

SOUTH-WESTERN
FEDERAL TAXATION

Raabe
Young
Nellen
Maloney

ESSENTIALS OF TAXATION

Individuals and Business Entities

2018

INCLUDED:

THOMSON REUTERS
CHECKPOINT
Student Edition

**H&R
BLOCK** TAX
SOFTWARE

ROGER
CPA Review

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**SOUTH-WESTERN
FEDERAL TAXATION**

2018 EDITION
**ESSENTIALS OF
TAXATION: INDIVIDUALS
AND BUSINESS ENTITIES**

General Editors

William A. Raabe

Ph.D., CPA
Milton, Wisconsin

James C. Young

Ph.D., CPA
Northern Illinois University

Annette Nellen

J.D., CPA, CGMA
San Jose State University

David M. Maloney

Ph.D., CPA
University of Virginia



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**South-Western Federal Taxation:
Essentials of Taxation, 2018 Edition****William A. Raabe, James C. Young,
Annette Nellen, David M. Maloney**SVP, General Manager: Social Sciences,
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Product Director: Jason Fremder

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Sr. Art Director: Michelle Kunkler

Text and Cover Designer: Red Hangar Design

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Authors for the South-Western Federal Taxation Series**Greg Carnes**Ph.D., CPA
University of
North Alabama**Andrew Cuccia**Ph.D., CPA
The University of
Oklahoma**Steven L. Gill**Ph.D., CPA
San Diego State
University**Kristina Zvinakis**Ph.D.
The University of
Texas at Austin



Preface

COMMITTED TO EDUCATIONAL SUCCESS

South-Western Federal Taxation (SWFT) is the most trusted and best-selling series in college taxation. We are focused exclusively on providing the most useful, comprehensive, and up-to-date tax texts, online study aids, tax preparation tools, and research tools to help instructors and students succeed in their tax courses and beyond.

SWFT is a comprehensive package of teaching and learning materials, significantly enhanced with each edition to meet instructor and student needs and to add overall value to learning taxation.

Essentials of Taxation: Individuals and Business Entities, 2018 Edition provides a dynamic learning experience inside and outside of the classroom. Built with resources and tools that have been identified as the most important, our complete learning system provides options for students to achieve success.

Essentials of Taxation: Individuals and Business Entities, 2018 Edition provides accessible, comprehensive, and authoritative coverage of the relevant tax code and regulations as they pertain to the individual or business taxpayer, as well as coverage of all major developments in Federal Taxation.

In revising the 2018 Edition, we focused on:

- **Accessibility. Clarity. Substance.** The text authors and editors made this their mantra as they revised the 2018 edition. Coverage has been

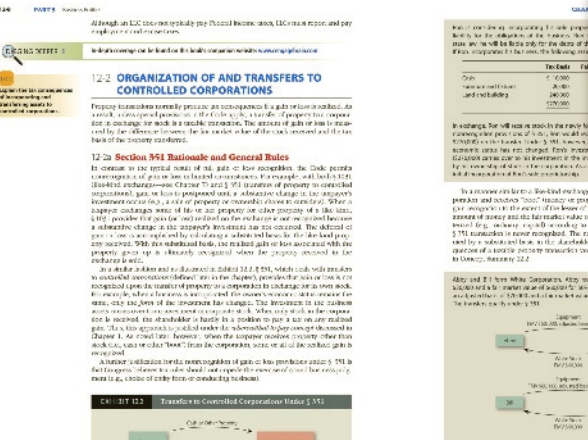
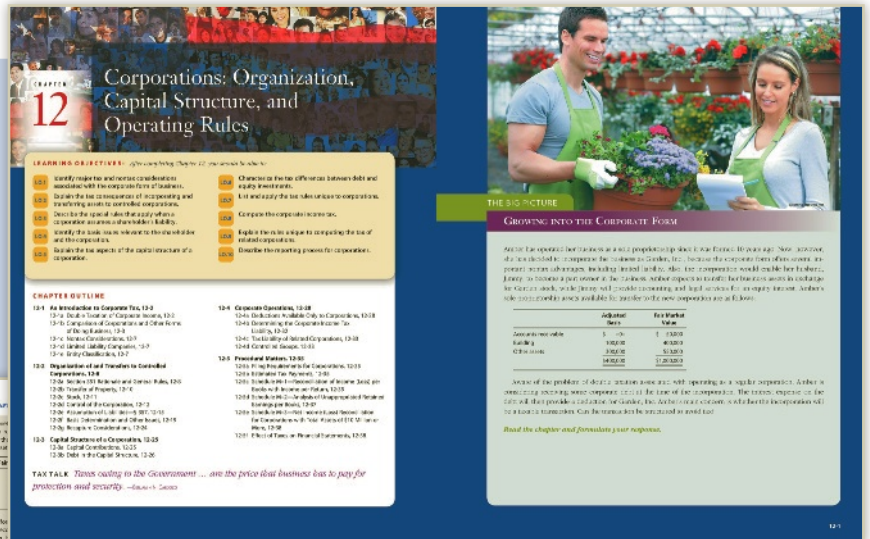
streamlined to make it more accessible to students, and difficult concepts have been clarified, all without losing the substance that makes up the *South-Western Federal Taxation* series.

- **Developing professional skills.** SWFT excels in bringing students to a professional level in their tax knowledge and skills, to prepare them for immediate success in their careers. In this regard, we include development of speaking and writing communications skills, the use of tax preparation and tax research software, orientation toward success on the CPA exam, consideration of the time value of money in the tax planning process, and facility with advanced applications of spreadsheet construction.
- **CengageNOWv2 as a complete learning system.** Cengage Learning understands that digital learning solutions are central to the classroom. Through sustained research, we continually refine our learning solutions in CengageNOWv2 to meet evolving student and instructor needs. CengageNOWv2 fulfills learning and course management needs by offering a personalized study plan, video lectures, auto-graded homework, auto-graded tests, and a full eBook with features and advantages that address common challenges.

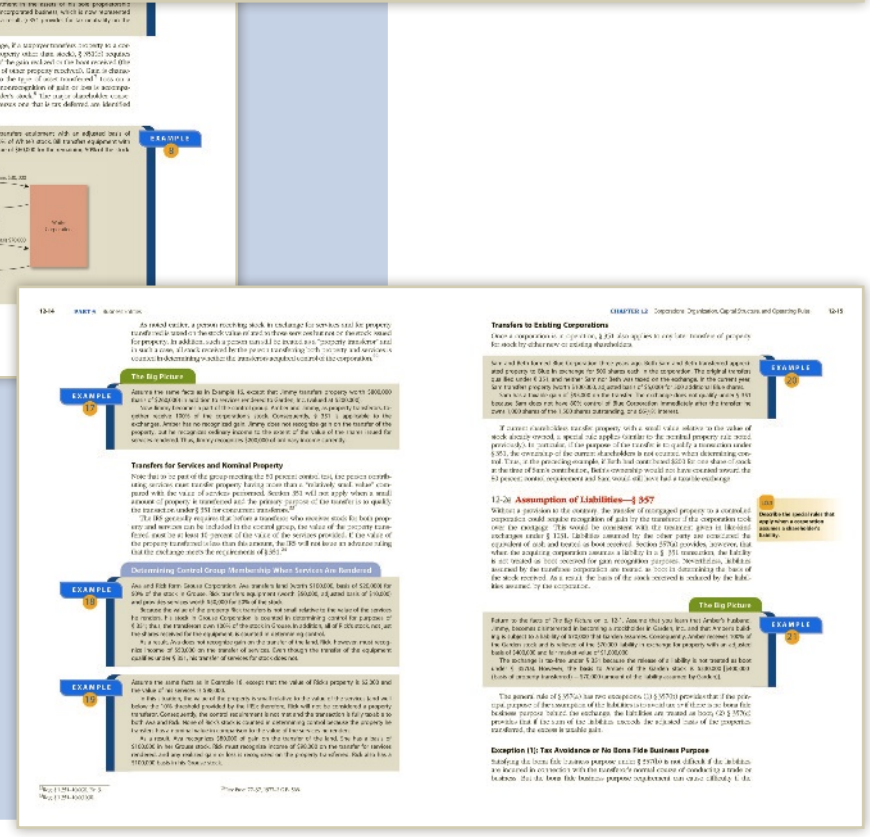
Learning Tools and Features to Help Students Make the Connection

FULL-COLOR DESIGN: We understand that students struggle with learning difficult tax code concepts and applying them to real-world scenarios. The 2018 edition uses color to bring the text to life, capture student attention, and present the tax code in a simple, yet logical format.

- Selected content is streamlined to guide students in focusing on the most important concepts for the CPA Exam while still providing in-depth coverage of topics.



- Examples are clearly labeled and directly follow concepts to assist with student application. An average of over 40 examples in each chapter use realistic situations to illustrate the complexities of the tax law and allow students to integrate chapter concepts with illustrations and examples.



COMPUTATIONAL EXERCISES: Students need lots of practice in areas such as computing tax return problems and adjusting rates. We have developed these exercises to give students practice in calculating the solutions they need to make business decisions.

- Found in end-of-chapter section of the textbook
- CengageNOWv2 provides algorithmic versions of these problems

Computational Exercises

1. **LO.2** Marie and Ethan form Roundtree Corporation with the transfer of the following. Marie performs personal services for the corporation with a fair market value of \$80,000 in exchange for 400 shares of stock. Ethan contributes an installment note receivable (basis \$25,000; fair market value \$30,000), land (basis \$50,000; fair market value \$170,000), and inventory (basis \$100,000; fair market value \$120,000) in exchange for 1,600 shares. Determine Marie and Ethan's current income, gain, or loss; calculate the basis that each takes in the Roundtree stock.
2. **LO.2** Grady exchanges qualified property, basis of \$12,000 and fair market value of \$18,000, for 60% of the stock of Eadie Corporation. The other 40% of the stock is owned by Pedro, who acquired it five years ago. Calculate Grady's current income, gain, or loss and the basis he takes in his shares of Eadie stock as a result of this transaction.
3. **LO.3** Jocelyn contributes land with a basis of \$60,000 and fair market value of \$90,000 and inventory with a basis of \$5,000 and fair market value of \$8,000 in exchange for 100% of Zion Corporation stock. The land is subject to a \$15,000 mortgage. Determine Jocelyn's recognized gain or loss and the basis in the Zion stock received.

ROGER CPA EXAM REVIEW QUESTIONS: The SWFT series continues to provide the most in-depth coverage of tax concepts, and selected Roger CPA Exam Review Questions are included to further prepare students for success on the CPA Exam.

- Located in selected end-of-chapter sections
- Tagged by concept in CengageNOWv2
- Similar questions to what students would actually find on the CPA Exam



Roger CPA Review Questions



1. In general, what is the current filing deadline for a C corporation?
 - a. March 15
 - b. April 15
 - c. The 15th day of the 3rd month after year-end
 - d. The 15th day of the 4th month after year-end
2. Crimson Corp. was organized as a calendar year corporation in January 2017, incurring \$51,000 in qualified organizational expenses, and began business in March 2017. What is the maximum amount Crimson may deduct for organizational expenditures on its 2017 corporate tax return?

a. \$4,000	c. \$6,350
b. \$6,611	d. \$7,133
3. Kellye and Becky formed Whoop! Shotz Corporation by contributing property with a fair market value of \$50,000 and \$70,000 cash, respectively, each for a 50% ownership in the newly formed company. What is Kellye's taxable gain in this situation if the adjusted basis in the property is \$25,000 and the company is valued at \$120,000?

a. \$0	c. \$25,000
b. \$10,000	d. \$35,000

See how the SWFT series helps students understand the big picture and the relevancy behind what they are learning.

