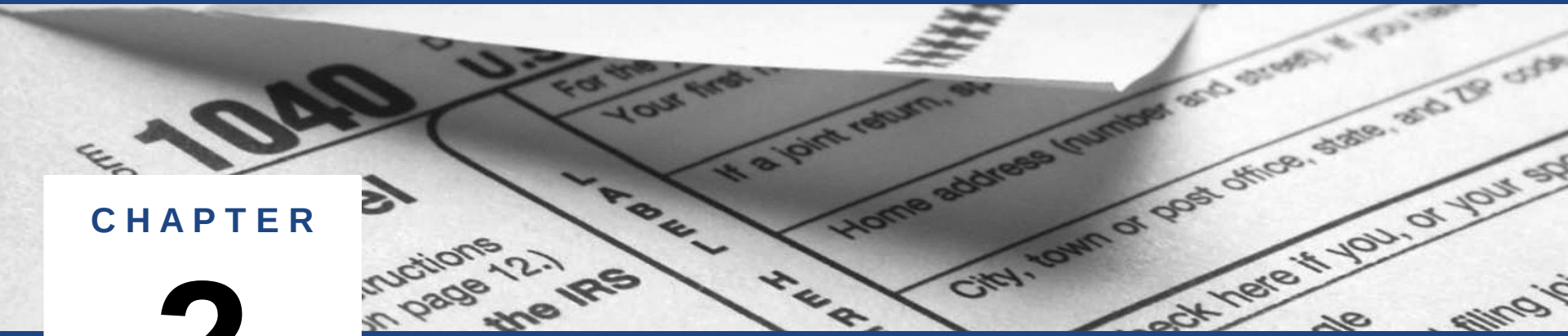
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CHAPTER

2

Working With The Tax Law

Comprehensive Volume

SOUTH-WESTERN FEDERAL TAXATION

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The Big Picture (slide 1 of 2)

- Fred and Megan Samuels review their financial and tax situation with their son, Sam, and daughter-in-law, Dana, who live with them
  - Fred and Megan are in the 28% tax bracket in 2016
  - Both Sam and Dana are age 21
- Sam, a student at a nearby university, owns some publicly traded stock that he inherited
    - A current sale would result in approximately $8,000 of gross income
      - ($19,000 amount realized – $11,000 adjusted basis)

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The Big Picture (slide 2 of 2)

- Fred and Megan provide about 55% of Sam and Dana's support
  - Although neither is now employed, Sam has earned $960 and Dana has earned $900
- The problem:
  - Should the stock be sold?
  - Would the sale prohibit Fred and Megan from claiming Sam and Dana as dependents?
  - Would the stock sale in 2016 result in a tax liability for Sam and Dana?
- Read the chapter and formulate your responses

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Statutory Sources of Tax Law
(slide 1 of 2)

- Internal Revenue Code
  - Codification of the Federal tax law provisions in a logical sequence
  - Have had three codes:
    - 1939, 1954, 1986

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Statutory Sources of Tax Law
(slide 2 of 2)

- Example of Code Citation: § 2(a)(1)(A)
  - § = Abbreviation for “Section”
  - 2 = section number
  - (a) = subsection
  - (1) = paragraph designation
  - (A) = subparagraph designation

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Legislative Process For Tax Bills

