

Taxes and Government Spending

Section 1 – What are Taxes?



Government Funding

- Citizens of the United States authorize the government, through the Constitution and elected officials, to raise money through taxes.



- Taxation is the primary way that the government collects money.



- Without revenue, or income from taxes, government would not be able to provide goods and services.



Taxes and the Constitution

The Power to Tax

- Article 1, Section 8, Clause 1 of the Constitution grants Congress the power to tax.
- The Sixteenth Amendment gives Congress the power to levy an income tax.

“The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.”

Limits on the Power to Tax

- The power to tax is also limited through the Constitution. According to the Constitution:
 1. The purpose of the tax must be for “the common defense and general welfare.”
 2. Federal taxes must be the same in every state.
 3. The government may not tax exports.

Tax Bases and Tax Structures

A **tax base** is the income, property, good, or service that is subject to a tax.

Proportional Taxes

- A **proportional tax** is a tax for which the percentage of income paid in taxes remains the same for all income levels.

Progressive Taxes

- A **progressive tax** is a tax for which the percent of income paid in taxes increases as income increases.

Regressive Taxes

- A **regressive tax** is a tax for which the percentage of income paid in taxes decreases as income increases.

Characteristics of a Good Tax

A good tax has the following characteristics:

Simplicity

Tax laws should be simple and easily understood.

Economy

Government administrators should be able to collect taxes without spending too much time or money.

Certainty

It should be clear to the taxpayer when the tax is due, how much is due, and how it should be paid.

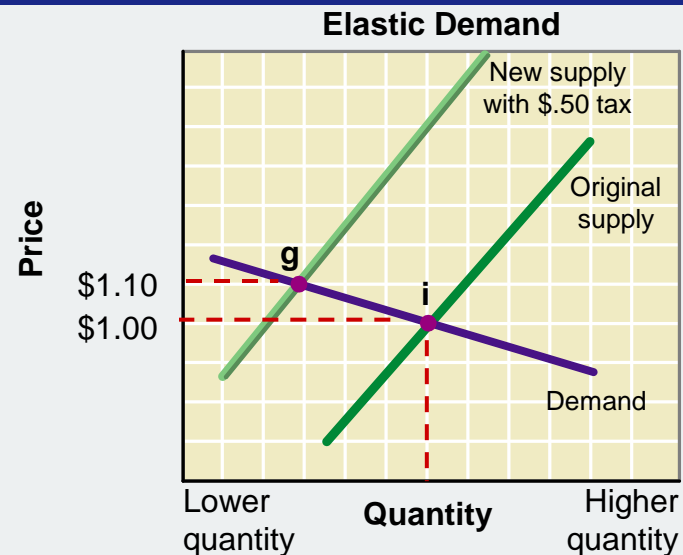
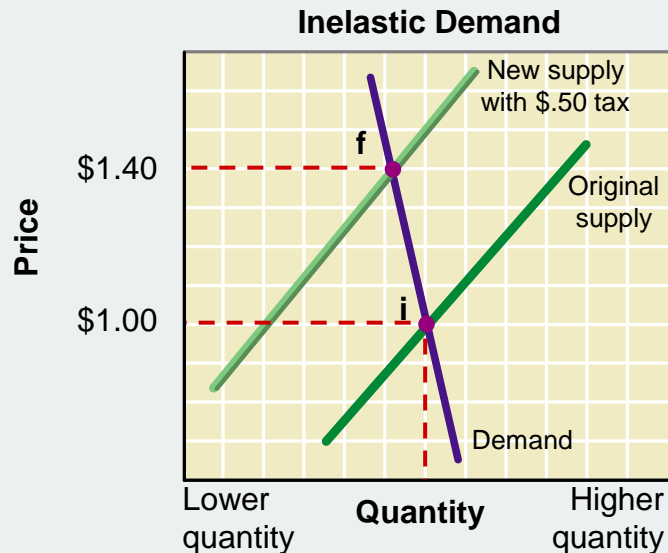
Equity

The tax system should be fair, so that no one bears too much or too little of the tax burden.

