

SOURCES OF INCOME

"Money doesn't grow on trees!" Have you ever heard this saying? It brings up a good question. How do you earn money? You may be surprised to find out that a job is not the only way to obtain money. In this lesson, you will look at the different ways people earn money or income.



OBJECTIVES

- Identify sources of income.
- Define key terms such as capital gains, dividends, commission, and interest.

VOCABULARY

capital gains	income earned by the sale of assets, such as stocks or property, which income is the difference between the price paid and the selling price
commission	a fee paid to an employee for their sale or services, which fee is usually based on a percentage of the sale price
dividends	money paid to people who own stock in a company from the company's earnings
income	the money received for work or products sold and from other sources, such as rent or investments
interest	money the bank gives you when you keep your money in one of their accounts
stockholder	an individual who owns one or more shares of stock in a joint stock company
taxable income	the portion of income that is subject to being taxed

Question #1 Matching

Match the terms to their definition.

1. capital gains	money paid to people who own stock in a company from the company's earnings
2. commission	an individual who owns one or more shares of stock in a joint stock company
3. dividends	money the bank gives you when you keep your money in one of their accounts
4. income	a fee paid to an employee for their sale or services, which fee is usually based on a percentage of the sale price
5. interest	the portion of income that is subject to being taxed
6. stockholder	income earned by the sale of assets, such as stocks or property, which income is the difference between the price paid and the selling price
7. taxable income	the money received for work or products sold and from other sources, such as rent or investments

SOURCES OF INCOME

We use money to make purchases and pay for services. But how do we acquire the money for that? Employment is the primary means of acquiring money, but there are other sources of **income**, as well. See if you can think of a few more ways that people receive money.

Perhaps you thought of gifts of money, allowance, or the money won in a lottery. Yes, these are sources of income. In some occupations, employees receive tips. A tip is also considered income. You may have had **interest** added to your savings account. If you let the bank keep your money, they pay you interest, and this gets added to your savings account. Interest from savings accounts is also considered income.

There are many sources of income. They are:

- salary;
- interest from accounts;
- capital gains;
- dividends from stock;
- commission;
- bonuses;
- gifts;
- winnings;
- tips;
- rent.

Some of these income sources are straightforward, and some need more explanation. Let's take a closer look at those that need more explanation.

Capital Gains

Capital gains is the income earned by the sale of assets, such as stocks or property. The gain is the difference between the purchase price and the selling price. In other words, this is your profit. Let's say you bought stock two years ago for \$2,000. Now, you decide to sell the stock. The stock has done well, and now you can sell it for \$3,200. You earned \$1,200. This is a capital gain and is considered income, as well. Let's look at another example. You bought a house ten years ago for \$125,000. You then sold it for \$199,000. What is the capital gain? \$74,000. Again, this is a source of income.

Commission

A **commission** is a fee paid to employees for their sale or services. The fee is usually based on a percentage of the sale price. Some sales representatives work solely on a sales commission, and others receive a salary plus commission. For example, Sharon works at a furniture store. She earns 9 percent commission on each sale. She just made a sale for \$10,000. Nine percent of \$10,000 equals \$900. For this sale, she earned \$900. This is her commission and part of her income.

Dividends

Dividends are money paid to people who own stock in a company. It is paid from the company's earnings or profit. A company reports its earnings on a quarterly basis, or once every three months. Based on these earnings, a company decides how much it will reinvest in the company, and how much it will pay the **stockholders**. The amount of dividend you receive depends on how many shares of the stock you own. Anita owns stock in company X. She received her account statement at the end

of the year. The statement showed that she owned 600 shares of the stock, worth \$9,552. Her dividends for the entire year were \$337.12. Not bad, but not enough to pay the rent.

