

Includes full coverage of the Tax Cuts and Jobs Act of 2017

SOUTH-WESTERN
FEDERAL TAXATION

Raabe
Young
Nellen
Maloney

ESSENTIALS OF TAXATION

Individuals and Business Entities

2019

Included:

THOMSON REUTERS
CHECKPOINT™

intuit
proconnect.

BECKER
PROFESSIONAL EDUCATION®

2017 Tax Rate Schedules

Single—Schedule X				Head of household—Schedule Z			
If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>	If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>
\$ 0	\$ 9,325	.....10%	\$ 0	\$ 0	\$ 13,350	.....10%	\$ 0
9,325	37,950	\$ 932.50 + 15%	9,325	13,350	50,800	\$ 1,335.00 + 15%	13,350
37,950	91,900	5,226.25 + 25%	37,950	50,800	131,200	6,952.50 + 25%	50,800
91,900	191,650	18,713.75 + 28%	91,900	131,200	212,500	27,052.50 + 28%	131,200
191,650	416,700	46,643.75 + 33%	191,650	212,500	416,700	49,816.50 + 33%	212,500
416,700	418,400	120,910.25 + 35%	416,700	416,700	444,550	117,202.50 + 35%	416,700
418,400	.....	121,505.25 + 39.6%	418,400	444,550	.....	126,950.00 + 39.6%	444,550
Married filing jointly or Qualifying widow(er)—Schedule Y-1				Married filing separately—Schedule Y-2			
If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>	If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>
\$ 0	\$ 18,650	.....10%	\$ 0	\$ 0	\$ 9,325	.....10%	\$ 0
18,650	75,900	\$ 1,865.00 + 15%	18,650	9,325	37,950	\$ 932.50 + 15%	9,325
75,900	153,100	10,452.50 + 25%	75,900	37,950	76,550	5,226.25 + 25%	37,950
153,100	233,350	29,752.50 + 28%	153,100	76,550	116,675	14,876.25 + 28%	76,550
233,350	416,700	52,222.50 + 33%	233,350	116,675	208,350	26,111.25 + 33%	116,675
416,700	470,700	112,728.00 + 35%	416,700	208,350	235,350	56,364.00 + 35%	208,350
470,700	.....	131,628.00 + 39.6%	470,700	235,350	.....	65,814.00 + 39.6%	235,350

2018 Tax Rate Schedules

Single—Schedule X				Head of household—Schedule Z			
If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>	If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>
\$ 0	\$ 9,525	.....10%	\$ 0	\$ 0	\$ 13,600	.....10%	\$ 0
9,525	38,700	\$ 952.50 + 12%	9,525	13,600	51,800	\$ 1,360.00 + 12%	13,600
38,700	82,500	4,453.50 + 22%	38,700	51,800	82,500	5,944.00 + 22%	51,800
82,500	157,500	14,089.50 + 24%	82,500	82,500	157,500	12,698.00 + 24%	82,500
157,500	200,000	32,089.50 + 32%	157,500	157,500	200,000	30,698.00 + 32%	157,500
200,000	500,000	45,689.50 + 35%	200,000	200,000	500,000	44,298.00 + 35%	200,000
500,000	.....	150,689.50 + 37%	500,000	500,000	.....	149,298.00 + 37%	500,000
Married filing jointly or Qualifying widow(er)—Schedule Y-1				Married filing separately—Schedule Y-2			
If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>	If taxable income is: Over—	<i>But not over—</i>	The tax is:	<i>of the amount over—</i>
\$ 0	\$ 19,050	.....10%	\$ 0	\$ 0	\$ 9,525	.....10%	\$ 0
19,050	77,400	\$ 1,905.00 + 12%	19,050	9,525	38,700	\$ 952.50 + 12%	9,525
77,400	165,000	8,907.00 + 22%	77,400	38,700	82,500	4,453.50 + 22%	38,700
165,000	315,000	28,179.00 + 24%	165,000	82,500	157,500	14,089.50 + 24%	82,500
315,000	400,000	64,179.00 + 32%	315,000	157,500	200,000	32,089.50 + 32%	157,500
400,000	600,000	91,379.00 + 35%	400,000	200,000	300,000	45,689.50 + 35%	200,000
600,000	.....	161,379.00 + 37%	600,000	300,000	.....	80,689.50 + 37%	300,000

Tax Formula for Individuals

Income (broadly defined).....	\$xx,xxx
Less: Exclusions.....	(x,xxx)
Gross income.....	\$xx,xxx
Less: Deductions for adjusted gross income.....	(x,xxx)
Adjusted gross income.....	\$xx,xxx
Less: The greater of—	
Total itemized deductions	
or standard deduction.....	(x,xxx)
Less: Personal and dependency exemptions*.....	(x,xxx)
Deduction for qualified business income**.....	(x,xxx)
Taxable income.....	\$xx,xxx
Tax on taxable income.....	\$ x,xxx
Less: Tax credits (including Federal income tax withheld and prepaid).....	(xxx)
Tax due (or refund).....	\$ xxx

*Exemption deductions are not allowed from 2018 through 2025.

**Only applies from 2018 through 2025.

Basic Standard Deduction Amounts

Filing Status	2017	2018
Single	\$ 6,350	\$12,000
Married, filing jointly	12,700	24,000
Surviving spouse	12,700	24,000
Head of household	9,350	18,000
Married, filing separately	6,350	12,000

Amount of Each Additional Standard Deduction

Filing Status	2017	2018
Single	\$1,550	\$1,600
Married, filing jointly	1,250	1,300
Surviving spouse	1,250	1,300
Head of household	1,550	1,600
Married, filing separately	1,250	1,300

Personal and Dependency Exemption

2017	2018*
\$4,050	\$4,150

*Note: Exemption deductions have been suspended from 2018 through 2025.



Powerful preparation. Maximum confidence.

The right tools to help prepare you for the Exam

With Becker Professional Education, you get a fully integrated CPA Exam Review course that helps you:

	<p>MOVE BEYOND MEMORIZATION TO APPLICATION Interactive simulations and videos move you beyond memorization, helping you apply concepts – a critical component of the CPA Exam.</p>	<p>CPA SkillMaster Videos Tackle Task-Based Simulations with confidence. Our expert instructors take you through the most complex questions step-by-step. <i>It's like having your own CPA coach!</i></p>
	<p>STUDY SMART Adapt2U pre-assessment provides you a recommended study path.</p>	
	<p>TRACK PROGRESS AND BUILD CONFIDENCE Mock exams, progress tests and a study planner help you focus on where you need the most help.</p>	
	<p>LEARN WHAT'S NEEDED Study with a course that replicates the CPA Exam.</p>	
	<p>CHOOSE FROM 3 FLEXIBLE COURSE FORMATS Choose from Self-Study, LiveOnline or Live Classroom formats.</p>	



AMT Formula for Individuals

Taxable income (increased by any standard deduction taken)

Plus or minus: Adjustments

Plus: Preferences

Equals: Alternative minimum taxable income (AMTI)

Minus: Exemption

Equals: Alternative minimum tax (AMT) base

Multiplied by: 26% or 28% rate

Equals: Tentative minimum tax before foreign tax credit

Minus: AMT foreign tax credit

Equals: Tentative minimum tax (TMT)

Minus: Regular tax liability (less any foreign tax credit)

Equals: AMT (if TMT > regular tax liability)

2017 AMT Exemption and Phaseout for Individuals

Filing Status	Exemption	Phaseout	
		Begins at	Ends at
Married, filing jointly	\$84,500	\$160,900	\$498,900
Single or Head of household	54,300	120,700	337,900
Married, filing separately	42,250	80,450	249,450

2018 AMT Exemption and Phaseout for Individuals

Filing Status	Exemption	Phaseout	
		Begins at	Ends at
Married, filing jointly	\$109,400	\$1,000,000	\$1,437,600
Single or Head of household	70,300	500,000	781,200
Married, filing separately	54,700	500,000	718,800

Income Tax Rates—Estates and Trusts

Tax Year 2018

Taxable Income		The Tax Is:	
Over—	But not Over—		Of the Amount Over—
\$ 0	\$ 2,550	10%	\$ 0
2,550	9,150	\$ 255.00 + 24%	2,550
9,150	12,500	1,839.00 + 35%	9,150
12,500	.....	3,011.50 + 37%	12,500

Income Tax Rates—C Corporations, 2018 and after

For all income levels, the tax rate is 21%.

