

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

Lesson Description

This lesson is based on an article written by St. Louis Fed Vice President and Deputy Director of Research, Cletus C. Coughlin, and published in the March 2006 issue of *National Economic Trends*, a St. Louis Fed publication. Individual federal income tax affects everyone and the article provides a basis for real-world application of learning. Using data collected from the Internal Revenue Service for the tax year 2003, students will become involved in an inquiry of individual federal income taxes. The lesson is divided into sections that address specific questions:

- ✓ Why do we have an individual income tax?
- ✓ What is individual federal income tax? How is it paid? When is it paid?
- ✓ How is the individual income tax structured?
- ✓ What is a perfect tax structure?
- ✓ What are the different categories of taxes?
- ✓ What is the correlation between tax burden and income groups?
- ✓ "What if" the tax structure were changed? What effects would a different tax structure have on taxpayers? What effect would a different tax structure have on the government?

Curriculum Connection

Civics/Government, Family and Consumer Science, Economics, Math, Writing

Objectives

Students will:

- ❑ Understand that the federal government collects individual federal income tax to pay for government expenditures.
- ❑ Become aware of the individual income tax, the collection procedures, filing of returns, and some of the IRS forms used.
- ❑ Learn that different income groups pay a different percentage of their income in taxes.
- ❑ Calculate individual federal income tax using different rates and structures.
- ❑ Improve their knowledge of the existing tax system.

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

National Economic Standards

Standard 16: Role of Government

There is an economic role for government to play 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.

Benchmarks:

- Most federal tax revenue comes from personal income and payroll taxes.
- Governments provide an alternative method to markets for supplying goods and services when it appears that the benefits to society of doing so outweigh the costs to society.
- Not all individuals will bear the same costs or share the same benefits of those policies.

Materials Needed

- ✓ *Inside the Vault* Spring 2006 issue (for reference)
- ✓ **Visual A**—*W-2 Form*
- ✓ **Visual B**—*Form 1040EZ*
- ✓ **Visual C**—*Sample Form 1040*
- ✓ **Visual D**—*Perfect Tax Structure*
- ✓ **Activity 1-A**—*Who Pays and How Much?*
(2003 Tax Tables A & B)
- ✓ **Activity 1-B**—*Twenty Questions*
- ✓ **Visual E**—*Kinds of Taxes*
- ✓ **Activity 2-A**—*What-If Worksheet*
- ✓ **Activity 2-B**—*What-If Table*
- ✓ **Activity 2-C**—*Instructions for What-If Table*
- ✓ **Calculators**
- ✓ **Activity 3**—*Income Tax: You Decide*

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

Key words and concepts

- **Ability to pay** – concept of tax fairness that states that people with different amount of income or wealth should pay tax at different rates
- **Adjusted gross income** – total income less statutory adjustments
- **Federal income tax** – taxes levied on personal income
- **Form W-2, Wage and Tax Statement** – form that employers must provide to employees by January 31 of each year that gives annual income and withholding information
- **Income** – money received from wages and salaries, rent, interest, and profit
- **Income tax** – tax on income
- **Individual income tax** – income tax levied on individuals
- **Internal Revenue Service** – the federal agency that collects income taxes in the United States
- **Proportional tax** – tax that takes the same percentage of income from people in all income groups
- **Progressive tax** – tax that takes a larger percentage of income from people in higher-income groups than from people in lower-income groups
- **Regressive tax** – tax that takes a larger percentage of income from people in lower-income groups than from higher income groups
- **Salary** – compensation received by employees for services performed paid as a fixed sum paid for a specific period of time
- **Taxes** – mandatory fees placed on income, property or goods to support government programs
- **Tax Refund** – money owed by the government to taxpayers when their total tax payments are greater than the total tax
- **Taxable income** – adjusted gross income less standardized or itemized deductions
- **Wages** – compensation received by employees for services performed usually based on an hourly rate of pay

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

Procedures

Note: The lesson is divided into sections. Each section begins with a question and the procedural steps allow students to discover the answers. Begin each section by asking the introductory question.

Section One: Why do we have a federal income tax?

1. Review and discuss the economic roles of government in a market economy. Lead the class in a discussion of federal government expenditures. Inform the class that national defense, Social Security, Medicare, income assistance, environment, agriculture, and interest on the national debt are primary expenditures of the federal government.
2. Pose the question: How does the federal government pay for its expenses?
3. After giving time for students to respond, explain that the Federal government collects taxes to pay for government operations, and goods and services.
4. Briefly share information on different types of federal taxes: excise tax, social security taxes, corporate income tax, and individual income tax.

Section Two: What is individual federal income tax? How is it paid? When is it paid?

