



2004 Massachusetts Resident Income Tax Form 1

Full-Year Residents Only
All Schedules and Instructions

TELEFILE
Telefile your return in an
8-minute call.
See the Telefile form inside to see if
you are eligible.



CALL OR CLICK. GET IT QUICK!

- Telefile Your Return
- E-File through Your Tax Preparer
- IRS "Free-File" Link on Our Website

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COMMONWEALTH OF MASSACHUSETTS
Department of Revenue

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E-File Today!

DOR
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www.mass.gov/dor

Completing Your Form 1

Please read this page carefully as it explains the correct method of completing your return.

Form 1 Massachusetts Resident Income Tax Return 2004

PRINT IN BLACK INK

FOR PRIVACY ACT NOTICE, SEE INSTRUCTIONS.

012345678
987654321

1. YOUR SOCIAL SECURITY NUMBER
2. SPOUSE'S SOCIAL SECURITY NUMBER

Note: Be sure to enter your Social Security number(s) above

MICHAEL MURRAY
PEGGY MURRAY
123 ANY STREET
ANYTOWN MA 02345

If name/address has changed since 2003, fill in oval: If taxpayer(s) is deceased, fill in appropriate oval(s) (see instr.): 1. 2.

State Election Campaign Fund (this contribution will not change your tax or reduce your refund) \$1 You \$1 Spouse, if filing jointly Total ▶ \$

1 Filing status: (select one only) Single Married filing joint return Married filing separate return. (Enter spouse's Soc. Sec. number in the appropriate space above.)

2 Exemptions: Fill in if noncustodial parent
a. Personal exemptions. If single or married filing separately, enter \$3,300. If head of household, enter \$5,100. If married filing jointly, enter \$6,600. ▶ a 6 6 0 0 0 0
b. Number of dependents. (Do not include yourself or your spouse.) Enter number ▶ 2 × \$1,000 b 2 0 0 0 0 0
c. Age 65 or over before 2005: You Spouse. Enter number ▶ × \$700 c
d. Blindness: You Spouse. Enter number ▶ × \$2,200 d
e. Other: 1. Medical/Dental ▶ From U.S. Schedule A, line 4 2. Adoption ▶ See instructions 1 + 2 = e
f. Total exemptions. Add items a, b, c, d and e. Enter here and on line 18. ▶ 2f 8 6 0 0 0 0

3 Wages, salaries, tips and other employee compensation (from all Forms W-2) ▶ 3 6 0 0 0 0 0 0

4 Taxable pensions and annuities (see instructions) ▶ 4

5 Mass. bank interest: a. ▶ 1 8 0 0 0 0 - b. exemption 2 0 0 0 0 0 = 5
Exemption: if married filing jointly, subtract \$200 from Total; otherwise subtract \$100 & enter result. Not less than "0."

6 Business/profession or farm income/loss (enclose Mass. or U.S. Sch. C or C-EZ or U.S. Sch. F) ▶ 6

7 Rental, royalty, REMIC, partnership, S corp., trust income/loss (enclose Massachusetts Sch. E) ▶ 7 X 4 5 0 0 0 0

8 a. Unemployment Compensation + b. Massachusetts state lottery winnings a + b = 8

9 Other income (alimony, taxable IRA/Keogh distr., winnings, fees) from Sch. X, line 5 (enclose Sch. X) ▶ 9
Not less than "0."

10 TOTAL 5.3% INCOME. Add lines 3 through 9. (Be sure to subtract any loss(es) in lines 6 or 7) 10 5 5 5 0 0 0 0

11 Amount paid to Social Security, Medicare, R.R., U.S. or Massachusetts retirement. Not more than \$2,000 per person. a. You ▶ 2 0 0 0 0 0 + b. Spouse ▶ 1 2 0 0 0 0 a + b = 11 3 2 0 0 0 0

12 Child under age 13, or disabled dependent/spouse care expenses (from worksheet in instructions) ▶ 12

13 Number of dependent member(s) of household under age 12, or dependents age 65 or over (not you or your spouse) as of 12/31/04, or disabled dependent(s) (only if single, head of household or married filing joint return and not claiming line 12). Not more than two: a. ▶ 2 × \$3,600 = 13 7 2 0 0 0 0

14 Rental deduction (rent paid in 2004): a. ▶ ÷ 2 = Not more than \$3,000 (\$1,500 if married filing separately) ▶ 14

15 Other deductions from Schedule Y, line 10 (enclose Schedule Y) ▶ 15

SIGN HERE: Under penalties of perjury, I declare that to the best of my knowledge and belief this return and enclosures are true, correct and complete.

Your signature: Michael Murray Date: 2 / 1 05
Spouse's signature (if filing jointly): Peggy Murray Date: 2 / 1 05
Print paid preparer's name: _____
Preparer's SSN or PTIN: _____
Paid preparer's phone: _____
Paid preparer's EIN: _____
May DOR discuss this return with the preparer? Yes No
I do not want my preparer to file my return electronically. Yes No

Name and Address

Use the preaddressed return in the front of the booklet we sent you. Print in black ink the Social Security number of each person filing the return in the space provided. If your address has changed, please make all changes on the preprinted form. If you did not receive a preaddressed booklet, print in **black ink** the full name and address. Enter names as they appear on your federal tax return.

Social Security Number

Be sure to enter the Social Security number of each person filing the return in the space provided.

Whole-Dollar Method

If using the whole-dollar method, be sure to fill in the appropriate oval. Then round off, to the nearest dollar, all amounts on the return and on any schedules. **Do not** use the whole-dollar method on worksheets that you use to reach amounts shown on your return.

\$1.00–\$1.49 =

\$1.50–\$1.99 =

Filling in the Ovals

Make sure all ovals applicable to your filing situation are filled in completely, as shown:

Filling in Dollar Amounts/Reporting Losses

When entering amounts on Form 1 and schedules, print your numbers in **black ink** as shown below. Be sure there is only one number per box. Numbers must be written completely within the boxes and should not touch them.

If you are reporting a loss in any line, mark over the "X" in the far left box for that line. Failure to do so will result in the loss being machine-read as a gain. Also, be sure to mark over the "X" boxes in the supporting schedules. **Do not** use parentheses or minus signs to indicate losses.

▶ If showing a loss, mark over X in box at left
X 1 2 3 4 5 6 7 8 9 0

When entering amounts, make sure to enter cents, even if using the whole dollar method, in the rightmost boxes. For example, \$1,000 should be entered as:

Mailing Checks and Enclosing Forms

Attach to Form 1, with a single staple only, your Form W-2 or 1099 withholding documents. If you are making a payment, complete Form PV, Payment Voucher. Form PV is attached to the back of the envelope found in this booklet. Be sure to use the appropriate "Payment Due" or "Refund Due" label on the envelope. Attach with a single staple your check or money order to the front of Form PV and enclose with your return. Do not staple supporting schedules to the Form 1 as this will delay the processing of your return.

Sign Your Return

After you have completed Form 1, sign your name at the bottom of page 1. Your spouse must also sign if this is a joint return. Write the date you signed the return. Form 1 is not considered a valid return unless it is signed. Original signatures are required or the return will not be accepted.

FILING TIP You may be able to lower your taxes by taking advantage of other deductions and/or other credits on Form 1. See lines 15 and 29 of Form 1 and Schedule Y and Schedule Z instructions for a complete list of other deductions and/or credits for which you may be eligible. Senior citizens, see line 39 and Schedule CB instructions for the Senior Circuit Breaker Credit.

See Schedule Y, line 9, Commuter Deduction

9 Commuter deduction (from worksheet in instructions) ▶ 9

You Can If You E-File!

What Is E-File?

E-File is filing your state personal income tax return electronically through one of three methods offered by the Massachusetts Department of Revenue (DOR). Last year, more than one million taxpayers electronically filed their state income tax returns in the Commonwealth. On average, they received their refunds in four days.

Telefile



Telefile allows eligible taxpayers to E-File by telephone. Millions of taxpayers have used Telefile, completing their calls in minutes. **It's free and available 24 hours a day, 7 days a week.** Call (617) 660-2004 or (413) 827-7100 to see if you qualify. The Telefile worksheet and instructions can be found in your Form 1 instruction booklet.

Paid Preparer



Millions of taxpayers have had their returns electronically filed through DOR-approved tax preparers. If your tax preparer does not offer E-File, ask him or her to give it a try!

Note: For tax years beginning on or after January 1, 2004, income tax return preparers who completed 200 or more original Massachusetts Forms 1 and 1-NR/PY, including those E-Filed, during the previous calendar year are required to use electronic means to file all personal income tax returns, unless the taxpayer specifically directs on the paper form that the filing be on paper.

If you prefer to file using paper, you must use a DOR-approved tax preparation software package that supports 2-Dimensional (2-D) barcodes. Visit www.mass.gov/dor for a list of approved preparers.

Be sure to use the proper address when mailing your 2-D barcoded return. **Refund/no tax due:** Massachusetts Department of Revenue, PO Box 7001, Boston, MA 02204-7001. **Payment:** Massachusetts Department of Revenue, PO Box 7002, Boston, MA 02204-7002.

Commercial Tax Preparation Software



You can also E-File using DOR-approved commercial tax filing websites or software products or you may be eligible to file your return electronically for free through the Massachusetts Free File Alliance. Visit www.mass.gov/dor for a complete listing of approved websites and products. If you prefer to file using a paper copy, you must use a product that incorporates 2-D barcodes into their software. This will expedite the processing of your return.

Be sure to use the proper address when mailing your 2-D barcoded return. **Refund/no tax due:** Massachusetts Department of Revenue, PO Box 7001, Boston, MA 02204-7001. **Payment:** Massachusetts Department of Revenue, PO Box 7002, Boston, MA 02204-7002.

Personal Identification Number (PIN)

If you received this booklet in the mail, be sure to retain the PIN printed on the back cover. You will need it to Telefile and to access the Department's telephone and Web-based systems that allow you to check the status of your refund and perform other actions. If you did not get this booklet in the mail and do not have a PIN, you will need the amount of your requested refund or tax due from your 2003 Massachusetts tax return to access these systems. If you are a first-time filer, you will still be able to access these systems without a PIN.

Why Should You E-File?

- ▶ **Less stress.** If you E-File you will not have to worry about math errors, missing schedules or other common mistakes which could delay your refund or cause other problems that take time to resolve. And E-File is safe. Plus, you will receive immediate confirmation that serves as proof you filed.
- ▶ **Fast refunds.** Whether you E-File in January or mid-April, you will receive your refund, on average, in four days. You also have the option of having your refund deposited directly into your bank account. (Some commercial tax preparation products may not offer direct deposit.)
- ▶ **Easy to use.** Whether you call or click to file your return, or have your preparer E-File for you, the E-File system walks you through it step by step, and does the calculations for you.
- ▶ **Convenient payment options.** If you have a tax due, you can file now and pay later (by April 15, 2005) through Web Services for Income at www.mass.gov/dor or by Electronic Funds Withdrawal, credit or check card. You can also file now and pay later using Form PV, Massachusetts Income Tax Payment Voucher (by April 15, 2005). Form PV is attached to the back of the envelope found in this booklet. If you choose to pay by check, be sure to include Form PV to ensure proper crediting of your account.

Filing Your Extension by Telephone or Via the Web

Certain taxpayers are required to file an automatic six-month extension of time to file Massachusetts income tax return by telephone or via DOR's website. This mandate is required for taxpayers who meet the following conditions:

- ▶ you owe no tax; or
- ▶ you are making a payment of \$5,000 or more. If there is a tax due with your extension, payment can be made through Electronic Funds Withdrawal

If you meet all the criteria above, you **must** file your extension by telephone or via the web. These options are also available to taxpayers not meeting the mandate conditions. Call (617) 660-2222 to file your extension by telephone or visit www.mass.gov/dor to file via the Web. If you do not have Form M-4868, complete the following worksheet before you call to determine whether or not you have a tax due.

| | |
|---|-------|
| 1. Enter amount from Form 1, line 31, plus any amount entered in line 33. | _____ |
| 2. Enter the total of Form 1, lines 35 through 39 | _____ |
| 3. Amount due. Subtract line 2 from line 1, not less than "0" | _____ |

Would You Like More Information?

For more information about E-File, visit DOR's website, www.mass.gov/dor or call (617) 887-MDOR, or toll-free in Massachusetts, 1-800-392-6089. DOR's website also offers visitors a searchable index of legal rulings; tax forms and publications; news releases; statistical data and related articles. In addition, our website provides timely information from our Local Services and Child Support Enforcement divisions.

4 Before You Begin

Form 1 Checklist

Use this checklist before mailing your return to help avoid any errors that may delay the processing of your return.

- Is your preprinted name and address correct?
- If you received a preaddressed Form 1 booklet in the mail, be sure to retain the four-digit Personal Identification Number (PIN) printed on the back cover. You may need it to use DOR's Web-based and/or Interactive Voice Response (IVR) applications, such as checking the status of your refund.
- Have you entered your Social Security number(s) on Form 1, even if you received a preaddressed booklet in the mail?
- Have you completed your Form 1 in black ink?
- Have you, and your spouse if married filing jointly, signed your return at the bottom of page 1 of Form 1?
- Are all ovals filled in as necessary?
- If using the whole-dollar method, have you filled in the correct oval?
- Have you printed all dollar amounts completely within the boxes?
- Have you marked an "X" in any form or schedule box that shows a loss?
- Is your Social Security number correct on your Form(s) W-2 or 1099? If incorrect, make the necessary changes on Form(s) W-2 or 1099.
- Have you attached with a single staple your Form(s) W-2 or 1099 to the return where indicated?
- If making a payment, have you attached with a single staple your check to the front of Form PV, Massachusetts Income Tax Payment Voucher, and enclosed (not stapled) Form PV with your return? Form PV is attached to the back of the envelope found in this booklet. Be sure to use the light blue mailing label when mailing your Form 1 with the Form PV.
- Are you filing an original copy of the form? Remember, photocopies of the forms and schedules are not acceptable.
- Visit www.mass.gov/dor to see the fill-in version of Form 1 and schedules. They are easier and quicker to process.
- See page 3 for the correct PO boxes if you are using a tax software product.

Major 2004 Tax Changes

Commuter Deduction

A deduction is allowed for certain amounts paid by an individual for tolls paid for through a Fast-Lane account or for weekly or monthly transit commuter passes for MBTA transit or commuter rail, not including amounts reimbursed or otherwise deductible. In the case of a single person or a married person filing a separate return or a head of household filing a separate return, this deduction applies only to the portion of such expended amount that exceeds \$150, and the total amount deducted cannot exceed \$750. In the case of a married couple filing a joint return, this deduction applies only to the portion of such amount expended by each individual that exceeds \$150, and the total amount deducted cannot exceed \$750 for each individual. See TIR 04-25.

Same-Sex Marriage

Beginning May 16, 2004, Massachusetts law permits same-sex couples to be married. See *Goodridge v. Department of Public Health*, 440 Mass. 309 (2003). Same-sex spouses will file as married persons, jointly or separately, for Massachusetts state income tax purposes. However, federal law does not recognize same-sex marriage, and same-sex spouses will remain individual filers for federal purposes. Same-sex spouses who file as head of household federally will generally not be eligible to file as head of household for Massachusetts purposes. The term "head of household" as used in Massachusetts derives from the federal definition, which generally allows the status only for unmarried persons.

Where elements of Massachusetts taxation derive from federal law, such as the definition of gross income, or state deductions that are based on a federal counterpart, same-sex spouses may need to perform special calculations to arrive at the proper Massachusetts tax figure. For more details, see TIR 04-17, Massachusetts Tax Issues Associated with Same-Sex Marriages.

Use Tax

Since 2002, the Massachusetts personal income tax return has had a line for consumers to report use tax on items that they may have purchased out of state or from Internet or mail order sellers who did not collect Massachusetts sales or use tax. Recent legislation permits taxpayers to use a schedule to self-report a "safe-harbor" amount of use tax based on their Massachusetts adjusted gross income. A taxpayer may pay this amount in lieu of the actual amount of use tax that would otherwise be due with respect to such purchases. Individual taxpayers electing to report use tax

under this method will not be assessed additional use tax on audit, even if the actual amount of use tax due would have been greater than the amount from the schedule. The amendment applies to purchases made on or after January 1, 2004.

The estimated liability applies only to purchases of any individual items each having a total sales price of less than \$1,000. For each taxable item purchased at a sales price of \$1,000 or greater, the actual use tax liability for each purchase must be added to the amount of the estimated liability. See line 33 instructions for more information.

Circuit Breaker Tax Credit Increased

A credit is allowed to an owner or tenant of residential property located in Massachusetts equal to the amount by which the real estate tax payment or the rent constituting real estate tax payment exceeds 10% of the taxpayer's total income, not to exceed \$820. The amount of the credit is subject to limitations based on the taxpayer's total income and the assessed value of the real estate, which must not exceed \$441,000. For tax year 2004, an eligible taxpayer's total income cannot exceed \$44,000 for a single individual who is not the head of a household, \$55,000 for a head of household, and \$66,000 for a husband and wife filing a joint return. In order to qualify for the credit, a taxpayer must be age 65 or older and must occupy the property as his or her principal residence.

The U.S. Internal Revenue Code as of January 1, 1998

Massachusetts generally adopts the federal treatment of items of income and the federal exclusions from gross income. In addition, certain deductions allowed for federal tax purposes are allowed for Massachusetts tax purposes. With certain exceptions, Massachusetts adopts the Internal Revenue Code (IRC) as amended and in effect on January 1, 1998. The exceptions, where Massachusetts adopts the current Internal Revenue Code, are listed below. TIR 02-18 explains recent Massachusetts legislation that adopts current Code for certain provisions of the personal income tax.

Federal Law Changes *not* Adopted by Massachusetts

Student Loan Interest Deductions

The Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107-16, expanded the benefits of the federal deduction at sec. 221 for certain student loan interest, but Massachusetts has not adopted the new federal changes. Massachusetts adopts the deduction allowed under the rules of IRC sec. 221, as in effect on January 1, 1998, for certain interest paid by the taxpayer for a qualified education loan for graduate or undergraduate education. The deduction is for interest paid on a qualified education loan during the first 60 months, not including any deferral or forbear-

ance period. For tax year 2004, the maximum deduction is \$2,500, with the allowable amount reduced for individuals with federal adjusted gross income over \$40,000 (\$60,000 if married filing jointly). See Schedule Y, line 5 instructions for more information.

However, in the case of interest payment on education debt for **undergraduate** education, a taxpayer may elect to take a more favorable Massachusetts deduction where the amount is not limited by the 1998 rules at sec. 221. For more information on the Massachusetts deduction, see Schedule Y, line 8.

Parking, T-Pass and Vanpool Fringe Benefits — IRC sec. 132(f)

The federal exclusion amounts for tax year 2004 are \$195 per month for employer-provided parking and \$100 per month for employer-provided vanpool and transit pass benefits combined. Massachusetts, however, follows the inflation adjustment formula allowed under the January 1, 1998 Code. The Massachusetts exclusion amounts for tax year 2004 are \$200 per month for employer-provided parking and \$75 per month for employer-provided vanpool and transit pass benefits combined. Furthermore, Massachusetts does not adopt the federal gross income exclusion for transit pass and employer-provided vanpool benefits if the employer offers the benefit as a reduction in salary and the employee chooses the benefit in lieu of salary. These differences will be reflected in the Form W-2 provided by your employer.

Federal “Bonus” Depreciation Law — IRC sec. 168(k)

The Massachusetts Legislature amended Massachusetts law in 2002 to decouple it from IRC sec. 168(k). Thus, Massachusetts does not adopt the special first-year depreciation allowance for certain property placed in service during the period beginning September 11, 2001 and ending December 31, 2004. The federal changes made in 2003 to IRC sec. 168(k) (Pub. L. 108-27), including extending the time period for acquisition of qualified property, increasing the depreciation allowance to 50% of the adjusted basis of the qualified property, and increasing the limitations on depreciation for luxury vehicles, are not, therefore, adopted in Massachusetts. For more information, see TIR 03-25, *Depreciable Business Assets; Modifications for Decoupling from Federal Bonus Depreciation*.

Federal Health Savings Accounts

As part of the Medicare Prescription Drug Improvement and Modernization Act of 2003 at Pub. L. 108-173, Congress enacted new IRC sec. 223 establishing Health Savings Accounts (HSAs). For federal income tax purposes, contributions to an HSA are excluded from gross income if made by an employer or deductible from gross income if made by an individual, the earnings in an HSA ac-

count accrue on a tax-free basis, and distributions from a HSA that are used to pay qualified medical expenses are excluded from gross income. Massachusetts has not adopted new IRC sec. 223 regarding HSAs. As a result of nonconformity with the federal law, Massachusetts does not allow the exclusion from gross income for employer contributions to an employee's HSA plan. Also, Massachusetts does not adopt the deduction for a contribution by an individual to an HSA. For Massachusetts purposes, earnings in an HSA are currently taxable. However, to the extent that the amount was previously taxed by Massachusetts, distributions from HSAs are not subject to tax.

Archer Medical Savings Account Deduction

Massachusetts adopts the federal Medical Savings Account (MSA) provisions under IRC sec. 220 as in effect on January 1, 1998. Due to differences between the Internal Revenue Code as amended and in effect as of January 1, 1998, and the current year, the Massachusetts deduction for an Archer MSA contribution is allowable only for contributions of individuals who were active MSA participants before January 1, 2001.

