Problem 2-7: Sample solution

The Talley Corporation had a taxable income of $365,000 from operations after all operating costs, but before (1) interest charges of $50,000 (2) dividends received of $15,000 (3) dividends paid of $25,000, and (4) income taxes. What are the firm's income tax liabiity and its after-tax income. What are the company's marginal and average tax rates on taxable income.

You first need to determine Talley's taxable income:

Income after operating costs:	$365,000.00
Less: Interest Expense	-$50,000.00
Plus: Taxable Dividends Received	$4,500.00
Only 30% of the $15,000 in dividends are taxable.	
Taxable Income:	$319,500.00

Next you need to calculate your tax liability from Table 2-6
Corporate Tax Rates as of January 2008, on page 71

$319,500 falls into the $100,000 to $335,000 bracket so the corporate tax
woud be: $22,250 + .39 ($319,500 - $100,000)
Base Amount plus marginal rate x difference between taxable income - lower base

Tax Liability = $107,855.00

Talley's marginal tax rate is 39% the rate on the last dollar of income subject to tax.
Talley's average tax rate is: Tax Liability / Amount of Income Subject to Tax
Average Tax Rate = $107,855/$319,500 = 33.76%