Tax Formula for Corporate Taxpayers

Income (from whatever source).....	\$ xxx,xxx
Less: Exclusions from gross income.....	— xx,xxx
Gross Income	\$ xxx,xxx
Less: Deductions.....	— xx,xxx
Taxable Income	\$ xxx,xxx
Tax rate.....	× 21%
Gross Tax	\$ xx,xxx
Less: Tax credits and prepayments.....	— x,xxx
Tax Due (or refund)	\$ xx,xxx



ProConnect™ Tax Online

Work like a pro.

Get the #1 cloud-based professional tax software for free.^{1,2}

Go beyond the basics and connect with the modern tools you need to work efficiently.

- **Work with confidence.**

Get returns done right the first time with access to all the forms you need, backed by industry-leading calculations and diagnostics.

- **Work smarter.**

Save time with logical data-entry worksheets instead of traditional forms-based methods. Plus, get quick training resources so it's easy to stay up to speed.

- **Work from anywhere.**

It's all online, so there's nothing to install or maintain. And whether you're on your mobile phone or laptop, PC or Mac – you're always good to go.

Visit [TaxEducation.Intuit.com](https://taxeducation.intuit.com) to get started.

Only one sign-up per student. No special code required. If you have trouble accessing or using the software, reach out to us at taxeducation_support@intuit.com anytime for help.

¹Based on Intuit internal data of the number of paid users of ProConnect Tax Online for Tax Year 2016 compared to publicly available statements from competitors for the same time period.

²If you sign-up for the free version of ProConnect Tax Online for students and educators, you will not have access to certain features, including functionality such as Electronic Filing Services and Intuit Link.

SOUTH-WESTERN
FEDERAL TAXATION

2019 EDITION
ESSENTIALS OF
TAXATION: INDIVIDUALS
AND BUSINESS ENTITIES

General Editors

William A. Raabe
Ph.D., CPA
Madison, Wisconsin

James C. Young
Ph.D., CPA
Northern Illinois University

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

David M. Maloney
Ph.D., CPA
University of Virginia

Contributing Authors

Hughlene A. Burton
Ph.D., CPA
University of North Carolina-Charlotte

Gregory Carnes
Ph.D., CPA
University of North Alabama

Andrew Cuccia
Ph.D., CPA
University of Oklahoma

William A. Raabe
Ph.D., CPA
Madison, Wisconsin

Toby Stock
Ph.D.
Ohio University

Kristina Zvinakis
Ph.D.
The University of Texas at Austin

SWFT Series Authors

James H. Boyd
Ph.D., CPA
Arizona State University

D. Larry Crumbley
Ph.D., CPA
Louisiana State University

Steven C. Dilley
J.D., Ph.D., CPA
Michigan State University

Steven L. Gill
Ph.D., CPA
San Diego State University

William H. Hoffman, Jr.
J.D., Ph.D., CPA
University of Houston

David M. Maloney
Ph.D., CPA
University of Virginia

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

Mark B. Persellin
Ph.D., CPA, CFP
St. Mary's University

Debra L. Sanders
Ph.D., CPA
Washington State
University, Vancouver

W. Eugene Seago
J.D., Ph.D., CPA
Virginia Polytechnic
Institute and State
University

James C. Young
Ph.D., CPA
Northern Illinois
University



**South-Western Federal Taxation:
Essentials of Taxation, 2019 Edition**

**William A. Raabe, James C. Young,
Annette Nellen, David M. Maloney**

Senior Vice President, Higher Ed Product, Content,
and Market Development: Erin Joyner

Product Director: Jason Fremder

Sr. Product Manager: John Barans

Sr. Content Manager: Nadia Saloom

Learning Designer: Jonathan Gross

Product Assistant: Aiyana Moore

Marketing Manager: Christopher P. Walz

Sr. Digital Delivery Lead: Tim Richison

Production Service: SPi Global

Senior Designer: Bethany Bourgeois

Text and Cover Designer: Red Hangar Design

Cover Image: John Lund/Blend Images/
Getty Images

Intellectual Property:

Analyst: Reba Frederics

Project Manager: Carly Belcher

Design Images:

Concept Summary, Global Tax Issues,

Bridge Discipline: iStock.com/enot-poloskun

Ethics & Equity: iStock.com/LdF

Problems/Tax Return Problems:

iStock.com/peepo

Financial Disclosure Insights: Vyaseleva Elena/
Shutterstock.com

Shutterstock.com

Tax Planning Strategies: Sergey Nivens/
Shutterstock.com

Shutterstock.com

Tax Fact: carroteater/Shutterstock.com

Digging Deeper: tuulijumala/Shutterstock.com

© 2019, 2018 Cengage Learning, Inc.

Unless otherwise noted, all content is © Cengage.

ALL RIGHTS RESERVED. No part of this work covered by the copyright herein may be reproduced or distributed in any form or by any means, except as permitted by U.S. copyright law, without the prior written permission of the copyright owner.

For product information and technology assistance, contact us at
**Cengage Customer & Sales Support, 1-800-354-9706 or
support.cengage.com.**

For permission to use material from this text or product,
submit all requests online at www.cengage.com/permissions.

All tax forms within the text are: Source: Internal Revenue Service

Tax software: Source: Intuit ProConnect

Becker CPA Review: Source: Becker CPA

ISSN: 1544-3590

2019 Annual Edition

Student Edition ISBN: 978-1-337-70297-3

Student Edition with Intuit ProConnect + RIA Checkpoint

ISBN: 978-1-337-70296-6

Cengage

20 Channel Center Street

Boston, MA 02210

USA

Cengage is a leading provider of customized learning solutions with employees residing in nearly 40 different countries and sales in more than 125 countries around the world. Find your local representative at www.cengage.com.

Cengage products are represented in Canada by Nelson Education, Ltd.

To learn more about Cengage platforms and services, register or access your online learning solution, or purchase materials for your course, visit www.cengage.com.



Preface

COMMITTED TO EDUCATIONAL SUCCESS

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

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

Essentials of Taxation: Individuals and Business Entities, 2019 Edition provides a dynamic learning experience inside and outside of the classroom. Built with resources and tools that have been identified as the most important, our complete learning system provides options for students to achieve success.

Essentials of Taxation: Individuals and Business Entities, 2019 Edition provides accessible, comprehensive, and authoritative coverage of the relevant tax code and regulations as they pertain to the individual or business taxpayer, as well as coverage of all major developments in Federal Taxation. This edition has been fully updated and revised to reflect changes included in the Tax Cuts and Jobs Act of 2017.

In revising the 2019 Edition, we focused on:

- **Accessibility. Clarity. Substance.** The text authors and editors made this their mantra as they revised the 2019 edition. Coverage has

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

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

Learning Tools and Features to Help Students Make the Connection

FULL-COLOR DESIGN: We understand that students struggle with learning difficult tax code concepts and applying them to real-world scenarios. The 2019 edition uses color to bring the text to life, capture student attention, and present the tax code in a simple, yet logical format.

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



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



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

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

Computational Exercises

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

BECKER PROFESSIONAL EDUCATION REVIEW QUESTIONS: End-of-chapter CPA review questions from Becker PREPARE STUDENTS FOR SUCCESS. Students review key concepts using proven questions from Becker Professional Education®—one of the industry's most effective tools to prepare for the CPA Exam.