THE BIG PICTURE

GOING INTERNATIONAL

VoiceGo, a domestic corporation, designs, manufactures, and sells specialty microphones for use in theaters. All of its activities take place in Florida, although it ships products to customers all over the United States. When it received inquiries about its products from foreign customers, VoiceGo decided to test the foreign market and placed ads in foreign trade journals. Soon it was taking orders from foreign customers.

VoiceGo is concerned about its potential foreign income tax exposure. Although it has no assets or employees in the foreign jurisdictions, it now is involved in international commerce. Is VoiceGo subject to income taxes in foreign countries? Must it pay U.S. income taxes on the profits from its foreign sales? What if VoiceGo pays taxes to other countries? Does it receive any benefit from these payments on its U.S. tax return?

Later, VoiceGo established a manufacturing plant in Ireland to meet the European demand for its products. VoiceGo incorporated the Irish operation as a controlled foreign corporation (CFC) named VoiceGo-Ireland. So long as VoiceGo-Ireland does not distribute profits to VoiceGo, will the profits escape U.S. taxation? What are the consequences to VoiceGo of being the owner of the CFC?

Read the chapter and formulate your response.

THE BIG PICTURE: Tax Solutions for the Real World.

Taxation comes alive at the start of each chapter as The Big Picture Examples give a glimpse into the lives, families, careers, and tax situations of typical individual or business filers. Students will follow the family, individual, or other taxpayer throughout the chapter showing students how the concepts they are learning play out in the real world.

Finally, to solidify student comprehension, each chapter concludes with a **Refocus on the Big Picture** summary and tax planning scenario. These scenarios apply the concepts and topics from the chapter in a reasonable and professional way.

BRIDGE DISCIPLINE BOXES AND END-OF-CHAPTER QUESTIONS:

Bridge Discipline boxes throughout the text present material and concepts from other disciplines such as economics, financial accounting, and finance. They help to bridge the gap between taxation issues and issues raised in other business courses. **Bridge Discipline questions**, in the end-of-chapter material, help test these concepts and give students the chance to apply concepts they've learned in the Bridge Discipline boxes.

BRIDGE DISCIPLINE Bridge to Cost Accounting and Executive Compensation

Multijurisdictional companies operate across state and country borders. The transfer price used by a company can have a significant effect on the amount of profits subject to taxation within a particular taxing jurisdiction. Companies face other concerns when establishing transfer pricing policies. For example, the internal determination of how a division of the company is performing may be based on transfer pricing between related entities within the global group. Furthermore, the compensation of the managers within those divisions may be tied directly to divisional performance.

If an intercompany price is set in a manner that optimizes the global tax position, a separate cost accounting policy may be required to determine an entity's profitability for purposes of compensating employees. Tax advisers often face resistance from operations managers when suggesting improved transfer pricing methods, because such improvements often change the traditional division of profits among different parts of the business.

FINANCIAL DISCLOSURE INSIGHTS Overseas Operations and Book-Tax Differences

Non-U.S. operations account for a large portion of the permanent book-tax differences of U.S. business entities. These differences may relate to different tax bases, different tax rate structures, or special provisions concerning tax-based financing with the other country. For instance, lower tax rates applied by Ireland, Bermuda, and the Netherlands recently reduced Apple's current-year tax rate from 35% to 26%, with cash tax outlays of only 19%.

Tax planning strategies using non-U.S. operations also are found in the deferred tax asset and liability accounts. Tax deferrals allowed under current U.S. tax rules and carryforwards of the foreign tax credit can be substantial for some businesses. For example, IBM recently reported a deferred tax asset relating to delays in using its FTCs amounting to about \$500 million. For the operating arm of General Electric, that amount was about \$2 billion.

FINANCIAL DISCLOSURE INSIGHTS:

Tax professionals need to understand how taxes affect the income statement and balance sheet. **Financial Disclosure Insights**, appearing throughout the text, use current data about existing taxpayers to highlight book-tax reporting differences, effective tax rates, and trends in reporting conventions.

DIGGING DEEPER: Designed to help students go further in their knowledge of certain topics, **Digging Deeper** links within the text provide more in-depth coverage that can be found on the book's website at www.cengagebrain.com.

DIGGING DEEPER 1

In-depth coverage can be found on this book's companion website: www.cengagebrain.com

TAX PLANNING FRAMEWORK:

To demonstrate the relevance of tax planning for business and individual taxpayers, *Essentials of Taxation: Individuals and Business Entities* presents a unique **tax planning framework**. Introduced in Chapter 1, this framework extends to a series of **Tax Planning Strategies** incorporated throughout the remainder of the text. The inclusion of the tax planning framework, and the planning strategies in each chapter, makes it easier than ever to understand the impact careful tax planning has in today's world.

EXHIBIT 1.3 General Framework for Income Tax Planning		
Tax Formula	Tax Planning Strategy	Tax Planning Examples
Income and exclusions	<ul style="list-style-type: none"> ➤ Avoid income recognition. ➤ Postpone recognition of income to achieve tax deferral. 	<ul style="list-style-type: none"> Compensate employees with nontaxable fringe benefits (see Example 19). Postpone sale of assets (see Example 20).
– Deductions	<ul style="list-style-type: none"> ➤ Maximize deductible amounts. ➤ Accelerate recognition of deductions to achieve tax deferral. 	<ul style="list-style-type: none"> Invest in stock of another corporation (see Example 21). Elect to deduct charitable contribution in year of pledge rather than in year of payment (see Example 22).

TAX PLANNING STRATEGIES
Nexus: To Have or Have Not

FRAMEWORK FOCUS: TAX RATE

Strategy: Shift Net Income from High-Tax Jurisdictions to Low-Tax Jurisdictions.

Most taxpayers try to avoid establishing nexus in a new state, for example, by providing a sales representative with a cash auto allowance rather than a company car, by restricting the location of inventory to only a few states, or by limiting a salesperson's activities to those that are protected by the solicitation standard of P.L. 86-272. This effort to avoid nexus stems in part from the additional compliance burden that falls upon the taxpayer when a new set of income tax returns, information forms, and deadlines must be dealt with in the new state.

Another concern is that the marginal tax rate that applies to the net taxable income generated by the taxpayer may increase. Such a tax increase occurs, of course, only when the applicable tax rate in the new state is higher than the rate that would apply in the home state. If a business already is based in a tax-friendly state such as Florida or Texas or in a no-tax state such as Nevada, its aggregate tax liability is sure to increase.

Still, nexus is not necessarily a bad thing. Consider what happens if a business based in California, Maryland, Wisconsin, or another high-tax jurisdiction purposely creates nexus in a low- or no-tax state. If the new state applies a lower marginal rate than is available in the home state or offers special exemptions or exclusions that match the taxpayer's operations, the aggregate tax bill can decrease. Then the planning efforts include determining which activities will create nexus in the new jurisdiction and meeting or maintaining that standard.

For instance, an entertainer based in Manhattan is subject to the high income taxes of New York City and New York State. By establishing a permanent office in Tennessee, nexus will be created, and some portion of the taxpayer's income will be subject to taxation there, instead of New York. These are permanent savings, accruing immediately to after-tax income and the share price of the stock of the taxpayer.

TAX PLANNING STRATEGIES: The tax planning framework extends to subsequent chapters as **Tax Planning Strategies boxes** that are tied to the topical coverage of the chapters. Planning Strategies often contain examples to further illustrate the concept for students. Because some tax planning strategies do not fit neatly into the framework, the text also provides tax planning strategies called **Thinking Outside the Framework**.

GLOBAL TAX ISSUES: The **Global Tax Issues** feature gives insight into the ways in which taxation is affected by international concerns and illustrates the effects of various events on tax liabilities across the globe.

GLOBAL TAX ISSUES
Choice of Organizational Form When Operating Overseas

When the management of a corporation decides to expand its business by establishing a presence in a foreign market, the new business venture may take one of several organizational forms. As each form comes with its respective advantages and disadvantages, making the best choice can be difficult.

One common approach is to conduct the foreign activity as a *branch* operation of the U.S. corporation. The foreign branch is not a separate legal entity, but a division of the U.S. corporation established overseas. As a result, any gains and losses produced by the foreign unit are included in the corporation's overall financial results.

Another possibility is to organize the foreign operations as a *subsidiary* of the U.S. parent corporation. If this route is

chosen, the subsidiary can be either a *domestic* subsidiary (i.e., organized in the United States) or a *foreign* subsidiary (organized under the laws of a foreign country).

One fundamental tax difference between these two approaches is that the gains and losses of a domestic subsidiary may be consolidated with the operations of the U.S. parent, while the operations of a foreign subsidiary cannot. Thus, the use of a domestic subsidiary to conduct foreign operations yields generally the same final result as the use of a branch. With both approaches, the financial statements of the U.S. parent reflect the results of its worldwide operations.

Take your students from Motivation to Mastery with CengageNOWv2

CengageNOWv2 is a powerful course management tool and online homework resource that elevates student thinking by providing superior content designed with the entire student workflow in mind.

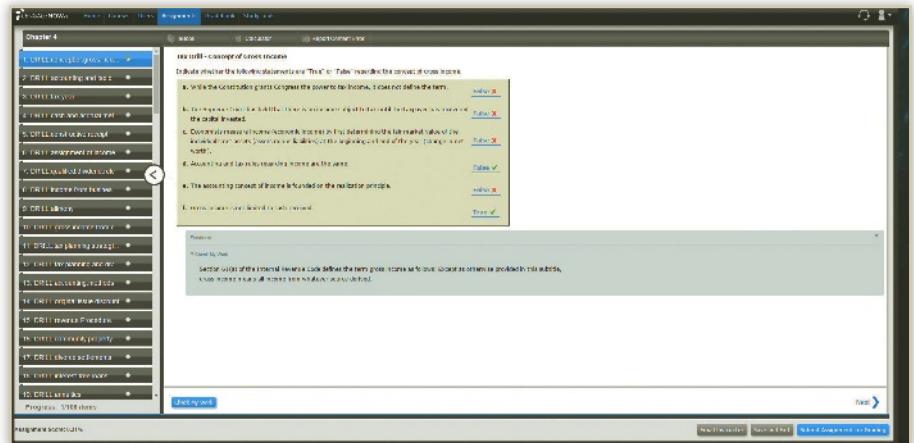


- **MOTIVATION:** engage students and better prepare them for class
- **APPLICATION:** help students learn problem-solving behavior and skills to guide them to complete taxation problems on their own
- **MASTERY:** help students make the leap from memorizing concepts to actual critical thinking

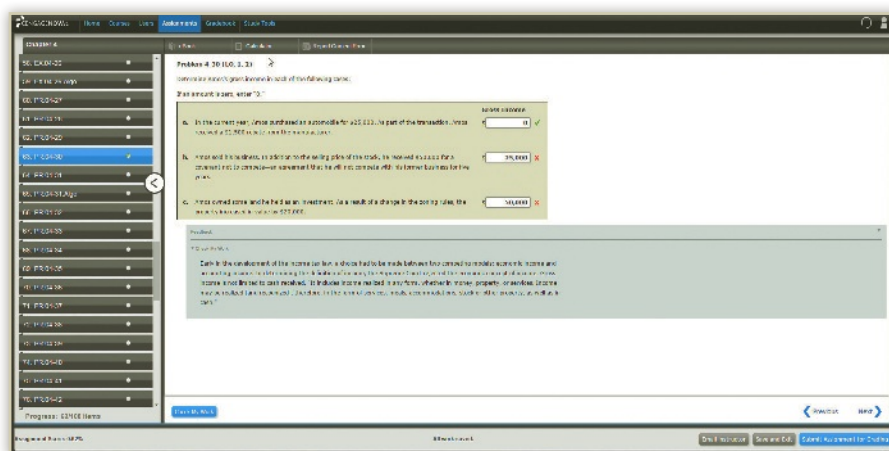
Motivation —

Many instructors find that students come to class unmotivated and unprepared. To help with engagement and preparedness, CengageNOWv2 for SWFT offers:

- **“Tax Drills” test students on key concepts and applications.** With three to five questions per learning objective, these “quick-hit” questions help students prepare for class lectures or review prior to an exam.



