

Income Sources



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People receive income from working and from other sources, such as investments. Another source of income for some people is government transfer payments. These payments help people who do not have other sources of income pay for their needs. Many workers receive benefits such as paid vacation or sick leave. You need to understand how benefits are a part of the total payments for a job. Various taxes must be paid on earnings. Taxes help cover the cost of government services and transfer payments. In this chapter, you will learn about income sources and benefits and about how taxes affect disposable income.

ONLINE RESOURCES

Personal Financial Literacy
Web site:

Data Files

Vocabulary Flashcards

Beat the Clock:

Income Sources

Chapter 2 Supplemental
Activity

Search terms:

- minimum wage
- government transfer payments
- unearned income
- disposable income
- entrepreneur

Earned Income and Benefits

OUTCOMES

- List and discuss types of earned income, such as wages, salaries, tips, and commissions.
- Discuss the advantages and disadvantages of self-employment.
- Describe employee benefits.

TYPES OF EARNED INCOME

Many people work for hourly wages; others work for an annual salary. Some people have additional income through tips or commissions. Some people work for themselves, which is called self-employment. All these types of income are earned income and are subject to income taxes and other taxes. A **tax** is a required payment for the support of a government. The tax may be based on items such as earnings, property values, or the sale price of an item. More information about taxes is provided later in this chapter.

Wages

Employees who work for wages are paid for each hour worked.

Minimum wage is the lowest pay rate allowed by law for each hour of work. The federal minimum wage is set by the U.S. Congress. In 2006, that rate was \$5.15 per hour. Many states have minimum wage laws that set a rate higher than the federal rate. The state minimum wage rates can be found on the U.S. Department of Labor Web site as shown in Figure 2-1.1 on page 30. In many jobs, new workers will begin at minimum wage. This is because they do not have the education or experience that would allow them to earn a higher wage rate.

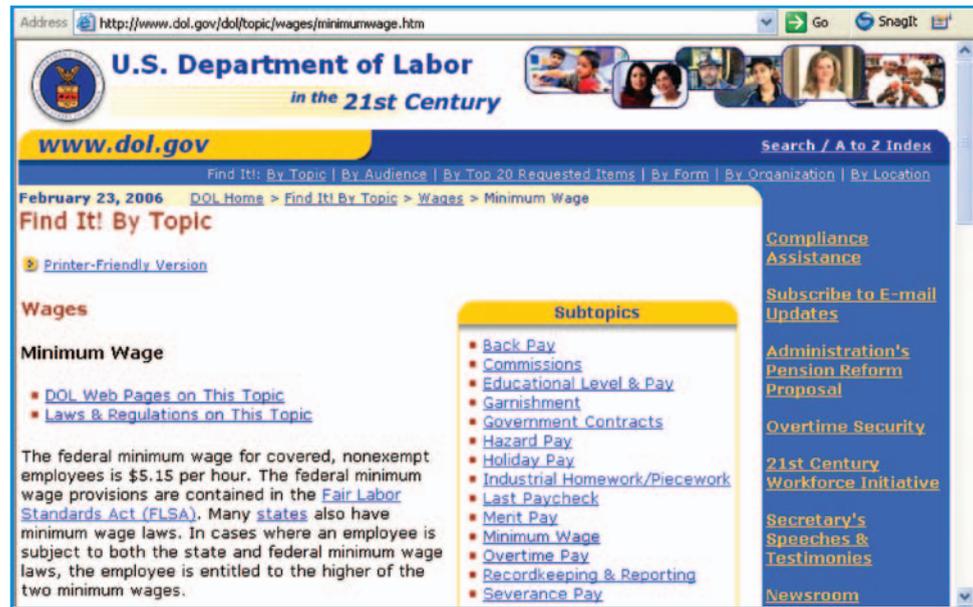
Employees who are paid by the hour must sometimes work more than the set regular number of hours. When this happens, they are entitled to extra pay called **overtime pay**. By law, overtime pay of at least 1½ times regular pay must be paid for hours worked above 40 work hours in a week. For example, a worker who earns \$8 per hour for regular pay might earn \$12 per hour for overtime pay. People who work on holidays may be entitled to even higher pay rates for those hours. Both federal and state laws control when extra pay is required for more time worked.

Salaries

Some people work for a set salary, such as \$3,000 a month or \$36,000 a year. Salaried workers usually do not keep time cards or count hours worked. They may have more flexibility in the times they work than do

FIGURE 2-1.1

Information about minimum wage can be found on the U.S. Department of Labor Web site.



Source: U.S. Department of Labor, <http://www.dol.gov/dol/topic/wages/minimumwage.htm> (accessed March 8, 2006).



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hourly workers. They often work more than 40 hours a week but do not receive overtime pay.

People who work for a salary must often be self-directed. They must complete their work in a timely manner with little supervision. Managers and supervisors are typically paid a salary.

Tips and Commissions

Some workers receive tips in addition to wages. A **tip** is money, often a percentage of the total bill, or a gift given to a person for performing a service. The amount of the tip may be based on the quality of service provided. For example, a waiter may receive tips in the form of money from customers. A caddy at a golf course might receive free tickets to a show as a tip. Some workers make most of their earnings from tips rather than hourly pay.

Tips are subject to federal taxes. Tips may be subject to state taxes as well. The law requires some employers (such as restaurants and hair salons) to withhold taxes based on tips, even though tips may have been received in cash directly from customers.¹

Some workers are paid a commission. A **commission** is a set fee or a percentage of a sale paid to a salesperson instead of or in addition to salary or wages. Sales commissions are earned only when a sale is made. If no sale is made, no

Some workers make most of their earnings from tips rather than wages.

¹ Internal Revenue Service, "Tips Are Subject to Taxes," <http://www.irs.gov/newsroom/article/0,,id=106783,00.html> (accessed February 23, 2006).

Success Skills

NETWORKING

Networking is the process of making contacts and building relationships with other people. Everyone you know is in your "network." All your contacts are important to you. They will help keep you informed about issues that affect your financial success. For example, you may learn about scholarships or grants from teachers or counselors in your network. Later in life, you may learn about a job opening from a friend at another company.

Your network may include many contacts. Record the name, address, phone number, and e-mail address of each one so

you can reach that person when you want to share information. Make a note of how you are related to or were introduced to each person. For example, you should include your school teachers, counselors, and principals. You should also include the leaders or members of community groups or other groups to which you belong. If you have a summer or part-time job, include the others with whom you work and your manager. Keep in touch with your contacts regularly. Let them know when you are looking for particular information, such as scholarships for which you can apply.

commission is received. In some types of jobs, such as real estate sales, the worker's entire earnings may be based on commission. For example, a real estate agent who arranges the sale of a home for \$200,000 might receive a \$12,000 commission. In other types of jobs, workers may be paid a base salary plus commissions. For example, a person who sells cars might receive a salary of \$10,500 a year plus 25 percent of the profit on each car sold.

SELF-EMPLOYMENT

Working for yourself is called self-employment. A person who takes the risks of being self-employed and owning a business is called an **entrepreneur**. Owning a business can be challenging, but it can have rewards as well. If the business fails, the money invested in the business may be lost. The owner may have to work long hours and do many different tasks to keep the business running. These can be disadvantages of owning a business. An advantage of owning a business is that the owner can make decisions about how the business will be run. She or he also keeps all the earnings or profits from the business. **Profit** is the amount left after all costs are deducted from the income of a business. This is another advantage of being an entrepreneur.

Some entrepreneurs want to keep their businesses small. They want to be able to oversee all the daily operations of the business. Others want their businesses to grow into large companies with many workers. In a large company, the owner cannot oversee all the daily operations.

