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Educational Expenses

For use in preparing
1998 Returns



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Important Changes

Education incentives. Beginning in 1998, a number of tax benefits are available to families who are saving for or paying higher education costs or who are repaying student loans. These benefits are briefly explained here. For more detailed information, get Publication 970, *Tax Benefits for Higher Education*.

- 1) **Education credits.** For qualified tuition and related expenses paid after December 31, 1997, for academic periods beginning after that date, you may be able to claim a **Hope credit** of up to \$1,500 for **each** eligible student. For qualified tuition and related expenses paid after June 30, 1998, for academic periods beginning after that date, you may be able to claim a **lifetime learning credit** of up to \$1,000 for **all** students. However, you cannot take the Hope credit and the lifetime learning credit for the same student in the same year.
- 2) **Student loans.** For payments due and paid after 1997, you may be able to deduct interest you pay on a qualified student loan. And, if a student loan is canceled, you may not have to include the canceled debt in income.
- 3) **Education IRA.** You may be able to contribute up to \$500 each year to an education IRA for a child under age 18. Contributions to an education IRA are not deductible, but amounts deposited in

the account grow tax free until withdrawn. Withdrawals from an education IRA to pay the child's qualified higher education expenses are also tax free.

- 4) **Withdrawals from traditional or Roth IRAs.** You can make withdrawals from your traditional or Roth IRA for qualified higher education expenses. (A traditional IRA is an IRA that is not a Roth IRA, SIMPLE IRA, or education IRA.) You will owe income tax on at least part of the withdrawal but you will not have to pay the 10% tax on early withdrawals.



You cannot claim more than one type of tax benefit for the same expense. If you use all or part of your qualifying educational expenses as the basis for any of the new benefits, you must reduce the amount of your qualifying educational expenses when computing your educational expense deduction.

Standard mileage rate. Generally, if you used your car for transportation to school, you can deduct 32½ cents per mile. Beginning in 1998, you can use this standard mileage rate for a car you lease, as well as a car you own. See *Using your car* under *What Educational Expenses Are Deductible?*

Limit on itemized deductions. If your adjusted gross income is more than \$124,500 (\$62,250 if you are married filing separately), your itemized deductions may be limited. See the instructions for line 28 of Schedule A (Form 1040).

Introduction

This publication discusses work-related educational expenses that you may be able to deduct as business expenses and the exclusion from income of employer-provided educational assistance benefits.

To be able to deduct educational expenses, you must:

- 1) Be working,
- 2) Itemize your deductions on Schedule A (Form 1040) if you are an employee, and
- 3) Meet the requirements discussed under *Qualifying Education*.

Educational expenses that are not work related, such as costs of sending children to college, are personal expenses that you cannot deduct. However, you may be eligible for other tax benefits explained in Publication 970.

Useful Items

You may want to see:

Publication

- 463** Travel, Entertainment, Gift, and Car Expenses
- 520** Scholarships and Fellowships
- 535** Business Expenses
- 970** Tax Benefits for Higher Education

Form (and Instructions)

- 2106** Employee Business Expenses
- 2106-EZ** Unreimbursed Employee Business Expenses
- Schedule A (Form 1040)** Itemized Deductions

See *How To Get More Information*, near the end of this publication, for information about getting these publications and forms.

Qualifying Education

You can deduct educational expenses only if they are for qualifying education. This is education that meets at least one of the following two tests.

- 1) The education is required by your employer or the law to keep your present salary, status, or job.
- 2) The education maintains or improves skills needed in your present work.

You can deduct the expenses for qualifying education even if the education could lead to a degree.

Education that does not qualify. Even if the education meets one of the two tests above, it does not qualify if it:

- 1) Is needed to meet the minimum educational requirements of your present trade or business, or
- 2) Is part of a program of study that can qualify you for a new trade or business.

See *Nonqualifying Education*, later, for more information.

You can use *Figure A* as a quick check to see if your education qualifies.

Education Required by Employer or by Law

Once you have met the minimum educational requirements for your job, your employer or the law may require you to get more education. This additional education is qualifying education if it is required for you to keep your present salary, status, or job, and the requirement serves a business purpose of your employer. The education must not be part of a program that will qualify you for a new trade or business.

When you get more education than your employer or the law requires, the additional education is qualifying only if it maintains or improves skills required in your present work. See *Education To Maintain or Improve Skills*.

Example. You are a teacher who has satisfied the minimum requirements for teaching. Your employer requires you to take an additional college course each year to keep your teaching job. You take a course and pay for it yourself. This is qualifying education even if you eventually receive a master's degree and an increase in salary because of this extra education.

Education To Maintain or Improve Skills

If your education is not required by your employer or a law, it must maintain or improve skills needed in your work. Education to maintain or improve skills includes refresher courses, courses on current developments, and academic or vocational courses.

Example. You repair televisions, radios, and stereo systems for XYZ Store. To keep up with the latest changes, you take special courses in radio and stereo service. These courses maintain and improve skills required in your work.



If the courses you take are needed to meet the minimum educational requirements for your work or to qualify you for a new trade or business, they are not qualifying education.

Present work. Education that relates to work you may enter in the future is not qualifying education. Education that prepares you for a future occupation includes any education that keeps you up-to-date for a return to work or that qualifies you to reenter a job you had in the past.

Temporary absence. If you stop work for a year or less and then go back to the same kind of work, your absence is ordinarily considered temporary. Education during a vacation, temporary leave, or other temporary absence from your job is considered related to your present job. However, after your temporary absence you must return to the same kind of work.

Example. You quit your biology research job to become a full-time biology graduate student for one year. If you return to work in biology research after completing the courses, the education is related to your present work. You may even choose to take a similar job with another employer.