Application —



Students need to learn problem-solving behavior and skills, to guide them to complete taxation problems on their own. However, as students try to work through homework problems, sometimes they become stuck and need extra help. To reinforce concepts and keep students on the right track, CengageNOWv2 for SWFT offers the following.

- **End-of-chapter homework from the text** is expanded and enhanced to follow the workflow a professional would use to solve various client scenarios. These enhancements better engage students and encourage them to think like a tax professional.

- **Algorithmic versions** of end-of-chapter homework are available for computational exercises and at least 15 problems per chapter.
- **“Check My Work” Feedback.** Homework questions include immediate feedback so students can learn as they go. Levels of feedback include an option for “check my work” prior to submission of an assignment.
- **Post-Submission Feedback.** After submitting an assignment, students receive even more extensive feedback explaining why their answers were incorrect. Instructors can decide how much feedback their students receive and when, including the full solution.
- **Built-in Test Bank** for online assessment.

Mastery —

- **NEW! Tax Form Problems** have been added to the 2018 edition. Students can now complete the Cumulative H&R Block Problems and other homework items found in the end-of-chapter manually or in a digital environment.
- **“What-If” Questions** allow students to develop a deeper understanding of the material as they are challenged to use their prior knowledge of the tax situations and critically think through new attributes to determine how the outcome will change.
- **An Adaptive Study Plan** comes complete with an eBook, practice quizzes, crossword puzzle, glossary, and flashcards. It is designed to help give students additional support and prepare them for the exam.

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EXTENSIVELY REVISED. DEFINITELY UP TO DATE.

Each year the *South-Western Federal Taxation* series is updated with thousands of changes to each text. Some of these changes result from the feedback we receive from instructors and students in the form of reviews, focus groups, web surveys, and personal e-mail correspondence with our authors and team members. Other changes come from our careful analysis of the evolving tax environment. **We make sure that every tax law change relevant to the introductory taxation course was considered, summarized, and fully integrated into the revision of text and supplementary materials.**

The *South-Western Federal Taxation* authors have made every effort to keep all materials up to date and accurate. All chapters contain the following general changes for the 2018 Edition.

- Updated materials to reflect changes made by Congress through legislative action.
- Streamlined chapter content (where applicable) to clarify material and make it easier for students to understand.
- Revised numerous materials as the result of changes caused by indexing of statutory amounts.
- Revised Problem Materials, Computational Exercises, and CPA Exam problems.
- Updated Chapter Outlines to provide an overview of the material and to make it easier to locate specific topics.
- Revised *Financial Disclosure Insights* and *Global Tax Issues* as to current developments.

In addition, the following materials are available online.

- An appendix that helps instructors broaden and customize coverage of important tax provisions of the Affordable Care Act. (Instructor Companion Website at www.cengage.com/login)
- The Depreciation and the Accelerated Cost Recovery System (ACRS) appendix. (Instructor Companion Website at www.cengage.com/login)
- The Taxation in the Real World weekly blog posts for instructors. (<https://community.cengage.com/t5/Taxation-in-the-Real-World-Blog/bg-p/taxationintherealworldblog>)

Chapter 1

- Updated materials to reflect inflation indexation including the unified transfer tax credit and exemption amount, annual gift tax exclusion amount, and FICA base amount.

- Revised and updated statistics about Federal income tax paid by income classes, Federal budget receipts and collections, national excise taxes on gasoline and cigarettes consumption, and Tax Freedom Day.

Chapter 2

- Updated the information on tax research techniques.
- Refocused tax research from conducting it to best practices.
- Updated CPA examination information to reflect changes to the exam starting in 2017.

Chapter 3

- Added comment about Federal tax treatment of compensation items *viz.* GAAP treatment.
- Updated statistics concerning goodwill on the balance sheets for selected U.S. corporations and regarding Schedule UTP reporting.
- Revised Global Tax Issues feature “Cash Stashed Overseas.”
- Removed discussion of Dynamic Benchmarking.

Chapter 4

- Reduced interest rates used in examples to better reflect today’s rates.
- Revised and clarified text and examples throughout the chapter.

Chapter 5

- Revised and clarified text and examples throughout the chapter. Modified materials as needed to reflect inflation indexation changes.
- Expanded discussion of executive compensation and added a new example.
- Revised discussion of research and experimentation expenses.
- Expanded discussion of § 179 (including several new examples), revised order of § 179 expense and additional first-year (bonus) depreciation (covering § 179 first), and added new materials on using § 179 and bonus depreciation effectively (including a new Concept Summary).

Chapter 6

- Revised and clarified text and examples throughout the chapter.
- Added a Digging Deeper topics on virtual currency, material participation, and real estate professionals.

Chapter 7

- Revised and clarified chapter materials; added multiple examples to illustrate concepts.
- Added a new Concept Summary on realized gains and losses and expanded discussion on this topic.
- Removed summary material on other nonrecognition provisions (§§ 1032, 1035, 1036, and 1044).
- Added a new tax form problem (the completion of a Form 8824 for a like-kind exchange).

Chapter 8

- Added Concept Summary 8.1, summarizing the characteristics of recognized gains and losses.
- Streamlined and clarified coverage throughout the chapter; added multiple examples to materials.

Chapter 9

- Revised and clarified text and examples throughout the chapter. Modified materials as needed to reflect inflation indexation changes.
- Modified Head of Household discussion and added examples.
- Added a research problem on tax reform.

Chapter 10

- Revised and clarified text and examples throughout the chapter. Modified materials as needed to reflect inflation indexation changes.
- Clarified the explanation of scholarships.
- Simplified the explanation of the adoption expenses credit.
- Added a research problem on tax expenditures.
- Added a Digging Deeper topic on education credits.

Chapter 11

- Streamlined coverage throughout the chapter; added multiple examples to illustrate text material.
- Updated materials for inflation adjustments.
- Clarified discussion of employee v. contractor issues.
- Added material concerning documentation of employee expenditures.

Chapter 12

- Added new Exhibit 12.2 (Transfers to Controlled Corporations Under § 351).
- Enhanced the explanation of the § 351 control requirement.
- Modified several aspects of the tax planning discussions.
- Added a reference to Treasury's Proposed Regulations under § 385 in the debt/equity area.
- Added present value components to end-of-chapter materials.

Chapter 13

- Revised and clarified chapter materials; added new examples.
- Revised Concept Summary 5.2 (Allocating E & P to Distributions) and added new examples to illustrate how E & P is allocated to distributions.

Chapter 14

- Clarified definitions of general and limited partners.
- Streamlined discussion of four major types of partnerships.
- Changed from “nonliquidating distribution” to “current distribution” throughout, but kept reference to nonliquidating distributions as an alternative name.
- Clarified and expanded comparisons of partnerships and C corporations (and aggregate and entity theories) throughout.

Chapter 15

- Updated S corporation filing statistics (including industry type).

- Added a new flowchart (Exhibit 15.1) dealing with the S election requirements.
- Revised and clarified text and examples throughout the chapter.

Chapter 16

- Expanded and updated the Digging Deeper topic on nexus.
- Added “repatriation” to the glossary.
- Added an Excel question to the end-of-chapter exercises.

Chapter 17

- Expanded coverage of corporate alternative minimum tax including a new overview section; expanded discussion of adjustments and preferences; added multiple examples to the materials.

- Updated chapter materials for inflation adjustments and for various computational formulas and amounts.

Chapter 18

- Added information on role of tax preparer on issues of reasonable compensation and payments between a corporation and shareholder.
- Added discussion of the potential impact of organizational form on the owner’s FICA tax liability.
- Combined LO regarding identifying which organizational forms result in double taxation with that related to effects of conduit versus entity approach to an entity.
- Significantly revised Bridge Discipline items regarding the perspectives to a business taken across tax and GAAP.

TAX LAW OUTLOOK

From your SWFT Series Editors:

Concerns about complexity, income inequity, job creation, and international competitiveness will keep income tax issues at the forefront of tax-related discussions throughout 2017 and 2018. Congress is reviewing tax proposals on middle-class tax relief and tax changes for the wealthy. Changes to the Affordable Care Act (ObamaCare) also are being considered.

Congress is also evaluating Federal corporate tax law changes in 2017 and 2018, including a decrease in the top tax rate and a move toward a territorial system in taxing income from overseas sources. Tax deferrals for unrepatriated global profits also may receive congressional and regulatory attention. Tax reform likely will include lower rates, and changes for businesses not operating as C corporations. State and local governments also have budget problems, and they are looking for new revenue sources, including a broadening of the income and sales/use tax bases. If major tax legislation is passed that affects this text, the SWFT editors will provide an update for adopters.

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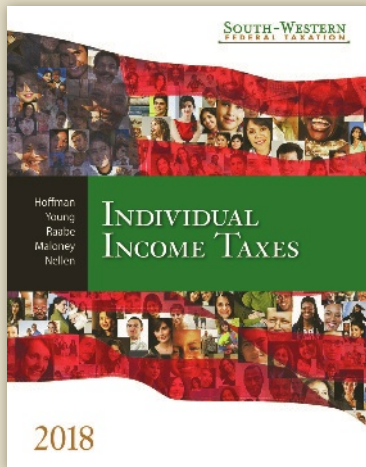
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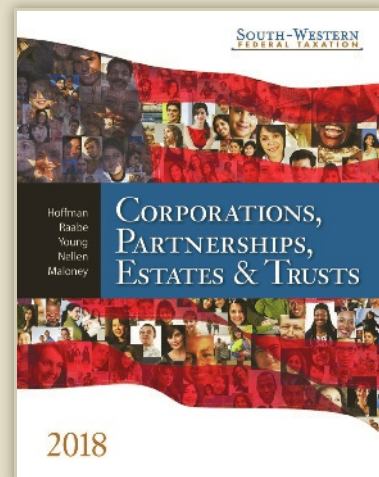
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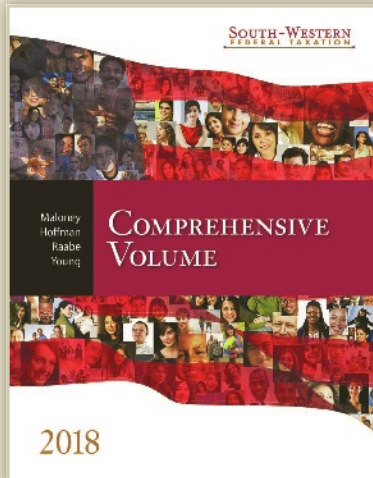
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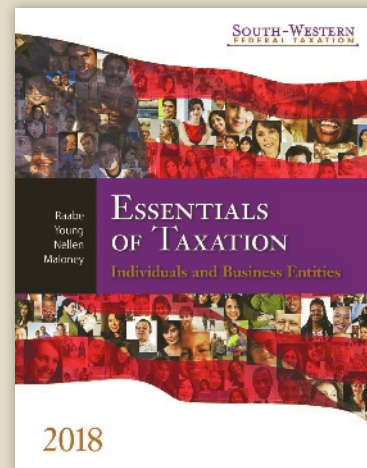
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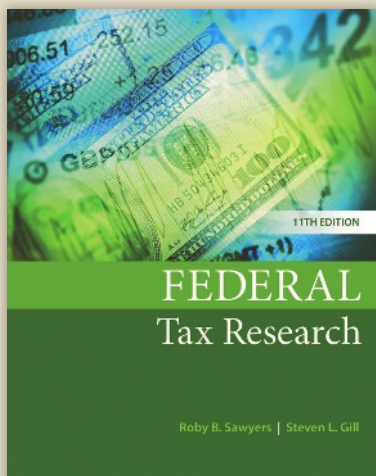
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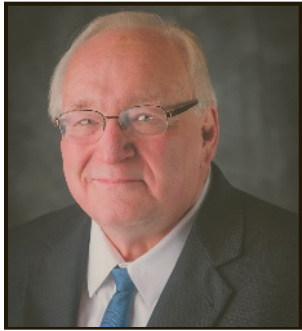
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ABOUT THE EDITORS



William A. Raabe, Ph.D., CPA, was the Wisconsin Distinguished Professor of Taxation. He taught at Ohio State, Arizona State, the Capital University (OH) Law School, and the Universities of Wisconsin – Milwaukee and Whitewater. A graduate of Carroll University (Wisconsin) and

the University of Illinois, Dr. Raabe's teaching and research interests include international and multistate taxation, technology in tax education, personal financial planning, and the economic impact of sports teams and fine arts groups. Dr. Raabe also writes the PricewaterhouseCoopers Tax Case Studies. He has written extensively about book-tax differences in financial reporting. Dr. Raabe has been a visiting tax faculty member for a number of public accounting firms, bar associations, and CPA societies. He has received numerous teaching awards, including the Accounting Educator of the Year award from the Wisconsin Institute of CPAs. He has been the faculty adviser for student teams in the Deloitte Tax Case Competition (national finalists at three different schools) and the PricewaterhouseCoopers Extreme Tax policy competition (national finalist). For more information about Dr. Raabe, visit BillRaabeTax.com and BillRaabeTax on YouTube and Twitter.



