This International Student Edition is for use outside of the U.S.

EVERGREEN RELEASE

McGRAW HILL'S ESSENTIALS OF FEDERAL TAXATION

2027

McGraw Hill

SPILKER ★ AYERS ★ BARRICK
LEWIS ★ ROBINSON ★ WEAVER ★ WORSHAM

McGraw Hill's

Essentials of Federal Taxation

2027

Brian C. Spilker
Brigham Young University
Editor

Benjamin C. Ayers
The University of Georgia

Troy K. Lewis
Brigham Young University

Connie D. Weaver
Texas A&M University

John A. Barrick
Brigham Young University

John R. Robinson
Texas A&M University

Ron G. Worsham
Brigham Young University

Mc Graw Hill

McGRAW HILL'S ESSENTIALS OF FEDERAL TAXATION 2027

Published by McGraw Hill LLC, 1325 Avenue of the Americas, New York, NY 10019.

This book is printed on acid-free paper.

$PrintCode

ISBN 978-1-265-89134-3
MHID 1-265-89134-6

Cover Image: *BNMK 0819/Shutterstock*

mheducation.com/highered

About the Authors

Brian C. Spilker (PhD, University of Texas at Austin, 1993) is the Robert Call/Deloitte Professor in the School of Accountancy at Brigham Young University. He teaches taxation at Brigham Young University. He received both BS (Summa Cum Laude) and MAcc (tax emphasis) degrees from Brigham Young University before working as a tax consultant for Arthur Young & Co. (now Ernst & Young). After his professional work experience, Brian earned his PhD at the University of Texas at Austin. He received the Price Waterhouse Fellowship in Tax Award and the American Taxation Association and Arthur Andersen Teaching Innovation Award for his work in the classroom. Brian has also been awarded for his use of technology in the classroom at Brigham Young University. Brian researches issues relating to tax information search, professional tax judgment, and taxpayer compliance. His research has been published in journals such as *The Accounting Review, Journal of Business Ethics, Organizational Behavior and Human Decision Processes, Journal of the American Taxation Association, Behavioral Research in Accounting, Issues in Accounting Education, Accounting Horizons, Journal of Accounting Education, Journal of Corporate Taxation, Journal of Accountancy,* and *The Tax Adviser*.

Brian Spilker

Ben Ayers (PhD, University of Texas at Austin, 1996) holds the Earl Davis Chair in Taxation and is the senior vice president for academic affairs and provost of the University of Georgia. He received a PhD from the University of Texas at Austin and an MTA and BS from the University of Alabama. Prior to entering the PhD program at the University of Texas, Ben was a tax manager at KPMG in Tampa, Florida, and a contract manager with Complete Health, Inc., in Birmingham, Alabama. He is the recipient of 11 teaching awards at the school, college, and university levels, including the Richard B. Russell Undergraduate Teaching Award, the highest teaching honor for University of Georgia junior faculty members. His research interests include the effects of taxation on firm structure, mergers and acquisitions, and capital markets and the effects of accounting information on security returns. He has published articles in journals such as *The Accounting Review, Journal of Finance, Journal of Accounting and Economics, Contemporary Accounting Research, Review of Accounting Studies, Journal of Law and Economics, Journal of the American Taxation Association,* and *National Tax Journal*. Ben was the 1997 recipient of the American Accounting Association's Competitive Manuscript Award, the 2003 and 2008 recipient of the American Taxation Association's Outstanding Manuscript Award, and the 2016 recipient of the American Taxation Association's Ray M. Sommerfeld Outstanding Tax Educator Award.

Benjamin Ayers

John Barrick (PhD, University of Nebraska at Lincoln, 1998) is currently an associate professor in the Marriott School at Brigham Young University. He served as an accountant at the U.S. Congress Joint Committee on Taxation during the 110th and 111th Congresses. He teaches taxation in the graduate and undergraduate programs at Brigham Young University. He received both BS and MAcc (tax emphasis) degrees from Brigham Young University before working as a tax consultant for Price Waterhouse (now PwC). After his professional work experience, John earned his PhD at the University of Nebraska at Lincoln. He was the 1998 recipient of the American Accounting Association, Accounting, Behavior, and Organization Section's Outstanding Dissertation Award. John researches issues relating to tax corporate political activity. His research has been published in journals such as *Organizational Behavior and Human Decision Processes, Contemporary Accounting Research,* and *Journal of the American Taxation Association*.

John Barrick

Troy K Lewis

Troy K. Lewis (CPA, CGMA, MAcc, Brigham Young University, 1995) is a teaching professor in and Associate Director of the School of Accountancy at Brigham Young University—Marriott School of Business. He teaches graduate and undergraduate courses in introductory taxation, property transactions, pass-through entity taxation, advanced individual taxation, and accounting for income taxes. He is the past chair of the Tax Executive Committee of the American Institute of CPAs (AICPA) in Washington, D.C., as well as the president of the Utah Association of CPAs (UACPA). He has testified six times before the U.S. Senate Finance Committee and the House Committee on Small Business. Prior to joining the faculty at BYU, he was a tax manager at Arthur Andersen and KPMG in Salt Lake City, Utah. In addition, he was employed for over a decade as the CERMO and Tax Director of Heritage Bank in St. George, Utah. He is the recipient of the AICPA Arthur J. Dixon Memorial Award and the Tax Section Distinguished Service Award, the BYU Marriott Ethics Teaching Award, and the UACPA Distinguished Service Award. Troy researches and publishes in professional tax journals in the areas of individual and pass-through taxation, qualified business income deduction, and property transactions as well as professional tax practice standards. His work has been published in journals such as *Practical Tax Strategies, Journal of Accountancy, Issues in Accounting Education,* and *The Tax Adviser*.

John Robinson

John Robinson (PhD, University of Michigan, 1981) is the Patricia '77 and Grant E. Sims '77 Eminent Scholar Chair in Business. Prior to joining the faculty at Texas A&M, John was the C. Aubrey Smith Professor of Accounting at the University of Texas at Austin, Texas, and he taught at the University of Kansas, where he was the Arthur Young Faculty Scholar. In 2009–2010 John served as the Academic Fellow in the Division of Corporation Finance at the Securities and Exchange Commission. He was the recipient of the Henry A. Bubb Award for outstanding teaching, the Texas Blazers Faculty Excellence Award, and the MPA Council Outstanding Professor Award. John also received the 2012 Outstanding Service Award from the American Taxation Association (ATA) and in 2017 was named the Ernst & Young and ATA Ray Sommerfeld Outstanding Educator. John served as the 2015–2016 president of the ATA. John conducts research in a broad variety of topics involving financial accounting, mergers and acquisitions, and the influence of taxes on financial structures and performance. His scholarly articles have appeared in *The Accounting Review, The Journal of Accounting and Economics, Journal of Finance, National Tax Journal, Journal of Law and Economics, Journal of the American Taxation Association, The Journal of the American Bar Association,* and *The Journal of Taxation*. John's research was honored with the 2003 and 2008 ATA Outstanding Manuscript Awards. In addition, John was the editor of *The Journal of the American Taxation Association* from 2002 to 2005 and served on the editorial board of *The Accounting Review*. Professor Robinson received his JD (*Cum Laude*) from the University of Michigan in 1979, and he teaches courses on individual and corporate taxation and advanced accounting.

Connie Weaver (PhD, Arizona State University, 1997) is a Professor Emerita of Accounting at Texas A&M University. She received a PhD from Arizona State University, an MPA from the University of Texas at Arlington, and a BS (chemical engineering) from the University of Texas at Austin. Prior to entering the PhD program, Connie was a tax manager at Ernst & Young in Dallas, Texas, where she became licensed to practice as a CPA. She taught taxation in the Professional Program in Accounting at Texas A&M University. She also taught undergraduate and graduate students at the University of Wisconsin–Madison and the University of Texas at Austin. She is the recipient of several teaching awards, including the American Taxation Association/Deloitte Teaching Innovations Award, the David and Denise Baggett Teaching Award, and the college and university level Association of Former Students Distinguished Achievement Award in teaching. In 2024, Connie was named the Ernst & Young and ATA Ray Sommerfeld Outstanding Educator. Connie's research interests include the effects of tax and financial incentives on corporate decisions and reporting. She has published articles in journals such as *The Accounting Review, Contemporary Accounting Research, Journal of the American Taxation Association, National Tax Journal, Accounting Horizons, Journal of Corporate Finance,* and *Tax Notes*. Connie served as an editor of *The Accounting Review* (2020–2023), as the senior editor of *The Journal of the American Taxation Association* (2017–2020), and on the editorial boards of *The Accounting Review, Contemporary Accounting Research, The Journal of the American Taxation Association,* and *Issues in Accounting Education*.

