

Example Two: Retired Minister

Rev. William K. Green is a retired minister. He is 69-years old. He is married to Sarah J. Green. She is 65-years old and is also retired. For 2010, Rev. Green received \$15,000 in pension income, all of which was designated in advance by the Board of Pensions as a housing allowance. Rev. Green had housing expenses of \$13,000. The home's fair rental value is \$1,200 per month (including furnishings and utilities). Housing allowances for retired ministers are not taxable in computing federal income tax to the extent that they do not exceed the lesser of actual housing expenses or the annual fair rental value of the home (including furnishings and utilities). Retirement benefits, whether or not designated in advance as a housing allowance, are not subject to self-employment taxes.

Rev. Green received \$12,000 of Social Security benefits in 2010, and his wife received \$6,000. None of this income is taxable, however, because the Green's income is not enough to expose their Social Security benefits to tax.

In 2010, Rev. Green received \$2,000 from occasional guest preaching engagements. He incurred \$590 in expenses as a result of these activities (\$440 of travel expenses and \$150 of meal expenses). Refer to page 28 regarding the reporting of employee business expenses. Note that Rev. Green will pay self-employment tax on this income (see Schedule SE) since it represents compensation from active ministry.

The parts of Rev. and Mrs. Green's income tax return are explained in the order they are completed. They are illustrated in the order that Rev. Green will assemble the return to send it to the IRS.

Form 1099R from the Board of Pensions

The Board of Pensions completed Form 1099R for Rev. Green as follows:

Box 1. The \$15,000 pension income Rev. Green receives from the Board of Pensions.

Box 2b. Taxable amount not determined. The Board of Pensions designated in advance 100 percent of pension income as a housing allowance. It is not taxable to the extent that it does not exceed the lesser of actual housing expenses or the annual fair rental value of the home (including furnishings and utilities).

Box 7. Rev. Green's pension income is a normal distribution.

Schedule C-EZ (Form 1040)

Some of Rev. Green's entries on Schedule C-EZ are explained here.

Line 1. Rev. Green reports the \$2,000 from occasional guest preaching engagements.

Line 2. Rev. Green reports his expenses related to the line 1 amount. He drove 880 miles for business use of his car, in connection with guest preaching. Rev. Green used the standard business mileage rate to figure his car expense. He multiplied the standard mileage rate of 50 cents by 880 miles for a total of \$440. He also incurred \$75 (\$150 x 50% nondeductible) in meal expenses in connection with the guest preaching for total expenses of \$515. However, he cannot deduct the part of his expenses allocable to his tax-free parsonage allowance. He attaches the required statement, Attachment 1 (shown later) to his return showing that 76 percent (or \$391) of his business expenses are not deductible because they are allocable to that tax-free allowance. He subtracts the \$391 from the \$515 and enters the \$124 difference on line 2.

Line 3. He enters his net profit of \$1,876 both on line 3 and on Form 1040, line 12.

Lines 4 through 8b. Rev. Green fills out these lines to report information about his car.

TurboTax tips: Listed below are tips for ministers who use TurboTax to complete their returns. These tips should not be construed as an endorsement or recommendation of the TurboTax software.

TurboTax does not appear to calculate the nondeductible portion of the expenses, which should be allocated to the tax-free portion of the housing allowance. The taxpayer will need to adjust the expenses (as shown in Attachment 1) and input the reduced figure into the software.

Schedule SE (Form 1040)

After Rev. Green prepares Schedule C-EZ, he fills out Schedule SE (Form 1040). He reads the chart on page 1 of the schedule, which tells him he can use Section A (Short Schedule SE) to figure his self-employment tax. Ministers are not church employees under this definition. He fills out the following lines in Section A.

Line 2. Rev. Green attaches a statement (see Attachment 2, later) that calculates his net profit of \$1,485 and he enters that amount here.

Line 4. He multiplies the \$1,485 by .9235 to get his net earnings from self-employment (\$1,371).

Line 5. The amount on line 4 is less than \$106,800, so Rev. Green multiplies the amount on line 4 (\$1,371) by .153 to get his self-employment tax of \$210. He enters that amount here and on Form 1040, line 56.

