PAYROLL AND ESTIMATED TAX

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Land Grant University
Tax Education Foundation

LEARNING OBJECTIVES

After completing this session, participants will be able to do the following:

- ✔ Use Form W-4 to determine an employee's income tax withholding
- ✔ Calculate the withholding amount
- ✔ Calculate employment taxes
- ✔ Know when to deposit taxes
- ✔ Complete payroll reports
- ✔ Report payments to an independent contractor
- ✔ Know when a taxpayer must pay estimated tax
- ✔ Calculate the amount of estimated tax
- ✔ Understand the penalty for failure to pay or timely pay estimated tax
- ✔ Calculate the estimated tax penalty using the annualized income installment method

INTRODUCTION

The first part of this chapter explains the employer's tax withholding, deposit, and reporting requirements. It discusses the specific requirements that are applicable to paid time off (such as vacation and sick leave), reimbursed employee expenses, and fringe benefits, and it briefly reviews an employer's obligation to report payments made to nonemployees.

The second part of this chapter explains when a taxpayer with self-employment or other income must pay estimated tax. It discusses how to calculate the estimated tax payments, and it provides a comprehensive example of a taxpayer whose income varies during the year and uses the annualized income installment method to avoid a penalty on failure to timely make estimated tax payments.

PAYROLL Employers must withhold and deposit income tax, social security tax, and Medicare tax, and they must pay employment taxes and unemployment taxes.

Employers that pay wages must withhold federal and state income tax, social security tax, and Medicare tax from an employee's wages. They must also pay the employer's share of social security tax and Medicare tax, state unemployment tax, and federal unemployment tax (FUTA) on an employee's wages. Generally, the employer deposits the withheld state and federal income tax and both the employer and employee's shares of social security and Medicare taxes.

This section discusses the general tax withholding, deposit, and reporting requirements. It explains the specific requirements that are applicable to paid time off (such as vacation and sick leave), reimbursed employee expenses, and fringe benefits. Finally, this section briefly reviews an employer's obligation to report payments made to nonemployees.

Income Tax Withholding

Employers use Form W-4, Employee's Withholding Allowance Certificate, to determine the amount of federal income tax to withhold from an employee's wages.

Form W-4

Each employee must complete Form W-4 and specify his or her filing status and number of allowances. For tax years beginning after December 31, 2017, and before January 1, 2026, the Tax Cuts and Jobs Act of 2017 (TCJA), Pub. L. No. 115-97, suspends the deduction for personal exemptions, and the number of allowances claimed on Form W-4 is instead based on the following:

1. Whether the taxpayer will file as single, head of household, MFJ, or MFS
2. Whether the taxpayer has income from more than one job
3. What credits the taxpayer expects to claim for children and other dependents
4. What other credits the taxpayer expects to claim for the year
5. What deductions, adjustments, and nonwage income (e.g., as dividends or interest) the taxpayer expects to have for the year

Figure 7.1 shows the draft 2019 Form W-4. Employees can also use the new withholding calculator at www.irs.gov/individuals/irs-withholding-calculator. The fewer allowances that the employee enters on the Form W-4, the more tax that will be withheld from the employee's paycheck.

PRACTITIONER NOTE

Review Withholding

The TCJA increased the standard deduction, removed personal exemptions, increased the child tax credit, limited or discontinued certain deductions, and changed the tax rates and brackets. Because of these changes, employers should encourage their employees to check the accuracy of their withholding allowances.

FIGURE 7.1 Form W-4

Form **W-4**

Department of the Treasury
Internal Revenue Service

Employee's Withholding Allowance Certificate

▶ Give Form W-4 to your employer.
▶ Go to *www.irs.gov/FormW4* for instructions and the latest information.
▶ The amount of, or exemption from, withholding is subject to review by the IRS.

OMB No. 1545-0074

2019

1 Your first name and middle initial	Last name	2 **Your social security number**
Home address (number and street or rural route)	3 ☐ Single or married filing separately ☐ Married filing jointly ☐ Head of household	
City or town, state, and ZIP code	4 **If your last name differs from that shown on your social security card, check here. You must call 800-772-1213 for a replacement card.** ▶ ☐	

Before you begin:

- See the instructions at *www.irs.gov/FormW4* before completing this form. If you have a simple tax situation, you may be able to use the brief instructions on the back of this form.
- You also can use the calculator at *www.irs.gov/W4App* to complete your Form W-4.
- If you hold more than one job at a time (or are married filing jointly and both you and your spouse have jobs), complete lines 5, 6, and 7 **only** for the highest paying job in the household.

5	Enter the amount, if any, of nonwage income not subject to withholding, such as interest and dividends	5	$
6	Enter the amount, if any, of itemized and other deductions	6	$
7	Enter the amount, if any, of tax credits, such as the child tax credit	7	$
8	Complete this line *only* if you have multiple jobs at the same time or file as married filing jointly and both you and your spouse work; otherwise, leave it blank. Enter the total pay of all lower paying jobs	8	$
9	Additional amount, if any, you want withheld from each paycheck	9	$
10	I claim exemption from withholding for 2019, and I certify that I meet **both** of the following conditions for exemption. • Last year I had a right to a refund of **all** federal income tax withheld because I had **no** tax liability, **and** • This year I expect a refund of **all** federal income tax withheld because I expect to have **no** tax liability. If you meet both conditions, write "Exempt" here ▶	10	

Under penalties of perjury, I declare that I have examined this certificate and, to the best of my knowledge and belief, it is true, correct, and complete.

Employee's signature
(This form is not valid unless you sign it.) ▶ **Date** ▶

11 Employer's name and address (**Employer:** Complete boxes 11 and 13 if sending to IRS and complete boxes 11, 12, and 13 if sending to State Directory of New Hires.)	12 First date of employment	13 Employer identification number (EIN)

TIP

Use this form so that your employer can withhold the correct amount of income tax from your pay. ***See the instructions and worksheets before completing this form.*** *You can find the latest instructions and information at* www.irs.gov/FormW4. *You also can use the calculator at* www.irs.gov/W4App *to complete your Form W-4.*

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. Cat. No. 10220Q Form **W-4** (2019)

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Employees may not base their withholding amounts on a fixed dollar amount or percentage. However, an employee may specify a dollar amount to be withheld in addition to the amount of withholding calculated on Form W-4. If a new employee does not provide a completed Form W-4, the employer must withhold income tax as if the employee is single with no withholding allowances. Employees who do not need to change their withholding can still use the earlier version of Form W-4.

PRACTITIONER NOTE

Withholding Calculator

The Treasury Inspector General for Tax Administration (TIGTA) analyzed the 2018 withholding calculator and identified that, in certain situations, the amount of withholding suggested by the calculator results in a taxpayer unknowingly having more withholding than is necessary. For the weekly, biweekly, and semimonthly pay frequency, the calculator determines withholding using one less periodic payment than actual. For example, a taxpayer who is paid biweekly will generally have 26 pay periods in 2018. However, the withholding calculator is using 25 pay periods rather than 26 pay periods to determine the withholding amount and may result in overwithholding. IRS management indicates that they are considering revising the calculator later in 2018 or when the 2019 calculator is released [TIGTA, Tax Cuts and Jobs Act: Assessment of Implementation Planning Efforts (April 11, 2018)].

PRACTITIONER NOTE

Financial Information

Employees do not have to complete Form W-4 lines 5 through 8. If the employee does not want to give the employer this financial information, the Form W-4 instructions direct the employee to leave those lines blank and use the online calculator or Publication 505 to calculate the additional withholding to enter on line 9 or the reduction to withholding to enter on line 7.

Employees can use the worksheets in the Form W-4 instructions to help complete the form. **Figure 7.2** shows the deductions worksheet to complete line 6, and **Figure 7.3** shows the credit worksheet to complete line 7.

FIGURE 7.2 Deductions Worksheet

Deductions Worksheet ***(Keep for your records.)***

Note: Use this worksheet **only** if you plan to itemize deductions, claim certain adjustments to income, or are eligible to take additional standard deductions.

Deductions from income

1	Enter an estimate of your 2019 itemized deductions. These include qualifying home mortgage interest, charitable contributions, state and local taxes (up to $10,000), and medical expenses in excess of 10% of your income. See Pub. 505 for details	**1** $________
2	Enter: • $XX,XXX if you're married filing jointly or a qualifying widow(er); • $XX,XXX if you're head of household; or • $XX,XXX if you're single or married filing separately	**2** $________
3	**Subtract** line 2 from line 1. If zero or less, enter "-0-"	**3** $________
4	Enter an estimate of your 2019 other deductions	**4** $________
5	**Add** lines 3 and 4 and enter the total here and on line 6 of Form W-4	**5** $________

FIGURE 7.3 Credit Worksheet

Credit Worksheet ***(Keep for your records.)***

Note: Use this worksheet **only** if you plan to take income tax credits on your 2019 income tax return.

1	**Child tax credit.** (See Pub. 972 for more information.) Enter $2,000 for each qualifying child under age 17 if: • You're married filing jointly and your income is less than $XXX,XXX; or • You're single, married filing separately, or head of household and your income is less than $XXX,XXX	1 $________
2	**Credit for other dependents.** (See Pub. 972 for more information.) Enter $500 for each other eligible dependent if: • You're married filing jointly and your income is less than $XX,XXX; or • You're single, married filing separately, or head of household and your income is less than $XXX,XXX	2 $________
3	**Education tax credits.** (See Pub. 970 for more information.) Enter the estimated lifetime learning credit or American opportunity tax credit you expect for 2019	3 $________
4	**Child and dependent care credit.** (See Form 2441 and Pub. 503 for more information.) Enter: • Up to $1,050 each for no more than 2 children or qualifying dependent(s) if your income is less than $15,000. • Up to a maximum ranging from $630 to $1,020 each for no more than 2 children or qualifying dependent(s) if your income is over $15,000 and less than $43,000. See Form 2441 to figure the maximum credit available for your income per child or qualifying dependent. • Up to $600 each for no more than 2 children or qualifying dependent(s) if your income is over $43,000	4 $________
5	**Foreign tax credit.** (See Pub. 514 for more information.) Enter the estimated foreign tax credit you expect for 2019	5 $________
6	**Other credits.** If you're eligible to take other credits, see Worksheet 1-6 of Pub. 505 and enter the amount from that worksheet here. Make sure you don't claim credits on Worksheet 1-6 that you have claimed on lines 1 through 5 above	6 $________
7	**Add** lines 1 through 6 and enter the total here and on Form W-4, line 7	7 $________

Withholding Calculation

Employers should make their prior year Form W-4 data conform to the new withholding method for 2019. Employers can do this by keeping the number of withholding allowances and additional withholding the same as it is on prior year Forms W-4, and assume lines 5, 6, 7, and 8 are zero. The withholding tables and formulas are adjusted to take older Forms W-4 into account. Whenever employers hire new employees or existing employees change their withholding in 2019, they should use the new method to compute employee withholding.