Connie Weaver

Ron Worsham (PhD, University of Florida, 1994) is a Professor Emeritus in the School of Accountancy at Brigham Young University. He taught taxation in the undergraduate and graduate programs at Brigham Young University. He also taught as a visiting professor at the University of Chicago. He received both BS and MAcc (tax emphasis) degrees from Brigham Young University before working as a tax consultant for Arthur Young & Co. (now Ernst & Young) in Dallas, Texas. While in Texas, he became licensed to practice as a CPA. After his professional work experience, Ron earned his PhD at the University of Florida. He has been honored for outstanding innovation in the classroom at Brigham Young University. Ron has published academic research in the areas of taxpayer compliance and professional tax judgment. He has also published legal research in a variety of areas. His work has been published in journals such as *Journal of the American Taxation Association, The Journal of International Taxation, The Tax Executive, Tax Notes, The Journal of Accountancy,* and *Practical Tax Strategies*.

Ron Worsham

TEACHING THE CODE IN CONTEXT

The bold, innovative approach used by McGraw Hill's Taxation *series has become the most popular choice of course materials among instructors and students—a remarkable achievement. It's apparent why the clear, organized, and engaging delivery of content, paired with the most current and robust tax code updates, has been adopted by more than 650 schools across the country.*

McGraw Hill's Taxation is designed to provide a unique, innovative, and engaging learning experience for students studying taxation. The breadth of the topical coverage, **the storyline approach to presenting the material,** the emphasis on the tax and nontax consequences of multiple parties involved in transactions, and the integration of financial and tax accounting topics make this book ideal for the modern tax curriculum.

> "Do you want the best tax text? This is the one to use. It has a storyline in each chapter that can relate to real life issues."
>
> Leslie A. Mostow
> – University of Maryland—College Park

> "This text provides broad coverage of important topics and does so in a manner that is easy for students to understand. The material is very accessible for students."
>
> Kyle Post
> – Tarleton State University

Since the first manuscript was written in 2005, 450 professors have contributed 500 book reviews, in addition to 30 focus groups and symposia. Throughout this preface, their comments on the book's organization, pedagogy, and unique features are a testament to the **market-driven nature of *Taxation's* development.**

> "I think this is the best book available for introductory and intermediate courses in taxation."
>
> Shane Stinson
> – University of Alabama

A MODERN APPROACH FOR TODAY'S STUDENT

McGraw Hill's Taxation series was built around the following five core precepts:

1. **Storyline Approach:** Each chapter begins with a storyline that introduces a set of characters or a business entity facing specific tax-related situations. Each chapter's examples are related to the storyline, providing students with opportunities to **learn the code in context.**

2. **Integrated Examples:** In addition to providing examples in context, we provide **"What if"** scenarios within many examples to **illustrate how variations in the facts might or might not change the answers.**

3. **Conversational Writing Style:** The authors took special care to write *McGraw Hill's Taxation* in a way that fosters a friendly dialogue between the content and each individual student. The tone of the presentation is intentionally conversational—creating the impression of ***speaking with* the student,** as opposed to *lecturing to* the student.

4. **Superior Organization of Related Topics:** *McGraw Hill's Taxation* provides two alternative topic sequences. In the *McGraw Hill's Taxation of Individuals and Business Entities* volume, the individual topics generally follow the tax form sequence, with an individual overview chapter and then chapters on income, deductions, investment-related issues, and the tax liability computation. The topics then transition into business-related topics that apply to individuals. This volume then provides a group of specialty chapters dealing with topics of particular interest to individuals (including students), including separate chapters on home ownership, compensation, and retirement savings and deferred compensation. Alternatively, in the *Essentials of Federal Taxation* volume, the topics follow a more traditional sequence, with topics streamlined (no specialty chapters) and presented in more of a life-cycle approach.

5. **Real-World Focus:** Students learn best when they see how concepts are applied in the real world. For that reason, real-world examples and articles are included in **Taxes in the Real World** boxes throughout the book. These vignettes demonstrate current issues in taxation and show the relevance of tax issues in all areas of business.

A STORYLINE APPROACH THAT RESONATES WITH STUDENTS

bbernard/Shutterstock

Storyline Summary

Taxpayers:	Bill and Mercedes
Family description:	Bill and Mercedes are married with one daughter, Margaret, and live in Tampa, Florida.
Employment status:	Bill is an economics professor; Mercedes is a small-business owner.
Filing status:	Married, filing jointly
Current situation:	Bill and Mercedes face an IRS audit involving a previous year's interest deductions.

Bill and Mercedes received a notice from the Internal Revenue Service (IRS) that their tax return is under audit for certain interest deductions. As you might expect, they are quite concerned, especially because it has been several years since they claimed the deductions and they worry that all their supporting documentation may not be in place. Several questions run through their minds. How could the IRS audit a tax return that was filed so long ago? Why was their tax return selected, and what should they expect during the audit? The interest deductions they reported were based on advice from their CPA. What would cause the IRS and a CPA to interpret the law differently? What is their financial exposure if the deductions are ultimately disallowed? Will they have to pay interest and penalties in addition to the tax they might owe? ■

Each chapter begins with a storyline that introduces a set of characters facing specific tax-related situations. This revolutionary approach to teaching tax emphasizes real people facing real tax dilemmas. Students learn to apply practical tax information to specific business and personal situations. As their situations evolve, the characters are brought further to life.

Examples

Examples are the cornerstone of any textbook covering taxation. For this reason, *McGraw Hill's Taxation* authors took special care to create clear and helpful examples that relate to the storyline of the chapter. Students learn to refer to the facts presented in the storyline and apply them to other scenarios—in this way, they build a greater base of knowledge through application. Many examples also include "What if" scenarios that add more complexity to the example or explore related tax concepts.

Example 2-1

Bill and Mercedes file their 2022 federal tax return on September 6, 2023, after receiving an automatic extension to file their return by October 15, 2023. In 2026, the IRS selects their 2022 tax return for audit. When does the statute of limitations end for Bill and Mercedes's 2022 tax return?

Answer: Assuming the six-year and "unlimited" statute of limitation rules do not apply, the statute of limitations ends on September 6, 2026 (three years after the later of the actual filing date and the *original* due date).

What if: When would the statute of limitations end for Bill and Mercedes for their 2022 tax return if the couple filed the return on March 22, 2023 (before the original due date of April 15, 2023)?

Answer: In this scenario, the statute of limitations would end on April 15, 2026 because the later of the actual filing date and the original due date is April 15, 2023.

THE PEDAGOGY YOUR STUDENTS NEED TO PUT THE CODE IN CONTEXT

Taxes in the Real World

Taxes in the Real World are short boxes used throughout the book to demonstrate the real-world use of tax concepts. Current articles on tax issues, the real-world application of chapter-specific tax rules, and short vignettes on popular news about tax are some of the issues covered in Taxes in the Real World boxes.

TAXES IN THE REAL WORLD Google: Not Authoritative on Tax Matters; Neither is AI

While Internet super giant Google may be a king of cyberspace knowledge, the Tax Court ruled in *Woodard v. Comm'r,* TC Summary Opinion 2009-150, that a Google search does not constitute reasonable cause to excuse a Harvard MBA/CPA from taking an incorrect tax return position. The Tax Court noted that although the taxpayer had not worked as an accountant for years before filing his tax return, "his accounting degree, MBA, and CPA training, no matter how stale, undoubtedly taught him what sources could be relied upon as definitive; such as, for example, the Internal Revenue Code and the income tax regulations, both of which are readily available on the Internet."

What about artificial intelligence (AI)? In "Is AI Generated Tax Advice Making the Grade," the IRS Taxpayer Advocate Service encouraged taxpayers to be vigilant when using tax preparation software, understand the limitations of AI-generated advice, and to not solely rely on AI-generated tax advice. What does the IRS recommend? Because taxpayers are ultimately responsible for the information reported on their tax returns, the Taxpayer Advocate Service advises taxpayers to review all information carefully, verify calculations, and seek assistance from qualified professionals if needed to ensure compliance with tax laws and regulations.

