

## TAXES AND THE ROLE OF GOVERNMENT FROM A BIBLICAL PERSPECTIVE PRESENTATION TO THE CBFA 2001 CONFERENCE

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What is the role of government and taxes as ordained by the Bible? This is a question that has been asked even during biblical times. In Matthew 22:17 Jesus was asked “*Tell us then, what is your opinion? Is it right to pay taxes to Caesar or not?*” This question was an attempt to trap Jesus. How would Jesus answer? Was God supreme? Must Caesar be obeyed? His response, “*Give to Caesar what is Caesar’s, and to God what is God’s*”<sup>1</sup> silenced those who asked the question. Jesus was informing Christians under the Roman yoke; that although God is the ultimate authority, there are individuals who have authority over us. The Lord also knew that conflict between these two authorities was inevitable. Whenever the secular power demands for itself honors that belong only to God, Christians must resist. When there is a conflict between the directions of the two authorities, the believer of Christ should recognize the supremacy of the Word of God and resist earthly governments and authorities.<sup>2</sup>

Government and taxes are an integral part of our society. But how do we implement such a strategy in our current society? How do we embrace the spirit of the early Christian Church for servitude as a means of following Jesus’ Commandments?

A strategy must be developed. A central focus of this paper is the provisions and effect of the Economic Growth And Tax Relief Reconciliation Act of 2001 (Tax Relief Act). President George W. Bush stated that the prior tax code is “full of inequities” and that his goal is to make the USTC more equitable and family friendly.<sup>3</sup>

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<sup>1</sup> Matthew 22:21.

<sup>2</sup> Mitchell, Lindell, *Pack of Lies 2 – The Christians Must Have No Voice In Government*, PG 1.

<sup>3</sup> Bush, George W.; *The President’s Agenda for Tax Relief*;

# **Taxes And The Role Of Government From A Biblical Perspective**

**Presentation  
For The  
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# Taxes And The Role Of Government From A Biblical Perspective

## I. Introduction

Income taxes, as we know them, became a reality with the passage of the 16<sup>th</sup> Amendment to the Constitution. At that time, the highest tax rate was 6% and the tax structure was relatively family neutral as to its effects or incentives to family structure. The income tax was considered at the time a short time fix to pay for the war effort during World War I. During the remainder of the century, taxes have become an increasingly integral part of our national politics. Perceived disincentives to traditional family structures have slowly become a part of the United States Tax Code (USTC). There has been an attempt in the Economic Growth And Tax Relief Reconciliation Act of 2001 (Tax Relief Act) to reduce the negative effects of taxes on the traditional family. Many individuals have viewed the USTC as being anti-family. President George W. Bush stated that the prior tax code is “full of inequities” and that his goal is to make the USTC more equitable and family friendly.<sup>1</sup>

The overall structure of this paper will be to first discuss the Biblical role of government and to identify the Biblical family structure. Next, the paper will discuss the role government and in particular the USTC has had on the family during the latter 1900’s and into the current century. It is the intention of the paper to then present the provisions of the Tax Relief Act and anticipate their impact upon the family structure and the citizens of this country.

## II. Biblical Role of Government, Church, and Family.

### Government and the Church

What is the role of government and taxes as ordained by the Bible? This is a question that has been asked even during biblical times. In Matthew 22:17 Jesus was asked “*Tell us then, what is your opinion? Is it right to pay taxes to Caesar or not?*” This question was an attempt to trap Jesus. How would Jesus answer? Was God supreme? Must Caesar be obeyed? His response, “*Give to Caesar what is Caesar’s, and to God what is God’s*”<sup>2</sup> silenced those who asked the question. Jesus was informing Christians under the Roman yoke; that although God is the ultimate authority, there are individuals who have authority over us. The Lord also knew that conflict between these two authorities was inevitable. Whenever the secular power demands for itself honors that belong only to God, Christians must resist. When there is a conflict between the directions of the two authorities, the believer of Christ should recognize the supremacy of the Word of God and resist earthly governments and authorities.<sup>3</sup>

Examples of the Bible’s attitude of government and its leaders are throughout the Bible. When Caesar Augustus issued the census decree, Joseph and Mary were obedient.<sup>4</sup> Additionally, God did not remove His people from Egypt until Pharaoh had given permission. (Of course

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<sup>1</sup> Bush, George W.; *The President’s Agenda for Tax Relief*;

<sup>2</sup> Matthew 22:21.

<sup>3</sup> Mitchell, Lindell, *Pack of Lies 2 – The Christians Must Have No Voice In Government*, PG 1.

<sup>4</sup> Luke 2:1.

there were other factors, but nevertheless God took the time to convince Pharaoh to release the Jewish people. In so convincing Pharaoh, God also showed His power.) Jesus taught and performed miracles in the presence of government officials and representatives. He was even able to work through a lowly tax collector. Jesus treated Pontius Pilate with the respect due Pilate's position. Jesus did not suggest open rebellion against the government, and even stopped Peter when Peter attempted to resist His arrest. (It was for the glory of God that the arrest was permitted.) False teachings were another matter. Jesus did not mince words when the Jewish leadership was misleading God's people in matters of eternal importance.