James C. Young is the Crowe Horwath Professor of Accountancy at Northern Illinois University. A graduate of Ferris State University (B.S.) and Michigan State University (M.B.A. and Ph.D.), Jim's research focuses on taxpayer responses to the income tax using archival data. His dissertation

received the PricewaterhouseCoopers/American Taxation Association Dissertation Award and his subsequent research has received funding from a number of organizations, including the Ernst & Young Foundation Tax Research Grant Program. His work has been published in a variety of academic and professional journals, including the *National Tax Journal*, *The Journal of the American Taxation Association*, and *Tax Notes*. Jim is a Northern Illinois University Distinguished Professor, received the Illinois CPA Society Outstanding Accounting Educator Award in 2012, and has received university teaching awards from Northern Illinois University, George Mason University, and Michigan State University.



Annette Nellen, CPA, CGMA, Esquire, directs San José State University's graduate tax program (MST) and teaches courses in tax research, tax fundamentals, accounting methods, property transactions, state taxation, employment tax, ethics, and tax policy. Professor

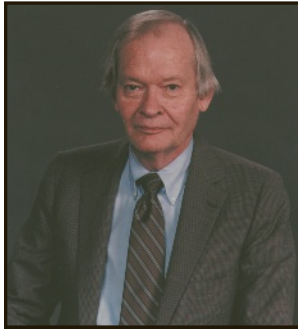
Nellen is a graduate of CSU Northridge, Pepperdine (MBA), and Loyola Law School. Prior to joining SJSU in 1990, she was with a Big 4 firm and the IRS. At SJSU, Professor Nellen is a recipient of the Outstanding Professor and Distinguished Service Awards. Professor Nellen is an active member of the tax sections of the AICPA and American Bar Association. In 2013, she received the AICPA Arthur J. Dixon Memorial Award, the highest award given by the accounting profession in the area of taxation. Professor Nellen is the author of *BloombergBNA Tax Portfolio*, *Amortization of Intangibles*, and the *BloombergBNA Internet Law Resource Center*, *Overview of Internet Taxation Issues*. She has published numerous articles in the *AICPA Tax Insider*, *Tax Adviser*, *State Tax Notes*, and *The Journal of Accountancy*. She has testified before the House Ways & Means and Senate Finance Committees and other committees on Federal and state tax reform. Professor Nellen maintains the 21st Century Taxation website and blog (www.21stcenturytaxation.com) as well as websites on tax reform and state tax issues (www.sjsu.edu/people/annette.nellen/).



David M. Maloney, Ph.D., CPA, is the Carman G. Blough Professor of Accounting Emeritus at the University of Virginia's McIntire School of Commerce. He completed his undergraduate work at the University of Richmond and his graduate work at the University

of Illinois at Urbana-Champaign. Upon joining the Virginia faculty in January 1984, Dr. Maloney taught Federal taxation in the graduate and undergraduate programs and was a recipient of major research grants from the Ernst & Young and KPMG Foundations. Dr. Maloney has published work in numerous professional journals, including *Journal of Taxation*, *The Tax Adviser*, *Tax Notes*, *Corporate Taxation*, *Accounting Horizons*, *Journal of Taxation of Investments*, and *Journal of Accountancy*.

William H. Hoffman, Jr.



On May 1, 2016, our founding editor, valued colleague, and co-author Bill Hoffman, passed away after a brief illness. Bill was born in Casper, Wyoming, in 1929 and also lived in both Belgium and Argentina during his youth, before moving to Port Arthur, Texas. He earned both undergraduate and law degrees from the

University of Michigan before serving in the Korean War as an officer in the U.S. Army's Judge Advocate General Corps. Following his return from military service, he completed both an MBA and a PhD at The University of Texas at Austin. Bill began his academic career at Louisiana State University, where he served as a professor of accounting and taxation, before moving to the University of Houston in 1967. Bill remained at Houston for the rest of his academic career, retiring in 1999.

During his time at Houston, Bill served as a professor, mentor, and doctoral advisor to countless students and colleagues. Desiring to help his students understand the intricacies of entity taxation (corporations, partnerships, and estates and trusts), he envisioned a new textbook for a second tax course in Houston's accounting program and brought together a team of authors to create the text in 1977. *South-Western Federal Taxation: Corporations, Partnerships, Estates and Trusts*—now in its forty-first edition—remains the market leader while continuing to evolve to meet the needs of twenty-first century faculty and students. The *Individual* and *Comprehensive* volumes followed shortly after the release of the *Corporations* volume, and the *Essentials* volume was added to the *SWFT Series* in 1997.

Over the past several months, we have heard from many former students and colleagues, who spoke of Bill's commitment to them, both in the classroom and in their lives, and to the tax profession at large. Here are a few of those comments.

- Through his writing and teaching, he was able to bring “to life” what could be a very challenging topic to many.
- The creation of the *Corporations* volume was driven by the fact that Bill needed material for his own class. This volume allowed many schools to create a second tax course and changed how accounting students prepared for a career in tax.
- Bill brought together an author team of both faculty and practitioners (both CPAs and attorneys); this created a unique tax series that emphasized both the law and its application. Over the years,

Bill consistently recruited new contributors, creating the strongest author team for business school tax texts.

- Bill was recognized in the profession as a dynamic and engaging teacher and was involved extensively in professional development seminars across the country.
- For me, Bill was many things, including professor, dissertation chair, mentor, editor, drinking buddy, and friend. One of my favorite memories of Bill is catching him at his desk, poring over a *BNA Daily Tax Report*, something he did unfailingly. I will miss our conversations and his keen tax insights.
- Bill was an innovator in the development of a new breed of textbooks that enabled professors to present taxation in a new and more relevant way. That pedagogy included especially the extensive use of teaching examples, forms problems, and advanced topics, so that the professor could tailor a course to local needs.
- Bill was a real pioneer in our field. His wit and enthusiasm were constant sources of amazement to me. He was always a mentor, and he shaped my academic career.
- He demanded excellence . . . and receiving a note affirming your work was truly something special.
- As my tax professor at LSU, Bill was the catalyst for my early development in tax research and writing. I owe a great deal of my success to Bill Hoffman's early advice, direction, and help. He was a tremendous writer, and he changed the teaching of taxation forever.
- He was a “giant” . . . he will be missed.

Although Bill loved the *SWFT Series* and the process of writing and creating its content, his first love was Bonnie, his wife of 64 years, and his family (which included five children and a number of grandchildren and great-grandchildren). Bonnie also made significant contributions to the *South-Western Federal Taxation Series* through the years (including keeping Bill “in line” as best she could). Together, they were an outstanding creative and editorial team.

We will miss Bill's sharp wit, his ability to clearly explain tax law (both verbally and in writing), the creativity he brought to his work, the scope of his tax knowledge, and his wonderful laugh. He truly enjoyed the competition created by rival textbooks, as he knew it would lead to a better *SWFT Series*. We will honor Bill by upholding the standards of excellence he demanded, as the *SWFT Series* continues to evolve.



Brief Contents

PART 1: THE WORLD OF TAXATION

CHAPTER 1	INTRODUCTION TO TAXATION	1-1
CHAPTER 2	WORKING WITH THE TAX LAW	2-1
CHAPTER 3	TAXES ON THE FINANCIAL STATEMENTS	3-1

PART 2: STRUCTURE OF THE FEDERAL INCOME TAX

CHAPTER 4	GROSS INCOME	4-1
CHAPTER 5	BUSINESS DEDUCTIONS	5-1
CHAPTER 6	LOSSES AND LOSS LIMITATIONS	6-1

PART 3: PROPERTY TRANSACTIONS

CHAPTER 7	PROPERTY TRANSACTIONS: BASIS, GAIN AND LOSS, AND NONTAXABLE EXCHANGES	7-1
CHAPTER 8	PROPERTY TRANSACTIONS: CAPITAL GAINS AND LOSSES, SECTION 1231, AND RECAPTURE PROVISIONS	8-1

PART 4: TAXATION OF INDIVIDUALS

CHAPTER 9	INDIVIDUALS AS THE TAXPAYER	9-1
CHAPTER 10	INDIVIDUALS: INCOME, DEDUCTIONS, AND CREDITS	10-1
CHAPTER 11	INDIVIDUALS AS EMPLOYEES AND PROPRIETORS	11-1

PART 5: BUSINESS ENTITIES

CHAPTER 12	CORPORATIONS: ORGANIZATION, CAPITAL STRUCTURE, AND OPERATING RULES	12-1
CHAPTER 13	CORPORATIONS: EARNINGS & PROFITS AND DISTRIBUTIONS	13-1
CHAPTER 14	PARTNERSHIPS AND LIMITED LIABILITY ENTITIES	14-1
CHAPTER 15	S CORPORATIONS	15-1

PART 6: SPECIAL BUSINESS TOPICS

CHAPTER 16	MULTIJURISDICTIONAL TAXATION	16-1
CHAPTER 17	BUSINESS TAX CREDITS AND CORPORATE ALTERNATIVE MINIMUM TAX	17-1
CHAPTER 18	COMPARATIVE FORMS OF DOING BUSINESS	18-1



