## CHAPTER <br> Planning Guide



| Levels |  |  |  | Resources |  | Chapter Opener | Section 1 | Section 2 | Section 3 | Chapter Assess |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| BL | OL | AL | ELL |  |  |  |  |  |  |  |
| FOCUS |  |  |  |  |  |  |  |  |  |  |
| BL | OL | AL | ELL | B | Daily Focus Skills Transparencies |  | 74 | 64 | 66 |  |
| TEACH |  |  |  |  |  |  |  |  |  |  |
| BL | OL |  | ELL | $\square$ | Guided Reading Activities* |  | p. 25 | p. 26 | p. 27 |  |
| BL | OL | AL | ELL | 5 | Economic Content Vocabulary Activities* |  | p. 9 | p. 9 | p. 9 |  |
|  | OL | AL |  | $\square$ | Critical Thinking Activities |  | p. 14 | p. 14 |  |  |
| BL | OL |  | ELL | $\square$ | Reading Essentials and Note-Taking Guide* |  | p. 73 | p. 76 | p. 79 |  |
|  |  | AL |  | 5 | Enrichment Activities |  |  | p. 9 |  |  |
|  | OL | AL |  | $\square$ | Free Enterprise Activities |  |  | p. 14 |  |  |
| BL | OL | AL | ELL | $\square$ | Primary and Secondary Source Readings |  |  |  | $\begin{array}{\|l} \hline \text { pp. 14, } \\ 27 \\ \hline \end{array}$ |  |
| BL | OL | AL | ELL | $\square$ | Economic Cartoons |  |  |  | p. 19 |  |
| BL | OL | AL | ELL | 5 | Hands-On Economics |  |  | p. 19 |  |  |
| BL | OL | AL | ELL | $\square$ | Math Practice for Economics |  |  | $\begin{aligned} & \text { pp. 13, } \\ & 14 \end{aligned}$ | p. 13 |  |
| BL | OL | AL | ELL | B | Economics Forms and Financial Pages Transparencies, Strategies, and Activities |  |  | pp. 1, 3 |  |  |
| BL | OL | AL | ELL | $\square$ | Personal Finance Activities |  |  |  | p. 15 |  |
| BL | OL | AL | ELL | $\square$ | Reinforcing Economic Skills |  |  | pp. 4, 24 | $\begin{aligned} & \text { pp. 17, } \\ & 18 \end{aligned}$ |  |
| BL | OL |  | ELL | $\square$ | High School Reading in the Content Area Strategies and Activities | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| BL | OL | AL | ELL | 名 | High School Writing Process Transparencies | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| BL | OL | AL | ELL | $\square$ | Writer's Guidebook | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| BL | OL | AL | ELL | (3) | StudentWorks Plus CD-ROM | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| BL | OL | AL | ELL | (3) | Vocabulary PuzzleMaker CD-ROM | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |

[^0]
## Planning Guide

- Interactive Lesson Planner
- Differentiated Lesson Plans
- Interactive Teacher Edition
- Fully editable blackline masters
- Economics \& You videos
- Printable reports of daily assignments
- Standards tracking system

| Levels |  |  |  | Resources |  | Chapter | Section | Section | Section | Chapter |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| BL | OL | AL | ELL |  |  | Opener | 1 | 2 | 3 | Assess |
| TEACH (continued) |  |  |  |  |  |  |  |  |  |  |
| BL | OL | AL | ELL | $\square$ | Economics \& You Video Program DVDHow the Government Spends, Collects and Owes | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| BL | OL | AL | ELL | (3) | Graph Coach CD-ROM | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
| Teacher Resources |  |  |  | $\square$ | Differentiated Instruction Strategies | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
|  |  |  |  | $\square$ | Success with English Learners | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |
|  |  |  |  | (3) | Presentation Plus! CD-ROM | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ | $\checkmark$ |


| ASSESS |  |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| BL | OL | AL | ELL | 5 | Section Quizzes and Chapter Tests | p. 109 | p. 110 | p. 111 | $\begin{aligned} & \text { pp. 113, } \\ & 117 \end{aligned}$ |
| BL | OL | AL | ELL | $\square$ | Authentic Assessment Strategies and Activities | p. 14 |  |  |  |
| BL | OL | AL | ELL | (3) | ExamView ${ }^{\text {® }}$ Assessment Suite CD-ROM | 9-1 | 9-2 | 9-3 | Ch. 9 |
| BL | OL | AL | ELL | (3) | Interactive Tutor Self-Assessment CD-ROM | 9-1 | 9-2 | 9-3 |  |
| CLOSE |  |  |  |  |  |  |  |  |  |
| BL |  |  | ELL | $\square$ | Reteaching Activities* | p. 9 | p. 9 | p. 9 |  |
| BL | OL |  | ELL | $\square$ | Reading and Study Skills Foldables | p. 56 |  |  |  |

[^1]
## Chapter Overviews

## Technology Product

The Glencoe Web site offers in-depth overviews that summarize the content of each chapter. The overviews consist of brief chapter summaries and separate overviews for each section. The chapter overviews

- summarize and reinforce chapter content;
- provide discussion points to use in class.


## Objectives

The overviews help students

- prepare for better understanding of chapter content;
- practice reading and comprehension skills.


## Steps

Provide students with the following steps to complete the activities:

- Locate the Web page for the textbook being studied on the Glencoe Web site glencoe.com.
- Click on Student Center under the textbook title.
- Once you are in the Student Center, select a unit from the Unit Resources menu and a chapter from the Chapter Activities menu using the drop-down arrows.
- Click on the Chapter Overviews link.

Have students read the chapter overview in preparation for a reading assignment or activity.

| Economics |  |  |  |
| :--- | :---: | :---: | :---: |
|  | Student | Teacher | Parent |
|  | $\bullet$ | $\bullet$ | $\bullet$ |
| Beyond the Textbook | $\bullet$ | $\bullet$ | $\bullet$ |
| Chapter Overviews | $\bullet$ |  | $\bullet$ |
| ePuzzles and Games | $\bullet$ |  | $\bullet$ |
| Concepts in Motion | $\bullet$ |  | $\bullet$ |
| Multi-Language Glossaries | $\bullet$ | $\bullet$ | $\bullet$ |
| Online Student Edition | $\bullet$ |  | $\bullet$ |
| Self-Check Quizzes | $\bullet$ |  | $\bullet$ |
| Student Web Activities | $\bullet$ |  | $\bullet$ |
| Study Central ${ }^{\text {M }}$ | $\bullet$ | $\bullet$ | $\bullet$ |
| Time Current Events | $\bullet$ | $\bullet$ |  |
| Teaching Today |  |  | $\bullet$ |
| Vocabulary eFlashcards |  | $\bullet$ |  |
| Web Activity Lesson Plans |  |  | $\bullet$ |

Glencoe Media Center
》 glencoe.com
Study-To-Go

- Vocabulary eFlashcards
- Self-Check Quizzes
> Audio/Video
- Student Edition Audio
- Spanish Summaries
- Economics \& You Videos


## Additional Chapter Resources



- Timed Readings Plus in Social Studies helps students increase their reading rate and fluency while maintaining comprehension. The 400-word passages are similar to those found on state and national assessments.
- Reading in the Content Area: Social Studies concentrates on six essential reading skills that help students better comprehend what they read. The book includes 75 high-interest nonfiction passages written at increasing levels of difficulty.
- Reading Social Studies includes strategic reading instruction and vocabulary support in Social Studies content for both ELLs and native speakers of English. www.jamestowneducation.com


Use this database to search more than 30,000 titles to create a customized reading list for your students.

- Reading lists can be organized by students' reading level, author, genre, theme, or area of interest.
- The database provides Degrees of Reading Power ${ }^{\text {TM }}$ (DRP) and Lexile ${ }^{T M}$ readability scores for all selections.
- A brief summary of each selection is included.

Leveled reading suggestions for this chapter: For students at a Grade 10 reading level:

- Your Money at Work: Taxes, by Ernestine Giesecke

For students at a Grade 11 reading level:

- Other Revenue Sources Should Be Pursued, by William Straus
For students at a Grade 12 reading level:
- Careers Inside the World of the Government, by Sue Hurwitz
* Review suggested books before assigning them.


National Council on Economic Education

## Voluntary Standards Emphasized in Chapter 9

Content Standard 16 There is an economic role for government in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

Content Standard 20 Federal government budgetary policy and the Federal Reserve System's monetary policy influence the overall levels of employment, output, and prices.

## Resources Available from NCEE

- Virtual Economics ${ }^{\circledR}$ : An Interactive Center for Economic Education Version 3.0
- Civics and Government: Focus on Economics, Second Edition
- Capstone: The Nation's High School Economics Course
- Focus: Institutions and Markets

To order these materials, or to contact your State Council on Economic Education about workshops and programs, call 1-800-338-1192 or visit the NCEE Web site at store.ncee.net.

## The BIG Idea

As students study the chapter, remind them to consider the chapter-based Big Idea. The Essential Question in the chapter launch activity below ties in to the Big Idea and helps students think about and understand important chapter concepts. In addition, the HandsOn Chapter Project relates the content from each section to the Big Idea. The steps in each section build on each other and culminate in the Wrap-Up Activity on the Visual Summary page.


To generate student interest and provide a springboard for class discussion, access the Economics \& You Topic 14 video, How the Government Spends, Collects and Owes, at glencoe.com or on the video DVD.

FOLDABLES Study Organizer

Dinah Zike's Foldables are
three-dimensional, interactive graphic organizers that help students practice basic writing skills, review key vocabulary terms, and identify main ideas. Have students complete this chapter's Foldable activity or activities in Dinah Zike's Reading and Study Skills Foldables booklet. OL

## Economics ONLINE

Introduce students to chapter content and key terms by having them access Chapter 9 -Chapter Overviews at glencoe.com.

## Why It Matters

You have just received your first paycheck and are looking forward to being paid \$8 per hour for the 20 hours you worked. You look at your check and . . . "What? This check isn't for $\$ 160$ ! Where's the rest of my money?" Make a list of the deductions that might be subtracted from your earnings. Read Chapter 9 to learn more about how governments raise revenue.

## The BIC Idea

All levels of government use tax revenue to provide essential goods and services.


## Activity: Launching the Chapter

Identifying Have students identify at least two sources of revenue for the federal, state, and local (county or city) levels of government. Next have students identify at least two goods or services provided by each of those levels of government. Ask students to create a chart presenting the information they identified.

Essential Question: What is one
source of revenue collected by each level of government? (taxes) Have students write a paragraph explaining how they think each of the levels of government spends the tax money it collects.

## Focus

Bellringer
Daily Focus Transparency 74


## GUIDE TO READING

## Answers to Graphic:

Equity: should be fair and just
Simplicity: should be simple enough for taxpayers and tax collectors to understand

Efficiency: should be easy to administer and successful at generating revenue

An enormous amount of money is required to run all levels of governmentand the need seems to be growing every year. Taxes are the primary way to do this, and taxes affect the things we do in more ways than you think.

Governments levy a variety of taxes, from sales taxes on items we purchase in
stores to the income tax we have to pay on our wages. One way in which we try to minimize taxes is by finding all the exemptions and deductions we are allowed to claim when we file our income tax returns. That is what the students in the news story were doing: helping their clients get the largest refund possible.

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i. | Reading |
| :--- |
| Strategies |

## Teacher Edition

- Setting a Purpose, p. 230
- Predicting, p. 230
- Previewing, p. 232
- Identifying, p. 234


## Additional Resources

- Guid. Read. Act., p. 25
- Read. Ess. \& NoteTaking Guide, p. 73


## Critical Thinking

Teacher Edition

- Analyzing Visuals, p. 234
- Contrasting, p. 235
- Analyzing, p. 237

Additional Resources

- Authentic Assess., p. 14


## Differentiated Instruction

Teacher Edition

- Logical/Math., p. 231
- ELL, p. 233

Additional Resources

- Reteach. Act., p. 9
- Quizzes and Tests, p. 109


## 四 <br> Writing

Teacher Edition

- Expository Writing, p. 232
- Persuasive Writing, p. 236


## Additional Resources

- High School Writing Process Trans.

Teacher Edition

- Visual Literacy, p. 233
- Using Tables and Charts, p. 235


## Additional Resources

- Reading and Study Skills Fold., p. 56
- Economic Content Vocab. Act., p. 9


## Teach

## R1 Reading Strategy

## Setting a Purpose Remind

 students that they read for different reasons. Ask students to set a purpose for reading the chapter by thinking about what they want to gain from the text. Explain that setting a purpose will help students focus on important information as they read. BL
## R2 Reading Strategy

Predicting Ask: How might interest deductions affect a person's decision to buy a home? Explain. (Students will likely predict that interest deductions encourage people to buy homes because they can deduct the interest on their mortgages; this lowers the total amount of taxes that people owe.) OL

Caption Answer: Deductions lower the total amount of taxes that people pay.
$\sin$ tax relatively high tax designed to raise revenue and discourage consumption of a socially undesirable product

## 「Economic Impact of Taxes

MAIN Idea Taxes affect the decisions we make in a variety of ways.
Economics \& You Have you ever not bought something because you could not afford the tax on it? Read on to find out how taxes affect our behavior.

Taxes and other governmental revenues influence the economy by affecting resource allocation, consumer behavior, and the nation's productivity and growth. In addition, the burden of a tax does not always fall on the party being taxed.

## Resource Allocation

The factors of production are affected whenever a tax is levied. A tax placed on a good or service at the factory raises the cost of production and the price of the product.

People react to the higher price in a predictable manner-they buy less. When sales fall, some firms cut back on production, which means that some resourcesland, capital, and labor-will have to go to other industries to be employed.

## Behavior Adjustment

Taxes are sometimes used to encourage or discourage certain types of activities. For example, homeowners can use interest
payments on mortgages as tax deduc-tions-a practice that encourages home ownership. Interest payments on other consumer debt, such as credit cards, are not deductible-a practice that makes credit card use less attractive.