A central question remains to be answered. What is the role of government when governing a people of faith? Should the government hold Biblical principles central? What is and should be the extent that faith plays in governing? Under the Old Testament model, government was established with God as the supreme authority. The New Testament does little to further clarify or hinder this perspective. Government itself was an institute ordained by God. In the beginning, God spoke to His people directly, through visions and dreams, or through angels and prophets. It was at the request of the people that a King (Saul) was selected by God and placed at the head of God's chosen people. But the underlying power, or perhaps it would be better to say the supreme power, is God. He directly selected rulers and judges in the past. Is God's hand still present? I believe that it is. Events happen with the full knowledge of God. The New Testament clarifies for us the supremacy of God's power and the need for a faith perspective for both government officials and citizens.

Many leaders in the United States, both past and present, govern(ed) according to Biblical principles. A constant theme of these leaders is that it is God that will provide protection for the United States against its enemies. Our 1<sup>st</sup> president, George Washington characterized himself as "...but the humble agent of a favoring heaven...." Thomas Jefferson called for a day of fasting and prayer in 1774 as a member of the Virginia Assembly. Former president James Madison made a motion to enact Benjamin Franklin's appeal for prayer at the Constitutional Convention. Abraham Lincoln was a man of faith that frequently turned to the Almighty during times of trials and frequently called the people to days of fasting and prayer.<sup>5</sup> There are many examples of faith-based leadership, from our founding fathers, to esteemed leaders such as Abraham Lincoln, to the faith expressed by our current president, George W. Bush. During colonial times, a book that was influential was *Lex Rex*, written by Samuel Rutherford. The premise of the book was that "law and government must be based on the Bible rather than the word of man. All men are under the law and not above it."<sup>6</sup> The only man of the clergy to sign the Declaration of Independence was John Witherspoon, a Presbyterian preacher. It is believed that he was responsible for weaving the principles of God's supremacy, as outlined in *Lex Rex*, into the Constitution of the United States.

## The Role Of The Believer

Turning to the role of the believer and the mission of the Christian Church, the roles are much more clarified in the Bible. In Matthew, Jesus instructs us:

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<sup>5</sup> Leidner, Gordon, *Lincoln's Faith In God*, ©2000 by Great American History

<sup>6</sup> Mitchell, Lindell, *Pack of Lies 2 – The Christian Must Have No Voice In Government*, pg 2

*Go therefore and make disciples of all the nations; baptize them into the name of the Father, and of the Son, and of the Holy Spirit; and teach them to obey every command which I have given you. And remember, I am with you always, day by day, until the Close of the Age.<sup>7</sup>*

Amen

There are further instructions in the teachings of Jesus Christ:

*A new commandment I give you, to love one another; that as I have loved you, you also may love one another.<sup>8</sup>*

*Dependent on Him, the whole body--its various parts closely fitting and firmly adhering to one another-- grows by the aid of every contributory link, with power proportioned to the need of each individual part, so as to build itself up in a spirit of love.<sup>9</sup>*

But how do we implement such a strategy in our current society? How do we embrace the spirit of the early Christian Church for servitude as a means of following Jesus' Commandments? Much of social history chronicles believers and the Church ministering to the needs of the poor, the sick, and the weak. Over time, government has usurped much of this responsibility from the Church. The current tax system serves many purposes other than merely raising revenue for the operations of government. Built in the tax system is the concept of transfer taxes, those funds that are taken from one set of citizens to be given to other citizens based on criteria established by the government. But is this a correct role of the government or should this be the role of the people? Or are we risking God's wrath by ignoring the alien, the fatherless, and the widow? (See Ezekiel 22:7) The ancient Hebrews lived in extended families or clans. It was responsibility of the extend family or clan to care for those within their own family or clan. A strong, well-functioning family can fulfill the physical and emotional needs of its members. Strong family ties provide the love and security that God intended for us and is a requirement for a joyful life.

President George W. Bush has indicated a willingness to return the responsibility to care for others in the community to faith-based organizations. How should we respond? Should we embrace this overture? Should we be cautious? Will faith-based organizations be faced with the daunting prospect of becoming accountable to the Federal government? The answer is complicated and difficult. In order to fully provide for our community without governmental funds is only possible with God's help. Are we willing to put our trust totally in God's hand. If the role of the early Church and its people is regained, then the need for taxes in general will be reduced as the need for social support safety nets (welfare) is reduced.

The bottom line is that the family is the cornerstone of the early Church and to Biblically based societies. It is also Biblical to support a government that is not in conflict with the Word of God. We are faced with a challenge to demand less from our Government and rely more from God. Are we ready?

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<sup>7</sup> Matthew 28:19-20 NIV.

<sup>8</sup> John 13:34 NIV.

<sup>9</sup> Ephesians 4:16 NIV.

### III. Governmental and United States Tax Code effect on the Traditional Family Structure.

In the United States, we are constantly bombarded with images and stories of the deterioration of the family unit. The number of single parent families continues to increase and divorce and unwed motherhood appear to have lost their stigma, both in the secular and the Christian world. With single parent families, there are new challenges.<sup>10</sup> God did not intend for society to be fragmented, or for families to be dysfunctional with ineffective individuals leading families. Has the government, which we have turned to for assistance and leadership, failed the family? There are many reports that the current tax structure and other aspects of government, from Social Security Benefits to Medicare/Medicaid do not support a strong and viable family unit, but may actually discourage a traditional family. Some anecdotal evidence is that married couples that are retired will frequently receive less than two retire individuals. In addition, the rules governing who receive Medicare/Medicaid benefits encourage married individuals to divorce so that the ill marital partner may receive government benefits.