Servicemembers Civil Relief Act

The Soldiers' and Sailors' Civil Relief Act of 1940 prohibits states from taxing the military compensation of service members whose domicile is in another state. In 2003, Congress enacted the Servicemembers Civil Relief Act (Pub. L. 108-189) which prevents the use of a nonresident servicemember's military compensation to increase the state tax liability for other income of the nonresident servicemember or spouse. The Act provides a benefit for certain nonresident taxpayers. For Massachusetts purposes, the Act requires a modification to the calculation of eligibility for “no tax status” and the “limited income credit” in those instances where the servicemember or spouse file as a Massachusetts nonresident or part-year resident. For more information, see TIR 04-6.

Military Family Tax Relief Act of 2003

The Military Family Tax Relief Act of 2003 (Pub. L. 108-121) added several provisions to federal law that provide benefits to taxpayers who are currently serving in the military. Because Massachusetts adopts the Internal Revenue Code as of January 1, 1998, most of these provisions have not been incorporated into Massachusetts law, including provisions that deal with the increased exclusion of specified death gratuity payments, exclusion of amounts received under the Department of Defense Homeowners Assistance Program, and deductions for expenses of National Guard members. However, as explained below, Massachusetts adopts the current Code for IRC sec. 121, which governs the exclusion of gain up to \$250,000 (\$500,000 for married couples filing

jointly) on the sale of a principal residence if they resided in the home for two of the five years preceding the sale. Thus, Massachusetts adopts the provision of the Military Family Tax Relief Act that amends IRC sec. 121 whereby qualified military and Foreign Service personnel can suspend (for up to 10 years) the time transferred away from home on official extended duty for purposes of applying the five-year portion of the two-out-of-five-year rule.

Massachusetts Adopts the Current Internal Revenue Code for Certain Federal Tax Provisions

Section 179 Expensing. Massachusetts follows current rules under IRC sec. 179 for expensing depreciable assets. The amount of capital investment that a small business can expense under IRC sec. 179 has been increased to \$102,000 for tax year 2004. The phase-out threshold governing the amount of expensing allowed has increased to \$410,000 for this period. See TIR 03-25 for more information.

Other areas in which Massachusetts applies the current Internal Revenue Code consist of:

- ▶ Treatment of contributions and distributions of qualified retirement plans, sec. 401(k) plans, sec. 403(b) plans, sec. 457 plans, SEPs (simplified employee pensions) and SIMPLE IRAs;
- ▶ Self-employed health insurance deduction under sec. 162(l);
- ▶ Deduction of employer contributions to qualified plans and other retirement plans under IRC sec. 404 (unless an exception applies);
- ▶ Exclusion of distributions from qualified tuition plans under IRC sec. 529;
- ▶ Exclusion of certain income derived from Roth IRAs as defined in IRC sec. 408A and Education IRAs as defined in IRC sec. 530;
- ▶ Treatment of a rollover from a traditional IRA to a Roth IRA;
- ▶ Exclusion of gain from the sale of a principal residence provided by IRC sec. 121;
- ▶ Trade or business deductions under IRC sec. 62(a)(1) unless an exception applies; and
- ▶ The limitations provided by IRC secs. 274(m) and (n) for the deduction of certain travel and meals and entertainment expenses.

For the above items, Massachusetts automatically adopts all changes to the Internal Revenue Code, including changes made after January 1, 1998. For more information, see TIRs 98-8, 98-15 and 02-18.

Filing Threshold for Estimated Personal Income Tax

Under prior law, a taxpayer was required to file a declaration of estimated tax for the taxable year if they reasonably expected to receive income that is taxable from sources other than wages upon which taxes are withheld. No declaration was required if

the amount of estimated tax was \$200 or less. Recent legislation raises the threshold for the filing of individual estimated taxes from \$200 to \$400. Also, the Act amends the provision imposing an addition to tax for underpayment of estimated tax to reflect the increased threshold of \$400. These changes are effective for tax years beginning on or after January 1, 2005.

Privacy Act Notice

Under the authority of 42 U.S.C. sec. 405(c)(2)(C)(i), and M.G.L. c. 62C, sec. 5, the Department of Revenue has the right to require an individual to furnish his or her Social Security number on a state tax return. This information is mandatory. The Department of Revenue uses Social Security numbers for taxpayer identification to assist in processing and keeping track of returns and in determining and collecting the proper amount of tax due. Under M.G.L. c. 62C, sec. 40, the taxpayer's identifying number is required to process a refund of overpaid taxes. Although tax return information is generally confidential pursuant to M.G.L. c. 62C, sec. 21, the Department of Revenue may disclose return information to other taxing authorities and those entities specified in M.G.L. c. 62C, secs. 21, 22 or 23, and as otherwise authorized by law.

Common Form 1 Mistakes

An incomplete or incorrect return can delay the processing of your return. Listed below are a number of tips to help us process your return as quickly as possible.

Note: You should **not** staple any items, other than any required Form(s) W-2 or 1099, to Form 1. Any enclosures such as schedules, statements, Form PV, etc. should simply be placed in the envelope along with Form 1 when mailing.

▶ **Missing Social Security Number(s).** Be sure to enter your Social Security number(s) in the spaces provided, even if you received a pre-addressed booklet in the mail.

▶ **Incorrect Computation.** The Department corrects many returns each year due to errors in computation. Before mailing your return, check your arithmetic to make sure the computations are correct.

▶ **Filing Status.** Be sure to fill in the correct oval in line 1, Filing Status. This line is frequently overlooked.

▶ **Exemptions.** Be sure that you specify the number of exemptions you are claiming in line 2, items b, c and d. Enter the appropriate number(s) in the small white box(es).

▶ **Missing Withholding Statement(s).** Be sure the state copy of Form(s) W-2 (Wages), W-2G (Winnings) and any Form 1099 that show Massachusetts income tax withheld are attached with a single staple. These forms are frequently missing and must be obtained later from you in order to process the return.

▶ **Missing Supporting Schedules.** Be sure all required schedules are enclosed to support the information on your Form 1. These include Massachusetts Schedules X, Y, Z, B, C, C-2, D, E, and CB. We cannot process your return without these forms.

▶ **Government Employee Pension Contributions.** If you were a state, local or county employee and made contributions to a Massachusetts state or local pension plan, your total wages for state purposes will be different from the amount you report on your U.S. return. Report your total state wages from your Form(s) W-2 on Form 1. This is generally box 16 of Form W-2.

▶ **Earned Income Credit.** You must have your federal earned income credit amount from your U.S. return or as computed by the IRS if you wish to claim the Earned Income Credit on Form 1.

▶ **Missing Signatures.** Thousands of unsigned returns are received by the Department every year. These returns must be returned to the taxpayers for signatures. If a joint return is filed, both spouses must sign the return. Make sure signatures are on the correct lines. Remember to sign your return at the bottom of page 1 of Form 1.

▶ **Missing Form PV.** If you are making a payment, make certain you fill out Form PV, Massachusetts Income Tax Payment Voucher, and attach with a single staple your payment to the front of Form PV. Form PV is attached to the back of the envelope found in this booklet. Enclose Form PV with your return. Be sure to use the light blue mailing label when mailing your Form 1 with the Form PV. **Note:** Go to www.mass.gov/dor and click on Web Services for Income for online payment options.

Filing Your Massachusetts Return

If you were a legal resident of Massachusetts and your gross income was more than \$8,000 — whether received from sources inside or outside of Massachusetts — you are required to file a Massachusetts income tax return. If your gross income was \$8,000 or less, you do not need to file a return.

If you did not live in Massachusetts but received Massachusetts source income in excess of your personal exemption amount multiplied by the ratio of your Massachusetts income to your total income, you must file as a nonresident on the Nonresident/Part-Year Resident Income Tax Return, Form 1-NR/PY. Generally, this means you must file Form 1-NR/PY if you were a nonresident of Massachusetts and you received Massachusetts source income in excess of \$3,300 if single, \$5,100 if head of household or \$6,600 if married filing jointly.

If, during the taxable year, you either moved to Massachusetts or terminated your status as a Massachusetts resident to establish residency outside the state, and your gross income was more than \$8,000 — whether received from sources inside or outside of Massachusetts — you must file as a part-year resident on the Nonresident/Part-Year Resident Income Tax Return, Form 1-NR/PY.

What Is Gross Income?

Massachusetts gross income includes the following:

- ▶ all wages, salaries, tips, bonuses, fees and other compensation;
 - ▶ taxable pensions and annuities;
 - ▶ pension income from another state or political subdivision before any deduction;
 - ▶ taxable IRA/Keogh and Roth IRA distributions;
 - ▶ alimony;
 - ▶ income from a business, trade, profession, partnership, S corporation, trust or estate;
 - ▶ rental, royalty and REMIC income;
 - ▶ unemployment compensation;
 - ▶ taxable interest and dividends;
 - ▶ gambling winnings;
 - ▶ capital gains;
 - ▶ taxable portion of scholarships and fellowships;
- and

- ▶ any other income not specifically exempt.
- Massachusetts gross income also includes the following which are not subject to U.S. income tax:
- ▶ interest from obligations of states and their political subdivisions, other than Massachusetts and its political subdivisions; and
 - ▶ income earned by a resident from foreign employment.

Massachusetts gross income does not include:

- ▶ interest on obligations of the U.S. and U.S. territories;
- ▶ amounts received as U.S. Social Security, public welfare assistance, Veterans Administration disability payments, G.I. Bill education payments, worker's compensation, gifts, accident or life insurance payments, or certain payments received by Holocaust survivors; and
- ▶ compensation earned by members of the armed forces for service in a combat zone (excluded to the same extent as under federal law).

Am I a Resident, Nonresident, or Part-Year Resident?

There are three different categories of resident status under Massachusetts tax law:

- 1. You are a Full-Year Resident** if your legal residence (domicile) is in Massachusetts or if you maintain a permanent place of abode in Massachusetts and during the year spend more than 183 days, in the aggregate, in the state. If you fit this description you should file a Massachusetts Resident Income Tax Return, Form 1.
- 2. You are a Nonresident** if you were not a resident of Massachusetts but earned Massachusetts income (e.g., from a job in Massachusetts). You must report such income by filing a Massachusetts Nonresident/Part-Year Resident Income Tax Return, Form 1-NR/PY.
- 3. You are a Part-Year Resident** if you either moved into or moved out of Massachusetts during the taxable year. In this case, you must reduce certain income, deductions and exemptions based on the number of days you were a resident or on the amount of your income that is subject to Massachusetts tax. Part-year residents must file a Massachusetts Nonresident/Part-Year Resident Income Tax Return, Form 1-NR/PY.

If **both** categories 2 and 3 apply to you, you will have to **file both** as a nonresident and as a part-year resident. In these cases, you must file **one** Massachusetts Form 1-NR/PY and complete the Resident/Nonresident Worksheet, Schedule R/NR, to calculate the portion of income earned while a part-year resident and the portion of income earned while a nonresident. If you are required to **file as both** a part-year resident and a nonresident, be sure to fill in the oval below the address section of Form 1-NR/PY to indicate that you are completing Schedule R/NR and enclose Schedule R/NR with your return.

See TIR 95-7 for more information regarding resident status. For information on how to file as a part-year resident/nonresident, visit DOR's website at www.mass.gov/dor or call (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

Are Military Personnel Required to File?

If you enlisted in the service as a Massachusetts resident and have not established a new domicile (legal residence) elsewhere, and if your gross income is more than \$8,000, you are required to file a Massachusetts resident income tax return. This applies even though you may be stationed outside of Massachusetts. The terms "legal residence" and "domicile" are used to denote that place where you have your permanent home and to which, whenever you are absent, you have the intention of returning. Nonresident military personnel stationed in Massachusetts may be subject to Massachusetts taxes and should file Form 1-NR/PY if they earn income other than from military sources.

The following example illustrates circumstances under which military pay is or is not taxable in Massachusetts. No guidance is intended on the tax status of such pay under the laws of other states. Generally, when income is taxable in two jurisdictions, a credit for taxes paid to the other jurisdiction is allowed on the taxpayer's return in the state of his/her residence.

***Example:** Betsy enlisted in the Navy in Massachusetts, but moved with her husband, Eric, from Massachusetts to Delaware when she was stationed there. They did not change their domicile to Delaware. She received military income while her husband received income working as a reporter for a local newspaper.*

Betsy's income from the Navy, as well as her husband's income from the newspaper, are both subject to Massachusetts income tax since she enlisted in the Navy in Massachusetts and they did not become legal residents of Delaware. Betsy and her husband are, therefore, Massachusetts residents, and any income they receive, whether derived in Massachusetts or not, is included in their Massachusetts gross income.

What Are the Rules for Filing a Joint Return?

A joint Form 1 is not allowed if both spouses were not Massachusetts residents for the same portion of 2004.

If you are legally married, you have the option of filing either a joint return or a married filing separate return. Married taxpayers who file a joint return are allowed to claim the following exemptions, deductions and credits which married taxpayers filing separate returns may not claim:

- ▶ a deduction of \$3,600 (\$7,200 for two or more dependents) for a dependent member of household under age 12, or dependent age 65 or over as of December 31, 2004 (not you or your spouse) or a disabled dependent;

- ▶ No Tax Status if joint Massachusetts AGI was \$14,200 or less plus \$1,000 for each dependent;
- ▶ Limited Income Credit if joint Massachusetts AGI is between \$14,200 and \$24,850 plus \$1,750 for each dependent;
- ▶ excess unused exemptions against interest income (other than interest from Massachusetts banks), dividends or capital gain income; and
- ▶ a senior circuit breaker tax credit which allows senior citizens meeting certain eligibility criteria to claim a refundable credit on their state income taxes for the real estate taxes paid on the Massachusetts residential property they own or rent, and which they occupy as their principal residence. The credit is the amount by which the real estate tax payment exceeds 10% of their total income, but not more than \$820. The credit is refundable to the extent the credit exceeds the taxpayer's tax liability.

If your spouse died during 2004, you may still choose to file a joint return.

How Do I File a Decedent's Return?

A final income tax return must be filed for a taxpayer who died during the taxable year. It must be signed and filed by his/her executor, administrator or surviving spouse for the portion of the year before the taxpayer's death. Be sure to fill in oval 1 if the taxpayer who was listed first on last year's income tax return is deceased, or oval 2 if the taxpayer who was listed second on last year's income tax return is deceased. Also, enclose a statement with the refund claimant's name and Social Security number clearly printed.

A joint return may be filed by a surviving spouse. In the case of the death of both spouses, a final return must be filed by their legal representative.

Any income received for the decedent for the taxable year after the decedent's death, and for succeeding taxable years until the estate is completed, must be reported each year on Massachusetts Form 2, Massachusetts Fiduciary Income Tax Return. Form 2 is available online at www.mass.gov/dor.

If the decedent's return shows a refund due, and if the Probate Court has not appointed a legal representative and none is contemplated, a Massachusetts Form M-1310, Statement of Claimant to Refund Due on Behalf of Deceased Taxpayer, must be enclosed with the return so the refund check may be made payable to the proper person.

Should I Make Estimated Tax Payments in 2005?

Every resident or nonresident who expects to pay more than \$400 in Massachusetts income tax on income which is not covered by Massachusetts withholding must pay Massachusetts estimated taxes. See line 37 instructions for more information.

8 Line by Line Instructions

When to File Your Return

Your Massachusetts Form 1 is due on or before April 15, 2005.

How Do I File for an Extension?

To receive an extension of time to file, you must file an application for automatic six-month extension of time to file Massachusetts income tax return and pay the amount of tax you expect to owe on or before the due date for filing your Massachusetts income tax return. The filing and approval of this form will extend the due date for six months. An approved extension means only that you will not be assessed a late return penalty for filing your return after the due date. Interest is charged on any tax not paid by the original due date.

If you are applying for an extension, see page 3 for information about filing by telephone or via the Web.

Note: Your extension will not be valid if you fail to pay 80% of your total tax liability through withholding, estimated tax payments or with your extension. Form M-4868 is available at www.mass.gov/dor or by calling (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

Must I File on a Calendar Year Basis?

No. You may file on a fiscal year basis if you keep your books and records on that fiscal year basis and if you receive permission from the Commissioner of Revenue. If you file on a fiscal year basis, you must file on or before the fifteenth day of the fourth month after the end of your fiscal year. Taxpayers filing on a fiscal year basis must complete and file Form 13, Notice of Designation of Fiscal Year, available at www.mass.gov/dor or by calling (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

What Should I Do If I Make a Mistake or Leave Something Off My Return?

If, after filing your income tax return, you receive an additional tax statement or discover that an error was made, **do not submit a second tax return**. If corrections are necessary, go to www.mass.gov/dor and use DOR's online abatement application or file Form CA-6, Application for Abatement/Amended Return. Form CA-6 is available at www.mass.gov/dor, or you may have one mailed to you by calling (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

What If I am Unable to Pay?

If you are unable to pay the full amount of tax that you owe, you should pay as much of your tax liability as possible with this return. You will receive a bill from the Department for the remaining amount of tax due plus accrued interest and penalty charges. If the amount of that bill is less than \$5,000 and you still cannot pay it in full, you must apply formally to the Department for a small payment agreement in order to avoid collection activity. You can apply for a small payment agreement by visiting Web Services for Income at www.mass.gov/dor.

Note: Do not mail your request for a payment agreement with your tax return. Requests can also be made once a bill is received by calling the Department at (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089. Setting up a small payment agreement will allow you to make monthly payments within a set time period to meet your unpaid liability.

Name and Address

Use the preaddressed return in the front of the booklet we sent you if all of the preprinted information is correct. Be sure to enter your Social Security number(s) in the space(s) provided. If you received a preaddressed Form 1 booklet in the mail, be sure to retain the four-digit Personal Identification Number (PIN) printed on the back cover. You will need it to use DOR's Web-based and/or Interactive Voice Response (IVR) applications, such as checking the status of your refund. If your address has changed, please make all of the necessary changes on the preaddressed form. If you did not receive a preaddressed return, print the full name, address, and Social Security number of each person filing the return in the spaces provided. Enter names as they appear on your federal return.

Social Security Number(s)

Be sure to enter your Social Security number(s) on your return, even if you received a preprinted booklet in the mail. Also, enter your Social Security number on page 2 of Form 1 and on page 2 of Schedules B or C, if filed. Failure to show the correct Social Security number in the space provided will delay the processing of your return. If filing jointly, list your numbers in the order they appear on your federal return. Also, be sure your employer has listed the correct Social Security number on your Form W-2. If you are married, you must list your spouse's Social Security number even if you are filing a separate return.

In instances where you, or your spouse if filing jointly, are a nonresident alien, enter "NRANRANRA" as your Social Security number in the appropriate space; if you have applied for but not yet received a Social Security number, enter "APPAPPAPP."

Name/Address Change

If you legally changed your name or address in 2004, fill in the oval. If you changed your name, enclose a copy of your Social Security card or driver's license showing your new name. Failure to include this documentation could delay processing of your return. If you move after filing, be sure to leave a forwarding address with your local post office and file a Change of Address Form with the Massachusetts Department of Revenue. This form is available to be filed online at www.mass.gov/dor, or by calling (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

Deceased Taxpayer

Be sure to fill in the appropriate oval if a taxpayer died during the taxable year. For further information, refer to the section "How Do I File a Decedent's Return?"

Voluntary Contribution to State Election Campaign Fund

You, and your spouse if filing jointly, may voluntarily contribute \$1 each to the State Election Campaign Fund. The purpose of this fund is to provide limited public financing for campaigns of eligible candidates for statewide and elective office. This contribution will not change your tax or reduce your refund.

Note: Lines without specific instructions are considered to be self-explanatory.

Line 1. Filing Status

Note: More than one filing status may apply to you. If so, you may wish to figure your taxes based upon more than one filing status to see which status is to your benefit.

Single

Fill in the "Single" oval if you were single as of December 31, 2004. This status applies to you if at the close of the taxable year you fit into any of the following categories:

- ▶ you were unmarried;
- ▶ you were a widow or widower whose spouse died before 2004; or
- ▶ you were legally separated under a final judgment of the probate court.

Please note that you are not single if: (1) you have obtained a judgment of divorce which has not yet become final; (2) you have a temporary support order; or (3) you and your spouse simply choose to live apart.

Married Filing Joint Return

Fill in the "Married filing joint return" oval if you were legally married as of December 31, 2004. Both spouses are responsible for the accuracy of all information entered on a joint return and both must sign. A joint return is allowed even if only one

spouse had income or if one spouse died during 2004. For further information, refer to the section “What Are the Rules for Filing a Joint Return?”

Note: Same-sex spouses filing a Massachusetts joint return should combine their figures from their separate U.S. returns.

Married Filing Separate Return

Fill in the “**Married filing separate return**” oval if you were legally married as of December 31, 2004, and if you and your spouse are not filing a joint return. Be sure to enter your spouse’s Social Security number in the space provided.

Head of Household

Fill in the “**Head of household**” oval if you qualify to file this status federally. This status is for unmarried people who paid over half the cost of keeping up a home for a qualifying person, such as a child who lived with you or your dependent parent. Certain married people who lived apart from their spouse for the last six months of 2004 may also be able to use this status. See IRS Publication 501, Exemptions, Standard Deduction, and Filing Information, for more information.