A so-called sin tax-a relatively high tax designed to raise revenue while reducing consumption of a socially undesirable product such as liquor or tobacco-is another example of how a tax can change behavior. For the tax to be effective, however, it has to be reasonably uniform from one city or state to the next so that consumers do not have alternative sales outlets that allow them to avoid the tax.

## Productivity and Growth

Taxes can affect productivity and economic growth by changing the incentives to save, invest, and work. For example, some people think that taxes are already quite high. Why, they argue, should they work to earn additional income if they have to pay much of it out in taxes?

While these arguments have validity, it is difficult to tell if we have reached the point where taxes are too high. For example, even the wealthiest individuals pay less than half of their taxable income to state and local governments in the form of income taxes. Are these taxes so high that people do not have the incentive to earn


Critical Thinking
Activities, p. 14

## Synthesizing Figures for Change in Government Revenues

Objective:
Learn how the government's revenues changed between 1995 and 1998.

Focus/Teach: Have students list what they believe are the three largest sources of government revenue. Write their ideas on the board. Then have students complete the activity.
Assess:
Close: Call on students to reveal their answers. Have students write a paragraph expanding upon their answer for question 6.

Differentiated Instruction Strategies
BL Ask: What does the table reveal about changes in the income tax rates between 1995 and 1998? (They Increased.)
AL Have students use the 2001
U.S. budget receipts to complete the activity again.
ELL Have students create a bar graph with the data from the completed table.

A tax on the producer increases the cost of production and causes a change in supply. Less of the tax can be shifted back to the taxpayer if demand is elastic, as in panel A . More of the tax can be shifted to the taxpayer if demand is inelastic, as in Panel B.
Economic Analysis If a tax is placed on medicine, who is likely to bear the
greater burden-the producer or the consumer?

an additional $\$ 10$ million because they can only keep half of it? Would they work any harder if income taxes took only 30 percent of their income? While we do not have exact answers to these questions, we do know that there must be some level of taxes at which productivity and growth would suffer.

## Incidence of a Tax

Finally, there is the matter of who actually pays the tax. This is known as the incidence of a tax-or the final burden of the tax.

Suppose a city wants to tax a local electric utility to raise revenue. If the utility is able to raise its rates, consumers will likely bear the burden of the tax in the form of higher utility bills. However, if the company's rates are regulated, and if the company's profits are not large enough to absorb the tax increase, then shareholders may get smaller dividends-placing the tax burden on the owners. The company
also might delay a pay raise-shifting the burden to its workers.

Supply and demand analysis can help us analyze the incidence of a tax. To illustrate, Figure 9.1 shows an elastic demand curve in Panel A and an inelastic demand curve in Panel B. Both panels have identical supply curves labeled S. Now, suppose that the government levies a $\$ 1$ tax on the producer, thereby shifting the supply curve up by the amount of the tax.

In Panel A, the product's market price increases by 60 cents, which means that the producer must have absorbed the other 40 cents of the tax. In Panel B, however, the same tax on the producer results in a $90-$ cent increase in price, which means that the producer absorbed only 10 cents of the tax. The figure clearly shows that it is much easier for a producer to shift the incidence of a tax to the consumer if the consumer's demand curve is relatively inelastic.

[^2]incidence of a tax final burden of a tax

## Hiflills Handbook See page R39 to learn about Formulating Questions.

## Differentiated Instruction

## Logical/Mathematical

Ask: What is the difference in curve D from Panel A to Panel B? (Curve D in Panel B is at a sharper vertical angle than curve $D$ in Panel A.) How do the shapes of the curves illustrate the concepts of elastic and inelastic demand? (In Panel $A$, the curve is more relaxed or flexible and is described as elastic. In Panel B, the curve is at a sharper angle and is more rigid; it is described as inelastic.) OL

Economic Analysis
Answer: the buyer

## Reading Check Answer: When

 businesses are taxed, they may decrease production, raise prices, or both. Consumers then may have access to fewer products and may pay higher prices.
## Leveled Activities

Reading Essentials and Note-Taking Guide, p. 73

The Economics of Taxation Biglea $\qquad$ $=\square$


CHAPTER 9 Sources of Government Revenue

## R Reading Strategy

Previewing Have students preview the subsection by scanning the main idea, headings, and images.
Ask: What do you think you will learn about in this subsection? Have students share their answers with another classmate. BL

## W Writing Support

Expository Writing Encourage students to imagine that they are writers for a current affairs magazine whose readers are middle school students. Ask them to write an article titled "The Economics of Taxation" that would be suitable for reading by that age group. OL

## DiddYouRnows

In the United States, the idea of taxing income goes back to the 1640s when the colony of Massachusetts Bay taxed the "faculties" (earning power) of individuals and the "returns and gains" of tradespeople and craftpersons.
 Student Web Activity Visit the Economics: Principles and Practices Web site at glencoe.com and click on Chapter 9-Student Web Activities for an activity on the individual income tax.
tax loophole exception or oversight in the tax law allowing a taxpayer to avoid paying certain taxes

## individual

 income tax federal tax levied on the wages, salaries, and other income of individuals
## Criteria for Effective Taxes

MAIN Idea To be effective, taxes must be equitable, easy to understand, and efficient.
Economics \& You Do you look forward to preparing your personal income tax returns? Read on to learn why you may be apprehensive about tax time.

Some taxes will always be needed, so we want to make them as fair and as effective W as possible. To do so, taxes must meet three criteria: equity, simplicity, and efficiency.

## Equity

The first criterion is equity, or fairness, which means that taxes should be impartial and just. Problems arise when we ask, what is fair? You might believe that everyone should pay the same amount. Your friend may think that wealthier people should pay more than those earning less.

There is no overriding guide to make taxes completely equitable. However, it does make sense to avoid tax loopholesexceptions or oversights in the tax law that allow some people and businesses to avoid paying taxes. Loopholes are fairness issues, and most people oppose them based on equity. As a result, taxes generally are viewed as being fairer if they have fewer exceptions, deductions, and exemptions.

## Simplicity

A second criterion is simplicity. Tax laws should be written so that both taxpayers and tax collectors can understand them. People seem more willing to tolerate taxes when they understand them.

The individual income tax-the federal tax on people's earnings-is a prime example of a complex tax. The entire federal code is thousands of pages long, and even the simplified instructions from the Internal

## CAREERS

## Certified Public Accountant

## The Work

* Prepare, analyze, and verify financial reports that inform the general public and business firms
* Provide clients with sound advice on tax advantages and disadvantages, and repare their income tax statements
* Establish an accounting system and manage cash resources


## Qualifications

* Strong mathematical skills and ability to analyze and interpret numbers and facts
* Ability to communicate results of analyses to clients and managers, both verbally and in writing
* Bachelor's degree in accounting, with many positions requiring an additional 30 hours beyond the usual 4-year bachelor's degree
* Successful completion of Uniform CPA Examination


Earnings

* Median annual earnings: \$50,770


## Job Growth Outlook

* Faster than average

Source: Occupational Outlook Handbook, 2006-2007 Edition

## Activity: Hands-On Economics

## Distinguishing Fact From Opinion

Tell students that failure to distinguish fact from opinion can complicate the debate over fairness and taxes. Remind students that facts can be proven but opinions are based on people's differing values and beliefs. Read aloud the following statements and ask students to identify which is a fact and which is an opinion.
a. The fairest tax is the one that everybody pays. (opinion)
b. The luxury tax on private aircraft led to higher unemployment among workers in that industry. (fact)
Have students search for editorials dealing with taxes in newspapers or magazines and identify other examples of facts and opinions in the writing. OL


Revenue Service (IRS) are lengthy and difficult to understand. As a result, many people dislike the individual income tax code.

A sales tax-a general tax levied on most consumer purchases-is much simpler. The sales tax is paid at the time of purchase, and the amount of the tax is computed and collected by the merchant. Some goods such as food and medicine may be exempt, but if a product is taxed, then everyone who buys the product pays the tax.

## Efficiency

A third criterion for an effective tax is efficiency. A tax should be relatively easy to administer and reasonably successful at generating revenue.

The individual income tax satisfies this requirement fairly well. An employer usually withholds a portion of an employee's pay and sends it to the IRS. At the end of the year, the employer notifies each employee of the amount of tax withheld so that the employee can settle any under- or overpayment with the IRS. Because of computerized payroll records, this withholding system is relatively easy.

After the close of the tax year on December 31 and before April 15 of the next year, employees file a tax return-an
annual report to the IRS summarizing total income, deductions, and taxes withheld. Any difference between the amount already paid and the amount actually owed is settled at that time. Most differences are due to deductions and expenses that lower the amount of taxes owed, as well as additional income not subject to tax withholding. State and local governments usually require tax returns to be filed at the same time.

Other taxes, especially those collected in toll booths on state highways, are considerably less efficient. The state has to invest millions of dollars in heavily reinforced booths that span the highway. The cost to commuters, besides the toll, is the wear and tear on their automobiles as they brake for toll booths along the road.

Efficiency also means that a tax should raise enough revenue to be worthwhile while not harming the economy. One example is the federal luxury tax on small private aircraft in the early 1990s. The IRS collected only $\$ 53,000$ in revenues during the first year of this tax because few planes were sold. This turned out to be less than the unemployment benefits paid to workers who lost jobs in that industry, so Congress quickly repealed that luxury tax.
$\sqrt{ }$ Reading Check Stating Why is equity important?

Highway Taxes In many states, you have to pay a toll to use certain roads. What does this photo imply about the efficiency of tolls?
sales tax general state or city tax levied on a product at the time of sale
tax return annual report by a taxpayer filed with the local, state, or federal government detailing income earned and taxes owed

CHAPTER 9, SECTION 1

## Skill Practice

Visual Literacy Ask students whether they have experienced a situation similar to the one shown in the image. Then ask: What is your opinion on the efficiency of toll roads? Record students' answers on the board under one of three headings: very efficient, somewhat efficient, or not efficient. Ask volunteers to comment on the outcome of the class tally. OL

## Differentiated Instruction

## English Language Learners

 Divide students into small groups. Have each group create three posters that illustrate the criteria for taxes. Ask for volunteers to display and explain the posters to the class. ELLCaption Answer: The photo implies that tolls are inefficient because they can cause traffic congestion.

## Reading Check Answer:

Equity assures that taxes will be impartial and just.

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## Additional Support

## Activity: Collaborative Learning

## Making Connections Ask students

 to raise their hands if they pay taxes. Ask a student whose hand was not raised if he or she buys clothing, gasoline, food, or magazines, and point out that in almost all states such articles are taxed when they are purchased. Ask another student whose hand was not raised if he or she attendsmusic concerts or sporting events, and point out that the cost of the ticket probably includes a special entertainment tax. Then have students choose a partner and create a chart containing two columns. In the first column, they will list goods or services they may have purchased in the last week on which they paid a tax. In
the second column, they will list goods or services they may have purchased in the last week on which they did not pay a tax. Have students compare and discuss their lists. OL

## C Critical Thinking

Analyzing Visuals Have students speculate about the condition of the road in the image. (lt has been repaired.)
Ask: What might have caused the road to deteriorate? (Possible answer: Heavy traffic and weather probably created wear and tear over time.) Invite students to give their opinions on the equity of gasoline and tire taxes. OL

## R Reading Strategy

Identifying Ask: How is the amount each person has to pay determined under the ability-topay principle? (The amount each pays depends on how much income each earns.) OL

Caption Answer: People who drive often may be the ones who can least afford to pay the taxes. In addition, benefits from the tax are hard to measure.

## $\sqrt{ }$ Reading Check Answer:

Answers will vary but should reflect an understanding of the principles of taxation.
benefit principle of taxation belief that taxes should be paid according to benefits received regardless of income
ability-to-pay principle of taxation belief that taxes should be paid according to level of income, regardless of benefits received

## Benefit Principle

 Gasoline and tire taxes are used to pay for the upkeep of roads. What are the limitations of gasoline taxes?
## Two Principles of Taxation

MAIN Idea Taxes can be levied on the basis of benefits received or the ability to pay.

Economics \& You Do you think the taxes you pay are fair? Read on to see if you prefer one principle of taxation over another.

Taxes in the United States are based on two principles that have evolved over the years. These principles are the benefit principle and the ability-to-pay principle.

## Benefit Principle

The benefit principle of taxation states that those who benefit from government goods and services should pay in proportion to the amount of benefits they receive.

Gasoline taxes are a good example of this principle. Because the gas tax is built into the price of gasoline, people who drive

more than others pay more gas taxes-and therefore pay for more of the upkeep of our nation's highways. Taxes on truck tires operate on the same principle. Since heavy vehicles like trucks are likely to put the most wear and tear on roads, a tire tax links the cost of highway upkeep to the user.

Despite its attractive features, the benefit principle has two limitations. The first is that those who receive government services may be the ones who can least afford to pay for them. Recipients of welfare payments or people who live in subsidized housing, for example, usually have the lowest incomes. Even if they could pay something, they would not be able to pay in proportion to the benefits they receive.

The second limitation is that benefits are often hard to measure. After all, the people who buy the gas are not the only ones who benefit from the roads built with gas taxes. Owners of property, hotels, and restaurants along the way are also likely to benefit from the roads that the gas tax helps provide.

## Ability-to-Pay Principle

The belief that people should be taxed according to their ability to pay, regardless of the benefits they receive, is called the ability-to-pay principle of taxation. An example is the individual income tax, which requires people with higher incomes to pay more than those who earn less.
This principle is based on two factors. First, we cannot always measure the benefits derived from government spending. Second, it assumes that people with higher incomes suffer less discomfort paying taxes than people with lower incomes.

For example, a family of four with an annual taxable income of $\$ 20,000$ needs every cent to pay for necessities. At a tax rate of about 13 percent, this family pays $\$ 2,623$-a huge amount for them. A family of four with taxable income of $\$ 100,000$ can afford to pay a higher average tax rate with much less discomfort.
$\sqrt{ }$ Reading Check Explaining Which principle of taxation do you prefer, and why?

## Extending the Content

Tax Equity Although the tax system has been modified to make it more equitable, it is impossible to have a system that is fair for everyone and that is seen by everyone as fair. An analysis of the benefit and ability-to-pay principles of taxation illustrates this point. As noted in the text on this page, it is often hard to measure exactly who benefits from a particular government service and even harder to assess how much benefit each person
receives. In addition, although two families may have equal incomes, because of different circumstances they may not have the same ability to pay. This difficulty in determining equity is one reason why there are several different kinds of taxes at the federal, state, and local levels.