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

Becker CPA Review Questions

- On January 1, year 5, Olinto Corp., an accrual basis, calendar year C corporation, had \$35,000 in accumulated earnings and profits. For year 5, Olinto had current earnings and profits of \$15,000 and made two \$40,000 cash distributions to its shareholders, one in April and one in September of year 5. What amount of the year 5 distributions is classified as dividend income to Olinto's shareholders?
 - \$15,000
 - \$35,000
 - \$50,000
 - \$80,000
- Fox Corp. owned 2,000 shares of Duffy Corp. stock that it bought in year 0 for \$9 per share. In year 8, when the fair market value of the Duffy stock was \$20 per share, Fox distributed this stock to a noncorporate shareholder. Fox's recognized gain on this distribution was:
 - \$40,000
 - \$22,000
 - \$18,000
 - \$0



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

THE BIG PICTURE

TAXES ON THE FINANCIAL STATEMENTS

Raymond Jones, the CEO of Acme Corporation, would like some help reconciling the amount of income tax expense on Acme's financial statements with the amount of income tax reported on the company's corporate income tax return for its first year of operations. He knows that an adjustment may be used simply to adjust the financial statement income by the company's combined federal and state 25 percent marginal income tax rate to get the financial tax expense. While the financial statements show book income before tax of \$75 million, the reported income tax expense is only \$5 million. In addition, the corporate tax return reports taxable income of \$10 million and federal income taxes payable of \$1.0 million (\$10 million \times 10%).

Without knowing the specifics of the company's financial statements, does Acme's situation look reasonable? Why is Acme's financial accounting tax expense not equal to \$6.25 million (\$75 million \times 10%)? What causes the \$1.0 million difference between the taxes derived on the financial statements and the taxes due on the tax return?

Read the chapter and determine your response.

THE BIG PICTURE: Tax Solutions for the Real World.

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

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

BRIDGE DISCIPLINE BOXES AND END-OF-CHAPTER QUESTIONS:

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

BRIDGE DISCIPLINE: Bridge to Financial Analysis

Financial analysts perform an important function for the capital markets in their detailed analysis of companies. The analyst works through the financial reports and other information about a company to produce an informed opinion on how a company is performing. Analysts' earnings forecasts often constitute an important factor in deciding when making decisions about investing in companies.

An experienced financial analyst typically will have a good handle on interpreting financial statement information.

However, even experienced analysts often will "stare" when it comes to interpreting the tax information contained in a financial statement, preferring to look at net income before taxes or even EBITDA, earnings before interest, taxes, depreciation, and amortization.

A great deal of useful information about a business is contained in its tax footnotes, and analysts might have an edge if they work at understanding the mysteries of taxes in the financial statements.

FINANCIAL DISCLOSURE INSIGHTS: Tax Losses and the Deferred Tax Asset

Although a current-year net operating loss (NOL) represents a failure of an entity's business model to some, others see it as an immediate tax refund. But when an NOL hits the balance sheet as a deferred tax asset, the story is not over. The NOL creates or increases a deferred tax asset that may or may not be used in future financial accounting reporting periods. The key question for a financial analyst is whether the entity will generate enough net revenue in future years to create a

positive tax liability that can be offset by the NOL carryover amount.

IFRS rules do not allow for a valuation allowance. Under IAS 12, a deferred tax asset is recorded only when it is "probable" (a higher standard than GAAP's "more likely than not") that the deferred tax amount will be realized, and then only to the extent of that probable amount. Thus, no offsetting valuation allowance is needed.

FINANCIAL DISCLOSURE INSIGHTS:

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

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

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

1 DIGGING DEEPER

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

EXHIBIT 1.3 General Framework for Income Tax Planning		
Tax Formula	Tax Planning Strategy	Tax Planning Examples
Income and exclusions	→ Avoid income recognition.	Compensate employees with nonqualifying fringe benefits (see Example 19).
	→ Postpone recognition of income to achieve tax deferral.	Postpone sale of assets (see Example 20).
- Deductions	→ Maximize deductible amounts.	Invest in stock of another corporation (see Example 21).
	→ Accelerate recognition of deductions to achieve tax deferral.	Elect to deduct charitable contribution in year of pledge rather than in year of payment (see Example 22).

TAX PLANNING STRATEGIES: NEVER TO HAVE OR HAVE NOT
FRAMEWORK FOCUS: TAX RATE

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

When preparing to avoid establishing a new business, for example, by providing a sales representative with a cash sales allowance (other than a company car, by restricting the location of inventory to only a few states, or by limiting a salesperson's activities to those that are protected by the solicitation exemption of 15, 80, 212). The effort to avoid new taxes is just from the additional compliance burden that falls upon the taxpayer when a new set of income tax returns, information returns, and deadlines must be dealt with in the new state.

Another concern is that the marginal tax rate that applies to the sale of the business generated by the taxpayer may increase. Such a tax increase occurs if income shifts when the applicable tax rate in the new state is higher than the rate that would apply in the home state. If income were already in hand in a low-tax state such as Florida or Texas, it is in the state with the lowest tax rate. As aggregate tax liability is sure to increase.

NET income is not necessarily a cash flow. Consider what happens if a business based in California, Maryland, Missouri, or another high-tax jurisdiction purposely sets up a new office in a low- or no-tax state. If the new state applies a lower marginal rate than is available in the home state or offers special exemptions or reductions that reach the taxpayer's operations, the aggregate tax liability decreases. Thus, the planning effort includes determining which activities will be moved to the new jurisdiction and avoiding or minimizing the cost.

For instance, an entrepreneur based in Maryland is subject to the high income tax rates of that state and may have been able to establish a permanent office in Wisconsin, where a lower rate would be applied, and some portion of the taxpayer's income will be subject to neither state, instead of the high rates. There are numerous examples, including considerations of other tax issues and the share price of the stock of the taxpayer.

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

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

GLOBAL TAX ISSUES: Filing a Joint Return

John Garth is a U.S. citizen and resident, but he spends much of his time in London, where his employer sends him on frequent assignments. John is married to Victoria, a citizen and resident of the United Kingdom.

Can John and Victoria file a joint return for U.S. Federal income tax purposes? Although § 6013(a)(1) specifically precludes the filing of a joint return if one spouse is a nonresident alien, another Code provision permits an exception. Under § 6013(g), the parties can elect to treat the nonqualifying spouse as a "resident" of the United States. This election would allow John and Victoria to file jointly.

But should John and Victoria make this election? If Victoria has considerable income of her own (from non-U.S. sources), the election could be ill-advised. As a nonresident alien, Victoria's non-U.S. source income would not be subject to the U.S. income tax, if she is treated as a U.S. resident, however, her non-U.S. source income will be subject to U.S. tax. Under the U.S. worldwide approach to taxation, all income (regardless of where earned) of anyone who is a resident or citizen of the United States is subject to tax.