Nonqualifying Education

You cannot deduct the costs of nonqualifying education, even if it meets one of the two tests described earlier for qualifying education. Nonqualifying education is education that:

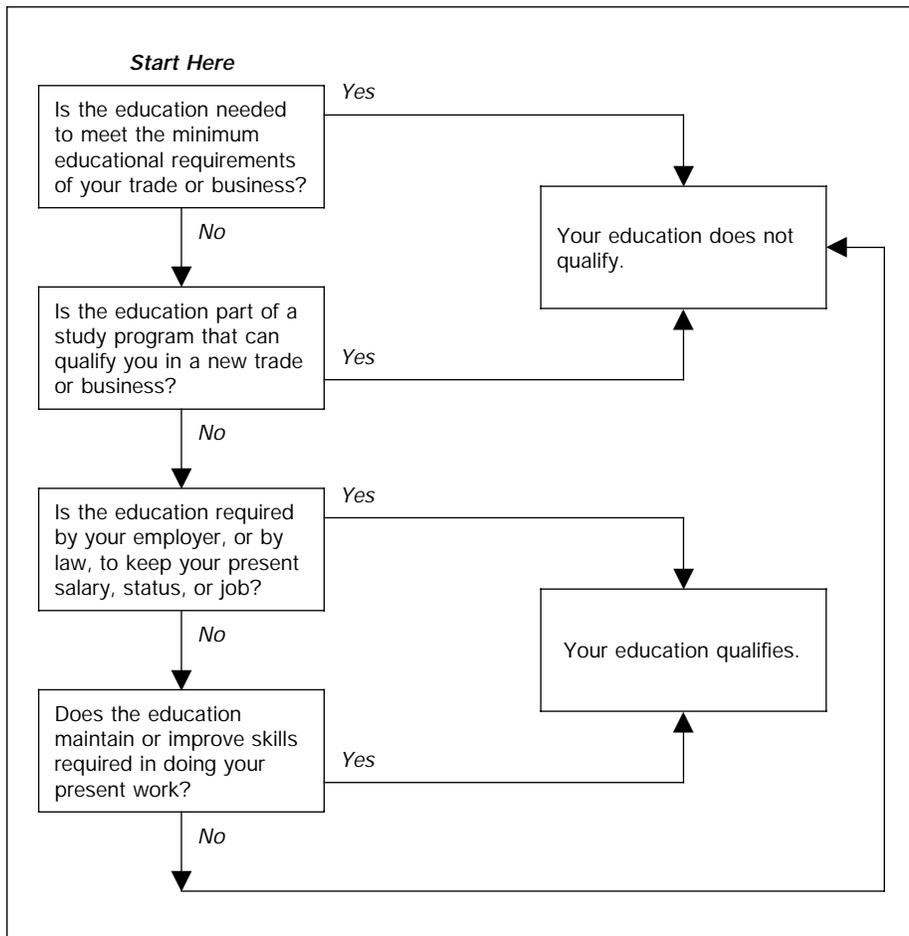
- 1) Is needed to meet the minimum educational requirements of your present trade or business, or
- 2) Is part of a program of study that can qualify you for a new trade or business.

Education To Meet Minimum Requirements

Education needed to meet the minimum educational requirements for your present trade or business is nonqualifying education. The minimum education necessary is determined by:

- 1) Laws and regulations,
- 2) Standards of your profession, trade, or business, and
- 3) Your employer's requirements.

Figure A. Does Your Education Qualify?



Once you have met the minimum educational requirements that were in effect when you were hired, you do not have to meet minimum educational requirements again. This means that if the minimum requirements change after you were hired, any education you need to meet the new requirements is qualifying education.



You have not necessarily met the minimum educational requirements of your trade or business simply because you are already doing the work.

Example 1. You are a full-time engineering student. You work part time as an engineer for a firm that will employ you after you finish college as a full-time engineer. Although your college engineering courses improve your skills in your present job, you have not met the minimum job requirements for a full-time engineer. The education is nonqualifying education.

Example 2. You are an accountant and you have met the minimum educational requirements of your employer. Your employer later changes the minimum educational requirements and requires you to take college courses to keep your job. These additional courses are not minimum requirements because you have already satisfied the initial minimum requirements. The education is qualifying education.

However, a new accountant coming into the firm has to satisfy the new minimum requirements. The education the new accountant needs to meet the new minimum requirements would be nonqualifying education.

Requirements for Teachers

This discussion applies to teachers and others employed by educational organizations. The state or school district usually sets the minimum educational requirements for teachers. It is the minimum number of college hours or college degree usually required of a person hired for that position.

If no requirements exist, you will have met the minimum educational requirements when you become a faculty member. You generally will be considered a faculty member when one or more of the following occurs.

- 1) You have tenure.
- 2) Your years of service count toward obtaining tenure.
- 3) You have a vote in faculty decisions.
- 4) Your school makes contributions for you to a retirement plan other than social security or a similar program.

Example 1. Your state law requires beginning secondary school teachers to have a bachelor's degree, including ten professional education courses. In addition, to keep the job, a teacher must complete a fifth year of training within 10 years from the date of hire. If the employing school certifies to the state Department of Education that qualified teachers cannot be found, the school may hire persons with only 3 years of college. However, to keep their job, these teachers must get a bachelor's degree and the required professional education courses within 3 years.

Under these facts, the bachelor's degree, whether or not it includes the ten professional education courses, is considered the minimum educational requirement for qualification as a teacher in your state.

If you have all the required education except the fifth year, you have met the minimum educational requirements. The fifth year of training is qualifying education unless it is part of a program of study that will qualify you for a new trade or business.

Example 2. Assume the same facts as in *Example 1* except that you have a bachelor's degree and only six professional education courses. The additional four education courses are qualifying education. Although you do not have all the required courses, you have already met the minimum educational requirements.

Example 3. Assume the same facts as in *Example 1* except that you are hired with only 3 years of college. The courses you take that lead to a bachelor's degree (including those in education) are qualifying education. They are needed to meet the minimum educational requirements for employment as a teacher.

Example 4. You have a bachelor's degree and you work as a temporary instructor at a university. At the same time, you take graduate courses toward an advanced degree. The rules of the university state that you may become a faculty member only if you get a graduate degree. Also, you may keep your job as an instructor only as long as you show satisfactory progress toward getting this degree. You have not met the minimum educational requirements to qualify you as a faculty member. The graduate courses are nonqualifying education.

Certification in a new state. Once you have met the minimum educational requirements for teachers for your state, you are considered to have met the minimum educational requirements in a new state. This is true even if you must get additional education to be certified in the new state. Any additional education you need is qualifying education.

Example. You hold a permanent teaching certificate in State A and are employed as a teacher in that state for several years. You move to State B and are promptly hired as a teacher. You are required, however, to complete certain prescribed courses to get a permanent teaching certificate in State B. These additional courses are qualifying education because the teaching position in State B involves the same general kind of work for which you were qualified in State A. You have already met the minimum requirements for teaching and have not entered a new trade or business.

Education That Qualifies You for a New Trade or Business

Education that is part of a program of study that can qualify you for a new trade or business is nonqualifying education. This is true even if you do not plan to enter that trade or business.

If you are an employee, a change of duties is not a new trade or business if the new du-

ties involve the same general kind of work you did in your old job.

