



Price Versus Cost

Suppose you buy a gallon of gas for \$3. How much did it cost you? You say, “Williams, that’s a silly question. It cost \$3.” That’s where you’re mistaken, because there’s a difference between price and cost. To prove that price and cost are not the same, consider the following. Suppose you live and work in New York City and routinely pay \$15 for a haircut. Imagine you were told that there’s a barber in Boise, Idaho, who can give you the identical haircut for just \$5. Would you start going to the Boise barber? I’m betting you’d answer no because even though the price is cheaper, the cost is greater.



We might think of price as the money that’s actually given in exchange for the transfer of ownership. When you purchased the gallon of gas, you simply transferred your ownership of \$3. What the gas cost you is a different matter. One way to determine the cost of a gallon of gas is to ask yourself what sacrifice you had to make in order to have \$3 to buy it. Say that your annual salary is \$75,000. Your total federal income tax, state income tax, local taxes and Social Security and Medicare taxes come to about 35 percent of your salary. That means that in order to purchase the \$3 gallon of gas required that you earned about \$4.60 in order to have \$3 after taxes. That means a gallon of gas costs you \$4.60 worth of sacrifice. But that’s not so costly as it is to a richer person — for example, someone earning a yearly salary of \$500,000. He has to earn more than \$5 before taxes in order to have \$3 after taxes to purchase gas.

If taxes only concealed hidden costs of what we buy, we’d be lucky, but taxes are destructive in another hidden way. Suppose I want to hire you to repair my computer. Having the work done is worth \$200 to me, and performing the work is worth \$200 to you. The transaction occurs because we have a meeting of the minds. Suppose Congress imposes a 30 percent income tax on you. That means that if you repaired my computer, you would receive not \$200, what it was worth to you to do the job, but instead \$140 after taxes. You might say the heck with repairing my computer; spending time with your family is worth more than \$140.

You might then offer that you’d do the job if I paid you \$283. That way, your after-tax earnings would be \$200 — what doing the job is worth to you. There’s a problem. The repair job was worth \$200 to me, not \$283. So it’s my turn to say the heck with it.

This simple example demonstrates that one effect of taxes is that of destroying transactions and hence jobs. But politicians have what economists call a zero-elasticity vision of the world. In other words, they’re fool enough to believe that people will behave after taxes are levied just as they behaved before and that the only effect of a tax is to bring in more revenue. Of course, a more flattering assessment is that politicians are not fools and know that their actions destroy transactions and hence jobs but they don’t give a damn and only care about revenue.



Written by [Walter E. Williams](#) on April 17, 2013

Here's a question: Would you and I, as well as our nation, be better off if you repaired my computer and I gave you \$200 in cash and we agreed not to report the transaction to the agents of Congress? I'd answer yes and no. Yes, because there'd be more transactions, more jobs and greater wealth. No, because we'd be criminals.

Taxes are necessary to fund the constitutionally mandated functions of the federal government. If Congress spent according to its authority under Article 1, Section 8 of our Constitution, taxes wouldn't be any more than 5 percent of the gross domestic product, as it was between 1787 and 1920, as opposed to today's 20 percent.

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