Progressive, proportional, and regressive are the three main types of taxes.

## Economic Analysis Under which type of tax do individuals with lower incomes

pay a smaller percentage than do those with higher incomes?

| Type of tax | Income of \$10,000 | Income of \$100,000 | Summary |
| :---: | :---: | :---: | :---: |
| Proportional <br> (City income tax) | \$97.50 or 0.975\% of income | \$975.00 or 0.975\% of income | As income goes up, the percentage of income paid in taxes stays the same. |
| Progressive (Federal income tax) | $\$ 1,000$ paid in taxes, or 10\% of total income | $\$ 25,000$ paid in taxes, or $25 \%$ of total income | As income goes up, the percentage of income paid in taxes goes up. |
| Regressive <br> (State sales tax) | $\$ 5,000$ in food and clothing purchases, taxed at 4\% for a total tax of $\$ 200$ or $2 \%$ of income | $\$ 20,000$ in food and clothing purchases, taxed at $4 \%$ for a total tax of $\$ 800$ or $0.8 \%$ of income | As income goes up, the percentage of income paid in taxes goes down. |

## Three Types of Taxes

MAIN Idea All taxes can be broken down into three categories-proportional, progressive, and regressive

Economics \& You You just learned about two principles of taxation. Find out how the principles apply to different types of taxes.

Three general types of taxes exist in the United States today-proportional, progressive, and regressive. As Figure 9.2 shows, each type of tax is classified according to the way in which the tax burden changes as income changes. To calculate the tax burden, we divide the amount that someone pays in taxes by their taxable income. If a person pays $\$ 100$ in taxes on a $\$ 10,000$ income, then the tax burden is 0.01 , or 1 percent.

## Proportional Tax

A proportional tax imposes the same percentage rate of taxation on everyone, regardless of income. If the income tax rate is 20 percent, an individual with $\$ 10,000$ in taxable income pays $\$ 2,000$ in taxes. A person with $\$ 100,000$ in taxable income pays $\$ 20,000$.

If the percentage tax rate is constant, the average tax rate-total tax paid divided by the total taxable income-also is constant, regardless of income. If a person's income goes up, the percentage of total income paid in taxes does not change.

Few proportional taxes are used in the United States. One example is the 15 percent tax rate on corporate dividends. Regardless of overall income and how much someone receives in corporate dividends, individuals only pay 15 percent of that amount in personal income taxes.

Another example is the tax that funds Medicare-a federal health-care program available to all senior citizens, regardless of income. The Medicare tax is 1.45 percent of income, with no limit on the amount of income taxed. As a result, everyone who receives a paycheck pays exactly the same rate, regardless of the size of the paycheck.

## Progressive Tax

A progressive tax is a tax that imposes a higher percentage rate of taxation on higher incomes than on lower ones. This tax uses a progressively higher marginal tax rate, the tax rate that applies to the next dollar of taxable income.
proportional tax tax in which the percentage of income paid in tax is the same regardless of the level of income
average tax rate total taxes paid divided by the total taxable income

Medicare federal health-care program for senior citizens
progressive tax tax in which the percentage of income paid in tax rises as the level of income rises
marginal tax rate tax rate that applies to the next dollar of taxable income

## Skill Practice

Using Tables and Charts
Ask: What would happen if a state sales tax became progressive? (People who made more money would have to pay higher sales taxes than people who made less money.) OL

## G Critical Thinking

Contrasting Have students make a chart listing the three types of taxes and the characteristics of each. (Proportional tax: imposes the same percentage rate of taxation on everyone, regardless of income. Progressive tax: imposes a higher percentage rate of taxation on higher incomes than on lower ones. Regressive tax: imposes a higher percentage rate of taxation on low incomes than on high incomes.) As students read the subsection, have them record examples of each type of tax.

## Economic Analysis

Answer: progressive tax

> Hands-On Chapter Project

## Step 1

## Explaining Taxation and Revenue Systems

In this project, students will explore the taxation and revenue systems of all levels of government in the United States.
Step 1: Principles of Taxation and Types of Taxes. Students will identify and explain two principles of taxation and three types of taxes.
Directions: Organize the class into groups of three. Have them imagine that their
group has been hired by the U.S. Treasury Department to create visual presentations to help taxpayers understand the taxation and revenue system of the United States.
Tell students that their group will create a pamphlet for taxpayers explaining the two principles of taxation and the three types of taxes. The pamphlet should focus on the attractive features of each principle of taxation and clearly explain each type of taxes. The text used in the pamphlet should be correctly spelled and

## W Writing Support

Persuasive Writing Ask each student to take a position on the individual income tax: Does it work best as a progressive tax, or would it work better as a regressive or proportional tax? Have students write a persuasive essay arguing their position. Remind them to anticipate and address possible counterpoints made by people with opposing views. AL

## Reading Check Answer:

Answers will vary but should demonstrate knowledge of the three types of taxes.
regressive tax tax in which the percentage of income paid in tax goes down as income rises

## Assess

## Use the Interactive Tutor

Self-Assessment CD-ROM to review Section 1, and then assign the Section 1 Review as homework or as an in-class activity.

## Close

Evaluating Write the following on the board: The only fair tax is a tax on someone else. Then have students discuss how equity can be achieved in the tax system. OL

SECTION

For example, suppose the law required everyone to pay a rate of 10 percent on all taxable income up to $\$ 7,500$, and then a rate of 15 percent on all income after that. If someone had taxable income of $\$ 5,000$, this person would have to pay 10 percent on the 5,001 st dollar earned. In this case, the marginal tax rate on the 5,001 st dollar would be 10 percent.

However, if the same person had taxable income of $\$ 7,500$, then the marginal tax rate would be 15 percent on the 7,501 st dollar earned. In either case, the marginal tax is always the tax that is paid on the very next dollar of taxable income.

The individual income tax code used in the United States today is structured just this way. It currently starts at 10 percent and then jumps to 15 percent, 25 percent, 28 percent, 33 percent, and 35 percent, depending on the amount of taxable income. One important outcome of this structure is that progressively higher marginal brackets also cause the average tax rate to go up as taxable income goes up.

## Regressive Tax

A regressive tax is a tax that imposes a higher percentage rate of taxation on low incomes than on high incomes. For example, a person in a state with a 4 percent sales tax and an annual income of $\$ 10,000$ may spend $\$ 5,000$ on food and clothing and pay sales taxes of $\$ 200$ (or . 04 times $\$ 5,000)$. A person with an annual income of $\$ 100,000$ may spend $\$ 20,000$ on food and clothing and pay state sales taxes of $\$ 800$ (or . 04 times $\$ 20,000$ ).

On a percentage basis, the person with the lower income pays 2 percent (or $\$ 200$ divided by $\$ 10,000$ ) of income in sales taxes, while the person with the higher income pays 0.8 percent (or $\$ 800$ divided by $\$ 100,000)$. As a result, the 4 percent sales tax is regressive because the individual with the higher income pays a smaller percentage of income in sales taxes than does the individual with the lower income.
$\sqrt{ }$ Reading Check Synthesizing Which of the types
of taxes should be used for income taxes? Why?

7 Review

## Vocabulary

1. Explain the significance of sin tax, incidence of a tax, tax loophole, individual income tax, sales tax, tax return, benefit principle of taxation, ability-to-pay principle of taxation, proportional tax, average tax rate, Medicare, progressive tax, marginal tax rate, and regressive tax.

## Main Ideas

2. Describing Use a graphic organizer like the one below to describe the economic impact of taxes.

3. Identifying What are the criteria for effective taxes?
4. Summarizing What are the main points of the two principles of taxation?

## Critical Thinking

5. The BIG Idea Compare and contrast the characteristics of proportional, progressive, and regressive taxes.
6. Evaluating Using the criteria described in this chapter, how would you evaluate the effectiveness of the personal income tax?
7. Analyzing Visuals School districts often are supported by property taxes. These taxes are based on a percentage of the value of a house or other real estate. Look at Figure 9.2 on page 235. In which category of taxes does the property tax fall?

## Applying Economics

8. Equity Which of the two principles of taxation-the benefit principle or the ability-to-pay principle-do you think is more equitable? Explain your answer. Be sure to include in your answer how the two principles differ from one another.

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## Answers

1. All definitions can be found in the section and the Glossary.
2. resource allocation (factors of production are affected whenever a tax is levied); behavior adjustment (taxes can encourage or discourage certain activities); productivity and growth (taxes can change incentives to save, invest, and work); incidence of a tax (the final burden of a tax is determined by supply and demand)
3. equity, simplicity, and efficiency
4. The benefit principle states that those who benefit from government goods and services should pay in proportion to the amount of benefits they receive. The ability-to-pay principle states that people should be taxed according to their ability to pay, regardless of the benefits they receive.
5. A proportional tax applies the same tax rate. A progressive tax imposes a higher percentage rate of taxation on higher incomes than on lower ones, whereas a
regressive tax imposes a higher percentage rate of taxation on low incomes than on high incomes. All three types generate revenue that helps run the government.
6. Answers will vary, but students should evaluate whether the personal income tax is fair, efficient, and easy to understand.
7. proportional
8. Answers will vary but should demonstrate an understanding of the principles of taxation.

## Profiles in teonomics

## Monica Garcia Pleiman (1964-)

- president and CEO of OMS, a technology consulting firm
- publisher of Hispanic lifestyles magazine Latino SUAVE
- cofounder of the Latina Chamber of Commerce


## Small Start

Denver-based businesswoman Monica Garcia Pleiman knew early what she wanted to do with her life. As the daughter of a small business owner, she learned that "hard work and entrepreneurial skills" could bring financial success. She also took her high school's only computer class-and loved it. In 1987 Pleiman earned a degree in Information Science, a 95 percent male program. After working for both large corporations and small companies, she formed the consulting firm Optimum Management Systems (OMS).

## Small Business

Pleiman uses several successful strategies. Her practice of sharing the credit and allowing employees to grow in their jobs has resulted in a loyal OMS workforce-unusual in today's highly competitive, ever-changing technology sector. She tries to maintain a small-business environment while providing large-company benefits. She also focuses on serving small and minority businesses. Finally, she has taken advantage of assistance by the federal government's Small Business Administration, including attending the Minority Business Executive Program sponsored by the SBA.

These strategies have paid off. OMS grew 910 percent from its start in 1998 to 2003. Revenues over \$7 million per year make it one of the country's most successful minority-owned businesses. This success allowed Pleiman to branch out and publish a new bilingual
lifestyle magazine, Latino SUAVE.

## Examining the Profile

1. Summarizing What strategies helped Pleiman become a successful entrepreneur?
2. For Further Research What types of assistance does the Small Business Administration offer to entrepreneurs?
$\qquad$

## Teach

## G Critical Thinking

Analyzing Ask: What contributed to Pleiman's success as an adult? (Possible answers: She learned about running a small business from her family. She earned a degree in a maledominated field. With six brothers, she learned how to compete with men.) OL

## Examining the Profile

## Answers:

1. She created a loyal workforce by sharing credit with employees and allowing them to grow in their jobs, she maintained a smallbusiness environment while providing large-company benefits, she focused on serving small and minority businesses, and she took advantage of assistance by the SBA.
2. Students should research and report on the types of assistance offered by the SBA. long line of hard workers. Her Spanish ancestors settled Colorado 200 years ago. With six brothers, "I learned how to compete against men, to prove I could make it as a woman and as a minority."

## Activity: Collaborative Learning

Designing Have students work together in small groups to design a poster celebrating the life and achievements of a famous minority entrepreneur. Students might choose Monica Garcia Pleiman; other examples might include Mary Kay Ash, John Johnson, Anita Roddick, Oprah Winfrey, and Wilson Wong. Students should research the life of their chosen figure and decide how to convey the
information in a visually appealing way. Encourage students to include quotes from or about the entrepreneur or personal anecdotes that will help bring the figure alive for viewers. Display students' posters in the classroom.

## Additional Support

## Teacher Tip

Managing Time After dividing students into groups, ask them to begin by writing a plan of action that outlines who will do what and when. Such a plan encourages efficient use of time as students proceed through the various steps of the assignment.


## GUIDE TO READING

## Answers to Graphic:

Federal: individual income taxes, FICA taxes, borrowing, corporate income taxes, excise taxes, estate and gift taxes, customs duties, miscellaneous fees

State: intergovernmental revenues, sales taxes, individual income taxes, other revenues

Local: intergovernmental revenues, property taxes, utility revenues, sales taxes, other revenue sources


Internal
Revenue Service (IRS) branch of the U.S. Treasury Department that collects taxes

The first federal income tax was enacted by the Union government in 1861 to help finance the Civil War. It was repealed in 1872. A later income tax was found unconstitutional in 1893 , but it had the potential to be a major source of revenue.
It was not until the ratification of the Sixteenth Amendment in 1913 that Congress
could enact the current individual income tax. Since then, the top marginal tax rate has varied widely, from 1 percent for incomes over $\$ 3,000$ in 1913 to 94 percent for the highest incomes during World War II. The Internal Revenue Service (IRS) is the branch of the U.S. Treasury Department in charge of collecting taxes today.

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> Resource
> Manager

## $\square$ Reading Strategies

## Teacher Edition

- Monitoring, p. 241
- Making Connections, p. 243
- Summarizing, p. 245
- Act. Prior Know., p. 246


## Additional Resources

- Guid. Read. Act., p. 26
- Read. Ess. \& NoteTaking Guide, p. 76


## Critical <br> Thinking

Teacher Edition

- Det. Cause/Effect, p. 240
- Speculating, p. 242
- Problem-Solving, p. 244


## Additional Resources

- Reinforcing Econ. Skills, pp. 4, 24

Differentiated
Instruction

Teacher Edition

- Adv. Learners, p. 239
- Logical/Math., p. 240
- Visual/Spatial, p. 242


## Additional Resources

- Hands-On Econ., p. 19
- Math Prac. for Econ., pp. 13, 14
- Free Enterprise Act., p. 14 Skill Practice

Teacher Edition

- Expository Writing, pp. 239, 246
- Personal Writing, p. 241


## Additional Resources

- Writer's Guidebook
- Crit. Think. Act., p. 14

Teacher Edition

- Analyzing Graphs, pp. 240, 244
- Interpreting Political Cartoons, p. 243


## Additional Resources

- Econ. Forms and Fin. Pages Trans., Strat. \& Act., pp. 1, 3
- Enrichment Act., p. 9


## Federal Government Revenue Sources

MAIN Idea Individual income taxes, FICA, and borrowing constitute the main sources of government revenue.

