

Notes Day 3: Marginal Tax Computations

2012 Tax Rates & Tax Brackets

Tax Rate	Single	Married Filing Joint	Married Filing Separate	Head of Household
10%	Up to \$8,700	Up to \$17,400	Up to \$8,700	Up to \$12,400
15%	\$8,701 – \$35,350	\$17,401 – \$70,700	\$8,701 – \$35,350	\$12,401 – \$47,350
25%	\$35,351 – \$85,650	\$70,701 – \$142,700	\$35,351 – \$71,350	\$47,351 – \$122,300
28%	\$85,651 – \$178,650	\$142,701 – \$217,450	\$71,351 – \$108,725	\$122,301 – \$198,050
33%	\$178,651 – \$388,350	\$217,451 – \$388,350	\$108,726 – \$194,175	\$198,051 – \$388,350
35%	Over \$388,350	Over \$388,350	Over \$194,175	Over \$388,350

Calculating Taxes

Once you have located your tax bracket, you can calculate your initial tax liability. You do not apply your tax rate to all of your income. Instead, you apply the appropriate rate for income in each bracket. So let's say the married couple making \$100,000 wants to see what they might owe in 2012.

1. Calculate 10% of income up to \$17,400. The couple makes more than \$17,400, so calculated 10% of the full amount (\$1,740)
2. Calculate 15% of income between \$17,401 and \$70,700. Once again, the couple makes more than the maximum amount so calculates the entire potential tax. In this case, you have to subtract first: \$70,700-\$17,401 is \$53,299. Then apply the 15% rate to get roughly \$7,995.
3. Calculate 25% of income between and \$70,701 and \$142,700. In this case, the couple makes \$100,000 and does not need to calculate the potential tax on the full income covered by the 25% bracket. Instead, calculate \$100,000 – \$70,701 to get \$29,299. Then multiply by 25% to get \$7,325.
4. Finally, add up all of the results from steps 1 -3. \$1,740 + \$7,995 +\$7,325 = \$17,060.

The couple could owe the IRS as much as \$17,060 on their \$100,000 in income. Note that even though they are in the 25% tax bracket they do not owe 25% of their income – instead they owe a maximum of 17%.

However, with [deductions](#), [exemptions](#) and credits, their actual owed tax will likely end up being much less. To project your own tax liability (and potential refund), you can use our [tax calculator](#).

Using Tax Brackets to Your Advantage

You can use the tax bracket thresholds to do a little [tax planning](#). For instance, the couple above was making \$100,000. In order to pay less than 25% on every single dollar of income, they would have to reduce income by nearly \$30,000 – which is possible if they are taking full advantage of [maxing out their 401ks](#).

At the same time, they can make \$42,000 more and pay the same rate on their last dollar of income as they are paying now. Only once they hit \$142,702 in income will they start paying 28% on their last dollar of income. So if they think they might bump up against the higher bracket in 2013 but have the chance to shift rental, investment, [freelance](#) (1099) or other income into 2012, they should do so. If they were making \$141,000 in 2012 and thought they would make less in 2013 they might want to shift income out of 2012 to avoid paying the higher rate. If they made just over \$142,700 they might want to make some extra payments to incur deductions and thus remain in the lower bracket.

Examples:

Calculate the tax owed using the marginal tax rates for 2012.

1. Deirdre is single with no dependents. Her **taxable income** is \$100,000. What tax bracket is Deirdre in? Using the marginal tax system, calculate what Deirdre's taxes will be. What is the actual percentage paid of her taxable income?

2. Robert is a head of household taking care of two dependent children. His **adjusted gross income** is \$60,000. Assuming that Robert is claiming the standard deduction, what is his taxable income? What tax bracket is Robert in? Using the marginal tax system, calculate what Robert's taxes will be. What is the actual percentage paid of his **taxable income**?

3. Jessica and Frank are married with no dependents. They file jointly. They each have \$90,000 in **taxable income**, making a combined **taxable income** of \$180,000. What tax bracket are Jessica and Frank in? Using the marginal tax system, calculate what Jessica and Frank's taxes will be. What is the actual percentage paid of their **taxable** income?

4. Kristy and Dan are married with no dependents. Kristy's taxable income is \$22,000 while Dan's taxable income is \$70,000.

- a) If Kristy and Dan file jointly, what tax bracket are they in?
- b) If Kristy and Dan file separately, what tax bracket will Kristy be in?
- c) Calculate the tax owed for Kristy and Dan if they file jointly.
- d) Calculate the tax Kristy will owe if she files her taxes separately.