Who Bears the Burden of a Tax?

To fully evaluate the fairness of a tax, it is important to think about who bears the burden of the tax. The incidence of a tax is the final burden of the tax.

Elasticities of Demand and Tax Effects



If demand is inelastic, a tax will increase the price of a good and consumers will bear a large burden of the tax. If demand is elastic, the opposite is true.

Section 1 Review

1. Why do governments impose taxes?
2. What is the difference between a progressive tax and a regressive tax?
3. What are the four characteristics of a good tax?
4. Suppose that your town decides to levy a tax to raise funds for construction, maintenance, and other expenses for local schools. Should the tax be proportional, progressive, or regressive? Explain your answer.

Section 2 – Federal Taxes

Federal Taxes – Pre Test

- How do we pay individual income taxes?
- What are the characteristics of corporate income taxes?
- What is the purpose of Social Security, Medicare, and unemployment taxes?
- What are other types of taxes?

Individual Income Taxes

“Pay-as-You-Earn” Taxation

- Federal income taxes are collected throughout the course of the year as individuals earn income.

Tax Withholding

- **Withholding** is the process by which employers take tax payments out of an employee’s pay before he or she receives it.

Tax Brackets

- The federal income tax is a progressive tax. In 1998, there were five rates, each of which applied to a different range of income.

Filing a Tax Return

- A **tax return** is a form on which you declare your income to the government and determine your taxable income.
- **Taxable income** is a person's total (or gross) income minus exemptions and deductions.

- **Exemptions** are set amounts that you subtract from your gross income for yourself, your spouse, and any dependents.

HOURS AND EARNINGS		TAXES AND DEDUCTIONS	
Hours	Earnings	Description	Amount
20	200.00	FICA	15.20
		Federal	10.25
		State	5.10
		City	1.00
		Total Taxes	31.55
TOTAL			
Taxable Wages		Less Taxes	Net Pay
200.00		31.55	168.45

- **Deductions** are variable amounts that you can subtract from your gross income.

Corporate Income Taxes

- Like an individual, a corporation must pay a federal tax on its taxable income.
- Corporate income taxes are progressive – as a company's profits increase so does the amount paid in taxes.

Social Security, Medicare, and Unemployment Taxes

Social Security Taxes

- This program is funded by the **Federal Insurance Contributions Act (FICA)**. Most of the FICA taxes you pay go to **Social Security**, or Old-Age, Survivors, and Disability Insurance (OASDI)

Medicare Taxes

–**Medicare** is a national health insurance program that helps pay for health care for people over 65 and for people with certain disabilities. Medicare is also funded by FICA taxes.

Unemployment Taxes

- Unemployment taxes are collected by both federal and state governments.
- Workers can collect “unemployment compensation” if they are laid off through no fault of their own and if they are actively looking for work.

Other Types of Taxes

Excise Taxes

- A tax on the sale or production of a good. Federal excise taxes range from gasoline to telephone services.

Estate Tax

- a tax on the estate, or total value of the money and property, of a person who has died. Estate taxes are paid before inheritors receive their share.

Gift Taxes

- a tax on the money or property that one living person gives to another.

Import Taxes

- Taxes on imported goods are called **tariffs.**

Section 2 Review

1. Explain “pay-as-you-earn” taxation.
2. Describe withholding and explain how it would affect a student with a part-time job.
3. What is the purpose of FICA?
4. The founders of the United States wanted to avoid establishing a permanent aristocracy, or group of wealthy families who could control a great deal of the nation’s wealth. How is this idea related to estate and gift taxes?