Basic Withholding

Withholding for an employee whose 2019 Form W-4 has no entries on lines 5 through 10 will be the amount from the withholding tables (or alternative methods) in Publication 15 (Circular E), Employer's Tax Guide, or Publication 15-A, Employer's Supplemental Tax Guide, for the proper pay period, with 2 withholding allowances for single or MFS, and 3 withholding allowances for MFJ or head of household. This also is the basis for calculating withholding for employees whose Forms W-4 include entries on lines 5, 6, 7, 8, and 9.

Adjusting Withholding

Employers must use the entries on their employees' 2019 Forms W-4, lines 5, 6, 7, 8, and 9, to adjust their income tax withholding. An employer that uses the wage bracket method takes the following steps:

1. Divide each of the amounts on lines 5, 6, 7, and 8 of the employee's Form W-4 by the total number of pay periods in the year.
2. Add the results from step 1 for lines 5 and 8 of the employee's Form W-4 to the employee's wages per pay period.
3. Subtract the result from step 1 for line 6 of the employee's Form W-4 from the result from step 2. (Depending upon the withholding method, the employer may need to adjust this amount by the value of the withholding allowances as described in Publications 15 or 15-A).

4. Figure the income tax withholding using the result from step 3 as wages, with 2 (single or MFS) or 3 (MFJ or head of household) allowances for the filing status on line 3 of Form W-4.
5. Reduce the income tax withholding result from step 4 by the income tax credits per pay period figured in step 1 for line 7 of Form W-4. Do not reduce withholding below zero.
6. Separately figure the income tax withholding on the amount, if any, from step 1 for line 8 of Form W-4. (As in step 4, depending on the withholding method, the employer may need to adjust this amount by the value of the withholding allowances).
7. Subtract the income tax withholding result from step 6 from the result in step 5, to figure the amount of income tax withholding per pay period.
8. Add the amount, if any, from Form W-4, line 9, to the income tax withholding per pay period figured in step 7. This is the amount of income tax to withhold per pay period for the employee.

Example 7.1 Calculating Withholding

Floyd Miller works for Acme Corp. Floyd gave a 2019 Form W-4 to Acme in December 2018. Floyd checked the MFJ box on line 3. The entry on line 5 is $925, the entry on line 6 is $1,925, the entry on line 7 is $500, and the entry on line 8 is $25,000. There is no entry on line 9. Acme uses a monthly payroll period and withholds income tax using the wage bracket method in the 2018 Publication 15. Floyd's taxable wages are $42,900 per year, or $3,575 ($42,900 ÷ 12) per pay period.

Acme does the following:

1. Acme divides the amounts on lines 5, 6, 7, and 8 by the total number of payroll periods in the year, 12, and rounds them to the nearest dollar. The line 5 amount per pay period is $77 ($925 ÷ 12). The line 6 amount per pay period is $160 ($1,925 ÷ 12). The line 7 amount per pay period is $42 ($500 ÷ 12). The line 8 amount per pay period is $2,083 ($25,000 ÷ 12).
2. Acme adds Floyd's per pay period taxable wage to the results in step 1 for lines 5 and 8. This results in $5,735 ($3,575 + $77 + $2,083) for step 2.
3. Acme subtracts the results from step 1 for line 6 from the result from step 2. The result for step 3 is $5,575 ($5,735 – $160).
4. Acme applies the withholding table for MFJ for monthly pay period and 3 withholding allowances to compute the income tax withholding for the result from step 3 ($5,575). The withholding amount is $397 per pay period.
5. Acme subtracts the result from step 1 for line 7 from the withholding result from step 4. The step 5 withholding result is $355 ($397 - $42).
6. Acme applies the withholding table for MFJ for monthly pay period and 3 withholding allowances to compute the income tax withholding on the per payroll period result from step 1 for line 8 ($2,083). The withholding amount is $9 per pay period.
7. Acme subtracts the result from step 6 from the result from step 4. The result for step 7 is $346 ($355 - $9) per pay period.
8. As there is no entry on line 9, Acme does not have to increase the result from step 7 by an amount from line 9. The final withholding from Floyd's wages is $346 per pay period.

Social Security and Medicare Tax

The Federal Insurance Contributions Act (FICA) provides for a federal system of old-age, survivors, and disability insurance (OASDI) and hospital insurance. The OASDI is financed by the social security tax and the hospital insurance is financed by the Medicare tax. Employers must withhold and remit the employee portion of these taxes from employee wages and also pay the employer share of these taxes.

Social security taxes are imposed by I.R.C. § 3101(a) (employee's portion) and I.R.C. § 3111(a) (employer's portion). The social security tax is 12.4% (6.2% for the employee and 6.2% for the employer). For 2018, the maximum amount of wages subject to social security tax is $128,400.

If the taxpayer had more than one employer during the year and total wages and compensation were over the wage base limit for the year, the total social security tax withheld may exceed the maximum amount for the tax year. The taxpayer may be able to claim the excess as a credit against his or her income tax. Although the employee can obtain a refund of the employee portion of social security taxes on his or her income tax return to the extent the employee portion of social security taxes have been paid on wages that exceed the contribution benefit because the employee had two or more employers, the employer is not entitled to a refund of the employer portion of social security tax on the wages.

Medicare tax is 2.9% of total wages (1.45% for the employee and 1.45% for the employer). There is no wage base limit.

Additional Medicare Tax

If an employee's wages exceed a certain threshold ($250,000 MFJ and $200,000 single), employers must withhold a 0.9% additional Medicare tax from wages that exceed $200,000 for a calendar year beginning in the pay period in which the employer pays wages to an employee that exceed $200,000 and continuing until the end of the calendar year. The additional Medicare tax is imposed only on the employee. There is no employer share of additional Medicare tax.

Practitioner Note

Religious Exemption

I.R.C. § 1402(g) grants an exemption from social security and Medicare taxes to members of recognized religious sects or divisions who are opposed to private or public insurance. See pages 199–200 in the *2016 National Income Tax Workbook* for additional Information.

Successor Employer

Wages paid by a predecessor employer may be treated as if paid by a successor for purposes of applying the social security wage base, the FUTA wage base (discussed later), and the $200,000 additional Medicare tax threshold. Under I.R.C. § 3121(a)(1), if a successor employer acquires substantially all the property used in a trade or business of a predecessor employer or used in a separate unit of a trade or business of a predecessor, and immediately after the acquisition employs an employee of the predecessor, then compensation paid by the predecessor employer is considered as having been paid by the successor employer.

Treas. Reg. § 31.3121(a)(1)-1(b)(2) provides that the following three tests must be met for the wages paid by a predecessor, for purposes of the annual wage limitation, to be treated as having been paid by a successor employer:

1. The successor employer during a calendar year acquired substantially all the property used in a trade or business or used in a separate unit of a trade or business of the predecessor employer.
2. The employee was employed in the trade or business of the predecessor employer immediately prior to the acquisition and is employed by the successor employer in the successor's trade or business immediately after the acquisition.
3. The wages were paid during the calendar year in which the acquisition occurred and prior to the acquisition.

Example 7.2 Successor Employer

Early in 2018, J&P Company bought all the assets of a plumbing business from Martin Company. Jack Brown, who had been employed by Martin Company, received $2,000 in wages before the assets were sold. After the sale, Jack went to work for J&P Company and earned $220,000.

The $2,000 paid by Martin Company and the first $126,400 ($128,400 maximum wages subject to social security tax − $2,000) of wages paid by J&P Company to Jack are subject to social security tax. All of Jack's wages earned during the year are subject to Medicare tax. J&P Company includes the $2,000 Jack received while employed by Martin Company in determining FUTA and the additional Medicare tax.

Tax Deposits

Generally, an employer must deposit federal income tax withheld and both the employer and employee portions of social security and Medicare taxes.

Deposit Schedule

If the total tax liability for either the current quarter or the prior quarter is less than $2,500, and the employer did not incur a $100,000 next-day deposit obligation (discussed later) during the current quarter, the employer can make the deposit with Form 941, Employer's Quarterly Federal Tax Return; or Form 944, Employer's Annual Federal Tax Return. Other employers deposit withheld income tax, social security, and Medicare tax on a monthly or semiweekly deposit schedule.

Before the beginning of each calendar quarter, an employer must determine which schedule to use. The deposit schedule is based on the total tax liability the employer reported on Form 941 during a lookback period. The *lookback period* for employers who file Form 941 is defined as the 12-month period ended the preceding June 30 for each calendar year [Treas. Reg. § 31.6302-1(b)(4)]. **Figure 7.4** shows the 2018 lookback period.

FIGURE 7.4 2018 Lookback Period

July 1, 2016 through September 30, 2016	October 1, 2016 through December 31, 2016	January 1, 2017 through March 31, 2017	April 1, 2017 through June 30, 2017

In general, an employer is a monthly depositor for the entire calendar year if the aggregate amount of employment taxes reported for the lookback period is $50,000 or less [Treas. Reg. § 31.6302-1(b)(2)]. An employer is a semiweekly depositor for the entire calendar year if the aggregate amount of employment taxes reported for the lookback period exceeds $50,000 [Treas. Reg. § 31.6302-1(b)(3)]. New employers are treated as having no employment tax liabilities for any part of the lookback period before the date the employer started or acquired its business.

When to Make Deposits

Monthly depositors must deposit employment taxes on payments made during a month by the fifteenth day of the following month. If the fifteenth day of the following month is a Saturday, Sunday, or legal holiday in the District of Columbia, taxes are treated as timely deposited if the employer makes the deposit on the next succeeding day that is not a Saturday, Sunday, or legal holiday. Deposits must be made by electronic funds transfer (EFT).

Under the *semiweekly rule,* an employer must deposit employment taxes by EFT by the dates set forth in **Figure 7.5.**

FIGURE 7.5 Employment Tax Semiweekly Rule Deadlines

Payment Dates	Deposit Date
Wednesday, Thursday, and/or Friday	On or before the following Wednesday
Saturday, Sunday, Monday, and/or Tuesday	On or before the following Friday

Example 7.3 Semiweekly Deposits

Grey, Inc. is a semiweekly schedule depositor and pays its employees monthly on the last Friday of each month. Although Grey has a semiweekly deposit schedule, it will deposit just once a month because it pays wages monthly. Grey's tax liability for the April 27, 2018 (Friday) payday must be deposited by May 2, 2018 (Wednesday) because under the semiweekly deposit schedule, liabilities for wages paid on Wednesday through Friday must be deposited by the following Wednesday.

