

# PERSONAL INCOME TAXES

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# PERSONAL INCOME TAXES

## HISTORY OF INCOME TAXES

- Elementary Roots Go Back To Caesar Augustus...Birth Of Christ
- 14th & 15th Century...Florentine Republic
  - Property Tax evolved into Income Tax
- 1643...New Plymouth Colony...Tax on One's "Faculties"
  - Appears to be based on a Person's ability "personal efforts" => Income
- 1646...Mass Bay Colony..."Gains on Artisans and Tradesmen"
  - All Supplements to the Primary Tax Base....Property!!!
- 1861-1862...U.S. Enacted Income Tax to Finance Civil War
  - By 1864...Maximum Tax Rate = 10% on Income of \$10,000

Repealed In 1872...Not administered with much vigor!!

# PERSONAL INCOME TAXES

## HISTORY OF INCOME TAXES

- 1894...Congress enacted new law incorporating 1864 Laws
- 1895...Deemed Unconstitutional
  - Article I, Section IX, Clause IV..... "There Shall Not Be A Direct Tax!"
- 1909...Congress passed Joint Resolution to Amend the Constitution
- 1913...2/3rds of States Ratify 16th Amendment.....
  - "Congress Shall Have The Right To 'Lay' And 'Collect' Taxes on Income from Whatever Source Derived"!!
- 1913...Congress Passes Tax Law
- 1939..."Internal Revenue Code"...Tax Revisions and Codification of Rules
- 1954...Internal Revenue Code....Presently in Use...  
As Considerably Amended

# **PERSONAL INCOME TAXES**

**TAX LAWS ARE AS MUCH A PART OF OUR ENVIRONMENT AS THE AIR WE BREATHE!!!**

**The Laws Have Become The Basis For:**

- 1) Raising Revenue**
- 2) Encouraging Investments**
- 3) Promoting Economic Development**
- 4) Social Responsibilities**

# PERSONAL INCOME TAXES

## CONCEPTS OF INCOME:

- **Economic – Changes in the value of the assets, plus “consumption of goods/services” ....**

Asset Values, 2010	\$320,000	
Asset Values, 2009	\$170,000	
Increase in Asset Values		\$150,000
2010 Consumption of goods/services		<u>\$ 75,000</u>
Total Income		<u>\$225,000</u>
- **Accounting - Transactional**
  - **The Excess of 'Consideration' Received over The Cost of Goods and Services Rendered!!!**
- **Tax – Transactional**
  - **All inflows of Assets in excess of Cost Recovery...LESS all Non-Capital outlays**

# **PERSONAL INCOME TAXES**

## **TYPES OF INCOME:**

- 1. Earned Income – money received for personal effort**
- 2. Investment Income (portfolio income) – money received in the form of dividends, interest, capital gains, and rent from investment property**
- 3. Passive Income – money received from business activities for which you are not actively participating**
- 4. Miscellaneous Income – Awards/Alimony/Lottery winnings/Prizes**
- 5. Tax-Exempt Income – Interest received from the obligations of a state or municipality**
- 6. Tax-Deferred Income – Income that will be taxed at a later date such as IRA/Pension & Retirement Accounts**

# **PERSON INCOME TAXES**

## **Types Of Taxable Individuals:**

- A. Single (None Of The Below)**
- B. Married Filing Jointly (Married As Of 12/31)**
- C. Married Filing Separately**
- D. Head Of Household**
- E. Surviving Spouse**

