes salaries, wages, tips, and professional fees. It also includes taxable scholarship and fellowship grants. (See <i>Scholarship and Fellowship Grants</i> in chapter 13.) Unearned income includes investment-type income such as interest, dividends, and capital gains. It also includes unemployment compensation, taxable social security benefits, pensions, annuities, and distributions of unearned income from a trust. Gross income is the total of your earned and unearned income.</p> <p>Caution: If your gross income was \$3,050 or more, you generally cannot be claimed as a dependent unless you were under age 19 or a full-time student under age 24. For details, see <i>Gross Income Test</i> in chapter 3.</p>
<p>Single dependents — Were you either age 65 or older or blind?</p> <p><input type="checkbox"/> No. You must file a return if any of the following apply.</p> <ul style="list-style-type: none"> • Your unearned income was more than \$750. • Your earned income was more than \$4,750. • Your gross income was more than the larger of: <ul style="list-style-type: none"> • \$750, or • Your earned income (up to \$4,500) plus \$250. <p><input type="checkbox"/> Yes. You must file a return if any of the following apply.</p> <ul style="list-style-type: none"> • Your unearned income was more than \$1,900 (\$3,050 if 65 or older and blind). • Your earned income was more than \$5,900 (\$7,050 if 65 or older and blind). • Your gross income was more than \$1,150 (\$2,300 if 65 or older and blind) plus the larger of: <ul style="list-style-type: none"> • \$750, or • Your earned income (up to \$4,500) plus \$250.
<p>Married dependents — Were you either age 65 or older or blind?</p> <p><input type="checkbox"/> No. You must file a return if any of the following apply.</p> <ul style="list-style-type: none"> • Your unearned income was more than \$750. • Your earned income was more than \$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: <ul style="list-style-type: none"> • \$750, or • Your earned income (up to \$4,500) plus \$250. <p><input type="checkbox"/> Yes. You must file a return if any of the following apply.</p> <ul style="list-style-type: none"> • Your unearned income was more than \$1,700 (\$2,650 if 65 or older and blind). • Your earned income was more than \$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 \$950 (\$1,900 if 65 or older and blind) plus the larger of: <ul style="list-style-type: none"> • \$750, or • Your earned income (up to \$4,500) plus \$250.

Children Under Age 14

If a child's only income is interest and dividends (including Alaska Permanent Fund dividends) and certain other conditions are met, a parent can elect to include the child's income on the parent's return. If this election is made, the child does not have to file a return. See *Parent's Election To Report Child's Interest and Dividends* in chapter 32.

Self-Employed Persons

You are self-employed if you:

- Carry on a trade or business as a sole proprietor,
- Are an independent contractor,
- Are a member of a partnership, or
- Are in business for yourself in any other way.

Self-employment can include work in addition to your regular full-time business activities, such as certain part-time work you do at home or in addition to your regular job.

Examples

A person who delivers newspapers would be subject to self-employment tax. A person working at home in a cottage industry—making quilts or pillows, for example—would be subject to self-employment tax.

In some instances, it is to your advantage to report income from self-employment, because if you do not already qualify, you will then become eligible for social security benefits. For more information on self-employed persons, see Chapter 38, *If You Are Self-Employed: How to File Schedule C*.

You must file a return if your gross income is at least as much as the filing requirement amount for your filing status and age (shown in *Table 1-1*). Also, you must file Form 1040 and **Schedule SE** (Form 1040), *Self-Employment Tax*, if:

- 1) Your net earnings from self-employment (excluding church employee income) were \$400 or more, or
- 2) You had church employee income of \$108.28 or more. (See *Table 1-3*.)

Table 1-3. **Other Situations When You Must File a 2003 Return**

<p>If any of the four conditions listed below apply, you must file a return, even if your income is less than the amount shown in <i>Table 1-1</i> or <i>Table 1-2</i>.</p> <ol style="list-style-type: none"> You owe any special taxes, such as: <ul style="list-style-type: none"> Social security or Medicare tax on tips you did not report to your employer. (See chapter 7.) Uncollected social security, Medicare, or railroad retirement tax on tips you reported to your employer. (See chapter 7.) Uncollected social security, Medicare, or railroad retirement tax on your group-term life insurance. This amount should be shown in box 12 of your Form W-2. Alternative minimum tax. (See chapter 31.) Tax on a qualified retirement plan, including an individual retirement arrangement (IRA). (See chapter 18.) Tax on an Archer MSA. (See Publication 969, <i>Medical Savings Accounts (MSAs)</i>.) Tax on a Coverdell ESA or qualified tuition program. (See Publication 970, <i>Tax Benefits for Education</i>.) Recapture of an investment credit or a low-income housing credit. (See the instructions for Form 4255, <i>Recapture of Investment Credit</i>, or Form 8611, <i>Recapture of Low-Income Housing Credit</i>.) Recapture tax on the disposition of a home purchased with a federally-subsidized mortgage. (See chapter 16.) Recapture of the qualified electric vehicle credit. (See chapter 37.) Recapture of an education credit. (See chapter 36.) Recapture of the Indian employment credit. (See the instructions for Form 8845, <i>Indian Employment Credit</i>.) Recapture of the new markets credit. (See Form 8874, <i>New Markets Credit</i>.) You received any advance earned income credit (EIC) payments from your employer. This amount should be shown in box 9 of your Form W-2. (See chapter 37.) You had net earnings from self-employment of at least \$400. (See <i>Self-Employed Persons</i> earlier in this chapter.) 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. (See Publication 533.)
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Use Schedule SE (Form 1040) to figure your self-employment tax. Self-employment tax is comparable to the social security and Medicare tax withheld from an employee's wages. For more information about this tax, get Publication 533, *Self-Employment Tax*.

TAXSAVER

Employing your spouse. In prior years, there was an advantage for a self-employed person whose earnings were slightly over the maximum tax base to employ a spouse in the business to lower his or her self-employment tax. The spouse's wages were not subject to social security taxes or self-employment tax. Now, however, the spouse's wages are subject to social security taxes. A self-employed person who has previously employed his or her spouse for this reason should consider terminating this practice.

Explanation

You are able to deduct one-half of your self-employment tax for the year in calculating your adjusted gross income. For details see Chapter 24, *Taxes You May Deduct*.

Self-employment tax has two parts: old age, survivor, and disability insurance (OASDI) and Medicare hospital insurance (HI). (The comparable social security tax withheld on an employee's wages consists of these same two parts.) In 2003, the cap on self-employment income subject to OASDI is \$87,900. There is no limit on the amount of self-employment income subject to the HI portion of the self-employment tax.

TAXALERT

The 2004 FICA wage and self-employment income base will be \$87,900.

Employees of foreign governments or international organizations. If you are a U.S. citizen who works in the United States for an international organization, a foreign government, or a wholly owned instrumentality of a foreign government, and your employer is not required to withhold social security and Medicare taxes from your wages, you must include your earnings from services performed in the United States when figuring your net earnings from self-employment.

Ministers. You must include income from services you performed as a minister when figuring your net earnings from self-employment, unless you have an exemption from self-employment tax. This also applies to Christian Science practitioners and members of a religious order who have not taken a vow of poverty. For more information, get Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*.

Aliens

Your status as an alien—resident, nonresident, or dual-status—determines whether and how you must file an income tax return.

The rules used to determine your alien status are discussed in Publication 519, *U.S. Tax Guide for Aliens*.

Resident alien. If you are a resident alien for the entire year, you must file a tax return following the same rules that apply to U.S. citizens. Use the forms discussed in this publication.

Nonresident alien. If you are a nonresident alien, the rules and tax forms that apply to you are different from those that apply to U.S. citizens and resident aliens. See Publication 519 to find out if U.S. income tax laws apply to you and which forms you should file.

Dual-status taxpayer. If you are a resident alien for part of the tax year and a nonresident alien for the rest of the year, you are a dual-status taxpayer. Different rules apply for each part of the year. For information on dual-status taxpayers, see Publication 519.

Explanation

For more information about foreign citizens living in the United States, see Chapter 43, *Foreign Citizens Living in the United States*.

Who Should File

Even if you do not have to file, you should file a federal income tax return to get money back if any of the following conditions apply.

- You had federal income tax withheld from your pay.
- You qualify for the earned income credit. See chapter 37 for more information.

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- 3) You qualify for the additional child tax credit. See chapter 35 for more information.
- 4) You qualify for the health coverage tax credit. See chapter 37 for more information.

Which Form Should I Use?

You must use one of three forms to file your return: Form 1040EZ, Form 1040A, or Form 1040. (But also see *Does My Return Have To Be on Paper*, later.)

Form 1040EZ

Form 1040EZ is the simplest form to use.

You can use Form 1040EZ if all of the following apply.

- 1) Your filing status is single or married filing jointly. If you were a non-resident alien at any time in 2003, your filing status must be married filing jointly.
- 2) You (and your spouse if married filing a joint return) were under age 65 and not blind at the end of 2003. If you were born on January 1, 1939, you are considered to be age 65 at the end of 2003.
- 3) You do not claim any dependents.
- 4) Your taxable income is less than \$50,000.
- 5) Your income is **only** from wages, salaries, tips, unemployment compensation, Alaska Permanent Fund dividends, taxable scholarship and fellowship grants, and taxable interest of \$1,500 or less.
- 6) You did not receive any advance earned income credit (EIC) payments.
- 7) You do not claim any adjustments to income, such as a deduction for IRA contributions or student loan interest.
- 8) You do not claim any credits other than the earned income credit.
- 9) You do not owe any household employment taxes on wages you paid to a household employee.

You must meet all of these requirements to use Form 1040EZ. If you do not, you must use Form 1040A or Form 1040.

TAXPLANNER

Even though it might be easier for you to file Form 1040EZ, you should carefully review your situation before doing so, especially if your income is close to the Form 1040EZ maximum level of \$50,000. Check what deductions you may be able to claim if you itemize them. (You cannot claim **itemized deductions** on Form 1040EZ.) If you have deductions that can be itemized and you do not claim them, you could be significantly overpaying your tax.

Figuring tax. On Form 1040EZ, you can use only the tax table to figure your tax. You cannot use Form 1040EZ to report any other tax.

Form 1040A

If you do not qualify to use Form 1040EZ, you may be able to use Form 1040A.

You can use Form 1040A if all of the following apply.

- 1) Your income is **only** from wages, salaries, tips, IRA distributions, pensions and annuities, taxable social security and railroad retirement benefits, taxable scholarship and fellowship grants, interest, ordinary dividends (including Alaska Permanent Fund dividends), capital gain distributions, and unemployment compensation.
- 2) Your taxable income is less than \$50,000.
- 3) Your adjustments to income are for only the following items.
 - a) Educator expenses.
 - b) IRA deduction.

- c) Student loan interest deduction.
- d) Tuition and fees deduction.
- 4) You do not itemize your deductions.
- 5) Your taxes are from only the following items.
 - a) *Tax Table*.
 - b) Alternative minimum tax. (See chapter 31.)
 - c) Advance earned income credit (EIC) payments, if you received any. (See chapter 37.)
 - d) Recapture of an education credit. (See chapter 36.)
 - e) Form 8615, *Tax for Children Under Age 14 With Investment Income of More Than \$1,500*.
 - f) *Qualified Dividends and Capital Gain Tax Worksheet*.
- 6) You claim only the following tax credits.
 - a) The credit for child and dependent care expenses. (See chapter 33.)
 - b) The credit for the elderly or the disabled. (See chapter 34.)
 - c) The child tax credit. (See chapter 35.)
 - d) The additional child tax credit. (See chapter 35.)
 - e) The education credits. (See chapter 36.)
 - f) The retirement savings contributions credit. (See chapter 37.)
 - g) The earned income credit. (See chapter 37.)
 - h) The adoption credit. (See chapter 37.)

You must meet all of the above requirements to use Form 1040A. If you do not, you must use Form 1040.

If you meet the above requirements, you can use Form 1040A even if you received employer-provided adoption benefits or dependent care benefits.

Caution. *If you receive a capital gain distribution that includes qualified 5-year gain, unrecaptured section 1250 gain, section 1202 gain, or collectibles (28%) gain, you cannot use Form 1040A. You must use Form 1040.*

TAXALERT

Form 1040A lets you report most retirement income, including pension and annuity payments, taxable social security and railroad retirement benefits, and payments from your IRA. Furthermore, it allows you to claim the credit for the elderly or the disabled and report your estimated tax payments. If you have been filing a Form 1040 because of these items, you can qualify for the easier-to-file Form 1040A. Be aware that you still cannot claim itemized deductions on Form 1040A. If you have deductions that can be itemized, you may be better off continuing to file a Form 1040.

