

## Transcript

### Intro to the W-4

When you get your paycheck from your employer, you will quickly appreciate that you are not getting your full gross pay, and if you imagine the width of what I'm drawing here, that's your full gross pay. You'll see you will get a good chunk of it. So this is the part that maybe is going to you, so you're going to get this chunk right over here. I'm trying to make a big fat arrow here, so this is what goes to you.

And then the other part is withheld, and it is given to the Federal or state governments to pay your Federal income tax, to pay state income tax, or to pay social security or Medicare taxes. So this right over here is withheld. So let me make this another big arrow just like that, so this right over here is withheld, and it's withheld for – let me just write this down – for Federal, state, social security tax, and Medicare.

So a question that you are maybe asking yourself, or maybe you should ask yourself, is how does the employer decide how much to withhold, and the answer is that's what a W-4 form is, so this is determined by a W-4 form. A W-4 form is typically one of the first forms you will fill out when you get a job, and it gives the employer the necessary information to make an estimate for withholding for all of these different purposes. So let's look at what an actual W-4 looks like.

Let's assume this is the W-4 for a single person making \$40,000 a year. So we look at the W-4, and I'm not going to go into everything line-by-line, that could take a little bit of a while, but the W-4 essentially starts off with a worksheet for calculating what we call withholding allowances, or sometimes just called allowances, and allowances, the more allowances you fill out on this form, the less will be withheld. Allowances are for things like having more expenses because you have dependents, or you're the head of the household, or whatever else, and so the more of I guess these obligations that you have, that you fill out here, that is going to lower your withholding

because in general, the more of those allowances you have, the less taxes that you will have to pay.

Now if you put too few allowances here, or let me clarify that. If you put too many allowances here, and you essentially underpay through your withholding, it's not like you just get away with that. You're going to have to make it up later when you true-up your taxes by April 15th the next year. So the W-4 determines what you withhold on a regular basis but it doesn't change what you're going to actually have to pay in the end. In fact, if you withhold too little, you might have to pay some penalty on some of the taxes that you didn't pay on a regular basis.

With that out of the way, let's actually look at what this looks like. So this first part, "Enter 1 for yourself if no one else can claim you as a dependent," and we see that the single person right over here, they put a 1 there. And then it says, "Enter 1 if you are single and have only one job, you are married and have only job and your spouse does not work, or your wages from a second job or your spouse's wages are \$1,500 or less."

Now you might say, "Well, if this is a single person, they would meet this criteria right over here, and so why didn't they put a 1 here?" And my guess is why they didn't put a 1 there is they actually want to over-withhold, or maybe not even over-hold, they just don't want to under-withhold. They would rather have lower allowances, have only one allowance, so that more is withheld every paycheck, so they're more likely to get a refund when they actually do their taxes as opposed to having to pay taxes.

The person might say, "Well, obviously I am single and I have only one job, so in theory I could have put a 1 here, but then I would have had more allowances which would have meant less withholding." And let me write that down just so that's clear. So more allowances, the more allowances you have, that means you have lower withholding. So the reason why that person might have elected to put the zero there, they might have wanted fewer allowances so they have more withholding, so that they are hopefully

paying their proper taxes or maybe overpaying the taxes so that maybe they get a refund.

Now the other thought might be, "Well, I want more cash now and I'm willing to be more likely to not get a refund and have to pay taxes at the end of the year," then maybe this person would have put a 1, and we can actually do that calculation.

And then in the rest, "Enter 1 for your spouse," well this person is single. "Enter number of dependents," so this person is zero dependents, clearly doesn't have any children and not supporting any other family members. "1, head of household," they put zero here. "1 if you have at least \$2,000 of child or dependent care expenses," once again a zero.

And as you see a pattern here, a lot of these questions are asking questions of "do you have dependents, do you have children," and that's because in general the tax code, I guess you could say, is sympathetic to the idea of, well, if you have more people dependent on you, that maybe you should pay less taxes, and so that's why a lot of these questions are about things like children and dependents. And at the end, line H, "Add lines A through G and enter total here," and of course this person only had 1 allowance, so when you summed them all up, you only have that 1 right over there.

And so after using this worksheet, you kind of fill out the non-worksheet part of the W-4, put your name. This person's name is Any Employee, and then their social security number, obviously a made-up one, their address, single, and then you say, "The total number of allowances that you are claiming from line H," so that was that 1 right over there.

And then if you really wanted to be careful and want to withhold even more, I guess to minimize your chance of having to pay extra when you true-up your taxes in the next year, or maybe to maximize your ability to get a refund – some people view that as kind of almost a savings mechanism –

you can actually have an additional amount withheld from every paycheck, or you might have some other sources of income that you know about, maybe it's an investment or something, and you say, "Well, let me just prepay some of my taxes there and have that withheld," but this person put a zero.

And then of course you sign it and then you date it, and you give it to your employer, and then your employer uses that to decide how much is actually withheld.