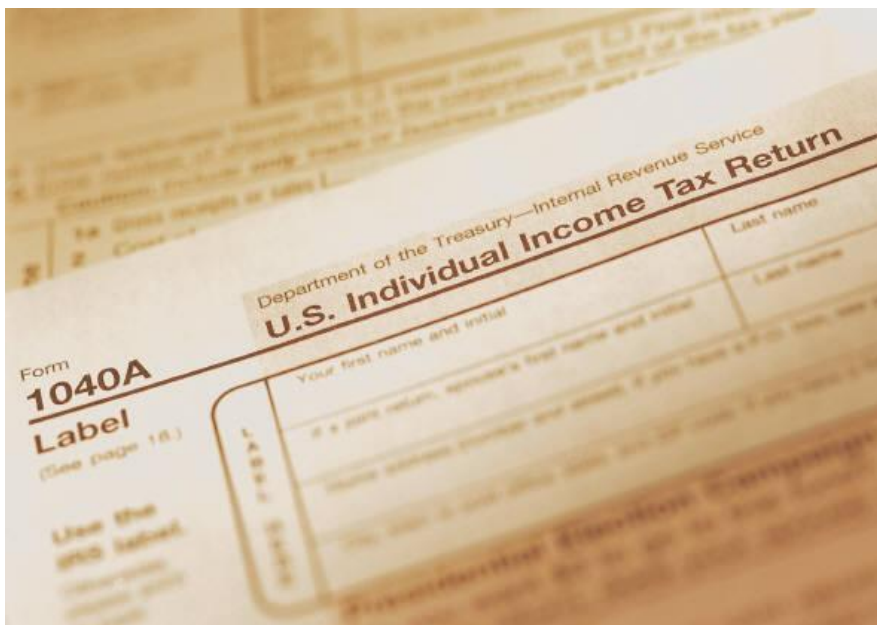


**Standard 2:** The student will identify and describe the impact of local, state, and federal taxes upon income and standard of living.

## Taxes: Voluntary Compliance



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. Then she subtracts the expenses from the amount received in checks. She 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 correct?

## Lesson Objectives

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



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

## Lesson

**M**ost people in our country believe that it is their civic duty to pay their taxes and to be honest with the government. However, a small minority look for ways to cheat the government by using phony deductions or failing to report their income appropriately.

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.

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 [www.irs.gov](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. Employees receive a form, called a W-2, in January of each year. The W-2 includes the information you need to complete your tax return. In some states, you are required to pay local and state personal income tax in addition to the federal. Other states, however, do not have local or state income tax. Oklahoma residents pay only state and federal personal income tax.



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 rather specific about what is legal.

### Ethical and Moral Issues

Failing to pay taxes is very risky. 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?



The answer is no. Most citizens believe that paying taxes is part of their responsibility to others and to society. Even though we may complain about paying and disagree with how the money is spent, we realize the importance of maintaining some level of government services.

Good citizenship is at the core of our society. It means doing your part for the common good, making your community and its processes work well, serving the community, and obeying the laws. Paying your taxes is part of being a good citizen. In addition, your tax dollars provide public goods and services designed to 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.

By paying taxes, you are assisting in providing many of the services people rely on every day. For example, having clean drinking water and safe roads for travel are two

factors that contribute to both our standard of living and our quality of life. Supporting social services for the elderly, paying military personnel to defend our nation, and sustaining other important programs combine to make life in our country better for the majority of our citizens. For many people, knowing their taxes help fund these services is enough motivation to pay taxes.

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 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 do not take money out of your retirement account when you get to be a certain age, the IRS will charge you a 50% penalty on the amount you were supposed to withdraw. And, yes, you would still owe the taxes on that amount too!

Sometimes you may just make an honest mistake when filing your taxes. In fact, accidental errors are the most common form of mistakes made when filing taxes. Your mistake, however, may still result in a fine or a penalty. If the IRS determines that you willfully committed fraud, then you can be tried in court, and, if found guilty, jailed. Tax fraud has imprisoned many criminals who failed to pay taxes on the money they obtained illegally! Sometimes it is easier to charge them with fraud than with some other crime.



**COMPLETE: CIVIC DUTIES AND TAXES – Activity 2.2.1**  
Ask your teacher to review your answers before continuing with this lesson.

In the box below, discuss some of the reasons people should pay their taxes:

- 1.
- 2.
- 3.
- 4.

What did you learn from this lesson?

How did it change your perspective on paying 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. It also helps us avoid being financially penalized or imprisoned by the IRS. Understanding your moral and ethical duty regarding taxes helps make April 15 an easier day!

*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, it 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 caught and penalized for her choices.*

Name: \_\_\_\_\_ Class Period: \_\_\_\_\_

## Taxes: Voluntary Compliance Review Lesson 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 the quality of life in the United States.
  - d. Provide goods and services that are too expensive for people to buy.

Name: \_\_\_\_\_ Class Period: \_\_\_\_\_



## Civic Duties and Taxes – Activity 2.2.1

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***

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***“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***

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

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

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

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