If an employer accumulates $100,000 or more in taxes on any day during a monthly or semiweekly deposit period, the employer must deposit the tax by the next business day, regardless of the employer's regular deposit schedule.

Payroll Reporting

Employers must file a payroll return for each quarter in which the employer pays wages that are subject to income tax withholding or social security and Medicare tax.

Form 941

Employers use Form 941 to report the following:

1. Wages paid
2. Tips reported by employees
3. Federal income tax withheld
4. The employer share and the employee share of social security and Medicare taxes
5. Additional Medicare tax withheld from employees
6. Any current quarter's adjustments to social security and Medicare taxes for fractions of cents, sick pay, tips, and group-term life insurance
7. Qualified small business payroll tax credit for increasing research activities

Figure 7.6 shows the due dates for Form 941.

FIGURE 7.6 Due Dates for Form 941

Form 941 is due by the last day of the month that follows the end of the quarter		
The Quarter Includes	**Quarter Ends**	**Form 941 Is Due**
1. January, February, March	March 31	April 30
2. April, May, June	June 30	July 31
3. July, August September	September 30	October 31
4. October, November, December	December 31	January 31

Form 944

If an employer believes that its employment taxes for the calendar year will be $1,000 or less, the employer can call the IRS and ask to file Form 944 instead of Form 941. After the employer contacts the IRS, the IRS will send a written notice that the filing requirement has been changed to Form 944. The employer must receive written notice from the IRS to file Form 944 instead of Form 941 before it files Form 944.

Form W-2

Employers must annually complete Form W-2, Wage and Tax Statement, for each employee. Form W-2 reports the total amount of wages paid, FICA taxes withheld, and federal and state income taxes withheld. Employers must also complete Form W-3, Transmittal of Wage and Tax Statements.

Employers file Forms W-2 and W-3 with the Social Security Administration (SSA) by January 31 of the year following the calendar year in which wages were paid. The employer can file the form by mail or electronically, but if an employer has more than 250 Forms W-2, all forms must be filed electronically. Employers must send the employee a copy of Form W-2 by January 31.

Matching Annual and Quarterly Reports

The amount of income tax withheld that is reported on Form W-3 should match the amounts reported on the quarterly or annual payroll returns. Generally, the social security and Medicare tax amounts shown on Forms 941 or annual Form 944, including current-year adjustments, should be approximately twice the amounts shown on Form W-3.

The SSA maintains a record of total social security and Medicare wages and tips processed for each employer. The totals are compared with the totals from the Forms 941 filed with the IRS. The IRS may contact employers whose reports to the IRS do not match the SSA amounts and ask for an explanation of the discrepancy and for additional wage evidence. Employers can use a year-end reconciliation worksheet to reconcile totals from each form [www.irs.gov/pub/irs-tege/year-end_reconciliation_worksheet.pdf] .

Amounts reported on Forms W-2 and W-3, and Forms 941 or Form 944, may not match if, for example, additional Medicare tax was withheld. The amount of Medicare tax that is reported on Form 941, line 5c, or Form 944, line 4c, will not be twice the amount of the Medicare tax withheld that is reported in box 6 of Form W-3. Employers should keep a reconciliation to document the discrepancy in case there are inquiries from the IRS or the SSA.

Penalties

An employer may be subject to a penalty for failure to file a correct Form W-2 and/or a failure to furnish a correct copy of Form W-2 to the employee. Each penalty is separate, and an information return may be subject to multiple penalties. An employer may also be subject to a penalty for failure to timely make deposits. In some cases, the IRS can hold an officer, director, or other person who is responsible for withholding and paying taxes liable for the tax.

Failure to File Correct Information Returns

Failure to file a correct information return includes any failure to file an information return, such as Form W-2, with the IRS on or before the required filing date, and any failure to include all the information required to be shown on the return. A penalty can also be assessed for the inclusion of incorrect information. The amount of the penalty is based on when the correct form is filed and is indexed for inflation.

The failure-to-file penalty will not apply if the failure to file was due to reasonable cause and not willful neglect, the error or omission was inconsequential, or the safe harbor for de minimis errors applies. The safe harbor generally applies if no single amount in error differs from the correct amount by more than $100 and no single amount reported for tax withheld differs from the correct amount by more than $25.

Failure to Furnish Correct Payee Statements

The failure to furnish correct payee statements, such as a Form W-2, applies to any failure to furnish a payee statement on or before the due date, and any failure to include all the information required to be shown on a payee statement. Inclusion of incorrect information can also result in a penalty. The amount of the penalty is based on when the employer furnishes the correct payee statement. The failure-to-furnish penalty will not apply if the error or omission was inconsequential.

Required Deposit Penalties

Penalties may apply if the taxpayer does not make required deposits on time or if he or she makes deposits for less than the required amount. The penalties do not apply if any failure to make a proper and timely deposit was due to reasonable cause and not to willful neglect. For amounts not properly or timely deposited, the penalty rates are as follows:

- 2% for deposits made 1 to 5 days late
- 5% for deposits made 6 to 15 days late
- 10% for deposits made 16 or more days late, but before 10 days from the date of the first IRS notice asking for the tax due
- 10% for amounts that should have been deposited, but instead were paid directly to the IRS, or paid with the tax return
- 15% for amounts still unpaid more than 10 days after the date of the first IRS notice asking for the tax due or the day on which the taxpayer received notice and demand for immediate payment, whichever is earlier

CROSS-REFERENCE

Certified Professional Employer Organizations

See the "IRS Issues" chapter for a discussion of a certified professional employer organization (CPEO). In some cases, use of a CPEO can relieve the employer from responsibility for withholding, depositing, and reporting requirements.

Trust Fund Recovery Penalty

Under I.R.C. § 6672, a responsible person can be held personally liable for a willful failure to collect, account for, and pay employment taxes. Taxes withheld are called trust fund taxes because the employer or other responsible person holds the employee's money in trust until the tax deposit is made. The trust fund recovery penalty (TFRP) is assessed against a responsible person who

- is responsible for collecting or paying withheld income and employment taxes, or for paying collected excise taxes; and
- willfully fails to collect or pay the taxes.

A responsible person is a person or group of people who has the duty to perform and the power to direct the collecting, accounting, and paying of trust fund taxes. A responsible person could be any of the following persons:

1. An officer or an employee of a corporation
2. A member or employee of a partnership
3. A corporate director or shareholder
4. A member of a board of trustees of a nonprofit organization
5. Another person with authority and control over funds to direct their disbursement

For willfulness to exist, the responsible person must have been, or should have been, aware of the outstanding taxes and either intentionally disregarded the law or was indifferent to its requirements. The payment of net wages to employees when funds are not available to pay withholding taxes is a willful failure to collect and pay over the taxes.

TFRP Penalty Amount

The amount of the TFRP penalty is equal to the employee's portion of FICA taxes and all income taxes withheld for the period. The IRS does not divide the assessments between responsible persons and can collect the full amount from any one responsible person.

Assessing the TFRP

Before assessing a TFRP, the IRS must mail or hand deliver to the taxpayer a 60-day notice of the proposed assessment. The IRS uses Letter 1153, which advises the taxpayer of the proposed penalty and his or her appeal rights. A taxpayer can agree to the penalty by signing Form 2751, Proposed Assessment of Trust Fund Recovery Penalty. Alternatively, a taxpayer can discuss the proposed penalty with the revenue officer group manager, request fast-track mediation, or file a timely written protest.

Federal Unemployment Taxes

The federal unemployment (FUTA) and state unemployment systems provide for payments of unemployment compensation to workers who have lost their jobs. In 2018, an employer is subject to FUTA tax on the wages the employer pays to employees who are not farm workers or household workers if

- the employer paid wages of $1,500 or more in any calendar quarter in 2017 or 2018, or
- the employer had one or more employees for at least some part of a day in any 20 or more different weeks in 2017 or 20 or more different weeks in 2018.

Most employers pay both federal and state unemployment taxes. Only employers, not employees, pay these taxes. For 2018, the FUTA tax rate is 6% and applies to the first $7,000 paid to each employee as wages during the year. Generally, the employer can take a credit against FUTA tax for amounts paid into state unemployment funds. The credit may be as much as 5.4% of FUTA taxable wages. If the employer is entitled to the maximum 5.4% credit, the FUTA tax rate after the credit is 0.6% (6.0% – 5.4%). The employer is entitled to the maximum credit if it paid state unemployment taxes in full, on time, and on all the same wages that are subject to FUTA tax (and the state is not a credit reduction state).

CROSS-REFERENCE

Certified Professional Employer Organizations

The Tax Increase Prevention Act of 2014, Pub. L. No. 113-295, requires the IRS to establish a voluntary certification program for professional employer organizations (PEOs). PEOs handle various payroll administration and tax-reporting responsibilities for their business clients and are typically paid a fee based on payroll costs. For wages paid to a work site employee, a certified PEO (CPEO) is eligible for the credit for state unemployment tax paid to a state unemployment fund, whether the CPEO or a customer of the CPEO made the contribution. See the "IRS Issues" chapter for more information about CPEOs.

If FUTA tax liability for any calendar quarter is $500 or less, the employer does not have to deposit the tax. Instead, the employer may carry it forward and add it to the liability figured in the next quarter. If FUTA tax liability for any calendar quarter is more than $500 (including any FUTA tax carried forward from an earlier quarter), the employer must deposit the tax by EFT. Generally, deposits are due by the last day of the first month that follows the end of the quarter.

The employer uses Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return, to report FUTA tax. Form 940 is due by January 31 for the previous year's reporting. However, if the employer deposited all FUTA tax when due, the employer can file Form 940 on or before February 10.

Paid Time Off

Paid time off (PTO) is time the employer provides for which the employee is compensated even in his or her absence. Common categories of PTO include sick pay and vacation leave. This section discusses the taxation of PTO and withholding on payments for PTO.

