

## CHAPTER TWO

### I've Got a Job! What's a W-4?



**Y**ou've just returned from your job interview at Macy's® when the telephone rings. It's the store manager calling to tell you that you've been hired as a sales clerk and to offer her congratulations. You've been instructed to report at 9:00 the next morning to fill out some paperwork, including a W-4.

A *what?* "Great," you think, "my first assignment and I'm already lost!" If you don't fill out this form correctly, you could end up unexpectedly owing tax when tax returns are due on April 15. Also, a mistake on this form could cause too much tax to be taken out of your paychecks, depriving you of that money until you file your return. Furthermore, you would lose the potential interest you could have earned on this money had you deposited it, for example, in a savings account. (The Internal Revenue Service [IRS] doesn't pay interest on refunds to taxpayers.)

When filling out any tax form, the key is to start at the top, take your time, and carefully follow directions. Don't approach a tax form the way you would a computer game, where you hardly ever read the instructions but rather just start playing. Here, it's vital to follow the instructions step by step. However, you can't follow the instructions if you don't know what they mean and how they apply to you.

A **W-4** (see Appendix II) is a form you fill out as a new employee so that your employer will *withhold* (keep) the correct amount of federal income tax from your paycheck. Remember that youth is not a factor in determining whether you must pay tax! To fill out a W-4, you'll need to understand a few key terms: withholding, exemption, unearned income, and dependent—all of which will be explained.

## EXEMPT STATUS

As mentioned above, **withholding** represents money that an employer deducts from an employee's paycheck to pay all or part of the employee's taxes. However, depending on how much you expect to make for the rest of the calendar year, you may not have to pay any federal income tax. In other words, you would be **exempt** from paying federal income tax.

"That sounds good to me," you're probably thinking. Well, if you start at the top of the W-4 form (see Appendix II) and read the instructions, you'll note that it directs you to lines 1, 2, 3, 4, and 7 if you are exempt. You are exempt if (1) you weren't required to pay federal income tax last year and (2) you don't expect to this year either. If the Macy's job is your first job, it's easy to meet the first requirement. But how do you know if you'll have to pay this year?

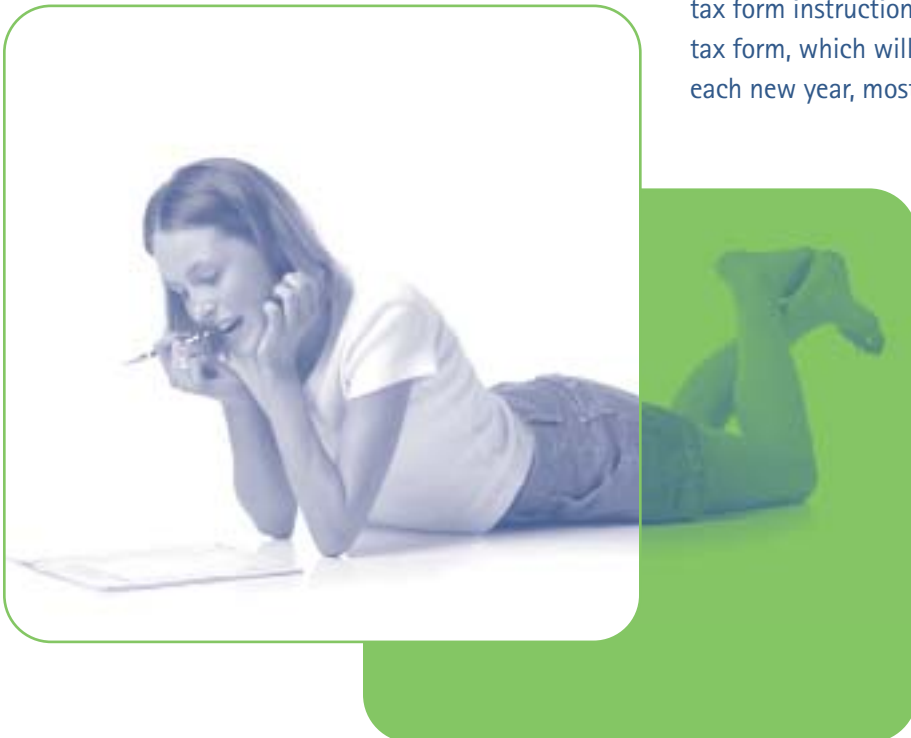
Whether you have to pay federal taxes this year will depend greatly on whether your parents or guardians can claim you as a dependent on their tax return. A **dependent** is a person who relies on another taxpayer for at least half of his or her support. "Support" includes food, shelter, clothing, medical and dental care, and education.

