

Tax Dollars & Sense: Tax Basics

Brought to you by the Denver Asset Building Coalition (DABC)



Denver Asset Building Coalition

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DABC Guidelines

Income Requirements for Our Tax Preparation Services:

- **Single Filers, Married Filing Separately: \$35,000**
- **Married Filing Jointly, Head of Household, Widower: \$65,000**

What to Bring with You When You File:

- **Taxpayers:**
 - Photo ID
 - Social Security Card or Individual Taxpayer Identification Number (ITIN)
- **Dependents:**
 - Social Security Card or ITIN

Choosing a Filing Status:

Options (You can only choose 1):

- 1. Single**
- 2. Married Filing Jointly**
- 3. Married Filing Separately**
- 4. Head of Household**
- 5. Widower with Qualifying Dependent**

Married Filing Separately

Caution - This filing status has some major drawbacks:

- Must pay tax on all Social Security received if you lived with your spouse at any time during the year;
- Cannot claim Earned Income Credit;
- Cannot claim Education credits.

Possible Solutions:

- File jointly, if possible
- Finalize divorce decree

Standard Deduction versus Itemized Deductions

The Standard Deduction:

All United States residents who file a Form 1040 - Individual Income Tax return are eligible for the standard deduction.

This amount is used to reduce your taxable income. This means that you only pay tax on income that exceeds the standard deduction amount.

Standard Deduction versus Itemized Deductions, continued:

Standard Deduction for 2020:

- Single, Married Filing Separately: \$12,400
- Head of Household: \$18,650
- Married Filing Jointly, Qualifying Widower with dependent child: \$24,800

**Note: If married filing separately, if one spouse itemizes, the other must also do so.

Standard Deduction versus Itemized Deductions

Itemized Deductions: The alternative to the Standard Deduction is to itemize your deductions. Review IRS Tax Form 1040 - Individual Income Tax Return, Schedule A for a comprehensive list of allowable itemized deductions.

Common Examples of Itemized Deductions:

- Medical and dental expenses
- Taxes you paid
 - State and local income taxes
 - Real estate taxes
 - Personal property taxes
- Home mortgage interest
- Investment interest
- Charitable donations;
- Casualty theft and losses

Standard Deduction versus Itemized Deductions, continued:

Should you itemize your deductions or take the standard deduction?

It is your choice!

Taxpayers are free to choose the best option for them. To determine whether to take the Standard deduction or itemize your deduction, compute your itemized deductions.

If the allowable itemized deductions add up to more than the Standard Deduction, the taxpayer should itemize.

Credits:

There are a variety of credits available to some taxpayers, each with its own set of rules and eligibility requirements. We will cover the ones listed below, which are the most common, but other credits are also available for qualifying taxpayers.

- Earned Income Tax Credit (EITC, sometimes abbreviated as EIC)
- Child Tax Credit
- Credit for Other Dependents
- Child and Dependent Care Credit
- Retirement Savings Contributions Credit (Saver's Credit)
- Education Credits

Credits: Earned Income Tax Credit

General Rules:

- Must have earned income.
- Must be a US citizen or resident alien for entire tax year.
- Must have a valid Social Security number for yourself/spouse and any qualifying children on your return.
- Investment income must be less than \$3,650 for 2020 (adjusted each year).
- Cannot have foreign earned income.
- Cannot be filing Married Filing Separately.
- Cannot be claimed as a dependent on another person's return.
- Age Range: At least age 25 by December 31st of the tax year, and age 64 or younger on December 31st of the tax year.
- This is a refundable credit.

Credits: Earned Income Tax Credit, continued:

Qualifying Child Rules:

1. Social Security Number: Child must have a valid Social Security Number.
2. Relationship Test: Must be son, daughter, stepchild, foster child, brother, sister, stepbrother, or descendant of any of these individuals. Adopted children are always treated as your own children.
3. Residence Test: Child must live with you for more than half of the year.
4. Age Test: Child must be under the age of 19 on December 31st of the tax year, or be a full time student and under the age of 24 on December 31st of the tax year.