Contents

Part 1: The World of Taxation

CHAPTER 1

INTRODUCTION TO TAXATION

1-1

The Big Picture: *A Typical Tax Year for a Modern Family*

THE STRUCTURE OF TAX SYSTEMS

1-4

Tax Rates

1-4

Tax Fact: *Carrying the Tax Burden*

1-5

Tax Bases

1-5

Incidence of Taxation

1-5

TYPES OF TAXES

1-6

Taxes on the Production and Sale of Goods

1-6

Global Tax Issues: *Why Is Gasoline Expensive? It Depends on Where You Live*

1-8

Employment Taxes

1-8

Taxes at Death

1-10

Gift Tax

1-11

Property Taxes

1-12

Tax Fact: *A Profile of Tax Collections*

1-13

Taxes on Privileges and Rights

1-13

Income Taxes

1-14

Tax Fact: *What Is the U.S. Tax Burden?*

1-16

Bridge Discipline: *Bridge to Political Science and Sociology*

1-17

Concept Summary: *Overview of Taxes in the United States*

1-17

Financial Disclosure Insights: *What Do You Mean by "Income" Anyway?*

1-18

INCOME TAXATION OF BUSINESS ENTITIES

1-18

Proprietorships

1-18

C Corporations

1-18

Partnerships

1-19

S Corporations

1-19

Limited Liability Companies and Limited Liability Partnerships

1-19

Dealings between Individuals and Their Business Entities

1-19

Financial Disclosure Insights: *Book-Tax Differences*

1-20

TAX PLANNING FUNDAMENTALS

1-20

Overview of Tax Planning and Ethics

1-20

A General Framework for Income Tax Planning

1-21

Tax Minimization Strategies Related to Income

1-22

Tax Minimization Strategies Related to Deductions

1-23

Tax Fact: *The Rewards of Tax Planning*

1-24

Tax Minimization Strategies Related to Tax Rates

1-24

Tax Fact: *The U.S. Federal Income Tax*

1-26

Tax Minimization Strategies Related to Credits

1-27

Thinking Outside the Framework

1-27

Bridge Discipline: *Bridge to Political Science, Economics, Sociology*

1-28

UNDERSTANDING THE FEDERAL TAX LAW

1-29

Revenue Needs

1-29

Economic Considerations

1-29

Global Tax Issues: *Outsourcing of Tax Return Preparation*

1-30

Social Considerations

1-30

Equity Considerations

1-31

Political Considerations

1-32

Influence of the Internal Revenue Service

1-33

Influence of the Courts

1-33

SUMMARY

1-33

Refocus on the Big Picture: *A Typical Tax Year for a Modern Family*

1-34

CHAPTER 2

WORKING WITH THE TAX LAW

2-1

The Big Picture: *Researching Tax Questions*

2-1

TAX LAW SOURCES

2-2

Statutory Sources of the Tax Law

2-2

Tax Fact: *Scope of the U.S. Tax System*

2-3

Administrative Sources of the Tax Law

2-6

Judicial Sources of the Tax Law

2-9

Concept Summary: *Federal Judicial System: Trial Courts*

2-11

Bridge Discipline: *Bridge to Public Policy*

2-16

WORKING WITH THE TAX LAW—TAX RESEARCH

2-17

Identifying the Problem

2-18

Refining the Problem

2-18

Locating the Appropriate Tax Law Sources

2-18

Bridge Discipline: *Bridge to Business Law*

2-19

Assessing Tax Law Sources

2-20

Arriving at the Solution or at Alternative Solutions

2-23

Communicating Tax Research

2-23

Updates

2-25

Tax Research Best Practices

2-25

Financial Disclosure Insights: *Where Does GAAP Come From?*

2-27

TAX RESEARCH ON THE CPA EXAMINATION

2-27

Bridge Discipline: *Bridge to Regulation and Oversight*

2-28

Refocus on the Big Picture: *Researching Tax Questions*

2-29

CHAPTER 3 TAXES ON THE FINANCIAL STATEMENTS 3-1

The Big Picture: *Taxes on the Financial Statements* 3-1

BOOK-TAX DIFFERENCES 3-2

Different Reporting Entities 3-2

Different Taxes 3-4

Different Methods 3-4

Financial Disclosure Insights: *Supersized Goodwill* 3-6

Tax Return Disclosures 3-6

Concept Summary: *Income Reporting: Book versus Tax* 3-7

INCOME TAXES IN THE FINANCIAL STATEMENTS 3-8

GAAP Principles 3-8

Financial Disclosure Insights: *The Book-Tax Income Gap* 3-9

Global Tax Issues: *Accounting for Income Taxes in International Standards* 3-10

Valuation Allowance 3-12

Tax Planning Strategies: *Releasing Valuation Allowances* 3-14

Tax Disclosures in the Financial Statements 3-15

Financial Disclosure Insights: *Tax Losses and the Deferred Tax Asset* 3-15

Tax Fact: *Effective Tax Rates for Fortune 100 Companies* 3-16

Concept Summary: *Steps in Determining the Book Tax Expense* 3-17

Special Issues 3-19

Tax Planning Strategies: *Tax Savings Are Not Always Created Equal* 3-20

Concept Summary: *Disclosures Under ASC 740-10 (FIN 48)* 3-20

Financial Disclosure Insights: *Corporate Tax Rate Cuts: Be Careful What You Wish For* 3-23

Tax Planning Strategies: *Reducing Effective Tax Rates with ASC 740-30 (APB 23)* 3-24

Global Tax Issues: *Cash Stashed Overseas* 3-25

Summary 3-25

BENCHMARKING 3-26

Refining the Analysis 3-26

Bridge Discipline: *Bridge to Financial Analysis* 3-26

Sustaining the Tax Rate 3-27

Uses of Benchmarking Analysis 3-28

Concept Summary: *Benchmarking Analysis* 3-28

Refocus on the Big Picture: *Taxes on the Financial Statements* 3-28

Part 2: Structure of the Federal Income Tax

CHAPTER 4 GROSS INCOME 4-1

The Big Picture: *Just What Is Included in Gross Income?* 4-1

THE TAX FORMULA 4-2

Components of the Tax Formula 4-2

Global Tax Issues: *From "All Sources" Is a Broad Definition* 4-3

GROSS INCOME—WHAT IS IT? 4-3

Concepts of Income 4-3

Financial Disclosure Insights: *What Does "Income" Mean to You?* 4-4

Comparing Accounting and Tax Concepts of Income 4-5

Form of Receipt 4-5

Concept Summary: *Gross Income Concepts* 4-6

YEAR OF INCLUSION 4-6

Taxable Year 4-6

Accounting Methods 4-6

Tax Planning Strategies: *Cash Receipts Method* 4-8

Bridge Discipline: *Bridge to Economics and Finance* 4-9

Special Rules for Cash Basis Taxpayers 4-10

Special Rules for Accrual Basis Taxpayers 4-11

Tax Planning Strategies: *Prepaid Income* 4-12

Concept Summary: *Income Tax Accounting* 4-13

INCOME SOURCES 4-13

Personal Services 4-13

Income from Property 4-13

Tax Fact: *How Much and What Type of Income?* 4-14

Global Tax Issues: *Which Foreign Dividends Get the Discounted Rate?* 4-15

Tax Fact: *Business Income and Loss* 4-16

Income Received by an Agent 4-16

Tax Planning Strategies: *Techniques for Reducing Investment Income* 4-17

SPECIFIC ITEMS OF GROSS INCOME 4-17

Gains and Losses from Property Transactions 4-18

Interest on Certain State and Local Government Obligations 4-20

Bridge Discipline: *Bridge to Public Economics* 4-20

Life Insurance Proceeds 4-21

Tax Planning Strategies: *Life Insurance* 4-22

Income from Discharge of Indebtedness 4-23

Tax Benefit Rule 4-25

Imputed Interest on Below-Market Loans 4-26

Financial Disclosure Insights: *Loans to Executives Prohibited* 4-27

Improvements on Leased Property 4-28

Concept Summary: *Income Recognition Rules* 4-29

Refocus on the Big Picture: *Just What Is Included in Gross Income?* 4-29

CHAPTER 5 BUSINESS DEDUCTIONS 5-1

The Big Picture: *Calculating Deductible Expenses* 5-1

OVERVIEW OF BUSINESS DEDUCTIONS 5-2

Ordinary and Necessary Requirement 5-2

Reasonableness Requirement 5-3

Common Business Deductions 5-3

Tax Planning Strategies: *Unreasonable Compensation* 5-4

THE TIMING OF EXPENSE RECOGNITION 5-4

Cash Method Requirements 5-4

Tax Planning Strategies: *Time Value of Tax Deductions* 5-5

Accrual Method Requirements 5-5

Expenses Accrued to Related Parties 5-6

DISALLOWANCE POSSIBILITIES	5-7	CHAPTER 6	
Public Policy Limitations	5-7	LOSSES AND LOSS LIMITATIONS	6-1
Global Tax Issues: Overseas Gun Sales Result in Large Fines	5-8	The Big Picture: Receiving Tax Benefits from Losses	6-1
Political Contributions and Lobbying Activities	5-8		
Excessive Executive Compensation	5-9	BAD DEBTS	6-2
Investigation of a Business	5-10	Specific Charge-Off Method	6-2
Transactions between Related Parties	5-11	Tax Fact: Just How Good Is Your Credit?	6-3
Expenses and Interest Related to Tax-Exempt Income	5-12	Concept Summary: The Tax Treatment of Bad Debts Using the Specific Charge-Off Method	6-3
Other Disallowance Possibilities	5-13	Business versus Nonbusiness Bad Debts	6-4
		Loans between Related Parties	6-4
RESEARCH AND EXPERIMENTAL EXPENDITURES	5-13		
Expense Method	5-13	WORTHLESS SECURITIES AND SMALL BUSINESS STOCK LOSSES	6-5
Deferral and Amortization Method	5-14	Worthless Securities	6-5
		Small Business Stock (§ 1244 Stock) Losses	6-5
DOMESTIC PRODUCTION ACTIVITIES DEDUCTION	5-14	Tax Planning Strategies: Maximizing the Benefits of Small Business (§ 1244 Stock) Losses	6-6
Calculation of the Domestic Production Activities Deduction	5-15		
Qualified Production Activities Income	5-15	CASUALTY AND THEFT LOSSES	6-6
		Definition of Casualty	6-6
OTHER BUSINESS EXPENSES	5-16	Deduction of Casualty Losses	6-7
Interest Expense	5-16	Tax Planning Strategies: Documentation of Related-Taxpayer Loans, Casualty Losses, and Theft Losses	6-8
Taxes	5-17	Definition of Theft	6-8
		Loss Measurement	6-9
CHARITABLE CONTRIBUTIONS	5-18	Casualty and Theft Losses of Individuals	6-10
Property Contributions	5-19	Concept Summary: Casualty Gains and Losses	6-11
Limitations Imposed on Charitable Contribution Deductions	5-20		
		NET OPERATING LOSSES	6-11
COST RECOVERY ALLOWANCES	5-21	Introduction	6-11
Overview	5-21	Carryback and Carryover Periods	6-12
Cost Recovery: In General	5-21		
Bridge Discipline: Bridge to Finance	5-22	THE TAX SHELTER PROBLEM	6-13
Modified Accelerated Cost Recovery System (MACRS)	5-23	Bridge Discipline: Bridge to Finance	6-14
Concept Summary: MACRS: Class Lives, Methods, and Conventions	5-24		
MACRS for Personal Property	5-24	AT-RISK LIMITATIONS	6-14
MACRS for Real Estate	5-27	Concept Summary: Calculation of At-Risk Amount	6-16
Straight-Line Election	5-27		
Election to Expense Certain Depreciable Assets (§ 179)	5-28	PASSIVE ACTIVITY LOSS LIMITS	6-16
Financial Disclosure Insights: Tax and Book Depreciation	5-31	Classification and Impact of Passive Activity Income and Loss	6-16
Additional First-Year Depreciation (Bonus Depreciation)	5-31	Taxpayers Subject to the Passive Activity Loss Rules	6-20
Using § 179 and Bonus Depreciation Effectively	5-32	Rules for Determining Passive Activities	6-21
Concept Summary: Using § 179 and Bonus Depreciation	5-33	Material Participation	6-21
Bridge Discipline: Bridge to Economics and the Business Cycle	5-33	Concept Summary: Tests to Determine Material Participation	6-22
Business and Personal Use of Automobiles and Other Listed Property	5-34	Rental Activities	6-24
Concept Summary: Listed Property Cost Recovery	5-38	Interaction of At-Risk and Passive Activity Loss Limits	6-24
Bridge Discipline: Bridge to Finance and Economics	5-38	Concept Summary: Passive Activity Loss Rules: Key Issues and Answers	6-25
Alternative Depreciation System (ADS)	5-39	Concept Summary: Treatment of Losses Subject to the At-Risk and Passive Activity Loss Limitations	6-26
		Special Rules for Real Estate	6-26
AMORTIZATION	5-39	Disposition of Passive Activities	6-29
Tax Planning Strategies: Structuring the Sale of a Business	5-40	Tax Planning Strategies: Utilizing Passive Activity Losses	6-30
		Refocus on the Big Picture: Receiving Tax Benefits from Losses	6-31
DEPLETION	5-40		
Intangible Drilling and Development Costs (IDCs)	5-40		
Depletion Methods	5-41		
Tax Planning Strategies: Switching Depletion Methods	5-42		
COST RECOVERY TABLES	5-42		
Refocus on the Big Picture: Calculating Deductible Expenses	5-46		

