Worksheet Solutions

Tax and Gourmet Chocolates

Theme 4: What Is Taxed and Why
Lesson 4: Direct and Indirect Taxes

Key Terms

direct tax—A tax that cannot be shifted to others, such as the federal income tax.
indirect tax—A tax that can be shifted to others such as business property taxes.
tax shift—The process that occurs when a tax that has been levied on one person or group is in fact paid by others.

Summary

Manufacturers like to produce and sell as much as possible without producing more than they can sell. When production equals what can be sold, supply and demand is balanced.

This balance depends on many factors, especially price. Raising prices may lower the quantity demanded. Lowering prices might have the reverse effect.

Manufacturers often raise prices to pay for a rise in expenses. Taxes—including sales, property, payroll, and income—can cause price increases. A **direct tax** is one that is paid directly to the government. An **indirect tax** may be shifted to others. A **tax shift** occurs when a business shifts its taxes to others.

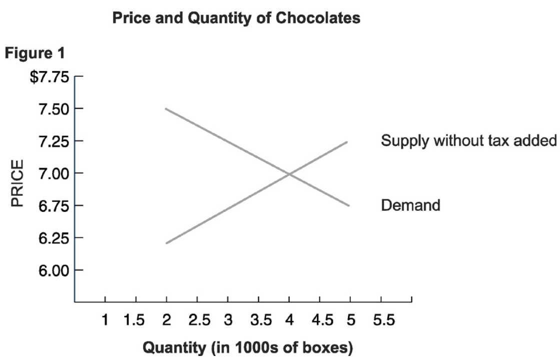
Activity 1

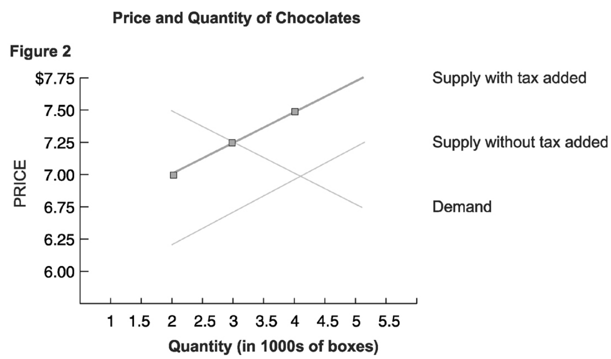
A chocolate manufacturer wants to shift part of the company's tax increases onto the price of their chocolate candies. Read each item below. Write a check mark next to the taxes that the company could pass on to customers.

	An increase in personal income tax rates for employees
√	An increase in property tax on the manufacturing plant
√	An increase in customs duties for imported chocolate
	An increase in property tax on the president's home
√	An increase in sales tax

Activity 2

Study the graphs below to understand what happened when a chocolate manufacturer shifted part of a tax increase onto the price of a box of chocolates. Figure 1 shows how the demand falls as the price rises. Intersecting lines show when supply and demand is balanced. Figure 2 shows what happens when a tax causes a producer to raise prices. Answer the questions below in the spaces provided.





1. When was supply and demand balanced before the tax? **4,000 boxes**
2. When was balance achieved after the tax? **3,000 boxes**

Activity 3

Answer the question below in the space provided.

- How did the tax affect sales of the candies? What effect might this have on government revenue in the long run?

  Suggested Answer: Sales of the candies dropped. Ultimately this could result in a loss of government revenue, because fewer sales could mean that the business would pay less in overall taxes.