

2019 | Comprehensive

Pearson's

# Federal Taxation 2019



**TIMOTHY J. RUPERT    KENNETH E. ANDERSON**



THOMAS R. POPE • D. DALE BANDY • N. ALLEN FORD • ANNA C. FOWLER • RICHARD J. JOSEPH  
DAVID S. HULSE • LEANN LUNA • CHARLENE HENDERSON • JARED MOORE • WILLIAM J. MOSER  
WILLIAM D. BRINK • SUSAN L. PORTER • MICHAEL S. SCHADEWALD

PEARSON'S  
FEDERAL TAXATION

2019

COMPREHENSIVE

*This page intentionally left blank*

PEARSON'S  
FEDERAL TAXATION

2019

COMPREHENSIVE

**EDITORS**

**TIMOTHY J. RUPERT**

*Northeastern University*

**KENNETH E. ANDERSON**

*University of Tennessee*

**CONTRIBUTING AUTHORS**

**THOMAS R. POPE**

*University of Kentucky*

**D. DALE BANDY**

*University of Central Florida (Emeritus)*

**N. ALLEN FORD**

*University of Kansas*

**ANNA C. FOWLER**

*University of Texas at Austin (Emeritus)*

**RICHARD J. JOSEPH**

*Bryant University*

**DAVID S. HULSE**

*University of Kentucky*

**LEANN LUNA**

*University of Tennessee*

**CHARLENE HENDERSON**

*Louisiana State University*

**JARED MOORE**

*Oregon State University*

**WILLIAM J. MOSER**

*Miami University*

**WILLIAM D. BRINK**

*Miami University*

**SUSAN L. PORTER**

*University of Virginia*

**MICHAEL S. SCHADEWALD**

*University of Florida*



330 Hudson Street, New York, NY 10013

**Vice President, Business, Economics, and UK Courseware:** Donna Battista  
**Director of Portfolio Management:** Adrienne D'Ambrosio  
**Specialist Portfolio Manager:** Lacey Vitetta  
**Editorial Assistant:** Elisa Marks  
**Vice President, Product Marketing:** Roxanne McCarley  
**Senior Product Marketer:** Tricia Murphy  
**Product Marketing Assistant:** Marianela Silvestri  
**Manager of Field Marketing, Business Publishing:** Adam Goldstein  
**Field Marketing Manager:** Nayke Popovich  
**Vice President, Production and Digital Studio, Arts and Business:** Etain O'Dea  
**Director of Production, Business:** Jeff Holcomb  
**Managing Producer, Business:** Melissa Feimer  
**Content Producer:** Emily Throne  
**Project Manager:** Melissa Pellerano  
**Operations Specialist:** Carol Melville  
**Design Lead:** Kathryn Foot  
**Manager, Learning Tools:** Brian Surette  
**Learning Tools Strategist:** Michael Trinchetto  
**Managing Producer, Digital Studio and GLP, Media Production and Development:** Ashley Santora  
**Managing Producer, Digital Studio and GLP:** James Bateman  
**Managing Producer, Digital Studio:** Diane Lombardo  
**Digital Studio Producer:** Mary Kate Murray  
**Digital Studio Producer:** Alana Coles  
**Digital Content Team Lead:** Noel Lotz  
**Digital Content Project Lead:** Martha LaChance  
**Full-Service Project Management, Composition, and Cover Design:** Integra Software Services  
**Cover Art:** Ryan Rodrick Beiler/Shutterstock  
**Printer/Binder:** LSC Communications, Inc./Willard  
**Cover Printer:** Phoenix Color/Hagerstown

**Photo credits:** Ryan Rodrick Beiler/Shutterstock; Andrea Izzotti/Shutterstock; Orhan Cam/Shutterstock

Copyright © 2019, 2018, 2017 by Pearson Education, Inc. or its affiliates. All Rights Reserved. Manufactured in the United States of America. This publication is protected by copyright, and permission should be obtained from the publisher prior to any prohibited reproduction, storage in a retrieval system, or transmission in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise. For information regarding permissions, request forms, and the appropriate contacts within the Pearson Education Global Rights and Permissions department, please visit [www.pearsoned.com/permissions/](http://www.pearsoned.com/permissions/).

Acknowledgments of third-party content appear on the appropriate page within the text, which constitutes an extension of this copyright page.

PEARSON, ALWAYS LEARNING, and MYLAB are exclusive trademarks owned by Pearson Education, Inc. or its affiliates in the U.S. and/or other countries.

Unless otherwise indicated herein, any third-party trademarks, logos, or icons that may appear in this work are the property of their respective owners, and any references to third-party trademarks, logos, icons, or other trade dress are for demonstrative or descriptive purposes only. Such references are not intended to imply any sponsorship, endorsement, authorization, or promotion of Pearson's products by the owners of such marks, or any relationship between the owner and Pearson Education, Inc., or its affiliates, authors, licensees, or distributors.

# OVERVIEW

		Preface xxviii
INDIVIDUALS	CHAPTER 1	AN INTRODUCTION TO TAXATION 1-1
	CHAPTER 2	DETERMINATION OF TAX 2-1
	CHAPTER 3	GROSS INCOME: INCLUSIONS 3-1
	CHAPTER 4	GROSS INCOME: EXCLUSIONS 4-1
	CHAPTER 5	PROPERTY TRANSACTIONS: CAPITAL GAINS AND LOSSES 5-1
	CHAPTER 6	DEDUCTIONS AND LOSSES 6-1
	CHAPTER 7	ITEMIZED DEDUCTIONS 7-1
	CHAPTER 8	LOSSES AND BAD DEBTS 8-1
	CHAPTER 9	BUSINESS AND EMPLOYEE EXPENSES AND DEFERRED COMPENSATION 9-1
	CHAPTER 10	DEPRECIATION, COST RECOVERY, AMORTIZATION, AND DEPLETION 10-1
	CHAPTER 11	ACCOUNTING PERIODS AND METHODS 11-1
	CHAPTER 12	PROPERTY TRANSACTIONS: NONTAXABLE EXCHANGES 12-1
	CHAPTER 13	PROPERTY TRANSACTIONS: SECTION 1231 AND RECAPTURE 13-1
	CHAPTER 14	SPECIAL TAX COMPUTATION METHODS, TAX CREDITS, AND PAYMENT OF TAX 14-1
CORPORATIONS	CHAPTER 1	TAX RESEARCH 1-1
	CHAPTER 2	CORPORATE FORMATIONS AND CAPITAL STRUCTURE 2-1
	CHAPTER 3	THE CORPORATE INCOME TAX 3-1
	CHAPTER 4	CORPORATE NONLIQUIDATING DISTRIBUTIONS 4-1
	CHAPTER 5	OTHER CORPORATE TAX LEVIES 5-1
	CHAPTER 6	CORPORATE LIQUIDATING DISTRIBUTIONS 6-1
	CHAPTER 7	CORPORATE ACQUISITIONS AND REORGANIZATIONS 7-1
	CHAPTER 8	CONSOLIDATED TAX RETURNS 8-1
	CHAPTER 9	PARTNERSHIP FORMATION AND OPERATION 9-1
	CHAPTER 10	SPECIAL PARTNERSHIP ISSUES 10-1
	CHAPTER 11	S CORPORATIONS 11-1
	CHAPTER 12	THE GIFT TAX 12-1
	CHAPTER 13	THE ESTATE TAX 13-1
	CHAPTER 14	INCOME TAXATION OF TRUSTS AND ESTATES 14-1
	CHAPTER 15	ADMINISTRATIVE PROCEDURES 15-1

TABLES	2017 TAX TABLES AND RATE SCHEDULES AND 2018 WITHHOLDING TABLES (PARTIAL) T-1
APPENDIX A	TAX RESEARCH WORKING PAPER FILE A-1
APPENDIX B	TAX FORMS B-1
APPENDIX C	MACRS TABLES C-1
APPENDIX D	GLOSSARY D-1
APPENDIX E	AICPA STATEMENTS ON STANDARDS FOR TAX SERVICES NOS. 1-7 E-1
APPENDIX F	COMPARISON OF TAX ATTRIBUTES FOR C CORPORATIONS, PARTNERSHIPS, AND S CORPORATIONS F-1
APPENDIX G	RESERVED G-1
APPENDIX H	ACTUARIAL TABLES H-1
APPENDIX I	INDEX OF CODE SECTIONS I-1
APPENDIX J	INDEX OF TREASURY REGULATIONS J-1
APPENDIX K	INDEX OF GOVERNMENT PROMULGATIONS K-1
APPENDIX L	INDEX OF COURT CASES L-1
APPENDIX M	SUBJECT INDEX M-1

# CONTENTS

## PREFACE xxviii

## INDIVIDUALS

### CHAPTER 1

#### ► AN INTRODUCTION TO TAXATION 1-1

#### History of Taxation in the United States 1-2

- Early Periods 1-2
- Revenue Acts from 1913 to the Present 1-3
- Revenue Sources 1-3

#### Types of Tax Rate Structures 1-4

- The Structure of Individual Income Tax Rates 1-4
- The Structure of Corporate Tax Rates 1-5
- Marginal, Average, and Effective Tax Rates for Taxpayers 1-5
- Determination of Taxable Income and Tax Due 1-6

#### Other Types of Taxes 1-7

- State and Local Income and Franchise Taxes 1-7
- Wealth Transfer Taxes 1-7
- Other Types of Taxes 1-11

#### Criteria for a Tax Structure 1-12

- Equity 1-12
- Certainty 1-13
- Convenience 1-13
- Economy 1-13
- Simplicity 1-14
- Objectives of the Federal Income Tax Law 1-14

#### Entities in the Federal Income Tax System 1-16

- Taxpaying Entities 1-17
- Flow-Through Entities 1-20
- Other Entities 1-23

#### Tax Law Sources 1-24

#### Enactment of a Tax Law 1-24

- Steps in the Legislative Process 1-24

#### Administration of the Tax Law and Tax Practice Issues 1-26

- Organization of the Internal Revenue Service 1-26
- Enforcement Procedures 1-27
- Selection of Returns for Audit 1-27
- Statute of Limitations 1-28
- Interest 1-28
- Penalties 1-28
- Administrative Appeal Procedures 1-29

#### Components of a Tax Practice 1-29

- Tax Compliance and Procedure 1-29
- Tax Research 1-30
- Tax Planning and Consulting 1-30
- Financial Planning 1-31

#### Computer Applications in Tax Practice 1-31

- Tax Return Preparation 1-31
- Tax Planning Applications 1-31
- Tax Research Applications 1-31

#### Problem Materials 1-32

- Discussion Questions 1-32
- Problems 1-34
- Tax Strategy Problem 1-36
- Case Study Problem 1-36
- Tax Research Problem 1-36