1. Introduce the personal income tax as a primary source of revenue for the government. The individual income tax was the largest share of total federal tax receipts in 2003, accounting for 43% of federal tax receipts. This income tax is collected on a "pay-as-you-earn" basis. Federal income tax is withheld from every paycheck and employers send the withholdings to the Internal Revenue Service. At the end of the year, the amount withheld should be approximately the same as the taxpayer's tax liability for the year.
-

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

2. Ask students to share thoughts on the “pay-as-you-earn” basis for collecting income tax. Is this good for taxpayers? Why? Is this good for the government? Why?
 3. By January 31 of each year, employers must furnish employees a form W-2, *Wage and Tax Statement*. Employers report information including federal income tax withheld, Social Security tax withheld, and Medicare tax withheld on this form. Employees use this form to complete their individual income tax form.
 4. Show **Visual A**. (Form W-2)
 5. Discuss some information included on the W-2 form:
 - Box 1 – the total income earned
 - Box 2 – amount of federal income tax withheld
 - Box 4 – amount of Social Security tax withheld
 - Box 6 – amount of Medicare tax withheld
 - Copy B – to be filed with Employee’s FEDERAL Tax Return
 6. Taxpayers use Form W-2 to complete their individual income tax returns, which must be filed by April 15 of each year with the Internal Revenue Service. If too much federal income tax has been withheld during the year, a taxpayer will receive a refund. If not enough has been withheld, the taxpayer will owe the government more money.
 7. Show **Visual B**. (Form 1040EZ)
 8. Discuss some information included on the form:
 - Line 1 – W-2 information
 - Line 2 – taxable interest information
 - Line 4 – adjusted gross income
 - Line 7 – Federal income tax withheld from box 2 of Form W-2
 - Line 10 – find tax by using tax table
-

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

9. Inform the class that Form 1040EZ can only be used by some taxpayers. Ask students to review the form to locate criteria for who can use the Form 1040EZ. (The top of form says "with no dependents" and line 2 gives a limit on interest. Is there any place on this form for business income? Refer to page 2 of the form for specific information on who can use the form.)
10. Show **Visual C**. (Sample Form 1040)
11. Identify this form for taxpayers who do not qualify for using the 1040EZ. Allow time for students to review and discuss the sample form.
 - What line includes W-2 information? (7)
 - What line includes interest income? (8a)
 - What line indicates the AGI? (34)
 - What line indicates how much federal income tax was withheld from earnings? (61)
 - Did the taxpayer have enough withheld from earnings during the year? (No, line 72)
 - Why did this taxpayer need to use Form 1040 instead of Form 1040EZ? (to include farming income on line 18)

Section Three: How is the federal individual tax structured?

1. Explain that there are different ways to structure the federal income tax. It has been a challenge in the United States to structure the "perfect" tax structure. Display **Visual D** and discuss the perfect tax structure as one that-
 - provides desirable incentives to work, save and invest;
 - is viewed as fair;
 - is easy to understand, and
 - generates sufficient revenues to fund spending decisions.

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

2. Provide Activity 1-A, *Income Taxes: Who Pays and How Much? 2003 Tax Tables A & B* to students. Explain the information and categories included in the tables.
3. Provide Activity 1-B, *Twenty Questions* to students. Allow students to work with partners to find answers to the twenty questions based on information in **Table A & Table B**.
4. Allow time for class discussion to answer the question "Who pays most of the income tax and how much do they pay?"
5. After recognizing that most of the federal income tax is paid by the top 50% income group, ask students to discuss the correlation of this system to the "perfect tax structure." How does our current individual income tax structure measure up?

Section Four: What are the different categories of taxes?

1. Show **Visual E**. (Kinds of Taxes)
2. Define and discuss three different kinds of taxes:
 - **Proportional taxes** – take the same percentage of income from people in all income groups
 - **Progressive taxes** – take a larger percentage of income from people in higher-income groups than from people in lower-income groups
 - **Regressive taxes** – take a larger percentage of income from people in lower-income groups than from higher income groups
3. Discuss the federal individual income tax as a progressive tax based on the ability-to-pay principle.

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

Section Five: What if the tax structure were changed? What effects would a different tax structure have on taxpayers? What effect would a different tax structure have on the government?

1. Provide materials to students:
 - ✓ Activity 1-A— *Income Taxes: Who Pays and How Much? 2003 Tax Tables A & B*
(This was also used in the previous activity.)
 - ✓ Activity 2-A— *What-If Worksheet*
 - ✓ Activity 2-B— *What-If Table*
 - ✓ Activity 2-C— *Instructions for What-If Table*
 - ✓ Calculators
2. Compare this assignment to completing an income tax return. Point out reading, calculations, referring from one sheet to another, and gathering of information to complete the activity are all involved.
3. To complete the assignment, give directions to read the ten income descriptions, calculate the AGI, and write the AGI in column 1 of **Table C**.
4. After completing column 1, direct students to use **Table A** and **Table B** to complete columns 2 and 3.
5. Inform the students that column 4 is a “What-if” calculation used as a representation of a progressive tax structure. An average tax rate for an entire income group does not mean that everyone pays the same tax rate. It is only an *average* of what taxpayers in that income group paid in 2003. Taxpayers in the same income group will have different tax rates based on deductions, tax credits, and individual circumstances.
6. To arrive at the “What-if” tax liability using the average tax rate for the income group, students should multiply the average tax rate in column 3 by the AGI in the first column to arrive at the tax liability in column 4.