Credits: Earned Income Tax Credit, continued:

Maximum Income Levels & Credit Amounts for Tax Year 2020:

No Dependents:

\$15,820 for Single, Head of Household or Widowed

\$21,710 for Married Filing Jointly

Maximum Credit Amount: \$538

One Dependent:

\$41,756 for Single, Head of Household or Widowed

\$47,646 for Married filing Jointly

Maximum Credit Amount: \$3,584

Credits: Earned Income Tax Credit, continued:

Maximum Income Levels & Credit Amounts for Tax Year 2020, continued:

Two Dependents:

\$47,440 for Single, Head of Household or Widowed

\$53,330 for Married Filing Jointly

Maximum Credit Amount: \$5,920

Three Dependents or More:

\$50,954 for Single, Head of Household or Widowed

\$56,844 for Married Filing Jointly

Maximum Credit Amount: \$6,660

Credits: Earned Income Tax Credit, continued:

To the left is a chart that shows how income limitations of the Earned Income Credit work.

This is a chart from 2018 for a Single parent with One Child.

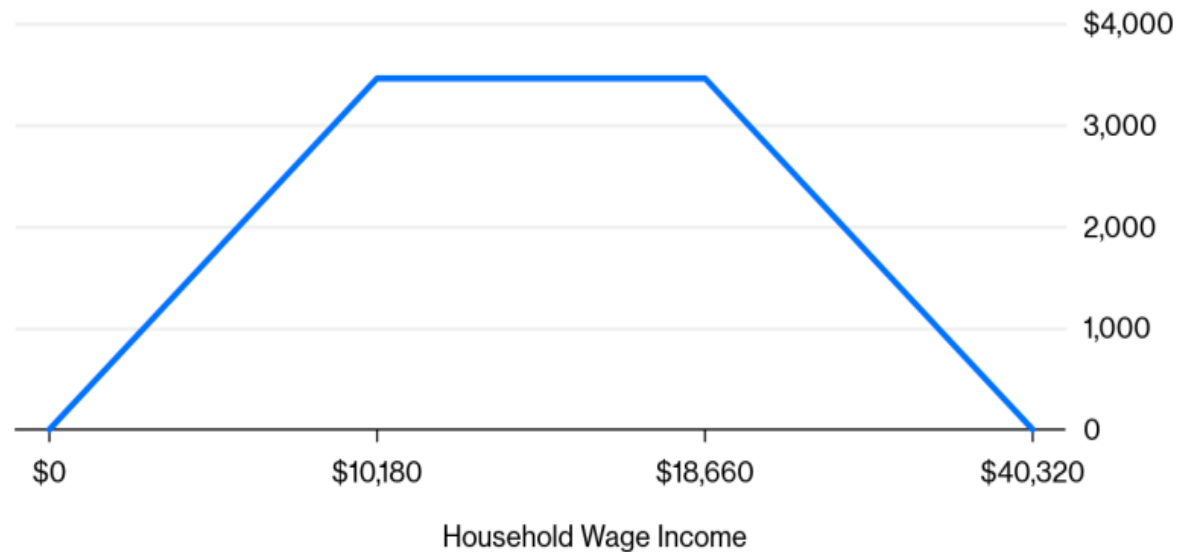
If the parent (i.e. the taxpayer) made more than \$40,320 in 2018, they would not qualify for the credit.

Notice that the credit amount increases as you begin to make money, then maximizes for taxpayers who made between \$10,180 and \$18,660, before decreasing and eventually phasing out completely at an income of \$40,320.

Giving Credit Where It's Due

The earned income tax credit rises with income, then phases out*

— EITC Benefit



* For a single parent with one child
Source: Tax Policy Center

Credits: Child Tax Credit & Credit for Other Dependents

General Rules for the Child Tax Credit:

- Social Security Number: Child must have a valid Social Security Number.
- Relationship Test: Must be son, daughter, stepchild, foster child, brother, sister, stepbrother, or descendant of any of these individuals. Adopted children are always treated as your own children.
- Support Test: Must provide over half of the child's support.
- Residence Test: Child must live with you for more than half of the year.
- Age Test: Child must be under the age of 17 on December 31st of the tax year.

Credits: Child Tax Credit & Credit for Other Dependents, continued:

Income Limitations for the Child Tax Credit:

Phase-In: Taxpayer(s) must earn \$2,500 of income to begin to phase into the credit.

Phase-Out: Taxpayer(s) begin to phase out of the credit if their income is \$200,000 (single/head of household) and \$400,000 (married filing jointly)

Maximum Amount for the Child Tax Credit: \$2,000 per child

- Maximum Amount per Child is \$2,000 under the age of 17 (i.e. age 16 or younger)
 - Nonrefundable: \$600
 - Refundable: \$1,400

Credits: Child Tax Credit & Credit for Other Dependents, continued:

Credit for Other Dependents:

Maximum Amount for the Credit for Other Dependents: \$500 per dependent

- This credit is available for all dependents who qualify as dependents, but are not eligible for the Child Tax Credit.
- This credit is available for to dependents who are US nationals (ATIN), US citizens (SSN), and US residents (ITIN).

