Chapter 14: Taxes and Government Spending
Section 1

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ECONOMICS

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Objectives

1. **Identify** the sources of the government's authority to tax.

2. **Describe** types of tax bases and tax structures.

3. **List** the characteristics of a good tax.

4. **Identify** who bears the burden of a tax.

Key Terms

- **tax:** a required payment to a local, state, or national government

- **revenue**: the income received by a government from taxes and other nontax sources

- **progressive tax**: a tax for which the percentage of income paid in taxes increases as income increases

- **proportional tax**: a tax for which the percentage of income paid in taxes remains the same at all income levels

- **regressive tax**: a tax for which the percentage of income paid in taxes decreases as income increases

Key Terms, cont.

- **tax base**: the income, property, good, or service that is subject to a tax

- **individual income tax**: a tax based on a person's earnings

- **corporate income tax**: a tax based on a company's profits

- **property tax**: a tax based on real estate and other property

- **sales tax**: a tax based on goods or services that are sold

- **incidence of tax**: the final burden of a tax

- ## What are the features of a tax system?
  - Fairness
  - Simplicity
  - Efficiency
  - Certainty
  - Balance between tax revenue and tax rates

Government's Authority to Tax

- We authorize the federal government, through the Constitution and our elected representatives in Congress, to raise money in the form of taxes.

  – Taxation is the primary way that the government collects money. Taxes give the government the money it needs to operate.

  – The first power granted to Congress is the power to tax, which is the basis of all federal laws.

Limits on the Government

- There are also limits on the government's power to tax.

  - The purpose of a tax must be "for the common defense and general welfare." A tax cannot bring in money that goes to individual interests.

  - Federal taxes must be the same in every state.

  - The government cannot tax exports, only imports.

Progressive Taxes

- Economists describe taxes based on their structure and according to the tax base.

- A progressive tax is a tax for which the percentage of income paid in taxes increases as income increases.
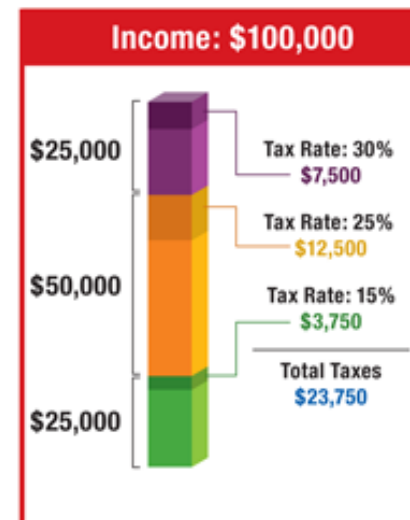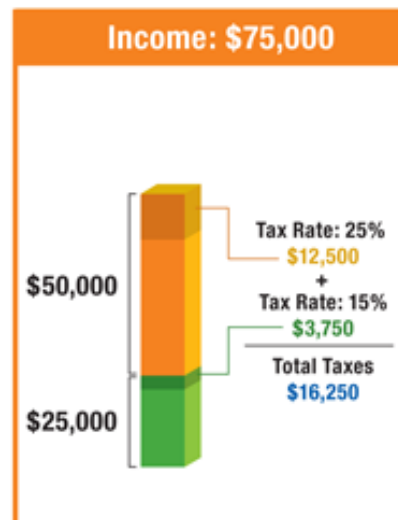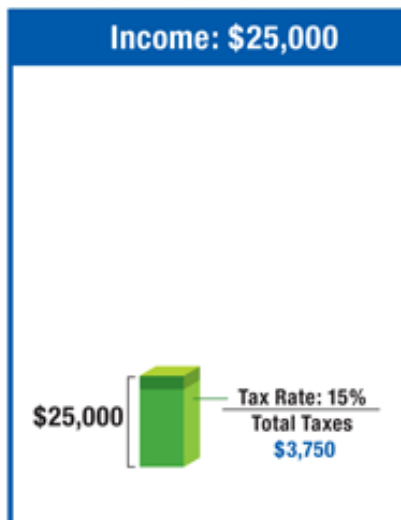
Other Taxes

- A proportional tax is a tax for which the percentage of income paid in taxes remains the same at all income levels.