Take your students from Motivation to Mastery with CengageNOWv2

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

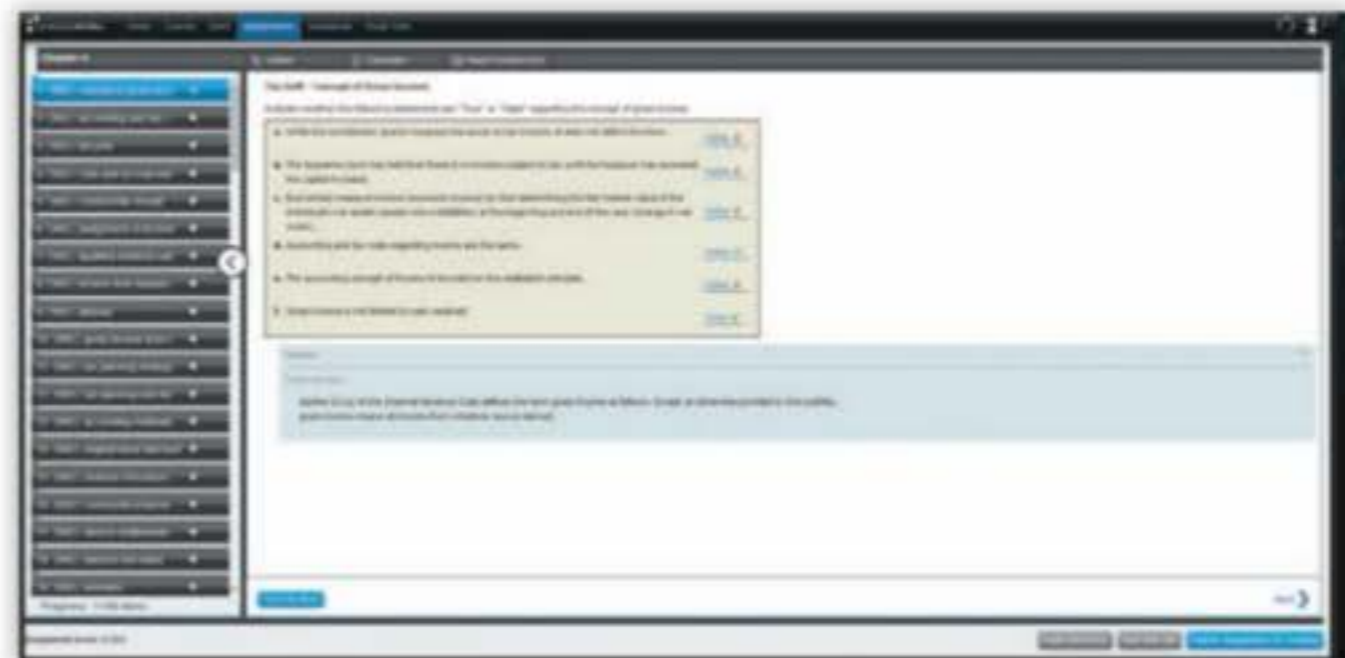


- ❑ **MOTIVATION:** engage students and better prepare them for class
- ❑ **APPLICATION:** help students learn problem-solving behavior and skills to guide them to complete taxation problems on their own
- ❑ **MASTERY:** help students make the leap from memorizing concepts to actual critical thinking

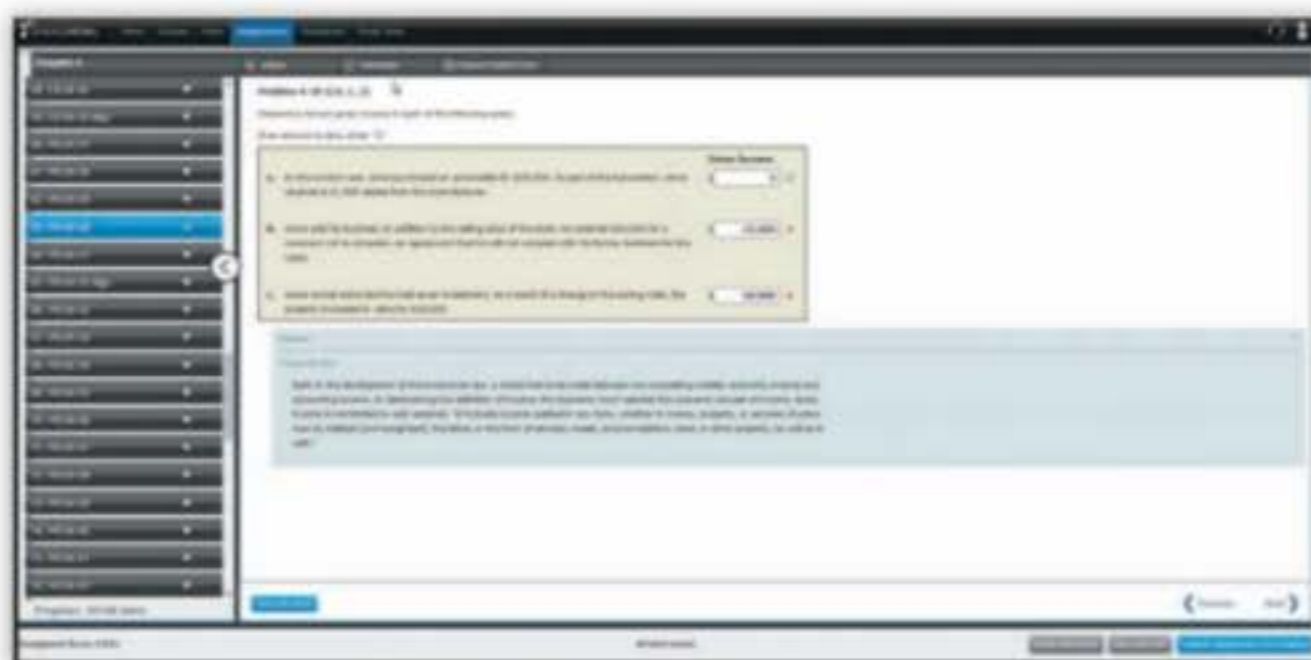
Motivation —

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

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



Application —



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

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

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

Mastery —

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

CengageNOWv2 Instant Access Code ISBN:
978-1-337-70376-5

Contact your Cengage Learning Consultant about different bundle options.



EXTENSIVELY REVISED. DEFINITELY UP TO DATE.

Each year the *South-Western Federal Taxation* series is updated with thousands of changes to each text. Some of these changes result from the feedback we receive from instructors and students in the form of reviews, focus groups, web surveys, and personal e-mail correspondence with our authors and team members. Other changes come from our careful analysis of the evolving tax environment. **Every tax law change relevant to the introductory taxation course was considered, summarized, and fully integrated into the revision of text and supplementary materials. This edition is fully updated and revised to reflect changes included in the Tax Cuts and Jobs Act (TCJA) of 2017. (Public Law 115-97; 12/22/17).**

The *South-Western Federal Taxation* authors have made every effort to keep all materials up to date and accurate. All chapters contain the following general changes for the 2019 Edition.

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

In addition, the following materials are available online.

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

Chapter 1

- Updated Exhibit 1.1 (Federal Tax Revenues) and Exhibit 1.4 (IRS Audit Types and Rates) with current data.
- Revised text to reflect the TCJA of 2017 and revised various inflation-adjusted information in the chapter.

- Added a new Research Problem to analyze a soda tax or sweetened beverage tax proposal against the AICPA's *Principles of Good Tax Policy*.

Chapter 2

- Created a new fact pattern for the Big Picture.
- Updated the Conference Committee Exhibit 2.2 for the TCJA of 2017.

Chapter 3

- Referenced the revised revenue recognition rules required by GAAP.
- Revised the comments regarding the balance sheet treatment of the deferred tax accounts.
- Updated data for goodwill on the balance sheet for certain U.S. corporations.
- Updated end-of-chapter materials, including Research Problems (including a reference to a recent Institute on Taxation and Economic Policy report).

Chapter 4

- Updated for changes made by the TCJA of 2017, such as to accounting methods and tax rates.
- Added basics of FBAR reporting requirements (Digging Deeper 4).

Chapter 5

- Added new materials related to the TCJA of 2017, including accounting method changes for both accrual and cash method corporations, executive compensation issues (including performance-based compensation now covered by the \$1 million limit, changing the definitions of "covered employees" and "publicly held corporation"), expanding the disallowance for fines and penalties, and disallowing deductions for local lobbying expenses.
- Updated material on research and experimental expenditures for changes made by the TCJA of 2017.
- Updated material to reflect TCJA of 2017 changes, including expanded immediate expensing, unlimited bonus depreciation, and changes to listed property rules.
- Added materials and examples related to using immediate expensing and bonus depreciation effectively.
- Modified other existing material to reflect changes dictated by the TCJA of 2017.

Chapter 6

- Added LO 11 and text Section 6-8 on the excess business loss limitation rule added by the TCJA of 2017.
- Updated casualty loss materials to reflect that personal casualty losses only allowed if due to a Federally declared disaster. Updated materials on personal casualty gain and loss netting.
- Revised net operating loss materials updated for changes by the TCJA of 2017.
- Made changes for clarity and simplicity.
- Updated end-of-chapter materials to reflect changes made by the TCJA of 2017.

Chapter 7

- Updated and revised for TCJA of 2017 changes.
- Added communications component to several end-of-chapter problems.
- Identified end-of-chapter problems that include a critical thinking component.

Chapter 8

- Modified the materials related to the definition of capital assets based on TCJA of 2017 changes (related to patents).
- Modified the material on the calculation of the alternative tax on net capital gains and qualified dividend income to reflect changes made by the TCJA of 2017.
- Updated end-of-chapter materials for the TCJA of 2017 and identified critical thinking items.
- Added communications requirements to several end-of-chapter problems.