Noncustodial Parent

Fill in this oval if you are a “**noncustodial parent.**” A noncustodial parent is defined as a person who has a minor child, but does not live with the child.

Note: If you are the biological parent of a child, but your parental rights have been terminated, you are not the noncustodial parent of that child.

Whole-Dollar Method

Rounding all amounts on your return will hasten processing of your return. If doing so, please fill in the appropriate oval. Then, round off, to the nearest dollar, all amounts on the return and on any enclosed schedule(s).

- ▶ For example, amounts between \$1.00 and \$1.49 should be entered as \$1.00 and amounts between \$1.50 and \$2.00 should be entered as \$2.00.
- ▶ Do not use the whole-dollar method in calculations on worksheets that you use to reach the amounts shown on your return.

Line 2. Exemptions

Line 2a: Personal Exemptions

Each taxpayer is entitled to claim a personal exemption. The amount of your personal exemption depends on your filing status as filled in line 1.

- ▶ If you are single or married filing a separate return, enter \$3,300 in line 2a.
- ▶ If filing as head of household, enter \$5,100 in line 2a.
- ▶ If married filing a joint return, enter \$6,600 in line 2a.

Line 2b: Number of Dependents

You may claim a \$1,000 exemption for each of your dependents if you claimed them on your U.S. return. Enter in the box in item b the number of dependents you listed on U.S. Form 1040, line 6c or U.S. Form 1040A, line 6c. Do not include yourself or your spouse. Then, multiply that total by \$1,000 and enter the total amount in line 2b.

Note: In a few cases, the number of dependents claimed for Massachusetts purposes and for U.S. purposes may differ. For U.S. tax purposes, a dependent exemption is not allowed for a person who would otherwise be a dependent but who files his/her own income tax return and claims a personal exemption. For Massachusetts tax purposes, you can claim a dependent exemption for such a person. If you claim such a dependent in Massachusetts, increase the number reported in item b from your U.S. return by the number of such additional dependents. Also, same-sex joint filers should combine the number of dependents from their federal returns to arrive at the number of Massachusetts dependents. See TIR 04-17 for more information.

Line 2c: Age 65 or Over Before 2005

You are allowed an additional \$700 exemption if you were age 65 or over before January 1, 2005. If your spouse was age 65 or over and you are filing a joint return, you may also claim a \$700 exemption for your spouse. Fill in the appropriate oval(s) and enter the total number of persons age 65 or over in the small box. Multiply that total by \$700 and enter the total in line 2c.

Line 2d: Blindness Exemption

You are allowed an additional \$2,200 exemption if you are legally blind. If your spouse is also legally blind and you are filing a joint return, you may also claim a \$2,200 exemption for your spouse. Fill in the appropriate oval(s) and enter the total number of blindness exemptions in the small box. Multiply that total by \$2,200 and enter the total in line 2d.

Legal Definition of Blindness

You are legally blind and qualify for the blindness exemption if your visual acuity with correction is 20/200 or less in the better eye, or if your peripheral field of vision has been contracted to a 10-degree radius or less, regardless of visual acuity.

Line 2e: Other: Medical/Dental Expenses and Adoption Agency Fee

You may claim an exemption for medical and dental expenses paid during 2004 only if you itemized these expenses on your U.S. Form 1040, Schedule A. If you are married filing a joint U.S. Form 1040, you must file a joint Massachusetts Form 1 to claim this exemption. Enter in line 2e, item 1 the amount reported on your U.S. Form

1040, Schedule A, line 4. **Note:** Same-sex joint filers should recalculate their U.S. Form 1040, Schedule A by combining allowable expenses as reported on U.S. Form 1040, Schedule A, line 1 and their adjusted gross incomes as reported on U.S. Form 1040, Schedule A, line 2 in calculating U.S. Form 1040, Schedule A, line 4.

If you paid adoption fees to a licensed adoption agency during 2004, you are eligible for an exemption of the total amount of the fees paid during the year. Fees paid during 2004 to an agency licensed to place children for adoption on account of the adoption process of a minor child regardless of whether an adoption actually took place during 2004 should also be included for this exemption. Enter this amount in line 2e, item 2.

Note: No deduction is allowed for any portion of expenses that are paid or reimbursed by an employer and excluded from gross income under IRC sec. 137.

Add items 1 and 2 and enter the total in line 2e.

Line 2f: Total Exemptions

Add items 2a through 2e and enter the total in line 2f. This amount should also be entered on line 18 of Form 1.

5.3% Income

Note: DOR and the IRS maintain an extensive exchange program, routinely sharing computer tapes and audit results. Discrepancies between income, deductions, and schedules reported federally and on this return, except those allowed under state law, will be identified and may result in a state audit or further investigation.

Line 3. Wages, Salaries, Tips and Other Employee Compensation

Report in line 3 total state wages and allocated tips from Form(s) W-2. Income earned by a Massachusetts resident in another state is subject to taxation in Massachusetts. Generally, your total wages and allocated tips will be the same amount reported on your U.S. 1040 or 1040A, line 7; or 1040EZ, line 1. Below are instances that require an adjustment to these amounts.

Massachusetts Legal Residents Working in a Foreign Country

Income earned by a Massachusetts resident in a foreign country is subject to taxation in Massachusetts. If you excluded part or all of the compensation earned in a foreign country on your U.S. return (under Section 911 of the U.S. IRC), you must include any such amount in line 3 for Massachusetts tax purposes.

State or Local Employees Contributing to Pension Plans

If you are a Massachusetts state, city, town or county employee and contributed to your pension plan, enter in line 3 the Massachusetts W-2 state wage amount. This is generally box 16 of Form W-2. This amount will be higher than the U.S. amount because your pension contributions are excluded from your income for U.S. tax purposes. Contributions up to \$2,000 per taxpayer may still be deducted in line 11.

Line 4. Taxable Pensions and Annuities

Income from most private pensions or annuity plans is taxable in Massachusetts. Certain government pensions, however, are exempt under Massachusetts law. In general, exempt pensions include contributory pensions from the U.S. Government or the Commonwealth of Massachusetts and its political subdivisions, and noncontributory military pensions. The following section describes some specific pensions which are exempt. If your pension is exempt, enter "0" in line 4 and note the source on the dotted line to the left.

If your pension is not exempt, you should generally enter in line 4 the taxable amount reported on your U.S. Form 1040, line 16b, or U.S. Form 1040A, line 12b. In some cases, however, Massachusetts law requires an adjustment to the federal amount. Distributions from annuity, stock bonus, pension, profit-sharing or deferred payment plans or contracts described in Sections 403(b) and 404 of the U.S. IRC must be adjusted to account for your contributions that have been previously taxed. Subtract from such income (as reported on your U.S. Form 1040, line 16a, or U.S. Form 1040A, line 12a) the amount of your contributions which was previously taxed by Massachusetts until the total of your taxed contributions is received. If your pension falls into this category, enter the adjusted amount in line 4. If you are receiving distributions from an IRA or Keogh plan, do not report the income here; instead, see the instructions for Schedule X, line 2.

Note: Massachusetts does not tax Social Security income; therefore, you should not report such income on Massachusetts Form 1.

What pensions are exempt?

- ▶ Pension income received from a contributory annuity, pension, endowment or retirement fund of the U.S. Government or the Commonwealth of Massachusetts and its political subdivisions.
- ▶ Pensions from other states or its political subdivisions which do not tax such income from Massachusetts or its political subdivisions may be eligible to be deducted from Massachusetts taxable income. This pension income, however, should be reported in line 4. Refer to Schedule Y, line 6 instructions to determine eligibility for this deduction.
- ▶ Noncontributory pension income or survivorship benefits received from the U.S. uniformed services (Army, Navy, Marine Corps, Air Force, Coast Guard, commissioned corps of the Public Health Service and National Oceanic and Atmospheric Administration) is exempt from taxation in Massachusetts.
- ▶ Massachusetts state court judges who were appointed on or after January 2, 1975 are participants in the Massachusetts contributory retirement system and their pensions are nontaxable. State court judges who were appointed prior to January 2, 1975 receive taxable noncontributory pensions.

If you retired under Chapter 32, Sections 56–60 of Massachusetts General Laws and are a veteran who began Massachusetts state service prior to July 1, 1939, all or part of your pension income may be subject to tax. If you elected to receive your proceeds from contributions in one lump-sum distribution, your original contributions to the retirement system are not taxable. Noncontributory pension income received after a lump-sum distribution is fully taxable and should be reported in line 4.

How do I report lump-sum distributions?

If you were an employee of the U.S., Massachusetts or one of its political subdivisions and left public employment prior to retirement, you are not required to report as income the lump-sum distribution.

Lump-sum distributions of qualified employee benefit plans in excess of the employee's contributions which were previously subject to Massachusetts tax (or not previously excluded from Massachusetts tax) must be reported in line 4. Generally, qualified rollovers are not taxable in Massachusetts to the extent they are not taxable on your U.S. return. Lump-sum distributions related to IRA/Keogh and Roth IRA distributions should be reported in line 9.

Rollover from a traditional IRA to a Roth IRA.

Taxpayers with \$100,000 or less in federal adjusted gross income are allowed to make partial or complete rollovers from existing IRAs to Roth IRAs. Any taxable portion of these rollovers included in federal gross income is also included in Massachusetts gross income, except for amounts previously subject to Massachusetts personal income tax. See Schedule X, line 2 instructions for further details.

Line 5. Interest from Massachusetts Banks

Enter in line 5a the total amount of interest received or credited to deposit accounts (term and time deposits, including certificates of deposit, savings accounts, savings shares, and NOW accounts) in Massachusetts banks. Then, enter your exemption amount in line 5b (if married filing jointly, enter \$200; otherwise, enter \$100). Subtract line 5b from 5a and enter the result in line 5, but not less than "0." **Note:** This exemption amount does not apply to your U.S. tax return.

Do **not** subtract interest forfeited or penalties charged to you for early savings withdrawal. You will be allowed to deduct these amounts on Schedule Y, line 2. All other interest, unless exempt, should be entered on Massachusetts Schedule B. Interest on an IRA/Keogh is not taxable until distributed.

Lines 6, 7 and 10. If showing a loss in lines 6, 7 or 10, be sure to mark over the "X" in the box to the left. Do not use parentheses or negative signs to indicate losses.

Line 6. Business/Profession or Farm Income or Loss

Enter in line 6 the amount of income or loss from a business or profession from Massachusetts Schedule C, line 31. You must enclose Massachusetts Schedule C with this return. Also, enclose a copy of your U.S. Schedule C or Schedule C-EZ if substituting U.S. Schedule C or C-EZ for Massachusetts Schedule C.

Note: You may substitute U.S. Schedule C or C-EZ for Massachusetts Schedule C if there are no differences between the amounts reported on U.S. Schedule C or C-EZ and amounts that would be reported on Massachusetts Schedule C. Be sure to write "No Massachusetts Differences" on the top of the U.S. Schedule C or C-EZ.

If you operate a farm as an individual or cooperative, enter the amount of income or loss from operating a farm from U.S. Schedule F, Profit or Loss from Farming, line 36. Enclose a copy of U.S. Schedule F. Complete a pro-forma U.S. Schedule F to report Massachusetts differences, such as bonus depreciation.

Line 7. Rental, Royalty, REMIC, Partnership, S Corporation, Trust Income or Loss

Enter in line 7 the total of: Massachusetts Schedule E, Part I, line 5; Part II, line 8; and Part III, line 11. Remember to subtract losses when calculating the total. You must enclose Massachusetts Schedule E. You must retain with your records documentation to substantiate any differences in amounts

entered on the Massachusetts and U.S. schedules. See Massachusetts Schedule E instructions for an explanation of possible differences.

Line 8a. Unemployment Compensation

If you received unemployment compensation, enter in line 8a the amount reported on U.S. Form 1040, line 19; 1040A, line 13; 1040EZ, line 3; or U.S. Telefile Tax Record, item D. If you elected voluntary withholding of Massachusetts state income taxes on your unemployment compensation, be sure to include the amount of Massachusetts state income tax withheld, as reported on Form 1099-G, on Form 1, line 35 and attach with a single staple, where indicated on the return, Form 1099-G.

Note: DOR routinely matches the amounts in line 8a with files from the Division of Unemployment Assistance.

Line 8b. Massachusetts State Lottery Winnings

Enter in line 8b all winnings from the Massachusetts state lottery. Do not enter less than "0." You may only deduct the price of your winning ticket. Lottery losses claimed as itemized deductions on U.S. Form 1040, Schedule A are not allowed on your Massachusetts return.

Note: DOR routinely matches the amounts in line 8b with files from the Lottery Commission.

Add lines 8a and 8b and enter the result in line 8.

Line 9. Other Income (from Schedule X)

Alimony Received, Taxable IRA/Keogh and Roth IRA Conversion Distributions, Other Gambling Winnings, Fees and Other 5.3% Income

"Other 5.3% income" includes the items listed above and must be included on Schedule X. Enter the total from Schedule X, line 5. Not less than "0." Be sure to enclose Schedule X with your return. Failure to enclose this schedule will delay the processing of your return.

Deductions

Lines 11 through 15

Massachusetts allowable deductions differ from "Itemized Deductions" on Schedule A of U.S. Form 1040. You may claim only the deductions specified on Massachusetts Form 1, lines 11 through 14 and Schedule Y.

Please read the instructions for lines 12 and 13 to determine which deduction you qualify for or which is better for you. You cannot claim a deduction in both lines 12 and 13.

You are not allowed to deduct amounts unless they are directly related to income that is subject to taxation and reported on Massachusetts Form 1.

Line 11. Amount Paid to Social Security (FICA), Medicare, Railroad, U.S. or Massachusetts Retirement Systems

If you have paid into any of the retirement systems listed above during 2004, you may deduct those contributions, up to a maximum of \$2,000.

Enter in lines 11a and 11b the amount you, and your spouse if filing jointly, paid to Social Security (FICA), Medicare or Railroad Retirement and the U.S. or Massachusetts retirement systems during 2004 as shown on your Form W-2, but not more than \$2,000 each. Payment amounts may not be combined or transferred from one spouse to the other. Add lines 11a and 11b and enter the result in line 11. Be sure to add any amount of Medicare tax withheld as shown on Form W-2 to the amount of Social Security tax withheld, the total not to exceed \$2,000 per person.

Note: Medicare premiums deducted from your Social Security or retirement payments are **not** deductible.

Payments to an IRA, Keogh, Simplified Employee Pension Plan (SEP), or Savings Incentive Match Plan for Employees (SIMPLE) Account are not deductible for Massachusetts income tax purposes.

Line 12. Child Under Age 13, or Disabled Dependent/Spouse Care Expenses

Massachusetts now allows taxpayers to exceed the federal limit on employment-related expenses for the care of a qualified child under the age of 13, a disabled dependent or a disabled spouse. The maximum deduction is \$4,800 for one qualifying individual, and \$9,600 for two or more qualifying individuals. Complete the following worksheet to calculate your Massachusetts child or disabled dependent/spouse care expense deduction. **Note:** You cannot claim this deduction if married filing a separate return.

Taxpayers who received dependent care benefits should complete a pro forma U.S. Form 2441 or U.S. Form 1040A, Schedule 2. When completing this pro forma form, taxpayers should enter \$4,800 (or \$9,600 for two or more qualifying persons) in line 28 of U.S. Form 2441 or line 22 of U.S. Form 1040A, Schedule 2. The amount from this pro forma Form 2441, line 32 or U.S. Form 1040A, Schedule 2, line 26 should then be entered in line 1 of the following worksheet.

Note: Same-sex joint filers should complete a pro forma U.S. Form 2441 or U.S. Form 1040A, Schedule 2. In addition to changing the maximum amount of the deduction allowed on U.S. Form 2441 or U.S. Form 1040A, Schedule 2 (see preceding paragraph), same-sex spouses should prepare the pro forma federal forms as though they were filing a joint federal return. See TIR 04-17 for more information.

Line 12 Worksheet — Child Under 13 or Disabled Dependent/Spouse Care Deduction

Use the following worksheet to calculate your Massachusetts child under age 13 or disabled dependent/spouse care deduction.

1. Enter the amount of qualified expenses you incurred and paid in 2004 for a qualifying person(s). This amount may exceed the federal limit of \$3,000 for one qualifying person or \$6,000 for two or more persons. However, do not enter more than \$4,800 for one qualifying person or \$9,600 for two or more persons _____
2. Enter the amount from U.S. Form 2441, line 4, or U.S. Form 1040A, Schedule 2, line 4 _____
3. Enter the amount from U.S. Form 2441, line 5, or U.S. Form 1040A, Schedule 2, line 5 _____
4. Enter the smallest of line 1, 2 or 3 _____
5. If you paid 2003 expenses in 2004, enter the amount of the allowed 2003 expenses used to compute the credit on U.S. Form 2441, line 9, or U.S. Form 1040A, Schedule 2, line 9. Otherwise, enter "0" _____
6. Add lines 4 and 5. Enter here and in Form 1, line 12 _____

Note: If you choose to take a deduction in line 12, you cannot take the deduction in line 13.

Line 13. Dependent Member(s) of Household Under Age 12, or Dependents Age 65 or Over (not you or your spouse) as of December 31, 2004, or Disabled Dependent

You may deduct \$3,600 for a dependent member of household, or \$7,200 for two or more dependents, under age 12, or dependent age 65 or over (not you or your spouse) as of December 31, 2004, or disabled dependent. Enter the number of qualified dependents in line 13a, not to exceed two, and multiply that amount by \$3,600. Enter the result in line 13. Only if single, head of household or married filing jointly. You cannot claim this deduction if married filing a separate return.

Note: You may claim an amount in line 13 only if there is no entry in line 12.

Line 14. 50% Rental Deduction

You may be entitled to a rental deduction equal to one-half (50%) of the rent you paid during 2004 (up to a maximum of \$3,000 per return) for your principal residence in Massachusetts. Enter the total amount of qualified rent paid by you during 2004 in line 14a. Divide line 14a by 2 and enter the result, **or \$3,000** (\$1,500 if married filing a separate return) — **whichever is smaller** — in line 14. **Note:** This deduction amount does not apply to your U.S. tax return.

What Qualifies for the Rental Deduction?

The deduction must be for rent you paid to a landlord for the rental or lease of your principal residence in Massachusetts.

If two or more persons jointly rent a unit, each occupant using it as his/her principal residence is entitled to a deduction based on the amount of rent that each person paid.

If the rent is paid by a third party (such as a parent) who maintains a principal residence elsewhere, no 50% rental deduction is allowed for either party.

A principal residence does not include any residence for vacation, an apartment for a person on a temporary assignment or a student or faculty member who has a principal residence elsewhere. It also does not include any apartment or house in Massachusetts of a nonresident who has a legal residence in another state or country.

Payment for occupying a hotel, motel or rooming house is not considered rent unless a rental agreement exists. All separately stated charges such as utilities, furnishings or parking cannot be included in rent for purposes of this deduction. Also, rent does not include any advance payments (such as security deposit, last month's rent, etc.) until actually applied as rent.

How Do I Calculate My Rental Deduction If I Am Married Filing Separately?

If a husband and wife file separate returns, they are each entitled to a rental deduction equal to 50% of the rent each pays, not to exceed \$1,500 per return. However, a married couple filing separately may allocate the rent deduction differently, provided the amount taken by each spouse does not exceed 50% of the rent actually paid by that spouse, and provided their combined rental deductions do not exceed \$3,000. If the allocation results in one spouse claiming a deduction in excess of \$1,500, that spouse must enclose with his/her return a statement signed by the other spouse indicating consent to the allocation. The statement must contain the name, address and Social Security number of the consenting spouse and the amount of rental deduction taken by that spouse.

Line 15. Other Deductions (from Schedule Y)

Allowable Employee Business Expenses, Penalty on Early Savings Withdrawal, Alimony Paid, Amounts Excludible Under MGL Ch. 41, Sec. 111F or U.S. Tax Treaty, Student Loan Interest Deduction, Medical Savings Account Deduction, Moving Expenses, Self-Employed Health Insurance Deduction, Certain Qualified Deductions From U.S. Form 1040, Deductible Amount of Qualified Contributory Pension Income from Another State or Political Subdivision, College Tuition Deduction, Undergraduate Student Loan Interest Deduction and Commuter Deduction

"Other deductions" include the items listed above and must be included on Schedule Y. Enter the total from Schedule Y, line 10. Be sure to enclose Schedule Y with your return. Failure to do so will delay the processing of your return.

Line 17. 5.3% Income After Deductions

Subtract line 16 from line 10. Enter the result in line 17. If line 16 exceeds line 10, enter "0" in line 17.

Line 19. 5.3% Income After Exemptions

Subtract line 18 from line 17. If line 18 exceeds line 17, enter "0" in line 19.

If line 18 exceeds line 17 and you were the beneficiary of an estate or trust taxed in Massachusetts, or if you received interest income (other than interest from Massachusetts banks), dividends or capital gain income, read the following section and complete the worksheet for Schedule B, line 36 and Schedule D, line 19, if applicable. All others proceed to line 20.

