



How the federal tax system affects what you can buy.

How much do you have to earn to have \$100 to spend?

Critics of the FairTax claim that the FairTax will increase the cost of everything you buy by 30%; that you will have to pay \$130 for an item with a price tag of \$100.

Let's take a look at how the existing federal income/payroll tax system affects what you can spend. The chart below shows how much a person has to earn today in order to have \$100 take-home pay to spend, depending on whether they are an employee or self-employed, and what their tax bracket is. The figures below are based on marginal tax rates, which means that they tell you how much additional money you would have to earn to have an additional \$100 to spend.

Employment Status	Income Tax Bracket		
	15%	25%	28%
Employee			
Gross Earnings	\$129.28	\$148.48	\$155.40
Income Tax	-\$19.39	-\$37.12	-\$43.51
Payroll tax at 7.65%	-\$9.89	-\$11.36	-\$11.89
Available Spending	\$100.00	\$100.00	\$100.00
Price to earnings multiplier	1.29	1.49	1.55
Self-employed person			
Gross Earnings	\$143.47	\$167.50	\$176.37
Income Tax	-\$21.52	-\$41.88	-\$49.38
Payroll tax at 15.3%	-\$21.95	-\$25.63	-\$26.98
Available Spending	\$100.00	\$100.00	\$100.00
Price to earnings multiplier	1.43	1.68	1.76

As a taxpayer, under the FairTax system, you would have to earn \$130 to spend \$100. Under the income/payroll tax system, in the 15% bracket, that same taxpayer would have to earn \$129 if he/she were an employee, or \$143 if self-employed in order to have an additional \$100 to spend. The self-employed person has a higher figure because he/she pays both the employer and employee portions of payroll taxes.

For a family in the 25% tax bracket, the difference is much greater. The employee would have to earn an additional \$149 to have \$100 to spend; for the self-employed person it would be an additional \$168 to have \$100 to spend.

So if you want to save \$10,000 for a down payment on a house or for college tuition, you would have to earn an additional \$2,928 to \$7,637 to be able to make that \$10,000 down payment, depending on your tax bracket and employment status.

Under the FairTax, you would get to keep all the income you earn. If you spend it, you would pay the tax; if you put it into savings you pay no tax. You also pay no tax if you spend it on education tuition or donate to charity as these items are not taxable.

Written by Karen Walby, Ph.D., June 21, 2010.