2021 Tax Brackets and Other Tax Changes

The IRS has announced its inflation adjustments for 2021 taxes

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On October 26, 2020, the Internal Revenue Service published the 2021 tax rates, allowances and thresholds applicable for the tax law provisions that are adjusted annually for inflation.1

For 2021 returns filed by individual taxpayers in 2022, the top tax rate will continue to be 37% but the standard deduction, tax bracket ranges, other deductions, and phase-outs will increase. (Note that, in April 2021, individual taxpayers will be filing their 2020 taxes, according to 2020 tax rules.)

Key Takeaways

- Tax rates remain constant for 2021
- Tax brackets, phase-outs for deductions and credits, thresholds, and ceilings Increase
- Contribution levels for retirement plans unchanged
- Cares Act RMD waiver, distribution and loan rules lapse after 2020

Standard Deduction

The standard deduction for 2021 will be $25,100, an increase of $300, for married couples filing joint returns; $12,550, an increase of $150, for single taxpayers' individual returns and married individuals filing separately; and $18,800, an increase of $150, for heads of households.

The additional standard deduction amount for an individual who is aged or blind will be $1,350; however, if the individual is unmarried and not a surviving spouse, the amount will be $1,700.

The standard deduction for an individual who can be claimed as a dependent on another taxpayer's return cannot exceed the greater of (1) $1,100, or (2) $350 plus the individual's earned income (but not more than the regular standard deduction, $12,550).

Same Tax Rates but Higher Brackets

The top rate of 37% will apply to taxable income over $628,300 for married couples' joint returns; over $523,600 for single taxpayers' individual returns and heads of household returns; and over $314,150 for married individuals filing separately. The tax rates and brackets for 2021 are provided in the chart below:

2021 Tax Brackets

Rate	Married Joint Return	Single Individual	Head of Household	Married Separate Return
10%	$19,900 or less	$9950 or less	$14,200 or less	$9950 or less
12%	Over $ 19,900	Over $9,950	Over $14,200	Over $9,950
22%	Over $ 81,050	Over $ 40,525	Over $54,200	Over $40,525
24%	Over $172,750	Over $86,375	Over $86,350	Over $ 86,375
32%	Over $329,850	Over $164,925	Over $164,900	Over $164,925
35%	Over $418,850	Over $209,425	Over $209,400	Over $209,425
37%	Over $628,300	Over $523,600	Over $523,600	Over $314,150

As provided in the 2017 Tax Cuts and Jobs Act, there is no personal exemption.

Capital Gains

Capital gains rates, which are lower than a taxpayer's ordinary income rate, depend on the taxpayer's taxable income and filing status. The maximum adjusted capital gains rates apply for both the regular income tax and the alternative minimum tax.

For 2021, the maximum zero rate amount on adjusted net capital gains for married persons will be $80,800 for joint returns and $40,400 for married individuals' separate returns; $54,100 for a head of household and $40,400 for single individual returns.

$445,850

The taxable income level that triggers the maximum capital gains tax of 20% for an individual. For married people filing jointly, the amount is $501,600.

The 15% rate amount will apply to adjusted net capital gains up to $501,600 for joint returns; $250,800 for married individuals' separate returns; $473,750 for head of household returns; and $445,850 for single individual returns. Above these ceilings, the applicable capital gains rate is set at 20%.

Under the alternative minimum tax (see below), these same rates and brackets apply to adjusted net capital gains.

Individual Tax Credits

The 2021 maximum amount of the earned income credit for low-income taxpayers and the taxable income levels for its thresholds and ceilings also have been adjusted for inflation. The maximum credit for three or more children will be $6,728. For married couples filing jointly the phase-out of the credit will begin at $25,470 of adjusted gross income (or earned income, if higher) and will be completed at $57,414. However, no earned income credit will be allowed if the aggregate amount of investment income—e.g., from interest, dividends, net capital gains or other passive activities—in 2021 exceeds $3,650. The maximum refundable portion of the $2000 child credit for each child under age 17 will be limited to $1,400 per child.

The credit for qualified adoption expenses, as well as the special credit for the adoption of a child with special needs, will be increased to $14,440. Similarly, the exclusion from an employee's income for adoption expenses that are paid or reimbursed under an employer plan will be increased to the same level.

The maximum $2,000 per return lifetime learning credit for qualified educational expenses for the taxpayer, spouse or dependent will phase out between modified adjusted gross income of $59,000 and $69,000 for single returns—and between $119,000 and $139,000 for joint returns—in 2021. The foreign earned income exclusion will increase $1,100 to $108,700.

