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Tax Withholding and Estimated Tax



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Introduction

The federal income tax is a pay-as-you-go tax. You must pay the tax as you earn or receive income during the year. There are two ways to pay as you go.

- **Withholding.** If you are an employee, your employer probably withholds income tax from your pay. Tax may also be withheld from certain other income — including pensions, bonuses, commissions, and

gambling winnings. In each case, the amount withheld is paid to the Internal Revenue Service (IRS) in your name.

- **Estimated tax.** If you do not pay your tax through withholding, or do not pay enough tax that way, you might have to pay estimated tax. People who are in business for themselves generally will have to pay their tax this way. You may have to pay estimated tax if you receive income such as dividends, interest, capital gains, rents, and royalties. Estimated tax is used to pay not only income tax, but self-employment tax and alternative minimum tax as well.

This publication explains both of these methods. It also explains how to take credit on your return for the tax that was withheld and for your estimated tax payments.

If you did not pay enough tax during the year either through withholding or by making estimated tax payments, you may have to pay a penalty. The IRS usually can figure this penalty for you. This underpayment penalty, and the exceptions to it, are discussed in chapter 4.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

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Important Changes for 2001

You should consider the items in this section when figuring any underpayment penalty for 2001. Figuring the penalty is discussed in chapter 4.

Penalty rate. The penalty for underpayment of 2001 estimated tax is figured at an annual rate of 8% for the number of days the underpayment remained unpaid from April 16, 2000, through June 30, 2001; 7% from July 1, 2001, through December 31, 2001; 6% from January 1, 2002, through April 15, 2002.

Estimated tax safe harbor for higher income individuals. For installment payments for tax years beginning in 2001, the estimated tax safe harbor for higher income individuals (other than farmers and fishermen) has been modified. If your adjusted gross income was more than \$150,000 (\$75,000 if married filing a separate return), you must have deposited the smaller of 90% of your expected tax for 2001 or **110%** of the tax shown on your 2000 return to avoid an estimated tax penalty.

Important Changes for 2002

You should consider the items in this section when you figure your estimated tax or how much income tax you want withheld from your pay for 2002. For more information on these and other tax changes, see Publication 553, *Highlights of 2001 Tax Changes*.

Estimated tax safe harbor for higher income individuals. For installment payments for tax years beginning in 2002, the estimated tax safe harbor for higher income individuals (other than farmers and fishermen) has been modified. If your adjusted gross income is more than \$150,000 (\$75,000 if married filing a separate return), you will have to deposit the smaller of 90% of your expected tax for 2002 or **112%** of the tax shown on your 2001 return to avoid an estimated tax penalty.

Certain withholding rates decreased. The withholding rates on the following items have been decreased.

- 1) **Gambling winnings.** The rate has decreased from 28% to 27%.
- 2) **Unemployment compensation.** The rate has decreased from 15% to 10%.
- 3) **Federal payments.** Withholding on certain federal payments is voluntary. The elective rates have been decreased to 7%, 10%, 15%, and 27%.
- 4) **Backup withholding.** The rate has decreased from 31% to 30%.
- 5) **Supplemental wages.** The rate has decreased from 28% to 27%.

Withholding on these items is discussed in chapter 1.

Tax rates reduced. For tax years beginning in 2002, the income tax rates have been reduced. The following items highlight these changes.

10% tax rate. The 10% tax rate is reflected in the tax tables and tax schedules. You do not have to make a separate computation or figure a credit to get the benefits of this rate.

Other tax rates. The other tax rates, 27.5%, 30.5%, 35.5%, and 39.1% are reduced to 27%, 30%, 35%, and 38.6%, respectively. These reduced rates should be reflected in amounts withheld (such as backup withholding) on certain payments made after 2001.

Earned income credit (EIC). Significant changes to the EIC take effect in 2002.

- Earned income will no longer include non-taxable employee compensation.
- The EIC will be based, in part, on adjusted gross income (AGI), *not* modified AGI.
- New rules will be used to determine which person can claim a qualifying child when two or more persons may be able to claim the same child.
- The definition of an eligible foster child will change. The child will have to live with you for more than half of the year, instead of the whole year.

- The EIC will no longer be reduced by the amount of alternative minimum tax shown on your return.

Higher education expenses. You may be able to deduct as an adjustment to income up to \$3,000 of qualified tuition and related expenses you paid. The expenses can be for you, your spouse, or your dependent.

Interest on student loans. Two changes apply to the deduction for student loan interest.

- The provision that limited your deduction to interest paid during the first 60 months is repealed.
- The modified AGI phaseout amounts are increased.

For more information on the deduction for student loan interest, see Publication 970.

Coverdell education savings accounts. The following changes apply to Coverdell education savings accounts.

- Contribution limit increases to \$2,000 per beneficiary.
- The income phase out increases for joint filers.
- Qualified education expenses include elementary and secondary school expenses.
- Age limits do not apply to "special needs" beneficiaries.
- Contributions may be made until April 15 of the following year.
- Tax-free distributions can be used for special needs services.

Employer-provided educational assistance. The following changes apply to employer-provided educational assistance.

- The exclusion is made permanent.
- The exclusion applies to graduate level courses.

Qualified tuition programs. The qualified tuition program (formerly qualified state tuition program) includes programs established and maintained by one or more eligible educational institutions. Two other changes affect this program.

- Distributions from a state program that are used to pay qualified higher education expenses are tax free. Other distributions are subject to 10% additional tax.
- Tax-free distributions can be used for special needs services.

Tax benefits for adoption. Changes apply to the adoption credit and to the exclusion for benefits under an employer-provided adoption assistance program. These changes include the following.

- The credit for children without special needs is made permanent.
- The exclusion under an adoption assistance program is made permanent.

- The credit and exclusion amounts increased to a maximum of \$10,000.
- The modified AGI phaseout amounts increased.

Benefits for public safety officer’s survivors.

For tax years beginning after 2001, a survivor annuity received by the spouse, former spouse, or child of a public safety officer killed in the line of duty will generally be excluded from the recipient’s income regardless of the date of the officer’s death. Survivor benefits received before 2002 are excluded only if the officer died after 1996.

Foreign earned income exclusion. The amount of foreign earned income that you can exclude will increase to \$80,000. See Publication 54.

Self-employed health insurance deduction. The part of your self-employed health insurance premiums that you can deduct as an adjustment to income increases to 70%.

Retirement savings plans. The following paragraphs highlight changes that affect individual retirement arrangements (IRAs) and pension plans.

Increased IRA contribution and deduction limit. Your maximum contribution (and any allowable deduction) limit is increased. Previ-

ously, the limit was \$2,000. The new limit depends on your age at the end of the year.

- If you are under age 50, the most you can contribute is the smaller of \$3,000, or your taxable compensation.
- If you are age 50 or older, the most you can contribute is the smaller of \$3,500, or your taxable compensation.

Rollovers of IRAs into qualified plans. For distributions after December 31, 2001, you may be able to roll over tax free, a distribution from your IRA into a qualified plan.

Rollovers of distributions from employer plans. For distributions after December 31, 2001, you can roll over both the taxable and nontaxable part of a distribution from a qualified plan into a traditional IRA.

Hardship exception to the 60-day rule. For distributions after December 31, 2001, the IRS may waive the 60-day requirement to roll over distributions from your IRA or your employer’s pension plan where the failure to do so would be against equity or good conscience, including casualty, disaster, or other events beyond your reasonable control.

Limit on elective deferrals. The maximum amount of elective deferrals under a salary reduction agreement that can be contributed to a qualified plan is increased to \$11,000 (\$12,000 if

you are age 50 or over). However, for SIMPLE plans, the amount is increased to \$7,000 (\$7,500 if you are age 50 or over).

New credit for elective deferrals and IRA contributions. You may be able to take a credit of up to \$1,000 for qualified retirement savings contributions.

Meal expenses when subject to “hours of service limits.” If you are subject to the Department of Transportation’s “hours of service” limits, the percentage of your business-related meal expenses that you can deduct has increased. For 2002 and 2003, you can deduct 65% if the meals take place during or incident to the period subject to those limits.

Important Reminder

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1-800-THE-LOST (1-800-843-5678)** if you recognize a child.

1.

Tax Withholding for 2002

Important Changes

Certain withholding rates decreased. The withholding rates on the following items have been decreased.

- 1) **Gambling winnings.** The rate has decreased from 28% to 27%.
- 2) **Unemployment compensation.** The rate has decreased from 15% to 10%.
- 3) **Federal payments.** Withholding on certain federal payments is voluntary. The elective rates have been decreased to 7%, 10%, 15%, and 27%.
- 4) **Backup withholding.** The rate has decreased from 31% to 30%.
- 5) **Supplemental wages.** The rate has decreased from 28% to 27%.

Introduction

This chapter discusses withholding on these types of income:

- Salaries and wages,
- Tips,
- Taxable fringe benefits,
- Sick pay,
- Pensions and annuities,
- Gambling winnings,
- Unemployment compensation, and
- Federal payments.

This chapter explains in detail the rules for withholding tax from each of these types of income. The discussion of salaries and wages includes an explanation of how to complete a Form W-4.

This chapter also covers backup withholding on interest, dividends, and other payments.

Useful Items

You may want to see:

Publication

- 919** How Do I Adjust My Tax Withholding?

Form (and Instructions)

- W-4** Employee's Withholding Allowance Certificate
- W-4P** Withholding Certificate for Pension or Annuity Payments

- W-4S** Request for Federal Income Tax Withholding From Sick Pay
- W-4V** Voluntary Withholding Request

See chapter 5 of this publication for information about getting these publications and forms.

Salaries and Wages

Income tax is withheld from the pay of most employees. Your pay includes your regular pay, bonuses, commissions, and vacation allowances. It also includes reimbursements and other expense allowances paid under a nonaccountable plan. See *Supplemental Wages*, later, for more information about reimbursements and allowances paid under an accountable plan.

Military retirees. Military retirement pay is treated in the same manner as regular pay for income tax withholding purposes, even though it is treated as a pension or annuity for other tax purposes.

Household workers. If you are a household worker, you can ask your employer to withhold income tax from your pay. A household worker is an employee who performs household work in a private home, local college club, or local fraternity or sorority chapter.

Tax is withheld only if you want it withheld and your employer agrees to withhold it. If you do not have enough income tax withheld, you may have to make estimated tax payments, as discussed in chapter 2.

Farmworkers. Income tax is generally withheld from your cash wages for work on a farm unless your employer both:

- 1) Pays you cash wages of less than \$150 during the year, and
- 2) Has expenditures for agricultural labor totaling less than \$2,500 during the year.

If you receive either noncash wages or cash wages not subject to withholding, you can ask your employer to withhold income tax. If your employer does not agree to withhold tax, or if not enough is withheld, you may have to make estimated tax payments, as discussed in chapter 2.

Determining Amount of Tax Withheld

The amount of income tax your employer withholds from your regular pay depends on two things.

- 1) The amount you earn.
- 2) The information you give your employer on Form W-4.

Form W-4 includes three types of information that your employer will use to figure your withholding.

- 1) Whether to withhold at the single rate or at the lower married rate.
- 2) How many withholding allowances you claim (each allowance reduces the amount withheld).

- 3) Whether you want an additional amount withheld.

If your income is low enough that you will not have to pay income tax for the year, you may be exempt from withholding. This is explained under *Exemption From Withholding*, later.

Note. You must specify a filing status and a number of withholding allowances on Form W-4. You cannot specify only a dollar amount of withholding.

New job. When you start a new job, you must fill out a Form W-4 and give it to your employer. Your employer should have copies of the form. If you need to change the information, you must fill out a new form.

If you work only part of the year (for example, you start working after the beginning of the year), too much tax may be withheld. You may be able to avoid overwithholding if your employer agrees to use the part-year method, explained later.

Changing your withholding. Events during the year may change your marital status or the exemptions, adjustments, deductions, or credits you expect to claim on your return. When this happens, you may need to give your employer a new Form W-4 to change your withholding status or number of allowances.

You **must** give your employer a new Form W-4 within 10 days after either of the following.

- 1) Your divorce, if you have been claiming married status.
- 2) Any event that decreases the number of withholding allowances you can claim.

Events that will decrease the number of withholding allowances you can claim include the following.

- 1) You have been claiming an allowance for your spouse, but you get divorced or your spouse begins claiming his or her own allowance on a separate Form W-4.
- 2) You have been claiming an allowance for a dependent, but you no longer expect to provide more than half the dependent's support for the year.
- 3) You have been claiming an allowance for your child, but you now find that he or she will earn more than \$3,000 during the year. In addition, he or she will be:
 - a) 24 or older by the end of the year, or
 - b) 19 or older by the end of the year and will not qualify as a student.

- 4) You have been claiming allowances for your expected deductions, but you now find that they will be less than you expected.

Generally, you can submit a new Form W-4 whenever you wish to change the number of your withholding allowances for any other reason.

If you change the number of your withholding allowances, you can request that your employer withhold using the cumulative wage method, explained later.

Changing your withholding for 2003. If events in 2002 will decrease the number of your

withholding allowances for 2003, you **must** give your employer a new Form W-4 by December 1, 2002. If an event occurs in December 2002, submit a new Form W-4 within 10 days. Events that will decrease the number of your allowances include the following.

- You claimed allowances for 2002 based on child care expenses, moving expenses, or large medical expenses, but you will not have these expenses in 2003.
- You have been claiming an allowance for your spouse, but he or she died in 2002.

Note. Because you can still file a joint return for 2002, your spouse's death will not affect the number of your withholding allowances until 2003. You will also have to change from married to single status for 2003, unless you can file as a qualifying widow or widower because you have a dependent child, or you remarry.

You must file a new Form W-4 showing single status by December 1 of the last year you are eligible to file as qualifying widow or widower.

Part-year method. If you work only part of the year and your employer agrees to use the part-year withholding method, less tax will be withheld from each wage payment than would be withheld if you worked all year. To be eligible for the part-year method, you must meet both the following requirements.

- 1) **You must use the calendar year** (the 12 months from January 1 through December 31) as your tax year. You cannot use a fiscal year.
- 2) **You must not expect to be employed for more than 245 days during the year.** To figure this limit, count all calendar days that you are employed (including week-ends, vacations, and sick days) beginning the first day you are on the job for pay and ending your last day of work. If you are temporarily laid off for 30 days or less, count those days too. If you are laid off for more than 30 days, do not count those days. You will not meet this requirement if you begin working before May 1 and expect to work for the rest of the year.

How to apply for the part-year method. You must ask in writing that your employer use this method. The request must state all three of the following.

- 1) The date of your last day of work for any prior employer during the current calendar year.
- 2) That you do not expect to be employed more than 245 days during the current calendar year.
- 3) That you use the calendar year as your tax year.

Cumulative wage method. If you change the number of your withholding allowances during the year, too much or too little tax may have been withheld for the period before you made the change. You may be able to compensate for this if your employer agrees to use the cumulative wage withholding method for the rest of the

year. You must ask in writing that your employer use this method.

To be eligible, you must have been paid for the same kind of payroll period (weekly, bi-weekly, etc.) since the beginning of the year.

Checking your withholding. After you have given your employer a Form W-4, you can check to see whether the amount of tax withheld from your pay is too little or too much. See *Getting the Right Amount of Tax Withheld*, later. If too much or too little tax is being withheld, you should give your employer a new Form W-4 to change your withholding.

Note. You cannot give your employer either a payment to cover withholding for past pay periods or a payment for estimated tax.

Completing Form W-4 and Worksheets

The discussion that follows explains in detail how to fill out Form W-4. It has more detailed information about some topics than the Form W-4 instructions.

In reading this discussion, you may find it helpful to refer to the filled-in Form W-4 in *Example 1.3*, later in this chapter.

Marital Status (Line 3 of Form W-4)

There is a lower withholding rate for people who can claim married status on line 3 of Form W-4. Everyone else must have tax withheld at the higher single rate. (Also, see *Getting the Right Amount of Tax Withheld*, later.)

You must claim **single** status if either of the following applies.

- 1) **You are single.** If you are divorced, or separated from your spouse under a court decree of separate maintenance, you are considered single.
- 2) **You are married, but either you or your spouse is neither a citizen nor a resident of the United States.** However, if one of you is a citizen or a resident, you can choose to have the other treated as a resident. You can then file a joint return and claim married status on your Form W-4. See *Nonresident Spouse Treated as a Resident* in chapter 1 of Publication 519, *U.S. Tax Guide for Aliens*, for more information.

You can claim **married** status if either of the following applies.

- 1) **You are married and neither you nor your spouse is a nonresident alien.** You are considered married for the whole year even if your spouse died during the year.
- 2) **You expect to be able to file your return as a qualifying widow or widower.** You usually can use this filing status if your spouse died within the previous 2 years and you provide a home for your dependent child. However, you must file a new Form W-4 showing your filing status as single by December 1 of the last year you are eligible to file as a qualifying widow or widower. For more information, see *Quali-*

fyng Widow(er) With Dependent Child under *Filing Status* in Publication 501, *Exemptions, Standard Deduction, and Filing Information*.

Some married people find that they do not have enough tax withheld at the married rate. This can happen, for example, when both spouses work. To avoid this, you can claim **married, but withhold at higher single rate** (even if you qualify for the married rate). Also, you can fill out the *Two-Earner/Two-Job Worksheet*, explained later.

Withholding Allowances (Line 5 of Form W-4)

The more allowances you claim on Form W-4, the less income tax your employer will withhold. You will have the most tax withheld if you claim "0" allowances. The number of allowances you can claim depends on the following factors.

- How many exemptions you can take on your tax return.
- Whether you have income from more than one job.
- What deductions, adjustments to income, and credits you expect to have for the year.
- Whether you will file as head of household.

If you are married, it also depends on whether your spouse also works and claims any allowances on his or her own Form W-4.

Form W-4 worksheets. Form W-4 has worksheets to help you figure how many withholding allowances you can claim. The worksheets are for your own records. Do not give them to your employer.

Complete only one set of Form W-4 worksheets, no matter how many jobs you have. If you are married and will file a joint return, complete only one set of worksheets for you and your spouse, even if you both earn wages and must each give a Form W-4 to your employers. Complete separate sets of worksheets only if you and your spouse will file separate returns.

If you are not exempt from withholding (see *Exemption From Withholding*, later), complete the *Personal Allowances Worksheet* on page 1 of the form. You should also use the worksheets on page 2 of the form to adjust the number of your withholding allowances for itemized deductions and adjustments to income, and for two-earner or two-job situations. If you want to adjust the number of your withholding allowances for certain tax credits, use the *Deductions and Adjustments Worksheet* on page 2 of Form W-4, even if you do not have any deductions or adjustments.

Complete all worksheets that apply to your situation. The worksheets will help you figure the maximum number of withholding allowances you are entitled to claim so that the amount of income tax withheld from your wages will match, as closely as possible, the amount of income tax you will owe at the end of the year.

Two jobs. If you have income from two jobs at the same time, complete only one set of Form W-4 worksheets. Then split your allowances

between the Forms W-4 for each job. You cannot claim the same allowances with more than one employer at the same time. You can claim all your allowances with one employer and none with the other, or divide them any other way.

Married individuals. If both you and your spouse are employed and expect to file a joint return, figure your withholding allowances using your combined income, adjustments, deductions, exemptions, and credits. Use only one set of worksheets. You can divide your total allowances any way, but you cannot claim an allowance that your spouse also claims.

If you and your spouse expect to file separate returns, figure your allowances separately based on your own individual income, adjustments, deductions, exemptions, and credits.

Alternative method of figuring withholding allowances. You can take into account most items of income, adjustments to income, deductions, and tax credits in figuring the number of your withholding allowances. Because the Form W-4 worksheets use a simplified method to take these items into account, they do not always result in withholding that is exactly equal to the tax you will owe. You do not have to use the worksheets if you use a more accurate method of figuring the number of withholding allowances.

The method you use must be based on withholding schedules, the tax rate schedules, and the 2002 Estimated Tax Worksheet in chapter 2. It must take into account only the items of income, adjustments to income, deductions, and tax credits that are taken into account on Form W-4.

You can use the number of withholding allowances determined under this alternative method rather than the number determined using the Form W-4 worksheets. You must still give your employer a Form W-4 claiming your withholding allowances.

Employees who are not citizens or residents. If you are neither a citizen nor a resident of the United States, you usually can claim only one withholding allowance. This rule does not apply if you are a resident of Canada or Mexico, or if you are a U.S. national. It also does not apply if your spouse is a U.S. citizen or resident and you have chosen to be treated as a resident of the United States. Special rules apply to residents of Korea, Japan, and India. For more information, see *Withholding From Compensation* in chapter 8 of Publication 519.

Personal Allowances Worksheet

Use the *Personal Allowances Worksheet* on page 1 of Form W-4 to figure your withholding allowances for all of the following that apply.

- Exemptions.
- Only one job.
- Head of household status.
- Child and dependent care credit.
- Child tax credit.

Exemptions (worksheet lines A, C, and D). You can claim one withholding allowance for each exemption you expect to claim on your tax return.

Self. You can claim an allowance for your exemption on line A unless another person can claim an exemption for you on his or her tax return. If another person is entitled to claim an exemption for you, you cannot claim an allowance for your exemption even if the other person will not claim your exemption or the exemption will be reduced or eliminated under the phaseout rule.

Spouse. You can claim an allowance for your spouse's exemption on line C unless your spouse is claiming his or her own exemption or another person can claim an exemption for your spouse. Do not claim this allowance if you and your spouse expect to file separate returns.

Dependents. You can claim one allowance on line D for each exemption you will claim for a dependent on your tax return.

Phaseout. For 2002, your deduction for personal exemptions is phased out if your adjusted gross income (AGI) falls within the following brackets.

Table 1.1

Single	\$137,300–\$259,800
Married filing jointly or qualifying widow(er)	\$206,000–\$328,500
Married filing separately	\$103,000–\$164,250
Head of household	\$171,650–\$294,150



If you expect your AGI to be more than the highest amount in the above bracket for your filing status, enter "0" on lines A, C, and D. If your AGI will fall within the bracket, use the following worksheet to figure the total allowances for those lines.

Worksheet 1.1

1. Enter your expected AGI _____
2. Enter:
 - \$137,300 if single
 - \$206,000 if married filing jointly or qualifying widow(er)
 - \$103,000 if married filing separately
 - \$171,650 if head of household _____
3. Subtract line 2 from line 1 _____
4. Divide the amount on line 3 by \$125,000 (\$62,500 if married filing separately). Enter the result as a decimal _____
5. Enter the number of allowances on lines A, C, and D of the Personal Allowances Worksheet without regard to the phaseout rule _____
6. Multiply line 4 by line 5. If the result is not a whole number, increase it to the next higher whole number _____
7. Subtract line 6 from line 5. This is the maximum number you should enter on lines A, C, and D of the Personal Allowances Worksheet _____

Only one job (worksheet line B). You can claim an additional withholding allowance if any of the following apply.

- You are single, and you have only one job at a time.
- You are married, you have only one job at a time, and your spouse does not work.
- Your wages from a second job or your spouse's wages (or the total of both) are \$1,000 or less.

If you qualify for this allowance, enter "1" on line B of the worksheet.

Head of household (worksheet line E). You can file as head of household if you are unmarried and pay more than half the cost of keeping up a home for yourself and your dependent or other qualifying individual. For more information, see *Head of Household* under *Filing Status* in Publication 501.

If you expect to file as head of household on your 2002 tax return, enter "1" on line E of the worksheet.

Child and dependent care credit (worksheet line F). Enter "1" on line F if you expect to claim a credit for at least \$1,500 of qualifying child or dependent care expenses on your 2002 return. Generally, qualifying expenses are those you pay for the care of your dependent who is under age 13 or for your spouse or dependent who is not able to care for himself or herself so that you can work or look for work. For more information, get Publication 503, *Child and Dependent Care Expenses*.

Instead of using line F, you can choose to take the credit into account on line 5 of the *Deductions and Adjustments Worksheet*, as explained later under *Tax credits*.

Child tax credit (worksheet line G). If your total income will be between \$15,000 and \$42,000 (\$20,000 and \$65,000 if married), enter "1" on line G for each eligible child. Enter 1 additional if you have three to five eligible children or 2 additional if you have six or more eligible children. If your total income will be between \$42,000 and \$80,000 (\$65,000 and \$115,000 if married), enter "1" on line G if you have one or two eligible children, enter "2" if you have three eligible children, enter "3" if you have four eligible children, or enter "4" if you have five or more eligible children.

An eligible child is any child:

- For whom you claim an exemption,
- Who will be under age 17 at the end of 2002,
- Who is your son, daughter, stepchild, grandchild, adopted child, or foster child, and
- Who is a U.S. citizen or resident alien.

For more information about the child tax credit, see the instructions in your Form 1040 or Form 1040A tax package.

Instead of using line G, you can choose to take the credit into account on line 5 of the *Deductions and Adjustments Worksheet*, as explained later under *Tax credits*.

Total personal allowances (worksheet line H). Add lines A through G and enter the total on line H. If you do not use either of the worksheets on the back of Form W-4, enter the number from line H on line 5 of Form W-4.

Deductions and Adjustments Worksheet

Fill out this worksheet to adjust the number of your withholding allowances for deductions, adjustments to income, and tax credits. Use the amount of each item you can reasonably expect to show on your return. However, do not use more than:

- 1) The amount shown for that item on your 2001 return (or your 2000 return if you have not yet filed your 2001 return), plus
- 2) Any additional amount related to a transaction or occurrence (such as the signing of an agreement or the sale of property) that you can prove has happened or will happen during 2001 or 2002.

Do not include any amount shown on your last tax return that has been disallowed by the IRS.

Example 1.1. On June 30, 2001, you bought your first home. On your 2001 tax return you claimed itemized deductions of \$6,600, the total mortgage interest and real estate tax you paid during the 6 months you owned your home. Based on your mortgage payment schedule and your real estate tax assessment, you can reasonably expect to claim deductions of \$13,200 for those items on your 2002 return. You can use \$13,200 to figure the number of your withholding allowances for itemized deductions.

Not itemizing deductions. If you expect to claim the standard deduction on your tax return, skip lines 1 and 2, and enter "0" on line 3 of the worksheet.

Itemized deductions (worksheet line 1). You can take the following deductions into account when figuring additional withholding allowances for 2002. You normally claim these deductions on Schedule A of Form 1040.

- 1) Medical and dental expenses that are more than 7.5% of your 2002 adjusted gross income (defined later).
- 2) State and local income taxes and property taxes.
- 3) Deductible home mortgage interest.
- 4) Investment interest up to net investment income.
- 5) Charitable contributions.
- 6) Casualty and theft losses that are more than 10% of your adjusted gross income.
- 7) Fully deductible miscellaneous itemized deductions, including:
 - a) Impairment-related work expenses of persons with disabilities,
 - b) Federal estate tax on income in respect of a decedent,
 - c) Repayment of more than \$3,000 of income held under a claim of right (that you included in income in an earlier year because at the time you thought you had an unrestricted right to it),
 - d) Unrecovered investments in an annuity contract under which payments have ceased because of the annuitant's death,
 - e) Gambling losses (up to the amount of gambling winnings reported on your return), and
 - f) Casualty and theft losses from income-producing property.

- 8) Other miscellaneous itemized deductions that are more than 2% of your adjusted gross income, including:
 - a) Unreimbursed employee business expenses, such as educational expenses, work clothes and uniforms, union dues and fees, and the cost of work-related small tools and supplies,
 - b) Safe deposit box rental,
 - c) Tax counsel and assistance, and
 - d) Fees paid to an IRA custodian.

Adjusted gross income for purposes of the worksheet is your estimated total income for 2002 minus any estimated adjustments to income (discussed later) that you include on line 4 of the worksheet.

Enter your estimated total itemized deductions on line 1 of the worksheet.



Reduction of itemized deductions.

For 2002, your total itemized deductions may be reduced if your adjusted gross income (AGI) is more than \$137,300 (\$68,650 if married filing separately). If you expect your AGI to be more than that amount, use the following worksheet to figure the amount to enter on line 1 of the Deductions and Adjustments Worksheet.

Worksheet 1.2

1. Enter the estimated total of your itemized deductions _____
2. Enter the amount included in line 1 for medical and dental expenses, investment interest, casualty or theft losses, and gambling losses _____
3. Subtract line 2 from line 1 _____
Note. If the amount on line 3 is zero, stop here and enter the amount from line 1 of this worksheet on line 1 of the Deductions and Adjustments Worksheet.
4. Multiply the amount on line 3 by .80 _____
5. Enter your expected AGI _____
6. Enter \$137,300 (\$68,650 if married filing separately) _____
7. Subtract line 6 from line 5 _____
8. Multiply the amount on line 7 by .03 _____
9. Enter the smaller of line 4 or line 8 _____
10. Subtract line 9 from line 1. Enter the result here and on line 1 of the *Deductions and Adjustments Worksheet* _____

Adjustments to income (worksheet line 4).

You can take the following adjustments to income into account when figuring additional withholding allowances for 2002. These adjustments appear on page 1 of your Form 1040 or 1040A.

- Contributions to a traditional IRA.
- Contributions to a retirement plan for self-employed individuals (Keogh plan or self-employed SEP or SIMPLE plan).
- Contributions to a medical savings account.
- Student loan interest deduction.
- Deduction for one-half of self-employment tax.
- Deduction for 70% of self-employed health insurance.

- Penalty on early withdrawal of savings.
- Alimony payments.
- Certain moving expenses.
- Net losses from Schedules C, D, E, and F of Form 1040 and from Part II of Form 4797, line 18b(2).
- Net operating loss carryovers.

Enter your estimated total adjustments to income on line 4 of the worksheet.

Tax credits (worksheet line 5). Although you can take most tax credits into account when figuring withholding allowances, the Form W-4 worksheets use only the child and dependent care credit (line F of the *Personal Allowances Worksheet*) and the child tax credit (line G). But you can take these credits and others into account by adding an extra amount on line 5 of the *Deductions and Adjustments Worksheet*.

If you take the child and dependent care credit into account on line 5, do **not** use line F of the *Personal Allowances Worksheet*. If you take the child tax credit into account on line 5, do **not** use line G.

In addition to the child and dependent care credit and child tax credit, you can take into account the following credits.