# PERSONAL INCOME TAXES

## 2010 TAX RATES:

<u>Filing Status</u>	<u>10%</u>	<u>15%</u>	<u>25.0%</u>	<u>28.0%</u>
Single	\$0 - \$ 8,375	\$ 8,375 - \$ 34,000	\$ 34,000 - \$ 82,400	\$ 82,400 - \$171,850
Married-Jointly	\$0 - \$16,750	\$16,750 - \$ 68,000	\$ 68,000 - \$137,300	\$137,300 - \$209,250
Married-Separate	\$0 - \$ 8,375	\$ 8,375 - \$ 34,000	\$ 34,000 - \$ 68,650	\$ 68,650 - \$104,625
Head Of Household	\$0 - \$11,950	\$11,950 - \$ 45,550	\$ 45,550 - \$117,650	\$117,650 - \$190,550
Surviving Spouse	\$0 - \$16,750	\$16,750 - \$ 68,000	\$ 68,000 - \$137,300	\$137,300 - \$209,250
<u>Above Each of the Last Brackets</u>		<u>33.0%</u>		<u>35%</u>
Single		\$171,950 - \$373,650		\$373,650 and over
Married-Jointly		\$209,250 - \$373,650		\$373,650 and over
Married-Separate		\$104,625 - \$186,825		\$186,825 and over
Head Of Household		\$190,550 - \$373,650		\$373,650 and over
Surviving Spouse		\$209,250 - \$373,650		\$373,650 and over

**See IRS tax schedules (on PDF) to follow**



# PERSONAL INCOME TAXES

## 2010 Individual Standard Deduction (In Lieu of Itemized Deductions)

Single	\$ 5,700
Married (Filing Jointly)	\$11,400
Married (Filing Separately)	\$ 5,700
Head Of Household	\$ 8,400
Surviving Spouse (2 Years From Death)	\$11,400

→ Plus: Additional Amount for Over 65 or Legally Blind!!!

- Married and Surviving Spouses.....\$1,100 for each
- Single and Head of Household.....\$1,400

→ Plus: Additional Amount for Real Estate Taxes

- Married and Surviving Spouses.....\$1,000 for each
- Single and Head of Household.....\$ 500

→ Plus: Additional Amount for Sales Taxes on New Vehicle

- Deductible on the first \$49,500 of new vehicle cost

2010 Personal and Dependent Exemption    \$3,650

2009: \$3,650

2008: \$3,500

2007: \$3,400

2006: \$3,300

2005: \$3,200

2004: \$3,100

2003: \$3,050

2002: \$3,000

2001: \$2,900

2000: \$2,800

1999: \$2,750

# PERSONAL INCOME TAXES

## Examples:

In 2010, Jay is a single taxpayer with adjusted gross income of \$75,800 and taxable income of \$64,075, claiming one exemption. He also purchased a new car that cost \$38,000 and paid \$2,375 in sales taxes.

The tax is calculated as follows:

• First \$8,375 x 10%	=	\$ 837.50
• Next \$25,625 x 15.0%	=	\$ 3,843.75
• Next \$30,075 x 25.0%	=	<u>\$ 7,518.75</u>
Total tax	=	<u>\$14,745.00</u>

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In 2010, Meg and Mack are married taxpayers with gross income from wages of \$129,450 and taxable income of \$108,750, claiming two exemptions. They also paid Real Estate Taxes of \$6,500 on a new house.

The tax is calculated as follows:

• First \$16,750 x 10%	=	\$ 1,675.00
• Next \$51,250 x 15.0%	=	\$ 7,687.50
• Next \$40,750 x 25.0%	=	<u>\$10,187.50</u>
Total tax	=	<u>\$19,550.00</u>

# **PERSONAL INCOME TAXES**

## **INDIVIDUAL.....CONCEPT OF TAXABLE INCOME**

ALL INCOME (BROADLY DEFINED)

LESS

EXCLUSIONS (STATUTORY)

EQUALS

GROSS INCOME FOR TAX PURPOSES

LESS

DEDUCTIONS FOR ADJUSTED GROSS INCOME (IRA etc)

EQUALS

ADJUSTED GROSS INCOME

LESS

ITEMIZED DEDUCTIONS OR STANDARD DEDUCTION (greater of)

EQUALS

TAXABLE INCOME BEFORE EXEMPTIONS

LESS

PERSONAL AND DEPENDENT EXEMPTIONS

EQUALS

TAXABLE INCOME

**NET TAX LIABILITY = TAX ON TAXABLE INCOME LESS TAX CREDITS!!!**

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## **ITEMIZED DEDUCTIONS (broad categories):**

- 1. MEDICAL (limited)**
- 2. CHARITABLE CONTRIBUTIONS (cash/property)**
- 3. INTEREST EXPENSES (limited)**
- 4. TAXES**
- 5. CASUALTY LOSSES**
- 6. MISCELLANEOUS**

# PERSONAL INCOME TAXES

## ITEMIZED DEDUCTIONS:

### CONTRIBUTIONS:

...The Government encourages "Social Responsibilities"

- Cash Or Property...Property Is Deductible At Fair Market Value
- How about a Church Social....Can ONLY Deduct Only In Excess of FMV of the Services/Food Received!!!
- Personal Services.....Not Deductible...However....Use Of Car Is!!!