Part 3: Property Transactions

CHAPTER 7
PROPERTY TRANSACTIONS: BASIS, GAIN AND LOSS, AND NONTAXABLE EXCHANGES **7-1**

The Big Picture: *Calculating Basis and Recognized Gain for Property Transactions* 7-1

DETERMINATION OF GAIN OR LOSS **7-2**

Realized Gain or Loss 7-2

Concept Summary: *Realized Gain or Loss* 7-3

Bridge Discipline: *Bridge to Financial Accounting* 7-7

Recognized Gain or Loss 7-7

Concept Summary: *Realized and Recognized Gain or Loss* 7-8

Nonrecognition of Gain or Loss 7-8

BASIS CONSIDERATIONS **7-9**

Determination of Cost Basis 7-9

Gift Basis 7-11

Tax Planning Strategies: *Gift Planning* 7-12

Inherited Property 7-13

Tax Planning Strategies: *Inherited Property* 7-14

Disallowed Losses 7-14

Concept Summary: *Wash Sale Rules* 7-16

Tax Planning Strategies: *Avoiding Wash Sales* 7-16

Conversion of Property from Personal Use to Business or Income-Producing Use 7-16

Summary of Basis Adjustments 7-17

Concept Summary: *Adjustments to Basis* 7-18

GENERAL CONCEPT OF A NONTAXABLE EXCHANGE **7-19**

LIKE-KIND EXCHANGES—§ 1031 **7-20**

Tax Planning Strategies: *Like-Kind Exchanges* 7-21

Like-Kind Property 7-21

Exchange Requirement 7-22

Boot 7-22

Basis and Holding Period of Property Received 7-23

Bridge Discipline: *Bridge to Economics* 7-25

INVOLUNTARY CONVERSIONS—§ 1033 **7-26**

Involuntary Conversion Defined 7-27

Replacement Property 7-27

Concept Summary: *Involuntary Conversions: Replacement Property Tests* 7-28

Time Limitation on Replacement 7-28

Nonrecognition of Gain 7-29

Tax Planning Strategies: *Recognizing Involuntary Conversion Gains* 7-30

OTHER NONRECOGNITION PROVISIONS **7-31**

Transfer of Assets to Business Entity—§§ 351 and 721 7-31

Sale of a Principal Residence—§ 121 7-31

Refocus on the Big Picture: *Calculating Basis and Recognized Gain for Property Transactions* 7-31

CHAPTER 8
PROPERTY TRANSACTIONS: CAPITAL GAINS AND LOSSES, SECTION 1231, AND RECAPTURE PROVISIONS **8-1**

The Big Picture: *Capital Gains and Losses, § 1231 Gains and Losses, and Recapture* 8-1

GENERAL SCHEME OF TAXATION **8-2**

Concept Summary: *Recognized Gain or Loss Characteristics* 8-2

CAPITAL ASSETS **8-3**

Definition of a Capital Asset 8-3

Statutory Expansions 8-5

SALE OR EXCHANGE **8-6**

Worthless Securities and § 1244 Stock 8-6

Retirement of Corporate Obligations 8-7

Options 8-7

Concept Summary: *Options: Consequences to the Grantor and Grantee* 8-9

Patents 8-9

Franchises, Trademarks, and Trade Names 8-10

Lease Cancellation Payments 8-11

Concept Summary: *Franchises: Consequences to the Franchisor and Franchisee* 8-12

HOLDING PERIOD **8-13**

General Rules 8-13

Special Holding Period Rules 8-13

Short Sales 8-14

Tax Planning Strategies: *Timing Capital Gains* 8-15

TAX TREATMENT OF CAPITAL GAINS AND LOSSES OF NONCORPORATE TAXPAYERS **8-16**

Capital Gains 8-16

Tax Planning Strategies: *Gifts of Appreciated Securities* 8-16

Global Tax Issues: *Capital Gain Treatment in the United States and Other Countries* 8-17

Concept Summary: *Capital Gains of Noncorporate Taxpayers* 8-18

Capital Losses 8-18

Capital Gain and Loss Netting Process 8-18

Tax Planning Strategies: *Matching Gains with Losses* 8-20

Small Business Stock 8-21

TAX TREATMENT OF CAPITAL GAINS AND LOSSES OF CORPORATE TAXPAYERS **8-22**

SECTION 1231 ASSETS **8-22**

Tax Fact: *Capital Gains for the Wealthy?* 8-23

Relationship to Capital Assets 8-23

Property Included 8-24

Property Excluded 8-24

Casualty or Theft and Nonpersonal-Use Capital Assets 8-25

General Procedure for § 1231 Computation 8-25

Concept Summary: *Section 1231 Netting Procedure* 8-26

SECTION 1245 RECAPTURE **8-29**

Bridge Discipline: *Bridge to Financial Accounting* 8-30

Section 1245 Property 8-30
 Observations on § 1245 8-30

SECTION 1250 RECAPTURE 8-31
 Unrecaptured § 1250 Gain (Real Estate 25% Gain) 8-31
Concept Summary: *Comparison of § 1245 and § 1250 Depreciation Recapture* 8-32
 Additional Recapture for Corporations 8-32
Tax Planning Strategies: *Selling Depreciable Real Estate* 8-33

EXCEPTIONS TO §§ 1245 AND 1250 8-34
 Gifts 8-34
 Death 8-34
 Charitable Transfers 8-34
 Certain Nontaxable Transactions 8-34
 Like-Kind Exchanges and Involuntary Conversions 8-35

REPORTING PROCEDURES 8-35
Tax Planning Strategies: *Timing of Recapture* 8-35
Refocus on the Big Picture: *Capital Gains and Losses, § 1231 Gains and Losses, and Recapture* 8-36

Part 4: Taxation of Individuals

CHAPTER 9 9-1
INDIVIDUALS AS THE TAXPAYER 9-1
The Big Picture: *A Divided Household* 9-1

THE INDIVIDUAL TAX FORMULA 9-2
Concept Summary: *Individual Income Tax Formula* 9-2
 Components of the Tax Formula 9-2

STANDARD DEDUCTION 9-6
 Basic and Additional Standard Deduction 9-6
 Special Limitations on the Standard Deduction for Dependents 9-8

PERSONAL EXEMPTIONS 9-8

DEPENDENCY EXEMPTIONS 9-9
 Qualifying Child 9-9
Concept Summary: *Tiebreaker Rules for Claiming Qualifying Child* 9-10
 Qualifying Relative 9-11
Tax Planning Strategies: *Multiple Support Agreements and the Medical Expense Deduction* 9-14
 Other Rules for Dependency Exemptions 9-14
Tax Planning Strategies: *Problems with a Joint Return* 9-15
 Comparison of Categories for Dependency Exemptions 9-15
 Phaseout of Exemptions 9-15
Concept Summary: *Tests for Dependency Exemption* 9-16

FILING STATUS AND FILING REQUIREMENTS 9-17
 Filing Status 9-17
Bridge Discipline: *Bridge to Equity or Fairness* 9-19
Global Tax Issues: *Filing a Joint Return* 9-20
 Filing Requirements 9-20

TAX DETERMINATION 9-21
 Tax Table Method 9-21
 Tax Rate Schedule Method 9-22
Tax Planning Strategies: *Shifting Income and Deductions across Time* 9-23
 Computation of Net Taxes Payable or Refund Due 9-23
 Additional Taxes for Certain Individuals 9-24
 Kiddie Tax—Unearned Income of Children Taxed at Parents’ Rate 9-25
Tax Planning Strategies: *Income of Certain Children* 9-26

TAX RETURN FILING PROCEDURES 9-26
 Selecting the Proper Form 9-26
Tax Fact: *What Form of Tax Compliance Is Right for You?* 9-26
 The E-File Approach 9-27
 When and Where to File 9-27
 Modes of Payment 9-27
Refocus on the Big Picture: *A Divided Household* 9-27

CHAPTER 10 10-1
INDIVIDUALS: INCOME, DEDUCTIONS, AND CREDITS 10-1
The Big Picture: *The Tax Implications of Life!* 10-1

OVERVIEW OF INCOME PROVISIONS APPLICABLE TO INDIVIDUALS 10-2

SPECIFIC INCLUSIONS APPLICABLE TO INDIVIDUALS 10-2
Bridge Discipline: *Bridge to Economics and Finance* 10-3
 Alimony and Separate Maintenance Payments 10-3
 Prizes and Awards 10-5
 Unemployment Compensation 10-5
 Social Security Benefits 10-5

SPECIFIC EXCLUSIONS APPLICABLE TO INDIVIDUALS 10-5
 Gifts and Inheritances 10-6
 Scholarships 10-6
 Damages 10-8
Concept Summary: *Taxation of Damages* 10-9
 Workers’ Compensation 10-9
 Accident and Health Insurance Benefits 10-9
 Educational Savings Bonds 10-10

ITEMIZED DEDUCTIONS 10-10
 Medical Expenses 10-11
 Taxes 10-15
Tax Planning Strategies: *Timing the Payment of Deductible Taxes* 10-16
 Interest 10-16
Concept Summary: *Deductibility of Personal, Student Loan, Investment, and Mortgage Interest* 10-20
 Charitable Contributions 10-20
Global Tax Issues: *Choose the Charity Wisely* 10-22
Concept Summary: *Determining the Deduction for Contributions of Appreciated Property by Individuals* 10-23
 Miscellaneous Itemized Deductions Subject to 2 Percent Floor 10-24