Credits: Child & Dependent Care Expenses

General Rule:

This credit is available to taxpayers who pay expenses for the care of a qualifying individual to enable the taxpayers to work or actively look for work.

Age Requirement:

- Child must be under the age of 13 (i.e. age 12 or under), incapacitated spouse or parent, or another dependent that meets the age requirement.
- If the qualifying child turned 13 during the tax year, the qualifying expenses include amounts incurred for the child while under age 13 when the care was provided.

Credits: Child & Dependent Care Expenses, continued:

Amount of Credit:

- Up to 20% to 35% (depending on income) of up to \$3,000 of expenses per child.

Earned Income Rule:

- Taxpayer must have earned income
- If Married Filing Jointly, both spouses must have earned income

**Remember: Expenses must be paid in order for taxpayer to work or look for work.

Credits: Retirement Savings Contributions Credit (Saver's Credit)

General Rules:

- Contributions must be made to IRA, ABLE account, or other retirement account
- Taxpayer must be age 18 or older.
- Taxpayer cannot be a full-time student.
- Taxpayer cannot be claimed as a dependent on another person's return

Up to \$1,000 if you contribute \$2,000 (see next slide)

AGI Limitations: \$19,250 for single filers, \$28,500 for Head of Household, and \$38,500 for Married filing Jointly

Credits: Retirement Savings Contributions Credit (Saver's Credit), continued:

*Information below is for the 2020 filing season

Credit Rate	Married Filing Jointly	Head of Household	All Other Filers
50% of Your Retirement Contribution	AGI not more than \$39,000	AGI not more than \$29,250	AGI not more than \$19,500
20% of Your Retirement Contribution	\$39,001 - \$42,500	\$29,251 - \$31,875	\$19,501 - \$21,250
10% of Your Retirement Contribution	\$42,501 - \$65,000	\$31,876 - \$48,750	\$21,251 - \$32,500
0% of Your Retirement Contribution	More than \$65,000	More than \$48,750	More than \$32,500

Credits: Education Credits

American Opportunity Credit

- Generally for undergraduate students but graduate students can claim the credit if they were still undergraduate students at the start of the tax year.
- Must be enrolled full time.
- Include out-of-pocket educational expenses of up to \$4,000 to compute the credit.
- Can be used 4 times.
- Up to \$2,500 credit
 - \$1,500 is not refundable
 - \$1,000 is refundable
- If the student is claimed as a dependent, put the credit on the parent's return
- Cannot have a felony drug conviction.
- Include expenses incurred for required textbooks and any other course-related materials.

Credits: Education Credits, continued:

Lifetime Learning Credit

- Undergraduate and graduate courses, as well as classes taken to acquire or improve job skills.
- Up to \$2,000 credit.
- Nonrefundable (i.e. it will only apply if the taxpayer has taxable income).
- You do not need to be a full-time student.

Tax Planning Tip: Use up the American Opportunity Credit first, then use the Lifetime Learning Credit in the later years.

Claiming a Refund: 3-Year Rule

3-Year Rule:

- Taxpayers must file their return within 3 years from the original due date, including extensions, in order to claim a refund.

Example 1: Taxpayer's 2017 tax return *original due date* was on April 15th, 2018.

- The taxpayer has until April 15th, 2021 to claim their 2017 tax refund.
- Note that the filing deadline for 2017 was actually Tuesday, April 18th, 2018, due to the 15th falling on a Saturday and a holiday on Monday, April 17th. Nonetheless, the “original due date” was April 15th, 2018 for refund purposes.

Example 2: If the taxpayer in Example 1 (above) filed an extension to file their 2017 tax return, they would have had until October 15th, 2018 to file their return.

- If the taxpayer filed an extension, the taxpayer will have until October 15th, 2021 to claim their 2017 tax refund.

Owing Money to the IRS

What if you owe money?

- The IRS has 10 years to collect on a balance due once the return has been filed.
- If you do not file a return, the time DOES NOT begin to run.
- If you need further assistance with a balance due, please see the DABC Low Income Taxpayer Clinic contact information on the next slide.

Thank you!

Feel Free to Reach out with Further Questions:



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