Some people start a business at an early age. Some people work for other businesses first to gain knowledge and experience. Some people

seek education about how to run a business before they start a company. Owning a business involves much risk for the entrepreneur. He or she may need to borrow money to start the business. Repaying the money and paying other debts of the business are responsibilities of the owner. The owner may need to reinvest part of the income from the business to help the business grow. The owner will typically have to work hard to make the company successful.

EMPLOYEE BENEFITS

Full-time workers usually have benefits provided by the employer. **Benefits** are forms of pay other than salary or wages. Paid vacation and holidays are examples of benefits. Some benefits are paid for by the company. For other benefits, such as health insurance, the worker may need to pay part or all of the cost.

A **cafeteria plan** is a benefit plan that allows workers to choose from a number of options. Workers may be able to save money by selecting only the options they need. Most plans include basic choices for health, life, and other insurance. Other options, such as a savings plan, may also be available.

Benefits increase the overall value a worker receives for a job. **Disposable income** refers to the money a person has available to spend or save after taxes have been paid. Money received from some benefits, such as a profit-sharing plan, can directly increase a worker's disposable income. Other benefits have the effect of increasing disposable income. For example, health insurance bought through a company plan may be cheaper than an individual policy. The money saved by buying the company plan is available to save or spend on other items.

Benefits are also important to workers for several other reasons:

- Workers are not taxed on most benefits. This means that workers receive something of value without paying tax as part of the cost.
- Some benefits allow workers to buy services at a cheaper price than they could otherwise. For example, group insurance costs a lot less than individual policies. Paying a lower cost for insurance increases the worker's disposable income.
- Some benefits that are offered to workers may not be available to individuals. Company retirement plans and stock options are examples of these benefits.
- Some benefits that are offered to workers may not be affordable at individual prices. For example, workers who have health problems might not be able to afford insurance at individual rates.
- Some benefits help workers reach financial goals. For example, some people find it hard to save money. With company-sponsored savings plans, saving becomes easier because the money is deducted from the worker's paycheck.

Pay Without Work

Pay without work refers to times when an employee who is not working will be paid. Vacation, holidays, and sick leave are examples of pay without work. Full-time and salaried employees usually get annual paid vacations.

Ethics

USING SICK LEAVE

Many employers provide sick leave for employees. Sick leave is a valuable benefit. Employers usually have rules about what situations qualify for use of sick leave. In some cases, the employee must be ill to use sick leave time. In other cases, the company may allow employees to use sick leave time to care for a sick child or other relative. An employee may be able to use

sick leave time to visit a doctor or hospital for tests or checkups.

Employers expect workers to be honest in their dealings with the company. Employees should know and follow the rules that apply to using sick leave. Pretending to be sick or to have another situation that qualifies for sick leave use is not ethical.

Typically, after the first year, an employee gets 1 or 2 weeks of vacation per year.

Most employers provide certain **paid holidays**. Examples of paid holidays are Thanksgiving, Christmas Day, Easter, Labor Day, Memorial Day, Veterans Day, and Presidents' Day. On those days, employees will be paid but will not have to work. Employees who do work on holidays may receive extra pay. Typically, working on holidays pays two times the regular rate of pay.

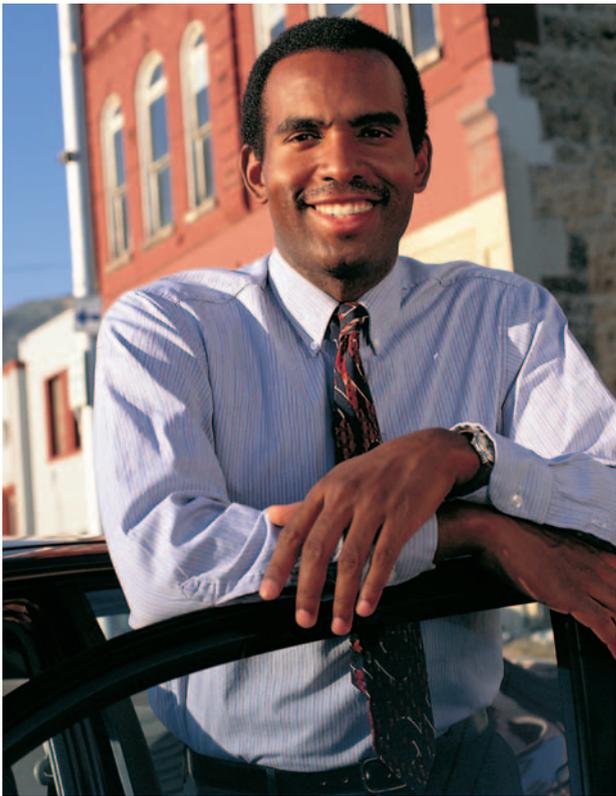
Many companies allow workers to take a certain number of sick leave days per year. **Sick leave** covers days the worker is paid even though she or he is not at work due to illness. Some companies allow the use of sick leave to care for a sick child or other family member. Typically, sick leave is 10 days a year. Some companies allow unused sick leave to accumulate. That means that workers can save sick leave and use it later. Workers might also get paid for unused sick leave at some time in the future.

Some companies also offer personal leave. **Personal leave** is time away from work for personal reasons. The worker usually does not have to give a reason. Typically, personal leave is 2 or 3 days a year. Unused personal leave usually is not carried forward to another year.

These and other pay-without-work benefits allow employees to rest and get away from work pressure and stress. They also allow workers to plan family vacations and special events and to enjoy a balanced and healthy life.

Educational Reimbursement

Some employers provide plans that reimburse (pay back) money spent on education. For example, some companies will pay for the cost of classes or training related to the worker's job. This training can benefit the company because the worker may be able to do a better job using the skills learned. The training benefits the worker on the present job. It may also improve the chances of getting a promotion or a better job with the same or a different company. Some employer plans will pay for classes



A perk that many people value is a preferred parking spot.

toward a degree. Getting a college degree paid for by an employer is a benefit of great value, not just for this job, but for all future jobs as well.

In a typical education plan, the worker might be paid 100 percent of the cost of tuition and books if an A grade is received in the class. If the worker earns a B grade, 90 percent of the costs will be paid. If the worker earns a C grade, 80 percent of the costs will be paid. If the worker's grade is below a C, no costs will be paid.

Perks

Providing high wages and good benefits like pay without work and education plans is one way that companies motivate workers. Other types of benefits, called perks, have a different value. They provide emotional satisfaction or social status rather than money. Examples of perks are a prime parking space, an office with a view, an expense account, and a company car. Some of these benefits are not taxable.

Insurance

Health insurance is an important benefit for many workers. The price paid for health insurance is called a premium. Premiums are typically paid by employers and employees. In the past, many employers paid the full price of insurance for employees. However, the costs of health care have risen steadily over the past several years. The costs are expected to continue increasing. Today, employees typically pay a portion or all of insurance premiums.

The premiums employees pay vary depending on the coverage provided. For example, an employee with a spouse and children would pay more for health insurance than a single employee. Group health insurance premiums are lower than those for individual policies.

Group life insurance is often available at work. The premium may be paid by the employer or the employee. In some companies, the employer pays for a certain amount of life insurance. For example, this amount may be twice the employee's annual salary. The employee may be able to purchase additional coverage at the group rate. The premium is often lower than for an individual policy. Life insurance paid for by the employee may be portable. A portable policy goes with the employee when he or she leaves the employer.

Disability insurance provides payments to replace income lost when illness or injury prevents the employee from working. This type of insurance is an option for many employees. Coverage for short-term disability (up to two years) is often paid for by the employer. The employee may be able to purchase long-term disability coverage. Long-term disability insurance typically covers periods longer than two years and up to retirement. The premiums are deducted from the employee's paycheck.

Workers' compensation is an insurance plan that employers are required to provide for employees. It pays medical and disability benefits to workers who are injured or contract diseases on the job. Benefits may be paid to the worker's family if the worker is killed on the job.