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

7. Ask students to refer to **Table B** and find the average tax rate of all taxpayers. After identifying 11.9% as the average tax rate of all taxpayers, ask students to use this percentage to complete column 5. This is only a “what-if” tax used as a representation of a proportional tax. The calculation is done to discover what effect using the average rate for all taxpayers would have on income tax liabilities of all income groups.
8. Use column 6 to identify the change the different tax structure and rates have on tax liability.
9. Compare the total income taxes paid at the bottom of column 4 and column 5.
 - Which tax structure results in more income taxes paid?
 - How would a change in the tax structure affect each income group?
 - How would a change in the tax structure affect the federal government?

Assessment

1. Provide Activity 3— *Income Tax: You Decide* to students. In this activity, students will use three different *what-if* tax structures to calculate individual federal income tax.
2. Since it has proven to be a major challenge to design the perfect tax system in the United States, challenge students to make the decision.
3. Instruct students to choose one of the three structures in the activity that comes closest to meeting the criteria for the perfect tax structure and write an essay defending their choice. Students should use supporting details and include information on the effects of their choice on individual taxpayers, society, and the government.

Inside the Vault - Income Taxes: Who Pays and How Much?

A Look at Individual Federal Income Tax

Lesson Plan

Extension Activities

Lead the class in a brainstorm session to name careers involving taxes such as accountants, Internal Revenue Service employees, tax consultants, and bookkeepers. Challenge students to use research skills to find information on these and other careers including the educational qualifications, average income levels, and the demand for each career. Refer students to the Bureau of Labor Statistics, U.S. Department of Labor, *Occupational Outlook Handbook, 2006-07 Edition*, on the internet at <http://www.bls.gov/> for career research.

Resources and Websites

<http://www.irs.gov>
<http://www.irs.gov/individuals/students/index.html>
<http://www.ncee.net>
<http://www.stlouisfed.org/publications/itv/default.html>
<http://research.stlouisfed.org/publications/net/>

Inside the Vault - Income Taxes

2003 Tax Tables A & B

Table A

Income Groups According to AGI Levels, 2003		
	Top 1%	more than \$295,495
	Top 5%	more than \$130,080
	Top 10%	more than \$94,891
	Top 25%	more than \$57,343
	Top 50%	more than \$29,019
	Bottom 50%	less than \$29,019

Table B

Federal Income Tax Burden by Income Group, 2003						
Income Group	Number of returns	AGI (\$ millions)	Income taxes paid (\$ millions)	Group's share of total AGI (%)	Group's share of Income taxes (%)	Average tax rate (%)
All taxpayers	128,609,786	6,287,586	747,939	100	100	11.9
Top 1%	1,286,098	1,054,567	256,340	16.77	34.27	24.31
Top 5%	6,430,489	1,960,676	406,597	31.18	54.36	20.74
Top 10%	12,860,979	2,663,470	492,452	42.36	65.84	18.49
Top 25%	32,152,447	4,078,277	627,380	64.86	83.88	15.38
Top 50%	64,304,893	5,407,851	722,027	86.01	96.54	13.35
Bottom 50%	64,304,893	879,735	25,912	13.99	3.46	2.95

Source: Internal Revenue Service, *Individual Income Tax Returns with Positive Adjusted Gross Income (AGI)*, Tables 5 and 6; www.irs.gov/taxstats/indtaxstats/article/0,,id=133521,00.html.

TWENTY QUESTIONS

Directions: Refer to Table A & Table B to answer these questions.

1. How many individual income tax returns were filed in 2003?
2. What was the average tax rate paid by all individuals in 2003?
3. What percent of income (AGI) is in the top 50 percent income group?
4. What percent of taxes paid were from the top 50 percent income group?
5. What percent of the income (AGI) came from the bottom 50 percent?
6. What percent of taxes did the bottom 50 percent group pay?
7. What was the average tax rate for the top 50 percent group?
8. What was the average tax rate for the bottom 50 percent group?
9. What percent of income (AGI) was in the top 25 percent group?
10. What percent of taxes did the top 25 percent income group pay?
11. What was the tax rate for the top 25 percent income group?
12. What percent of income (AGI) was in the top 10 percent income group?
13. What percent of taxes did the top 10 percent income group pay?
14. What was the tax rate for the top 10 percent income group?
15. What percent of income (AGI) was in the top 5 percent income group?
16. What percent of taxes did the top 5 percent income group pay?
17. What was the tax rate for the top 5 percent income group?
18. What percent of income (AGI) was in the top 1 percent income group?
19. What percent of taxes did the top 1 percent income group pay?
20. What was the tax rate for the top 1 percent income group?

TWENTY QUESTIONS

Directions: Refer to Table A & Table B to answer these questions.