### CHAPTER 2

#### ► DETERMINATION OF TAX 2-1

#### Formula for Individual Income Tax 2-2

- Basic Formula 2-2
- Definitions 2-3
- Tax Formula Illustrated 2-6

#### Deductions from Adjusted Gross Income 2-7

- Itemized Deductions 2-7
- Standard Deduction 2-10
- Dependency Requirements 2-12
- Child Credit 2-18

#### Determining the Amount of Tax 2-19

- Filing Status 2-20
- Joint Return 2-20
- Surviving Spouse 2-21
- Head of Household 2-22
- Single Taxpayer 2-22
- Married Filing Separately 2-22
- Abandoned Spouse 2-23
- Children with Unearned Income 2-24
- Additional Medicare Tax and Net Investment Income Tax 2-27

#### Business Income and Business Entities 2-27

#### Treatment of Capital Gains and Losses 2-30

- Definition of *Capital Assets* 2-30
- Tax Treatment of Gains and Losses 2-30

#### Tax Planning Considerations 2-30

- Shifting Income Between Family Members 2-30
- Splitting Income 2-31
- Maximizing Itemized Deductions 2-31
- Filing Joint or Separate Returns 2-32

#### Compliance and Procedural Considerations 2-33

- Who Must File 2-33
- Due Dates and Extensions 2-34
- Use of Forms 1040, 1040EZ, and 1040A 2-35
- System for Reporting Income 2-35

#### Problem Materials 2-36

- Discussion Questions 2-36
- Issue Identification Questions 2-37
- Problems 2-37



- Tax Strategy Problems 2-42
- Tax Form/Return Preparation Problems 2-42
- Case Study Problems 2-43
- Tax Research Problems 2-43

## CHAPTER 3

### ► GROSS INCOME: INCLUSIONS 3-1

#### Economic, Accounting, and Tax Concepts of Income 3-2

- Economic Concept 3-2
- Accounting Concept 3-2
- Tax Concept of Income 3-3

#### To Whom Is Income Taxable? 3-6

- Assignment of Income 3-6
- Allocating Income Between Married People 3-6
- Income of Minor Children 3-8

#### When Is Income Taxable? 3-8

- Cash Method 3-8
- Accrual Method 3-11
- Hybrid Method 3-12

#### Items of Gross Income: Sec. 61(a) 3-13

- Compensation 3-13
- Business Income 3-13
- Gains from Dealings in Property 3-13
- Interest 3-13
- Rents and Royalties 3-15
- Dividends 3-16
- Alimony and Separate Maintenance Payments 3-19
- Pensions and Annuities 3-20
- Income from Life Insurance and Endowment Contracts 3-22
- Income from Discharge of Indebtedness 3-23
- Income Passed Through to Taxpayer 3-23
- Other Items of Gross Income 3-23
- Prizes, Awards, Gambling Winnings, and Treasure Finds 3-24
- Illegal Income 3-24
- Unemployment Compensation 3-24
- Social Security Benefits 3-24
- Insurance Proceeds and Court Awards 3-26
- Recovery of Previously Deducted Amounts 3-26
- Claim of Right 3-27

#### Tax Planning Considerations 3-27

- Shifting Income 3-27
- Divorce Settlements 3-28
- Prepaid Income 3-28
- Taxable, Tax-Exempt, or Tax-Deferred Bonds 3-29
- Reporting Savings Bond Interest 3-29
- Deferred Compensation Arrangements 3-30

#### Compliance and Procedural Considerations 3-30

#### Problem Materials 3-31

- Discussion Questions 3-31
- Issue Identification Questions 3-34
- Problems 3-35
- Comprehensive Problems 3-38
- Tax Strategy Problems 3-38
- Tax Form/Return Preparation Problem 3-39
- Case Study Problems 3-39
- Tax Research Problem 3-40

## CHAPTER 4

### ► GROSS INCOME: EXCLUSIONS 4-1

#### Items That Are Not Income 4-2

- Unrealized Income 4-2
- Self-Help Income 4-3
- Rental Value of Personal-Use Property 4-3
- Selling Price of Property 4-3

#### Major Statutory Exclusions 4-4

- Gifts and Inheritances 4-4
- Life Insurance Proceeds 4-5
- Awards for Meritorious Achievement 4-7
- Scholarships and Fellowships 4-7
- Distributions from Qualified Tuition Programs 4-7
- Payments for Injury and Sickness 4-8
- Employee Fringe Benefits 4-10
- Foreign-Earned Income Exclusion 4-19
- Income from the Discharge of a Debt 4-20
- Exclusion for Gain from Small Business Stock 4-22
- Other Exclusions 4-22

#### Tax Planning Considerations 4-23

- Employee Fringe Benefits 4-23
- Self-Help Income and Use of Personally Owned Property 4-24

#### Compliance and Procedural Considerations 4-24

#### Problem Materials 4-25

- Discussion Questions 4-25
- Issue Identification Questions 4-26
- Problems 4-26
- Comprehensive Problem 4-30
- Tax Strategy Problems 4-30
- Tax Form/Return Preparation Problems 4-31
- Case Study Problems 4-31
- Tax Research Problems 4-32

## CHAPTER 5

### ► PROPERTY TRANSACTIONS: CAPITAL GAINS AND LOSSES 5-1

#### Determination of Gain or Loss 5-3

- Realized Gain or Loss 5-3
- Recognized Gain or Loss 5-5

#### Basis Considerations 5-5

- Cost of Acquired Property 5-5
- Property Received as a Gift: Gifts After 1921 5-7
- Property Received from a Decedent 5-8
- Property Converted from Personal Use to Business Use 5-10
- Allocation of Basis 5-11

#### Definition of a Capital Asset 5-13

- Influence of the Courts 5-14
- Other IRC Provisions Relevant to Capital Gains and Losses 5-14

#### Tax Treatment for Capital Gains and Losses of Noncorporate Taxpayers 5-16

- Capital Gains 5-16
- Adjusted Net Capital Gains (ANCG) 5-18
- Capital Losses 5-19

#### Tax Treatment of Capital Gains and Losses: Corporate Taxpayers 5-22

**Sale or Exchange 5-22**

- Worthless Securities 5-23
- Retirement of Debt Instruments 5-23
- Options 5-26
- Patents 5-27
- Franchises, Trademarks, and Trade Names 5-27
- Lease Cancellation Payments 5-28

**Holding Period 5-29**

- Property Received as a Gift 5-29
- Property Received from a Decedent 5-29
- Nontaxable Exchanges 5-30
- Receipt of Nontaxable Stock Dividends and Stock Rights 5-30
- Justification for Preferential Treatment of Net Capital Gains 5-30
- Mobility of Capital 5-31
- Mitigation of the Effects of Inflation and the Progressive Tax System 5-31
- Lowers the Cost of Capital 5-31

**Tax Planning Considerations 5-32**

- Selection of Property to Transfer by Gift 5-32
- Selection of Property to Transfer at Time of Death 5-33

**Compliance and Procedural Considerations 5-33**

- Documentation of Basis 5-33
- Reporting of Capital Gains and Losses on Schedule D 5-34

**Problem Materials 5-41**

- Discussion Questions 5-41
- Issue Identification Questions 5-42
- Problems 5-42
- Comprehensive Problem 5-47
- Tax Strategy Problems 5-47
- Tax Form/Return Preparation Problems 5-48
- Case Study Problems 5-49
- Tax Research Problems 5-49

**CHAPTER 6****► DEDUCTIONS AND LOSSES 6-1****Classifying Deductions as For Versus From Adjusted Gross Income (AGI) 6-3****Criteria for Deducting Business and Investment Expenses 6-4**

- Business or Investment Activity 6-5
- Ordinary Expense 6-7
- Necessary Expense 6-7
- Reasonable Expense 6-8
- Expenses and Losses Incurred Directly by the Taxpayer 6-8

**General Restrictions on the Deductibility of Expenses 6-9**

- Capitalization Versus Expense Deduction 6-10
- Expenses Related to Exempt Income 6-11
- Expenditures Contrary to Public Policy 6-12
- Other Expenditures Specifically Disallowed 6-14

**Proper Substantiation Requirement 6-17****When an Expense Is Deductible 6-18**

- Cash Method 6-18
- Accrual Method 6-20

**Special Disallowance Rules 6-23**

- Wash Sales 6-23
- Transactions Between Related Parties 6-26
- Hobby Activities 6-29
- Vacation Home 6-30
- Expenses of an Office in the Home 6-34

**Tax Planning Considerations 6-35**

- Hobby Losses 6-35
- Unreasonable Compensation 6-36
- Timing of Deductions 6-36

**Compliance and Procedural Considerations 6-37**

- Proper Classification of Deductions 6-37
- Proper Substantiation 6-37
- Business Versus Hobby 6-37

**Problem Materials 6-38**

- Discussion Questions 6-38
- Issue Identification Questions 6-39
- Problems 6-40
- Comprehensive Problems 6-45
- Tax Strategy Problems 6-46
- Tax Form/Return Preparation Problems 6-46
- Case Study Problem 6-49
- Tax Research Problems 6-49

**CHAPTER 7****► ITEMIZED DEDUCTIONS 7-1****Medical Expenses 7-2**

- Qualified Individuals 7-2
- Qualified Medical Expenses 7-3
- Amount and Timing of Deduction 7-6

**Taxes 7-9**

- Definition of a Tax 7-9
- Deductible Taxes 7-9
- Limits on Itemized Deductions for State and Local Taxes 7-9
- State and Local Income Taxes 7-10
- State and Local Sales Taxes 7-10
- Personal Property Taxes 7-10
- Real Estate Taxes 7-11
- Self-Employment Tax 7-12
- Nondeductible Taxes 7-12

**Interest 7-12**

- Definition of Interest 7-13
- Classification of Interest Expense 7-13
- Timing of the Interest Deduction 7-19

**Charitable Contributions 7-21**

- Qualifying Organization 7-21
- Type of Property Contributed 7-22
- Deduction Limitations 7-25
- Application of Carryovers 7-26
- Special Rules for Charitable Contributions Made by Corporations 7-27
- Summary of Charitable Contributions Deduction Limitations 7-27

**Casualty and Theft Losses 7-28****Tax Planning Considerations 7-29**

- Medical Expense Deduction 7-29
- Interest Expense Deduction 7-30
- Deduction for Charitable Contributions 7-31

**Compliance and Procedural Considerations 7-32**

- Medical Expenses 7-32
- Charitable Contributions 7-32
- Taxes 7-34

**Problem Materials 7-36**

- Discussion Questions 7-36
- Issue Identification Questions 7-37
- Problems 7-38
- Comprehensive Problem 7-41
- Tax Strategy Problems 7-42
- Tax Form/Return Preparation Problems 7-42
- Case Study Problems 7-44
- Tax Research Problems 7-45