The USTC may inadvertently influence a couples' decision to marry or co-habitat outside the bounds of marriage. Taxpayers that remain single and decide to live together may face a lower tax burden than individuals who chose to marry. This bias has been referred to as the Marriage Penalty.

The bias against families is rife within the USTC. However, there have been some positive provisions, such as the Hope and Lifetime Learning Education Credits, and IRA's. Additionally, taxpayers are allowed to deduct what is referred to as a personal exemption and standard deduction to help offset the average costs of living.

### IV. Discussion of the Economic Growth And Tax Relief Reconciliation Act of 2001 (Tax Relief Act).

#### Tax Relief Act Background

The tax reform was a major component George W. Bush presidential campaign. He stated his position on faith and how that faith has shaped his view of families and the role of government. To his credit, he introduced a plan to congress that followed the principles set out in his position papers during the campaign. Some of the goals of the Tax Relief Act were as follows<sup>11</sup>: (1) Increasing Tax Fairness; (2) Promoting Social Goals; (3) Preserving Prosperity & Stimulation of the Economy. As passed, The Tax Relief Act is forecast to reduce taxes by \$1.35 trillion by 2011. As such, it is the largest tax cut since 1981. To

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<sup>10</sup>As reported by Steven Simpson a study of Missouri children demonstrated that children were eight (8) times more likely to die from abuse or neglect where there is a non-married partner living in the same household. Additionally, Mandara and Murray found that children with non-married partners tended to have problems with self-esteem.

<sup>11</sup> <http://www.bushtaxrelief.com/about.asp>, June 7, 2001, pgs 1-7

comply with Congressional budget rules, the Tax Relief Act has a sunset provision. All provisions contained in the Tax Relief Act will expire after December 31, 2010.

## Strengthening Of The Economy

The health of the economy is a key to the perceived well being of the population. A declining economy may spell unemployment and other financial challenges to the family. Each presidential administration has strived to ensure an expanding economy that provides for job stability and growth. During To this The Tax Relief Act had a one-time bonus for taxpayers during the summer of 2001. Refund checks were mailed out to taxpayers. The timing of the checks was based on the last name of the taxpayers. The refund tax checks were intended to represent an advance refund of Federal Income Taxes. The new lowest tax rate is 10 % (reduced from the old minimum tax rate of 15% on the 1<sup>st</sup> \$6,150. As such, the checks represent 5% (15% less 10%) on the 1<sup>st</sup> \$6,000 of taxable income, as determined by the tax return filed during tax year 2000. As such, it is possible that not all individuals that should get a refund based on 2001 income will get a refund due to either their filing status or income in tax year 2000. It is also possible that individuals that qualified for a refund based on their 2000 tax return will receive a refund despite not qualifying for a refund based on 2001 income and/or filing status.<sup>12</sup> The lower tax rates are expected to rekindle the economy, but the anticipated effect may be hampered by the fact that the tax rate reductions are back-loaded<sup>13, 14</sup>.

Additionally, the current administration recognized that the Federal Income Tax is an every increasing burden to the United States Economy. One possible measurement of the tax burden to society as a whole is tax as a percentage of gross national product (GNP). Tax, as represented as a percentage of the GNP<sup>15</sup>, has increased during the prior 40 years, as represented by Table 1. Of course, the converse of this argument may be that the federal government has been producing more. The settlement of this is beyond the scope of this paper.

### ***Tax As A Percentage of Gross National Product<sup>16</sup>***

***Table 1***

<b><i>Decade</i></b>	<b><i>Percentage</i></b>
<b><i>1960's</i></b>	17.8%
<b><i>1970's</i></b>	17.9%
<b><i>1980's</i></b>	18.3%

<sup>12</sup> Lewis, Roy; *Quirks in the 2001 Tax Act*; June 8, 2001, p 2.

<sup>13</sup> The term back-loaded is a term that refers to the fact that many of the benefits are not available to taxpayers immediately, but instead become available over a period of years.

<sup>14</sup> Mitchell, Daniel, *Economy Demands A Bigger Cut*; p 1.

<sup>15</sup> Gross National Product

<sup>16</sup> PriceWaterhouseCooper, LLP, *The Tax Relief Act of 2001*, PG 2.

<b>1990's</b>	18.6%
<b>2000 Old Law</b>	20.2%
<b>Estimated Under The Tax Relief Act</b>	19.2%

Looking at the Tax Freedom Day can show a second measure of the increasing burden tax on the average working individual. Table 2 shows the progression of the Tax Freedom Day during the prior 20 years. Incredibly, the average worker works a third of each day in order to pay his/her tax bill. The increased tax burden is a factor in the perception that couples must have two wage earners in order to make ends meet.

The primary vehicle of reducing the overall tax burden in the current Tax Relief Act was the reduction of individual income tax rates. The downside of the Tax Relief Act is that the savings are not immediate. The taxpayers will not receive the full benefit of the reduced tax rates until the year 2007.

