

Your Business **TAX** Guide

Questions

What you don't know could really cost you

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A: Well, of course! Refer to the "What's New" section of the Form 1040 instructions, the Form 1040A instructions or the Form 1040EZ instructions.

Q: Really, I don't owe taxes. I checked three times. So, can I file electronically after April 17?

A: Yes, you can electronically file your return after April 17. To do so, you must file Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, on or before April 17.

Q: How long does it take after you've filed to receive a refund?

A: What? You want your money back? Sheesh. Processing time for refund returns depends on the method used for filing. If you e-file opting for direct deposit and have not received your refund within three weeks after filing your return (eight weeks if you filed a paper return opting for a paper check), you can check your refund status by clicking on "Where's My Refund?" then go to "Get My Refund Status."

Or, you can call the Refund Hotline at 800-829-1954. Have a copy of your current tax return in front of you before you call.

Q: I almost hate to ask this, but can my refund be used to pay other debts?

A: Yep. State and federal agencies refer to the IRS the names of taxpayers who are behind in their support payments, taxes, and loans.

Your refund may not go to you if you are delinquent in child or child and spousal support payments, have a past due federal debt (such as a student loan), or owe state income taxes.

Q: I am in a disaster area and heard the IRS could help me.

A: If you have been affected by a presidentially declared disaster, the IRS may help you by allowing additional time for filing returns and making payments, and in some circumstances, waiving penalties if the disaster has caused you to file or pay late.

The IRS may also provide free copies or transcripts of previously filed returns. You may be eligible to file for a casualty loss deduction on the prior year's tax return.

Q: I cashed some Series E, Series EE and Series I savings bonds. How do I report the interest?

A: If your total taxable interest for the year is more than \$1,500, you report (and separately identify) the interest on Schedule B of Form 1040 or Schedule 1 of Form 1040A.

If your total interest is not more than \$1,500 for the year, report the savings bond interest with your other interest on the "Interest" line of your tax return. For more information, go to www.irs.gov.

Q: This is the first year that I received retirement benefits. Are any of my benefits taxable?

A: If you receive retirement benefits in the form of pension or annuity payments, the amounts you receive may be fully or partly taxable in the year received.

Refer to Tax Topic 410, Pensions and Annuities, or Publication 575, Pension and Annuity Income. Or Tax Topic 423 or Publication 915, Social Security and Equivalent Railroad Retirement Benefits.

Q: I retired last year and started receiving Social Security payments. Do I have to pay taxes on my Social Security benefits?

A: To make this perfectly clear: It depends.

Compare the base amount for your filing status with the total of one-half of your Social Security payments plus all your income from other sources, including tax-exempt interest.

If you are married and file a joint return, you must combine your incomes and your Social Security when figuring the taxable portion of the benefits.

The taxable amount of the benefits is figured on a work sheet in the Form 1040 or Form 1040A instruction book, or in Publication 915, Social Security and Equivalent Railroad Retirement Benefits. Refer to Tax Topic 423, Social Security and Equivalent Railroad Retirement Benefits.

Q: How do I figure the cost basis when the stocks I'm selling were purchased at various times and at different

prices?

A: We're tempted to say first, clear your schedule for the day - you're gonna need it. Second, take a couple of aspirin before you begin.

If you can identify which shares of stock you sold, your basis is what you paid for the shares sold (plus sales commissions). If you sell a block of the same kind of stock, you can report all the shares sold at the same time as one sale, writing VARIOUS in the "date acquired" column of Form 1040, Schedule D.

If you cannot adequately identify the shares you sold and you bought the shares at various times for different prices, the basis of the stock sold is the basis of the shares you acquired first (first-in first-out). You cannot use the average price per share to figure gain or loss on the sale of stock. Refer to Publication 550, Investment Income and Expenses.

Q: If I sell my home and use the money I receive to pay off the mortgage, do I have to pay taxes on that money?

A: It is not the money you receive for the sale of your home, but the amount of gain on the sale over your cost, or basis, that determines whether you will have to include any proceeds as taxable income on your return.

If you can exclude all of the gain, you do not need to report the sale on your tax return. Refer to Publication 523, Selling Your Home.

Q: How do I calculate the average basis for the sale of mutual fund shares?