Chapter 9

- Eliminated learning objective and section on personal exemptions.
- Added new section on AMT and NIIT.
- Updated to reflect changes made by the TCJA of 2017, including tax rates, standard deduction, the child and dependent tax credits, AMT, and the new calculation of the kiddie tax.
- Added information about new Form 1040SR that starts in 2019.
- Updated chapter materials to reflect inflation adjustments.
- Revised and clarified materials as needed throughout the chapter.
- Updated end-of-chapter materials to reflect TCJA of 2017 changes and inflation adjustments.

Chapter 10

- Added a crowdfunding question to the Big Picture.
- Made modifications to remove miscellaneous itemized deduction due to the TCJA of 2017.
- Updated to reflect changes made by the TCJA of 2017, including deductions and the child and dependent tax credits.
- Updated chapter materials to reflect inflation adjustments.
- Revised and clarified materials as needed throughout the chapter.
- Updated end-of-chapter materials to reflect TCJA of 2017 changes and inflation adjustments.

Chapter 11

- Streamlined coverage throughout the chapter; added multiple examples to illustrate text material.
- Updated materials for inflation adjustments.
- Clarified discussion of employee v. contractor issues.
- Explained the effects of TCJA of 2017 on various employee expenses, including meals and entertainment, teachers' expenses, moving costs, and legacy itemized deductions.
- Provided extensive materials concerning the deduction for qualified business income.
- Added material concerning documentation of employee expenditures.

Chapter 12

- Updated for the TCJA of 2017.
- Added new content on the business interest deduction limitation, excessive executive compensation, and restrictions on corporate accumulations.
- Revised end-of-chapter materials extensively to reflect TCJA of 2017 changes; added communications component to several problems; added Microsoft Excel component to one problem.

Chapter 13

- Updated chapter for changes made by the TCJA of 2017, including tax rates and repeal of the § 199 deduction.
- Revised and updated chapter materials as needed; clarified chapter materials when necessary.
- Updated end-of-chapter materials as needed.

Chapter 14

- Clarified definitions of general and limited partners.
- Streamlined discussion of four major types of partnerships.
- Changed from “nonliquidating distribution” to “current distribution” throughout, but kept reference to nonliquidating distributions as an alternative term.
- Integrated a discussion of the deduction for qualified business income as it pertains to partnerships and limited liability entities.
- Clarified and expanded comparisons of partnerships and C corporations (and aggregate and entity theories) throughout.

Chapter 15

- Revised materials affected by the TCJA of 2017, including the application of the § 199A deduction.
- Clarified AAA treatment of unrecognized losses for distributed property.

Chapter 16

- Updated for changes made by the TCJA of 2017 regarding international provisions.

Chapter 17

- Revised business credit materials affected by the TCJA of 2017, including the rehabilitation tax credit, foreign tax credit, and the new family leave credit.
- Revised material affected by the TCJA of 2017, including individual AMT exemption amounts and repeal of corporate AMT.
- Expanded solution and explanations for Microsoft Excel problems.

Chapter 18

- Clarified the availability of limited liability by business entities at the state level.
- Revised materials affected by the TCJA of 2017, including tax rates, distribution policies, the application of the § 199A deduction, and the use of NOLs.

TAX LAW OUTLOOK

From your SWFT Series Editors

Given the significant changes made by the Tax Cuts and Jobs Act of 2017, we are anticipating guidance from the Treasury Department and IRS in many areas, including the qualified business income deduction, excess business losses, net operating losses, and various changes to itemized deductions (including the cap on state and local taxes). Taxpayers and their advisors will be evaluating how all of these changes affect their financial planning strategies and will adjust their plans appropriately.

Small businesses will deliberate about the tax and legal form in which they should organize, taking into account the QBI deduction and other 2017 tax law changes. State and local issues will focus on the forms of interstate transactions and new definitions of nexus, and multinational businesses will deal with the new rules that move toward a territorial approach to cross-border taxation.

The SWFT editors will be monitoring these activities and provide updates to adopters as needed.

SUPPLEMENTS SUPPORT STUDENTS AND INSTRUCTORS

Built around the areas students and instructors have identified as the most important, our integrated supplements package offers more flexibility than ever before to suit the way instructors teach and students learn.

Online and Digital Resources for Students



CengageNOWv2 is a powerful course management and online homework tool that provides robust instructor control and customization to optimize the student learning experience and meet desired outcomes.

CengageNOWv2 Instant Access Code ISBN:
978-1-337-70376-5

Contact your Cengage Learning Consultant about different bundle options.

THOMSON REUTERS CHECKPOINT™ Thomson Reuters Checkpoint™ is the leading online tax research database used by professionals. There are three simple ways Checkpoint™ helps introduce students to tax research:

- Intuitive web-based design makes it fast and simple to find what you need.
- Checkpoint™ provides a comprehensive collection of primary tax law, cases, and rulings along with analytical insight you simply can't find anywhere else.
- Checkpoint™ has built-in productivity tools such as calculators to make research more efficient—a resource more tax pros use than any other.

Six months' access to Checkpoint™ (after activation) is packaged automatically with every NEW copy of the textbook.*

intuit proconnect™ More than software: Put the experience of ProConnect™ Tax Online on your side.

- Get returns done right the first time with access to all the forms you need, backed by industry-leading calculations and diagnostics.
- Save time with logical data-entry worksheets instead of traditional forms-based methods.
- It's all online, so there's nothing to install or maintain.

Online access to ProConnect™ Tax Online software is offered with each NEW copy of the textbook—at no additional cost to students.*

CENGAGE.com Students can use **Cengage.com** to select this textbook and access Cengage Learning content, empowering them to choose the most suitable format and giving them a better chance of success in the course. Buy printed materials, eBooks, and digital resources directly through Cengage Learning and save at **Cengage.com**.

Online Student Resources

Students can go to **www.cengage.com** for free resources to help them study as well as the opportunity to purchase additional study aids. These valuable free study resources will help students earn a better grade:

- Flashcards use chapter terms and definitions to aid students in learning tax terminology for each chapter.
- Online glossary for each chapter provides terms and definitions from the text in alphabetical order for easy reference.
- Learning objectives can be downloaded for each chapter to help keep students on track.
- Tax tables used in the textbook are downloadable for reference.

CENGAGE UNLIMITED The first-of-its-kind digital subscription designed specially to lower costs.

Students get total access to everything Cengage has to offer on demand—in one place. That's 20,000 eBooks, 2,300 digital learning products, and dozens of study tools across 70 disciplines and over 675 courses.

www.cengage.com/unlimited

Printed Resources for Students

Looseleaf Edition (978-1-337-70298-0)

This version provides all the pages of the text in an unbound, three-hole punched format for portability and ease of use. Online access to ProConnect™ Tax Online software is included with every NEW textbook as well as Checkpoint™ from Thomson Reuters.*

*NEW printed copies of the textbook are automatically packaged with access to Checkpoint™ and Intuit ProConnect™ Tax Online tax software. If students purchase the eBook, they will not automatically receive access to Checkpoint™ and Intuit ProConnect™ Tax Online software. They must purchase the tax media pack offering both of these products. The ISBN is 978-1-337-70176-1 and can be purchased at **www.cengage.com**.

Comprehensive Supplements Support Instructors' Needs



CengageNOWv2 is a powerful course management and online homework tool that provides robust instructor control and customization to optimize the student learning experience and meet desired outcomes. In addition to the features and benefits mentioned earlier for students, CengageNOWv2 includes these features for instructors:

- **Learning Outcomes Reporting** and the ability to analyze student work from the gradebook. Each exercise and problem is tagged by topic, learning objective, level of difficulty, estimated completion time, and business program standards to allow greater guidance in developing assessments and evaluating student progress.
- **Built-in Test Bank for online assessment.** The Test Bank files are included in CengageNOWv2 so that they may be used as additional homework or tests.

Solutions Manual

Written by the *South-Western Federal Taxation* editors and authors, the Solutions Manual features solutions arranged in accordance with the sequence of chapter material.