<b>Tax Freedom Day Table 2<sup>1</sup></b>			
<b>Tax Year</b>	<b>Freedom Day</b>	<b>Number of Days</b>	<b>% Of Year</b>
<b>1980</b>	April 21	112	30.5 %
<b>1990</b>	April 22	112	30.6 %
<b>2000</b>	May 3	124	33.8 %

### **Earned Income Tax Credit (EITC)**

The current tax system has a cruel twist, namely that taxpayers who face the highest marginal tax rate<sup>17</sup> are often those that are least able to pay. Individuals who are subject to the Earned Income Tax Credit<sup>18</sup> phase-out are subject to the highest marginal rates in the system. The Bush website points out “Many single moms face higher marginal tax rates than the wealthy.”<sup>19</sup> It was the position of the Bush presidential campaign that such provisions in the current tax code cripple the ability of individuals to better their economic position, as the next dollar earned will have a diminished reward. The then presidential candidate George W. Bush, stated, his tax proposal “... promotes the values that make the American economy second to none -- access to the middle class, family, equal opportunity, and the entrepreneurial spirit.”<sup>20</sup> The Bush administration further states that such a hurdle is a hindrance to families becoming part of the ‘middle class.’ The tax rate faced by the working poor has been reduced but the basic

<sup>17</sup> Marginal tax rate is that tax rate that an individual experienced on the last dollar earned. Due to various factors, the marginal rate is often different the statutory tax rate.

<sup>18</sup> The Earned Income Tax Credit is a credit against taxes due that were intended to reduce the tax burden on the low-income taxpayer.

<sup>19</sup> <http://www.bushtaxrelief.com/about.asp>, June 7, 2001

<sup>20</sup> <http://www.bushtaxrelief.com/about.asp>, June 7, 2001, PG 1.

problems of the earned income credit were not addressed in the current tax bill. This appears to be an area that awaits another tax bill.

There is also a small marriage penalty of approximately \$250 for married individuals that would have otherwise qualified for the EITC as individuals. This is particularly an area that should be addressed, as the individuals that qualify for the EITC are low-income taxpayers. The total marriage penalty related to individuals who qualify for the EITC is estimated to be \$3.1 billion for tax year 2000.<sup>21</sup>

## Charitable Giving

A goal of the Tax Relief Act is to address certain social concerns. One of these concerns was discussed in the previous section, namely to remove the incentive for couples to live together. A second area that the Administration felt needed to be addressed is the current decline in the amount of charitable giving.<sup>22</sup> To this end, the administration promoted that all individuals be able to deduct amounts given to charitable organizations. Under the current system, only taxpayers that are able to itemize their deductions on Schedule A of the Federal Form 1040 are able to deduct charitable giving for the year. By requiring individuals to itemize, effectively only taxpayers that own a home with a large mortgage are able to reduce their tax liability by contributing to charitable entities.<sup>23</sup>

The Administration may be ineffective in increasing charitable giving, however. Representative Dick Armev stated, "Generosity is rooted in our national character, not a tax deduction granted by politicians in Washington."<sup>24</sup> Additionally, Representative Armev pointed out research conducted during the 1980's that indicated giving was not tied to tax deductibility.

## Marriage Penalty and Tax Rates

In the Bible, the notion of family is a strong image. The optimal family structure is a family that has married parents, a male and a female.<sup>25</sup> Another factor in the current tax system that appears contrary to a Biblically based tax system is the oft-mentioned marriage penalty. This marriage penalty was an inadvertent consequence to a tax system that has not kept up with changes in the social-economic condition of the nation. When the tax system was began in 1913<sup>26</sup> there was only 1 status, that of a taxpayer. Each individual wage earner was taxed using a progressive tax rate that varied from 1% to 6%. Additionally, the first \$20,000 was not taxed at all. The primary focus of the federal income tax was to pay for the war effort. Under this tax system, less than 5% of United States citizens paid federal income taxes.

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<sup>21</sup> Holtzblatt, Janet, and Rebelein, Robert; *Measuring the Effect of the EITC on Marriage Penalties and Bonuses*, PG 1107.

<sup>22</sup> George W. Bush for President Official Site: Issues, <http://www.georgewbush.com/taxes.html>, May 21, 2001

<sup>23</sup> As in most generalizations, there are exceptions, such as those taxpayers with large medical deductions and or other special factors that are not common to most taxpayers.

<sup>24</sup> Armev, Dick; *Response to Tax Critics*; January 29, 1996.

<sup>25</sup> Genesis 2:24, Matthew 19:5, Mark 10:7, Ephesians 5:31.

<sup>26</sup> Enabled by the passage of the 16<sup>th</sup> Amendment to the United States Constitution.

However, a problem arose in states that were community property states. In those states, the state laws provided that all assets of the married couple were shared equally together. If one individual earned \$40,000, it was considered under state law that each of the married individuals earned \$20,000. As such, there was unequal treatment of the same income from state to state, depending on whether the state was a community property state or not. To fix this perceived inequity, the married filing joint status was added. The prevalent social-economic status at that point was that there was only one primary wage earner in the family. Under that condition, the married filing joint status provided savings over the previous tax system for the married couples in non-community property states, and a tax cost for those couples in community property states. However, under either scenario the married wage earner was taxed less for the same income level than if that wage earner had been single.