Form 1040

If you cannot use Form 1040EZ or Form 1040A, you **must** use Form 1040. You can use Form 1040 to report all types of income, deductions, and credits.

You may have received Form 1040A or Form 1040EZ in the mail because of the return you filed last year. If your situation has changed this year, it may be to your advantage to file Form 1040 instead. You may pay less tax by filing Form 1040 because you can take itemized deductions, some adjustments to income, and credits you cannot take on Form 1040A or Form 1040EZ.

You must use Form 1040 if any of the following apply.

- 1) Your taxable income is \$50,000 or more.
- 2) You itemize your deductions.
- 3) You had income that cannot be reported on Form 1040EZ or Form 1040A.
- 4) You claim any adjustments to gross income other than the adjustments listed earlier under *Form 1040A*.

- 5) Your Form W-2, box 12, shows uncollected employee tax (social security and Medicare tax) on tips (see chapter 7) or group-term life insurance (see chapter 6).
- 6) You received \$20 or more in tips in any one month and did not report all of them to your employer. (See chapter 7.)
- 7) You claim any credits other than the credits listed earlier under *Form 1040A*.
- 8) You have to file other forms with your return to report certain exclusions, taxes, or transactions.

Does My Return Have To Be on Paper?

You may be able to file a paperless return using IRS *e-file* (electronic filing). It's so easy, 53 million taxpayers preferred *e-file* over filing a paper tax return last year.

This section explains how to *e-file*:

- Using an Authorized IRS *e-file* Provider,
- Using your personal computer, or
- Using a telephone (TeleFile).

IRS e-file

Table 1-4 lists the benefits of IRS e-file. IRS e-file uses automation to replace most of the manual steps needed to process paper returns. As a result, the processing of e-file returns is faster and more accurate than the processing of paper returns. However, as with a paper return, you are responsible for making sure your return contains accurate information and is filed on time.

Using *e-file* does not affect your chances of an IRS examination of your return.

Example

You expect a \$3,000 refund. If you can receive your refund in 3 weeks by filing electronically instead of 3 months by filing a paper form, you could save money by investing the re-

fund sooner. Assuming you can earn 7% after tax on your money, you might save \$45. However, the company that files your return electronically will usually charge you a separate fee for this service. This should be considered in your decision to file electronically.

Electronic signatures. Create your own personal identification number (PIN) and use a tax professional or file your own paperless return electronically. If you are married filing jointly, you and your spouse will each need to create a PIN and enter these PINs as your electronic signatures.

A PIN is any combination of five numbers you choose, except five zeros. If you use a PIN, there is nothing to sign and nothing to mail—even your Forms W-2.

To verify your identity, you will be asked to enter your adjusted gross income (AGI) from your **originally** filed 2002 income tax return, if applicable. Do not use your AGI from an amended return (Form 1040X). AGI is the amount shown on your 2002 Form 1040, line 35; Form 1040A, line 21; Form 1040EZ, line 4; and on the TeleFile Tax Record, line 1. If you do not have your 2002 income tax return, call the IRS at **1-800-829-1040** to get a free transcript of your account. You will also be asked to enter your date of birth (DOB). Make sure your DOB is accurate and matches the information on record with the Social Security Administration by checking your annual Social Security Statement.

Caution. You cannot sign your return electronically if you are a first-time filer under age 16 at the end of 2003, or if you are **filing Form 3115, 5713, 8283 (if completing Section B), 8332, or 8609.**

For more details on the Self-Select PIN method, visit **www.irs.gov/efile** and click on "IRS *e-file* for Individual Taxpayers." **Forms 8453 and 8453-OL.** Your return is not complete without your signature. If you are not eligible or choose not to sign your return electronically, you must complete, sign, and file Form 8453, *U.S. Individual Income Tax Declaration for an IRS e-file Return*, or Form 8453-OL, *U.S. Individual Income Tax Declaration for an IRS e-file On-line Return*, whichever applies.

Table 1-4. **Benefits of IRS e-file**

Free File Options!	<ul style="list-style-type: none"> • At least 60 percent of taxpayers—or 78 million—are eligible to use free commercial online tax preparation software to <i>e-file</i>. • Visit www.irs.gov/efile to see if you qualify and to access these free services offered by the tax software industry (not the IRS).
Fast! Easy! Convenient!	<ul style="list-style-type: none"> • Get your refund in half the time as paper filers do, even faster and safer with Direct Deposit—in as few as 10 days. • Sign electronically and file a completely paperless return. • Receive an electronic proof of receipt within 48 hours that the IRS received your return. • If you owe, you can <i>e-file</i> and authorize an electronic funds withdrawal or pay by credit card. If you <i>e-file</i> before April 15, 2004, you can schedule an electronic funds withdrawal from your checking or savings account as late as April 15, 2004. • Prepare and file your federal and state returns together and save time.
Accurate! Secure!	<ul style="list-style-type: none"> • IRS computers quickly and automatically check for errors or other missing information. • The error rate for <i>e-filed</i> returns is less than 1 percent. • The chance of being audited does not differ whether you <i>e-file</i> or file a paper tax return. • Your bank account information is safeguarded along with other tax return information. The IRS does not have access to credit card numbers.

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State returns. In most states, you can file an electronic state return simultaneously with your federal return. For more information, check with your local IRS office, state tax agency, tax professional, or the IRS web site at www.irs.gov/efile.

Refunds. You can have a refund check mailed to you, or you can have your refund deposited directly to your checking or savings account.

With *e-file*, your refund will be issued in half the time as when filing on paper. If you choose Direct Deposit, you can receive your refund in as few as 10 days.

Explanation: Direct Deposit Refunds

Direct Deposit refunds will usually be issued 2 to 3 weeks from the date the electronic return is accepted. However, the Treasury Department does not guarantee that a refund will be issued by a specific date or for the anticipated amount.

The following conditions may delay refunds and/or change refund amounts. Direct Deposit elections generally will not be honored in these cases:

1. Taxpayer owes back taxes, either individual or business.
2. Taxpayer owes delinquent child support.
3. Taxpayer has a certain delinquent debt, such as student loans.
4. The last name and social security number of the primary taxpayer are not the same as on last year's return. If this is the case, the return will be delayed at least 1 week for rematching.
5. The estimated tax payments reported on the return do not match the estimated tax payments recorded on the IRS master file. This generally occurs when:
 - a. The spouse made separate payments and filed a joint return, or vice versa; or
 - b. The return was filed before the January 15, 2004, estimated tax payment was credited to the taxpayer's account.
6. The taxpayer has a Schedule E claiming a deduction for a questionable tax shelter.
7. The taxpayer is claiming a blatantly unallowable deduction.

TAXPLANNER

A refund anticipation loan (RAL) is a loan made to you based on your expected refund. The loan is a contract between you and a financial institution. Generally, the financial institution will require that you sign an authorization that permits the institution to debit your account after the refund has been credited to it. You can expect to pay a fee to the electronic filer, who, with your permission, submits information to the financial institution, and a fee to the financial institution. These fees are in addition to the tax preparation fee and electronic filing fee. Generally, Direct Deposit takes 2 to 3 weeks before you receive your refund. An RAL could speed up the time for you to have your money by about 2 weeks but at a relatively high "interest cost." For example, if your expected refund is \$1,000 and the fee is \$30, the "interest cost" to you for the 2 weeks' use of the money comes to over 75% on an annualized basis.

Offset against debts. As with a paper return, you may not get all of your refund if you owe certain past-due amounts, such as federal tax, state tax, a student loan, or child support. See *Offset against debts* under *Refunds*, later.

Explanation: Composition of an Electronic Return

In total, an electronic return contains the same information as a comparable return filed entirely on paper documents. An electronic return consists of:

1. Electronic portion of return—Data transmitted to the IRS electronically
2. Nonelectronic portion of return—Paper documents (filed with the IRS at a later date) that contain information that cannot be electronically transmitted, such as taxpayer signatures and documents prepared by third parties

Electronic Portion of Return

For 2003 returns, most forms and schedules, including Form 1040 and Form 1040A, can be transmitted electronically and are considered the "electronic portion" of the return.

Nonelectronic Portion of Return

Some parts of your return *cannot* be filed electronically, including the following:

- Form 8453, *U.S. Individual Income Tax Declaration for Electronic Filing*, required for all electronic returns
- Copy B Form W-2, W-2G, or 1099-R, which would normally be attached to the front of a paper return
- Other information documents that are voluntarily being included with the return by the taxpayer as supporting material

Exclusions from Electronic Filing

The following are some of the types of returns that are excluded from electronic filing:

- Decedent returns, including joint returns filed by surviving spouses
- Returns with a power of attorney currently in effect for the refund to be sent to a third party
- Returns subject to community property rules with filing status "Married Filing Separately"
- Returns with Social Security numbers within the range 900-00-0000 through 999-99-9998. These are temporary Social Security numbers

Refund inquiries. If you do not receive your refund within 3 weeks after your electronically-filed return was accepted by IRS, see *Past-Due Refund* later.

Balance due. If you owe tax, you must pay it by April 15, 2004, to avoid late-payment penalties and interest. You can make your payment electronically by credit card or by scheduling an electronic funds withdrawal from your checking or savings account.

See *How To Pay*, later, for information on how to pay the balance due.

Using an Authorized IRS e-file Provider

Many tax professionals electronically file tax returns for their clients. As a taxpayer, you have two options.

- 1) You can prepare your return, take it to an Authorized IRS *e-file* Provider, and have the provider transmit it electronically to the IRS.
- 2) You can have a tax professional prepare your return and transmit it for you electronically.

You may personally enter your self-selected PIN or complete **Form 8879**, *IRS e-file Signature Authorization*, to authorize the provider to enter your self-selected PIN on your return.

Note. Tax professionals may charge a fee for IRS *e-file*. Fees may vary depending on the professional and the specific services rendered.

Using Your Personal Computer

You can file your tax return in a fast, easy, convenient way using your personal computer. A computer with a modem or Internet access and tax preparation software are all you need. You can *e-file* from the comfort of your home 24 hours a day, 7 days a week. Best of all, you may qualify for Free File.

If you do not qualify for the Free File options, visit our Partners Page for partners that offer other free or low-cost filing options.

IRS approved tax preparation software is available for online use on the Internet, for download from the Internet, and in retail stores.

For information on Free File, Partners Page, and tax preparation software, visit our website at www.irs.gov/efile.

Using a Telephone (TeleFile)

For millions of eligible taxpayers, TeleFile is the easiest way to file. TeleFile allows you to file your simple federal tax return using a touch-tone telephone. Only taxpayers who met the qualifications for Form 1040EZ in the prior year are eligible to receive the TeleFile tax package for the current year. A TeleFile tax package is automatically mailed to you if you are eligible. TeleFile is completely paperless—there are no forms to mail in. Just follow the instructions in the TeleFile tax package. TeleFile is filed directly with the IRS, usually in 10 minutes, and it's FREE. **Tip.** *Parents: If your children receive a TeleFile tax package, please encourage them to use TeleFile.*

Through Employers and Financial Institutions

Some businesses offer free *e-file* to their employees, members, or customers. Others offer it for a fee. Ask your employer or financial institution if they offer IRS *e-file* as an employee, member, or customer benefit.

Free Help With Your Return

Free help in preparing your return is available nationwide from IRS-trained volunteers. The Volunteer Income Tax Assistance (VITA) program is designed to help low-income taxpayers and the Tax Counseling for the Elderly (TCE) program is designed to assist taxpayers age 60 or older with their tax returns. Some locations offer free electronic filing and all volunteers will let you know about the credits and deductions you may be entitled to claim. To find a site near you, call 1-800-829-1040. Or to find the nearest AARP TaxAide site, visit AARP's website at www.aarp.org/taxaide or call 1-888-227-7669.

When Do I Have To File?

April 15, 2004, is the due date for filing your 2003 income tax return if you use the calendar year. For a quick view of due dates for filing a return with or without an extension of time to file (discussed later), see Table 1-5.

If you use a fiscal year (a year ending on the last day of any month except December, or a 52-53 week year), your income tax return is due by the 15th day of the 4th month after the close of your fiscal year.

When the due date for doing *any* act for tax purposes—filing a re-

turn, paying taxes, etc.—falls on a Saturday, Sunday, or legal holiday, the due date is delayed until the next business day.

Filing on time. Your paper return is filed on time if it is mailed in an envelope that is properly addressed, has enough postage, and is postmarked by the due date. If you send your return by registered mail, the date of the registration is the postmark date. The registration is evidence that the return was delivered. If you send a return by certified mail and have your receipt postmarked by a postal employee, the date on the receipt is the postmark date. The postmarked certified mail receipt is evidence that the return was delivered.

