



THE BASIC'S – FEDERAL TAX FORM 1040 Continued

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In the continuing series of articles on the basics of tax returns. Last month, page one of the 1040 form was analyzed, this month our story continues on page two. The Adjusted Gross Income (AGI) is transferred from the bottom of page one to the top of page two.

The first section on the page two is the deductions section. Everyone has two deductions. The first is like a “cost of living” deduction. There is a standard amount based on your filing status or, if greater than the standard, itemized deductions can be used. Itemized deductions are figured on Schedule A and include mortgage interest, taxes, charitable giving, some portion of medical expenses and several other expenses. The next article will cover this in more detail.

The other deduction is for the number of exemptions claimed on the return. In 2007, the amount per exemption was \$3400 each for the taxpayer, spouse and each dependent. A person who files but is claimed as a dependent on another return will get \$0 of exemption deduction. With the deductions subtracted, the taxable income is now calculated.

The middle section of the form is the tax, credit, refund and payment section. The taxable income is calculated with the adjustments and deductions subtracted. The tax is figured from the tables or from other forms. The AMT tax is added if appropriate, then credits are applied. Credits are the best subtraction, because, even in the 15% bracket, one dollar of credit is worth 15 dollars of deduction. All credits are transferred from some other form to the 1040. If you have credits, your return is more complex, because they can be handled differently depending on your income and the kind of credit. Credits will be discussed in a future article.

After the tax is calculated and the credits and payments are applied, your refund or required payment is calculated. The IRS is encouraging direct deposit of refunds by sending those faster than paper checks. Some people do not want direct deposit because they do not want to IRS to know their bank account information. It is a fact that if the IRS believes it needs to know your banking information, it can get it, whether the information is on your return or not. Leaving it off of your return is no safeguard.

The last section of the form, the signature section, is little used in the age of e-filing, but is important nonetheless. The first area is the third party designee. The purpose of checking “yes” in that box is to allow the IRS to call the preparer if there is a problem processing the return and only for processing problems. If you have paid a tax preparer to create your return why would you not want that person to solve any processing problems.

The other important area is the occupation box. The occupation classifies the taxpayer. A realtor with mileage seems normal, but a bank teller with mileage might raise a red (audit) flag. Even something that seems simple can have consequences when dealing with the IRS.