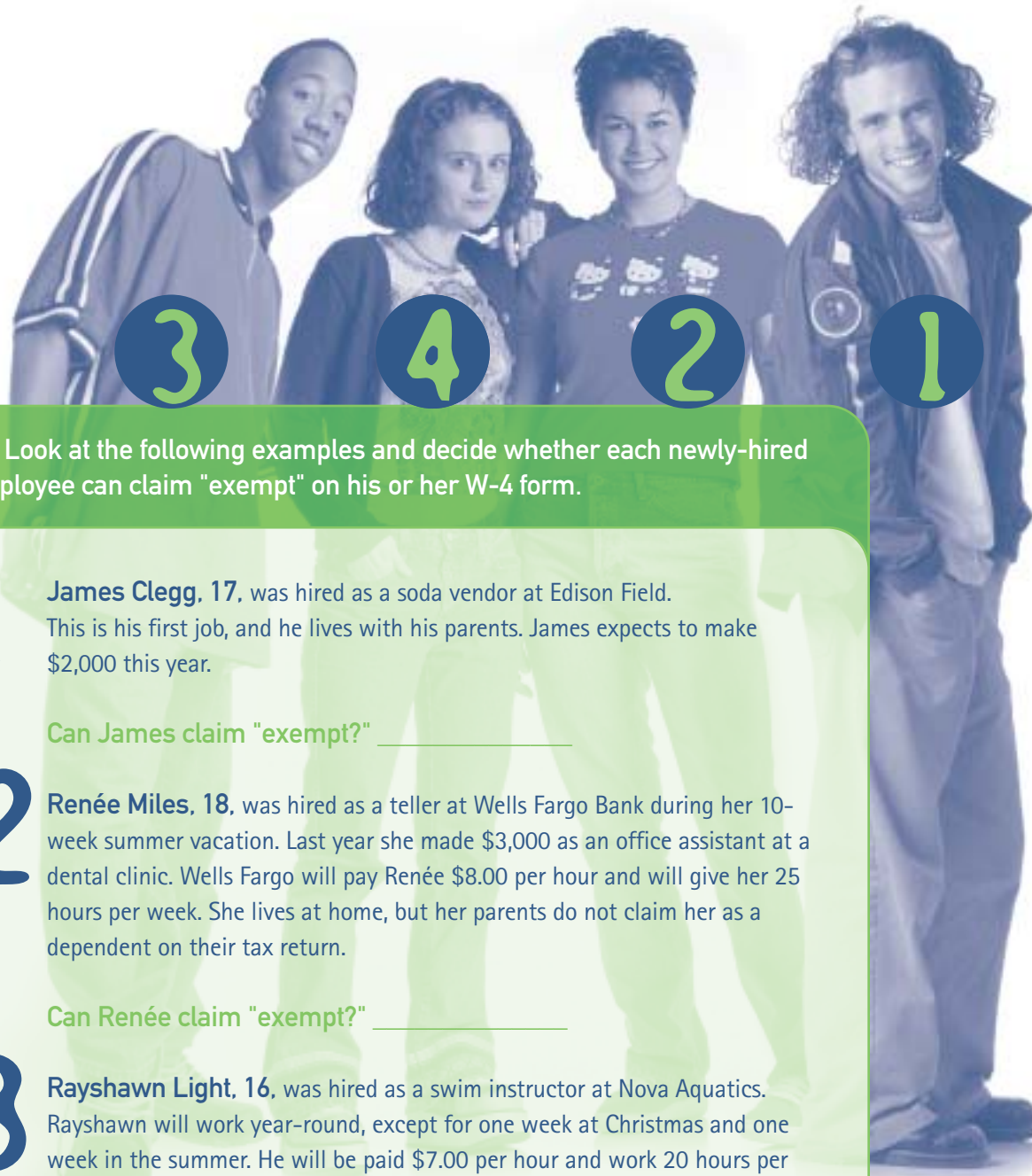
For the purposes of a high school student, if you live with your parents or other relatives or guardians and you're under 19 years old, you can be claimed as a dependent regardless of how much money you make. While your parents may choose not to claim you as a dependent, the test is whether they *can* if they want to. If (as is most likely the case) your parents can claim you as a dependent and you're under 19, then if you expect to make \$4,550 or less this calendar year, you will likely not have to pay federal income tax. The \$4,550 is called your *standard deduction*, which will be discussed in greater detail in Chapter 8.

Where can you find this \$4,550 figure? It's located in most tax form instruction booklets and on the back of the 1040EZ tax form, which will be addressed later. Beginning shortly after each new year, most post offices and public libraries offer free tax forms and instruction booklets.

These documents are also available year-round online.

If you are at least 19 years old but under 24, your parents can still claim you as a dependent as long as you're a full-time student.





Look at the following examples and decide whether each newly-hired employee can claim "exempt" on his or her W-4 form.

**1** **James Clegg, 17**, was hired as a soda vendor at Edison Field. This is his first job, and he lives with his parents. James expects to make \$2,000 this year.

Can James claim "exempt?" \_\_\_\_\_

**2** **Renée Miles, 18**, was hired as a teller at Wells Fargo Bank during her 10-week summer vacation. Last year she made \$3,000 as an office assistant at a dental clinic. Wells Fargo will pay Renée \$8.00 per hour and will give her 25 hours per week. She lives at home, but her parents do not claim her as a dependent on their tax return.