### MEDICAL EXPENSES

For The Cure...Mitigation...Control...Treatment...Prevention of Illness both Physical and Mental and Includes Also any Expenditures that affect the structure or function of the body

- 1) congenital abnormality
- 2) injury accident/trauma
- 3) disfiguring disease

DEDUCTIBLE TO THE EXTENT THAT THE TOTAL EXPENSES EXCEED 7.5% OF ADJUSTED GROSS INCOME

Examples of includable items:

- 1) Prescription Drugs/Medicines/Insulin
- 2) Medical Insurance Premiums...not life insurance or disability
- 3) Capital Expenditures....BY PRESCRIPTION....deductible in full to the extent that expenditure does not increase the fair market value of house
  - 1) Air Conditioner for asthma
  - 2) Swimming Pool for Heart ailment
  - 3) Elevator
- 4) Transportation costs
- 5) Eyeglasses
- 6) Psychiatric care
- 7) Lodging (with limitations) including accompanying individual)

# PERSONAL INCOME TAXES

## TAXES:

...Typically, Any Tax Imposed On The General Public For The General Public Welfare, Except Sales Taxes..(but partially allowed)...ALSO...Must Be State or Local...!!

### Not deductible:

- Fees Are Not Deductible....special benefits received
- Marriage licenses...fishing...hunting..

### Other Non-deductible Taxes:

- Gift/Inheritance
- Employee share of FICA taxes withheld
- Gasoline + Excise taxes
- Road Improvements/Betterments
- State or Local Sales Taxes (partially deductible)

### Deductible Taxes:

- Real Estate and Property Taxes (includes MV Excise in MA)
- Income Taxes (State and Local)
- State & Local Withholding Taxes Are Deductible + Last Year's balance paid This Year
- State And Local Income Tax Refunds are Includable In Income

## INTEREST:

...Generally...Interest Incurred for Debts of Personal Nature!! ...must be the Taxpayer's Liability!! (Co-Signed is Ok!!)

### Non-deductible Interest:

- Interest paid on Car Loans
- Interest paid on Credit Cards
- Interest paid on Consumer Credits Loans

### Deductible Interest:

- Points on a New Mortgage...Points from Refinancing requires amortization
- Interest paid on Qualified Residence Indebtedness"
- Home Equity Loans
- Borrow on H.E.L. to finance a car purchase and deduct interest!!!

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## OTHER DEDUCTIONS:

- Casualty And Theft Losses
- Miscellaneous Deductions (deductible to the extent that it exceeds 2% of AGI)
  - Tax return Preparation.....OK...must be paid in taxable year
  - Unreimbursed employee expenses....mileage and trave
  - Investment expense...advice...safe deposit box
  - Professional Dues/Union Dues/Business Subscriptions
  - Uniforms and Work Clothes
  - Job hunting expenses