The marriage penalty was a phenomenon of having two wage earners in the same family. When both of the spouses are working professionals, the tax paid on their combined wages is higher than if they simply had decided to co-habitat without being married. By co-habiting, individuals can also receive a second hidden benefit. The second benefit is that itemized deductions can be manipulated to maximize the tax situation for the unmarried couple. Married individuals do not have the ability to manipulate itemized deductions to the same degree. Such a situation was not considered a common occurrence at a time when one spouse was the “bread winner” and the other cared for the home and family.

Reducing the statutory tax rates was used to reduce the overall tax burden on individuals. The changes in the current rates are shown in Table 3. Table 3 details the phase-in of the change in existing rates. Whereas the reduction in rates does provide for tax relief, the tax relief is phased in over a period of five years. Starting in 2007, the new tax rates will be fully phased in. Table 4 shows the anticipated final rates in tax year 2007, assuming no further congressional action.

<b>Rate Reduction Schedule<sup>27</sup></b>					
<b>Table 3</b>					
<b>Original Rates &gt;</b>	<b>15% Rate</b>	<b>28% Rate</b>	<b>31% Rate</b>	<b>36% Rate</b>	<b>39.6% Rate</b>
<b>Calendar Year</b>					
<b>2001<sup>28</sup></b>	Refund Credit	27%	30%	35%	38.6%
<b>2002-2003</b>	Partial 10%	27%	30%	35%	38.6%
<b>2004-2005</b>	No Change	26%	29%	34%	37.6%
<b>2006 And Later</b>	No Change	25%	28%	33%	35%

<sup>27</sup> CCH Tax Briefing: Tax Relief Reconciliation Act of 2001 – Special Report, pg 2, ©2001, CCH Incorporated

<sup>28</sup> Effective July 1, 2001.

**Projected 2007 Tax Rate Table  
Table 4**

<b>Single Income</b>	<b>Tax Rate</b>	<b>Married Income</b>	<b>Tax Rate</b>
<b>\$0 to \$6,150</b>	10%	\$0 to \$12,300	10%
<b>\$6,150 to \$31,700</b>	15%	\$12,300 to \$57,130	15%
<b>\$31,700 to \$76,800</b>	25%	\$57,130 to \$128,000	25%
<b>\$76,800 to \$160,250</b>	28%	\$128,000 to \$195,050	28%
<b>\$160,250 to \$348,350</b>	33%	\$195,050 to \$348,350	33%
<b>\$348,350 and over</b>	35%	\$348,350 and over	35%

This reduction in statutory rates will reduce the tax burden on taxpayers and is anticipated to stimulate the economy by allowing individuals to keep more of their income from each paycheck. The thinking is that taxpayers will then spend this additional income and provide a boost to the economy.

The reduction of tax rates will be phased in over the following six (6) years. As such, the economy will continue to receive a stimulus during the following six (6) years. The effect of the marriage penalty will be somewhat mitigated after the implementation of the Projected 2007 Tax Rates as shown in Table 4.

As is demonstrated by the taxes due calculations shown in Table 5, the marriage penalty will be reduced, but not eliminated for many married couples. The maximum penalty due to tax rates is \$14, 635, which is obviously a large amount. Even at the more normal level of each individual earning \$31,710, the family, as a result of tax rates only, will be penalized \$627 per year for being married.

**Effect of the 2007 Projected Tax Rates on the Portion of the Marriage Penalty Due to Tax Rates  
Table 5**

<b>Table Income Level Per Person</b>	<b>Individual Tax Due</b>		<b>Married, Filing Joint Tax Due</b>		<b>Marriage Savings / (Marriage Penalty)</b>		
<b>Person</b>	<b>1 Person Working</b>	<b>2 Persons Working</b>	<b>1 Person Working</b>	<b>2 Persons Working</b>	<b>1 Person Working</b>	<b>2 Person Working</b>	<b>Person</b>
<b>\$6,150</b>	\$615	\$1,230	\$1,230	\$1,230	\$ 0	\$ 0	
<b>\$31,710</b>	\$4,448	\$8,895	\$8,895	\$9,522	\$ 308	(\$ 627)	
<b>\$76,800</b>	\$15,723	\$31,445	\$31,445	\$32,840	\$ 2,851	(\$ 1,395)	
<b>\$160,250</b>	\$39,089	\$78,177	\$78,177	\$85,845	\$ 4,387	(\$ 7,668)	
<b>\$348,350</b>	\$101,162	\$202,323	\$202,323	\$216,958	\$ 6,127	(\$14,635)	
<b>\$400,000</b>	\$119,239	\$238,478	\$238,478	\$253,113	\$ 6,127	(\$14,635)	

A second cause of the tax penalty is the standard deduction. The standard deduction for 2000 was \$7,350 for married, filing joint taxpayers and \$4,400 for single taxpayers. Table 6 shows the change in standard deductions for married, filing joint taxpayers as a percentage of the

standard deductions for single taxpayers. By the year 2009 the standard deduction will no longer be a factor in the creation a marriage penalty.