- Credit for the elderly or the disabled. See Publication 524, *Credit for the Elderly or the Disabled*.
- Mortgage interest credit. See *Mortgage Interest Credit* in Publication 530, *Tax Information for First-Time Homeowners*.
- Foreign tax credit, except any credit that applies to wages not subject to U.S. income tax withholding because they are subject to income tax withholding by a foreign country. See Publication 514, *Foreign Tax Credit for Individuals*.
- Qualified electric vehicle credit. See the instructions for Form 8834, *Qualified Electric Vehicle Credit*.
- Credit for prior year minimum tax if you paid alternative minimum tax in an earlier year. See the instructions for Form 8801, *Credit for Prior Year Minimum Tax — Individuals, Estates, and Trusts*.
- Earned income credit, unless you requested advance payment of the credit. See Publication 596, *Earned Income Credit*.
- Adoption credit. See Publication 968, *Tax Benefits for Adoption*.
- General business credit. See Form 3800, *General Business Credit*.
- Hope credit. See Publication 970, *Tax Benefits for Higher Education*.
- Lifetime learning credit. See Publication 970, *Tax Benefits for Higher Education*.

To figure the amount to add on line 5 for tax credits, multiply your estimated total credits by the appropriate number from the following tables.

Table 1.2

**Credit Table A
Married Filing Jointly
or Qualifying Widow(er)**

If combined estimated wages are:	Multiply credits by:
\$0 to 29,000	10.0
29,001 to 64,000	6.7
64,001 to 130,000	3.7
130,001 to 189,000	3.3
189,001 to 324,000	2.9
over 324,000	2.6

**Credit Table B
Single**

If estimated wages are:	Multiply credits by:
\$0 to 14,000	10.0
14,001 to 36,000	6.7
36,001 to 75,000	3.7
75,001 to 149,000	3.3
149,001 to 315,000	2.9
over 315,000	2.6

**Credit Table C
Head of Household**

If estimated wages are:	Multiply credits by:
\$0 to 23,000	10.0
23,001 to 50,000	6.7
50,001 to 110,000	3.7
110,001 to 170,000	3.3
170,001 to 320,000	2.9
over 320,000	2.6

**Credit Table D
Married Filing Separately**

If estimated wages are:	Multiply credits by:
\$0 to 13,000	10.0
13,001 to 30,000	6.7
30,001 to 63,000	3.7
63,001 to 93,000	3.3
93,001 to 160,000	2.9
over 160,000	2.6

Example 1.2. You are married and expect to file a joint return for 2002. Your combined estimated wages are \$65,000. Your estimated tax credits include a child and dependent care credit of \$960 and a mortgage interest credit of \$1,700.

In *Credit Table A*, the number for your combined estimated wages (\$64,001 to \$130,000) is 3.7. Multiply your total estimated tax credits of \$2,660 by 3.7. Add the result, \$9,842, to the amount you would otherwise show on line 5 of the *Deductions and Adjustments Worksheet* and enter the total on line 5. Because you choose to account for your child and dependent care credit this way, you do not use line F of the *Personal Allowances Worksheet*.

Nonwage income (worksheet line 6). Enter on line 6 your estimated total nonwage income (other than tax-exempt income). Nonwage income includes interest, dividends, net rental income, unemployment compensation, alimony received, gambling winnings, prizes and awards, hobby income, capital gains, royalties, and partnership income.

If line 6 is more than line 5, you may not have enough income tax withheld from your wages. See *Getting the Right Amount of Tax Withheld*, later.

Net deductions and adjustments (worksheet line 7). If line 7 is less than \$3,000 enter "0" on line 8. If line 7 is \$3,000 or more, divide it by \$3,000, drop any fraction, and enter the result on line 8.

Two-Earner/Two-Job Worksheet

You should complete this worksheet if you have more than one job **or** are married and you and your spouse both work **and** the combined earnings from all jobs are more than \$35,000.



If you use this worksheet and your earnings are more than \$125,000 (\$175,000 if you are married), see Publication 919 to check that you are having enough tax withheld.

Reducing your allowances (worksheet lines 1 – 3). On line 1 of the worksheet, enter the number from line H of the *Personal Allowances Worksheet* (or line 10 of the *Deductions and Adjustments Worksheet*, if used). Using *Table 1* on the Form W-4, find the number listed beside the amount of your estimated wages for the year from your **lowest** paying job (or if lower, your spouse's job). Enter that number on line 2.

Subtract line 2 from line 1 and enter the result (but not less than zero) on line 3 and on Form W-4, line 5. If line 1 is more than or equal to line 2, do not use the rest of the worksheet (or skip to line 8 if you expect to owe amounts other than income tax).

If line 1 is less than line 2, you should complete lines 4 through 9 of the worksheet to figure the additional withholding needed to avoid underwithholding.

Other amounts owed. If you expect to owe amounts other than income tax, such as self-employment tax, include them on line 8. The total is the additional withholding needed for the year.

Example 1.3

Joyce Green works in a bookstore and expects to earn about \$13,300. Her husband, John, works full time at the Acme Corporation, where his expected pay is \$48,500. They file a joint income tax return and claim exemptions for their two children. Because they file jointly, they use only one set of Form W-4 worksheets to figure the number of withholding allowances. The Greens' worksheets and John's W-4 are shown on the next page.

Personal Allowances Worksheet. On this worksheet, John and Joyce claim allowances for themselves and their children by entering "1" on line A, "1" on line C, and "2" on line D. Because both John and Joyce will receive wages of more than \$1,000, they are not entitled to the additional withholding allowance on line B. The Greens expect to have child and dependent care expenses of \$2,400. They enter "1" on line F of the worksheet. Because they are married, their total income will be between \$20,000 and \$65,000 and they have two eligible children, they enter "2" on line G.

They enter their total personal allowances, 7, on line H.

Deductions and Adjustments Worksheet. Because they plan to itemize deductions and claim adjustments to income, the Greens use this worksheet to see whether they are entitled to additional allowances.

The Greens' estimated itemized deductions total \$11,200, which they enter on line 1 of the worksheet. Because they will file a joint return, they enter \$7,850 on line 2. They subtract \$7,850 from \$11,200 and enter the result, \$3,350, on line 3.

The Greens expect to have an adjustment to income of \$3,000 for their deductible IRA contributions. They do not expect to have any other adjustments to income. They enter \$3,000 on line 4.

The Greens add line 3 and line 4 and enter the total, \$6,350, on line 5.

Joyce and John expect to receive \$600 in interest and dividend income during the year. They enter \$600 on line 6 and subtract line 6 from line 5. They enter the result, \$5,750, on line 7. They divide line 7 by \$3,000, and drop the fraction to determine one additional allowance. They enter "1" on line 8.

The Greens enter "7" (the number from line H of the *Personal Allowances Worksheet*) on line 9 and add it to line 8. They enter "8" on line 10.

Two-Earner/Two-Job Worksheet. The Greens use this worksheet because they both work and together earn over \$35,000. They enter "8" (the number from line 10 of the *Deductions and Adjustments Worksheet*) on line 1.

Next, they use *Table 1* on the Form W-4 to find the number to enter on line 2 of the worksheet. Because they will file a joint return and their expected wages from their lowest paying job are \$13,300, they enter "2" on line 2. They subtract line 2 from line 1 and enter "6" on line 3 of the worksheet and on Form W-4, line 5.

John and Joyce Green can take a total of 6 withholding allowances between them. They decide that John will take all 6 allowances on his Form W-4. Joyce, therefore, cannot claim any allowances on hers. She will enter "0" on line 5 of the Form W-4 she gives to her employer.

Getting the Right Amount of Tax Withheld

In most situations, the tax withheld from your pay will be close to the tax you figure on your return if you follow these two rules.

- 1) You accurately complete all the Form W-4 worksheets that apply to you.
- 2) You give your employer a new Form W-4 when changes occur.

But because the worksheets and withholding methods do not account for all possible situations, you may not be getting the right amount withheld. This is most likely to happen in the following situations.

- You are married and both you and your spouse work.
- You have more than one job at a time.
- You have nonwage income, such as interest, dividends, alimony, unemployment compensation, or self-employment income.

Form W-4 (2002)

Purpose. Complete Form W-4 so your employer can withhold the correct Federal income tax from your pay. Because your tax situation may change, you may want to refigure your withholding each year.

Exemption from withholding. If you are exempt, complete only lines 1, 2, 3, 4, and 7 and sign the form to validate it. Your exemption for 2002 expires February 16, 2003. See **Pub. 505**, Tax Withholding and Estimated Tax.

Note: You cannot claim exemption from withholding if (a) your income exceeds \$750 and includes more than \$250 of unearned income (e.g., interest and dividends) and (b) another person can claim you as a dependent on their tax return.

Basic instructions. If you are not exempt, complete the **Personal Allowances Worksheet** below. The worksheets on page 2 adjust your withholding allowances based on itemized deductions, certain credits, adjustments to

income, or two-earner/two-job situations. Complete all worksheets that apply. **However, you may claim fewer (or zero) allowances.**

Head of household. Generally, you may claim head of household filing status on your tax return only if you are unmarried and pay more than 50% of the costs of keeping up a home for yourself and your dependent(s) or other qualifying individuals. See line **E** below.

Tax credits. You can take projected tax credits into account in figuring your allowable number of withholding allowances. Credits for child or dependent care expenses and the child tax credit may be claimed using the **Personal Allowances Worksheet** below. See **Pub. 919**, How Do I Adjust My Tax Withholding? for information on converting your other credits into withholding allowances.

Nonwage income. If you have a large amount of nonwage income, such as interest or dividends, consider making estimated tax payments using **Form 1040-ES**, Estimated Tax for Individuals. Otherwise, you may owe additional tax.

Two earners/two jobs. If you have a working spouse or more than one job, figure the total number of allowances you are entitled to claim on all jobs using worksheets from only one Form W-4. Your withholding usually will be most accurate when all allowances are claimed on the Form W-4 for the highest paying job and zero allowances are claimed on the others.

Nonresident alien. If you are a nonresident alien, see the **Instructions for Form 8233** before completing this Form W-4.

Check your withholding. After your Form W-4 takes effect, use Pub. 919 to see how the dollar amount you are having withheld compares to your projected total tax for 2002. See Pub. 919, especially if you used the **Two-Earner/Two-Job Worksheet** on page 2 and your earnings exceed \$125,000 (Single) or \$175,000 (Married).

Recent name change? If your name on line 1 differs from that shown on your social security card, call 1-800-772-1213 for a new social security card.

Personal Allowances Worksheet (Keep for your records.)

Example 1.3

A	Enter "1" for yourself if no one else can claim you as a dependent	A	<u>1</u>
B	Enter "1" if: <ul style="list-style-type: none"> • You are single and have only one job; or • You are married, have only one job, and your spouse does not work; or • Your wages from a second job or your spouse's wages (or the total of both) are \$1,000 or less. 	B	<u> </u>
C	Enter "1" for your spouse . But, you may choose to enter "-0-" if you are married and have either a working spouse or more than one job. (Entering "-0-" may help you avoid having too little tax withheld.)	C	<u>1</u>
D	Enter number of dependents (other than your spouse or yourself) you will claim on your tax return	D	<u>2</u>
E	Enter "1" if you will file as head of household on your tax return (see conditions under Head of household above)	E	<u> </u>
F	Enter "1" if you have at least \$1,500 of child or dependent care expenses for which you plan to claim a credit	F	<u>1</u>
(Note: Do not include child support payments. See Pub. 503, Child and Dependent Care Expenses, for details.)			
G	Child Tax Credit (including additional child tax credit):		
	<ul style="list-style-type: none"> • If your total income will be between \$15,000 and \$42,000 (\$20,000 and \$65,000 if married), enter "1" for each eligible child plus 1 additional if you have three to five eligible children or 2 additional if you have six or more eligible children. • If your total income will be between \$42,000 and \$80,000 (\$65,000 and \$115,000 if married), enter "1" if you have one or two eligible children, "2" if you have three eligible children, "3" if you have four eligible children, or "4" if you have five or more eligible children. 		
H	Add lines A through G and enter total here. Note: This may be different from the number of exemptions you claim on your tax return. ▶	H	<u>7</u>
	For accuracy, complete all worksheets that apply. <ul style="list-style-type: none"> • If you plan to itemize or claim adjustments to income and want to reduce your withholding, see the Deductions and Adjustments Worksheet on page 2. • If you have more than one job or are married and you and your spouse both work and the combined earnings from all jobs exceed \$35,000, see the Two-Earner/Two-Job Worksheet on page 2 to avoid having too little tax withheld. • If neither of the above situations applies, stop here and enter the number from line H on line 5 of Form W-4 below. 		

Cut here and give Form W-4 to your employer. Keep the top part for your records.

Form W-4 Department of the Treasury Internal Revenue Service	<h2>Employee's Withholding Allowance Certificate</h2> <p>▶ For Privacy Act and Paperwork Reduction Act Notice, see page 2.</p>	OMB No. 1545-0010 <h1 style="margin: 0;">2002</h1>
1 Type or print your first name and middle initial Last name John M. Green		2 Your social security number 444 00 4444
Home address (number and street or rural route) 28 Fairway City or town, state, and ZIP code Anytown, State 00000		3 <input type="checkbox"/> Single <input checked="" type="checkbox"/> Married <input type="checkbox"/> Married, but withhold at higher Single rate. Note: If married, but legally separated, or spouse is a nonresident alien, check the "Single" box.
		4 If your last name differs from that on your social security card, check here. You must call 1-800-772-1213 for a new card. ▶ <input type="checkbox"/>
5 Total number of allowances you are claiming (from line H above or from the applicable worksheet on page 2)		5 <u>6</u>
6 Additional amount, if any, you want withheld from each paycheck		6 \$
7 I claim exemption from withholding for 2002, and I certify that I meet both of the following conditions for exemption: <ul style="list-style-type: none"> • 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 ▶		7
Under penalties of perjury, I certify that I am entitled to the number of withholding allowances claimed on this certificate, or I am entitled to claim exempt status.		
Employee's signature (Form is not valid unless you sign it.) ▶ John M. Green		Date ▶ January 4, 2002
8 Employer's name and address (Employer: Complete lines 8 and 10 only if sending to the IRS.)		9 Office code (optional)
		10 Employer identification number

Deductions and Adjustments Worksheet

Note: Use this worksheet only if you plan to itemize deductions, claim certain credits, or claim adjustments to income on your 2002 tax return.

1 Enter an estimate of your 2002 itemized deductions. These include qualifying home mortgage interest, charitable contributions, state and local taxes, medical expenses in excess of 7.5% of your income, and miscellaneous deductions. (For 2002, you may have to reduce your itemized deductions if your income is over \$137,300 (\$68,650 if married filing separately). See **Worksheet 3** in Pub. 919 for details.) **1** \$ 11,200

2 Enter: { \$7,850 if married filing jointly or qualifying widow(er)
\$6,900 if head of household
\$4,700 if single
\$3,925 if married filing separately } **2** \$ 7,850

3 **Subtract** line 2 from line 1. If line 2 is greater than line 1, enter “-0-” **3** \$ 3,350

4 Enter an estimate of your 2002 adjustments to income, including alimony, deductible IRA contributions, and student loan interest **4** \$ 3,000

5 **Add** lines 3 and 4 and enter the total. Include any amount for credits from **Worksheet 7** in Pub. 919. **5** \$ 6,350

6 Enter an estimate of your 2002 nonwage income (such as dividends or interest) **6** \$ 600

7 **Subtract** line 6 from line 5. Enter the result, but not less than “-0-” **7** \$ 5,750

8 **Divide** the amount on line 7 by \$3,000 and enter the result here. Drop any fraction **8** 1

9 Enter the number from the **Personal Allowances Worksheet**, line H, page 1 **9** 7

10 **Add** lines 8 and 9 and enter the total here. If you plan to use the **Two-Earner/Two-Job Worksheet**, also enter this total on line 1 below. Otherwise, **stop here** and enter this total on Form W-4, line 5, page 1. **10** 8

Two-Earner/Two-Job Worksheet

Note: Use this worksheet only if the instructions under line H on page 1 direct you here.

1 Enter the number from line H, page 1 (or from line 10 above if you used the **Deductions and Adjustments Worksheet**) **1** 8

2 Find the number in **Table 1** below that applies to the **lowest** paying job and enter it here **2** 2

3 If line 1 is **more than or equal to** line 2, subtract line 2 from line 1. Enter the result here (if zero, enter “-0-”) and on Form W-4, line 5, page 1. **Do not** use the rest of this worksheet **3** 6

Note: If line 1 is **less than** line 2, enter “-0-” on Form W-4, line 5, page 1. Complete lines 4–9 below to calculate the additional withholding amount necessary to avoid a year end tax bill.

4 Enter the number from line 2 of this worksheet **4** _____

5 Enter the number from line 1 of this worksheet **5** _____

6 **Subtract** line 5 from line 4 **6** _____

7 Find the amount in **Table 2** below that applies to the **highest** paying job and enter it here **7** \$ _____

8 **Multiply** line 7 by line 6 and enter the result here. This is the additional annual withholding needed **8** \$ _____

9 Divide line 8 by the number of pay periods remaining in 2002. For example, divide by 26 if you are paid every two weeks and you complete this form in December 2001. Enter the result here and on Form W-4, line 6, page 1. This is the additional amount to be withheld from each paycheck **9** \$ _____

Table 1: Two-Earner/Two-Job Worksheet

Married Filing Jointly				All Others			
If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above
\$0 - \$4,000	0	44,001 - 50,000	8	\$0 - \$6,000	0	75,001 - 95,000	8
4,001 - 9,000	1	50,001 - 55,000	9	6,001 - 11,000	1	95,001 - 110,000	9
9,001 - 15,000	2	55,001 - 65,000	10	11,001 - 17,000	2	110,001 and over	10
15,001 - 20,000	3	65,001 - 80,000	11	17,001 - 23,000	3		
20,001 - 25,000	4	80,001 - 95,000	12	23,001 - 28,000	4		
25,001 - 32,000	5	95,001 - 110,000	13	28,001 - 38,000	5		
32,001 - 38,000	6	110,001 - 125,000	14	38,001 - 55,000	6		
38,001 - 44,000	7	125,001 and over	15	55,001 - 75,000	7		

Table 2: Two-Earner/Two-Job Worksheet

Married Filing Jointly		All Others	
If wages from HIGHEST paying job are—	Enter on line 7 above	If wages from HIGHEST paying job are—	Enter on line 7 above
\$0 - \$50,000	\$.450	\$0 - \$30,000	\$.450
50,001 - 100,000800	30,001 - 70,000800
100,001 - 150,000900	70,001 - 140,000900
150,001 - 270,000	1,050	140,001 - 300,000	1,050
270,001 and over	1,150	300,001 and over	1,150

Privacy Act and Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. The Internal Revenue Code requires this information under sections 3402(f)(2)(A) and 6109 and their regulations. **Failure to provide a properly completed form will result in your being treated as a single person who claims no withholding allowances; providing fraudulent information may also subject you to penalties.** Routine uses of this information include giving it to the Department of Justice for civil and criminal litigation, to cities, states, and the District of Columbia for use in administering their tax laws, and using it in the National Directory of New Hires.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB

control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete this form will vary depending on individual circumstances. The estimated average time is: **Recordkeeping**, 46 min.; **Learning about the law or the form**, 13 min.; **Preparing the form**, 59 min. If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **Do not** send the tax form to this address. Instead, give it to your employer.

- You will owe additional amounts with your return, such as self-employment tax.
- Your withholding is based on obsolete Form W-4 information for a substantial part of the year.
- Your earnings are more than \$125,000 if you are single or \$175,000 if you are married.

To make sure you are getting the right amount of tax withheld, get Publication 919. It will help you compare the total tax to be withheld during the year with the tax you can expect to figure on your return. It also will help you determine how much, if any, additional withholding is needed each payday to avoid owing tax when you file your return. If you do not have enough tax withheld, you may have to make estimated tax payments. See chapter 2 for information about estimated tax.

Rules Your Employer Must Follow

It may be helpful for you to know some of the withholding rules your employer must follow. These rules can affect how to fill out your Form W-4 and how to handle problems that may arise.

New Form W-4. When you start a new job, your employer should give you a Form W-4 to fill out. Your employer will use the information you give on the form to figure your withholding beginning with your first payday.

If you later fill out a new Form W-4, your employer can put it into effect as soon as possible. The deadline for putting it into effect is the start of the first payroll period ending 30 or more days after you turn it in.

No Form W-4. If you do not give your employer a completed Form W-4, your employer must withhold at the highest rate — as if you were single and claimed no allowances.

Repaying withheld tax. If you find you are having too much tax withheld because you did not claim all the withholding allowances you are entitled to, you should give your employer a new Form W-4. Your employer cannot repay any of the tax previously withheld.

However, if your employer has withheld more than the correct amount of tax for the Form W-4 you have in effect, you do not have to fill out a new Form W-4 to have your withholding lowered to the correct amount. Your employer can repay the amount that was incorrectly withheld. If you are not repaid, your Form W-2 will reflect the full amount actually withheld.

Sending your Form W-4 to the IRS. Your employer will usually keep your Form W-4 and use it to figure your withholding. Under normal circumstances, it will not be sent to the IRS. However, your employer must send a copy of your Form W-4 to the IRS for verification in both of the following situations.

- 1) You claim more than 10 withholding allowances.
- 2) You claim exemption from withholding and your wages are expected to usually be more than \$200 a week. See *Exemption From Withholding*, later.

The IRS may ask you for information showing how you figured either the number of allowances you claimed or your eligibility for exemption from withholding. If you choose, you can give this information to your employer to send to the IRS along with your Form W-4.

If the IRS determines that you cannot take all the allowances claimed on your Form W-4, or that you are not exempt as claimed, it will inform both you and your employer and will specify the maximum number of allowances you can claim. The IRS also may ask you to fill out a new Form W-4. However, your employer cannot figure your withholding on the basis of more allowances than the maximum number determined by the IRS.

If you believe you are exempt or can claim more withholding allowances than determined by the IRS, you can complete a new Form W-4, stating on the form, or in a written statement, any circumstances that have changed or any other reasons for your claim. You can send it directly to the IRS or give it to your employer to send to the IRS. Your employer must continue to figure your withholding on the basis of the number of allowances previously determined by the IRS until the IRS advises your employer to withhold on the basis of the new Form W-4.

There is a penalty for supplying false information on Form W-4. See *Penalties*, later.

Social security (FICA) tax. Generally, each employer for whom you work during the tax year must withhold social security tax up to the annual limit.

Exemption From Withholding

If you claim exemption from withholding, your employer will not withhold federal income tax from your wages. The exemption applies only to income tax, not to social security or Medicare tax.

You can claim exemption from withholding for 2002 only if **both** the following situations apply.

- 1) For **2001** you had a right to a refund of all federal income tax withheld because you had no tax liability.
- 2) For **2002** you expect a refund of all federal income tax withheld because you expect to have no tax liability.

Use *Figure A*, later in this chapter, to help you decide whether you can claim exemption from withholding. Do not use *Figure A* if you:

- Are 65 or older,
- Are blind,
- Will itemize deductions on your 2002 return.
- Will claim an exemption for a dependent on your 2002 return.
- Will claim any tax credits on your 2002 return.

These situations are discussed later.

Student. If you are a student, you are not automatically exempt. If you work only part time or during the summer, you may qualify for exemption from withholding.

Example 1.4. You are a high school student and expect to earn \$2,500 from a summer job. You do not expect to have any other income during the year, and your parents will be able to claim an exemption for you on their tax return. You worked last summer and had \$375 federal income tax withheld from your pay. The entire \$375 was refunded when you filed your 2001 return. Using *Figure A*, you find that you can claim exemption from withholding.

Example 1.5. The facts are the same as in *Example 1.4*, except that you have a savings account and expect to have \$320 interest income during the year. Using *Figure A*, you find that you cannot claim exemption from withholding because your unearned income will be more than \$250 and your total income will be more than \$750.



You may have to file a tax return, even if you are exempt from withholding. See *Publication 501*, Exemptions, Standard Deduction, and Filing Information, to see whether you must file a return.



Age 65 or older or blind. If you are 65 or older or blind, use one of the following worksheets to help you decide whether you can claim exemption from withholding. Do not use either worksheet if you will itemize deductions or claim exemptions for dependents or claim tax credits on your 2002 return — instead, see *Itemizing deductions or claiming exemptions or credits*, following the worksheets.

Worksheet 1.3 Exemption From Withholding Worksheet for 65 or Older or Blind

Use this worksheet only if, for **2001**, you had a right to a refund of all federal income tax withheld because you had no tax liability.

Caution. This worksheet does not apply if you can be claimed as a dependent. See *Worksheet 1.4* instead.

1. Check the boxes below that apply to you.

65 or older Blind

2. Check the boxes below that apply to your spouse if you will claim your spouse's exemption on your 2002 return.

65 or older Blind

3. Add the number of boxes you checked in 1 and 2 above. Enter the result _____

You **can** claim exemption from withholding if:

Your filing status is:	and the number on line 3 above is:	and your 2002 total income will be no more than:
------------------------	------------------------------------	--

Single	1	\$ 8,850
	2	10,000

Head of household	1	\$11,050
	2	12,200

Married filing separately for both 2001 and 2002	1	\$ 7,825
	2	8,725
	3	9,625
	4	10,525

Other married	1	\$14,750*
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status	2	15,650*
	3	16,550*
	4	17,450*

*Include both spouses' income whether you will file separately or jointly.

Qualifying	1	\$11,750
widow(er)	2	12,650

You **cannot** claim exemption from withholding if your total income will be **more than** the amount shown for your filing status.

Worksheet 1.4

Exemption From Withholding Worksheet for Dependents Who Are 65 or Older or Blind

Use this worksheet only if, for **2001**, you had a right to a refund of all federal income tax withheld because you had **no tax liability**.

- Enter your expected earned income plus \$250 _____
- Minimum amount \$750
- Compare lines 1 and 2. Enter the **larger** amount _____
- Enter the appropriate amount from the following table _____

Filing Status Amount

Single	\$4,700
Married filing separately	3,925

- Compare lines 3 and 4. Enter the **smaller** amount _____
- Enter the appropriate amount from the following table _____

Filing Status Amount

Single	
Either 65 or older or blind	\$1,150
Both 65 or older and blind	2,300
Married filing separately	
Either 65 or older or blind	900
Both 65 or older and blind	1,800

- Add lines 5 and 6. Enter the result _____
- Enter your total expected income _____

You **can** claim exemption from withholding if line 7 is equal to or more than line 8. If line 8 is more than line 7, you **cannot** claim exemption from withholding.

Itemizing deductions or claiming exemptions or credits. If you had no tax liability for 2001, and you will either:

- Itemize deductions,
- Claim an exemption for a dependent, or
- Claim a tax credit,

use the *2002 Estimated Tax Worksheet* in Form 1040-ES (also see chapter 2), to figure your 2002 expected tax liability. You can claim exemption from withholding only if your total expected tax liability (line 13c of the worksheet) is zero.

Claiming exemption from withholding. To claim exemption, you must give your employer a Form W-4. Print "Exempt" on line 7.

Your employer must send the IRS a copy of your Form W-4 if you claim exemption from withholding and your pay is expected to usually be more than \$200 a week. If it turns out that you do not qualify for exemption, the IRS will send both you and your employer a written notice.

If you claim exemption, but later your situation changes so that you will have to pay income tax after all, you must file a new Form W-4 within 10 days after the change. If you claim exemption in 2002, but you expect to owe income tax for 2003, you must file a new Form W-4 by December 1, 2002.

An exemption is good for only one year. You must give your employer a new Form W-4

by February 15 each year to continue your exemption.

Supplemental Wages

Supplemental wages include bonuses, commissions, overtime pay, and certain sick pay. The payer can figure withholding on supplemental wages using the same method used for your regular wages. If these payments are identified separately from regular wages, your employer or other payer of supplemental wages can withhold income tax from these wages at a flat rate of 27%.

Expense allowances. Reimbursements or other expense allowances paid by your employer under a nonaccountable plan are treated as supplemental wages. A nonaccountable plan is a reimbursement arrangement that does not require you to account for, or prove, your business expenses to your employer or does not require you to return your employer's payments that are more than your proven expenses.

Reimbursements or other expense allowances paid under an accountable plan that are more than your proven expenses are treated as paid under a nonaccountable plan if you do not return the excess payments within a reasonable period of time.

For more information about accountable and nonaccountable plans, see chapter 6 of Publication 463, *Travel, Entertainment, Gift, and Car Expenses*.

Penalties

You may have to pay a penalty of \$500 if both of the following apply.

- You make statements or claim withholding allowances on your Form W-4 that reduce the amount of tax withheld.
- You have no reasonable basis for those statements or allowances at the time you prepare your Form W-4.

There is also a criminal penalty for willfully supplying false or fraudulent information on your Form W-4 or for willfully failing to supply information that would increase the amount withheld. The penalty upon conviction can be either a fine of up to \$1,000 or imprisonment for up to one year, or both.

These penalties will apply if you deliberately and knowingly falsify your Form W-4 in an attempt to reduce or eliminate the proper withholding of taxes. A simple error — an honest mistake — will not result in one of these penalties. For example, a person who has tried to figure the number of withholding allowances correctly, but claims seven when the proper number is six, will not be charged a Form W-4 penalty. However, see chapter 4 for information on the underpayment penalty.

Tips

The tips you receive while working on your job are considered part of your pay. You must in-

clude your tips on your tax return on the same line as your regular pay. However, tax is not withheld directly from tip income, as it is from your regular pay. Nevertheless, your employer will take into account the tips you report when figuring how much to withhold from your regular pay.

Reporting tips to your employer. If you receive tips of \$20 or more in a month while working for any one employer, you must report to your employer the total amount of tips you receive on the job during the month. The report is due by the 10th day of the following month.

If you have more than one job, make a separate report to each employer. Report only the tips you received while working for that employer, and only if they total \$20 or more for the month.

How employer figures amount to withhold.

The tips you report to your employer are counted as part of your income for the month you report them. Your employer can figure your withholding in either of two ways.

- By withholding at the regular rate on the sum of your pay plus your reported tips.
- By withholding at the regular rate on your pay plus an amount equal to 27% of your reported tips.

Not enough pay to cover taxes. If your regular pay is too low for your employer to withhold all the tax (including social security tax, Medicare tax, or railroad retirement tax) due on your pay plus your tips, you can give your employer money to cover the shortage.

If you do not give your employer money to cover the shortage, your employer will first withhold as much social security tax, Medicare tax, or railroad retirement tax as possible, up to the proper amount, and then withhold income tax up to the full amount of your pay. If not enough tax is withheld, you may have to make estimated tax payments. When you file your return, you also may have to pay any social security tax, Medicare tax, or railroad retirement tax your employer could not withhold.

Tips not reported to your employer. On your tax return, you must report **all** the tips you receive during the year, even tips you do not report to your employer. Make sure you are having enough tax withheld, or are paying estimated tax, to cover all your tip income.