Other types of group insurance coverage may also be available. For example, the employer may offer dental, vision, or long-term care.

Retirement Plans

Some companies offer 401(k) retirement plans. This type of plan allows employees to put aside money for retirement that is not subject to federal income tax at the time it is earned. Some states also do not require that state income tax be paid on money placed in a 401(k). The employer may match the contribution to some extent, such as 25 percent or more. The money put into the plan will be taxed later when it is taken from the account. Deductions for the plan are made from the worker's pay.

Some companies offer retirement accounts that are paid for entirely by the employer. These accounts are also called pension plans. Pension plans provide payments to retired workers. Typically, employees must work for the company for a certain number of years to qualify. The payment amounts vary depending on the number of years worked, the worker's salary, and other factors. This type of fringe benefit is being offered by fewer companies now than in the past.

Profit-Sharing Plans

A profit-sharing plan means that when the company does well, employees are paid a share of the profits. This money can be paid in cash, or it can be added to a retirement account. When the money is paid in cash, it is taxable in the year received. When the money is added to a retirement account, it is taxed when withdrawn by the employee.

Stock Option Plans

Some companies allow employees to buy stock in the company at a reduced price. The purchase price of the stock may be deducted from the employee's pay. This is a convenient way to acquire stock, and it does not involve brokerage or trading fees. Other companies may give shares of stock in the company to employees as a benefit.

Health Flexible Spending Arrangements

A health flexible spending arrangement (FSA) allows employees to set aside money to pay for qualified medical expenses. The money set aside is not included in the amount on which employment or federal income taxes are paid. The plans are often set up by employers as an employee benefit. Deductions are made from the employee's pay to fund the account. The employer may also contribute. The employee files claims to be paid from the account for qualified expenses.

2-1 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What does the term *minimum wage* mean? Why do people often have to start a new job for minimum wage?
2. What is overtime pay? How much is overtime pay compared to regular pay?
3. How is being paid a salary different from being paid hourly wages?
4. Give an example of a worker whose pay may include tips.
5. What are some advantages of self-employment? What are some disadvantages?
6. What are employee benefits? Give two examples. Why are employee benefits important to employees?
7. Give three examples of pay without work.
8. Why is educational reimbursement a valuable benefit for employees?
9. Give two examples of perks that employees might want.
10. Why are employees at many companies expected to help pay for the cost of health insurance?
11. Describe two types of retirement plans offered by companies as a benefit.
12. How does a health flexible spending arrangement (FSA) benefit employees?

2-1 Activity 1 Compute Gross Pay

Gross pay is the amount of salary or wages a worker receives before deductions are made. Deductions may be taken for taxes and some benefits, such as health insurance premiums. Tips and commissions are included in gross pay.

To calculate gross pay, multiply the hourly rate times the number of hours worked. If tips or commissions are included, add them to the total salary or hourly wages earned.

1. Kim Chin works for an hourly rate of \$6.50. This week Kim worked 39 hours. What is Kim's gross pay for this week?

2. Juan Perez is paid a monthly salary of \$500. He is also paid a 10 percent commission on sales he makes. This month, Juan made \$7,575 in sales. What is Juan's gross salary for this month?
3. Alice Jones worked 32 hours this week. She is paid \$4.00 per hour. She also earned \$250 in tips. What is Alice's gross pay for this week?
4. John O'Malley worked 40 regular hours and 10 overtime hours this week. His regular rate of pay is \$8.50. For overtime pay, he earns 1.5 times his regular pay. What is John's gross pay for this week?
5. Gloria Adams is starting a new job. She will be paid \$10.50 per hour. She plans to work 40 hours per week for 50 weeks a year. What will her gross yearly pay be? The value of the benefits Gloria will receive amounts to 30 percent of her gross pay. What will the value of her benefits be? What is the total value of the pay and benefits Gloria will receive?



Unearned Income

OUTCOMES

- List private sources of unearned income.
- List several types of government transfer payments.
- Explain the difference between in-kind and in-cash transfer payments.
- Discuss the costs and benefits of paying taxes.

PRIVATE SOURCES

Unearned income is money received from sources other than working in a job, either for yourself or for someone else. There are several private sources of unearned income. For example, interest earnings on a savings account is money received that the owner does not work to get. People who buy stocks in a corporation may receive dividend payments.



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All sources of income offer financial security to retired people.

CLASSIFICATION OF TYPES OF INCOME		
Earned Income	Unearned Income	Variable Income
Salaries and wages	Dividends	Business profits
Commissions	Interest	Royalties
Bonuses	Capital gains	Rents
Professional fees	Gambling winnings	
Tips	Alimony	
	Social Security benefits	
	Pensions	
	Annuities	

FIGURE 2-2.1
TYPES OF INCOME

Source: Internal Revenue Service, <http://www.irs.gov/businesses/small/international/article/0,,id=96811,00.html> (accessed March 6, 2006).

A **dividend** is money shared with stockholders when a corporation makes profits. Retired people may receive pension payments. These are examples of unearned income.

The Internal Revenue Service (IRS) lists some types of income as variable income. The income may be earned or unearned, depending on the situation in which it is received. Royalties and rent are examples of variable income. Figure 2-2.1 shows different types of income as listed by the IRS.

Unearned income is taxable. However, the tax rates may be lower than income tax rates on earned income. For example, qualified dividend income is subject to a maximum 15 percent tax rate. Because this income is not earned, it also is not subject to employment taxes.

Building Communications Skills

CRITICAL LISTENING

Critical listening involves evaluating the information you hear. The goal is to consider only the important or relevant information. Unneeded, untrue, or conflicting information can be ignored. When you listen critically, you are able to make good decisions based on what is accurate and useful.

For example, pretend you are buying a used car. The seller is telling you about the

car and its features. He tells you that the car runs great and will run for years to come. It is the best car he ever had. These statements are not useful for making a decision about whether to buy the car. Next, the seller tells you that the car was serviced regularly (and he can prove it), has traveled 34,000 miles, and was kept in a garage every night. Using this information can help you make a good decision.

GOVERNMENT TRANSFER PAYMENTS

Money and benefits received from local, state, or federal governments are called **transfer payments**. Transfer payments are made from many different programs. Transfer payments increase the disposable income of those who receive them.

Some transfer payments provide income to retired people. When people get older, they stop working. However, their needs continue. In fact, some needs increase, such as the need for medical care. For some people, medical care and prescriptions are their largest expenses. Retired people also need health insurance. Social Security and Medicare programs provide benefits for these retired workers.

Other programs provide benefits to help low-income families with medical needs or living expenses. For example, Medicaid is a program of medical aid designed for those unable to afford medical service. It is financed by the state and federal governments in the United States.

Examples of transfer payments provided from state and federal governments are shown in Figure 2-2.2. Transfer payments may be in-cash or in-kind payments. Examples of each are discussed in the following sections.

In-Kind Transfer Payments

In-kind transfer payments include food stamps, rent subsidies, and vouchers that can be exchanged for goods and services. People do not receive money directly. Instead, they are provided with the means to get goods and services. In-kind payments are made available to those in need.

The federal government and state governments make in-kind transfer payments. For example, Medicaid is a program of medical aid designed for those unable to afford medical service. It is financed by the state and

FIGURE 2-2.2

Transfer payments are made possible by taxes collected from taxpayers.