Can Renée claim "exempt?" \_\_\_\_\_

**3** **Rayshawn Light, 16**, was hired as a swim instructor at Nova Aquatics. Rayshawn will work year-round, except for one week at Christmas and one week in the summer. He will be paid \$7.00 per hour and work 20 hours per week. Rayshawn lives with his parents, who claim him as a dependent on their return. This is his first job.

Can Rayshawn claim "exempt?" \_\_\_\_\_

**4** **Midori Tanaka, 19**, was hired as a yoga instructor at Yoga Place. Midori is a part-time student at UCI and lives with her parents. This is her first job, and she expects to make approximately \$3,500 this year.

Can Midori claim "exempt?" \_\_\_\_\_



**In example 1, James can claim exempt.** He did not have to pay federal income tax last year because he didn't have a job. This year he will make less than \$4,550, and his parents can claim him as a dependent. By claiming exempt, James will not have any state or federal income tax withheld from his paychecks.



**In example 2, Renée can also claim exempt.** She earned \$3,000 last year, so she likely did not have to pay federal income tax. This year, she will earn \$2,000 ( $\$8 \text{ per hour} \times 25 \text{ hours per week} \times 10 \text{ weeks} = \$2,000$ ). Finally, even though her parents *chose* not to claim her as a dependent, they *can* because she lives with them, relies on their support, and is under 19.



**In example 3, Rayshawn should not claim exempt.** Even though he didn't have a job last year and his parents claim him as a dependent, he will earn \$7,700 ( $\$7 \text{ per hour} \times 20 \text{ hours per week} \times 50 \text{ weeks per year}$ ). If Rayshawn claimed exempt, he would end up owing a fair amount of state and federal tax when he files his return. Furthermore, Rayshawn may face penalties by improperly claiming exempt. (These penalties are discussed in Chapter 7.)



**In example 4, Midori should not claim exempt.** Even though she didn't have to pay taxes last year, she will likely have to this year. As a 19-year-old part-time student, she could not claim exempt, even though she lives with her parents. Midori needs to attend school full-time to regain the ability to claim exempt.

## I DON'T QUALIFY FOR EXEMPT STATUS, SO WHAT DO I DO?

**I**f you cannot claim exempt status, then you need to fill out the personal allowances worksheet on the W-4 to figure out your total exemptions. The more exemptions you claim, the less tax will be withheld from your paycheck. Claiming "0" exemptions will result in the largest amount of tax being withheld. Later in this book, when you practice filling out a 1040 form, you'll see that each exemption you claim will reduce by \$2,900 the amount of income on which you must pay tax. In other words, if you had income of \$5,900 and you claimed one exemption, the amount of income that the federal government requires you to pay tax on would be \$3,000 ( $\$5,900 - \$2,900$ ). The lower your taxable income (as you will learn in Chapter 7), the lower your tax. Now, let's begin working through the personal allowances worksheet on the W-4.

On line A, you are to enter "1" for yourself if no one else can claim you as a dependent. But since your parents can claim you as a dependent, you won't be able to take an exemption for yourself. Therefore, leave line A blank.

Line B is related to line A. So, since you couldn't enter "1" on line A, you can't enter "1" for being single on line B. The reason you aren't allowed to claim a personal exemption is

because your parents can claim one for you on their tax return. If you were also allowed to claim a personal exemption, then it could lead to dishonest parents attempting to transfer some of their income to your tax return, thereby receiving an additional tax break. In other words, they could "hide" up to \$2,900 on your tax return. That money would be tax-free after you claimed a personal exemption.

Why, then, are your parents allowed to claim exemptions? The reason is that caring for and raising a family can be very expensive. Therefore, parents need as much of their paychecks as possible to pay for the items their family requires. Claiming exemption for themselves and their children allows parents to receive a larger bulk of their paycheck, reducing the amount of federal and state income tax withheld.

Lines C-G allow exemptions for a spouse, dependents, if you file as a head of household, if you have child care expenses, or for child tax credits. As none of these apply to your situation, enter "0" exemptions on line H and on line 5. This means that the amount of federal income tax withheld from your paycheck will likely be enough to cover your tax liability for the year. This protects you from owing a great deal of taxes at the end of the year, and in all likelihood will result in a refund to you of the excess tax you paid.

## WHAT IF I MAKE A MISTAKE?

**I**f you claim exempt and it turns out that you earn more than \$4,550, you will likely owe tax when you file your tax return. If, after claiming exempt, you think this will be the case, then you do have some options.

First, if any change occurs that affects the number of exemptions to which you're entitled, you may file a new W-4 certificate. If you don't want to go through the hassle of filling out a new W-4, you can prepare for an upcoming tax payment by putting aside money from each paycheck in an account that earns interest, like a savings account. By doing so, you ensure that you will have the money you need if you have to pay tax, but you'll also be earning interest on that money.

If, on the other hand, you don't initially claim exempt but you could have, then you will likely receive a refund of the income tax deducted from your paychecks when you file your return. You also have the option of filing a new W-4.