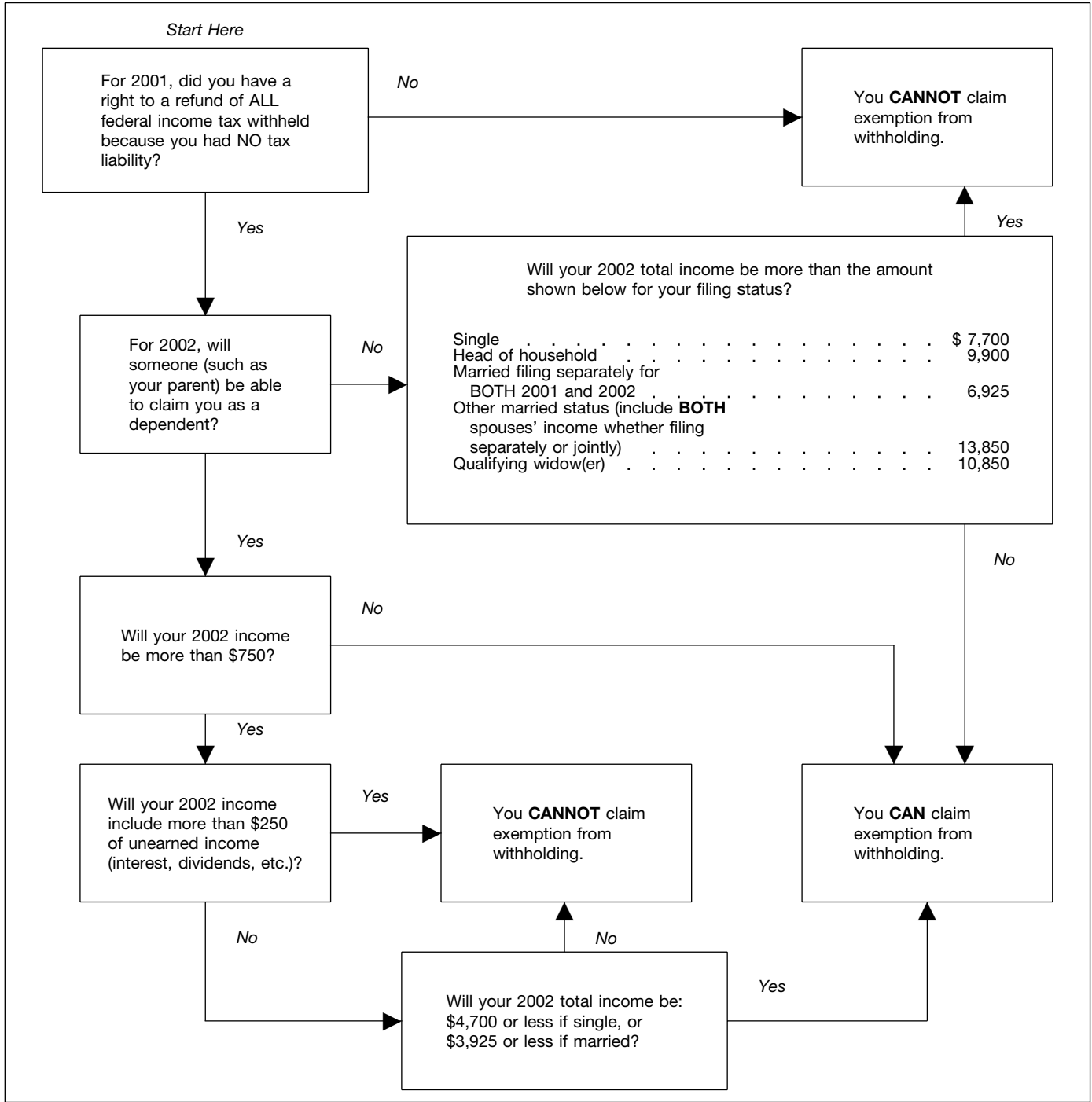
Allocated tips. If you work in a large establishment that serves food or beverages to customers, your employer may have to report an allocated amount of tips on your Form W-2.

Your employer should not withhold income tax, social security tax, Medicare tax, or railroad retirement tax on the allocated amount. Withholding is based only on your pay plus your **reported tips**. Your employer should refund to you any incorrectly withheld tax.

More information. For more information on the withholding rules for tip income and on tip allocation, get Publication 531, *Reporting Tip Income*.

Figure A. Exemption From Withholding on Form W-4

Note: Do not use this chart if you are 65 or older or blind, or if you will itemize your deductions or claim exemptions for dependents or tax credits. Instead, see the discussions in this chapter under *Exemption From Withholding*.



Taxable Fringe Benefits

The value of certain noncash fringe benefits you receive from your employer is considered part of your pay. Your employer generally must withhold income tax on these benefits from your regular pay for the period the benefits are paid or considered paid.

For information on fringe benefits, see *Fringe Benefits under Employee Compensation* in Publication 525.

Your employer can choose not to withhold income tax on the value of your personal use of a car, truck, or other highway motor vehicle provided by your employer. Your employer must notify you if this choice is made.

When benefits are considered paid. Your employer can choose to treat a fringe benefit as paid by the pay period, by the quarter, or on some other basis as long as the benefit is considered paid at least once a year. Your employer can treat the benefit as being paid on one or more dates during the year, even if you get the entire benefit at one time.

Special rule. Your employer can choose to treat a benefit provided during November or December as paid in the next year. Your employer must notify you if this rule is used.

Example 1.6. Your employer considers the value of benefits paid from November 1, 2000, through October 31, 2001, as paid to you in 2001. To determine the total value of benefits paid to you in 2002, your employer will add the value of any benefits paid in November and December of 2001 to the value of any benefits paid in January through October of 2002.

Exceptions. Your employer cannot choose when to withhold tax on certain benefits. These benefits are transfers of either real property or personal property of a kind normally held for investment (such as stock). Your employer must withhold tax on these benefits at the time of the transfer.

How withholding is figured. Your employer can either add the value of a fringe benefit to your regular pay and figure income tax withholding on the total or withhold 27% of the benefit's value.

If the benefit's actual value cannot be determined when it is paid or treated as paid, your employer can use a reasonable estimate. Your employer must determine the actual value of the benefit by January 31 of the next year. If the actual value is more than the estimate, your employer must pay the IRS any additional withholding tax required. Your employer has until April 1 of that next year to recover from you the additional tax paid to the IRS for you.

How your employer reports your benefits. Your employer must report on Form W-2, *Wage and Tax Statement*, the total of the taxable fringe benefits paid or treated as paid to you during the year and the tax withheld for the benefits. These amounts can be shown either on the Form W-2 for your regular pay or on a separate Form W-2. If your employer provided you with a car, truck, or other motor vehicle and chose to treat all of your use of it as personal, its value must be either separately shown on Form W-2 or reported to you on a separate statement.

Sick Pay

Sick pay is a payment to you to replace your regular wages while you are temporarily absent from work due to sickness or personal injury. To qualify as sick pay, it must be paid under a plan to which your employer is a party.

If you receive sick pay from your employer or an agent of your employer, income tax must be withheld. An agent who does not pay regular wages to you may choose to withhold income tax at a flat 27% rate.

However, if you receive sick pay from a third party who is not acting as an agent of your employer, income tax will be withheld only if you choose to have it withheld. See *Form W-4S*, later.

If you receive payments under a plan in which your employer does not participate (such as an accident or health plan where you paid all the premiums), the payments are not sick pay and usually are not taxable.

Union agreements. If you receive sick pay under a collective bargaining agreement between your union and your employer, the agreement may determine the amount of income tax withholding. See your union representative or your employer for more information.

Form W-4S. If you choose to have income tax withheld from sick pay paid by a third party, such as an insurance company, you must fill out Form W-4S. Its instructions contain a worksheet you can use to figure the amount you want withheld. They also explain restrictions that may apply.

Give the completed form to the payer of your sick pay. The payer must withhold according to your directions on the form.

If you do not request withholding on Form W-4S, or if you do not have enough tax withheld, you may have to make estimated tax payments. If you do not pay enough estimated tax or have enough income tax withheld, you may have to pay a penalty. See chapters 2 and 4.

Form W-4S remains in effect until you change or cancel it, or stop receiving payments. You can change your withholding by giving a new Form W-4S or a written notice to the payer of your sick pay.

Pensions and Annuities

Income tax usually will be withheld from your pension or annuity distributions unless you choose not to have it withheld. This rule applies to distributions from:

- A traditional individual retirement arrangement (IRA),
- A life insurance company under an endowment, annuity, or life insurance contract,
- A pension, annuity, or profit-sharing plan,
- A stock bonus plan, and
- Any other plan that defers the time you receive compensation.

The amount withheld depends on whether you receive payments spread out over more than one year (periodic payments), within one year (nonperiodic payments), or as an eligible rollover distribution (ERD). You cannot choose not to have income tax withheld from an ERD. ERDs are discussed later.

Nontaxable part. The part of your pension or annuity that is a return of your investment in your retirement plan — the amount you paid into the plan or its cost to you — is not taxable. Income tax will not be withheld from the part of your pension or annuity that is not taxable. The tax withheld will be figured on, and cannot be more than, the taxable part.

For information about figuring the part of your pension or annuity that is not taxable, see Publication 575, *Pension and Annuity Income*.

Periodic Payments

Withholding from periodic payments of a pension or annuity is figured in the same way as withholding from salaries and wages. To tell the payer of your pension or annuity how much you want withheld, fill out **Form W-4P** or a similar form provided by the payer. Follow the rules discussed under *Salaries and Wages*, earlier, to fill out your Form W-4P.

Note. Use Form W-4, not Form W-4P, if you receive any of the following.

- 1) Military retirement pay.
- 2) Payments from a nonqualified deferred compensation plan.

- 3) Payments from state and local deferred compensation plan.

Withholding rules. The withholding rules for pensions and annuities differ from those for salaries and wages in the following ways.

- 1) **If you do not fill out a withholding certificate**, tax will be withheld as if you were married and claiming three withholding allowances. This means that tax will be withheld only if your pension or annuity is at least \$1,280 a month (or \$15,360 a year).
- 2) **You can choose not to have tax withheld**, regardless of how much tax you owed last year or expect to owe this year. You do not have to qualify for exemption. See *Choosing Not To Have Income Tax Withheld*, later.
- 3) **If you do not give the payer your social security number** (in the required manner) or the IRS notifies the payer before any payment or distribution is made that you gave it an incorrect social security number, tax will be withheld as if you were single and were claiming no withholding allowances. This means that tax will be withheld if your pension or annuity is at least \$230 a month (or \$2,760 a year).

Effective date of withholding certificate. If you give your withholding certificate (Form W-4P or a similar form) to the payer by the time your payments start, it will be put into effect by the first payment made more than 30 days after you submit the certificate.

If you give the payer your certificate after your payments start, it will be put into effect with the first payment made on or after January 1, May 1, July 1, or October 1, whichever is at least 30 days after you submit it. However, the payer can elect to put it into effect earlier.

Nonperiodic Payments

Tax will be withheld at a 10% rate on any nonperiodic payments you receive.

Because withholding on nonperiodic payments does not depend on withholding allowances or whether you are married or single, you cannot use Form W-4P to tell the payer how much to withhold. But you can use Form W-4P to specify that an additional amount be withheld. You can also use Form W-4P to choose not to have tax withheld or to revoke a choice not to have tax withheld.



You may need to use Form W-4P to ask for additional withholding. If you do not have enough tax withheld, you may need to make estimated tax payments, as explained in chapter 2.

Eligible Rollover Distributions

Distributions you receive that are eligible to be rolled over tax free into a qualified retirement or annuity plans are subject to a 20% withholding tax.

This type of distribution is called an **eligible rollover distribution (ERD)**. This is the taxable part of any distribution from a qualified pension

plan or tax-sheltered annuity that is not any of the following.

- 1) A minimum required distribution.
- 2) One of a series of substantially equal periodic pension or annuity payments made over:
 - a) Your life (or your life expectancy) or the joint lives of you and your beneficiary (or your life expectancies), or
 - b) A specified period of 10 or more years.
- 3) A hardship distribution.

The payer of a distribution must withhold at a 20% rate on any part of an ERD that is not rolled over directly to another qualified plan. You cannot elect not to have withholding on these distributions.

Choosing Not To Have Income Tax Withheld

You can choose not to have income tax withheld from your pension or annuity. This rule does not apply to eligible rollover distributions. The payer will tell you how to make this choice. If you use Form W-4P, check the box on line 1 to make this choice. This choice will remain in effect until you decide you want withholding.

The payer must withhold if either of the following applies:

- 1) You do not give the payer your social security number (in the required manner), or
- 2) The IRS notifies the payer, before any payment or distribution is made, that you gave it an incorrect social security number.

If you do not have any income tax withheld from your pension or annuity, or if you do not have enough withheld, you may have to make estimated tax payments. See chapter 2.

If you do not pay enough tax either through estimated tax or withholding, you may have to pay a penalty. See chapter 4 for information about this penalty.

Outside the United States. If you are a U.S. citizen or resident alien and you do not want to have tax withheld from pension or annuity benefits, you must give the payer of the benefits a home address in the United States or in a U.S. possession. Otherwise, the payer must withhold tax. For example, the payer would have to withhold tax if you provide a U.S. address for a nominee, trustee, or agent to whom the benefits are to be delivered, but do not provide your own home address in the United States or in a U.S. possession.

Notice required of payer. The payer of your pension or annuity must send you a notice telling you about your right to choose not to have tax withheld.

Generally, the payer will not send a notice to you if it is reasonable to believe that the entire amount you will be paid is not taxable.

Revoking a choice not to have tax withheld. The payer of your pension or annuity will tell you how to revoke your choice not to have income tax withheld from periodic or nonperiodic payments. If you use Form W-4P to revoke the

choice, print "Revoked" by the checkbox on line 1 of the form.

If you use Form W-4P to revoke the choice for periodic payments and you do not complete line 2 of the form, the payer will withhold as if you were married and claiming three allowances.

Gambling Winnings

Income tax is withheld from certain kinds of gambling winnings. For 2002, the amount withheld is 27% of the proceeds paid (the amount of your winnings minus the amount of your bet).

Gambling winnings of more than \$5,000 from the following sources are subject to income tax withholding.

- Any sweepstakes, wagering pool, or lottery.
- Any other wager if the proceeds are at least 300 times the amount of the bet.

It does not matter whether your winnings are paid in cash, in property, or as an annuity. Winnings not paid in cash are taken into account at their fair market value.

Gambling winnings from bingo, keno, and slot machines are generally not subject to income tax withholding. However, you may need to provide the payer with a social security number to avoid withholding. See *Backup withholding on gambling winnings*, later. If you receive gambling winnings not subject to withholding, you may need to make estimated tax payments. (See chapter 2.)

If you do not pay enough tax through withholding or estimated tax payments, you may be subject to a penalty. (See chapter 4.)

Form W-2G. If a payer withholds income tax from your gambling winnings, you should receive a Form W-2G, *Certain Gambling Winnings*, showing the amount you won and the amount withheld.

Report the tax withheld on line 59 of Form 1040.

Information to give payer. If the payer asks, you must give the payer all the following information.

- Your name, address, and social security number.
- Whether you made identical wagers (explained next).
- Whether someone else is entitled to any part of the winnings subject to withholding. If so, you must complete Form 5754, *Statement by Person(s) Receiving Gambling Winnings*, and return it to the payer. The payer will use it to prepare a Form W-2G for each of the winners.

Identical wagers. You may have to give the payer a statement of the amount of your winnings, if any, from identical wagers. If this statement is required, the payer will ask you for it. You provide this statement by signing Form W-2G or, if required, Form 5754.

Identical wagers include two bets placed in a pari-mutuel pool on one horse to win a particular race. However, the bets are not identical if one bet is "to win" and one bet is "to place." In

addition, they are not identical if the bets were placed in different pari-mutuel pools. For example, a bet in a pool conducted by the racetrack and a bet in a separate pool conducted by an offtrack betting establishment in which the bets are not pooled with those placed at the track are not identical wagers.

Backup withholding on gambling winnings.

If you have any kind of gambling winnings and do not give the payer your social security number, the payer may have to withhold income tax at the rate of 30%. This rule applies to keno winnings of more than \$1,500, bingo and slot machine winnings of more than \$1,200, and certain other gambling winnings of more than \$600.

Unemployment Compensation

You can choose to have income tax withheld from unemployment compensation. To make this choice, you will have to fill out **Form W-4V** (or a similar form provided by the payer) and give it to the payer. The amount withheld will be 10% of each payment.

Unemployment compensation is taxable. So, if you do not have income tax withheld, you may have to make estimated tax payments. See chapter 2.

If you do not pay enough tax either through withholding or estimated tax, you may have to pay a penalty. See chapter 4.

Form 1099-G. If income tax is withheld from your unemployment compensation, you will receive a Form 1099-G, *Certain Government Payments*. Box 1 will show the amount of unemployment compensation you got for the year. Box 4 will show the amount of tax withheld.

Federal Payments

You can choose to have income tax withheld from certain federal payments you receive. These payments are:

- 1) Social security benefits,
- 2) Tier 1 railroad retirement benefits,
- 3) Commodity credit loans you choose to include in your gross income, and
- 4) Payments under the Agricultural Act of 1949 (7 U.S.C. 1421 et seq.), or title II of the Disaster Assistance Act of 1988, as amended, that are treated as insurance proceeds and that you received because:

- a) Your crops were destroyed or damaged by drought, flood, or any other natural disaster, or
- b) You were unable to plant crops because of a natural disaster described in (a).

To make this choice, you will have to fill out **Form W-4V** (or a similar form provided by the payer) and give it to the payer. For 2002, you

can choose to have 7%, 10%, 15%, or 27% of each payment withheld.

If you do not choose to have income tax withheld, you may have to make estimated tax payments. See chapter 2.

If you do not pay enough tax either through withholding or estimated tax, you may have to pay a penalty. See chapter 4.

More information. For more information about the tax treatment of social security and railroad retirement benefits, get Publication 915, *Social Security and Equivalent Railroad Retirement Benefits*. Get Publication 225, *Farmer's Tax Guide*, for information about the tax treatment of commodity credit loans or crop disaster payments.

Backup Withholding

Banks or other businesses that pay you certain kinds of income must file an information return (Form 1099) with the IRS. The information return shows how much you were paid during the year. It also includes your name and taxpayer identification number (TIN). TINs are explained later in this discussion.

These payments generally are not subject to withholding. However, "backup" withholding is required in certain situations.

Payments subject to backup withholding. Backup withholding can apply to most kinds of payments that are reported on Form 1099. These include:

- **Interest payments** (Form 1099–INT),
- **Dividends** (Form 1099–DIV),
- **Patronage dividends**, but only if at least half the payment is in money (Form 1099–PATR),
- **Rents, profits, or other gains** (Form 1099–MISC),
- **Commissions, fees**, or other payments for work you do as an independent contractor (Form 1099–MISC),
- **Payments by brokers** (Form 1099–B),
- **Payments by fishing boat operators**, but only the part that is in money and that represents a share of the proceeds of the catch (Form 1099–MISC), and
- **Royalty payments** (Form 1099–MISC).

Backup withholding may also apply to gambling winnings. See *Backup withholding on gambling winnings* under *Gambling Winnings*, earlier.

Payments not subject to backup withholding. Backup withholding does not apply to

payments reported on Form 1099–MISC (other than payments by fishing boat operators and royalty payments) unless at least one of the following three situations applies.

- 1) The amount you receive from any one payer is \$600 or more.
- 2) The payer had to give you a Form 1099 last year.
- 3) The payer made payments to you last year that were subject to backup withholding.

Form 1099 and backup withholding are generally not required for a payment of less than \$10.

Withholding rules. When you open a new account, make an investment, or begin to receive payments reported on Form 1099, the bank or other business will give you **Form W–9, Request for Taxpayer Identification Number and Certification**, or a similar form. You must show your TIN on the form and, if your account or investment will earn interest or dividends, you also must certify (under penalties of perjury) that your TIN is correct and that you are not subject to backup withholding.

For 2002, the payer must withhold at a flat 30% rate in the following situations.

- You do not give the payer your TIN in the required manner.
- The IRS notifies the payer that the TIN you gave is incorrect.
- You are required, but fail, to certify that you are not subject to backup withholding.
- The IRS notifies the payer to start withholding on interest or dividends because you have underreported interest or dividends on your income tax return. The IRS will do this only after it has mailed you four notices over at least a 120-day period.

Taxpayer identification number (TIN). Your TIN is one of the following three numbers.

- 1) Your social security number (SSN).
- 2) Your employer identification number.
- 3) An IRS individual taxpayer identification number (ITIN). Aliens who do not have an SSN and are not eligible to get one should get an ITIN. **Form W–7, Application for IRS Individual Taxpayer Identification Number**, is used to apply for an ITIN.

An ITIN is for tax use only. It does not entitle you to social security benefits or change your employment or immigration status under U.S. law.

For more information on ITINs, get Publication 1915, *Understanding Your IRS Individual Taxpayer Identification Number*.

How to prevent or stop backup withholding.

If you have been notified by a payer that the TIN you gave is incorrect, you can usually prevent backup withholding from starting or stop backup withholding once it has begun by giving the payer your correct name and TIN. You must certify that the TIN you give is correct.

However, the payer will provide additional instructions if the TIN you gave needs to be validated by the Social Security Administration or by the IRS. This may happen if both the following conditions exist.

- 1) The IRS notifies the payer twice within 3 calendar years that a TIN you gave for the same account is incorrect.
- 2) The incorrect TIN is still being used on the account when the payer receives the second notice.

Underreported interest or dividends. If you have been notified that you underreported interest or dividends, you must request a determination from the IRS to prevent backup withholding from starting or to stop backup withholding once it has begun. You must show that at least one of the following situations applies.

- No underreporting occurred.
- You have a bona fide dispute with the IRS about whether an underreporting occurred.
- Backup withholding will cause or is causing an undue hardship and it is unlikely that you will underreport interest and dividends in the future.
- You have corrected the underreporting by filing a return if you did not previously file one and by paying all taxes, penalties, and interest due for any underreported interest or dividend payments.

If the IRS determines that backup withholding should stop, it will provide you with certification and will notify the payers who were sent notices earlier.

Penalties. There are civil and criminal penalties for giving false information to avoid backup withholding. The civil penalty is \$500. The criminal penalty, upon conviction, is a fine of up to \$1,000 or imprisonment of up to one year, or both.

2.

Estimated Tax for 2002

Important Changes for 2002

Estimated tax safe harbor for higher income individuals. For installment payments for tax years beginning in 2002, the estimated tax safe harbor for higher income individuals (other than farmers and fishermen) has been modified. If your adjusted gross income is more than \$150,000 (\$75,000 if married filing a separate return), your withholding and estimated tax payments must be at least the smaller of 90% of your tax liability for 2002 or **112%** of the tax shown on your 2001 return (provided your 2001 return covered all 12 months) to avoid an estimated tax penalty.

Important Reminders

Who must pay estimated tax. You must pay estimated tax unless the total tax shown on your return minus the amount you paid through withholding (including excess social security and railroad retirement tax withholding) will be less than \$1,000.

Payment of estimated tax by electronic funds withdrawal. You may be able to pay your estimated tax by authorizing an automatic withdrawal from your checking or savings account. For more information, see *Payment by Electronic Funds Withdrawal* under *How To Pay Estimated Tax*, later.

Employment taxes on household employees. If you either receive income from which tax is withheld or must make estimated tax payments, you must include any expected employment (social security, Medicare, and federal unemployment) taxes for household employees when figuring your estimated tax.

Introduction

Estimated tax is the method used to pay tax on income that is not subject to withholding. This includes income from self-employment, interest, dividends, alimony, rent, gains from the sale of assets, prizes, and awards. You also may have to pay estimated tax if the amount of income tax being withheld from your salary, pension, or other income is not enough.

Estimated tax is used to pay both income tax and self-employment tax, as well as other taxes and amounts reported on your tax return. If you do not pay enough through withholding or by making estimated tax payments, you may be

charged a penalty. If you do not pay enough by the due date of each payment period (see *When To Pay Estimated Tax*, later), you may be charged a penalty even if you are due a refund when you file your tax return. For information on when the penalty applies, see chapter 4.



It would be helpful for you to keep a copy of your 2001 tax return and an estimate of your 2002 income nearby while reading this chapter.

Topics

This chapter discusses:

- Who must make estimated tax payments,
- How to figure estimated tax (including illustrated examples),
- When to pay estimated tax,
- How to figure each payment, and
- How to pay estimated tax.

Useful Items

You may want to see:

Publication

- 553** Highlights of 2001 Tax Changes

Form (and Instructions)

- 1040-ES** Estimated Tax for Individuals

See chapter 5 for information about how to get this publication and form.

Who Must Make Estimated Tax Payments?

If you had a tax liability for 2001, you may have to pay estimated tax for 2002.

General Rule

You must make estimated tax payments for 2002 if both of the following apply.

- 1) You expect to owe at least \$1,000 in tax for 2002, after subtracting your withholding and credits, and
- 2) You expect your withholding and credits to be less than the smaller of:
 - a) 90% of the tax to be shown on your 2002 tax return, or
 - b) 100% of the tax shown on your 2001 tax return. Your 2001 tax return must cover all 12 months.



If all your income will be subject to income tax withholding, you probably do not need to make estimated tax payments.

Example 2.1. To figure whether she should pay estimated tax for 2002, Jane, who files as

head of household, uses the following information.

Expected AGI for 2002	\$61,125
AGI for 2001	\$58,950
Tax shown on 2001 return	\$10,500
Tax expected to be shown on 2002 return	\$11,500
Tax expected to be withheld in 2002	\$10,400

Jane uses *Figure B* (on the next page). Jane's answer to the chart's first question is YES — she expects to owe at least \$1,000 for 2002 after subtracting her withholding from her expected tax (\$11,500 – \$10,400 = \$1,100). Her answer to the chart's second question is also YES — she expects her income tax withholding (\$10,400) to be at least 90% of the tax to be shown on her 2002 return (\$11,500 × 90% = \$10,350). Jane does not need to pay estimated tax.

Example 2.2. The facts are the same as in *Example 2.1*, except that Jane expects only \$8,500 tax to be withheld in 2002. Because that is less than \$10,350, her answer to the chart's second question is NO.

Jane's answer to the chart's third question is also NO — she does not expect her income tax withholding (\$8,500) to be at least 100% of the tax shown on her 2001 return (\$10,500). Jane must make estimated tax payments for 2002.

Example 2.3. The facts are the same as in *Example 2.2*, except that the tax shown on Jane's 2001 return was \$8,000. Because she expects to have more than \$8,000 withheld in 2002, her answer to the chart's third question is YES. Jane does not need to pay estimated tax for 2002.

Married Taxpayers

To figure whether you must make estimated tax payments, apply the rules discussed here to your separate estimated income. If you can make joint estimated tax payments, you can apply these rules on a joint basis.

You and your spouse can make joint estimated tax payments even if you are not living together.

You and your spouse cannot make joint estimated tax payments if:

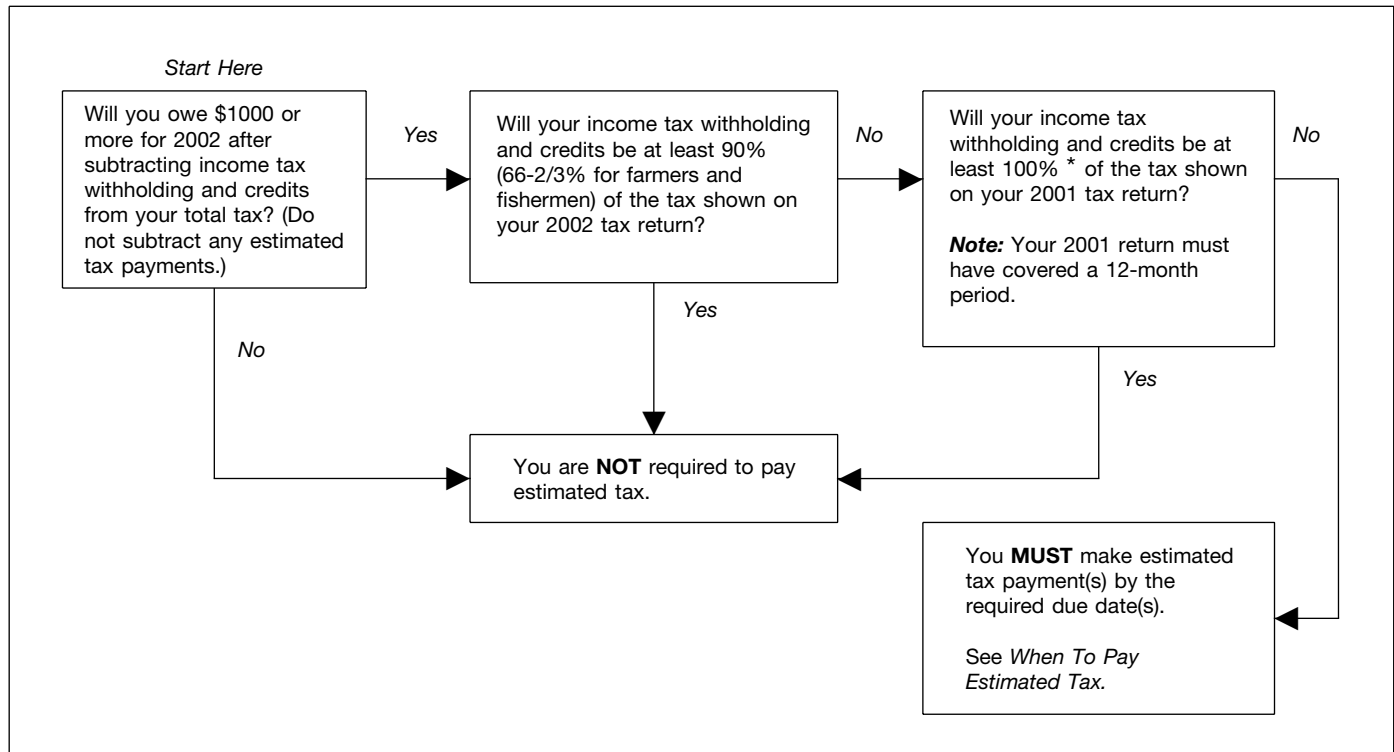
- 1) You are legally separated under a decree of divorce or separate maintenance,
- 2) Either spouse is a nonresident alien, or
- 3) You and your spouse have different tax years.

Whether you and your spouse make joint estimated tax payments or separate payments will not affect your choice of filing a joint tax return or separate returns for 2002.

