

Teacher Lesson Plan

Theme 4: What Is Taxed and Why
Lesson 3: Income Tax Facts

Time Frame

One to two class periods

Curriculum Area(s)

- Economics
- Civics/Government
- Technology
- History/Social Studies

Purpose

To help students understand that taxation involves a compromise of conflicting goals and that people who have the same income may not pay the same amount in taxes

Objectives

Students will be able to

- describe the “pay-as-you-earn” system of tax collection.
- explain that as the result of special tax treatment of certain activities and different sources of income, people with the same income may pay different amounts of taxes.

Materials

Online

[Student Lesson—Income Tax Facts](#)

[Activity 1: Income Distribution](#)

[Activity 2: Tax Facts Crossword](#)

[Assessment—Income Tax Facts](#)

[Assessment Solutions—Income Tax Facts](#)

Print (PDF)

[Teacher Lesson Plan](#)

[Info Sheet—Payroll Taxes](#)

[Worksheet—Analyzing Specific Tax Situations](#)

[Worksheet Solutions—Analyzing Specific Tax Situations](#)

[Assessment—Income Tax Facts](#)

[Assessment Solutions—Income Tax Facts](#)

[Complete Lesson Pack](#)

Web Links

[U.S. Census Bureau Historical Income Tables](#)

<http://www.census.gov/hhes/www/income/histinc/h03ar.html>

[The Tax History Project/Presidential Tax Returns](#)

<http://www.taxhistory.org/www/website.nsf/Web/PresidentialTaxReturns?OpenDocument>

Background

Taxation represents a compromise of conflicting goals. One goal is fairness. Other goals include: boosting productivity and economic prosperity; encouraging well-educated citizens; promoting strong families; and limiting the government burden.

Income taxes are collected on a “pay-as-you-earn” basis. Employers withhold taxes from every paycheck and send the money to the IRS on the employee’s behalf. At year’s end, this amount should be roughly equal to one’s **tax liability**.

Tax **withholding** benefits both taxpayers and the government. Without withholding, many would find it difficult to save enough money to pay their income taxes all at once. Government services might be disrupted and unreliable without continuous funding.

Income taxes are partly structured around the concepts of **vertical equity** and **horizontal equity**. Vertical equity asserts that unequals should not be taxed the same amount or the same percentage. Horizontal equity states that equals should be taxed equally. Despite these concepts, it is possible that two families or two businesses with identical incomes will pay different income taxes. **Tax deductions**, **exemptions**, and **tax credits** may lower tax liability. The government allows this special tax treatment to support or encourage behaviors, spending patterns, and lifestyles considered desirable.

Key Terms

exemptions—Amount that taxpayers can claim for themselves, their spouses, and eligible dependents. There are two types of exemptions—personal and dependency. Each exemption reduces the income subject to tax. The exemption amount is a set amount that changes from year to year.

horizontal equity—The concept that people in the same income group should be taxed at the same rate. “Equals should be taxed equally.”

tax credit—A dollar-for-dollar reduction in the tax. Can be deducted directly from taxes owed.

tax deduction—An amount (often a personal or business expense) that reduces income subject to tax.

tax liability (or total tax bill)—The amount of tax that must be paid. Taxpayers meet (or pay) their federal income tax liability through withholding, estimated tax payments, and payments made with the tax forms they file with the government.

vertical equity—The concept that people in different income groups should pay different rates of taxes or different percentages of their incomes as taxes. “Unequals should be taxed unequally.”

withholding (“pay-as-you-earn” taxation)—Money, for example, that employers withhold from employees’ paychecks. This money is deposited for the government. (It will be credited against the employees’ tax liability when they file their returns.) Employers withhold money for federal income taxes, Social Security taxes and state and local income taxes in some states and localities.

Opening the Lesson

Ask students:

- On what date must income tax returns be filed with the Internal Revenue Service?

on or before April 15

Explain that although April 15 is the filing deadline, it typically is not the day when most income taxes are paid. Most taxes are paid throughout the year when employers withhold tax money from each paycheck and send the money to the IRS.

Developing the Lesson

When an employer withholds taxes from an employee's pay to make "pay-as-you-earn" contributions to the IRS, the amount withheld reflects some of the deductions that the employee will claim when he or she files income tax forms. Ask students:

- How does tax withholding benefit both taxpayers and the government?

Without withholding, many would find it difficult to save enough money to pay their income taxes all at once. Government services might be disrupted and unreliable without continuous funding.

Explain that it is often difficult to agree on tax fairness. The "ability-to-pay" principle—in which taxes are based on one's income—is accepted by most as fair. People with higher incomes generally pay a higher percentage of their income as taxes than do people with lower incomes.

Although American taxpayers favor the principles of horizontal equity and vertical equity, those with equal incomes do not always pay the same tax amount. Certain factors, such as the number of dependents in a taxpayer's household, affect income tax liability. Help students understand that taxable income is less than total income because of exemptions and deductions.

Online Activities

Direct students to [Student Lesson—Income Tax Facts](#).

Have students complete one or more of the following activities.

[Activity 1: Income Distribution](#)—Take a virtual field trip to find out how much Americans earned.

[Activity 2: Tax Facts Crossword](#)—Use the clues to solve this tax crossword.

Print Activity

Print [Worksheet—Analyzing Specific Tax Situations](#) and distribute it to students.

[Worksheet Solutions—Analyzing Specific Tax Situations](#)

Classroom Activity

Have students look at [Info Sheet—Payroll Taxes](#) and explain the different sums withheld: federal income tax, Social Security (FICA) tax, Medicare, state tax, and local tax. Ask why money is withheld from the paycheck. Make sure students understand that withheld money goes for taxes.

- Ask students to look at Example 1 and determine how much was withheld for federal tax.
\$116.17
- How much was withheld for state tax in Example 2? **\$42.34**
- How much was withheld for Medicare in Example 3? **\$14.61**
- What accounts for the differences in withholding among the three examples?

differences in earnings; different tax rates; whether state and local taxes are withheld; exemptions

Concluding the Lesson

Have students describe the purpose of withholding and explain what factors determine the total tax liability at the end of the year. Guide students to see that taxes withheld may not be equal to the total tax liability and could result in students' owing money or receiving a refund. Ask students:

- Do you think exemptions, credits, and deductions are a good idea?
Answers will vary.
- Should the principles of horizontal and vertical equity be strictly followed?
Answers will vary.

Online Assessment

Direct students to complete Assessment—Income Tax Facts for this lesson.
Assessment Solutions—Income Tax Facts

Print Assessment

Print Assessment—Income Tax Facts, and have students complete it on paper.
Assessment Solutions—Income Tax Facts

Links

Go to Theme 6, Lesson 1 for information on the Internal Revenue Service.