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AS SEEN IN USA TODAY APRIL 6, 2004

Weak enforcement spurs more tax filers to cheat

Today's debate: Paying federal taxes

Our view:

Properly funded, IRS would have tools to track down scofflaws.

Writing Uncle Sam a check for taxes owed is a springtime ritual everyone happily would avoid. Even so, from now through April 15, millions of Americans will be filling out tax forms and paying their fair share to keep the federal government running.

Even more painful for the honest filers who fork over the money is the fact that their ranks are dwindling. According to the IRS, the number of companies and individuals who cheat on their taxes is growing because the agency lacks the staff to enforce compliance with the tax code.

The IRS estimates it loses \$250 billion a year from those who fudge on their returns, fail to file or engage in tax-avoidance ruses. The lost revenue equals 10% of the federal budget and nearly covers Medicare's cost.

Cracking down on cheats is a less-controversial way to reduce a record \$500 billion deficit than cutting programs or raising tax rates. Yet Congress has spurned requests by the Clinton and Bush administrations to give the IRS more money to go after scofflaws.

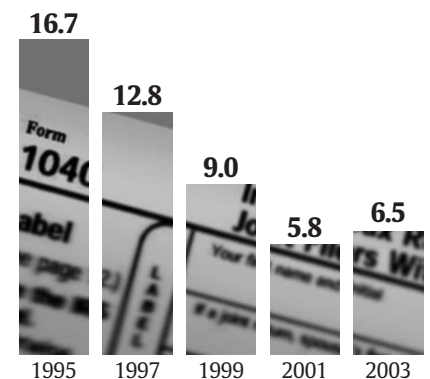
Lawmakers have been loath to enhance tax-collection enforcement even though the investment more than pays for itself. According to a study released last week by a board Congress created to oversee the IRS, a \$1 billion – or 10% – increase in the agency's budget would yield at least \$5 billion a year in collections. President Bush has gone halfway by proposing a \$490 million increase for the fiscal year that begins Oct. 1.

Even if approved by lawmakers, the additional funds would not make up for a decade of congressional cutbacks that have hampered the IRS' ability to do its job. Consider:

► **Fewer agents.** Since 1996, the number of IRS agents has been slashed from 22,983 to 16,749, a 27% drop.

Tax audits are rare

The chances of being audited by the IRS have begun to rise for the first time in years. Audits per 1,000 tax returns



Source: IRS

By Karl Gelles, USA TODAY

That has led to a decline in the number of individuals audited, from 1.9 million to 849,000. Criminal cases brought against alleged tax cheats have dropped by nearly half. Civil cases have fallen by more than 60%.

► **More shelters.** In 2003, the IRS was able to pursue only 18% of abusive tax scams it discovered. Had it challenged all of these cases, it would have collected an additional \$447 million. The IRS suspects it is losing billions

Presented by:



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more put in an increasing array of sophisticated shelters that it has been unable to detect as a result of too few investigators.

► **More cheats.** As IRS enforcement efforts have lagged, the public's acceptance of cheating has risen. Since 1999, the percentage who say it is OK to cheat "a little here and there" has grown from 8% to 12%, according to a poll by the IRS oversight board. The number saying it is OK to cheat "as much as possible" has grown from 3% to 5%.

IRS critics in Congress say agency cutbacks were needed to curb its past abuses. They say it has received more money in recent years as it has reformed its ways.

Indeed, congressional hearings in the 1990s exposed an overzealous agency that harassed thousands of honest taxpayers with overly aggressive audits. Under congressional pressure, the IRS has become more customer-friendly. Now it is properly focusing its firepower where most cheating occurs: on the complex returns of

corporations and rich individuals. But it still lacks the funds to do that job right.

Tackling tax cheats is a sensible way to bring in more money to a deficit-ridden Treasury – and reassure honest taxpayers that they're not the exception on April 15.

IRS has enough resources

Opposing view:
Simplified tax code would be more effective in reducing fraud.

By Richard Shelby

Our nation's federal income tax system depends on the compliance of American taxpayers. It is part of the social compact between the people and their government to provide for the public good. Most Americans make every effort to comply with the law and pay their taxes. But, as with any law, there always will be some who intentionally seek to avoid compliance or engage in outright fraud.

