

# TAX REFUNDS—WHY YOU *DON'T* WANT THEM

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*The information contained herein is for educational use only and should not be construed as tax, financial, or legal advice. Each individual's situation is unique and may require specialized treatment. It is, therefore, imperative that you consult with tax and legal professionals prior to implementation of any strategies discussed.*

What—no check from the IRS?! You want *me* to pay them? Learn to calculate just what you owe; not a penny more! Should you use the annualized method to calculate your estimated tax liability? Should you make your 4<sup>th</sup> quarter payment in December? Should you send money with your request for a filing extension?



## I. Basic Tax Calculation

Form <b>1040</b> (See instructions on page 12.) Use the IRS label. Otherwise, please print or type. L A B E L  H E R E	Department of the Treasury—Internal Revenue Service <b>U.S. Individual Income Tax Return 2007</b>	IRS Use Only—Do not write or staple in this space. OMB No. 1545-0074
For the year Jan. 1–Dec. 31, 2007, or other tax year beginning _____, 2007, ending _____, 20		
Your first name and initial _____ Last name _____		Your social security number _____
If a joint return, spouse's first name and initial _____ Last name _____		Spouse's social security number _____
Home address (number and street). If you have a P.O. box, see page 12. _____ Apt. no. _____		▲ You must enter your SSN(s) above. ▲
City, town or post office, state, and ZIP code. If you have a foreign address, see page 12. _____		Checking a box below will not change your tax or refund.
Presidential Election Campaign <input type="checkbox"/> Check here if you, or your spouse if filing jointly, want \$3 _____		
<b>Filing Status</b> Check only one box.		
1 <input type="checkbox"/> Single 2 <input type="checkbox"/> Married filing jointly (even if only one spouse has income) 3 <input type="checkbox"/> Married filing separately (each spouse must file a separate return and full name and address must be shown)		

Income (Wages, Investments, Pensions, etc.)  
 – Adjustments (IRA contributions, Tuition, Moving expenses, etc.)

= Adjusted Gross Income (AGI)  
 – Deductions (Standard \$5,800 in 2011 or Itemized)  
 – Personal Exemptions (\$3,700 in 2011)

= Taxable Income

➔ Tax  
 + Alternative Minimum Tax (AMT)  
 – Non-refundable Credits (Child-care, Education, etc.)  
 + Additional Taxes (Self-employment, Household employee, etc.)

= Total Tax  
 – Prior Tax Payments (Withholdings, Estimated payments, Prior-year refund, etc.)  
 – Refundable Credits (Earned Income, Excess Social Security, etc.)

= Tax Due or Refund

**Monica Haven, E.A., J.D., L.L.M.**


1534 South Edris Drive \* Los Angeles, CA 90035 \* (310) 286-9161 \* FAX (310) 557-1626 \* e-mail: [mhaven@pobox.com](mailto:mhaven@pobox.com)

## II. Additional Amounts Due



### A. Penalties (IRC § 6651)

1. Late Filing (Failure to File)
  - 5% of unpaid balance for each month or part of a month the return is late (max. 25%)
  - If more than 60 days late, the minimum penalty is the lesser of \$100 or tax due
  - No penalty if the return shows a refund
  - If the taxpayer is subject to Failure to File and Failure to Pay Penalties for the same month, the Failure to File Penalty is reduced by the Failure to Pay Penalty
2. Late Payment (Failure to Pay)
  - 0.5% for each month or part of a month there is an unpaid balance (max. 25%)

 **TAX TIP:** Timely filing of the return or extension avoids the Late Filing Penalty, although Late Payment Penalty and interest may continue to accrue

### B. Interest –currently 3% for early 2011

- Applied to the underpaid amount for the number of days late at currently applicable rates
- Interest in *not* deductible on Schedule A

### C. Safe Harbor Rule

No Late Payment Penalty if:

- Tax due is < \$1,000, or
- Taxpayer had no tax liability on prior-year return that covered 12 months.
- 90% of the tax shown on current year return, or
- Payments equal 100% of the tax shown prior-year  
OR 110% of prior-year tax if AGI > \$150,000 (\$75,000 MFS)

### D. Abatement

- No Late Filing Penalty if reasonable cause rather than willful neglect, including:
  - Taxpayer's or immediate family member's death or serious illness
  - Unavoidable absence on the filing date
  - Destruction of residence or business
- No Late Payment Penalty if unable to pay despite exercise of ordinary care and prudence
- Interest only rarely abated, i.e. if due to IRS error; or an extension in a presidentially-declared disaster area; or on erroneous tax refunds (< \$50,000) required to be repaid

## III. Payments

### A. Withholdings

### B. Quarterly Payments

- Four equal installments to avoid a penalty
- Send checks payable to "US Treasury" with Form 1040-ES voucher to:

Internal Revenue Service Center  
P.O. Box 510000  
San Francisco, CA 94151



- If installment is paid late, penalty is charged for the number of days the payment is late
- Interest is charged but is not compounded
- A 4<sup>th</sup> quarter payment is not required if the return is filed and tax is paid by January 31<sup>st</sup>