TRANSFER PAYMENT EXAMPLES

Aid to Families with Dependent Children	Payments to needy families with children. Programs vary by state.
Medicaid	Benefits that provide health care and related services for low-income individuals
Veterans' benefits	Benefits for veterans (those who have completed active military service), their families, and their survivors
Supplemental Security Income (SSI)	Benefits for low-income elderly and disabled persons
State-provided medical care plans	Benefits for people who cannot afford health insurance
Social Security	Benefits for retired people, disabled workers, and their dependents
Medicare	Health insurance for retired people and those who receive Social Security benefits
Unemployment compensation	Benefits for workers who are laid off or dismissed from jobs. To qualify, individuals must have worked for a required time. Program rules vary by state.
Workers' compensation	Benefits for workers who become injured or ill on the job



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Transfer payments help people who are in need.

federal governments in the United States. Many people age 65 or older qualify for Medicare hospital insurance (Part A) based on their own or their spouse's work record. Some people under age 65 who are disabled may also qualify for Medicare hospital insurance. This is another type of in-kind transfer payment.

In-Cash Transfer Payments

In-cash transfer payments are money in the form of a check, debit card, or other direct payment. For example, after Hurricane Katrina, flood victims were given debit cards worth \$1,000. They used the cards to buy food,

Focus on . . .

SOCIAL SECURITY BENEFITS

Most workers in the United States pay into the Social Security fund. A Social Security number is assigned to each person's account. Payments are made into the account by employees. The payments are matched by employers. Based on the amount paid into the account and other factors, the worker will receive monthly benefit checks when retired.

Each year while paying into the fund, workers should receive a Social Security Statement. The statement allows workers to see that earnings are being posted properly to the account. If you are a worker and do not receive a statement, you should request one. A statement can be requested at a local Social Security office or on the Social Security Web site. A link to this site is provided on the Web site for this textbook.

clothing, and other items. Social Security payments, unemployment benefits, and workers' compensation payments are examples of in-cash payments. People receive checks or have direct deposits made to their checking accounts.

COSTS AND BENEFITS OF PAYING TAXES

Taxes are collected from many sources. Income taxes, use taxes, and excise taxes are examples. Income taxes are paid on earned and unearned income. You will learn more about income taxes later in this chapter.

Use taxes are paid by people who use certain goods or services provided by the government. For example, people who visit a state or national park may be charged a use tax. This money is used to help pay for operation of the park. Drivers may have to pay a toll to be able to cross a bridge. This use tax helps to pay for the bridge maintenance and operation.

Another form of tax is called the **excise tax**. Excise taxes are charged on the purchase of specific goods, such as motor fuel, cigarettes, and alcohol. They are also charged on services such as phone service, utilities, and garbage collection. Excise taxes are usually included in the price of the product or service. They help pay for the cost of government goods and services. When the excise tax is on a product that is not considered essential for a normal standard of living, such as an expensive car, it is often called a luxury tax.

Costs of Paying Taxes

Paying taxes reduces the disposable income of an individual. The person has less money available to save or spend than if taxes were not paid. This is the main cost of paying taxes for an individual. When people have



Gasoline excise taxes help pay for roads and highways.

less money to spend, the economy of the area may be affected. When people spend less on goods and services, businesses have lower sales. Lower sales may lead to lower profits. Workers may have to be laid off or dismissed from their jobs. Charitable groups may receive less money from donations. Having less money means the groups are able to help fewer people in need. In fact, cutting taxes is a method governments can use to stimulate the economy.

Benefits of Paying Taxes

Paying taxes can benefit the person making the payments and others who do not make payments. For example, Social Security tax provides a system of old-age, survivors, and disability insurance. Workers pay Social Security tax during their working years. When they retire, workers receive payments from the fund. This is an example of a direct benefit from paying taxes.

Money collected from various taxes is used by governments to provide goods and services for citizens. For example, roads and highways are paid for with government money—either federal or state. Everyone (whether or not they paid taxes) is able to use them. Government transfer payments, in-kind and in-cash, are funded with taxes.

Everyone benefits from government goods and services that are paid for with tax dollars. Examples include public education, national defense, police protection, and parks. Most individuals could not afford to pay for these items. Not everyone benefits directly from every type of tax. For example, some people may never visit a state or national park. However, everyone benefits from some government services.



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Taxes help provide parks for everyone to enjoy.

2-2 REVIEW

1-1 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. How is unearned income different from earned income?
2. List three sources of private unearned income.
3. What are government transfer payments? How are in-kind payments different from in-cash payments?
4. From Figure 2-2.2, explain how Medicaid is different from Medicare.
5. What is an excise tax? Give one example of a product that has an excise tax.
6. What is the main direct cost of paying taxes for an individual?
7. How can having citizens pay high taxes affect the economy?
8. Give one example of how paying taxes can directly benefit a person.
9. How are government transfer payments funded?
10. Give one example of goods or services funded by taxes that benefit everyone.

1-1 Activity 1 Taxes, Taxes, Taxes



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Many different types of taxes are paid by people in your area. Work in a group with two or three classmates to learn about the kind of taxes being paid.

1. To learn about the taxes paid by people in your area, interview people. Ask adult relatives or friends who work to tell you what types of taxes are deducted from their pay. Call or visit officials in local government or search the Internet to learn about other taxes.
2. List all types of taxes paid by people who live and work in your city, county, or state. Include sales taxes, use taxes, excise taxes, income taxes, property taxes, and so on. You may find taxes listed on bills for phone, utilities, water, sewer, and garbage services. You will also find taxes on gasoline, cigarettes, and other luxuries.
3. To your list of local and state taxes, add federal income taxes, Social Security and Medicare taxes, workers' compensation taxes (if paid by employees in your state), and other taxes of any kind.

Taxes and Other Deductions

OUTCOMES

- Explain how taxes affect disposable income.
- List types of deductions required for taxes.
- Compute net pay.
- List examples of optional deductions from pay.
- Complete a Form I-9 and a Form W-4.
- Complete a federal income tax return.

TAXES AND DISPOSABLE INCOME

Wages, salaries, and profits from owning a business are taxable. Unearned income, such as interest from a savings account, is also taxable. As you learned earlier, *disposable income* refers to the money left to save or spend after taxes are paid. Lower taxes result in higher disposable income. Higher taxes result in lower disposable income.

REQUIRED DEDUCTIONS

Workers are required to have money withheld from their paychecks for income tax, Social Security tax, and Medicare tax. Other taxes and deductions may also be withheld. Many states have a state income tax. Some counties and cities have an income tax.

Taxes and payments for other items are subtracted from the worker's gross pay to calculate net pay. The paycheck stub in Figure 2-3.1 on page 46 shows a worker's gross earnings, deductions, and net pay.

Income Tax Withholding

Federal and state income taxes are withheld according to income amount and the number of exemptions claimed on Form W-4. A sample form is shown in Figure 2-3.2 on page 46. Exemptions are persons you claim on your tax return as dependents. The Internal Revenue Service provides details of how a person qualifies as a dependent. For example, your child who lives with you and for whom you provide more than 50 percent of living expenses would be a dependent. The more exemptions you claim, the less tax is withheld. Everyone is allowed to claim one exemption (unless that person is claimed as an exemption by someone else). People who are married or have children can claim more exemptions. Federal

FIGURE 2-3.1

This paycheck stub shows deductions taken from a worker's pay.

EMPLOYEE NAME	EMPLOYEE ID	PAY PERIOD	CHECK DATE	CHECK NO.	
Gloria M. Perez	482975	2/1/20-- thru 2/14/20--	2/21/20--	A001161	
EARNINGS		HOURS	RATE	THIS PERIOD	YEAR-TO-DATE
Regular	80	\$13.00	\$1,040.00	\$3,120.00	
Overtime					
TAXES					
			\$82.19	\$246.57	
			64.48	193.44	
			15.08	45.24	
			34.27	102.81	
			3.14	9.42	
			\$199.16	\$597.48	
DEDUCTIONS					
			\$150.00	\$450.00	
			12.00	36.00	
			52.00	156.00	
			10.00	30.00	
			\$224.00	\$672.00	
NET PAY			\$616.84	\$1,850.52	

income tax withholding rates can be viewed at the Internal Revenue Service Web site. A link to this site is provided on the Web site for this textbook.