# PERSONAL INCOME TAXES

## TAX INCENTIVES AND COLLEGE FINANCIAL PLANNING:

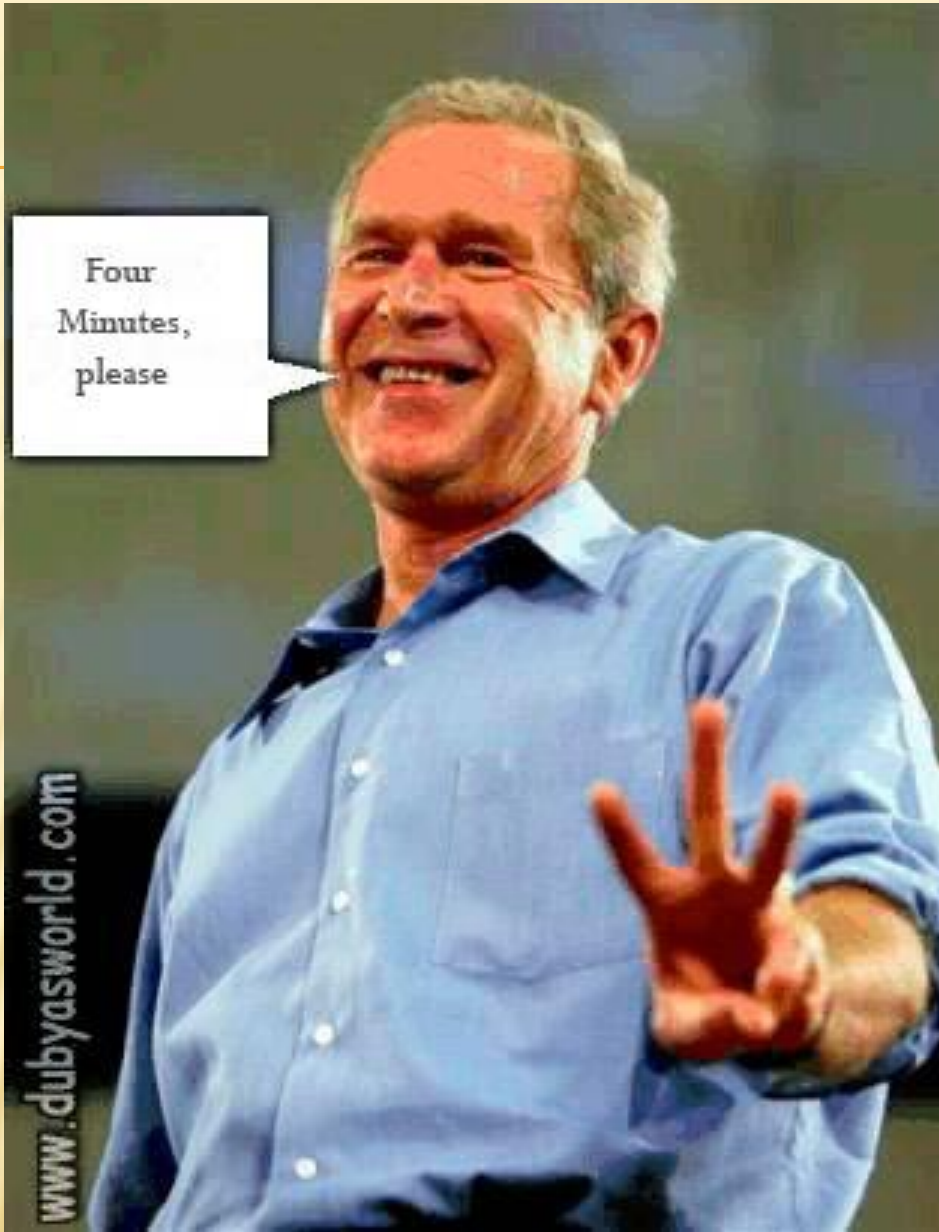
- The US Government has authorized two types of tax-advantaged investment accounts designed to help you save for college: Section 529 College Savings Plans (529 plans) and Coverdell Education Savings Accounts (CESAs). Your contributions to these plans aren't deductible, but 529 plans and CESAs both allow tax-free withdrawals to pay for qualified education expenses.
- You can also save for college by contributing to a Section 529 prepaid tuition plan. This type of account doesn't offer tax breaks on your investments, but it does allow you to pay tuition at today's rates no matter how old your child is. In other words, if you just had a baby, and if tuition at your local public college is now \$10,000 annually, you would be allowed to pay for the baby's future college costs at today's rate: \$10,000 per year. No matter how much tuition subsequently rises, you won't have to pay an extra penny when the child is old enough to start taking classes. This can greatly reduce the amount of money you may need to save for college, but it limits your child's college choices, as only some schools offer prepaid tuition plans.

**See 1040EZ tax return (on PDF) to follow**



TIM

BEAK!



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