1. How many individual income tax returns were filed in 2003?
128,609,786
2. What was the average tax rate paid by all individuals in 2003?
11.9%
3. What percent of income (AGI) is in the top 50 percent income group?
86.01%
4. What percent of taxes paid were from the top 50 percent income group? **96.54%**
5. What percent of the income (AGI) came from the bottom 50 percent?
13.99%
6. What percent of taxes did the bottom 50 percent group pay?
3.46%
7. What was the average tax rate for the top 50 percent group?
13.35%
8. What was the average tax rate for the bottom 50 percent group?
2.95%
9. What percent of income (AGI) was in the top 25 percent group?
64.86%
10. What percent of taxes did the top 25 percent income group pay?
83.88%
11. What was the tax rate for the top 25 percent income group?
15.38%
12. What percent of income (AGI) was in the top 10 percent income group?
42.36%
13. What percent of taxes did the top 10 percent income group pay?
65.84%
14. What was the tax rate for the top 10 percent income group?
18.49%
15. What percent of income (AGI) was in the top 5 percent income group?
31.18%
16. What percent of taxes did the top 5 percent income group pay?
54.36%
17. What was the tax rate for the top 5 percent income group?
20.74%
18. What percent of income (AGI) was in the top 1 percent income group?
16.77%
19. What percent of taxes did the top 1 percent income group pay?
34.27%
20. What was the tax rate for the top 1 percent income group?
24.31%

Calculate the adjusted gross income (AGI) for the following *what-if* income descriptions. Use the answers to complete **column 1** on **Table C**. (Activity 2-B)

What if—

- A. You earned \$9.50 an hour in wages. You worked 40 hours a week and were paid for 52 weeks. \$19,760
- B. You worked all year for a monthly salary of \$8,000. You also had \$275 in interest income. \$96,275
- C. You earned \$14.00 an hour in wages and worked 40 hours a week for 50 weeks. \$28,000
- D. You worked for a monthly salary of \$5,000 and you had \$1600 in interest income. \$61,600
- E. You have a part-time job that paid \$6.75 an hour. You worked 20 hours a week for 25 weeks. Your spouse worked all year at a full-time job that paid \$4,000 a month. $\$3,375 + \$48,000 = \$51,375$
- F. Your yearly salary was \$42,000. Your spouse earned \$11.50 an hour and worked 40 hours a week for 52 weeks out of the year.
 $\$23,920 + \$42,000 = \$65,920$
- G. Your monthly salary was \$4,000 and you were paid for twelve months. Your spouse earned a salary of \$3,000 a month for each month of the year. \$84,000
- H. For the year, you had \$2,450 in taxable interest. You worked for a salary of \$8,000 a month for the entire year. Your spouse earned a salary of \$4,500 a month for each month of the year. \$152,450
- I. You worked at a full-time job that paid \$12.95 an hour. You worked 40 hours a week and were paid for 52 weeks. Your spouse worked 25 hours a week for 52 weeks at a part-time job that paid \$9.50 an hour.
 $\$26,936 = \$12,350 = \$39,286$
- J. For the year, you had \$5,875 in taxable interest and you earned \$7,500 in salary each month of the year. \$95,875

Inside the Vault - Income Taxes

What-If Worksheet

Calculate the adjusted gross income (AGI) for the following *what-if* income descriptions. Use the answers to complete **column 1** on **Table C**. (Activity 2-B)

What if—

- A. You earned \$9.50 an hour in wages. You worked 40 hours a week and were paid for 52 weeks.
- B. You worked all year for a monthly salary of \$8,000. You also had \$275 in interest income.
- C. You earned \$14.00 an hour in wages and worked 40 hours a week for 50 weeks.
- D. You worked for a monthly salary of \$5,000 and you had \$1600 in interest income.
- E. You have a part-time job that paid \$6.75 an hour. You worked 20 hours a week for 25 weeks. Your spouse worked all year at a full-time job that paid \$4,000 a month.
- F. Your yearly salary was \$42,000. Your spouse earned \$11.50 an hour and worked 40 hours a week for 52 weeks out of the year.
- G. Your monthly salary was \$4,000 and you were paid for twelve months. Your spouse earned a salary of \$3,000 a month for each month of the year.
- H. For the year, you had \$2,450 in taxable interest. You worked for a salary of \$8,000 a month for the entire year. Your spouse earned a salary of \$4,500 a month for each month of the year.
- I. You worked at a full-time job that paid \$12.95 an hour. You worked 40 hours a week and were paid for 52 weeks. Your spouse worked 25 hours a week for 52 weeks at a part-time job that paid \$9.50 an hour.
- J. For the year, you had \$5,875 in taxable interest and you earned \$7,500 in salary each month of the year.

Inside the Vault - Income Taxes

What-If Table

Table C

What-if income	(1) AGI	(2) Income Group	(3) Average Tax Rate	(4) Tax Liability based on Average Tax Rate	(5) Tax Liability based on 11.9% Proportional Tax Rate	(6) Difference in Tax Liability
A						
B						
C						
D						
E						
F						
G						
H						
I						
J						
<u>Total Income taxes paid</u>						

