



**Topic:** "Marginal Rates of Income Tax Simplified"  
**Opinion by:** Justice Doug Campbell  
**Date:** November 28, 2014  
**See Also:** Issue No. 5: "The Marginal Rate Chart"  
Issue No. 6: "Marginal Rate-Sample Calculations"

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*This memorandum was prepared by Justice Doug Campbell in reply to the request of ACJ O'Neil as outlined in his Notice to the Bar dated November 6, 2014. It represents Justice Campbell's personal viewpoint and may or may not require some adjustment to conform to the preferences or practices of individual Judges. That will be left up to the Judge and the lawyer, if any, involved. Readers who make use of the within material do so therefore at their own discretion and subject to their own judgment.*

- Formulation:** 1) Given "Divorce-Mate", "Child View" and other computer generated Family Law Tax calculators, knowledge about the concept of "Marginal" income tax rates and "Average" income tax rates has become irrelevant to the practice of Family Law..... NOT!!
- 2) A working knowledge of "Marginal Rates" is an important tool for Family Lawyers.

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**Context:** *This is the first of a series of Memos designed to promote an understanding of the concept of Marginal Rates of Income Tax. That understanding will allow the reader to instantly estimate the tax implications of any tax deduction/income inclusion such as Spousal Support. This Issue No.4 will be followed by 2 additional commentaries on this subject.*

"Marginal" is a word which, for the within purpose, is best associated with the word "extra". By that I mean that the "marginal" rate of tax is the rate that will apply to an *extra* dollar of income, given an existing amount of income. *Why is that important? ...Stay tuned!*

*I digress:* The Canadian tax system is *progressive*. As a taxpayer's income rises through various thresholds or "brackets", those next dollars of income will attract income tax at ever increasing rates. These are called *marginal rates*. The highest in Nova Scotia is 50%.

So, if a taxpayer is said to face a marginal tax bracket of 50%, *this does not mean* that she will pay income tax at the rate of 50% on her entire income; rather it means that her current income is at such a level that her "top dollars" *and therefore her next dollars* will attract tax equal to 50% of those *extra* income dollars. Thus, if she pays or receives spousal support, she will save (or owe, as the case may be) 50% of that amount in income tax.

Re-stated: If you know the Spouses' Marginal Rates (which you will know from the Chart), you can safely "ballpark" the tax saved by the payor and the tax owed by the recipient arising from a given tax deduction (or income inclusion) such as Spousal Support.

See my simplified marginal rate chart below and the example that follows: (*The chart contains short-cuts which require explanation. This will occur later*).

Taxable Income	Basic Tax	Tax on Next	Marginal Rate
<b>Above :</b>			
11,138	0	18,452	25.00%
29,590	4,113	29,590	33.50%
59,180	14,026	28,727	38.67%
87,907	25,134	48,363	43.10%
136,270	45,979	13,730	46.50%
150,000	52,363	remainder	50.00%

I digress: *I have color-coded my comments below. Please connect the colors in the chart as you read the colored numbers in the narrative for ease of reference.*

*A study of the chart:* The Income Tax **brackets** are to be read **vertically** in the left column. As an example, an income from \$59,180 to \$87,907 will attract tax at 38.67% on those dollars that fall within that range (up to a maximum \$28,727 of additional income). So, if a taxpayer had a taxable income<sup>1</sup> of \$60,180, the chart promotes a calculation which shows that her tax would be \$14,412.70. Here is the Math:

$$\begin{array}{r}
 \text{Tax on the first } \$59,180 = \$14,026.00 \\
 \text{Plus } 38.67\% \text{ of } \$1,000 = \$ 386.70 \\
 \text{Total Tax} \qquad \qquad \qquad \text{\$14,412.70}
 \end{array}$$

So, to return to the meaning of "marginal" tax rates, the above math illustrates that the taxpayer does not pay income tax of 38.67% of her entire income of \$60,180:  $(60,180 \times 38.67\% =$

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<sup>1</sup> ignore the meaning of that term "taxable income" until later)

\$23,272.00); instead, she pays **her marginal rate**, ( 38.67 %), on only \$1,000. Her total tax bill is \$14,412.70.

Re-stated, she pays zero dollars of tax on the first **\$11,138** (*because every taxpayer has a personal exemption and most have a CPP tax credit, the combination of which serves to eliminate the tax on those dollars*) ; she pays **\$4,113** on her next **\$18,452** of income ( which is 25%<sup>2</sup> ); she pays 33.5% on her next dollars ( $29,590 \times 33.5\% = 9,913 + 4,113 = \$14,026$ ); and then **38.67 %** on her final \$1,000 dollars of income.

**Summary:** There are 4 Marginal Rates that apply to this \$60,180 Income tax payor: 0%, 25%, 33.5% and 38.67%. She only pays **38.67 %** on her "top" dollars, which top dollars, in my example, equates to \$1,000.

So, in light of all this, what is meant by her "Average" rate of tax?

**Long Answer:** *The weighted-average of 0%, 25%, 33.5% and 38.67%.*

**Short Answer:** *Her tax bill divided by her Income:  $14,412.70/60,180 = 23.95\%$ .*

Thus: A top "Marginal" tax rate for a particular Taxpayer is much different (**38.67%**) than an "Average" rate (23.95%) for that Taxpayer. As illustrated above, top "marginal rate" is the rate of tax on **only** the dollars in the applicable top tax bracket. "Average" tax rate is the overall rate of tax on **all** of the income dollars.

That's *enough for this Issue...* (Please keep these remarks in mind when you read Issue No. 5 and Issue No. 6).

**In the next Issues, I will do 4 things:**

- 1) Discuss the shortcuts in my above Chart;
- 2) Show a sample calculation to "ballpark" tax savings/tax added by Spousal Support in a simple case;
- 3) Show a more complicated calculation regarding the above when the tax bracket is "straddled" with other brackets; and
- 4) Distinguish Tax Deductions from Tax Credits.

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<sup>2</sup> From the 25% tax, I actually subtract \$500 as a rough estimate of the tax savings on EI contribution and the employment tax credit. This sometimes causes a small inaccuracy in the chart since most taxpayers, but not all, are eligible for both. This is a shortcut and will occasionally not apply.