Applying Exemptions for the Beneficiary of an Estate or Trust Taxed in Massachusetts

If you are reporting income on Form 1 and were also the beneficiary of an estate or trust, you may apply excess exemptions to your income taxed at 5.3% on Form 2, Massachusetts Fiduciary Income Tax Return. If you are single, head of household, or married filing jointly, you may then apply any remaining excess exemptions to your interest income (other than interest from Massachusetts banks), dividends or 12% capital gain income reported on Form 1. Any excess amount should then be applied against interest income (other than interest from Massachusetts banks), dividends or 12% capital gain income reported on Form 2 before applying any remaining excess amount against long-term capital gain income re-

ported on Form 1. Any excess amount still remaining should then be applied against long-term capital gain income reported on Form 2. You must complete and file with your Form 2 a copy of Form 20A, Beneficiary's Claim for Exemptions Applicable to Fiduciary Income, in order to apply the excess exemptions to your Form 2 income. Forms 2 and 20A are available at www.mass.gov/dor.

Line 20. Interest and Dividend Income

If you have any interest income other than interest from deposits in banks located in Massachusetts, dividend income in excess of \$1,500, certain capital gains or losses, or any adjustments to interest income (other than interest from Massachusetts banks), you must complete Schedule B. Be sure to enclose Massachusetts Schedule B. To determine if you need to file Schedule B, refer to the Schedule B instructions in this booklet.

Enter in line 20 the amount from Schedule B, line 38. If not required to file Schedule B, enter dividend income of \$1,500 or less (from U.S. Form 1040 or 1040A, line 9a) in line 20.

Tax on 5.3% Income

Line 22. 5.3% Tax (from Tax Table)

Based upon the amount in line 21, find the proper amount of tax in the blue table at the back of this booklet. Enter the tax in line 22. If line 21 is more than \$24,000, multiply the amount in line 21 by .053 and enter the result in line 22. You must use the tax table if line 21 is \$24,000 or less.

Note: Personal income tax forms must provide an election to voluntarily pay tax at a rate of 5.85% on taxable income which would otherwise be taxed at a rate of 5.3%. The election to pay tax at the rate of 5.85% does not apply to items of income taxed at 12% (short-term capital gains and gains on collectibles). If choosing the optional 5.85% tax rate, multiply line 21 and Schedule D, line 20 by .0585 and fill in the oval.

12% Income & Tax

Line 23. 12% Income from Certain Capital Gains

If you have any interest income other than interest from deposits in banks located in Massachusetts, dividend income in excess of \$1,500, certain capital gains or losses, or any adjustments to interest income (other than interest from Massachusetts banks), you must complete Schedule B. Be sure to enclose Massachusetts Schedule B. To determine if you need to file Schedule B, refer to the Schedule B instructions in this booklet.

Enter in line 23a the amount from Schedule B, line 39. Multiply this amount by .12 (12%) and enter the tax in line 23.

Long-Term Capital Gain Income & Tax

Line 24. Schedule D (Long-Term Capital Gains and Losses Excluding Collectibles)

Enter in line 24 the amount from Schedule D, line 21, **but not less than "0."** To determine if you need to file Schedule D, refer to the Schedule D instructions in this booklet.

Schedule B, Line 36 and Schedule D, Line 19 Worksheet — Exemptions from Interest and Dividend Income, 12% Income and Long-Term Capital Gain Income (Only if Single, Head of Household, or Married Filing Jointly)

If your total exemptions in line 18 are more than the amount of your 5.3% income after deductions in line 17, the excess may be applied against all your interest and dividend income and income taxed at 12%. Any remaining excess amount may then be applied against all your long-term capital gain income. (If you are the beneficiary of a Massachusetts trust or estate, see the instructions for line 19.) Complete the following worksheet only if line 17 is less than line 18 to determine if you qualify for the excess exemption. Enter all losses as "0."

1. Enter amount from Schedule B, line 35. Not less than "0"
2. Enter amount from Form 1, line 18
3. Enter amount from Form 1, line 17
4. Subtract line 3 from line 2. If "0" or less, you do not qualify for this exemption. Omit remainder of worksheet
5. Excess exemptions applied against interest and dividend income and 12% income. If line 1 is larger than line 4, enter line 4 here and in Schedule B, line 36 and omit remainder of worksheet. If line 4 is equal to or larger than line 1, enter line 1 here and in Schedule B, line 36. Complete lines 6 through 8
6. Subtract line 5 from line 4. If "0" you have no remaining excess exemptions. Omit remainder of worksheet
7. Enter Schedule D, line 18. Not less than "0"
8. Excess exemptions applied against long-term capital gain income. If line 7 is larger than line 6, enter line 6 here and in Schedule D, line 19. If line 6 is equal to or larger than line 7, enter line 7 here and in Schedule D, line 19.

Excess Exemptions

If excess exemptions were used in calculating lines 20, 23 or 24 (see Schedule B, line 36 and/or Schedule D, line 19), be sure to fill in the oval in line 24.

Line 25. Credit Recapture Amount

If any Brownfields Credit (BC), Economic Opportunity Area Credit (EOA) or Low Income Housing Credit (LIH) property is disposed of or ceases to be in qualified use prior to the end of its useful life, the difference between the credit taken and the total credit allowed for actual use must be added back to your tax on Form 1. Complete and enclose Schedule H-2, Credit Recapture. Schedule H-2 is available at www.mass.gov/dor or by calling (617) 887-MDOR or toll-free in Massachusetts 1-800-392-6089.

Massachusetts Adjusted Gross Income (AGI)

No Tax Status — Single, Married Filing a Joint Return or Head of Household Only

If your Massachusetts AGI was \$8,000 or less if single, \$12,700 or less plus \$1,000 per dependent if head of household, or \$14,200 or less plus \$1,000 per dependent if married filing a joint return, you qualify for No Tax Status and are not required to pay any Massachusetts income taxes.

Limited Income Credit — Single, Married Filing a Joint Return or Head of Household Only

If you do not qualify for No Tax Status, but you are single and your Massachusetts AGI is between \$8,000 and \$14,000, or if you are filing as head of household and your Massachusetts AGI is between \$12,700 and \$22,225 plus \$1,750 per dependent, or if you are married filing a joint return and your Massachusetts AGI is between \$14,200 and \$24,850 plus \$1,750 per dependent, you **may** qualify for the Limited Income Credit. This credit is an alternative tax calculation that can result in a significant tax reduction for people whose income is close to the No Tax Status threshold.

Massachusetts AGI

Massachusetts AGI is not the same as taxable income. Massachusetts AGI includes:

- wages, salaries, tips;
- taxable pensions and annuities;
- pension income from another state or political subdivision before any deduction;
- taxable IRA/Keogh and Roth IRA distributions;
- fees and unemployment compensation;
- income or loss from a business or profession;

- income or loss from partnerships, S corporations and trusts;
- rents, royalties and REMIC income;
- alimony and other 5.3% income;
- interest from Massachusetts banks before exemptions; and
- other interest, dividends, and capital gains.

Complete the Massachusetts AGI Worksheet below to see if you may qualify for the College Tuition Deduction (Schedule Y, line 7), No Tax Status or the Limited Income Credit.

Massachusetts AGI Worksheet

1. Enter your total 5.3% income from Form 1, line 10. Not less than "0"*
2. Enter the total of Schedule Y, lines 1 through 5.
3. Subtract line 2 from line 1. Not less than "0"
4. Enter total Massachusetts bank interest or the interest exemption amount, whichever is smaller, from Form 1, line 5a or line 5b

Note: If Form 1, line 10 is a loss, do not complete line 4 above. Instead, combine Form 1, line 10 with the smaller amount of total Massachusetts bank interest or the interest exemption amount. Enter the result in line 4 above, unless the result is a loss. If the result is a loss, enter "0."

5. Enter amount from Schedule B, line 35. If there is no entry in Schedule B, line 35 or if not filing Schedule B, enter the amount from Form 1, line 20
6. Enter the amount from Schedule D, line 18.** Not less than "0"
7. Add lines 3 through 6

If you are single and the total in line 7 is \$8,000 or less, you qualify for No Tax Status (see line 26 instructions). If you are single but do not qualify for No Tax Status, and your total in line 7 is \$14,000 or less, complete line 27 and see line 28 instructions for the Limited Income Credit. If you are filing as head of household or married filing a joint return, compare line 7 with the No Tax Status/Limited Income Credit chart to see if you may qualify for No Tax Status or the Limited Income Credit.

*Add back any Abandoned Building Renovation deduction claimed on Schedule(s) C and/or E before entering an amount in line 1.

**If filing Schedule D-IS, Installment Sales, see the Schedule D-IS instructions for the amount to enter in line 6. Schedule D-IS and instructions are available on DOR's website at www.mass.gov/dor.

Line 26. No Tax Status

If you qualify for No Tax Status, fill in the oval in line 26, enter "0" in line 27 and omit lines 28 through 30. Also, enter "0" in line 31 and complete Form 1. However, if there is an amount entered in line 25, Credit Recapture Amount, enter that amount in line 27 and complete lines 29 and 30.

Note: If married filing separately, you do not qualify for No Tax Status.

Line 27. Total Tax

Add line 22 (5.3% tax), line 23 (12% tax), line 24 (tax on long-term capital gains) and line 25 (credit recapture amount). Enter the total in line 27.

Line 28. Limited Income Credit

Line 28 Worksheet — Limited Income Credit (Only if Single, Head of Household, or Married Filing Jointly)

1. Enter amount from line 7 of Massachusetts AGI Worksheet
2. Enter \$8,000 if single. If married filing a joint return or head of household, enter the amount from the blue column of the No Tax Status/Limited Income Credit chart
3. Subtract line 2 from line 1.
4. Enter in line 4 the amount of tax from Form 1, line 27
5. Multiply line 3 by 10% (.10)
6. If line 4 is smaller than line 5, you are not eligible for this credit. Enter "0." If line 4 is larger than line 5, subtract line 5 from line 4 and enter the result here and in line 28 on Form 1

Line 29. Other Credits (from Schedule Z)

Lead Paint Credit, Economic Opportunity Area Credit, Full Employment Credit, Septic Credit, Brownfields Credit, Low-Income Housing Credit, Credit for Income Tax Paid to Another State or Jurisdiction and Energy Credit

"Other credits" include the items listed above and must be included on Schedule Z. Enter the total from Schedule Z, line 3. Be sure to enclose Schedule Z with your return. Failure to do so will delay the processing of your return.

Line 32. Voluntary Contributions

You may contribute any amount you choose to the following funds. Remember, these amounts are added to your tax. They increase the amount of your payment or reduce the amount of your refund.

a. Organ Transplant Fund: The Organ Transplant Fund is administered by the Massachusetts Department of Public Health. All contributions received by the Fund assist patients with the costs of medications without which they might lose their transplanted organs.

b. Endangered Wildlife Conservation: The Natural Heritage and Endangered Species Fund is administered by the Division of Fisheries and Wildlife. Contributions are used to protect and restore rare and endangered wildlife and plants, and their habitats. This fund has helped restore and conserve in the Commonwealth populations of the Bald Eagle, Hessel's Hairstreak Butterfly, the Redbelly Turtle and the Plymouth Gentian.

c. Massachusetts AIDS Fund: The Massachusetts AIDS Fund is administered by the Massachusetts Department of Public Health. Contributions are used for research, experimental treatment and education related to Acquired Immune Deficiency Syndrome (AIDS). Massachusetts residents living with AIDS receive experimental treatment through clinical trials which are wholly supported with this Fund. The Fund also educates people with AIDS about treatment options and how to gain access to medication and experimental treatment.

d. Massachusetts United States Olympic Fund: Contributions to this fund are used to assist Massachusetts residents in paying all or part of any costs associated with the development, maintenance and operation of the United States Olympic Team participating in the Olympics and the United States Paralympic Team participating in the Paralympics. Add items a, b, c and d and enter the total in line 32.

Line 33. Massachusetts Use Tax Due On Out-of-State Purchases Made in 2004

A 5% Massachusetts use tax is due on your taxable purchases from out-of-state businesses of tangible personal property purchased for use in Massachusetts on which you did not pay Massachusetts sales or use tax. The use tax does not apply to out-of-state purchases that are exempt from the sales tax (for example, clothing that costs \$175 or less). Examples of taxable items include automobiles, computers, furniture, jewelry, cameras, appliances, and any other item that is not exempt. Generally, anyone who pays a sales or use tax to another state or territory of the United States on tangible personal property to be used in Massachusetts is entitled to a credit against the Massachusetts use tax, up to 5%. This credit is allowed for sales or use tax paid to another state only if that state has a corresponding credit similar to the Massachusetts credit. See TIR 03-1 for more information. Prepare and retain with your records a list of your out-of-state purchases in 2004 that are subject to the Massachusetts use tax.

Recent legislation permits taxpayers to use the following table to self-report a "safe-harbor" amount of use tax based on their Massachusetts adjusted gross income. A taxpayer may pay this amount in lieu of the actual amount of use tax that would otherwise be due with respect to such purchases. Individual taxpayers electing to report use tax under this method will not be assessed additional use tax on audit, even if the actual amount of use tax due would have been greater than the amount from the schedule. The amendment applies to purchases made on or after January 1, 2004.

No Tax Status/Limited Income Credit Chart

Filing status:

| Number of dependents (from Form 1, line 2b): | Head of household. Line 7 of the AGI worksheet is less than or equal to: | | Married filing a joint return. Line 7 of the AGI worksheet is less than or equal to: | |
|---|--|---|--|---|
| | Blue Column | Red Column | Blue Column | Red Column |
| 0 | \$12,700 | \$22,225 | \$14,200 | \$24,850 |
| 1 | 13,700 | 23,975 | 15,200 | 26,600 |
| 2 | 14,700 | 25,725 | 16,200 | 28,350 |
| 3 | 15,700 | 27,475 | 17,200 | 30,100 |
| 4 | 16,700 | 29,225 | 18,200 | 31,850 |
| 5 | 17,700 | 30,975 | 19,200 | 33,600 |
| 6 | 18,700 | 32,725 | 20,200 | 35,350 |
| | you qualify for No Tax Status | you may qualify for the Limited Income Credit | you qualify for No Tax Status | you may qualify for the Limited Income Credit |

If the number of dependents is more than 6, add \$1,000 per dependent to the blue column for No Tax Status, or \$1,750 per dependent to the red column for the Limited Income Credit.

If you qualify for No Tax Status, see the instructions for line 26. If you may qualify for the Limited Income Credit, go to line 27 and complete the worksheet for line 28.

The estimated liability applies only to purchases of any individual items each having a total sales price of less than \$1,000. For each taxable item purchased at a sales price of \$1,000 or greater, the actual use tax liability for each purchase must be added to the amount of the estimated liability derived from the table below. See TIR 04-26.

| Mass. AGI per return* | Use tax liability |
|------------------------------|------------------------------|
| \$ 0 – \$ 25,000 | \$ 0 |
| 25,001 – 40,000 | 15 |
| 40,001 – 60,000 | 25 |
| 60,001 – 80,000 | 35 |
| 80,001 – 100,000 | 45 |
| Above \$100,000 | Multiply Mass. AGI* by .0005 |

* Line 7 of Massachusetts AGI worksheet on page 13.

Complete the worksheet below to calculate your use tax if you are not self-reporting a “safe-harbor” amount. For more information about use tax, visit DOR’s website at www.mass.gov/dor.

**Form 1, Line 33 Worksheet —
Use Tax Due on Out-of-State Purchases**

1. Total of purchases in 2004 subject to Massachusetts use tax _____
2. Use tax. Multiply line 1 by .05 (5%) _____
3. Credit for sales/use tax paid to other states or jurisdictions. Add the amount of any sales/use tax paid to another state or jurisdiction, or 5% of the sales price, whichever is less, on each purchase reported in line 1 _____
4. Total amount due. Subtract line 3 from line 2. Not less than “0.” Enter the result here and on Form 1, line 33 _____

Line 35. Massachusetts Income Tax Withheld

This represents all income taxes withheld for the Commonwealth of Massachusetts as indicated on your copies of Forms W-2, W-2G and certain 1099s, if applicable. Enter the total of all Massachusetts withholdings in line 35. Attach, with a single staple, state copies to your return; otherwise your claim of amounts withheld will not be allowed. If you have lost your state copy, ask the payer for a duplicate. Copies of 1099s need only be attached if they show an amount for Massachusetts tax withheld.

Line 36. 2003 Overpayment Applied to Your 2004 Estimated Tax

Include the exact amount of any 2003 overpayment you applied to your 2004 estimated taxes on your 2003 Massachusetts Form 1, line 43 or Form 1-NR/PY, line 48. Do not include any 2003 refund in this line.

Line 37. 2004 Massachusetts Estimated Tax Payments

If you paid Massachusetts estimated income tax for 2004, enter in line 37 the total of all Massachusetts estimated tax payments. Be sure to include any last quarter (of 2004) payment made on or before January 15, 2005. Do not include any 2003 overpayment applied to your 2004 estimated tax. Every resident who expects to pay more than \$400 in Massachusetts income tax on income which is not covered by Massachusetts withholding must pay Massachusetts estimated taxes. Estimated tax payments can be made online by using Web Services for Income by visiting www.mass.gov/dor or by filing Massachusetts Form 1-ES.

Income which is not subject to withholding includes:

- salaries and wages where the employer is not subject to Massachusetts withholding;
- dividends and interest, including interest from Massachusetts banks;
- gains from capital assets;
- income from an individual trade, business, profession, partnership or S corporation;
- income from any estate or trust not taxed directly;
- certain pensions;
- taxable Keogh or IRA distributions;
- rental, royalty or REMIC income;
- unemployment compensation (from which no Massachusetts income tax was withheld);
- alimony received;
- contributions to SIMPLE accounts;
- illegal income; and
- any other income received while a Massachusetts resident from which Massachusetts tax will not be withheld.

Generally, the first payment must be filed on or before April 15 of the taxable year. The estimated tax may be paid in full with the first payment or in four installments on or before April 15, June 15, September 15 of the current taxable year and January 15 of the following year.

If you wish to verify estimated tax payments that have already been made, check the Estimated Tax Payment History Application at www.mass.gov/dor. You will need to know the PIN that appeared on the back of your Form 1 booklet or the amount of last year’s refund or balance due to access your account.

You may request your employer to withhold additional amounts from your salary on Form M-4, Massachusetts Employee’s Withholding Exemption Certificate to cover the taxes on other income so that you do not have to file and pay estimated taxes.

If 80% of the tax is not paid throughout the year through withholding and/or estimated payments, a penalty may be imposed.

Line 38. Earned Income Credit

The earned income credit is a tax credit for certain taxpayers who work and have earned income under \$35,458. Taxpayers who qualify for and claim the federal earned income credit are allowed a refundable credit equal to 15% of the federal amount. If the credit due the taxpayer exceeds the amount of the total income tax payable for the year by the taxpayer, the excess amount of the credit will be refunded to the taxpayer without interest. You must enter the number of qualifying children, if any, in line 38a. Then, enter the federal earned income credit amount from your U.S. Form 1040, line 65a, 1040A, line 41a; 1040EZ, line 8a; or U.S. Telefile Tax Record, item L. Multiply this amount by .15 (15%) and enter the result in line 38.

If you choose to have the IRS compute your federal earned income credit, wait until the IRS notifies you of that amount before making an entry in line 38. If you have not received your earned income credit amount as computed by the IRS by April 15, 2005, you may file Massachusetts Form M-4868, Application for Automatic Six-Month Extension of Time to File Massachusetts Income Tax Return. See page 3 for information about filing your extension by telephone or via the Web. For more information about the federal earned income tax credit, see IRS publication 596, available at www.irs.gov.

Line 39. Senior Circuit Breaker Credit

Certain senior citizens in Massachusetts may be eligible to claim a refundable credit on their state income taxes for the real estate taxes paid on the Massachusetts residential property they own or rent and which they occupy as their principal residence. The maximum credit allowed is \$820 for the tax year beginning January 1, 2004. If the credit due the taxpayer exceeds the amount of the total income tax payable for the year by the taxpayer, the excess amount of the credit will be refunded to the taxpayer without interest. To determine if you qualify for this credit, refer to the Senior Circuit Breaker Credit instructions in this booklet.

If you qualify for this credit and you are a homeowner, enter the amount from Schedule CB, Circuit Breaker Credit, line 20; if you are a renter, enter the amount from line 24. Be sure to complete and enclose Schedule CB with your return.

Line 40. Payments Made with Extension

If you filed Massachusetts Form M-4868, Application for Automatic Six-Month Extension of Time to File Massachusetts Income Tax Return, for 2004 on or before April 15, 2005, enter in line 40 the amount you paid with Massachusetts Form M-4868, line 7.

Refund Amount

Line 42. Overpayment

If line 34 is smaller than line 41, subtract line 34 from line 41 and enter the result in line 42. This is the amount of your overpayment. If line 34 is larger than line 41, go to line 45. If line 34 and line 41 are equal, enter "0" in line 44.

Line 43. Amount of Overpayment You Want Applied to Your 2005 Massachusetts Estimated Tax

Enter the amount of your 2004 overpayment that you wish to apply to your 2005 Massachusetts estimated tax. Once an election is made to apply your overpayment to your 2005 estimated tax, it cannot be refunded later or applied to any additional tax you may owe for 2004. The amount entered in this line can only be claimed as a credit on your 2005 Massachusetts return.

