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Estimating answers to calculations

We employ a variety of estimation methods as dictated by the type of outcome variables examined. For the continuous variable measuring the percent of time employed since leaving school, we are able to use ordinary least squares (OLS). For the dichotomous variables alcohol abuse or dependence, used drugs in the past month, ever in poverty between ages 25-29, and ever on welfare between ages 21-33, we employ logistic regressions. In the case of marriage and fertility outcomes, where there are multiple combinations of a single outcome variable, we estimate a multinomial logistic. The variables, "number of years in poverty" and "number of years on welfare," are count variables that are estimated using a negative binomial regression. Finally, to estimate the time since leaving school that is needed to acquire a steady job (lasting at least two years) requires estimating a survivor function which we approximate with the Weibull distribution. A more detailed description of the estimation methods is included in Appendix A. What is important is the interpretation of the values reported from these regressions. They fall into two categories: marginal effects and odds ratios. We report marginal effects for OLS, negative binomial, and Weibull regressions. For each of these methods, the marginal effect measures the change in the outcome variable for a unit change in an explanatory variable. In the case of a categorical variable, each marginal effect is relative to the effect of an omitted category. For example, we divide age of initiation into four categories. In the regressions, initiation between ages 11-15 is omitted and serves as the reference category. Odds ratios are reported for logistic and multinomial logistic regressions. Odds ratios measure the relative probability of the estimated outcome among one group relative to the reference group. The choice of reference group is the same across all types of estimations. Odds ratios for multinomial logistics are difficult to interpret because there are multiple equations. As an alternative we create predicted values for each outcome combination for each category of the relevant explanatory variable. Thus, we would have a predicted probability of observing each of the six adult family formation outcomes given each of the four age of initiation categories. Companies can induce higher sales revenue by offering customers a short time period to pay for goods and services. This creates accounts receivable, an asset that indicates a company expects to receive cash in an upcoming time period. Though sound in principle, not every customer will pay the money owed to a company. This failure to pay accounts receivable leads companies to declare the expected uncollectible accounts receivable. A common method is the percent of credit sales that determines total uncollectible accounts. Review the previous year’s general ledger. Calculate the total credit sales by adding up all sales involving accounts receivable. Look at the final income statement from the previous year to determine the amount of bad debts expense. This is the total accounts receivables written off as uncollectible. Divide the total bad debts expense by total credit sales. This percentage is the expected bad debts expense for upcoming periods. For example, if total bad debts was $1,000 and total credit sales was $10,000, then the expected bad debts is 10 percent, since $1,000 / $10,000 = .10 = 10 percent (multiply be 100 to get a percentage). Multiply current credit sales from the percentage in Step 4 to estimate current uncollectible accounts receivable. If current credit sales is $15,000, then the estimated uncollectible accounts receivable is $1,500, since $15,000 * .10 = $1,500. Photo credit: ©iStock.com/VeniThe federal personal income tax that is administered by the Internal Revenue Service (IRS) is the largest source of revenue for the U.S. federal government. Nearly all working Americans are required to file a tax return with the IRS each year. In addition to this, most people pay taxes throughout the year in the form of payroll taxes that are withheld from their paychecks.Income taxes in the U.S. are calculated based on tax rates that range from 10% to 37%. Taxpayers can lower their tax burden and the amount of taxes they owe by claiming deductions and credits.A financial advisor can help you understand how taxes fit into your overall financial goals. Financial advisors can also help with investing and financial plans, including retirement, homeownership, insurance and more, to make sure you are preparing for the future.Calculating Income Tax RateThe United States has a progressive income tax system. This means there are higher tax rates for higher income levels. These are called “marginal tax rates," meaning they do not apply to total income, but only to the income within a specific range. These ranges are called brackets.Income falling within a specific bracket is taxed at the rate for that bracket. The table below shows the tax brackets for the federal income tax, and it reflects the rates for the 2020 tax year, which are the taxes due in early 2021.Single FilersTaxable IncomeRate$0 - $9,87510%$9,875 - $40,12512%$40,125 - $85,52522%$85,525 - $163,30024%$163,300 - $207,35032%$207,350 - $518,40035%$518,400+37%Married, Filing JointlyTaxable IncomeRate$0 - $19,75010%$19,750 - $80,25012%$80,250 - $171,05022%$171,050 - $326,60024%$326,600 - $414,70032%$414,700 - $622,05035%$622,050+37%Married, Filing SeparatelyTaxable IncomeRate$0 - $9,87510%$9,875 - $40,12512%$40,125 - $85,52522%$85,525 - $163,30024%$163,300 - $207,35032%$207,350 - $311,02535%$311,025+37%You’ll notice that the brackets vary depending on whether you are single, married or a head of household. These different categories are called filing statuses. Married persons can choose to file separately or jointly. While it often makes sense to file jointly, filing separately may be the better choice in certain situations.Based on the rates in the table above, a single filer with an income of $50,000 would have a top marginal tax rate of 22%. However, that taxpayer would not pay that rate on all $50,000. The rate on the first $9,875 of taxable income would be 10%, then 12% on the next $30,250, then 22% on the final $9,875 falling in the third bracket. This is because marginal tax rates only apply to income that falls within that specific bracket. Based on these rates, this hypothetical $50,000 earner owes $6,790, which is an effective tax rate of about 13.6%.Calculating Taxable Income Using Exemptions and DeductionsOf course, calculating how much you owe in taxes is not quite that simple. For starters, federal tax rates apply only to taxable income. This is different than your total income, otherwise known as gross income. Taxable income is always lower than gross income since the U.S. allows taxpayers to deduct certain income from their gross income to determine taxable income.To calculate taxable income, you begin by making certain adjustments from gross income to arrive at adjusted gross income (AGI). Once you have calculated adjusted gross income, you can subtract any deductions for which you qualify (either itemized or standard) to arrive at taxable income.Note that there are no longer personal exemptions at the federal level. Prior to 2018, taxpayers could claim a personal exemption, which lowered taxable income. The new tax plan signed by President Trump in late 2017 eliminated the personal exemption, though.Deductions are somewhat more complicated. Many taxpayers claim the standard deduction, which varies depending on filing status, as shown in the table below.Filing StatusStandard Deduction AmountSingle$12,400Married, Filing Jointly$24,800Married, Filing Separately$12,400Head of Household$18,650Some taxpayers, however, may choose to itemize their deductions. This means subtracting certain eligible expenses and expenditures. Possible deductions include those for student loan interest payments, contributions to an IRA, moving expenses and health-insurance contributions for self-employed persons. The most common itemized deductions also include:Deduction for state and local taxes paid - Also known as the SALT deduction, it allows taxpayers to deduct up to $10,000 of any state and local property taxes plus either their state and local income taxes or sales taxes.Deduction for mortgage interest paid - Interest paid on the mortgages of up to two homes, with it being limited to your first $1 million of debt. Homes purchased after Dec. 15, 2017 have this lowered to the first $750,000 of the mortgage.Deduction for charitable contributionsDeduction for medical expenses that exceed 7.5% of AGIKeep in mind that most taxpayers don’t itemize their deductions. If the standard deduction is larger than the sum of your itemized deductions (as it is for many taxpayers), you'll receive the standard deduction.Once you have subtracted deductions from your adjusted gross income, you have your taxable income. If your taxable income is zero, that means you do not owe any income tax.How to Calculate Federal Tax Credits©iStock.com/PgiamUnlike adjustments and deductions, which apply to your income, tax credits apply to your tax liability, which means the amount of tax that you owe.For example, if you calculate that you have tax liability of $1,000 based on your taxable income and your tax bracket, and you are eligible for a tax credit of $200, that would reduce your liability to $800. In other words, you would only owe $800 to the federal government.Tax credits are only awarded in certain circumstances, however. Some credits are refundable, which means you can receive payment for them even if you don’t owe any income tax. By contrast, nonrefundable tax credits can reduce your liability no lower than zero. The list below describes the most common federal income tax credits.The Earned Income Tax Credit is a refundable credit for taxpayers with income below a certain level. The credit can be up to $6,660 per year for taxpayers with three or more children, or lower amounts for taxpayers with two, one or no children.The Child and Dependent Care Credit is a nonrefundable credit of up to $3,000 (for one child) or $6,000 (for two or more children) related to childcare expenses incurred while working or looking for work.The Adoption Credit is a nonrefundable credit equal to certain expenses related to the adoption of a child.The American Opportunity Tax Credit is a partially refundable credit of up to $2,500 per year for enrollment fees, tuition, course materials and other qualified expenses for your first four years of post-secondary education.There are