2001 separate returns and 2002 joint return. If you plan to file a joint return with your spouse for 2002, but you filed separate returns for 2001, your 2001 tax is the total of the tax shown on your separate returns. You filed a separate return if you filed as single, head of household, or married filing separately.

2001 joint return and 2002 separate returns. If you plan to file a separate return for 2002, but you filed a joint return for 2001, your 2001 tax is your share of the tax on the joint return. You file a separate return if you file as

Figure B. Do You Have To Pay Estimated Tax?



* 112% if less than two-thirds of your gross income for 2001 and 2002 is from farming or fishing and your 2001 adjusted gross income was more than \$150,000 (\$75,000 if your filing status for 2002 is married filing a separate return).

single, head of household, or married filing separately.

To figure your share of the tax on a joint return, first figure the tax both you and your spouse would have paid had you filed separate returns for 2001 using the same filing status as for 2002. Then multiply the tax on the joint return by the following fraction:

$$\frac{\text{The tax you would have paid had you filed a separate return}}{\text{The total tax you and your spouse would have paid had you filed separate returns}}$$

Example 2.4. Joe and Heather filed a joint return for 2001 showing taxable income of \$48,000 and a tax of \$7,557. Of the \$48,000 taxable income, \$40,000 was Joe's and the rest was Heather's. For 2002, they plan to file married filing separately. Joe figures his share of the tax on the 2001 joint return as follows:

Tax on \$40,000 based on a separate return	\$8,172
Tax on \$8,000 based on a separate return	<u>1,204</u>
Total	\$9,376
Joe's percentage of total (\$8,172 ÷ \$9,376)	87%
Joe's share of tax on joint return tax (\$7,557 × 87%)	<u>\$6,575</u>

Special Rules for Farmers and Fishermen and Higher Income Taxpayers

There are special rules for farmers, fishermen, and certain higher income taxpayers.

Farmers and Fishermen

If at least two-thirds of your gross income for 2001 or 2002 is from farming or fishing, substitute 66 $\frac{2}{3}$ % for 90% in 2a) under *General Rule*, earlier.

For definitions of gross income from farming and gross income from fishing, see *Farmers and Fishermen* later under *When To Pay Estimated Tax*.

Higher Income Taxpayers

If your adjusted gross income (AGI) for 2001 was more than \$150,000 (\$75,000 if your filing status for 2002 is married filing a separate return), substitute 112% for 100% in 2b) under *General Rule*, earlier. This rule does not apply to farmers and fishermen.

For 2001, AGI is the amount shown on Form 1040, line 34; Form 1040A, line 20; and Form 1040EZ, line 4.

Aliens

Resident and nonresident aliens may also have to make estimated tax payments. Resident aliens should follow the rules in this publication, unless noted otherwise. Nonresident aliens should get **Form 1040-ES(NR)**, U.S. Estimated Tax for Nonresident Alien Individuals.

Avoiding Estimated Tax

If you receive salaries and wages, you can avoid having to make estimated tax payments by asking your employer to take more tax out of your earnings. To do this, file a new Form W-4 with your employer. See chapter 1.

Estimated tax payments not required. You do not have to pay estimated tax for 2002 if you meet all three of the following conditions.

- 1) You had no tax liability for 2001.
- 2) You were a U.S. citizen or resident for the whole year.
- 3) Your 2001 tax year covered a 12-month period.

You had no tax liability for 2001 if your total tax (defined later under *Required Annual Payment*) was zero or you did not have to file an income tax return.

Estates and Trusts

Estates and trusts also must make estimated tax payments. However, estates (and certain grantor trusts that receive the residue of the decedent's estate under the decedent's will) are exempt from paying estimated tax for the first two years after the decedent's death.

Estates and trusts must use **Form 1041-ES**, *Estimated Income Tax for Estates and Trusts*, to figure and pay estimated tax.

How To Figure Estimated Tax

To figure your estimated tax, you must figure your expected adjusted gross income, taxable income, taxes, deductions, and credits for the year.

When figuring your 2002 estimated tax, it may be helpful to use your income, deductions, and credits for 2001 as a starting point. Use your

2001 federal tax return as a guide. You can use Form 1040-ES to figure your estimated tax.

You must make adjustments both for changes in your own situation and for recent changes in the tax law. For 2002, there are several changes in the law. These changes are discussed under *Important Changes for 2002* at the beginning of this publication. For information about these and other changes in the law, get Publication 553, *Highlights of 2001 Tax Changes*, or visit the IRS Web Site at www.irs.gov.


Form 1040-ES includes a worksheet to help you figure your estimated tax. Keep the worksheet for your records. *Example 2.9* illustrates the use of the worksheet. A blank worksheet appears later in this chapter.

Expected Adjusted Gross Income

Your expected adjusted gross income for 2002 (line 1 of the *2002 Estimated Tax Worksheet*) is your expected total income minus your expected adjustments to income.

Total income. Include in your total income all the income you expect to receive during the year, even income that is subject to withholding. However, do not include income that is tax exempt.

Total income includes all income and loss for 2002 that, if you had received it in 2001, would have been included in the total on line 22 of Form 1040, line 15 of Form 1040A, or line 4 of Form 1040EZ. When figuring your net earnings from self-employment, be sure to use only 92.35% of your total net profit from self-employment.


 **Social security and railroad retirement benefits.** If you expect to receive social security or tier 1 railroad retirement benefits during the year, use *Worksheet 2.1* to figure the amount of expected taxable benefits you should include on line 1 of the *2002 Estimated Tax Worksheet*.

Worksheet 2.1

1. Enter your expected social security and railroad retirement benefits _____
2. Enter one-half of line 1 _____
3. Enter your expected total income. Do not include any social security and railroad retirement benefits, nontaxable interest income, nontaxable IRA distributions, or nontaxable pension distributions _____
4. Enter your expected nontaxable interest income _____
5. Add lines 2, 3, and 4 _____
6. Enter your expected adjustments to income except any student loan interest deduction _____
7. Subtract line 6 from line 5 _____
8. Enter \$25,000 (\$32,000 if you expect to file married filing a joint return; \$0 if you expect to file married filing a separate return and expect to live with your spouse at any time during the year) _____
9. Subtract line 8 from line 7. If zero or less, stop here. Do not include any social security or railroad retirement benefits on line 1 of your *2002 Estimated Tax Worksheet* _____

10. Enter \$9,000 (\$12,000 if you expect to file married filing a joint return; \$0 if you expect to file married filing a separate return and expect to live with your spouse at any time during the year) _____
11. Subtract line 10 from line 9. If zero or less, enter -0- _____
12. Enter the smaller of line 9 or line 10 _____
13. Enter one-half of line 12 _____
14. Enter the smaller of line 2 or line 13 _____
15. Multiply line 11 by 85% (.85). If line 11 is zero, enter -0- _____
16. Add lines 14 and 15 _____
17. Multiply line 1 by 85% (.85) _____
18. Enter the smaller of line 16 or line 17. This is the amount of your expected taxable social security and railroad retirement benefits. Include this amount in the total on line 1 of your *2002 Estimated Tax Worksheet* _____

Adjustments to income. Be sure to subtract from your expected total income all of the adjustments you expect to take on your 2002 tax return. If you are using your 2001 return as a guide and filed Form 1040, your adjustments for 2001 were on lines 23-31a. If you filed Form 1040A, your 2001 adjustments were on lines 16 and 17.

 **Self-employed.** If you expect to have income from self-employment, use the following worksheet to figure your expected self-employment tax. The result on line 10 of the worksheet is your deduction for one-half of your self-employment tax. Include this amount in the adjustments you subtract from your total income to arrive at your expected AGI. If you file a joint return and both you and your spouse have net earnings from self-employment, you must each complete a separate worksheet.

Worksheet 2.2


1. Enter your expected income and profits subject to self-employment tax _____
2. Multiply the amount on line 1 by .9235 _____
3. Multiply the amount on line 2 by .029 _____
4. Social security tax maximum income \$84,900
5. Enter your expected wages (if subject to social security tax) _____
6. Subtract line 5 from line 4 _____
- Note.** If line 6 is zero or less, enter -0- on line 8 and skip to line 9.
7. Enter the smaller of line 2 or line 6 _____
8. Multiply the amount on line 7 by .124 _____
9. Add line 3 and line 8. Enter the result here and on line 11 of your *2002 Estimated Tax Worksheet* _____
10. Multiply the amount on line 9 by .50. This is your deduction for one-half your self-employment tax. _____

Expected Taxable Income

Reduce your expected adjusted gross income for 2002 by either your expected itemized deductions or your standard deduction and by your exemptions (lines 2 through 5 of the *2001 Estimated Tax Worksheet*).

Itemized deductions. If you expect to claim itemized deductions on your 2002 tax return, subtract them from your expected adjusted gross income.

Itemized deductions are the deductions that can be claimed on Schedule A of Form 1040.

 **Reduction of itemized deductions.** For 2002, your total itemized deductions may be reduced if your adjusted gross income (AGI) is more than \$137,300 (\$68,650 if married filing separately). If you expect your AGI to be more than that amount, use the following worksheet to figure the amount to enter on line 2 of the *2002 Estimated Tax Worksheet*.

Worksheet 2.3

1. Enter the estimated total of your itemized deductions _____
2. Enter the amount included in line 1 for medical and dental expenses, investment interest, casualty or theft losses, and gambling losses _____
3. Subtract line 2 from line 1 _____
- Note.** If the amount on line 3 is zero, stop here and enter the amount from line 1 of this worksheet on line 2 of the *2002 Estimated Tax Worksheet*.
4. Multiply the amount on line 3 by .80 _____
5. Enter the amount from line 1 of the *2002 Estimated Tax Worksheet* _____
6. Enter \$137,300 (\$68,650 if married filing separately) _____
7. Subtract line 6 from line 5 _____
8. Multiply the amount on line 7 by .03 _____
9. Enter the smaller of line 4 or line 8 _____
10. Subtract line 9 from line 1. Enter the result here and on line 2 of the *2002 Estimated Tax Worksheet* _____

Standard deduction. If you expect to claim the standard deduction on your 2002 tax return, subtract it from your expected adjusted gross income. Use the *2002 Standard Deduction Tables* at the end of this chapter to find your standard deduction.

No standard deduction. The standard deduction for some individuals is zero. Your standard deduction will be zero if you:

- 1) File a separate return and your spouse itemizes deductions,
- 2) Are a nonresident alien, or
- 3) Make a return for a period of less than 12 months because you change your accounting period.

Exemptions. After you have subtracted either your expected itemized deductions or your standard deduction from your expected adjusted gross income, reduce the amount remaining by \$3,000 for each exemption you expect to take on your 2002 tax return (lines 4 and 5 of the *2002 Estimated Tax Worksheet*). If another person (such as your parent) can claim an exemption for you on his or her tax return, you cannot claim your own personal exemption. This is true even if the other person will not claim your exemption or the exemption will be reduced or eliminated under the phaseout rule.

Phaseout. For 2002, your deduction for personal exemptions is phased out if your adjusted gross income (AGI) falls within the following brackets.

Table 2.1

Single	\$137,300-\$259,800
Married filing jointly or qualifying widow(er)	\$206,000-\$328,500

Married filing separately \$103,000–\$164,250
 Head of household \$171,650–\$294,150

If the amount on line 1 of your *2002 Estimated Tax Worksheet* is more than the highest amount in the bracket for your filing status, enter “–0–” on line 4 of your *2002 Estimated Tax Worksheet*. If your AGI will fall within the bracket, use the following worksheet to figure the amount to enter on line 4 of your *2002 Estimated Tax Worksheet*.

Worksheet 2.4

1. Multiply \$3,000 by the number of exemptions you plan to claim _____
2. Enter the amount from line 1 of your *2002 Estimated Tax Worksheet* _____
3. Enter:
 - \$137,300 if single
 - \$206,000 if married filing jointly or qualifying widow(er)
 - \$103,000 if married filing separately
 - \$171,650 if head of household _____
4. Subtract line 3 from line 2 _____
5. Divide the amount on line 4 by \$2,500 (\$1,250 if married filing separately). If the result is not a whole number, increase it to the next whole number _____
6. Multiply the number on line 5 by .02. Enter the result as a decimal, but not more than 1 _____
7. Multiply the amount on line 1 by the decimal on line 6 _____
8. Subtract line 7 from line 1. Enter the result here and on line 4 of your *2002 Estimated Tax Worksheet* _____

Expected Taxes and Credits

After you have figured your expected taxable income, follow the steps below to figure your expected taxes, credits, and total tax for 2002. Most people will have entries for only a few of these steps. However, you should check every step to be sure that you do not overlook anything.

Step 1. Figure your expected income tax (line 6 of the *2002 Estimated Tax Worksheet*). Use the *2002 Tax Rate Schedules* at the end of this chapter or in the instructions to Form 1040–ES to figure your expected income tax. You must use a special method to figure tax on the income of a child under age 14 who has more than \$1,500 of investment income. See *Tax on Investment Income of Child Under 14* in Publication 929, *Tax Rules for Children and Dependents*.

Tax on net capital gain. The regular income tax rates for individuals do not apply to a net capital gain. Instead, your net capital gain is taxed at a lower maximum rate.

The term “net capital gain” means the amount by which your net long-term capital gain for the year is more than your net short-term capital loss.



The maximum rate may be 8%, 10%, 20%, 25%, or 28%, or a combination of those rates. Use *Worksheet 2.5* to figure your tax if you have capital gain.

Worksheet 2.5

1. Enter the amount from line 5 of your *2002 Estimated Tax Worksheet* _____
2. Enter the net capital gain expected for 2002 _____

3. Combine the net short-term capital loss and 28% rate gain or loss expected for 2002. If zero or less, enter 0 _____
 4. Enter the unrecaptured section 1250 gain expected for 2002 _____
 5. Add lines 3 and 4 _____
 6. Subtract line 5 from line 2. If zero or less, enter 0 _____
 7. Subtract line 6 from line 1. If zero or less, enter 0 _____
 8. Enter the **smaller** of line 1 or \$46,700 (\$27,950 if single; \$23,350 if married filing separately; \$37,450 if head of household) _____
 9. Enter the **smaller** of line 7 or line 8 _____
 10. Subtract line 2 from line 1. If zero or less, enter 0 _____
 11. Enter the **larger** of line 9 or line 10 _____
 12. Tax on amount on line 11 from the *2002 Tax Rate Schedule* _____
- Note.** If line 7 is more than line 8, go to line 18.
13. Subtract line 9 from line 8. If zero or less, enter 0 _____
 14. Multiply line 13 by 10% (.10) _____
 15. Enter the amount, if any, of your qualified 5-year gain. Do not enter more than the amount on line 13. _____
 16. Multiply line 15 by 2% (.02) _____
 17. Subtract line 16 from line 14 _____
- Note.** If line 13 minus line 15 is more than zero and equal to line 6, enter 0 on lines 20, 25, and 28, and go to line 29.
18. Enter the **smaller** of line 1 or line 6 _____
 19. Subtract line 13 from line 18 _____
 20. Multiply line 19 by 20% (.20) _____
- Note.** If line 4 is zero or blank, skip lines 21 through 25 and read the note above line 26.
21. Enter the **smaller** of line 2 or line 4 _____
 22. Add lines 2 and 11 _____
 23. Subtract line 1 from line 22. If zero or less, enter 0 _____
 24. Subtract line 23 from line 21. If zero or less, enter 0 _____
 25. Multiply line 24 by 25% (.25) _____
- Note.** If line 3 is zero or blank, go to line 29.
26. Add lines 11, 13, 19, and 24 _____
 27. Subtract line 26 from line 1. If zero or less, enter 0 _____
 28. Multiply line 27 by 28% (.28) _____
 29. Add lines 12, 17, 20, 25, and 28 _____
 30. Tax on the amount on line 1 from the *2002 Tax Rate Schedule* _____
 31. **Tax.** Enter the **smaller** of line 29 or line 30 here and on line 6 of the *2002 Estimated Tax Worksheet* _____

A **collectibles gain or loss** is any gain or loss from the sale or exchange of a work of art, rug, antique, metal, gem, stamp, coin, or alcoholic beverage or other collectible that is a capital asset and that was held more than one year.

Step 2. Add your expected taxes (line 8 of the *2002 Estimated Tax Worksheet*). Include on line 8 the sum of:

- 1) Your tax on line 6,
- 2) Your expected alternative minimum tax from Form 6251 (line 41 of the 2001 Form 1040) on line 7,
- 3) Your expected additional taxes from Form 8814, *Parents' Election To Report Child's Interest and Dividends*, and Form 4972, *Tax on Lump-Sum Distributions* (line 40 box a and box b of the 2001 Form 1040), and
- 4) Any recapture of education credits.

Step 3. Subtract your expected credits (line 9 of the *2002 Estimated Tax Worksheet*). If you

are using your 2001 return as a guide and filed Form 1040, your total credits for 2001 were shown on line 51. If you filed Form 1040A, your total credits for 2001 were on line 33.

If your credits on line 9 of the worksheet are more than your taxes on line 8, enter “–0–” on line 10 and go on to Step 4.

Step 4. Add your expected self-employment tax (line 11 of the *2002 Estimated Tax Worksheet*). You should have already figured your self-employment tax (see *Expected Adjusted Gross Income* earlier in this chapter).

Step 5. Add your expected other taxes (line 12 of the *2002 Estimated Tax Worksheet*).

Other taxes include:

- 1) Taxes on accumulation distribution of trusts,
- 2) Taxes on distributions from an MSA,
- 3) Taxes on early distributions from:
 - a) An IRA or other qualified plan,
 - b) An annuity, or
 - c) A modified endowment contract entered into after June 20, 1988,
- 4) Advance earned income credit payments,
- 5) Household employment taxes (before subtracting advance EIC payments made to your employee(s) if:
 - a) You will have federal income tax withheld from wages, pensions, annuities, gambling winnings, or other income, or
 - b) You would be required to make estimated tax payments even if you did not include household employment taxes when figuring your estimated tax, and
- 6) Write-in amounts on line 58 of Form 1040.

Do not include tax on recapture of a federal mortgage subsidy, social security and Medicare tax on unreported tip income, or uncollected employee social security and Medicare or RRTA tax on tips or group-term life insurance.

If you filed Form 1040 for 2001, any of the taxes in items 1, 2, or 3 above would have been included in the total on line 55 of that form.

If you filed a 2001 Form 1040A, your only “other taxes” were any advance earned income credit payments on line 35.

Step 6. Subtract your expected earned income credit, additional child tax credit, and Form 4136 fuel tax credit (line 13b of the *2002 Estimated Tax Worksheet*). These are shown on lines 61a, 63, and 65 of the 2001 Form 1040.

To figure your expected fuel tax credit, do not include fuel tax for the first three quarters of the year that you expect to have refunded to you.

The earned income credit is shown on line 39a of the 2001 Form 1040A. The additional child tax credit is shown on line 40 of the 2001 Form 1040A.

The result of steps 1 through 6 is your **total expected tax** for 2002 (line 13c of the *2002 Estimated Tax Worksheet*).

2002 Estimated Tax Worksheet (keep for your records)

1 Enter amount of adjusted gross income you expect in 2002 (see instructions)	1		
2 • If you plan to itemize deductions, enter the estimated total of your itemized deductions. } Caution: <i>If line 1 above is over \$137,300 (\$68,650 if married filing separately), your deduction may be reduced. See Pub. 505 for details.</i> • If you do not plan to itemize deductions, see Standard Deduction on page 2 and enter your standard deduction here. }	2		
3 Subtract line 2 from line 1	3		
4 Exemptions. Multiply \$3,000 by the number of personal exemptions. If you can be claimed as a dependent on another person's 2002 return, your personal exemption is not allowed. Caution: <i>See Pub. 505 to figure the amount to enter if line 1 above is over: \$206,000 if married filing jointly or qualifying widow(er); \$171,650 if head of household; \$137,300 if single; or \$103,000 if married filing separately</i>	4		
5 Subtract line 4 from line 3	5		
6 Tax. Figure your tax on the amount on line 5 by using the 2002 Tax Rate Schedules on page 2. Caution: <i>If you have a net capital gain, see Pub. 505 to figure the tax</i>	6		
7 Alternative minimum tax from Form 6251	7		
8 Add lines 6 and 7. Also include any tax from Forms 4972 and 8814 and any recapture of the education credits (see instructions)	8		
9 Credits (see instructions). Do not include any income tax withholding on this line.	9		
10 Subtract line 9 from line 8. If zero or less, enter -0-.	10		
11 Self-employment tax (see instructions). Estimate of 2002 net earnings from self-employment \$..... ; if \$84,900 or less , multiply the amount by 15.3%; if more than \$84,900 , multiply the amount by 2.9%, add \$10,527.60 to the result, and enter the total. Caution: <i>If you also have wages subject to social security tax, see Pub. 505 to figure the amount to enter.</i>	11		
12 Other taxes (see instructions)	12		
13a Add lines 10 through 12	13a		
b Earned income credit, additional child tax credit, and credit from Form 4136	13b		
c Total 2002 estimated tax. Subtract line 13b from line 13a. If zero or less, enter -0- ▶	13c		
14a Multiply line 13c by 90% (66% for farmers and fishermen).	14a		
b Enter the tax shown on your 2001 tax return (112% of that amount if you are not a farmer or fisherman and the adjusted gross income shown on line 34 of that return is more than \$150,000 or, if married filing separately for 2002, more than \$75,000)	14b		
c Required annual payment to avoid a penalty. Enter the smaller of line 14a or 14b . . ▶ Caution: <i>Generally, if you do not prepay (through income tax withholding and estimated tax payments) at least the amount on line 14c, you may owe a penalty for not paying enough estimated tax. To avoid a penalty, make sure your estimate on line 13c 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 may pay the amount shown on line 13c. For details, see Pub. 505.</i>	14c		
15 Income tax withheld and estimated to be withheld during 2002 (including income tax withholding on pensions, annuities, certain deferred income, etc.)	15		
16 Subtract line 15 from line 14c. (Note: <i>If zero or less or line 13c minus line 15 is less than \$1,000, stop here. You are not required to make estimated tax payments.</i>)	16		
17 If the first payment you are required to make is due April 15, 2002, enter ¼ of line 16 (minus any 2001 overpayment that you are applying to this installment) here, and on your payment voucher(s) if you are paying by check or money order. (Note: <i>Household employers, see instructions.</i>)	17		

Required Annual Payment

You figure the total amount you must pay for 2002 through withholding and estimated tax payments on lines 14a through 14c of the *2002 Estimated Tax Worksheet*.

General rule. The total amount you must pay is the **smaller** of:

- 1) 90% of your total expected tax for 2002, or
- 2) 100% of the total tax shown on your 2001 return. Your 2001 tax return must cover all 12 months.

Exceptions. There are exceptions to the general rule for certain higher income taxpayers and for farmers and fishermen.

Higher income taxpayers. If your adjusted gross income (AGI) for 2001 was more than \$150,000 (\$75,000 if your filing status for 2002 is married filing a separate return), substitute 112% for 100% in (2) above. This rule does not apply to farmers and fishermen.

For 2001, AGI is the amount shown on Form 1040 – line 34; Form 1040A – line 20; and Form 1040EZ – line 4.

Farmers and fishermen. If at least two-thirds of your gross income for 2001 or 2002 is from farming or fishing, your required annual payment is the smaller of:

- 1) 66 $\frac{2}{3}$ % (.6667) of your total tax for 2002, or
- 2) 100% of the total tax shown on your 2001 return. (Your 2001 tax return must cover all 12 months.)

For definitions of “gross income from farming” and “gross income from fishing,” see *Farmers and Fishermen* later under *When To Pay Estimated Tax*.

Total tax for 2001. Your 2001 total tax on Form 1040 is the amount on line 58 reduced by the total of the amounts on lines 54, 61a, and 63, any credit from Form 4136 included on line 65, any recapture of a federal mortgage subsidy and any uncollected social security, Medicare, or railroad retirement tax included on line 58, and any tax on excess contributions to IRAs and medical savings accounts, and on excess accumulations in qualified retirement plans from Form 5329 included on line 55.

On Form 1040A, it is line 36 reduced by the amounts on lines 39a and 40. On Form 1040EZ, it is line 11 reduced by line 9a.

Example 2.5. Jeremy Martin’s total tax on his 2001 return was \$45,000, and his expected tax for 2002 is \$70,000. His 2001 AGI was \$180,000. Because Jeremy had more than \$150,000 of AGI in 2001, he figures his required annual payment as follows. He determines that 90% of his expected tax for 2002 is \$63,000 (.90 × \$70,000). Next, he determines that 112% of the tax shown on his 2001 return is \$50,400. Finally, he determines that his required annual payment is \$50,400, the smaller of the two.

Total Estimated Tax Payments

Figure the total amount you must pay for 2002 through estimated tax payments on lines 15 and 16 of the *2002 Estimated Tax Worksheet*. Sub-

tract your expected withholding from your required annual payment. You usually must pay this difference in four equal installments. (See *When To Pay Estimated Tax* and *How To Figure Each Payment*, later.)

If your total expected tax on line 13c, minus your expected withholding on line 15, is less than \$1,000, you do not need to make estimated tax payments.

Withholding. Your expected withholding for 2002 includes the income tax you expect to be withheld from all sources (wages, pensions and annuities, etc.). It also includes excess social security and railroad retirement tax you expect to be withheld from your wages.

For this purpose, you will have excess social security or tier 1 railroad retirement tax withholding for 2002 only if your wages from two or more employers are more than \$84,900.

When To Pay Estimated Tax

For estimated tax purposes, the year is divided into four payment periods. Each period has a specific payment due date. If you do not pay enough tax by the due date of each of the payment periods, you may be charged a penalty even if you are due a refund when you file your income tax return. The following chart gives the payment periods and due dates for estimated tax payments.

Table 2.3

For the period:	Due date:
Jan. 1* through March 31	April 15
April 1 through May 31	June 15
June 1 through August 31	September 15
Sept. 1 through Dec. 31	Jan. 15 next year**

*If your tax year does not begin on January 1, see *Fiscal year taxpayers*, later.

**See *January payment*, later.

Saturday, Sunday, holiday rule. If the due date for making an estimated tax payment falls on a Saturday, Sunday, or legal holiday, the payment will be on time if you make it on the next day that is not a Saturday, Sunday, or legal holiday. For example, a payment due Saturday, June 15, 2002, will be on time if you make it by Monday, June 17, 2002.

January payment. If you file your 2002 Form 1040 or Form 1040A by January 31, 2003, and pay the rest of the tax you owe, you do not need to make your estimated tax payment that would be due on January 15, 2003.

Example 2.6. Janet Adams does not pay any estimated tax due for 2002. She files her 2002 income tax return and pays the balance due as shown on her return on January 24, 2003.

Janet’s estimated tax for the fourth payment period is considered to have been paid on time. However, she may owe a penalty for not making the first three estimated tax payments. Any penalty for not making those payments will be figured up to January 24, 2003.

Fiscal year taxpayers. If your tax year does not start on January 1, your payment due dates are:

- 1) The 15th day of the 4th month of your fiscal year,
- 2) The 15th day of the 6th month of your fiscal year,
- 3) The 15th day of the 9th month of your fiscal year, and
- 4) The 15th day of the 1st month after the end of your fiscal year.

You do not have to make the last payment listed above if you file your income tax return by the last day of the first month after the end of your fiscal year and pay all the tax you owe with your return.

When To Start

You do not have to make estimated tax payments until you have income on which you will owe the tax. If you have income subject to estimated tax during the first payment period, you must make your first payment by the due date for the first payment period. You can pay all your estimated tax at that time, or you can pay it in installments. If you choose to pay in installments, make your first payment by the due date for the first payment period. Make your remaining installment payments by the due dates for the later periods.

No income subject to estimated tax during first period. If you first have income subject to estimated tax during a later payment period, you must make your first payment by the due date for that period. You can pay your entire estimated tax by the due date for that period or you can pay it in installments by the due date for that period and the due dates for the remaining periods. The following chart shows the dates for making installment payments.

Table 2.4

If you first have income on which you must pay estimated tax:	Make a payment by:	Make later installments by:
Before April 1	April 15	June 15 September 15 January 15 next year*
After March 31 and before June 1	June 15	September 15 January 15 next year*
After May 31 and before Sept. 1	September 15	January 15 next year*
After August 31	January 15 next year*	(None)

*See *January payment* and *Saturday, Sunday, holiday rule* under *When To Pay Estimated Tax*, earlier.

Change in estimated tax. After making your first estimated tax payment, changes in your income, adjustments, deductions, credits, or exemptions may make it necessary for you to refigure your estimated tax. Pay the unpaid balance of your amended estimated tax by the next payment due date after the change or in install-

ments by that date and the due dates for the remaining payment periods.

How much to pay to avoid penalty. To determine how much you should pay by each payment due date, see *How To Figure Each Payment*, later. If the earlier discussions of *No income subject to estimated tax during first period* or *Change in estimated tax* apply to you, you may need to read the explanation of the *Annualized Income Installment Method*, later, to avoid a penalty.

Farmers and Fishermen

If at least two-thirds of your gross income for 2001 or 2002 is from farming or fishing, you have only one payment due date for your 2002 estimated tax — January 15, 2003. The due dates for the first three payment periods, discussed earlier under *When To Pay Estimated Tax*, do not apply to you.

If you file your 2002 Form 1040 by March 1, 2003, and pay all the tax you owe, you do not need to pay estimated tax.

Joint returns. On a joint return, you must add your spouse's gross income to your gross income to determine if at least two-thirds of your total gross income is from farming or fishing.

Gross income. Your gross income is all income you receive in the form of money, goods, property, and services that is not exempt from tax. To determine whether two-thirds of your gross income for 2001 was from farming or fishing, use as your gross income the total of the **income** (not loss) amounts shown in the following locations.

- 1) Form 1040, lines 7, 8a, 9, 10, 11, 15b, 16b, 19, 20b, and 21.
- 2) Schedule C (Form 1040), line 7.
- 3) Schedule C–EZ (Form 1040), line 1.
- 4) Schedule D (Form 1040), line 1, column f (gains only), and lines 8 and 13, column f (gains only).
- 5) Schedule D–1 (Form 1040), line 1, column f (gains only), and line 8, column f (gains only).
- 6) Schedule E (Form 1040), lines 3, 4, 31, 36, and 38.
- 7) Schedule F (Form 1040), line 11.
- 8) Form 2439, Box 1a.
- 9) Form 4684, lines 15 and 36 (gains only).
- 10) Form 4797, line 2, column g (gains only), and line 6 (gains only).
- 11) Form 6252, line 26 or line 37 (gains only).
- 12) Form 6781, line 8 (gain only) and line 9 (gain only).
- 13) Form 8824, line 22 (unless the installment method applies).
- 14) Form 4835, line 7.
- 15) Schedule K–1 (Form 1065), lines 15b and 15c (less any partnership amounts included in (1) through (14)).