- A regressive tax is a tax for which the percentage of income paid in taxes decreases as income increases.

  – A sales tax is regressive because higher income households spend a lower proportion of their incomes on taxable goods and services.

  – Checkpoint: Is the federal income tax proportional, progressive, or regressive?
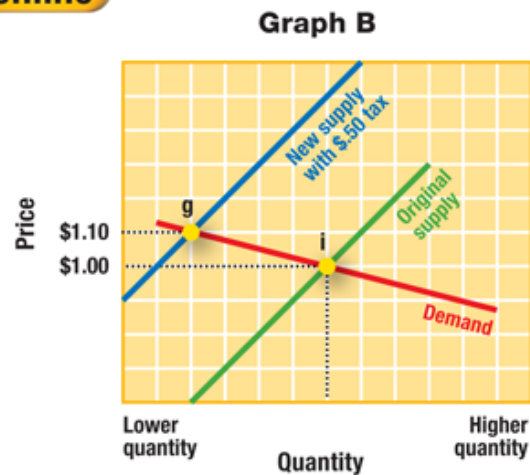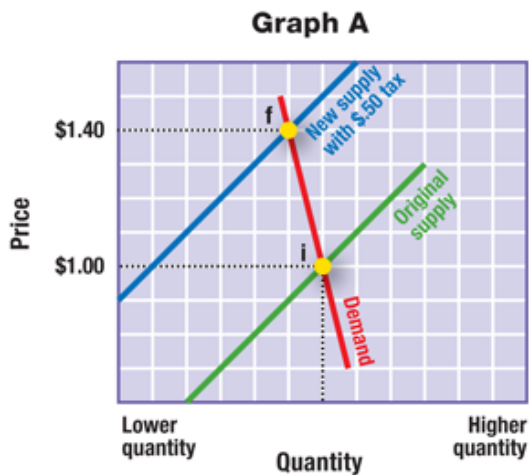
Tax Bases

- ## Different taxes have different tax bases.
    - The individuals income tax is based on a person's earnings.
    - The corporate income tax is based on a company's profits.
    - The property tax is based on real estate and other property.
    - The sales tax is based on goods and services that are sold.

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Elasticities of Demand and Tax Effects

- Taxes affect more than just the people who pay them.
- Producers often pass on a portion of tax to consumers.
  - Generally, the more inelastic the demand, the more easily the seller can shift the tax to consumers.
  - Under what conditions, elastic or inelastic demand, would price of a good increase from $1.00 to $1.10?

Tax Rates in Different Countries

Percent of Earnings Paid in Income and Social Security Taxes

Country	Rate
Mexico	5%
Korea	10.6%
Ireland	14.8%
Japan	19.5%
United States	23.4%
Canada	24.2%
United Kingdom	26.8%
Sweden	31.1%
Denmark	40.9%
Germany	42.7%

Taxes paid by single taxpayers with no children

Characteristics of a Good Tax

- Checkpoint: What are the four characteristics of a good tax?
  - **Simplicity**—tax law should be easy to understand
  - **Efficiency**—the tax should be able to be collected without spending too much time or money
  - **Certainty**—it should be clear when the tax is due, how much is due, and how to pay the tax
  - **Equity**—the tax system should ensure that no one bears too much or too little of the tax

Determining Fairness

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- Economists have proposed two different ideas about how to measure the fairness of a tax.

  - The benefits-received principle holds that a person should pay taxes based on the level of benefits he or she expects to receive from the government.

  - The gasoline tax is an example of the benefits-received principle.

Determining Fairness, cont.

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- The ability-to-pay principle holds that people should pay taxes according to their ability to pay.

- Good taxes generate enough, but not too much, revenue. Citizens needs are met, but not to such an extensive degree that the tax discourages production.

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Review

- Now that you have learned about the features of a tax system, go back and answer the Chapter Essential Question.

  - How can taxation meet the needs of government and the people?