

2021 TAX GUIDE

How to Prepare for Tax Season

Presented by Michelle Werth, AWMA®

In this guide, we'll explore ways to help you prepare for the upcoming tax season.

Keep in mind, this guide is for informational purposes only and is not a replacement for real-life advice, so make sure to consult your tax, legal, and accounting professionals before modifying your strategy.

April 15, 2021 is the deadline the Internal Revenue Service sets for filing your 2020 tax returns. If you believe you will miss that deadline, you should consider filing for an extension.

Here's a quick summary of the major changes for 2020:^{1,2}

- Each of the tax brackets will see an increase.
- The deduction limit restrictions will increase for traditional IRAs.
- A rise in income limits for Roth IRA contributions.
- Contribution limits increase for employer-sponsored plans.
- A rise in standard deductions for every filing status
- A rise in limits for HSA contributions.
- A rise in estate tax exemption limits.
- No required minimum distributions (RMDs) for 2020

Remember, if you spend your Health Savings Account funds on nonmedical expenses before age 65, you may be required to pay ordinary income tax as well as a 20% penalty. After age 65, you may be required to pay ordinary income taxes on HSA funds used for nonmedical expenses. HSA contributions are exempt from federal income tax; however, they are not exempt from state taxes in certain states.

The Tax Brackets

The tax brackets are: 10%, 12%, 22%, 24%, 32%, 35%, and 37%. Here are the tax brackets and the corresponding income ranges.³

2020 Tax Rate	Single	Married Filing Jointly
10%	\$0 to \$9,875	\$0 to \$19,750
12%	\$9,876 to \$40,125	\$19,751 to \$80,250
22%	\$40,126 to \$85,525	\$80,251 to \$171,050
24%	\$85,526 to \$163,300	\$171,051 to \$326,600
32%	\$163,301 to \$207,350	\$326,601 to \$414,700
35%	\$207,351 to \$518,400	\$414,701 to \$622,050
37%	\$518,401+	\$622,051+

These new rates are scheduled to expire in 2025 unless Congress acts to make them permanent. Exemptions also changed under the new tax code.

Here is an overview of the standard deductions:²

Tax Year	2019	2020
Single	\$12,200	\$12,400
Married filing jointly	\$24,400	\$24,800
Married filing separately	\$12,200	\$12,800
Head of household	\$18,350	\$18,650

The higher standard deductions may make it more attractive (compared to itemizing) for many taxpayers. Taxpayers who had itemized, to take advantage of deductions for high mortgage interest, large charitable donations, or local taxes, may be unable to reach the standard deduction's higher limit.

How to Prepare

While the tax deadlines for tax year 2019 were adjusted to account for issues related to the COVID-19 pandemic, the filing dates in 2021 have not been changed as of this writing. You should begin preparing early to avoid any unforeseen challenges.⁴

Get a checkup: As a starter, the I.R.S. urges taxpayers to conduct paycheck checkups. The agency provides tools and resources to help you calculate the correct amount to have withdrawn from your paycheck.

The calculator is designed to help you determine if your employer is withholding adequate amounts from your paycheck.

The calculator asks for your projected gross income, your current withholding number, the current amount of federal taxes withheld, and other paycheck-related questions.⁵

The calculator leads you through various screens that require you to enter requested numbers into boxes. The calculator looks similar to a tax-filing form.

Once the calculator generates the estimated taxes, which you'll either owe or be refunded, it offers suggestions on how to change your withholding amount or request to get additional money withheld from your check.

To avoid headaches, mark your calendar with the following key dates^{8,9}:

April 15, 2021

2020 INDIVIDUAL TAX RETURNS DUE

Most taxpayers have until April 15 to file tax returns.

INDIVIDUAL TAX RETURN EXTENSION FORM DUE

If you can't file your taxes on time, file your request for an extension by April 15 to push your deadline back to October 15, 2021.

1ST QUARTER 2020 ESTIMATED TAX PAYMENT DUE

Pay your first estimated tax payment for 2021 by April 15.

LAST DAY TO MAKE A 2020 IRA CONTRIBUTION

If you haven't already contributed fully to your retirement account for 2020, April 15 is your last chance to fund a Traditional IRA or a Roth IRA; however, if you received a filing extension, you have until October 15 to contribute to a Keogh or SEP plan.

June 15, 2021

2ND QUARTER 2021 ESTIMATED TAX PAYMENT DUE

Pay your second estimated tax payment for 2021 by June 15.

September 15, 2021

3RD QUARTER 2020 ESTIMATED TAX PAYMENT DUE

Pay your third estimated tax payment for 2021 by September 15.

October 15, 2021

EXTENDED INDIVIDUAL TAX RETURNS DUE

If you received an extension, you have until October 15 to file your 2020 tax return.

January 15, 2022

4TH QUARTER 2021 ESTIMATED TAX PAYMENT DUE

If you are self-employed or have other fourth-quarter income that requires you to pay quarterly estimated taxes, postmark this payment by January 15, 2022.

If the calculator shows that you are expected to owe taxes at the end of the year, you might consider filing a new Form W-4, Employee's Withholding Allowance Certificate.^{6,7} The I.R.S.-provided calculator is designed to give feedback based on certain assumptions. It is not intended to give specific tax, legal, or accounting advice.

The calculator is not a replacement for real-life advice, so please make sure to consult a professional before modifying your tax strategy.