Social Security Tax

Social Security tax is withheld by the federal government. The purpose of this tax is to provide a system of old-age, survivors, and disability insurance. The rate of the tax and the amount of income that is taxable change each year. In 2006, the rate was 6.2 percent on earnings up to \$94,200. Money withheld for this tax is paid into an account under your name and

FIGURE 2-3.2

Form W-4 shows the number of exemptions claimed.

Cut here and give Form W-4 to your employer. Keep the top part for your records.

Form **W-4** **Employee's Withholding Allowance Certificate** OMB No. 1545-0074
 Department of the Treasury Internal Revenue Service **2006**

▶ Whether you are entitled to claim a certain number of allowances or exemption from withholding is subject to review by the IRS. Your employer may be required to send a copy of this form to the IRS.

1 Type or print your first name and middle initial. Last name
Gloria M. **Perez**

2 Your social security number
000 22 2105

Home address (number and street or rural route)
123 Maple Street

3 Single Married Married, but withhold at higher Single rate.
 Note. If married, but legally separated, or spouse is a nonresident alien, check the "Single" box.

City or town, state, and ZIP code
Monticello, KY 42633-0123

4 If your last name differs from that shown on your social security card, check here. You must call 1-800-772-1213 for a new card. ▶

5 Total number of allowances you are claiming (from line H above or from the applicable worksheet on page 2) **5** **1**

6 Additional amount, if any, you want withheld from each paycheck **6** \$

7 I claim exemption from withholding for 2006, and I certify that I meet **both** of the following conditions for exemption.
 • Last year I had a right to a refund of **all** federal income tax withheld because I had **no** tax liability **and**
 • This year I expect a refund of **all** federal income tax withheld because I expect to have **no** tax liability.
 If you meet both conditions, write "Exempt" here ▶ **7**

Under penalties of perjury, I declare that I have examined this certificate and to the best of my knowledge and belief, it is true, correct, and complete.

Employee's signature (Form is not valid unless you sign it.) ▶ **Gloria M. Perez** Date ▶ **May 20, 20--**

8 Employer's name and address (Employer: Complete lines 8 and 10 only if sending to the IRS.) 9 Office code (optional) 10 Employer identification number (EIN)

For Privacy Act and Paperwork Reduction Act Notice, see page 2. Cat. No. 10220Q Form **W-4** (2006)

Department of Homeland Security U.S. Citizenship and Immigration Services		OMB No. 1615-0047; Expires 03/31/07	
Employment Eligibility Verification			
Please read instructions carefully before completing this form. The instructions must be available during completion of this form. ANTI-DISCRIMINATION NOTICE: It is illegal to discriminate against work eligible individuals. Employers CANNOT specify which document(s) they will accept from an employee. The refusal to hire an individual because of a future expiration date may also constitute illegal discrimination.			
Section 1. Employee Information and Verification. To be completed and signed by employee at the time employment begins.			
Print Name: Last <i>Perez</i>	First <i>Gloria</i>	Middle Initial <i>M.</i>	Maiden Name <i>Valdez</i>
Address (Street Name and Number) <i>123 Maple Street</i>		Apt. #	Date of Birth (month/day/year) <i>3/20/1979</i>
City <i>Monticello</i>	State <i>KY</i>	Zip Code <i>42633-0123</i>	Social Security # <i>000222105</i>
I am aware that federal law provides for imprisonment and/or fines for false statements or use of false documents in connection with the completion of this form.		I attest, under penalty of perjury, that I am (check one of the following): <input checked="" type="checkbox"/> A citizen or national of the United States <input type="checkbox"/> A Lawful Permanent Resident (Alien #) A _____ <input type="checkbox"/> An alien authorized to work until _____ (Alien # or Admission #) _____	
Employee's Signature <i>Gloria M. Perez</i>		Date (month/day/year) <i>May 20, 20--</i>	

Social Security number. The employer pays the same amount into your account. People who are self-employed must pay 12.4 percent on earnings up to \$94,200. Amounts may be different for the current year. Your account continues to grow as you are working and paying the tax. Social Security tax is also known as FICA because it was created by the Federal Insurance Contribution Act.²

Employers are required to verify that workers are eligible for employment. When a worker begins a job, the worker is required to complete Section 1 of Form I-9, Employment Eligibility Verification. Section 1 of the form is shown in Figure 2-3.3. The employee must enter a name, an address, and a Social Security number. The Social Security number recorded on this form is used to report Social Security taxes for the employee. The form also shows whether the employee is a citizen of the United States, a lawful permanent resident, or an alien who is authorized to work. The employer must verify the information by looking at certain documents. A U.S. passport, a driver's license, and a U.S. Social Security card are examples of these documents.

Medicare Tax

Medicare tax is withheld by the federal government. This tax pays for medical care for retired persons and those who receive Social Security benefits. In 2006, workers paid 1.45 percent on all earnings for this tax. The employer also pays the same amount into your account. In 2006, people who were self-employed paid 2.9 percent on all earnings.³ Amounts may be different for the current year.

² Social Security Online, "Electronic Fact Sheet," <http://www.ssa.gov/pubs/10003.html> (accessed February 23, 2006).

³ Ibid.



Focus on . . .

WORKPLACE SAFETY

All workers are entitled, by law, to a safe place to work. This includes safe working methods and safety training. Workers' compensation costs are based, in part, on the safety record of the company. Having a safe workplace and reducing the number of accidents or injuries benefits both workers and the company.

Safety begins with good work attitudes. Safety is part of everyone's job. All workers must understand safety needs and make safety a priority. Major work-related accidents, injuries, and illnesses are related to the following factors:

- Carelessness of workers
- Failure to use safety equipment
- Lack of awareness of dangers
- Not knowing how to avoid and reduce risks
- Lack of a practiced and workable emergency plan

An emergency plan is a vital part of safety. An effective emergency plan provides for the safety of workers, employees, visitors, and others. A good emergency plan has the following parts:

- Detailed steps to follow in an emergency
- A list of who is responsible for each activity
- A list of who has back-up roles
- A second plan in case one course of action fails
- A data back-up system
- A process to communicate status
- Practice drills so that everyone will know what to do in a real emergency

Emergency plans should be in writing and shared with everyone. If special training is required, it should be completed and practiced regularly.

Following an emergency plan helps prevent injuries in times of danger.



© Getty Images/PhotoDisc

Workers' Compensation Insurance

Workers' compensation is an insurance plan that pays medical and disability benefits to workers who are injured or contract diseases on the job. Benefits may be paid to the worker's family if the worker is killed on the job. The laws that cover workers' compensation vary by state. In some states, the entire cost of the insurance is paid by the employer. In other states, such as Oregon, the worker must also pay some fees related to workers' compensation. In those states, workers may have the fees deducted from their paychecks.



Workers' compensation provides benefits for people who are injured on the job.