Source: "Is AI Generated Tax Advice Making the Grade." June 11, 2024. taxpayeradvocate.irs.gov/news/tax-tips/.

The Key Facts

The Key Facts provide quick synopses of the critical pieces of information presented throughout each chapter.

have an understated tax liability. Common computer initiatives include the **DIF (Discriminant Function) system,** the **document perfection program,** and the **information matching program.** The most important of these initiatives is the DIF system. The DIF system assigns a score to each tax return that represents the probability the tax liability on the return has been underreported (a higher score = a higher likelihood of underreporting). The IRS derives the weights assigned to specific tax return attributes from historical IRS audit adjustment data from the National Research Program.[7] The DIF system then uses these (undisclosed) weights to score each tax return based on the tax return's characteristics. Returns with higher DIF scores are reviewed to determine whether an audit is the best course of action.

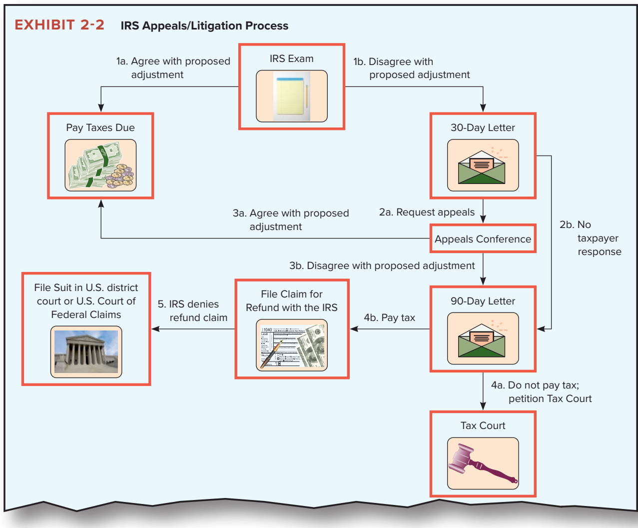
THE KEY FACTS

IRS Audit Selection

- The IRS uses a number of computer programs and outside data sources to identify tax returns that may have an understated tax liability.
- Common computer initiatives include the DIF

Exhibits

Today's students are visual learners, and *McGraw Hill's Taxation* understands this student need by making use of clear and engaging charts, diagrams, and tabular demonstrations of key material.



(Notepad): Imageroller/Alamy Stock Photo; (Court): Jill Braaten/McGraw Hill

"This is the best text I have found for both my students and myself. Easier to read than other textbooks I have looked at, good examples, and, as mentioned before, I appreciate the instructor resources."

Esther Ehrlich, CPA
– The University of Texas at El Paso

PRACTICE MAKES PERFECT WITH A WIDE VARIETY OF ASSIGNMENT MATERIAL

AI/Critical Thinking Questions

Evaluating the output from an AI tool is increasingly important. Is the output correct or incorrect? How do I know that? To help students build skills in this area, each chapter features AI/Critical Thinking Questions with responses generated using an AI query tool. Students are asked to determine whether the AI-generated answers are correct or not, and then explain the rationale behind their answers.

AI/CRITICAL THINKING QUESTIONS

AI/Critical Thinking Questions are available in Connect®. connect

60. Suppose you asked your favorite AI query tool the following question: "Is total income on Form 1040 the same thing as gross income?" The AI tool provided the following response: LO 4-1

Total income and gross income are not exactly the same thing on Form 1040 (the individual tax return), although they are related concepts. Total income and gross income refer to different subsets of income on the individual tax return.

1. **Gross Income:** Gross income, which is also referred to as gross taxable income or adjusted gross income (AGI), includes all income from different sources before any deductions. Gross income includes wages, salary, self-employment income, rental income, interest income, dividends, capital gains, and other types of income.
2. **Total Income:** Total income is a broader term than gross income. Total income includes all income received by an individual during the tax year whether the income is taxable or not. Total income includes gross income that is taxable but it also includes income items that are not taxable such as gifts, inheritances, and certain Social Security benefits. Total income is reported on a specific line on the individual tax return but it is included for informational purposes and may not be directly used to calculate your tax liability.

In summary, gross income is a subgroup of total income. Gross income is an important number for calculating taxable income and thus the tax liability on the individual tax return. Total income includes a wider range of sources of income than gross

Summary

LO 5-1 Apply the concept of realization and explain when taxpayers recognize gross income.

- Income is typically realized with a transaction that allows economic benefit to be identified and measured.
- Unless realized income is deferred or excluded, it is included in gross income in the period dictated by the taxpayer's accounting method.
- The accrual method of accounting recognizes income in the period it is earned, and this method is typically used by large corporations.
- The cash method of accounting recognizes income in the period received, and this method offers a simple and flexible method of accounting typically used by individuals.
- The return of capital principle, constructive receipt doctrine, and assignment of income doctrine affect how much income is recognized, when income is recognized, and who recognizes income, respectively.

LO 5-2 Understand the distinctions between the various sources of income, including income from services and property.

Learning Objectives

Upon completing this chapter, you should be able to:

LO 5-1 Apply the concept of realization and explain when taxpayers recognize gross income.

LO 5-2 Understand the distinctions between the various sources of income, including income from services and property.

LO 5-3 Apply basic income exclusion and deferral provisions to compute gross income.

Summary

A unique feature of *McGraw Hill's Taxation* is the end-of-chapter summary organized around learning objectives. Each objective has a brief, bullet-point summary that covers the major topics and concepts for that chapter, including references to critical exhibits and examples. All end-of-chapter material is tied to learning objectives.

DISCUSSION QUESTIONS

Discussion Questions are available in Connect®. connect

1. Based on the definition of gross income in §61 and related regulations, what is the general presumption regarding the taxability of income realized? LO 5-1
2. Based on the definition of gross income in §61, related regulations, and judicial rulings, what are the three criteria for recognizing taxable income? LO 5-1
3. Describe the concept of realization for tax purposes. LO 5-1
4. Compare and contrast realization of income with recognition of income. LO 5-1
5. Tim is a plumber who joined a barter club. This year Tim exchanged plumbing services for a new roof. The roof is properly valued at $2,500, but Tim would have billed only $2,200 for the plumbing services. What amount of income should Tim recognize on the exchange of his services for a roof? Would your answer change if Tim would have normally billed $3,000 for his services? LO 5-1
6. Andre constructs and installs cabinets in homes. Blair sells and installs carpet in apartments. Andre and Blair worked out an arrangement whereby Andre installed cabinets in Blair's home and Blair installed carpet in Andre's home. Neither Andre nor Blair believes they are required to recognize any gross income on this exchange because neither received cash. Do you agree with them? Explain. LO 5-1
7. What issue precipitated the return of capital principle? Explain. LO 5-1

Discussion Questions

Discussion questions, available in Connect, are provided for each of the major concepts in each chapter, providing students with an opportunity to review key parts of the chapter and answer evocative questions about what they have learned.

Problems

Problems are designed to test the comprehension of more complex topics. Each problem at the end of the chapter is tied to one of that chapter's learning objectives, with multiple problems for critical topics.

PROBLEMS

Select problems are available in Connect®.

connect

LO 2-1 45. Ahmed does not have enough cash on hand to pay his taxes. He was excited to hear that he can request an extension to file his tax return. Does this solve his problem? What are the ramifications if he doesn't pay his tax liability by April 15?

LO 2-1 46. Molto Stancha Corporation had zero earnings this fiscal year; in fact, it lost money. Must the corporation file a tax return?

LO 2-1 47. The estate of Monique Chablis earned $450 of income this year. Is the estate required to file an income tax return?

Tax Form Problems

Tax form problems are a set of requirements included in the end-of-chapter material. These problems require students to complete a tax form (or part of a tax form), providing students with valuable experience and practice with filling out these forms. These requirements—and their relevant forms—are also included in Connect, with select problems available in both static and algorithmic format. Each tax form problem includes an icon to differentiate it from regular problems.

Research Problems

Research problems are special problems throughout the end-of-chapter assignment material. These require students to do both basic and more complex research on topics outside of the scope of the book. Each research problem includes an icon to differentiate it from regular problems.

LO 5-1 research 45. Devon owns 1,000 shares of stock worth $10,000. This year he received 200 additional shares of this stock from a stock dividend. His 1,200 shares are now worth $12,500. Must Devon include the dividend paid in stock in income?