Other Miscellaneous Deductions	10-25	Entertainment Expenses	11-26
Overall Limitation on Certain Itemized Deductions	10-25	Tax Planning Strategies: <i>Entertainment Expenses</i>	11-27
Tax Planning Strategies: <i>Effective Utilization of Itemized Deductions</i>	10-26	Other Employee Expenses	11-28
INDIVIDUAL TAX CREDITS	10-27	Classification of Employee Expenses	11-31
Adoption Expenses Credit	10-27	Tax Planning Strategies: <i>Unreimbursed Employee Business Expenses</i>	11-32
Child Tax Credit	10-27	Contributions to Individual Retirement Accounts	11-32
Credit for Child and Dependent Care Expenses	10-28	Concept Summary: <i>Traditional IRAs and Roth IRAs Compared</i>	11-35
Education Tax Credits	10-30	INDIVIDUALS AS PROPRIETORS	11-35
Earned Income Credit	10-31	Income of a Proprietorship	11-36
AFFORDABLE CARE ACT PROVISIONS	10-32	Deductions Related to a Proprietorship	11-36
Individual Shared Responsibility Payment	10-32	Retirement Plans for Self-Employed Individuals	11-37
Premium Tax Credit	10-32	Tax Planning Strategies: <i>Important Dates Related to IRAs and Keogh Plans</i>	11-38
Refocus on the Big Picture: <i>The Tax Implications of Life!</i>	10-33	Tax Planning Strategies: <i>Factors Affecting Retirement Plan Choices</i>	11-39
CHAPTER 11		Accounting Periods and Methods	11-39
INDIVIDUALS AS EMPLOYEES AND PROPRIETORS	11-1	Estimated Tax Payments	11-39
The Big Picture: <i>Self-Employed versus Employee—What’s the Difference?</i>	11-1	HOBBY LOSSES	11-40
EMPLOYEE VERSUS SELF-EMPLOYED	11-2	General Rules	11-41
Factors Considered in Classification	11-2	Presumptive Rule of Profit-Seeking	11-41
Bridge Discipline: <i>Bridge to Equity or Fairness and Business Law</i>	11-3	The Deductible Amount	11-42
Tax Planning Strategies: <i>Self-Employed Individuals</i>	11-4	Refocus on the Big Picture: <i>Self-Employed versus Employee—What’s the Difference?</i>	11-43
EXCLUSIONS AVAILABLE TO EMPLOYEES	11-4	Part 5: Business Entities	
Employer-Sponsored Accident and Health Plans	11-5	CHAPTER 12	
Medical Reimbursement Plans	11-5	CORPORATIONS: ORGANIZATION, CAPITAL STRUCTURE, AND OPERATING RULES	12-1
Bridge Discipline: <i>Bridge to Economic and Societal Needs</i>	11-6	The Big Picture: <i>Growing into the Corporate Form</i>	12-1
Long-Term Care Insurance Benefits	11-6	AN INTRODUCTION TO CORPORATE TAX	12-2
Meals and Lodging Furnished for the Convenience of the Employer	11-7	Double Taxation of Corporate Income	12-2
Group Term Life Insurance	11-8	Global Tax Issues: <i>Choice of Organizational Form When Operating Overseas</i>	12-3
Qualified Tuition Reduction Plans	11-9	Comparison of Corporations and Other Forms of Doing Business	12-3
Other Employee Fringe Benefits	11-9	Tax Fact: <i>Corporations’ Reporting Responsibilities</i>	12-4
Cafeteria Plans	11-10	Bridge Discipline: <i>Bridge to Finance</i>	12-5
Flexible Spending Plans	11-11	Concept Summary: <i>Tax Treatment of Business Forms Compared</i>	12-6
Concept Summary: <i>Employee Fringe Benefits</i>	11-11	Nontax Considerations	12-7
General Classes of Excluded Benefits	11-11	Limited Liability Companies	12-7
Concept Summary: <i>General Classes of Fringe Benefits</i>	11-15	Entity Classification	12-7
Foreign Earned Income	11-16	ORGANIZATION OF AND TRANSFERS TO CONTROLLED CORPORATIONS	12-8
EMPLOYEE EXPENSES	11-17	Section 351 Rationale and General Rules	12-8
Transportation Expenses	11-17	Concept Summary: <i>Shareholder Consequences: Taxable Corporate Formation versus Tax-Deferred § 351 Transaction</i>	12-10
Travel Expenses	11-18	Transfer of Property	12-10
Moving Expenses	11-20	Stock	12-11
Tax Planning Strategies: <i>Transportation and Travel Expenses</i>	11-21	Control of the Corporation	12-12
Concept Summary: <i>Meeting and Not Meeting the Distance Test</i>	11-21	Tax Planning Strategies: <i>Utilizing § 351</i>	12-13
Global Tax Issues: <i>Expatriates and the Moving Expense Deduction</i>	11-22	Assumption of Liabilities—§ 357	12-15
Tax Planning Strategies: <i>Moving Expenses</i>	11-23		
Education Expenses	11-23		
Tax Planning Strategies: <i>Education Expenses</i>	11-24		
Targeted Tuition Deduction	11-25		

Global Tax Issues: <i>Does § 351 Cover the Incorporation of a Foreign Business?</i>	12-16	CONSTRUCTIVE DIVIDENDS	13-16
Concept Summary: <i>Tax Consequences of Liability Assumption</i>	12-18	Types of Constructive Dividends	13-17
Tax Planning Strategies: <i>Avoiding § 351</i>	12-19	Global Tax Issues: <i>A Worldwide View of Dividends</i>	13-18
Basis Determination and Other Issues	12-19	Tax Treatment of Constructive Dividends	13-18
Recapture Considerations	12-24	Tax Planning Strategies: <i>Constructive Dividends</i>	13-19
Tax Planning Strategies: <i>Other Considerations When Incorporating a Business</i>	12-24	STOCK DIVIDENDS	13-21
CAPITAL STRUCTURE OF A CORPORATION	12-25	STOCK REDEMPTIONS	13-22
Capital Contributions	12-25	Bridge Discipline: <i>Bridge to Finance</i>	13-22
Debt in the Capital Structure	12-26	Global Tax Issues: <i>Non-U.S. Shareholders Prefer Capital Gain Treatment in Stock Redemptions</i>	13-23
CORPORATE OPERATIONS	12-28	Tax Planning Strategies: <i>Stock Redemptions</i>	13-24
Deductions Available Only to Corporations	12-28	CORPORATE LIQUIDATIONS	13-24
Tax Planning Strategies: <i>Organizational Expenditures</i>	12-32	The Liquidation Process	13-24
Determining the Corporate Income Tax Liability	12-32	Liquidating and Nonliquidating Distributions Compared	13-24
Tax Liability of Related Corporations	12-33	Tax Planning Strategies: <i>Corporate Liquidations</i>	13-25
Controlled Groups	12-33	RESTRICTIONS ON CORPORATE ACCUMULATIONS	13-25
PROCEDURAL MATTERS	12-35	Refocus on the Big Picture: <i>Taxing Corporate Distributions</i>	13-26
Filing Requirements for Corporations	12-35	CHAPTER 14	
Estimated Tax Payments	12-35	PARTNERSHIPS AND LIMITED LIABILITY ENTITIES	14-1
Schedule M-1—Reconciliation of Income (Loss) per Books with Income per Return	12-35	The Big Picture: <i>The Tax Consequences of Partnership Formation and Operations</i>	14-1
Concept Summary: <i>Conceptual Diagram of Schedule M-1 (Form 1120)</i>	12-36	OVERVIEW OF PARTNERSHIP TAXATION	14-2
Schedule M-2—Analysis of Unappropriated Retained Earnings per Books	12-37	Forms of Doing Business—Federal Tax Consequences	14-2
Bridge Discipline: <i>Bridge to Financial Accounting</i>	12-38	Tax Fact: <i>Partnership Power</i>	14-3
Schedule M-3—Net Income (Loss) Reconciliation for Corporations with Total Assets of \$10 Million or More	12-38	Definition of a Partnership	14-3
Effect of Taxes on Financial Statements	12-38	Bridge Discipline: <i>Bridge to Finance</i>	14-4
Refocus on the Big Picture: <i>Growing into the Corporate Form</i>	12-39	Partnership Taxation and Reporting	14-4
		Partner's Ownership Interest in a Partnership	14-6
		Bridge Discipline: <i>Bridge to Business Law</i>	14-7
CHAPTER 13		FORMATION OF A PARTNERSHIP: TAX EFFECTS	14-8
CORPORATIONS: EARNINGS & PROFITS AND DISTRIBUTIONS	13-1	Gain or Loss on Contributions to the Partnership	14-8
The Big Picture: <i>Taxing Corporate Distributions</i>	13-1	Concept Summary: <i>Partnership/LLC Taxation</i>	14-9
CORPORATE DISTRIBUTIONS—OVERVIEW	13-2	Exceptions to Nonrecognition	14-9
EARNINGS AND PROFITS (E & P)	13-2	Tax Issues Related to Contributed Property	14-11
Tax Fact: <i>Who Pays Dividends?</i>	13-3	Inside and Outside Bases	14-12
Computation of E & P	13-3	Tax Accounting Elections	14-12
Summary of E & P Adjustments	13-7	Concept Summary: <i>Partnership Formation and Basis Computation</i>	14-13
Allocating E & P to Distributions	13-7	Initial Costs of a Partnership	14-13
Concept Summary: <i>Computing E & P</i>	13-8	OPERATIONS OF THE PARTNERSHIP	14-15
Bridge Discipline: <i>Bridge to Finance</i>	13-11	Schedules K and K-1	14-15
Tax Planning Strategies: <i>Corporate Distributions</i>	13-11	Global Tax Issues: <i>Withholding Procedures Apply to Foreign Partners</i>	14-18
Concept Summary: <i>Allocating E & P to Distributions</i>	13-13	Partnership Allocations	14-18
Bridge Discipline: <i>Bridge to Investments</i>	13-13	Concept Summary: <i>Tax Reporting of Partnership Activities</i>	14-19
NONCASH DIVIDENDS	13-13	Basis of a Partnership Interest	14-20
Noncash Dividends—Effect on the Shareholder	13-14	Bridge Discipline: <i>Bridge to Financial Accounting</i>	14-21
Noncash Dividends—Effect on the Corporation	13-14	Tax Fact: <i>What Do Partnerships Do?</i>	14-22
Bridge Discipline: <i>Bridge to Finance</i>	13-16	Partner's Basis, Gain, and Loss	14-23

Loss Limitations 14-25
Tax Planning Strategies: *Make Your Own Tax Shelter* 14-26
Concept Summary: *Partner's Basis in Partnership Interest* 14-28

TRANSACTIONS BETWEEN PARTNER AND PARTNERSHIP 14-28
 Guaranteed Payments 14-28
 Other Transactions between a Partner and a Partnership 14-29
 Partners as Employees 14-30
Tax Planning Strategies: *Transactions between Partners and Partnerships* 14-31
Concept Summary: *Partner-Partnership Transactions* 14-31

LIMITED LIABILITY COMPANIES 14-32
 Taxation of LLCs 14-32
 Advantages of an LLC 14-32
 Disadvantages of an LLC 14-33
Concept Summary: *Advantages and Disadvantages of the Partnership Form* 14-33

SUMMARY 14-34
Refocus on the Big Picture: *The Tax Consequences of Partnership Formation and Operations* 14-34

CHAPTER 15 S CORPORATIONS 15-1
The Big Picture: *Converting a C Corporation to an S Corporation* 15-1

AN OVERVIEW OF S CORPORATIONS 15-2

QUALIFYING FOR S CORPORATION STATUS 15-3
 Definition of a Small Business Corporation 15-3
Bridge Discipline: *Bridge to Business Law* 15-3
Tax Planning Strategies: *When to Elect S Corporation Status* 15-4
Tax Fact: *The Business of S Corporations* 15-5
Tax Planning Strategies: *Beating the 100-Shareholder Limit* 15-6
 Making the Election 15-6
 Shareholder Consent 15-7
Tax Planning Strategies: *Making a Proper Election* 15-7
 Loss of the Election 15-7
Tax Planning Strategies: *Preserving the S Election* 15-9

OPERATIONAL RULES 15-10
 Computation of Taxable Income 15-10
 Allocation of Income and Loss 15-12
Tax Fact: *A "Small" Business Corporation* 15-13
 Tax Treatment of Distributions to Shareholders 15-13
Tax Planning Strategies: *Salary Structure* 15-14
Tax Planning Strategies: *The Accumulated Adjustments Account* 15-18
Concept Summary: *Distributions from an S Corporation* 15-18
 Tax Treatment of Noncash Distributions by the Corporation 15-18
 Shareholder's Basis in S Stock 15-19
Concept Summary: *Consequences of Noncash Distributions* 15-20
Tax Planning Strategies: *Working with Suspended Losses* 15-22
 Treatment of Losses 15-22

Tax Planning Strategies: *Loss Considerations* 15-23
Concept Summary: *Treatment of S Corporation Losses* 15-24
 Other Operational Rules 15-24
Bridge Discipline: *Bridge to Public Finance* 15-25

ENTITY-LEVEL TAXES 15-26
 Tax on Pre-Election Built-In Gain 15-26
Tax Planning Strategies: *Managing the Built-In Gains Tax* 15-27
Tax Fact: *No Double Taxation?* 15-28
 Passive Investment Income Penalty Tax 15-28
Tax Fact: *The S Corporation Economy* 15-29
Tax Planning Strategies: *Avoid PII Pitfalls* 15-29