**CHAPTER 8**

► **LOSSES AND BAD DEBTS 8-1**

**Transactions That May Result in Losses 8-2**

- Sale or Exchange of Property 8-2
- Expropriated, Seized, Confiscated, or Condemned Property 8-3
- Abandoned Property 8-3
- Worthless Securities 8-3
- Demolition of Property 8-4

**Classifying the Loss on the Taxpayer's Tax Return 8-4**

- Ordinary Versus Capital Loss 8-5
- Disallowance Possibilities 8-6

**Passive Losses 8-7**

- Computation of Passive Losses and Credits 8-7
- Carryovers 8-8
- Definition of a Passive Activity 8-10
- Taxpayers Subject to Passive Loss Rules 8-12
- Real Estate Businesses 8-14
- Other Rental Real Estate Activities 8-15

**Casualty and Theft Losses 8-17**

- Casualty Defined 8-17
- Theft Defined 8-19
- Deductible Amount of Casualty Loss 8-19
- Limitations on Personal-Use Property 8-20
- Netting Casualty Gains and Losses on Personal-Use Property 8-21
- Casualty Gains and Losses Attributable to Business and Investment Property 8-22
- Timing of Casualty Loss Deduction 8-22

**Bad Debts 8-24**

- Bona Fide Debtor-Creditor Relationship 8-24
- Taxpayer's Basis in the Debt 8-25
- Debt Must Be Worthless 8-26
- Nonbusiness Bad Debts 8-26
- Business Bad Debts 8-28
- Deposits in Insolvent Financial Institutions 8-28

**Net Operating Losses 8-29**

- Computing the Net Operating Loss for Individuals 8-29
- Carryover Periods 8-32

**Excess Business Losses 8-33**

**Tax Planning Considerations 8-33**

- Bad Debts 8-33
- Casualties 8-34

**Compliance and Procedural Considerations 8-34**

- Casualty Losses 8-34
- Worthless Securities 8-34

**Problem Materials 8-35**

- Discussion Questions 8-35
- Issue Identification Questions 8-37
- Problems 8-37
- Tax Strategy Problems 8-41
- Tax Form/Return Preparation Problems 8-42
- Case Study Problems 8-44
- Tax Research Problem 8-44

**CHAPTER 9**

► **BUSINESS AND EMPLOYEE EXPENSES AND DEFERRED COMPENSATION 9-1**

**Part I: Employee and Self-Employed Expenses 9-2**

**Classification and Limitations of Employee Expenses 9-2**

- Nature of the Employment Relationship 9-3
- Limitations on Unreimbursed Employee Expenses 9-4

**Travel Expenses 9-5**

- Deductibility of Travel Expenses 9-5
- Definition of Travel Expenses 9-6
- General Qualification Requirements 9-6
- Business Versus Pleasure 9-8
- Foreign Travel 9-9
- Additional Limitations on Travel Expenses 9-9

**Transportation Expenses 9-10**

- Definition and Classification 9-10
- Treatment of Automobile Expenses 9-11
- Reimbursement of Automobile Expenses 9-13

**Entertainment Expenses 9-13**

- 50% Disallowance for Meal and Entertainment Expenses 9-14
- Classification of Expenses 9-14
- Business Meals 9-15
- Entertainment Facilities and Club Dues 9-16
- Business Gifts 9-16
- Limitations on Entertainment Tickets 9-17

**Reimbursed Employee Business Expenses 9-17**

**Moving Expenses 9-20**

- Expense Classification 9-21
- Definition of Moving Expenses 9-21
- Treatment of Employer Reimbursements 9-22

**Education Expenses 9-22**

- Classification of Education Expenses 9-23
- General Requirements for a Deduction 9-24

**Office in Home Expenses 9-25**

- General Requirements for a Deduction 9-25
- Deductions and Limitations 9-26

**Part II: Deferred Compensation 9-28**

- Qualified Pension and Profit-Sharing Plans 9-29
- Qualification Requirements for a Qualified Plan 9-30
- Tax Treatment to Employees and Employers 9-31
- Nonqualified Plans 9-33
- Employee Stock Options 9-35
- Plans for Self-Employed Individuals 9-37
- Simplified Employee Pensions (SEP IRAs) 9-39
- Simple Retirement Plans 9-39
- Individual Retirement Accounts (IRAs) 9-39
- Traditional IRA 9-40

Roth IRA 9-41  
 Coverdell Education Savings Account 9-44  
 Health Savings Accounts 9-45

#### Tax Planning Considerations 9-45

Moving Expenses 9-45  
 Providing Nontaxable Compensation to Employees 9-46  
 Rollovers to Roth IRA 9-46

#### Compliance and Procedural Considerations 9-47

Substantiating Travel and Entertainment Expenses 9-47  
 Reporting Employee Business Expenses 9-47  
 Reporting Office in Home Expenses 9-48  
 Qualification of Pension and Profit-Sharing Plans 9-48

#### Problem Materials 9-51

Discussion Questions 9-51  
 Issue Identification Questions 9-54  
 Problems 9-54  
 Comprehensive Problem 9-61  
 Tax Strategy Problem 9-62  
 Tax Form/Return Preparation Problems 9-62  
 Case Study Problems 9-63  
 Tax Research Problem 9-64

## CHAPTER 10

### ► DEPRECIATION, COST RECOVERY, AMORTIZATION, AND DEPLETION 10-1

#### Depreciation and Cost Recovery 10-2

General Considerations 10-2  
 Depreciation Methods 10-4  
 Calculation of Depreciation 10-5  
 MACRS Restrictions 10-12

#### Amortization 10-17

Sec. 197 Intangibles 10-17  
 Research and Experimental Expenditures 10-19  
 Computer Software 10-20

#### Depletion, Intangible Drilling and Development Costs 10-21

Depletion Methods 10-22  
 Treatment of Intangible Drilling and Development Costs 10-23

#### Tax Planning Considerations 10-24

Alternative Depreciation System Under MACRS 10-24  
 Use of Units of Production Depreciation 10-24  
 Structuring a Business Combination 10-24

#### Compliance and Procedural Considerations 10-25

Reporting Cost Recovery, Depreciation, Depletion, and Amortization Deductions 10-25

#### Problem Materials 10-28

Discussion Questions 10-28  
 Issue Identification Questions 10-30  
 Problems 10-30  
 Comprehensive Problem 10-35  
 Tax Strategy Problem 10-36  
 Tax Form/Return Preparation Problems 10-36  
 Case Study Problems 10-37  
 Tax Research Problem 10-37

## CHAPTER 11

### ► ACCOUNTING PERIODS AND METHODS 11-1

#### Accounting Periods 11-2

Required Payments and Fiscal Years 11-3  
 Changes in the Accounting Period 11-4  
 Returns for Periods of Less than 12 Months 11-5

#### Overall Accounting Methods 11-7

Cash Receipts and Disbursements Method 11-7  
 Accrual Method 11-9  
 Hybrid Method 11-10

#### Inventories 11-11

Determination of Inventory Cost 11-11

#### Special Accounting Methods 11-15

Long-Term Contracts 11-15  
 Installment Sales Method 11-17  
 Deferred Payment Sales 11-21

#### Imputed Interest 11-22

Imputed Interest Computation 11-23  
 Accrual of Interest 11-23  
 Gift, Shareholder, and Other Loans 11-24

#### Change in Accounting Methods 11-25

Amount of Change 11-26  
 Reporting the Amount of the Change 11-27  
 Obtaining IRS Consent 11-27

#### Tax Planning Considerations 11-28

Accounting Periods 11-28  
 Accounting Methods 11-28  
 Installment Sales 11-28

#### Compliance and Procedural Considerations 11-28

Reporting Installment Sales on Form 6252 11-28  
 Procedures for Changing to LIFO 11-30

#### Problem Materials 11-30

Discussion Questions 11-30  
 Issue Identification Questions 11-31  
 Problems 11-32  
 Comprehensive Problem 11-34  
 Tax Strategy Problems 11-35  
 Tax Form/Return Preparation Problem 11-35  
 Case Study Problems 11-35  
 Tax Research Problems 11-36

## CHAPTER 12

### ► PROPERTY TRANSACTIONS: NONTAXABLE EXCHANGES 12-1

#### Like-Kind Exchanges 12-2

Like-Kind Property Defined 12-2  
 A Direct Exchange Must Occur 12-4  
 Three-Party Exchanges 12-4  
 Receipt of Boot 12-5  
 Basis of Property Received 12-6  
 Exchanges Between Related Parties 12-7  
 Transfer of Non-Like-Kind Property 12-8  
 Holding Period for Property Received 12-8

#### Involuntary Conversions 12-9

Involuntary Conversion Defined 12-10  
 Tax Treatment of Gain Due to Involuntary Conversion into Boot 12-10  
 Replacement Property 12-12  
 Obtaining Replacement Property 12-13  
 Time Requirements for Replacement 12-14

#### Sale of Principal Residence 12-15

Principal Residence Defined 12-16  
 Sale of More than One Principal Residence Within a Two-Year Period 12-17  
 Nonqualified Use After 2008 12-19  
 Involuntary Conversion of a Principal Residence 12-20

**Tax Planning Considerations 12-20**

- Avoiding the Like-Kind Exchange Provisions 12-20
- Sale of a Principal Residence 12-21

**Compliance and Procedural Considerations 12-22**

- Reporting of Involuntary Conversions 12-22
- Reporting of Sale or Exchange of a Principal Residence 12-23

**Problem Materials 12-23**

- Discussion Questions 12-23
- Issue Identification Questions 12-24
- Problems 12-25
- Comprehensive Problem 12-29
- Tax Strategy Problem 12-29
- Tax Form/Return Preparation Problems 12-30
- Case Study Problem 12-31
- Tax Research Problems 12-31

**CHAPTER 13**

► **PROPERTY TRANSACTIONS: SECTION 1231 AND RECAPTURE 13-1**  
History of Sec. 1231 13-2

**Overview of Basic Tax Treatment for Sec. 1231 13-3**

- Net Gains 13-3
- Net Losses 13-3
- Tax Rate for Net Sec. 1231 Gain 13-4

**Section 1231 Property 13-5**

- Section 1231 Property Defined 13-5
- Real or Depreciable Property Used in Trade or Business 13-5
- Involuntary Conversions 13-6
- Condemnations 13-6
- Other Involuntary Conversions 13-7

**Procedure for Sec. 1231 Treatment 13-7**

**Recapture Provisions of Sec. 1245 13-8**

- Purpose of Sec. 1245 13-9

**Recapture Provisions of Sec. 1250 13-10**

- Purpose of Sec. 1250 13-11
- Section 1250 Property Defined 13-11
- Unrecaptured Section 1250 Gain 13-12
- Taxation of Gains on Sale or Exchange of Depreciable Real Property 13-12
- Low-Income Housing 13-15