numerous other credits, including credits for the installation of energy-efficient equipment, a credit for foreign taxes paid and a credit for health insurance payments in some situations.Calculating Your Tax RefundPhoto credit: ©iStock.com/ShaneKatoWhether or not you get a tax refund depends on the amount of taxes you paid during the year. This is because they were withheld from your paycheck. However, it also depends on your tax liability and whether or not you received any refundable tax credits.When you file your tax return, if the amount of taxes you owe (your tax liability) is less than the amount that was withheld from your paycheck during the course of the year, you will receive a refund for the difference. This is the most common reason people receive a tax refund.If you paid no taxes during the year and owe no taxes, but are eligible for one or more refundable tax credits, you will also receive a refund equal to the refundable amount of the credits.Paying Your TaxesIf you aren’t getting a tax refund and instead owe money come tax day, there may be a way to lessen the sting. For starters, you should still file your taxes on time. Otherwise, you will also have to pay a fee for filing late.If you don’t think you can afford your full tax bill, then you should pay as much as you can and contact the IRS. The agency may be able to offer you a few payment options to help you pay off your bill. For example, the IRS may offer a short-term extension or temporarily delay collection. You may also have the option to pay your remaining bill over multiple installments. You will likely still pay any interest charges on overdue balances, but in some cases, the IRS may even waive penalties or fees. Again, you should call the agency at the number above to discuss your options.As you pay your tax bill, another thing to consider is using a tax-filing service that lets you pay your taxes by credit card. That way you can at least get valuable credit card rewards and points when you pay your bill. The IRS has authorized three payment processors to collect tax payments by credit card: PayUSAtax, Pay1040 and OfficialPayments. However, it’s important to keep in mind that all three processors charge fees of nearly 2% of your payment for credit card transactions. Double check that any rewards you earn are worth that extra cost, though.The cheapest way to pay a tax bill is still via a check or via IRS Direct Pay, which allows you to pay your bill directly from a savings or checking account. All major tax filing services will provide you with instructions for both of these payment options.State and Local Income TaxesMany states, as well as some cities and counties, have their own income taxes. These are collected in addition to the federal income tax. States that have a state income tax require that you file a separate state tax return, as they have their own rules. If you're curious about a particular state’s tax system and rules, visit one of our state tax pages.Photo credits: ©iStock.com/Veni, ©iStock.com/Pgiam, ©iStock.com/ShaneKato Benefit estimates depend on your date of birth and on your earnings history. For security, the "Quick Calculator" does not access your earnings record; instead, it will estimate your earnings based on information you provide. So benefit estimates made by the Quick Calculator are rough. Although the "Quick Calculator" makes an initial assumption about your past earnings, you will have the opportunity to change the assumed earnings (click on "See the earnings we used" after you complete and submit the form below). Lots of business owners get caught with tax surprises at startup or when they begin to make a profit. The surprise comes because they don't realize they must pay estimated taxes on their business income. Learn how to do a quick general calculation to find out how much you might have to pay in estimated taxes and when you are required to file. If your business is in Texas or another area where FEMA issued a disaster declaration due to winter storms in 2021, the IRS has extended the filing and payment deadlines for estimated taxes April 15, 2021, to June 15, 2021. You are probably a small business owner paying taxes as a sole proprietor, LLC owner, or partner. In these cases, you must pay your business income taxes through your personal tax return. This is called "pass-through taxation." Let's say you make a profit this year in your business. If you were an employee, you would have payroll tax deductions for income taxes due on your income (business and personal). But as a business owner, you aren't an employee, so no taxes on your income from the business are taken out. You are also required to pay Social Security and Medicare taxes on your business income. The combination of income taxes and Social Security/Medicare taxes on your business income is called "self-employment taxes." Your payments to yourself as an owner are considered an owner's draw, not a salary, and taxes haven't been withheld the way they would be from an employee's paycheck. This is where estimated taxes come in. You must pay quarterly estimated tax to avoid penalties and interest on late payments. When you consider whether you must pay estimated taxes, you'll need to look at all of your income for the tax year, including any income from employment (not as a business owner), capital gains, and