Table C

What-if income	(1) AGI	(2) Income Group	(3) Average Tax Rate	(4) Tax Liability based on Average Tax Rate	(5) Tax Liability based on 11.9% Proportional Tax Rate	(6) Difference in Tax Liability
A	\$19,760	Bottom 50%	2.95%	\$582.92	\$2,351.44	\$1,768.52 more
B	\$96,275	Top 10%	18.49%	\$17,801.25	\$11,456.73	\$6,344.52 less
C	\$28,000	Bottom 50%	2.95%	\$826.00	\$3,332.00	\$2,506.00 more
D	\$61,600	Top 25%	15.38%	\$9,474.08	\$7,330.40	\$2,143.68 less
E	\$51,375	Top 50%	13.35%	\$6,858.56	\$6,113.63	\$744.93 less
F	\$65,920	Top 25%	15.38%	\$10,138.50	\$7,844.48	\$2,294.02 less
G	\$84,000	Top 25%	15.38%	\$12,919.20	\$9,996.00	\$2,923.20 less
H	\$152,450	Top 5%	20.74%	\$31,618.13	\$18,141.55	\$13,476.58 less
I	\$39,286	Top 50%	13.35%	\$5,244.68	\$4,675.03	\$569.65 less
J	\$95,875	Top 10%	18.49%	\$17,727.29	\$11,409.13	\$6,318.16 less
<u>Total Income taxes paid</u>				\$113,190.60	\$82,650.39	\$30,540.22 less

Inside the Vault - Income Taxes

What-If Table

Instructions:

1. Refer to the "What-If" income descriptions on the *What-If Worksheet* to find the AGI in column 1 of **Table C**.
2. Use the AGI in column 1 and refer to **Table A** and **Table B** on Activity 1-A to complete columns 2 and 3.
3. Figure the tax liability in column 4 based on the average tax rate for each income group provided in **Table B**.

Note: This is only a "what-if" tax used as a representation of a progressive tax structure. Taxpayers in the same income group will have different tax rates based on deductions, tax credits, and individual circumstances.

4. Write the sum of all tax liabilities in column 4 at the bottom of the column.
5. Figure the tax liability in column 5 based on a proportional tax rate of 11.9%.

Note: This is only a "what-if" tax used as a representation of a proportional tax. Since the average tax rate for all taxpayers is 11.9%, the calculation is done to discover what effect using the average rate for all taxpayers would have on income tax liabilities of all income groups.

6. Write the sum of all tax liabilities in column 5 at the bottom of the column.
7. Compare the tax liability in column 4 to the tax liability in column 5. Write the difference in column 6. Write *more* or *less* after each figure in column 6 to designate if more or less tax is owed using column 5.

Income Tax: You Decide

Instructions:

Different tax structures result in different tax rates or percentages for levels of income. In the table below, there are seven different income levels listed in the AGI (Adjusted Gross Income) column. There are three different tax structures for each income level: **Tax A**, **Tax B**, and **Tax C**. The percentage of AGI that is due in taxes is provided for each tax structure. Complete the chart by calculating the tax due for each income level based for each tax structure.

AGI	TAX A		TAX B		TAX C	
	Tax Rate	Tax	Tax Rate	Tax	Tax Rate	Tax
\$15,000	12%		3%		16%	
\$30,000	12%		10%		15%	
\$40,000	12%		13%		14%	
\$60,000	12%		15%		13%	
\$95,000	12%		18%		12%	
\$150,000	12%		24%		11%	
\$250,000	12%		29%		10%	

1. Which tax structure is an example of a proportional tax?
2. Which tax structure is an example of a regressive tax?
3. Which tax structure is an example of a progressive tax?
4. Which tax structure in the table comes closest to meeting the criteria for "the perfect tax structure?" On a separate sheet of paper, write an essay defending your choice. Include information on the effects of your choice on individual taxpayers, society, and the government.

Income Tax: You Decide**Instructions:**

Different tax structures result in different tax rates or percentages for levels of income. In the table below, there are seven different income levels listed in the AGI (Adjusted Gross Income) column. There are three different tax structures for each income level: **Tax A**, **Tax B**, and **Tax C**. The percentage of AGI that is due in taxes is provided for each tax structure. Complete the chart by calculating the tax due for each income level based for each tax structure.

AGI	TAX A		TAX B		TAX C	
	Tax Rate	Tax	Tax Rate	Tax	Tax Rate	Tax
\$15,000	12%	\$1,800	3%	\$450	16%	\$2,400
\$30,000	12%	\$3,600	10%	\$3,000	15%	\$4,500
\$40,000	12%	\$4,800	13%	\$5,200	14%	\$5,600
\$60,000	12%	\$7,200	15%	\$9,000	13%	\$7,800
\$95,000	12%	\$11,400	18%	\$17,100	12%	\$11,400
\$150,000	12%	\$18,000	24%	\$36,000	11%	\$16,500
\$250,000	12%	\$30,000	29%	\$72,500	10%	\$25,000

1. Which tax structure is an example of a proportional tax? *Tax A*
2. Which tax structure is an example of a regressive tax? *Tax C*
3. Which tax structure is an example of a progressive tax? *Tax B*
4. Which tax structure in the table comes closest to meeting the criteria for "the perfect tax structure?" On a separate sheet of paper, write an essay defending your choice. Include information on the effects of your choice on individual taxpayers, society, and the government.

Form

W-2

**Wage and Tax
Statement**

(99)

2003

Department of the Treasury—Internal Revenue Service

**For Privacy Act and Paperwork Reduction
Act Notice, see separate instructions.**

Copy A For Social Security Administration—Send this entire page with Form W-3 to the Social Security Administration; photocopies are **not** acceptable.