Solutions to all homework items are tagged with their Estimated Time to Complete, Level of Difficulty, and Learning Objective(s), as well as the AACSB's and AICPA's core competencies—giving instructors more control than ever in selecting homework to match the topics covered. The Solutions Manual also contains the lettered answers (only) to the end-of-chapter Becker CPA Review Questions. **Available on the Instructor Companion Website at www.cengage.com/login.**

PowerPoint® Lectures with Notes

The Instructor PowerPoint® Lectures contain more than 30 slides per chapter, including outlines and instructor guides, concept definitions, and key points. **Available on the Instructor Companion Website at www.cengage.com/login.**

Test Bank

Written by the *South-Western Federal Taxation* editors and authors, the Test Bank contains approximately 2,200 items and solutions arranged in accordance with the sequence of chapter material.

Each test item is tagged with its Estimated Time to Complete, Level of Difficulty, and Learning Objective(s),

as well as the AACSB's and AICPA's core competencies—for easier instructor planning and test item selection. The 2019 Test Bank is available in Cengage's test generator software, Cognero.

Cengage Learning Testing Powered by Cognero is a flexible, online system that allows you to:

- author, edit, and manage Test Bank content from multiple Cengage Learning solutions
- create multiple test versions in an instant
- deliver tests from your LMS, your classroom, or wherever you want
- create tests from school, home, the coffee shop—anywhere with internet access. (No special installs or downloads needed.)

Test Bank files in Word format as well as versions to import into your LMS are available on the Instructor Companion Website. **Cognero Test Banks available via single sign-on (SSO) account at www.cengage.com/login.**

Other Instructor Resources

All of the following instructor course materials are available online at www.cengage.com/login. Once logged into the site, instructors should select this textbook to access the online Instructor Resources.

- Instructor Guide
- Edition-to-edition correlation grids by chapter
- Detailed answer feedback for the end-of-chapter Becker CPA Review Questions in Word format (Lettered answers only are available in the Solutions Manual.)
- An appendix that helps instructors broaden and customize coverage of important tax provisions of the Affordable Care Act
- The Depreciation and the Accelerated Cost Recovery System (ACRS) appendix

Custom Solutions

Cengage Learning Custom Solutions develops personalized solutions to meet your taxation education needs. Consider the following for your adoption of *South-Western Federal Taxation 2019 Edition*.

- Remove chapters you do not cover or rearrange their order to create a streamlined and efficient text.
- Add your own material to cover new topics or information.
- Add relevance by including sections from Sawyers/Gill's *Federal Tax Research* or your state's tax laws and regulations.

ACKNOWLEDGMENTS

We want to thank all the adopters and others who participated in numerous online surveys as well as the following individuals who provided content reviews and feedback in the development of the *South-Western Federal Taxation* 2019 titles.

William A. Raabe / James C. Young / Annette Nellen / David M. Maloney

- Lindsay G. Acker, *University of Wisconsin-Madison*
 Deborah S. Adkins, *Nperspective, LLC*
 Mark P. Altieri, *Kent State University*
 Amy An, *University of Iowa*
 Susan E. Anderson, *Elon University*
 Henry M. Anding, *Woodbury University*
 Jennifer A. Bagwell, *Ohio University*
 George Barbi, *Lanier Technical College*
 Terry W. Bechtel, *Texas A&M University – Texarkana*
 Chris Becker, *LeMoyne College*
 John G. Bell
 Tamara Berges, *UCLA*
 Ellen Best, *University of North Georgia*
 Tim Biggart, *Berry College*
 Rachel Birkey, *Illinois State University*
 Patrick M. Borja, *Citrus College / California State University, Los Angeles*
 Dianne H. Boseman, *Nash Community College*
 Cathalene Bowler, *University of Northern Iowa*
 Madeline Brogan, *Lone Star College – Montgomery*
 Darryl L. Brown, *Illinois Wesleyan University*
 Timothy G. Bryan, *University of Southern Indiana*
 Robert S. Burdette, *Salt Lake Community College*
 Ryan L. Burger, *Concordia University Nebraska*
 Lisa Busto, *William Rainey Harper College*
 Julia M. Camp, *Providence College*
 Al Case, *Southern Oregon University*
 Machiavelli W. Chao, *Merage School of Business University of California, Irvine*
 Eric Chen, *University of Saint Joseph*
 Christine Cheng, *Louisiana State University*
 James Milton Christianson, *Southwestern University and Austin Community College*
 Wayne Clark, *Southwest Baptist University*
 Ann Burstein Cohen, *University at Buffalo, The State University of New York*
 Ciril Cohen, *Fairleigh Dickinson University*
 Dixon H. Cooper, *University of Arkansas*
 Rick L. Crosser, *Metropolitan State University of Denver*
 John P. Crowley, *Castleton University*
 Richard G. Cummings, *University of Wisconsin-Whitewater*
 Susan E. M. Davis, *South University*
 Dwight E. Denman, *Newman University*
 James M. DeSimpelare, *Ross School of Business at the University of Michigan*
 John Dexter, *Northwood University*
 James Doering, *University of Wisconsin – Green Bay*
 Michael P. Donohoe, *University of Illinois at Urbana Champaign*
 Deborah A. Doonan, *Johnson & Wales University*
 Monique O. Durant, *Central Connecticut State University*
 Wayne L. Edmunds, *Virginia Commonwealth University*
 Rafi Efrat, *California State University, Northridge*
 Charles R. Enis, *The Pennsylvania State University*
 Frank J. Faber, *St. Joseph's College*
 A. Anthony Falgiani, *University of South Carolina, Beaufort*
 Jason Fiske, *Thomas Jefferson School of Law*
 John Forsythe, *Eagle Gate College*
 Alexander L. Frazin, *University of Redlands*
 Carl J. Gabrini, *College of Coastal Georgia*
 Kenneth W. Gaines, *East-West University, Chicago, Illinois*
 Carolyn Galantine, *Pepperdine University*
 Sheri Geddes, *Hope College*
 Alexander Gelardi, *University of St. Thomas*
 Daniel J. Gibbons, *Waubensee Community College*
 Martie Gillen, *University of Florida*
 Charles Gnizak, *Fort Hays State University*
 J. David Golub, *Northeastern University*
 George G. Goodrich, *John Carroll University*
 Marina Grau, *Houston Community College – Houston, TX*
 Vicki Greshik, *University of Jamestown College*
 Jeffrey S. Haig, *Santa Monica College*
 Marcy S. Hampton, *University of Central Florida*
 June Hanson, *Upper Iowa University*
 Donald Henschel, *Benedictine University*
 Susanne Holloway, *Salisbury University*
 Susan A. Honig, *Herbert H. Lehman College*
 Jeffrey Hoopes, *University of North Carolina*
 Christopher R. Hoyt, *University of Missouri (Kansas City) School of Law*
 Marsha M. Huber, *Youngstown State University*
 Carol Hughes, *Asheville-Buncombe Technical Community College*
 Helen Hurwitz, *Saint Louis University*
 Richard R. Hutaff, *Wingate University*
 Zite Hutton, *Western Washington University*
 Brad Van Kalsbeek, *University of Sioux Falls*
 John E. Karayan, *Woodbury University*
 Carl Keller, *Missouri State University*
 Cynthia Khanlarian, *Concord University*
 Bob Kilpatrick, *Northern Arizona University*
 Gordon Klein, *Lecturer, UCLA Anderson School*
 Taylor Klett, *Sam Houston State University*
 Aaron P. Knappe, *Peru State College*
 Cedric Knott, *Colorado State University – Global Campus*
 Ausher M. B. Kofsky, *Western New England University*
 Emil Koren, *Saint Leo University*
 Jack Lachman, *Brooklyn College – CUNY*
 Richard S. Leaman, *University of Denver*
 Adena Lejeune, *Louisiana College*
 Gene Levitt, *Mayville State University*
 Teresa Lightner, *University of North Texas*
 Sara Linton, *Roosevelt University*
 Roger Lirely, *The University of Texas at Tyler*
 Jane Livingstone, *Western Carolina University*
 Heather Lynch, *Northeast Iowa Community College*
 Michael J. MacDonald, *University of Wisconsin-Whitewater*
 Mabel Machin, *Florida Institute of Technology*
 Maria Alaina Mackin, *ECPI University*
 Anne M. Magro, *George Mason University*
 Richard B. Malamud, *California State University, Dominguez Hills*
 Harold J. Manasa, *Winthrop University*
 Barry R. Marks, *University of Houston – Clear Lake*
 Dewey Martin, *Husson University*
 Anthony Masino, *East Tennessee State University*
 Norman Massel, *Louisiana State University*
 Bruce W. McClain, *Cleveland State University*
 Allison M. McLeod, *University of North Texas*
 Meredith A. Menden, *Southern New Hampshire University*
 Robert H. Meyers, *University of Wisconsin-Whitewater*
 John G. Miller, *Skyline College*

