Where the Money Actually Comes From

A Plain-Language Guide to Taxes, Spending, and the Law Behind Them

Author: Jason D. McCoy — Pre-Failure Research Group

Version 1.0 — PFRG Inflation & Tax Burden Project, Part 1 of 2 — September 2026

Why This Exists

Every year, politicians on every side promise to cut your taxes, fix inflation, and stop government waste — usually all at once, usually without saying exactly how. This document does not argue for a side. It lays out, in plain language, what the law actually says, where the money actually comes from and goes, and what the real numbers are as of September 2026. Every figure here is checked against the primary source — the actual government agency or the actual text of the law.

> Part 2 of this project takes these facts and stress-tests the most common claims people make about fixing inflation and taxes at the same time. This document, Part 1, is the foundation everything else stands on.

Part One: Where the Government's Power to Tax and Spend Comes From

Before the numbers, it is worth answering a question a lot of people have but rarely see answered directly: when did the federal government get the authority to do any of this?

Taxing Your Income: The 16th Amendment (1913)

The Constitution always let Congress collect taxes. But for most of the 1800s, a national tax on people's income ran into a wall: any "direct" tax had to be divided up among the states based on population, which makes almost no sense for an income tax. In 1895, the Supreme Court used this rule to strike down an income tax law, and that stood as the law of the land for the next 18 years.

The 16th Amendment, ratified February 3, 1913, changed that. It says Congress can tax income "from whatever source derived" without dividing it up by state population. Congress passed the modern federal income tax almost immediately afterward. Everything in the tax code today traces back to this one amendment.

The Government's Power to Spend on Programs Like Social Security: 1936–1937

The Constitution gives Congress the power to spend for the "general welfare," but for over a century nobody was totally sure how far that went. One view (associated with James Madison) said Congress could only spend on things tied to its other specific powers. A broader view (associated with Alexander Hamilton) said Congress could tax and spend for the general welfare as its own standalone power.

The Supreme Court settled this in favor of the broader, Hamiltonian view in *United States v. Butler* (1936) and, a year later, *Helvering v. Davis* (1937) — which specifically upheld Social Security's payroll tax as constitutional. This is the legal foundation underneath almost every major federal program not tied to something like national defense.

> Worth knowing: this reading of the Constitution has been settled law for about 90 years, but it is still debated by some legal scholars who think the courts stretched the "general welfare" language further than originally intended. That is a real, ongoing disagreement in constitutional law, even though it has not changed how the government actually operates since the 1930s.

Part Two: The Numbers, As They Actually Stand Today

All figures below are current as of September 16, 2026, sourced directly from the Bureau of Labor Statistics (BLS), the Congressional Budget Office (CBO), the Internal Revenue Service (IRS), and the Government Accountability Office (GAO).

Inflation: What's Actually Driving It

As of August 2026, overall prices (CPI) were up 3.4% year over year. Core inflation, excluding food and energy, is running at just 2.4% — the lowest since March 2021. The gap comes down almost entirely to energy, up 16.3%, driven by a spike in global crude prices after shipping disruptions through the Strait of Hormuz — a chokepoint on the other side of the world, not a U.S. production problem.

Measure	12-Month Change
Overall inflation (CPI)	+3.4%
Core inflation (ex. food & energy)	+2.4%
Food	+2.7%
Energy	+16.3%
Shelter	+3.0%
Medical care services	+2.5%

The Federal Reserve Just Raised Rates

On September 16, 2026, the Federal Reserve's rate-setting committee voted unanimously (12–0) to raise its target rate a quarter point, to 3.75%–4.00%. The Fed said the economy is growing at a solid pace and investment is strong, but inflation remains above target.

The Federal Budget: Bigger Picture

Measure	FY2026 Amount
Revenue	$5.6 trillion
Spending	$7.4 trillion
Deficit	$1.9 trillion
Debt held by the public	~101% of GDP

The deficit is projected at $1.9 trillion this year alone, against a 50-year historical average of about half that, relative to the economy. CBO reported the actual deficit through the first 10 months of FY2026 was already about $1.8 trillion, $169 billion ahead of the same period last year.