LO 5-1 research 46. XYZ declared a $1 per share dividend on August 15. The date of record for the dividend was September 1 (the stock began selling *ex-dividend* on September 2). The dividend was paid on September 10. Ellis is a cash-method taxpayer. Determine if he must include the dividends in gross income under the following independent circumstances.

Planning Problems

Planning problems are another unique set of problems included in the end-of-chapter assignment material. These require students to test their tax planning skills after covering the chapter topics. Each planning problem includes an icon to differentiate it from regular problems.

LO 2-2 planning 59. The IRS recently completed an audit of Shea's tax return and assessed $15,000 additional tax. Shea requested an appeals conference but was unable to settle the case at the conference. She is contemplating which trial court to choose to hear her case. Provide a recommendation based on the following alternative facts:

a) Shea resides in the 2d Circuit, and the 2d Circuit has recently ruled against the position Shea is litigating.

b) The Federal Circuit Court of Appeals has recently ruled in favor of Shea's position.

c) The issue being litigated involves a question of fact. Shea has a very appealing story to tell but little favorable case law to support her position.

Comprehensive and Tax Return Problems

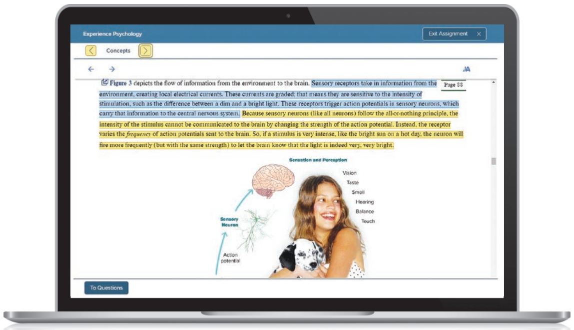
Comprehensive and tax return problems address multiple concepts in a single problem. Comprehensive problems are ideal for cumulative topics; for this reason, they are located at the end of all chapters. **Tax return problems are also available in *Connect* and in the *Instructor Resource Center*. These problems range from simple to complex and cover individual taxation, corporate taxation, partnership taxation, and S corporation taxation.**

McGraw Hill connect®

Your complete course platform

Connect enables you to build deeper connections with your students through cohesive digital content and tools, creating engaging learning experiences. We are committed to providing you with the right resources and tools to support all your students along their personal learning journeys.

90%
student satisfaction



Laptop: Getty Images; Woman/dog: George Doyle/Getty Images

Every learner is unique

In Connect, instructors can assign an adaptive reading experience with SmartBook®. Rooted in advanced learning science principles, SmartBook delivers a personalized experience, focusing students on their learning gaps and ensuring the time they spend studying is time well spent.
mheducation.com/highered/connect/smartbook

Study anytime, anywhere

Encourage your students to download the free ReadAnywhere® app so they can access their online eBook, SmartBook, or Adaptive Learning Assignments when it's convenient, even when they're offline. Because the app automatically syncs with students' Connect accounts, all their work is available every time it is opened.
mheducation.com/readanywhere

"I really liked this app—it made it easy to study when you don't have your textbook in front of you."

Jordan Cunningham, a student at *Eastern Washington University*

Effective tools for efficient studying

Connect is designed to help students be more productive with simple, flexible, intuitive tools that maximize study time and meet students' individual learning needs and prepare them with real-world application. Get learning that works for everyone with Connect.

SUPPORT AT every step

Education for all

McGraw Hill works directly with Accessibility Services departments and faculty to meet the learning needs of all students. Please contact your Accessibility Services Office, and ask them to email **accessibility@mheducation.com**, or visit **mheducation.com/about/accessibility** for more information.

Affordable solutions, added value

Make technology work for you with LMS integration for single sign-on access, mobile access to the digital textbook, and reports to quickly show you how each of your students is doing. And with Affordable Access programs, you can provide all these tools at the lowest available market price to your students. Ask your McGraw Hill representative for more information.

Solutions for your challenges

A product isn't a solution. Real solutions are affordable, reliable, and come with training and ongoing support when you need it and how you want it. Visit **supportateverystep.com** for videos and resources both you and your students can use throughout the term.

Updated and relevant content

Our Evergreen™ Delivery Model provides you with the most relevant and updated content, tools, and accessibility. Engage students and freshen up assignments with up-to-date coverage of select topics and new questions, all without having to switch editions or build a new course.

DIGITAL LEARNING ASSETS TO IMPROVE STUDENT OUTCOMES

> "The quality of the online materials in Connect and Learnsmart are market-leading and unmatched in the tax arena."
>
> Jason W. Stanfield
> – Ball State University

Connect helps students learn more efficiently by providing feedback and practice material when they need it, where they need it. Connect grades homework automatically and gives immediate feedback on any questions students may have missed. The extensive assignable, gradable end-of-chapter content includes problems, comprehensive problems (available as auto-graded tax forms), and discussion questions. Also, select questions have been redesigned to test students' knowledge more fully. They now include tables for students to work through rather than requiring that all calculations be done offline.

New! Application-Based Activities

Prepare students for the real world with Application-Based Activities (ABAs) in Connect. These highly interactive, assignable exercises boost engagement and provide a safe space to apply concepts learned to real-world, course-specific problems. Each ABA involves the application of multiple concepts, providing the ability to synthesize information and use critical-thinking skills to solve realistic scenarios.

Applying Alteryx Exercises in Connect

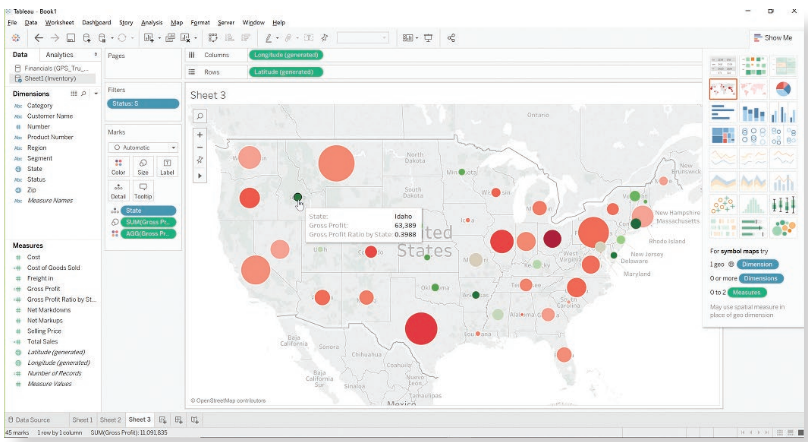
Build students' data analytics skills while introducing them to real-world application using Alteryx, a cutting edge data analytics tool. Students will learn to address technical tax issues by downloading and manipulating data to build Alteryx workflows and then interpreting the data to answer auto-graded questions in Connect.

Integrated Excel

Our new Integrated Excel assignments pair the power of Microsoft Excel with the power of Connect. A seamless integration of Excel within Connect, Integrated Excel questions allow students to work in live, auto-graded Excel spreadsheets—no additional logins, no need to upload or download files. Instructors can choose to grade by formula or solution value, and students receive instant cell-level feedback via integrated Check My Work functionality.

Tableau Dashboard Activities

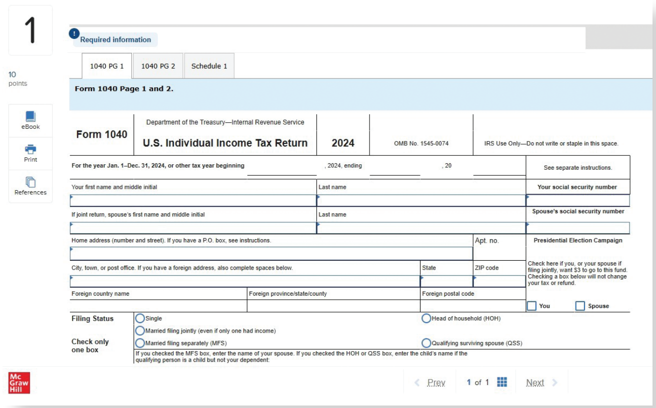
Tableau Dashboard Activities allow students to explore live Tableau dashboards directly integrated into Connect through interactive filters and menus as well as auto-graded questions focused on both



calculations and analysis. Students can check their understanding and apply what they are learning within the framework of analytics and critical thinking.