Economics \& You Have you ever wondered what "FICA" on your pay stub means? Read on to find out about one of the main federal revenue sources.

The federal government gets its revenue from a number of sources. Taxes are the primary source of revenue, but borrowing also plays a big part. As shown in Figure 9.3, the four largest sources of government revenue are individual income taxes, Social Security taxes, borrowing, and corporate income taxes.

## Individual Income Taxes

The main source of federal government revenue is the individual income tax. In most cases, the tax is collected with a payroll withholding system, a system that
requires an employer to automatically deduct income taxes from a worker's paycheck and send them directly to the IRS.

Because inflation can push a worker into a higher tax bracket, the tax code is also indexed. Indexing is an upward revision of the tax brackets to keep workers from paying more in taxes just because of inflation. Workers might otherwise move into a higher tax bracket when they receive a pay raise that makes up for inflation.

## FICA Taxes

The second most important federal revenue source is FICA. FICA is the Federal Insurance Contributions Act tax, which is levied on employers and employees equally to pay for Social Security and Medicare. These two taxes are sometimes called payroll taxes because they are deducted from paychecks.
In 2007 the Social Security component of FICA was 6.2 percent of wages and salaries up to $\$ 97,500$. Above that amount, Social Security taxes are not collected, regardless of income. This means that a person with
payroll withholding system system that automatically deducts income taxes from paychecks on a regular basis
indexing adjustment of the tax brackets to offset the impact of inflation

FICA
Federal Insurance Contributions Act; tax levied on employers and employees to support Social Security and Medicare
payroll tax tax on wages and salaries deducted from paychecks to finance Social Security and Medicare

## Figure 9.3 Federal Government Revenue Sources



Source: Economic Report of the President, 2006

- In 2001 the federal government saved 1.7ç of every dollar it spent. By 2007, the government was borrowing 12.8 C for every dollar spent. The federal government now borrows more from investors than it collects from corporations in taxes.
Economic Analysis What is the percentage of total revenue for the first four items?


## Activity: Hands-On Economics

Comparing and Contrasting Ask students to compare the Social Security tax and the Medicare tax. Have them make a chart stating the purpose of each tax and the similarities and differences between the two taxes. (The taxes are both payroll deductions. However, Social Security is a proportional tax up to a $\$ 72,600$ income and regressive thereafter. Medicare tax is proportional because the individual pays the same percentage regardless of the amount of income.) Students may
also wish to provide several examples of incomes and the taxes levied on those amounts. Finally, ask students to hypothesize why the government handles the two taxes differently. OL

## CHAPTER 9, SECTION 2

## Teach

## Differentiated Instruction

Advanced Learners Have the class debate the following proposition: The only equitable type of tax is the individual income tax. Encourage students to take notes during the debate. Have them use these notes to write a paragraph supporting or challenging the proposition. AL

## W Writing Support

## Expository Writing Have

 students research the Social Security tax. Topics they might cover include its history, its original purpose, changes in collections and payments, its connection to the U.S. Constitution, or problems with the system. Ask students to present their findings in a written report. OL
## Economic Analysis

Answer: 2001-46.8\%;
2007-45\%

## S Skill Practice

Analyzing Graphs Ask: Which two countries have the lowest ratio of tax revenues to GDP? (the United States and Japan) BL

## D Differentiated Instruction

## Logical/Mathematical Have

 students determine what would be withheld for Social Security and Medicare from the paycheck of an individual who worked 40 hours at $\$ 6.50$ per hour. $(40 \times$ $\$ 6.50=\$ 260$ total pay; 6.2\% of $\$ 260=\$ 16.12$ for Social Security tax; 1.45\% of \$260 = \$3.77 for Medicare) Invite students to write similar word problems for other classmates to solve.
## G Critical Thinking

## Determining Cause and

 Effect Ask: Why has the federal government become more reliant on borrowing as a source of revenue? (because since 2001 it has spent more than it has collected) OL
## Differentiated Instruction

$\Omega$ The Global Economy
CTOU

## High Taxes-Are You Sure?

You examine your paycheck and are dismayed to see how much money has been taken out for taxes. Before you get too outraged, however, do the math. What percentage of the total amount has been withheld for taxes? Ten percent? Twenty percent? This is a far cry less than would be withheld in many other countries.

One measure of a country's tax burden is the ratio of its tax revenues to gross domestic product (GDP). Despite the criticism over high taxes in the United States, our federal government's revenues as a percentage of GDP are much lower than people realize. Sweden is usually ranked first as the country with the world's highest taxes, whereas the United States boasts one of the lowest tax revenue-to-GDP ratios in the industrial world.


Source: Organization for Economic Co-operation and Development (OECD)
corporate income tax tax on corporate profits
excise tax general revenue tax levied on the manufacture or sale of selected items
taxable income of $\$ 97,500$ pays the same Social Security tax- $\$ 6,045$-as does someone who earns $\$ 1,000,000,000$.

In 1965 Congress added Medicare to the Social Security program. The Medicare component of FICA is taxed at a flat rate of 1.45 percent. Unlike Social Security, there is no cap on the amount of income taxed, which makes it a proportional tax.

## Borrowing

Borrowing by the federal government is the third-largest source of federal revenue. Because tax revenues fluctuate, the government never knows exactly how much it will need to borrow. Therefore, it continues with its spending as allocated in the budget. If it does not collect enough money in taxes and user fees, it simply borrows the rest by selling bonds to investors.

Figure 9.3 shows that the federal government has become dependent on this source of funds, with the amount of money borrowed exceeding the total amount of taxes collected from corporations. The increased
borrowing has been mainly due to the increased levels of government spending since 2001 that have outpaced federal revenue collection.

## Corporate Income Taxes

The fourth-largest source of federal revenue is the corporate income tax-the tax a corporation pays on its profits. The corporation is taxed separately from individuals because the corporation is recognized as a separate legal entity.

Several marginal tax brackets, which are slightly progressive, apply to corporations. The first is at 15 percent on all income under $\$ 50,000$. The marginal brackets then rise slightly after that, and eventually a 35 percent marginal tax applies to all profits in excess of $\$ 18.3$ million.

## Excise Taxes

The excise tax-a tax on the manufacture or sale of selected items such as gasoline and liquor-is the fifth-largest source of federal government revenue. Some early

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Math Practice for
Economics, p. 13

## Analyzing a Paycheck

Objective: Understand the importance of analyzing a paycheck.
Focus: Ask how many students have received a paycheck. Have them share their understanding of the deductions listed on it.
Teach: Have students answer the activity questions.
Assess: Review the answers as a class.
Close: Ask students to explain what they might achieve by analyzing a paycheck.

## Differentiated Instruction Strategies

BL Fill in the paycheck stub and have students complete the questions about it.
AL Have students create three different paycheck stubs, each for 40-hour weeks but at differing pay rates.
ELL Have students create a chart that lists and defines gross pay, FICA, federal taxes, state taxes, retirement, and net pay.
excise taxes were on carriages, snuff, and liquor. Today federal excise taxes are levied on telephone services, tires, legal betting, and coal. Because low-income families spend larger portions of their incomes on these goods than do high-income families, excise taxes tend to be regressive.

## Estate and Gift Taxes

The estate tax is the tax on the transfer of property when a person dies. Estate taxes can range from 18 to 50 percent of the value of the estate, although estates worth less than $\$ 2,000,000$ are exempt. The exemption will be raised to $\$ 3,500,000$ by 2009 , but because these amounts are so high, fewer than 2 percent of all estates pay any tax at all.

The gift tax is a tax on the transfer of money or wealth and is paid by the person who makes the gift. The gift tax is used to make sure that wealthy people do not try to avoid taxes by giving away their estates before they die. Figure 9.3 shows that estate and gift taxes account for only a small fraction of total federal government revenues.

## Customs Duties

A customs duty is a charge levied on goods brought into the United States from other countries. The Constitution gives

Congress the authority to levy customs duties. Congress then can decide which foreign imports will be taxed and at what rate. Many types of goods are covered, ranging from automobiles to silver ore. The duties are relatively low and produce little federal revenue today. Before the enactment of the income tax amendment, however, they were the largest income source for the federal government.

## Miscellaneous Fees

Finally, only a fraction of federal revenue is collected through various miscellaneous fees. One example of a miscellaneous fee is a user fee-a charge levied for the use of a good or service. User fees were widely promoted by President Ronald Reagan, who wanted to find revenue sources that did not involve taxes.

User fees include entrance charges at national parks, as well as the fees ranchers pay when their animals graze on federal land. These fees are essentially taxes based on the benefit principle, because only the individuals who use the services pay them. People also seem more comfortable with them since they are not called "taxes."

## $\sqrt{ }$ Reading Check Explaining Why are corporations

 taxed separately from individuals?
gift tax tax paid by the donor on transfer of money or wealth
customs duty tax on imported products
user fee fee paid for the use of a good or service such as Kenai Fjords National Park in Alaska have to pay an entrance fee. How are user fees assessed?

CHAPTER 9, SECTION 2

## Reading Strategy

Monitoring Ask: What does the gift tax prevent? (It prevents wealthy people from trying to avoid taxes by giving away their estates before they die.) OL

## W Writing Support

Personal Writing Have students write a journal entry giving their opinion of user fees. Tell them to include whether they think the fees are equitable and why some people may be more comfortable with the fees since they are not called "taxes." OL

Caption Answer: They are based on the benefit principle, where only the individuals who use the services pay for them.

$\sqrt{ }$ Reading Check Answer:<br>Corporations are recognized as separate legal entities.

## Leveled Activities



## C Critical Thinking

Speculating Ask: What might happen to state services such as welfare, education, and hospitals if the federal government didn't help fund them? (Students will likely say that some state services would be nonexistent or would provide substandard service.) OL

## D <br> Differentiated Instruction

Visual/Spatial Have students keep a record of the total amount of sales taxes that they pay during a week. Ask: Did sales taxes play a role in your purchasing decisions? How would your spending behavior have differed if there were no sales tax? (Answers will vary but should reflect the personal impact ofsales taxes.) $\mathbf{O L}$

## Economic Analysis

Answer: The two largest sources of revenue for state governments are intergovernmental revenue and sales taxes. The two largest sources of revenue for local governments are intergovernmental revenue and property taxes.
intergovernmental revenue funds that one level of government receives from another level of government

## 羅

Skills Handbook
See page R50 to learn about Using Bar and Circle Graphs.

## State Government Revenue Sources

MAIN Idea States rely on funds from the federal government in addition to income taxes and sales taxes.

Economics \& You Do you ever wonder why you pay a tax on items you purchase in a store? Read on to learn about sales taxes.

State governments collect their revenues from several sources. Figure 9.4 shows the relative proportions of these sources, the largest of which are examined below.

## Intergovernmental Revenues

The largest source of state revenue consists of intergovernmental revenue-funds collected by one level of government that are distributed to another level of government for expenditures. States receive the majority of these funds from the federal
government to help fund the state's expenC ditures for welfare, education, highways, health, and hospitals.

## Sales Taxes

Most states also have implemented sales taxes to add to their revenue. A sales tax is a general tax levied on consumer purchases of nearly all products. The tax is a percentage of the purchase price, which is added to the final price the consumer pays. Merchants collect the tax at the time of sale. The taxes are then turned over to the proper state government agency on a monthly or other periodic basis. Most states allow merchants to keep a small portion of what they collect to compensate for their time and bookkeeping costs. The sales tax is the second largest source of revenue for states, although five states-Alaska, Delaware, Montana, New Hampshire, and Oregondo not have a general sales tax.

## Figure $9.4 \quad$ State and Local Government Revenue Sources



## Activity: Collaborative Learning

Behavior and Taxes To learn more about how taxes affect the behavior of taxpayers, divide students into groups of three to interview a variety of taxpayers in your community, including small-business owners, high school students with part-time jobs, large-business managers, and retired persons. Instruct students to ask their subjects to name federal, state, and local taxes that they pay. Students should then ask their subjects to
describe how paying taxes affects their economic behavior-hiring new workers, expanding the business, buying products, saving, and so on. Have each pair of students compile and summarize their findings, making special note of any differences among the four groups of taxpayers interviewed. Invite a volunteer from each group to share their findings with the class. OL


## Individual Income Taxes

All but seven states-Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming-rely on the individual income tax for revenue. The tax brackets in each state vary considerably, and taxes can be progressive in some states and proportional in others.

## Other Revenues

States rely on a variety of other revenue sources, including interest earnings on surplus funds; tuition and fees collected from state-owned colleges, universities, and technical schools; corporate income taxes; and hospital fees.

While the percentages for revenue sources in Figure 9.4 are representative of most states, wide variations among states exist. For example, Alaska is the only state without either a general sales tax or an income tax, so it has to rely on other taxes and fees for its operating revenue.
$\sqrt{ }$ Reading Check Contrasting How do states without individual income taxes find sources of revenue?

## Local Government Revenue Sources

MAIN Idea Local governments rely mostly on intergovernmental revenue and property taxes.
Economics \& You Do you hope to own a house some day? Read on to learn how this will add another tax to those you are already paying.

Like state governments, local governments have a variety of revenue sources, as shown in Figure 9.4. These sources include taxes and funds from state and federal governments. The main categories are discussed below.

## Intergovernmental Revenues

Local governments receive the largest part of their revenues-slightly more than one-third-in the form of intergovernmental transfers from state governments. These funds are generally intended for education and public welfare. A much smaller amount comes directly from the federal government, mostly for urban renewal.