Line 6. Rev. Green multiplies the amount on line 5 by .5 to get his deduction for one-half of self-employment tax of \$105. He enters that amount here and on Form 1040, line 27.

TurboTax tips: The software does not appear to reduce self-employment wages by the business expenses allocated to tax free income. The taxpayer will need to adjust net self-employment income (as shown in Attachment 2) and input the reduced figure into the software.

Schedule M (Form 1040)

For 2010, taxpayers should use Schedule M to figure the amount available for the Making Work Pay Credit. Rev. Green fills out Schedule M as explained here.

Line 1a. Rev. and Mrs. Green do not have wages of more than \$12,903 so they check “No.” Rev. Green computes his earned income using the earned income worksheet found in the instructions to Schedule M and enters his earned income of \$1,771 (\$1,876 from Schedule C-EZ less \$105 self-employment tax deduction from line 27 of Form 1040).

Line 2. He multiplies line 1a by 6.2%, which equals \$110, and enters this amount on line 2.

Line 3. Rev. Green enters \$800 (for married filing jointly).

Line 4. He enters \$110 which is the lesser of lines 2 or 3.

Line 5. Rev. Green enters the amount from Form 1040, line 38.

Line 6. He enters \$150,000 (for married filing jointly).

Line 7. Since the amount on line 5 is less than the amount on line 6, Rev. Green checks “No” and enters the amount from line 4 on line 9.

Line 9. Rev. Green enters \$110 from line 4.

Line 10. Rev. Green did not receive these types of payments so he responds “No” and enters zero on line 10.

Line 11. Rev. Green subtracts line 10 from line 9 and enters \$110 here and on Form 1040, line 63.

Schedule L (Form 1040)

For 2010, taxpayers taking the standard deduction should use Schedule L to increase the standard deduction by new motor vehicle taxes paid for certain vehicles purchased in 2009, or a net disaster loss. Since Rev. Green did not have these items, he does not complete Schedule L.

Form 1040

After Rev. Green prepares Schedule C-EZ and Schedule SE, he fills out Form 1040. Rev. Green files a joint return with his wife. First he fills out the address area and completes the appropriate lines for his filing status and exemptions. Then he fills out the rest of the form as follows:

Line 12. He reports his net profit of \$1,876 from Schedule C-EZ, line 3.

Line 16a and 16b. Rev. Green reports his total pension income of \$15,000 on line 16a. He reports the taxable amount (\$2,000) as computed on Attachment 1 (shown later) on line 16b.

Line 20a and 20b. Since none of Rev. Green’s Social Security benefits are taxable, he does not report any amounts on line 20a or 20b.

Line 27. He enters \$105, one-half of his SE tax from Schedule SE, line 6.

Line 37. Subtract line 36 from line 22. This is his adjusted gross income and he carries this amount forward to line 38.

Line 39a. He checks the boxes indicating that he and his wife were born before January 2, 1946, and enters “2” in the “total” box.

Line 40. Rev. Green enters his standard deduction of \$13,600, which takes into consideration the fact he and his wife were born before January 2, 1946.

Line 42. He multiplies the number of exemptions claimed (2 from Line 6d) by \$3,650 and enters an exemption amount of \$7,300 on line 42.

Line 43. Rev. Green has no taxable income.

Line 56. He enters the self-employment tax from Schedule SE, line 5.

Line 61. Rev. Green did not have any income tax withheld from his pension.

Line 63. He enters the \$110 Make Work Pay Credit from Schedule M, line 11.

Line 76. Amount Rev. Green owes to the IRS.