Sick Pay

Sick pay is a payment made to an employee for a period in which the employee is temporarily absent from work due to personal injury, disability, or sickness. It may be paid by either the employer or a third party, such as an insurance company. Sick pay includes both short and long-term benefits and is often expressed as a percentage of the employee's regular wages. Sick pay does not include the following payments:

- Disability retirement payments
- Workers' compensation
- Payments to public employees that are for a work-related injury
- Medical expense payments
- Payments unrelated to absence from work, including payments for permanent loss of a member or function of the body, permanent loss of the use of a member or function of the body, or permanent disfigurement of the body

Withholding Requirements

Sick pay paid by the employer is generally included in the employee's income and is subject to federal income tax withholding, social security, Medicare, and FUTA taxes. However, if the employee paid the premiums on an accident or health insurance policy (or the employer made the payments and the employee included them in income), the benefits paid under the policy are not taxable. Sick pay paid to the employee's estate or survivor after the calendar year of the employee's death is not subject to federal income tax withholding, social security, Medicare, or FUTA taxes.

If both the employer and the employee contributed to the sick pay plan under a group insurance policy, the taxable sick pay is calculated by multiplying total sick pay by the percentage of the policy's cost that the employer contributed for the 3 policy years before the calendar year in which the sick pay is paid. If the policy was in effect fewer than 3 years, the taxpayer uses the cost for the policy years in effect or, if in effect less than 1 year, a reasonable estimate of the cost for the first policy year.

Social security, Medicare, and FUTA taxes do not apply to sick pay paid more than 6 calendar months after the last calendar month in which the employee worked.

Example 7.4 Contributions to Group Policy

Dan Davidson, an employee of Crestwood Corporation, was seriously injured in a car accident on January 1, 2017. Dan's last day of work was December 31, 2016. The accident was not job-related. Key Life Insurance Company, which is not an agent of Crestwood, paid Dan $2,000 sick pay each month for 10 months, beginning in January 2017. Dan submitted a Form W-4S, Request for Federal Income Tax Withholding From Sick Pay, to Key, requesting $210 be withheld from each payment for federal income tax. Dan received no payments from Crestwood from January 2017 through October 2017, and he returned to work on November 1, 2017.

For the policy year in which the car accident occurred, Dan paid a part of the premiums for his coverage and Crestwood paid the remaining portion. During the 3 policy years before the calendar year of the accident, Crestwood paid 70% of the total of the net premiums for its employees' insurance coverage, and its employees paid 30%.

For social security and Medicare tax purposes, Dan's taxable sick pay was $8,400 [($2,000 × 70%) taxable portion per payment × 6 months]. Only the six $2,000 checks that Dan received from January through June are included in the calculation. The check that Dan received in July (the seventh check) was received more than 6 months after the month in which Dan last worked. Of each $2,000 payment that Dan received, $600 (30% × $2,000) is not subject to social security and Medicare taxes because Dan's after-tax contribution is 30% of the premiums during the 3 policy years before the calendar year of the accident.

Example 7.5 Payments after a 6-Month Absence from Work

Carl Carlson worked for XYZ Company and became entitled to receive sick pay on December 11, 2017. Carl took a 9-month absence from work due to illness. XYZ paid him sick pay for those 9 months, and Carl returned to work on September 17, 2018. Sick pay that Carl received after 6 months, or June 30, 2018, is not subject to social security, Medicare, or FUTA tax (but it is subject to federal income tax withholding). However, if Carl worked 1 day in the 9-month period, the 6-month period starts over.

Reporting Requirements

The rules for depositing and reporting sick pay are the same as the rules for regular wage payments. Employers may either combine sick pay with other wages and prepare a single Form W-2 for each employee or prepare separate Forms W-2 for each employee, one reporting sick pay and the other reporting regular wages. The employer must file and furnish Form W-2 even if all the sick pay is nontaxable. Sick pay is reported with compensation in box 1 of Form W-2. Any sick pay that was paid by a third party and is nontaxable (because the employee paid for the sick pay plan) is reported in box 12 with code J (nontaxable sick pay).

Vacation Pay

Vacation pay is treated as a regular wage payment for withholding and reporting purposes. If vacation pay is paid in addition to the regular wage payment, the withholding rules applicable to supplemental wage payments apply [Treas. Reg. § 31.3402(g)-1(c)]. Supplemental wages are all wages paid by an employer that are not regular wages and include wage payments made without regard to an employee's payroll period, but also may include payments made for a payroll period. If supplemental wages are paid with regular wages and not specifically stated, the federal income tax withholding is the same as for regular wages. If supplemental wages are $1,000,000 or less and are paid separately or separately stated, the amount of the tax that must be withheld from supplemental wages is determined using the aggregate procedure or the flat-rate method. Regardless of how the federal tax withholding is calculated, supplemental wages are subject to social security, Medicare, and FUTA tax.

Aggregate Procedure

Under the aggregate procedure, supplemental wages that are paid concurrently with regular wages for a payroll period are aggregated with regular wages. The amount of tax to be withheld is determined as if the supplemental wages and the regular wages are a single wage payment.

Flat-Rate Method

Under the flat-rate method, the employer determines withholding on supplemental wages using a flat percentage, regardless of the number of withholding allowances the employee claimed on Form W-4. The tax rate applicable for flat-rate withholding on supplemental wages paid after December 31, 2017, is 22%.

PRACTITIONER NOTE

Supplemental Wage Payments Over $1,000,000

If a supplemental wage payment, when added to all supplemental wage payments previously made by one employer to an employee during the calendar year, exceeds $1,000,000, the employer must withhold on 37% of the excess amount.

Accumulated PTO

PTO that is not used during the year generally accumulates. Accumulated PTO may be paid out to the employee if the employee retires or is terminated. Payment of accumulated PTO benefits is reported as a supplemental wage payment and subject to the supplemental wage withholding rules (discussed previously).

Business Expense Reimbursements

In general, business expense reimbursements paid under an accountable plan are not included in an employee's wages, while reimbursements paid under nonaccountable plans are included in wages.

Accountable Plans

An arrangement is an accountable plan if it meets the following requirements:

1. Business connection. The employer provides advances; allowances, including per diem allowances, allowances for meals and incidental expenses, and mileage allowances; or reimbursements only for business expenses that are allowable as deductions, and that are paid or incurred by the employee in connection with the performance of services as an employee of the employer [Treas. Reg. § 1.62-2(d)(1)].
2. Substantiation. The employer requires the employee to give the employer substantiation of each business expense within a reasonable period of time [Treas. Reg. § 1.62-2(e)].
3. Returning amounts in excess of expenses. The employer requires the employee to return to the employer within a reasonable period of time the amount paid under the arrangement that exceeds the substantiated expenses [Treas. Reg. § 1.62-2(f)].

Amounts treated as paid under an accountable plan are excluded from the employee's gross income, are not reported as wages or other compensation on the employee's Form W-2, and are exempt from the withholding and payment of employment taxes [Treas. Reg. § 1.62-2(c)(4)].

PRACTITIONER NOTE

Failure to Return Excess Amounts

If the arrangement meets the requirements of an accountable plan, but the employee fails to return, within a reasonable time, any amount in excess of the amount of the expenses substantiated, only the amounts paid under the arrangement that are not in excess of the substantiated expenses are treated as paid under an accountable plan [Treas. Reg. § 1.62-2(c)(2)(ii)].

Nonaccountable Plans

Generally, if an arrangement does not satisfy one or more of the requirements of an accountable plan, all amounts paid under the arrangement are treated as paid under a nonaccountable plan [Treas. Reg. § 1.62-2(c)(3)(i)].

OBSERVATION

Voluntary Substantiation and Return of Excess

An employee who receives payments under a nonaccountable plan cannot compel the employer to treat the payments as paid under an accountable plan by voluntarily substantiating the expenses and returning any excess to the employer [Treas. Reg. § 1.62-2(c)(3)(i)].

Amounts treated as paid under a nonaccountable plan are included in the employee's gross income, must be reported as wages or other compensation on the employee's Form W-2, and are subject to withholding and payment of employment taxes. If the amounts reimbursed are included in the employee's gross income, the employee may be able to deduct these on Form 2106, Employee Business Expenses, as a miscellaneous itemized deduction subject to the 2%-of-AGI floor [Treas. Reg. § 1.62-2(c)(5)]. However, for tax years beginning after December 31, 2017, and before January 1, 2026, miscellaneous itemized deductions that are subject to the 2%-of-AGI floor are suspended.

CROSS-REFERENCE

Accountable Plan

See the "Individual Issues" chapter for a sample accountable plan.

Example 7.6 Separate Arrangement

Under an arrangement that meets the requirements of an accountable plan, Broadmoor County reimburses its employees for lodging and meal expenses incurred when they travel away from home on county business. For its own convenience, the county also separately pays certain of its employees a $25 monthly allowance to cover the cost of small miscellaneous office expenses. Broadmoor County does not require its employees to substantiate these miscellaneous expenses and does not require them to return the amounts by which the monthly allowance exceeds the miscellaneous expenses.

The monthly allowance arrangement is a nonaccountable plan. Broadmoor County must report the monthly allowances as wages or other compensation on the employees' Forms W-2 and must withhold and pay employment taxes on the monthly allowances when paid. The nonaccountable plan providing the monthly allowances is treated as separate from the accountable plan providing reimbursements for lodging and meal expenses incurred for travel away from home on county business [Treas. Reg. § 1.62-2(j), Example 4].

Example 7.7 Excessive Advances

In anticipation of employee business expenses that Verity Corporation does not reasonably expect to exceed $400 in any quarter, Verity nonetheless advances $1,000 to its employee Amy Anderson for such expenses. Whenever Amy substantiates an expense, Verity provides an additional advance in an amount equal to the amount substantiated, thereby providing a continuing advance of $1,000.

Because the amounts advanced under this arrangement are not reasonably calculated so as not to exceed the amount of anticipated expenditures and because the advance of money is not made on a day within a reasonable period of the day that the anticipated expenditures are paid or incurred, the arrangement is a nonaccountable plan. The arrangement does not have a business connection and does not reasonably calculate the advance. Thus, Verity must report the entire amount of each advance as wages or other compensation and must withhold and pay employment taxes on the entire amount of each advance when paid [Treas. Reg. § 1.62-2(j), Example 5].

Fringe Benefits

A fringe benefit is a form of pay for the performance of services. Generally, fringe benefits are included in wages under [I.R.C. § 3401(a); Treas. Reg. § 31.3401(a)-1]. However, some employer-provided fringe benefits are specifically excluded from the employee's income.

