

CHAPTER 5

TAXES

How Much of Your Income Will You Keep?

WHAT'S AHEAD

- 5.1** Taxes and Your Paycheck
- 5.2** File a Tax Return
- 5.3** Taxes and Government
- 5.4** Government Spending

LESSON 5.1

Taxes and Your Paycheck

GOAL

- ▶ Describe payroll taxes and factors that determine withholding.

KEY TERMS

- payroll tax
- income tax
- Federal Insurance Contributions Act (FICA)
- withholding
- gross income
- net income
- Form W-4
- Internal Revenue Service (IRS)
- allowance

Payroll Taxes

- ▶ Income taxes
- ▶ FICA, or contributions to Social Security and Medicare

Withholding

- ▶ **Your paycheck stub**
 - ▶ Gross income
 - ▶ Net income
- ▶ **Form W-4**
 - ▶ Your responsibility for proper withholding
 - ▶ Allowances
 - ▶ Adjusting your allowance
 - ▶ Overwithholding as a way to save

CHECKPOINT 5.1

- What are payroll taxes and how is the amount that is withheld from income determined?

CHECKPOINT 5.1 ANSWER

- **What are payroll taxes and how is the amount that is withheld from income determined?**
- Payroll taxes are calculated according to income as it is earned and paid by employee, employers, or both.
- The amount that is withheld is based on the employee's level of income and information provided on the W-4 form completed by the employee.

LESSON 5.2

File a Tax Return

GOALS

- ▶ Identify sources of information you need to complete your income tax return.
- ▶ Complete a federal Form 1040EZ.
- ▶ Describe how taxes differ for a self-employed person versus an employee.
- ▶ Explain why more than half of individual income tax returns are filed online.

KEY TERMS

- tax return
- Form W-2
- Form 1099-INT
- Form 1040EZ
- dependent
- deduction
- Social Security number
- taxable income

Your Income Tax Return

- ▶ A tax return is a set of forms that taxpayers use to calculate their tax obligation.

Sources of Information for Your Tax Return

- ▶ Form W-2
- ▶ Form 1099-INT

Income Tax Forms

- ▶ Form 1040EZ
- ▶ Form 1040A or 1040

How to Complete a 1040EZ

- ▶ Identify yourself
- ▶ Income
- ▶ Payments and tax
- ▶ Refund
- ▶ Amount you owe
- ▶ Sign
- ▶ Check for accuracy and file your return

Self-Employment Tax

- ▶ Paying on a quarterly basis
- ▶ Schedule C (1040)

Electronic Filing

- ▶ Advantages of electronic filing
 - ▶ Shorter processing time
 - ▶ Faster refund
- ▶ Filing options
 - ▶ IRS web site
 - ▶ Tax preparation software

CHECKPOINT 5.2

- What tax information is provided to you by your employer and your bank?
- What information do you need to calculate the amount of additional tax you owe or refund that is owed to you using a Form 1040EZ?
- What are the differences in the way traditional employees and self-employed people pay their taxes?
- How can you file your tax return online? What is the advantage of filing online?

CHECKPOINT 5.2 ANSWERS

- What tax information is provided to you by your employer and your bank?
- Employers provide Forms W-2, which summarize earnings and withholdings.
- Banks provide Forms 1099-INT, which summarize interest income.

CHECKPOINT 5.2 ANSWERS

- What information do you need to calculate the amount of additional tax you owe or refund that is owed to you using a Form 1040EZ?
- Amount of your earned income
 - Interest income
 - Income tax withholdings

CHECKPOINT 5.2 ANSWERS

➤ What are the differences in the way traditional employees and self-employed people pay their taxes?

- Taxpayers who work for an employer have their taxes deducted each pay period.
- Self-employed taxpayers calculate the amount of tax they owe each quarter and pay that amount to the government.

CHECKPOINT 5.2 ANSWERS

- How can you file your tax return online? What is the advantage of filing online?
- Use your tax preparation software to enter your tax information electronically or pay a tax service to do it for you.
 - Online filing generally allows you to get your tax refund faster.