A: In order to figure your gain or loss using an average basis, you must have acquired the shares at various times and prices and have left them on deposit in a managed account. Wait! It gets better.

There are two average basis methods:

- Single-category method. Add up the cost of all the shares you own in the fund. Divide by the total number of shares you own. This gives you your average per share. Multiply that number by the number of shares sold.

- Double-category method. First, divide your shares into two categories, long-term and short-term. Then use the steps above to get an average basis for each category. The average basis for that category is then the basis of each share in the sale from that category.

Once you elect to use an average basis method, you must continue to use it for all accounts in the same fund.

Refer to Publication 564, Mutual Fund Distributions, Sales, Exchanges and Redemptions.

Q: Am I being ripped off by my mutual fund company? I never sold a share, yet I received a 1099-DIV showing a capital gain. Why do I have to report capital gains from my mutual funds if I never sold any shares?

A: The short answer: Because.

The longer answer: One of the ways the fund makes money for its investors is to sell its assets at a gain. If the asset was held by the mutual fund for more than one year, the nature of the income is capital gain, which gets passed on to you.

These are called capital gain distributions, which are distinguished from income that is from other profits,

called ordinary dividends.

If your capital gains distribution is automatically reinvested, the reinvested amount is the basis of the additional shares purchased.

Q: How do I calculate the minimum amount that must be withdrawn from my IRA after age 70½?

A: Refer to Chapter 1 of Publication 590, Individual Retirement Arrangements (IRAs).

Generally the minimum distribution is computed using one of three tables found in Publication 590.

Table I is used by beneficiaries.

Table II is for use by owners who have spouses who are more than 10 years younger.

Table III is generally for use by unmarried owners and owners who have spouses who are not more than 10 years younger.

Q: Are alimony payments considered taxable income?

A: If you received alimony, separate maintenance, and similar payments from your spouse or former spouse, the amounts are taxable to you in the year received. Isn't America wonderful?

The amount is reported on Form 1040. You cannot use Form 1040A or Form 1040EZ. Refer to Tax Topic 406, Alimony Received, or Publication 504, Divorced or Separated Individuals.

Q: Can I deduct alimony paid to my former spouse?

A: This may somewhat reduce the pain of making payments. If you are divorced or separated, you may be able to deduct the alimony or separate maintenance payments.

Refer to Tax Topic 452, Alimony Paid, and Publication 504, Divorced or Separated Individuals.

Q: Believe it or not, I have tried to give you IRS folks some of my money. But you apparently don't need it since my check hasn't been cashed yet. What should I do?

A: You can call 800-829-1040 and ask an IRS representative if the payment has been credited to your account. If it has not and the check has not cleared, you may choose to place a stop-payment on the original check and send another payment.

Q: Can I ask to make installment payments on the amount I owe?

A: Yes. If you cannot pay the full amount due as shown on your return, you can ask to

make monthly installment payments.

You will be charged a one-time fee of \$43, as well as interest on any tax not paid by its due date, and you may be charged a late payment penalty even if your request to pay in installments is granted.

To request an installment agreement, send Form 9465, Installment Agreement Request, with your return or call 800-829-1040. Refer to Tax Topic 202, What to do if You Can't Pay Your Tax, or Publication 594, Understanding the Collection Process.

Q: I filed my taxes electronically, but you rejected my tax return. What do I do now?

A: Your next action depends on the reason your return was rejected. If you made a mistake in entering the Social Security number or misspelled a name, you can fix these errors and have the return sent again to the IRS.

There are other errors that will cause you to have to file using a paper return.

You can call our Customer Service number at 800-829-1040. Refer to Tax Topic 252, Electronic Filing.

Q: If two single people (never married) have a child and live together, providing equal support, can they both claim head of household status?

A: No. Only the person who paid more than half the cost of keeping up a home for the year would qualify for the head of household filing status.

If both people paid exactly the same amount, neither would qualify for the head of household filing status. Refer to Publication 501, Exemptions, Standard Deduction, and Filing Information.

Q: I am divorced with one dependent child. This year my ex-spouse will claim the child as an exemption. Does this mean I cannot qualify as head of household?