CORRECTED (if checked)

| | | | | | |
|---|--|--|---|--|--|
| PAYER'S name, street address, city, state, and ZIP code The Board of Pensions of the Presbyterian Church (USA) 2000 Market Street Philadelphia, PA 19103-3298 1-800-773-7752 | | 1 Gross distribution \$ 15,000.00 | OMB No. 1545-0119 2010 Form 1099-R | | Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. Copy B Report this income on your federal tax return. If this form shows federal income tax withheld in box 4, attach this copy to your return. |
| PAYER'S federal identification number 23-1352040 | | 2a Taxable amount \$ | 2b Taxable amount not determined <input checked="" type="checkbox"/> Total distribution <input type="checkbox"/> | | |
| PAYER'S federal identification number 23-1352040 | | RECIPIENT'S identification number 202-20-2002 | 3 Capital gain (included in box 2a) \$ | 4 Federal income tax withheld \$ | This information is being furnished to the Internal Revenue Service. |
| RECIPIENT'S name William K. Green | | 5 Employee contributions /Designated Roth contributions or insurance premiums \$ | 6 Net unrealized appreciation in employer's securities \$ | | |
| Street address (including apt. no.) 787 Adams Street | | 7 Distribution code(s) 7 | IRA/SEP/SIMPLE <input type="checkbox"/> | 8 Other \$ % | |
| City, state, and ZIP code Anytown, NY 10002 | | 9a Your percentage of total distribution % | 9b Total employee contributions \$ | | |
| 1st year of desig. Roth contrib. | | 10 State tax withheld \$ \$ | 11 State/Payer's state no. | 12 State distribution \$ \$ | |
| Account number (see instructions) | | 13 Local tax withheld \$ \$ | 14 Name of locality | 15 Local distribution \$ \$ | |

Form **1099-R**

Department of the Treasury - Internal Revenue Service

**SCHEDULE C-EZ
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Name of proprietor

William K. Green

Net Profit From Business

(Sole Proprietorship)

▶ **Partnerships, joint ventures, etc., generally must file Form 1065 or 1065-B.**
▶ **Attach to Form 1040, 1040NR, or 1041.** ▶ **See instructions on page 2.**

OMB No. 1545-0074

2010

Attachment
Sequence No. **09A**

Social security number (SSN)

202-20-2002

Part I General Information

**You May Use
Schedule C-EZ
Instead of
Schedule C
Only If You:**

- Had business expenses of \$5,000 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as either a sole proprietor, qualified joint venture, or statutory employee.

And You:

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service

Minister

B Enter business code (see page 2)

▶ 8 1 3 0 0 0

C Business name. If no separate business name, leave blank.

D Enter your EIN (see page 2)

E Business address (including suite or room no.). Address not required if same as on page 1 of your tax return.

City, town or post office, state, and ZIP code

Part II Figure Your Net Profit

1 Gross receipts. Caution. See the instructions for Schedule C, line 1, and check the box if:

- This income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, or
- You are a member of a qualified joint venture reporting only rental real estate income not subject to self-employment tax.

} . . . ▶

1 2,000

2 Total expenses (see page 2). If more than \$5,000, you **must** use Schedule C

2 124 *

3 Net profit. Subtract line 2 from line 1. If less than zero, you **must** use Schedule C. Enter on both **Form 1040, line 12**, and **Schedule SE, line 2**, or on **Form 1040NR, line 13**. (If you checked the box on line 1, **do not** report the amount from line 3 on Schedule SE, line 2.) Estates and trusts, enter on **Form 1041, line 3**

3 1,876

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ 07/15/05

5 Of the total number of miles you drove your vehicle during 2010, enter the number of miles you used your vehicle for:

a Business 880 **b** Commuting (see page 2) 0 **c** Other 12,711

6 Was your vehicle available for personal use during off-duty hours? **Yes** **No**

7 Do you (or your spouse) have another vehicle available for personal use? **Yes** **No**

8a Do you have evidence to support your deduction? **Yes** **No**

b If "Yes," is the evidence written? **Yes** **No**

**SCHEDULE SE
(Form 1040)**

Self-Employment Tax

OMB No. 1545-0074

2010
Attachment
Sequence No. **17**

Department of the Treasury
Internal Revenue Service (99)

▶ **Attach to Form 1040 or Form 1040NR.**

▶ **See Instructions for Schedule SE (Form 1040).**

Name of person with **self-employment** income (as shown on Form 1040)