OPTIONAL DEDUCTIONS

Employees may have optional deductions made from their pay. Full-time workers usually have benefits provided by the employer. Employees may share in the cost of some benefits, such as health insurance. Workers may also have money deducted from their pay for items such as the following:

- Health insurance
- Life insurance
- Disability insurance
- Dental insurance
- Vision insurance
- Long-term care insurance
- Savings plan
- Retirement plan
- Health flexible spending plan
- Stock purchase plan

FEDERAL TAX FILING

If you are a U.S. citizen or resident, whether you must file a federal income tax return depends upon your gross income, your filing status, your age, and whether you are a dependent. After taxes are filed the first time, the IRS may send paper forms to use in filing. Forms can be accessed online at the IRS Web site. A link to the site is found on the Web site for this textbook. Users can download, save, and print tax forms needed for filing federal tax returns.

a Control number		OMB No. 1545-0008		Safe, accurate, FAST! Use 		Visit the IRS website at www.irs.gov/efile .	
b Employer identification number (EIN) 00-000000				1 Wages, tips, other compensation \$25,688.00		2 Federal income tax withheld \$2,136.94	
c Employer's name, address, and ZIP code ABC Company 781 Weston Street Monticello, KY 42633-0781				3 Social security wages \$27,040.00		4 Social security tax withheld \$1,676.48	
				5 Medicare wages and tips \$27,040.00		6 Medicare tax withheld \$392.08	
				7 Social security tips		8 Allocated tips	
d Employee's social security number 000 22 2105				9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial Last name Suff. Gloria M. Perez 123 Maple Street Monticello, KY 42633-0123				11 Nonqualified plans		12a See instructions for box 12 D \$1,352.00	
				13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b	
				14 Other		12c	
						12d	
f Employee's address and ZIP code				15 State Employer's state ID number KY 00000		16 State wages, tips, etc. \$25,688.00	
				17 State income tax \$891.02		18 Local wages, tips, etc. \$27,040.00	
				19 Local income tax \$81.64		20 Locality name Mont.	

Form **W-2 Wage and Tax Statement** **2006** Department of the Treasury—Internal Revenue Service
Copy B—To Be Filed With Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

Form W-2

Form W-2 is used to report the taxable income a worker received during the calendar year. This form is required to prepare an income tax return. Employers are required to send workers a W-2 for the calendar year (January 1 through December 31) by the following January 31. A sample Form W-2 is shown in Figure 2-3.4. The information on the form is sent to the federal, state, and local governments as well as to the worker. Multiple copies are provided for the worker to attach to tax forms and to keep on file. If the worker's tax returns are filed in paper form, the appropriate copy should be attached to each return.

Note that the amount shown in box 1, *Wages, tips, other compensation*, and in box 16, *State wages, tips, etc.*, is \$25,688.00. This figure is the amount of gross pay less the money paid into a 401(k) plan. Money paid into a 401(k) plan is not subject to federal income taxes until it is withdrawn, usually during retirement. Some states also defer taxes on money paid into a 401(k) plan.

Form 1040EZ

Several different forms can be used to file a federal tax return. The form that should be used depends on the type of income and deductions claimed. Form 1040EZ, shown in Figure 2-3.5 on page 51, is designed for use by single and joint filers with no dependents. This is a simple, one-page form that can be completed using information found on the filer's Form W-2 and tax tables provided by the IRS. Refer to Figure 2-3.5 as you read the following points about Form 1040EZ. Note that this form

Form **1040EZ** Department of the Treasury—Internal Revenue Service **Income Tax Return for Single and Joint Filers With No Dependents (99) 2005** OMB No. 1545-0074

Label (See page 11.) **Use the IRS label.** Otherwise, please print or type.

Presidential Election Campaign (page 12)

Your first name and initial: **Gloria M.** Last name: **Perez**

If a joint return, spouse's first name and initial: Last name:

Home address (number and street). If you have a P.O. box, see page 11. Apt. no.: **123 Maple Street**

City, town or post office, state, and ZIP code. If you have a foreign address, see page 11. **Monticello, KY 42633-0123**

Your social security number: **000 22 2105**

Spouse's social security number:

▲ You must enter your SSN(s) above. ▲

Checking a box below will not change your tax or refund.

Check here if you, or your spouse if a joint return, want \$3 to go to this fund? You Spouse

Income Attach Form(s) W-2 here. Enclose, but do not attach, any payment.	1	Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2. Attach your Form(s) W-2.	1	25,688	00
	2	Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.	2		
	3	Unemployment compensation and Alaska Permanent Fund dividends (see page 13).	3		
	4	Add lines 1, 2, and 3. This is your adjusted gross income .	4	25,688	00
	5	If someone can claim you (or your spouse if a joint return) as a dependent, check the applicable box(es) below and enter the amount from the worksheet on back. <input type="checkbox"/> You <input type="checkbox"/> Spouse If someone cannot claim you (or your spouse if a joint return), enter \$8,200 if single ; \$16,400 if married filing jointly . See back for explanation.	5	8,200	00
	6	Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-. This is your taxable income .	6	17,488	00
Payments and tax	7	Federal income tax withheld from box 2 of your Form(s) W-2.	7	2,136	94
	8a	Earned income credit (EIC) .	8a		
	b	Nontaxable combat pay election.	8b		
9	Add lines 7 and 8a. These are your total payments .	9	2,136	94	
10	Tax . Use the amount on line 6 above to find your tax in the tax table on pages 24–32 of the booklet. Then, enter the tax from the table on this line.	10	2,256	00	
Refund Have it directly deposited! See page 18 and fill in 11b, 11c, and 11d.	11a	If line 9 is larger than line 10, subtract line 10 from line 9. This is your refund .	11a		
	b	Routing number	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
	d	Account number			
Amount you owe	12	If line 10 is larger than line 9, subtract line 9 from line 10. This is the amount you owe . For details on how to pay, see page 19.	12	119	06
Third party designee	Do you want to allow another person to discuss this return with the IRS (see page 19)? <input type="checkbox"/> Yes. Complete the following. <input checked="" type="checkbox"/> No				
Sign here Joint return? See page 11. Keep a copy for your records.	Designee's name	Phone no.	Personal identification number (PIN)		
Your signature	Date	Your occupation	Daytime phone number		
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation			
Paid preparer's use only	Preparer's signature	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN	
Firm's name (or yours if self-employed), address, and ZIP code	EIN	Phone no. ()			

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 23. Cat. No. 11329W Form **1040EZ** (2005)

is for 2005. The form for the current year may differ somewhat but will contain similar information.

- The filer's name, address, and Social Security number are entered in the boxes in the *Label* section near the top of the form. For a joint return, the spouse's name and Social Security number would also be included.
- In the *Income* section (lines 1 through 6), line 1 provides space to enter wages, salaries, and tips. Taxable interest of \$1,500 or less can be entered on line 2.
- Line 3 is for unemployment payments received and Alaska Permanent Fund dividends.
- Line 4 is for adjusted gross income. This amount is the total of lines 1, 2, and 3.
- Line 5 shows the amount that can be deducted from adjusted gross income. For a single filer, as shown in the figure, the amount is \$8,200. For a married couple filing jointly, the amount would be \$16,400. This amount is not counted as part of the income on which tax must be paid.
- Line 6 should have a 0 (zero) if line 5 (the deduction) is larger than line 4. This means you have no taxable income. Line 6 should show the amount of adjusted gross income (line 4) minus the standard deduction (line 5) if the line 4 amount is larger than line 5. This amount is the taxable income.
- Line 7 in the *Payments and tax* section should show the amount of federal income tax withheld. This number comes from a Form W-2.
- Line 8a is for an earned income credit (EIC). This is a credit for certain people who work. The credit may give the filer a refund, even if the filer does not owe tax. A separate worksheet can be completed by those who think they may qualify for an EIC. Line 8b is for nontaxable combat pay.
- Line 9 is for total payments (lines 7 and 8a).
- Line 10 is for the tax on the taxable income amount. The tax is found by looking at tax tables provided by the IRS. If filing using a paper form, you can find the tax tables in the paper booklet. Tax tables can also be found on the IRS Web site.
- Line 11a in the *Refund* section is where a refund amount, if any, appears. This amount is found by subtracting tax (line 10) from total payments (line 9).
- Line 12 in the *Amount you owe* section is where the amount of tax the filer has to pay, if any, appears. This amount is found by subtracting total payments (line 9) from the tax amount (line 10).
- The *Third party designee* section is where the filer can allow another person to discuss the tax return with the IRS.
- The *Sign here* section is where the filer signs and dates the form.
- If another party fills out the tax return, that person's information should be recorded in the *Paid preparer's use only* section.