Line 44. Refund Amount

Subtract line 43 from line 42. Enter the result in line 44. This is the amount of your refund. **Note:** Your state tax refund may be taxable on your U.S. tax return if you deducted state income tax paid as an itemized deduction on U.S. Schedule A.

Direct Deposit

You may elect to have your refund deposited directly into your savings or checking account. Check with your financial institution to make sure that it accepts direct deposit and verify the routing transit number (RTN) of the issuing financial institution. If we are unable to honor your request for a direct deposit, a paper check will be sent to you.

A sample check from JANE TAXPAYER, JOHN TAXPAYER, 123 Main Street, Anyplace, MA 02000. The check is dated 12/34 and has a serial number 15-00000000. The amount is \$ [redacted]. The routing number is 020250029 and the account number is 020201186. The check is payable to the order of [redacted].

The routing number of your financial institution is nine digits and begins with 01 through 12 or 21 through 32. The account number can be up to 17 characters (both numbers and letters). Omit hyphens, spaces and special symbols. Enter the number from left to right and leave any unused boxes blank. You **must enter** the routing number and the account number in the spaces provided in line 44 if you are requesting direct deposit. Failure to do so will result in your request for direct deposit being denied. See sample check above for location of this information.

Note: Only one direct deposit is allowed per account number.

Tax Due

Line 45. Tax Due

If line 34 is larger than line 41, subtract line 41 from line 34, and enter the result in line 45. This is the amount of tax you owe with your return. Pay in full with your return. Go to Web Services for Income at www.mass.gov/dor for online payment options. If you need to mail your payment, make your check or money order payable to the Commonwealth of Massachusetts and write your Social Security number on the front of your check or money order in the lower left corner. Complete and remove Form PV, Massachusetts Income Tax Payment Voucher, attached to the back of the envelope included in this booklet. Attach with a single staple the check to the front of Form PV and enclose Form PV with your return. Form PV **must** be included with your check to ensure proper crediting of your account. Be sure to use the light blue mailing label when mailing your Form 1 with the Form PV.

Failure to file or failure to pay the proper amount of tax when due will result in an increasing amount of interest and penalties. It is to your advantage to file when your return is due, whether or not you are able to make full payment.

If you owe any interest, penalty or addition for the underpayment of estimated tax, add those amounts to the tax you owe and enter the total amount in line 45.

What Are Interest and Penalties?

Interest: If you fail to pay the tax when due, interest will be charged. For an explanation of how interest is compounded in Massachusetts, see TIR 92-6 or call the Customer Service Bureau at (617) 887-MDOR or toll-free, in Massachusetts at 1-800-392-6089.

Penalty for Late Payment: The penalty for late payment is ½% per month (or fraction thereof) of the tax due, up to a maximum of 25%.

Penalty for Failure to File: The penalty for failure to file a tax return by the due date is 1% per month (or fraction thereof) of the tax due, up to a maximum of 25%. If you were required to file a tax return for income received in any prior year and you did not file, you must file for that prior year.

Penalty for Protested ("Bad") Check: If your check is not honored by your bank because of insufficient funds or any other reason, a penalty may be added equal to 2% of the amount of the check or \$10, whichever is greater (but no more than the amount of the check).

Addition for Underpayment of Estimated Tax: You will generally be subject to this addition to tax if you did not have withholding and/or estimated payments equal to 80% of the total tax liability re-

quired to be paid and your 2004 tax due after credits and withholding is greater than \$200. (For tax years on or after January 1, 2005, this threshold is increased to \$400.) The 80% requirement is reduced to 66⅔% for individuals who receive two-thirds of their income from fishing or farming. If you failed to meet these requirements, you must complete and enclose Massachusetts Form M-2210 to calculate the amount you must add to line 45. You do not have to complete Form M-2210 if the balance due with your return is \$200 or less.

You may not be subject to an underpayment penalty if you qualify for one of the following exceptions:

- ▶ you are a qualified farmer or fisherman and are paying the full amount of the tax due on or before March 1, 2005;
- ▶ you were a Massachusetts resident and were not liable for 2003 taxes (where the taxable year was 12 months); or
- ▶ the sum of your estimated payments and withholding equals or exceeds your 2003 total tax due (where the taxable year was 12 months and a return was filed).

If you qualify for one of these exceptions, please fill in the oval marked "EX" under line 45 on Form 1 and enclose Form M-2210 indicating which of the exceptions applies to your circumstances.

A limited number of taxpayers may also qualify for a waiver of the underpayment penalty for one or more installments if:

- ▶ the underpayment was because of casualty or disaster; or
- ▶ during 2003 or 2004 you retired after reaching age 62 or became disabled and the underpayment was due to reasonable cause and not willful neglect.

If you think you qualify for one of these waivers, go to www.mass.gov/dor and use DOR's online application for abatement/amended return at www.mass.gov/dor or enclose Form M-2210 and an explanatory statement with your return and fill in the oval marked "EX" under line 45. If your waiver is not for all four installments, complete Form M-2210 to calculate the underpayment penalty for the installments which are not covered by the waiver. Form M-2210 is available by visiting www.mass.gov/dor.

Penalty for Failure to Report Federal Change: If the U.S. Internal Revenue Service changes your income for a prior year (generally through audit), file an online application for abatement/amended return at www.mass.gov/dor within one year of the final federal determination to avoid this penalty. This penalty is equal to 10% of the additional tax due or \$100, whichever is smaller. If the change indicates a refund, file an online application for abatement/amended return within one year, including acceptance of an amended federal return by the Internal Revenue Service.

Sign Here

Now that you have completed Form 1, sign your name. Your spouse must also sign if this is a joint return. Write the date you signed the return. Remember to sign your name(s) at the bottom of page 1 of Form 1.

Attach to your Form 1, with a single staple, all state copies of your Forms W-2, W-2G and any Forms 1099 which included Massachusetts withholding. If making a payment, be sure to attach with a single staple your check or money order to the front of Form PV and enclose Form PV with your Form 1. Form PV is attached to the back of the envelope found in this booklet. Form PV **must** be included with your check to ensure proper crediting of your account. Make your check or money order payable to Commonwealth of Massachusetts and be sure to sign the check and write your Social Security number on it. Also, be sure to use the light blue mailing label when mailing your Form 1 with the Form PV.

Paid Preparer Must Sign Your Return

Generally, anyone you pay to prepare your return must sign it in the space provided. Tax return preparers are authorized to sign the return by means of a rubber stamp, mechanical device, or computer software program, which must include either a facsimile or printed name of the preparer. Preparers are personally responsible for affixing their signatures to returns. The preparer must give you a copy of the return for your records. Someone who prepares your return but does not charge you should not sign your return.

Paid Preparer Authorization

If you want to allow the Massachusetts Department of Revenue (DOR) to discuss your 2004 tax return with the paid preparer who signed it, fill in the "Yes" oval in the signature area of the return. This authorization applies only to the individual whose signature appears in the "Paid Preparer" section of your return. It does not apply to the firm, if any, shown in that section.

If you fill in the "Yes" oval, you, and your spouse if filing a joint return, are authorizing DOR to call the paid preparer to answer any questions that may arise during the processing of your return. You are also authorizing the paid preparer to:

- give DOR any information that is missing from your return;
- call DOR for information about the processing of your return or the status of your refund or payment(s); and
- respond to certain DOR notices that you have shared with the preparer about math errors, offsets and return preparation. The notices will not be sent to the preparer.

You are not authorizing the paid preparer to receive any refund check, bind you to anything (including any additional tax liability), or otherwise represent you before DOR. If you want to expand the paid preparer's authorization, see Form M-2848, Power of Attorney and Declaration of Representative. Form M-2848 is available by visiting www.mass.gov/dor.

The authorization cannot be revoked. However, the authorization will automatically end no later than the due date (without regard to extensions) for filing your 2005 tax return. This is April 15, 2006 for most people.

E-File Opt Out

For tax years beginning on or after January 1, 2004, income tax return preparers who completed 200 or more original Massachusetts Forms 1 and 1-NR-PY, including those E-filed, during the previous calendar year are required to use electronic means to file all personal income tax returns, unless the taxpayer specifically directs on the paper form that the filing be on paper. Fill in oval if you do not want your preparer to file your return electronically. See TIR 04-30 for more information.

Mailing

If you are expecting a refund or if you have no tax due, use the white mailing label on the back of the envelope that came with this booklet. If you do not have one, mail Form 1 to: **Massachusetts Department of Revenue, PO Box 7000, Boston, MA 02204-7000.**

If you have a tax due, use the light blue mailing label on the back of the envelope that came with this booklet. If you do not have one, mail Form 1 to: **Massachusetts Department of Revenue, PO Box 7003, Boston, MA 02204-7003.**

Note: If using a tax software product, be sure to use the correct PO box. See page 3.

Note: Schedule lines without specific instructions are considered to be self-explanatory. Be sure to list on each schedule the name and Social Security number that appears first on Form 1. Do not cut or separate schedules.

Schedule X

Other Income

Be sure to enclose with Form 1.

Line 1. Alimony Received

Enter in Schedule X, line 1 the total amount of all periodic payments of alimony or separate maintenance received under a court judgment or decree, or for excess alimony amounts recaptured, as reported on U.S. Form 1040, line 11. Payments specified as child support are not taxable.

Line 2. Taxable IRA/Keogh and Roth IRA Conversion Distributions

Complete the Schedule X, line 2 worksheet to calculate the taxable portion of any amount you received as an Individual Retirement Account (IRA), Keogh or Roth IRA conversion distribution. Since Massachusetts does not allow a deduction for amounts originally contributed to an IRA or Keogh, the distributions are not taxable until the full amount of your contributions which were previously subject to Massachusetts taxes are recovered.

Note: Contributions made to Keogh accounts prior to 1975 were deductible when made. Therefore, no deduction may be taken from a Keogh distribution for amounts contributed before 1975.

Massachusetts generally adopts the federal conversion rules for partial or complete rollovers from existing IRAs to Roth IRAs. Generally, the rollover amount is treated as a distribution and included in federal gross income to the extent it is attributable to investment growth or previously deducted contributions. See TIR 98-8, *Massachusetts 1998 Reducing Income Taxes Act*, for further details.

Schedule X, Line 2 Worksheet — Taxable IRA/Keogh Plan and Roth IRA Conversion Distributions

Complete this worksheet to report conventional IRA/Keogh distributions or Roth IRA conversion distributions.

1. Total IRA/Keogh plan distributions, Roth IRA conversion distributions received during 2004
2. Total IRA/Keogh plan contributions previously taxed by Massachusetts
3. Total distributions received in previous years
4. Subtract line 3 from line 2. If line 3 is larger than line 2, enter "0"
5. Taxable IRA/Keogh distributions or Roth IRA conversion distributions. Subtract line 4 from line 1 and enter the result here. Not less than "0"

Note: You must complete separate worksheets if married filing a joint return and both you and your spouse received IRA/Keogh Plan and/or Roth IRA conversion distributions.

Line 3. Other Gambling Winnings

Enter in Schedule X, line 3 all gambling winnings from casinos, raffles, races, beano or other events of chance, wherever held, and winnings from non-Massachusetts lotteries. Do not enter less than "0." You may only deduct the price of the winning ticket. Gambling losses are not deductible under Massachusetts law. Gambling losses claimed as itemized deductions on U.S. Form 1040, Schedule A are not allowed on your Massachusetts return.

Line 4. Fees and Other 5.3% Income

The following items should be reported on line 4 of Schedule X. **Do not enter less than "0."** Enclose additional statements if more space is needed.

- ▶ All fee income, such as payments for jury duty, election worker payments, director's fees, compensation received as executor or administrator of an estate, and commission income or tips not reported in line 3 of Form 1 are taxable. Also, report all bartering income not reported on Schedule C (the fair market value of goods or services received in payment for your services).
- ▶ All prizes and awards won in a quiz program, drawing, beauty contest, etc. are taxable at fair market value. Awards and bonuses received from your employer for performance of services not part of a qualified award plan are also taxable.
- ▶ Other Massachusetts 5.3% income reported on U.S. Form 1040, line 21 and not reported elsewhere in Form 1, lines 3 through 8 or Schedule X, lines 1 through 3 must be reported in line 4 of Schedule X.
- ▶ Pre-1996 installment sales classified as ordinary income for Massachusetts purposes (from Massachusetts Schedule D, line 9) are taxed as 5.3% income and must be reported on line 4 of Schedule X.
- ▶ Embezzled or other income from illegal activities is taxable and should be reported on Schedule X, line 4.

The following items should **not** be reported on your Massachusetts return:

- ▶ Any "net operating loss" reported as a negative amount on U.S. Form 1040, line 21 cannot be entered on Schedule X. A net operating loss from a business or profession cannot be carried forward or backward to offset individual income in any other year under Massachusetts law.
- ▶ Refunds of U.S. and Massachusetts income taxes are not considered income under Massachusetts law. If you received interest on refunds, report such interest on Massachusetts Schedule B.

Schedule Y

Other Deductions

Be sure to enclose with Form 1.

Line 1. Allowable Employee Business Expenses

Generally, reimbursed employee business expenses are not included in your wages or salary and therefore are not allowed as deductions. However, there are unreimbursed and certain reimbursed expenses for which you are allowed a deduction. Complete the following worksheet in order to calculate your Massachusetts employee business expense deduction. The expenses must relate to income reported in lines 3 or 9 on Form 1.

Employees may deduct the following:

- ▶ unreimbursed travel and transportation expenses including lodging and meals away from home incurred by an employee; and
- ▶ all federally deductible unreimbursed employee business expenses, if the employee is a salesperson who solicits business for an employer away from the employer's place of business. Unreimbursed expenses are only deductible if all of the following conditions are met:
 - ▶ you itemize deductions;
 - ▶ if you filed a joint U.S. return, you must file a joint Massachusetts return; and
 - ▶ your unreimbursed business expenses taken together with the other miscellaneous itemized deductions reported on U.S. Form 1040, Schedule A, lines 20, 21 and 22 exceed 2% of your federal adjusted gross income reported on U.S. Form 1040, Schedule A, line 25. See the following worksheet for Schedule Y, line 1.

If you are a qualified performing artist or a fee-basis state or local government official, do not complete the worksheet. Enter on Schedule Y, line 5 your federally deductible business expenses included on U.S. Form 1040, line 35 and fill in the appropriate oval in Schedule Y, line 5. On the dotted line next to line 5, be sure to indicate the type of deduction being taken, as identified on U.S. Form 1040, line 35. For example, qualified performing arts-related expenses should be identified as "QPA" and employee business expenses of fee-basis state or local government officials should be identified as "FBO."

Note: Same-sex joint filers should recalculate their U.S. Form 1040, Schedule A by combining allowable expenses as reported on U.S. Form 1040, Schedule A, lines 23 and 27 and their adjusted gross incomes as reported on U.S. Form 1040, Schedule A, line 24 in calculating U.S. Form 1040, Schedule A, line 26. Same-sex joint filers should also recalculate their U.S. Form 2106 or 2106 EZ by combining allowable expenses as re-

ported on U.S. Form 2106, lines 4, 9b and 10 or U.S. Form 2106-EZ, lines 4, 5 and 6. See TIR 04-17 for more information.

Schedule Y, Line 1 — Massachusetts Employee Business Expense Deduction Worksheet

1. Enter the amount from U.S. Form 2106, line 10, or 2106-EZ, line 6. _____
2. If you are an employee other than an outside salesperson, enter the amount of unreimbursed expenses included in U.S. Form 2106 or 2106-EZ, line 4 _____
3. If you are an employee other than an outside salesperson, enter the amount of unreimbursed meals and entertainment expenses included in U.S. Form 2106, line 9, column B or 2106-EZ, line 5, except for meals incurred while away from home. _____
4. If you are an individual with a disability, enter the amount of impairment-related expenses included in line 1 and claimed on line 27 of U.S. Schedule A _____
5. Add lines 2 through 4. Enter the result here. _____
6. Subtract line 5 from line 1. Enter the result here _____
7. Enter the amount from U.S. Schedule A, line 26 _____
8. Enter the smaller amount of line 6 or line 7 here and on Schedule Y, line 1 _____

Line 2. Penalty on Early Savings Withdrawal

If you were charged a penalty because of early withdrawal of savings, and interest on the savings that such a penalty relates to is reported on this return or on a prior year Massachusetts return, you may deduct the penalty. This deduction is the same as the amount allowable on U.S. Form 1040, line 33. Enter this amount in line 2 of Schedule Y.

Line 3. Alimony Paid

Enter in Schedule Y, line 3 the total amount that you paid to your former spouse during 2004 for alimony or separate maintenance under court decree, or for excess alimony amounts recaptured, as reported on U.S. Form 1040, line 34a. **Note:** Alimony payments specified as child support are not deductible.

Line 4. Amounts Excludible Under MGL Ch. 41, Sec. 111F or U.S. Tax Treaty Included in Form 1, Line 3.

Massachusetts allows an exclusion from income of amounts received by a firefighter or police officer incapacitated in the line of duty, per MGL Ch. 41, sec. 111F, and an exclusion from income of amounts received by qualifying students exempt under a U.S. tax treaty.

Enter any excludible amount of income received while you were a firefighter or police officer incapacitated in the line of duty in line 4 of Schedule Y that was included in Form 1, line 3, and fill in the appropriate oval.

If you were a qualifying student or a taxpayer with income exempt under a U.S. tax treaty, enter any excludible amount of income received that was exempt under a U.S. tax treaty in line 4 of Schedule Y that was included in Form 1, line 3, and fill in the appropriate oval.

Line 5. Other Qualified Deductions

You may claim **only** the deductions listed below for Schedule Y, line 5. If you are entitled to claim any of the deductions in line 5, fill in the appropriate oval(s) and enter the total amount of deductions claimed in line 5.

► **Student Loan Interest Deduction:** Enter the amount from U.S. Form 1040, line 26 or 1040A, line 18 and fill in the appropriate oval in line 5 of Schedule Y. For tax year 2004, the maximum deduction is \$2,500, with the allowable amount reduced for individuals with federal adjusted gross income over \$40,000 (\$60,000 if married filing jointly). For information on how to reduce this amount, click on the Guide to Taxes of the Personal Income section of DOR's website at www.mass.gov/dor. This deduction is only allowed if not claiming the same expenses in line 8 of Schedule Y, Undergraduate Student Loan Interest deduction. Also, taxpayers with federal adjusted gross income over \$55,000 (\$75,000 if married filing jointly) may not claim this deduction.

Note: Same-sex joint filers must use the "Student Loan Interest Deduction" worksheet in the instructions to U.S. Form 1040 or 1040A making sure to combine their income figures, and performing the calculation as though they were filing a joint federal return. See TIR 04-17 for more information.

► **Archer Medical Savings Account (MSA) Deduction:** Due to differences between the Internal Revenue Code as amended and in effect as of January 1, 1998, and the current year, the Massachusetts deduction for an Archer MSA contribution is allowable only for contributions of individuals who were active MSA participants before January 1, 2001. Enter only the portion of the Archer MSA deduction included on U.S. Form 1040, line 35 attributable to an individual who was an active MSA participant before January 1, 2001 and fill in the appropriate oval in line 5 of Schedule Y. Do not include amounts contributed for any person who was not an active MSA participant before January 1, 2001.

► **Moving Expenses:** Enter the amount from U.S. Form 1040, line 29 and fill in the appropriate oval in line 5 of Schedule Y.

► **Self-Employed Health Insurance Deduction:** Enter the amount from U.S. Form 1040, line 31. **Note:** If you elected to claim the federal credit under sec. 35 and had to reduce the amount on U.S. Form 1040, line 31 by the amount of the federal credit, you may add back the amount of the credit to the amount entered on U.S. Form 1040, line 31. Fill in the appropriate oval in line 5 of Schedule Y.

► **Certain Qualified Deductions from U.S. Form 1040: Do not include** any amounts reported on U.S. Form 1040, lines 23 through 34a that are included in Form 1040, line 35 total. Enter **only** amounts included in U.S. Form 1040, line 35 as an adjustment, **except** amounts contributed to sec. 501(c)(18) pension plans. For Massachusetts purposes, contributions to sec. 501(c)(18) pension plans are not deductible. On the dotted line next to line 5, be sure to indicate the type of deduction being taken, as identified on U.S. Form 1040, line 35. Identify qualified performing arts-related expenses as "QPA"; jury duty pay given to your employer as "Jury Pay"; reforestation amortization as "RFST"; repayment of supplemental unemployment benefits under the Trade Act of 1974 as "Sub-Pay TRA"; the deduction for clean-fuel vehicles as "Clean-Fuel"; employee business expenses of fee-basis state or local government officials as "FBO"; and deductible expenses related to income reported on U.S. Form 1040, line 21 and Massachusetts Schedule X, line 4 from the rental of personal property engaged in for profit as "PPR." Fill in the appropriate oval in line 5 of Schedule Y.

Line 6. Deductible Amount of Qualified Contributory Pension Income from Another State or Political Subdivision Included in Form 1, Line 4

Massachusetts allows a deduction for contributory pension income received from another state or one of its political subdivisions which does not tax such income from Massachusetts or its political subdivisions. For guidelines to determine which state's pensions are exempt in Massachusetts, see TIR 95-9. Enter any deductible amount of such income in line 6 of Schedule Y that was included in Form 1, line 4.

