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Understanding and Managing Your Estimated Taxes

What are Estimated Taxes? Estimated taxes are periodic payments that individuals are required to make to the IRS throughout the year to cover income that is not subject to withholding, such as self-employment income, rental income, investment income, and other sources. These payments help you avoid a large tax bill when you file your annual tax return.

Why Pay Estimated Taxes? The IRS expects taxpayers to pay taxes on their income as they earn it. If a significant portion of your income is not subject to withholding (e.g. self-employment income), making estimated tax payments ensures that you are meeting your tax obligations throughout the year. This helps you avoid penalties and interest on any underpayment when you file your tax return.

How to Pay Estimated Taxes:

You can make your estimated tax payments online using the IRS Electronic Federal Tax Payment System (EFTPS) or through the IRS Direct Pay option. Alternatively, you can mail your payments using the payment vouchers provided with Form 1040-ES.

A rule of thumb to avoid the penalty for underpayment of estimated tax is to pay in under the "safe harbor" provision, which is at least 90% of the tax due for the current year, or 100% of the tax due from the prior year, whichever is smaller. There are special rules if your adjusted gross income exceeds $150,000 (or $75,000 if married filing separately): you must pay the lower of 90% of the tax due for the current year or 110% of the tax due from the prior year.

Most states have similar thresholds for estimated taxes and online systems to accept payments. Alabama's Form 40ES can be used to determine your estimated tax liability. The state accepts payments at My Alabama Taxes and they mirror the thresholds above for safe harbor from the underpayment of estimated tax penalty.

IRS Website Resource: For more detailed information and guidance, you can refer to the IRS webpage on the basics of estimated taxes for individuals: IRS Estimated Taxes Basics. Additionally, you can use the Tax Withholding Estimator provided by the IRS to see if you are withholding adequately throughout the year.

If you have any questions or need assistance in calculating your estimated taxes, please feel free to reach out.

Best regards,

Himmelwright Huguley Boles, LLC

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