Taxes Most people have to pay taxes to all levels of government. What does the cartoon imply about the impact of taxes on people?

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## Activity: Interdisciplinary Connection

History Before the Civil War, the federal government collected most of its revenues from tariffs, or taxes on imports, and from the sale of public lands. During the war, a variety of taxes, including a 5 percent income tax, were imposed to pay for the costs of fighting. After the war, many of these taxes were dropped, but others, including increased property taxes, were added. However, the typical homeowner paid only about $\$ 90$ in
annual property taxes and only about 1 percent of the population ever paid income tax. By 1872, no one was paying income tax because the tax had been repealed. Have students identify which parts of the U.S. Constitution deal with taxation. OL

## Skill Practice

Interpreting Political Cartoons Ask: What is the importance of the chart hanging on the wall? (It shows a drop in production.) How do the visual clues relate to the cartoon's quote? (Both the clues and the quote indicate that the employee is not motivated to work.) OL

## $R$ Reading Strategy

Making Connections Have students identify the state and local taxes they pay. (Possible answers: sales tax, individual income tax, user fees) Then have them consider the state and local taxes they might pay if they were business owners. (Possible answers: corporate income tax, property tax, various license and user fees) OL

Caption Answer: Taxes affect productivity and economic growth by changing incentives for people to save, invest, and work.
$\sqrt{ }$ Reading Check Answer: They rely on other taxes and fees.

## Additional Support

## CHAPTER 9, SECTION 2

## S Skill Practice

Analyzing Graphs Have students identify their states' level of taxes and then compare and contrast the level with that of neighboring states. (Answers will vary according to students' location.) OL

## C Critical Thinking

Problem-Solving Ask: What is the main disadvantage of property taxes? (It is difficult to assign value to personal property.) How do most communities solve this problem? (They hire one or more individuals to assess the value of a few big-ticket items such as buildings and motor vehicles. Other property taxes are seldom collected.) OL

## Economic Analysis

Answer: Highest level of taxes: Maine, Washington D.C., New York, Hawaii, Rhode Island. Lowest level of taxes: Alaska, New Hampshire, Delaware, Tennessee, Alabama

## Hands-On Chapter Project

## Step 2

## Explaining Taxation and Revenue Systems

## Step 2: Revenue Systems at the Federal, State, and Local Levels.

 Students will examine the federal, state,and local government's revenue systems, Students will examine the federal, state,
and local government's revenue systems, and provide examples of at least three revenue sources at each level.

State income is the sum of all income earned by all people in the state. State and local governments receive a percentage of that income as tax revenue from a number of sources. The five states without sales taxes-Alaska, Delaware, Montana, New Hampshire, and Oregon-rely on other taxes to provide state revenues.
Economic Analysis Which states have the highest level of taxes? The lowest level?

property tax tax on tangible and intangible possessions such as real estate, buildings, furniture stocks, bonds, and bank accounts
tax assessor person who examines and assesses property values for tax purposes

## natural

 monopoly market structure in which average costs of production are lowest when a single firm exists (also see page 176)
## Property Taxes

The second-largest source of revenue for local governments is the property tax-a tax on tangible and intangible possessions. Such possessions usually include real estate, buildings, furniture, farm animals, stocks, bonds, and bank accounts. Most states also assess a property tax on automobiles.

The property tax that raises the most revenue is the tax on real estate. Taxes on other personal property, with the exception of automobiles, are seldom collected because of the problem of valuation. For example, how would the tax assessor-the person who assigns value to property for tax purposes-know the reasonable value of everyone's wedding silver, furniture, clothing, or other tangible property? Instead, most communities find it more efficient to hire one or more individuals to assess the value of a few big-ticket items such as buildings and motor vehicles.

## Utility Revenues

The third-largest source of local revenue is the income from public utilities that supply water, electricity, sewerage, and even telecommunications. Because of economies of scale, many of of these companies are natural monopolies.

A community needs only one set of electrical power lines or underground water pipes, for example, so one company usually supplies all of the services. When people pay their utility bills, the payments are counted as a source of revenue for local governments.

## Sales Taxes

Many cities have their own sales taxes. Merchants collect these taxes along with the state sales taxes at the point of sale. While these taxes typically are much lower than state sales taxes, they are the fourth most important source of local government revenues.

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Directions: Ask student groups to work together to complete Step 2. One group member should examine federal revenue sources, another group member should examine state revenue sources, and the third group member should examine local government revenue sources. After gathering information, the group members will come back together to
create a booklet, using illustrations and correct grammar and punctuation, to report their findings.
Identifying Have students give an example of a source of revenue at the federal, state, and local levels. OL
(Chapter Project continued in Section 3.)

## Other Revenue Sources

Figure 9.4 on page 242 shows a variety of ways in which local governments collect their remaining revenues. Some local governments receive a portion of their funds from hospital fees. Others may collect income taxes from individuals and profit taxes from corporations. Still another revenue source for local governments is the interest on invested funds.

If local governments spend more than they collect in revenues, they can borrow from investors. While borrowed funds are small compared to those of the federal government, they form an important source of local government funding.

Local governments look for revenues in a number of ways. Still, the revenue sources available in general are much more limited than those available to the state and federal levels of government.

[^3]

Tax Assessments Tax assessors determine the value of property for tax purposes. Why are property taxes important for local communities?


## Vocabulary

1. Explain the significance of Internal Revenue Service (IRS), payroll withholding system, indexing, FICA, payroll tax, corporate income tax, excise tax, estate tax, gift tax, customs duty, user fee, intergovernmental revenue, property tax, tax assessor, and natural monopoly.

## Main Ideas

2. Listing Use a graphic organizer like the one below to list the federal government's major revenue sources.

3. Describing How do the major revenue sources for state and local governments differ?

## Critical Thinking

4. The BIG Idea Federal, state, and local governments receive revenue from various sources. Which source do you think best satisfies the tax criteria discussed in Section 1? Defend your answer in a written paragraph.
5. Drawing Conclusions Why do you think sales taxes are generally applied to food and beverages purchased in restaurants, but not to those purchased in stores?
6. Analyzing Visuals Look at Figure 9.4 on page 242. Why do you think the revenue from income taxes and property taxes differ so much between state and local governments?
7. Synthesizing How do excise taxes differ from other taxes such as sales taxes or estate taxes?

## Applying Economics

8. User Fees User fees have been compared to taxes based on the benefit principle of taxation. Define user fees in your own words. What are the pros and cons of user fees for national parks?

## Reading Strategy

Summarizing Ask students to list examples of other revenue sources for local government. (hospital fees, income taxes, profit taxes from corporations, interest on invested funds, borrowed funds) BL

Caption Answer: They provide a significant revenue source.

## $\sqrt{ }$ Reading Check Answer:

real estate

## Assess

- Use the Interactive Tutor Self-Assessment CD-ROM to review Section 2, and then assign the Section 2 Review as homework or as an in-class activity.


## Close

Categorizing Have students create a three-column chart with the headings "Federal," "State," and "Local" and then list revenue sources for each. OL

## Answers

1. All definitions can be found in the section and the Glossary.
2. individual income taxes, Social Security taxes, borrowing, corporate income taxes
3. States rely on funds from the federal government in addition to income taxes and sales taxes. Local governments rely mostly on intergovernmental revenue and property taxes.
4. Answers will vary but should demonstrate knowledge of revenue sources and tax evaluation criteria.
5. Possible answer: Food and beverages at grocery stores are necessities, whereas dining out is more of a luxury.
6. Property taxes are a major source of funding for local governments, but they are not for state governments. Income taxes are more important for state governments than for local governments.
7. An excise tax is a tax on the manufacture or sale of selected items. Other taxes such as sales taxes and estate taxes cover a broader range.
8. Answers will vary but should demonstrate an understanding of user fees.

## Focus

## R Reading Strategy

## Activating Prior Knowledge

Call students' attention to the title of the feature. Ask: Why might people dread tax returns? (Possible answer: It is a complicated, time-consuming process.) OL

## Teach

## W Writing Support

Expository Writing Have students write four questions about the information in the paragraph. Then have them choose one of the questions and research to find the answer. OL

## Analyzing the Impact

## Answers:

1. It contains almost 17,000 pages of tax code and more than 600 forms.
2. Answers will vary but should reflect an understanding of a flat tax.

## Additional Support

## GISE STUDY

## Dreaded Tax Returns

## Buried in Paper

Every spring, you can tell it's close to the April 15 tax deadline by the anxious faces of frustrated taxpayers and exhausted accountants. The U.S. tax system is one of the most complicated in the world, with almost 17,000 pages of tax code and more than 600 forms. Record keeping, education, and compliance cost the nation $\$ 265$ billion annually. In 2005 it took about 115,000 Internal Revenue Service (IRS) employees and almost $\$ 10.7$ billion to collect about $\$ 1$ trillion from 125 million taxpayers and 7 million businesses.


Source: Internet Revenue Service

## Time is Money

Because the tax code has become so complex, more and more Americans hire tax preparers to help them with their returns. On top of that, about 2.2 million taxpayers overpay-by an average of \$438-because they either don't itemize deductions or don't include all deductions or exemptions they could claim. Although many Americans file their tax returns online, they still spend an average of 17 hours completing the forms. The complexity of the system has caused many people to long for a simpler flat-tax system.


## The European Solution

- Several eastern European countries have adopted a flat tax, where everyone pays the same percentage above an exempt amount, regardless of income. The first was the Baltic republic of Estonia, which adopted a flat tax rate of 26 percent in 1994. Most Estonians take only 5 to 20 minutes to complete and electronically file an "e-postcard." The country's tax department spends one penny for every dollar of income tax collected, compared to 25 cents the IRS spends in the United States.


## NEWS FLASH <br> The Longest Return

return was 24,000 pages lurn General Electric's 2006 tax it would have been ages long. Had they filed a paper return, 237-megabyte electronic retur feet high; instead, they filed a - gabyte electronic return.

## Analyzing the Impact

1. Summarizing Why is the U.S. income tax system so complicated?
2. Drawing Conclusions Do you think it is easier for a small country like Estonia to implement a flat tax than it would be for the United States? Explain.

$$
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$$

## Extending the Content

## April 15: The Real Due Date?

On February 3, 1913, Congress adopted the 16th Amendment and instituted the income tax. They originally set March 1 as the deadline for filing taxes. Five years later, with the Revenue Act of 1918, they moved the date to March 15. That date was the deadline for the next 37 years. In 1955 it was changed to April 15, which is the present due date-for most years, that is. By law, filing and payment
deadlines that fall on Saturday, Sunday, or legal holidays are set for the next business day. Therefore, in certain years, the deadline date might be April 17 or April 18. In those years, taxpayers may have an extra day or two to file their returns.

|  | GUIDE TO |
| :---: | :---: |
| Section Preview |  |
| In this section, you will learn that tax reform was to make the individur complex than ever. | one consequence of dual tax code more |
| Content Vocabulary |  |
| - payroll withholding statement <br> - accelerated depreciation (p. 249) <br> - investment tax credit (p. 249) <br> - alternative minimum tax (p. 249) <br> - capital gains (p. 250) <br> - flat tax (p. 251) <br> - value-added tax (VAT) (p. 252) |  |

Academic Vocabulary

- concept (p. 251) • controversial (p. 252)

Reading Strategy
Listing As you read the section, complete a graphic organizer like the one below by listing the advantages and disadvantages of the flat tax. Include a definition of flat tax in your own words.

|  | Advantages | Disadvantages |
| :--- | :--- | :--- |
| Flat tax |  |  |
| Value-added tax |  |  |

## ISSUES in the NEWS

## A Trophy Loophole

One of the looniest tax loopholes imaginable . . . [is] . . . a tax break for big-game hunters who can deduct the cost of an expensive safari when they donate the stuffed trophy to a museum. By using tax-code provisions designed to encourage charitable donations, a hunter can give away a trophy specimen.
This gives a fat tax break to the hunter. It's also created a system of tax dodging and shady dealing. Little-known museums exist largely to take in the trophies and sign tax receipts.

Senator Charles Grassley . . . wants to end such hunting deductions [but] a similar proviso is missing from a tax overhaul in the House. . .
-The San Francisco Chronicle


Thhe individual tax code is incredibly complex. The complete code is about 17,000 pages long and contains approximately 9 million words. It has been estimated that Americans spend more than 7 billion hours every year filling out their federal tax returns for the IRS.

Every year, magazines like Money ask professional tax preparers to fill out tax returns for a hypothetical family-only to
find out that no two returns are the same. If experts can't get it right, then the rest of us will obviously have a difficult time. Also, it is all too easy for lawmakers to insert spe-cial-interest provisions in the tax code, such as the one in the news story above.

It is no wonder that the tax code has been amended about 14,000 times in the last 20 years-and Congress is still not done with changes!

## Focus

## Bellringer

Daily Focus Transparency 66


## GUIDE TO READING

## Answer to Graphic:

Flat tax: advantagessimple for taxpayers, closes tax loopholes, reduces need for tax accountants, preparers and the IRS; disadvantagesremoves many incentives, rate to replace current revenues unknown, may not stimulate further economic growth

Value-added tax: advantages -hard to avoid, tax incidence is widely spread, easy to collect, encourages savings; disadvan-tages-virtually invisible

## Resource Manager

## $R$ Reading Strategies

Teacher Edition

- Questioning, p. 249
- Identifying, p. 251
- Inferring, p. 254

Additional Resources

- Guid. Read. Act., p. 27
- Read. Ess. \& NoteTaking Guide, p. 79


## Critical Thinking

Teacher Edition

- Analyzing, p. 250
- Pred. Consequences, p. 252

Additional Resources

- Math Prac. for Econ., p. 13
- Pri./Sec. Source Read., p. 27
 Differentiated
Instruction

Teacher Edition

- Intrapersonal, p. 248
- ELL, p. 251


## Additional Resources

- Econ. Content Vocab. Act., p. 9
- Reinforcing Econ. Skills, pp. 17, 18


## W Writing Support

Teacher Edition

- Persuasive Writing, pp. 250, 259
- Personal Writing, p. 253


## Additional Resources

- High School Reading in the Content Area Strat. and Act.