**Additional Recapture for Corporations 13-16**

- Summary of Secs. 1231, 1245, and 1250 Gains 13-17

**Recapture Provisions—Other Applications 13-18**

- Gifts of Property Subject to Recapture 13-18
- Transfer of Property Subject to Recapture at Death 13-18
- Charitable Contributions 13-18
- Like-Kind Exchanges 13-19
- Involuntary Conversions 13-19
- Installment Sales 13-19
- Section 179 Expensing Election 13-20
- Conservation and Land Clearing Expenditures 13-20
- Intangible Drilling Costs and Depletion 13-21
- Gain on Sale of Depreciable Property Between Related Parties 13-22

**Tax Planning Considerations 13-23**

- Avoiding the Recapture Provisions 13-23

**Compliance and Procedural Considerations 13-24**

- Reporting Sec. 1231 Gains and Losses on Form 4797 13-24
- Reporting Gains Recaptured as Ordinary Income on Form 4797 13-24
- Reporting Casualty or Theft Gain or Loss on Form 4684 13-24

**Problem Materials 13-28**

- Discussion Questions 13-28
- Issue Identification Questions 13-29
- Problems 13-30
- Comprehensive Problem 13-35
- Tax Strategy Problems 13-35
- Tax Form/Return Preparation Problems 13-36
- Case Study Problems 13-36
- Tax Research Problem 13-37

**CHAPTER 14**

► **SPECIAL TAX COMPUTATION METHODS, TAX CREDITS, AND PAYMENT OF TAX 14-1**

**Alternative Minimum Tax 14-2**

- AMT Computation 14-3
- AMT Tax Rates and Brackets 14-3
- AMT Exemption Amount 14-3
- AMT Tax Preference Items 14-4
- AMT Adjustments 14-4
- AMT Credits 14-6
- Summary Illustration of the AMT Computation 14-7

**Self-Employment Tax 14-8**

- What Constitutes Self-Employment Income 14-9

**Personal and Business Tax Credits 14-10**

- Use and Importance of Tax Credits 14-10
- Value of a Credit Versus a Deduction 14-10
- Nonrefundable Personal Tax Credits 14-11
- Foreign Tax Credit 14-17
- Business Related Tax Credits 14-19
- Refundable Personal Credits 14-23

**Provisions Related to Health Insurance 14-24**

- Health Insurance Premium Assistance Credit (Also Known as Premium Tax Credit) 14-24

**Payment of Taxes 14-26**

- Withholding of Taxes 14-27
- Estimated Tax Payments 14-28

**Tax Planning Considerations 14-30**

- Avoiding the Alternative Minimum Tax 14-31
- Avoiding the Underpayment Penalty for Estimated Tax 14-31
- Cash-Flow Considerations 14-31
- Use of General Business Tax Credits 14-31
- Foreign Tax Credits and the Foreign Earned Income Exclusion 14-32

**Compliance and Procedural Considerations 14-32**

- Alternative Minimum Tax (AMT) Filing Procedures 14-32

Withholdings and Estimated Tax Payments 14-32  
 General Business Tax Credits 14-33  
 Nonrefundable Personal Tax Credits 14-33

### **Problem Materials 14-32**

Discussion Questions 14-33  
 Issue Identification Questions 14-35  
 Problems 14-36  
 Comprehensive Problem 14-40  
 Tax Strategy Problem 14-41  
 Tax Form/Return Preparation Problems 14-42  
 Case Study Problems 14-43  
 Tax Research Problem 14-43

## **CORPORATIONS**

### **CHAPTER 1**

#### **► TAX RESEARCH 1-1**

#### **Overview of Tax Research 1-2**

#### **Steps in the Tax Research Process 1-3**

#### **Importance of the Facts to the Tax Consequences 1-5**

Creating a Factual Situation Favorable to the  
 Taxpayer 1-6

#### **The Sources of Tax Law 1-7**

The Legislative Process 1-7  
 The Internal Revenue Code 1-8  
 Treasury Regulations 1-9  
 Administrative Pronouncements 1-11  
 Judicial Decisions 1-14  
 Tax Treaties 1-24  
 Tax Periodicals 1-24

#### **Tax Services 1-25**

#### **The Internet as a Research Tool 1-26**

Keyword Searches 1-27  
 Search by Citation 1-28  
 Noncommercial Internet Services 1-28

#### **Citators 1-28**

Using the Citator 1-30

#### **Professional Guidelines for Tax Services 1-30**

Treasury Department *Circular 230* 1-30  
 AICPA's Statements on Tax Standards 1-31

#### **Sample Work Papers and Client Letter 1-34**

#### **Problem Materials 1-34**

Discussion Questions 1-34  
 Problems 1-35  
 Comprehensive Problem 1-38  
 Tax Strategy Problem 1-38  
 Case Study Problem 1-39  
 Tax Research Problems 1-39

### **CHAPTER 2**

#### **► CORPORATE FORMATIONS AND CAPITAL STRUCTURE 2-1**

#### **Organization Forms Available 2-2**

Sole Proprietorships 2-2  
 Partnerships 2-3  
 Corporations 2-5

Limited Liability Companies 2-8  
 Limited Liability Partnerships 2-8

#### **Check-the-Box Regulations 2-8**

#### **Legal Requirements and Tax Considerations Related to Forming a Corporation 2-9**

Legal Requirements 2-9  
 Tax Considerations 2-9

#### **Section 351: Deferring Gain or Loss Upon Incorporation 2-12**

The Property Requirement 2-12  
 The Control Requirement 2-13  
 The Stock Requirement 2-16  
 Effect of Sec. 351 on the Transferors 2-16  
 Tax Consequences to Transferee  
 Corporation 2-20  
 Assumption of the Transferor's Liabilities 2-22  
 Other Considerations in a Sec. 351  
 Exchange 2-25

#### **Choice of Capital Structure 2-27**

Characterization of Obligations as Debt or  
 Equity 2-27  
 Debt Capital 2-28  
 Equity Capital 2-29  
 Capital Contributions by Shareholders 2-29  
 Capital Contributions by Nonshareholders 2-31

#### **Worthlessness of Stock or Debt Obligations 2-32**

Securities 2-32  
 Unsecured Debt Obligations 2-33

#### **Tax Planning Considerations 2-34**

Avoiding Sec. 351 2-34

#### **Compliance and Procedural Considerations 2-36**

Reporting Requirements Under Sec. 351 2-36

#### **Problem Materials 2-37**

Discussion Questions 2-37  
 Issue Identification Questions 2-38  
 Problems 2-38  
 Comprehensive Problems 2-43  
 Tax Strategy Problems 2-44  
 Case Study Problems 2-44  
 Tax Research Problems 2-45

### **CHAPTER 3**

#### **► THE CORPORATE INCOME TAX 3-1**

#### **Corporate Elections 3-2**

Choosing a Calendar or Fiscal Year 3-2  
 Accounting Methods 3-4

#### **Determining a Corporation's Taxable Income and Tax Liability 3-5**

Corporate Tax Rate 3-5  
 Sales and Exchanges of Property 3-5  
 Business Expenses 3-8  
 Special Deductions 3-14  
 Exceptions for Closely Held Corporations 3-19

#### **Controlled Groups of Corporations 3-21**

What Is a Controlled Group? 3-21  
 Application of the Controlled Group Test 3-25  
 Special Rules Applying to Controlled Groups 3-25  
 Consolidated Tax Returns 3-26

**Tax Planning Considerations 3-27**

Compensation Planning for Shareholder-Employees 3-27

**Compliance and Procedural Considerations 3-29**

Estimated Taxes 3-29  
Requirements for Filing and Paying Taxes 3-33  
When the Return Must Be Filed 3-33  
Tax Return Schedules 3-33

**Financial Statement Implications 3-37**

Scope, Objectives, and Principles of ASC 740 3-38  
Temporary Differences 3-39  
Deferred Tax Assets and the Valuation Allowance 3-39  
Accounting for Uncertain Tax Positions 3-40  
Balance Sheet Classification 3-41  
Tax Provision Process 3-41  
Comprehensive Example – Year 1 3-42  
Comprehensive Example – Year 2 3-45  
Other Transactions 3-49

**Problem Materials 3-49**

Discussion Questions 3-49  
Issue Identification Questions 3-50  
Problems 3-51  
Comprehensive Problem 3-58  
Tax Strategy Problem 3-59  
Tax Form/Return Preparation Problems 3-60  
Case Study Problems 3-65  
Tax Research Problems 3-65

**CHAPTER 4**

► **CORPORATE NONLIQUIDATING DISTRIBUTIONS 4-1**

**Nonliquidating Distributions in General 4-2**

**Earnings and Profits (E&P) 4-3**

Current Earnings and Profits 4-3  
Distinction Between Current and Accumulated E&P 4-6

**Nonliquidating Property Distributions 4-8**

Consequences of Nonliquidating Property Distributions to the Shareholders 4-8  
Consequences of Property Distributions to the Distributing Corporation 4-9  
Constructive Dividends 4-11

**Stock Dividends and Stock Rights 4-13**

Nontaxable Stock Dividends 4-14  
Nontaxable Stock Rights 4-14  
Effect of Nontaxable Stock Dividends on the Distributing Corporation 4-15  
Taxable Stock Dividends and Stock Rights 4-15

**Stock Redemptions 4-16**

Tax Consequences of the Redemption to the Shareholder 4-17

Attribution Rules 4-18

Substantially Disproportionate Redemptions 4-20

Complete Termination of the Shareholder's Interest 4-21

Redemptions Not Essentially Equivalent to a Dividend 4-23

Partial Liquidations 4-23

Redemptions to Pay Death Taxes 4-25

Effect of Redemptions on the Distributing Corporation 4-26

**Preferred Stock Bailouts 4-27**

Sec. 306 Stock Defined 4-28

Dispositions of Sec. 306 Stock 4-28

Redemptions of Sec. 306 Stock 4-29

Exceptions to Sec. 306 Treatment 4-30

**Stock Redemptions by Related Corporations 4-30**

Brother-Sister Corporations 4-30

Parent-Subsidiary Corporations 4-32

**Tax Planning Considerations 4-33**

Avoiding Unreasonable Compensation 4-33

Bootstrap Acquisitions 4-34

Timing of Distributions 4-35

**Compliance and Procedural Considerations 4-36**

Corporate Reporting of Nondividend Distributions 4-36

Agreement to Terminate Interest Under Sec. 302(b)(3) 4-36

**Problem Materials 4-37**

Discussion Questions 4-37

Issue Identification Questions 4-38

Problems 4-39

Comprehensive Problem 4-45

Tax Strategy Problem 4-46

Case Study Problems 4-46

Tax Research Problems 4-47

**CHAPTER 5**

► **OTHER CORPORATE TAX LEVIES 5-1**

**Use of C Corporation to Avoid Income Taxes 5-2**

**Personal Holding Company Tax 5-3**

Personal Holding Company Defined 5-4

Stock Ownership Requirement 5-4

Passive Income Requirement 5-4

Calculating the PHC Tax 5-8

Avoiding the PHC Designation and Tax Liability by Making Dividend Distributions 5-10