Advice may include changing the number of allowances you're claiming (line 5) or requesting your employer withhold additional money (line 6).

Taxpayers who receive pension income may use Form W-4P.⁷ Once completed, send the form to your payer if you're adjusting or making changes.

What Do You Need to Have to Use the Calculator?

To generate a calculation, the I.R.S. recommends you have these documents:

- A recent paystub
- A recent income tax return
- A copy of a completed Form 1040, which will help you estimate your income

The calculator will not request you provide personal or private information. It will, however, ask you the number of children you expect to claim for the Child Tax Credit and the Earned Income Tax Credit.

Taxpayers with more complex tax issues may follow the instructions in Publication 505, Tax Withholding and Estimated Tax.⁷

Who Should Use the Calculator?

The I.R.S. urges taxpayers who have questions or concerns about changes in the tax code to use the calculator.

Specifically, the agency advises you to check your withholding if you:

- Have a two-income household.
- Have two or more jobs.
- Work only part of the year.
- Can claim child tax and other credits.
- Have dependents who are 17 and older.
- Itemized your deductions last year.
- Are a high earner or have a complex tax return.
- Received a large tax refund or paid a large tax bill.

Looking at Itemizing

The I.R.S. has revamped the way itemized deductions can be claimed on Schedule A. Schedule A is a separate tax form attached to standard 1040 forms.⁸

Changes to the itemized deductions for 2020 include:

- Itemized deductions are not limited if your adjusted gross income (AGI) exceeds a certain amount. Your adjusted gross income is the portion of your income that is taxable.
- Total deductions from state and local income, sales, and property taxes are limited to \$10,000. It's \$5,000 if you're married and filing separately.
- Job-related and other miscellaneous expenses – that were subject to the 2% AGI limit – can no longer be deducted.
- Certain other expenses, such as gambling losses, can still be deducted.
- Deductions for the interest on mortgage debt – incurred after December 15, 2017 – are limited to up to \$750,000 of the home's loan amount.
- The cash charity contribution limit is 60% of your AGI.

Other changes in deductibles include:

You may no longer deduct moving expenses unless you're on active duty in the U.S. military.

The Child Tax Credit rose to \$2000 per qualifying child. The refundable portion of the credit (referred to as the additional child tax credit) is limited to \$1,400 and applies when taxpayers are unable to fully use the \$2,000 nonrefundable tax credit

to offset their taxes. The credits phase out at income thresholds of \$200,000 or \$400,000 for married taxpayers filing jointly.⁹

The tax code established a tax credit of up to \$500 for other dependents who may not qualify for the child tax credit. Children who you plan to claim as dependents must have Social Security numbers prior to the due date of your tax return. Children who don't have Social Security numbers, but have individual taxpayer identification numbers, may be claimed under the new credit for other dependents.

Preparing for the Tax Season

Here are a few reasons why you may want to consider preparing early:

- Your home, job, or relationships changed in 2020.
- You need to start saving money if you think you may owe taxes.
- You want to ensure you qualify for tax deductions.

You can make changes throughout the year to ensure your tax preparations go smoothly.

Specifically, you can make periodic assessments of your paycheck withholdings, so that you'll get a refund or reduce or eliminate your tax burden.

You should keep track of and store your tax and other financial records to avoid delays or frantic preparations as the filing deadline approaches. Records may include W-2 forms, canceled checks, certain receipts, and previous year returns.

Items to Remember

Here is a list of other items to start gathering:¹⁰

- Pay stubs
- Mortgage payment records
- Closing paperwork on home purchases
- Receipts for items or services you may want to claim as itemized deductions
- Records on charitable giving and donations
- Mileage logs on cars used for business
- Business travel receipts
- Credit card and bank statements to verify deductions
- Medical bills
- 1099-G forms for state and local taxes
- 1099 forms for dividends or other income

During the first three months of 2021, make sure you receive your W-2 and 1099 forms as well as other tax documents. Leave adequate time to collect documents and prepare to file your taxes prior to the April 15, 2021 deadline.

Capital losses: You can claim losses only if they exceed capital gains. You're

allowed to claim the difference up to \$3,000 per year if you're married filing jointly or \$1,500 if you're filing separate returns. Net losses that exceed \$3,000 can be carried over into future years.¹¹

Deductions for capital losses can only be applied to investment property sales, but not the sale of investment property that was held for personal use.

Get organized: Find a place to store your tax documents until it's time to prepare to file. A good record-keeping system may alleviate concerns later as the deadline gets closer.

If you have your documents or prior-year returns stored on your computer, make sure you back them up on a thumb drive or other device or system in case your computer is hacked or stolen.

How Long?

The I.R.S. provides recommended timelines for retaining financial documents:¹²

1. You should keep your tax records for three years if item number 4 (below) does not apply to you.
2. You should keep records for three years from your original filing date of your return (which is typically prior to the April 15 deadline) or two years from the date you paid your taxes. Select whichever is the later date. This is if you claimed a credit or refund after you filed your return.
3. You should keep your records for seven years if you claimed a loss from worthless securities or a bad-debt deduction.
4. You should keep your records for six years if you failed to report income that you should have and the income was more than 25% of the gross income listed on your return.
5. You should keep employment tax records for at least four years after the due date on the taxes or after you paid the taxes. Select whichever is later.

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