SUMMARY 15-30
Refocus on the Big Picture: *Converting a C Corporation to an S Corporation* 15-30

Part 6: Special Business Topics

CHAPTER 16 MULTIJURISDICTIONAL TAXATION 16-1
The Big Picture: *Going International* 16-1

THE MULTIJURISDICTIONAL TAXPAYER 16-2

U.S. TAXATION OF MULTINATIONAL TRANSACTIONS 16-2
Bridge Discipline: *Bridge to International Law* 16-3
 Sources of Law 16-5
 Tax Issues 16-5
Tax Fact: *U.S. Income Tax Treaties in Force* 16-6
Tax Fact: *Where Do We Stand?* 16-8
Global Tax Issues: *Deferral and Repatriation* 16-9
Tax Planning Strategies: *Sourcing Income from Sales of Inventory* 16-9
Tax Fact: *Corporate Use of the Foreign Tax Credit* 16-10
Tax Planning Strategies: *Utilizing the Foreign Tax Credit* 16-11
Financial Disclosure Insights: *Overseas Operations and Book-Tax Differences* 16-14
Tax Planning Strategies: *Avoiding Constructive Dividends* 16-17
Tax Fact: *The Inbound Sector* 16-18
Financial Disclosure Insights: *Tax Rates in Non-U.S. Jurisdictions* 16-19
Concept Summary: *U.S. Income Tax Treatment of a Non-U.S. Person's Income* 16-19

CROSSING STATE LINES: STATE AND LOCAL INCOME TAXATION IN THE UNITED STATES 16-19
Tax Fact: *State Tax Revenue Sources* 16-20
 Sources of Law 16-20
 Tax Issues 16-21
Tax Planning Strategies: *Nexus: To Have or Have Not* 16-23
Financial Disclosure Insights: *State/Local Taxes and the Tax Expense* 16-26
Concept Summary: *Corporate Multistate Income Taxation* 16-26

Tax Planning Strategies: Where Should My Income Go?	16-27		
COMMON CHALLENGES	16-27		
Authority to Tax	16-27		
Bridge Discipline: <i>Bridge to Cost Accounting and Executive Compensation</i>	16-28		
Division of Income	16-28		
Transfer Pricing	16-28		
Bridge Discipline: <i>Bridge to Economic Development and Political Science</i>	16-29		
Tax Havens	16-29		
Interjurisdictional Agreements	16-30		
Refocus on the Big Picture: <i>Going International</i>	16-30		
CHAPTER 17			
BUSINESS TAX CREDITS AND CORPORATE ALTERNATIVE MINIMUM TAX	17-1		
The Big Picture: <i>Dealing with Tax Credits and the AMT</i>	17-1		
BUSINESS-RELATED TAX CREDIT PROVISIONS	17-2		
General Business Credit	17-2		
Tax Fact: <i>Where Have All the Credits Gone?</i>	17-3		
Tax Credit for Rehabilitation Expenditures	17-4		
Bridge Discipline: <i>Bridge to Finance</i>	17-5		
Work Opportunity Tax Credit	17-6		
Research Activities Credit	17-7		
Energy Credits	17-9		
Disabled Access Credit	17-9		
Credit for Small Employer Pension Plan Startup Costs	17-9		
Credit for Employer-Provided Child Care	17-10		
Global Tax Issues: <i>Sourcing Income in Cyberspace—Getting It Right When Calculating the Foreign Tax Credit</i>	17-11		
Foreign Tax Credit	17-11		
Small Employer Health Insurance Credit	17-12		
Concept Summary: <i>Tax Credits</i>	17-12		
CORPORATE ALTERNATIVE MINIMUM TAX	17-13		
The AMT Formula	17-14		
An Overview of Corporate Adjustments and Preferences	17-15		
AMT Adjustments	17-16		
AMT Preferences	17-21		
Tax Planning Strategies: <i>Avoiding Preferences and Adjustments</i>	17-22		
Adjusted Current Earnings (ACE)	17-23		
Concept Summary: <i>Determining the ACE Adjustment</i>	17-24		
Concept Summary: <i>How Various Transactions Affect ACE and E & P</i>	17-25		
Alternative Tax Net Operating Loss Deduction	17-26		
Computation of Alternative Minimum Taxable Income	17-27		
Tax Planning Strategies: <i>Optimum Use of the AMT and Regular Corporate Income Tax Rate Difference</i>	17-27		
Tax Planning Strategies: <i>Controlling the Timing of Preferences and Adjustments</i>	17-28		
AMT Rate and Exemption	17-28		
Minimum Tax Credit	17-28		
Other Aspects of the AMT	17-29		
Tax Planning Strategies: <i>The S Corporation Option</i>	17-29		
INDIVIDUAL ALTERNATIVE MINIMUM TAX	17-29		
Refocus on the Big Picture: <i>Dealing with Tax Credits and the AMT</i>	17-30		
		CHAPTER 18	
		COMPARATIVE FORMS OF DOING BUSINESS	18-1
		The Big Picture: <i>Choosing a Business Form and Other Investments</i>	18-1
		FORMS OF DOING BUSINESS	18-2
		NONTAX FACTORS AFFECTING THE CHOICE OF BUSINESS FORM	18-2
		Limited Liability	18-3
		Tax Fact: <i>Revenue Relevance of Corporate versus Individual Taxpayers</i>	18-4
		Other Factors	18-4
		Capital Formation	18-4
		THE CONDUIT AND ENTITY PERSPECTIVES OF LEGAL BUSINESS FORMS	18-5
		Effect on the Taxation of Business Operations	18-5
		Global Tax Issues: <i>Do Corporations Pay Taxes?</i>	18-5
		Tax Planning Strategies: <i>Planning for the AMT</i>	18-6
		Effect on the Ability to Specially Allocate Income among Owners	18-7
		Effect on the Tax Treatment of Capital Contributions	18-7
		Tax Fact: <i>Profitability of Partnerships</i>	18-8
		Effect on the Basis of an Ownership Interest	18-8
		Bridge Discipline: <i>Bridge to Business Law and Financial Accounting</i>	18-9
		Effect on the Application of the At-Risk and Passive Activity Loss Rules	18-9
		Effect on the Tax Treatment of Distributions	18-11
		Effect on Other Taxes	18-11
		MINIMIZING DOUBLE TAXATION	18-12
		Making Deductible Distributions	18-12
		Deferring Distributions	18-13
		Making Return-of-Capital Distributions	18-14
		Electing S Corporation Status	18-14
		Tax Fact: <i>Income Tax Returns Filed by Business Entities</i>	18-14
		Bridge Discipline: <i>Bridge to Economics</i>	18-15
		DISPOSING OF A BUSINESS	18-15
		Sole Proprietorships	18-16
		Partnerships and Limited Liability Companies	18-16
		C Corporations	18-17
		Tax Planning Strategies: <i>Selling Stock or Assets</i>	18-18
		S Corporations	18-18
		Concept Summary: <i>Tax Treatment of Disposition of a Business</i>	18-19
		CONVERSION TO OTHER ENTITY TYPES	18-20
		Sole Proprietorship	18-20
		C Corporation	18-21
		Partnership	18-21
		OVERALL COMPARISON OF BUSINESS FORMS	18-21
		Concept Summary: <i>Tax Attributes of Different Forms of Doing Business (Assume That Partners and Shareholders Are All Individuals)</i>	18-22
		Refocus on the Big Picture: <i>Choosing a Business Form and Other Investments</i>	18-25

APPENDIXES

TAX RATE SCHEDULES AND TABLES	A-1
TAX FORMS	B-1
GLOSSARY	C-1
TABLE OF CODE SECTIONS CITED	D-1
TABLE OF REGULATIONS CITED	D-8
TABLE OF REVENUE PROCEDURES AND REVENUE RULINGS CITED	D-11

TABLE OF CASES CITED	E-1
PRESENT VALUE AND FUTURE VALUE TABLES	F-1
TAX FORMULAS	G-1
INDEX	I-1

Online Appendixes

DEPRECIATION AND THE ACCELERATED COST RECOVERY SYSTEM (ACRS)
AFFORDABLE CARE ACT PROVISIONS



PART

1

THE WORLD OF TAXATION

CHAPTER 1

Introduction to Taxation

CHAPTER 2

Working with the Tax Law

CHAPTER 3

Taxes on the Financial Statements

Part 1 provides an introduction to taxation in the United States. Various taxes imposed by Federal, state, and local governments are discussed. A unique tax planning framework is presented that is applied throughout the book in developing tax planning strategies for both business entities and individual taxpayers. The tax research process, including the relevance of the legislative, administrative, and judicial sources of the tax law, is also discussed. Part 1 concludes with a chapter on accounting for income taxes, as a bridge to materials discussed in other accounting courses and an introduction to the financial disclosure effects of the tax law.

Introduction to Taxation

LEARNING OBJECTIVES: *After completing Chapter 1, you should be able to:*

- | | |
|---|---|
| <p>LO.1 Define and illustrate the components of a tax.</p> <p>LO.2 Identify the various taxes affecting business entities and individuals.</p> <p>LO.3 Describe the basic tax formula for individuals and taxable business entities.</p> <p>LO.4 Identify and explain the tax systems that apply to business entities and their owners.</p> | <p>LO.5 Identify tax planning opportunities and apply a general framework for tax planning.</p> <p>LO.6 Explain the economic, social, equity, and political considerations that underlie the tax law.</p> <p>LO.7 Describe the role played by the IRS and the courts in the evolution of the Federal tax system.</p> |
|---|---|

CHAPTER OUTLINE

1-1 The Structure of Tax Systems, 1-4

- 1-1a Tax Rates, 1-4
- 1-1b Tax Bases, 1-5
- 1-1c Incidence of Taxation, 1-5

1-2 Types of Taxes, 1-6

- 1-2a Taxes on the Production and Sale of Goods, 1-6
- 1-2b Employment Taxes, 1-8
- 1-2c Taxes at Death, 1-10
- 1-2d Gift Tax, 1-11
- 1-2e Property Taxes, 1-12
- 1-2f Taxes on Privileges and Rights, 1-13
- 1-2g Income Taxes, 1-14

1-3 Income Taxation of Business Entities, 1-18

- 1-3a Proprietorships, 1-18
- 1-3b C Corporations, 1-18
- 1-3c Partnerships, 1-19
- 1-3d S Corporations, 1-19
- 1-3e Limited Liability Companies and Limited Liability Partnerships, 1-19
- 1-3f Dealings between Individuals and Their Business Entities, 1-19

1-4 Tax Planning Fundamentals, 1-20

- 1-4a Overview of Tax Planning and Ethics, 1-20
- 1-4b A General Framework for Income Tax Planning, 1-21
- 1-4c Tax Minimization Strategies Related to Income, 1-22
- 1-4d Tax Minimization Strategies Related to Deductions, 1-23
- 1-4e Tax Minimization Strategies Related to Tax Rates, 1-24
- 1-4f Tax Minimization Strategies Related to Credits, 1-27
- 1-4g Thinking Outside the Framework, 1-27

1-5 Understanding the Federal Tax Law, 1-29

- 1-5a Revenue Needs, 1-29
- 1-5b Economic Considerations, 1-29
- 1-5c Social Considerations, 1-30
- 1-5d Equity Considerations, 1-31
- 1-5e Political Considerations, 1-32
- 1-5f Influence of the Internal Revenue Service, 1-33
- 1-5g Influence of the Courts, 1-33

1-6 Summary, 1-33

TAX TALK *How many people were taxed, who was taxed, and what was taxed tell more about a society than anything else.* —CHARLES ADAMS