Also add your pro rata share of S corporation gross income (less any S corporation amounts included in (1) through (14)).

Gross income from farming. This is income from cultivating the soil or raising agricultural commodities. It includes the following amounts.

- 1) Income from operating a stock, dairy, poultry, bee, fruit, or truck farm.
- 2) Income from a plantation, ranch, nursery, range, orchard, or oyster bed.
- 3) Crop shares for the use of your land.
- 4) Gains from sales of draft, breeding, dairy, or sporting livestock.

For 2001, gross income from farming is the total of the amounts from:

- 1) Line 11 of Schedule F (Form 1040), *Profit or Loss From Farming*,
- 2) Line 7 of Form 4835, *Farm Rental Income and Expenses*,
- 3) Your share of a partnership's or S corporation's gross income from farming,
- 4) Your share of distributable net income from farming of an estate or trust,
- 5) Your gains from sales of draft, breeding, dairy, or sporting livestock shown on Form 4797, *Sales of Business Property*.

Wages you receive as a farm employee and wages you receive from a farm corporation are not gross income from farming.

Gross income from fishing. This is income from catching, taking, harvesting, cultivating, or farming any kind of fish, shellfish (for example, clams and mussels), crustaceans (for example, lobsters, crabs, and shrimp), sponges, seaweeds, or other aquatic forms of animal and vegetable life.

Gross income from fishing includes the following amounts.

- 1) Income for services as an officer or crew member of a vessel while the vessel is engaged in fishing.
- 2) Your share of a partnership's or S corporation's gross income from fishing.
- 3) Income for services normally performed in connection with fishing.

Services normally performed in connection with fishing include:

- Shore service as an officer or crew member of a vessel engaged in fishing, and
- Services that are necessary for the immediate preservation of the catch, such as cleaning, icing, and packing the catch.

Fiscal year farmers and fishermen. If you are a farmer or fisherman, but your tax year does not start on January 1, you can either:

- 1) Pay all your estimated tax by the 15th day after the end of your tax year, or
- 2) File your return and pay all the tax you owe by the 1st day of the 3rd month after the end of your tax year.


How To Figure Each Payment

After you have figured your estimated tax, figure how much you must pay by the due date of each payment period. You should pay enough by each due date to avoid a penalty for that period. If you do not pay enough during any payment period, you may be charged a penalty even if you are due a refund when you file your tax return. The penalty is discussed in chapter 4.

Regular Installment Method

If your first estimated tax payment is due April 15, 2002, you can figure your required payment for each period by dividing your annual estimated tax due (line 16 of the *2001 Estimated Tax Worksheet*) by 4. Use this method only if your income is basically the same throughout the year.

If you do not receive your income evenly throughout the year, your required estimated tax payments may not be the same for each period. See *Annualized Income Installment Method*, later.

 **Amended estimated tax.** If you refigure your estimated tax during the year, or if your first estimated tax payment is due after April 15, 2002, figure your required payment for each remaining payment period using the following worksheet.

Worksheet 2.6

1. Amended total estimated tax due _____
2. Multiply line 1 by:
.50 if next payment is due
June 17, 2002
.75 if next payment is due
September 16, 2002
1.00 if next payment is due
January 15, 2003 _____
3. Estimated tax payments for all previous periods _____
4. **Next required payment:** Subtract line 3 from line 2 and enter the result (but not less than zero) here and on your payment-voucher for your next required payment _____
If the payment on line 4 is due January 15, 2003, **stop here.** Otherwise, go on to line 5.
5. Add lines 3 and 4 _____
6. Subtract line 5 from line 1 and enter the result (but not less than zero) _____
7. **Each following required payment:** If the payment on line 4 is due June 17, 2002, enter one-half of the amount on line 6 here and on the payment-vouchers for your payments due September 16, 2002, and January 15, 2003. If the amount on line 4 is due September 16, 2002, enter the full amount on line 6 here and on the payment-voucher for your payment due January 15, 2003 _____

Example 2.7. Early in 2002, Mira figures her estimated tax due is \$1,800. She makes estimated tax payments on April 15 and June 17 of \$450 each ($\$1,800 \div 4$).

On July 10, she sells investment property at a gain. Her refigured estimated tax is \$4,100. Her required estimated tax payment for the third payment period is \$2,175, figured as follows.

**Filled-in Worksheet 2.6 for Mira
(Example 2.7)**

1. Amended total estimated tax due \$4,100
 2. Multiply line 1 by:
 - .50 if next payment is due
June 17, 2002
 - .75 if next payment is due
September 16, 2002
 - 1.00 if next payment is due
January 15, 2003 3,075
 3. Estimated tax payments for all previous periods 900
 4. **Next required payment:** Subtract line 3 from line 2 and enter the result (but not less than zero) here and on your payment-voucher for your next required payment \$2,175
- If the payment on line 4 is due January 15, 2003, **stop here.** Otherwise, go on to line 5.
5. Add lines 3 and 4 3,075
 6. Subtract line 5 from line 1 and enter the result (but not less than zero) 1,025
 7. **Each following required payment:** If the payment on line 4 is due June 17, 2002, enter one-half of the amount on line 6 here and on the payment-vouchers for your payments due September 16, 2002, and January 15, 2003. If the amount on line 4 is due September 16, 2002, enter the full amount on line 6 here and on the payment-voucher for your payment due January 15, 2003 \$1,025

If Mira's estimated tax does not change again, her required estimated tax payment for the fourth payment period will be \$1,025.

File Form 2210 to avoid penalty. If your estimated tax payment for a previous period is less than one-fourth of your amended estimated tax, you may be charged a penalty for underpayment of estimated tax for that period when you file your tax return. To avoid the penalty, you must file Form 2210 with your 2002 tax return. You must also show that the total of your withholding and estimated tax payment for the period was at least as much as your annualized income installment. See chapter 4 for more information.

Annualized Income Installment Method

If you do not receive your income evenly throughout the year (for example, your income from a repair shop you operate is much larger in the summer than it is during the rest of the year), your required estimated tax payment for one or more periods may be less than the amount figured using the regular installment method.

To see whether you can pay less for any period, complete the blank *2002 Annualized Estimated Tax Worksheet (Worksheet 2.10)* later in this chapter. (**Note.** You must first complete the *2002 Estimated Tax Worksheet* through line 16.) The worksheet annualizes your tax at the end of each period based on a reasonable estimate of your income, deductions, and other items relating to events that occurred since the beginning of the tax year through the end of the period. Use the result you figure on line 26d to make your estimated tax payments and complete your payment-vouchers.

See *Example 2.10* for an illustration of the worksheet.

Note. If you use the annualized income installment method to figure your estimated tax

payments, you **must** file Form 2210 with your 2002 tax return. See *Annualized Income Installment Method* in chapter 4 for more information.

Instructions For Worksheet 2.10

The top of the worksheet shows the dates for each payment period. The periods build; that is, each period includes all previous periods. After the end of each payment period, complete the worksheet column for the period from the beginning of the tax year through the end of that payment period to figure the payment due for that period.

Line 1. Enter your adjusted gross income for each period. This is your gross income, including your share of partnership or S corporation income or loss, for the period, minus your adjustments to income for that period. (See *Expected Adjusted Gross Income* under *How To Figure Estimated Tax*, earlier.)

Self-employment income. If you had self-employment income, first complete Section B. Use the amounts on line 35c when figuring the amount of adjusted gross income to enter on line 1.

Line 4. Be sure to consider all deduction limits figured on Schedule A.

Line 6. Multiply line 4 by line 5 and enter the result on line 6, unless line 3 is more than \$137,300 (\$68,650 if married filing separately). In that case, use the following worksheet to figure the amount to enter on line 6. Complete this worksheet for each period.

Worksheet 2.7

1. Enter the amount from line 4 of Section A _____
 2. Enter the amount included in line 1 for medical and dental expenses, investment interest, casualty or theft losses, and gambling losses _____
 3. Subtract line 2 from line 1 _____
 4. Enter the number from line 5 of Section A _____
 5. Multiply the amount on line 1 by the number on line 4 _____
- Note.** If the amount on line 3 is zero, stop here and enter the amount from line 5 on line 6 of Section A.
6. Multiply the amount on line 3 by the number on line 4 _____
 7. Multiply the amount on line 6 by .80 _____
 8. Enter the amount from line 3 of Section A _____
 9. Enter \$137,300 (\$68,650 if married filing separately) _____
 10. Subtract line 9 from line 8 _____
 11. Multiply the amount on line 10 by .03 _____
 12. Enter the smaller of line 7 or line 11 _____
 13. Subtract line 12 from line 5. Enter the result here and on line 6 of Section A _____

Line 7. See the *2002 Standard Deduction Tables* at the end of this chapter. Find your standard deduction in the appropriate table.

Line 10. Multiply \$3,000 by your total expected exemptions, unless line 3 is more than the amount shown for your filing status in the following table.

Table 2.5

Single	\$137,300
Married filing jointly or qualifying widow(er)	\$206,000
Married filing separately	\$103,000
Head of household	\$171,650

In that case, use the following worksheet to figure the amount to enter on line 10.

Worksheet 2.8

1. Multiply \$3,000 by your total expected exemptions _____
2. Enter the amount from line 3 of Section A _____
3. Enter the amount shown for your filing status from Table 2.5 _____
4. Subtract line 3 from line 2 _____
5. Divide the amount on line 4 by \$2,500 (\$1,250 if married filing separately). If the result is not a whole number, increase it to the next whole number _____
6. Multiply the number on line 5 by .02. Enter the result as a decimal, but not more than 1 _____
7. Multiply the amount on line 1 by the decimal on line 6 _____
8. Subtract line 7 from line 1. Enter the result here and on line 10 of Section A _____

Line 12. Use the *2002 Tax Rate Schedules* at the end of this chapter or in the instructions to Form 1040-ES to figure your annualized income tax. For the special method that must be used to figure tax on the income of a child under 14 who has more than \$1,500 investment income, see *Tax on Investment Income of Child Under 14* in Publication 929, *Tax Rules for Children and Dependents*.

Capital gains tax computation. The regular income tax rates for individuals do not apply to a net capital gain. Instead, your net capital gain is taxed at a lower maximum rate.

The term "net capital gain" means the amount by which your net long-term capital gain for the year is more than your net short-term capital loss.

The maximum rate may be 8%, 10%, 20%, 25%, or 28%, or a combination of those rates.



Use the following worksheet to figure the amount to enter on line 12 if the amount on line 1 includes capital gain.

Worksheet 2.9

1. Enter the amount from line 11 of your *2002 Annualized Estimated Tax Worksheet* _____
2. Enter the net capital gain expected for 2002 _____
3. Combine the net short-term capital loss and 28% rate gain or loss expected for 2002. If zero or less, enter 0 _____
4. Enter the unrecaptured section 1250 gain expected for 2002 _____
5. Add lines 3 and 4 _____
6. Subtract line 5 from line 2. If zero or less, enter 0 _____
7. Subtract line 6 from line 1. If zero or less, enter 0 _____
8. Enter the **smaller** of line 1 or \$46,700 (\$27,950 if single; \$23,350 if married filing separately; \$37,450 if head of household) _____
9. Enter the **smaller** of line 7 or line 8 _____
10. Subtract line 2 from line 1. If zero or less, enter 0 _____
11. Enter the **larger** of line 9 or line 10 _____
12. Tax on amount on line 11 from the *2002 Tax Rate Schedule* _____

Worksheet 2.10. **2002 Annualized Estimated Tax Worksheet** (Note: For instructions, see *Annualized Income Installment Method* in Chapter 2.)

Section A (For Figuring Your Annualized Estimated Tax Payments) —Complete each column after end of period shown.					
Estates and trusts: Use the following ending dates in each column—2/28, 4/30, 7/31, 11/30.		1/1/01 to 3/31/01	1/1/01 to 5/31/01	1/1/01 to 8/31/01	1/1/01 to 12/31/01
1 Adjusted gross income for each period. (Caution: See instructions.) Self-employed: Complete Section B first.	1				
2 Annualization amounts. (Estates and trusts, do not use the amounts shown to right. Instead, use 6, 3, 1.71429, and 1.09091.)	2	4	2.4	1.5	1
3 Annualized income. Multiply line 1 by line 2.	3				
4 Itemized deductions for period. If you do not expect to itemize, enter zero and skip to line 7. (Estates and trusts, enter -0-, skip to line 9, and enter the amount from line 3 on line 9.)	4				
5 Annualization amounts.	5	4	2.4	1.5	1
6 Multiply line 4 by line 5. (Caution: See instructions and Worksheet 2.7.)	6				
7 Standard deduction from 2002 tables.	7				
8 Enter the larger of line 6 or line 7.	8				
9 Subtract line 8 from line 3.	9				
10 Multiply \$3,000 by your total expected exemptions. (Caution: See instructions and Worksheet 2.8.)	10				
11 Subtract line 10 from line 9.	11				
12 Tax on the amount on line 11 from the 2002 Tax Rate Schedules. (Caution: See instructions and Worksheet 2.9.)	12				
13 Self-employment tax from line 35a of Section B.	13				
14 Other taxes for each payment period.	14				
15 Total tax. Add lines 12, 13, and 14.	15				
16 Credits for each period.	16				
17 Subtract line 16 from line 15. (If less than zero, enter zero.)	17				
18 Applicable percentage.	18	22.5%	45%	67.5%	90%
19 Multiply line 17 by line 18.	19				
20 Add amounts on line 25a of all preceding columns.	20				
21 Annualized income installment. Subtract line 20 from line 19. (If less than zero, enter zero.)	21				
22 Divide line 14c of the Form 1040-ES Estimated Tax Worksheet by 4.	22				
23 Subtract line 25a of preceding column from line 24 of preceding column.	23				
24 Add lines 22 and 23.	24				
25a Enter the smaller of line 21 or line 24. (Caution: See instructions.)	25a				
b Total required payments for the period. Add lines 20 and 25a.	25b				
c Estimated tax payments made (line 25d of all previous columns) and tax withholding through the due date for the period.	25c				
d Estimated tax payment required by the next due date. Subtract line 25c from line 25b and enter the result (but not less than zero) here and on your payment-voucher.	25d				

Worksheet 2.10. (continued) **2002 Annualized Estimated Tax Worksheet**

Section B (For Figuring Your Annualized Estimated Self-Employment Tax) —Complete each column after end of period shown.		1/1/01 to 3/31/01	1/1/01 to 5/31/01	1/1/01 to 8/31/01	1/1/01 to 12/31/01
27	Net earnings from self-employment for the period 27				
28	Prorated social security tax limit. 28	\$21,225	\$35,375	\$56,600	\$84,900
29	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 29				
30	Subtract line 29 from line 28. If zero or less, enter -0- 30				
31	Annualization amounts 31	0.496	0.2976	0.186	0.124
32	Multiply line 31 by the smaller of line 27 or line 30 . 32				
33	Annualization amounts 33	0.116	0.0696	0.0435	0.029
34	Multiply line 27 by line 33. 34				
35a	Add lines 32 and 34. Enter the result here and on line 13 of Section A 35a				
b	Annualization amounts 35b	8	4.8	3	2
c	Deduction for one-half of self-employment tax. Divide line 35a by 35b. Enter the result here. Also use this result to figure your adjusted gross income on line 1 35c				

- Note.** If line 7 is more than line 8, go to line 18.
13. Subtract line 9 from line 8. If zero or less, enter 0 _____
 14. Multiply line 13 by 10% (.10) _____
 15. Enter the amount, if any, of your qualified 5-year gain. Do not enter more than the amount on line 13. _____
 16. Multiply line 15 by 2% (.02) _____
 17. Subtract line 16 from line 14. _____
- Note.** If line 13 minus line 15 is more than zero and equal to line 6, enter 0 on lines 20, 25, and 28, and go to line 29.
18. Enter the **smaller** of line 1 or line 6 _____
 19. Subtract line 13 from line 18 _____
 20. Multiply line 19 by 20% (.20) _____
- Note.** If line 4 is zero or blank, skip lines 21 through 25 and read the note above line 26.
21. Enter the **smaller** of line 2 or line 4 _____
 22. Add lines 2 and 11 _____
 23. Subtract line 1 from line 22. If zero or less, enter 0 _____
 24. Subtract line 23 from line 21. If zero or less, enter 0 _____
 25. Multiply line 24 by 25% (.25) _____
- Note.** If line 3 is zero or blank, go to line 29.
26. Add lines 11, 13, 19, and 24 _____
 27. Subtract line 26 from line 1. If zero or less, enter 0 _____
 28. Multiply line 27 by 28% (.28) _____
 29. Add lines 12, 17, 20, 25, and 28 _____
 30. Tax on the amount on line 1 from the 2002 Tax Rate Schedule _____
 31. **Tax.** Enter the **smaller** of line 29 or line 30 here and on line 12 of the 2002 Annualized Estimated Tax Worksheet _____

A **collectibles gain or loss** is any gain or loss from the sale or exchange of a work of art, rug, antique, metal, gem, stamp, coin, or alcoholic beverage or other collectible that is a capital asset and that was held more than one year.

Line 13. Enter your self-employment tax for each period from line 35a.

Line 14. Include all the taxes you will owe (other than income tax and self-employment tax) because of events that occurred during the period.

If you filed a 2001 Form 1040, these include:

- 1) Taxes on qualified plans, including IRAs, and other tax favored accounts,
- 2) Advance earned income credit,
- 3) Household employment taxes that are reported on your income tax return, and
- 4) Write-in amounts on line 58 of Form 1040.

Do not include tax on recapture of a federal mortgage subsidy, social security and Medicare tax on unreported tip income, and any uncollected social security, Medicare, or railroad retirement tax.

If you filed a 2001 Form 1040A, "other tax" is any advance earned income credit payments on line 35 of that form.

Line 16. Include all the credits (other than withholding credits) you can claim because of events that occurred during the period. If you are using your 2001 return as a guide and filed Form 1040, your 2001 credits included the credits on lines 61a, 63, and 65, and the credits that are included in the total on line 51. If you filed Form 1040A, your 2001 credits included the credits on lines 39a, and 40.

Line 26a. If line 24 is smaller than line 21 and you are not certain of the estimate of your 2002 tax, you can avoid a penalty by entering the amount from line 21 on line 26a.

Line 26c. Include all estimated tax payments credited to 2002 and federal income tax withholding through the payment due date for the period. Also include excess social security and excess railroad retirement for the period.

Your withholding is considered paid in four equal installments, one on the due date of each payment period. To figure the amount to include on line 26c for each period, multiply your total expected withholding for 2002 by:

- 1) 25% (.25) for the first period,
- 2) 50% (.50) for the second period,

- 3) 75% (.75) for the third period, or
- 4) 100% (1.00) for the fourth period.

You may choose to include your actual withholding through the due date for each period on line 26c. You can make this choice separately for the taxes withheld from your wages and all other withholding. For an explanation of what to include in withholding, see *Total Estimated Tax Payments* under *How To Figure Estimated Tax*, earlier.

Section B. If you had income from self-employment during any period, complete the worksheet column for that period to figure your annualized self-employment tax **before** you complete the worksheet column for that period in *Section A*.

Nonresident aliens. If you will file Form 1040NR and you **do not** receive wages as an employee subject to U.S. income tax withholding, the instructions for the worksheet are modified as follows.

- 1) Skip the first column.
- 2) On line 1, enter your income for the period that is effectively connected with a U.S. trade or business.
- 3) On line 17, increase your entry by the amount determined by multiplying your income for the period that is **not** effectively connected with a U.S. trade or business by the following:
 - a) 72% for the second column,
 - b) 45% for the third column, and
 - c) 30% for the fourth column. However, if you can use a treaty rate lower than 30%, use the percentages determined by multiplying your treaty rate by 2.4, 1.5, and 1, respectively, instead of the above percentages.

- 4) On line 22, enter one-half of the amount from line 16c of the Form 1040-ES(NR) *2002 Estimated Tax Worksheet* in the second column, and one-fourth in the third and fourth columns.
- 5) On lines 20 and 23, skip column (b).
- 6) On line 26c, if you do not use the actual withholding method, include one-third of your total expected withholding in the second column and two-thirds in the third and fourth columns.

See Publication 519 for more information.

Estimated Tax Payments Not Required

You do not have to make estimated tax payments if your withholding in each payment period is at least one-fourth of your required annual payment or at least your required annualized income installment for that period. You also do not have to make estimated tax payments if you will pay enough through withholding to keep the amount you will owe with your return under \$1,000.

How To Pay Estimated Tax

There are five ways to pay estimated tax.

- 1) **By crediting an overpayment** on your 2001 return to your 2002 estimated tax.
- 2) **By sending in your payment** with a payment-voucher from **Form 1040-ES**.
- 3) **By paying electronically** using the Electronic Federal Tax Payment System (EFTPS). For EFTPS information, call **1-800-945-8400** or **1-800-555-4477**.
- 4) **By electronic funds withdrawal (direct debit)** if you are filing Form 1040 or Form 1040A electronically.
- 5) **By credit card** using a pay-by-phone system.

In addition, if you are a beneficiary of an estate or trust, and the trustee elects to credit 2002 trust payments of estimated tax to you, you can treat the amount credited as paid by you on January 15, 2003.

Crediting an Overpayment

When you file your Form 1040 or Form 1040A for 2001 and you have an overpayment of tax, you can apply part or all of it to your estimated tax for 2002. On line 69 of Form 1040, or line 44 of Form 1040A, write the amount you want credited to your estimated tax rather than refunded. The amount you have credited should be taken into account when figuring your estimated tax payments.

You can use all the credited amount toward your first payment, or you can spread it out in

any way you choose among any or all of your payments.

If you ask that an overpayment be credited to your estimated tax for the next year, the payment is considered to have been made on the due date of the first estimated tax installment (April 15 for calendar year taxpayers). You cannot have any of that amount refunded to you after that due date until the close of that tax year. You also cannot use that overpayment in any other way after that date.

Example 2.8. When Kathleen finished filling out her 2001 tax return, she saw that she had overpaid her taxes by \$750. Kathleen knew she would owe additional tax in 2002. She credited \$600 of the overpayment to her 2002 estimated tax and had the remaining \$150 refunded to her.

In September, she amended her 2001 return by filing Form 1040X, *Amended U.S. Individual Income Tax Return*. It turned out that she owed \$250 more in tax than she had thought. This reduced her 2001 overpayment from \$750 to \$500. Because the \$750 had already been applied to her 2002 estimated tax or refunded to her, the IRS billed her for the additional \$250 she owed, plus penalties and interest. Kathleen could not use any of the \$600 she had credited to her 2002 estimated tax to pay this bill.

Using the Payment-Vouchers

Each payment of estimated tax must be accompanied by a payment-voucher from Form 1040-ES. If you made estimated tax payments last year, you should receive a copy of the 2002 Form 1040-ES in the mail. It will have payment-vouchers preprinted with your name, address, and social security number. Using the preprinted vouchers will speed processing, reduce the chance of error, and help save processing costs.

If you did not pay estimated tax last year, you will have to get a copy of Form 1040-ES from the IRS. See chapter 5. After you make your first payment, a Form 1040-ES package with the preprinted vouchers will be mailed to you. Follow the instructions in the package to make sure you use the vouchers correctly.

Use the window envelopes that came with your Form 1040-ES package. If you use your own envelopes, make sure you mail your payment-vouchers to the address shown in the Form 1040-ES instructions for the place where you live.



Do not use the address shown in the Form 1040 or Form 1040A instructions.

If you file a joint return and you are making joint estimated tax payments, please enter the names and social security numbers on the payment voucher in the same order as they will appear on the joint return.

Change of address. You must notify the IRS if you are making estimated tax payments and

you changed your address during the year. You must send a clear and concise written statement to the IRS Center where you filed your last return and provide all of the following:

- Your full name (and your spouse's full name),
- Your signature (and spouse's signature),
- Your old address (and spouse's old address if different),
- Your new address, and
- Your social security number (and spouse's social security number).

You can use **Form 8822, Change of Address**, for this purpose.

You can continue to use your old pre-printed payment-vouchers until the IRS sends you new ones. However, **do not** correct the address on the old voucher.

Payment by Electronic Funds Withdrawal

You can make a 2002 estimated tax payment when you electronically file your 2001 Form 1040 or Form 1040A by authorizing an electronic funds withdrawal (direct debit) from your checking or savings account. Whether or not you have a balance due on your electronically filed tax return, you can schedule one estimated tax payment with an effective date of April 15, 2002, June 17, 2002, or September 16, 2002. **Do not** send in a Form 1040-ES payment voucher when you schedule an estimated tax payment by electronic funds withdrawal.

Payment by Credit Card

You can use your American Express® Card, Discover® Card, or MasterCard® card to make estimated tax payments. Call toll free or access by Internet one of the service providers listed below and follow the instructions of the provider. Each provider will charge a convenience fee based on the amount you are paying. You can find out what the fee will be by calling the provider's toll-free automated customer service number or visiting the provider's Web Site shown below.

PhoneCharge, Inc.
1-888-ALLTAXX (1-888-255-8299)
1-877-851-9964 (Customer Service)
www.1888ALLTAXX.com

Official Payments Corporation
1-800-2PAY-TAX (1-800-272-9829)
1-877-754-4413 (Customer Service)
www.officialpayments.com

See the Form 1040-ES instructions for more information.

Illustrated Examples

The following examples show how to figure estimated tax payments under the regular installment method and under the annualized income installment method.

Example 2.9: Regular Installment Method

Early in 2002, Anne and Larry Jones figure their estimated tax payments for the year. They expect to receive the following income during 2002:

Larry's salary	\$29,200
Unemployment compensation	600
Anne's net profit from self-employment	38,500
Net rental income	2,671
Interest income	2,300
Dividends	3,745
Total	<u>\$77,016</u>

They also use the following expected items to figure their estimated tax:

Adjustment to income for IRA contributions	\$ 1,000
Itemized deductions	8,300
Deduction for exemptions (\$3,000 × 2)	6,000
2001 total tax	15,220
Withholding	5,795

The Joneses plan to file a joint return. They use the *2002 Estimated Tax Worksheet* included in Form 1040-ES to figure their estimated tax payments. Their filled-in worksheet follows this discussion.

Expected adjusted gross income. Anne can claim an income tax deduction for one-half of her self-employment tax as a business expense. So before the Joneses figure their expected adjusted gross income, they figure Anne's expected self-employment tax, as follows:

Filled-in Worksheet 2.2 for Anne Jones (Example 2.9)

1. Enter your expected income and profits subject to self-employment tax	\$38,500
2. Multiply the amount on line 1 by .9235	<u>\$35,555</u>
3. Multiply the amount on line 2 by .029	<u>\$1,031</u>
4. Social security tax maximum income	<u>\$84,900</u>
5. Enter your expected wages (if subject to social security tax)	-0-
6. Subtract line 5 from line 4	<u>\$84,900</u>
Note. If line 6 is zero or less, enter -0- on line 8 and skip to line 9.	
7. Enter the smaller of line 2 or line 6	<u>\$35,555</u>
8. Multiply the amount on line 7 by .124	<u>\$4,409</u>
9. Add line 3 and line 8. Enter the result here and on line 11 of your 2002 <i>Estimated Tax Worksheet</i>	<u>\$5,440</u>
10. Multiply the amount on line 9 by .50. This is your deduction for one-half of your self-employment tax	<u>\$2,720</u>

The Joneses enter \$35,555 on the dotted line and \$5,440 in the blank on line 11 of the worksheet. They subtract one-half of that amount, \$2,720, and their \$1,000 adjustment for IRA contributions from their \$77,016 total income to find their expected adjusted gross income, \$73,296. They enter that amount on line 1 of the worksheet.

Expected taxable income. The Joneses find their standard deduction, \$7,850, in the *2002*

Standard Deduction Tables. This is smaller than their expected itemized deductions, so they enter \$8,300 on line 2 of the worksheet. They subtract the amount on line 2 from the amount on line 1 and enter the result, \$64,996, on line 3. They enter their deduction for exemptions, \$6,000, on line 4. After subtracting this amount, their expected taxable income on line 5 is \$58,996.

Expected taxes and credits. The Joneses use the *2002 Tax Rate Schedule Y-1* at the end of this chapter to figure their expected income tax, and enter \$9,724 on line 6 of the worksheet. They do not expect to owe any other taxes that would be entered on lines 7 or 12, or have any credits that would be entered on lines 9 or 13b, so they leave those lines blank.

The Joneses' total expected tax on line 13c, after adding Anne's self-employment tax, is \$15,164.

Estimated tax. The Joneses multiply their total expected tax by 90% and enter \$13,648 on line 14a of the worksheet. They enter their 2001 tax on line 14b. Their required annual payment on line 14c is the smaller amount, \$13,648.

They enter Larry's expected withholding, \$5,795, on line 15 and subtract it from their required annual payment. Their estimated tax on line 16 is \$7,853.

Required estimated tax payment. The Joneses' first estimated tax payment is due April 15, 2002. They enter one-fourth of their estimated tax, \$1,964, on line 17 of the worksheet and on their Form 1040-ES payment-voucher due April 15. They mail the voucher with their payment to the address shown for their area in the Form 1040-ES instructions, and record the payment on the *Record of Estimated Tax Payments* in the instructions.

If their estimated tax does not change during the year, the Joneses also will pay \$1,963 estimated tax by June 17 and September 16, 2002, and January 15, 2003.

Example 2.10: Annualized Income Installment Method

The facts are the same as in *Example 2.9*, except that the Joneses do not expect to receive their income evenly throughout the year. Anne expects to receive the largest portion of her self-employment income during the last few months of the year, and the Joneses' rental income is from a vacation home rented only in the summer months.

After completing their *2002 Estimated Tax Worksheet*, the Joneses decide to use the annualized income installment method to see if they can pay less than \$1,964 estimated tax for one or more payment periods. They complete the *2002 Annualized Estimated Tax Worksheet (Worksheet 2.10)* in this chapter. Their filled-in worksheet follows their filled-in *2002 Estimated Tax Worksheet* at the end of this example.

First Period

On April 1, 2002, the Joneses complete the first column of the worksheet for the period January 1 through March 31. They had the following income for the period:

Larry's salary	\$ 6,900
Unemployment compensation	600
Anne's net profit from self-employment	3,000
Net rental income	-0-
Interest income	500
Dividends	462
Total	<u>\$11,462</u>

They also take into account the following items for the period:

Adjustment to income for IRA contributions	\$ 150
Itemized deductions	1,200
Withholding	1,350

Annualized adjusted gross income. Before the Joneses figure their adjusted gross income for the period, they first figure Anne's self-employment tax in Section B, and then her adjustment to income for self-employment tax.