Example 1. You are an accountant. Your employer requires you to get a law degree at your own expense. You register at a law school for the regular curriculum that leads to a law degree. Even if you do not intend to become a lawyer, the education is nonqualifying because the law degree will qualify you for a new trade or business.

Example 2. You are a general practitioner of medicine. You take a 2-week course to review developments in several specialized fields of medicine. The course does not qualify you for a new profession. It is qualifying education because it maintains or improves skills required in your present profession.

Example 3. While working in the private practice of psychiatry, you enter a program to study and train at an accredited psychoanalytic institute. The program will lead to qualifying you to practice psychoanalysis. The psychoanalytic training does not qualify you for a new profession. It is qualifying education because it maintains or improves skills required in your present profession.

Bar or CPA Review Course

Review courses to prepare for the bar examination or the certified public accountant (CPA) examination are nonqualifying education. These are personal expenses that qualify you for a new profession.

Qualifications for Teachers

All teaching and related duties are considered the same general kind of work. A change in duties in any of the following ways is not considered a change to a new business.

- 1) Elementary school teacher to secondary school teacher.
- 2) Teacher of one subject, such as biology, to teacher of another subject, such as art.
- 3) Classroom teacher to guidance counselor.
- 4) Classroom teacher to school administrator.

What Educational Expenses Are Deductible?

If your education meets the requirements described earlier under *Qualifying Education*, you can generally deduct your educational expenses. If you are not self-employed, you must itemize your deductions. However, see *Expenses Relating to Tax-Exempt and Excluded Income*, later.

Deductible expenses. The following educational expenses can be deducted.

- 1) Tuition, books, supplies, lab fees, and similar items.
- 2) Certain transportation and travel costs.

- 3) Other educational expenses, such as costs of research and typing when writing a paper as part of an educational program.

Nondeductible expenses. Educational expenses do not include personal or capital expenses. For example, you cannot deduct the dollar value of vacation time or annual leave you take to attend classes. This amount is a personal expense.

Unclaimed reimbursement. If you do not claim reimbursement that you are entitled to receive from your employer, you cannot deduct the expenses that apply to the reimbursement.

Example. Your employer agrees to pay your educational expenses if you file a voucher showing your expenses. You do not file a voucher, and you do not get reimbursed. Because you did not file a voucher, you cannot deduct the expenses on your tax return.

Transportation Expenses

If your education qualifies, you can deduct local transportation costs of going directly from work to school. If you are regularly employed and go to school on a **temporary basis**, you can also deduct the costs of returning from school to home.

If your attendance at school is realistically expected to last (and does in fact last) for one year or less, you go to school on a temporary basis unless there are facts and circumstances that would indicate otherwise. If your attendance at school is realistically expected to last for more than 1 year or if there is no realistic expectation that the attendance will last for 1 year or less, the attendance is not temporary, regardless of whether it actually lasts for more than 1 year. If attendance at school initially is realistically expected to last for one year or less, but at some later date the attendance is realistically expected to last more than 1 year, that attendance will be treated as temporary (unless there are facts and circumstances that would indicate otherwise) until your expectation changes. It will not be treated as temporary after the date you determine it will last more than 1 year.



The above explanation of attendance on a temporary basis is the result of a recent change. Under the former definition, "temporary" meant an irregular or short-term basis (generally a matter of days or weeks).



You can file an amended return on Form 1040X, Amended U.S. Individual Income Tax Return, for any year that is affected by this change. However, you generally must file the amendment within three years from the time you filed the return or within two years from the time you paid the tax, whichever is later.

If you are regularly employed and go directly from home to school on a temporary basis, you can deduct the round-trip costs of transportation in going from your home to school to home. This is true regardless of the location of the school, the distance traveled, or whether you attend school on nonwork days.

Transportation expenses include the actual costs of bus, subway, cab, or other fares, as well as the costs of using your car. Transportation expenses do not include

amounts spent for travel, meals, or lodging while you are away from home overnight.

Example 1. You regularly work in Camden, New Jersey, and go directly from work to home. You also attend school every night for 3 weeks to take a course that improves your job skills. Since you are attending school on a temporary basis, you can deduct your daily round-trip transportation expenses in going between home and school. This is true regardless of the distance traveled.

Example 2. Assume the same facts as in *Example 1* except that on certain nights you go directly from work to school and then home. You can deduct your transportation expenses from your regular work site to school and then home.

Example 3. Assume the same facts as in *Example 1* except that you attend the school for six consecutive Saturdays, non-work days. Since you are attending school on a temporary basis, you can deduct your round-trip transportation expenses in going between home and school.

Example 4. Assume the same facts as in *Example 1* except that you attend classes twice a week for 15 months. Since your attendance in school is not considered temporary, you cannot deduct your transportation expenses in going between home and school. If you go directly from work to school, you can deduct the one-way transportation expenses of going from work to school. If you go from work to home to school and return home, your transportation expenses cannot be more than if you had gone directly from work to school.

Using your car. If you use your car (whether you own or lease it) for transportation to school, you can deduct your actual expenses or use the standard mileage rate to figure the amount you can deduct. The standard mileage rate for 1998 is 32½ cents per mile. Whichever method you use, you may also deduct parking fees and tolls. See Publication 463 for information on deducting your actual expenses of using a car.

Travel Expenses

You can deduct expenses for travel, meals (subject to the 50% limit), and lodging if:

- 1) You travel overnight to obtain qualified education, and
- 2) The main purpose of the trip is to attend a work-related course or seminar.

Travel expenses for qualifying education are treated the same as travel expenses for other employee business purposes. For more information, see Publication 463.



You cannot deduct expenses for personal activities, such as sightseeing, visiting, or entertaining.

Mainly personal travel. If your travel away from home is mainly personal, you cannot deduct all of your expenses for travel, meals, and lodging. You can deduct only your expenses for lodging and 50% of your expenses for meals during the time you attend the qualified educational activities.

Whether a trip's purpose is mainly personal or educational depends upon the facts and circumstances. An important factor is the comparison of time spent on personal activ-

ities with time spent on educational activities. If you spend more time on personal activities, the trip is considered mainly educational only if you can show a substantial nonpersonal reason for traveling to a particular location.

Example 1. John works in Newark, New Jersey. He traveled to Chicago to take a deductible one-week course at the request of his employer. While there, he took a sightseeing trip, entertained some friends, and took a side trip to Pleasantville for a day. Since the trip was mainly for business, he can deduct his round-trip airfare to Chicago, but he cannot deduct his transportation expenses of going to Pleasantville. He can deduct only the meals (subject to the 50% limit) and lodging connected with his educational activities.