That is why enforcement of our tax laws is so important. If enforcement is lax or ineffective, it encourages more people to commit fraud. Although a recent General Accounting Office (GAO) report determined that it was uncertain whether tax fraud is on the rise, funding for IRS tax enforcement has been and continues to be an important priority for the Bush

administration and Congress. For the past several years, Congress consistently has increased funding for tax-law enforcement, including a \$265 million increase last year.

While Congress has provided the necessary resources for the IRS to carry out its mission, the IRS has squandered nearly \$5 billion on failed attempts to upgrade its decades-old computer system in an effort to improve customer service and compliance activities. This clearly illustrates that money is not always the answer.

Long term, a strong enforcement capability supported by necessary funding will continue to be a key part of combating tax fraud. But it never will be enough. Our federal tax code is a large part of the problem.

Our tax code and its regulations total more than 54,000 pages that are complex, confusing and costly to comply with. Comprehensive reform of

the tax code itself could go a long way to reducing tax fraud by making the process simpler, and the system fairer, for all taxpayers.

A less-complex tax code would provide fewer opportunities for cheaters and reduce the paperwork burden for all Americans.

I continue to believe that the only escape from this antiquated system is to scrap our existing code and for Congress to adopt a flat-rate tax. Until that time, we will continue to rely on the IRS to ensure that the tax code is fairly administered and appropriately enforced. With 100,000 employees and an annual budget that exceeds \$10 billion, I believe that the IRS has the resources it needs to get the job done.

Sen. Richard Shelby, R-Ala., chairs the Senate subcommittee that funds the IRS.

Today's debate: Paying federal taxes

Objectives:

Students will:

- read and discuss two views on enforcing tax laws.
- calculate the taxes various individuals would pay under both a proportional and a progressive tax system.
- draw conclusions about the pros and cons of each system.

Concepts:

- percentages
- socioeconomics
- progressive, regressive and proportional tax systems
- responsibility
- government revenue
- budgeting
- fraud

Preparation:

1. Print out the IRS 2003 Tax Rate Schedules at <http://www.irs.gov/formspubs/article/0,,id=109877,00.html>. Give one copy to each student. (Or, you can ask students to access the info online and print it out themselves.)
2. Pre-reading: Ask students if they have ever heard their parents talk about paying taxes. Why do many people feel the task is so burdensome? Why does the government collect taxes? Is paying taxes a civic duty?
3. Distribute the debate, "Paying federal taxes." Have students read both views silently. As a class, discuss the questions on the following page.
4. Review the three tax systems described under "Background." Ask students which one sounds the most equitable? Why?
5. Give each student a copy of the graphic organizer. Review the directions for the graphic, and ask individuals to complete it in class or for homework. After, student pairs should compare their charts and collaborate on the questions listed beneath the graphic.

Activity at a glance:

- Grade level: 9-12
- Subjects: civics, government, math, personal finance
- Estimated time for this activity: 60-90 minutes

Materials:

- Reading: "Today's debate: Paying federal taxes" (one copy per student)
- Graphic organizer: "Progressive vs. Flat Tax"
- 2003 IRS tax rate schedules available at <http://www.irs.gov/formspubs/article/0,,id=109877,00.html> (one copy per student)
- USA TODAY newspapers



Today's debate: Paying federal taxes

Discussion:

According to USA TODAY's view, why are more individuals and companies cheating on their taxes? How much does the IRS estimate it loses to tax cheating each year? How does tax evasion and fraud affect society? What factors have hampered the IRS's ability to effectively do its job? According to Sen. Richard Shelby, on what does our nation's federal income tax system depend? What happens when enforcement of tax laws is lax or ineffective? What measures does Shelby believe are necessary to enforce tax laws? What are the penalties for tax evasion?

Background:

There are three types of tax systems. In a *progressive* tax system, the tax rate increases with wealth. Therefore, the rich pay a larger percentage of their income in taxes than do the poor. In a *regressive* system, the poor put a larger percentage of their income toward taxes than the rich. In a *proportional* system, the government collects the same percentage of income from every citizen. Currently, the U.S. has a progressive system. However, many people, like Sen. Shelby, believe a proportional system – or a flat-rate tax – would be more efficient and equally fair. A flat-rate federal income tax proposes that all Americans be taxed at the same rate, usually around 17%.*

(*Source: National Center for Policy Analysis)

Activity:

To determine the impact that switching to a flat tax would have on Americans, complete the graphic organizer on the following page. Assume that the flat-tax rate would be 17%. To estimate taxes using the current rate schedule, use the IRS print-out (from <http://www.irs.gov/formspubs/article/0,,id=109877,00.html>).