Social security number of person
with **self-employment** income ▶

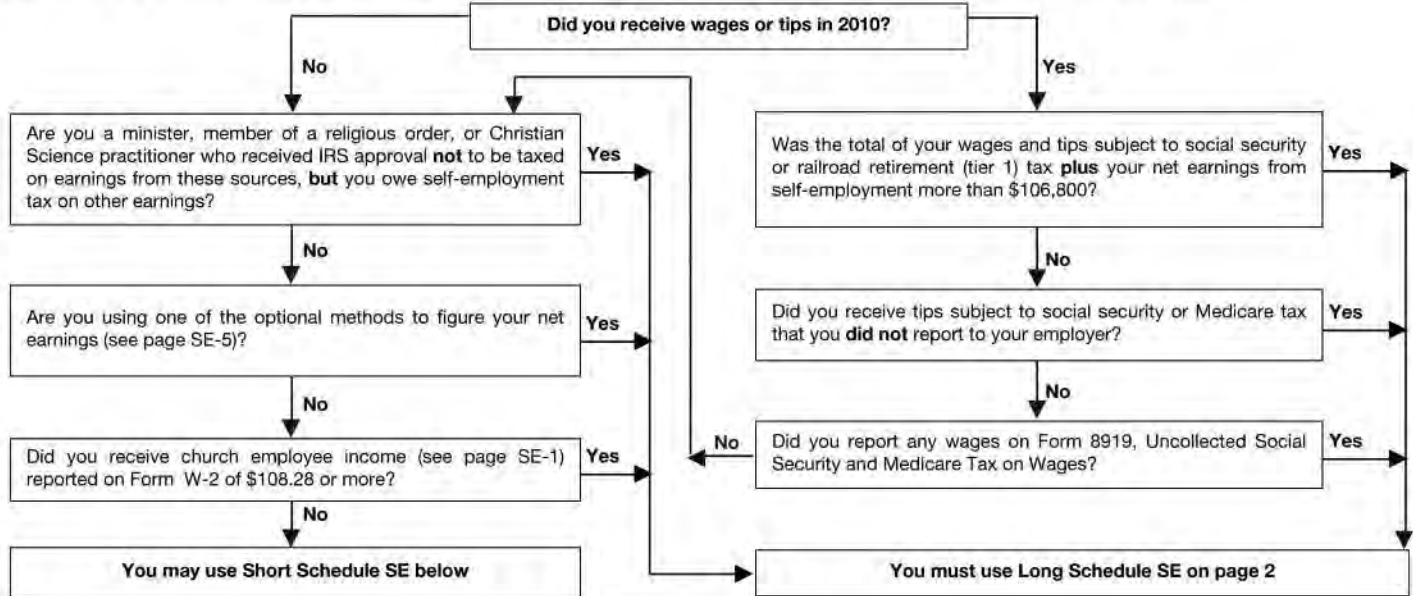
202-20-2002

William K. Green

Before you begin: To determine if you must file Schedule SE, see the instructions on page SE-1.

May I Use Short Schedule SE or Must I Use Long Schedule SE?

Note. Use this flowchart **only** if you must file Schedule SE. If unsure, see *Who Must File Schedule SE* on page SE-1.



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

| | | | |
|-----------|--|--------------|------------|
| 1a | Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A | | |
| b | If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 6b, or listed on Schedule K-1 (Form 1065), box 20, code Y | (|) |
| 2 | Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Ministers and members of religious orders, see page SE-1 for types of income to report on this line. See page SE-3 for other income to report | 1,485 | * |
| 3 | Combine lines 1a, 1b, and 2. Subtract from that total the amount on Form 1040, line 29, or Form 1040NR, line 29, and enter the result (see page SE-3) | 1,485 | |
| 4 | Multiply line 3 by 92.35% (.9235). If less than \$400, you do not owe self-employment tax; do not file this schedule unless you have an amount on line 1b ▶ | 1,371 | |
| 5 | Self-employment tax. If the amount on line 4 is: • \$106,800 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 56, or Form 1040NR, line 54 • More than \$106,800, multiply line 4 by 2.9% (.029). Then, add \$13,243.20 to the result. Enter the total here and on Form 1040, line 56, or Form 1040NR, line 54 | 210 | |
| 6 | Deduction for one-half of self-employment tax. Multiply line 5 by 50% (.50). Enter the result here and on Form 1040, line 27, or Form 1040NR, line 27 | | |
| | | 6 | 105 |

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 11358Z

Schedule SE (Form 1040) 2010

* See statement attached.