Line 7. College Tuition Deduction

A deduction is allowed for tuition payments paid by you, for yourself or a dependent, to a qualifying two- or four-year college leading to an undergraduate or associate's degree, diploma or certificate. Tuition payments for students pursuing graduate degrees at such a college or university are not eligible for the college tuition deduction. The deduction is equal to the amount by which the tuition payments, less any scholarships, grants or financial aid received, exceed 25% of Massachusetts AGI. Qualified tuition expenses include only those expenses

designated as tuition or mandatory fees required for the enrollment or attendance of the taxpayer or any dependent of the taxpayer at an eligible educational institution. No deduction is allowed for any amount paid for room and board, books, supplies, equipment, personal living expenses, meals, lodging, travel or research, athletic fees, insurance expenses or other expenses unrelated to an individual's academic course of instruction. Complete the Massachusetts AGI Worksheet and the Schedule Y, line 7 worksheet to see if you may qualify for this deduction. See TIR 97-13 for more information.

Schedule Y, Line 7 Worksheet — College Tuition Deduction

1. Enter total tuition payments paid by you, for yourself or a dependent, to a qualifying two- or four-year college in 2004 _____
2. Enter amount of scholarships, grants or financial aid received in 2004 for amounts shown in line 1 _____
3. Subtract line 2 from line 1. If "0" or less, you do not qualify for this deduction _____
4. Enter amount from line 7 of the Massachusetts AGI Worksheet _____
5. Multiply line 4 by .25 _____
6. If line 3 is smaller than line 5, you are not eligible for this deduction. Enter "0." If line 3 is larger than line 5, subtract line 5 from line 3 and enter the result here and in line 7 on Schedule Y _____

Line 8. Undergraduate Student Loan Interest Deduction

A deduction is allowed for interest paid on a qualified undergraduate student loan. To be eligible for the deduction, the "education debt" must be a loan that is administered by the financial aid office of a two-year or four-year college at which you, or a qualified dependent, were enrolled as an undergraduate student. Additionally, the loan must have been secured through a state student loan program, a federal student loan program, or a commercial lender, and must have been spent solely for the purposes of paying tuition and other expenses directly related to the school enrollment. Enter the amount of such interest paid in Schedule Y, line 8. This deduction is only allowed if not claiming the same expenses in line 5 of Schedule Y, Student Loan Interest Deduction.

Line 9. Commuter Deduction

A deduction is allowed for certain amounts paid by an individual for tolls paid for through a FastLane account or for weekly or monthly transit commuter passes for MBTA transit or commuter rail, not including amounts reimbursed or otherwise deductible. In the case of a single person or a married person filing a separate return or a head of household filing a separate return, this deduction applies

only to the portion of such expended amount that exceeds \$150, and the total amount deducted cannot exceed \$750. In the case of a married couple filing a joint return, this deduction applies only to the portion of such amount expended by each individual that exceeds \$150, and the total amount deducted cannot exceed \$750 for each individual. Also, one spouse cannot transfer his or her excess deduction to the other spouse; separate worksheets must be completed to calculate the deduction. See TIR 04-25 for additional information. Complete the worksheet below to calculate the commuter deduction.

**Schedule Y, Line 9 Worksheet —
Commuter Deduction**

1. Enter amount paid for tolls through a FastLane account _____
2. Enter amount paid for weekly or monthly transit commuter passes for MBTA transit or commuter rail. (do not include amounts reimbursed or otherwise deductible) _____
3. Add lines 1 and 2. If \$150 or less, you do not qualify for this deduction. Omit remainder of this worksheet. Otherwise, complete lines 4 through 6. _____
4. Enter \$150 _____
5. Subtract line 4 from line 3. _____
6. Enter the lesser of line 5 or \$750 here and on Schedule Y, line 9. _____

Schedule Z

Other Credits

Be sure to enclose with Form 1.

Line 1. Part 1 Credits

► **Lead Paint:** If you incurred expenses for covering or removing lead paint on residential premises in Massachusetts, you may claim a credit for expenses up to \$1,500 for each residential unit. The basic rules are explained on Massachusetts Schedule LP, Credit for Removing or Covering Lead Paint on Residential Premises. If you qualify for the credit, complete Schedule LP and fill in the appropriate oval in Part 1.

► **Economic Opportunity Area Credit:** Massachusetts allows a credit equal to 5% of the cost of qualifying property purchased for business use within an Economic Opportunity Area (EOA). If you qualify for the credit, complete Schedule EOA and fill in the appropriate oval in Part 1.

► **Full Employment Credit:** Every employer who participates in the Full Employment Program and continues to employ a participant for at least one full month after any Full Employment Program subsidy for that participant has expired may claim

the Full Employment Credit. A qualified employer may claim a credit equal to \$100 per month of eligible employment per participant, with a maximum credit of \$1,200 per participant. Qualified participants and employers are those who participate in the Full Employment Program under the rules of the Department of Transitional Assistance (DTA). A five-year carryover of any unused credit is allowed. If you qualify for this credit, complete Massachusetts Schedule FEC, Full Employment Credit, and fill in the appropriate oval in Part 1.

► **Septic Credit:** An owner of residential property located in Massachusetts who occupies the property as his or her principal residence is allowed a credit of a maximum of \$1,500 per taxable year for expenses incurred to comply with the sewer system requirements of Title V as promulgated by the Department of Environmental Protection or to connect to a municipal sewer system pursuant to a federal court order, administrative consent order, state court order, consent decree or similar mandate. The amount of the credit is 40% of the cost, up to \$15,000, for design and construction expenses for repair or replacement of a failed cesspool or septic system. The maximum aggregate amount of the credit is \$6,000. A five-year carryover of any unused credit is allowed. See TIRs 97-12, 98-8, 99-5, 99-20 and DOR Directive 01-6 for more information. If you qualify for this credit, complete Massachusetts Schedule SC, Septic Credit, and fill in the appropriate oval in Part 1.

► **Brownfields Credit:** Taxpayers are allowed a credit for amounts expended to rehabilitate contaminated property owned or leased for business purposes and located within an economically distressed area. In general, the credit is 25% or 50% of certain environmental response and removal costs incurred between August 1, 1998, and January 1, 2007, provided that the taxpayer commences and diligently pursues an environmental response action before August 5, 2003. The credit that may be taken in any taxable year is limited to 50% of the taxpayer's tax liability. A five-year carryforward of unused credit is allowed, provided the taxpayer continues to maintain the remedies required by law. For more information, see TIRs 99-13 and 00-9.

► **Low-Income Housing Credit:** A low-income housing credit is available to individual taxpayers. The Department of Housing and Community Development will allocate the low-income housing credit from a pool of available credits granted under section 42 of the Internal Revenue Code among qualified low-income housing projects. A taxpayer allocated a federal low-income housing credit may also be eligible for a state credit based on the credit amount allocated to a low-income

housing project that the taxpayer owns. A five-year carryforward of unused credit is allowed. See TIR 99-19 for more information. If you qualify for the credit, fill in the appropriate oval in Part 1.

Enter the total amount of all credits claimed in Part 1 in Schedule Z, line 1 and complete lines 2 and 3.

Line 2. Part 2 Credits for Residents and Part-Year Residents Only

► **Income Tax Paid to Another State:** If any of the income reported on this return is subject to taxation in another state or jurisdiction and you have filed a return and paid taxes in the other state or jurisdiction, complete the Schedule Z, line 2 worksheet on the next page and fill in the appropriate oval in Part 2. Do not include taxes paid to the U.S. government. (This credit does not apply to city or local taxes.) You are allowed to claim a credit for taxes paid to the following jurisdictions: (a) other states in the U.S.; (b) any territory or dependency of the U.S. (including Puerto Rico, the Virgin Islands, Guam, the District of Columbia); or (c) the Dominion of Canada or any of its provinces (less any U.S. credit amount allowable from U.S. Form 1116).

The total credit which you calculate on this worksheet is the smaller of the amount of taxes due to other jurisdictions (net of certain adjustments) or the portion of your Massachusetts tax due on your gross income that is taxed in such other jurisdictions.

Credit is not given for a property tax due to another jurisdiction on account of capital stock or property. This does not refer to a tax on gain or income from the sale of capital stock or property, as included on Schedule B or D. Credit is also not given for any interest and penalties paid on a tax due to another jurisdiction.

You must complete separate worksheets if you had 5.3% and interest income (other than interest from Massachusetts banks), dividends or capital gain income taxed by another jurisdiction. If you use this worksheet to calculate a credit for interest income (other than interest from Massachusetts banks), dividends or capital gain income, substitute interest income (other than interest from Massachusetts banks), dividends or capital gain income for 5.3% income in line 1. You must also substitute Schedule B, line 7 (interest and dividend income) and Schedule B, line 13 (taxable 12% capital gains) or Schedule D, line 12, (gross long-term capital gains and losses), but not less than "0," for Form 1, line 10 in line 2 of the worksheet, and the total of Form 1, line 20 multiplied by .053 (tax on interest and dividend income) and Form 1, line 23 (12% tax) or line 24 (tax on long-term capital gains) for Form 1, line 19 in line 4 of the worksheet.

- When using this worksheet to calculate credit for interest income (other than interest from Massachusetts banks), dividends or capital gain income, enter in line 1 such income taxed in another jurisdiction calculated as if it was earned in Massachusetts.
- If you choose to pay the optional 5.85% tax rate, substitute .0585 for .053 in line 4 of the worksheet.

Note: Be sure to enter the two-letter state or jurisdictional postal code for each state or jurisdiction for which you are taking the credit. Visit the United States Postal Service's website at www.usps.com and click on "Service Guides" for a list of these codes.

**Schedule Z, Line 2 Worksheet —
Income Tax Paid to Another Jurisdiction**

Note: If you have income other than from Form 1, line 10 taxed by other jurisdictions, see instructions.

- Enter the total 5.3% income included in Form 1, line 10 on which you paid taxes to another jurisdiction.
- Enter the total of Form 1, line 10 and the total Massachusetts bank interest or the interest exemption amount, whichever is smaller, from Form 1, line 5a or line 5b.
- Divide line 1 by line 2.
- Multiply Form 1, line 19 by .053.
- Enter any Limited Income Credit from Form 1, line 28.
- Subtract line 5 from line 4.
- Multiply line 6 by line 3.
- Enter the total tax paid to other jurisdictions on income also reported on this return unless the tax was paid to Canada. If the tax was paid to Canada, the amount reported in this line must be reduced by the amount claimed as a foreign tax credit on U.S. Form 1040, line 46. Credit is only allowable for amount of tax paid.
- Enter the smaller of lines 7 or 8 here and on Schedule Z, line 2.

Energy: If you had expenditures for certain renewable energy source items, such as equipment which uses or transmits solar or wind energy to heat, cool, or provide hot water for your principal residence in Massachusetts, you may qualify for a credit. Massachusetts does not allow a credit for expenditures on items such as: insulation, storm or thermal windows or doors, caulking, weatherstripping, heat pumps (air and water), wood burning stoves or furnaces, and costs for energy conservation. If you qualify for the credit, complete Schedule EC, Residential Energy Credit, and fill in the appropriate oval in Part 2.

Enter the total amount of the credits claimed in Part 2 in Schedule Z, line 2. Then, add line 1 and line 2 and enter the result in Schedule Z, line 3 and in Form 1, line 29.

Schedule E, Part I

Note: If showing a loss, be sure to mark over the "X" in the box to the left.

Rental, Royalty and REMIC Income or Loss

Line 1a. Rental and Royalty Income or Loss

Enter total rental and royalty income or loss included in U.S. Form 1040, Schedule E, Part I, line 26 and U.S. Schedule E, Part V, line 40.

Line 1b. Real Estate Mortgage Investment Conduit (REMIC) Income or Loss

Enter total Real Estate Mortgage Investment Conduit (REMIC) residual income or loss from U.S. Schedule E, Part IV, line 39.

Line 2. Massachusetts Differences

Enter and explain any differences between total rental, royalty and REMIC income on the U.S. return and the same type of income on your Massachusetts return. Possible differences include trust provisions, deductible royalties from approved U.S. energy conservation patents, passive losses, and "bonus" depreciation as described below. Explain the differences in the space provided or enclose an additional sheet if necessary.

Trust Provisions

Enter any rental, royalty or REMIC income or loss shown on your U.S. return that is taxed on a Massachusetts Fiduciary Return, Form 2.

Deductible Royalties from U.S. Energy Conservation Patents

Enter any income you received from certain U.S. patents that are approved by the Massachusetts Division of Energy Resources as being useful for energy conservation or for alternative energy development. For more information, contact the Division of Energy Resources by calling (617) 727-4732. If such approved patent income is other than royalty income, use the applicable schedule and explain.

Passive Losses

As a result of differences in U.S. and Massachusetts rules in 1987, the calculations you made for passive losses on your 1987 U.S. and Massachusetts returns may have differed. Differences in amounts reported in 1987 for U.S. and Massachusetts tax purposes should be adjusted when the property is disposed of or the deduction is used up. In addition, passive losses allowed for Massachusetts tax purposes in 1987, but carried over for U.S.

tax purposes, cannot be used again for Massachusetts tax purposes when such carryover losses are eventually allowed for U.S. tax purposes.

To the extent there are applicable adjustments for Massachusetts differences, taxpayers must calculate allowable losses on a pro forma U.S. Form 8582, Passive Activity Loss Limitations.

Note: Same-sex joint filers should use Federal Form 8582 to recalculate their loss limitations as though they were filing a joint federal return. See TIR 04-17 for more information.

"Bonus" Depreciation

Massachusetts depreciation has been decoupled from the federal "bonus" depreciation law. Massachusetts does not adopt the special first-year depreciation allowance for certain property placed in service during the period beginning September 11, 2001 and ending December 31, 2004. The federal changes made in 2003 to IRC sec. 168(k) (Pub. L. 108-27), including extending the time period for acquisition of qualified property, increasing the depreciation allowance to 50% of the adjusted basis of the qualified property, and increasing the limitations on depreciation for luxury vehicles, are not, therefore, adopted in Massachusetts. For more information, see TIR 03-25, Depreciable Business Assets; Modifications for Decoupling from Federal Bonus Depreciation.

Line 4. Abandoned Building Renovation Deduction

In line 4 enter 10% of the costs of renovating a qualifying abandoned building in an Economic Opportunity Area. For further information, contact the Massachusetts Office of Business Development by calling (617) 973-8600.

Line 5. Total Rental, Royalty and REMIC Income or Loss for Massachusetts

Subtract line 4 from line 3. Remember to subtract losses when calculating the total. This figure should be added to any amount(s) in Schedule E, Part II, line 8 and/or Part III, line 11 and the total entered on Form 1, line 7.

Schedule E, Part II

Note: If showing a loss, be sure to mark over the "X" in the box to the left.

Income or Loss From Partnerships and S Corporations

Line 1. Partnership and S Corporation Income or Loss

Enter your total partnership and S corporation income or loss from your U.S. Form 1040, Schedule E, Part II, line 32.

Line 2. Massachusetts Differences

Enter and explain any differences between total partnership and S corporation income on the U.S. return and the same type of income on your Massachusetts return. Explain the differences in the space provided or enclose an additional sheet if necessary. Refer back to Schedule E, Part I, line 2 instructions for further guidance. If you use information from Massachusetts Schedule 3K-1 and/or SK-1, take care not to duplicate adjustments already made for differences in U.S. and Massachusetts tax treatments.

Line 4. Abandoned Building Renovation Deduction

Enter 10% of the costs of renovating a qualifying abandoned building in an Economic Opportunity Area. For further information, refer to the instructions for Schedule E, Part I, line 4.

Line 6. Interest (other than from Massachusetts banks) and Dividends

Enter interest (other than from Massachusetts banks) and dividends from trade or business activity(ies) if included in line 5 from partnerships and S corporations. This income must be reported in Massachusetts Schedule B, line 3. This information should be provided by the S corporation or partnership.

Line 7. Interest from Massachusetts Banks

Enter interest from Massachusetts banks from trade or business activity(ies) if included in line 5. This income must be reported on Form 1, line 5a. This information should be provided by the S corporation or partnership.

Line 8. Total Income or Loss from Partnerships and S Corporations

Subtract the total of lines 6 and 7 from line 5. Remember to subtract losses when calculating the total. This figure should be added to any amount(s) in Schedule E, Part I, line 5 and/or Part III, line 11 and the total entered on Form 1, line 7.

Schedule E, Part III

Note: If showing a loss, be sure to mark over the "X" in the box to the left.

Income or Loss From Grantor-Type Trusts and Non-Massachusetts Estates and Trusts

Line 1. Estate and Trust Income or Loss

Enter your total estate and trust income or loss from your U.S. Schedule E, Part III, line 37.

Line 2. Massachusetts Differences

Enter and explain any differences between estate and trust income or loss on the U.S. return and the same type of income on your Massachusetts return. Explain the differences in the space provided or enclose an additional sheet if necessary. See explanation in Schedule E, Part I, line 2.

Line 4. Abandoned Building Renovation Deduction

Enter 10% of the costs of renovating a qualifying abandoned building in an Economic Opportunity Area. For further information, refer to the instructions for Schedule E, Part I, line 4.

Line 6. Estate or Nongrantor-Type Trust Income

Enter estate or nongrantor-type trust income taxed directly on your Massachusetts Fiduciary Return, Form 2, if included in line 5. If you do not know this amount, check either your U.S. Schedule K-1 or contact your trustee or other fiduciary.

Line 8. Interest (other than from Massachusetts banks) and Dividends

Enter interest (other than from Massachusetts banks) and dividends if included in line 7 and enter on Massachusetts Schedule B, line 3.

Line 9. Adjustment of 5.3% Income

Enter the total of interest from Massachusetts banks if included in line 7. This income must be reported on Form 1, line 5a. Enter the total of pension and annuity income if included in line 7. This income must be reported on Form 1, line 4.

Line 11. Income or Loss from Grantor-Type and Non-Massachusetts Estates and Trusts

Subtract line 10 from line 7. Remember to subtract losses when calculating the total. This figure should be added to any amount(s) in Schedule E, Part I, line 5 and/or Part II, line 8 and the total entered on Form 1, line 7.

Schedule B

Note: If showing a loss, be sure to mark over the "X" in the box to the left.

Interest, Dividends and Certain Capital Gains and Losses

You must file Massachusetts Schedule B if you had:

- ▶ dividend income in excess of \$1,500;
- ▶ any interest income other than from Massachusetts banks taxed at 5.3%;
- ▶ short-term capital gains or losses;
- ▶ carryover short-term losses from prior years;
- ▶ long-term gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes;
- ▶ gains or losses from the sale, exchange or involuntary conversion of property used in a trade or business;
- ▶ net long-term capital gains and losses; or
- ▶ excess exemptions.

Collectibles are defined as any capital asset that is a collectible within the meaning of Internal Revenue Code section 408(m), as amended and in effect for the taxable year, including works of art, rugs, antiques, metals, gems, stamps, alcoholic beverages, certain coins, and any other items treated as collectibles for federal tax purposes.

- ▶ You need not file Massachusetts Schedule B if all interest income you had was from Massachusetts banks (reportable in Form 1, line 5a), and your gross dividend income was \$1,500 or less (dividend income of \$1,500 or less is reportable on Form 1, line 20), and you have no short-term capital gains or losses, long-term gains on collectibles and pre-1996 installment sales, gains or losses from the sale, exchange or involuntary conversion of property used in a trade or business, allowable deductions from your trade or business, carryover short-term losses from prior years, net long-term capital gains or losses, or excess exemptions.
- ▶ You must complete Massachusetts Schedule B if your interest or dividend income includes: dividends taxed directly to trusts or estates on a Massachusetts Fiduciary Return, Form 2; distributions that are returns of capital; or exempt portions of any interest or dividends from a mutual fund or dividends from current earnings of a corporate trust that are taxed directly on a Massachusetts Corporate Trust Return, Form 3F.

Part 1. Interest and Dividend Income

Line 1. Total Interest Income

Enter your total interest income from your U.S. Form 1040 or 1040A, lines 8a and 8b, U.S. Form 1040EZ, line 2, or U.S. Telefile Tax Record, item C.

Line 2. Total Ordinary Dividends

Enter your total ordinary dividends from your U.S. Schedule B, Part II, line 6 (Form 1040) or U.S. Schedule 1, Part II, line 6 (Form 1040A). If you did not file U.S. Schedule B or U.S. Schedule 1, enter the amount from U.S. Form 1040 or 1040A, line 9a.

Line 3. Other Interest and Dividends

Enter the following amounts and their sources (enclose additional statement if more space is necessary):

- ▶ Interest from obligations of other states and their political subdivisions (including your share, if any, from a partnership, an S corporation and a grantor-type trust or non-Massachusetts trust). Do not include exempt interest already included in line 1;
- ▶ Taxable distributions from Massachusetts S corporations not reported in Schedule B, line 2. Distributions in excess of the Massachusetts accumulated adjustments account are dividends to the extent of the corporation's Massachusetts accumulated earnings and profits. For more information, see Regulation 830 CMR 62.17A.1;
- ▶ Interest and dividends from a partnership, S corporation, grantor-type trust, or non-Massachusetts estate or trust from Massachusetts Schedule E. Generally, portfolio interest and dividend income from partnerships and S corporations should already be included in the Schedule B, line 1 and line 2 amounts;
- ▶ Interest from a trade or business that is reported on Massachusetts Schedule C, line 32; or
- ▶ Interest or dividends from a mutual fund, if such distributions are not included in line 1 or line 2. See line 6.