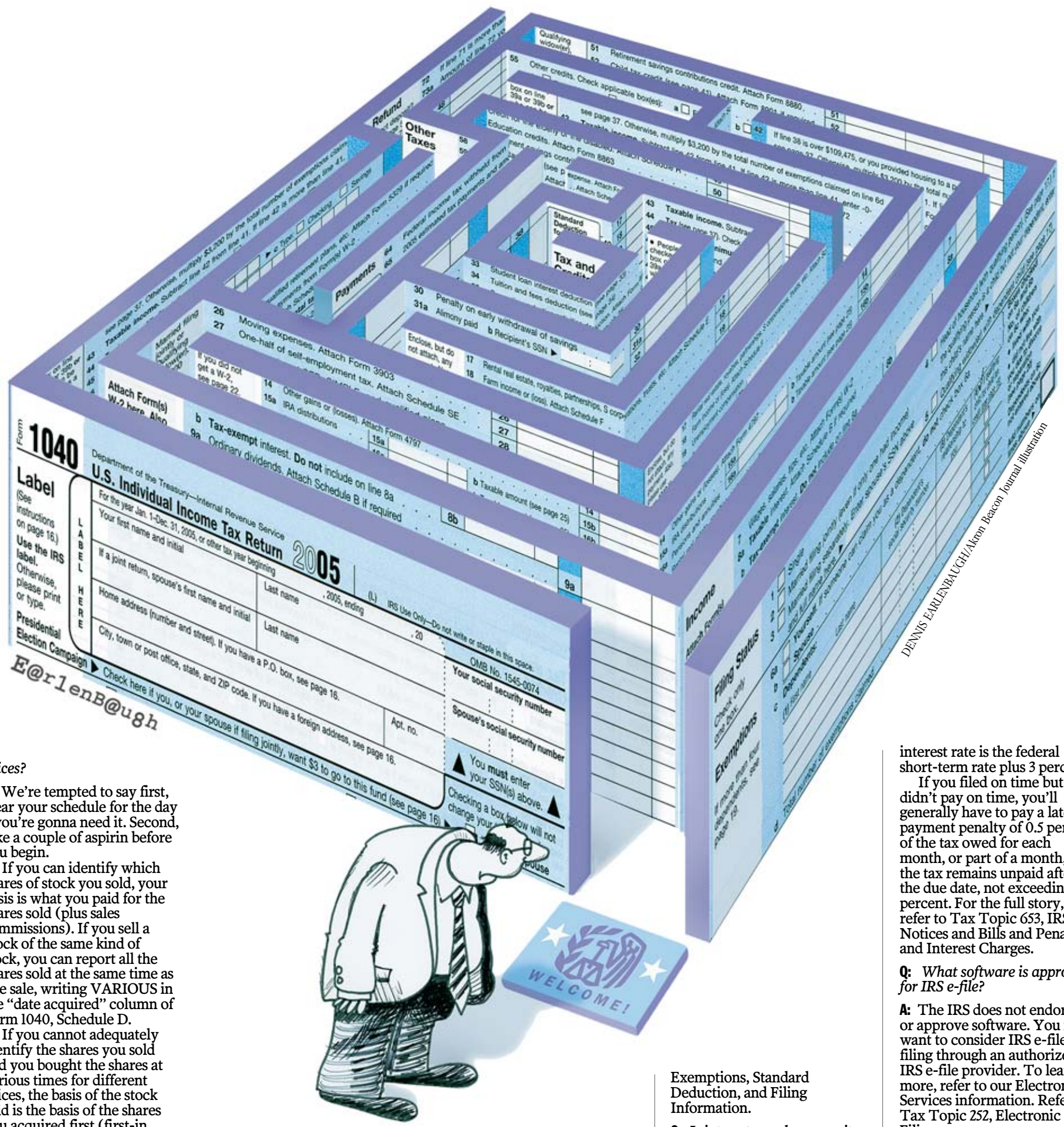
A: You can file as head of household even though you do not claim your unmarried dependent child as an exemption if you meet certain requirements:

1. You are unmarried or are considered unmarried on the last day of the year.

2. You paid more than half the cost of keeping up a home for the year.

3. A qualifying person must live with you in the home for more than half the year (except for temporary absences such as school).

Refer to Publication 501,



interest rate is the federal short-term rate plus 3 percent.