Skill Practice

Teacher Edition

- Using Tables and Charts, p. 249
- Analyzing Info., p. 258


## Additional Resources

- Personal Finance Act., p. 15
- Reteach. Act., p. 9


## Teach

## D Differentiated Instruction

Intrapersonal Ask students who work to bring paycheck stubs to class. Then review Figure 9.6 with them. Point out that while paycheck stubs may differ in appearance, most contain similar information. Have students locate where the federal, state, city, and Social Security tax amounts are noted on the paycheck stub in their textbook. Ask: Which of these taxes are federal taxes? (federal income, FICA) Then have students locate the various categories on their own paycheck stubs. OL
$\sqrt{ }$ Reading Check Answer: The federal and state governments supply withholding tables for employers to use in determining deductions.

## Economic Analysis

Answer: about 27 percent

Differentiated Instruction
payroll
withholding statement document attached to a paycheck summarizing pay and deductions

Personal Finance Handbook
See pages R24-R27 for more information on paying taxes.

## Examining Your Paycheck

MAIN Idea The income taxes you pay are summarized on the stub that is attached to your paycheck.

Economics \& You Do you have a job where your taxes are taken out before you are paid? Read on to learn how these taxes are deducted from your paycheck.

Most of the federal, state, and local taxes are deducted directly from your paycheck. Employers list these deductions on the payroll withholding statement-the stub attached to a paycheck that summarizes income, tax withholdings, and other deductions, as shown in Figure 9.6.

The worker to whom the check belongs makes $\$ 10$ an hour and receives a check every two weeks. If the length of the workweek is 40 hours, the worker's gross pay amounts to $\$ 800$. The worker is single, has no deductions, and lives and works in Kentucky.

According to withholding tables the federal government supplied for that year, biweekly workers making at least $\$ 800$, but
less than $\$ 820$, have $\$ 104.70$ withheld from their paychecks every pay period. Similar tables for the state of Kentucky specify that $\$ 40.01$ is withheld for state income taxes. Because these are both estimates, and because even minor differences between the amounts withheld and the amount actually owed can grow, the worker will file state and federal tax returns between January 1 and April 15 of the following year to settle the differences.
Another deduction is the half-percent city income tax that amounts to $\$ 4$. Because the amount is relatively small, most cities do not require taxpayers to file separate year-end tax forms.

The FICA tax amounts to 7.65 percent ( 6.20 percent for Social Security and 1.45 percent for Medicare) of $\$ 800$, or $\$ 61.20$. The FICA is deducted from the gross pay, along with $\$ 3.20$ in miscellaneous deductions, which leaves a net pay of $\$ 586.89$.

If the worker has insurance payments or retirement contributions, or puts money into a credit union, more deductions will appear on the pay stub.

## $\sqrt{ }$ Reading Check Summarizing How are payroll deductions calculated?

Figure $9.6 \quad$ Biweekly Paycheck and Withholding Statement

The withholding statement attached to your paycheck summarizes the federal and state tax deductions from your pay. Other withholdings may include city income taxes and voluntary deductions, such as health insurance payments and savings plans.
Economic Analysis What percentage of this individual's pay has been deducted from the paycheck?



Economic Cartoons, p. 19

## Flight of the IRS

Objective: Understand the message of an economic cartoon.
Focus/Teach: Have students share their impressions of the IRS. Then have them study the cartoon and answer the questions that follow.
Assess: $\quad$ Review the answers to questions 1 through 4 as a class.
Ask students whether they think most people have a positive or negative opinion of the IRS.

## Differentiated Instruction Strategies

L Ask students to summarize the cartoonist's message in one sentence.
AL Have students draw a cartoon about the IRS or taxes that alludes to a different movie.
ELL Explain to students the plot of The Wizard of Oz. If possible, show them pictures of similar scenes in the movie.

| If taxable income <br> is over... | But not over $\ldots$ | The tax is: |
| :---: | :---: | :---: |
| $\$ 0$ | $\$ 7,550$ | $10 \%$ of the amount over $\$ 0$ |
| $\$ 7,550$ | $\$ 30,650$ | $\$ 755$ plus $15 \%$ of the amount over $\$ 7,550$ |
| $\$ 30,650$ | $\$ 74,200$ | $\$ 4,220$ plus $25 \%$ of the amount over $\$ 30,650$ |
| $\$ 74,200$ | $\$ 154,800$ | $\$ 15,107.50$ plus $28 \%$ of the amount over $\$ 74,200$ |
| $\$ 154,800$ | $\$ 336,550$ | $\$ 37,675.50$ plus $33 \%$ of the amount over $\$ 154,800$ |
| $\$ 336,550$ | no limit | $\$ 97,653.00$ plus $35 \%$ of the amount over $\$ 336,550$ |
| Source: IRS Schedule $X$ |  |  |

- According to the individual income tax table, a single individual with $\$ 6,000$ of taxable income would pay $\$ 6,000 \times .10$, or $\$ 600$ in taxes.
Economic Analysis
How much in taxes would an individual with \$40,000 of taxable income pay?


## Tax Reform

MAIN Idea Numerous changes have been made to the federal income tax code since 1981.
Economics and You Do you or your family pay federal income taxes? Read on to learn why keeping up with the tax code is so difficult.

Tax reform has received considerable attention recently. Since 1981, there have been more changes in the tax code than at any other time in our nation's history.

## Tax Reform in 1981

When Ronald Reagan was elected president in 1980, he believed that high taxes were the main stumbling block to economic growth. In 1981 he signed the Economic Recovery Tax Act, which included large tax reductions for individuals and businesses.

Before the Recovery Act, the individual tax code had 16 marginal tax brackets ranging from 14 to 70 percent. The act lowered the marginal rates in all brackets, capping the highest marginal tax at 50 percent. In comparison, today's tax code, shown in Figure 9.7, has six marginal brackets ranging from 10 to 35 percent.

Businesses also got tax relief in the form of accelerated depreciation-earlier and larger depreciation charges-which allowed firms to reduce federal income
tax payments. Another section of the act introduced the investment tax credit-a reduction in business taxes that are tied to investment in new plants and equipment. For example, a company might purchase a $\$ 50,000$ machine that qualified for a 10 percent, or $\$ 5,000$, tax credit. If the firm owed $\$ 12,000$ in taxes, the credit reduced the tax owed to $\$ 7,000$.

## Tax Reform: 1986, 1993

By the mid-1980s, the idea that the tax code favored the rich and powerful was gaining momentum. In 1983 more than 3,000 millionaires paid no income taxes.

In 1986 Congress passed sweeping tax reform that made it difficult for the very rich to avoid taxes altogether. The alternative minimum tax-the personal income tax rate that applies whenever the amount of taxes paid falls below a designated level-was strengthened. Under this provision, people had to pay a minimum tax of 20 percent, regardless of other circumstances or loopholes in the tax code.

As the United States entered the 1990s, the impact of 10 years of tax cuts was beginning to show. Government spending was growing faster than revenues, and the government had to borrow more. The resulting tax reform of 1993 was driven more by the need for the government to balance its
accelerated depreciation schedule that spreads depreciation over fewer years to generate larger tax reductions

## investment

 tax credit tax credit given for purchase of equipmentalternative minimum tax personal income tax rate that applies to cases in which taxes would otherwise fall below a certain level

( HkSkills Handbook See page R54 to learn about Understanding Percentages.

## Skill Practice

Using Tables and Charts
Have students study the Tax Table for Single Individuals, 2006. Call their attention to the percentage increases in the column marked "The tax is."
Then ask: What conclusion can you draw from the information in the column? (Students will likely conclude that the higher an individual's income, the higher percentage of taxes he or she will pay.) OL

## R Reading Strategy

Questioning Before students read about tax reform, have them write three questions that they think will be answered in the text. As they read the passage, encourage them to look for the answers to their questions, and write them down. OL

## Economic Analysis

Answer: \$6,557.50 (tax of \$4,220
plus $25 \%$ of the amount over $\$ 30,650$, which is $\$ 2,337.50$, equals $\$ 6,557.50$ )

## Leveled Activities

Guided Reading Activities, p. 27



Primary and Secondary Source
Readings, p. 14


## Critical Thinking

Analyzing Ask: What were the two forces that created the tax reform in 1997? Explain. (One force was economic; the government had unexpectedly high tax revenues in 1997. The other force was political; the Republicans had gained a majority in Congress. They reduced the tax on capital gains and lowered inheritance taxes.) OL

## W Writing Support

Persuasive Writing Ask students to take a position on whether the tax cuts of 1997 favored the wealthy. Allow them to conduct additional research if necessary. Then have students write a newspaper editorial presenting their opinion. OL

## Economic Analysis

Answer: After 1981, revenue collections increased dramatically.

## Hands-On Chapter Project

 Step 3Although a recession in 2001 reduced revenues from 2002 to 2003, total revenue collections by all levels of government have grown dramatically over the years.
Economic Analysis How does the graph reflect the tax reforms since 1981?

Total Government Receipts as a Percentage of GDP


Source: Economic Report of the President, 2006
capital gains profits from the sale of an asset held for 12 months or longer
budget than to overhaul the tax brackets As a result, two top marginal tax brackets of 36 and 39.6 percent were added.

## Tax Reform in 1997

The next significant reform followed four years later with the Taxpayer Relief Act of 1997. The forces that created it were both economic and political.

On the economic side, the government found itself with unexpectedly high tax revenues in 1997. The two new marginal tax brackets of 36 and 39.6 percent that had been added in 1993, along with the closure of some tax loopholes, meant that most people paid more taxes than before.

On the political side, the Republicans had gained a firm majority in Congress and now saw a need to fulfill a commitment to their supporters. They reduced the tax on capital gains-profits from the sale of an asset held for 12 months or longer-from 28 to 20 percent. The new law also lowered inheritance taxes.
[ Some people thought that the tax cuts favored the wealthy, and even the government agreed. An analysis by the United States Treasury Department determined that nearly half of the benefits went to the top 20 percent of wage and income earners. The lowest 20 percent received less than 1 percent of the tax reductions. With all its changes, the 1997 federal tax law became the most complicated ever.

## Tax Reform in 2001

By 2001 politicians faced a new issue: the federal government was actually collecting more taxes than it was spending. These surpluses were projected to continue to the year 2010. Surpluses could have been used to repay some of the money the government borrowed in the 1980s or to fund new federal spending. The government also could cut taxes to "give the money back to the people." In the end, President Bush backed a massive $\$ 1.35$ billion, "temporary" 10-year tax cut due to expire in 2011.

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## Explaining Taxation and Revenue Systems

Step 3: The Present U.S. Tax System and Alternative Tax Approaches. Students will explain our present tax system and alternative tax approaches.
Directions: Have students meet in their groups of three. They will research our present tax system, the flat tax, and the value-added tax. They will then present their findings in a multimedia report.

Analyzing Visuals Have students decide on at least one visual they would like to use in their multimedia presentation to increase understanding. They can then assign a group member to create it. OL
(Chapter Project will continue in Visual Summary.)

The main feature of the 2001 tax reform was to reduce the top four marginal tax brackets of $27,30,35$, and 38.6 percent to $25,28,33$, and 35 percent by 2006 . The law also introduced a 10 percent tax bracket and eliminated the estate tax on the wealthiest 2 percent of taxpayers by 2010.

## Tax Reform in 2003

Slow economic growth in 2002 convinced the Bush administration and Congress to accelerate many of the 2001 tax reforms. Specifically, the top four marginal tax brackets were reduced immediately rather than in 2006.

For lower income taxpayers, the top end of the 10 percent bracket was increased modestly. The child tax credit was also expanded from $\$ 600$ to $\$ 1,000$. Finally, the 20 percent capital gains tax bracket was reduced from 20 to 15 percent.

The 2003 tax cuts put the federal government back in the same situation as in 1993. A series of tax cuts reduced taxes in upper income brackets, and government was still spending more than it collected in taxes.

## Permanent Tax Cuts by 2011?

The tax cuts of 2001 and 2003 were "temporary" in the sense that they were due to expire in 2011. Whether that happens or not will depend on several things.

One complicating factor is that the rate of economic growth in the six years following the 2001 tax cuts was slightly lower than the rate of growth in the six years following the 1993 tax increase. This makes it difficult to argue that lower taxes are needed for higher rates of growth

However, the biggest factor will be the extent to which the federal government continues to spend more than it collects in taxes. If the present trend continues, it will be difficult to preserve the tax cuts because the government will need so much additional revenue.
$\sqrt{ }$ Reading Check Inferring Why have tax reforms occurred so frequently in recent years?

## Alternative Tax Approaches

MAIN Idea The need for new federal revenues will influence future tax reform.

Economics and You You learned earlier about state sales taxes. Read on to find out how another tax is similar to the sales tax.

Some people want to change the personal income tax; others want to replace it with something else. Because of this, we hear a lot about two alternatives: the flat tax and the value-added tax.

## The Flat Tax

The concept of a flat tax-a proportional tax on individual income after a specified threshold has been reached-did not receive much attention until Republican candidate Steve Forbes and others raised the issue in the 1996 presidential elections.

The primary advantage of the flat tax is the simplicity it offers to the taxpayer. A person would still have to fill out an income tax return every year but could skip many current steps, such as itemizing deductions. A second advantage is that a flat tax would close most tax loopholes if it did away with most deductions and exemptions. Finally, a flat tax reduces the need for tax accountants, tax preparers, and even a large portion of the IRS. As a result, Americans would no longer have to spend 7 billion hours every year preparing tax returns.

However, a flat tax also has disadvantages because it would remove many of the incentives built into the current tax code.


Tax Exempt? Each year taxpayers take advantage of a long list of deductions and tax credits to reduce their tax burden. In the year 2006, the Tax Foundation reported that a record 43.4 million tax returns from 91 million individuals showed no taxes due. Combined with the 15 million Americans who don't file returns at all, about 41 percent of the U.S. population did not contribute to the federal treasury.