Example 2. Sue works in Boston. She went to a university in Michigan to take a qualifying course for work. She took one course, which is one-fourth of a full course load of study. She spent the rest of the time on personal activities. Her trip is mainly personal because three-fourths of her time is considered personal time and her reasons for taking the course in Michigan were all personal. She cannot deduct the cost of her round-trip train ticket to Michigan. She can deduct one-fourth of the meals (subject to the 50% limit) and lodging costs for the time she attended the university.

Example 3. Dave works in Nashville and recently traveled to California to take a deductible 2-week seminar. While there, he spent an extra 8 weeks on personal activities. The facts, including the extra 8-week stay, show that his main purpose was to take a vacation. He cannot deduct his round-trip airfare or his meals and lodging for the 8 weeks. He can deduct only his expenses for meals (subject to the 50% limit) and lodging for the 2 weeks he attended the seminar.

Cruises and conventions. Certain cruises and conventions offer seminars or courses as part of their itinerary. Even if these are work related, your deduction for travel may be limited. This applies to:

- 1) Travel by ocean liner, cruise ship, or other form of luxury water transportation, and
- 2) Conventions outside the North American area.

For a discussion of the limits on travel expense deductions that apply to cruises and conventions, see *Luxury Water Travel and Conventions* in Publication 463.

Meal Expenses

If your educational expenses qualify for deduction, you can deduct the cost of meals that qualify as travel expenses.

50% limit. You can deduct only 50% of your qualifying business-related meals if you were not reimbursed by your employer. This includes meals while traveling away from home to obtain your education.

Employees must use Form 2106 or 2106-EZ to apply the 50% limit. See the form instructions for information on how to figure the 50% limit.

Travel as Education

You cannot deduct the cost of travel that is a form of education, even if it is directly related to your duties in your work or business.

Example. You are a French language teacher. While on sabbatical leave granted for travel, you traveled through France to improve your knowledge of the French language. You chose your itinerary and most of your activities to improve your French language skills. You cannot deduct your travel expenses as educational expenses. This is true even if you spent most of your time learning French by visiting French schools and families, attending movies or plays, and engaging in similar activities.

Expenses Relating to Tax-Exempt and Excluded Income

Some educational assistance you receive may be tax-exempt or excluded income. This is income you receive that you are not required to report on your tax return.

The following discussions illustrate how to treat qualified educational expenses that are related to tax-exempt or excluded income from several sources: scholarships, veterans' educational assistance, and the Education Savings Bond Program.

Scholarships

If you receive a tax-exempt scholarship, you must subtract the amount of the scholarship from your qualified educational expenses.

Example. Your tuition for qualifying education is \$8,000. You receive a tax-exempt scholarship of \$6,000 to help pay the tuition. You can include only \$2,000 (\$8,000 – \$6,000) as qualified educational expenses.

Part of scholarship is tax exempt. If only part of your scholarship is tax exempt, you subtract only the tax-exempt part from your qualified educational expenses.

Example. Your tuition for qualifying education is \$8,000. You receive a \$6,000 scholarship of which \$4,000 is tax exempt and \$2,000 is taxable. You can include only \$4,000 (\$8,000 – \$4,000) as qualified educational expenses.

Part of tuition qualifies. If only part of your tuition is for qualifying education, you subtract only part of the tax-exempt scholarship from the qualified educational expenses.

Example. Your total tuition is \$8,000. The tuition for the courses that are qualifying education is \$3,200. Your tax-exempt scholarship is \$6,000. To determine the part of the scholarship that must be subtracted from the qualified educational expenses, multiply the scholarship (\$6,000) by a fraction. The top number of the fraction is the tuition for qualifying education, \$3,200, and the bottom number is the total tuition, \$8,000.

$$\$6,000 \times \frac{\$3,200}{\$8,000} = \$2,400$$

The result, \$2,400, is the amount of the scholarship you must subtract from your qualified educational expenses. You can include only \$800 (\$3,200 – \$2,400) as qualified educational expenses.

More information. For more information on scholarships, see Publication 520.

Veterans

Any educational assistance payment you receive from the Department of Veterans Affairs (VA) is tax exempt. This includes payments for living expenses.

VA programs that pay educational expenses only. If you receive payments under a VA program that pays only for educational expenses, such as tuition, books, and similar expenses, you must subtract the part of the VA payment that applies to qualifying education from your qualified educational expenses.

Example. Your tuition is \$1,000 and all classes are qualifying education. You receive a \$780 educational assistance payment from the VA that is solely for educational expenses. You can include only \$220 (\$1,000 – \$780) as qualified educational expenses.

VA programs that pay living expenses and educational expenses. If you receive payments under a VA program that pays for both living expenses and educational expenses, you must subtract from your qualified educational expenses only the part of the VA payment that applies to educational expenses for qualifying education.

Generally, 50% of the VA payments are for subsistence or living expenses. For married veterans, the percentage is higher.

Example. Your tuition is \$1,000 and all classes are qualifying education. You receive a \$780 educational assistance payment from the VA. Under this program, \$390 of the payment is for living expenses and \$390 is for educational expenses. You can include only \$610 (\$1,000 – \$390) as qualified educational expenses.

VA payments used for both qualifying and nonqualifying education. If you use a VA payment for educational expenses to pay for both qualifying and nonqualifying education, you must subtract only part of the payment from qualified educational expenses. To find out what part of the VA payment to subtract, multiply the VA payment by a fraction. The numerator (top number) is the cost of the qualifying education. The denominator (bottom number) is the total cost of your qualifying and nonqualifying education.

Example. Your tuition and fees for three courses are \$1,500. Only two of the three courses are qualifying education. The two courses cost \$1,000. You receive a \$780 educational assistance payment from the VA under a program that covers tuition and fees only. The payment does not include any amount for living expenses. Since two-thirds (\$1,000 ÷ \$1,500) of the total expenses are for qualifying education, subtract two-thirds of the VA payment ($\frac{2}{3} \times \$780 = \520) from the \$1,000 cost of the qualifying education. You can include \$480 (\$1,000 – \$520) as qualified educational expenses.

Education Savings Bond Program

You may be able to exclude from your gross income all or part of the interest you received on the redemption of qualified U.S. savings bonds if you pay qualified higher educational expenses during the same year. This exclu-

sion is known as the *Education Savings Bond Program*.

If you exclude interest under the Education Savings Bond Program, you must subtract the excluded interest from your qualified educational expenses.