On line 27 of Section B, they enter \$2,771, which is Anne's net profit from self-employment for the period, \$3,000, multiplied by .9235. The prorated social security tax limit is preprinted on line 28. She has no social security wages, so they enter zero on line 29, and \$21,225 on line 30. Anne's annualized social security tax on line 32 is \$1,374, $(\$2,771 \times .496)$. Her annualized medicare tax on line 34 is \$321 $(\$2,771 \times .116)$. Her total annualized self-employment tax on line 35a is \$1,695. They enter that amount on line 13 of Section A.

The Joneses figure their adjustment to income for Anne's self-employment tax on lines 35b and 35c. They figure the amount to be \$212 $(\$1,695 \div 8)$. They subtract that amount and their \$150 IRA contributions from their \$11,462 total income and enter their adjusted gross income for the period, \$11,100, on line 1 of Section A. They multiply that amount by 4 and enter their annualized adjusted gross income, \$44,400, on line 3.

Annualized taxable income. The Joneses figure their annualized itemized deductions $(\$1,200 \times 4)$ on lines 4 through 6 of Section A. Because the result is smaller than their standard deduction, they enter their \$7,850 standard deduction on line 8. After subtracting that amount and their \$6,000 deduction for exemptions, the Joneses' annualized taxable income on line 11 is \$30,550.

Annualized taxes and credits. The Joneses use the *2002 Tax Rate Schedule Y-1* at the end of this chapter to figure their annualized income tax, \$3,983, on line 12 of Section A.

The Joneses have no other taxes or credits for the period that would be entered on lines 14 or 16, so they leave those lines blank and enter \$5,678 $(\$3,983 + \$1,695)$ on lines 15 and 17. This is their annualized total tax.

Required estimated tax payment. The Joneses' annualized income installment on line 21 of Section A is \$1,278 $(\$5,678 \times 22.5\%)$. On lines 22 and 24 they enter \$3,412, one-fourth of their \$13,648 required annual payment under the regular installment method of figuring estimated tax payments (from line 14c of the *2002 Estimated Tax Worksheet*). Because \$1,278 is smaller, they enter that amount on lines 25a and 25b.

Larry's total expected withholding for the year is \$5,795. The Joneses can treat one-fourth of that amount, \$1,449, as paid on April 16, or they can choose to use Larry's actual

withholding for the period, \$1,350. The Joneses enter \$1,449 on line 25c.

On line 25d, the Joneses' required estimated tax payment for the period under the annualized income installment method is \$0 (\$1,278 - \$1,449). They do not have a Form 1040-ES payment-voucher due April 15, 2002.

Second, Third, and Fourth Periods

After the end of each remaining payment period, the Joneses complete the column of the worksheet for that period (from the beginning of the year through the end of that payment period) in the same way they did for the first period. They had the following income for each period:

	Second Jan. 1- May 31	Third Jan. 1- Aug. 31	Fourth Jan. 1- Dec. 31
Larry's salary	\$11,800	\$19,200	\$29,200

Unemployment compensation	600	600	600
Anne's net profit from self-employment	6,000	15,850	38,500
Net rental income	668	2,671	2,671
Interest income	850	1,450	2,300
Dividends	674	1,708	3,745
Total	\$20,592	\$41,479	\$77,016

They also take into account the following items for each period:

	Second Jan. 1- May 31	Third Jan. 1- Aug. 31	Fourth Jan. 1- Dec. 31
Adjustment to income for IRA contributions	\$ 250	\$ 400	\$1,000
Itemized deductions	2,700	6,400	8,300

For the second period, as for the first, the annualized income installment method allows the Joneses to pay less than their required payment under the regular installment method of figuring estimated tax payments. They make up the difference in the third and fourth periods when their income is higher.

Because the Joneses are using the annualized income installment method, they will file Form 2210 with their tax return for 2002.

2002 Estimated Tax Worksheet (keep for your records)

1 Enter amount of adjusted gross income you expect in 2002 (see instructions)	1	73,296	
2 • If you plan to itemize deductions, enter the estimated total of your itemized deductions. Caution: If line 1 above is over \$137,300 (\$68,650 if married filing separately), your deduction may be reduced. See Pub. 505 for details.	2	8,300	
• If you do not plan to itemize deductions, see Standard Deduction on page 2 and enter your standard deduction here.			
3 Subtract line 2 from line 1	3	64,996	
4 Exemptions. Multiply \$3,000 by the number of personal exemptions. If you can be claimed as a dependent on another person's 2002 return, your personal exemption is not allowed. Caution: See Pub. 505 to figure the amount to enter if line 1 above is over: \$206,000 if married filing jointly or qualifying widow(er); \$171,650 if head of household; \$137,300 if single; or \$103,000 if married filing separately	4	6,000	
5 Subtract line 4 from line 3	5	58,996	
6 Tax. Figure your tax on the amount on line 5 by using the 2002 Tax Rate Schedules on page 2. Caution: If you have a net capital gain, see Pub. 505 to figure the tax	6	9,724	
7 Alternative minimum tax from Form 6251	7		
8 Add lines 6 and 7. Also include any tax from Forms 4972 and 8814 and any recapture of the education credits (see instructions)	8	9,724	
9 Credits (see instructions). Do not include any income tax withholding on this line.	9		
10 Subtract line 9 from line 8. If zero or less, enter -0-.	10	9,724	
11 Self-employment tax (see instructions). Estimate of 2002 net earnings from self-employment \$ <u>35,555</u> ; if \$84,900 or less , multiply the amount by 15.3%; if more than \$84,900 , multiply the amount by 2.9%, add \$10,527.60 to the result, and enter the total. Caution: If you also have wages subject to social security tax, see Pub. 505 to figure the amount to enter.	11	5,440	
12 Other taxes (see instructions)	12		
13a Add lines 10 through 12	13a	15,164	
b Earned income credit, additional child tax credit, and credit from Form 4136	13b		
c Total 2002 estimated tax. Subtract line 13b from line 13a. If zero or less, enter -0- ▶	13c	15,164	
14a Multiply line 13c by 90% (66⅔% for farmers and fishermen).	14a	13,648	
b Enter the tax shown on your 2001 tax return (112% of that amount if you are not a farmer or fisherman and the adjusted gross income shown on line 34 of that return is more than \$150,000 or, if married filing separately for 2002, more than \$75,000)	14b	15,220	
c Required annual payment to avoid a penalty. Enter the smaller of line 14a or 14b . . . ▶	14c	13,648	
Caution: Generally, if you do not prepay (through income tax withholding and estimated tax payments) at least the amount on line 14c, you may owe a penalty for not paying enough estimated tax. To avoid a penalty, make sure your estimate on line 13c 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 may pay the amount shown on line 13c. For details, see Pub. 505.			
15 Income tax withheld and estimated to be withheld during 2002 (including income tax withholding on pensions, annuities, certain deferred income, etc.)	15	5,795	
16 Subtract line 15 from line 14c. (Note: If zero or less or line 13c minus line 15 is less than \$1,000, stop here. You are not required to make estimated tax payments.)	16	7,853	
17 If the first payment you are required to make is due April 15, 2002, enter ¼ of line 16 (minus any 2001 overpayment that you are applying to this installment) here, and on your payment voucher(s) if you are paying by check or money order. (Note: Household employers, see instructions.)	17	1,964	

Filled-in 2002 Annualized Estimated Tax Worksheet for Example 2.10

Section A (For Figuring Your Annualized Estimated Tax Payments) —Complete each column after end of period shown.						
Estates and trusts: Use the following ending dates in each column—2/28, 4/30, 7/31, 11/30.		1/1/01 to 3/31/01	1/1/01 to 5/31/01	1/1/01 to 8/31/01	1/1/01 to 12/31/01	
1	Adjusted gross income for each period. (Caution: See instructions.) Self-employed: Complete Section B first.	1	11,100	19,918	39,959	73,296
2	Annualization amounts. (Estates and trusts, do not use the amounts shown to right. Instead, use 6, 3, 1.71429, and 1.09091.)	2	4	2.4	1.5	1
3	Annualized income. Multiply line 1 by line 2.	3	44,400	47,803	59,939	73,296
4	Itemized deductions for period. If you do not expect to itemize, skip to line 7 and enter zero. (Estates and trusts, enter -0-, skip to line 9, and enter the amount from line 3 on line 9.)	4	1,200	2,700	6,400	8,300
5	Annualization amounts.	5	4	2.4	1.5	1
6	Multiply line 4 by line 5. (Caution: See instructions and Worksheet 2.7.)	6	4,800	6,480	9,600	8,300
7	Standard deduction from 2002 tables.	7	7,850	7,850	7,850	7,850
8	Enter the larger of line 6 or line 7.	8	7,850	7,850	9,600	8,300
9	Subtract line 8 from line 3.	9	36,550	39,953	50,339	64,996
10	Multiply \$3,000 by your total expected exemptions. (Caution: See instructions and Worksheet 2.8.)	10	6,000	6,000	6,000	6,000
11	Subtract line 10 from line 9.	11	30,550	33,953	44,339	58,996
12	Tax on the amount on line 11 from the 2002 Tax Rate Schedules. (Caution: See instructions and Worksheet 2.9.)	12	3,983	4,493	6,051	9,725
13	Self-employment tax from line 35a of Section B.	13	1,695	2,035	3,359	5,440
14	Other taxes for each payment period.	14				
15	Add lines 12, 13, and 14.	15	5,678	6,528	9,410	15,165
16	Credits for each period.	16				
17	Total tax. Subtract line 16 from line 15. (If less than zero, enter zero.)	17	5,678	6,528	9,410	15,165
18	Applicable percentage.	18	22.5%	45%	67.5%	90%
19	Multiply line 17 by line 18.	19	1,278	2,938	6,352	13,649
20	Add amounts on line 25a of all preceding columns.	20		1,278	2,938	6,352
21	Annualized income installment. Subtract line 20 from line 19. (If less than zero, enter zero.)	21	1,278	1,660	3,414	7,297
22	Divide line 14c of the Form 1040-ES Estimated Tax Worksheet by 4.	22	3,412	3,412	3,412	3,412
23	Subtract line 25a of preceding column from line 24 of preceding column.	23		2,134	3,886	3,884
24	Add lines 22 and 23.	24	3,412	5,546	7,298	7,296
25a	Enter the smaller of line 21 or line 24. (Caution: See instructions.)	25a	1,278	1,660	3,414	7,296
b	Total required payments for the period. Add lines 20 and 25a.	25b	1,278	2,938	6,352	13,648
c	Estimated tax payments made (line 25d of all previous columns) and tax withholding through the due date for the period.	25c	1,449	2,898	4,386	7,801
d	Estimated tax payment required by the next due date. Subtract line 25c from line 25b and enter the result (but not less than zero) here and on your payment-voucher.	25d	-0-	40	1,966	5,847

Filled-in 2002 Annualized Estimated Tax Worksheet for Example 2.10 (continued)

Section B (For Figuring Your Annualized Estimated Self-Employment Tax) —Complete each column after end of period shown.						
		1/1/02 to 3/31/02	1/1/02 to 5/31/02	1/1/02 to 8/31/02	1/1/02 to 12/31/02	
27	Net earnings from self-employment for the period	27	2,771	5,541	14,637	35,555
28	Prorated social security tax limit.	28	\$21,225	\$35,375	\$56,600	\$84,900
29	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	29	0	0	0	0
30	Subtract line 29 from line 28. If zero or less, enter -0-	30	21,225	35,375	56,600	84,900
31	Annualization amounts	31	0.496	0.2976	0.186	0.124
32	Multiply line 31 by the smaller of line 27 or line 30	32	1,374	1,649	2,722	4,409
33	Annualization amounts	33	0.116	0.0696	0.0435	0.029
34	Multiply line 27 by line 33.	34	321	386	637	1,031
35a	Add lines 32 and 34. Enter the result here and on line 13 of Section A	35a	1,695	2,035	3,359	5,440
b	Annualization amounts	35b	8	4.8	3	2
c	Deduction for one-half of self-employment tax. Divide line 35a by 35b. Enter the result here. Also use this result to figure your adjusted gross income on line 1.	35c	212	424	1,120	2,720

2002 Tax Rate Schedules

Caution: Do not use these Tax Rate Schedules to figure your 2001 taxes. Use only to figure your 2002 estimated taxes.

Single—Schedule X

If line 5 is:		The tax is:	of the amount over—
Over—	But not over—		
\$0	\$6,000	10%	\$0
6,000	27,950	\$600.00 + 15%	6,000
27,950	67,700	3,892.50 + 27%	27,950
67,700	141,250	14,625.00 + 30%	67,700
141,250	307,050	36,690.00 + 35%	141,250
307,050		94,720.00 + 38.6%	307,050

Head of household—Schedule Z

If line 5 is:		The tax is:	of the amount over—
Over—	But not over—		
\$0	\$10,000	10%	\$0
10,000	37,450	\$1,000.00 + 15%	10,000
37,450	96,700	5,117.50 + 27%	37,450
96,700	156,600	21,115.00 + 30%	96,700
156,600	307,050	39,085.00 + 35%	156,600
307,050		91,742.50 + 38.6%	307,050

Married filing jointly or Qualifying widow(er)—Schedule Y-1

If line 5 is:		The tax is:	of the amount over—
Over—	But not over—		
\$0	\$12,000	10%	\$0
12,000	46,700	\$1,200.00 + 15%	12,000
46,700	112,850	6,405.00 + 27%	46,700
112,850	171,950	24,265.50 + 30%	112,850
171,950	307,050	41,995.50 + 35%	171,950
307,050		89,280.50 + 38.6%	307,050

Married filing separately—Schedule Y-2

If line 5 is:		The tax is:	of the amount over—
Over—	But not over—		
\$0	\$6,000	10%	\$0
6,000	23,350	\$600.00 + 15%	6,000
23,350	56,425	3,202.50 + 27%	23,350
56,425	85,975	12,132.75 + 30%	56,425
85,975	153,525	20,997.75 + 35%	85,975
153,525		44,640.25 + 38.6%	153,525

2002 Standard Deduction Tables

Caution: If you are married filing a separate return and your spouse itemizes deductions, or if you are a dual-status alien, you cannot take the standard deduction even if you were 65 or older or blind.

Table 1. Standard Deduction Chart for Most People*

If Your Filing Status is:	Your Standard Deduction is:
Single	\$4,700
Married filing joint return or Qualifying widow(er) with dependent child	7,850
Married filing separate return	3,925
Head of household	6,900

*DO NOT use this chart if you are 65 or older or blind, OR if someone can claim you (or your spouse if married filing jointly) as a dependent.

Table 2. Standard Deduction Chart for People Age 65 or Older or Blind*

Check the correct number of boxes below. Then go to the chart.
 You 65 or older Blind
 Your spouse, if claiming spouse's exemption 65 or older Blind
Total number of boxes you checked

If Your Filing Status is:	And the Number in the Box Above is:	Your Standard Deduction is:
Single	1	\$5,850
	2	7,000
Married filing joint return or Qualifying widow(er) with dependent child	1	8,750
	2	9,650
	3	10,550
	4	11,450
Married filing separate return	1	4,825
	2	5,725
	3	6,625
	4	7,525
Head of household	1	8,050
	2	9,200

*If someone can claim you (or your spouse if married filing jointly) as a dependent, use Table 3, instead.

Table 3. Standard Deduction Worksheet for Dependents*

If you are 65 or older or blind, check the correct number of boxes below. Then go to the worksheet.
 You 65 or older Blind
 Your spouse, if claiming spouse's exemption 65 or older Blind
Total number of boxes you checked

1. Enter your earned income (defined below) plus \$250.	1. _____
2. Minimum amount	2. <u> \$750 </u>
3. Compare the amounts on lines 1 and 2. Enter the larger of the two amounts here	3. _____
4. Enter on line 4 the amount shown below for your filing status. <ul style="list-style-type: none"> • Single, enter \$4,700 • Married filing separate return, enter \$3,925 • Married filing jointly or Qualifying widow(er) with dependent child, enter \$7,850 • Head of household, enter \$6,900 	4. _____
5. Standard deduction. a. Compare the amounts on lines 3 and 4. Enter the smaller of the two amounts here. If under 65 and not blind, stop here. This is your standard deduction. Otherwise, go on to line 5b. b. If 65 or older or blind, multiply \$1,150 (\$900 if married or qualifying widow(er) with dependent child) by the number in the box above. Enter the result c. Add lines 5a and 5b. This is your standard deduction for 2002.	5a. _____ 5b. _____ 5c. _____
Earned income includes wages, salaries, tips, professional fees, and other compensation received for personal services you performed. It also includes any amount received as a scholarship that you must include in your income.	

*Use this worksheet ONLY if someone can claim you (or your spouse if married filing jointly) as a dependent.

3.

Credit for Withholding and Estimated Tax for 2001

Important Change

Excess social security or railroad retirement tax withholding. You can claim a credit for excess social security or tier 1 railroad retirement tax withholding for 2001 only if your total wages from two or more employers were more than \$80,400.

Introduction

When you file your 2001 income tax return, take credit for all the income tax and excess social security or railroad retirement tax withheld from your salary, wages, pensions, etc. Also, take credit for the estimated tax you paid for 2001. These credits are subtracted from your tax. You should file a return and claim these credits, even if you do not owe tax.

If the total of your withholding and your estimated tax payments for any payment period is less than the amount you needed to pay by the due date for that period, you may be charged a penalty, even if the total of these credits is more than your tax for the year.

Topics

This chapter discusses:

- How to take credit for withholding,
- How to take credit for estimated taxes you paid, and
- How to take credit for excess social security or railroad retirement tax withholding.

Withholding

If you had income tax withheld during 2001, you should receive a statement by January 31, 2002, showing your income and the tax withheld. Depending on the source of your income, you will receive:

- Form W-2, *Wage and Tax Statement*,
- Form W-2G, *Certain Gambling Winnings*, or
- A form in the 1099 series.

Forms W-2 and W-2G. You file Form W-2 with your income tax return. File Form W-2G with your return if it shows any federal income tax withheld from your winnings.

You should get at least two copies of each form you receive. Attach one copy to the front of your federal income tax return. Keep one copy for your records. You should also receive copies to file with your state and local returns.

Form W-2

Your employer should give you a Form W-2 for 2001 by January 31, 2002. You should receive a separate Form W-2 from each employer you worked for.

If you stop working before the end of the year, your employer can give you your Form W-2 at any time after you leave your job. However, your employer must give it to you by January 31 of the following year (or the next day that is not a Saturday, Sunday, or holiday if January 31 is a Saturday, Sunday, or holiday).

If you ask for the form, your employer must give it to you within 30 days after receiving your written request or within 30 days after your final wage payment, whichever is later.

If you have not received your Form W-2 by February 1, 2002, you should ask your employer for it. If you do not receive it by February 15, call the IRS. The number is listed in the Form 1040, Form 1040A, and Form 1040EZ instructions. You will be asked for the following information:

- 1) Your employer's name, address, and telephone number, and, if known, your employer's identification number.
- 2) Your address, social security number, and daytime telephone number.
- 3) The dates of employment.
- 4) An estimate of your total wages and federal income tax withheld.

Form W-2 shows your total pay and other compensation and the income tax, social security tax, and Medicare tax that was withheld during the year. Include the federal income tax withheld (as shown on Form W-2) on:

- Line 59, if you file Form 1040,
- Line 37, if you file Form 1040A, or
- Line 8, if you file Form 1040EZ.

Form W-2 is also used to report any taxable sick pay you received and any income tax withheld from your sick pay.

Form W-2G

If you had gambling winnings in 2001, the payer may have withheld 27½% or 28% as income tax. If tax was withheld, the payer will give you a Form W-2G showing the amount you won and the amount of tax withheld.

Report the amounts you won on line 21 of Form 1040. Take credit for the tax withheld on line 59 of Form 1040. If you had gambling winnings, you must use Form 1040; you cannot use Form 1040A or Form 1040EZ.

Gambling losses can be deducted on Schedule A (Form 1040) as a miscellaneous itemized deduction. However, you cannot deduct more

than the gambling winnings you report on line 21.

The 1099 Series

Most forms in the 1099 series are not filed with your return. You should receive these forms by February 1, 2002. Keep these forms for your records. There are several different forms in this series, including:

- Form 1099-B, *Proceeds From Broker and Barter Exchange Transactions*,
- Form 1099-DIV, *Dividends and Distributions*,
- Form 1099-G, *Certain Government and Qualified State Tuition Program Payments*,
- Form 1099-INT, *Interest Income*,
- Form 1099-MISC, *Miscellaneous Income*,
- Form 1099-OID, *Original Issue Discount*,
- Form 1099-R, *Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*,
- Form SSA-1099, *Social Security Benefit Statement*, and
- Form RRB-1099, *Payments by the Railroad Retirement Board*.

If you received the types of income reported on some forms in the 1099 series, you may not be able to use Form 1040A or Form 1040EZ. See the instructions to these forms for details.

Form 1099-R. Attach Form 1099-R to your return if federal income tax withholding is shown in box 4. Include the amount withheld in the total on line 59 of Form 1040, or on line 37 of Form 1040A. You cannot use Form 1040EZ if you received payments reported on Form 1099-R.

Backup withholding. If you were subject to backup withholding on income you received during 2001, include the amount withheld, as shown on your Form 1099, in the total on line 59 of Form 1040, or line 37 of Form 1040A.

Form Not Correct

If you receive a form with incorrect information on it, you should ask the payer for a corrected form. Call the telephone number or write to the address given for the payer on the form. The corrected Form W-2G or Form 1099 you receive will be marked "Corrected." A special form, Form W-2c, *Corrected Wage and Tax Statement*, is used to correct a Form W-2.

Form Received After Filing

If you file your return and you later receive a form for income that you did not include on your return, you should report the income and take credit for any income tax withheld by filing Form 1040X.

Separate Returns

If you are married but file a separate return, you can take credit only for the tax withheld from your own income. Do not include any amount

withheld from your spouse's income. However, different rules may apply if you live in a community property state.

Community property states. The following are community property states.

- Arizona,
- California,
- Idaho,
- Louisiana,
- Nevada,
- New Mexico,
- Texas,
- Washington, and
- Wisconsin.

If you live in a community property state and file a separate return, you and your spouse must each report half of all community income in addition to your own separate income. Each of you takes credit for half of all taxes withheld on the community income. If you were divorced during the year, each of you generally must report half the community income and can take credit for half the withholding on that community income for the period before the divorce.

For more information on these rules, and some exceptions, see Publication 555, *Community Property*.

Fiscal Years

If you file your tax return on the basis of a fiscal year (a 12-month period ending on the last day of any month except December), you must follow special rules, described below, to determine your credit for federal income tax withholding.

Normal withholding. During your fiscal year, one calendar year will end and another will begin. You can claim credit on your tax return only for the tax withheld during the calendar year ending in your fiscal year. You cannot claim credit for any of the tax withheld during the calendar year beginning in your fiscal year. You will be able to claim credit for that withholding on your return for next year.

The Form W-2 or 1099-R you receive for the calendar year that ends during your fiscal year will show the tax withheld and the income you received during that calendar year.

Although you take credit for all the withheld tax shown on the form, report only the part of the income shown on the form that you received during your fiscal year. Add to that the income you received during the rest of your fiscal year.

Example 3.1. Miles Hanson files his return for a fiscal year ending June 30. In January 2002, he received a Form W-2 that showed that his wages for 2001 were \$15,600 and that his income tax withheld was \$1,409.40. His records show that he had received \$7,500 of the wages by June 30, 2001, and \$8,100 from July 1 through December 31, 2001.

On his return for the fiscal year ending June 30, 2002, Miles will report the \$8,100 he was paid in July through December of 2001, plus whatever he was paid during the rest of the fiscal year — January 1, 2002, to June 30, 2002. However, he takes credit for all \$1,409.40 that

was withheld during 2001. On his return for the fiscal year ending June 30, 2002, he cannot take credit any tax withheld during 2002.

On his return for the fiscal year ending June 30, 2003, Miles takes credit for any income tax withheld in 2002.

Backup withholding. If income tax has been withheld under the backup withholding rule, take credit for it on your tax return for the fiscal year in which you received the payment.

Example 3.2. Emily Smith's records show that she received income in February 2002 from which \$50 was withheld under the backup withholding rule. On her tax return for the fiscal year ending June 30, 2002, Emily takes credit for withheld income tax of \$50.

Estimated Tax

Take credit for all your estimated tax payments for 2001 on line 60 of Form 1040 or line 38 of Form 1040A. Include any overpayment from 2000 that you had credited to your 2001 estimated tax. You must use Form 1040 or Form 1040A if you paid estimated tax. You cannot use Form 1040EZ.

If you were a beneficiary of an estate or trust, include on line 60, Form 1040, any trust payments of estimated tax credited to you (from line 14a of Schedule K-1 (Form 1041), *Beneficiary's Share of Income, Deductions, Credits, Etc.*). On the dotted line next to line 36 of Schedule E (Form 1040) write "ES payment claimed" and the amount. Do not include this amount in the total on line 36. The payment is treated as being made by you on January 15, 2002.

Name changed. If you changed your name, and you made estimated tax payments using your old name, attach a brief statement to the front of your tax return indicating:

- When you made the payments,
- The amount of each payment,
- Which IRS address you sent the payments to,
- Your name when you made the payments, and
- Your social security number.

The statement should cover payments you made jointly with your spouse as well as any you made separately.

Separate Returns

If you and your spouse made separate estimated tax payments for 2001 and you file separate returns, you can take credit only for your own payments.

If you made joint estimated tax payments, you must decide how to divide the payments between your returns. One of you can claim all of the estimated tax paid and the other none, or you can divide it in any other way you agree on. If you cannot agree, you must divide the payments in proportion to each spouse's individual tax as shown on your separate returns for 2000.

Example 3.3. James and Evelyn Brown made joint estimated tax payments for 2001 totaling \$3,000. They file separate Forms 1040. James' tax is \$4,000 and Evelyn's is \$1,000. If they do not agree on how to divide the \$3,000, they must divide it proportionately between their returns. Because James' tax (\$4,000) is 80% of the total tax (\$5,000) due for both of them, his share of the estimated tax is \$2,400 (80% of \$3,000). The balance, \$600 (20% of \$3,000), is Evelyn's share.

Divorced Taxpayers

If you made joint estimated tax payments for 2001, and you were divorced during the year, either you or your former spouse can claim all of the joint payments, or you each can claim part of them. If you cannot agree on how to divide the payments, you must divide them in proportion to each spouse's individual tax as shown on your separate returns for 2001. See *Example 3.3*, earlier.

If you claim any of the joint payments on your tax return, enter your former spouse's social security number (SSN) in the space provided on the front of Form 1040 or Form 1040A. If you divorced and remarried in 2001, enter your present spouse's SSN in that space and write your former spouse's SSN, followed by "DIV," to the left of line 60, Form 1040, or line 38, Form 1040A.

Excess Social Security or Railroad Retirement Tax Withholding

Most employers must withhold social security tax from your wages. The federal government and state and local governments in some cases do not have to withhold social security tax from their employees' wages. If you work for a railroad employer, that employer must withhold tier 1 railroad retirement (RRTA) tax and tier 2 RRTA tax.

Two or more employers. If you worked for two or more employers in 2001, too much social security tax or RRTA tax may have been withheld from your pay. You may be able to claim the excess as a credit against your income tax when you file your return. *Table 3.1* shows the maximum amount that should have been withheld for any of these taxes for 2001. Figure the excess withholding on the appropriate worksheet following *Table 3.1*. Use *Worksheet 1* to figure excess social security tax; use *Worksheet 2* to figure excess tier 1 RRTA tax; use *Worksheet 3* to figure excess tier 2 RRTA tax.

Note: If you worked for both a railroad employer and a nonrailroad employer, use *Worksheet 2* to figure excess social security and tier 1 RRTA tax.

Joint returns. If you are filing a joint return, you cannot add any social security or RRTA tax withheld from your spouse's income to the amount withheld from your income. You must figure the excess separately for both you and your spouse to determine if either of you has excess withholding.

Table 3.1

Type of Tax	Maximum wages subject to tax	Tax rate	Maximum tax to be withheld
Social security	\$80,400	6.2%	\$4,984.80
Railroad employees			
Tier 1 railroad retirement (RRTA)	\$80,400	6.2%	\$4,984.80
Tier 2 RRTA	\$59,700	4.9%	\$2,925.30

Note. All wages are subject to Medicare tax withholding.

Employer's error. If any one employer withheld too much social security or RRTA tax, you cannot claim the excess as a credit against your income tax or file a claim for refund of the excess. Your employer must adjust this for you.

Worksheet for Nonrailroad Employees

Unless you worked for a railroad during 2001, figure the excess on the following worksheet.

Worksheet 3.1

- Add all social security tax withheld (but not more than \$4,984.80 for each employer). This tax should be shown in box 4 of your Forms W-2. Enter the total here _____
- Enter any uncollected social security tax on tips or group-term life insurance included in the total on Form 1040, line 58 _____
- Add lines 1 and 2. If \$4,984.80 or less, stop here. You cannot claim the credit. _____
- Social security limit 4,984.80
- Excess. Subtract line 4 from line 3. _____

Where to claim credit for excess social security withholding. If you file Form 1040A, include the excess in the total on line 41. Write "Excess SST" and show the amount of the credit in the space to the left of the line. If you file Form 1040, enter the excess on line 62.

You cannot claim excess SST withholding on Form 1040EZ.

Example 3.4. In 2001, Tom Martin earned \$48,000 working for the Shoe Company and

\$36,200 working for Leather Design. Shoe Company withheld \$2,976 for social security tax. Leather Design withheld \$2,244.40 for social security tax. Because he worked for two employers and earned more than \$80,400, he had too much social security tax withheld. Tom figures his credit of \$235.60 as follows:

Filled-in Worksheet 3.1 for Tom Martin (Example 3.4)

- Add all social security tax withheld (but not more than \$4,984.80 for each employer). This tax should be shown in box 4 of your Forms W-2. Enter the total here \$5,220.40
- Enter any uncollected social security tax on tips or group-term life insurance included in the total on Form 1040, line 58 0
- Add lines 1 and 2. If \$4,984.80 or less, stop here. You cannot claim the credit. 5,220.40
- Social security tax limit 4,984.80
- Excess. Subtract line 4 from line 3. \$235.60

Worksheets for Railroad Employees



Publication 17 contains a worksheet on page 259 under How to figure the credit if you worked for a railroad. Do not use that worksheet if you are claiming a refund of excess tier 2 tax.

