## The Circular Flow of the Economy

Tax revenue flows from the private sector to the public sector. The government uses the money to pay for goods, services, and operations. The amount of money people earn and spend affects the taxes they pay, and thus, the amount of money the government collects and has available to spend. During good economic times, unless the government lowers tax rates, the government generally collects more taxes. During rough economic times, people generally earn less income and make fewer purchases. Revenue from income tax and sales tax may fall. When the government collects less money from taxes than it wants to spend, it must raise tax rates or borrow money to meet its expenses.

## Property Taxes

Property taxes are taxes on property, especially real estate, but also can be on boats, automobiles (often paid along with license fees), recreational vehicles, and business inventories. The more that individuals or businesses own, the higher the taxes they pay. During good economic times, some buy new or larger homes. Businesses may build or remodel facilities, thus making them more valuable properties. Then property tax revenues increase.

## Sales Taxes

Sales taxes are taxes on retail products and are based on a set percentage of retail cost. Some states also levy a tax on services, such as car or home repairs. Sales taxes usually are imposed on retail items, with the exception of some food and medicine purchases. During good economic times, people may purchase more household goods and clothes. People may eat out more often or spend more on entertainment. These purchases increase state and local collections from sales taxes.

## Excise Taxes

Excise taxes are taxes on the sale or use of specific products or transactions. Some excise taxes are "luxury" taxes on large expensive items, such as some luxury cars or boats. Others are "sin" taxes on items considered unhealthy, such as alcohol and tobacco products. The gasoline tax is an excise tax. The more consumers spend, the more the government collects.

## Income Taxes

Income taxes are 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). When an individual's income rises, he or she pays more income tax. The same is often the case with a business or corporation. As business profits go up, so do the corporate taxes that the business pays. When businesses are profitable, unemployment is low, and salaries are rising, income tax revenue generally rises.

## Payroll Taxes

Payroll taxes are paid by employers and employees to finance specific programs, such as Social Security and Medicare. Payroll taxes are based on earned income, so when income rises or the number of earners grows, so do the government collections from payroll taxes.