PHC Tax Calculation 5-11

**Accumulated Earnings Tax 5-12**

Corporations Subject to the Penalty Tax 5-12

Proving a Tax-Avoidance Purpose 5-13

Evidence Concerning the Reasonableness of an Earnings Accumulation 5-14

Calculating the Accumulated Earnings Tax 5-18

Comprehensive Example 5-21

**Tax Planning Considerations 5-22**

- Avoiding the Personal Holding Company Tax 5-22
- Avoiding the Accumulated Earnings Tax 5-23

**Compliance and Procedural Considerations 5-23**

- Personal Holding Company Tax 5-23
- Accumulated Earnings Tax 5-24

**Problem Materials 5-24**

- Discussion Questions 5-24
- Issue Identification Questions 5-26
- Problems 5-26
- Comprehensive Problem 5-30
- Tax Strategy Problems 5-30
- Case Study Problems 5-31
- Tax Research Problems 5-32

**CHAPTER 6****► CORPORATE LIQUIDATING DISTRIBUTIONS 6-1****Overview of Corporate Liquidations 6-2**

- The Shareholder 6-2
- The Corporation 6-3
- Definition of a Complete Liquidation 6-4

**General Liquidation Rules 6-5**

- Effects of Liquidating on the Shareholders 6-5
- Effects of Liquidating on the Liquidating Corporation 6-6

**Liquidation of a Controlled Subsidiary 6-10**

- Overview 6-10
- Requirements 6-11
- Effects of Liquidating on the Shareholders 6-12
- Effects of Liquidating on the Subsidiary Corporation 6-13

**Special Reporting Issues 6-15**

- Pertaining to Shareholders 6-15
- Pertaining to the Liquidating Corporation 6-16

**Recognition of Gain or Loss When Property Is Distributed in Retirement of Debt 6-17**

- General Rule 6-17
- Satisfaction of the Subsidiary's Debt Obligations 6-17

**Tax Planning Considerations 6-18**

- Timing the Liquidation Transaction 6-18
- Recognition of Ordinary Losses When a Liquidation Occurs 6-19
- Obtaining 80% Ownership to Achieve Sec. 332 Benefits 6-19
- Avoiding Sec. 332 to Recognize Losses 6-20

**Compliance and Procedural Considerations 6-20**

- General Liquidation Procedures 6-20
- Section 332 Liquidations 6-21
- Plan of Liquidation 6-21

**Problem Materials 6-21**

- Discussion Questions 6-21
- Issue Identification Questions 6-23

Problems 6-24

- Comprehensive Problem 6-30
- Tax Strategy Problems 6-31
- Case Study Problems 6-32
- Tax Research Problems 6-33

**CHAPTER 7****► CORPORATE ACQUISITIONS AND REORGANIZATIONS 7-1****Taxable Acquisition Transactions 7-2**

- Asset Acquisitions 7-2
- Stock Acquisitions 7-4

**Comparison of Taxable and Nontaxable Acquisitions 7-10**

- Taxable and Nontaxable Asset Acquisitions 7-10
- Comparison of Taxable and Nontaxable Stock Acquisitions 7-11

**Types of Reorganizations and Their Tax Consequences 7-14**

- The Target or Transferor Corporation 7-14
- The Acquiring or Transferee Corporation 7-15
- Shareholders and Security Holders 7-16

**Acquisitive Reorganizations 7-19**

- Type A Reorganization 7-19
- Type C Reorganization 7-25
- Type D Reorganization 7-28
- Type B Reorganization 7-29
- Type G Reorganization 7-33

**Divisive Reorganizations 7-33**

- Divisive Type D Reorganization 7-33
- Divisive Type G Reorganization 7-38

**Other Reorganizations 7-38**

- Type E Reorganization 7-38
- Type F Reorganization 7-40

**Judicial Restrictions on the Use of Corporate Reorganizations 7-40**

- Continuity of Interest 7-41
- Continuity of Business Enterprise 7-41
- Business Purpose Requirement 7-42
- Step Transaction Doctrine 7-42

**Tax Attributes 7-43**

- Assumption of Tax Attributes 7-43
- Limitation on Use of Tax Attributes 7-43

**Tax Planning Considerations 7-46**

- Why Use a Reorganization Instead of a Taxable Transaction? 7-46
- Avoiding the Reorganization Provisions 7-47

**Compliance and Procedural Considerations 7-47**

- Section 338 Election 7-47
- Plan of Reorganization 7-47
- Party to a Reorganization 7-48
- Ruling Requests 7-48



**Financial Statement Implications 7-48**

- Taxable Asset Acquisition 7-48
- Nontaxable Asset Acquisition 7-49
- Stock Acquisition 7-50
- Pricing the Acquisition 7-50
- Net Operating Losses 7-51

**Problem Materials 7-51**

- Discussion Questions 7-51
- Issue Identification Questions 7-52
- Problems 7-53
- Comprehensive Problem 7-61
- Tax Strategy Problems 7-62
- Case Study Problems 7-63
- Tax Research Problems 7-63

**CHAPTER 8**

► **CONSOLIDATED TAX RETURNS 8-1**

**Definition of an Affiliated Group 8-2**

- Requirements 8-2
- Comparison with Controlled Group Definitions 8-4

**Consolidated Tax Return Election 8-4**

- Consolidated Return Regulations 8-4
- Termination of Consolidated Tax Return Filing 8-5

**Consolidated Taxable Income 8-6**

- Accounting Periods and Methods 8-6
- Income Included in the Consolidated Tax Return 8-6
- Calculation of Consolidated Taxable Income and Tax 8-8

**Intercompany Transactions 8-8**

- Basic Concepts 8-8
- Matching and Acceleration Rules 8-10
- Applications of Matching and Acceleration Rules 8-12
- Relevance of Matching and Acceleration Rules 8-18

**Items Computed on a Consolidated Basis 8-18**

- Charitable Contribution Deduction 8-19
- Net Sec. 1231 Gain or Loss 8-19
- Capital Gains and Losses 8-19
- Dividends-Received Deduction 8-20
- Regular Tax Liability 8-22
- Tax Credits 8-22
- Estimated Tax Payments 8-23

**Net Operating Losses (NOLs) 8-24**

- Current Year NOL 8-25
- Carryovers of Consolidated NOLs 8-25
- Special Loss Limitations 8-26

**Stock Basis Adjustments 8-30**

- Tiering Up of Stock Basis Adjustments 8-31
- Excess Loss Account 8-32

**Tax Planning Considerations 8-32**

- Advantages of Filing a Consolidated Tax Return 8-32
- Disadvantages of Filing a Consolidated Tax Return 8-33

**Compliance and Procedural Considerations 8-33**

- The Basic Election and Return 8-33
- Parent Corporation as Agent for the Consolidated Group 8-34
- Separate Entity Treatment of Intercompany Transactions 8-35
- Liability for Taxes Due 8-35

**Financial Statement Implications 8-35**

- Intercompany Transactions 8-35
- SRLY Losses 8-37

**Problem Materials 8-38**

- Discussion Questions 8-38
- Issue Identification Questions 8-39
- Problems 8-40
- Comprehensive Problems 8-47
- Tax Strategy Problem 8-48
- Tax Form/Return Preparation Problem 8-48
- Case Study Problem 8-50
- Tax Research Problems 8-50

**CHAPTER 9**

► **PARTNERSHIP FORMATION AND OPERATION 9-1**

**Definition of a Partnership 9-2**

- General and Limited Partnerships 9-2

**Overview of Taxation of Partnership Income 9-4**

- Partnership Profits and Losses 9-4
- The Partner's Basis 9-4
- Partnership Distributions 9-5

**Tax Implications of Formation of a Partnership 9-5**

- Contribution of Property 9-6
- Contribution of Services 9-10
- Organizational and Syndication Expenditures 9-12

**Partnership Elections 9-12**

- Partnership Tax Year 9-12
- Other Partnership Elections 9-15

**Partnership Reporting of Income 9-16**

- Partnership Taxable Income 9-16
- Separately Stated Items 9-16
- Partnership Ordinary Income 9-17
- Special Deductions and Limitations 9-17

**Partner Reporting of Income 9-20**

- Partner's Distributive Share 9-20
- Special Allocations 9-21

**Basis for Partnership Interest 9-24**

- Beginning Basis 9-24
- Effects of Liabilities 9-24
- Effects of Operations 9-27

**Special Loss Limitations 9-29**

- At-Risk Loss Limitation 9-29
- Passive Activity Limitations 9-29
- Limitation on Excess Business Losses 9-30

**Transactions Between a Partner and the Partnership 9-31**

- Sales of Property 9-31
- Guaranteed Payments 9-32

**Family Partnerships 9-33**

- Capital Ownership 9-33
- Donor-Donee Allocations of Income 9-34

**Tax Planning Considerations 9-35**

- Timing of Loss Recognition 9-35
- Guaranteed Payments 9-35

**Compliance and Procedural Considerations 9-36**

- Reporting to the IRS and the Partners 9-36
- IRS Audit Procedures 9-37

**Problem Materials 9-38**

- Discussion Questions 9-38
- Issue Identification Questions 9-39
- Problems 9-40
- Comprehensive Problems 9-48
- Tax Strategy Problem 9-49
- Tax Form/Return Preparation Problems 9-50
- Case Study Problems 9-54
- Tax Research Problems 9-55

**CHAPTER 10****► SPECIAL PARTNERSHIP ISSUES 10-1****Nonliquidating Distributions 10-2**

- Recognition of Gain 10-2
- Basis Effects of Distributions 10-4
- Holding Period and Character of Distributed Property 10-7

**Nonliquidating Distributions with Sec. 751 10-7**

- Section 751 Assets Defined 10-7
- Exchange of Sec. 751 Assets and Other Property 10-9

**Liquidating or Selling a Partnership Interest 10-11**

- Liquidating Distributions 10-12
- Sale of a Partnership Interest 10-16

**Other Partnership Termination Issues 10-19**

- Retirement or Death of a Partner 10-19
- Exchange of a Partnership Interest 10-20
- Income Recognition and Transfers of a Partnership Interest 10-22
- Termination of a Partnership 10-22
- Mergers and Consolidations 10-23
- Division of a Partnership 10-24

**Optional and Mandatory Basis Adjustments 10-24**

- Adjustments on Transfers 10-25
- Adjustments on Distributions 10-27

**Special Forms of Partnerships 10-28**

- Tax Shelters and Limited Partnerships 10-28
- Publicly Traded Partnerships 10-28
- Limited Liability Companies 10-29
- Limited Liability Partnerships 10-30
- Limited Liability Limited Partnership 10-31

