



# Tax Reduction Letter

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## Internal Revenue Code Section 6654

Failure by individual to pay estimated income tax.

(a) Addition to the tax. Except as otherwise provided in this section, in the case of any underpayment of estimated tax by an individual, there shall be added to the tax under chapter 1 and the tax under chapter 2 for the taxable year an amount determined by applying—

- (1) the underpayment rate established under section 6621,
- (2) to the amount of the underpayment,
- (3) for the period of the underpayment.

(b) Amount of underpayment; period of underpayment. For purposes of subsection (a)

(1) Amount. The amount of the underpayment shall be the excess of—

- (A) the required installment, over
- (B) the amount (if any) of the installment paid on or before the due date for the installment.

(2) Period of underpayment. The period of the underpayment shall run from the due date for the installment to whichever of the following dates is the earlier—

- (A) the 15th day of the 4th month following the close of the taxable year, or
- (B) with respect to any portion of the underpayment, the date on which such portion is paid.

(3) Order of crediting payments. For purposes of paragraph (2)(B), a payment of estimated tax shall be credited against unpaid required installments in the order in which such installments are required to be paid.

(c) Number of required installments; due dates. For purposes of this section—

- (1) Payable in 4 installments. There shall be 4 required installments for each taxable year.
- (2) Time for payment of installments.

In the case of the following required installments:

	The due date is:
1st .....	April 15
2nd .....	June 15

3rd ..... September 15  
4th ..... January 15 of the fol-  
lowing taxable year.

(d) Amount of required installments. For purposes of this section—

(1) Amount.

(A) In general. Except as provided in paragraph (2), the amount of any required installment shall be 25 percent of the required annual payment.

(B) Required annual payment. For purposes of subparagraph (A), the term 'required annual payment' means the lesser of—

(i) 90 percent of the tax shown on the return for the taxable year (or, if no return is filed, 90 percent of the tax for such year), or

(ii) 100 percent of the tax shown on the return of the individual for the preceding taxable year.

Clause (ii) shall not apply if the preceding taxable year was not a taxable year of 12 months or if the individual did not file a return for such preceding taxable year.

(C) Limitation on use of preceding year's tax.

(i) In general. If the adjusted gross income shown on the return of the individual for the preceding taxable year beginning in any calendar year exceeds \$ 150,000, clause (ii) of subparagraph (B) shall be applied by substituting the applicable percentage for '100 percent'. For purposes of the preceding sentence, the applicable percentage shall be determined in accordance with the following table:

If the preceding taxable year begins in:	The applicable percentage is:
1998.....	105
1999.....	108.6
2000.....	110
2001.....	112
2002 or thereafter.....	110

(ii) Separate returns. In the case of a married individual (within the meaning of section 7703) who files a separate return for the taxable year for which the amount of the installment is being determined, clause (i) shall be applied by substituting '\$ 75,000' for '\$ 150,000'.

(iii) Special rule. In the case of an estate or trust, adjusted gross income shall be determined as provided in section 67(e).

(D) Special rule for 2009.

(i) In general. Notwithstanding subparagraph (C), in the case of any taxable year beginning in 2009, clause (ii) of subparagraph (B) shall be applied to any qualified individual by substituting "90 percent" for "100 percent".

(ii) Qualified individual. For purposes of this subparagraph, the term "qualified individual" means any individual if—

(I) the adjusted gross income shown on the return of such individual for the preceding taxable year is less than \$ 500,000, and

(II) such individual certifies that more than 50 percent of the gross income shown on the return of such individual for the preceding taxable year was income from a small business. A certification under subclause (II) shall be in such form and manner and filed at such time as the Secretary may by regulations prescribe.

(iii) Income from a small business. For purposes of clause (ii), income from a small business means, with respect to any individual, income from a trade or business the average number of employees of which was less than 500 employees for the calendar year ending with or within the preceding taxable year of the individual.

(iv) Separate returns. In the case of a married individual (within the meaning of section 7703) who files a separate return for the taxable year for which the amount of the installment is being determined, clause (ii)(I) shall be applied by substituting "\$ 250,000" for "\$ 500,000".