Private delivery services. If you use a private delivery service designated by the IRS to send your return, the postmark date generally is the date the private delivery service records in its database or marks on the mailing label. The private delivery service can tell you how to get written proof of this date.

The following are designated private delivery services.

- Airborne Express (Airborne): Overnight Air Express Service, Next Afternoon Service, and Second Day Service.
- DHL Worldwide Express (DHL): DHL "Same Day" Service and DHL USA Overnight.
- Federal Express (FedEx): FedEx Priority Overnight, FedEx Standard Overnight, FedEx 2Day, FedEx International Priority, and FedEx International First.
- United Parcel Service (UPS): UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, UPS 2nd Day Air A.M., UPS Worldwide Express Plus, and UPS Worldwide Express.

Caution. *Private delivery services cannot deliver items to P.O. boxes. You must use the U.S. Postal Service to mail any item to an IRS P.O. box address.*

Electronically filed returns. If you use IRS *e-file*, your return is considered filed on time if the authorized electronic return transmitter postmarks the transmission by the due date. An authorized electronic return transmitter is a participant in the IRS *e-file* program that transmits electronic tax return information directly to the IRS.

The electronic postmark is a record of when the authorized electronic return transmitter received the transmission of your electronically filed return on its host system. The date and time in your time zone controls whether your electronically filed return is timely.

Filing late. If you do not file your return by the due date, you may have to pay a failure-to-file penalty and interest. For more information, see *Penalties*, later. Also see *Interest* under *Amount You Owe*.

If you were due a refund but you did not file a return, you generally must file within 3 years from the date the return was due (including extensions) to get that refund.

Nonresident alien. If you are a nonresident alien and earn wages subject to U.S. income tax withholding, your 2003 U.S. income tax return (Form 1040NR or Form 1040NR-EZ) is due by:

- April 15, 2004, if you use a calendar year, or
- The 15th day of the 4th month after the end of your fiscal year if you use a fiscal year.

Table 1-5. **When To File Your 2003 Return**

For U.S. citizens and residents who file returns on a calendar year.

	For Most Taxpayers	For Certain Taxpayers Outside the U.S.
No extension requested	April 15, 2004	June 15, 2004
Automatic extension Form 4868 filed, or credit card payment made	August 16, 2004	August 16, 2004
2nd extension Form 2688 filed after getting automatic extension	October 15, 2004	October 15, 2004

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If you do not earn wages subject to U.S. income tax withholding, your return is due by:

- June 15, 2004, if you use a calendar year, or
- The 15th day of the 6th month after the end of your fiscal year, if you use a fiscal year.

Get Publication 519 for more filing information.

Filing for a decedent. If you must file a final income tax return for a taxpayer who died during the year (a decedent), the return is due by the 15th day of the 4th month after the end of the decedent's normal tax year. In most cases, for a 2003 return, this will be April 15, 2004. See *Final Return for the Decedent* in chapter 4.

Extensions of Time To File

You may be able to get an extension of time to file your return. Special rules apply for those who were:

- Outside the United States, or
- Serving in a combat zone.

Automatic Extension. If you cannot file your 2003 return by the due date, you may be able to get an automatic 4-month extension of time to file.

Example. If your return is due on April 15, 2004, you will have until August 16, 2004, to file.

Caution. If you do not pay the tax due by the regular due date (generally, April 15), you will owe interest. You may also be charged penalties, discussed later.

How to get the automatic extension. You can get the automatic extension by:

- 1) Using IRS *e-file* (electronic filing), or
- 2) Filing a paper form.

E-file options. There are three ways you can use *e-file* to get an extension of time to file. If you *e-file*, you will get a confirmation number when you complete the transaction. Keep the number with your records.

Complete **Form 4868**, *Application for Automatic Extension of Time To File U.S. Individual Income Tax Return*, to use as a worksheet. If you think you may owe tax when you file your return, use *Part III* of the form to estimate your balance due. Do not send Form 4868 to the IRS.

E-file by phone. You can file Form 4868 by phone any time from February 2 through April 15, 2004. You will need to provide certain information from your tax return for 2002. If you wish to make a payment by electronic funds withdrawal, see *Electronic payment options*, under *How To Pay*, later in this chapter.

E-file using your personal computer or a tax professional. You can use a tax software package with your personal computer or a tax professional to file Form 4868 electronically. You will need to provide certain information from your tax return for 2002. If you wish to make a payment by electronic funds withdrawal, see *Electronic payment options*, under *How To Pay*, later in this chapter.

E-file and pay by credit card. You can get an extension by paying part or all of your estimate of tax due by using a credit card. You can do this by phone or over the Internet. You do not file Form 4868. See *Credit card*, under *How To Pay*, later in this chapter.

Filing a paper Form 4868. You can get an extension of time to file by filing a paper Form 4868. Mail it to the address shown in the form instructions.

If you want to make a payment with the form, make your check or money order payable to the "United States Treasury." Write your SSN, daytime phone number, and "2003 Form 4868" on your check or money order.

TAXALERT

The IRS offers some relief to taxpayers unable to pay the amount owed with the filing of Form 4868. The IRS permits

Form 4868 to be filed and an automatic 4-month extension obtained even though the tax properly estimated to be due is not paid in full when the form is filed. No late filing penalty will be assessed under these circumstances. However, it is still required that the tax liability shown on Form 4868 be properly estimated based on the information available to the taxpayer. Furthermore, unless at least 90% of the taxpayer's actual tax liability was paid prior to the original due date of the return through withholding or estimated payment, a late payment penalty of 1 to 2% per month will be assessed for each month from the original due date to the date of payment plus the regular rate of interest on underpayments.

When to file. You must request the automatic extension by the due date for your return. You can file your return any time before the 4-month extension period ends.

TAXSAVER

An extension of time to file will not be valid if it does not show a "proper" estimate of tax liability. A proper estimate is based on all the facts and information you have at the time of filing. If your estimate is found to be improper, your extension will be invalid and you will be subject to failure-to-file penalties. See *Penalties*, later.

Some tax experts contend that you should request the maximum extension allowed for filing your return, arguing that your chances of an audit are reduced, because IRS field agents will have less time to conduct the audit. Other tax experts contend that you're better off filing on April 15, because that way you get lost in the crowd. Both theories are oversimplifications of IRS procedures.

When you file your return. Enter any payment you made related to the extension of time to file on line 66, Form 1040. If you file Form 1040EZ or Form 1040A, include that payment in your total payments on line 9 of Form 1040EZ or line 43 of Form 1040A. Also print "Form 4868" and the amount paid in the space to the left of line 9 or line 43.

Extension beyond 4 months. If you get the 4-month extension and you later find that you are not able to file within the 4-month extension period, you may be able to get 2 more months to file, for a total of 6 months.

You can apply for an extension beyond the 4-month extension either by writing a letter to the IRS or by filing **Form 2688**, *Application for Additional Extension of Time To File U.S. Individual Income Tax Return*. Except in cases of undue hardship, a request for additional time will not be approved unless you have first used the automatic 4-month extension. Form 2688 or your letter will not be considered if you file it after the extended due date.

Caution. You should ask for the extension early so that, if it is not approved, you still will be able to file on time.

To get an extension beyond the automatic 4-month extension, you must give all the following information.

- The reason for requesting the extension.
- The tax year to which the extension applies.
- The length of time needed for the extension.
- Whether another extension of time to file has already been requested for this tax year.

You must sign the request for this extension, or it may be signed by your attorney, CPA, enrolled agent, or a person with a power of attorney. If

you are unable to sign the request because of illness or for another good reason, a person with a close personal or business relationship to you can sign for you, stating why you could not sign the request.

E-file. Refer to your tax software package or tax preparer for ways to file Form 2688 electronically. You will need to provide certain information from your tax return for 2002. If you file electronically, do not mail the Form 2688.

Explanation

Generally, only causes that are beyond your control will be acceptable as reasons for an additional extension. In addition to personal sickness or injury and to a death or serious illness in your immediate family, some acceptable reasons, drawn from IRS proceedings and court cases, include the following:

1. You have a substantial number of security transactions during the taxable year, some quite complex, and there has not been sufficient time to gather and analyze all the required information.
2. You have invested in oil properties and received the information from the operators too late to complete your return adequately by the due date.
3. You have a complicated deduction problem with your medical expenses that is under study by your tax advisors, and it may not be resolved in time to prepare your tax return adequately.
4. You sold securities in the taxable year that you had held for some years, and you have not as yet been able to determine the tax basis of such securities. You have checked your records but may have to go back to old records of your broker to determine the correct figures.
5. A partnership on the accrual basis in which you are a member initiated a profit-sharing plan at the end of the tax year, the contribution to which depends on approval of the plan by the IRS. Such approval has not yet been received.
6. Any other situation in which there is a "reasonable cause"—for example, the destruction by fire or other casualty of your business records or a lack of funds to pay the tax when you can demonstrate that this lack occurred despite the exercise of ordinary business care and prudence.

Extension approved. If your application for this extension is approved, you will be notified by the IRS.

If the IRS later determines that the statements made on your request for this extension are false or misleading and an extension would not have been approved at the time based on the true facts, the extension will be null and void. You will have to pay the failure-to-file penalty (discussed later under *Civil Penalties*).

Extension not approved. If your application for this extension is not approved, you must file your return by the extended due date of the automatic extension. You may be allowed to file within 10 days of the date of the notice you get from the IRS if the end of the 10-day period is later than the due date. The notice will tell you if the 10-day grace period is granted.

No further extensions. If you are in the United States, an extension of more than 6 months will not be approved.

TaxPLANNER

An extension of time to file is not an extension of time to pay. If you are unable to pay the full amount of tax due with your tax return because of financial hardship, you should still file

the tax return along with a "good faith" payment of as much of the tax due as you can afford to pay. You should complete Form 9465 to request the privilege of paying the remaining tax in installments. This form should be attached to the front of the return when it is filed. However, the IRS will impose a \$43 fee for entering into an installment agreement. You can expect a decision back from the IRS within 30 days regarding your installment request; but **you still will be subject to interest and the failure-to-pay penalty on the unpaid tax.**

The IRS will continue to send you a bill for the unpaid tax, interest, and penalty until the total amount is paid. After the tax is completely paid, you can request in writing that the penalty be waived due to reasonable cause because of financial hardship. The IRS has total discretion in waiving penalties and may require you to prove your financial hardship.

If your tax return is already in the formal collection process (i.e., you have been contacted by an IRS official regarding a delinquent tax liability) and you are unable to pay the tax due, you may request an installment agreement with the IRS officer. If he or she agrees, the installment agreement is made using Form 433-D, and you will be required to provide financial information. You may need to seek professional tax advice if this is the case.

Individuals Outside the United States

You are allowed an automatic 2-month extension (until June 15, 2004, if you use the calendar year) to file your 2003 return and pay any federal income tax due if:

- 1) You are a U.S. citizen or resident, and
- 2) On the due date of your return:
 - a) You are living outside of the United States and Puerto Rico, and your main place of business or post of duty is outside the United States and Puerto Rico, **or**
 - b) You are in military or naval service on duty outside the United States and Puerto Rico.

However, if you pay the tax due after the regular due date (generally, April 15), interest will be charged from that date until the date the tax is paid.

If you served in a combat zone or qualified hazardous duty area, you may be eligible for a longer extension of time to file. See *Individuals Serving in Combat Zone*, later, for special rules that apply to you.

Married taxpayers. If you file a joint return, only one spouse has to qualify for this automatic extension. If you and your spouse file separate returns, this automatic extension applies only to the spouse who qualifies.

How to get the extension. To use this special automatic extension, you must attach a statement to your return explaining what situation qualified you for the extension. (See the situations listed under (2), earlier.)

Extensions beyond 2 months. If you cannot file your return within the automatic 2-month extension period, you may be able to get an additional 2-month extension, for a total of 4 months. Generally, you must file a paper Form 4868 by the end of the automatic extension period (usually June 15) to get this additional 2-month extension. Write "Taxpayer Abroad" across the top of Form 4868.

This additional 2-month extension of time to file is **not** a further extension of time to pay. You can use a credit card to pay your estimate of tax due. See *How To Pay*, later in this chapter.

Extension beyond 4 months. If you are still unable to file your return within the 4-month extension period, you may be able to get an extension for 2 more months, for a total of 6 months. See *Extension beyond 4 months*, earlier.

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No further extension. An extension of more than 6 months will generally not be granted. However, if you are outside the United States and meet certain tests, you may be granted a longer extension. For more information, see *Further extensions* under *When To File and Pay* in Publication 54.

