

Teacher Lesson Plan

Theme 4: What Is Taxed and Why
Lesson 2: Taxes in a Market Economy

Time Frame

One to four hours

Curriculum Area(s)

- Economics
- Civics/Government
- Technology
- History/Social Studies

Purpose

To help students understand the role of taxes in the market economy

Objectives

Students will be able to

- define market economy and explain the role that taxes play in it.
- describe the impact of government spending on the economy.

Materials

Online

[Student Lesson—Taxes in a Market Economy](#)

[Activity 1: The Circular Flow of Economy](#)

[Activity 2: Taxing Times](#)

[Activity 3: Income Tax Revenue](#)

[Activity 4: Consumer Spending Patterns](#)

[Assessment—Taxes in a Market Economy](#)

[Assessment Solutions—Taxes in a Market Economy](#)

Print (PDF)

[Teacher Lesson Plan](#)

[Info Sheet—Taxes and the Economy](#)

[Worksheet—The Effect of Taxes](#)

[Worksheet Solutions—The Effect of Taxes](#)

[Assessment—Taxes in a Market Economy](#)

[Assessment Solutions—Taxes in a Market Economy](#)

[Complete Lesson Pack](#)

Web Links

[Government Spending and GDP](http://www.whitehouse.gov/omb/budget/) <http://www.whitehouse.gov/omb/budget/>

[Income 2001 Graph](http://www.census.gov/hhes/www/img/incpov01/fig02.jpg) <http://www.census.gov/hhes/www/img/incpov01/fig02.jpg>

[Consumer Spending Patterns](http://www.bls.gov/news.release/cesan.nr0.htm) <http://www.bls.gov/news.release/cesan.nr0.htm>

Background

The United States has a **market economy**—an economic system based on free enterprise. In a market economy, money moves from the consumer to businesses when consumers buy goods and services. The government relies on tax revenue from the market economy.

Businesses pay sales tax, based on the purchase price of the goods. Other taxes include corporate income tax, based on business profits. In general, when a business's sales grow, so do its tax payments.

Taxpayers pay income taxes and payroll taxes to the federal government and may also pay income tax to state and local governments. Generally, the greater the income, the more a taxpayer will pay. Taxpayers pay sales taxes on goods purchased.

The government impacts the economy through the goods and services it purchases and provides. About one-third of the nation's economy is based on government spending. Most revenue for government spending comes from the collection of taxes.

When the economy is growing, consumers earn more and make more purchases. This increases business profits and boosts sales and corporate income tax revenue. Consumers may buy bigger homes (thus increasing revenue from property tax), travel more (thus increasing revenue from gasoline tax), and so on. In this way the government collects more taxes and has more money available to spend.

Key Terms

market economy—An economic system based on private enterprise that rests upon three basic freedoms: freedom of the consumer to choose among competing products and services, freedom of the producer to start or expand a business, and freedom of the worker to choose a job and employer.

Opening the Lesson

Explain the difference between a consumer and a producer. A consumer is one who uses goods or services and a producer is one who makes or provides goods or services or owns the resources that do so. Ask students:

- When have you been a consumer?
Answers will vary. One example may be shopping for clothes.
- When have you acted as producers?
Student answers will vary. Some examples could include babysitting or yard work services.

Explain that a worker is one who gets paid by a producer to provide goods or services.

Developing the Lesson

Ask students:

- What would you do if you received a pay raise or earned an increase in allowance?
Students might identify items they would purchase with the added money.
- How might your purchases affect the nation's economy?
Lead students to understand that the money they spend would provide money to businesses that produce goods or services. Because businesses pay corporate income taxes based on profit, the more profitable the company, the more income tax it generally pays. In state or local communities with sales tax, the purchase would provide sales tax revenue.

In general, the more people spend to purchase goods and services, the greater the revenue the government receives. During good economic times, government tax revenues often grow unless the government lowers tax rates. The government thus has more money to spend on services and purchases.

Online Activities

Direct students to Student Lesson—Taxes in a Market Economy.

Have students complete one or more of the following activities.

Activity 1: The Circular Flow of Economy—Study the circular flow of economy to discover the relationship between the government, businesses, and you.

Activity 2: Taxing Times—Calculate the amount of taxes owed by individual taxpayers.

Activity 3: Income Tax Revenue—Take a virtual field trip to learn about changes in income and income tax revenue.

Activity 4: Consumer Spending Patterns—Take a virtual field trip to learn more about consumer spending in the 1990s.

Print Activity

Distribute Worksheet—The Effect of Taxes to students.

Worksheet Solutions—The Effect of Taxes

Classroom Activity

Have students read Info Sheet—Taxes and the Economy. Ask students to name taxes that they or other family members have paid recently. Record them on the board, grouping them by type: property, sales, excise, income, and payroll taxes.

Divide students into teams, with the task of managing our economy. Have them examine each of the tax sources on the Info Sheet. Ask students:

- What would you do if tax revenue from that source rose?
- Would you increase government spending?
- Would you reduce the tax rate?
- Would you pay down government debt?

Next, ask students to discuss what happens when the economic climate has deteriorated and tax revenue has dropped. Ask students:

- Would you increase tax rates or cut spending?

Answers will vary.

Concluding the Lesson

As a review of the market economy, ask:

- Which sectors of the economy use labor?
government and businesses
- Which sectors consume goods and services produced by businesses?
households and government
- Which sectors use goods and services provided by government?
households and businesses
- How do you participate in the economy?
by providing labor while working, paying taxes to the government, and buying goods and services

Online Assessment

Direct students to complete [Assessment—Taxes in a Market Economy](#) for this lesson.
[Assessment Solutions—Taxes in a Market Economy](#)

Print Assessment

Print [Assessment—Taxes in a Market Economy](#), and have students complete it on paper.

[Assessment Solutions—Taxes in a Market Economy](#)

Links

To learn more about how the government decides what role it will play in the economy, go to [Theme 5, Lesson 2](#).

Visit the White House for more information on [Government Spending and GDP](#).