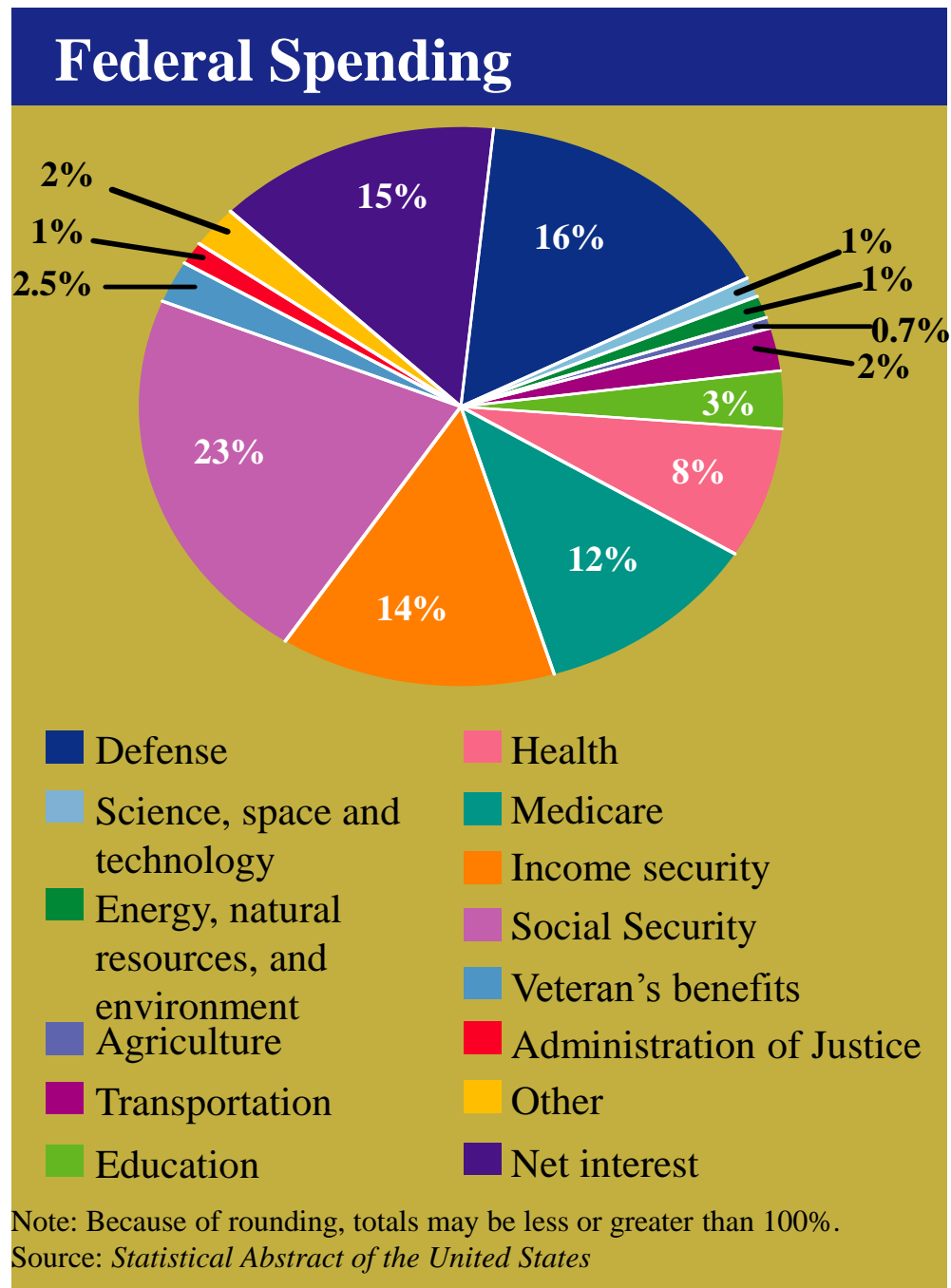
Section 3 – Federal Spending

Federal Spending

- What is the difference between mandatory and discretionary spending?
- What are some major entitlement programs?
- What are some of the categories of discretionary spending?
- How does federal aid impact state and local governments?