SCHEDULE M
(Form 1040A or 1040)

Making Work Pay Credit

OMB No. 1545-0074

2010
Attachment
Sequence No. **166**

Department of the Treasury
Internal Revenue Service (99)

▶ **Attach to Form 1040A or 1040.**

▶ **See separate instructions.**

Name(s) shown on return

William K. & Sarah J. Green

Your social security number

202-20-2002



To take the making work pay credit, you must include your social security number (if filing a joint return, the number of either you or your spouse) on your tax return. A social security number does not include an identification number issued by the IRS. Only the Social Security Administration issues social security numbers.



You cannot take the making work pay credit if you can be claimed as someone else's dependent or if you are a nonresident alien.

Important: Check the "No" box on line 1a and see the instructions if:

- (a) You have a net loss from a business,
- (b) You received a taxable scholarship or fellowship grant not reported on a Form W-2,
- (c) Your wages include pay for work performed while an inmate in a penal institution,
- (d) You received a pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan, or
- (e) You are filing Form 2555 or 2555-EZ.

1a Do you (and your spouse if filing jointly) have 2010 wages of more than \$6,451 (\$12,903 if married filing jointly)?
 Yes. Skip lines 1a through 3. Enter \$400 (\$800 if married filing jointly) on line 4 and go to line 5.
 No. Enter your earned income (see instructions) **1a** 1,771

b Nontaxable combat pay included on line 1a (see instructions) **1b**

2 Multiply line 1a by 6.2% (.062) **2** 110

3 Enter \$400 (\$800 if married filing jointly) **3** 800

4 Enter the **smaller** of line 2 or line 3 (unless you checked "Yes" on line 1a) **4** 110

5 Enter the amount from Form 1040, line 38*, or Form 1040A, line 22 **5** 3,771

6 Enter \$75,000 (\$150,000 if married filing jointly) **6** 150,000

7 Is the amount on line 5 more than the amount on line 6?
 No. Skip line 8. Enter the amount from line 4 on line 9 below.
 Yes. Subtract line 6 from line 5 **7**

8 Multiply line 7 by 2% (.02) **8**

9 Subtract line 8 from line 4. If zero or less, enter -0- **9** 110

10 Did you (or your spouse, if filing jointly) receive an economic recovery payment in **2010**? You may have received this payment in 2010 if you did not receive an economic recovery payment in 2009 but you received social security benefits, supplemental security income, railroad retirement benefits, or veterans disability compensation or pension benefits in November 2008, December 2008, or January 2009 (see instructions).
 No. Enter -0- on line 10 and go to line 11.
 Yes. Enter the total of the payments you (and your spouse, if filing jointly) received in **2010**. Do not enter more than \$250 (\$500 if married filing jointly) **10** 0

11 Making work pay credit. Subtract line 10 from line 9. If zero or less, enter -0-. Enter the result here and on Form 1040, line 63; or Form 1040A, line 40 **11** 110

*If you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico, see instructions.

Name, Address, and SSN

See separate instructions.

PRINCE LEARLY
For the year Jan. 1-Dec. 31, 2010, or other tax year beginning , 2010, ending , 20
Your first name and initial Last name
William K. Green
If a joint return, spouse's first name and initial Last name
Sarah J. Green
Home address (number and street). If you have a P.O. box, see instructions. Apt. no.
787 Adams Street
City, town or post office, state, and ZIP code. If you have a foreign address, see instructions.
Anytown, New York 10002

OMB No. 1545-0074
Your social security number
2 0 2 | 2 0 | 2 0 0 2
Spouse's social security number
3 0 3 | 3 0 | 3 0 0 3
Make sure the SSN(s) above and on line 6c are correct.