Lines 5 and 6

Enter only amounts related to income that you have already included in lines 1, 2, and 3.

Line 5. Total Interest from Massachusetts Banks

Enter the total interest included in Form 1, line 5a (prior to the exemption amount being subtracted) only if it has been included in lines 1 or 3 of this schedule.

Line 6. Other Interest and Dividends to Be Excluded

Enter the total interest and dividends from the following sources (enclose an additional statement, if necessary):

- ▶ Interest on U.S. debt obligations. Enter interest received on U.S. Treasury bills, notes and bonds, savings bonds or other obligations of the United States, including its territories or dependencies. Such interest is tax-exempt in Massachusetts. For further information concerning exempt obligations of the United States, see TIR 89-8;

▶ Interest and dividends taxed directly to Massachusetts estates and trusts. Enter the interest and dividends that are taxed directly to a Massachusetts estate or trust (reportable on a Massachusetts Fiduciary Return, Form 2);

- ▶ Any distribution which is a return of capital included in total gross dividends, line 2;
- ▶ Any interest or dividends from obligations of the Commonwealth of Massachusetts or its political subdivisions held by you;
- ▶ Any exempt portion of interest or dividends from a mutual fund included in lines 1, 2 or 3 of this schedule. Enter only the exempt portion of interest or dividends derived from obligations of the U.S. government or the Commonwealth of Massachusetts or its political subdivisions;
- ▶ Any dividends from current earnings of a corporate trust only if such entity is taxed directly on a Massachusetts Corporate Trust Return, Massachusetts Form 3F; or
- ▶ Any interest on pre-retirement distributions from state and municipal contributory pension plans.

Do not enter in line 6 either of the following:

- ▶ Dividends from the earnings and profits accumulated prior to January 1, 1971 by any corporate trust which was not taxed directly by Massachusetts in prior years, even though such an entity is taxed directly now (obtain from the entity the taxable status of dividends paid to you); or
- ▶ Dividends from any corporate trust which is not taxed directly by Massachusetts. Such entities include: those not doing business in Massachusetts; regulated investment companies or real estate investment trusts (both as defined under the U.S. Internal Revenue Code, Sections 851 and 856); or holding companies (as defined in Massachusetts General Laws, Chapter 62, section 8).

Line 8. Allowable Deductions from Your Trade or Business

Enter the amount from Massachusetts Schedule C-2, line 8 if you qualify for an excess trade or business deduction. Generally, taxpayers may not use excess 5.3% deductions to offset other income. However, where the taxpayer files a Massachusetts Schedule C or Schedule E, Massachusetts law allows such offsets if the following requirements are met: the excess 5.3% deductions must be adjusted gross income deductions allowed under MGL Ch. 62, sec. 2(d); and these excess deductions may only be used to offset other income which is effectively connected with the active conduct of a trade or business or any other income allowed under IRC, sec. 469(d)(1)(B) to offset losses from passive activities.

Line 9. Subtotal Interest and Dividend Income

Subtract line 8 from line 7. If you have no short-term capital gains or losses, net long-term capital gains or losses, carryover short-term losses from prior years, long-term gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes, gains or losses from the sale, exchange or involuntary conversion of property used in a trade or business and held for one year or less, allowable deductions from your trade or business, or excess exemptions, omit lines 10 through 37. Enter the amount from line 9 in line 38 of Schedule B and on Form 1, line 20, and omit lines 39 and 40 of Schedule B. Otherwise, complete Parts 2, 3 and 4.

Part 2. Short-Term Capital Gains and Losses and Long-Term Gains on Collectibles and Pre-1996 Installment Sales

If there are any differences between U.S. and Massachusetts amounts reported in lines 10, 11, 12, 16 and 17, be sure to enter the Massachusetts amount. Possible differences include:

- ▶ Short-term capital gains taxed directly to Massachusetts estates and trusts (reportable on a Massachusetts Fiduciary Return, Form 2);
- ▶ Upon the sale of stock of an S corporation, the federal basis must be modified according to Massachusetts Income Tax Regulation, 830 CMR 62.17A.1; and
- ▶ Massachusetts has adopted basis adjustment rules to take into account differences between Massachusetts and federal tax laws. For more information regarding basis adjustment rules, see TIR 88-7.

Line 10. Short-Term Capital Gains

Enter the gross short-term capital gains included in U.S. Schedule D, lines 1, 2, 4 and 5, column (f).

Line 11. Long-Term Capital Gains on Collectibles and Pre-1996 Installment Sales

Enter the amount of long-term capital gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes, from Massachusetts Schedule D, line 11.

Line 12. Gain on Sale of Business Property

Enter from U.S. Form 4797 the amount of gain from the sale, exchange or involuntary conversion of property used in a trade or business and held for one year or less.

Line 14. Allowable Deductions from Your Trade or Business

Enter the amount from Massachusetts Schedule C-2, line 11 if you qualify for an excess trade or business deduction. Generally, taxpayers may not use excess 5.3% deductions to offset other income. However, where the taxpayer files a Massachusetts Schedule C or Schedule E, Massachusetts law allows such offsets if the following requirements are met: the excess 5.3% deductions must be adjusted gross income deductions allowed under MGL Ch. 62, sec. 2(d); and these excess deductions may only be used to offset other income which is effectively connected with the active conduct of a trade or business or any other income allowed under IRC, sec. 469(d)(1)(B) to offset losses from passive activities.

Line 16. Short-Term Capital Losses

Enter the gross short-term capital losses included in U.S. Schedule D, lines 1, 2, 4 and 5, column (f).

Line 17. Loss on Sale of Business Property

Enter from U.S. Form 4797 the amount of loss from the sale, exchange or involuntary conversion of property used in a trade or business and held for one year or less.

Line 18. Prior Years Short-Term Unused Losses

You may use short-term losses accumulated in the previous taxable years beginning after 1981 in the computation of short-term gain or loss for the current year. Enter here the amount from your 2003 Massachusetts Schedule B, line 40.

Line 19. Subtotal Interest and Dividends and Certain Capital Gains and Losses

Combine lines 15 through 18. If "0" or greater, omit lines 20 through 23 and enter the amount from line 19 in line 24. If less than "0," complete line 20.

Line 20. Short-Term Losses Applied Against Interest and Dividends

Enter the smaller of line 9 or line 19 (considered as a positive amount). Not more than \$2,000.

Line 21. Available Short-Term Losses

Combine lines 19 and 20. This amount should be "0" or less. If line 21 is less than "0," go to line 22. If line 21 is "0," omit lines 22 through 28 and go to Part 3.

If Schedule B, line 21 is a loss and Schedule D, line 12 is a loss, omit line 22, enter the amount from line 21 in line 23 and line 40, omit lines 24 through 28 and complete Parts 3 and 4.

Line 22. Short-Term Losses Applied Against Long-Term Gains

If Schedule B, line 21 is a loss and Schedule D, line 12 is greater than "0," enter the smaller of Schedule B, line 21 (considered as a positive amount) or Schedule D, line 12 in Schedule B, line 22 and in Schedule D, line 13.

Line 23. Short-Term Losses for Carryover in 2005

Combine line 21 and line 22 and enter the result in line 23 and in line 40, omit lines 24 through 28 and complete Part 3 and Part 4.

Line 24. Short-Term Gains and Long-Term Gains on Collectibles

Enter the amount from Schedule B, line 19. If Schedule D, line 12 is "0" or greater, omit line 25 and enter the amount from line 24 in line 26. If Schedule D, line 12 is a loss, go to Schedule B, line 25.

Line 25. Long-Term Losses Applied Against Short-Term Gains

If Schedule B, line 24 is greater than "0," and Schedule D, line 12 is a loss, enter the smaller of Schedule B, line 24 or Schedule D, line 12 (considered as a positive amount) in Schedule B, line 25 and in Schedule D, line 13.

Line 27. Long-Term Gains Deduction

Complete only if lines 11 and 26 are greater than "0." If there is no entry in line 11, enter "0." If line 11 shows a gain, enter 50% of line 11 minus 50% of losses in lines 16, 17, 18 and 25, but not less than "0."

Example: Jack has a long-term capital gain on collectibles of \$1,000 entered in line 11 and line 15. He does not have any other interest income (other than interest from Massachusetts banks) and dividend income. Jack also has a short-term capital loss of \$100 entered in line 16 and a prior year short-term unused loss of \$200 entered in line 18. Jack enters \$350 in line 27: **\$500 (50% of \$1,000) minus \$150 (50% of \$300) = \$350.**

Part 3. Adjusted Gross Interest, Dividends Short-Term Capital Gains and Long-Term Gains on Collectibles

Line 31. Subtotal Interest and Dividends

If Schedule D, line 14 is "0" or greater, omit Schedule B, line 32 and enter the amount from Schedule B, line 31 in Schedule B, line 33. If Schedule D, line 14 is a loss, go to Schedule B, line 32.

Line 32. Long-Term Losses Applied Against Interest and Dividends

If Schedule B, line 31 is a positive amount and Schedule D, line 14 is a loss, complete the Long-Term Capital Losses Applied Against Interest and Dividends Worksheet for Schedule B, Line 32 and Schedule D, Line 15. When completing the worksheet, be sure to enter all losses as a positive amount.

Part 4. Taxable Interest, Dividends and Certain Capital Gains

Line 36. Excess Exemptions

Enter the amount from line 5 of the Excess Exemption Worksheet. Complete only if single, head of household or married filing a joint return and Form 1, line 18 is greater than Form 1, line 17.

Long-Term Capital Losses Applied Against Interest and Dividends Worksheet for Schedule B, Line 32 and Schedule D, Line 15. Complete only if Schedule B, line 31 is a positive amount and Schedule D, line 14 is a loss. Enter all losses as positive amounts.

1. Enter amount from Schedule B, line 29 _____
2. Enter the lesser of line 1 or \$2,000 _____
3. Enter the amount from Schedule B, line 30 _____
4. Subtract line 3 from line 2. If "0" or less omit the remainder of worksheet. Otherwise, complete lines 5 and 6 _____
5. Enter any loss from Schedule D, line 14 as a positive amount. Otherwise, enter "0" _____
6. If line 4 is smaller than or equal to line 5, enter line 4 here and in Schedule B, line 32 and in Schedule D, line 15. If line 4 is larger than line 5, enter line 5 here and in Schedule B, line 32 and in Schedule D, line 15. _____

Schedule D

Note: If showing a loss, be sure to mark over the “X” in the box to the left.

Long-Term Capital Gains and Losses Excluding Collectibles

You must complete Massachusetts Schedule D if you had long-term gains or losses from the sale or exchange of capital assets or from similar transactions which are granted capital gain or loss treatment on your U.S. return, or if you had capital gain distributions. If you did not file U.S. Schedule D but are reporting capital gain distributions on U.S. Form 1040, line 13 or 1040A, line 10, you must complete Massachusetts Schedule D (see line 5 instructions). Include gains from all property, wherever located. Long-term capital gains are gains on the sale or exchange of capital assets that have been held for more than one year on the date of the sale or exchange. Long-term capital losses are losses on the sale or exchange of capital assets that have been held for more than one year on the date of the sale or exchange.

The law defines “capital gain income” as gain from the sale or exchange of a capital asset. The definition of “capital asset” includes: (1) an asset which is a capital asset under IRC sec. 1221, or (2) property that is used in a trade or business within the meaning of IRC sec. 1231(b) without regard to the holding period as defined in said sec. 1231(b).

Differences

Significant differences between the U.S. and Massachusetts capital gain provisions are:

- ▶ IRC sec. 1244 losses reported as ordinary losses on your U.S. return must be reported on Massachusetts Schedule D;
 - ▶ If you made a federal election under § 3181 of the Tax Relief Act of 1997 to recognize gain on the deemed sale of a capital asset held on January 1, 2001, Massachusetts does not follow the federal rules at § 311 for determining the basis of the asset. See TIR 02-3. If you sold a capital asset in 2004 for which you made a federal § 311 election, the Massachusetts initial basis will not be the federal basis. The Massachusetts initial basis will be determined as of the date the asset was first acquired;
 - ▶ Upon the sale of stock of an S corporation, the federal basis must be modified according to Massachusetts Income Tax Regulation, 830 CMR 62.17A.1; and
 - ▶ Massachusetts has adopted basis adjustment rules to take into account differences between Massachusetts and federal tax laws. For more information regarding basis adjustment rules, see TIR 88-7.
- Net ordinary losses that are itemized deductions on U.S. Schedule A are not allowable.

Installment Sales

If a sale was treated as an installment sale for U.S. income tax purposes, it may be treated the same way on your Massachusetts income tax return. Gains from pre-1996 installment sales are classified as either capital gains or ordinary income under the Massachusetts law in effect on the date the sale or exchange took place.

Gains from pre-1996 installment sales that are classified as capital gains should be reported as 12% income on Massachusetts Schedule B. If the asset was held for more than one year when it was sold, the gain will be eligible for a 50% long-term deduction. Gains from pre-1996 installment sales that are classified as capital gains included on Massachusetts Schedule D, line 3 should be reported on Massachusetts Schedule D, line 11 (“Long-term gains on collectibles and pre-1996 installment sales”). The amount of such gain is then reported on Massachusetts Schedule B, Part 2, line 11.

Gains from pre-1996 installment sales classified as ordinary income and that are included on Massachusetts Schedule D, line 3 should be reported on Massachusetts Schedule D, line 9 (“Differences”). The amount of such gain classified as ordinary income should then be reported on Form 1, line 9 (“Other income”) and included on Schedule X, line 4 and identified as “2004 gain from pre-1996 installment sale.”

Note: If you are reporting capital gains on installment sales that occurred during January 1, 1996 through December 31, 2001, do **not** file Schedule D. Instead, you must file Schedule D-IS, Installment Sales. If you are reporting an installment sale occurring on or after January 1, 2002, report those gains on Schedule D. Schedule D-IS can be obtained on DOR’s website at www.mass.gov/dor.

If you wish to report a sale on your Massachusetts return as an installment sale, you must apply in writing to the Department of Revenue’s Installment Sales Unit. The Commissioner of Revenue must approve your application to report the sale on the installment basis in Massachusetts before you file your return, and appropriate security must be posted. An explanatory statement must be enclosed with each return for the life of the installment sale. For further information contact the Installment Sales Unit at (617) 887-6950.

Long-Term Capital Gains and Losses, Excluding Collectibles

Line 1. Long-Term Capital Gains and Losses

Enter the gain or loss included in U.S. Schedule D, line 8, column f.

Line 2. Additional Long-Term Capital Gains and Losses

Enter the gain or loss included in U.S. Schedule D, line 9, column f.

Line 3. Gain from Sales of Business Property and Other Long-Term Gains and Losses

Enter the gain or loss included in U.S. Schedule D, line 11, column f.

Line 4. Net Long-Term Gain or Loss from Partnerships, S Corporations, Estates and Trusts

Enter the gain or loss included in U.S. Schedule D, line 12, column f.

Line 5. Capital Gain Distributions

If you did not file U.S. Schedule D, enter the capital gain distributions reported to you by a mutual fund or real estate investment trust included in the amount from U.S. Form 1040, line 13 or 1040A, line 10.

If you did file a U.S. Schedule D, enter the capital gain distributions reported to you by a mutual fund or real estate investment trust included in U.S. Schedule D, line 13, column f.

Line 6. Massachusetts Long-Term Capital Gains and Losses Included in U.S. Form 4797, Part II

Enter amounts included in U.S. Form 4797, Part II treated as capital gains or losses for Massachusetts purposes (not included in lines 1 through 5 above). These include ordinary gains from the sale of Section 1231 property, recapture amounts under Sections 1245, 1250 and 1255, Section 1244 losses and the loss on the sale, exchange or involuntary conversion of property used in a trade or business.

Line 7. Carryover Losses from Previous Years

If you have a carryover loss from a prior year, enter in line 7 the total amount of carryover losses from your 2003 Schedule D, line 22.

Line 9. Differences

Enter any differences between the gains or losses reportable for Massachusetts tax purposes and the U.S. gains or losses reported in Massachusetts Schedule D, lines 1 through 7. Differences include:

- ▶ Net gains or losses taxed to a Massachusetts estate or trust. Enter in line 9 only gains or losses of a Massachusetts estate or trust that are taxed directly on the Massachusetts Fiduciary Return, Form 2, if you are the beneficiary and if you included the amounts on Schedule D, line 4. Do not

enter gains or losses from any grantor-type trust or from an estate or trust that is not subject to taxation in Massachusetts;

- ▶ Pre-1996 installment sales classified as ordinary income for Massachusetts purposes;
- ▶ Long-term capital gains or losses from transactions reported as installment sales for U.S. income tax purposes but not for Massachusetts; and
- ▶ Massachusetts has adopted basis adjustment rules to take into account differences between Massachusetts and federal tax laws.

Line 10. Adjusted Capital Gains and Losses

Exclude/subtract line 9 from line 8 and enter the result in line 10.

- ▶ If line 9 is a loss, add loss as a positive number to the amount recorded in line 8. See the following examples:

| Schedule D | | | | |
|------------|---------|---------|---------|--------|
| Line | ex. A | ex. B | ex. C | ex. D |
| 8 | \$1,000 | \$1,000 | \$ 700* | \$700* |
| 9 | 500 | 300* | 500 | 500* |
| 10 | 500 | 1,300 | 1,200* | 200* |

*denotes loss

- ▶ If in line 9 you entered amounts which increase the amounts reported from U.S. to Massachusetts, for example, a long-term gain reported as installment sales for U.S. tax purposes but not for Massachusetts, add the amount in line 9 to the amount in line 8.

Line 11. Long-Term Gains on Collectibles and Pre-1996 Installment Sales

Enter in line 11 the amount of long-term gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes that are included in line 10.

Long-term gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes are taxed at the 12% rate and should be entered on Schedule B, line 11.

Collectibles are defined as any capital asset that is a collectible within the meaning of Internal Revenue Code section 408(m), as amended and in effect for the taxable year, including works of art, rugs, antiques, metals, gems, stamps, alcoholic beverages, certain coins, and any other items treated as collectibles for federal tax purposes.

Line 12. Subtotal

Subtract line 11 from line 10 and enter the result in line 12.

If Schedule D, line 12 is a loss and Schedule B, line 21 is less than "0," omit Schedule D, lines 13 through 15, enter the amount from Schedule D, line 12 in Schedule D, line 16, omit Schedule D, lines 17 through 21 and enter the amount from Schedule D, line 16 in Schedule D, line 22, and enter "0" on Form 1, line 24.

If Schedule D, line 12 is a gain and Schedule B, line 21 is a loss, go to Schedule D, line 13.

If Schedule D, line 12 is a loss and Schedule B, line 24 is "0" or greater, go to Schedule D, line 13.

If Schedule D, line 12 is a gain, and Schedule B, line 24 is "0" or greater, omit Schedule D, lines 13 through 15 and enter the amount from Schedule D, line 12 in Schedule D, line 16.

Line 13. Capital Losses Applied Against Capital Gains

If Schedule D, line 12 is a positive amount and Schedule B, line 21 is a loss, enter the smaller of Schedule D, line 12 or Schedule B, line 21 (considered as a positive amount) in Schedule D, line 13 and in Schedule B, line 22.

If Schedule D, line 12 is a loss and Schedule B, line 24 is a positive amount, enter the smaller of Schedule D, line 12 (considered as a positive amount) or Schedule B, line 24 in Schedule D, line 13 and in Schedule B, line 25.

Line 14. Subtotal

If line 12 is greater than "0," subtract line 13 from line 12. If line 12 is less than "0," combine lines 12 and 13.

If Schedule D, line 14 is a loss and Schedule B, line 24 is "0" or greater and Schedule B, line 31 is a positive amount, go to Schedule D, line 15.

If Schedule D, line 14 is a loss, and Schedule B, line 21 is "0" or less, omit Schedule D, line 15, enter the amount from Schedule D, line 14 in Schedule D, line 16, omit Schedule D, lines 17 through 21 and enter the amount from Schedule D, line 16 in Schedule D, line 22, and enter "0" on Form 1, line 24.

Line 15. Long-Term Capital Losses Applied Against Interest and Dividends

If Schedule D, line 14 is a loss, and Schedule B, line 24 is "0" or greater and Schedule B, line 31 is a positive amount, complete the Long-Term Capital Losses Applied Against Interest and Dividends Worksheet for Schedule B, Line 32 and Schedule D, Line 15.

Line 16. Subtotal

Combine line 14 and line 15. If Schedule D, line 16 is "0," enter "0" in lines 17 through 20 and omit lines 21 and 22. If Schedule D, line 16 is a loss, omit lines 17 through 21 and enter the amount from line 16 in line 22.