***Standard Deduction Increases***

***Table 6***

<b><i>Calendar Year</i></b>	<b><i>Joint Return Standard Deduction As a Percentage of Single Return Standard Deductions.</i></b>
<b><i>2000</i></b>	167 %
<b><i>2005</i></b>	174 %
<b><i>2006</i></b>	184 %
<b><i>2007</i></b>	187 %
<b><i>2008</i></b>	190 %
<b><i>2009 and thereafter</i></b>	200 %

The reduction in the tax rates was made retroactive to the beginning of the 2001 tax year. During this summer, taxpayers should be expecting to receive tax refund checks for the amount of income taxes estimated due based on the prior years reported income and tax status as reported on the 2000 Tax Year Federal Income Return. This is anticipated to provide a one-time charge to the economy. The assumption made by many is that individuals will immediately spend the check, as such recharging the economy. If taxpayers choose not to spend their tax refund checks, then a much-needed boost in the economy will not happen. Factors that will affect whether the refund checks will be spent or saved include the expectations of how the economy will perform, their own personal economic outlook, the level of job security, etc.

**Federal Estate, Gift and Generation-Skipping Taxes**

Next, the Bush Administration was concerned about the ‘Death Tax’s’ effect on family business. The Administration’s position is that family businesses, which often include traditional retail stores and farms, are frequently asset rich and cash poor. Due to this, the business is liquidated to provide the funds necessary to pay the estate taxes when the owner of the business passes away. The removal of the federal estate tax will allow for family businesses to be passed from generation to generation intact. As such, the federal estate tax will expire for the tax year 2010. However, as the Tax Relief Act expires on December 31, 2010, the expiration of the federal estate tax may be a one-year event. The legislation will phase in repeal of the estate tax by the increase of the estate tax exemption. The current level of the federal estate tax exemption is \$675,000. This will increase to \$1 million in 2002, and to \$3.5 million in 2009. As the exemption is increased, the federal estate tax rate will decrease from the current 55% maximum rate to 45% in 2009. Also to be removed is the Gift tax. The gift tax annual exclusion of \$10,000 per year per person will remain unchanged through 2009. However, the total lifetime exclusion will increase to \$1 million in 2002 and stay at that level perpetually. For tax year 2010, the gift tax rate has been reduced to 35%. Table 7 shows the changes in detail for the Estate and Gift taxes, as well as the Generation-Skipping Tax.

***Tax Rates And Exemption Amounts For The Federal Estate, Gift, and Generation-Skipping Taxes***  
***Table 7***

<b><i>Calendar Year</i></b>	<b>Estate Tax Exemption</b>	<b>Generation-Skipping Tax Exemption</b>	<b>Gift Tax Exemption</b>	<b>Highest Estate, Generation-Skipping And Gift Tax Rates</b>
<b><i>2001 (Under Existing Law)</i></b>	\$ 675,000	\$1,060,000 <sup>29</sup>	\$ 675,000	55 %
<b><i>2002</i></b>	\$1,000,000	\$1,060,000	\$1,000,000	50 %
<b><i>2003</i></b>	\$1,000,000	\$1,060,000	\$1,000,000	49 %
<b><i>2004</i></b>	\$1,500,000	\$1,500,000	\$1,000,000	48 %
<b><i>2005</i></b>	\$1,500,000	\$1,500,000	\$1,000,000	47 %
<b><i>2006</i></b>	\$2,000,000	\$2,000,000	\$1,000,000	46 %
<b><i>2007</i></b>	\$2,000,000	\$2,000,000	\$1,000,000	45 %
<b><i>2008</i></b>	\$2,000,000	\$2,000,000	\$1,000,000	45 %
<b><i>2009</i></b>	\$3,500,000	\$3,500,000	\$1,000,000	45 %
<b><i>2010</i></b>	N/A – Tax is Repealed	N/A – Tax is Repealed	\$1,000,000	35% (Gift Tax Only) 0.0% (Estate & Generation-Skipping Taxes)
<b><i>2011 and Thereafter</i></b> <sup>30</sup>	\$1,000,000	\$1,000,000	\$1,000,000	55 %

### **Family Tax Deferred Savings – Education IRA’s<sup>31</sup>**

The Tax Relief Act also addresses the area of education. Meeting the expenses of a child’s college education is a concern for many American families. Education Savings Accounts (ESA) allowed families to set aside up to \$500 per year for a child to provide for college expenses.

The Tax Relief Act modified the ESA, or Educational IRA, in a number of ways. First, the annual contribution limit was increased from \$500 to 2,000 beginning in 2002. Also, the income phase out range, the point where individuals are no longer allowed the deduction for an ESA was increased to \$220,000 from \$190,000 starting in tax year 2002. Next, withdrawals can be made tax-free for K-12 expenses related to a child’s education. These expenses can include the purchase of home computers, computer peripherals, and computer technology, as

<sup>29</sup> The Generation-Skipping Tax exemption in 2001, 2002, 2003, and 2011 is #1million, as indexed for inflation since 1997. The amount is \$1,060,000 in 2001 and may change for the years 2002, 2003, and 2011.

<sup>30</sup> Assuming no additional tax acts passed to extend the elimination of the Federal Estate, Generation-Skipping Tax, and Gift Tax. The long-term future of the elimination is at best, uncertain.

<sup>31</sup> IRA – Individual Retirement Accounts

well as Internet access and related services beginning in 2002. Currently, withdrawals are only allowed for college expenses.