Included Benefits

Examples of employer-provided fringe benefits that must be included in income include the following:

- A vehicle provided for the employee's personal use
- A flight on an employer-provided aircraft for personal purposes
- A free or discounted commercial airline flight for personal purposes
- A vacation
- A discount on property or services
- Membership in a country club or other social club
- A ticket to an entertainment or sporting event

[Treas. Reg. § 1.61-21(a)(1)]

A fringe benefit provided in connection with the performance of services is considered to have been provided as compensation for such services. In general, a taxable fringe benefit is included in the income of the person performing the services in connection with which the fringe benefit is furnished, even if that person did not actually receive the fringe benefit.

An employee must include in gross income the amount by which the FMV of the taxable fringe benefit exceeds the amount that the employee paid for the benefit. Such amounts are subject to withholding and employment taxes in the same manner as wage compensation.

CROSS-REFERENCE

Fringe Benefits

See the discussion of employer-provided transportation, entertainment, and meals in the "Business Issues" chapter.

Excluded Benefits

Some fringe benefits are excluded from income, such as qualified tuition reductions provided to an employee under I.R.C. § 117(d); meals or lodging furnished to an employee for the convenience of the employer under I.R.C. § 119; benefits provided under a dependent care assistance program under I.R.C. § 129; and no-additional-cost services, qualified employee discounts, working condition fringes, and de minimis fringes under I.R.C. § 132 [Treas. Reg. § 1.61-21(a)(2)].

PRACTITIONER NOTE

Additional Resources

See IRS Publication 15-B, *Employer's Tax Guide to Fringe Benefits*, for more information on valuing and determining the taxability of fringe benefits.

Reporting and Withholding for Taxable Fringe Benefits

Generally, the employer must determine the value of noncash fringe benefits no later than January 31 of the following year. For employment tax and withholding purposes, the employer can treat noncash fringe benefits (including personal use of employer-provided highway motor vehicles) as paid on a pay period, quarter, semiannual, annual, or other basis, but the benefits must be treated as paid no less frequently than annually. For investment property and real property, the employer must use the actual date that it transferred the property to the employee.

The employer does not have to choose the same period for all employees. It can withhold more frequently for some employees than for others. The employer can change the period as often as it likes, but all benefits provided in a calendar year must be treated as paid no later than December 31 of the calendar year.

The employer can add the value of fringe benefits to regular wages for a payroll period and calculate income tax withholding on the total amount. Alternatively, the employer can withhold federal income tax on the value of fringe benefits at the flat rate that applies to supplemental wages (discussed earlier). The employer must withhold income, social security, and Medicare taxes on the date or dates it chooses to treat the benefits as paid, and it must deposit the amounts withheld in the same manner that it makes deposits for regular wage compensation.

Noncash Wages for Farm Labor

Farm employees may receive part of their compensation in the form of noncash fringe benefits. A farm employer may provide employees with housing, meals, use of vehicles, farm products, and other goods and commodities. Noncash farm wages, including commodity wages, are not subject to federal income tax withholding or social security or Medicare taxes even if they are included in gross income [I.R.C. § 3121(a)(8)(A)]. However, noncash wages, including commodity wages, are treated as cash wages if the substance of the transaction is a cash payment (i.e., if the noncash wages can be immediately converted to cash) [Rev. Rul. 79-207, 1979-2 C.B. 351]. Noncash wages treated as cash wages are subject to social security taxes, Medicare taxes, and federal income tax withholding.

Example 7.8 Noncash Wages Paid to Farm Employees

Mary Winston is an employee of Peterson Farms. Peterson paid Mary $10,000 of cash wages and farm produce with a $3,500 value on the date received. The $3,500 in commodity wages is not subject to social security or Medicare taxes. Peterson reports $13,500 ($10,000 + $3,500) in box 1, and $10,000 in boxes 3 and 5 of Mary's Form W-2.

Independent Contractors

As discussed earlier, an employer must withhold, deposit, and report income and employment taxes on wages paid to employees. This section discusses the payer's withholding and reporting requirements for payments to independent contractors.

CROSS-REFERENCE

Worker Classification

See pages 293–298 of the *2016 National Income Tax Workbook* for a detailed discussion of the classification of a worker as an employee or an independent contractor.

Withholding

Generally, an employer has no obligation to withhold income or employment taxes from amounts paid to an independent contractor. However, backup withholding may be required in the following circumstances:

1. The payee fails to furnish his or her taxpayer identification number (TIN) to the payer in the manner required.
2. The IRS notifies the payer that the TIN furnished by the payee is incorrect.
3. The payee failed to include a reportable interest or dividend payment on his or her tax return or failed to file his or her return to report the interest or dividend payment, and the IRS has mailed at least four notices to the payee over 120 days. For a payee who filed a return for the tax year, any deficiency of tax attributable to underreporting has been assessed.
4. The payee fails to certify that he or she is not subject to backup withholding for underreporting interest and dividends.

If backup withholding is required, the payer must deduct and withhold 24% federal income tax from payments [I.R.C. § 3406].

Generally, no backup withholding is required for amounts reported on Form 1099-MISC, Miscellaneous Income, (discussed later) if the amount paid is less than $600, the payer did not have to give the payee a Form 1099 in the previous year, and the payer made no payments to the payee in the prior year that were subject to backup withholding.

PRACTITIONER NOTE

Estimated Tax Payments

Because a payer does not typically withhold income and employment taxes on payments to independent contractors, self-employed persons must pay estimated taxes on their earnings. See the later discussion of the amount and timing of estimated tax payments.

Reporting

Payers report backup withholding on Form 945, Annual Return of Withheld Federal Income Tax, which the payer must file by January 31. Payment should be made with Form 945 only if total taxes for the year are less than $2,500 and are paid with the return, or the payer is a monthly schedule depositor making a payment in accordance with the accuracy-of-deposits rule. Otherwise, the payer must make these payments electronically.

Payers may have to file Form 1099-MISC to report payments for services performed by independent contractors if the payment is $600 or more. Additionally, payers must file Form 1099-MISC for each person for whom income tax was withheld under the backup withholding rules regardless of the payment amount.

Some payments do not have to be reported on Form 1099-MISC, although they may be taxable to the recipient. For example, Form 1099-MISC is not required for most payments to a corporation (including a limited liability company that is taxed as a C or S corporation).

PRACTITIONER NOTE

Form W-9

A payer that is required to file Form 1099-MISC must obtain the correct TIN, which may be a social security number (SSN), individual taxpayer identification number (ITIN), adoption taxpayer identification number (ATIN), or employer identification number (EIN). Payers can request this information from the independent contractor using Form W-9, Request for Taxpayer Identification Number and Certification. The contractor must provide accurate identification information and may be subject to a penalty if he or she fails to provide the correct TIN or makes a false statement.

ESTIMATED TAX Taxpayers may have to make estimated tax payments if their tax withholding is less than their anticipated tax liability.

Taxpayers who expect their tax liability to be greater than the amount of tax withheld from income sources may be required to make estimated tax payments. If the taxpayer fails to make estimated payments, or fails to make the payments on time, the taxpayer may have to pay an underpayment penalty. This section reviews the general rules for who must pay estimated tax and how to calculate estimated tax payment amounts. It discusses when the taxpayer must make estimated tax payments and includes a comprehensive example of a seasonal worker who uses the annualized income method. Finally, this section explains when the taxpayer will be charged a penalty and some of the common exceptions to the underpayment penalty.

When Estimated Payments Are Required

Individual taxpayers may have to make estimated tax payments on self-employment income; interest; dividends; rent; and gains from the sale of assets, prizes, and awards. They may also have to pay estimated tax if not enough income tax is withheld from their salary, pension, or other income. Generally, taxpayers must pay estimated tax if both of the following apply:

1. The taxpayer expects to owe at least $1,000 in tax for the current year, after subtracting any tax withholding and refundable credits.
2. The taxpayer expects his or her tax withholding and refundable credits to be less than the smaller of
   a. 90% of the tax on the current-year tax return, or
   b. 100% of the tax on the prior-year tax return [110% if the taxpayers prior-year AGI was more than $150,000 ($75,000 for MFS)]. The prior-year tax return must have covered all 12 months.

PRACTITIONER NOTE

Farmers and Fishermen

Special rules apply to farmers and fishermen. If at least two-thirds of the taxpayer's gross income is from farming or fishing, the estimated tax is generally owed if current-year withholding and refundable credits is less than the smaller of 66% of the tax on the current-year return or 100% of the tax on the prior-year return. Under I.R.C. § 6654(i), only one payment (rather than the usual four payments) is required. Farmers and fishermen may also choose not to make an estimated tax payment if they file their returns and pay the full amount of tax due by March 1.

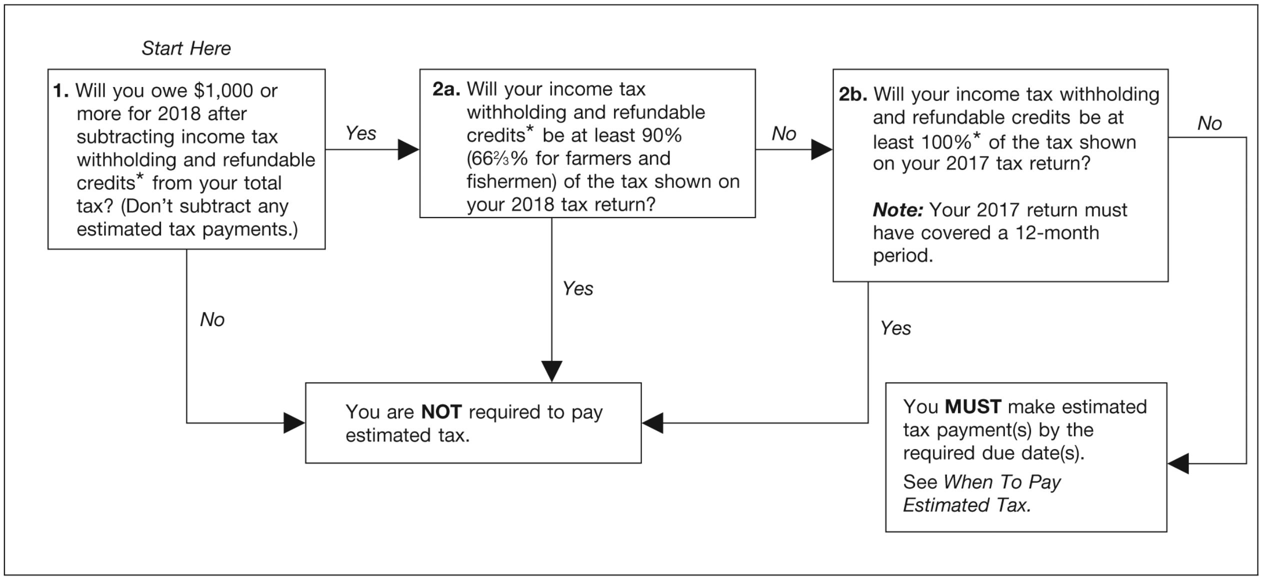
Taxpayers do not have to make estimated tax payments if all three of the following conditions are met:

1. The taxpayer had no tax liability for the prior tax year.
2. The taxpayer was a US citizen or resident alien for the entire year.
3. The prior tax year covered a 12-month period.