## CHAPTER 9, SECTION 3

Reading Strategy

Identifying Ask: What are two factors that might prevent the tax cuts in 2001 and 2003 from becoming permanent? (First, the rate of economic growth in the years following the 2001 tax cuts was lower than the rate of growth in the years following the 1992 tax increase. This makes it difficult to argue that lower taxes are needed for economic growth. Second, if the federal government continues to spend more than it collects in taxes, it will be difficult to preserve the tax cuts.) OL

## D <br> Differentiated Instruction

## English Language Learners

Have students use a dictionary to find the definition of the word flat. (smooth, level, even) Then have them explain how flat could apply to taxes. (It would mean taxes would be smooth and even, without increases or decreases.)

## ELL

## $\sqrt{ }$ Reading Check Answer:

to increase and decrease government revenues

## Extending the Content

Support of the Flat Tax Steve Forbes is a newspaper and magazine publisher who sought the Republican presidential nomination in 1996 and 2000. His grandfather founded Forbes, the business magazine which is still owned by the Forbes family. Steve Forbes was born in Morristown, New Jersey, in 1947 and graduated from Princeton University in 1970. While still in college, Forbes started Business

Today, a magazine that came out three times a year. In 1993 Forbes became chairman of Empower America, a research center dedicated to conservative principles. He supports a flat tax and an end to the federal government's progressive income tax.

## Critical Thinking

## Predicting Consequences

Ask students if they have ever shopped at a factory outlet mall. Discuss the concept of outlet malls-manufacturers selling directly to the public through their own store. Ask: How do you think a federal value-added tax would affect the trend of factory outlet malls? Would the number of malls increase, decrease, or remain the same? On what do you base your prediction? (Students may note that a valueadded tax could increase the number of factory outlet malls. Outlet malls could sell products more cheaply because they could circumvent the retailers' tax that increases prices.) OL

## Economic Analysis

Answer: proportional; everyone pays the same percentage rate regardless of income

## Additional Support

- The VAT is like a national sales tax added to each stage of production. As a result, it is built into the final price of a product and is less visible to consumers. The third and fifth columns show the value added at each stage, and the fourth and sixth columns show the cumulative values.

Economic Analysis Is a VAT regressive, proportional, or progressive? Why?

| 2 | No taxes |  | With a $10 \%$ value-added tax |  |  |
| :---: | :--- | :---: | :---: | :---: | :---: |
|  | Value <br> added |  | Cumulative <br> value | Value added <br> with a 10\% VAT | Cumulative <br> with VAT |
| Step 1 | Loggers fell trees and sell the timber to the <br> mills for processing. | $\$ 1$ | $\$ 1$ | $\$ 1+\$ .10=\$ 1.10$ | $\$ 1.10$ |
| Step 2 | Mills cut the timber into blanks that will be <br> used to make bats. | $\$ 1$ | $\$ 2$ | $\$ 1+\$ .10=\$ 1.10$ | $\$ 2.20$ |
| Step 3 | Bat manufacturers shape and paint or varnish <br> the bats and sell them to wholesalers. | $\$ 5$ | $\$ 7$ | $\$ 5+\$ .50=\$ 5.50$ | $\$ 7.70$ |
| Step 4 | Wholesalers sell the bats to retail outlets <br> where consumers can buy them. | $\$ 1$ | $\$ 8$ | $\$ 1+\$ .10=\$ 1.10$ | $\$ 8.80$ |
| Step 5 | Retailers put the bats on the shelves and <br> wait for consumers. | $\$ 2$ | $\$ 10$ | $\$ 2+\$ .20=\$ 2.20$ | $\$ 11.00$ |
| Step 6 | Consumers buy the bats for: | $\$ 10$ |  | $\$ 11.00$ |  |

value-added tax (VAT) tax on the value added at every stage of the production process

For example, the tax code now allows homeowners to deduct interest payments on home mortgages. Other incentives include deductions for education, training, and child care.

Another problem is that no one knows exactly what rate is needed to replace the revenues collected under the current tax system. Supporters of the flat tax argue that a 15 percent rate would work. Other estimates by the U.S. Treasury put the tax closer to 23 percent-which represents more of a burden on low-income earners because their taxes would increase compared to current rates.

Finally, there is no clear answer as to whether a flat tax would further stimulate economic growth. After all, the extraordinary growth of the American economy in the 1990s, the longest period of peacetime prosperity in our history, took place when taxes were much higher.

## The Value-Added Tax

Another controversial proposal is to adopt the equivalent of a national sales tax by taxing consumption rather than income. This could be done with a value-added tax (VAT)—a tax placed on the value that manufacturers add at each stage of production. The United States currently does not have a VAT, although it is widely used in Europe.

To see how the VAT works, consider how the tax impacts the manufacturing and selling of wooden baseball bats. First, loggers cut the trees and sell the timber to lumber mills. The mills process the logs for sale to bat manufacturers. The manufacturers then shape the wood into baseball bats.

After the bats are painted or varnished, they are sold to a wholesaler. The wholesaler sells them to retailers, who sell them to consumers. As Figure 9.9 shows, a VAT tax is levied at each stage of production.

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## Activity: Interdisciplinary Connection

History Show students that the fairness of income taxes has been debated for thousands of years by reading the following quote from Plato (circa 428-348 в.c.): "When there is an income tax, the just man will pay more and the unjust less on the same amount of income."
Ask: Based on this quote, do you think Plato would prefer a flat tax on income or the current progressive income tax system?
(Students should mention that, under the present system, taxpayers can use loopholes to pay less than others with the same income. As a result, Plato would probably prefer the flat tax.) Invite students to find additional tax-related quotes from historical figures. Discuss the quotes as a class and speculate on how the figures might feel about the current U.S. tax system. OL

The VAT has several advantages. First, it is hard to avoid because it is built into the price of the product being taxed. Second, the tax incidence is widely spread, which makes it harder for a single firm to shift the burden of the tax to another group.

Third, the VAT is easy to collect, because firms make their VAT payments directly to the government. Consequently, even a relatively small VAT can raise a tremendous amount of revenue, especially when it is applied to a broad range of goods and services.

Finally, some supporters claim that the VAT would encourage people to save more than they do now. After all, if none of your money is taxed until it is spent, you might think more carefully about purchases, decide to spend less-and save more.

The main disadvantage of the VAT is that it tends to be virtually invisible. In the baseball bat example, consumers may be aware that bat prices went from $\$ 10$ to $\$ 11$, but they might attribute this to a shortage of good wood, higher wages, or some other factor. In other words, it is difficult for taxpayers to be vigilant about higher taxes if they cannot see them.

## Inevitability of Future Reforms

The tax code is more complex now than at any time since 1981-a fact that virtually guarantees future attempts to simplify it. The recent flat tax movement provides just one such example. While simplification is desirable, unexpected events often require new expenditures-which in turn may require changes in the tax code. The unexpected cost of the war in Iraq, along with the enormous damage inflicted by hurricane Katrina in 2005, are two examples of such unexpected costs.

Reform also can result from political change, which tends to be abrupt as one party leaves office and another enters. New administrations often display a sense of urgency to finally do things the "right" way, or to clean up the presumed excesses of their predecessors.

Finally, it is difficult for politicians to give up the power to modify behavior, influence resource allocation, support pet projects, or grant concessions to special interest groups by changing the tax code.
$\sqrt{\text { Reading Check }}$ Describing How does a valueadded tax work? Why is it useful?


## Vocabulary

1. Explain the significance of payroll withholding statement, accelerated depreciation, investment tax credit, alternative minimum tax, capital gains, flat tax, and value-added tax (VAT).

## Main Ideas

2. Identifying What are the major types of federal, state and local taxes on the payroll withholding statement?
3. Listing Use a graphic organizer like the one below to list the advantages and disadvantages of the value-added tax.

| Value-Added Tax |  |
| :---: | :---: |
| Advantages | Disadvantages |
|  |  |

## Critical Thinking

4. The BHG Idea What factors led to the tax reform measures passed in 1981, 1986, 1997, and 2001?
5. Summarizing What changes would you recommend if you were in charge of revising the federal tax code? Explain your answer in a written paragraph.
6. Analyzing Visuals Look at Figure 9.7 on page 249. How can you tell whether this tax is progressive regressive, or proportional?
7. Cause and Effect Describe the factors that are likely to cause future revisions of the tax code.

## Applying Economics

8. Flat Tax Use examples to explain what might happen to donations for charitable organizations under a flat tax.

## Writing Support

Personal Writing Have students write a letter to one of their congressional representatives explaining why they support or oppose tax reform. Tell students to keep their letters brief and to the point. AL

## $\sqrt{ }$ Reading Check Answer:

A VAT refers to taxes placed on the value that manufacturers add during production. It is easy to collect, hard to avoid, and may encourage people to save more.

## Assess

(3) Use the Interactive Tutor Self-Assessment CD-ROM to review Section 3, and then assign the Section 3 Review as homework or as an in-class activity.

## Close

Making Decisions Ask: If
there is one thing you could change in the tax laws, what would it be? Why? Discuss answers as a class. OL

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## Answers

1. All definitions can be found in the section and the Glossary.
2. federal income tax, state income tax, FICA (Social Security and Medicare), and possibly local income tax
3. Advantages: hard to avoid, tax incidence widely spread, easy to collect, might encourage more saving
Disadvantages: difficult for taxpayers to be vigilant since VAT is "invisible," competes with state sales taxes.
4. There were high taxes blocking economic growth, Congress felt that too many of the rich were able to completely avoid paying taxes, there was high tax revenue, Republicans were commited to reducing inheritance taxes and providing tax breaks for people with long-term investments, and the federal government was collecting more taxes than it was spending.
5. Answers will vary but should reflect knowledge of the current federal tax code.
6. The tax is progressive, based on a percentage of taxable income
7. Factors likely to cause future revisions include the desire to simplify the tax code, the appearance of unexpected costs, political change, and the reluctance of politicians to give up their power to change the tax code.
8. Answers will vary but should demonstrate an understanding of the flat tax.

## BusinessWeek

## Teach

R Reading Strategy
Inferring Have students explain why Kia built a plant in Slovakia. (Slovakia had low taxes.) Ask: If more countries in Europe enact flat taxes, what might happen to manufacturing companies? (They may build plants in countries with flat tax systems.) OL

## BusinessWeek ONLINDE

To find up-to-date news and analysis on the economy, business, technology, markets, entrepreneurs, investments, and finance, have students search feature articles and special reports on the BusinessWeek Web site, www.businessweek.com.

## Examining the Newsclip

## Answers:

1. One low income tax rate is paid by all, there are no loopholes or graduated rates, and there is no need to enforce complex laws.
2. They were not in the former Soviet bloc.

## Additional Support

# BusinessWeek NEwsculp 

Aflat tax has often been debated in the United States. Today Russia and several countries in Eastern Europe utilize it as a way to keep taxes simple and avoid tax loopholes. This has spurred Western Europe to take a closer look.

## Europe Circles the Flat Tax

The flat tax. In the eyes of many fiscal conservatives, it's the Holy Grail of public policy: One low income tax rate paid by all but the poorest wageearners, who are exempt. No loopholes for the rich to exploit. No graduated rates that take a higher percentage of income from people who work hard to earn more. No need for a huge bureaucracy to police fiendishly complex tax laws. U.S. conservatives have been pushing the idea for decades. But it has gotten its first real road test in the former Soviet bloc, where at least eight countries, from minuscule Estonia to giant Russia, have enacted flat taxes since the mid-1990s.
Most of these countries' economies are growing at a far-healthier clip than those of their neighbors to the west. So it's no surprise that calls for a flat tax are now being heard in Western Europe, the most heavily taxed zone on the planet. . . . Even without pressure from the East, many Western European governments face growing complaints about the complexity of their tax regimes. . .

| Flat TAXES |  |  |  |
| :--- | :--- | :--- | :---: |
| Country | Year | Rate |  |
| Estonia | 1994 | $23 \%$ |  |
| Latvia | 1995 | $25 \%$ |  |
| Russia | 2001 | $13 \%$ |  |
| Serbia | 2003 | $14 \%$ |  |
| Slovakia | 2003 | $19 \%$ |  |
| Ukraine | 2003 | $13 \%$ |  |
| Georgia | 2004 | $12 \%$ |  |
| Romania | 2005 | $16 \%$ |  |

Source: Hoover Institution


Drawn by low taxes, Kia built a manufacturing plant in Slovakia.
There's no guarantee, of course, that flat taxes would work as well in Western Europe as they have in the countries to the east. In the former Soviet bloc, most of the countries that enacted flat taxes gained revenue as people who had worked in the shadow economy began reporting their income and paying taxes. The former tax dodgers figured that with rates so low, it was no longer worth running the risk of breaking the law. Moscow, which introduced a flat tax in 2001, saw its income tax revenues more than double in real terms from 2000 to 2004.
-Reprinted from BusinessWeek

## Examining the Newsclip

1. Analyzing According to the article, why do fiscal conservatives promote a flat tax?
2. Determining Cause and Effect Why might Western European countries not see similar revenue increases?

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## Extending the Content

Is Flat Really Flat? Many Eastern European nations that were former members of the Soviet bloc have introduced a statutory flat personal rate as part of their reform packages in the hopes of generating sufficient revenue for government expenses. The results have been positive, but experts point out that many of these countries are using variations of a flat income tax rather than implementing the original concept. In these situations, Social

Security contributions make much larger contributions to the total tax revenue than personal income tax. The combination of a flat income tax, high Social Security contributions, and indirect taxation means that there is a tax burden on individuals that is often higher than suggested by the original concept of a flat tax.

Types of Taxes All taxes in the United States can be broken down into three categories: proportional, progressive, and regressive.

| Proportional | Progressive | Regressive |
| :--- | :--- | :--- |
| - Percentage of income paid | - Percentage of income paid |  |
| in taxes stays the same |  |  |
| in taxes goes up as income |  |  |
| regardless of income | goes up | - Percentage of income paid <br> in taxes goes down as income <br> goes up |
| - Example: Medicare |  |  |

Government Revenue Sources Federal, state, and local revenue sources differ. Much of the federal revenue is sent on to state and local governments.
Alternative Tax Approaches Because the federal tax code has become so large and cumbersome, people have discussed the flat tax and the value-added tax as two alternatives.