(v) Estates and trusts. In the case of an estate or trust, adjusted gross income shall be determined as provided in section 67(e).

(2) Lower required installment where annualized income installment is less than amount determined under paragraph (1).

(A) In general. In the case of any required installment, if the individual establishes that the annualized income installment is less than the amount determined under paragraph (1)—

(i) the amount of such required installment shall be the annualized income installment, and

(ii) any reduction in a required installment resulting from the application of this subparagraph shall be recaptured by increasing the amount of the next required installment determined under paragraph (1) by the amount of such reduction (and by increasing subsequent required installments to the extent that the reduction has not previously been recaptured under this clause).

(B) Determination of annualized income installment. In the case of any required installment, the annualized income installment is the excess (if any) of—

(i) an amount equal to the applicable percentage of the tax for the taxable year computed by placing on an annualized basis the taxable income, alternative minimum taxable income, and adjusted self-employment income for months in the taxable year ending before the due date for the installment, over

(ii) the aggregate amount of any prior required installments for the taxable year.

(C) Special rules. For purposes of this paragraph—

(i) Annualization. The taxable income, alternative minimum taxable income, and adjusted self-employment income shall be placed on an annualized basis under regulations prescribed by the Secretary.

(ii) Applicable percentage.

In the case of the following required installments:	The applicable percentage is:
1st .....	22.5
2nd .....	45
3rd .....	67.5
4th .....	90.

(iii) Adjusted self-employment income. The term "adjusted self-employment income" means self-employment income (as defined in section 1402(b)); except that section 1402(b) shall be applied by placing wages (within the meaning of section 1402(b)) for months in the taxable year ending before the due date for the installment on an annualized basis consistent with clause (i).

(D) Treatment of subpart F and section 936 income.

(i) In general. Any amounts required to be included in gross income under section 936(h) or 951(a) (and credits properly allocable thereto) shall be taken into account in computing any annualized income installment under subparagraph (B) in a manner similar to the manner under which partnership income inclusions (and credits properly allocable thereto) are taken into account.

(ii) Prior year safe harbor. If a taxpayer elects to have this clause apply to any taxable year—

(I) clause (i) shall not apply, and

(II) for purposes of computing any annualized income installment for such taxable year, the taxpayer shall be treated as having received ratably during such taxable year items of income and credit described in clause (i) in an amount equal to the amount of such items shown on the return of the taxpayer for the preceding taxable year (the second preceding taxable year in the case of the first and second required installments for such taxable year).

(e) Exceptions.

(1) Where tax is small amount. No addition to tax shall be imposed under subsection (a) for any taxable year if the tax shown on the return for such taxable year (or, if no return is filed, the tax), reduced by the credit allowable under section 31, is less than \$ 1,000.

(2) Where no tax liability for preceding taxable year. No addition to tax shall be imposed under subsection (a) for any taxable year if—

(A) the preceding taxable year was a taxable year of 12 months,

(B) the individual did not have any liability for tax for the preceding taxable year, and

(C) the individual was a citizen or resident of the United States throughout the preceding taxable year.

(3) Waiver in certain cases.

(A) In general. No addition to tax shall be imposed under subsection (a) with respect to any underpayment to the extent the Secretary determines that by reason of casualty, disaster, or other unusual circumstances the imposition of such addition to tax would be against equity and good conscience.

(B) Newly retired or disabled individuals. No addition to tax shall be imposed under subsection (a) with respect to any underpayment if the Secretary determines that—

(i) the taxpayer—

(I) retired after having attained age 62, or

(II) became disabled,

in the taxable year for which estimated payments were required to be made or in the taxable year preceding such taxable year, and

(ii) such underpayment was due to reasonable cause and not to willful neglect.

(f) Tax computed after application of credits against tax. For purposes of this section, the term "tax" means—

(1) the tax imposed by chapter 1 (other than any increase in such tax by reason of section 143(m)), plus

(2) the tax imposed by chapter 2, minus

(3) the credits against tax provided by part IV of subchapter A of chapter 1, other than the credit against tax provided by section 31 (relating to tax withheld on wages).

(g) Application of section in case of tax withheld on wages.

