



Taxes: Voluntary Compliance

Standard 2

The student will identify and describe the impact of local, state, and federal taxes upon income and standard of living.

Lesson Objectives

- Explain the legal and financial consequences of failing to pay taxes.
- Recognize the moral and ethical reasons for paying taxes.

Personal Financial Literacy Vocabulary

Ethics: A set of principles or beliefs that govern an individual's actions.

Morals: A system of values and principles of conduct that promotes good customs and virtues while condemning bad customs and vices.

Standard of living: The quality and quantity of goods and services available to people, and the way these goods and services are distributed within a country.

Quality of life: The overall enjoyment of life and sense of well-being.

Voluntary compliance: A system that relies on individual citizens to report their income freely and voluntarily, calculate their tax liability correctly, and file a tax return on time, according to the rules established by the Internal Revenue Service.

Introduction

Ashlee and Brittany need to earn money for cheerleading camp. They decide they should start mowing lawns. They agree to pay all of their expenses first, then divide the rest of the money earned 50/50.

Ashlee keeps a record of every lawn they mow, the expenses paid, and her personal income.

Brittany writes down all of the checks they receive and the expenses they pay, but does not keep a record of any income received from customers paying cash. She sees no reason to worry about cash payments because there is no record she received the money.

Which one of the girls is doing it correctly?

Lesson

While people in the United States are required to pay taxes, the system operates on a principle called “voluntary compliance”. In other words, it is based on the honor system—especially when it comes to filing your personal income taxes. Employers are required to withhold certain taxes and then report those withholdings to the state and federal government.

Most people in the United States believe it is their civic duty to pay their taxes and to honestly report their earnings. However, a small minority often look for ways to cheat the system by using fake deductions or inaccurately reporting their income.

You may have heard or read about people who say that paying taxes is illegal, a violation of their religious beliefs, or not required by the U.S. Constitution. Regardless of their reasoning, the courts have repeatedly ruled that paying taxes is mandatory. Sadly, many people have been misled by shady, “tax savings” reports and end up paying severe penalties for not complying with the law. If you do not report the correct amount of income (called underreporting taxable income) or if you do not file a tax return, you can face criminal prosecution. In other words, you can be heavily fined or even imprisoned for failing to pay your taxes accurately and on time.

The Internal Revenue Service (IRS), a division of the U.S. Department of Treasury, is charged with the responsibility of maintaining confidence in the federal tax system. To ensure people comply with the law, the IRS has the right to audit a person’s tax return. Basically, that means it can question anything that you have reported to the federal government. One of the best ways to avoid a tax audit is to file your income tax return on time. Additionally, you should keep good records of your income and expenses—and always

be honest with the information you report.

The IRS is also a valuable source of information if you have questions about taxes. For more information, you can visit the IRS Web site at <http://www.irs.gov>.

Reporting Your Taxes

Each spring, you will hear people talk about paying their taxes. According to law, everyone who receives a paycheck is required to submit a tax return to the IRS by April 15 each year. Employees receive a form, called a W-2, in January of each year from their employers. The W-2 includes the information needed to complete a federal or state tax return, if the state where you earned the income requires it. Oklahoma is one of the states that requires personal income tax. Interestingly, some cities in the United States also require people to pay city income taxes, but no cities in Oklahoma are among them.

As part of the filing process, you have the legal right to use a variety of deductions and exemptions to reduce your overall tax burden. That is where the voluntary compliance issue sets in. What you report as expenses, deductions, and other earnings is a personal choice even though the law is specific about what is legal.

Ethical and Moral Issues

Failing to pay taxes is high risk. One incentive for paying your personal income taxes—or any other required tax—is knowing you have done nothing illegal if you are questioned or audited by the government. But is this the only reason? No! Most citizens believe that paying taxes is part of their responsibility to others and to society. Even though people often complain about paying taxes or voice disapproval with how the government spends money, the vast majority of the population understands the importance of paying taxes to support the government and the services it provides.

Good citizenship is at the core of any democratic nation. It means doing your part for the common good, supporting the role of government at all levels, serving the local community, and obeying the laws enacted to maintain a civil society. Paying your taxes is part of being a good citizen.

In addition, your tax dollars provide public goods and services that increase our country's standard of living and quality of life. Standard of living relates to the level of wealth within the country while quality of life reflects what makes people happy. Without a tax structure, it would be impossible for a country to provide necessities that people use every day. For example, having clean drinking water and safe roads for travel are two factors that contribute to both standard of living and quality of life. Supporting social

DID YOU KNOW?