Additionally, corporations and other entities can make contributions to ESA's for individuals beginning in 2002. Previously, contributions to ESA's were limited to individuals. All contributions can be made until April 15<sup>th</sup> beginning with 2002. Finally, withdrawals will be allowed effective in 2002 for actual living expenses tax-free. Previously, only direct college expenses could be paid by ESAs. Currently, if an individual makes contribution to both an ESA and a qualified tuition plan for the same beneficiary, then that individual must pay an excise tax. This excise tax was repealed beginning in 2002.

If the beneficiary is a special needs beneficiary of an ESA then the restriction of contributions for beneficiary over the age of 18 was removed. Additionally, a deemed distribution at the age of 30 is not required. Both provisions are effective in 2002.

The HOPE and Lifetime Learning credits are another mechanism that is at the disposal of families and individuals to assist in paying for higher education expenses. The credits are a mechanism to reduce their tax bills by allowing a tax credit for expenses paid towards tuition and direct supplies. Beginning in 2002, the credit will be available for other expenses other than tuition and direct supplies.

Many states have passed Qualified Tuition plans, which allow the cost of a college education at state schools to be prepaid. These plans allow the cost of college to be paid in advance and often include a provision to protect the beneficiary from future tuition increases. The use of such plans were encourage via the passage of many favorable provisions in the Tax Relief Act. The provisions are effective in the year 2002.

1. The allowance of tax-free distributions from qualified state tuition plans.
2. The allowance of private prepaid tuition plans (as long as a distribution is not made prior to 2004).
3. The allowance of the use of Qualified Plans for the payment of actual college related living expenses.
4. Tax-free rollovers will be allowed as long as the beneficiary does not change.
5. Cousins will now be included in the definition of family members for the funding of Qualified Plans.
6. The HOPE and Lifetime Learning credits can be used to fund Qualified Plans.
7. If the beneficiary is a special needs individual, then the Qualified Plan can be used to cover enrollment and other costs.
8. Should an individual withdrawal from a Qualified Plan for non-allowed purposes, and then an additional 10 percent tax shall be imposed on certain distributions.

In the past, employer-provided education assistance had been periodically excluded from the recipient's income, or included in the recipient's income. The exclusion of employer-provided education assistance has been made into a permanent exclusion for both undergraduate and graduate education effective in 2002. This represents both an expansion (to include graduate education) and the providing of a sense of security, as the exclusion in the past was a non-permanent provision.

Finally, individuals will be allowed to deduct payments for interest made on student loans beyond the previously limit of 60-months. Additionally, the phase out point has been increased to \$130,000 for married couples and \$65,000 for single taxpayers, indexed for inflation. Additional, an “above-the-line” deduction for certain costs of higher education will be allowed for taxpayers. The limits are \$3,000 in 2002 and 2003 and \$4,000 in 2004 and 2005) for taxpayers with AGI below \$130,000 (\$65,000 for singles).

### Family Tax Deferred Savings – Regular IRA’s & 401(k)’s

An important consideration for all families is planning for the future and retirement. Congress had previously passed provisions allowing for IRA’s and 401(k)’s. These retirement accounts allow for the tax-free growth of funds to provide for the future. However, the accounts do not come without significant limitations and restrictions. The Tax Relief Act lightened these restrictions up significantly, allowing for increased coverage and portability, as well as reducing regulatory burdens. The changes in annual contributions limits are shown in Table 8. There were many other administrative changes, but these will not be discussed in this paper.

<i>Annual Contribution Limit<sup>32</sup></i>			
<i>Table 8</i>			
<i>Year</i>	IRAs/Roth IRAs	401(k)/403(b)/457 plans <sup>33</sup>	SIMPLE plans <sup>34</sup>
<b>2001</b>	\$2,000	--	--
<b>2002</b>	\$3,000	\$11,000	\$ 7,000
<b>2003</b>	\$3,000	12,000	8,000
<b>2004</b>	\$3,000	13,000	9,000
<b>2005</b>	\$4,000	14,000	10,000
<b>2006</b>	\$4,000	15,000	(Indexed)
<b>2007</b>	\$4,000	(Indexed)	
<b>2008</b>	\$5,000		
<b>2009</b>	(Indexed)		

Should individuals be concerned with the ability to save? The current personal savings rate, according to the Whitehouse Economic Statistics Briefing Room, is 1.1% of personable disposable income for the 1<sup>st</sup> quarter of 2001. This is an alarmingly low number. As can be seen in Table 9, the personal saving rate has been on a decline. As such, any action by the Federal government to encourage personal savings would be positive.