Figure 7.7 shows how to determine if estimated payments are required in 2018.

FIGURE 7.7 Determining If Estimated Tax Payments Are Required

Figure 2-A. **Do You Have To Pay Estimated Tax?**



* Use the refundable credits shown on the 2018 Estimated Tax Worksheet, line 11b.

** 110% if less than two-thirds of your gross income for 2017 and 2018 is from farming or fishing and your 2017 adjusted gross income was more than $150,000 ($75,000 if your filing status for 2018 is married filing a separate return).

Source: IRS Publication 505, *Tax Withholding and Estimated Tax*, Figure 2-A

Example 7.9 Estimated Tax Payments Not Required

Gail Force files as head of household, takes the standard deduction, and expects no refundable credits for 2018. She uses the information in **Figure 7.8** to determine whether she must make estimated tax payments.

FIGURE 7.8 Gail's 2017 and 2018 AGI, Tax, and Payments

2018 expected AGI	\$74,550
2017 AGI	\$57,150
2017 tax liability	\$6,188
2018 expected tax liability	\$6,989
2018 withholding	\$6,000

Gail's estimated tax liability for 2018 after applying tax withholding and refundable credits is \$989 (\$6,989 − \$6,000 = \$989). Because Gail expects to owe less than \$1,000 for 2018, she does not have to make any estimated tax payments.

Example 7.10 Estimated Tax Payments Required

The facts are the same as in Example 7.9, except that Gail expects only \$5,500 of tax withholding in 2018. Gail's estimated tax liability for 2018 after applying tax withholding and refundable credits is \$1,489 (\$6,989 −\$5,500), which is more than \$1,000. Gail's estimated tax withholding (\$5,500) and refundable credits (\$0) are less than 90% of her expected 2018 tax (\$6,989 × 90% = \$6,290), and less than 100% of her 2017 tax liability (\$6,188). Therefore, Gail must make estimated tax payments for 2018.

PLANNING POINTER

Increase Tax Withholding

Gail could also increase her tax withholding by submitting a new Form W-4 to her employer. See the earlier discussion of withholding and Form W-4.

Calculating Estimated Tax Payments

To calculate estimated tax payments, taxpayers must calculate their expected AGI, taxable income, taxes, deductions, and credits for the year. Taxpayers can use the worksheet in Form 1040-ES, Estimated Tax for Individuals, to determine estimated tax.

Example 7.11 Calculating Estimated Tax

The facts are the same as in Example 7.10. Gail estimates that she will have \$18,000 of itemized deductions, resulting in \$56,550 (\$74,550 AGI – \$18,000) of taxable income. Using the 2018 tax rate schedule, Gail estimates her tax liability as \$6,989 [\$5,944 + {(56,550 – 51,800) × 22%}]. **Figure 7.9** shows the calculation of Gail's \$172 quarterly (\$688 annual) estimated tax payments using the worksheet in Form 1040-ES.

FIGURE 7.9 Gail Force's Estimated Tax Calculation Worksheet

2018 Estimated Tax Worksheet

Keep for Your Records

1	Adjusted gross income you expect in 2018 (see instructions)			1	74,550
2a	Deductions • If you plan to itemize deductions, enter the estimated total of your itemized deductions. These include qualifying home mortgage interest, charitable contributions, state and local taxes (up to $10,000), and medical expenses in excess of 7.5% of your income.* • If you don't plan to itemize deductions, enter your standard deduction.			2a	18,000
b	If you qualify for the deduction under section 199A, enter the estimated amount of the deduction you are allowed on your qualified business income from a qualified trade or business			2b	0
c	Add lines 2a and 2b ▶			2c	18,000
3	Subtract line 2c from line 1			3	56,550
4	**Tax.** Figure your tax on the amount on line 3 by using the **2018 Tax Rate Schedules**. **Caution:** *If you will have qualified dividends or a net capital gain, or expect to exclude or deduct foreign earned income or housing, see Worksheets 2-5 and 2-6 in Pub. 505 to figure the tax*			4	6,989
5	Alternative minimum tax from **Form 6251** or included on **Form 1040A, line 28**			5	0
6	Add lines 4 and 5. Add to this amount any other taxes you expect to include in the total on Form 1040, line 44			6	6,989
7	Credits (see instructions). **Do not** include any income tax withholding on this line			7	0
8	Subtract line 7 from line 6. If zero or less, enter -0-			8	6,989
9	Self-employment tax (see instructions)			9	0
10	Other taxes (see instructions)			10	0
11a	Add lines 8 through 10			11a	6,989
b	Earned income credit, additional child tax credit, fuel tax credit, net premium tax credit, refundable American opportunity credit, and refundable credit from Form 8885			11b	0
c	**Total 2018 estimated tax.** Subtract line 11b from line 11a. If zero or less, enter -0- ▶			11c	6,989
12a	Multiply line 11c by 90% (66⅔% for farmers and fishermen)	12a	6,290		
b	Required annual payment based on prior year's tax (see instructions)	12b	6,188		
c	**Required annual payment to avoid a penalty.** Enter the **smaller** of line 12a or 12b ▶			12c	6,188
	Caution: *Generally, if you do not prepay (through income tax withholding and estimated tax payments) at least the amount on line 12c, you may owe a penalty for not paying enough estimated tax. To avoid a penalty, make sure your estimate on line 11c is as accurate as possible. Even if you pay the required annual payment, you may still owe tax when you file your return. If you prefer, you can pay the amount shown on line 11c. For details, see chapter 2 of Pub. 505.*				
13	Income tax withheld and estimated to be withheld during 2018 (including income tax withholding on pensions, annuities, certain deferred income, etc.)			13	5,500
14a	Subtract line 13 from line 12c Is the result zero or less? ☐ **Yes.** Stop here. You are not required to make estimated tax payments. ☑ **No.** Go to line 14b.	14a	688		
b	Subtract line 13 from line 11c Is the result less than $1,000? ☐ **Yes.** Stop here. You are not required to make estimated tax payments. ☑ **No.** Go to line 15 to figure your required payment.	14b	1,489		
15	If the first payment you are required to make is due April 17, 2018, enter ¼ of line 14a (minus any 2017 overpayment that you are applying to this installment) here, and on your estimated tax payment voucher(s) if you are paying by check or money order			15	172

*When figuring your 2018 estimated taxes, and estimating your deductions, you might want to take into account that the standard deduction for all filing statuses has increased substantially and many itemized deductions have been eliminated or the deduction amount has been reduced. See the items under *What's New*.

PRACTITIONER NOTE

Seasonal Income

If the taxpayer does not receive his or her income evenly throughout the year, the required estimated tax payments may not be the same for each period. See the later discussion of the annualized income installment method.

When to Make Estimated Payments

For estimated tax purposes, the year is divided into four payment periods and each period has a specified payment due date. Failure to pay enough tax by the due date of each of the payment periods may result in assessment of an underpayment penalty (discussed later). **Figure 7.10** shows the estimated tax payment due dates for a 2018 calendar-year taxpayer. If the date falls on a Saturday, Sunday, or legal holiday, the payment is due on the following business day.

FIGURE 7.10 2018 Estimated Tax Payment Due Dates

For the Period	Due Date
January 1–March 31	April 17, 2018
April 1–May 31	June 15, 2018
June 1–August 31	September 17, 2018
September 1–December 31	January 15, 2019*

*If the taxpayer files the 2018 Form 1040, U.S. Individual Income Tax Return, by January 31 of the next year and pays the remaining tax owed, then no estimated payment is required by January 15.

How Payments Are Applied

If the taxpayer fails to make one of the required estimated tax installment payments, any subsequent payment is applied to the earlier liability. The taxpayer must fully pay the earliest liability before payments are applied to later installments.

Withholding and Social Security

Any withholding or excess social security tax is applied evenly among the required installments. However, taxpayers may apply withholding against the specific income it is connected to by completing Form 2210, Underpayment of Estimated Tax by Individuals, Estates, and Trusts (discussed later), and checking box D in Part II of the form.

Joint Payments of Estimated Tax

Estimated payments made by spouses who file separate returns may be credited or made on behalf of just one spouse or divided in any way the spouses agree [Treas. Reg. § 1.6654-2(e)(5)(ii)(A)]. If the spouses cannot agree on an allocation, the IRS allocates the payments based on the spouses' separate tax liabilities [Treas. Reg. § 1.6654-2(e)(5)(ii)(B)].

7

Example 7.12 Joint Estimated Tax Payments

Harold and Wanda Whitcomb made a $19,500 joint payment of estimated tax for the 2018 tax year. Harold and Wanda subsequently filed separate returns showing $11,500 and $8,000 tax, respectively. In addition, Harold's return showed $500 self-employment tax. If Harold and Wanda cannot agree to a division of the estimated tax paid, the amount of the tax payments is allocated based on each spouse's share of the tax liabilities.

Harold owes $12,000 tax ($11,500 + $500) and Wanda owes $8,000 tax. Their total tax is $20,000 ($12,000 + $8,000). The proportion of taxes shown on Harold's return to the total amount is 60% ($12,000 ÷ $20,000), and $11,700 (60% × $19,500) of the estimated tax payments are allocated to Harold. The remaining $7,800 ($19,500 − $11,700) of estimated tax payments are allocated to Wanda [Treas. Reg. § 1.6654-2(e)(6), Example].

How to Pay Estimated Tax

There are several ways to pay estimated tax:

- The taxpayer can credit an overpayment from the prior-year return to the current-year estimated tax.
- The taxpayer can pay by direct transfer from a bank account or pay by debit or credit card using a pay-by-phone system or the internet.
- The taxpayer can send a payment (check or money order) with a payment voucher from Form 1040-ES.

Credit an Overpayment

The taxpayer can credit an overpayment from a prior year to estimated tax owed for the current year. On the prior-year return, the taxpayer enters the amount that he or she wants credited to estimated tax rather than refunded. The taxpayer then takes that amount into account when calculating the current-year estimated tax payments. If the taxpayer timely filed the prior-year return, the credit is treated as a payment made on April 15 of the current year.