Professional athletes like Russell Westbrook and Tom Brady play games in several different states and cities around the United States. Did you know they have to file a tax return in every state where they play (if it has an income tax) and in many of the cities where the games are held. The same is true for entertainers like Ariana Grande or Maroon 5.

services for the elderly, paying military personnel to defend the nation, and sustaining other important programs combine to make life in a country better for the majority of its citizens. For many people, knowing their taxes help fund services like these is enough motivation to pay what they owe.

Of course, failing to file or deliberately choosing to underpay can result in various fines and penalties. If you underpay your taxes — knowingly pay less than you are required to pay — the most common action of the IRS is to charge the tax and impose a penalty with interest increasing the amount you owe. For example, if you take money out of your retirement account too early, the IRS will make you pay taxes on the withdrawal plus a 10% penalty on the money you withdrew.

Or, if you fail to report your earnings accurately, you may face penalties up to 25 percent of your unpaid taxes plus interest on the amount you underpaid. And, yes, you would still owe the taxes on that amount too. Even if you happen to make an honest mistake or accidental error when filing your taxes, you may still be required to pay rather stiff penalties or fines. If the IRS determines that you willfully committed fraud on your tax return, you can be tried in court; and if found guilty, you may be sent to jail for an extended period of time.

REMINDER

*When preparing your budget, be sure to include deposits to your savings account as a **FIXED** expense. The best budgets always start with paying yourself first!*

While some of these situations may seem extreme, it is important to understand your responsibilities regarding taxes.

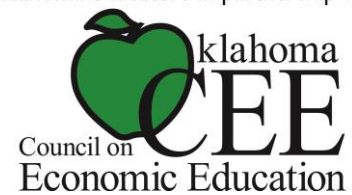
Conclusion

Paying taxes is part of living in a democratic society. Even if you do not like paying taxes, it is a moral and ethical responsibility of all U.S. citizens. Being honest about your personal income tax and voluntarily complying with the laws can help you avoid severe financial penalties that may wreck your financial future.

FINAL NOTE: If you said Ashlee, then you are correct. Ashlee's recordkeeping would allow her to report all of her income, whether paid with a check or with cash, on her personal income tax return. Her ethical behavior shows good citizenship and voluntary compliance with state and federal tax laws.

Brittany's behavior displays not only poor judgment, but is also unethical and illegal. If continued later in life, it could lead to serious consequences. While she may save a few dollars in taxes, she runs the risk of being penalized or facing time in prison.

This lesson was written and created by Oklahoma educators in partnership with



Name: _____ Class Period: _____

Taxes: Voluntary Compliance Review 2.2

Answer the following questions and give the completed lesson to your teacher to review.

1. People pay taxes for many reasons. Which of the following is NOT one of those reasons?
 - a. civic duty
 - b. moral reasons
 - c. fear of IRS penalties and imprisonment
 - d. controlling how their tax dollars are spent

2. If you knowingly underpay your taxes, the IRS can impose all of the following EXCEPT
 - a. collecting the taxes.
 - b. assessing a penalty.
 - c. bringing charges ending in imprisonment.
 - d. forcing your children to pay your tax burden.

3. An honor system under which you pay your taxes is called
 - a. voluntary compliance.
 - b. mandatory compliance.
 - c. individual compliance.
 - d. corporate compliance.

4. Federal and state income tax returns are due every year on
 - a. January 31.
 - b. April 15.
 - c. July 15.
 - d. December 31.

5. The primary purpose of taxes is to
 - a. allow people to have free goods and services.
 - b. take money from one group and give it to another.
 - c. provide services that improve our quality of life.
 - d. provide goods and services that are too expensive for people to buy.

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Civic Duties and Taxes Activity 2.2A

Read each of the following quotations and explain what each of the quotations means to you.

“Taxes are what we pay for a civilized society.” Justice Oliver Wendell Holmes

“People want just (or fair) taxes more than they want lower taxes. They want to know that every man is paying his proportionate share according to his wealth.” Will Rogers

“Collecting more taxes than absolutely necessary is legalized robbery.” President Calvin Coolidge

“Ask not what your country can do for you, but what you can do for your country.” President John F. Kennedy

Write a quote in the space below that expresses your view about civic responsibility.

Name: _____ Class Period: _____

Voluntary Compliance Activity 2.2B

Complete the following assignment and give it to your teacher for review.

1. List three reasons that people should pay their taxes.
 - a. _____
 - b. _____
 - c. _____

2. Explain three things that you learned from this lesson.
 - a. _____
 - b. _____
 - c. _____

3. You have been asked to prepare an advertisement showing why it is important to pay your taxes, accurately and timely. Provide your advertisement in the space below. You may write the words to a rap song, draw an illustration, or use another creative form to best illustrate your answer.