Cat. No. 10134D

Do Not Cut, Fold, or Staple Forms on This Page — Do Not Cut, Fold, or Staple Forms on This Page

Label

(See page 12.)

Use the IRS
label.Otherwise,
please print
or type.Presidential
Election
Campaign
(page 12)L
A
B
E
L

H
E
R
E

Your first name and initial

Last name

If a joint return, spouse's first name and initial

Last name

Home address (number and street). If you have a P.O. box, see page 12.

Apt. no.

City, town or post office, state, and ZIP code. If you have a foreign address, see page 12.

Your social security number

Spouse's social security number

▲ Important! ▲

You **must** enter your
SSN(s) above.**Note.** Checking "Yes" will not change your tax or reduce your refund.

Do you, or your spouse if a joint return, want \$3 to go to this fund? ▶

You Spouse
☐ Yes ☐ No ☐ Yes ☐ No

Income

Attach
Form(s) W-2
here.Enclose, but
do not attach,
any payment.**Note.** You
must check
Yes or No. }

- 1**
- Wages, salaries, and tips. This should be shown in box 1 of your Form(s) W-2.
-
- Attach your Form(s) W-2.

1

- 2**
- Taxable interest. If the total is over \$1,500, you cannot use Form 1040EZ.

2

- 3**
- Unemployment compensation and Alaska Permanent Fund dividends
-
- (see page 14).

3

- 4**
- Add lines 1, 2, and 3. This is your
- adjusted gross income**
- .

4

- 5**
- Can your parents (or someone else) claim you on their return?

Yes. Enter amount from **No.** If **single**, enter \$7,800.
☐ worksheet on back. ☐ If **married filing jointly**, enter \$15,600.
See back for explanation.

5

- 6**
- Subtract line 5 from line 4. If line 5 is larger than line 4, enter -0-.
-
- This is your
- taxable income**
- .

▶ 6

Payments
and tax

- 7**
- Federal income tax withheld from box 2 of your Form(s) W-2.

7

- 8**
- Earned income credit (EIC).**

8

- 9**
- Add lines 7 and 8. These are your
- total payments**
- .

▶ 9

- 10**
- Tax.**
- Use the amount on
- line 6 above**
- to find your tax in the tax table on pages
-
- 24–28 of the booklet. Then, enter the tax from the table on this line.

10

Refund

Have it directly
deposited! See
page 19 and fill
in 11b, 11c,
and 11d.

- 11a**
- If line 9 is larger than line 10, subtract line 10 from line 9. This is your
- refund**
- .

▶ 11a

- ▶
- b**
- Routing number
-
-
-
-
-
-
-
-
-
-
- ▶
- c**
- Type:
- ☐
- Checking
- ☐
- Savings

- ▶
- d**
- Account number
-
-
-
-
-
-
-
-
-
-
-
-
-
-
-
-

Amount
you owe

- 12**
- If line 10 is larger than line 9, subtract line 9 from line 10. This is
-
- the
- amount you owe**
- . For details on how to pay, see page 20.

▶ 12

Third party
designeeDo you want to allow another person to discuss this return with the IRS (see page 20)? ☐ **Yes.** Complete the following. ☐ **No**Designee's
name ▶Phone
no. ▶ ()Personal identification
number (PIN) ▶ Sign
hereJoint return?
See page 11.
Keep a copy
for your
records.Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and
accurately lists all amounts and sources of income I received during the tax year. Declaration of preparer (other than the taxpayer) is based
on all information of which the preparer has any knowledge.

Your signature

Date

Your occupation

Daytime phone number

()

Spouse's signature. If a joint return, **both** must sign.

Date

Spouse's occupation

Paid
preparer's
use onlyPreparer's
signature ▶

Date

Check if
self-employed ☐

Preparer's SSN or PTIN

Firm's name (or
yours if self-employed),
address, and ZIP code ▶

EIN

Phone no. ()

**Use
this
form if**

- Your filing status is single or married filing jointly.
- You (and your spouse if married filing jointly) were under age 65 and not blind at the end of 2003. If you were born on January 1, 1939, you are considered to be age 65 at the end of 2003.
- You do not claim any dependents.
- Your taxable income (line 6) is less than \$50,000.
- You do not claim a deduction for educator expenses, the student loan interest deduction, or the tuition and fees deduction.
- You do not claim an education credit, the retirement savings contributions credit, or the health coverage tax credit.
- You had **only** wages, salaries, tips, taxable scholarship or fellowship grants, unemployment compensation, or Alaska Permanent Fund dividends, and your taxable interest was not over \$1,500. **But** if you earned tips, including allocated tips, that are not included in box 5 and box 7 of your W-2, you may not be able to use Form 1040EZ (see page 13). If you are planning to use Form 1040EZ for a child who received Alaska Permanent Fund dividends, see page 14.
- You did not receive any advance earned income credit payments.

If you are not sure about your filing status, see page 11. If you have questions about dependents, use TeleTax topic 354 (see page 6). If you **cannot use this form**, use TeleTax topic 352 (see page 6).

**Filling in
your
return**

For tips on how to avoid common mistakes, see page 21.