Individuals Serving in Combat Zone

The deadline for filing your tax return, paying any tax you may owe, and filing a claim for refund is automatically extended if you serve in a combat zone. This applies to members of the Armed Forces, as well as merchant marines serving aboard vessels under the operational control of the Department of Defense, Red Cross personnel, accredited correspondents, and civilians under the direction of the Armed Forces in support of the Armed Forces.

Combat zone. For purposes of the automatic extension, the term “combat zone” includes the following areas.

- 1) The Persian Gulf area, effective January 17, 1991.
- 2) The qualified hazardous duty area of Bosnia and Herzegovina, Croatia, and Macedonia, effective November 21, 1995.
- 3) The qualified hazardous duty area of the Federal Republic of Yugoslavia (Serbia/Montenegro), Albania, the Adriatic Sea, and the Ionian Sea north of the 39th parallel, effective March 24, 1999.
- 4) Afghanistan, effective September 19, 2001.

See Publication 3, *Armed Forces' Tax Guide*, for information about other tax benefits available to military personnel serving in a combat zone.

Extension period. The deadline for filing your return, paying any tax due, and filing a claim for refund is extended for at least 180 days after the later of:

- 1) The last day you are in a combat zone or the last day the area qualifies as a combat zone, or
- 2) The last day of any continuous qualified hospitalization for injury from service in the combat zone.

In addition to the 180 days, your deadline is also extended by the number of days you had left to take action with the IRS when you entered the combat zone. For example, you have 3 1/2 months (January 1–April 15) to file your tax return. Any days left in this period when you entered the combat zone (or the entire 3 1/2 months if you entered it before the beginning of the year) are added to the 180 days. See *Extension of Deadline* in Publication 3 for more information.

The above rules on the extension for filing your return also apply when you are deployed outside the United States (away from your permanent duty station) while participating in a designated contingency operation.

How Do I Prepare My Return?

This section explains how to get ready to fill in your tax return and when to report your income and expenses. It also explains how to complete certain sections of the form. You may find *Table 1–6* helpful when you prepare your return.

In most cases, based on what you filed last year, the IRS will mail you Form 1040, Form 1040A, or Form 1040EZ with related instructions, or a TeleFile package. Before you fill in the form, look at the form instructions to see if you need, or would benefit from filing, a different form this year. Also see if you need any additional forms or schedules. You may also want to read *Does My Return Have To Be on Paper*, earlier.

If you do not receive a tax return package in the mail, or if you need other forms, you can order them or print them from the Internet. See *How To Get Tax Help* in the back of this publication.

Substitute tax forms. You cannot use your own version of a tax form unless it meets the requirements explained in Publication 1167, *General Rules and Specifications for Substitute Forms and Schedules*.

Table 1–6. Six Steps for Preparing Your Return

- 1 — Get your records together for income and expenses.
- 2 — Get the forms, schedules, and publications you need.
- 3 — Fill in your return.
- 4 — Check your return to make sure it is correct.
- 5 — Sign and date your return.
- 6 — Attach all required forms and schedules.

Explanation

The tax forms provided in the back of this book meet these requirements. You may also obtain tax forms via the Internet by visiting the IRS site at www.irs.gov.

Form W–2. If you are an employee, you should receive Form W–2 from your employer. You will need the information from this form to prepare your return. See *Form W–2* under *Credit for Withholding and Estimated Tax* in chapter 5.

If you do not receive Form W–2 by February 2, 2004, contact your employer. If you still do not get the form by February 16, the IRS can help you by requesting the form from your employer. When you request IRS help, be prepared to provide the following information.

- Your name, address (including zip code), and phone number.
- Your SSN.
- Your dates of employment.
- Your employer’s name, address (including zip code), and phone number.

Form 1099. If you received certain types of income, you may receive a Form 1099. For example, if you received taxable interest of \$10 or more, the payer generally must give you a Form 1099–INT. If you have not received it by February 2, 2004, contact the payer. If you still do not get the form by February 16, call the IRS for help.

When Do I Report My Income and Expenses?

You must figure your taxable income on the basis of a tax year. A “tax year” is an annual **accounting period** used for keeping records and reporting income and expenses. You must account for your income and expenses in a way that clearly shows your taxable income. The way you do this is called an **accounting method**. This section explains which accounting periods and methods you can use.

Accounting Periods

Most individual tax returns cover a **calendar year**—the 12 months from January 1 through December 31. If you do not use a calendar year, your accounting period is a **fiscal year**. A regular fiscal year is a 12-month period that ends on the last day of any month except December. A 52–53 week fiscal year varies from 52 to 53 weeks and always ends on the same day of the week.

You choose your accounting period (tax year) when you file your first income tax return. It cannot be longer than 12 months.

TAXPLANNER

To operate on a fiscal year accounting basis, you must keep your books and records based on that fiscal year. Because

most individual taxpayers keep their personal financial records on a calendar year basis, it is easier to use a calendar year period.

It is virtually impossible for an individual to secure permission to change to a fiscal year accounting period without justification. Usually, the justification must be that you are involved in a cyclical business from which self-employment or partnership income flows. Furthermore, in most cases, that income has to be your sole or principal source of income.

More information. For more information on accounting periods, including how to change your accounting period, see Publication 538, *Accounting Periods and Methods*.

Accounting Methods

Your accounting method is the way you account for your income and expenses. Most taxpayers use either the cash method or an accrual method. You choose a method when you file your first income tax return. If you want to change your accounting method after that, you generally must get IRS approval.

Cash method. If you use this method, report all items of income in the year in which you actually or constructively receive them. Generally, you deduct all expenses in the year you actually pay them. This is the method most individual taxpayers use.

Explanation

Accounting methods are important because they determine when you recognize income and when you deduct expenses for tax purposes. The cash method allows you more flexibility and control over your tax liability.

Individuals who do not own and operate their own business *must* use the cash method. However, the IRS will not permit you to use the cash method if you own your own business and if inventories of unsold goods or materials are on hand at the end of the year.

TAXALERT

IRS officials have expressed the view that you may not use the cash method for any substantial business activity, even one providing only personal or professional services. The law does not support this view. Nevertheless, in conducting audits, the IRS has been aggressive in urging taxpayers to change to the accrual method of accounting.

TAXPLANNER

Generally, most taxpayers who expect to be in the same tax bracket from one year to the next and who want to reduce their current tax bill as much as possible should attempt to defer income to a subsequent year and to take deductions in the current year. (If you suspect you might be in a higher tax bracket in a subsequent year, however, you would want to do just the opposite.)

You might consider lumping together your deductions in a single year. For example, in some states and cities, you may pay property, state, and local income taxes in either December or January, giving you the opportunity to pay 2 years' worth of these taxes in a single calendar year. You can also control when you make charitable contributions. To some extent, you can also control when you make interest payments on a mortgage.

Constructive receipt. Generally, you constructively receive income when it is credited to your account or set apart in any way that makes it available to you. You do not need to have physical possession of it. For example, interest credited to your bank account on December 31, 2003, is taxable income to you in 2003 if you could have withdrawn it in 2003 (even if the amount is not entered in your passbook or withdrawn until 2004).

Garnisheed wages. If your employer uses your wages to pay your debts, or if your wages are attached or garnished, the full amount is constructively received by you. You must include these wages in income for the year you would have received them.

Brokerage and other accounts. Profits from a brokerage account, or similar account, are fully taxable in the year you earn them. This is true even if:

- 1) You do not withdraw the earnings,
- 2) The credit balance in the account may be reduced or eliminated by losses in later years, or
- 3) Current profits are used to reduce or eliminate a debit balance from previous years.

Example

You sold your ABC Company stock on December 15, 2003, realizing a gain of \$5,000. You did not withdraw the cash in your account until January 6, 2004. The gain is taxable income to you for 2003.

Debts paid for you. If another person cancels or pays your debts (but not as a gift or loan), you have constructively received the amount and generally must include it in your gross income for the year. See *Canceled Debts* in chapter 13 for more information.

Example

Your new employer pays the balance of the mortgage due on your home that is not covered by the selling price so you can move to Florida to work for him. The payments are not intended to be a gift or a loan to you. The amount your employer pays on the mortgage is income to you in the year that he pays it.

Payment to third party. If a third party is paid income from property you own, you have constructively received the income. It is the same as if you had actually received the income and paid it to the third party.

Payment to an agent. Income an agent receives for you is income you constructively received in the year the agent receives it. If you indicate in a contract that your income is to be paid to another person, you must include the amount in your gross income when the other person receives it.

Explanation

The IRS considers you to have received income in the year that your agent receives it, but if a person who is not your agent or creditor receives your income, then you do not have to consider that amount as income until you personally obtain it. The key question is whether you can control the receipt of the income during the year. If you can, the income is taxable to you in that year.

Example

ABC Company mailed you a \$500 dividend check on December 9, 2003. The post office inadvertently delivered the check on December 31 to Mr. Wheat on the other side of town. You

didn't receive the check until January 6, 2004. The \$500 in dividends is taxable to you in 2004, because Mr. Wheat was not your agent. You should carefully explain this turn of events when you prepare your return because the IRS document-matching program will have a Form 1099 from ABC Company that lists the \$500 as having been paid to you in 2003.

TAXPLANNER

It is possible to structure a sale of property so that the sale funds are deposited in an escrow account and then disbursed to you in the next tax year. The advantage to you in this arrangement is that you have the security of knowing that the sale proceeds exist, but, at the same time, you're able to defer taxes on the funds until they become income to you in the following tax year. To do this, the escrow arrangement must be agreed on by both the buyer and the seller. The arrangement must follow other specific guidelines as well. You will need to seek professional advice.

Check received or available. A valid check you received or that was made available to you before the end of the tax year is constructively received by you in that year, even if you do not cash the check or deposit it in your account until the next year.

No constructive receipt. There may be facts to show that you did not constructively receive income.

Example. Alice Johnson, a teacher, agreed to her school board's condition that, in her absence, she would receive only the difference between her regular salary and the salary of a substitute teacher hired by the school board. Therefore, Alice did not constructively receive the amount by which her salary was reduced to pay the substitute teacher.

Explanation

The IRS does not consider you to have paid an expense if you use a note in lieu of cash to make the payment. In this case, you have only made a promise to pay sometime in the future. However, the IRS considers you to have made a payment if you use cash borrowed from a third party to pay an expense.

Example

If you give a note to your doctor promising to pay him for medical services already rendered, you have not yet paid the expense in the IRS's eyes. However, if you borrow money from your bank and use the cash to pay your doctor, you have paid the expense for tax purposes. Similarly, if you pay by credit card, you have made the payment for tax purposes. Paying by credit card is just like borrowing from a third party. **More information.** For more information on the determination of medical and dental expenses, see Chapter 23, *Medical and Dental Expenses*, and Publication 502, *Medical and Dental Expenses*.

Exception

Individual Retirement Arrangements. If you qualify for a tax-deductible contribution, you may take a deduction for a contribution to an Individual Retirement Arrangement (IRA) in 1 year, even though you do not make the actual cash contribution to your account until the following year; that is, you may file your tax return showing a deduction for a contribution to your IRA, although you have not yet made the contribution. The deduction is valid as long as you make the

contribution on or before April 15 of the following year, even if you get a filing extension. **More information.** For more information, see Chapter 18, and Publication 590, *Individual Retirement Arrangements (IRAs)* and Education Savings Account (ESAs).

Accrual method. If you use an accrual method, you generally report income when you earn it, rather than when you receive it. You generally deduct your expenses when you incur them, rather than when you pay them.

Income paid in advance. Prepaid income is generally included in gross income in the year you receive it. Your method of accounting does not matter as long as the income is available to you. Prepaid income may include rent or interest you receive in advance and pay for services you will perform later.

Additional information. For more information on accounting methods, including how to change your accounting method, get Publication 538.

Social Security Number

You must enter your social security number (SSN) in the space provided on your return. Be sure the SSN on your return is the same as the SSN on your social security card. If you are married, enter the SSNs for both you and your spouse, whether you file jointly or separately.

If you are filing a joint return, write the SSNs in the same order as the names. Use this same order in submitting other forms and documents to the IRS.

Name change. If you changed your name because of marriage, divorce, etc., immediately notify your Social Security Administration (SSA) office so the name on your tax return is the same as the one the SSA has on its records. This will help prevent delays in issuing your refund and safeguard your future social security benefits.

Dependent's social security number. You must provide the SSN of each dependent you claim, regardless of the dependent's age. This requirement applies to **all dependents** (not just your children) claimed on your tax return.

Exception. If your child was born and died in 2003 and you do not have an SSN for the child, you may attach a copy of the child's birth certificate instead. If you do, enter "DIED" in column (2) of line 6c (Form 1040 or 1040A).