LESSON 5.3

Taxes and Government

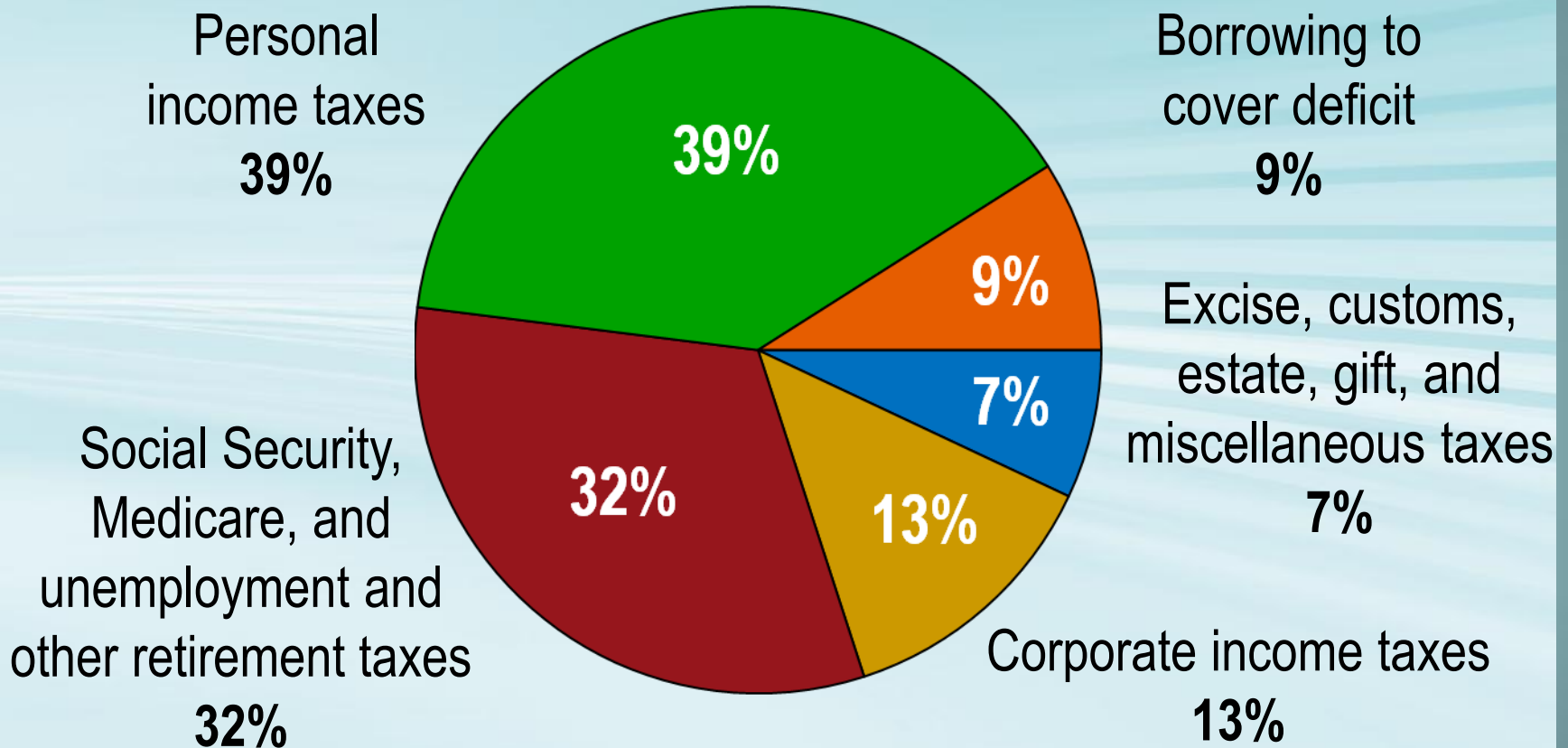
GOALS

- ▶ Describe where the federal government gets the money it spends.
- ▶ Explain principles and types of taxation.

KEY TERMS

- Sales tax
- Property tax
- Excise tax
- Estate tax
- Gift tax
- Business or license tax
- Customs duty or tariff

Sources of Federal Government Income for 2006



Social Security and Medicare

- ▶ Contributions to Social Security
- ▶ Contributions to Medicare
- ▶ Your employer's contribution

Principles of Taxation

- ▶ **Benefit principle**
- ▶ **Ability-to-pay principle**

Taxes and Income

- ▶ Progressive taxes
- ▶ Regressive taxes
- ▶ Proportional taxes

How Taxes Are Collected

- ▶ Direct taxes
- ▶ Indirect taxes
- ▶ Pay-as-you-earn taxes

Types of Taxes

- ▶ Income taxes
- ▶ Sales taxes
- ▶ Property taxes
- ▶ Excise taxes
- ▶ Estate and gift taxes
- ▶ Business and license taxes
- ▶ Customs duties and tariffs

CHECKPOINT 5.3

- What are the major sources of revenue for the federal government?
- What is the main difference between state or local taxes and federal income taxes?

CHECKPOINT 5.3 ANSWERS

➤ What are the major sources of revenue for the federal government?

- Personal income taxes
- Social Security and Medicare taxes
- Corporate income taxes
- Borrowing
- Other taxes that include excise, customs, estate, gift, and miscellaneous taxes

CHECKPOINT 5.3 ANSWERS

- What is the main difference between state or local taxes and federal income taxes?

Federal taxes take a larger percentage of consumers' income than do state and local taxes.

LESSON 5.4

Government Spending

GOALS

- ▶ Identify how taxes can influence consumer decisions.
- ▶ Explain how the government spends the money it receives.

