

EXAMPLE 2 Determining Taxable Income

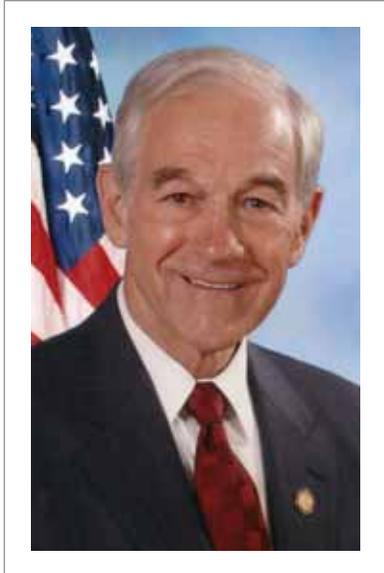
The Internal Revenue Service (IRS) estimates that about \$290 billion in income goes unreported each year in the United States. Which of the following do you think is part of your taxable income for the IRS?

- a. \$20 per week you receive for babysitting your niece
- b. \$500,000 you win in a state lottery
- c. \$40 per night you receive in tips as a food server
- d. \$1000 monthly payment by your employer for your medical insurance
- e. \$15 per month interest you receive from a savings account
- f. \$50,000 interest you receive from municipal bonds
- g. \$250,000 profit you receive from selling your home
- h. \$30,000 inheritance you receive from your spouse
- i. \$2000 per month you receive for child support from your former spouse

SOLUTION

IRS regulations are complicated and open to interpretation. In addition, there are annual changes to IRS regulations as to what constitutes taxable income. If an IRS audit claims that you owe more tax, you can hire an accountant and an attorney to challenge the audit. With that said, here is one tax accountant's opinion regarding the above list.

- a. Babysitting: This is a wage and is taxable.
- b. Lottery winnings: Lottery and gambling winnings are taxable.
- c. Tips: Tips are taxable.
- d. Employer-provided medical insurance: At this time, this is *not* taxable.
- e. Interest from savings accounts: This type of interest is taxable.
- f. Interest from municipal bonds: This interest is generally *not* taxable.
- g. Profit from the sale of a home: This is generally *not* taxable.
- h. Inheritance: Inheritance from a spouse is generally *not* taxable.
- i. Child support: This is *not* taxable.



Ron Paul is a congressman for the 14th Congressional District of Texas. His libertarian positions on political issues have often clashed with both Republican and Democratic party leaders. Paul ran for president of the United States in 1988 and 2008.

 **Checkpoint**

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Income taxes were imposed at various times in history, generally because of national emergencies. With the adoption of the 16th Amendment of the U.S. Constitution in 1913, the government established the present form of federal income tax. Some people, such as presidential candidate Ron Paul, have claimed that the amendment is unconstitutional. What do you think?

“Ron Paul supports the elimination of the income tax and the Internal Revenue Service (IRS). He asserts that Congress had no power to impose a direct income tax and has called for the repeal of the 16th Amendment to the Constitution, which was ratified on February 3, 1913.”

“End the Income Tax, Abolish the IRS,” *RonPaul.com*, 2009