Pay Online

The taxpayer can make an estimated tax payment at IRS.gov/Payments by any of the following methods:

- A transfer directly from the taxpayer's checking or savings account
- Payment by credit card or debit card (processing fees are charged)
- Electronic funds withdrawal
- Online payment agreement (if the taxpayer cannot pay the full amount owed)

CROSS-REFERENCE

Installment Agreement

See the "Tax Practice" chapter for a discussion of how to request an installment agreement, and other collection alternatives.

PRACTITIONER NOTE

Phone and Mobile Device Payments

The taxpayer can also pay by debit or credit card by calling one of the IRS debit or credit card service providers. Alternatively, the taxpayer can make a payment from his or her mobile device by downloading the IRS2Go mobile application.

Mail a Payment

The taxpayer can pay by check or money order using the estimated tax payment voucher. There is a separate estimated tax payment voucher for each due date

Estimated Tax Penalties

Taxpayers are generally required to pay income tax as income is earned. If the taxpayer makes insufficient payments throughout the year, the IRS may assess a penalty for underpayment of estimated tax. Failure to make timely payments can also result in a penalty, even if a refund is due when the taxpayer files his or her return.

Amount of the Estimated Tax Penalty

The estimated tax penalty is calculated using the underpayment rate, which is the federal short-term interest rate plus 3 percentage points [I.R.C. § 6621(a)(2)]. Different rates apply to corporations. The underpayment rate is determined quarterly. A penalty for one of the four quarterly payment periods may be calculated using a different rate than another quarterly period. For the first two quarters of 2018, the underpayment rate was 4% and 5%, respectively.

The estimated tax penalty is calculated separately for each payment and is based on the number of days between the due date and the payment date. See Table 4.1 in IRS Publication 505, *Tax Withholding and Estimated Tax*, for a calendar to determine the number of days that a payment is late.

Form 2210

Taxpayers may use Form 2210, Underpayment of Estimated Tax by Individuals, Estates, and Trusts, to determine if the taxpayer owes a penalty for underpayment of estimated tax, to calculate the penalty, to request a reduction in the penalty, and to apply excess withholding to specific income. Taxpayers determine if they must file Form 2210 using the chart on the first page of the form. The first page of the 2017 form is shown in **Figures 7.11** and **7.12** (the 2018 form was not available at the time of this publication).

FIGURE 7.11 Form 2210, Page 1

Form **2210**

Department of the Treasury
Internal Revenue Service

Underpayment of Estimated Tax by Individuals, Estates, and Trusts

▶ **Go to *www.irs.gov/Form2210* for instructions and the latest information.**

▶ **Attach to Form 1040, 1040A, 1040NR, 1040NR-EZ, or 1041.**

OMB No. 1545-0074

20**17**

Attachment Sequence No. **06**

Name(s) shown on tax return | **Identifying number**

Do You Have To File Form 2210?

Complete lines 1 through 7 below. Is line 7 less than $1,000? — **Yes** → **Don't file Form 2210.** You don't owe a penalty.

No ↓

Complete lines 8 and 9 below. Is line 6 equal to or more than line 9? — **Yes** → You don't owe a penalty. **Don't file Form 2210** (but if box **E** in Part II applies, you must file page 1 of Form 2210).

No ↓

You may owe a penalty. Does any box in Part II below apply? — **Yes** → You **must** file Form 2210. Does box **B, C,** or **D** in Part II apply?

- **Yes** → You must figure your penalty.
- **No** → You **aren't** required to figure your penalty because the IRS will figure it and send you a bill for any unpaid amount. If you want to figure it, you may use Part III or Part IV as a worksheet and enter your penalty amount on your tax return, but **file only page 1 of Form 2210.**

No ↓

Don't file Form 2210. You aren't required to figure your penalty because the IRS will figure it and send you a bill for any unpaid amount. If you want to figure it, you may use Part III or Part IV as a worksheet and enter your penalty amount on your tax return, but **don't file Form 2210.**

FIGURE 7.12 Form 2210, Part II

Part II **Reasons for Filing.** Check applicable boxes. If none apply, **don't** file Form 2210.

A ☐ You request a **waiver** (see instructions) of your entire penalty. You must check this box and file page 1 of Form 2210, but you aren't required to figure your penalty.

B ☐ You request a **waiver** (see instructions) of part of your penalty. You must figure your penalty and waiver amount and file Form 2210.

C ☐ Your income varied during the year and your penalty is reduced or eliminated when figured using the **annualized income installment method.** You must figure the penalty using Schedule AI and file Form 2210.

D ☐ Your penalty is lower when figured by treating the federal income tax withheld from your income as paid on the dates it was actually withheld, instead of in equal amounts on the payment due dates. You must figure your penalty and file Form 2210.

E ☐ You filed or are filing a joint return for either 2016 or 2017, but not for both years, and line 8 above is smaller than line 5 above. You must file page 1 of Form 2210, but you **aren't** required to figure your penalty (unless box **B, C,** or **D** applies).

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 11744P Form **2210** (2017)

If the taxpayer does not have to file Form 2210, then he or she is not required to calculate the penalty. The IRS will calculate the penalty and send the taxpayer a notice showing how it was calculated. If the return is timely filed (not including extensions), and the penalty assessed on the notice is paid by the due date of the notice, no interest is charged on the penalty.

If the taxpayer must file Form 2210 but requests a waiver of the entire penalty, the taxpayer must check box A in Part II of Form 2210, as shown in **Figure 7.12**. The taxpayer files only page 1 of Form 2210, and the IRS will calculate the penalty. Similarly, if the taxpayer is filing jointly for the prior year and separately for the current year (or vice versa), and the maximum annual payment based on the prior-year return is smaller than 90% of the current-year tax, the taxpayer checks box E in Part II and files only the first page.

If the penalty would be reduced by submitting Form 2210, the taxpayer can send the form separately from the tax return, after the taxpayer receives a notice. If the reduction is due to the annualized income installment method, then the taxpayer must complete and submit Form 2210 and Schedule A1, Annualized Income Installment Method (discussed later).

Waiver of the Penalty

The IRS can waive the penalty for underpayment of estimated tax if a casualty or other unusual circumstance occurred and it would be inequitable to impose the penalty [I.R.C. § 6654(e)(3)(A)]. Additionally, the IRS can waive the penalty if the taxpayer retired (after reaching age 62) or became disabled in either of the 2 preceding tax years, there was reasonable cause for the underpayment, and the underpayment was not the result of willful neglect [I.R.C. § 6654(e)(3)(B)]. A taxpayer requesting a waiver based on an unusual circumstance, retirement, or disability must check box A or B in Part II of Form 2210 and attach an explanation with supporting documentation.

CROSS-REFERENCE

Disaster Relief

The penalty for underpayment of estimated tax generally is not automatically waived because of a natural disaster. However, if there is a federally declared disaster, the IRS may automatically postpone the payment due dates for taxpayers in the disaster area. See the discussion of disaster relief in the “Individual Issues” chapter.

Annualized Income Installment Method

For taxpayers who do not receive income evenly during the year, the required estimated tax payment for one or more periods may be more or less than the amount calculated using the regular installment method. The annualized income installment method calculates the tax liability at the end of each payment period based on a reasonable estimate of income, deductions, and other items from the beginning of the tax year through the end of the period.

Example 7.13 Annualized Income Installment Method

Tom Katt is a W-2 wage earner, and he owns and operates a business as a Christmas light installer. Tom files his tax return as head of household. Tom reports his income from the business on Schedule C (Form 1040), Profit or Loss From Business (Sole Proprietorship). Tom receives all his income from the light installation business in the fourth quarter of the calendar year. Tom elects to apply the annualized income installment method for his 2018 estimated tax payments.

Tom’s 2017 total tax liability was $17,850. His 2018 tax liability is $14,033 plus $4,945 of self-employment (SE) tax. **Figure 7.13** shows Tom’s income from all sources, federal withholding, and estimated tax payments by estimated tax payment period.

FIGURE 7.13 Tom Katt's Income, Federal Withholding, and Estimated Tax Payments by Estimated Tax Payment Period

	1/1–3/31	4/1–5/31	6/1–8/31	9/1–12/31	Total Year
W-2 income	$16,500	$11,000	$16,500	$22,000	$66,000
Business income (Schedule C)	0	0	0	35,000	35,000
Total income	$16,500	$11,000	$16,500	$57,000	$101,000
Federal tax withholding	$1,500	$1,000	$1,500	$ 2,000	$ 6,000
Estimated tax payments	0	0	0	11,080	11,080
Total payments	$1,500	$1,000	$1,500	$13,080	$17,080

Tom will itemize deductions on his 2018 tax return. **Figure 7.14** shows Tom's itemized deductions by estimated tax payment period.

FIGURE 7.14 Tom Katt's Itemized Deductions Paid by Estimated Tax Payment Period

Description	1/1–3/31	4/1–5/31	6/1–8/31	9/1–12/31	Total
Charitable contributions	$1,500	$1,500	$1,500	$3,000	$7,500
Mortgage interest	1,850	1,850	1,850	1,850	7,400
Real estate taxes	750	750	750	750	3,000
State income tax	600	600	600	600	2,400
State estimated tax	0	0	0	3,000	3,000
Total	$4,700	$4,700	$4,700	$9,200	$23,300
Cumulative total	$4,700	$9,400	$14,100	$23,300	$23,300

Figure 7.15 shows Tom's Form 2210, Part I. Figures 7.15, 7.16, and 7.17 show the 2017 form, as the 2018 form was not available at the time of this publication. The form calculates a $17,080 minimum tax payment for 2018. The form does not include any QBI deduction.

FIGURE 7.15 Tom Katt's Form 2210, Page 1

Form **2210**
Department of the Treasury
Internal Revenue Service

Underpayment of Estimated Tax by Individuals, Estates, and Trusts
► Go to *www.irs.gov/Form2210* for instructions and the latest information.
► Attach to Form 1040, 1040A, 1040NR, 1040NR-EZ, or 1041.

OMB No. 1545-0074
2017
Attachment Sequence No. 06

Name(s) shown on tax return | **Identifying number**

Do You Have To File Form 2210?

Complete lines 1 through 7 below. Is line 7 less than $1,000? — **Yes** → **Don't file Form 2210.** You don't owe a penalty.

No ↓

Complete lines 8 and 9 below. Is line 6 equal to or more than line 9? — **Yes** → You don't owe a penalty. **Don't file Form 2210** (but if box **E** in Part II applies, you must file page 1 of Form 2210).