**Tax Planning Considerations 10-31**

- Liquidating Distribution or Sale to Partners 10-31

**Problem Materials 10-32**

- Discussion Questions 10-32
- Issue Identification Questions 10-33

Problems 10-33

Comprehensive Problems 10-43

Tax Strategy Problem 10-44

Case Study Problem 10-44

Tax Research Problems 10-45

**CHAPTER 11****► S CORPORATIONS 11-1****Should an S Election Be Made? 11-3**

- Advantages of S Corporation Treatment 11-3
- Disadvantages of S Corporation Treatment 11-3

**S Corporation Requirements 11-4**

- Shareholder-Related Requirements 11-4
- Corporation-Related Requirements 11-5

**Election of S Corporation Status 11-7**

- Making the Election 11-8
- Termination of the Election 11-9

**S Corporation Operations 11-13**

- Taxable Year 11-13
- Accounting Method Elections 11-14
- Ordinary Income or Loss and Separately Stated Items 11-14
- Special S Corporation Taxes 11-15

**Taxation of the Shareholder 11-19**

- Income Allocation Procedures 11-19
- Income Pass-Through to Shareholders 11-20
- Loss and Deduction Pass-Through to Shareholders 11-21
- Family S Corporations 11-25

**Basis Adjustments 11-25**

- Basis Adjustments to S Corporation Stock 11-25
- Basis Adjustments to Shareholder Debt 11-27

**S Corporation Distributions 11-28**

- Corporations Having No Earnings and Profits 11-28
- Corporations Having Accumulated Earnings and Profits 11-29

**Other Rules 11-33**

- Tax Preference Items and Other AMT Adjustments 11-34
- Transactions Involving Shareholders and Other Related Parties 11-34
- Fringe Benefits Paid to a Shareholder-Employee 11-34

**Tax Planning Considerations 11-35**

- Election to Allocate Income Based on the S Corporation's Accounting Methods 11-35
- Increasing the Benefits from S Corporation Losses 11-36
- Salary Levels 11-37
- Passive Income Requirements 11-37

**Compliance and Procedural Considerations 11-38**

- Making the Election 11-38
- Filing the Corporate Tax Return 11-39
- Estimated Tax Payments 11-39

Consistency Rules 11-40  
Sample S Corporation Tax Return 11-40

**Problem Materials 11-41**

Discussion Questions 11-41  
Issue Identification Questions 11-42  
Problems 11-43  
Comprehensive Problems 11-49  
Tax Strategy Problems 11-51  
Tax Form/Return Preparation Problems 11-51  
Case Study Problem 11-54  
Tax Research Problems 11-54

**CHAPTER 12**

► **THE GIFT TAX 12-1**

**The Unified Transfer Tax System 12-2**

History and Purpose of Transfer Taxes 12-2  
Unified Rate Schedule 12-3  
Impact of Taxable Gifts on Death Tax Base 12-3  
Unified Credit 12-3

**Gift Tax Formula 12-4**

Determination of Gifts 12-4  
Exclusions and Deductions 12-4  
Gift-Splitting Election 12-4  
Cumulative Nature of Gift Tax 12-6  
Unified Credit 12-6

**Transfers Subject to the Gift Tax 12-7**

Transfers for Inadequate Consideration 12-7  
Statutory Exemptions from the Gift Tax 12-8  
Cessation of Donor's Dominion and Control 12-10  
Valuation of Gifts 12-11  
Gift Tax Consequences of Certain Transfers 12-13

**Exclusions 12-16**

Amount of the Exclusion 12-16  
Present Interest Requirement 12-16

**Gift Tax Deductions 12-18**

Marital Deduction 12-19  
Charitable Contribution Deduction 12-21

**The Gift-Splitting Election 12-22**

**Computation of the Gift Tax Liability 12-23**

Effect of Previous Taxable Gifts 12-23  
Unified Credit Available 12-24  
Comprehensive Illustration 12-25

**Basis Considerations for a Lifetime Giving Plan 12-26**

Property Received by Gift 12-26  
Property Received at Death 12-27

**Below-Market Loans: Gift and Income Tax Consequences 12-28**

General Rules 12-28  
*De Minimis* Rules 12-28

**Tax Planning Considerations 12-29**

Tax-Saving Features of *Inter Vivos* Gifts 12-29  
Negative Aspects of Gifts 12-30

**Compliance and Procedural Considerations 12-30**

Filing Requirements 12-30  
Due Date 12-31  
Gift-Splitting Election 12-31

Liability for Tax 12-31  
Determination of Value 12-32  
Statute of Limitations 12-32

**Problem Materials 12-33**

Discussion Questions 12-33  
Issue Identification Questions 12-34  
Problems 12-34  
Comprehensive Problem 12-37  
Tax Strategy Problems 12-38  
Tax Form/Return Preparation Problems 12-38  
Case Study Problems 12-39  
Tax Research Problems 12-39

**CHAPTER 13**

► **THE ESTATE TAX 13-1**

**Estate Tax Formula 13-2**

Gross Estate 13-2  
Deductions 13-3  
Adjusted Taxable Gifts and Tax Base 13-4  
Tentative Tax on Estate Tax Base 13-4  
Reduction for Post-1976 Gift Taxes 13-4  
Unified Credit 13-5

**The Gross Estate: Valuation 13-6**

Date-of-Death Valuation 13-6  
Alternate Valuation Date 13-7

**The Gross Estate: Inclusions 13-8**

Comparison of Gross Estate with Probate Estate 13-9  
Property in Which the Decedent Had an Interest 13-9  
Dower or Curtesy Rights 13-10  
Transferor Provisions 13-10  
Annuities and Other Retirement Benefits 13-13  
Jointly Owned Property 13-14  
General Powers of Appointment 13-15  
Life Insurance 13-16  
Consideration Offset 13-17  
Recipient Spouse's Interest in QTIP Trust 13-17

**Deductions 13-18**

Debts and Funeral and Administration Expenses 13-18  
Losses 13-19  
Charitable Contribution Deduction 13-19  
Marital Deduction 13-20

**Computation of Tax Liability 13-23**

Taxable Estate and Tax Base 13-23  
Tentative Tax and Reduction for Post-1976 Gift Taxes 13-23  
Unified Credit 13-23  
Portability Between Spouses of Exemption Amount 13-24  
Other Credits 13-24  
Comprehensive Illustration 13-25

**Liquidity Concerns 13-28**

Deferral of Payment of Estate Taxes 13-28  
Stock Redemptions to Pay Death Taxes 13-29  
Special Use Valuation of Farm Real Property 13-29

**Generation-Skipping Transfer Tax 13-30****Tax Planning Considerations 13-31**

- Use of *Inter Vivos* Gifts 13-32
- Use of Basic Exclusion Amount 13-32
- What Size Marital Deduction Is Best? 13-33
- Use of Disclaimers 13-33
- Role of Life Insurance 13-33
- Qualifying the Estate for Installment Payments 13-34
- Where to Deduct Administration Expenses 13-34

**Compliance and Procedural Considerations 13-35**

- Filing Requirements 13-35
- Due Date 13-35
- Valuation 13-35
- Election of Alternate Valuation Date 13-35

**Problem Materials 13-36**

- Discussion Questions 13-36
- Issue Identification Questions 13-37
- Problems 13-37
- Comprehensive Problems 13-41
- Tax Strategy Problems 13-42
- Tax Form/Return Preparation Problems 13-43
- Case Study Problems 13-44
- Tax Research Problems 13-45

**CHAPTER 14****► INCOME TAXATION OF TRUSTS AND ESTATES 14-1****Basic Concepts 14-2**

- Inception of Trusts 14-2
- Inception of Estates 14-2
- Reasons for Creating Trusts 14-3
- Basic Principles of Fiduciary Taxation 14-3

**Principles of Fiduciary Accounting 14-4**

- The Importance of Identifying Income and Principal 14-4
- Principal and Income: The Uniform Act 14-5
- Categorization of Depreciation 14-6

**Formula for Taxable Income and Tax Liability 14-7**

- Gross Income 14-7
- Deductions for Expenses 14-7
- Distribution Deduction 14-9
- Personal Exemption 14-9
- Credits 14-10

**Distributable Net Income 14-10**

- Significance of DNI 14-11
- Definition of DNI 14-11
- Manner of Computing DNI 14-11

**Determining a Simple Trust's Taxable Income 14-13**

- Allocation of Expenses to Tax-Exempt Income 14-14
- Determination of DNI and the Distribution Deduction 14-15
- Tax Treatment for Beneficiary 14-15
- Shortcut Approach to Proving Correctness of Taxable Income 14-16

- Effect of a Net Operating Loss 14-16
- Effect of a Net Capital Loss 14-16
- Comprehensive Illustration: Determining a Simple Trust's Taxable Income 14-17

**Determining Taxable Income for Complex Trusts and Estates 14-19**

- Determination of DNI and the Distribution Deduction 14-20
- Tax Treatment for Beneficiary 14-21
- Effect of a Net Operating Loss 14-24
- Effect of a Net Capital Loss 14-24
- Comprehensive Illustration: Determining a Complex Trust's Taxable Income 14-24

**Income in Respect of a Decedent 14-27**

- Definition and Common Examples 14-27
- Significance of IRD 14-28

**Grantor Trust Provisions 14-30**

- Purpose and Effect 14-30
- Revocable Trusts 14-31
- Post-1986 Reversionary Interest Trusts 14-31
- Retention of Administrative Powers 14-31
- Retention of Economic Benefits 14-31
- Control of Others' Enjoyment 14-32

**Tax Planning Considerations 14-33**

- Ability to Shift Income 14-33
- Timing of Distributions 14-33
- Property Distributions 14-34
- Choice of Year-End for Estates 14-34
- Deduction of Administration Expenses 14-34

**Compliance and Procedural Considerations 14-35**

- Filing Requirements 14-35
- Due Date for Return and Tax 14-35
- Documents to Be Furnished to IRS 14-35
- Sample Simple and Complex Trust Returns 14-35

**Problem Materials 14-36**

- Discussion Questions 14-36
- Issue Identification Questions 14-37
- Problems 14-37
- Comprehensive Problem 14-40
- Tax Strategy Problems 14-40
- Tax Form/Return Preparation Problems 14-41
- Case Study Problems 14-42
- Tax Research Problems 14-43

**CHAPTER 15****► ADMINISTRATIVE PROCEDURES 15-1****Role of the Internal Revenue Service 15-2**

- Enforcement and Collection 15-2
- Interpretation of the Statute 15-2

**Audits of Tax Returns 15-3**

- Percentage of Returns Examined 15-3
- Selection of Returns for Audit 15-3
- Disclosure of Uncertain Tax Positions 15-5
- Alternatives for a Taxpayer Whose Return Is Audited 15-5