See chapter 1 of Publication 550, *Investment Income and Expenses*, for more information on the Education Savings Bond Program.

How To Treat Reimbursements

How you treat any reimbursements you receive depends on the arrangement you have with your employer.

There are two basic types of reimbursement arrangements — **accountable plans** and **nonaccountable plans**. You can tell the type of plan you are reimbursed under by the way the reimbursement is reported on your Form W-2.

Accountable Plans

If you are reimbursed under an accountable plan, your employer should not include any reimbursement in your income in box 1 of your Form W-2. To be an accountable plan, your employer's reimbursement arrangement must require you to meet all three of the following rules.

- 1) Your expenses must have a business connection — that is, your expenses must be deductible under the rules for qualifying education explained earlier.
- 2) You must adequately account to your employer for your expenses within a reasonable period of time.
- 3) You must return any reimbursement or allowance in excess of the expenses accounted for within a reasonable period of time.

Any part of your reimbursement that does not meet all three rules is considered paid under a nonaccountable plan.

Expenses equal reimbursement. If your expenses equal your reimbursement, you do not complete Form 2106 or 2106-EZ. Because your expenses and reimbursements are equal, you do not have a deduction.

Excess expenses. If your expenses are more than your reimbursement, you can deduct your excess expenses. This is discussed later under *Where To Deduct Expenses*.

Allocating your reimbursements for meals. Because your excess meal expenses are subject to the 50% limit, you must figure them separately from your other expenses. If your employer paid you a single amount to cover both meals and other expenses, you must allocate the reimbursement so that you can figure your excess meal expenses separately. You make the allocation as follows:

- 1) Divide your meal expenses by your total expenses.
- 2) Multiply your total reimbursement by the result from (1). This is the allocated reimbursement for your meal expenses.

- 3) Subtract the amount figured in (2) from your total reimbursement. The difference is the allocated reimbursement for your other qualified educational expenses.

Example. Your employer paid you an expense allowance of \$2,000 under an accountable plan. The allowance was to cover all of your expenses of traveling away from home to take a 2-week training course for work. There was no indication of how much of the reimbursement was for each type of expense. Your actual expenses equal \$2,500 (\$425 for meals + \$700 lodging + \$150 transportation expenses + \$1,225 for books and tuition).

You must allocate the reimbursement between the \$425 meal expenses and the \$2,075 other expenses. The allocated reimbursement for meals is \$340 and the allocated reimbursement for other expenses is \$1,660, figured in the following steps.

- 1) You divide \$425 (your meal expenses) by \$2,500 (your total expenses). The result is .17.
- 2) You multiply \$2,000 (your reimbursement) by .17. The \$340 result is the allocated reimbursement for your meal expenses.
- 3) You subtract \$340 from \$2,000. The \$1,660 difference is the allocated reimbursement for your other qualified educational expenses.

Your excess meal expenses are \$85 (\$425 – \$340) and your excess other expenses are \$415 (\$2,075 – \$1,660). After you apply the 50% limit to your meals, you have an educational expense deduction of \$457.50 $[(\$85 \times 50\%) + \$415]$.

Nonaccountable Plans

Your employer will combine the amount of any reimbursement or other expense allowance paid to you under a nonaccountable plan with your wages, salary, or other pay and report the total in box 1 of your Form W-2.

You can deduct your expenses regardless of whether they are more than, less than, or equal to your reimbursement. This is discussed later under *Where To Deduct Expenses*. An illustrated example of a nonaccountable plan, using Form 2106-EZ, is shown at the end of this publication.

Reimbursements for nondeductible expenses. Reimbursements you received for nondeductible expenses are treated as paid under a nonaccountable plan. You must include them in your income. For example, you must include in your income reimbursements your employer gave you for expenses of education that:

- 1) You need to meet the minimum educational requirements for your job, or
- 2) Are part of a program of study that can qualify you for a new trade or business.

Where To Deduct Expenses

Self-employed persons and employees report their educational expenses differently.

The following information explains what forms you must use to deduct your qualified educational expenses.

Self-Employed Persons

If you are self-employed, you must report your qualified educational expenses on the appropriate form used to report your business income and expenses (Schedule C, C-EZ, or F). If your educational expenses include expenses for a car or truck, travel, or meals, report them the same way you report other business expenses for those items. See the instructions for the form you file for information on how to complete it.

Employees

If you are an employee, you can deduct qualified educational expenses only if they were not reimbursed by your employer or exceeded your reimbursement. (Amounts your employer paid under a nonaccountable plan and included in box 1 of your Form W-2 are not considered reimbursements.)

Include your qualified educational expenses with your deduction for any other employee business expenses on line 20 of Schedule A (Form 1040). (Special rules for expenses of certain performing artists and fee-basis officials and for impairment-related work expenses are explained later.) This deduction is subject to the 2%-of-adjusted-gross-income limit that applies to most miscellaneous itemized deductions.

Form 2106 or 2106-EZ. To figure your deduction for employee business expenses, including qualified educational expenses, you generally must complete Form 2106 or 2106-EZ.

Form not required. Do not complete either Form 2106 or 2106-EZ if:

- You were not reimbursed for any of your expenses, and
- You are not claiming travel, transportation, or meal expenses.

If you meet both of these requirements, enter the expenses directly on line 20 of Schedule A (Form 1040). (Special rules for expenses of certain performing artists and fee-basis officials and for impairment-related work expenses are explained later.)

Using Form 2106-EZ. This form is shorter and easier to use than Form 2106. Generally, you can use this form if:

- You were not reimbursed for any of your expenses, and
- You are using the standard mileage rate if you are claiming vehicle expenses.

If you do not meet both of these requirements, use Form 2106.

Performing artists and fee-basis officials.

If you are a qualified performing artist, or a state (or local) government official who is paid in whole or in part on a fee basis, you can deduct your qualified educational expenses as an adjustment to gross income rather than as an itemized deduction. Include your qualified educational expenses with any other employee business expenses on line 32 of Form 1040. You do not have to itemize your deductions on Schedule A (Form 1040), and the deduction is not subject to the 2%-of-adjusted-gross-income limit. You must complete Form 2106 or 2106-EZ to figure your deduction even if you meet the requirements described earlier under *Form not required*.

For more information on qualified performing artists, see Publication 463.

Impairment-related work expenses. If you are disabled and have impairment-related work expenses that enable you to get qualifying education, you can deduct them on line 27 of Schedule A (Form 1040). They are not subject to the 2%-of-adjusted-gross-income limit. To deduct these expenses, you must complete Form 2106 or 2106-EZ even if you meet the requirements described earlier under *Form not required*.