Additional resources:

- The Internal Revenue Service offers teachers over 30 comprehensive lessons on understanding taxes. The site also features tax trivia and pages for students. Visit: http://www.irs.gov/app/understandingTaxes/jsp/teacher_home.jsp.

Activity extensions:

- Prepare a true/false quiz for your parents based on information from the debate. After they take your quiz, check it and discuss any errors by referencing the editorial. Finally, ask your parents how they feel about paying taxes. What is the most challenging aspect of preparing their tax return?
- Income and other kinds of taxes date back to Ancient Egyptian, Grecian and Roman cultures. Why do you think it is necessary for a government to tax its citizens? How would a government exist without the revenue that it generates from taxes? In small groups, make a list of all of the different types of taxes that are levied on individuals, e.g., sales tax, gas tax, real estate tax, etc. Then, consider the types of taxes that are levied on businesses and industries, e.g., import/export taxes, capital gains taxes, etc. With all the different types of taxes, how do you think lawmakers account for the USA's national debt?
- Research what the experts say about the flat tax. Then, with a partner, prepare a "Today's debate" that discusses its pros and cons.

Progressive vs. Flat Tax

Directions: Calculate the amount of taxes that each person or couple below would have paid for 2003. Use the IRS 2003 Tax Rate Schedules found at <http://www.irs.gov/formspubs/article/0,,id=109877,00.html>. (For the flat-rate amount, simply perform the necessary calculation.) In 2003, most parents received a tax credit of \$1,000 per child. You can deduct this amount from the middle column as well. (Couples who earned over \$110,000 probably received less than \$1,000 per child. Keep this in mind when working on Profile #7.) After performing your calculations, check them against a partner's. Then, together, answer the questions on the following page.

Note: Under the current tax system, there are countless other deductions that people at all income levels can take. Moreover, some flat-tax proposals include personal deductions and those for dependents. Others do not. In the interest of expediency, this activity does not take these factors into account. Rather, the worksheet is intended simply to reveal broad trends.

Profile	Estimated tax under current system	Amount of tax under 17% flat rate system with no deductions
1. A minimum-wage worker in a small city earns \$10,712 as a cashier at a fast-food restaurant. Filing status: Single		
2. A single mom in a rural area earns \$27,000 as a kindergarten teacher. She supports two children. Filing status: Head of household		
3. A middle-age man who supports a wife and two children earns \$32,000 as an electrician in a small city. Filing status: Married filing jointly		
4. A recent college grad who lives with his parents earns \$32,000 a year working as a junior systems analyst at a large corporation in a metropolitan area. Filing status: Single		
5. A professional couple in Washington, DC have a combined income of \$90,000 and three children. Filing status: Married filing jointly		
6. A professional couple in Washington, DC have a combined income of \$180,000 and no dependents. Filing status: Married filing jointly		



Profile	Estimated tax under current system	Amount of tax under 17% flat rate system with no deductions
7. A professional couple in Washington, DC have a combined income of \$550,000 and five dependents. Filing status: Married filing jointly		
8. A former president earns \$17 million through speaking engagements, book deals, etc. He is married to a lawyer with one adult child. Filing status: Married filing jointly		
9. A high-profile professional golfer earns approximately \$77 million in prize money and endorsements each year. He is married with no children. Filing status: Married filing jointly		

1. Under a flat-rate system with no deductions, what financial circumstances (e.g., number of dependents) would *not* influence a person's tax rate?

2. Who benefits most from the current tax system? From the flat-rate system?

3. What are the pros and cons of each type of taxation?

4. In your opinion, which system is the most equitable?

5. If the U.S. did adopt a flat-rate tax system, would you recommend that it include certain deductions? If so, what would they be? If not, why not? Are there other changes or exceptions that you would make to the flat-rate system?