No social security number. File **Form SS-5, Application for a Social Security Card**, with your local SSA office to get an SSN for yourself or your dependent. It usually takes about 2 weeks to get an SSN. If you or your dependent is not eligible for an SSN, see *Individual taxpayer identification number (ITIN)*, later.

If you are a U.S. citizen, you must show proof of age, identity, and citizenship with your Form SS-5. If you are 18 or older, you must appear in person with this proof at an SSA office.

Form SS-5 is available at any SSA office or on the Internet at **www.ssa.gov**. If you have any questions about which documents you can use as proof of age, identity, or citizenship, contact your SSA office.

If your dependent does not have an SSN by the time your return is due, you may want to ask for an extension of time to file, as explained earlier under *When Do I Have To File*.

If you do not provide a required SSN or if you provide an incorrect SSN, your tax may be increased and any refund may be reduced.

Adoption taxpayer identification number (ATIN). If you are in the process of adopting a child who is a U.S. citizen or resident and cannot get an SSN for the child until the adoption is final, you can apply for an ATIN to use instead of an SSN.

File **Form W-7A, Application for Taxpayer Identification Number for Pending U.S. Adoptions**, with the IRS to get an ATIN if **all** of the following are true.

- You have a child living with you who was placed in your home for legal adoption by an authorized placement agency.
- You cannot get the child's existing SSN even though you have made a reasonable attempt to get it from the birth parents, the placement agency, and other persons.
- You cannot get an SSN for the child from the SSA because, for example, the adoption is not final.
- You cannot get an Individual Taxpayer Identification Number (ITIN) (discussed later) for the child.
- You are eligible to claim the child as a dependent on your tax return.

After the adoption is final, you must apply for an SSN for the child. You cannot continue using the ATIN.

See Form W-7A for more information.

Nonresident alien spouse. If your spouse is a nonresident alien and you file a joint or separate return, your spouse must have either an SSN or an ITIN. If your spouse is not eligible for an SSN, see the next discussion.

Individual taxpayer identification number (ITIN). The IRS will issue you an ITIN if you are a nonresident or resident alien and you do not have and are not eligible to get an SSN. To apply for an ITIN, file **Form W-7** with the IRS. It usually takes about 4 to 6 weeks to get an ITIN. Enter this number on your tax return wherever your SSN is requested.

Alien dependent. If your dependent is a nonresident or resident alien who does not have and is not eligible to get an SSN, file Form W-7 with the IRS to apply for an ITIN. Enter this number on your return wherever the dependent's SSN is requested.

Caution. An ITIN is for tax use only. It does not entitle you or your dependent to social security benefits or change the employment or immigration status of either of you under U.S. law.

Penalty for not providing social security number. If you do not include your SSN or the SSN of your spouse or dependent as required, you may have to pay a penalty. See the discussion on *Penalties*, later, for more information.

SSN on correspondence. If you write to the IRS about your tax account, be sure to include your SSN (and the name and SSN of your spouse, if you filed a joint return) in your correspondence. Because your SSN is used to identify your account, this helps the IRS respond to your correspondence promptly.

Presidential Election Campaign Fund

This fund was set up to help pay for presidential election campaigns. If you have a tax liability of at least \$3, you may have \$3 of your tax liability go to this fund by checking the *Yes* box on Form 1040, Form 1040A, or Form 1040EZ. If you are filing a joint return and have a tax liability of at least \$6, your spouse may also have \$3 go to the fund. If you check *Yes*, it will not change the tax you pay or the refund you will receive.

Computations

The following information on entering numbers on your tax return may be useful in making the return easier to complete.

Rounding off dollars. You may round off cents to whole dollars on your return and schedules. If you do round to whole dollars, you must round all amounts. To round, drop amounts under 50 cents and increase amounts from 50 to 99 cents to the next dollar. For example, \$1.39 becomes \$1 and \$2.50 becomes \$3.

If you have to add two or more amounts to figure the amount to enter on a line, include cents when adding the amounts and round off only the total.

Example. You receive two Forms W-2: one showing wages of \$5,000.55 and one showing wages of \$18,500.73. On Form 1040, line 7, you would enter \$23,501 ($\$5,000.55 + \$18,500.73 = \$23,501.28$), not \$23,502 ($\$5,001 + \$18,501$).

Equal amounts. If you are asked to enter the smaller or larger of two equal amounts, enter that amount.

Example. Line 1 is \$500. Line 3 is \$500. Line 5 asks you to enter the smaller of line 1 or 3. Enter \$500 on line 5.

Negative amounts. If you need to enter a negative amount, put the amount in parentheses rather than using a minus sign. To combine positive and negative amounts, add all the positive amounts together and then subtract the negative amounts.

Attachments

Depending on the form you file and the items reported on your return, you may have to complete additional schedules and forms and attach them to your return.

Tip. IRS e-file is *paperless*. There's nothing to sign, attach, or mail, not even your Forms W-2.

Form W-2. Form W-2 is a statement from your employer of wages and other compensation paid to you and taxes withheld from your pay. You should have a Form W-2 from each employer. Be sure to attach a copy of Form W-2 in the place indicated on the front page of your return. Attach it only to the front page of your return, not to any attachments. For more information, see *Form W-2* in chapter 5.

If you received a Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, showing federal income tax withheld, attach a copy of that form in the place indicated on the front page of your return.

Form 1040EZ. There are no additional schedules to file with Form 1040EZ.

Form 1040A. Attach the additional schedules and forms that you had to complete behind the Form 1040A in order by number. If you are filing Schedule EIC, put it last. Do not attach items unless required to do so.

Form 1040. Attach any forms and schedules behind Form 1040 in order of the "Attachment Sequence Number" shown in the upper right corner of the form or schedule. Then arrange all other statements or attachments in the same order as the forms and schedules they relate to and attach them last. Do not attach items unless required to do so.

TAXPLANNER

If you fail to organize your return according to the prescribed sequence numbers, the IRS, upon receipt of your return, will disassemble it and put it back together in the proper order. This procedure may result in the loss of a page of your return, causing some delay in its processing.

Third Party Designee

You can authorize the IRS to discuss your return with a friend, family member, or any other person you choose. If you check the *Yes* box in the *Third party designee* area of your 2003 tax return and provide the information required, you are authorizing:

- 1) The IRS to call the designee to answer any questions that arise during the processing of your return, and
- 2) The designee to:
 - a) Give information that is missing from your return to the IRS,
 - b) Call the IRS for information about the processing of your return or the status of your refund or payments,
 - c) Call the IRS to ask for copies of notices or transcripts related to your return, and
 - d) Respond to certain IRS notices about math errors, offsets (see *Refunds*, later), and return preparation.

The authorization will automatically end no later than the due date (without any extensions) for filing your 2004 tax return. This is April 15, 2005, for most people.

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See your form instructions for more information.

Tip. If you want to allow the paid preparer who signed your return to discuss it with the IRS, just enter "Preparer" in the space for the designee's name.

Signatures

You must sign and date your return. If you file a joint return, both you and your spouse must sign the return, even if only one of you had income.

Caution. If you file a joint return, both spouses are generally liable for the tax, and the entire tax liability may be assessed against either spouse. See chapter 2.

Tip. If you e-file your return, you can use an electronic signature to sign your return. See Does My Return Have To Be on Paper, earlier.

If you are due a refund, it cannot be issued unless you have signed your return.

Enter your occupation in the space provided in the signature section. If you file a joint return, enter both your occupation and your spouse's occupation. Entering your daytime phone number may help speed the processing of your return.

When someone can sign for you. You can appoint an agent to sign your return if you are:

- 1) Unable to sign the return because of disease or injury,
- 2) Absent from the United States for a continuous period of at least 60 days before the due date for filing your return, or
- 3) Given permission to do so by the IRS office in your area.

Power of attorney. A return signed by an agent in any of these cases must have a power of attorney (POA) attached that authorizes the agent to sign for you. You can use a POA that states that the agent is granted authority to sign the return, or you can use **Form 2848, Power of Attorney and Declaration of Representative**. Part I of Form 2848 must state that the agent is granted authority to sign the return.

Unable to sign. If the taxpayer is mentally incompetent and cannot sign the return, it must be signed by a court-appointed representative who can act for the taxpayer.

If the taxpayer is mentally competent but physically unable to sign the return or POA, a valid "signature" is defined under state law. It can be anything that clearly indicates the taxpayer's intent to sign. For example, the taxpayer's "X" with the signatures of two witnesses might be considered a valid signature under a state's law.

Spouse unable to sign. If your spouse is unable to sign for any reason, see *Signing a joint return* in chapter 2.

Child's return. If a child has to file a tax return but cannot sign the return, the child's parent, guardian, or another legally responsible person must sign the child's name, followed by the words "By (your signature), parent for minor child."

Paid Preparer

Generally, anyone you pay to prepare, assist in preparing, or review your tax return must sign it and fill in the other blanks in the paid preparer's area of your return.

If the preparer is self-employed (that is, not employed by any person or business to prepare the return), he or she should check the self-employed box in the *Paid Preparer's Use Only* space on the return.

The preparer must give you a copy of your return in addition to the copy filed with the IRS.

If you prepare your own return, leave this area blank. If another person prepares your return and does not charge you, that person should not sign your return.

If you have questions about whether a preparer must sign your return, contact any IRS office.

Explanation

Paid preparer authorization. In the signature area of your 2003 tax return, you are asked whether the IRS can discuss the return with the paid preparer who signed the return. If you check the "Yes" box, you are authorizing:

- 1) The IRS to call the paid preparer to answer any questions that arise during the processing of your return, and
- 2) The paid preparer to:
 - a) Give information that is missing from your return to the IRS,
 - b) Call the IRS for information about the processing of your return or the status of your refund or payments, and
 - c) Respond to certain IRS notices that you have shown the preparer. These notices about math errors, offsets (see *Refunds*, later), and return preparation will be sent to you, not the preparer.

The authorization cannot be revoked. However, it will automatically end no later than the due date (without any extensions) for filing your 2003 tax return. This is April 15, 2004, for most people.

See your form instructions for more information.

TAXALERT

A person who is paid to prepare all or a substantial portion of your income tax return must sign it. In addition, the IRS says that a tax consultant who is paid to review a tax return that you have already prepared and signed is also considered a tax return preparer and must sign it.

If an individual who prepares your return refuses to sign it, you are probably dealing with someone you should not rely on. While you could still file the return, you should probably consider using another tax preparer. If you have to pay the first preparer, you should report the matter to the IRS.

Refunds

When you complete your return, you will determine if you paid more income tax than you owed. If so, you can get a refund of the amount you overpaid or, if you file Form 1040 or Form 1040A, you can choose to apply all or part of the overpayment to your next year's (2004) estimated tax. You cannot have your overpayment applied to your 2004 estimated tax if you file Form 1040EZ.

Caution. If you choose to have a 2003 overpayment applied to your 2004 estimated tax, you cannot change your mind and have any of it refunded to you after the due date (without extensions) of your 2003 return.

Follow the form instructions to complete the entries to claim your refund and/or to apply your overpayment to your 2004 estimated tax.

Tip. If your refund for 2003 is large, you may want to decrease the amount of income tax withheld from your pay in 2004. See chapter 5 for more information.

Explanation

If you choose to apply all or part of your overpayment to your next year's estimated tax, the estimated tax installment payment is considered made on April 15. Your first installment may be reduced accordingly. For more information, see Chapter 5, *Tax Withholding and Estimated Tax*, and Publication 505, *Tax Withholding and Estimated Tax*.

Direct Deposit. Instead of getting a paper check, you may be able to have your refund deposited directly into your account at a bank or other

financial institution. Follow the form instructions to request Direct Deposit.

If the Direct Deposit cannot be done, the IRS will send a check instead.

Overpayment less than one dollar. If your overpayment is less than one dollar, you will not get a refund unless you ask for it in writing.

Cashing your refund check. Cash your tax refund check soon after you receive it. Checks not cashed within 12 months of the date they are issued will be canceled and the proceeds returned to the IRS.

If your check has been canceled, you can apply to the IRS to have it reissued.

Refund more or less than expected. If you receive a check for a refund you are not entitled to, or for an overpayment that should have been credited to estimated tax, do not cash the check. Call the IRS.

If you receive a check for more than the refund you claimed, do not cash the check until you receive a notice explaining the difference.

If your refund check is for less than you claimed, it should be accompanied by a notice explaining the difference. Cashing the check does not stop you from claiming an additional amount of refund.

If you did not receive a notice and you have any questions about the amount of your refund, you should wait 2 weeks. If you still have not received a notice, call the IRS.

