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About Income

The total income that you earn is your **gross income**. The money that you take home is your **net income**: your gross income minus the withholdings and deductions that apply.

Since you can manage only the money that you receive, in this user guide income refers to your net income, the money that you can spend any way you choose.

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Everyday terms

Here are the everyday terms that apply to receiving income.

- How you receive your net income is referred to as a **paycheck** regardless of the type of income.
- You receive your paychecks on **payday**.
- A **pay period** is the duration of time during which you earn the money that will be paid to you on the payday at the end of the pay period. (e.g. monthly, twice monthly, weekly, every two weeks)
- Paydays can happen on:
 - the last day of each pay period, or
 - a designated number of days after each pay period.

Income types

There are three types of income:

- **Active** (earned) - Money earned from working that requires your time. You actively work and you are paid for it. Examples are:
 - salary
 - wages
 - bonuses
 - commissions
 - contract work
- **Portfolio** (unpredictable) - Money from selling an investment for more than what you paid (capital gains) or interest earned from an investment. Examples are:
 - stocks
 - bonds
 - mutual funds
 - buying/selling real estate or other assets such as automobiles
- **Passive** (inactive) - Money generated from assets you own or the proceeds from a benefit or trust fund where you are not actively working. Examples are:
 - rental income
 - business income (only if you are not required to be there)
 - company and military retirement

- social security benefits
- creating/selling intellectual property such as software

Income lifespan

Each income has a lifespan that indicates how long the income is expected to last.

- **For the foreseeable** future is when there is currently no known end to how long checks will be received.
- **A set number of times** is when a known number of checks will be received.
- **Until a date** is when checks will no longer be received on or after a given date.

Paychecks

Jobs are typically categorized by how a person's gross paycheck amount is calculated.

- **Salaried income** is when a person is paid a fixed amount regardless of how many hours they work during a pay period.
- **Hourly employment** is when the amount of each paycheck is the number of hours worked during a pay period times an hourly wage.
- **Unpredictable income** is when the amount earned depends on how often a task is accomplished, such as selling real estate, selling cars, or spending billable hours working with clients.

The way incomes are categorized in You Need A Cash Plan is the same except for salaried incomes when the paycheck amounts depend on the hours worked in a pay period.

- Always the same, or nearly the same (salaried)
- Based on time worked during each pay period (hourly and salaried with inconsistent paycheck amounts that depend on hours worked)
- Unpredictable

An example of a salaried income that is treated as an hourly income is a professional who earns \$400 per day working on Tuesdays and Thursdays.

Pay periods end on the 1st and 15th of each month, which means that the number of Tuesdays and Thursdays in each pay period can be different. The paycheck amounts for each pay period, therefore, can be different.

In You Need A Cash Plan this unpredictable salaried income is set up as an hourly income working eight hours per day on Tuesdays and Thursdays with an hourly rate of \$50 (\$400/8).

The net hourly rate used by You Need A Cash Plan to calculate expected paycheck amounts is calculated by dividing a net paycheck amount by the number of hours worked in the pay period. This calculation could look like this:

Paycheck amount after withholdings and deductions	\$1,312
Number of Tuesdays and Thursdays in the pay period	4
Number of hours worked	4 workdays * 8 hours/workday = 32
Net hourly rate used by PerNetFlow	$\$1,312 / 32 = \41

Payroll withholdings and deductions

The subtractions from your gross pay on payday are of two types:

- **Withholdings** - These are mandatory taxes. Your employer is required by law to withhold taxes from your paycheck and submit them to federal and state agencies on your behalf.

Federal and state laws dictate the amount of income taxes that you owe each calendar year. You set the amounts that you want withheld to pay those taxes. You reconcile your income tax withholdings for a year with the amount you owed by filing your federal and state tax returns the following year on or before April 15th. If you withheld too much you get a refund. If the amount withheld from your paychecks was not enough, you pay the difference with your return.

- **Deductions** - These are voluntary amounts for benefits and contributions that you choose, such as health insurance or donations to a charity. Involuntary amounts could also be court-ordered garnishments for child support, alimony, or wage attachments.

Here are the most common types of payroll withholdings and deductions:

Withholdings	Federal income tax	You fill in an IRS (#) W-4 form to specify how much you want withheld. (##)
	State income tax	How much is specified by each state.
	Social security (FICA) (###)	How much is specified by federal law.
	Medicare (FICA)	How much is specified by federal law.
Deductions	Insurance policy	Premium for employer insurance policy (more on insurance in Chapter 17) or contribution to your health savings account.
	Retirement	Employer retirement plan (typically 401(k)).
	Court-ordered garnishments	Child support, alimony or wage garnishments.
	Tax liens	Pay back taxes.
	Union dues	Union dues may be automatically deducted.
	Charitable contributions	Of your choice
	U.S. Savings Bond purchases	To learn about, go to treasurydirect.gov/savings-bonds
	Money owed your company	e.g. uniforms, tools or equipment

(#) IRS - Internal Revenue Service

(##) IRS Tax Withholding Estimator - irs.gov/individuals/tax-withholding-estimator

(###) FICA - Federal Insurance Contributions Act

An in-depth discussion of payroll withholdings and deductions is beyond the scope of this user guide. The intent here is to make you aware that the amount of your paychecks will be less than what you earned. Hopefully you will be informed of the details by your employer as part of your hiring orientation. For more details any time, check with your accounting office, payroll office, or your supervisor.

When paydays happen

There is no standard schedule for paydays. Paydays are set by whoever is issuing the paycheck.

- You Need A Cash Plan is a standard planning tool that works for everybody. For that to be possible, the unpredictability of paydays cannot be a part of the program's money management process. Removing the unpredictable receipt of paychecks from consideration in the program is accomplished by ignoring paydays. This is done on paydays by depositing your paycheck in full into your checking account, and
- Recording the deposit in You Need A Cash Plan.

You do nothing else with your paychecks. What this does is turn your checking account into a cash reservoir similar to the reservoir behind a dam. The water entering a dam reservoir arrives on its own natural schedule. The water accumulated in the reservoir can be used on a schedule that is not dependent on the river flowing in as long as the water outflow is not more than the river inflow.

Your income works the same way. Your checking account is your cash reservoir that is fed by your income deposits. You can plan how you will be using the money that accumulates in your checking account independent of when you get paid.