Line 17. Allowable Deductions From Your Trade or Business

Generally, taxpayers may not use excess 5.3% trade or business deductions to offset other income. However, where the taxpayer files a Massachusetts Schedule C or Schedule E, Massachusetts law allows such offsets if the following requirements are met: the excess 5.3% deductions must be adjusted gross income deductions allowed under MGL Ch. 62, sec. 2(d); and these excess deductions may only be used to offset other income which is effectively connected with the active conduct of a trade of business or any other income allowed under IRC, sec. 469(d)(1)(B) to offset losses from passive activities. Enclose Schedule C-2 with your return.

Enter in line 17 the amount from Schedule C-2, line 14.

Line 19. Excess Exemptions

Enter in line 19 the amount from line 8 of the Excess Exemption Worksheet.

Line 21. Tax On Long-Term Capital Gains

Multiply line 20 by .053 (5.3%) and enter the result here and in Form 1, line 24.

Note: If choosing the optional 5.85% tax rate, multiply line 20 by .0585 and enter the result here and in Form 1, line 24.

Line 22. Available Losses for Carryover

Enter the amount from Schedule D, line 16, only if it is a loss.

Schedule C

Note: If showing a loss, be sure to mark over the “X” in the box to the left.

Substituting U.S. Schedules C or C-EZ

If you are substituting U.S. Schedule C or Schedule C-EZ for Massachusetts Schedule C and there are no differences between the amounts reported on U.S. Schedule C or Schedule C-EZ and amounts that would be reported on Massachusetts Schedule C, write “No Massachusetts Differences” on the top of U.S. Schedule C or Schedule C-EZ.

Profit or Loss from Business or Profession

Massachusetts Schedule C is provided to report income and deductions from each business or profession operated as a sole proprietorship.

If your business deductions, excluding the Abandoned Building Renovation Deduction, exceed Schedule C income and any other income taxable at the 5.3% rate, such excess deductions may be subtracted from the other income that is effectively connected with the active conduct of your trade or business and any other income allowed under IRC Section 469(d)(1)(B) to offset losses from passive activities. To compute the excess trade or business deductions use Massachusetts Schedule C-2. This form is available by visiting www.mass.gov/dor, or you may have one mailed to you by calling (617) 887-MDOR.

Registration Information

In the space provided, describe the business or professional activity that provided your principal source of income reported on line 1. If you owned more than one business, you must complete a separate Schedule C for each business. Give the general field or activity and the type of product or service.

Employer Identification Number

You need an Employer Identification number (EIN) only if you had a Keogh plan or were required to file an employment, excise, estate, trust, or alcohol, tobacco and firearms tax return. If you do not have an EIN, leave the line blank. Do **not** enter your Social Security number.

Small Business Energy Exemption

If you are claiming the small business energy exemption from the sales tax on purchases of taxable energy or heating fuel during 2004, you must have five or fewer employees. You must enter the number of your employees in the space provided.

Accounting Method

If you filed a return on the accrual basis last year, your return for this year must be on the same basis. If a taxpayer requesting permission to change an accounting method for Massachusetts purposes is eligible for an automatic change of accounting method federally, and has correctly followed the most recently issued federal revenue procedure for requesting an automatic change, then the taxpayer should file his/her annual return using the new method and write at the top, “Automatic Change of Accounting Method — filed in compliance with DOR Directive 02-13.” The taxpayer should enclose a copy of federal Form 3115, together with any required statements. See DOR Directive 02-13 for further information.

Material Participation

Indicate if you materially participated in the operation of this business during 2004. If you did not materially participate and have a loss from this business, see line 33 for further instructions.

Line 1a. Gross Receipts or Sales

In the boxes provided, enter gross receipts or sales from your business. Be sure to include on this line amounts you received in your trade or business as shown on Form 1099-MISC, Miscellaneous Income. If the nature of your business is such that you have gross or other income that is interest (other than from Massachusetts banks) and dividend income, exclude this income from lines 1 and 4 on Massachusetts Schedule C and include it in line 32 and in Schedule B, line 3. Examples of interest (other than from Massachusetts banks) and dividend income are interest received on loans, notes receivable or charge accounts that you accept in the ordinary course of business, and dividends on stocks received in payment for goods and services. Capital gains from the sale or exchange of assets used in your business are not reported on Schedule C. Use U.S. Form 4797 and report the amount in Form 1, Schedule B and/or Schedule D. You must also exclude from Schedule C any income and expenses that pertain to activities for yourself as distinguished from those performed for your customers. Such income must be reported by class of income in Schedules B and D. Personal expenses are not deductible. If you received Form W-2 and the “Statutory employee” box in item 13 of that form was checked, report your income and expenses related to that income on Schedule C. Enter your statutory employee in-

come from box 1 of Form W-2 on line 1 of Schedule C and fill in the oval. Statutory employees include full-time life insurance agents, certain agent or commission drivers and traveling salespersons and certain homeworkers. If you had both self-employment income and statutory employee income, do not combine these amounts on a single Schedule C. In this case, you must file two Schedules C.

Line 4. Other Income

If you received bartering income, you must report the fair market value of goods or services received in payment for your goods and services in line 4. Do not include interest income (other than from Massachusetts banks) and dividends here (see line 32).

Line 7. Bad Debts From Sales or Services

Include debts and partial debts from sales or services that were included in income and are definitely known to be worthless. If you later collect a debt that you deducted as a bad debt, include it as income in the year collected.

Note: Cash method taxpayers cannot take a bad debt deduction unless the amount was previously included in income.

Line 11. Depreciation and Section 179 Deduction

Massachusetts adopts the current federal rules at section 179 for expensing certain depreciable business assets. For property placed in service in tax years beginning on or after January 1, 2004, the maximum section 179 expensing allowance is \$102,000.

Massachusetts depreciation has been decoupled from the federal “bonus” depreciation law. Massachusetts does not adopt the special first-year depreciation allowance for certain property placed in service during the period beginning September 11, 2001 and ending December 31, 2004. The federal changes made in 2003 to IRC sec. 168(k) (Pub. L. 108-27), including extending the time period for acquisition of qualified property, increasing the depreciation allowance to 50% of the adjusted basis of the qualified property, and increasing the limitations on depreciation for luxury vehicles, are not, therefore, adopted in Massachusetts. For more information, see TIR 03-25, Depreciable Business Assets; Modifications for Decoupling from Federal Bonus Depreciation.

Line 17. Pension and Profit-Sharing Plans

Enter your deduction for contributions to a pension, profit-sharing or annuity plan, or plans for the benefit of your employees. If the plan includes you as a self-employed person, do not include contributions made as an employer on your behalf. See TIR 02-18 for more information.

Line 23. Meals and Entertainment

Line 23a. Enter your total business meal and entertainment expenses. Include meals while traveling away from home for business. Instead of the actual cost of your meals while traveling away from home, you may use the standard meal allowance. Business meal expenses are deductible only if they are (a) directly related to or associated with the conduct of your trade or business, (b) not lavish or extravagant and (c) incurred while you or your employee is present at the meal. Club dues are not allowed as a business deduction.

Line 23b. Generally, you may deduct only 50% of your business meal and entertainment expenses, including meals incurred while traveling away from home on business. However, you may fully deduct meals and entertainment furnished or reimbursed to an employee if you properly treat the expense as wages subject to withholding. You may also fully deduct meals and entertainment provided to a nonemployee to the extent the expenses are includible in the gross income of that person and reported on Form 1099-MISC. Figure how much of the amount on line 23a is subject to the 50% limit. Then, enter 50% of that amount on line 23b. This amount should be subtracted from the amount in line 23a. Enter the result in line 23 of Massachusetts Schedule C.

Line 30. Abandoned Building Renovation Deduction

Massachusetts allows businesses to deduct 10% of the costs incurred in renovating certain buildings located in an Economic Opportunity Area (EOA). The buildings must be designated as abandoned by the Economic Assistance Coordinating Council. The renovation deduction may be taken in addition to any other deduction for which the renovation costs may qualify.

For more information, contact the Massachusetts Office of Business Development, 10 Park Plaza, Suite 3720, Boston, MA 02116, or call (617) 973-8600.

In line 30 enter 10% of the costs of renovating a qualifying abandoned building.

Line 33. If You Have a Loss

Fill in the oval in line 33a if all of your investment is at risk. Enter your loss from line 31 on Form 1, line 6 **unless** you answered "no" to the question on material participation on the front of Schedule C. If you answered "no" to this question, complete a pro forma copy of U.S. Form 8582 that reflects only income being reported on your Massachusetts return. Enter in Massachusetts Schedule C, line 31 your allowable loss calculated on Form 8582.

Fill in the oval in line 33b if only some of your investment is at risk. To determine the amount of your allowable loss, complete a pro forma copy of U.S. Form 6198 that reflects only income being reported on your Massachusetts return. Enter the amount calculated on U.S. Form 6198 in line 31 unless you answered "no" to the question on material participation on the front of Schedule C. In this case, your loss is further limited. Use the amounts calculated on your pro forma U.S. Form 6198 to complete a pro forma U.S. Form 8582. If your at-risk amount is "0" or less, enter "0" in line 31.

Senior Circuit Breaker Tax Credit

What Is It?

For tax years beginning on or after January 1, 2001, senior citizens in Massachusetts may be eligible to claim a refundable credit on their state income taxes for the real estate taxes they paid on the Massachusetts residential property they own or rent and which they occupy as their principal residence. The maximum credit allowed is \$820 for the tax year beginning January 1, 2004. See TIR 04-32 for more information.

Eligible taxpayers who own their property may claim a credit equal to the amount by which their property tax payments in tax year 2004 (excluding any exemptions and/or abatements), including water and sewer debt charges, exceed 10% of their "total income" for the same current tax year. Taxpayers residing in communities that do not include water and sewer debt service in their property tax assessments may claim, in addition to their property tax payments, 50% of the water and sewer use charges actually paid during the tax year when figuring their credit.

Renters may claim a credit in the amount by which 25% of their annual rental payment is more than 10% of their total income.

For purposes of the tax credit, a taxpayer's "total income" includes taxable income as well as exempt income such as Social Security, Treasury bills and public pensions. For a complete list of what constitutes "total income," see TIR 01-19.

Who Is Eligible for the Credit?

To be eligible for the credit for the 2004 tax year, a taxpayer must be 65 years of age or older before January 1, 2005 (for joint filers, it is sufficient if one taxpayer is 65 years of age or older), must own or rent residential property in Massachusetts and occupy the property as his or her principal residence, and must not be the dependent of another taxpayer. The taxpayer's total income cannot exceed \$44,000 for a single filer who is not the head of a household, \$55,000 for a head of household, or \$66,000 for taxpayers filing jointly. No credit is allowed for a married taxpayer unless a joint return is filed. Moreover, the assessed valuation of the real estate cannot exceed \$441,000.

No credit is allowed if the taxpayer claims the "married filing separate" status, receives a federal or state rent subsidy, rents from a tax-exempt entity, or is the dependent of another taxpayer.

Is the Tax Credit Considered Income?

Tax credits received by eligible taxpayers are not considered income for the purpose of obtaining eligibility or benefits under other means-tested assistance programs including food, medical, housing, energy and educational assistance programs.

How Does a Taxpayer Claim the Credit?

Taxpayers who are eligible for the tax credit in the 2004 tax year can claim the credit by submitting a completed Schedule CB, Circuit Breaker Credit, with their 2004 state income tax return. Eligible taxpayers who do not normally file a state income tax return may obtain a refund by filing a return with Schedule CB. As with all claimed tax credits and deductions, the taxpayer must keep all pertinent records, receipts and other documentation supporting his or her claim for the credit.

Line 1. Living Quarters Status During 2004

Be sure to fill in the appropriate oval. If you were a renter in 2004 and you received any federal and/or state subsidy, or you rent from a tax-exempt entity, you do not qualify for the Circuit Breaker Credit.

Line 2. Assessed Value of Principal Residence as of January 1, 2004

Enter the amount of the assessed value of your principal residence as of January 1, 2004. If you own a multi-family home, mixed-use property, or more than one acre of land, only the assessed value of the principal residence, together with the land that immediately surrounds and is associated with that residence, not to exceed one acre, should be used. If the assessed value is over \$441,000, you do not qualify for the credit. Contact your local city or

town's assessors' office if you have any questions in determining the amount of the assessed value of your principal residence as of January 1, 2004.

Income Calculation

Qualifying income for the Circuit Breaker Credit (Schedule CB, lines 3 through 12) is the taxpayer's Massachusetts AGI as defined in MGL Ch. 62, sec. 2 increased by various amounts that may have been excluded or subtracted when originally calculating the taxpayer's Massachusetts AGI, less certain exemptions claimed by the taxpayer. Amounts added back to Massachusetts AGI in computing qualifying income include income from Social Security, retirement, pension or annuities, cash public assistance, tax-exempt interest and dividends, net capital losses, long-term capital losses, certain capital gains, income from a partnership or trust not otherwise included in the taxpayer's Massachusetts AGI, and gross receipts (for example, the return of capital or gifts) from any other source except the tax credit itself. The exemptions allowed which decrease the total income amount are those allowed for blindness, dependents and taxpayers who are at least age 65 by the end of the tax year.

Line 4. Total Social Security Benefits Received

Enter in line 4 the amount of Social Security benefits received in 2004. Social Security benefits include retirement, disability, dependent and survivorship.

Line 5. Pension, Annuities, IRA/Keogh Distributions Not Taxed on Your Massachusetts Tax Return

Enter in line 5 the amount of pension, annuities, IRA/Keogh distributions not taxed on your Massachusetts Form 1. See Form 1, line 4 instructions, Pension and Annuities, for a list of exempt items that must be included in Schedule CB, line 5 as part of total income for the purposes of calculating the Circuit Breaker Credit.

Line 6. Miscellaneous Income Including Cash Public Assistance

Enter the amount of miscellaneous income, including cash public assistance, received during 2004. This includes but is not limited to food stamps and welfare payments, disability income, gifts, sick pay and worker's compensation.

Line 12. Qualifying Income

Subtract line 11 from line 7. You do not qualify for the Circuit Breaker Credit if you are filing as "Single" and line 12 is greater than \$44,000; or if you are filing as "Head of household" and line 12 is greater than \$55,000; or if you are filing as "Married filing jointly" and line 12 is greater than \$66,000.

Credit Calculation

If you filled in the "Homeowner" oval in line 1, complete lines 13 through 20, if you filled in the "Renter" oval in line 1, go to line 21.

Line 13. Real Estate Taxes Paid in Calendar Year 2004 for Your Principal Residence

Enter the amount of real estate taxes paid in calendar year 2004. Be sure to include real estate tax payments made pursuant to the Community Preservation Act, the Cape Cod Open Space Land Acquisition Program and/or paid to a tax-levying district.

Note: Real estate taxes paid in a calendar or taxable year generally reflect taxes assessed for two different fiscal years. If a community collects taxes quarterly, a taxpayer may have made four payments during a calendar year. These payments are billed as due on the following dates: February 1, May 1, August 1, and November 1. If a community collects taxes semi-annually, a taxpayer may have made two payments during the calendar year. The first payment is billed as due on May 1 and the second as due on November 1, or thirty days after it is mailed, if the bill is mailed after October 1. If you own a multi-family home, mixed-use property, or your principal residence has a land area in excess of one acre, contact your local city or town's collector's office if you have any questions in determining the amount of real estate taxes paid in calendar year 2004 for your principal residence.

Line 14. Adjustments to Real Estate Taxes Paid

Enter the amount from line 4 of the Adjustments to Real Estate Taxes Paid Worksheet for Schedule CB, line 14, on page 2 of Schedule CB. Adjustments to real estate taxes paid include:

- ▶ Abatements granted by local assessors or earned through the Senior Work Program*;
- ▶ Exemptions granted by cities or towns to qualifying veterans, surviving spouses, blind persons and the elderly*;
- ▶ Interest charges assessed due to delinquent payments; and
- ▶ Betterments or special assessments levied upon the property.

*Do not exclude this amount if it was already reflected on your tax bill and you did not pay it.

Line 16. Water and Sewer Use Charges Paid in 2004

Contact your town official to determine if your community has elected to include water and sewer debt charges in the property tax assessment. Taxpayers residing in communities that do not include water and sewer debt charges in the property tax assessments may include 50% of the actual water and sewer use charges paid during the taxable year. If they have elected to include those charges in the property tax assessment, enter "0" in line 16. If they have not elected to include those charges, enter 50% of your actual water and sewer use charges paid in 2004 in line 16.

If you own a multi-family home, mixed-use property, or your principal residence has a land area in excess of one acre, see TIR 01-19 for information on how to prorate water and sewer use charges.

Line 20. Credit

Enter the lesser of line 19 or \$820 here and on Form 1, line 39.

Line 21. Rent Paid for Your Principal Residence in 2004

Enter in line 21a the total amount of rent paid for your principal residence in 2004. Divide that amount by 4 (25%) and enter the result in line 21. In the space provided, be sure to enter your landlord's name and address. If you received any federal and/or state rent subsidy, or you rent from a tax-exempt entity, you do not qualify for the Circuit Breaker Credit.

Line 24. Credit

Enter the lesser of line 23 or \$820 here and on Form 1, line 39.

Department of Revenue Resources

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What kind of help is available

The instructions in the Department of Revenue's tax forms should provide answers to most taxpayer questions. If you have questions about completing your Massachusetts tax form, you can call us at (617) 887-MDOR or toll-free in Massachusetts at 1-800-392-6089 Monday through Friday, between 8:45 a.m. and 5:00 p.m. DOR's website at www.mass.gov/dor is also a valuable resource for tax information 24 hours a day. Thousands of taxpayers use DOR's website to e-mail and receive prompt answers to their general tax inquiries. Interactive applications that allow taxpayers to check the status of their refunds and review their quarterly estimated tax payment histories are available through our website or by calling our main information lines listed above.

Where to get forms and publications



Most Massachusetts tax forms and publications are available via the DOR website. The address for the Department's website is www.mass.gov/dor.



To obtain Massachusetts forms and publications by phone, call the Department's main information lines at (617) 887-MDOR or toll-free in Massachusetts at 1-800-392-6089. Please note that many forms and publications are available 24 hours a day by calling the Department's automated forms request system at the numbers listed above.



During the income tax filing season, you can pick up Massachusetts personal income tax forms at your local library or at IRS district offices across the state.



Certain forms and publications can be obtained through DOR's Fax on Demand system. For a complete Fax on Demand menu, please call (617) 887-1900 using the handset and the keypad on your fax machine.

For help in one of the following specific areas

- ▶ Certificates of Good Standing (617) 887-6550
- ▶ Teletype (TTY) (617) 887-6140
- ▶ Vision-impaired taxpayers can contact DOR by calling one of the phone numbers listed above to receive assistance.
- ▶ Upon request, this publication is available in an alternative format. Please send your request to: Office of Affirmative Action, PO Box 9550, Boston, MA 02114-9550 or call (617) 626-3410.
- ▶ Installment Sales (617) 887-6950
- ▶ Small Business Workshop (617) 887-5660

To report allegations of suspected misconduct or impropriety involving Department of Revenue employees, call the Inspectional Services Division's Integrity Hot Line at 1-800-568-0085 or write to PO Box 9568, Boston, MA 02114-9568.

Massachusetts

Department of

Revenue

PO Box 7011

Boston, MA 02204

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MASSACHUSETTS



Dear Taxpayer,

The Department of Revenue (DOR) encourages you to file your state income tax return electronically this year. More than one million taxpayers took advantage of e-filing last year and received their refunds, on average, in three days – one of the fastest turnaround times in the country. E-filing is a safe and proven alternative, and DOR is committed to using technology to make filing your state income taxes easier than ever this year.

Whether you use Telefile, DOR-approved commercial software products or a tax preparer, the best way to guarantee a rapid refund is to e-file your state income tax return. Each e-file method is easy to use, secure and convenient. You will receive confirmation that your state income tax return was received. In addition to saving time, you will significantly reduce the chance of error. If you are due a refund, you may have it deposited directly into your bank account. In cases where a payment is required, funds can be directly debited from your bank account and scheduled for withdrawal as late as April 15, 2005. A number of software vendors also offer free e-filing for eligible taxpayers. Please visit our website, www.mass.gov/dor for details on the Massachusetts Free File Alliance.

If you use third party software and do not file a return electronically, you are required to submit the paper return with the required 2-Dimensional (2-D) bar coding. Returns submitted to DOR without the required 2-D bar codes will be rejected and returned to you for proper re-filing to avoid penalties. Please visit our website to learn more about 2-D bar coding and for a list of authorized software providers.

This year, we are also enhancing our online assistance. Now, you can use our website to check on the status of your tax refund, make an estimated income or regular tax payment through Web Services for Income, file an abatement/amended return, update your address and review your estimated tax payment history. You can also find information concerning the new commuter tax deduction for those who use the Turnpike and MBTA, the Massachusetts Turnpike Fuels Tax Refund Program and other frequently asked questions. There is a wealth of information available to you, and it's only a click away.

DOR is committed to making this tax season as efficient as possible. For information or assistance, please visit our website or call our Customer Service Bureau at (617) 887-MDOR or toll-free in Massachusetts at (800) 392-6089.

Sincerely,

A handwritten signature in black ink that reads "Alan LeBovidge". The signature is written in a cursive, flowing style.

Alan LeBovidge
Commissioner

Important Mailing Information!
When mailing a return generated from a 2-D software product, be sure to use one of the special 2-D PO boxes listed on page 3.