Key Terms

- **flat tax** — Another term for a proportional tax.
- **proportional tax** — A tax that takes the same percentage of income from all income groups.
- **regressive tax** — A tax that takes a larger percentage of income from low-income groups than from high-income groups.
- **sales tax** — A tax on retail products based on a set percentage of retail cost.

Summary

With a proportional or flat tax, each individual or household pays the same fixed rate. For example, low-income taxpayers would pay 10 percent, middle-income taxpayers would pay 10 percent, and high-income taxpayers would pay 10 percent. The sales tax is an example of a proportional tax because all consumers, regardless of income, pay the same fixed rate. Although individuals are taxed at the same rate, flat taxes can be considered regressive because a larger portion of income is taken from those with lower incomes. For example, a 6% sales tax on a $1000 computer ($60) would take a greater portion of a $10,000 income than of a $50,000 income.

Activity 1

Complete the proportional tax chart below. To find the amount of tax, use this formula:

\[
\text{Income} \times \text{percentage of income paid in tax} = \text{amount of tax.}
\]

Example: $15,000 \times .10 (10\%) = $1,500.

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<thead>
<tr>
<th>PROPORTIONAL TAX</th>
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<tbody>
<tr>
<td>Income</td>
<td>Percentage of Income Paid in Tax</td>
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<tr>
<td>$5,000</td>
<td>10%</td>
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<td>$10,000</td>
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<td>$25,000</td>
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Activity 2

The Armey-Shelby flat tax proposal is also based on a 17 percent rate. The Armey-Shelby tax, however, applies that rate only on income over $35,400 for a family of four. In other words, if the family made $50,000, they would be taxed on $14,600 ($50,000–$35,400).

1. How is the attempt to exempt a certain amount from the tax a way to make the tax less regressive?

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2. Using the Armey-Shelby tax exemption of $35,400, how much tax would a family of four earning $25,000 pay in taxes?

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Activity 3

The Greens and the Smiths live in a state that has a proportional sales tax. Read the following details about each family. Then, on a separate sheet of paper, write a short essay explaining the regressive effect of this proportional sales tax on each family.

The Greens, a family of four, earn $20,000 a year and spend 70 percent of their income on taxable consumer goods. The Smiths, also a family of four, earn $200,000 a year, enough to allow them to invest or save 30 percent of their income. They spend only 40 percent of their income on taxable consumer goods.