

Worksheet Solutions

Tax Revenue and Decision Making

Theme 4: What Is Taxed and Why
Lesson 1: Federal/State/Local Taxes

Key Terms

income taxes—Taxes on income, both earned (salaries, wages, tips, commissions) and unearned (interest, dividends). Income taxes can be levied on both individuals (personal income taxes) and businesses (business and corporate income taxes).

property taxes—Taxes on property, especially real estate, but also can be on boats, automobiles (often paid along with license fees), recreational vehicles, and business inventories.

transaction taxes—Taxes on economic transactions, such as the sale of goods and services. These can be based on a set of percentages of the sales value (ad valorem—sales taxes), or they can be a set amount on physical quantities (“per unit”—gasoline taxes).

Summary

Most federal revenue comes from income taxes. State and local revenue comes from **transaction taxes, income taxes, and property taxes**. The type and amount of tax varies from state to state and between local communities. States have the power to make, collect, and spend their own taxes.

Sales taxes are the most common kind of transaction taxes. Taxes withheld from a paycheck include income taxes. Homeowners pay property tax, but renters may contribute to their landlord’s property tax with each rental payment.

Activity 1

Imagine that you are a member of the city council in Springville. This year Springville received a \$60,000 grant from the federal government to help support certain public services. Congress has recently voted to reduce this funding to \$45,000 next year. Your job is to decide how to manage the reduced funding for five Springville services.

The table below shows the amount Springville received this year and how the Springville City Council divided the grant among five public services. The table also shows the total amount the government will provide next year. How would you divide the new grant to fund the five services? Complete the chart to show how much you would give each service. Calculate the difference between the old amounts and the new ones. Be sure to use the entire \$45,000 grant, but do not exceed that amount.

| HOW SPRINGVILLE SPENDS ITS MONEY | | | |
|---|-------------------------|-------------------------|--------------------|
| Service | Amount This Year | Amount Next Year | Difference |
| Emergency youth shelter | \$12,000 | Answers will vary. | Answers will vary. |
| Wastewater treatment | \$13,000 | Answers will vary. | Answers will vary |
| Occupational development center | \$15,000 | Answers will vary. | Answers will vary |
| Bus system | \$10,000 | Answers will vary. | Answers will vary |
| Mental health service | \$10,000 | Answers will vary. | Answers will vary |
| GRANT AMOUNT | \$60,000 | \$45,000 | \$15,000 |

Activity 2

To avoid cutting services, City Council members have proposed various ways to raise additional revenue. Some have proposed increasing property taxes. Others want to increase the local sales tax from 1 percent to 2 percent. Another proposal is to charge individual income taxes at a flat rate of 2 percent.

1. If a consumer spends \$4,000 per year on taxable items, how much additional sales tax would he or she pay per year under the proposed plan? **\$40**
2. How many of these consumers would it take to make up the difference between the old federal grant and the new one? **375**
3. If a couple's taxable earnings are \$35,000 per year, how much local income tax would the couple pay under the proposed plan? **\$700**
4. About how many such taxpayers would it take to make up the difference between the old federal grant and the new one? **between 21 and 22**

Activity 3

Propose a solution for Springville's problem. You can cut services and/or increase local taxes. If you increase taxes, tell what type of tax it will be and who will pay it. Tell what you will do with excess money you collect beyond that needed to restore services to their existing levels. Explain who will benefit the most from your plan. Tell who will be affected negatively by your plan. Write your solution on a separate sheet of paper.

Answers will vary, but the figures should add up correctly for whatever plan the students adopt. Students' responses should also indicate an understanding that there are costs and benefits associated with the plan they propose.