5.1 Flat Tax & Political Philosophy

- Calculate a flat income tax.
- Identify types of taxes.
- Analyze an indirect tax.

Study Tip

Income tax is paid on taxable income, which is gross income minus deductions, where "deductions" depend on the taxing authority.

Calculating a Flat Income Tax

A **flat tax** (short for **flat rate tax**) is a tax system with a constant tax rate. In the United States, the federal income tax is not a flat tax. People with higher incomes not only pay more income tax, they pay a higher tax rate (see Section 5.2). As of the writing of this text, seven states have a flat income tax.

- Colorado 4.63%
- Indiana 3.40%
- Michigan 4.35%
- Utah 5.00%
- Illinois 5.00%
- Massachusetts 5.30%
- Pennsylvania 3.07%

Additionally, there are seven states with no income tax: Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming.

EXAMPLE 1 Calculating a Flat Income Tax

Two people who live in Utah have the following taxable incomes.

Utah State Tax Commission
Utah Individual Income Tax Return **2010 TC-40**
All State Income Tax Dollars Fund Education
incometax.utah.gov

a. \$20,000 **b.** \$2,000,000

How much state income tax does each person owe?

SOLUTION

Each person owes 5% of his or her taxable income.

Note that a flat tax means that everyone pays the same rate, *not* the same amount.

a.

9. **Utah taxable income** (subtract total of lines 7 and 8 from line 6) ··· • 9 20,000 .00
10. **Utah tax calculation -** multiply line 9 by 5% (.05) ··········· • 10 1,000 .00

b.

9. **Utah taxable income** (subtract total of lines 7 and 8 from line 6) ··· • 9 2,000,000 .00
10. **Utah tax calculation -** multiply line 9 by 5% (.05) ··········· • 10 100,000 .00

Taxable Income: \$20,000 Taxable Income: \$2,000,000

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Is the following logic valid? Explain your reasoning.

> Flat income taxes are not fair because the rich should have to pay more income taxes than the poor.

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