No ↓

You may owe a penalty. Does any box in Part II below apply? — **Yes** → You **must** file Form 2210. Does box **B, C,** or **D** in Part II apply?

- **Yes** → You must figure your penalty.
- **No** → You **aren't** required to figure your penalty because the IRS will figure it and send you a bill for any unpaid amount. If you want to figure it, you may use Part III or Part IV as a worksheet and enter your penalty amount on your tax return, but **file only page 1 of Form 2210.**

No ↓

Don't file Form 2210. You aren't required to figure your penalty because the IRS will figure it and send you a bill for any unpaid amount. If you want to figure it, you may use Part III or Part IV as a worksheet and enter your penalty amount on your tax return, but **don't file Form 2210.**

Part I Required Annual Payment

1	Enter your 2017 tax after credits from Form 1040, line 56 (see instructions if not filing Form 1040)			1	14,033
2	Other taxes, including self-employment tax and, if applicable, Additional Medicare Tax and/or Net Investment Income Tax (see instructions)			2	4,945
3	Refundable credits, including the premium tax credit (see instructions)			3	(0)
4	Current year tax. Combine lines 1, 2, and 3. If less than $1,000, **stop;** you don't owe a penalty. **Don't** file Form 2210			4	18,978
5	Multiply line 4 by 90% (0.90)	5	17,080		
6	Withholding taxes. **Don't** include estimated tax payments (see instructions)			6	6,000
7	Subtract line 6 from line 4. If less than $1,000, **stop;** you don't owe a penalty. **Don't** file Form 2210			7	12,978
8	Maximum required annual payment based on prior year's tax (see instructions)			8	17,850
9	**Required annual payment.** Enter the **smaller** of line 5 or line 8			9	17,080

Next: Is line 9 more than line 6?

☐ **No.** You **don't** owe a penalty. **Don't** file Form 2210 unless box **E** below applies.

☑ **Yes.** You may owe a penalty, but **don't** file Form 2210 unless one or more boxes in Part II below applies.

- If box **B, C,** or **D** applies, you must figure your penalty and file Form 2210.
- If box **A** or **E** applies (but not **B, C,** or **D**) file only page 1 of Form 2210. You **aren't** required to figure your penalty; the IRS will figure it and send you a bill for any unpaid amount. If you want to figure your penalty, you may use Part III or IV as a worksheet and enter your penalty on your tax return, but **file only page 1 of Form 2210.**

Tom then checks box C in Part II and completes Form 2210, Schedule A1, Annualized Income Installment Method. **Figure 7.16** shows his completed Schedule A1.

FIGURE 7.16 Tom Katt's Form 2210, Schedule A1

Form 2210 (2017) Page **4**

Schedule AI—Annualized Income Installment Method (See the instructions.)

Estates and trusts, **don't** use the period ending dates shown to the right. Instead, use the following: 2/28/17, 4/30/17, 7/31/17, and 11/30/17.		**(a)** 1/1/17–3/31/17	**(b)** 1/1/17–5/31/17	**(c)** 1/1/17–8/31/17	**(d)** 1/1/17–12/31/17
Part I Annualized Income Installments					
1 Enter your adjusted gross income for each period (see instructions). (Estates and trusts, enter your taxable income without your exemption for each period.)	1	16,500	27,500	44,000	98,527
2 Annualization amounts. (Estates and trusts, see instructions)	2	4	2.4	1.5	1
3 Annualized income. Multiply line 1 by line 2	3	66,000	66,000	66,000	98,527
4 If you itemize, enter itemized deductions for the period shown in each column. All others enter -0-, and skip to line 7. **Exception:** Estates and trusts, skip to line 9 and enter amount from line 3	4	4,700	9,400	14,100	23,300
5 Annualization amounts	5	4	2.4	1.5	1
6 Multiply line 4 by line 5 (see instructions if line 3 is more than $156,900)	6	18,800	22,560	21,150	23,300
7 In each column, enter the full amount of your standard deduction from Form 1040, line 40, or Form 1040A, line 24. (Form 1040NR or 1040NR-EZ filers, enter -0-. **Exception:** Indian students and business apprentices, see instructions.)	7	18,000	18,000	18,000	18,000
8 Enter the **larger** of line 6 or line 7	8	18,800	22,560	21,150	23,300
9 Subtract line 8 from line 3	9	47,200	43,440	44,850	75,227
10 In each column, multiply $4,050 by the total number of exemptions claimed (see instructions if line 3 is more than $156,900). (Estates, trusts, and Form 1040NR or 1040NR-EZ filers, see instructions.)	10	N/A	N/A	N/A	N/A
11 Subtract line 10 from line 9. If zero or less, enter -0-	11	47,200	43,440	44,850	75,227
12 Figure your tax on the amount on line 11 (see instructions)	12	5,395	4,939	5,113	11,098
13 Self-employment tax from line 34 (complete Part II below)	13	0	0	0	4,945
14 Enter other taxes for each payment period including, if applicable, Additional Medicare Tax and/or Net Investment Income Tax (see instructions)	14	0	0	0	0
15 Total tax. Add lines 12, 13, and 14	15	5,395	4,939	5,113	16,043
16 For each period, enter the same type of credits as allowed on Form 2210, Part I, lines 1 and 3 (see instructions)	16	0	0	0	0
17 Subtract line 16 from line 15. If zero or less, enter -0-	17	5,395	4,939	5,113	16,043
18 Applicable percentage	18	22.5%	45%	67.5%	90%
19 Multiply line 17 by line 18	19	1,214	2,223	3,451	14,439
Complete lines 20–25 of one column before going to line 20 of the next column.					
20 Enter the total of the amounts in all previous columns of line 25	20		1,214	2,223	3,451
21 Subtract line 20 from line 19. If zero or less, enter -0-	21	1,214	1,009	1,228	10,988
22 Enter 25% (0.25) of line 9 on page 1 of Form 2210 in each column	22	4,270	4,270	4,270	4,270
23 Subtract line 25 of the previous column from line 24 of that column	23		3,056	6,317	9,359
24 Add lines 22 and 23	24	4,270	7,326	10,587	13,629
25 Enter the **smaller** of line 21 or line 24 here and on Form 2210, Part IV, line 18 ▶	25	1,214	1,009	1,228	10,988
Part II Annualized Self-Employment Tax (Form 1040 and Form 1040NR filers only)					
26 Net earnings from self-employment for the period (see instructions)	26	0	0	0	32,323
27 Prorated social security tax limit (for 2018)	27	~~$31,800~~	~~$53,000~~	~~$84,800~~	~~$127,200~~
28 Enter actual wages for the period subject to social security tax or the 6.2% portion of the 7.65% railroad retirement (tier 1) tax. **Exception:** If you filed Form 4137 or Form 8919, see instructions	28	$32,100 16,500	$53,500 11,000	$85,600 16,500	$128,400 22,000
29 Subtract line 28 from line 27. If zero or less, enter -0-	29	15,600	42,500	69,100	106,400
30 Annualization amounts	30	0.496	0.2976	0.186	0.124
31 Multiply line 30 by the **smaller** of line 26 or line 29	31	0	0	0	4,008
32 Annualization amounts	32	0.116	0.0696	0.0435	0.029
33 Multiply line 26 by line 32	33	0	0	0	937
34 Add lines 31 and 33. Enter here and on line 13 above ▶	34	0	0	0	4,945

Form **2210** (2017)

Line 1 includes income from all sources. The first-period through third-period columns show only the W-2 income Tom earns evenly throughout the year. The fourth-period column includes both W-2 income and business income from the lighting business minus $2,473 (one-half of SE tax).

Tom reports his itemized deductions on line 4 (see Figure 7.14). Part II on page 4 calculates SE tax for each estimated tax period. Line 25 is the income tax liability for each estimated tax period.

Tom then completes Part IV of Form 2210 to calculate his $0 estimated tax penalty. **Figure 7.17** shows Tom's completed Part IV.

FIGURE 7.17 Tom Katt's Form 2210, Part IV

Form 2210 (2017) Page **3**

Part IV **Regular Method** (See the instructions if you are filing Form 1040NR or 1040NR-EZ.)

Section A—Figure Your Underpayment		**Payment Due Dates** (a) 4/15/17	(b) 6/15/17	(c) 9/15/17	(d) 1/15/18
18 **Required installments.** If box C in Part II applies, enter the amounts from Schedule AI, line 25. Otherwise, enter 25% (0.25) of line 9, Form 2210, in each column	18	1,214	1,009	1,228	10,988
19 Estimated tax paid and tax withheld (see the instructions). For column (a) only, also enter the amount from line 19 on line 23. If line 19 is equal to or more than line 18 for all payment periods, stop here; you don't owe a penalty. **Don't file Form 2210 unless you checked a box in Part II**	19	1,500	1,000	1,500	13,080
Complete lines 20 through 26 of one column before going to line 20 of the next column.					
20 Enter the amount, if any, from line 26 in the previous column	20		286	277	549
21 Add lines 19 and 20	21		1,286	1,777	13,629
22 Add the amounts on lines 24 and 25 in the previous column	22		0	0	0
23 Subtract line 22 from line 21. If zero or less, enter -0-. For column (a) only, enter the amount from line 19	23	1,500	1,286	1,777	13,629
24 If line 23 is zero, subtract line 21 from line 22. Otherwise, enter -0-	24		0	0	
25 **Underpayment.** If line 18 is equal to or more than line 23, subtract line 23 from line 18. Then go to line 20 of the next column. Otherwise, go to line 26 ▶	25				
26 Overpayment. If line 23 is more than line 18, subtract line 18 from line 23. Then go to line 20 of the next column	26	286	277	549	

Section B—Figure the Penalty (Use the Worksheet for Form 2210, Part IV, Section B—Figure the Penalty in the instructions.)

27 **Penalty.** Enter the total penalty from line 14 of the Worksheet for Form 2210, Part IV, Section B—Figure the Penalty. Also include this amount on Form 1040, line 79; Form 1040A, line 51; Form 1040NR, line 76; Form 1040NR-EZ, line 26; or Form 1041, line 26. **Don't file Form 2210 unless you checked a box in Part II** ▶	27	0

Form **2210** (2017)

Part IV reconciles Tom's actual deposits for each estimated tax period with the amount owed for that period. The annualized income installment method shows that Tom had no underpayment in any of the four periods. If Tom did not use the annualized income installment method, Tom's estimated tax liability would have been $4,270 ($17,080 ÷ 4) per period and he would have had an underpayment in each of the first three periods.