If you received a scholarship or fellowship grant or tax-exempt interest income, such as on municipal bonds, see the booklet before filling in the form. Also, see the booklet if you received a Form 1099-INT showing Federal income tax withheld or if Federal income tax was withheld from your unemployment compensation or Alaska Permanent Fund dividends.

Remember, you must report all wages, salaries, and tips even if you do not get a Form W-2 from your employer. You must also report all your taxable interest, including interest from banks, savings and loans, credit unions, etc., even if you do not get a Form 1099-INT.

**Worksheet
for
dependents
who
checked
"Yes" on
line 5**

(keep a copy for your records)

Use this worksheet to figure the amount to enter on line 5 if someone can claim you (or your spouse if married filing jointly) as a dependent, even if that person chooses not to do so. To find out if someone can claim you as a dependent, use TeleTax topic 354 (see page 6).

A. Amount, if any, from line 1 on front	_____		
	+ 250.00	Enter total ►	A. _____
B. Minimum standard deduction	_____		B. 750.00
C. Enter the larger of line A or line B here	_____		C. _____
D. Maximum standard deduction. If single , enter \$4,750; if married filing jointly , enter \$9,500	_____		D. _____
E. Enter the smaller of line C or line D here. This is your standard deduction	_____		E. _____
F. Exemption amount.			
• If single, enter -0-.			
• If married filing jointly and—			
—both you and your spouse can be claimed as dependents, enter -0-.			
—only one of you can be claimed as a dependent, enter \$3,050.			
G. Add lines E and F. Enter the total here and on line 5 on the front	_____		G. _____

If you checked "No" on line 5 because no one can claim you (or your spouse if married filing jointly) as a dependent, enter on line 5 the amount shown below that applies to you.

- Single, enter \$7,800. This is the total of your standard deduction (\$4,750) and your exemption (\$3,050).
- Married filing jointly, enter \$15,600. This is the total of your standard deduction (\$9,500), your exemption (\$3,050), and your spouse's exemption (\$3,050).

**Mailing
return**

Mail your return by **April 15, 2004**. Use the envelope that came with your booklet. If you do not have that envelope or if you moved during the year, see the back cover for the address to use.



Label

(See instructions on page 19.)

Use the IRS label. Otherwise, please print or type.

Presidential Election Campaign (See page 19.)

Label Here

For the year Jan. 1–Dec. 31, 2003, or other tax year beginning , 2003, ending , 20

OMB No. 1545-0074

Your first name and initial

Last name

Your social security number

If a joint return, spouse's first name and initial

Last name

Spouse's social security number

Home address (number and street). If you have a P.O. box, see page 19.

Apt. no.

City, town or post office, state, and ZIP code. If you have a foreign address, see page 19.

▲ Important! ▲

You must enter your SSN(s) above.

You Spouse
☐ Yes ☐ No ☐ Yes ☐ No

Note. Checking "Yes" will not change your tax or reduce your refund.

Do you, or your spouse if filing a joint return, want \$3 to go to this fund? . . . ▶

Filing Status

Check only one box.

- 1 ☐ Single
2 ☐ Married filing jointly (even if only one had income)
3 ☐ Married filing separately. Enter spouse's SSN above and full name here. ▶
4 ☐ Head of household (with qualifying person). (See page 20.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 ☐ Qualifying widow(er) with dependent child. (See page 20.)

Exemptions

If more than five dependents, see page 21.

6a ☐ **Yourself.** If your parent (or someone else) can claim you as a dependent on his or her tax return, **do not** check box 6a

b ☐ **Spouse**

c **Dependents:**

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> If qualifying child for child tax credit (see page 21)
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>
				<input type="checkbox"/>

No. of boxes checked on 6a and 6b

No. of children on 6c who:

- lived with you
- did not live with you due to divorce or separation (see page 21)

Dependents on 6c not entered above

Add numbers on lines above ▶

d Total number of exemptions claimed

Income

Attach Forms W-2 and W-2G here. Also attach Form(s) 1099-R if tax was withheld.

If you did not get a W-2, see page 22.

Enclose, but do not attach, any payment. Also, please use Form 1040-V.

- 7 Wages, salaries, tips, etc. Attach Form(s) W-2
8a **Taxable** interest. Attach Schedule B if required
b **Tax-exempt** interest. **Do not** include on line 8a 8b
9a Ordinary dividends. Attach Schedule B if required
b Qualified dividends (see page 23) 9b
10 Taxable refunds, credits, or offsets of state and local income taxes (see page 23)
11 Alimony received
12 Business income or (loss). Attach Schedule C or C-EZ
13a Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ ☐
b If box on 13a is checked, enter post-May 5 capital gain distributions 13b
14 Other gains or (losses). Attach Form 4797
15a IRA distributions . . . 15a b Taxable amount (see page 25)
16a Pensions and annuities 16a b Taxable amount (see page 25)
17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E
18 Farm income or (loss). Attach Schedule F
19 Unemployment compensation
20a Social security benefits . . 20a b Taxable amount (see page 27)
21 Other income. List type and amount (see page 27)
22 Add the amounts in the far right column for lines 7 through 21. This is your **total income** ▶

Adjusted Gross Income

- 23 Educator expenses (see page 29)
24 IRA deduction (see page 29)
25 Student loan interest deduction (see page 31)
26 Tuition and fees deduction (see page 32)
27 Moving expenses. Attach Form 3903
28 One-half of self-employment tax. Attach Schedule SE
29 Self-employed health insurance deduction (see page 33)
30 Self-employed SEP, SIMPLE, and qualified plans
31 Penalty on early withdrawal of savings
32a Alimony paid b Recipient's SSN ▶
33 Add lines 23 through 32a
34 Subtract line 33 from line 22. This is your **adjusted gross income** ▶

Tax and Credits**Standard Deduction for—**

• People who checked any box on line 36a or 36b or who can be claimed as a dependent, see page 34.