If you worked for a railroad during 2001, figure your excess withholding on the following worksheets.

Worksheet 3.2

- Add all social security and tier 1 RRTA tax withheld (but not more than \$4,984.80 for each employer). Social security tax should be shown in box 4 and tier 1 RRTA should be shown in box 14 of your Forms W-2. Enter the total here _____
- Enter any uncollected social security and tier 1 RRTA tax on tips or group-term life insurance included in the total on Form 1040, line 58 _____

- Add lines 1 and 2. If \$4,984.80 or less, stop here. You cannot claim the credit. _____
- Social security and tier 1 RRTA tax limit 4,984.80
- Excess. Subtract line 4 from line 3. _____

Where to claim credit for excess tier 1 RRTA withholding. If you file Form 1040A, include the excess in the total on line 41. Write "Excess SST" and show the amount of the credit in the space to the left of the line. If you file Form 1040, enter the excess on line 62.

You cannot claim excess tier 1 RRTA withholding on Form 1040EZ.

Worksheet 3.3

- Add all tier 2 RRTA tax withheld (but not more than \$2,925.30 for each employer). Box 14 of your Forms W-2 should show tier 2 RRTA tax. Enter the total here _____
- Enter any uncollected tier 2 RRTA tax on tips or group-term life insurance included in the total on Form 1040, line 58 _____
- Add lines 2 and 3. If \$2,925.30 or less, stop here. You cannot claim the credit. _____
- Tier 2 RRTA tax limit 2,925.30
- Excess. Subtract line 4 from line 3. _____

How to claim refund of excess tier 2 RRTA . To claim a refund of tier 2 tax, use Form 843, *Claim for Refund and Request for Abatement*. Be sure to attach a copy of all of your W-2 forms.

4.

Underpayment Penalty for 2001

Important Change

Penalty rate. The penalty for underpayment of 2001 estimated tax is figured at an annual rate of 8% for the number of days the underpayment remained unpaid from April 16, 2001, through June 30, 2001; 7% from July 1, 2001, through December 31, 2001; and 6% from January 1, 2002, through April 15, 2002.

Important Reminders

Household employment taxes. When figuring the penalty for failure to pay estimated income tax, you generally must include with your estimated taxes any household employment taxes that you may have to pay.

Failure to pay estimated tax. You will not be liable for the penalty for failure to pay estimated income tax if the total tax shown on your return minus the amount you paid through withholding (including excess social security and railroad retirement tax withholding) is less than \$1,000.

Exception to use of prior year's tax. Certain taxpayers (other than farmers and fishermen) must use 110% of their 2000 tax to figure any 2001 underpayment penalty. See *Higher income taxpayers* under *General Rule*, later.

Introduction

If you did not pay enough tax either through withholding or by making estimated tax payments, you will have an underpayment of estimated tax and you may have to pay a penalty.

Having completed copies of your latest federal income tax returns may help you through this chapter.

No penalty. Generally, you will *not* have to pay a penalty for 2001 if any of the following situations applies.

- The total of your withholding and estimated tax payments was at least as much as your 2000 tax (or 110% of your 2000 tax if your adjusted gross income was more than \$150,000 — \$75,000 if your 2001 filing status is married filing separately), and you paid all required estimated tax payments on time.
- The tax balance due on your return is no more than 10% of your total 2001 tax, and

you paid all required estimated tax payments on time.

- Your total 2001 tax (defined later) minus your withholding is less than \$1,000.
- You did not have a tax liability for 2000.
- You did not have any withholding taxes and your current year tax less any household employment taxes is less than \$1,000.

Special rules apply if you are a farmer or fisherman.

IRS can figure the penalty for you. If you think you owe the penalty but you do not want to figure it yourself when you file your tax return, you may not have to. Generally, the IRS will figure the penalty for you and send you a bill. However, you must complete Form 2210 or Form 2210-F and attach it to your return if you are able to lower or eliminate your penalty. See *Form 2210*, later.

Topics

This chapter discusses:

- The general rule for the underpayment penalty,
- Special rules for certain individuals,
- Exceptions to the underpayment penalty,
- How to figure your underpayment and the amount of your penalty on Form 2210, and
- How to ask IRS to waive the penalty.

Useful Items

You may want to see:

Form (and Instructions)

- 2210** Underpayment of Estimated Tax by Individuals, Estates, and Trusts
- 2210-F** Underpayment of Estimated Tax by Farmers and Fishermen

See chapter 5 for information about getting these forms.

General Rule

In general, you may owe a penalty for 2001 if the total of your withholding and estimated tax payments did not equal at least the *smaller* of:

- 1) 90% of your 2001 tax, or
- 2) 100% of your 2000 tax. (Your 2000 tax return must cover a 12-month period.)

Your 2001 tax, for this purpose, is your *Total tax for 2001*, defined under *Exceptions*, later.

Special rules for certain individuals. There are special rules for farmers and fishermen, and for certain higher income taxpayers.

Farmers and fishermen. If at least two-thirds of your gross income for 2000 or 2001 is from farming or fishing, substitute 66 $\frac{2}{3}$ % for 90% in (1) above.

See *Farmers and Fishermen* later.

Higher income taxpayers. If less than two-thirds of your gross income for 2000 and 2001 is from farming or fishing and your adjusted gross income (AGI) for 2000 was more than \$150,000 (\$75,000 if your filing status is married filing a separate return in 2001), substitute 110% for 100% in (2) above.

For 2000, AGI is the amount shown on Form 1040 — line 34; Form 1040A — line 19; and Form 1040EZ — line 4.

Penalty figured for each period. Because the penalty is figured separately for each payment period, you may owe a penalty for a payment period even if you later paid enough to make up the underpayment. If you did not pay enough tax by the due date of any of the payment periods, you may owe a penalty even if you are due a refund when you file your income tax return.

Example 4.1. You did not make estimated tax payments for 2001 because you thought you had enough tax withheld from your wages. Early in January 2002, you made an estimate of your total 2001 tax. Then you realized that your withholding was \$2,000 less than the amount needed to avoid a penalty for underpayment of estimated tax.

On January 11, you made an estimated tax payment of \$3,000, the difference between your withholding and your estimate of your total tax. Your final return shows your total tax to be \$50 less than your estimate, so you are due a refund.

You do not owe a penalty for your payment due January 15, 2002. However, you may owe a penalty through January 11, 2002 for your underpayments for the earlier payment periods.

Minimum required each period. You will owe a penalty for any 2001 payment period for which your estimated tax payment plus your withholding for the period and overpayments for previous periods was less than the *smaller* of:

- 1) 22.5% of your 2001 tax, or
- 2) 25% of your 2000 tax. (Your 2000 tax return must cover a 12-month period.)

Note. If you are subject to the rule for higher income taxpayers, discussed earlier, substitute 27.5% for 25% in (2) above.

When penalty is charged. If you miss a payment or you paid less than the minimum required in a period, you may be charged an underpayment penalty from the date the amount was due to the date the payment is made.

Trust payments of estimated tax credited to you. If you were a beneficiary of an estate or trust that credited its estimated tax payments to you, treat the amount credited (line 14a of Schedule K-1 (Form 1041), *Beneficiary's Share of Income, Deductions, Credits, Etc.*) as an estimated tax payment made by you on January 15, 2002.

Amended returns. If you file an amended return by the due date of your original return, use the tax shown on your amended return to figure your required estimated tax payments. If you file an amended return after the due date of the original return, use the tax shown on the original return.

However, if you and your spouse file a joint return after the due date to replace separate

returns you originally filed by the due date, use the tax shown on the joint return to figure your required estimated tax payments. This rule applies only if both original separate returns were filed on time.

2000 separate returns and 2001 joint return. If you file a joint return with your spouse for 2001, but you filed separate returns for 2000, your 2000 tax is the total of the tax shown on your separate returns. You filed a separate return if you filed as single, head of household, or married filing separately.

2000 joint return and 2001 separate returns. If you file a separate return for 2001, but you filed a joint return with your spouse for 2000, your 2000 tax is your share of the tax on the joint return. You filed a separate return if you filed as single, head of household, or married filing separately.

To figure your share of the taxes on a joint return, first figure the tax both you and your spouse would have paid had you filed separate returns for 2000 using the same filing status as for 2001. Then multiply the tax on the joint return by the following fraction:

$$\frac{\text{The tax you would have paid had you filed a separate return}}{\text{The total tax you and your spouse would have paid had you filed separate returns}}$$

Example 4.2. Lisa and Paul filed a joint return for 2000 showing taxable income of \$48,000 and a tax of \$7,747. Of the \$48,000 taxable income, \$40,000 was Lisa's and the rest was Paul's. For 2001, they file married filing separately. Lisa figures her share of the tax on the 2000 joint return as follows:

2000 Tax on \$40,000 based on a separate return	\$ 8,357
2000 Tax on \$8,000 based on a separate return	1,204
Total	<u>\$ 9,561</u>
Lisa's percentage of total (\$8,357 ÷ \$ 9,561)	87.41%
Lisa's percentage of tax on joint return (\$7,747 × 87.41%)	<u>\$ 6,772</u>

Form 2210. In most cases, you do not need to file Form 2210. The IRS will figure the penalty for you and send you a bill. If you want us to figure the penalty for you, leave the penalty line on your return blank. Do **not** file Form 2210. If you want to figure your penalty, complete Part I, Part II, and either Part III or Part IV of Form 2210. See *Reasons for filing* to determine whether you should file Form 2210. If you use Form 2210, you cannot file Form 1040EZ.

On Form 1040, enter the amount of your penalty on line 71. If you owe tax on line 70, add the penalty to your tax due and show your total payment on line 70. If you are due a refund, subtract the penalty from the overpayment you show on line 67.

On Form 1040A, enter the amount of your penalty on line 46. If you owe tax on line 45, add the penalty to your tax due and show your total payment on line 45. If you are due a refund, subtract the penalty from the overpayment you show on line 42.

Lowering or eliminating the penalty. You may be able to lower or eliminate your penalty if

you file Form 2210. You **must** file Form 2210 with your return if any of the following applies.

- You request a waiver. See *Waiver of Penalty*, later.
- You use the annualized income installment method. See the explanation of this method under *Figuring Your Underpayment*, later.
- You use your actual withholding for each payment period for estimated tax purposes. See *Actual withholding method* under *Figuring Your Underpayment*, later.
- You base any of your required installments on the tax shown on your 2000 return and you filed or are filing a joint return for either 2000 or 2001 but not for both years.

Exceptions

Generally, you do not have to pay an underpayment penalty if either of the following conditions apply:

- Your total tax is less than \$1,000, or
- You had no tax liability last year.

Less Than \$1,000 Due

You do not owe a penalty if the total tax shown on your return minus the amount you paid through withholding (including excess social security and railroad retirement tax withholding) is less than \$1,000.

Total tax for 2001. For 2001, your total tax on Form 1040 is the amount on line 58 reduced by the total of the following amounts.

- 1) Any recapture of a federal mortgage subsidy from Form 8828 included on line 58.
- 2) Any social security or Medicare tax on tips not reported to your employer on line 54.
- 3) Any tax on excess contributions to IRAs and medical savings accounts, and any tax on excess accumulations in qualified retirement plans from Form 5329 included on line 55.
- 4) Any uncollected social security, Medicare, or railroad retirement tax included on line 58.
- 5) Any earned income credit on line 61a.
- 6) Any additional child tax credit on line 63.
- 7) Any credit for federal tax on fuels from Form 4136 included on line 65.

Your total tax on Form 1040A is the amount on line 36 minus the amount on lines 39a and 40. Your total tax on Form 1040EZ is the amount on line 11 minus the amount on line 9a.

Paid through withholding. For 2001, the amount you paid through withholding on Form 1040 is the amount on line 59 plus any excess social security or railroad retirement tax withholding on line 62. On Form 1040A, the amount you paid through withholding is the amount on line 37, plus any excess social security or rail-

road retirement tax withholding included in the total on line 41. On Form 1040EZ, it is the amount on line 8.

No Tax Liability Last Year

You do not owe a penalty if you had no tax liability last year and you were a U.S. citizen or resident for the whole year. For this rule to apply, your tax year must have included all 12 months of the year.

You had no tax liability for 2000 if your total tax was zero or you did not need to file an income tax return.

Example 4.3. Ray, who is single and 22 years old, was unemployed for most of 2000. He earned \$2,700 in wages before he was laid off, and he received \$2,500 in unemployment compensation afterwards. He had no other income. Even though he had gross income of \$5,200, he did not have to pay income tax because his gross income was less than the filing requirement for a single person under age 65 (\$7,200 for 2000). He filed a return only to have his withheld income tax refunded to him.

In 2001, Ray began regular work as an independent contractor. Ray made no estimated tax payments in 2001. Even though he did owe tax at the end of the year, Ray does not owe the underpayment penalty for 2001 because he had no tax liability in 2000.

Total tax for 2000. For 2000, your total tax on Form 1040 is the amount on line 57 reduced by the total of the following amounts.

- 1) Any recapture of a federal mortgage subsidy from Form 8828 included on line 57.
- 2) Any social security or Medicare tax on tips not reported to your employer on line 53.
- 3) Any tax on excess contributions to IRAs and medical savings accounts, and any tax on excess accumulations in qualified retirement plans from Form 5329 included on line 54.
- 4) Any uncollected social security, Medicare, or railroad retirement tax included on line 57.
- 5) Any earned income credit on line 60a.
- 6) Any additional child tax credit on line 62.
- 7) Any credit for federal tax on fuels from Form 4136 included on line 64.

Your total tax on Form 1040A is the amount on line 35 minus the amount on lines 38a and 39. Your total tax on Form 1040EZ is the amount on line 10 minus the amount on line 8a.

Figuring Your Required Annual Payment

Figure your required annual payment in Part II of Form 2210, following the line-by-line instructions. If you rounded the entries on your return to whole dollars, you can round on Form 2210.

Example 4.4. The tax on Ivy Fields' 2000 return was \$10,000 (her AGI was not more than \$150,000). The tax on her 2001 return (Form

1040, line 40) is \$11,000. She does not claim any credits or pay any other taxes.

For 2001, Ivy had \$1,600 income tax withheld and paid \$6,800 estimated tax. Her total payments were \$8,400. 90% of her 2001 tax is \$9,900. Because she paid less than her 2000 tax and less than 90% of her 2001 tax, and does not meet an exception, Ivy knows that she owes a penalty for underpayment of estimated tax. She decides to figure the penalty on Form 2210 and pay it with her \$2,600 tax balance when she files her tax return.

Ivy's required annual payment is \$9,900 ($\$11,000 \times 90\%$) because that is smaller than her 2000 tax.

Ivy's filled-in Form 2210 is shown at the end of this chapter. Her required annual payment of \$9,900 is shown on line 14.

Different 2000 filing status. If you file a separate return for 2001, but you filed a joint return with your spouse for 2000, see *2000 joint return and 2001 separate returns*, earlier, to figure the amount to enter as your 2000 tax on line 13 of Form 2210.

Short Method for Figuring the Penalty

You may be able to use the short method in Part III of Form 2210 to figure your penalty for underpayment of estimated tax. If you qualify to use this method, it will result in the same penalty amount as the regular method. However, either the annualized income installment method or the actual withholding method, explained later, may result in a lower penalty.

You can use the short method **only** if you meet one of the following requirements.

- 1) You made no estimated tax payments for 2001 (it does not matter whether you had income tax withholding); or
- 2) You paid estimated tax in four **equal** amounts on the due dates.

Note. If any payment was made earlier than the due date, you can use the short method, but using it may cause you to pay a larger penalty than using the regular method. If the payment was only a few days early, the difference is likely to be small.

If you do not meet either requirement, figure your penalty using the regular method in Part IV, Form 2210.

You **cannot** use the short method if any of the following applies.

- 1) You made any estimated tax payments late.
- 2) You checked the box on line 1b or 1c in Part I of Form 2210.
- 3) You are filing Form 1040NR or 1040NR-EZ and you did not receive wages as an employee subject to U.S. income tax withholding.

Note. If you use the short method, you cannot use the annualized income installment method to figure your underpayment for each

payment period. Also, you cannot use your actual withholding during each period to figure your payments for each period. These methods, which may give you a smaller penalty amount, are explained later under *Figuring Your Underpayment*.

Completing Part III. Complete Part III following the line-by-line instructions.

First, figure your total underpayment for the year (line 18) by subtracting the total of your withholding and estimated tax payments (line 17) from your required annual payment (Part II, line 14). Then figure the penalty you would owe if the underpayment remained unpaid up to April 15, 2002. This amount (line 19) is the maximum estimated tax penalty on your underpayment.

Next, figure any part of the maximum penalty you do not owe (line 20) because your underpayment was paid before the due date of your return. For example, if you filed your 2001 return and paid the tax balance on April 3, 2002, you do not owe the penalty for the 12-day period from April 4 through April 15. Therefore, you would figure the amount to enter on line 20 using 12 days.

Finally, subtract from the maximum penalty amount (line 19) any part you do not owe (line 20). The result (line 21) is the penalty you owe. Enter that amount on line 71 of Form 1040 or line 46 of Form 1040A. Attach Form 2210 to your return only if you checked one of the boxes in Part I.

Example 4.5. The facts are the same as in *Example 4.4*. Ivy paid her estimated tax payments in four installments of \$1,700 ($\$6,800 \div 4$) each on the dates they were due.

Ivy qualifies to use the short method to figure her estimated tax penalty. Using the annualized income installment method or actual withholding will not give her a smaller penalty amount because her income and withholding were distributed evenly throughout the year. Therefore, she figures her penalty in Part III of Form 2210 and leaves Part IV (not shown) blank.

Ivy figures her \$1,500 total underpayment for the year (line 18) by subtracting the total of her withholding and estimated tax payments (\$8,400) from her \$9,900 required annual payment (Part II, line 14). The maximum penalty on her underpayment (line 19) is $\$66 (\$1,500 \times .04397)$.

Ivy plans to file her return and pay her \$2,600 tax balance on March 16, 2002, 30 days before April 15. Therefore, she does not owe part of the maximum penalty amount. The part she does not owe (line 20) is figured as follows.

$$\$1,500 \times 30 \times .00016 = \$7$$

Ivy subtracts the \$7 from the \$66 maximum penalty and enters the result, \$59, on line 21 and on line 71 of her Form 1040. She adds \$59 to her \$2,600 tax balance and enters the result, \$2,659 on line 70 of her Form 1040. Ivy files her return on March 16 and attaches a check for \$2,659. Because Ivy did not check any of the boxes in Part I, she does not attach Form 2210 to her tax return.

Ivy's filled-in Form 2210, Part III is shown at the end of this chapter.

Regular Method for Figuring the Penalty

You **must** use the regular method in Part IV of Form 2210 to figure your penalty for underpayment of estimated tax if any of the following apply to you.

- You paid one or more estimated tax payments on a date other than the due date.
- You paid at least one, but less than four, installments of estimated tax.
- You paid estimated tax payments in unequal amounts.
- You use the annualized income installment method to figure your underpayment for each payment period.
- You use your actual withholding during each payment period to figure your payments.

If you use the regular method, figure your underpayment for each payment period in Section A, then figure your penalty for each payment period in Section B.

Figuring Your Underpayment (Section A of Part IV)

Figure your underpayment of estimated tax for each payment period in Section A following the line-by-line instructions. Complete each line for a payment period column before completing the next column.

Required installment. Your required payment for each payment period (line 22) is usually one-fourth of your required annual payment (Part II, line 14). However, if you are using the annualized income installment method (described later), first complete Schedule AI (Form 2210), and then enter the amounts from line 25 of that schedule on line 22 of Form 2210.

Payments. On line 23, enter in each column the total of:

- 1) Your estimated tax paid after the due date for the previous column and by the due date shown, and
- 2) One-fourth of your withholding.

For special rules for figuring your payments, see the instructions for Form 2210.

If you file Form 1040, your withholding is the amount on line 59, plus any excess social security or railroad retirement tax withholding on line 62. If you file Form 1040A, your withholding is the amount on line 37, plus any excess social security or railroad retirement tax withholding included in the total on line 41.

Actual withholding method. Instead of using one-fourth of your withholding to figure your payments, you can choose to establish how much was actually withheld by the due dates and use those amounts. You can make this choice separately for the tax withheld from your wages and for all other withholding.

Using your actual withholding may result in a smaller penalty if most of your withholding occurred early in the year.

Table 4-1. Calendar to Determine Number of Days a Payment is Late

Instructions. First, find the number for the payment due date. Then, find the number for the date the payment was made. Finally, subtract the payment due date number from the payment date number. The answer is the number of days the payment is late.

Example. The payment due date is June 15 (61). The payment was made on November 4 (203). The payment is 142 days late (203 - 61).

Tax Year 2001													
Day of Month	2001 April	2001 May	2001 June	2001 July	2001 Aug.	2001 Sept.	2001 Oct.	2001 Nov.	2001 Dec.	2002 Jan.	2002 Feb.	2002 March	2002 April
1		16	47	77	108	139	169	200	230	261	292	320	351
2		17	48	78	109	140	170	201	231	262	293	321	352
3		18	49	79	110	141	171	202	232	263	294	322	353
4		19	50	80	111	142	172	203	233	264	295	323	354
5		20	51	81	112	143	173	204	234	265	296	324	355
6		21	52	82	113	144	174	205	235	266	297	325	356
7		22	53	83	114	145	175	206	236	267	298	326	357
8		23	54	84	115	146	176	207	237	268	299	327	358
9		24	55	85	116	147	177	208	238	269	300	328	359
10		25	56	86	117	148	178	209	239	270	301	329	360
11		26	57	87	118	149	179	210	240	271	302	330	361
12		27	58	88	119	150	180	211	241	272	303	331	362
13		28	59	89	120	151	181	212	242	273	304	332	363
14		29	60	90	121	152	182	213	243	274	305	333	364
15	0	30	61	91	122	153	183	214	244	275	306	334	365
16	1	31	62	92	123	154	184	215	245	276	307	335	
17	2	32	63	93	124	155	185	216	246	277	308	336	
18	3	33	64	94	125	156	186	217	247	278	309	337	
19	4	34	65	95	126	157	187	218	248	279	310	338	
20	5	35	66	96	127	158	188	219	249	280	311	339	
21	6	36	67	97	128	159	189	220	250	281	312	340	
22	7	37	68	98	129	160	190	221	251	282	313	341	
23	8	38	69	99	130	161	191	222	252	283	314	342	
24	9	39	70	100	131	162	192	223	253	284	315	343	
25	10	40	71	101	132	163	193	224	254	285	316	344	
26	11	41	72	102	133	164	194	225	255	286	317	345	
27	12	42	73	103	134	165	195	226	256	287	318	346	
28	13	43	74	104	135	166	196	227	257	288	319	347	
29	14	44	75	105	136	167	197	228	258	289		348	
30	15	45	76	106	137	168	198	229	259	290		349	
31		46		107	138		199		260	291		350	

If you use your actual withholding, you must check the box on line 1c, Part I of Form 2210 and complete Form 2210 and file it with your return.

Regular Installment Method

The filled-in form for the following example is shown at the end of this chapter.

Example 4.6. Ben Brown's 2001 total tax (Form 1040, line 58) is \$7,031, the total of his \$4,685 income tax and \$2,346 self-employment tax. (His 2000 AGI was less than \$150,000.) He does not owe any other taxes or claim any credits other than for withholding. His 2000 tax was \$6,116.

Ben's employer withheld \$3,228 income tax during 2001. Ben made no estimated tax payment for either the first or second period, but he paid \$1,000 each on September 2, 2001, and January 12, 2002, for the third and fourth periods. Because the total of his withholding and estimated tax payments, \$5,228 (\$3,228 + \$1,000 + \$1,000), was less than 90% of his 2001 tax (\$6,328), and was also less than his 2000 tax

(\$6,116), Ben knows he owes a penalty for underpayment of estimated tax. He decides to figure the penalty on Form 2210 and pay it with his \$1,803 tax balance (\$7,031 - \$5,228) when he files his tax return on April 15, 2002.

Ben's required annual payment (Part II, line 14) is \$6,116. Because his income and withholding were distributed evenly throughout the year, Ben enters one-fourth of his required annual payment, \$1,529, in each column of line 22. On line 23, he enters one-fourth of his withholding, \$807 in the first two columns and \$1,807 (\$807 plus \$1,000 estimated tax payment) in the last two columns.

Ben has an underpayment (line 29) for each payment period even though his withholding and estimated tax payments for the third and fourth periods were more than his required installments (line 22). This is because the estimated tax payments made in the third and fourth periods are first applied to underpayments for the earlier periods. Part IV, Section A, of Ben's Form 2210 is shown at the end of this chapter.

Annualized Income Installment Method (Schedule AI)

If you did not receive your income evenly throughout the year (for example, your income from a repair shop you operated was much larger in the summer than it was during the rest of the year), you may be able to lower or eliminate your penalty by figuring your underpayment using the annualized income installment method. Under this method, your required installment (line 22) for one or more payment periods may be less than one-fourth of your required annual payment.

To figure your underpayment using this method, complete Schedule AI of Form 2210. The schedule annualizes your tax at the end of each payment period based on your income, deductions, and other items relating to events that occurred since the beginning of the tax year through the end of the period.

If you use the annualized income installment method, you must check the box on line 1b of Form 2210. You also must attach Form 2210 and Schedule AI to your return.



If you use Schedule A1 for any payment due date, you must use it for all payment due dates.

Completing Schedule A1 of Form 2210. Follow your Form 2210 instructions to complete Schedule A1. For each period shown on Schedule A1, figure your income and deductions based on your method of accounting. If you use the cash method of accounting (used by most people), include all income actually or constructively received during the period and all deductions actually paid during the period.

Note. Each period includes amounts from the previous period(s).

- **Period (a)** includes items for January through March.
- **Period (b)** includes items for January through May.
- **Period (c)** includes items for January through August.
- **Period (d)** includes items for the entire year.

Example 4.7. The facts are the same as in Example 4.6, except that Ben did not receive his income evenly throughout the year. Therefore, he decides to figure his required installment for each period (line 22 of Form 2210) using the annualized income installment method.

Ben's filled-in Schedule A1 and Part IV of Form 2210 using this method are shown at the end of this chapter.

Ben's wages during 2001 were \$21,000 (\$1,750 a month). His net earnings from a business he started during the year were \$16,600, received as follows:

April through May	\$4,600
June through August	4,000
September through December	8,000

Before Ben can figure his adjusted gross income for each period (line 1 of Schedule A1), he must figure his deduction for self-employment tax for each period. He completes Part II of Schedule A1 first.

Ben had no self-employment income for the first period, so he leaves the lines in that column blank. His self-employment income was \$4,600 for the second period, \$8,600 (\$4,600 + \$4,000) for the third period, and \$16,600 (\$8,600 + \$8,000) for the fourth period. He multiplies each amount by 92.35% (.9235) to find the amounts to enter on line 26. He then fills out the rest of Part II.

Ben figures the amounts to enter on line 1 of Schedule A1 as follows:

1st Column —1/1/01 to 3/31/01:	
\$1,750 per month × 3 months	\$5,250
2nd Column —1/1/01 to 5/31/01:	
\$1,750 per month × 5 months	8,750
Plus: Self-employment income through 5/31/01	4,600
Less: Self-employment tax deduction (\$1,560 ÷ 4.8)	(325)
	<u>\$13,025</u>
3rd Column —1/1/01 to 8/31/01:	
\$1,750 per month × 8 months	\$14,000
Plus: Self-employment income through 8/31/01	8,600
Less: Self-employment tax deduction (\$1,822 ÷ 3)	(607)
	<u>\$21,993</u>

4th Column —1/1/01 to 12/31/01:	
\$1,750 per month × 12 months	\$21,000
Plus: Self-employment income through 12/31/01	16,600
Less: Self-employment tax deduction (\$2,346 ÷ 2)	(1,173)
	<u>\$36,427</u>

Ben completes the rest of Schedule A1 to determine the amounts to put on Form 2210, line 22.

Ben then figures his underpayment in Part IV, Section A. He finds that he overpaid his estimated tax for the first payment period, but he underpaid his estimated tax for the other three periods. Example 4.9 illustrates how Ben completes Part IV, Section B, of his Form 2210.

Figuring Your Penalty (Section B of Part IV)

Figure the amount of your penalty in Section B, Part IV of Form 2210, following the instructions. The penalty is imposed on each underpayment shown on line 29, Section A, for the number of days through April 15, 2001, that it remained unpaid. (You may find it helpful to show the date of payment beside each amount on line 29.)

There are three rate periods to figure the penalty. Use *Rate Period 1* (lines 31 and 32) to apply the 8% rate in effect between April 16, 2001 and June 30, 2001. Use *Rate Period 2* (lines 33 and 34) to apply the 7% rate in effect between July 1, 2001 and December 31, 2001. Use *Rate Period 3* (lines 35 and 36) to apply the 6% rate in effect between January 1, 2002 and April 15, 2002.

Aid for counting days. Table 4-1 provides a simple method to count the number of days between payment dates or between a due date and a payment date.

- 1) Find the number for the date the payment was due.
- 2) Find the number for the date the payment was made.
- 3) Subtract the due date "number" from the payment date "number."

For example, if a payment was due on June 15 (61), but was not paid until November 4 (203), the payment was 142 (203 - 61) days late.

Payments. Before completing Section B, make a list of the payments you made after the due date (or the last day payments could be made on time) for the earliest payment period an underpayment occurred. For example, if you had an underpayment for the first payment period, list your payments after April 15, 2001. You can use the tables in the Form 2210 instructions to make your list. Follow those instructions for listing income tax withheld and payments made with your return. Use the list to determine when each underpayment was paid.

Underpayment paid in two or more parts. If an underpayment was paid in two or more parts on different dates, you must figure the penalty separately for each part. (You may find it helpful to show the underpayment on line 29, Section A, broken down into the parts paid on different dates.)

Figuring the penalty. Form 2210 for 2001 has 3 rate periods. Figure the underpayment penalty by applying the appropriate rate against

each underpayment shown on line 29. If an underpayment remained unpaid for more than one rate period, the penalty on that underpayment will be figured using more than one rate.

Use lines 31, 33, and 35 to figure the number of days the underpayment remained unpaid. (Also see Table 4-1.) Use lines 32, 34, and 36 to figure the actual penalty amount by applying the rate against the underpayment for the number of days it remained unpaid.

If an underpayment remained unpaid for the entire period, use Table 4-2 to determine the number of days to enter for each period.