Presidential Election Campaign

Check here if you, or your spouse if filing jointly, want \$3 to go to this fund You Spouse

Filing Status

Check only one box.

- 1 Single
2 Married filing jointly (even if only one had income)
3 Married filing separately. Enter spouse's SSN above and full name here.
4 Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here.
5 Qualifying widow(er) with dependent child

Exemptions

6a Yourself. If someone can claim you as a dependent, do not check box 6a
b Spouse
c Dependents:
(1) First name Last name (2) Dependent's social security number (3) Dependent's relationship to you (4) if child under age 17 qualifying for child tax credit (see page 15)
Boxes checked on 6a and 6b 2
No. of children on 6c who:
lived with you
did not live with you due to divorce or separation (see instructions)
Dependents on 6c not entered above
Add numbers on lines above 2

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a W-2, see page 20.

Enclose, but do not attach, any payment. Also, please use Form 1040-V.

Table with 3 columns: Description, Amount, Total. Rows include Wages (7), Taxable interest (8a), Tax-exempt interest (8b), Ordinary dividends (9a), Qualified dividends (9b), Taxable refunds (10), Alimony received (11), Business income (12), Capital gain (13), Other gains (14), IRA distributions (15a), Pensions (16a), Rental real estate (17), Farm income (18), Unemployment (19), Social security (20a), Other income (21), Total income (22).

Adjusted Gross Income

Table with 3 columns: Description, Amount, Total. Rows include Educator expenses (23), Business expenses (24), Health savings (25), Moving expenses (26), Self-employment tax (27), Self-employed SEP (28), Self-employed health (29), Penalty on early withdrawal (30), Alimony paid (31a), IRA deduction (32), Student loan interest (33), Tuition and fees (34), Domestic production (35), Adjusted gross income (36), Total adjusted gross income (37).

Attachment 2. Computation of expenses, allocable to tax-free ministerial income, that are nondeductible.

| <u>% of Nondeductible Expenses</u> | | | | |
|--|-----------|-----------------|------------------|------------------|
| | | <u>Taxable</u> | <u>Tax-Free</u> | <u>Total</u> |
| Parsonage allowance: | | | | |
| Ministerial retirement benefits designated as housing allowance | \$ 15,000 | | | |
| Actual expenses | \$ 13,000 | | | |
| Fair rental value of home (including furnishings and utilities)(\$1,200 x 12) | \$ 14,400 | | | |
| | | | | |
| Taxable portion of allowance (excess of amount designated & paid over lesser of actual expenses or fair rental value) | \$ 2,000 | \$ 2,000 | | \$ 2,000 |
| Tax-free portion of allowance (lesser of amount designated, actual expenses or fair rental value) | | | \$ 13,000 | 13,000 |
| Gross income from occasional guest preaching engagements | | 2,000 | | 2,000 |
| Ministerial Income | | <u>\$ 4,000</u> | <u>\$ 13,000</u> | <u>\$ 17,000</u> |
| % of nondeductible expenses: \$13,000/\$17,000 = 76% | | | | |

| <u>Schedule C-EZ Deduction Computation</u> | | | |
|--|--|--|---------------|
| Business use of car (880 miles driven x 50¢) | | | \$ 440 |
| Meal expenses (\$150 less 50% reduction) | | | <u>75</u> |
| Unadjusted Schedule C-EZ expenses | | | \$ 515 |
| Nondeductible part of expenses: \$515 X 76% | | | <u>(391)</u> |
| Schedule C-EZ deductions, line 2 | | | <u>\$ 124</u> |
| None of the other deductions claimed in the return are allocable to tax-free income. | | | |

Attachment 2. Computation of Net Earnings from Self-Employment

| <u>Computation for Schedule SE (Form 1040)</u> | | |
|---|--|-----------------|
| Gross income from Schedule C-EZ | | \$ 2,000 |
| Less: | | |
| Unadjusted Schedule C-EZ expenses | | <u>(515)</u> |
| Net Self Employment Income, Schedule SE, Line 2 | | <u>\$ 1,485</u> |