Other Forms

Form 1040A is a two-page form that allows more options for income and deductions to be entered. Some sections require the filer to attach additional forms, often called schedules. Taxpayers might use Form 1040A instead of Form 1040EZ if they have more than \$1,500 in interest income. Form 1099-INT shows the interest income earned during the year. Form 1099-INT is shown in Figure 2-3.6 on page 53. This form is sent to individuals by the bank or other institution that pays the interest. If tax returns are filed in paper form, the appropriate copy of the form should be attached to the return.

FIGURE 2-3.6

Form 1099-INT shows interest income earned.

<input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		2005 Interest Income	
PAYER'S name, street address, city, state, ZIP code, and telephone no. First Bank 201 Main Street Monticello, KY 42633-0201		Payer's RTN (optional)	OMB No. 1545-0112 Form 1099-INT
PAYER'S Federal identification number 00-0827701	RECIPIENT'S identification number 000-22-0011	1 Interest income not included in box 3 \$ 2,500.00	
RECIPIENT'S name Mr. William Patel Street address (including apt. no.) 206 Brookhaven Drive City, state, and ZIP code Somerset, KY 42502-0206		2 Early withdrawal penalty \$	3 Interest on U.S. Savings Bonds and Treas. obligations \$
		4 Federal income tax withheld \$	5 Investment expenses \$
Account number (see instructions) 4000326	2nd TIN not. <input type="checkbox"/>	6 Foreign tax paid \$	7 Foreign country or U.S. possession
Form 1099-INT		Department of the Treasury - Internal Revenue Service	

Copy C For Payer

For Privacy Act and Paperwork Reduction Act Notice, see the **2005 General Instructions for Forms 1099, 1098, 5498, and W-2G.**

Technology Corner

E-FILING

E-filing is a fast, safe way to file a federal tax return electronically. In 2005, more than 68 million Americans filed their tax returns electronically. Several options are available for using e-file. The filer can hire an *Authorized IRS e-file Provider*. This is a tax preparer who is approved by the IRS and can e-file the tax return for you. Another option is to purchase or get free tax preparation software that supports e-filing. Users prepare the return and e-file using a computer with a modem.⁴

Some people can prepare and file a tax return online. This option is called Free File. It is available to filers who have \$50,000 or less of adjusted gross income. A link on the

IRS Web site takes users to a list of companies that provide free filing services. Each company may also have a list of requirements, so a company must be chosen carefully. Once a company is selected, the user answers questions and provides the information needed to complete the return. The filing company sends the return to the IRS electronically.

Using e-file provides fast results for those entitled to a refund. Refunds are often received much more quickly than when a paper return is filed. Having the refund deposited directly into a checking account makes receiving refunds fast and safe.

⁴ Internal Revenue Service, "Individual E-file Program Overview," <http://www.irs.gov/efile/article/0,,id=118451,00.html> (accessed March 9, 2006).

2-3 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. How does the amount of tax a person pays affect the person's disposable income?
2. List three types of required deductions for taxes.
3. How is net pay calculated?
4. What is an exemption as it relates to a Form W-4?
5. Give an example of a person who may qualify as a dependent and can be claimed as an exemption on your Form W-4.
6. What form must a new employee complete to provide a Social Security number and claim status as a citizen of the United States, a lawful permanent resident, or an alien who is authorized to work?
7. Medicare taxes pay for what services?
8. To whom does workers' compensation pay benefits?
9. List four factors related to workplace accidents and injuries.
10. List the parts of a good emergency plan.
11. List three optional deductions that might be taken from a worker's pay.

2-3 Activity 1 Complete Employment Forms



When you begin a new job, you will be asked to complete a Form I-9 and a Form W-4. Practice completing these forms in this activity.

1. Open and print the PDF file *CHO2 Form I-9* from the data files.
2. Complete the employee portion of the form at the top of page 2 using your information. If you do not have a Social Security number or want to keep your number private, use 000-22-1111 as the number. Refer to Figure 2-3.3 on page 47 for an example form.
3. Open and print the PDF file *CHO2 Form W-4* from the data files.
4. Complete the Employee's Withholding Allowance Certificate portion of the form using your information. If you do not have a Social Security number or want to keep your number private, use 000-22-1111. For this activity, indicate that you are single, and claim one exemption. Refer to Figure 2-3.2 on page 46 for an example form.

EXPLORING CAREERS IN FINANCE



Do you like to work with numbers? Would you enjoy creating long-term plans to reach goals? If the answer is yes, a career in finance might be right for you. Jobs in finance involve managing money and other assets. Banking, investments, and insurance are part of this career area. Retirement planning and financial counseling are also part of the finance career cluster.

Jobs in finance are found in government and in private companies. This job area also presents good opportunities for entrepreneurs. For example, accountants and financial advisors may form their own small businesses. The need for jobs in the finance area is expected to grow in the next few years. The outlook will vary somewhat by job.

Skills Needed

Some of the skills and traits needed for a career in finance include the following:

- Math skills
- Analytical skills
- Communications skills
- Computer skills
- Decision-making skills
- Problem-solving skills
- Honesty
- Leadership

Job Titles

Many jobs are available in the finance area. Some job titles for this career area include the following:

- Accountant
- Auditor
- Bank teller
- Budget analyst
- Claims adjuster
- Financial manager
- Insurance underwriter
- Loan officer
- Personal financial advisor
- Stockbroker (securities sales agent)
- Tax examiner

Explore a Job

1. Choose a job in finance to explore further. Select a job from the list above, or choose another job in this career area.
2. Access the *Occupational Outlook Handbook* online. A link to the site is provided on the Web site for this textbook.
3. Search for more information about the job you selected to answer these questions:
 - What is the nature of the work this job involves?
 - What is the job outlook for this job?
 - What training or qualifications are needed for this job?
 - What are the median annual earnings for this job (given in the Earnings section of the Web page)?

REVIEW

Summary

- Sources of earned income include wages, salaries, tips, commissions, and self-employment. Earned income is subject to income taxes and other taxes.
- Minimum wage is the lowest hourly pay rate allowed by law. Many states have minimum wage laws that set a rate higher than the federal rate.
- By law, overtime pay of at least 1½ times the regular rate must be paid for hours worked above 40 work hours in a week.
- Networking is the process of making contacts and building relationships with other people.
- Disposable income refers to the money a person has available to spend or save after taxes have been paid.
- Benefits are forms of pay other than salary or wages. Benefits can directly increase disposable income or can have the effect of increasing disposable income.
- Benefits such as profit sharing and retirement accounts provide valuable resources for workers later in their lives.
- Unearned income is money or benefits received without working directly to earn them. Examples of unearned income are interest and dividends.
- Paying taxes reduces the disposable income of an individual. This is the main cost of paying taxes for an individual.
- Government transfer payments are funded by taxes collected by the government. This is a benefit of paying taxes.
- Government goods and services are available to all people who qualify, regardless of taxes paid. This is a benefit of paying taxes.
- Required deductions for taxes reduce disposable income.
- Workplace safety is required by law; it is everyone's responsibility.
- If you are a U.S. citizen or resident, whether you must file a federal income tax return depends upon your gross income, your filing status, your age, and whether you are a dependent.
- E-filing is a fast, safe way to file a federal tax return electronically.