Spending Categories

- **Mandatory spending** refers to money that lawmakers are required by law to spend on certain programs or to use for interest payments on the national debt.
- **Discretionary spending** is spending about which government planners can make choices.



Discretionary Spending

Defense Spending

- Spending on defense accounts for about half of the federal government's discretionary spending.

Other Discretionary Spending

- Other discretionary spending categories include:
 - education
 - training
 - environmental cleanup
 - national parks and monuments
 - scientific research
 - land management
 - farm subsidies
 - foreign aid

Entitlements

An entitlement program is a social welfare program that people are “entitled” to if they meet certain eligibility requirements.

Social Security

- Social Security is the largest category of government spending.

Medicare

- Medicare pays for certain health benefits for people over 65 or people who have certain disabilities and diseases.

Medicaid

- Medicaid benefits low-income families, some people with disabilities, and elderly people in nursing homes. Medicaid costs are shared by the federal and state governments.

Section 3 Review

1. All of the following are examples of mandatory spending except
 - (a) defense spending.
 - (b) Medicare.
 - (c) Social Security.
 - (d) Medicaid.

2. An entitlement program is
 - (a) a program to provide benefits paid to everyone.
 - (b) a program to provide benefits paid to government employees only.
 - (c) a program to provide benefits to people who meet certain requirements.
 - (d) a program to provide benefits to illegal aliens.

**Section 4 –
State and Local
Taxes and
Spending**

State and Local Taxes and Spending

- How do states use budgets to plan their spending?
- How are state taxes spent?
- What are the sources of state tax revenue?
- How do local governments obtain and use revenues?

State Budgets

Operating Budgets

- pays for day-to-day expenses. Ex: salaries, supplies, and maintenance of state facilities.

Capital Budgets

- pays for major capital, or investment, spending.

Balanced budgets

- Some states have laws requiring balanced budgets.
- These laws only apply to a state's operating budget.

State Spending Categories



Education

- State education budgets help finance public state universities and provide some aid to local governments for elementary, middle, and high schools.

Public Safety

- State governments operate state police systems, as well as correctional facilities within a state.

Highways and Transportation

- Building and maintaining highways.
- States also pay for waterways and airports.

Public Welfare

- State funds support some public hospitals and clinics.
- States also help pay for and administer federal benefits programs.

Arts and Recreation

- State parks and some museums and historical sites

Administration

- Like the federal government, state governments spend money just to keep running.

State Tax Revenues

Limits to State Taxation

- Because trade and commerce are considered national enterprises, states cannot tax imports or exports. They also cannot tax goods sent between states.

Sales Taxes

- Sales taxes are the main source of revenue for many states.

Other State Taxes

- state income taxes
- excise taxes
- corporate income taxes
- business taxes
- property taxes.

Local Government Spending and Revenues

The Jobs of Local Government

- The following is a brief list of the many functions that local governments carry out or assist in:
 - Public school systems
 - Law enforcement
 - Fire protection
 - Public transportation
 - Public facilities, such as libraries and hospitals
 - Parks and recreational facilities
 - Record keeping (birth/death certificates, wills, etc.)

Local Government Revenues

- Property taxes are the main source of local revenue. These taxes are paid by people who own homes, apartments, buildings, or land.
- Local governments sometimes collect excise, sales, and income taxes as well.
- Some taxes, such as room and occupancy taxes, are aimed at nonresidents in order for local governments to earn additional revenue.

Section 4 Review

1. Describe the difference between a state's operating budget and its capital budget?
2. What is a balanced budget?
3. What are the main sources of state revenue? How do they differ from the main sources of local revenue?
4. Describe the difference between real property and personal property.

Section 4 Review

1. For most state governments, the main source of revenue is a
 - (a) room tax.
 - (b) property tax.
 - (c) general excise tax.
 - (d) statewide sales tax.

2. The main source of revenue for local governments is
 - (a) a property tax.
 - (b) an excise tax.
 - (c) a sales tax.
 - (d) an income tax.