For more information on impairment-related work expenses, see Publication 463.

Employer-Provided Educational Assistance

Educational assistance benefits you receive from your employer under an educational assistance program are tax free, up to \$5,250 each year. This means your employer should not include the benefits with your wages, tips, and other compensation shown in box 1 of your Form W-2.

 **You must reduce your deductible educational expenses by the amount of any tax-free educational assistance benefits you received for those expenses.**

Educational assistance program. To qualify as an educational assistance program, the plan must be written and meet certain other requirements. Your employer can tell you whether there is a qualified program where you work.

Educational assistance. Tax-free educational assistance benefits include payments for tuition, fees and similar expenses, books, supplies, and equipment. The payments must be for undergraduate-level courses that begin before June 1, 2000. The payments do not have to be for work-related courses.

Educational assistance benefits do **not** include payments for the following items.

- 1) Meals, lodging, transportation, or tools or supplies (other than textbooks) that you can keep after completing the course of instruction.
- 2) Education involving sports, games, or hobbies unless the education has a reasonable relationship to the business of your employer, or is required as part of a degree program.
- 3) Graduate-level courses that began after June 30, 1996, and are normally taken under a program leading to a law, business, medical, or other advanced academic or professional degree.

Benefit over \$5,250. If your employer gives you more than \$5,250 of educational assistance benefits during the year, the amount over \$5,250 is generally taxable. Your employer should include the taxable amount in your wages (box 1 of your Form W-2).

However, if the payments also qualify as a working condition fringe benefit, your employer can exclude all of the payments from your wages. A working condition fringe benefit is a benefit which, had you paid for it, you could deduct as an employee business expense.

Refund Procedures

The \$5,250 annual exclusion for employer-provided educational assistance benefits previously expired for tax years beginning after 1994. Subsequently, the exclusion was reinstated retroactively and extended to benefits received for courses beginning before June 1, 2000. Therefore, you are entitled to a refund of any income, social security, and Medicare taxes you paid on excludable benefits for 1995, 1996, and 1997.

Income tax refund. You are entitled to an income tax refund for 1995 if excludable benefits were included with your wages on your Form W-2. To get your refund, you need a Form W-2c from your employer showing the corrected wages for 1995.

Claim your refund by filing Form 1040X, *Amended U.S. Individual Income Tax Return*, with the IRS. To speed up processing of the Form 1040X, print "IRC 127" in the top margin. If the correction of your wages is the only adjustment to the original return, enter only your name, address, social security number, and tax year on the Form 1040X. Then sign the form and attach your Form W-2c. The IRS will figure the refund based on the W-2c information provided.

 **If you exclude employer-provided educational assistance from your gross income, you cannot deduct educational expenses that were paid for by that assistance. If you claimed a deduction for educational expenses on your original return, you need to make an adjustment.**

 **If you made nondeductible contributions to your individual retirement arrangement (IRA) for 1995, your reduced adjusted gross income due to correction of your wages may allow you to treat the contributions as deductible. To do this, enter the corrected nondeductible amount on a Form 8606 and attach it to the Form 1040X.**

Social security and Medicare taxes refund. You are entitled to a refund of any social security and Medicare taxes withheld by your employer on excludable benefits in 1995, 1996, and 1997. Ask your employer to refund these taxes.

If you are not able to get a refund of these taxes from your employer, you can file Form 843, *Claim for Refund and Request for Abatement*, with the IRS. To speed up processing of the form, print "IRC 127" in the top margin. Attach a statement from your employer listing any taxes the employer refunded to you and any taxes the employer claimed as a refund, or was authorized by you to claim as a refund. If you cannot get this statement, you must make the same statement (to the best of your knowledge and belief) and explain why you could not get it from your employer.

Recordkeeping



You must keep records as proof of any deduction claimed on your tax return. Generally, you should keep your records for 3 years from the date of filing the tax return and claiming the deduction.

If you are an employee who is reimbursed for expenses and you give your records and documentation to your employer, you do not have to keep duplicate copies of this information. However, you should keep your records for a 3-year period if:

- 1) You claim deductions for expenses that are more than your reimbursement,
- 2) Your employer does not use adequate accounting procedures to verify expense accounts,
- 3) You are related to your employer, or
- 4) Your expenses are reimbursed under a nonaccountable plan.

Examples of records to keep. If any of the above cases apply to you, you must be able to prove that your expenses are deductible. You should keep adequate records or have sufficient evidence that will support your expenses. Estimates or approximations do not qualify as proof of an expense. Some examples of what can be used to help prove your expenses are:

- Documents such as transcripts, course descriptions, catalogs, etc., showing periods of enrollment in educational institutions, principal subjects studied, and descriptions of educational activity.
- Canceled checks and receipts to verify amounts you spent for tuition and books, meals and lodging while away from home overnight for educational purposes, travel and transportation, and other educational expenses.
- Statements from your employer explaining whether the education was necessary for you to keep your job, salary, or status; how the education helped maintain or improve skills needed in your job; how much educational expense reimbursement you received, identified by kind of expense; and the type of certificate and subjects taught, if you are a teacher.
- Complete information about any scholarship or fellowship grants, including amounts you received during the year.

Illustrated Example Using Form 2106-EZ

Victor Jones teaches math at a private high school in North Carolina. He was selected to attend a 3-week math seminar at a university in California. The seminar will improve his skills in his current job and is qualifying education. He was reimbursed for his expenses under his employer's nonaccountable plan, so his reimbursement of \$2,100 is included in the wages shown on his Form W-2. Victor will file Form 1040.

His actual expenses for the seminar are as follows:

Lodging	\$1,050
Meals	526
Airfare	550
Taxi fares	50
Tuition and books	<u>400</u>
Total Expenses	<u><u>\$2,576</u></u>

Because Victor's reimbursement was included in his income, he files Form 2106-EZ

with his tax return. He shows his expenses for the seminar in Part II of the form. He enters \$1,650 (\$1,050 + \$550 + \$50) on line 3 to account for his lodging, airfare, and taxi fares. He enters \$400 on line 4 for his tuition and books. On the line to the left of line 5, Victor enters \$526 for meal expenses. He multiplies that amount by 50% and enters the result,

\$263, on line 5. On line 6, Victor totals the amounts from lines 3 through 5. He carries the total, \$2,313, to line 20 of Schedule A (Form 1040).

Since he does not claim any vehicle expenses, Victor leaves Part III blank. His filled-in form is shown on the next page.