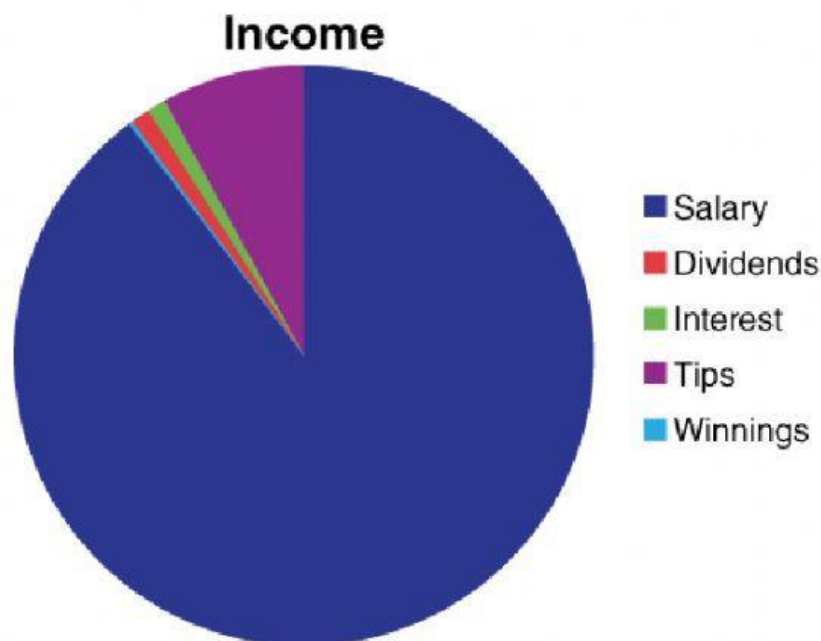
Rent

If you own rental property and you rent to another individual, the rent you collect from them is a source of income. In addition, if you own a house and you rent a room to a friend or roommate, the rent you collect from such a person is also a source of income.

So Money Does Grow on Trees!

It sounds like people can earn money in so many different ways that it practically grows on trees! How much are people really earning from all of these sources? Shelby asked her Aunt Colleen what percentage of her income comes from tips, interest, salary, dividends, and winnings. Her aunt said nearly 85 percent of her income is from her salary. That means just a small fraction of her income comes from other means.

Here are the results shown in a pie graph:



So, salary is, for the most part, the primary way to earn money. The other sources of income are very small in comparison. Because Aunt Colleen works as a hair stylist, a fair amount of her income comes from tips.

To test whether people obtain most of their income from their job, ask a few friends or adults what percentage of their income comes from each of the sources of income discussed in this lesson. You

can create a chart to help you visualize the information. Keep in mind that asking about someone's income can be a touchy subject, so asking about percentages should help.

Taxable Income

The state and federal governments require that you pay taxes on most of the income you earn. That means a certain percentage of the income must be sent to the government. It is called **taxable income**. For example, taxable income includes salary or tips received at work and interest received from a bank. You must pay taxes on these. In a few situations, it isn't necessary to pay taxes on income. For example, gifts or money given to you to repay a loan isn't taxable income.

Taxable income includes:

- salary;
- interest on any bank accounts;
- interest on all bonds except municipal (tax-free) bonds;
- dividends;
- bonuses;
- unemployment compensation;
- tips;
- capital gains;
- gambling and lottery winnings;
- most withdrawals from a retirement account.

In this lesson, you've learned many financial terms. Let's test your knowledge of these terms. Simply click the definition and drag it to line it up with the term it defines.

Question #2TrueFalse

Wages from an employer are the only source of income.

- ☐ True
- ☐ False

Question #3MultipleChoice

Tips are considered ____.

- ☐ dividends
- ☐ taxable income
- ☐ gains
- ☐ a bonus

Question #4MultipleSelect

Choose all that apply.

Select each source of income.

- ☐ a gift check from your great aunt
- ☐ a check from your roommate for rent
- ☐ interest deposited into your checking account
- ☐ a few dollars your friend loaned you
- ☐ the tip your client left you

Question #5MultipleChoice

Susan bought some land. She sold it for \$3,000 more than she paid for it. The \$3,000 is an example of ____.

- ☐ dividends
- ☐ interest
- ☐ rent
- ☐ capital gains

Question #6MultipleChoice

Rick works off commission. He earns 10 percent of all manufacturing equipment he sells. If he made a sale of \$9,000, how much was his commission?

- ☐ \$90
- ☐ \$900
- ☐ \$9,000
- ☐ \$100

Question #7MultipleChoice

When a company makes earnings or a profit, and they share this profit with the stockholders, it's called ____.

- ☐ interest
- ☐ gains
- ☐ dividends
- ☐ tips