## xx Comprehensive ► Contents

90-Day Letter 15-7  
Litigation 15-7

### Requests for Rulings 15-9

Information to Be Included in Taxpayer's Request 15-9  
Will the IRS Rule? 15-10  
When Rulings Are Desirable 15-10

### Due Dates 15-10

Due Dates for Returns 15-10  
Extensions 15-11  
Due Dates for Payment of the Tax 15-11  
Interest on Tax Not Timely Paid 15-12

### Failure-to-File and Failure-to-Pay Penalties 15-13

Failure to File 15-15  
Failure to Pay 15-16

### Estimated Taxes 15-17

Payment Requirements 15-17  
Penalty for Underpaying Estimated Taxes 15-18  
Exceptions to the Penalty 15-19

### Other More Severe Penalties 15-20

Negligence 15-20  
Substantial Understatement 15-21  
Transactions without Economic Substance 15-22  
Civil Fraud 15-22  
Criminal Fraud 15-23

### Statute of Limitations 15-24

General Three-Year Rule 15-24  
Six-Year Rule for Substantial Omissions 15-24  
When No Return is Filed 15-26  
Other Exceptions to Three-Year Rule 15-26  
Refund Claims 15-27

### Liability for Tax 15-27

Joint Returns 15-27  
Transferee Liability 15-29

### Tax Practice Issues 15-29

Statutory Provisions Concerning Tax Return  
Preparers 15-29  
Reportable Transaction Disclosures 15-30  
Rules of *Circular 230* 15-31  
Statements on Standards for Tax Services 15-32

Tax Accounting and Tax Law 15-35  
Accountant-Client Privilege 15-36

### Problem Materials 15-37

Discussion Questions 15-37  
Issue Identification Questions 15-38  
Problems 15-38  
Comprehensive Problem 15-41  
Tax Strategy Problem 15-41  
Case Study Problem 15-41  
Tax Research Problems 15-41

## T A B L E S

### 2017 Tax Tables and Rate Schedules and 2018 Withholding Tables (Partial) T-1

## A P P E N D I C E S

### ► APPENDIX A

#### Tax Research Working Paper File A-1

### ► APPENDIX B

#### Tax Forms B-1

### ► APPENDIX C

#### MACRS Tables C-1

### ► APPENDIX D

#### Glossary D-1

### ► APPENDIX E

#### AICPA Statements on Standards for Tax Services Nos. 1-7 E-1

▶ APPENDIX F

**Comparison of Tax Attributes for C Corporations,  
Partnerships, and S Corporations F-1**

▶ APPENDIX G

**Reserved G-1**

▶ APPENDIX H

**Actuarial Tables H-1**

▶ APPENDIX I

**Index of Code Sections I-1**

▶ APPENDIX J

**Index of Treasury Regulations J-1**

▶ APPENDIX K

**Index of Government Promulgations K-1**

▶ APPENDIX L

**Index of Court Cases L-1**

▶ APPENDIX M

**Subject Index M-1**

*This page intentionally left blank*

# ABOUT THE EDITORS



TIMOTHY J. RUPERT

**Timothy J. Rupert** is a Professor at the D'Amore-McKim School of Business at Northeastern University. He received his B.S. in Accounting and his Master of Taxation from the University of Akron. He also earned his Ph.D. from Penn State University. Professor Rupert's research has been published in such journals as *The Accounting Review*, *The Journal of the American Taxation Association*, *Behavioral Research in Accounting*, *Advances in Taxation*, *Applied Cognitive Psychology*, *Advances in Accounting Education*, and *Journal of Accounting Education*. In 2010, he received the Outstanding Educator Award from the Massachusetts Society of CPAs. He also has received the University's Excellence in Teaching Award and the D'Amore-McKim School's Best Teacher of the Year award multiple times. He is active in the American Accounting Association and the American Taxation Association (ATA) and has served as president, vice president, and secretary of the ATA.



KENNETH E. ANDERSON

**Kenneth E. Anderson** is the Pugh CPAs Professor of Accounting at the University of Tennessee. He earned a B.B.A. from the University of Wisconsin–Milwaukee and subsequently attained the level of tax manager with Arthur Young (now part of Ernst & Young). He then earned a Ph.D. from Indiana University. He teaches corporate taxation, partnership taxation, and tax strategy. Professor Anderson also is the Director of the Master of Accountancy Program. He has published articles in *The Accounting Review*, *The Journal of the American Taxation Association*, *Advances in Taxation*, the *Journal of Accountancy*, the *Journal of Financial Service Professionals*, and a number of other journals.



*This page intentionally left blank*

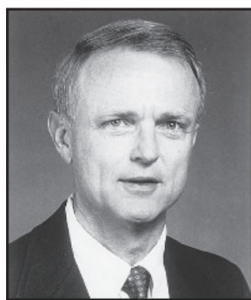
# ABOUT THE AUTHORS



**Thomas R. Pope** is the Ernst & Young Professor of Accounting at the University of Kentucky. He received a B.S. from the University of Louisville and an M.S. and D.B.A. in Business Administration from the University of Kentucky. He teaches international taxation, partnership and S corporation taxation, tax research and policy, and introductory taxation and has won outstanding teaching awards at the University, College, and School of Accountancy levels. He has published articles in *The Accounting Review*, the *Tax Adviser*, *Taxes*, *Tax Notes*, and a number of other journals. Professor Pope's extensive professional experience includes eight years with Big Four accounting firms. Five of those years were with Ernst & Whinney (now part of Ernst & Young), including two years with their National Tax Department in Washington, D.C. He subsequently held the position of Senior Manager in charge of the Tax Department in Lexington, Kentucky. Professor Pope also has been a leader and speaker at professional tax conferences all over the United States and is active as a tax consultant.



**D. Dale Bandy** is the Professor Emeritus in the School of Accounting at the University of Central Florida. He received a B.S. from the University of Tulsa, an M.B.A. from the University of Arkansas, and a Ph.D. from the University of Texas at Austin. He helped to establish the Master of Science in Taxation programs at the University of Central Florida and California State University, Fullerton, where he previously taught. In 1985, he was selected by the California Society of Certified Public Accountants as the Accounting Educator of the year. Professor Bandy has published 8 books and more than 30 articles in accounting and taxation. His articles have appeared in the *Journal of Taxation*, the *Journal of Accountancy*, *Advances in Taxation*, the *Tax Adviser*, *The CPA Journal*, *Management Accounting*, and a number of other journals.



**N. Allen Ford** is the Larry D. Homer/KPMG Peat Marwick Distinguished Teaching Professor of Professional Accounting at the University of Kansas. He received an undergraduate degree from Centenary College in Shreveport, Louisiana, and both the M.B.A. and Ph.D. in Business from the University of Arkansas. He has published over 40 articles related to taxation, financial accounting, and accounting education in journals such as *The Accounting Review*, *The Journal of the American Taxation Association*, and *The Journal of Taxation*. He served as president of the American Taxation Association in 1979–80. Professor Ford has received numerous teaching awards, at the college and university levels. In 1993, he received the Byron T. Shutz Award for Distinguished Teaching in Economics and Business. In 1996, he received the Ray M. Sommerfeld Outstanding Tax Educator Award, which is jointly sponsored by the American Taxation Association and Ernst & Young, and in 1998 he received the Kansas Society of CPAs Outstanding Education Award.



**Anna C. Fowler** is the John Arch White Professor Emeritus in the Department of Accounting at the University of Texas at Austin. She received her B.S. in accounting from the University of Alabama and her M.B.A. and Ph.D. from the University of Texas at Austin. Active in the American Taxation Association throughout her academic career, she served on the editorial board of its journal and held many positions, including president. She is a former member of the American Institute of CPA's Tax Executive Committee and a former chair of the AICPA's Regulation/Tax Subcommittee for the CPA exam. She has published a number of articles, most of which have dealt with estate planning or real estate transaction issues. In 1999, she received the Outstanding Accounting Educator Award of the Texas Society of CPAs and in 2002 the Ray M. Sommerfeld Outstanding Educator Award, co-sponsored by the American Taxation Association and Ernst & Young.



**Richard J. Joseph** is the President and Chief Executive Officer of Babson Global, Inc., a wholly owned education subsidiary of Babson College. At Babson Global, he is responsible for financial and operational management, client relationships, and executive decision making. Dr. Joseph is former Provost-for-Term and Chief Academic Officer of Bryant University, Rhode Island. In this role, he oversaw Bryant's faculty affairs, academic programs, College of Arts and Sciences, College of Business, and School of Health Sciences. Before joining Bryant, he was Provost and Global Dean of Hult International Business School. There, he played a major role in establishing Hult academic centers in Shanghai, Dubai, London, and San Francisco. Before his term at Hult, he served 13 years on the Tax Faculty and Administration of the University of Texas at Austin. Prior to embarking on his academic career, Dr. Joseph worked as an international banker at Citibank, Riyadh; an investment banker at Lehman Brothers, New York; a securities trader at Becker Paribas, Dallas, and Bear Stearns, New York; and a mergers and acquisitions lawyer for the Bass Group, Fort Worth. A graduate *magna cum laude* of Harvard College, Oxford University, and the University of Texas at Austin School of Law, he is co-editor of the *Handbook of Mergers and Acquisitions* (Oxford University Press) and author of *The Origins of the American Income Tax* (Syracuse University Press). He has written numerous commentaries in the *Financial Times*, *The Christian Science Monitor*, *Tax Notes*, and *Tax Notes International*.



**David S. Hulse** is an Associate Professor of Accountancy at the University of Kentucky, where he teaches introductory and corporate taxation courses. He received an undergraduate degree from Shippensburg University, an M.S. from Louisiana State University, and a Ph.D. from the Pennsylvania State University. Professor Hulse has published a number of articles on tax issues in academic and professional journals, including *The Journal of the American Taxation Association*, *Advances in Taxation*, the *Journal of Financial Service Professionals*, the *Journal of Financial Planning*, and *Tax Notes*.



**LeAnn Luna** is a Professor of Accounting at the University of Tennessee. She is a CPA and holds an undergraduate degree from Southern Methodist University, an M.T. from the University of Denver College of Law, and a Ph.D. from the University of Tennessee. She has taught introductory taxation, corporate and partnership taxation, and tax research. Professor Luna also holds a joint appointment with the Center for Business and Economic Research at the University of Tennessee, where she interacts frequently with state policymakers on a variety of policy-related issues. She has published articles in the *Journal of Accounting and Economics*, *National Tax Journal*, *The Journal of the American Taxation Association*, and *State Tax Notes*.



**Charlene Henderson** is a faculty member in the Department of Accounting at Louisiana State University. She earned undergraduate and master's degrees in accounting from Mississippi State University. After working in public accounting and banking, she earned a Ph.D. from Arizona State University. She has taught introductory taxation, corporate taxation, and tax research. Her research has appeared in several journals, including *Journal of the American Taxation Association*, *Journal of Accounting Auditing and Finance*, *Auditing: A Journal of Practice and Theory*, and a number of other journals.