Unreimbursed Employee Business Expenses

Department of the Treasury
Internal Revenue Service

▶ Attach to Form 1040.

Your name <p style="text-align: center;">Victor Jones</p>	Social security number <p style="text-align: center;">123 : 00 : 4321</p>	Occupation in which you incurred expenses <p style="text-align: center;">Teaching</p>
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Part I General Information

You May Use This Form ONLY if All of the Following Apply:

- You are an employee deducting expenses attributable to your job.
- You **do not** get reimbursed by your employer for any expenses (amounts your employer included in box 1 of your Form W-2 are not considered reimbursements).
- If you are claiming vehicle expense,
 - a You are using the standard mileage rate for 1998, **and**
 - b If you owned the vehicle, you also used the standard mileage rate for the year you first placed your vehicle in service.

Part II Figure Your Expenses

1 Vehicle expense using the standard mileage rate. Complete Part III and multiply line 8a by 32½¢ (.325)	1		
2 Parking fees, tolls, and transportation, including train, bus, etc., that did not involve overnight travel or commuting to and from work	2		
3 Travel expense while away from home overnight, including lodging, airplane, car rental, etc. Do not include meals and entertainment	3	1,650	
4 Business expenses not included on lines 1 through 3. Do not include meals and entertainment	4	400	
5 Meals and entertainment expenses: \$ <u>526</u> x 50% (.50) (Employees subject to Department of Transportation (DOT) hours of service limits: Multiply meal expenses by 55% (.55) instead of 50%. For more details, see instructions.)	5	263	
6 Total expenses. Add lines 1 through 5. Enter here and on line 20 of Schedule A (Form 1040). (Fee-basis state or local government officials, qualified performing artists, and individuals with disabilities: See the instructions for special rules on where to enter this amount.)	6	2,313	

Part III Information on Your Vehicle. Complete this part ONLY if you are claiming vehicle expense on line 1.

- 7 When did you place your vehicle in service for business purposes? (month, day, year) ▶ / /
- 8 Of the total number of miles you drove your vehicle during 1998, enter the number of miles you used your vehicle for:
- a Business b Commuting c Other
- 9 Do you (or your spouse) have another vehicle available for personal use? Yes No
- 10 Was your vehicle available for use during off-duty hours? Yes No
- 11a Do you have evidence to support your deduction? Yes No
- b If "Yes," is the evidence written? Yes No

General Instructions

Section references are to the Internal Revenue Code.

Changes To Note

- The standard mileage rate has been increased to 32½ cents for each mile of business use in 1998.
- Beginning in 1998, you may use the standard mileage rate instead of actual expenses for leased vehicles, but you must use the rate for the entire lease period (except for the period, if any, that began before January 1, 1998).

• For tax years beginning in 1998, employees subject to Department of Transportation (DOT) hours of service limits are allowed to deduct 55% of their allowable business meal expenses. For more details, see the line 5 instructions.

Purpose of Form

You may use Form 2106-EZ instead of Form 2106 if you meet all the requirements listed in Part I of this form.

Recordkeeping

You cannot deduct expenses for travel (including meals unless you used the standard meal allowance), entertainment, gifts, or use of a car

or other listed property, unless you keep records to prove the time, place, business purpose, business relationship (for entertainment and gifts), and amounts of these expenses. Generally, you must also have receipts for all lodging expenses (regardless of the amount) and any other expense of \$75 or more.

Additional Information

If you need more information about employee business expenses, you will find the following publications helpful:

- Pub. 463**, Travel, Entertainment, Gift, and Car Expenses
- Pub. 529**, Miscellaneous Deductions

How To Get More Information

You can order free publications and forms, ask tax questions, and get more information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Free tax services. To find out what services are available, get Publication 910, *Guide to Free Tax Services*. It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

 **Personal computer.** With your personal computer and modem, you can access the IRS on the Internet at www.irs.ustreas.gov. While visiting our Web Site, you can select:

- *Frequently Asked Tax Questions* to find answers to questions you may have.
- *Fill-in Forms* to complete tax forms online.
- *Forms and Publications* to download forms and publications or search publications by topic or keyword.
- *Comments & Help* to e-mail us with comments about the site or with tax questions.
- *Digital Dispatch* and *IRS Local News Net* to receive our electronic newsletters on hot tax issues and news.

You can also reach us with your computer using any of the following.

- Telnet at iris.irs.ustreas.gov
- File Transfer Protocol at ftp.irs.ustreas.gov
- Direct dial (by modem) **703-321-8020**

 **TaxFax Service.** Using the phone attached to your fax machine, you can receive forms, instructions, and tax

information by calling **703-368-9694**. Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.



Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call **1-800-829-3676** to order current and prior year forms, instructions, and publications.
- *Asking tax questions.* Call the IRS with your tax questions at **1-800-829-1040**.
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **1-800-829-4059** to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call **1-800-829-4477** to listen to pre-recorded messages covering various tax topics.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we evaluate the quality of our telephone services in several ways.

- A second IRS representative sometimes monitors live telephone calls. That person only evaluates the IRS assistor and does not keep a record of any taxpayer's name or tax identification number.
- We sometimes record telephone calls to evaluate IRS assistors objectively. We hold these recordings no longer than one week and use them only to measure the quality of assistance.
- We value our customers' opinions. Throughout this year, we will be surveying our customers for their opinions on our service.



Walk-in. You can pick up certain forms, instructions, and publications at many post offices, libraries, and

IRS offices. Some libraries and IRS offices have an extensive collection of products available to print from a CD-ROM or photocopy from reproducible proofs.



Mail. You can send your order for forms, instructions, and publications to the Distribution Center nearest to you and receive a response 7 to 15 workdays after your request is received. Find the address that applies to your part of the country.

- **Western part of U.S.:**
Western Area Distribution Center
Rancho Cordova, CA 95743-0001
- **Central part of U.S.:**
Central Area Distribution Center
P.O. Box 8903
Bloomington, IL 61702-8903
- **Eastern part of U.S. and foreign addresses:**
Eastern Area Distribution Center
P.O. Box 85074
Richmond, VA 23261-5074



CD-ROM. You can order IRS Publication 1796, *Federal Tax Products on CD-ROM*, and obtain:

- Current tax forms, instructions, and publications.
- Prior-year tax forms, instructions, and publications.
- Popular tax forms which may be filled-in electronically, printed out for submission, and saved for recordkeeping.
- Internal Revenue Bulletins.