Offset against debts. If you are due a refund but have not paid certain amounts you owe, all or part of your refund may be used to pay all or part of the past-due amount. This includes past-due federal income tax, other federal debts (such as student loans), state income tax, and child and spousal support payments. You will be notified if the refund you claimed has been offset against your debts.

Joint return and injured spouse. When a joint return is filed and only one spouse owes a past-due amount, the other spouse can be considered an *injured spouse*. An injured spouse can get a refund for his or her share of the overpayment that would otherwise be used to pay the past-due amount.

To be considered an injured spouse, you must:

- 1) File a joint return,
- 2) Have reported income (such as wages, interest, etc.),
- 3) Have made and reported tax payments (such as federal income tax withheld from wages or estimated tax payments), or claimed the earned income credit or other refundable credit, and
- 4) Have an overpayment, all or part of which may be applied against the past-due amount.

If you are an injured spouse, you can obtain your portion of the joint refund by completing **Form 8379, Injured Spouse Claim and Allocation**. Follow the instructions on the form.

Amount You Owe

When you complete your return, you will determine if you have paid the full amount of tax that you owe. If you owe additional tax, you should pay it with your return.

If the IRS figures your tax for you, you will receive a bill for any tax that is due. You should pay this bill within 30 days (or by the due date of your return, if later). See *Tax Figured by IRS* in chapter 31.

Caution. If you do not pay your tax when due, you may have to pay a failure-to-pay penalty. See Penalties, later. For more information about your balance due, see Publication 594, The IRS Collection Process.

Tip. If the amount you owe for 2003 is large, you may want to increase the amount of income tax withheld from your pay or make estimated tax payments for 2004. See chapter 5 for more information.

How To Pay

If you have an amount due on your tax return, you can pay by check, money order, or credit card. If you filed electronically, you also may be able to make your payment electronically.

Tip. You do not have to pay if the amount you owe is less than \$1.

Check or money order. If you pay by check or money order, make it out to the "United States Treasury." Show your correct name, ad-

dress, SSN, daytime phone number, and the tax year and form number on the front of your check or money order. If you are filing a joint return, enter the SSN shown first on your tax return.

For example, if you file Form 1040 for 2003 and you owe additional tax, show your name, address, SSN, daytime phone number, and "2003 Form 1040" on the front of your check or money order. If you file an amended return (Form 1040X) for 2002 and you owe tax, show your name, address, SSN, daytime phone number, and "2002 Form 1040X" on the front of your check or money order.

Enclose your payment with your return, but do not attach it to the form. If you filed Form 1040, please complete **Form 1040-V, Payment Voucher**, and enclose it with your payment and return. Form 1040-V will help us process your payment more accurately and efficiently. Follow the instructions that come with the form.

Do not mail cash with your return. If you pay cash at an IRS office, keep the receipt as part of your records.

Payment not honored. If your check or money order is not honored by your bank (or other financial institution) and the IRS does not receive the funds, you still owe the tax. In addition, you may be subject to a dishonored check penalty.

Electronic payment options. Electronic payment options are convenient, safe and secure methods for paying individual income taxes. There's no check to write, money order to buy, or voucher to mail.

Credit card. You can use your American Express®, Discover®, MasterCard®, or Visa® credit card.

To pay by credit card, call a service provider and follow the recorded instructions. You can also pay by credit card over the Internet using a service provider's web site.

The service providers charge a convenience fee based on the amount you are paying. Fees may vary between the providers. You will be told what the fee is during the transaction and will have the option to continue or end the transaction. You may also obtain the convenience fee by calling the service provider's automated customer service telephone number or visiting their respective web site.

Caution. Do not add the convenience fee to your tax payment.

TaxPLANNER

Be careful about paying your taxes by credit card. Most of the payment options demand that you pay a "convenience fee" for using your card. Also, if you won't be paying off your balance right away, the interest your credit card charges may be much higher than the interest the IRS charges for late payment.

If you pay by credit card, write the confirmation number you were given at the end of the transaction and the tax payment amount in the upper left corner of page 1 of your tax return.

Service Providers

Link2Gov Corporation

To make a payment, call1-888-PAY-1040SM
or1-888-729-1040
For Customer Service.....1-888-658-5465
Web Addresswww.PAY1040.com

Official Payments Corporation

To make a payment, call1-800-2PAY-TAXSM
or1-800-272-9829
For Customer Service.....1-877-754-4413
Web Addresswww.officialpayments.com

You can *e-file* and pay in a single step by authorizing a credit card payment. This option is available through some tax software packages and tax professionals. You can also pay by credit card using the telephone or the Internet.

20 THE INCOME TAX RETURN

Electronic funds withdrawal. You can *e-file* and pay in a single step by authorizing an electronic funds withdrawal from your checking or savings account. This option is available through tax software packages, tax professionals, and TeleFile. If you select this payment option, you will need to have your account number, your financial institution's routing transit number, and account type (checking or savings). You can schedule the payment for any future date up to and including the return due date (April 15, 2004).

Caution. *Be sure to check with your financial institution to make sure that an electronic funds withdrawal is allowed and to get the correct routing and account numbers.*

Electronic Federal Tax Payment System (EFTPS). EFTPS offers another way to pay your federal taxes. Best of all, it's free and available to business and individual taxpayers. In fact, it's recommended for estimated tax payments (Form 1040-ES) and installment agreement payments. For details on how to enroll, visit www.EFTPS.gov or call EFTPS Customer Service at 1-800-555-4477 or 1-800-945-8400.

Estimated tax payments. Do not include any 2004 estimated tax payment in the payment for your 2003 income tax return. See chapter 5 for information on how to pay estimated tax.

Interest

Interest is charged on tax you do not pay by the due date of your return. Interest is charged even if you get an extension of time for filing.

Tip. *If the IRS figures your tax for you, interest cannot start earlier than the 31st day after the IRS sends you a bill. For information, see Tax Figured by IRS in chapter 32.*

Interest on penalties. Interest is charged on the failure-to-file penalty, the accuracy-related penalty, and the fraud penalty from the due date of the return (including extensions) to the date of payment. Interest on other penalties starts on the date of notice and demand, but is not charged on penalties paid within 21 calendar days from the date of the notice (or within 10 business days if the notice is for \$100,000 or more).

Interest due to IRS error or delay. All or part of any interest you were charged can be forgiven if the interest is due to an unreasonable error or delay by an officer or employee of the IRS in performing a ministerial or managerial act.

A ministerial act is a procedural or mechanical act that occurs during the processing of your case. A managerial act includes personnel transfers and extended personnel training. A decision concerning the proper application of federal tax law is not a ministerial or managerial act.

The interest can be forgiven only if you are not responsible in any important way for the error or delay and the IRS has notified you in writing of the deficiency or payment. For more information, get Publication 556, *Examination of Returns, Appeal Rights, and Claims for Refund*.

Interest and certain penalties may also be suspended for a limited period if you filed your return by the due date (including extensions) and the IRS does not provide you with a notice specifically stating your liability and the basis for it before the close of the 18-month period beginning on the later of:

- The date the return is filed, or
- The due date of the return without regard to extensions.

For more information, get Publication 556.

TAXPLANNER

If you owe additional tax, it is *not* a good idea to file your return by January 31. As long as you have planned well and have paid enough in estimated taxes to avoid a penalty, you would be better off keeping any other tax you owe in your savings account, where it will earn interest for 2 1/2 months, rather than paying your tax bill early.

Installment Agreement

If you cannot pay the full amount due with your return, you can ask to make monthly installment payments. However, you will be charged interest and may be charged a late payment penalty on the tax not paid by April 15, 2004, even if your request to pay in installments is granted. If your request is granted, you must also pay a fee. To limit the interest and penalty charges, pay as much of the tax as possible with your return. But before requesting an installment agreement, you should consider other less costly alternatives, such as a bank loan.

To ask for an installment agreement, use **Form 9465, *Installment Agreement Request***. You should receive a response to your request within 30 days. But if you file your return after March 31, it may take longer for a reply.

In addition to paying by check or money order, you can use a credit card or EFTPS to make installment agreement payments. See *Credit card* and *Electronic Federal Tax Payment System (EFTPS)*, under *How To Pay*, earlier.

Guaranteed availability of installment agreement. The IRS must agree to accept the payment of your tax liability in installments if, as of the date you offer to enter into the agreement:

- 1) Your total taxes (not counting interest, penalties, additions to the tax, or additional amounts) do not exceed \$10,000,
- 2) In the last 5 years, you (and your spouse if the liability relates to a joint return) have not:
 - a) Failed to file any required income tax return,
 - b) Failed to pay any tax shown on any such return, or
 - c) Entered into an installment agreement for the payment of any income tax,
- 3) You show you cannot pay your income tax in full when due,
- 4) The tax will be paid in full in 3 years or less, and
- 5) You agree to comply with the tax laws while your agreement is in effect.

Gift To Reduce the Public Debt

You can make a contribution (gift) to reduce the public debt. If you wish to do so, make a **separate** check payable to "Bureau of the Public Debt."

Send your check to:

Bureau of the Public Debt
Department G
P.O. Box 2188
Parkersburg, WV 26106-2188.

Or, enclose your separate check in the envelope with your income tax return. Do not add this gift to any tax you owe.

You can deduct this gift as a charitable contribution on next year's tax return if you itemize your deductions on Schedule A (Form 1040).

Peel-Off Address Label

After you have completed your return, peel off the label with your name and address from the back of your tax return package and place it in the appropriate area of the Form 1040, Form 1040A, or Form 1040EZ you send to the IRS. If you have someone prepare your return, give that person your label to use on your tax return.

If you file electronically and you are not eligible or choose not to sign your return using your self-selected PIN, use your label on Form 8453 or 8453-OL. (More information on electronic filing is found earlier in this chapter.)

The label helps the IRS to correctly identify your account. It also saves processing costs and speeds up processing so that refunds can be issued sooner.

Caution. *You must write your SSN in the spaces provided on your tax return.*

Correcting the label. Make necessary name and address changes on the label. If you have an apartment number that is not shown on the label, please write it in. If you changed your name, see the discussion under *Social Security Number*, earlier.

No label. If you did not receive a tax return package with a label, print or type your name and address in the spaces provided at the top of Form 1040 or Form 1040A. If you are married filing a separate return, do not enter your spouse's name in the space at the top. Instead, enter his or her name in the space provided on line 3.

If you file Form 1040EZ and you do not have a label, print or type this information in the spaces provided.

P.O. box. If your post office does not deliver mail to your street address and you have a P.O. box, print your P.O. box number on the line for your present home address instead of your street address.

Foreign address. If your address is outside the United States or its possessions or territories, enter the information on the line for "City, town or post office, state, and ZIP code" in the following order:

- 1) City,
- 2) Province or state, and
- 3) Name of foreign country. (*Do not* abbreviate the name of the country.)

Follow the country's practice for entering the postal code.

TAXALERT

You are not excused from filing a return because you have not received the proper forms from the IRS. In addition to any IRS office (check the telephone book), you may usually obtain the necessary forms at your local post office, public library, or bank. Forms that you can use to file your return are provided at the back of this book. You may also obtain tax forms via the Internet by visiting the IRS site at www.irs.gov.

Where Do I File?

After you complete your return, you must send it to the IRS. You can mail it or you may be able to file it electronically. See *Does My Return Have To Be on Paper*, earlier.

Mailing your return. If an addressed envelope came with your tax forms package, you should mail your return in that envelope.

If you do not have an addressed envelope or if you moved during the year, mail your return to the address shown at the end of this publication for the area where you now live.

What Happens After I File?

After you send your return to the IRS, you may have some questions. This section discusses concerns you may have about recordkeeping, your refund, and what to do if you move.

What Records Should I Keep?

You must keep records so that you can prepare a complete and accurate income tax return. The law does not require any special form of records. However, you should keep all receipts, canceled checks or other proof of payment, and any other records to support any deductions or credits you claim.

If you file a claim for refund, you must be able to prove by your records that you have overpaid your tax.

TAXPLANNER

See the detailed listing of tax records to keep at the end of the *Ernst & Young Individual Tax Organizer* in the front of this book.

How long to keep records. You must keep your records for as long as they are important for the federal tax law.

Keep records that support an item of income or a deduction appearing on a return until the period of limitations for the return runs out. (A period of limitations is the period of time after which no legal action can be brought.) For assessment of tax you owe, this generally is 3 years from the date you filed the return. For filing a claim for credit or refund, this generally is 3 years from the date you filed the original return, or 2 years from the date you paid the tax, whichever is later. Returns filed before the due date are treated as filed on the due date.

If you did not report income that you should have reported on your return, and it is more than 25% of the income shown on the return, the period of limitations does not run out until 6 years after you filed the return. If a return is false or fraudulent with intent to evade tax, or if no return is filed, an action can generally be brought at any time.