(1) In general. For purposes of applying this section, the amount of the credit allowed under section 31 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each due date for such taxable year, unless the taxpayer establishes the dates on which all amounts were actually withheld, in which case the amounts so

withheld shall be deemed payments of estimated tax on the dates on which such amounts were actually withheld.

(2) Separate application. The taxpayer may apply paragraph (1) separately with respect to—

(A) wage withholding, and

(B) all other amounts withheld for which credit is allowed under section 31.

(h) Special rule where return filed on or before January 31. If, on or before January 31 of the following taxable year, the taxpayer files a return for the taxable year and pays in full the amount computed on the return as payable, then no addition to tax shall be imposed under subsection (a) with respect to any underpayment of the 4th required installment for the taxable year.

(i) Special rules for farmers and fishermen. For purposes of this section—

(1) In general. If an individual is a farmer or fisherman for any taxable year—

(A) there shall be only 1 required installment for the taxable year,

(B) the due date for such installment shall be January 15 of the following taxable year,

(C) the amount of such installment shall be equal to the required annual payment determined under subsection (d)(1)(B) by substituting "66 2/3 percent" for "90 percent" and without regard to subparagraph (C) of subsection (d)(1), and

(D) subsection (h) shall be applied—

(i) by substituting "March 1" for "January 31", and

(ii) by treating the required installment described in subparagraph (A) of this paragraph as the 4th required installment.

(2) Farmer or fisherman defined. An individual is a farmer or fisherman for any taxable year if—

(A) the individual's gross income from farming or fishing (including oyster farming) for the taxable year is at least 66 2/3 percent of the total gross income from all sources for the taxable year, or

(B) such individual's gross income from farming or fishing (including oyster farming) shown on the return of the individual for the preceding taxable year is at least 66 2/3 percent of the total gross income from all sources shown on such return.

(j) Special rules for nonresident aliens. In the case of a nonresident alien described in section 6072(c):

(1) Payable in 3 installments. There shall be 3 required installments for the taxable year.

(2) Time for payment of installments. The due dates for required installments under this subsection shall be determined under the following table:

In the case of the following required installments:	The due date is:
1st .....	June 15
2nd .....	September 15
3rd .....	January 15 of the following taxable year.

(3) Amount of required installments.

(A) First required installment. In the case of the first required installment, subsection (d) shall be applied by substituting '50 percent' for '25 percent' in subsection (d)(1)(A).

(B) Determination of applicable percentage. The applicable percentage for purposes of subsection (d)(2) shall be determined under the following table:

In the case of the following required installments:	The applicable percentage is:
1st .....	45
2nd .....	67.5
3rd .....	90.

(k) Fiscal years and short years.

(1) Fiscal years. In applying this section to a taxable year beginning on any date other than January 1, there shall be substituted, for the months specified in this section, the months which correspond thereto.

(2) Short taxable year. This section shall be applied to taxable years of less than 12 months in accordance with regulations prescribed by the Secretary.

(l) Estates and trusts.

(1) In general. Except as otherwise provided in this subsection, this section shall apply to any estate or trust.

(2) Exception for estates and certain trusts. With respect to any taxable year ending before the date 2 years after the date of the decedent's death, this section shall not apply to—

(A) the estate of such decedent, or

(B) any trust—

(i) all of which was treated (under subpart E of part I of subchapter J of chapter 1) as owned by the decedent, and

(ii) to which the residue of the decedent's estate will pass under his will (or, if no will is admitted to probate, which is the trust primarily responsible for paying debts, taxes, and expenses of administration).

(3) Exception for charitable trusts and private foundations. This section shall not apply to any trust which is subject to the tax imposed by section 511 or which is a private foundation.

(4) Special rule for annualizations. In the case of any estate or trust to which this section applies, subsection (d)(2)(B)(i) shall be applied by substituting "ending before the date 1 month before the due date for the installment" for "ending before the due date for the installment".

(m) Special rule for Medicare tax. For purposes of this section, the tax imposed under section 3101(b)(2) (to the extent not withheld) shall be treated as a tax imposed under chapter 2.

(n) Regulations. The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section.