The CD-ROM can be purchased from National Technical Information Service (NTIS) for \$25.00 by calling 1-877-233-6767 or for \$18.00 on the Internet at www.irs.ustreas.gov/cdorders. The first release is available in mid-December and the final release is available in late January.

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Tax Publications for Individual Taxpayers

See *How To Get More Information* for a variety of ways to get publications, including by computer, phone, and mail.

General Guides

- 1 Your Rights as a Taxpayer
- 17 Your Federal Income Tax (For Individuals)
- 225 Farmer's Tax Guide
- 334 Tax Guide for Small Business
- 509 Tax Calendars for 1999
- 553 Highlights of 1998 Tax Changes
- 595 Tax Highlights for Commercial Fishermen
- 910 Guide to Free Tax Services

Specialized Publications

- 3 Armed Forces' Tax Guide
- 378 Fuel Tax Credits and Refunds
- 463 Travel, Entertainment, Gift, and Car Expenses
- 501 Exemptions, Standard Deduction, and Filing Information
- 502 Medical and Dental Expenses
- 503 Child and Dependent Care Expenses
- 504 Divorced or Separated Individuals
- 505 Tax Withholding and Estimated Tax
- 508 Educational Expenses
- 514 Foreign Tax Credit for Individuals
- 516 U.S. Government Civilian Employees Stationed Abroad
- 517 Social Security and Other Information for Members of the Clergy and Religious Workers
- 519 U.S. Tax Guide for Aliens
- 520 Scholarships and Fellowships
- 521 Moving Expenses
- 523 Selling Your Home
- 524 Credit for the Elderly or the Disabled
- 525 Taxable and Nontaxable Income
- 526 Charitable Contributions
- 527 Residential Rental Property
- 529 Miscellaneous Deductions

- 530 Tax Information for First-Time Homeowners
- 531 Reporting Tip Income
- 533 Self-Employment Tax
- 534 Depreciating Property Placed in Service Before 1987
- 537 Installment Sales
- 541 Partnerships
- 544 Sales and Other Dispositions of Assets
- 547 Casualties, Disasters, and Thefts (Business and Nonbusiness)
- 550 Investment Income and Expenses
- 551 Basis of Assets
- 552 Recordkeeping for Individuals
- 554 Older Americans' Tax Guide
- 555 Community Property
- 556 Examination of Returns, Appeal Rights, and Claims for Refund
- 559 Survivors, Executors, and Administrators
- 561 Determining the Value of Donated Property
- 564 Mutual Fund Distributions
- 570 Tax Guide for Individuals With Income From U.S. Possessions
- 575 Pension and Annuity Income
- 584 Nonbusiness Disaster, Casualty, and Theft Loss Workbook
- 587 Business Use of Your Home (Including Use by Day-Care Providers)
- 590 Individual Retirement Arrangements (IRAs) (Including Roth IRAs and Education IRAs)
- 593 Tax Highlights for U.S. Citizens and Residents Going Abroad
- 594 Understanding the Collection Process
- 596 Earned Income Credit
- 721 Tax Guide to U.S. Civil Service Retirement Benefits

- 901 U.S. Tax Treaties
- 907 Tax Highlights for Persons with Disabilities
- 908 Bankruptcy Tax Guide
- 911 Direct Sellers
- 915 Social Security and Equivalent Railroad Retirement Benefits
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- 926 Household Employer's Tax Guide
- 929 Tax Rules for Children and Dependents
- 936 Home Mortgage Interest Deduction
- 946 How To Depreciate Property
- 947 Practice Before the IRS and Power of Attorney
- 950 Introduction to Estate and Gift Taxes
- 967 IRS Will Figure Your Tax
- 968 Tax Benefits for Adoption
- 970 Tax Benefits for Higher Education
- 971 Innocent Spouse Relief
- 1542 Per Diem Rates
- 1544 Reporting Cash Payments of Over \$10,000
- 1546 The Problem Resolution Program of the Internal Revenue Service

Spanish Language Publications

- 1SP Derechos del Contribuyente
- 579SP Cómo Preparar la Declaración de Impuesto Federal
- 594SP Comprendiendo el Proceso de Cobro
- 596SP Crédito por Ingreso del Trabajo
- 850 English-Spanish Glossary of Words and Phrases Used in Publications Issued by the Internal Revenue Service
- 1544SP Informe de Pagos en Efectivo en Exceso de \$10,000 (Recibidos en una Ocupación o Negocio)

Commonly Used Tax Forms

See *How To Get More Information* for a variety of ways to get forms, including by computer, fax, phone, and mail. For fax orders only, use the catalog numbers when ordering.

Form Number and Title	Catalog Number	Form Number and Title	Catalog Number
1040 U.S. Individual Income Tax Return	11320	2106 Employee Business Expenses	11700
Sch A & B Itemized Deductions & Interest and Ordinary Dividends	11330	2106-EZ Unreimbursed Employee Business Expenses	20604
Sch C Profit or Loss From Business	11334	2210 Underpayment of Estimated Tax by Individuals, Estates and Trusts	11744
Sch C-EZ Net Profit From Business	14374	2441 Child and Dependent Care Expenses	11862
Sch D Capital Gains and Losses	11338	2848 Power of Attorney and Declaration of Representative	11980
Sch E Supplemental Income and Loss	11344	3903 Moving Expenses	12490
Sch EIC Earned Income Credit	11339	4562 Depreciation and Amortization	12906
Sch F Profit or Loss From Farming	11346	4868 Application for Automatic Extension of Time To File U.S. Individual Income Tax Return	13141
Sch H Household Employment Taxes	12187	4952 Investment Interest Expense Deduction	13177
Sch J Farm Income Averaging	25513	5329 Additional Taxes Attributable to IRAs, Other Qualified Retirement Plans, Annuities, Modified Endowment Contracts, and MSAs	13329
Sch R Credit for the Elderly or the Disabled	11359	6251 Alternative Minimum Tax—Individuals	13600
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1040A U.S. Individual Income Tax Return	11327	8582 Passive Activity Loss Limitations	63704
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Sch 2 Child and Dependent Care Expenses for Form 1040A Filers	10749	8812 Additional Child Tax Credit	10644
Sch 3 Credit for the Elderly or the Disabled for Form 1040A Filers	12064	8822 Change of Address	12081
1040EZ Income Tax Return for Single and Joint Filers With No Dependents	11329	8829 Expenses for Business Use of Your Home	13232
1040-ES Estimated Tax for Individuals	11340	8863 Education Credits	25379
1040X Amended U.S. Individual Income Tax Return	11360		