Auto-Graded Tax Forms

The auto-graded **Tax Forms,** also called the Comprehensive Problems—Static (Tax Form) in Connect, provide a much-improved student experience when solving the tax form–based problems. The tax form simulation allows students to apply tax concepts by completing the actual tax forms online with automatic feedback and grading for both students and instructors.



Source: irs.gov.

TaxACT®

TaxAct Professional *McGraw Hill's Taxation* offers the educational version of TaxAct Professional, one of the leading preparation software companies in the market today. TaxAct features in-depth form instructions that supplement *Individuals* and *Business Entities,* making it easier than ever to integrate software into the classroom. Students are provided with the latest tax forms via the Check for Updates from the Online tab in the program so that at the start of the semester, each student will be prepared to work with the most up-to-date information available. With over 120 tax forms, schedules, and worksheets, TaxAct is sure to have the course materials you will need throughout the semester.

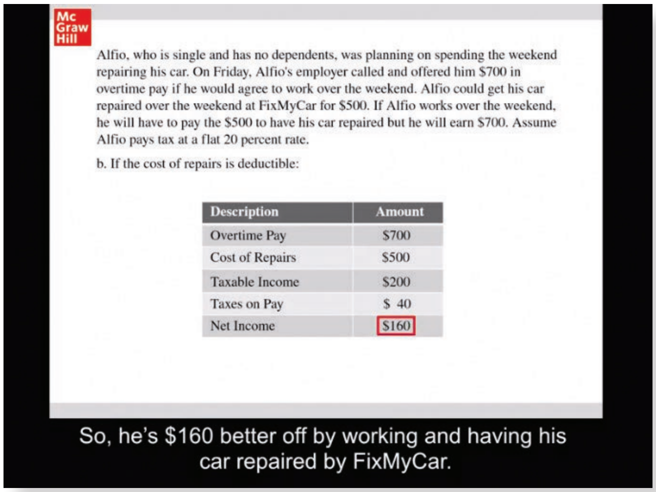
Please note, TaxAct is only compatible with PCs and not Macs. However, we offer easy-to-complete licensing agreement templates that are accessible within Connect and the Instructor Resources Center to enable school computer labs to download the software onto campus hardware for free.

UWorld CPA

UWorld **UWorld CPA Review content is integrated directly into your Connect course** and provides the highest quality CPA Exam multiple-choice questions, helping students master key concepts they will see on the CPA Exam. In addition to access throughout Connect, UWorld provides a wide variety of options for you to integrate their entire suite of CPA Review resources directly into your program. To learn more visit: https://accounting.uworld.com/cpa-review/partner/university.

Guided Examples

The **Guided Examples,** or "hint" videos, in Connect provide a narrated, animated, step-by-step walk-through of select problems similar to those assigned. These short presentations can be turned on or off by instructors and provide reinforcement when students need it most.



McGraw Hill Customer Experience Group Contact Information

At McGraw Hill, we understand that getting the most from new technology can be challenging. That's why our services don't stop after you purchase our products. You can contact our Product Specialists 24 hours a day to get product training online. Or you can search the knowledge bank of Frequently Asked Questions on our support website. For Customer Support, call **800-331-5094,** or visit www.mhhe.com/support. One of our Technical Support Analysts will be able to assist you in a timely fashion.

SUPPLEMENTS FOR INSTRUCTORS

Assurance of Learning Ready

Many educational institutions today are focused on the notion of *assurance of learning,* an important element of many accreditation standards. *McGraw Hill's Taxation* is designed specifically to support your assurance of learning initiatives with a simple, yet powerful, solution.

Each chapter in the book begins with a list of numbered learning objectives, which appear throughout the chapter as well as in the end-of-chapter assignments. Every test bank question for *McGraw Hill's Taxation* maps to a specific chapter learning objective in the textbook. Each test bank question also identifies topic area, level of difficulty, Bloom's Taxonomy level, and AICPA and Business Competency skill area.

Test Builder in Connect

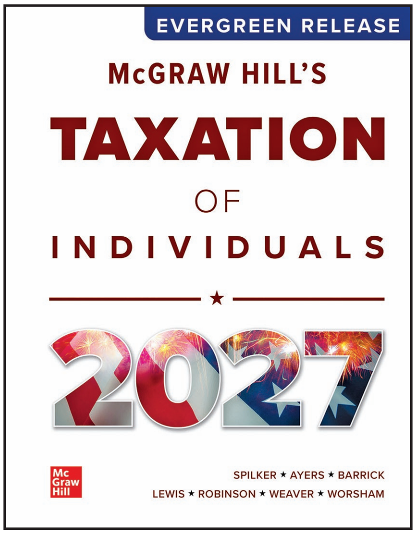
Available within Connect, Test Builder is a cloud-based tool that enables instructors to format tests that can be printed or administered within an LMS. Test Builder offers a modern, streamlined interface for easy content configuration that matches course needs, without requiring a download.

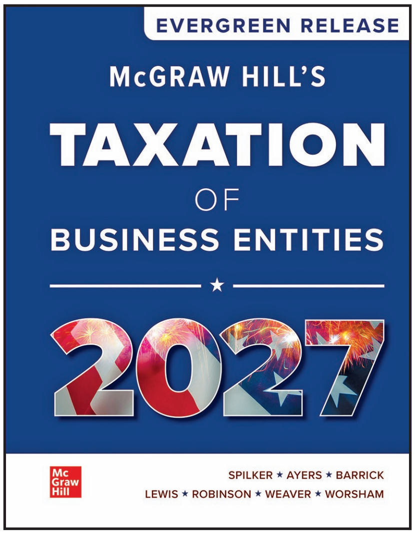
Test Builder allows you to:

- access all test bank content from a particular title.
- easily pinpoint the most relevant content through robust filtering options.
- manipulate the order of questions or scramble questions and/or answers.
- pin questions to a specific location within a test.
- determine your preferred treatment of algorithmic questions.
- choose the layout and spacing.
- add instructions and configure default settings.

Test Builder provides a secure interface for better protection of content and allows for just-in-time updates to flow directly into assessments.

Four Volumes to Fit Four Course Approaches





McGraw Hill's Taxation of Individuals is organized to emphasize topics that are most important to undergraduates taking their first tax course. The first three chapters provide an introduction to taxation and then carefully guide students through tax research and tax planning. Part II discusses the fundamental elements of individual income tax, starting with the tax formula in Chapter 4 and then proceeding to more discussion on income, deductions, investments, and computing tax liabilities in Chapters 5–8. Part III then discusses tax issues associated with business-related activities. Specifically, this part addresses business income and deductions, accounting methods, and tax consequences associated with purchasing assets and property dispositions (sales, trades, or other dispositions). Part IV is unique among tax textbooks; this section combines related tax issues for compensation, retirement savings, and home ownership.

Part I: Introduction to Taxation
1. An Introduction to Tax
2. Tax Compliance, the IRS, and Tax Authorities
3. Tax Planning Strategies and Related Limitations

Part II: Basic Individual Taxation
4. Individual Income Tax Overview, Dependents, and Filing Status
5. Gross Income and Exclusions
6. Individual Deductions
7. Investments
8. Individual Income Tax Computation and Tax Credits

Part III: Business-Related Transactions
9. Business Income, Deductions, and Accounting Methods
10. Property Acquisition and Cost Recovery
11. Property Dispositions

Part IV: Specialized Topics
12. Compensation
13. Retirement Savings and Deferred Compensation
14. Tax Consequences of Home Ownership

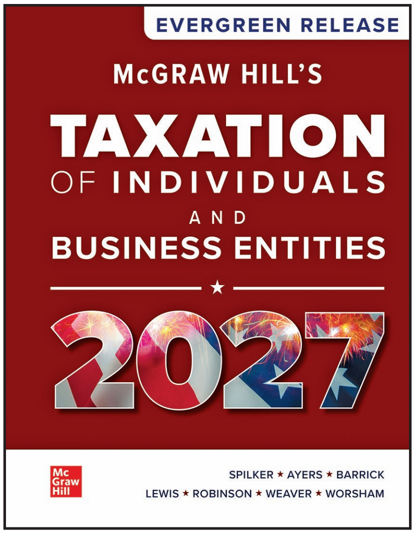
McGraw Hill's Taxation of Business Entities begins with the process for determining gross income and deductions for businesses, and the tax consequences associated with purchasing assets and property dispositions (sales, trades, or other dispositions). Part II provides a comprehensive overview of entities and the formation, reorganization, and liquidation of corporations. Unique to this series is a complete chapter on accounting for income taxes, which provides a primer on the basics of calculating the income tax provision. Included in the narrative is a discussion of temporary and permanent differences and their impact on a company's book "effective tax rate." Part III provides a detailed discussion of partnerships and S corporations. The last part of the book covers state and local taxation, multinational taxation, and transfer taxes and wealth planning.