CHAPTER 9 Sources of Government Revenue

## Explaining Taxation and Revenue Systems

## Step 4: Bringing It All Together.

Students will synthesize what they learned in previous steps.

Directions: Instruct each group to collect the work they've completed throughout the chapter. Collections should include the pamphlet and summary report from Step 1, the booklet from Step 2, and the multimedia presentation from Step 3. Then, review the

Big Idea with students by asking volunteers to explain how all levels of the government use tax revenue to provide essential goods and services. Have students compose their thoughts into a paragraph in their journals. OL

Drawing Conclusions Have students review the types of taxes in the table. Ask: Why might the U.S. tax system be considered cumbersome? (Possible answer: The tax code for a system with three categories is large, complicated, and difficult to understand. It requires the services of tax preparers, tax accountants, and an enormous government agency.)
Analyzing Visuals Have students describe the graphic representation of a flat tax. (Possible answer: a straight, horizontal line) Next, have them describe the graphic representation of a valueadded tax. (Possible answer: stairsteps, with a percentage of value-added tax on each step, leading up to a cumulative value) Ask students to share how the representations help them understand both tax alternatives. BL

## ExamViéw <br> Assessment Suite

This easy-to-use software includes extensive question banks and allows you to create fully customized tests that can be administered in print or online.

## Review Content Vocabulary

| 1. $b$ | 2. h |
| :--- | ---: |
| 3. $j$ | 4. d |
| 5. $g$ | 6. i |
| 7. f | 8. e |
| 9. c | 10. $a$ |

## Review Academic <br> Vocabulary

11. evolved
12. concept
13. implement
14. validity
15. considerably
16. controversial

## Review the Main Ideas

17. to promote or discourage consumer buying
18. It may impact the poor, and its benefits are uncertain.
19. because those with higher incomes pay a smaller percentage of income in taxes than those with lower incomes
20. equity: should be impartial and just; simplicity: laws should be written clearly; efficiency: should be easy to collect and cost-effective
21. Social Security and Medicare
22. excise: on certain manufactured items; estate: on transfer of property at death; gift: applied to transfer of wealth; customs: on imported goods
23. State: other governments; sales taxes, income taxes; interest earnings. Local: intergovernmental revenue; property taxes

## Review Content Vocabulary <br> On a separate sheet of paper, choose the letter of the term identified by each phrase below.

a. ability-to-pay
f. VAT
b. payroll tax
g. tax return
c. estate tax
h. regressive tax
d. excise tax
i. sales tax
e. FICA
j. capital gains

1. tax on wages and salaries withheld from paycheck
2. average tax per dollar decreases as taxable income increases
3. profits from an asset held 12 months or longer
4. tax on the manufacture or sale of certain items
5. annual report to the government detailing income earned and taxes owed
6. large source of revenue for state governments
7. national sales tax on value added at each stage of production
8. Social Security and Medicare taxes
9. tax on the transfer of property when a person dies
10. tax paid by those who can most afford to pay

## Review Academic Vocabulary

Replace the underlined word in each sentence below with the appropriate synonym from the following list: validity, evolved, implement, considerably, concept, and controversial.
11. The tax code has developed into a complicated system.
12. The idea of a flat tax has been debated for a long time.
13. The government needs tax revenue to fulfill its goals.
14. The IRS questioned the legitimacy of the deduction.
15. The tax code has changed substantially since its origin.
16. Abolishing tax deductions would be an unpopular move by the government.

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24. taxes (Federal, state, FICA, city), insurance payments, retirement contributions, credit union contributions
25. The Economic Recovery Tax Act reduced marginal tax rates. The Taxpayer Relief Act reduced capital gains and inheritance taxes, and added education deductions. Reforms strengthened alternative minimum tax, added some tax brackets and reduced others, reduced estate tax and capital gains tax, and increased the child tax credit.

## Review the Main Ideas

Section 1 (pages 229-236)
17. Describe how taxes can be used to affect people's behavior.
18. Describe the limitations of the benefit principle of taxation.
19. Explain why a sales tax is considered to be a regressive tax.
20. Explain the three criteria used to evaluate taxes.

## Section 2 (pages 238-245)

21. Identify the two components of FICA.
22. Distinguish between excise taxes, estate and gift taxes, and customs duties.
23. List the main sources of revenue for state and local governments by using a graphic organizer like the one below.

| Sources of Revenue |  |
| :---: | :---: |
| State | Local |
|  |  |

Section 3 (pages 247-253)
24. Discuss the deductions that are withheld from paychecks.
25. Describe the major tax reform bills enacted since 1981.
26. Explain why Congress enacted the alternative minimum tax.
27. Identify the advantages and disadvantages of a flat tax.

## Critical Thinking

28. The BIG Idea If you were an elected official who wanted to increase tax revenues, which of the following taxes would you prefer to use: individual income, sales, property, corporate income, user fees, VAT, or flat? Provide reasons for your decision.
29. to ensure that the rich would pay some taxes
30. Advantages: simplicity, closes tax loopholes. Disadvantages: questionable rate needed to place current revenues, uncertainty over stimulation of economic growth.

## Critical Thinking

28. Answers will vary but should indicate an understanding of the different types of taxes.
29. Inferring Why do you think Alaska has no sales tax or personal income tax?
30. Comparing and Contrasting What were the goals of the Economic Recovery Tax Act of 1981, the 1986 tax reform, and 2001 tax changes?
31. Synthesizing For one week, keep a list of all taxes you hear or read about in the news media or pay in your community. Classify your journal entries into three categories: federal, state, and local taxes. Then draw a matrix like the one below and classify each in the appropriate place. Which taxes appeared in the news most frequently?

32. Analyzing What provisions of tax measures enacted in the last 20 years benefit taxpayers with higher incomes?

## Applying Economic Concepts

33. User Fees In your own words, write a rationale for a user fee that you think should be enacted.
34. Taxes Some people object to state and local governments imposing sales and property taxes. What would you say to these people in defense of the two taxes?

## Thinking Like an Economist

35. Critical Thinking Describe how an economist might go about analyzing the consequences of shifting from the individual income tax to a consumption tax like the VAT.

## Writing About Economics

36. Expository Writing Does the concept of a flat income tax meet the three criteria for effective taxes? Write a brief summary of your findings and use it to either support or oppose such a proposal.

## Math Practice

37. After deductions and exemptions, Mindy's unmarried brother had taxable income of $\$ 98,000$ in 2006. According to the tax table in Figure 9.7 on page 249, what will he owe in federal income taxes? What did he pay in Social Security taxes? What did he pay in Medicare taxes?

## Analyzing Visuals

38. Look at Figure 9.3 on page 239 and compare the revenue from the various sources for the years 2001 and 2007. In which categories did revenues decrease? How did the federal government make up these decreases?

## Interpreting Cartoons

39. Critical Thinking Look at the cartoon below. Who are the people seated in the chairs? Whom do the figures in the bottom left corner represent? What statement is the cartoonist trying to make?


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29. Possible answer: Alaska has alternative sources of revenue (oil royalties).
30. The Economic Recovery Tax Act of 1981 reduced taxes, while the 1986 measure made it difficult for the very rich to avoid taxes altogether. The 2001 tax change eliminated the estate tax on the wealthiest 2 percent of taxpayers.
31. Answers will vary but should demonstrate understanding of the tax types and principles.
32. Economic Recovery Tax Act of 1981, Taxpayer Relief Act of 1997, and the reforms in 2001 and 2003

## Applying Economic Concepts

33. Answers will vary but should reflect knowledge of user fees.
34. Answers will vary but should reference sales and property taxes.

## Economics ONLINE

Have students visit the Web site at glencoe.com to review Chapter 9 and take the SelfCheck Quiz.

## Thinking Like an Economist

35. Answers will vary but should show an understanding of the advantages and disadvantages of a consumption tax.

## Writing About Economics

36. Answers will vary but should include students' opinions on whether a flat income tax meets the criteria for effective taxes.

## Math Practice

37. Mindy's brother will owe $\$ 21,771.50$ in federal income taxes. He paid $\$ 6,076$ in Social Security taxes and \$1,421 in Medicare taxes.

## Analyzing Visuals

38. Revenues decreased for Social Security taxes, excise taxes, estate and gift taxes, miscellaneous taxes, and individual income taxes. The federal government made up these decreases by increasing corporate income taxes and borrowing.

## Interpreting Cartoons

39. Answers will vary but might reflect the view that the Reagan tax cuts greatly reduced taxes on the wealthy and on businesses while doing little to help the average taxpayer.

## Focus

Have students read the opening two paragraphs of the feature. Ask if they were aware that buying and selling on the Internet is not subject to taxation. Then have students discuss how this relates to the equality criterion for taxes.

## Teach

## S Skill Practice

Analyzing Information Divide students into pairs. Then draw students' attention to the column of Internet sales and taxes. Have them pay close attention to the state and local revenue loss section. Ask: How could state and local governments use an estimated $\$ 25$ billion that are lost in revenue to benefit its citizens? (Answers will vary, but students should be able to tell how state agencies and services could benefit from that much lost revenue.) Have a volunteer from each pair share their ideas with the class. OL

## Additional Support

## DEATIE IN EONOMICS

## Should E-Commerce Be Taxed?

Alot of buying and selling occurs on the Internet-so much, in fact, that rumblings of an e-commerce sales tax have become a roar. In 2005 more than 700,000 people in the United States earned either full- or part-time income on eBay. This statistic alone ensures that a tax showdown between the IRS and e-commerce retailers is on the horizon.

Can you sift through the debate to determine whether or not buying and selling online should be subject to taxation? As you read the selections, ask yourself: "Should e-commerce be taxed?"

## PRO SALES TAX REVENUE LOSSES

Inability to collect the [e-commerce sales] tax potentially has a number of important implications. Firms have an incentive to locate production and sales activity to avoid tax collection responsibility, thereby imposing economic efficiency losses on the overall economy. The sales tax becomes more regressive as those who are least able to purchase online are more likely to pay sales taxes than those who purchase online more frequently.

Further, state and local government

Internet sales in 2003
$\$ 1.27$ trillion
Taxable internet sales in 2003 $\$ 751$ billion

## Sales on which taxes

 were not collected$\$ 236.3$ billion in 2003
$\$ 329.2$ billion in 2008*
State and local revenue loss
$\$ 15.5$ billion in 2003
\$21.5-33.7 billion in 2008*

* 2008 figures are estimated tax revenues are reduced. . . . [T]he Census Bureau reports a combined \$1.16 trillion in . . . e-commerce transactions by manufacturers, whole salers, service providers, and retailers, and Forrester Research, Inc.'s expectations continue to be for strong growth in e-commerce in coming years. Thus, the revenue erosion continues to represent a significant loss to state and local government.
-Dr. Donald Bruce and Dr. William F. Fox,
Professors, Center for Business and Economic Research,
University of Tennessee

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## Extending the Content

Possible Options for Internet Sales In 1999 the Graziadio Business Report published by the Graziadio School of Business and Management proposed three options for collecting tax revenues from Internet sales. The National Sales Tax Option (NST) proposed that the federal government impose a uniform tax on all domestic e-commerce, collect the tax electronically, and then remit the proceeds to the states. The Freedom of States (FS) option
proposed that all states be free to impose whatever tax they wished. The Internet Tax Equality Option (ITE) proposed that the federal government would create some uniform regulations but would give states freedom to determine their own tax rates and exemptions.

## -ON ONLINE TAX PROPOSAL MISGUIDED

The Direct Marketing Association (DMA) is cautioning legislators about bills introduced . . . that would allow states to force online sellers to collect sales taxes for all state and local taxing jurisdictions. . . . The failure of . . . these bills to address a reduction in the number of tax jurisdictions is a key flaw, and remains a critical obstacle to a workable streamlined sales tax program. There are currently approximately 7,600 different sales tax jurisdictions in this country, including states, counties and municipalities, and even block-by-block areas that collect additional sales taxes, such as sewer districts, sports arena districts or library districts. Currently, only businesses with a physical presence or "nexus" within a state are required to collect taxes for the jurisdictions within that state. ...

The bills would also create a barrier to entry for small entrepreneurs, who rely on the Internet to help create markets, and a barrier to growth for medium-sized businesses seeking to grow

operations or expand a customer base. Many would not be able to afford the effort and expense it would take to collect and remit sales taxes for each of the thousands of jurisdictions, much less the cost of a possible audit at any time by 46 different state revenue departments.
-Direct Marketing Association, www.the-dma.org

## Analyzing the Issue

1. Identifying What is the main argument in support of an e-commerce sales tax?
2. Summarizing Why does the DMA think it is not possible for online merchants to implement sales taxes?
3. Deciding With which opinion do you agree? Explain your reasoning.

## Assess/ Close

## W Writing Support

Persuasive Writing Have students imagine that they are entrepreneurs who have a small business that relies on the Internet. Have them write a newspaper editorial expressing their opinions about online tax proposals. Students should use information from the text to support their point of view.

## Analyzing the Impact

## Answers:

1. State and local government tax revenues are reduced.
2. There are thousands of different sales tax jurisdictions (states, counties, and cities). Collecting and remitting sales taxes for each of these would be costly.
3. Answers will vary but should demonstrate an understanding of the controversy.

## Additional Support

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## Activity: Technology Connection

Identifying Points of View Point out to students that e-commerce and taxation will continue to be debated until the IRS and e-commerce retailers reach resolution. Organize students into groups, and have them use the Internet to research the major arguments for and against taxing
e-commerce businesses. Encourage them to use their findings to create a Web site designed to inform people about the debate. Call on groups to display and discuss their Web site designs. OL

## Teacher Tip

Arranging Student Groups
Students in the class most likely have varying Web-design skills. Suggest that students divide the responsibilities so that those who are less involved in the Web site creation have a greater role in other parts of the project.


[^0]:    *Also available in Spanish

[^1]:    *Also available in Spanish

[^2]:    $\sqrt{\text { Reading Check }}$ Summarizing How do taxes affec businesses and consumers?

[^3]:    $\sqrt{ }$ Reading Check Recalling Which property tax earns the most revenue for local governments?