If you filed on time but didn't pay on time, you'll generally have to pay a late payment penalty of 0.5 percent of the tax owed for each month, or part of a month, that the tax remains unpaid after the due date, not exceeding 25 percent. For the full story, refer to Tax Topic 653, IRS Notices and Bills and Penalty and Interest Charges.

Q: What software is approved for IRS e-file?

A: The IRS does not endorse or approve software. You may want to consider IRS e-file by filing through an authorized IRS e-file provider. To learn more, refer to our Electronic Services information. Refer to Tax Topic 252, Electronic Filing.

Q: How about help with a tax preparer?

A: First, remember that you and all other taxpayers are responsible for the accuracy of all entries made on tax returns, which include related schedules, forms and supporting documentation. This remains true whether the return is prepared by the taxpayer or by a preparer.

You should avoid preparers who:

- Claim they can obtain larger refunds than other preparers.
- Base their fee on the refund.

Also, never sign a blank tax form.

Finally, remember that tax evasion is a felony, punishable by up to five years' in prison and a \$250,000 fine.

Q: I'm a waiter and do pretty well. Of my allocated tips, I tip out 15 percent to the busboy and 5 percent to the bar. Where do I deduct this on my return?

A: You cannot deduct tip-outs (the tips you split with other employees) on your tax return. Nor can you deduct them from your allocated tips.

The practice of tipping out is one of the reasons you should keep a detailed daily log of your tips.

Publication 1244, Employee's Daily Record of Tips and Report to Employer, includes Forms 4070 and 4070A, Employee's Report of Tips to Employer, that provides lines to record the necessary information. Refer to Publication 531, Reporting Tip Income.

Q: I didn't get my W-2 by Jan. 31, so I asked my employer for it, but I still don't have it. What should I do?

A: If you don't receive your Form W-2 by Feb. 15, contact the IRS for assistance at 800-829-1040. Refer to Tax Topic 154, Form W-2 - What To Do If Not Received.

Q: I own stock which became worthless last year. Can I take a bad debt deduction?

A: If you own securities and they become totally worthless, you can take a deduction for a loss, but not for a bad debt.

The worthless securities are treated as though they were capital assets sold on the last day of the tax year if they were capital assets in your hands.

Report worthless securities on Form 1040, Schedule D. Refer to Chapter 4 of Publication 550, Investment Income and Expenses (Including Capital Gains and Losses).

For more information on bad debts, refer to Tax Topic 453, Bad Debt Deduction.

Exemptions, Standard Deduction, and Filing Information.

Q: Is interest on a home equity line of credit deductible as a second mortgage?

A: You may deduct home equity debt interest, as an itemized deduction, if you are legally liable to pay the interest, pay the interest in the tax year, secure the debt with your home, and do not exceed certain limitations.

Refer to Publication 936, Home Mortgage Interest Deduction, and Tax Topic 505, Interest Expense.

Q: My father is in a nursing home, and I pay for the entire cost. Can I deduct the expenses on my tax return?

A: You may deduct qualified medical expenses you pay for yourself, your spouse, and your dependents, including a person you claim as a dependent under a Multiple Support Agreement.

Nursing home expenses are allowable as medical expenses in certain instances.

If you, your spouse, or your dependent is in a nursing home, and the primary reason for being there is for medical care, the entire cost, including meals and lodging, is a medical expense. If the individual is in the home mainly for personal reasons, then only the cost of the actual medical care is a medical expense, and the cost of the meals and lodging is not deductible.

Refer to Publication 502, Medical and Dental Expenses.

Q: My last name is actually spelled Mxyzptlk. But somehow the name came out spelled backwards on my refund check, which is a no-no where I come from. How can I correct the spelling of my name with IRS?

A: The name on the refund check is spelled the way it appears on your tax return. If the address label you receive is spelled wrong, do not use the label. Instead, print the information on the tax return. You can also call 800-829-1040 and the IRS can change the spelling over the phone.

Q: Do I need to change my maiden name to my married name on my Social Security card for us to file jointly?

A: You can still file Married Filing Jointly without changing your name with the Social Security Administration. However, you do need to show your maiden name on the tax return instead of your married name.

Q: What kind of penalties and interest will I be charged for paying and filing my taxes late?

A: Interest, compounded daily, is charged on any unpaid tax from the due date of the return until the date of payment. The