Key Terms

benefits
cafeteria plan
commission
disposable income
dividend
entrepreneur

excise tax
minimum wage
overtime pay
paid holidays
personal leave
profit

sick leave
tax
tip
transfer payments
unearned income

ACTIVITY 1

Review Key Terms

Use the key terms from Chapter 2 to complete the following sentences:

1. A(n) _____, or business owner, takes the risks of owning and operating a business.
2. Money received from sources other than working in a job is called _____.
3. Money left over to spend or save after taxes are paid is called _____.
4. Most companies have _____, such as Christmas, Veterans Day, or Memorial Day.
5. _____ is time away from work for personal reasons.
6. The lowest pay rate allowed by law for each hour of work is called _____.
7. Money received from customers, called a(n) _____, is based on quality of service.
8. _____ are forms of pay other than salary or wages, such as paid vacations or holidays.
9. Days you are paid for even though you are not at work due to illness are called _____.
10. Earnings that are paid only when efforts result in a sale are called a(n) _____.
11. Earnings paid when an employee works more than 40 hours in a 1-week period are called _____.
12. Money or benefits received from government without working for them when they are received are called _____.
13. A(n) _____ is cash paid to stockholders of a corporation.
14. A benefits package, called a(n) _____, is where employees can pick and choose the benefit options they want to have.
15. _____ are taxes charged on the purchase of specific goods, such as motor fuel, cigarettes, and alcohol.
16. A(n) _____ is a required payment for the support of a government.
17. _____ is the amount left after all costs are deducted from the income of a business.



ACTIVITY 2

Math Minute

Complete these problems to build your math skills. You may use spreadsheet software or complete the problems manually.

Gross pay includes regular hours times regular pay, plus overtime hours times overtime pay. The overtime pay rate is $1\frac{1}{2}$ times the regular rate of pay.

1. Max worked 44 hours last week. His hourly rate is \$6.00. What was his gross pay (regular pay plus overtime pay)?
2. Elaine worked 48 hours last week. Her hourly rate is \$7.50. What was her gross pay?
3. Jackson worked 44 hours last week. His hourly rate is \$8.60. He has the following deductions taken from his gross earnings. What was his net pay?
 - Federal income tax withheld at the rate of 10%
 - Social Security tax withheld at the rate of 6.2%
 - Medicare tax withheld at the rate of 1.45%
 - Health insurance premiums of \$12.80
 - Union dues of \$8.50
4. Rachelle worked 46 hours last week; her hourly rate is \$7.90. She has the following deductions taken from her gross earnings. What was her net pay?
 - Federal income tax withheld at the rate of 10%
 - Social Security tax withheld at the rate of 6.2%
 - Medicare tax withheld at the rate of 1.45%
 - Health insurance premiums of \$11.20

ACTIVITY 3

Professional Careers



www.thomsonedu.com/school/pfl

Work with a classmate to complete this activity. Pick a career in which the worker earns a salary, such as teacher, manager, or accountant. Do some online and library research or interview a worker in this profession to answer the following questions:

1. How many hours a week does a beginning-level employee work?
2. What is the beginning pay level?
3. What kinds of benefits currently are being offered to people in this profession?
4. Would you like to do this kind of work? Why or why not?

ACTIVITY 4

Unemployment Compensation



www.thomsonedu.com/school/pfl

When workers are laid off from their jobs, they may be entitled to unemployment compensation benefits. These benefits are taxable income. Each state has unemployment compensation rules; the federal government also has a program.

Visit your state Web site to find out how unemployment compensation laws and insurance work in your state. Find answers to the following questions:

1. What are the requirements for drawing unemployment benefits?
2. How is the amount of the benefit determined?
3. For how long can a person draw benefits?

ACTIVITY 5

Evaluate and Select Benefits



1. Open and print the *Word* file *CH02 Benefits* found in the data files. A cafeteria plan of benefit choices, along with their dollar value, is shown in the document.
2. Assume that your salary is \$1,600 per month and that your total benefits package (including salary) can total up to \$2,000.
3. Review and evaluate the list of benefits offered. Decide which ones would be of the most value to you. You can go over \$2,000 in total pay and benefits costs only if you wish to have any payments over \$2,000 deducted from your paycheck.
4. Indicate your choices on the form.

ACTIVITY 6

Complete Tax Form 1040EZ



1. Open and print the PDF file *CH02 Form 1040EZ* found in the data files.
2. Enter your name, address, and Social Security number in the boxes in the *Label* section of the form. If you do not have a Social Security number or want to keep your number private, use 000-22-1111 as the number. You are filing a single return.
3. Your Form W-2 shows that you have \$29,521.00 of taxable income. Enter this amount on line 1.
4. Your 1099-INT shows that you have \$421.00 in taxable interest. Enter this amount on line 2.

5. Find the total of lines 1, 2, and 3. Enter the total on line 4 for adjusted gross income.
6. On line 5, enter **\$8,200.00**, the amount for a single filer. This amount is not counted as part of the income on which tax must be paid.
7. Subtract the amount on line 5 from the amount on line 4 to find your taxable income. Enter this amount on line 6.
8. Your Form W-2 shows federal income tax withheld as \$2,850.00. Enter this amount on line 7.
9. Enter the amount shown on line 7 on line 9 for total payments.
10. Open the PDF file *2005 Partial Tax Tables* from the data files. Find the amount of tax that applies to the amount shown on line 6. Enter this amount on line 10.
11. Subtract the amount on line 9 from the amount on line 10. This is the amount of tax you owe. Enter the amount on line 12.
12. Sign and date the form in the *Sign here* section. Enter **Sales Associate** for your occupation. Enter your phone number.

ACTIVITY 7 Complete Tax Form 1040A



1. Open and print the PDF file *CH02 Form 1040A* found in the data files.
2. Enter your name, address, and Social Security number in the boxes in the *Label* section of the form. If you do not have a Social Security number or want to keep your number private, use 000-22-1111 as the number. You are filing a single return.
3. In the *Filing status* section, place an **x** in box 1 for Single.
4. In the *Exemptions* section, place an **x** in box 6a for Yourself. Enter **1** in the blank at the right (*Boxes checked on 6a and 6b*). Enter **1** in the box at the right on line 6d.
5. Your Form W-2 shows that you have \$28,429.00 of taxable income. Enter this amount on line 7.
6. Your 1099-INT shows that you have \$1,825.00 in taxable interest. Enter this amount on line 8a.
7. Find the total of lines 7 and 8a. Enter the total on line 15 for total income. Enter the same amount on lines 21 and 22 for adjusted gross income.
8. On line 24, enter **\$5,000.00** for the standard deduction for a single filer.
9. Subtract the amount on line 24 from the amount on line 22. Enter this amount on line 25.
10. On line 26, enter **\$3,200.00**, the amount for one exemption.
11. Subtract the amount on line 26 from the amount on line 25 to find your taxable income. Enter this amount on line 27.

12. Open the PDF file *2005 Partial Tax Tables* from the data files. Find the amount of tax that applies to the amount shown on line 27. Enter this amount on line 28. Enter the same amount on lines 36 and 38.
13. Your Form W-2 shows federal income tax withheld as \$2,726.00. Enter this amount on line 39. Enter the same amount on line 43 for total payments.
14. Subtract the amount on line 43 from the amount on line 38. This is the amount of tax you owe. Enter this amount on line 47.
15. Sign and date the form in the *Sign here* section. Enter **Sales Associate** for your occupation. Enter your phone number.

ACTIVITY 8

Emergency Plans



Work in a group with three or four other students to complete this activity.

1. You have learned that safety procedures and emergency plans are important in the workplace. Such plans are also important in schools. Consult your school handbook, the school Web site, or other materials available to learn about the emergency plans for your school. You may need to talk with a principal, counselor, or school safety or security officer.
2. Choose one of the following situations and find the plan that should be followed in that situation. Be prepared to share the main points of the plan with the class.
 - Fire in the building
 - Severe weather (tornado, hurricane, blizzard)
 - Bomb threat
 - Hostage situation
 - Chemical spill or other dangerous substance release
 - Bus accident
 - Other emergency