Table 4-2
Chart of Total Days

	Column (a)	Column (b)	Column (c)	Column (d)
line 31	76	15	NA	NA
line 33	184	184	98	NA
line 35	105	105	105	90

Example 4.8. In Example 4.6, Ben Brown determined that he had an underpayment for all four payment periods.

Ben's filled-in Form 2210 is shown at the end of this chapter. This example illustrates Part IV, Section B, of that form.

Ben's 2001 tax is \$7,031. His minimum required payment for each period is \$1,529 (\$6,116 ÷ 4). His \$3,228 withholding is considered paid in four equal installments of \$807, one on each payment due date. Therefore, he must make estimated tax payments of \$722 each period. Ben made estimated tax payments of \$1,000 on September 2, 2001, and \$1,000 on January 12, 2002. He plans to file his return and pay his \$1,803 tax balance (\$7,031 tax - \$5,228 withholding and estimated tax payments) on April 15, 2002. Therefore, he is considered to have made the following payments for tax year 2001:

April 15, 2001	\$ 807
June 15, 2001	807
September 2, 2001	1,000
September 15, 2001	807
January 12, 2002	1,000
January 15, 2002	807
April 15, 2002	1,803

Penalty for first period (April 15, 2001) — column (a). Ben's \$722 underpayment for the first payment period was paid by applying \$722 of his \$807 payment on June 15, 2001. The \$722 remained unpaid 61 days (April 16 through June 15, 2001). Ben enters "61" on line 31 and figures this part of the penalty on line 32.

Penalty for second period (June 15, 2001) — column (b). Ben figures his second period underpayment as follows.

- 1) Of the \$807 he paid for the second period, \$722 is applied to the underpayment remaining from the first period.
- 2) That leaves \$85 (\$807 - \$722) to apply to his second period required installment of \$1,529.
- 3) The result, \$1,444 (\$1,529 - \$85) is Ben's underpayment for the second period.

The \$1,444 underpayment is paid in two parts by applying the \$1,000 paid on September

2 and \$444 of his \$807 September 15 payment. To help him figure his penalty, Ben shows each part of the underpayment paid on different dates on line 29.

For **Rate Period 1**, the entire underpayment remained unpaid 15 days (June 16 through June 30). Ben enters "15" on line 31 and figures this part of his penalty on line 32.

For **Rate Period 2**, \$1,000 of the underpayment remained unpaid for 64 days (July 1 through September 2) and \$444 remained unpaid for 77 days (July 1 through September 15). Ben enters "64" and "77" on line 33. He figures this part of the penalty on line 34 by adding the result of the two penalty computations.

Penalty for third period (September 24, 2001) — column (c). Ben figures his third period underpayment as follows.

- 1) Of the \$1,807 he paid for the third period, \$1,444 is applied to the underpayment remaining from the second period.
- 2) That leaves \$363 (\$1,807 – \$1,444) to apply to his third period required installment of \$1,529.
- 3) The result, \$1,166 (\$1,529 – \$363) is Ben's underpayment for the third period.

The \$1,166 underpayment is paid in two parts by applying his \$1,000 payment on January 12, 2001, and \$166 of his \$807 payment on January 15. On line 29, Ben shows each part of the underpayment paid on different dates.

For **Rate Period 2**, the entire underpayment remained unpaid 98 days (September 25 through December 31). Ben enters "98" on line 33 and figures this part of his penalty on line 34.

For **Rate Period 3**, \$1,000 of the underpayment remained unpaid for 12 days (January 1 through January 12) and \$444 remained unpaid for 15 days (January 1 through January 15). Ben enters "15" and "12" on line 35 and figures his penalty for each part of the underpayment on line 36. He includes both penalty amounts on line 36.

Penalty for fourth period (January 15, 2002) — column (d). Ben figures his fourth period underpayment as follows.

- 1) Of the \$1,807 he paid for the fourth period, \$1,166 is applied to the underpayment remaining from the third period.
- 2) That leaves \$641 (\$1,807 – \$1,166) to apply to his fourth period required installment of \$1,529.
- 3) The result, \$888 (\$1,529 – \$641) is Ben's underpayment for the fourth period.

The \$888 underpayment was paid April 15, 2002, with his tax return. The \$888 remained unpaid 90 days (January 16 through April 15, 2002). Ben enters that number on line 35 and figures his penalty on line 36.

Total penalty. Ben's total penalty for 2001 on line 37 is \$70.66, the total of all amounts on lines 32, 34, and 36 in all columns. Ben enters that amount on line 71 of his Form 1040. He also adds \$71 to his \$1,803 tax balance and enters the \$1,874 total on line 70. He files his return on April 15 and includes a check for \$1,874. He keeps his completed Form 2210 for his records.

Example 4.9. In *Example 4.7*, Ben Brown's first underpayment was for the second payment period.

Ben's filled-in Schedule AI and Part IV of Form 2210 are shown at the end of this chapter. This example illustrates completion of Part IV, Section B, of Ben's Form 2210 under the annualized income installment method.

Ben made the same payments listed in the table in *Example 4.8*.

Penalty for second period — column (b). Ben's \$598 underpayment for the second payment period was paid by applying \$598 of his \$1,000 September 2, 2001 payment. To help him figure his penalty, Ben shows the date the underpayment was paid on line 29.

For **Rate Period 1**, the entire underpayment remained unpaid 15 days (June 16 through June 30). Ben enters "15" on line 31 and figures this part of his penalty on line 32.

For **Rate Period 2**, the entire underpayment remained unpaid for 64 days (July 1 through September 2). Ben enters "64" on line 33 and figures this part of his penalty on line 34.

Penalty for third period — column (c). Ben's \$246 underpayment for the third payment period was paid by applying \$246 of his \$1,000 payment on January 12, 2002.

For **Rate Period 2**, the entire underpayment remained unpaid 98 days (September 25 through December 31, 2001). Ben enters "98" on line 33 and figures this part of the penalty on line 34.

For **Rate Period 3**, the entire underpayment remained unpaid 12 days (January 1, 2002, through January 12, 2002). Ben enters "12" on line 35 and figures this part of the penalty on line 36.

Penalty for fourth period — column (d). Ben's \$653 underpayment for the fourth payment period was paid on April 15, 2002, with his tax return. The entire amount remained unpaid 90 days (January 16 through April 15, 2002). Ben enters that number on line 35 and figures this part of the penalty on line 36.

Total penalty. Ben's total penalty for 2001 on line 37 is \$24.08, the total of all amounts on lines 32, 34, and 36 in all columns. Ben enters that amount on line 71 of his Form 1040. He also adds \$24 to his \$1,803 tax balance and enters the \$1,827 total on line 70. He files his return on April 15 and includes a check for \$1,827. Because he used the annualized income installment method, he **must** attach Form 2210, including Schedule AI, to his return and check the box on line 1b of Form 2210.

Farmers and Fishermen

If you are a farmer or fisherman, the following special rules for underpayment of estimated tax apply to you.

- 1) The penalty for underpaying your 2001 estimated tax will not apply if you file your return and pay all the tax due by March 1, 2002. If you are a fiscal year taxpayer, the penalty will not apply if you file your return

and pay the tax due by the first day of the third month after the end of your tax year.

- 2) Any penalty you owe for underpaying your 2001 estimated tax will be figured from one payment due date, January 15, 2002.
- 3) The underpayment penalty for 2001 is figured on the difference between the amount of 2001 withholding plus estimated tax paid by the due date and the smaller of:
 - a) 100% of the tax shown on your 2000 return, or
 - b) 66% (rather than 90%) of your 2001 tax.

Even if these special rules apply to you, you will not owe the penalty if you meet either of the two conditions discussed earlier under *Exceptions*.

See chapter 2 to see whether you are a farmer or fisherman who is eligible for these special rules.

Form 2210–F. Use Form 2210–F to figure any underpayment penalty. Do not attach it to your return unless you check box 1a or box 1b. Also, if neither box applies to you and you owe a penalty, you do not need to complete Form 2210–F. The IRS can figure your penalty and send you a bill.

Waiver of Penalty

The IRS can waive the penalty for underpayment if either of the following applies.

- 1) You did not make a payment because of a casualty, disaster, or other unusual circumstance and it would be inequitable to impose the penalty.
- 2) You retired (after reaching age 62) or became disabled in 2000 or 2001 and both the following requirements are met:
 - a) You had a reasonable cause for not making the payment, and
 - b) Your underpayment was not due to willful neglect.

How to request a waiver. To request a waiver, you **must** complete Form 2210 as follows.

- 1) Check the box on line 1a.
- 2) Complete line 2 through line 20 (or through line 36 if you use the regular method) without regard to the waiver.
- 3) Write the amount you want waived in parentheses on the dotted line next to line 21 (line 37 for the regular method).
- 4) Subtract this amount from the total penalty you figured without regard to the waiver. Enter the result on line 21 (line 37 for the regular method).
- 5) Attach Form 2210 and a statement to your return explaining the reasons you were unable to meet the estimated tax require-

ments and the time period for which you are requesting a waiver.

- 6) If you are requesting a penalty waiver due to a casualty, disaster, or other circumstance, include supporting documentation, such as police and insurance company reports.
- 7) If you are requesting a penalty waiver due to retirement or disability, attach documentation that shows your retirement date (and your age on that date) or the date you became disabled.

The IRS will review the information you provide and will decide whether or not to grant your request for a waiver.

Farmers and fishermen. To request a waiver, you **must** complete Form 2210–F as follows.

- 1) Check the box on line 1a.
- 2) Complete line 2 through line 18 without regard to the waiver.
- 3) Write the amount you want waived in parentheses on the dotted line next to line 19.
- 4) Subtract this amount from the total penalty you figured without regard to the waiver. Enter the result on line 19.
- 5) Attach Form 2210–F and a statement to your return explaining the reasons you were unable to meet the estimated tax requirements.

- 6) If you are requesting a penalty waiver due to a casualty, disaster, or other circumstance, include supporting documentation, such as police and insurance company reports.
- 7) If you are requesting a penalty waiver due to retirement or disability, attach documentation that shows your retirement date (and your age on that date) or the date you became disabled.

The IRS will review the information you provide and will decide whether or not to grant your request for a waiver.

**Underpayment of
Estimated Tax by Individuals, Estates, and Trusts**

▶ See separate instructions.

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

Name(s) shown on tax return

Ivy Fields

Identifying number

222 - 00 - 2222

In most cases, you do not need to file Form 2210. The IRS will figure any penalty you owe and send you a bill. File Form 2210 only if one or more boxes in Part I apply to you. If you do not need to file Form 2210, you still may use it to figure your penalty. Enter the amount from Part III, line 21, or Part IV, line 37, on the penalty line of your return, but do not attach Form 2210.

Part I Reasons for Filing—If 1a, 1b, or 1c below applies to you, you may be able to lower or eliminate your penalty. But you **must** check the boxes that apply and file Form 2210 with your tax return. If 1d below applies to you, check that box and file Form 2210 with your tax return.

- 1** Check whichever boxes apply (if none apply, see the text above Part I and **do not file Form 2210**):
- a** You request a **waiver**. In certain circumstances, the IRS will waive all or part of the penalty. See **Waiver of Penalty** on page 2 of the instructions.
 - b** You use the **annualized income installment method**. If your income varied during the year, this method may reduce the amount of one or more required installments. See page 5 of the instructions.
 - c** You had Federal income tax withheld from wages and, for estimated tax purposes, you treat the withheld tax as paid on the dates it was actually withheld, instead of in equal amounts on the payment due dates. See the instructions for line 23 on page 3.
 - d** Your required annual payment (line 14 below) is based on your 2000 tax and you filed or are filing a joint return for either 2000 or 2001 but not for both years.

Part II Required Annual Payment

Example 4.4

2 Enter your 2001 tax after credits (see page 2 of the instructions)	2	11,000
3 Other taxes (see page 2 of the instructions)	3	
4 Add lines 2 and 3	4	11,000
5 Earned income credit	5	
6 Additional child tax credit	6	
7 Credit for Federal tax paid on fuels	7	
8 Add lines 5, 6, and 7	8	- 0 -
9 Current year tax. Subtract line 8 from line 4	9	11,000
10 Multiply line 9 by 90% (.90)	10	9,900
11 Withholding taxes. Do not include any estimated tax payments on this line (see page 3 of the instructions)	11	1,600
12 Subtract line 11 from line 9. If less than \$1,000, stop here; you do not owe the penalty. Do not file Form 2210	12	9,400
13 Enter the tax shown on your 2000 tax return (110% of that amount if the adjusted gross income shown on that return is more than \$150,000, or, if married filing separately for 2001, more than \$75,000). Caution: See page 3 of the instructions	13	10,000
14 Required annual payment. Enter the smaller of line 10 or line 13 If line 11 is equal to or more than line 14, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked box 1d above.	14	9,900

Part III Short Method (**Caution:** See page 3 of the instructions to find out if you can use the short method. If you checked box **1b** or **1c** in Part I, skip this part and go to Part IV.)

Example 4.5

15 Enter the amount, if any, from line 11 above	15	1,600
16 Enter the total amount, if any, of estimated tax payments you made	16	6,800
17 Add lines 15 and 16	17	8,400
18 Total underpayment for year. Subtract line 17 from line 14. If zero or less, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked box 1d above	18	1,500
19 Multiply line 18 by .04397 (see page 3 of the instructions if you are eligible for relief due to the September 11, 2001, terrorist attacks)	19	66
20 • If the amount on line 18 was paid on or after 4/15/02, enter -0-. • If the amount on line 18 was paid before 4/15/02, make the following computation to find the amount to enter on line 20.		
Amount on line 18 × Number of days paid before 4/15/02 × .00016	20	7
21 Penalty. Subtract line 20 from line 19. Enter the result here and on Form 1040, line 71; Form 1040A, line 46; Form 1040NR, line 69; Form 1040NR-EZ, line 26; or Form 1041, line 26, but do not file Form 2210 unless you checked one or more of the boxes in Part I above	21	59

**Underpayment of
Estimated Tax by Individuals, Estates, and Trusts**

Department of the Treasury
Internal Revenue Service

▶ See separate instructions.
▶ Attach to Form 1040, 1040A, 1040NR, 1040NR-EZ, or 1041.

Name(s) shown on tax return: Ben Brown Identifying number: 333 - 00 - 3333

In most cases, you do not need to file Form 2210. The IRS will figure any penalty you owe and send you a bill. File Form 2210 only if one or more boxes in Part I apply to you. If you do not need to file Form 2210, you still may use it to figure your penalty. Enter the amount from Part III, line 21, or Part IV, line 37, on the penalty line of your return, but do not attach Form 2210.

Part I Reasons for Filing—If 1a, 1b, or 1c below applies to you, you may be able to lower or eliminate your penalty. But you **must** check the boxes that apply and file Form 2210 with your tax return. If 1d below applies to you, check that box and file Form 2210 with your tax return.

- 1 Check whichever boxes apply (if none apply, see the text above Part I and **do not file Form 2210**):
 - a You request a **waiver**. In certain circumstances, the IRS will waive all or part of the penalty. See **Waiver of Penalty** on page 2 of the instructions.
 - b You use the **annualized income installment method**. If your income varied during the year, this method may reduce the amount of one or more required installments. See page 5 of the instructions.
 - c You had Federal income tax withheld from wages and, for estimated tax purposes, you treat the withheld tax as paid on the dates it was actually withheld, instead of in equal amounts on the payment due dates. See the instructions for line 23 on page 3.
 - d Your required annual payment (line 14 below) is based on your 2000 tax and you filed or are filing a joint return for either 2000 or 2001 but not for both years.

Part II Required Annual Payment Example 4.6

2 Enter your 2001 tax after credits (see page 2 of the instructions)	2	4,685
3 Other taxes (see page 2 of the instructions)	3	2,346
4 Add lines 2 and 3	4	7,031
5 Earned income credit	5	
6 Additional child tax credit	6	
7 Credit for Federal tax paid on fuels	7	
8 Add lines 5, 6, and 7	8	- 0 -
9 Current year tax. Subtract line 8 from line 4	9	7,031
10 Multiply line 9 by 90% (.90)	10	6,328
11 Withholding taxes. Do not include any estimated tax payments on this line (see page 3 of the instructions)	11	3,228
12 Subtract line 11 from line 9. If less than \$1,000, stop here; you do not owe the penalty. Do not file Form 2210	12	3,803
13 Enter the tax shown on your 2000 tax return (110% of that amount if the adjusted gross income shown on that return is more than \$150,000, or, if married filing separately for 2001, more than \$75,000). Caution: See page 3 of the instructions	13	6,116
14 Required annual payment. Enter the smaller of line 10 or line 13. If line 11 is equal to or more than line 14, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked box 1d above.	14	6,116

Part III Short Method (Caution: See page 3 of the instructions to find out if you can use the short method. If you checked box 1b or 1c in Part I, skip this part and go to Part IV.)

15 Enter the amount, if any, from line 11 above	15	
16 Enter the total amount, if any, of estimated tax payments you made	16	
17 Add lines 15 and 16	17	
18 Total underpayment for year. Subtract line 17 from line 14. If zero or less, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked box 1d above	18	
19 Multiply line 18 by .04397 (see page 3 of the instructions if you are eligible for relief due to the September 11, 2001, terrorist attacks)	19	
20 <ul style="list-style-type: none"> • If the amount on line 18 was paid on or after 4/15/02, enter -0-. • If the amount on line 18 was paid before 4/15/02, make the following computation to find the amount to enter on line 20. 	20	
21 Penalty. Subtract line 20 from line 19. Enter the result here and on Form 1040, line 7f; Form 1040A, line 46; Form 1040NR, line 69; Form 1040NR-EZ, line 26; or Form 1041, line 26, but do not file Form 2210 unless you checked one or more of the boxes in Part I above	21	

Part IV Regular Method (See page 3 of the instructions if you are filing Form 1040NR or 1040NR-EZ.)

	Payment Due Dates Example 4.6				
	(a) 4/15/01	(b) 6/15/01	(c) 9/24/01	(d) 1/15/02	
22 Required installments. If box 1b applies, enter the amounts from Schedule AI, line 25. Otherwise, enter 25% (.25) of line 14, Form 2210, in each column	22	1,529	1,529	1,529	1,529
23 Estimated tax paid and tax withheld (see page 3 of the instructions). For column (a) only, also enter the amount from line 23 on line 27. If line 23 is equal to or more than line 22 for all payment periods, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked a box in Part I. Complete lines 24 through 30 of one column before going to the next column.	23	807	807	807 + 1,000 1,807	807 + 1,000 1,807
24 Enter amount, if any, from line 30 of previous column	24				
25 Add lines 23 and 24	25		807	1,807	1,807
26 Add amounts on lines 28 and 29 of the previous column	26		722	1,444	1,166
27 Subtract line 26 from line 25. If zero or less, enter -0-. For column (a) only, enter the amount from line 23	27	807	85	363	641
28 If the amount on line 27 is zero, subtract line 25 from line 26. Otherwise, enter -0-	28		- 0 -	- 0 -	
29 Underpayment. If line 22 is equal to or more than line 27, subtract line 27 from line 22. Then go to line 24 of next column. Otherwise, go to line 30	29	6/15 722	9/2 1,000 9/15 444 1,444	1/12 1,000 1/15 166 1,166	4/15 888
30 Overpayment. If line 27 is more than line 22, subtract line 22 from line 27. Then go to line 24 of next column	30				

Section B—Figure the Penalty (Complete lines 31 through 36 of one column before going to the next column.)

	Example 4.6			
	4/15/01	6/15/01	9/24/01	1/15/02
Rate Period 1				
31 April 16, 2001—June 30, 2001 Number of days from the date shown above line 31 to the date the amount on line 29 was paid or 6/30/01, whichever is earlier	Days: 31 61	Days: 15		
32 Underpayment on line 29 (see page 4 of the instructions) × Number of days on line 31 365 × .08	\$ 9.65	\$ 4.75		
Rate Period 2				
33 July 1, 2001—December 31, 2001 Number of days from the date shown above line 33 to the date the amount on line 29 was paid or 12/31/01, whichever is earlier	Days: 33	Days: 64 77	Days: 98	
34 Underpayment on line 29 (see page 5 of the instructions) × Number of days on line 33 365 × .07	\$ 12.27	\$ 6.56	\$ 21.91	
Rate Period 3				
35 January 1, 2002—April 15, 2002 Number of days from the date shown above line 35 to the date the amount on line 29 was paid or 4/15/02, whichever is earlier	Days: 35	Days: 12	Days: 15	Days: 90
36 Underpayment on line 29 (see page 5 of the instructions) × Number of days on line 35 365 × .06	\$ 1.97	\$.41	\$ 13.14	
37 Penalty. Add all amounts on lines 32, 34, and 36 in all columns. Enter the total here and on Form 1040, line 7f; Form 1040A, line 46; Form 1040NR, line 69; Form 1040NR-EZ, line 26; or Form 1041, line 26, but do not file Form 2210 unless you checked one or more of the boxes in Part I				37 \$ 70.66

Schedule AI—Annualized Income Installment Method (See pages 5 and 6 of the instructions.) Example 4.7

Estates and trusts, **do not** use the period ending dates shown to the right. Instead, use the following: 2/28/01, 4/30/01, 7/31/01, and 11/30/01.

	(a)	(b)	(c)	(d)
	1/1/01-3/31/01	1/1/01-5/31/01	1/1/01-8/31/01	1/1/01-12/31/01

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.)	5,250	13,025	21,993	36,427
2	Annualization amounts. (Estates and trusts, see instructions.)	4	2.4	1.5	1
3	Annualized income. Multiply line 1 by line 2	21,000	31,260	32,990	36,427
4	Enter your itemized deductions for the period shown in each column. If you do not itemize, enter -0- and skip to line 7. (Estates and trusts, enter -0-, skip to line 9, and enter the amount from line 3 on line 9.)	1,500	2,500	4,000	6,000
5	Annualization amounts	4	2.4	1.5	1
6	Multiply line 4 by line 5 (see instructions if line 3 is more than \$66,475)	6,000	6,000	6,000	6,000
7	In each column, enter the full amount of your standard deduction from Form 1040, line 36, or Form 1040A, line 22 (Form 1040NR or 1040NR-EZ filers, enter -0-. Exception: Indian students and business apprentices, enter standard deduction from Form 1040NR, line 35 or Form 1040NR-EZ, line 11.)	4,550	4,550	4,550	4,550
8	Enter the larger of line 6 or line 7	6,000	6,000	6,000	6,000
9	Subtract line 8 from line 3	15,000	25,260	26,990	30,427
10	In each column, multiply \$2,900 by the total number of exemptions claimed (see instructions if line 3 is more than \$99,725). (Estates and trusts and Form 1040NR or 1040NR-EZ filers, enter the exemption amount shown on your tax return.)	2,900	2,900	2,900	2,900
11	Subtract line 10 from line 9	12,100	22,360	24,090	27,527
12	Figure your tax on the amount on line 11 (see instructions)	1,819	3,356	3,611	4,188
13	Form 1040 filers only, complete Part II and enter your self-employment tax from line 34 below		1,560	1,822	2,346
14	Enter other taxes for each payment period (see instructions)				
15	Total tax. Add lines 12, 13, and 14	1,819	4,916	5,433	6,534
16	For each period, enter the same type of credits as allowed on Form 2210, lines 2, 5, 6, and 7 (see instructions)				
17	Subtract line 16 from line 15. If zero or less, enter -0-	1,819	4,916	5,433	6,534
18	Applicable percentage	22.5%	45%	67.5%	90%
19	Multiply line 17 by line 18	409	2,212	3,667	5,881
	Caution: Complete lines 20–25 of one column before going to the next column.				
20	Add the amounts in all previous columns of line 25		409	2,212	3,667
21	Subtract line 20 from line 19. If zero or less, enter -0-	409	1,803	1,455	2,214
22	Enter 25% (.25) of line 14 on page 1 of Form 2210 in each column	1,529	1,529	1,529	1,529
23	Subtract line 25 of the previous column from line 24 of the previous column		1,120	846	920
24	Add lines 22 and 23 and enter the total	1,529	2,649	2,375	2,449
25	Enter the smaller of line 21 or line 24 here and on Form 2210, line 22 ▶	409	1,803	1,455	2,214

Part II Annualized Self-Employment Tax

26	Net earnings from self-employment for the period (see instructions)		4,248	7,942	15,330
27	Prorated social security tax limit	\$20,100	\$33,500	\$53,600	\$80,400
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		8,750	14,000	21,000
29	Subtract line 28 from line 27. If zero or less, enter -0-		24,750	39,600	59,400
30	Annualization amounts	0.496	0.2976	0.186	0.124
31	Multiply line 30 by the smaller of line 26 or line 29		1,264	1,477	1,901
32	Annualization amounts	0.116	0.0696	0.0435	0.029
33	Multiply line 26 by line 32		296	345	445
34	Add lines 31 and 33. Enter the result here and on line 13 above ▶		1,560	1,822	2,346

Part IV Regular Method (See page 3 of the instructions if you are filing Form 1040NR or 1040NR-EZ.)

Section A—Figure Your Underpayment		Payment Due Dates Example 4.7				
		(a) 4/15/01	(b) 6/15/01	(c) 9/24/01	(d) 1/15/02	
22	Required installments. If box 1b applies, enter the amounts from Schedule AI, line 25. Otherwise, enter 25% (.25) of line 14, Form 2210, in each column .	22	409	1,803	1,455	2,214
23	Estimated tax paid and tax withheld (see page 3 of the instructions). For column (a) only, also enter the amount from line 23 on line 27. If line 23 is equal to or more than line 22 for all payment periods, stop here; you do not owe the penalty. Do not file Form 2210 unless you checked a box in Part I Complete lines 24 through 30 of one column before going to the next column.	23	807	807	807 + 1,000 1,807	807 + 1,000 1,807
24	Enter amount, if any, from line 30 of previous column	24		398		
25	Add lines 23 and 24	25		1,205	1,807	1,807
26	Add amounts on lines 28 and 29 of the previous column	26			598	246
27	Subtract line 26 from line 25. If zero or less, enter -0-. For column (a) only, enter the amount from line 23	27	807	1,205	1,209	1,561
28	If the amount on line 27 is zero, subtract line 25 from line 26. Otherwise, enter -0-	28		- 0 -	- 0 -	
29	Underpayment. If line 22 is equal to or more than line 27, subtract line 27 from line 22. Then go to line 24 of next column. Otherwise, go to line 30. . . ▶	29		9/2 598	1/12 246	4/15 653
30	Overpayment. If line 27 is more than line 22, subtract line 22 from line 27. Then go to line 24 of next column	30	398			

Section B—Figure the Penalty (Complete lines 31 through 36 of one column before going to the next column.)

		Rate Period Example 4.9				
		4/15/01	6/15/01	9/24/01	1/15/02	
Rate Period 1	April 16, 2001—June 30, 2001					
	31	Number of days from the date shown above line 31 to the date the amount on line 29 was paid or 6/30/01, whichever is earlier	Days: 31	Days: 15		
	32	Underpayment on line 29 (see page 4 of the instructions) × $\frac{\text{Number of days on line 31}}{365} \times .08$ ▶	\$	\$ 1.97		
Rate Period 2	July 1, 2001—December 31, 2001					
	33	Number of days from the date shown above line 33 to the date the amount on line 29 was paid or 12/31/01, whichever is earlier	Days: 33	Days: 64	Days: 98	
	34	Underpayment on line 29 (see page 5 of the instructions) × $\frac{\text{Number of days on line 33}}{365} \times .07$ ▶	\$	\$ 7.34	\$ 4.62	
Rate Period 3	January 1, 2002—April 15, 2002					
	35	Number of days from the date shown above line 35 to the date the amount on line 29 was paid or 4/15/02, whichever is earlier	Days: 35	Days: 12	Days: 90	
	36	Underpayment on line 29 (see page 5 of the instructions) × $\frac{\text{Number of days on line 35}}{365} \times .06$ ▶	\$	\$.49	\$ 9.66	
37	Penalty. Add all amounts on lines 32, 34, and 36 in all columns. Enter the total here and on Form 1040, line 71; Form 1040A, line 46; Form 1040NR, line 69; Form 1040NR-EZ, line 26; or Form 1041, line 26, but do not file Form 2210 unless you checked one or more of the boxes in Part I . . . ▶	37				\$ 24.08

5.

How To Get Tax Help

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

Contacting your Taxpayer Advocate. If you have attempted to deal with an IRS problem unsuccessfully, you should contact your Taxpayer Advocate.

The Taxpayer Advocate represents your interests and concerns within the IRS by protecting your rights and resolving problems that have not been fixed through normal channels. While Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that your case is given a complete and impartial review.

To contact your Taxpayer Advocate:

- Call the Taxpayer Advocate at **1-877-777-4778**.
- Call the IRS at **1-800-829-1040**.
- Call, write, or fax the Taxpayer Advocate office in your area.
- Call **1-800-829-4059** if you are a TTY/TDD user.

For more information, see Publication 1546, *The Taxpayer Advocate Service of the IRS*.

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



Personal computer. With your personal computer and modem, you can access the IRS on the Internet at www.irs.gov. While visiting our web site, you can:

- Find answers to questions you may have.
- Download forms and publications or search for forms and publications by topic or keyword.
- View forms that may be filled in electronically, print the completed form, and then save the form for recordkeeping.

- View Internal Revenue Bulletins published in the last few years.
- Search regulations and the Internal Revenue Code.
- Receive our electronic newsletters on hot tax issues and news.
- Get information on starting and operating a small business.

You can also reach us with your computer using File Transfer Protocol at ftp.irs.gov.



TaxFax Service. Using the phone attached to your fax machine, you can receive forms and instructions by calling **703-368-9694**. Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.

For help with transmission problems, call the FedWorld Help Desk at **703-487-4608**.



Phone. Many services are available by phone.

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

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

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



Walk-in. You can walk in to many post offices, libraries, and IRS offices to pick up certain forms, instructions, and publications. Some IRS offices, libraries, grocery stores, copy centers, city and county governments, credit unions, and office supply stores have an extensive collection of products available to print from a CD-ROM or photocopy from reproducible proofs. Also, some IRS offices and libraries have the Internal Revenue Code, regulations, Internal Revenue Bulletins, and Cumulative Bulletins available for research purposes.



Mail. You can send your order for forms, instructions, and publications to the Distribution Center nearest to you and receive a response within 10 workdays after your request is received. Find the address that applies to your part of the country.

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



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

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

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

IRS Publication 3207, *Small Business Resource Guide*, is an interactive CD-ROM that contains information important to small businesses. It is available in mid-February. You can get one free copy by calling **1-800-829-3676** or visiting the IRS web site at www.irs.gov.

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