- Tracie L. Miller-Nobles, *Austin Community College*
 Jonathan G. Mitchell, *Stark State College*
 Richard Mole, *Hiram College*
 David Morack, *Lakeland University*
 Lisa Nash, CPA, MA, *Vincennes University*
 Mary E. Netzler, *Eastern Florida State College*
 Joseph Malino Nicassio, *Westmoreland County Community College*
 Mark R. Nixon, *Bentley University*
 Garth Novack, *Pantheon Heavy Industries & Foundry*
 Claude R. Oakley, *DeVry University, Georgia*
 Al Oddo, *Niagara University*
 Sandra Owen, *Indiana University – Bloomington*
 Vivian J. Paige, *Old Dominion University*
 Carolyn Payne, *University of La Verne*
 Ronald Pearson, *Bay College*
 Thomas Pearson, *University of Hawaii at Manoa*
 Nichole L. Pendleton, *Friends University*
 Chuck Pier, *Angelo State University*
 Lincoln M. Pinto, *DeVry University*
 Sonja Pippin, *University of Nevada – Reno*
 Steve Platau, *The University of Tampa*
 Walfyette Powell, *Strayer University*
 Dennis Price, *Samford University*
 Darlene Pulliam, *West Texas A&M University*
 John S. Repsis, *University of Texas at Arlington*
 John D. Rice, *Trinity University*
 Jennifer Hardwick Robinson, *Trident Technical College*
 Shani N. Robinson, *Sam Houston State University*
 Donald Roth, *Dordt College*
 Richard L. Russell, *Jackson State University*
 Robert L. Salyer, *Northern Kentucky University*
 Rhoda Sautner, *University of Mary*
 Bunney L. Schmidt, *Keiser University*
 Allen Schuldenfrei, *University of Baltimore*
 Eric D. Schwartz, *LaRoche College*
 Tony L. Scott, *Norwalk Community College*
 Randy Serrett, *University of Houston – Downtown*
 Wayne Shaw, *Southern Methodist University*
 Paul A. Shoemaker, *University of Nebraska – Lincoln*
 Kimberly Sipes, *Kentucky State University*
 Georgi Smatrakalev, *Florida Atlantic University*
 Randy Smit, *Dordt College*
 Leslie S. Sobol, *California State University Northridge*
 Marc Spiegel, *University of California, Irvine*
 Teresa Stephenson, *University of Wyoming*
 Beth Stetson, *Oklahoma City University*
 Debra Stone, *Eastern New Mexico University*
 Frances A. Stott, *Bowling Green State University*
 Todd S. Stowe, *Southwest Florida College*
 Julie Straus, *Culver-Stockton College*
 Martin Stub, *DeVry University*
 James Sundberg, *Eastern Michigan University*
 Kent Swift, *University of Montana*
 Robert L. Taylor, *Lees-McRae College*
 Francis C. Thomas, *Richard Stockton College of New Jersey*
 Randall R. Thomas, *Upper Iowa University*
 Ronald R. Tidd, *Central Washington University*
 MaryBeth Tobin, *Bridgewater State University*
 James P. Trebby, *Marquette University*
 James M. Turner, *Georgia Institute of Technology*
 Anthony W. Varnon, *Southeast Missouri State University*
 Adria Palacios Vasquez, *Texas A&M University – Kingsville*
 Terri Walsh, *Seminole State College of Florida*
 Marie Wang
 Natasha R. Ware, *Southeastern University*
 Mark Washburn, *Sam Houston State University*
 Bill Weispfenning, *University of Jamestown (ND)*
 Andrew L. Whitehair
 Kent Williams, *Indiana Wesleyan University*
 Candace Witherspoon, *Valdosta State University*
 Sheila Woods, *DeVry University, Houston, TX*
 Xinmei Xie, *Woodbury University*
 Thomas Young, *Low Star College – Tomball*

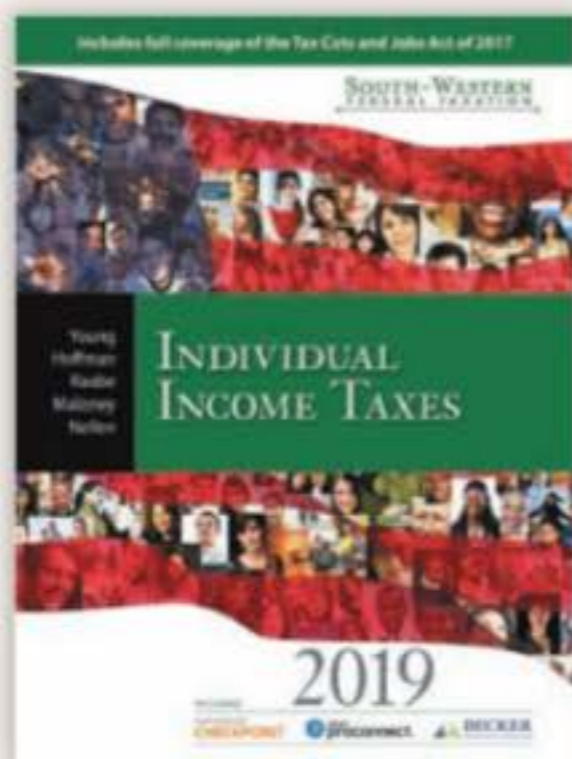
SPECIAL THANKS

We are grateful to the faculty members who have diligently worked through the problems and test questions to ensure the accuracy of the **South-Western Federal Taxation** homework, solutions manuals, test banks, and comprehensive tax form problems. Their comments and corrections helped us focus on clarity as well as accuracy and tax law currency. We also thank Thomson Reuters for its permission to use Checkpoint™ with the text.

- Sandra A. Augustine, *Hilbert College*
 Bradrick M. Cripe, *Northern Illinois University*
 Stephanie Lewis, *The Ohio State University*
 Kate Mantzke, *Northern Illinois University*
 Ray Rodriguez, *Murray State University*
 George R. Starbuck, *McMurry University*
 Donald R. Trippeer, *State University of New York College at Oneonta*
 Raymond Wacker, *Southern Illinois University, Carbondale*
 Michael Weissenfluh, *Tillamook Bay Community College*

The South-Western Federal Taxation Series

To find out more about these books, go to www.cengage.com.



INDIVIDUAL INCOME TAXES, 2019 EDITION

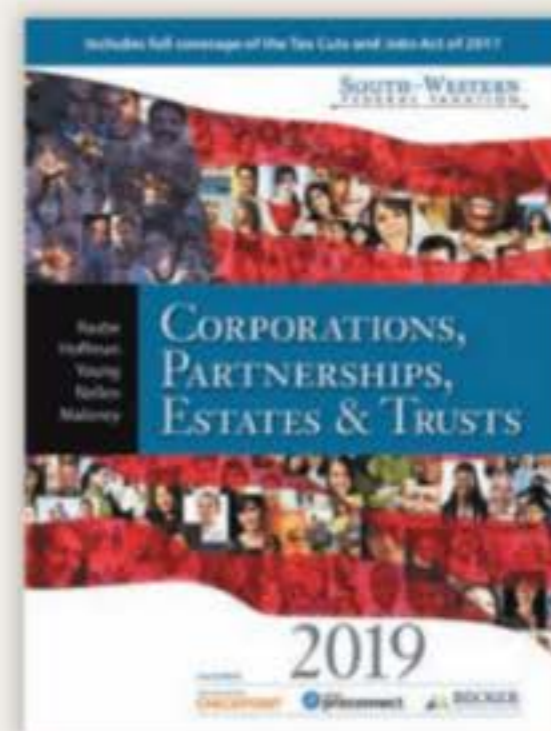
(YOUNG, HOFFMAN, RAABE, MALONEY, NELLEN, Editors) provides accessible, comprehensive, and authoritative coverage of the relevant tax code and regulations as they pertain to the individual taxpayer, as well as coverage of all major developments in Federal taxation. This edition is fully updated and revised to reflect changes included in the Tax Cuts and Jobs Act of 2017.