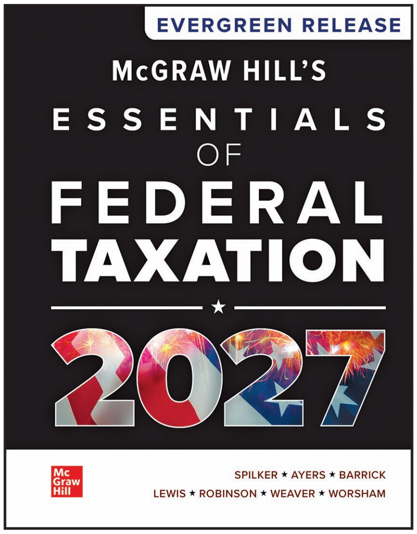
Part I: Business-Related Transactions
1. Business Income, Deductions, and Accounting Methods
2. Property Acquisition and Cost Recovery
3. Property Dispositions

Part II: Entity Overview and Taxation of C Corporations
4. Business Entities Overview
5. Corporate Operations
6. Accounting for Income Taxes
7. Corporate Taxation: Nonliquidating Distributions
8. Corporate Formation, Reorganization, and Liquidation

Part III: Taxation of Flow-Through Entities
9. Forming and Operating Partnerships
10. Dispositions of Partnership Interests and Partnership Distributions
11. S Corporations

Part IV: Multijurisdictional Taxation and Transfer Taxes
12. State and Local Taxes
13. The U.S. Taxation of Multinational Transactions
14. Transfer Taxes and Wealth Planning





McGraw Hill's Taxation of Individuals and Business Entities covers all chapters included in the two split volumes in one convenient volume. See Table of Contents.

McGraw Hill's Essentials of Federal Taxation is designed for a one-semester course, covering the basics of taxation of individuals and business entities. To facilitate a one-semester course, *McGraw Hill's Essentials of Federal Taxation* folds the key topics from the investments, compensation, retirement savings, and home ownership chapters in *Taxation of Individuals* into three individual taxation chapters that discuss gross income and exclusions, for AGI deductions, and from AGI deductions, respectively. The essentials volume also includes a two-chapter C corporation sequence that uses a life-cycle approach covering corporate formations and then corporate operations in the first chapter and nonliquidating and liquidating corporate distributions in the second chapter. This volume is perfect for those teaching a one-semester course and for those who struggle to get through the 25-chapter comprehensive volume.

Acknowledgments

A HEARTFELT THANKS TO THE MANY COLLEAGUES WHO SHAPED THIS BOOK

The version of the book you are reading would not be the same book without the valuable suggestions, keen insights, and constructive criticisms of the reviewers below. Each professor listed here contributed in substantive ways to the organization of chapters, coverage of topics, and use of pedagogy. We are grateful to them for taking the time to read chapters or attend reviewer conferences, focus groups, and symposia in support of the development for the book:

Previous Edition Reviewers
Donna Abelli, *Mount Ida College*
Joseph Assalone, *Rowan College at Gloucester County*
Dr. Valeriya Avdeev, *William Paterson University*
Victoria Badura, *Metropolitan Community College*
Robyn Barrett, *St. Louis Community College*
Kevin Baugess, *ICDC College*
Christopher Becker, *Coastal Carolina University*
Jeanne Bedell, *Keiser University*
Marcia Behrens, *Nichols College*
Michael Belleman, *St. Clair County Community College*
David Berman, *Community College of Philadelphia*
Tim Biggart, *Berry College*
Cynthia Bird, *Tidewater Community College*
Lisa Blum, *University of Louisville*
Rick Blumenfeld, *Sierra College*
Cindy Bortman Boggess, *Babson College*
William A. Bottiglieri, *Iona College*
Cathalene Bowler, *University of Northern Iowa*
Justin Breidenbach, *Ohio Wesleyan University*
Suzon Bridges, *Houston Community College*
Stephen Bukowy, *UNC Pembroke*
Esther Bunn, *Stephen F. Austin State University*
Megan Burke, *Texas Woman's University*
Holly Caldwell, *Bridgewater College*
James Campbell, *Thomas College*
Alisa Carini, *University of California San Diego Extension*
Ronald Carter, *Patrick Henry Community College*
Cynthia Caruso, *Endicott College*
Al Case, *Southern Oregon University*
Paul Caselton, *University of Illinois–Springfield*
Machiavelli (Max) Chao, *University of California–Irvine*
Amy Chataginer, *Mississippi Gulf Coast Community College*
Christine Cheng, *Louisiana State University*
Lisa Church, *Rhode Island College*
Marilyn Ciolino, *Delgado Community College*
Wayne Clark, *Southwest Baptist University*
Ann Cohen, *University at Buffalo, SUNY*
Sharon Cox, *University of Illinois–Urbana-Champaign*
Terry Crain, *University of Oklahoma–Norman*
Roger Crane, *Indiana University East*
Cheryl Crespi, *Central Connecticut State University*
Brad Cripe, *Northern Illinois University*
Curtis J. Crocker, *Southern Crescent Technical College*
Richard Cummings, *University of Wisconsin–Whitewater*
Joshua Cutler, *University of Houston*
William Dams, *Lenoir Community College*
Nichole Dauenhauer, *Lakeland Community College*
Susan Snow Davis, *Green River College*
Ginger DeLatte, *Texas A&M–Corpus Christi*
Jim Desimpelare, *University of Michigan–Ann Arbor*
Julie Dilling, *Moraine Park Technical College*
Steve Dombrock, *Carroll University*
Dr. Vicky C. Dominguez, *College of Southern Nevada*
Keith Donnelly, *SUNY Brockport*
Michael P. Donohoe, *University of Illinois–Urbana-Champaign*
John Dorocak, *California State University–San Bernardino*
Katharine Drake, *University of Arizona*
Amy Dunbar, *University of Connecticut–Storrs*
Bob Duquette, *Lehigh University*
John Eagan, *Morehouse College*
Reed Easton, *Seton Hall University*
Esther Ehrlich, CPA, *The University of Texas at El Paso*
Elizabeth Ekmekjian, *William Paterson University*
Ann Esarco, *Columbia College, Columbia*
Frank Faber, *St. Joseph's College*
Michael Fagan, *Raritan Valley Community College*
Frank Farina, *Catawba College*
Andrew Finley, *Claremont McKenna*
Tim Fogarty, *Case Western Reserve University*
Wilhelmina Ford, *Middle Georgia State University*
Michele Frank, *Miami University*
George Frankel, *San Francisco State University*
Lawrence Friedken, *Penn State University*
Stephen Gara, *Drake University*
Lauren Garrett, *Shippensburg University*
Robert Gary, *University of New Mexico*
Sheri Geddes, *Hope College*
Greg Geisler, *Indiana University*
Alex Gialanella, *Fordham University*
Earl Godfrey, *Gardner Webb University*
Thomas Godwin, *Purdue University*
David Golub, *Northeastern University*
Marina Grau, *Houston Community College*
Brian Greenstein, *University of Delaware*
Patrick Griffin, *Lewis University*
Lillian Grose, *University of Holy Cross*
Thomas Guarino, *Plymouth State University*
Rosie Hagen, *Virginia Western Community College*
Joni Hammond, *Georgia Southwestern State University*
Marcye Hampton, *University of Central Florida*
Connie Hardgrove, *College of Central Florida*
Cass Hausserman, *Portland State University*
Rebecca Helms, *Ivy Tech Community College*
Melanie Hicks, *Liberty University*
Mary Ann Hofmann, *Appalachian State University*
Robert Joseph Holdren, *Muskingum University*