KEY TERM

- public good

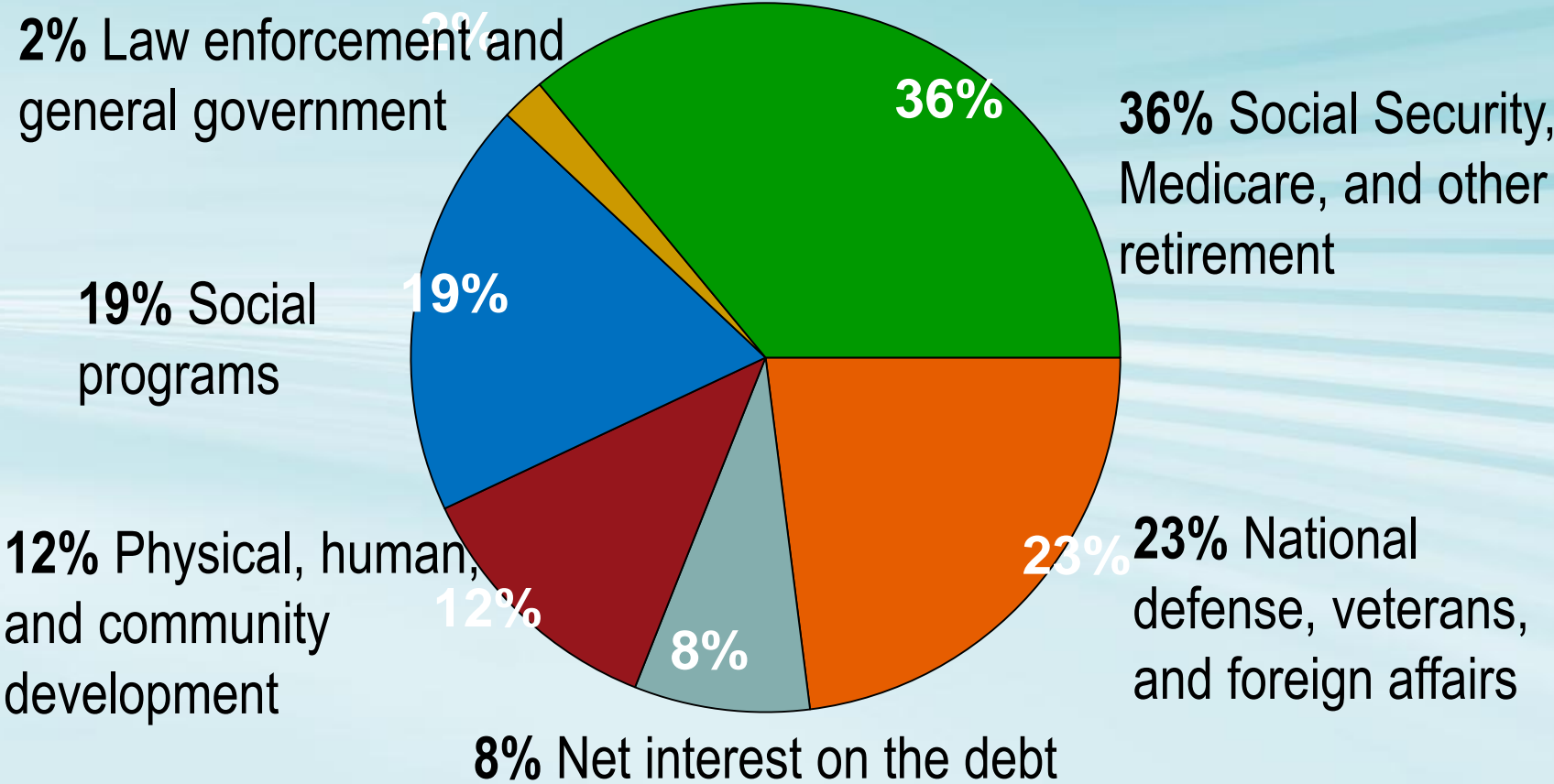
The Power to Influence

- ▶ “Sin” taxes
- ▶ Tax cuts
- ▶ Charities

Government Spending

- ▶ Social Security, Medicare, and other retirement
- ▶ Social programs
- ▶ National defense, veterans, and foreign affairs
- ▶ Physical, human, and community development
- ▶ Net interest on the debt
- ▶ Law enforcement and general government
- ▶ Debt reduction

U.S. Government Spending for 2006



Examples of What State and Local Governments Provide

- ▶ Building and maintaining roads
- ▶ Operating police and fire protection services
- ▶ Maintaining a criminal justice system
- ▶ Building and staffing schools
- ▶ Building and operating state colleges and universities
- ▶ Supporting medical facilities
- ▶ Constructing and operating sewage treatment plants
- ▶ Operating unemployment compensation programs

CHECKPOINT 5.4

- How can taxes influence your buying decisions? How can your local government use taxes to help local workers?
- Describe the categories of federal government spending. What types account for the largest part of the total?

CHECKPOINT 5.4 ANSWERS

- How can taxes influence your buying decisions?
How can your local government use taxes to help local workers?
- Taxes influence buying decisions by raising or lowering prices.
 - Local governments can lure businesses to an area by offering lower taxes to businesses willing to locate there.

CHECKPOINT 5.4 ANSWERS

- Describe the categories of federal government spending. What types account for the largest part of the total?
- Types of federal spending include Social Security, Medicare and other retirement programs; social programs; national defense; physical, human, and community development; law enforcement; and payments of interest on the national debt.
- More than half of total federal spending goes for Social Security/Medicare (36%) and for national defense (23%).