• All others:
Single or Married filing separately, \$4,750

Married filing jointly or Qualifying widow(er), \$9,500

Head of household, \$7,000

35	Amount from line 34 (adjusted gross income)	35	
36a	Check <input type="checkbox"/> You were born before January 2, 1939, <input type="checkbox"/> Blind. <input type="checkbox"/> Spouse was born before January 2, 1939, <input type="checkbox"/> Blind. Total boxes checked ▶ 36a		
b	If you are married filing separately and your spouse itemizes deductions, or you were a dual-status alien, see page 34 and check here ▶ 36b <input type="checkbox"/>		
37	Itemized deductions (from Schedule A) or your standard deduction (see left margin)	37	
38	Subtract line 37 from line 35	38	
39	If line 35 is \$104,625 or less, multiply \$3,050 by the total number of exemptions claimed on line 6d. If line 35 is over \$104,625, see the worksheet on page 35	39	
40	Taxable income. Subtract line 39 from line 38. If line 39 is more than line 38, enter -0-	40	
41	Tax (see page 36). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972	41	
42	Alternative minimum tax (see page 38). Attach Form 6251	42	
43	Add lines 41 and 42 ▶	43	
44	Foreign tax credit. Attach Form 1116 if required	44	
45	Credit for child and dependent care expenses. Attach Form 2441	45	
46	Credit for the elderly or the disabled. Attach Schedule R	46	
47	Education credits. Attach Form 8863	47	
48	Retirement savings contributions credit. Attach Form 8880	48	
49	Child tax credit (see page 40)	49	
50	Adoption credit. Attach Form 8839	50	
51	Credits from: a <input type="checkbox"/> Form 8396 b <input type="checkbox"/> Form 8859	51	
52	Other credits. Check applicable box(es): a <input type="checkbox"/> Form 3800 b <input type="checkbox"/> Form 8801 c <input type="checkbox"/> Specify	52	
53	Add lines 44 through 52. These are your total credits	53	
54	Subtract line 53 from line 43. If line 53 is more than line 43, enter -0- ▶	54	

Other Taxes

55	Self-employment tax. Attach Schedule SE	55	
56	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	56	
57	Tax on qualified plans, including IRAs, and other tax-favored accounts. Attach Form 5329 if required	57	
58	Advance earned income credit payments from Form(s) W-2	58	
59	Household employment taxes. Attach Schedule H	59	
60	Add lines 54 through 59. This is your total tax ▶	60	

Payments

If you have a qualifying child, attach Schedule EIC.

61	Federal income tax withheld from Forms W-2 and 1099	61	
62	2003 estimated tax payments and amount applied from 2002 return	62	
63	Earned income credit (EIC)	63	
64	Excess social security and tier 1 RRTA tax withheld (see page 56)	64	
65	Additional child tax credit. Attach Form 8812	65	
66	Amount paid with request for extension to file (see page 56)	66	
67	Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885	67	
68	Add lines 61 through 67. These are your total payments ▶	68	

Refund

Direct deposit? See page 56 and fill in 70b, 70c, and 70d.

69	If line 68 is more than line 60, subtract line 60 from line 68. This is the amount you overpaid	69	
70a	Amount of line 69 you want refunded to you ▶	70a	
b	Routing number <input type="text"/>	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
d	Account number <input type="text"/>		
71	Amount of line 69 you want applied to your 2004 estimated tax ▶	71	

Amount You Owe

72	Amount you owe. Subtract line 68 from line 60. For details on how to pay, see page 57 ▶	72	
73	Estimated tax penalty (see page 58)	73	

Third Party Designee

Do you want to allow another person to discuss this return with the IRS (see page 58)? ☐ Yes. Complete the following. ☐ No

Designee's name ▶	Phone no. ▶ ()	Personal identification number (PIN) ▶ <input type="text"/>
--------------------------	------------------------	--

Sign Here

Joint return? See page 20. Keep a copy for your records.

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number ()
Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation	

Paid Preparer's Use Only

Preparer's signature ▶	Date	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code ▶	EIN	Phone no. ()	

The Perfect Tax Structure

1. provides desirable incentives to work, save and invest;
2. is viewed as fair;
3. is easy to understand, and
4. generates sufficient revenues to fund spending decisions.

Kinds of Taxes

- **Proportional taxes** - take the same percentage of income from people in all income groups
- **Progressive taxes** - take a larger percentage of income from people in higher-income groups than from people in lower-income groups
- **Regressive taxes** - take a larger percentage of income from people in lower-income groups than from higher income groups