dividends. The IRS says you don't have to pay estimated taxes if you meet all three of these conditions: You had no tax liability for the previous year, You were a U.S. citizen or resident for the entire year, and Your previous tax year was for a full 12 months. You must pay estimated taxes if: (a) You owe $1,000 or more for the year ($500 for corporations), over the amount of withholding from any salary as an employee or refundable credits, or (b) Your total withholding and refundable credits are: Less than 90% of the tax shown on your current year's tax return, or Less than 100% of the tax shown on your previous year's tax return. If you don't pay enough through withholding and timely estimated tax payments, you may be charged a penalty. You may also be charged a penalty if your estimated tax payments are late, even if you got a refund. Payments are due four times a year: 1st payment – April 15 (except for 2021 payments due June 15) 2nd payment – June 15 3rd payment – September 15 4th payment – January 15 of the next year. If your income is steady throughout the year, you can divide your payments up into four equal payments. If your business is seasonal, or you have a change in your business income, you may have to make smaller or larger payments in one or more quarters. You can use the quarterly vouchers included in IRS Form 1040-ES to make these payments. If you use a tax preparer or tax preparation software to prepare your tax return, they will include an estimated tax calculation and copies of vouchers. You must make the payments yourself in one of three ways: Mailing in the payment with the voucher Paying online using IRS Direct Pay, your credit or debit card, or one of the other IRS payment options By phone See IRS Form 1040-ES for copies of vouchers and details on these and other payment methods. You can make additional estimated tax payments to make up for a quarter with more income, and you can also make your estimated payments weekly, bi-weekly, or monthly, as long as you have paid enough by the quarterly due date. It's easier to make these payments online, through one of the IRS-approved payment methods. To calculate estimated business taxes from Schedule C you will need to combine this business income with information on other income, tax withholding, deductions, and credits on your personal tax return. You will also need to calculate self-employment tax (Social Security/Medicare taxes for business owners) and include self-employment taxes in determining estimated taxes due. When you estimate your taxes for the year, include all sources of income in addition to your business income and self-employment tax, including: Salary Tips Pension Dividends Alternative minimum tax Winnings, prizes and awards Interest and capital gains Here is a list of the information you will need: An estimate of your business income for the tax year. You can use your income from previous years, or take your income up to the current date and estimate income for the rest of the year. An estimate of business expenses for the year, using previous years as a guideline or using year-to-date expenses and projecting them through the end of the year. Because your estimated taxes depend on your personal tax situation, you will need to include personal income, deductions, credits, exemptions, and any withholding of federal income taxes from your personal income. In the same way as business income and expenses, you can use information from prior tax returns or use year-to-date and project to the end of the year. You can calculate your estimated tax payments by asking your tax preparer to run an estimate, by using the IRS estimated tax calculation worksheet, or by getting a rough estimate from your previous year's return prepared with tax software: You can use the estimated tax calculation worksheet provided by the IRS on Form 1040-ES or using the worksheets included in Publication 505. Corporations usually use Form 1120-W to calculate their estimated tax. Use tax preparation software to run a rough calculation of estimated taxes for the next year. If you use the same software every year, you can start with last year's return for information. The tax software includes self-employment taxes. If your business and personal income are fairly steady from year to year, it provides a rough estimate for tax planning purposes. Be sure your tax preparation software is the small business or self-employed version. Before you buy, check to be sure it includes Schedule C and Schedule SE (for self-employment taxes). Business tax return versions are usually for a specific business type, like partnerships, corporations, and S corporations. Owners of partnerships, LLCs, and S corporations are not employees of the business. They receive payments periodically from the business, and these payments are added to their personal tax returns. These payments are not subject to withholding, so estimated taxes may need to be paid. To calculate estimated tax payments, use the process described above. The information contained in this article is not tax or legal advice and is not a substitute for such advice. State and federal laws change frequently, and the information in this article may not reflect your own state’s laws or the most recent changes to the law. For current tax or legal advice, please consult with an accountant or an attorney.