

Individual Estimated Taxes

Congress has provided two complementary methods to ensure the current payment of taxes by individuals as income is earned. The first method—withholding—is intended to satisfy the tax obligations of most wage earners. The second method—payment of estimated taxes—covers situations in which there might be inadequate withholding (when a person has a high salary or investment income) or no withholding (when a person is self-employed or has no income except for investments).

While there is no obligation on an individual to pay estimated tax, a penalty is imposed if estimated tax payments are inadequate. Individuals thus face the choice of either making adequate estimated tax payments on a timely basis or incurring a penalty.

To avoid the penalty, an individual taxpayer must timely pay the amount of each required installment. A required installment is 25 percent of the "required annual payment," unless the taxpayer chooses to annualize income. The required annual payment is the smaller of:

- 90 percent of the tax shown on the current year's tax return, or
- 100 percent (or a higher amount for high-income taxpayers) of the tax shown on the taxpayer's return for the preceding tax year, provided the preceding tax year consisted of twelve months and a return was filed for that preceding tax year.

The first exception can be satisfied by paying the tax in equal installments or in installments based on each period's earnings placed on an annualized basis.

For high-income taxpayers whose adjusted gross income (AGI) shown on the preceding year's tax return exceeds \$150,000 (or \$75,000 for a married individual filing separately), the required annual payment is the lesser of 90 percent of the tax for the current year, or 110% of the tax shown on the return for the preceding tax year.

For purposes of the estimated tax rules, the term "tax" means income tax (including the alternative minimum tax) and self-employment tax, reduced by any credits against tax (other than the credit for taxes withheld). In addition, household employment taxes are included in determining the amount of estimated tax payments.

Amounts withheld from a taxpayer's wages or as backup withholding are treated as a payment of estimated tax and divided equally among the required installment dates, unless the taxpayer establishes the actual dates withheld.

The due dates for required installments are April 15, June 15, September 15, and January 15 of the following tax year.