You may need to keep records relating to the basis of property longer than the period of limitations. Keep those records as long as they are important in figuring the basis of the original or replacement property. Generally, this means for as long as you own the property and, after you dispose of it, for the period of limitations that applies to you. See chapter 14 for information on basis.

Note. If you receive a Form W-2, keep Copy C until you begin receiving social security benefits. This will help protect your benefits in case there is a question about your work record or earnings in a particular year. Review the information shown on your annual (for workers over age 25) *Social Security Statement*.

Copies of returns. You should keep copies of tax returns you have filed and the tax forms package as part of your records. They may be helpful in amending filed returns or preparing future ones.

If you need a copy of a prior year tax return, you can get it from the IRS. Use **Form 4506**, *Request for Copy of Tax Return*. There is a charge for a copy of a return, which you must pay with Form 4506. It may take up to 60 days to process your request.

Transcript. You can use **Form 4506-T**, *Request for Transcript of Tax Return*, to ask for a transcript of your return filed this year or during the 3 preceding years. It will show most lines from your original return, including accompanying forms and schedules. A transcript usually contains the information that a third party (such as a mortgage company) requires.

Tax account information. If you need a statement of your tax account showing any later changes that you or the IRS made to the original return, you will need to ask the IRS for your tax account information. You should have your name and address, SSN or employer identification number (if applicable), tax period, and form number available. You will get the following information:

- Type of return filed,
- Filing status,
- Federal income tax withheld,
- Tax shown on return,
- Adjusted gross income,
- Taxable income,
- Self-employment tax,
- Number of exemptions,
- Refund,
- Earned income credit, and
- Mortgage interest deduction or real estate tax deduction.



Where Do You File?

If an envelope addressed to "Internal Revenue Service Center" came with this booklet, please use it. If you do not have one or if you moved during the year, mail your return to the Internal Revenue Service Center shown that applies to you.



Envelopes without enough postage will be returned to you by the post office. Your envelope may need additional postage if it contains more than five pages or is oversized (for example, it is over 1/4" thick). Also, include your complete return address.

IF you live in...	THEN use this address if you:	
	Are not enclosing a check or money order...	Are enclosing a check or money order...
Alabama, Florida, Georgia, Mississippi, North Carolina, Rhode Island, South Carolina, West Virginia	Internal Revenue Service Center Atlanta, GA 39901-0002	Internal Revenue Service Center Atlanta, GA 39901-0102
Maine, Massachusetts, New Hampshire, New York, Vermont	Internal Revenue Service Center Andover, MA 05501-0002	Internal Revenue Service Center Andover, MA 05501-0102
Delaware, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, South Dakota, Wisconsin	Internal Revenue Service Center Kansas City, MO 64999-0002	Internal Revenue Service Center Kansas City, MO 64999-0102
Connecticut, District of Columbia, Maryland, New Jersey, Pennsylvania	Internal Revenue Service Center Philadelphia, PA 19255-0002	Internal Revenue Service Center Philadelphia, PA 19255-0102
Arkansas, Colorado, Kentucky, Louisiana, New Mexico, Oklahoma, Tennessee, Texas	Internal Revenue Service Center Austin, TX 73301-0002	Internal Revenue Service Center Austin, TX 73301-0102
Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon, Utah, Washington, Wyoming	Internal Revenue Service Center Fresno, CA 93888-0002	Internal Revenue Service Center Fresno, CA 93888-0102
Ohio, Virginia	Internal Revenue Service Center Memphis, TN 37501-0002	Internal Revenue Service Center Memphis, TN 37501-0102
All APO and FPO addresses, American Samoa, nonpermanent residents of Guam or the Virgin Islands*, Puerto Rico (or if excluding income under Internal Revenue Code section 933), dual-status aliens, a foreign country: U.S. citizens and those filing Form 2555, 2555-EZ, or 4563	Internal Revenue Service Center Philadelphia, PA 19255-0215 USA	Internal Revenue Service Center Philadelphia, PA 19255-0215 USA

* Permanent residents of Guam should use: Department of Revenue and Taxation, Government of Guam, P.O. Box 23607, GMF, GU 96921; permanent residents of the Virgin Islands should use: V.I. Bureau of Internal Revenue, 9601 Estate Thomas, Charlotte Amalie, St. Thomas, VI 00802.

TAXPLANNER

We recommend that you keep all your canceled checks for 6 years. It would be wise to keep your income tax returns permanently. You should keep documents showing your basis in a piece of property for as long as you own that piece of property. If you sell a piece of property, you should keep your records showing your basis in the old property for at least 6 years after the sale.

If you do not keep the requisite records, it may be impossible for you to prove that you incurred deductible expenses or to establish your basis for gain or loss. Without such proof, the IRS can deny you a deduction. If you acquire property from an estate or by gift, it is advisable to secure a copy of the valuation of the estate or of the gift tax return so that you can determine the donor's basis in the property that you have been given. Knowing the donor's basis, you can easily determine your gain or loss when you sell the property. See Chapter 14, *Basis of Property*, for more details on determining gains and losses from the sale of property.

Example

Your parents buy a house for you as a wedding present. You sell the house 10 years later. The only record of the initial

transaction is in the county real estate records. You believe there were other costs associated with the purchase, but you cannot find any records of them. If you claim the additional unsupported costs and the IRS examines your return for the year of the sale, it's likely that those costs will not be allowed. If you claim the additional costs and do not disclose on your return the lack of records to substantiate them, you could be subject to a penalty.

More information. For more information on recordkeeping, get Publication 552, *Recordkeeping for Individuals*.

Interest on Refunds

If you are due a refund, you may get interest on it. The interest rates are adjusted quarterly.

If the refund is made within 45 days after the due date of your return, no interest will be paid. If you file your return after the due date (including extensions), no interest will be paid if the refund is made within 45 days after the date you filed. If the refund is not made within this 45-day period, interest will be paid from the due date of the return or from the date you filed, whichever is later.

Accepting a refund check does not change your right to claim an additional refund and interest. File your claim within the period of time that

applies. See *Amended Returns and Claims for Refund*, later. If you do not accept a refund check, no more interest will be paid on the overpayment included in the check.

Interest on erroneous refund. All or part of any interest you were charged on an erroneous refund generally will be forgiven. Any interest charged for the period before demand for repayment was made will be forgiven unless:

- 1) You, or a person related to you, caused the erroneous refund in any way, or
- 2) The refund is more than \$50,000.

For example, if you claimed a refund of \$100 on your return, but the IRS made an error and sent you \$1,000, you would not be charged interest for the time you held the \$900 difference. You must, however, repay the \$900 when the IRS asks.

Past-Due Refund

You can check on the status of your 2003 refund if it has been at least 6 weeks from the date you filed your return (3 weeks if you filed electronically). Be sure to have a copy of your 2003 tax return available because you will need to know the filing status, the first SSN shown on the return, and the **exact** whole-dollar amount of the refund. To check on your refund, do one of the following.

- Go to www.irs.gov, and click on **Where's My Refund**.
- Call **1-800-829-4477** for automated refund information and follow the recorded instructions.
- Call **1-800-829-1954** during the hours shown in your form instructions.

Change of Address

If you have moved, file your return using your new address.

If you move after you filed your return, you should give the IRS clear and concise written notification of your change of address. Send the notification to the Internal Revenue Service Center serving your old address. You can use **Form 8822, Change of Address**. If you are expecting a refund, also notify the post office serving your old address. This will help in forwarding your check to your new address (unless you chose Direct Deposit of your refund).

Be sure to include your SSN (and the name and SSN of your spouse, if you filed a joint return) in any correspondence with the IRS.

What If I Made a Mistake?

Errors may delay your refund or result in notices being sent to you. If you discover an error, you can file an amended return or claim for refund.

Amended Returns and Claims for Refund

You should correct your return if, after you have filed it, you find that:

- 1) You did not report some income,
- 2) You claimed deductions or credits you should not have claimed,
- 3) You did not claim deductions or credits you could have claimed, or
- 4) You should have claimed a different filing status. (You cannot change your filing status from married filing jointly to married filing separately after the due date of the original return. However, an executor may be able to make this change for a deceased spouse.)

If you need a copy of your return, see *Copies of returns* under *What Records Should I Keep*, earlier in this chapter.

Form 1040X. Use Form 1040X, *Amended U.S. Individual Income Tax Return*, to correct a return you have already filed. An amended tax return cannot be filed electronically under the *e-file* system.

Completing Form 1040X. On Form 1040X, write your income, deductions, and credits as you originally reported them on your return,

the changes you are making, and the corrected amounts. Then figure the tax on the corrected amount of taxable income and the amount you owe or your refund.

If you owe tax, pay the full amount with Form 1040X. The tax owed will not be subtracted from any amount you had credited to your estimated tax.

If you cannot pay the full amount due with your return, you can ask to make monthly installment payments. See *Installment Agreement*, earlier.

If you overpaid tax, you can have all or part of the overpayment refunded to you, or you can apply all or part of it to your estimated tax. If you choose to get a refund, it will be sent separately from any refund shown on your original return.

Filing Form 1040X. After you finish your Form 1040X, check it to be sure that it is complete. Do not forget to show the year of your original return and explain all changes you made. Be sure to attach any forms or schedules needed to explain your changes. Mail your Form 1040X to the Internal Revenue Service Center serving the area where you now live (as shown in the instructions to the form). Do not use the addresses listed at the end of this publication.

File a separate form for each tax year involved.

Time for filing a claim for refund. Generally, you must file your claim for a credit or refund within 3 years after the date you filed your original return or within 2 years after the date you paid the tax, whichever is later. Returns filed before the due date (without regard to extensions) are considered filed on the due date (even if the due date was a Saturday, Sunday, or legal holiday). These time periods are suspended while you are financially disabled, discussed later.

If the last day for claiming a credit or refund is a Saturday, Sunday, or legal holiday, you can file the claim on the next business day.

If you do not file a claim within this period, you may not be entitled to a credit or a refund.

Late-filed return. If you were due a refund but you did not file a return, you generally must file your return within 3 years from the date the return was due (including extensions) to get that refund. Generally, your return must be postmarked no later than 3 years from the date the return was due (including extensions). For information on postmarks, see *Filing on time*, under *When Do I Have To File*, earlier.

Limit on amount of refund. If you file your claim within 3 years after the date you filed your return, the credit or refund cannot be more than the part of the tax paid within the 3-year period (plus any extension of time for filing your return) immediately before you filed the claim. This time period is suspended while you are financially disabled, discussed later.

Tax paid. Payments, including estimated tax payments, made before the due date (without regard to extensions) of the original return are considered paid on the due date. For example, income tax withheld during the year is considered paid on the due date of the return, April 15 for most taxpayers.

Example 1. You made estimated tax payments of \$500 and got an automatic extension of time to August 15, 2001, to file your 2000 income tax return. When you filed your return on that date, you paid an additional \$200 tax. On August 16, 2004 (next business day after August 15, 2004), you filed an amended return and claimed a refund of \$700. Because you filed your claim within 3 years after you filed your original return, you can get a refund of up to \$700, the tax paid within the 3 years plus the 4-month extension period immediately before you filed the claim.

Example 2. The situation is the same as in *Example 1*, except you filed your return on October 27, 2001, 2 1/2 months after the extension period ended. You paid an additional \$200 on that date. On October 27, 2004, you filed an amended return and claimed a refund of \$700. Although you filed your claim within 3 years from the date you filed your original return, the refund was limited to \$200, the tax paid within the 3 years plus the 4-month extension period immediately before you filed the claim. The estimated tax of \$500 paid before that period cannot be refunded or credited.

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If you file a claim more than 3 years after you file your return, the credit or refund cannot be more than the tax you paid within the 2 years immediately before you file the claim.

Example 3. You filed your 2000 tax return on April 16, 2001. You paid taxes of \$500. On November 1, 2002, after an examination of your 2000 return, you had to pay an additional tax of \$200. On May 13, 2004, you file a claim for a refund of \$300. However, because you filed your claim more than 3 years after you filed your return, your refund will be limited to the \$200 you paid during the 2 years immediately before you filed your claim.

Financially disabled. The time periods for claiming a refund are suspended for the period in which you are financially disabled. For a joint income tax return, only one spouse has to be financially disabled for the time period to be suspended. You are financially disabled if you are unable to manage your financial affairs because of a medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months. However, you are not treated as financially disabled during any period your spouse or any other person is authorized to act on your behalf in financial matters.

To claim that you are financially disabled, you must send in the following written statements with your claim for refund.

