

LEARN | Understanding the Effective Tax Rate

TAX EDUCATION CENTER

The effective tax rate is a blended rate applied to your client's taxable income after deductions and represents his or her average tax rate.

Did You Know?

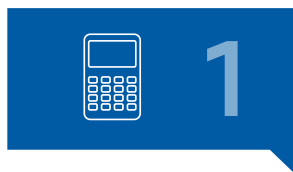
The effective tax rate is more important for clients to consider than the marginal tax rate. The effective tax rate is the amount of taxes paid as a percentage of your total taxable income whereas the marginal tax rate is the highest tax bracket applied to the last dollar earned.

Key Takeaway

The effective tax rate provides a more realistic picture of a client's true tax burden.

How to Calculate the Effective Tax Rate

For this example, we use a married couple filing jointly in 2023 with taxable income (total income less deductions) of \$400,000.



FIRST

Calculate Total Taxable Income

\$400,000 puts the couple in the 32% tax bracket (their marginal tax rate)



SECOND

Determine Taxes Owed From Each Bracket

Use the tax rate for each bracket:

Income: \$0 to \$23,850	Marginal rate: 10%	Tax: \$2,385
Income: \$23,850 to \$96,950	Marginal rate: 12%	Tax: \$8,772
Income: \$96,950 to \$206,700	Marginal rate: 22%	Tax: \$24,145
Income: \$206,700 to \$394,600	Marginal rate: 24%	Tax: \$45,096
Income: \$394,600 to \$501,050	Marginal rate: 32%	Tax: \$1,728
		Total tax: \$82,126



THIRD

Divide Income Tax Owed by Total Income

$\$82,126 \div \$400,000$

Effective tax rate: 20.53%



Bottom Line

The effective tax rate can be significantly lower than the rate associated with your clients' tax brackets and help clients withhold more accurately. In this example, 20.53% is significantly lower than the marginal tax rate of 32%.

Next Step

Use the effective tax rate to help clients adjust withholding accordingly and minimize tax surprises.

Examples provided are for illustrative and informational purposes only and not intended to be reflective of results you can expect to achieve.

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