**Jared Moore** is the Mary Ellen Phillips Associate Professor of Accounting at Oregon State University (OSU). He earned his undergraduate, Master of Taxation, and Ph.D. degrees at Arizona State University. He is a CPA (AZ-inactive) and worked in both public and private accounting before pursuing his doctoral degree. Professor Moore has received several teaching awards, including the Byron L. Newton Award for Excellence in Teaching at OSU, and has taught individual and business taxation, introductory and intermediate financial accounting, and doctoral-level financial accounting research. His research interests include both tax and financial accounting, and he has published in journals including the *Journal of the American Taxation Association* and the *National Tax Journal*.



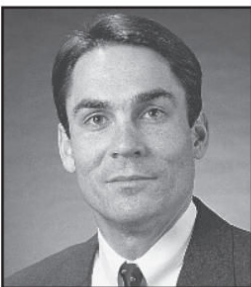
**William J. Moser** is an Assistant Professor in the Department of Accountancy at the Farmer School of Business at Miami University. He received his B.S. in Accountancy from Miami University in 1995, his Masters in Accountancy with an emphasis in taxation from Northern Illinois University in 1997, and his Ph.D. from the University of Arizona in 2005. He has co-authored articles in the *Journal of Accounting Research*, *the Journal of Financial and Quantitative Analysis*, *Review of Accounting Studies*, *The Journal of the American Taxation Association*, and the *Journal of Business, Finance and Accounting*. Professor Moser has received numerous teaching awards including the Provost's Outstanding Junior Faculty Teaching Award at University of Missouri in 2010 and the Grant Thornton Teaching Excellence Award in 2009.



**William D. Brink**, Ph.D., CPA, CFP is an Assistant Professor in the Department of Accountancy at the Farmer School of Business at Miami University in Oxford, Ohio. He received his B.S. from Appalachian State University in 2005 and his Masters in Accountancy from The University of North Carolina Wilmington in 2007. Before attending the University of South Carolina to obtain his Ph.D. in Accountancy in 2014, he worked in public accounting for RSM McGladrey. He teaches tax courses at both the undergraduate and graduate level focusing on individual taxation, business taxation, tax policy, tax academic research, and tax legal research. He has co-authored articles in *Journal of Business Ethics*, *Journal of the American Taxation Association*, *Behavioral Research in Accounting*, *Advances in Accounting Education*, *Advances in Taxation*, *The Conversation*, *CGMA Magazine*, and *The Tax Advisor*. He was the Winner of the Outstanding Author Contribution in the 2017 Emerald Literati Network Awards for Excellence for an article published in *Advances in Accounting Education* and has received numerous teaching awards.



**Susan Porter** is an Associate Professor of Commerce at the University of Virginia where she teaches both undergraduate and graduate tax courses. She earned her undergraduate degree from Babson College. After working in public and private accounting, she earned a Ph.D. from the University of Washington. She has published articles in the *Journal of Accounting and Economics*, *Contemporary Accounting Research*, *Journal of Accounting, Auditing, and Finance*, *The Journal of the American Taxation Association*, and a number of other journals.



**Michael S. Schadewald**, Ph.D., CPA, is a Clinical Associate Professor in the Fisher School of Accounting at the University of Florida, where he teaches courses in accounting and taxation. A graduate of the University of Minnesota, Professor Schadewald has published more than 50 articles in academic and professional journals, including *The Accounting Review*, *Journal of Accounting Research*, and *Contemporary Accounting Research*. He also has served on numerous editorial boards, including *The Journal of the American Taxation Association*, *International Tax Journal*, *Journal of State Taxation*, and *Issues in Accounting Education*. Prior to joining the faculty at the University of Florida, Professor Schadewald taught at the University of Wisconsin-Milwaukee, where he also served as the Director of the Deloitte Center for Multistate Taxation, and the University of Texas in Austin. Prior to entering academics, he worked in the Milwaukee office of Arthur Young (now EY).

# PREFACE

## New to this Edition

---

### INDIVIDUALS

- Complete updating of the chapter material for the provisions in the Tax Cuts and Jobs Act of 2017 affecting individual taxpayers, including an explanation of the new rules and the related implications of the following items:
  - Reduction in marginal tax rates
  - Elimination of personal and dependency exemptions
  - Changes in the deductibility of state and local taxes and casualty losses
  - Elimination of miscellaneous itemized deductions
  - Changes to the alternative minimum tax
  - Increase in the child tax credit
- Complete updating of significant court cases and IRS rulings and procedures during 2017 and early 2018
- All tax rate schedules have been updated to reflect the rates and inflation adjustments for 2018
- Whenever new updates become available, they will be accessible via MyLab Accounting
- Updating of the end-of-chapter tax return problems to 2017 (2017 tax forms are included because the 2018 tax forms were not available when this edition went to print), but also including a supplemental explanation for each tax return problem of how the solution will change for the 2018 tax year given the provisions of the Tax Cuts and Jobs Act.

### CORPORATIONS

- Complete updating of the chapter material for the provisions in the Tax Cuts and Jobs Act of 2017 affecting corporations and other entities, including an explanation of the new rules and the related implications of the following items:
  - Reduced corporate tax rate
  - Qualified business income deduction
  - New limitations on interest, business losses, and NOLs
  - New rules for the taxation of international transactions
  - The comprehensive corporate tax return, Problem C:3-65, has all new numbers for the 2017 forms
- The comprehensive partnership tax return, Problem C:9-58, has all new numbers for the 2017 forms
- The comprehensive S corporation tax return, Problem C:11-62, has all new numbers for the 2017 forms
- All tax rate schedules have been updated to reflect the rates and inflation adjustments for 2018
- Whenever new updates become available, they will be accessible via MyLab Accounting

### SOLVING TEACHING AND LEARNING CHALLENGES

The Rupert/Anderson 2019 Series in Federal Taxation is appropriate for use in any first course in federal taxation, and comes in a choice of three volumes:

- Federal Taxation 2019: Individuals
- Federal Taxation 2019: Corporations, Partnerships, Estates & Trusts (the companion book to Individuals)
- Federal Taxation 2019: Comprehensive (14 chapters from Individuals and 15 chapters from Corporations)

\*\* For a customized edition of any of the chapters for these texts, contact your Pearson representative and he or she can create a custom text for you.

- The *Individuals* volume covers *all* entities, although the treatment is often briefer than in the *Corporations* and *Comprehensive* volumes. The *Individuals* volume, therefore, is appropriate for colleges and universities that require only one semester of taxation as well as those that require more than one semester of taxation. Further, this volume adapts the suggestions of the Model Tax Curriculum as promulgated by the American Institute of Certified Public Accountants.
- The *Corporations, Partnerships, Estates & Trusts* and *Comprehensive* volumes contain three comprehensive tax return problems whose data change with each edition, thereby keeping the problems fresh. Problem C:3-65 contains the comprehensive corporate tax return, Problem C:9-58 contains the comprehensive partnership tax return, and Problem C:11-62 contains the comprehensive S corporation tax return, which is based on the same facts as Problem C:9-58 so that students can compare the returns for these two entities.
- The *Corporations, Partnerships, Estates & Trusts* and *Comprehensive* volumes contain sections called Financial Statement Implications, which discuss the implications of Accounting Standards Codification (ASC) 740. The main discussion of accounting for income taxes appears in Chapter C:3. The financial statement implications of other transactions appear in Chapters C:7, C:8, and C:16 (*Corporations* volume only).

Rupert/Anderson 2019 Series in Federal Taxation has an appropriate blend of technical content of the tax law with a high level of readability for students. It is focused on enabling students to apply tax principles within the chapter to real-life situations using many strong pedagogical aids:

### Real-World Example

These comments relate the text material to events, cases, and statistics occurring in the tax and business environment. The statistical data presented in some of these comments are taken from the IRS's Statistics of Income at [www.irs.gov](http://www.irs.gov).

### Book-to-Tax Accounting Comparison

These comments compare the tax discussion in the text to the accounting and/or financial statement treatment of this material. Also, the last section of Chapter C:3 discusses the financial statement implications of federal income taxes.

### What Would You Do in This Situation?

Unique to the Rupert/Anderson series, these boxes place students in a decision-making role. The boxes include many *controversies* that are as yet unresolved or are currently being considered by the courts. These boxes make extensive use of **Ethical Material** as they represent choices that may put the practitioner at odds with the client.

### Stop & Think

These “speed bumps” encourage students to pause and apply what they have just learned. Solutions for each issue are provided in the box.

### Ethical Point

These comments provide the ethical implications of material discussed in the adjoining text. Apply what they have just learned.

### Tax Strategy Tip

These comments suggest tax planning ideas related to material in the adjoining text.

### Additional Comment

These comments provide supplemental information pertaining to the adjacent text.

## MyLab Accounting

---

### Reach Every Student with MyLab Accounting

MyLab is the teaching and learning platform that empowers you to reach every student. By combining trusted author content with digital tools and a flexible platform, MyLab personalizes the learning experience and improves results for each student. Learn more about MyLab Accounting at <https://www.pearsonmylabandmastering.com/>

**Powerful Homework and Test Manager** Create, import, and manage online homework and media assignments, quizzes, and tests. Create assignments from online questions directly correlated to this and other textbooks. Homework questions include “Help Me Solve This” guided solutions to help students understand and master concepts. You can choose from a wide range of assignment options, including time limits and maximum number of attempts allowed. In addition, you can create your own questions—or copy and edit ours—to customize your students’ learning path.

### Deliver Trusted Content

You deserve teaching materials that meet your own high standards for your course. That’s why we partner with highly respected authors to develop interactive content and course-specific resources that you can trust — and that keep your students engaged.

**Dynamic Study Modules** Dynamic Study Modules help students study effectively on their own by continuously assessing their activity and performance in real time. Here’s how it works: students complete a set of questions with a unique answer format that also asks them to indicate their confidence level. Questions repeat until the student can answer them all correctly and confidently. Once completed, Dynamic Study Modules explain the concept using materials from the text. These are available as graded assignments prior to class, and accessible on smartphones, tablets, and computers. Instructors can now remove questions from Dynamic Study Modules to better fit their course. Available for select titles.

### Empower Each Learner

Each student learns at a different pace. Personalized learning pinpoints the precise areas where each student needs practice, giving all students the support they need — when and where they need it — to be successful.

**Study Plan** The Study Plan acts as a tutor, providing personalized recommendations for each of your students based on his or her ability to master the learning objectives in your course. This allows students to focus their study time by pinpointing the precise areas they need to review, and allowing them to use customized practice and learning aids—such as videos, eText, tutorials, and more—to get them back on track. Using the report available in the Gradebook, you can then tailor course lectures to prioritize the content where students need the most support—offering you better insight into classroom and individual performance.