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- A taxpayer who underpays an installment cannot avoid the penalty by overpaying the next installment. (In contrast, an employee who has insufficient withholding mid-year can eliminate an underpayment penalty by increasing withholding for the remainder of the year.)
- ☞ **TAX TIP:** Front-load estimated tax payments—by overpaying in early quarters excess can be automatically “rolled-over” to next quarter



**NOTE:** California now requires front-loading: 30% in Q1, 40% in Q2, 0% in Q3, 30% in Q4

C. Form 2210: Underpayment of Estimated Tax

- Not required to be filed with the return unless exception claimed [see § III.D below]
- IRS will calculate the penalty and bill the taxpayer
- No interest is charged on the penalty if the return was filed by the due date and the penalty is paid by the date specified on the bill

D. Exceptions to Penalty

1. Casualty, disaster or other unusual circumstance, such as becoming disabled after age 62
2. Annualized Income Installment Method
  - Quarterly payments can be calculated based on actual income in each quarter
  - Under this method, your required installment for one or more payment periods may be less than one-fourth of your required annual payment.

☞ **TAX TIP:** Use if income was higher in later quarters since this method will reduce the required quarterly payments at the beginning of the year
3. Using Actual Payment Dates for Withholding From Wages
  - Withholding from wages is considered to have been paid in 4 equal installments but taxpayer can elect to apply withholding to the quarter it was actually paid

☞ **TAX TIP:** Use if a large amount of tax was withheld at the beginning of the year
4. Switch from or to Joint Return
  - If a taxpayer is switching from a joint to an individual return, the prior-year tax used to calculate the required annual payment is the taxpayer’s separate liability
  - If taxpayers are filing jointly in the current year, they must use their combined prior-year tax to calculate the required annual payment

IV. Payments

A. Due dates

Quarter	
1 <sup>st</sup>	April 18 <sup>th</sup> , 2011
2 <sup>nd</sup>	June 15 <sup>th</sup> , 2011
3 <sup>rd</sup>	September 15 <sup>th</sup> , 2011
4 <sup>th</sup>	January 16 <sup>th</sup> , 2012




B. Payment Options

1. e-Pay
  - Taxpayer must enroll with EFTPS at [www.eftps.com](http://www.eftps.com) or (800) 555-8778
  - Provide SS #, as well bank routing and account numbers at least day prior to due date
  - No charge by US Dept. of Treasury, but verify whether bank has processing fee

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 **TAX TIP:** To use EFTPS, you must enroll online about 3 weeks prior to payment deadline to give the IRS time to send PIN and enrollment trace number via mail before obtaining an internet password online.

2. Automatic Debit
  - Available through tax preparation software and tax professionals
3. Credit Card (VISA, MasterCard, American Express, Discover)
  - The IRS does not receive or charge any fees and will not reimburse fees to taxpayers
  - Fees are non-deductible personal expenses or deductible business expenses

Service Provider	Telephone	Web Site	Convenience Fees (% of tax payment)	Customer Service
Official Payments Corporation	1-800-2PAY-TAX (1-800-272-9829)	<a href="http://officialpaymentsdebit.com">officialpaymentsdebit.com</a>	2.49%	1-877-754-4413
LINK2GOV Corporation	1-888-PAY1040 (1-888-729-1040)	<a href="http://pay1040.com">pay1040.com</a>	2.49%	1-888-658-5465

#### V. Options for Taxpayers Unable to Pay Tax Due

- A. Pay late
  - Pay as much as possible with return or extension and pay balance when billed by IRS
  - Cost: Interest at federal rate plus late payment penalty of 0.5% monthly
- B. Pay by credit card
  - Cost: Percentage of tax as a convenience fee plus interest at the credit card rate
- C. Installment Agreement (Form 9465)
  - Generally approved by IRS if the unpaid liability is  $\leq$  \$25,000 and tax will be paid within 5 years
  - If an installment agreement from a prior year is in effect, request consolidation
  - Failure to make a required payment may void agreement
  - Cost: Late Payment Penalty and interest on unpaid balance continue to accrue  
\$105 user fee is charged to establish agreement; \$52 if using direct debit to pay  
Interest and late payment penalties continue to accrue
- D. Extension of Time to Pay
  - Form 1127 Application for Extension of Time for Payment of Tax for six-month extension
  - Taxpayer must show that he cannot sell assets or borrow to pay the tax except under terms that would cause severe loss and undue hardship
  - Cost: If approved, the Late Payment Penalty is waived but interest continues to accrue



#### VI. Over-payments

- Refunds under \$1 will only be refunded on written request
- All or part of the refund may be used to pay certain debts such as student loans or state tax judgments
- Refund can be applied to next year's tax liability
- State tax refund is taxable on federal return if Schedule A was filed in prior year
- Refund can be automatically deposited to taxpayer's bank account
- Refund status can be checked by clicking "Where's My Refund?" at [www.irs.gov](http://www.irs.gov)
- Interest paid by the IRS is compounded daily beginning 45 days after the later of the original due date or the actual filing date—no interest is paid for the period prior to the filing date for late filed returns
- Interest on overpayments of estimated taxes begins to accrue only after the due date of the return
- Interest will be calculated at 5% (in Q3 of 2008) [adjusted quarterly] and is taxable

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