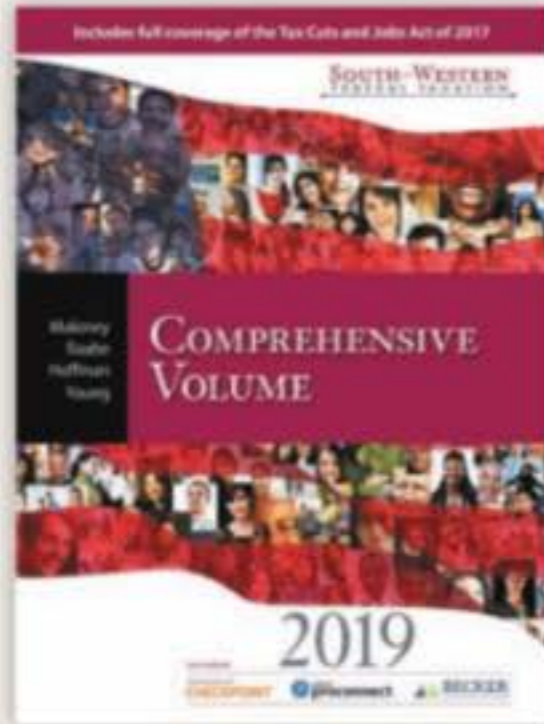
(ISBN 978-1-337-70254-6)

CORPORATIONS, PARTNERSHIPS, ESTATES & TRUSTS, 2019 EDITION

(RAABE, HOFFMAN, YOUNG, NELLEN, MALONEY, Editors) covers tax concepts as they affect corporations, partnerships, estates, and trusts. The authors provide accessible, comprehensive, and authoritative coverage of relevant tax code and regulations, as well as all major developments in Federal income taxation. This edition is fully updated and revised to reflect changes included in the Tax Cuts and Jobs Act of 2017. This market-leading text is intended for students who have had a previous course in tax.

(ISBN 978-1-337-70291-1)





COMPREHENSIVE VOLUME, 2019 EDITION

(MALONEY, RAABE, HOFFMAN, YOUNG, Editors)

Combining the number one individual tax text with the number one corporations text, *Comprehensive Volume, 2019 Edition* is a true winner. An edited version of the first two *South-Western Federal Taxation* textbooks, this book is ideal for undergraduate or graduate levels. This text works for either a one-semester course in which an instructor wants to integrate coverage of individual and corporate taxation or for a two-semester sequence in which the use of only one book is desired.

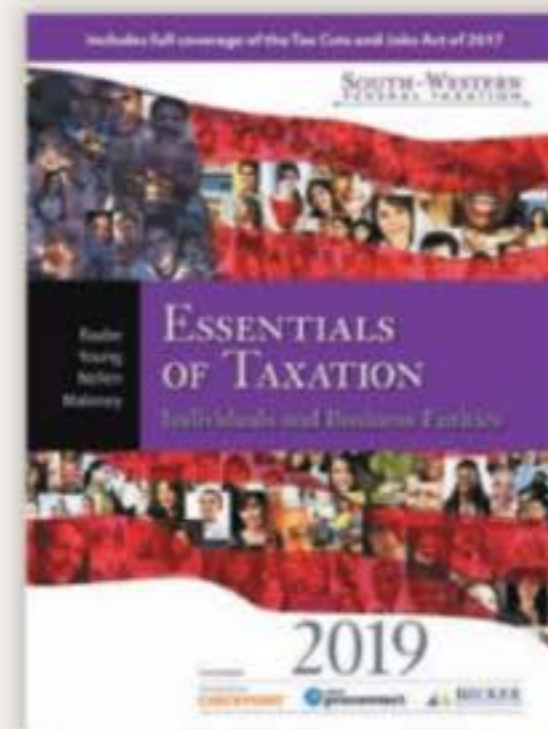
(ISBN 978-1-337-70301-7)

ESSENTIALS OF TAXATION: INDIVIDUALS AND BUSINESS ENTITIES, 2019 EDITION

(RAABE, YOUNG, NELLEN, MALONEY, Editors)

emphasizes tax planning and the multidisciplinary aspects of taxation. Formerly titled *Taxation of Business Entities*, this text is designed with the AICPA Model Tax Curriculum in mind, presenting the introductory Federal taxation course from a business entity perspective. Its **Tax Planning Framework** helps users fit tax planning strategies into an innovative pedagogical framework. The text is an ideal fit for programs that offer only one course in taxation where users need to be exposed to individual taxation, as well as corporate and other business entity taxation. This text assumes no prior course in taxation has been taken.

(ISBN 978-1-337-70296-6)



FEDERAL TAX RESEARCH, 11E

(SAWYERS AND GILL) *Federal Tax Research*, Eleventh Edition, offers hands-on tax research analysis and fully covers computer-oriented tax research tools. Also included in this edition is coverage on international tax research, a review of tax ethics, and many new real-life cases to help foster a true understanding of Federal tax law.

(ISBN 978-1-337-28298-7)

ABOUT THE EDITORS



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

teaching and research interests include international and multistate taxation, technology in tax education, personal financial planning, and the economic impact of sports teams and fine arts groups. Dr. Raabe also writes the PricewaterhouseCoopers Tax Case Studies, an extensive, well-respected set of advanced tax learning resources. Dr. Raabe has been a visiting tax faculty member for a number of public accounting firms, bar associations, and CPA societies. He has received numerous teaching awards, including the Accounting Educator of the Year award from the Wisconsin Institute of CPAs. He has been the faculty adviser for student teams in the Deloitte Tax Case Competition (national finalists at three different schools) and the PricewaterhouseCoopers Extreme Tax policy competition (national finalist).



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

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



Annette Nellen, CPA, CGMA, Esquire, directs San José State University's graduate tax program (MST) and teaches courses in tax research, tax fundamentals, accounting methods, property transactions, employment tax, ethics, leadership, and tax policy. Professor Nellen is a graduate of CSU Northridge, Pepperdine

(MBA), and Loyola Law School. Prior to joining SJSU in 1990, she was with a Big 4 firm and the IRS. At SJSU, Professor Nellen is a recipient of the Outstanding Professor and Distinguished Service Awards. Professor Nellen is an active member of the tax sections of the AICPA and American Bar Association, including chairing the AICPA Tax Executive Committee from October 2016 to May 2019. In 2013, she received the AICPA Arthur J. Dixon Memorial Award, the highest award given by the accounting profession in the area of taxation. Professor Nellen is the author of *BloombergBNA Tax Portfolio*, *Amortization of Intangibles*, and the *BloombergBNA Internet Law Resource Center*, *Overview of Internet Taxation Issues*. She has published numerous articles in the *AICPA Tax Insider*, *Tax Adviser*, *State Tax Notes*, and *The Journal of Accountancy*. She has testified before the House Ways & Means and Senate Finance Committees and other committees on Federal and state tax reform. Professor Nellen maintains the 21st Century Taxation website and blog (www.21stcenturytaxation.com) as well as websites on tax policy and reform, virtual currency, and state tax issues (www.sjsu.edu/people/annette.nellen/).



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

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



Brief Contents

PART 1: THE WORLD OF TAXATION

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

PART 2: STRUCTURE OF THE FEDERAL INCOME TAX

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

PART 3: PROPERTY TRANSACTIONS

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

PART 4: TAXATION OF INDIVIDUALS

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

PART 5: BUSINESS ENTITIES

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

PART 6: SPECIAL BUSINESS TOPICS

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