Where the $5.6 Trillion in Revenue Actually Comes From

Source	FY2026 Amount	Share
Individual income tax	$2.75 trillion	49%
Payroll taxes (SS & Medicare)	$1.83 trillion	33%
Corporate income tax	$404 billion	7%
Customs duties (tariffs)	$418 billion	7%
Everything else	$197 billion	4%

> Corporate income tax is a little over $400 billion — smaller than customs duties, and less than a seventh the size of individual income tax. Individual income tax and payroll taxes together make up 82% of all federal revenue. Any plan promising large tax relief without touching those two sources is, mathematically, promising something that does not add up.

Individual Income Tax, As It Stands in 2026

The current brackets (10%, 12%, 22%, 24%, 32%, 35%, 37%) and standard deduction ($16,100 single / $32,200 married filing jointly) were made permanent by the One Big Beautiful Bill Act (OBBBA), signed July 4, 2025. Before that law, these rates were temporary and scheduled to expire.

Payroll Taxes — The Tax Most People Forget About

Every paycheck has payroll tax withheld: 6.2% for Social Security and 1.45% for Medicare, matched by your employer. Self-employed people pay both halves themselves — 12.4% and 2.9%. This structure has not changed at all in the current round of tax law, making it arguably the most stable number in the federal budget (see the table in Part Three).

The Tax Gap: Money Legally Owed But Not Paid

The IRS estimates that in 2022, about $696 billion in taxes were legally owed but not paid on time. After late payments and enforcement recover some of it, the net tax gap is about $606 billion. Most of it (74%) comes from individual income tax underreporting, not corporate avoidance.

Improper Government Payments

Federal agencies reported an estimated $186 billion in “improper payments” in FY2025. This is not the same as $186 billion in proven fraud — about $153 billion (82%) were overpayments, which can result from simple errors or outdated eligibility information, not necessarily theft.

Tariffs: A More Complicated Picture Than It Looks

Tariffs imposed under a law called IEEPA were struck down by the Supreme Court in February 2026 — the Court found the executive branch lacked authority to impose them that way, and no vote in Congress was ever taken on them at all. CBO now projects FY2026 tariff revenue will come in about

$250 billion below its earlier estimate, partly because roughly $166 billion already collected is expected to be refunded.

Part Three: How Tax Law Actually Gets Made — and Un-Made

A law is a law, whether it passed with two votes to spare or unanimous support. But how a law passed tells you something the text alone does not: how much scrutiny it got, and how easily a future Congress could undo it.

- **Budget reconciliation:** a special process letting certain budget bills pass the Senate with a simple majority (51 votes) instead of the 60 normally needed. Everything in the bill must be primarily budget-related (the “Byrd Rule”), and the Senate Parliamentarian can strike anything that does not qualify. This is how OBBBA passed (House 215–214; Senate 51–50, Vice President breaking a procedural tie).
- **Riding a “must-pass” bill:** bills that fund the government or the military tend to pass no matter what, so unrelated provisions sometimes get attached.

Where Today’s Tax Law Actually Came From

Provision	How It Became Law	How Easily It Could Change
Income tax brackets & deduction	Made permanent by OBBBA, via reconciliation	One future reconciliation bill, simple majority
Payroll tax (SS & Medicare)	Rooted in the 1930s Social Security Act	Most durable number in the tax code
Corporate tax rate (21% flat)	2017 tax law, via reconciliation	Rate unchanged; OBBBA changed write-off timing instead
Capital gains rates	Unchanged since 2012	Reconciliation-reversible, hasn’t moved in a decade+
Child Tax Credit	Made permanent by OBBBA; added SSN requirement	Reconciliation-reversible
Tariffs (until Feb. 2026)	Executive action under IEEPA — no vote at all	Already overturned by the Supreme Court

> The tax code you deal with every April is, legally speaking, one simple-majority vote away from changing. Payroll tax has not moved in decades and is the closest thing to a permanent feature of the system. Tariffs are not even laws passed by Congress at all — they can be imposed and struck down entirely through executive and judicial action, with no vote required at any point.

This research is presented for public understanding and does not constitute financial, legal, or tax advice. All figures are sourced to BLS, CBO, IRS, and GAO publications current as of September 16, 2026. Pre-Failure Research Group LLC, Iowa. Part 2 of this project, “Testing the Big Claims About Taxes and Inflation,” is available as a companion document.