Alternative Minimum Tax

The alternative minimum tax (AMT) applies to alternative minimum taxable income (AMTI), i.e., regular taxable income with certain tax benefits added back, in excess of an exemption level.

For 2021, the exemption levels will be $114,600 for joint returns; $73,600 for unmarried individuals; and $57,300 for married persons' separate returns. These exemption levels phase out between $1,047,200 and $1,505,600 for joint returns; $523,600 and $818,000 for unmarried individuals; and $523,600 and $752,800 for married persons' separate returns.

The AMT rate is 26% for AMTI up to a maximum AMTI of $199,900 for returns of married couples and single individuals ($99,500 for married filing separately). All AMTI in excess of these levels will be taxed at 28%.

Increased Allowances: Fringe Benefits, MSAs and Estates

In 2021, allowances for certain employee fringe benefits will continue at their 2020 levels. The qualified transportation and qualified parking fringes will maintain their monthly limit of $270. The maximum salary reduction for contributions to health flexible spending accounts will continue at $2,750 for the year. However, for cafeteria plans that permit carryovers of unused amounts, the maximum carryover amount will increase by $50 to $550.

Certain thresholds and ceilings for participants in Medical Savings Accounts also will be increased. For self-only coverage, the plan's annual deductible for 2021 must be at least $2,400 and no more than $3,600 with a maximum out-of-pocket expense of $4800, an increase of $50 for each amount. For family coverage, the deductible must be at least $4,800 but no more than $7,150, an increase of $50 for both amounts. The out-of-pocket expense maximum for family coverage will increase by $100 to $8,750 for 2021.

For a decedent dying in 2021, the exemption level for the estate tax will increase to $11,700,000 from $11,580,000. The annual gift tax exclusion of $15,000 per recipient will continue at the same level.

Retirement Plans

The IRS also announced the 2021 limitations on retirement plan contributions and their phase-out ranges. The income exclusion for employee contributions to employer retirement plans, such as 401(k)s, 403(b)s, 457 plans and the federal government's Thrift Savings Plan will remain at $19,500. The catch-up contribution for employees age 50 and older will continue at $6500. For SIMPLE retirement accounts the limitation will remain $13,500.

Although the deductible amount for IRA contributions will remain at $6000 with the catch-up contribution for individuals age 50 or over continuing at $1000, the phase-out levels for the deduction are adjusted upwards. If either a taxpayer or their spouse is covered by a workplace retirement plan during the year, the deduction may be reduced or phased out until it is eliminated.

- If an individual is an active participant in an employer retirement plan, the deduction will phase out for adjusted gross incomes between $66,000 and $76,000 for single individuals and heads of households, and between $105,000 and $125,000 for joint returns.
- For an IRA contributor who is not an active participant in another plan but whose spouse is an active contributor, the phase out ranges from $198,000 to $208,000.
- For a married active contributor filing a separate return, there is no adjustment and the phase-out range will remain $0 to $10,000.

These phase-outs do not apply if neither a taxpayer nor his or her spouse is covered by a workplace retirement plan.

For 2021 contributions to Roth IRAs, the phase-out is $125,000 to $140,000 for single taxpayers and heads of households and $198,000 to $208,000 for joint returns. The Roth IRA phase-out for a married individual's separate return will continue at $0 to $10,000.

Low-income taxpayers who make contributions to 401(k), 403(b), SIMPLE, SEP or certain 457 plans as well as traditional and Roth IRAS are entitled to claim a nonrefundable tax credit in addition to their exclusions or deductions. Married taxpayers filing joint returns will be eligible to claim a credit for contributions of up to $4000 at a rate or 50% with adjusted gross income (AGI) up to $39,500; at a rate of 20% with AGI up to $43,000; and at a rate of 10% with AGI up to $66,000.

Heads of households will be able to claim a credit for up to $2000 of contributions at a rate of 50% with AGI up to $29,625; at a rate of 20% with AGI up to $32,250; and at a rate of 10% with AGI up to $49,500. All other taxpayers will be eligible to claim a credit for up to $2000 of contributions at a rate of 50% with AGI up to $19,750; at a rate of 20% with AGI up to $21,500; and at a rate of 10% with AGI up to $33,000.

The more liberal 2020 rules for borrowing and taking distributions from retirement plans—and the waiver of RMDs—disappear, starting with the 2021 tax year.

2020 Retirement Plan Rules: Not Effective in 2021.

Taxpayers should be aware that special tax provisions enacted as part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act, applied only for 2020. In particular, the liberalized rules on certain distributions and loans from retirement plans, and the waiver of required minimum distributions (RMDs) from plans, will not be effective in 2021, unless re-enacted by new legislation.