- 1) A statement from your qualified physician that includes:
 - a) The name and a description of your physical or mental impairment,
 - b) The physician's medical opinion that the impairment prevented you from managing your financial affairs,
 - c) The physician's medical opinion that the impairment was or can be expected to result in death, or that its duration has lasted, or can be expected to last, at least 12 months,
 - d) The specific time period (to the best of the physician's knowledge), and
 - e) The following certification signed by the physician: "Thereby certify that, to the best of my knowledge and belief, the above representations are true, correct, and complete."
- 2) A statement made by the person signing the claim for credit or refund that no person, including your spouse, was authorized to act on your behalf in financial matters during the period of disability (or the exact dates that a person was authorized to act for you).

Exceptions for special types of refunds. If you file a claim for one of the items listed below, the dates and limits discussed earlier may not apply. These items, and where to get more information, are as follows.

- Bad debt. (See *Nonbusiness Bad Debts* in chapter 15.)
- Worthless security. (See *Worthless securities* in chapter 15.)
- Foreign tax paid or accrued. (See Publication 514, *Foreign Tax Credit for Individuals*.)
- Net operating loss carryback. (See Publication 536, *Net Operating Losses (NOLs) for Individuals, Estates, and Trusts*.)
- Carryback of certain business tax credits. (See Form 3800, *General Business Credit*.)
- Claim based on an agreement with the IRS extending the period for assessment of tax.
- Injured spouse claim. (See *Offset against debts*, earlier.)

Processing claims for refund. Claims are usually processed shortly after they are filed. Your claim may be accepted as filed, disallowed, or subject to examination. If a claim is examined, the procedures are the same as in the examination of a tax return.

If your claim is disallowed, you will receive an explanation of why it was disallowed.

Taking your claim to court. You can sue for a refund in court, but you must first file a timely claim with the IRS. If the IRS disallows your claim or does not act on your claim within 6 months after you file it, you can then take your claim to court. For information on the burden of proof in a court proceeding, see Publication 556.

The IRS provides a fast method to move your claim to court if:

- You are filing a claim for a credit or refund based solely on contested income tax or on estate tax or gift tax issues considered in your previously examined returns, and
- You want to take your case to court instead of appealing it within the IRS.

When you file your claim with the IRS, you get the fast method by requesting in writing that your claim be immediately rejected. A notice of claim disallowance will then be promptly sent to you.

You have 2 years from the date of mailing of the notice of disallowance to file a refund suit in the United States District Court having jurisdiction or in the United States Court of Federal Claims.

Interest on refund. If you receive a refund because of your amended return, interest will be paid on it from the due date of your original return or the date you filed your original return, whichever is later, to the date you filed the amended return. However, if the refund is not made within 45 days after you file the amended return, interest will be paid up to the date the refund is paid.

Reduced refund. Your refund may be reduced by an additional tax liability that has been assessed against you.

Also, your refund may be reduced by amounts you owe for past-due child support, debts to another federal agency, or for state tax. If your spouse owes these debts, see *Offset against debts*, earlier, for the correct refund procedures to follow.

Effect on state tax liability. If your return is changed for any reason, it may affect your state income tax liability. This includes changes made as a result of an examination of your return by the IRS. Contact your state tax agency for more information.

TAXPLANNER

The IRS routinely shares information with most states that have state income taxes. If you file an amended federal tax return showing a balance due, you may avoid interest on tax due to the state and any penalties by taking the initiative and filing amended state tax returns when that is appropriate.

Penalties

The law provides penalties for failure to file returns or pay taxes as required.

Civil Penalties

If you do not file your return and pay your tax by the due date, you may have to pay a penalty. You may also have to pay a penalty if you substantially understate your tax, file a frivolous return, or fail to supply your SSN or individual taxpayer identification number. If you provide fraudulent information on your return, you may have to pay a civil fraud penalty.

Filing late. If you do not file your return by the due date (including extensions), you may have to pay a **failure-to-file** penalty. The penalty is based on the tax not paid by the due date (without regard to extensions). The penalty is usually 5% for each month or part of a month that a return is late, but not more than 25%.

Fraud. If your failure to file is due to fraud, the penalty is 15% for each month or part of a month that your return is late, up to a maximum of 75%.

Return over 60 days late. If you file your return more than 60 days after the due date or extended due date, the minimum penalty is the smaller of \$100 or 100% of the unpaid tax.

Exception. You will not have to pay the penalty if you show that you failed to file on time because of reasonable cause and not because of willful neglect.

Paying tax late. You will have to pay a **failure-to-pay** penalty of 1/2 of 1% (.50%) of your unpaid taxes for each month, or part of a

month, after the due date that the tax is not paid. This penalty does not apply during the automatic 4-month extension of time to file period if you paid at least 90% of your actual tax liability on or before the due date of your return and pay the balance when you file the return.

The monthly rate of the failure-to-pay penalty is half the usual rate (.25% instead of .50%) if an installment agreement is in effect for that month. You must have filed your return by the due date (including extensions) to qualify for this reduced penalty.

If a notice of intent to levy is issued, the rate will increase to 1% at the start of the first month beginning at least 10 days after the day that the notice is issued. If a notice and demand for immediate payment is issued, the rate will increase to 1% at the start of the first month beginning after the day that the notice and demand is issued.

This penalty cannot be more than 25% of your unpaid tax. You will not have to pay the penalty if you can show that you had a good reason for not paying your tax on time.

Combined penalties. If both the failure-to-file penalty and the failure-to-pay penalty (discussed earlier) apply in any month, the 5% (or 15%) failure-to-file penalty is reduced by the failure-to-pay penalty. However, if you file your return more than 60 days after the due date or extended due date, the minimum penalty is the smaller of \$100 or 100% of the unpaid tax.

Accuracy-related penalty. You may have to pay an accuracy-related penalty if you underpay your tax because:

- 1) You show *negligence* or *disregard* of the rules or regulations, or
- 2) You substantially understate your income tax.

The penalty is equal to 20% of the underpayment. The penalty will not be figured on any part of an underpayment on which the fraud penalty (discussed later) is charged.

Negligence or disregard. The term “negligence” includes a failure to make a reasonable attempt to comply with the tax law or to exercise ordinary and reasonable care in preparing a return. Negligence also includes failure to keep adequate books and records. You will not have to pay a negligence penalty if you have a reasonable basis for a position you took.

The term “disregard” includes any careless, reckless, or intentional disregard.

TAXPLANNER

The IRS has a comprehensive program to compare the amounts of income reported as paid by payers on Form 1099 series information returns with the amounts of income reported by the payees in their income tax returns. If this document-matching program discloses apparently underreported income, you will receive a notice of additional tax due that may include imposition of a 20% negligence penalty. If you receive an information return showing income paid to you that, through no fault of your own, you did not receive in 2003 or that for some reason is not taxable to you, you should nevertheless report as income on your return the entire amount shown by the information return and subtract from that the amount you believe to be erroneous. Following this procedure usually will avoid automatic generation of the IRS notice and the inconvenience and frustration of corresponding with the IRS to get the matter resolved.

Adequate disclosure. You can avoid the penalty for disregard of rules or regulations if you adequately disclose on your return a position that has at least a reasonable basis. See *Disclosure statement*, later.

This exception will not apply to an item that is attributable to a tax shelter. In addition, it will not apply if you fail to keep adequate books and records, or substantiate items properly.

Substantial understatement of income tax. You understate your tax if the tax shown on your return is less than the correct tax. The understatement is substantial if it is more than the larger of 10% of the correct tax or \$5,000. However, the amount of the understatement may be reduced to the extent the understatement is due to:

- 1) **Substantial authority**, or
- 2) **Adequate disclosure** and a reasonable basis.

If an item on your return is attributable to a tax shelter, there is no reduction for an adequate disclosure. However, there is a reduction for a position with substantial authority, but only if you reasonably believed that your tax treatment was more likely than not the proper treatment.

Substantial authority. Whether there is or was substantial authority for the tax treatment of an item depends on the facts and circumstances. Some of the items that may be considered are court opinions, Treasury regulations, revenue rulings, revenue procedures, and notices and announcements issued by the IRS and published in the *Internal Revenue Bulletin* that involve the same or similar circumstances as yours.

Disclosure statement. To adequately disclose the relevant facts about your tax treatment of an item, use **Form 8275, Disclosure Statement**. You must also have a reasonable basis for treating the item the way you did.

In cases of substantial understatement only, items that meet the requirements of Revenue Procedure 2002-66 (or later update) are considered adequately disclosed on your return without filing Form 8275.

Use **Form 8275-R, Regulation Disclosure Statement**, to disclose items or positions contrary to regulations.

Reasonable cause. You will not have to pay a penalty if you show a good reason (reasonable cause) for the way you treated an item. You must also show that you acted in good faith.

Explanation

The IRS's explanation of the penalty for substantial understatement and how to avoid it oversimplifies a very complex situation.

Under regulations issued by the IRS, the following items may generally be considered substantial authority:

- Internal Revenue Code and other statutory provisions
- Temporary and final IRS regulations
- Court cases
- Administrative pronouncements (including revenue rulings and revenue procedures)
- Tax treaties and regulations issued as a result of a treaty
- Congressional intent as reflected in committee reports, joint explanatory statements of managers included in conference committee reports, and statements made in Congress by one of a bill's managers prior to enactment of a bill
- General explanations of tax legislation prepared by the Joint Committee on Taxation (the Blue Book)
- Proposed IRS regulations
- Information or press releases, notices, announcements, and any other similar documents published by the IRS in the *Internal Revenue Bulletin*
- Private letter rulings, technical advice memoranda, actions on decisions, and general counsel memoranda after they have been released to the public, if they are dated after March 12, 1981

Frivolous return. You may have to pay a penalty of \$500 if you file a frivolous return. A frivolous return is one that does not include enough information to figure the correct tax or that contains information clearly showing that the tax you reported is substantially incorrect.

26 THE INCOME TAX RETURN

You will have to pay the penalty if you filed this kind of return because of a frivolous position on your part or a desire to delay or interfere with the administration of federal income tax laws. This includes altering or striking out the preprinted language above the space provided for your signature.

This penalty is added to any other penalty provided by law.

Explanation

Congress enacted this penalty to attack a great variety of tax protest activities, including:

1. Irregular tax forms not in processible form
2. References to spurious constitutional arguments as a basis for not completing tax forms
3. Unallowable deductions claimed as a protest against military expenses
4. Deliberate use of incorrect Tax Tables
5. Presentation of clearly inconsistent information, such as a taxpayer who lists only two dependents while claiming 99 exemptions for withholding purposes

TAXALERT

Unlike most other penalties, the penalty for filing a frivolous return is not based on your tax liability. The penalty for filing a frivolous return will be assessed immediately and added to any other penalties.

The penalty must be paid in full upon notice and demand from IRS even if you protest the penalty.

Fraud. If there is any underpayment of tax on your return due to fraud, a penalty of 75% of the underpayment due to fraud will be added to your tax.

Joint return. The fraud penalty on a joint return does not apply to a spouse unless some part of the underpayment is due to the fraud of that spouse.

Failure to supply social security number. If you do not include your SSN or the SSN of another person where required on a return, statement, or other document, you will be subject to a penalty of \$50 for

each failure. You will also be subject to a penalty of \$50 if you do not give your SSN to another person when it is required on a return, statement, or other document.

For example, if you have a bank account that earns interest, you must give your SSN to the bank. The number must be shown on the Form 1099-INT or other statement the bank sends you. If you do not give the bank your SSN, you will be subject to the \$50 penalty. (You also may be subject to "backup" withholding of income tax. See chapter 5.)

You will not have to pay the penalty if you are able to show that the failure was due to reasonable cause and not willful neglect.

Failure to furnish tax shelter registration number. A person who sells (or otherwise transfers) to you an interest in a tax shelter must give you the tax shelter registration number or be subject to a \$100 penalty. If you claim any deduction, credit, or other tax benefit because of the tax shelter, you must attach **Form 8271, Investor Reporting of Tax Shelter Registration Number**, to your return to report this number. You will have to pay a penalty of \$250 for each failure to report a tax shelter registration number on your return. The penalty can be excused if you have a reasonable cause for not reporting the number.

Criminal Penalties

You may be subject to criminal prosecution (brought to trial) for actions such as:

- 1) Tax evasion,
- 2) Willful failure to file a return, supply information, or pay any tax due,
- 3) Fraud and false statements, or
- 4) Preparing and filing a fraudulent return.

TAXALERT

In addition to any of the other penalties discussed in this section, you can be charged a penalty for paying your tax with a bad check. The penalty may not be imposed if you submit a bad check in good faith and with reasonable cause to believe that it will be paid. The penalty is 2% of the amount of the check or, if the check is less than \$750, the lesser of \$15 or the amount of the check.