Bambi Hora, *University of Central Oklahoma*
David Horn, *Metropolitan State University*
Carol Hughes, *Asheville Buncombe Technical Community College*
Helen Hurwitz, *Saint Louis University*
Rik Ichiho, *Dixie State University*
Kerry Inger, *Auburn University*
Paul Johnson, *Mississippi Gulf Coast CC–JD Campus*
Athena Jones, *University of Maryland Global Campus*
Andrew Junikiewicz, *Temple University*
Susan Jurney, *University of Arkansas–Fayetteville*
Beth R. Kane, *Northwestern University and Johnson Wales University*
Sandra Kemper, *Regis University*
Jon Kerr, *Baruch College–CUNY*
Lara Kessler, *Grand Valley State University*
Janice Klimek, *University of Central Missouri*
Pamela Knight, *Columbus Technical College*
Satoshi Kojima, *East Los Angeles College*
Dawn Konicek, *Idaho State University*
Jack Lachman, *Brooklyn College*
Brandon Lanciloti, *Freed-Hardeman University*
Stacie Laplante, *University of Wisconsin–Madison*
Suzanne Laudadio, *Durham Tech*
Stephanie Lewis, *The Ohio State University–Columbus*
Teresa Lightner, *University of North Texas*
Robert Lin, *California State University–East Bay*
Chris Loiselle, *Cornerstone University*
Bruce Lubich, *Penn State–Harrisburg*
Elizabeth Lyon, *California State University–Sacramento*
Narelle Mackenzie, *San Diego State University, National University*
Michael Malmfeldt, *Shenandoah University*
Kate Mantzke, *Northern Illinois University*
Robert Martin, *Kennesaw State University*
Anthony Masino, *East Tennessee State University*
Paul Mason, *Baylor University*
Lisa McKinney, *University of Alabama at Birmingham*
Allison McLeod, *University of North Texas*
Lois McWhorter, *Somerset Community College*
Janet Meade, *University of Houston*
Michele Meckfessel, *University of Missouri–St. Louis*
Frank Messina, *University of Alabama at Birmingham*
R. Miedaner, *Lee University*
Ken Milani, *University of Notre Dame*
Syed M. Moiz, *University of Wisconsin, Platteville*
Karen Morris, *Northeast Iowa Community College*
Stephanie Morris, *Mercer University*
Michelle Moshier, *University at Albany*
Leslie Mostow, *University of Maryland–College Park*
James Motter, *Indiana University–Purdue University Indianapolis*
Jackie Myers, *Sinclair Community College*
Michael Nee, *Cape Cod Community College*
Liz Ott, *Casper College*
Sandra Owen, *Indiana University–Bloomington*
Edwin Pagan, *Passaic County Community College*
Jeff Paterson, *Florida State University*
Ronald Pearson, *Bay College*
Martina Peng, *Franklin University*
Michael Wayne Penn Jr., *University of Illinois–Urbana-Champaign*
Dr. Theresa Phipps, *Slippery Rock University*
James Pierson, *Franklin University*
Sonja Pippin, *University of Nevada–Reno*
Jonathan David Pittard, *University of California–Riverside*
Anthony Pochesci, *Rutgers University*
Kyle Post, *Tarleton State University*
Christopher Proschko, *Texas State University*
Joshua Racca, *University of Alabama*
Nirmalee Raddatz, *University of Memphis*
Francisco Rangel, *Riverside City College*
Pauline Ash Ray, *Thomas University*
Luke Richardson, *University of South Florida*
Rodney Ridenour, *Montana State University Northern*
John Robertson, *Arkansas State University*
Jennifer Robinson, *Trident Technical College*
Nicholas Robinson, *Eastern Illinois University*
Susan Robinson, *Georgia Southwestern State University*
Morgan Rockett, *Moberly Area Community College*
Miles Romney, *Michigan State University*
Abbie Sadler, *University of Richmond*
Ananth Seetharaman, *Saint Louis University*
Alisa Shapiro, *Raritan Valley Community College*
Deanna Sharpe, *University of Missouri*
Wayne Shaw, *Southern Methodist University*
Sonia Singh, *University of Florida*
Georgi Smatrakalev, *Florida Atlantic University*
Lucia Smeal, *Georgia State University*
Pamela Smith, *University of Texas at San Antonio*
Adam Spoolstra, *Johnson County Community College*
Joe Standridge, *Sonoma State*
Jason Stanfield, *Ball State University*
George Starbuck, *McMurry University*
James Stekelberg, *University of Arizona*
Teresa Stephenson, *University of Alaska Anchorage*
Shane Stinson, *University of Alabama*
Terrie Stolte, *Columbus State Community College*
Pamela J. Strickland, *Campbell University*
Gloria Jean Stuart, *Georgia Southern University*
Kenton Swift, *University of Montana*
MaryBeth Tobin, *Bridgewater State University*
Erin Towery, *University of Georgia*
Ronald Unger, *Temple University*
Glenn Walberg, *University of Vermont*
Karen Wallace, *Ramapo College*
Stephanie Walton, *Louisiana State University*
Natasha Ware, *Southeastern University*
Luke Watson, *University of Florida*
Sarah Webber, *University of Dayton*
Cassandra Weitzenkamp, *Peru State College*
Marvin Williams, *University of Houston–Downtown*
Chris Woehrle, *American College*
Jennifer Wright, *Drexel University*
Massood Yahya-Zadeh, *George Mason University*
James Yang, *Montclair State University*
Scott Yetmar, *Cleveland State University*
Xiaoli (Charlie) Yuan, *Elizabeth City State University*
Zhen Zhang, *Towson University*
Mingjun Zhou, *DePaul University*

We would like to thank the many talented people who made valuable contributions to the creation of this new release. William A. Padley of Madison Area Technical College, Deanna Sharpe of the University of Missouri–Columbia, and Troy Lewis of Brigham Young University checked the page proofs and solutions manual for accuracy; we greatly appreciate the hours they spent checking tax forms and double-checking our calculations throughout the book. Troy Lewis, Deanna Sharpe, and Matt Lowenkron of Glendale Community College—Arizona accuracy checked the test bank. Thank you to Troy Lewis, Matt Lowenkron of Glendale Community College—Arizona, and Jason W. Stanfield for your contributions to the Smartbook revision for this edition. Special thanks to Troy Lewis for his sharp eye and valuable feedback throughout the revision process. Finally, Deanna Sharpe, Troy Lewis, Matt Lowenkron, Abby Helton of Eastern Kentucky University, and Vivian J. Paige, MBA, MSA, CPA, CGMA, greatly contributed to the accuracy of McGraw Hill's Connect for the new release.

We are especially grateful to J. T. Eagan and Jaclyn Barkow for their contributions to the Tableau Dashboard Activities and Guided Examples, as well as Temple University instructors Wayne Williams, David Jones, and Ronald Unger for their assistance in developing the Data Analytics Problems. Thanks also to J. T. Eagan and Jaclyn Barkow for assistance in developing the Integrated Excel Exercises.

We also appreciate the expert attention given to this project by the staff at McGraw Hill Education, especially Kathleen Klehr, Executive Portfolio Manager; Laura Hurst Spell, Freelance Product Developer; Rachel Hinton, Senior Product Developer; Amanda Lam, Associate Product Developer; Brian Nacik and Jill Eccher, Content Project Managers; John Rohling, Marketing Manager; Rebecca Olson, VP, Portfolio; Selena Hicks, Marketing Director; and Sandy Ludovissy, Senior Buyer.

Changes in *Essentials of Federal Taxation*, 2027

For the new release of McGraw Hill's *Essentials of Federal Taxation,* many changes were made in response to feedback from reviewers and focus group participants:

- **The text** has been **updated to reflect tax law changes through February 18, 2026.**
- All tax forms have been **updated to the most recent forms available as of the end of 2025.**

Other notable changes in the new release include:

Chapter 1

- Updated tax rates for 2026 and Examples 1-3 through 1-7.
- Updated Social Security wage base for 2026.
- Updated unified tax credit for 2026.
- Updated Taxes in the Real World discussing the One Big Beautiful Bill Act (OBBBA).
- Updated Taxes in the Real World: National Debt for the current debt limit.

Chapter 2

- Updated gross income thresholds by filing status for 2026.
- Updated discussion of tax return due dates and extensions for C corporations for tax years beginning in 2026.
- Updated penalty amounts for failure to file a tax return and failure to pay tax owed.