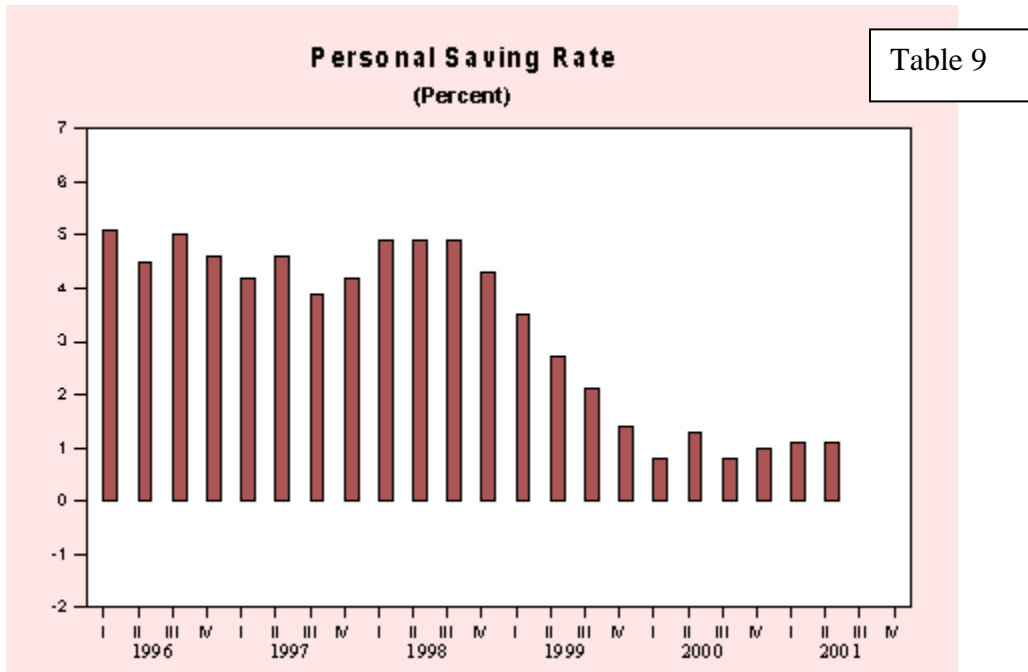
An immediate question could be why is the savings rate declining and what is the significance of the decline. The decline, if it continues for a period of time, may result in a lowering of available capital for borrowing. Families may also be unable to whether the temporary joblessness of one or both of the wage earners in the family. Finally, a low savings rate may

<sup>32</sup> Arthur Anderson, *Newsletter*, Page 9.

<sup>33</sup> An additional \$5,000 “catch-up” pre-tax contributions is allowed for 401(k), 403(b) and 457 plans by individuals age 50 and older, phased in over five years beginning in 2002, and indexed for inflation.

<sup>34</sup> An additional \$2,500 for SIMPLE plans by individual’s age 50 and older, phased in over five years beginning in 2002, and indexed for inflation.

indicate a potential dependence on the social catch net for help in rough periods. The full significance of the low savings rate on our society is a subject for another research project.



## V. Summary

There were additional provisions dealing with business that this paper will not address. The focus of this paper is on the direct effects on the family of the Tax Relief Act. As such, many of the provisions dealing with the AMT and the Business taxes will not be discussed in this paper. However, as can be seen by what was discussed, the Tax Relief Act is a massive tax bill. Many of the issues raised by the inequities of the tax code were not addressed, or were not fully resolved. The marriage penalty effect has been removed for low income, but still exists for high-income families. The tax burden on low-income taxpayers was reduced, but the earned income tax credit was not directly addressed.

A major concern of the Tax Relief Act is that the reductions in the tax rates are to be phased in over a period of 5 years. Therefore, taxpayers will not receive the full benefit of the tax rate decreases until 2007. Additionally, the provisions that address educational savings accounts and IRA's do not take effect until 2002. Many taxpayers will need to wait to receive the promised tax benefits.

Since many of the provisions of the Tax Relief Act do not take effect until the future, taxpayers are at the whim of Congress as to whether they will ever be able to benefit fully from the reduction of the various tax rate reductions and the changes to the educational savings accounts, IRA's and the Federal estate, gift, and generation-skipping tax provisions.

The last major issue is that the Tax Relief Act has a sunset provision. The date for the expiration of the provisions of the Tax Relief Act is December 31, 2010. As such, without

future actions by Congress, the benefits will expire and the tax rates and much of the tax code will return to what it was prior to the passage of the Tax Relief Act.

Potential future trouble spots are the Alternative Minimum Tax (AMT) and the implications of the changes to the Federal Estate, Gift and Generation-Skipping Tax provisions (Transfer Taxes). First, many of the tax credit that have been available to reduce potential AMT liabilities will be lost beginning in 2004. Additionally, the lower Federal Income Tax rates will cause more taxpayers to pay AMT. As such, unless Congress intervenes, AMT may become an unexpected and unwelcome surprise to many taxpayers. Many taxpayers may actually see an increase in their overall tax bill.

With the sunset provisions, AMT on the horizon, and the likelihood of Congressional action if the economy does not recover as quickly as expected makes one ask the question of whether the benefits of the Tax Relief Act are real or only illusionary? This uncertainty can only create a state of concern among the tax paying public. The perception that Administration is family friendly may be brought into question.

To its credit, the Administration has stated, “The best way to help all families is to let each family keep more of its income – and spend it as it deems appropriate.”<sup>35</sup> As such, we are in a unique situation to further the strengthening of the traditional family structure with the current president. We, as a nation, and as fellow believers, should not miss this chance to present to government our views on the future direction of the country and this administration. We need to step forward with a unified agenda that is based on the Bible and has been thoroughly prayed upon for direction and guidance from our Creator.

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<sup>35</sup> George W. Bush for President Official Site: Issues, <http://www.georgewbush.com/taxes.html>, May 21, 2001.

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