Chapter 3

- Updated tax rates to 2026 tax rates for both chapter text and problems.
- Updated Exhibit 3-3 for 2026 tax rates.
- Updated Example 3-7 for 2026 tax brackets.
- Updated Example 3-8 for 2026 tax brackets.
- Updated discussion of income-shifting examples to account for inflation adjustments.
- Updated inflation-adjusted tax preparer penalty amount relating to head of household filing status.
- Updated inflation-adjusted tax preparer penalty amount relating to head of household filing status. Added new Taxes in the Real World "Big Bucks for the IRS."

Chapter 4

- Updated tax formula in Exhibit 4-1 to reflect tax law changes from the One Big Beautiful Bill Act of 2025 (OBBBA).
- Updated tax rates to 2026 rates and standard deductions for both chapter text and problems.
- Updated Exhibit 4-6 for tax law changes from the OBBBA.
- Updated Exhibit 4-7 to reflect standard deduction amounts for 2026.
- Inserted new Exhibit 4-8 describing tax deductions introduced by the OBBBA.
- Updated and revised text and problems to reflect changes introduced by the OBBBA.
- Added new Taxes in the Real World dealing with itemizing deductions versus claiming the standard deduction.
- Updated text and problems to reflect inflation adjustment for 2026 gross income threshold for qualifying relative.
- Updated inflation-adjusted tax preparer penalty amount relating to head of household filing status.

Chapter 5

- Updated for new 90 percent deduction limit for gambling losses.
- Updated discussion of exclusion for discharge of indebtedness of student loans.
- Updated for 2026 exclusion for dependent care benefits.
- Updated for 2026 health saving accounts amounts.
- Updated for 2026 amounts for qualified transportation benefits.
- Updated for 2026 flexible spending account contributions and carryover amounts.
- Updated for 2026 foreign income exclusion amounts.
- Updated for 529 plan distribution rules for 2026.
- Updated for annual gift tax exclusion and unified tax credit for 2026.
- Updated U.S. Series EE bond interest income exclusion for 2026.
- Updated annual compensation limit and maximum annual benefit for defined benefit plans for 2026.
- Updated annual defined contribution plan limits for 2026.
- Revised Appendix A and related discussion about how taxpayers determine whether capital gains are taxed at 0, 15, 20, 25, or 28 percent or ordinary tax rates for 2026 tax rate schedules.

Chapter 6

- Updated excess business loss limitation for 2026.
- Updated moving expense discussion for exception for members of the U.S. intelligence community.
- Updated health saving accounts discussion for 2026.
- Updated discussion of deduction for interest on qualified education loan for 2026.
- Updated modified AGI phase-out thresholds for deductible contributions to traditional IRAs and contributions to Roth IRAs.

Chapter 7

- Updated mileage rate for medical expense itemized deduction for 2026.
- Updated for state and local tax deduction cap for 2026.
- Updated discussion of the order of the charitable contribution deduction AGI limitations for 2026.
- Added discussion of the new 0.5 percent AGI floor for charitable contributions.
- Updated discussion of casualty losses for 2026.
- Updated discussion of new 90 percent deduction limit for gambling losses.
- Added discussion of educator expense deduction as an other itemized deduction for elementary and secondary school teachers.
- Added discussion of new reduction in itemized deductions for taxpayers in the 37 percent tax bracket.
- Updated standard deduction amounts for 2026 amounts.
- Updated discussion for deduction for qualified business income for 2026, including new minimum qualified business deduction for active qualified trade or businesses.
- Clarified discussion of deduction for qualified tip income, deduction for qualified overtime compensation, and deduction for qualified car loan interest.
- Added discussion of new limited charitable contribution deduction as an other from AGI deduction for taxpayers who do not itemize their deductions.

Chapter 8

- Updated tax rate schedules for 2026.
- Updated discussion of kiddie tax for 2026.
- Updated AMT calculation, exemption and tax rate schedule for 2026.
- Updated Social Security tax wage base and self-employment tax base for 2026.
- Updated discussion of child and dependent care credit for 2026.
- Updated discussion of earned income credit for 2026.

Chapter 9

- Revised illustration and calculation of the gross receipts test.
- Updated examples for new inflation adjustments.
- Added a new *Taxes in the Real World* example of when a liability becomes fixed and determinable.
- Updated illustrations of accrual treatment of advanced payments for services.
- Explained and illustrated small business accounting regulations.
- Revised example computation of taxable income comparing accrual and cash accounting methods.
- Revised and updated completed Schedule C.
- Updated mileage deductions for travel.

Chapter 10

- Updated Exhibit 10-2 for Weyerhaeuser's 2024 assets.
- Updated tax rates to 2026 rates.
- Revised intro to special rules section.
- Revised section on §179 amounts to reflect the inflation adjustments for 2026.
- Updated Examples 10-11 through 10-13 for 2026 §179 amounts.
- Updated bonus depreciation to reflect phase out of 100 percent in 2026.
- Revised the discussion of bonus depreciation.
- Revised Example 10-14 for revised bonus depreciation.
- Updated discussion and Exhibit 10-10 relating to automobile depreciation limits.
- Revised Exhibit 10-14 for changes to §179 and bonus depreciation.
- Added new section on special depreciation on qualified production property.
- Updated §179 amount for SUVs for 2026 inflation amount changes.
- Revised Taxes in the Real World "Yelp and R&D expenditures."
- Updated and revised end-of-chapter problems for §179 amounts and bonus depreciation rules.

Chapter 11

- Updated tax rates for 2026.
- Revised Taxes in the Real World "Buyer Beware."
- Added discussion of §1245 recapture for qualified production property from the OBBBA.
- Added new Example 11-10 to illustrate §1245 recapture of QPP.

Chapter 12

- Updated qualified business income (QBI) deduction discussion, related examples, and problems to reflect law changes under the One Big Beautiful Bill Act (OBBBA) of 2025.

- Updated QBI specified service and wage-based limitation phase-in thresholds for 2026.
- Updated Social Security wage base limitation for 2026, including related discussion, examples and problems.
- Updated excess business loss threshold for 2026 to reflect changes under the OBBBA.
- Updated gross receipts test threshold for 2026.

Chapter 13

- Revised Exhibit 13-2 to reflect the individual income tax formula after changes under the One Big Beautiful Bill Act of 2025 (OBBBA).
- Updated gross receipts test for cash method to reflect inflation-adjusted threshold for 2026.
- Revised Exhibit 13-3 to reflect changes under the OBBBA.
- Revised and updated taxes in the real world dealing with Meta stock options.
- Significantly revised the charitable contribution discussion and examples to reflect changes introduced by the OBBBA.
- Added a new Taxes in the Real World about corporations bunching charitable contributions to address tax law changes under the OBBBA.
- Significantly revised the Taxes in the Real World dealing with Microstrategy Inc. and the corporate alternative minimum tax.
- Updated tax return due date discussion to reflect 2026 tax law.
- Updated dates in examples and problems from 2025 to 2026 to reflect changes made by the OBBBA.

Chapter 14

- Added discussion of unrealized gains and current E&P.
- Added discussion of current E&P adjustment due to 1 percent of modified taxable income floor limitation on charitable contributions added by the One Big Beautiful Bill Act of 2025 (OBBBA).
- Added problem addressing current E&P calculation problem with charitable contribution limited by 1% of modified taxable income floor.
- Clarified discussion of stock attribution rules.

Chapter 15

- Updated discussion on excess business loss limitation to reflect inflation adjustments of threshold amounts.
- Updated discussion on the availability of the cash method to partnerships with corporate partners to reflect inflation adjustments to the average annual gross receipts test.
- Updated discussion on the applicability of the limitation on business interest expense to partners and partnerships to reflect inflation adjustments to the average annual gross receipts test.
- Revised the graphic in Exhibit 15-4.
- Updated Exhibit 15-8 to include 2025 tax forms.
- Updated Taxes in the Real World dealing with hedge funds.
- Updated Form 1065 late filing penalty amounts.
- Revised end-of-chapter problems to reflect inflation adjustments.

Chapter 16

- Updated dates in the text and related examples.

Chapter 17

- Updated requirement to use the accrual method for certain S corporations for 2026.
- Updated excess business loss limitation for 2026.
- Updated Social Security tax wage base for 2026.

As We Go to Press

The new release is current through February 18, 2026. You can visit the *Connect Library* for updates that occur after this date.

Table of Contents

501-1111

6 Individual For AGI Deductions

7 Individual From AGI Deductions

8 Individual Income Tax Computation and Tax Credits