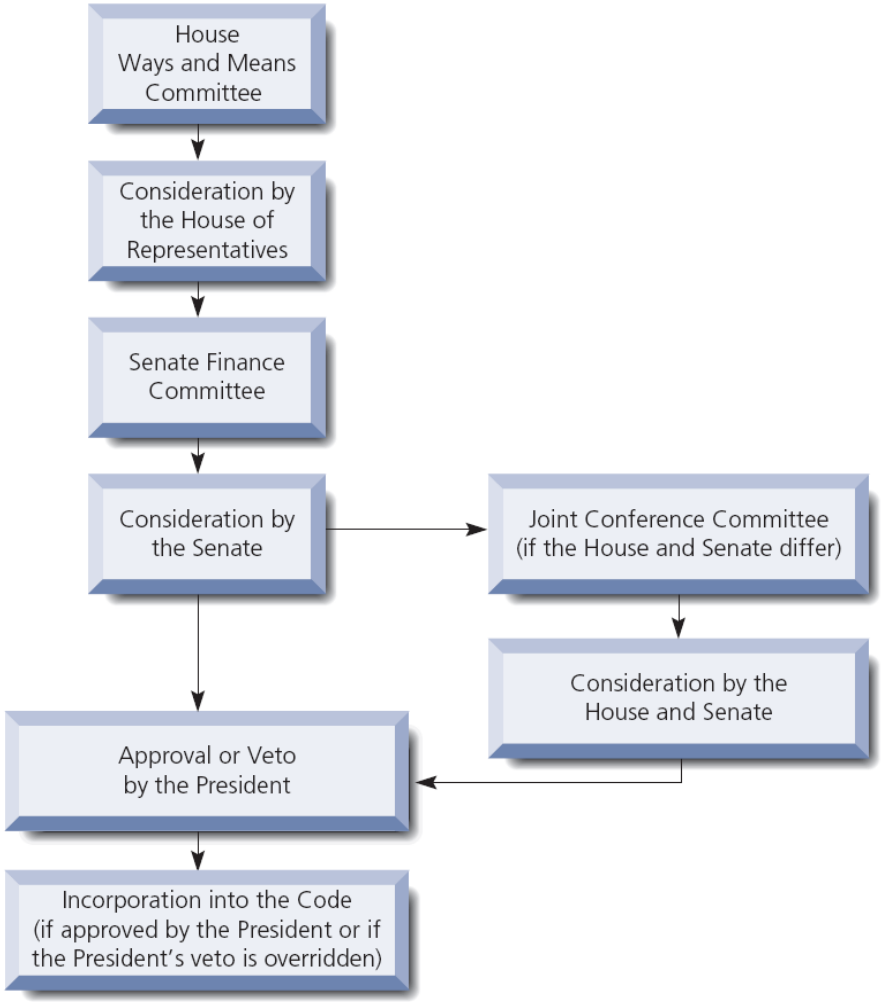


Exhibit 2.1

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Administrative Sources of Tax Law
(slide 1 of 2)

- Treasury Department Regulations
- Revenue Rulings
- Revenue Procedures
- Various other administrative pronouncements

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Administrative Sources of Tax Law

(slide 2 of 2)

Source	Location	Authority
Regulations	*Federal Register*	Force and effect of law.
Temporary Regulations	*Federal Register* *Internal Revenue Bulletin* *Cumulative Bulletin*	May be cited as a precedent.
Proposed Regulations	*Federal Register* *Internal Revenue Bulletin* *Cumulative Bulletin*	Preview of final Regulations.
Revenue Rulings Revenue Procedures Treasury Decisions Actions on Decisions	*Internal Revenue Bulletin* *Cumulative Bulletin*	Do not have the force and effect of law.
General Counsel Memoranda Technical Advice Memoranda	Tax Analysts' *Tax Notes;* Thomson Reuters *Checkpoint**; Commerce Clearing House *IntelliConnect*	May not be cited as a precedent.
Letter Rulings	Thomson Reuters and Commerce Clearing House tax services	Applicable only to taxpayer addressed. No precedential force.

* Thomson Reuters *Checkpoint* includes a wide variety of tax resources. The most significant are materials produced by the Research Institute of America (RIA), including the *Federal Tax Coordinator 2d.*

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Regulations (slide 1 of 4)

- Issued by U.S. Treasury Department
- Provide general interpretations and guidance in applying the Code

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Regulations (slide 2 of 4)

- Issued as:
  - Proposed: preview of final regulations
    - Do not have force and effect of law
  - Temporary: issued when guidance needed quickly
    - Same authoritative value as final regulations
  - Final:
    - Force and effect of law

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Regulations (slide 3 of 4)

- Example of Regulation citation:
  - Reg. § 1.2
    - Refers to Regulations under Code § 2
    - Subparts may be added for further identification
    - The numbering patterns of these subparts often have no correlation with the Code subsections

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Regulations (slide 4 of 4)

- Example of Proposed Regulation citation: Prop. Reg. § 1.2
- Example of Temporary Regulation citation: Temp. Reg. § 1.6081–8T

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Revenue Rulings (slide 1 of 2)

- Officially issued by National Office of IRS
  - Provide specific interpretations and guidance in applying the Code
  - Less legal force than Regulations
  - Issued in IRB and accumulated in the Cumulative Bulletins

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Revenue Rulings (slide 2 of 2)

- Example of Revenue Ruling citation
  - Rev.Rul. 2015–9, 2015–21 I.R.B. 972
    - Explanation: Revenue Ruling Number 9, appearing on page 972 of the 21st weekly issue of the Internal Revenue Bulletin for 2015

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Revenue Procedures (slide 1 of 2)

- Concerned with the internal management practices and procedures of the IRS
  - Issued similar to Revenue Rulings
  - Issued in IRB and accumulated in the Cumulative Bulletins

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Revenue Procedures (slide 2 of 2)

- Example of Revenue Procedure citation
  - Rev. Proc. 92-29, 1992-1 CB 748
    - 29th Rev. Procedure in 1992 found in volume 1 of Cumulative Bulletin on page 748

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Letter Rulings (slide 1 of 2)

- Provide guidance to taxpayer on how a transaction will be taxed before proceeding with it
  - Issued for a fee upon a taxpayer's request
  - Describe how the IRS will treat a proposed transaction
- Apply only to the taxpayer who asks for and obtains the ruling
  - Post-1984 letter rulings may be substantial authority for purposes of the accuracy-related penalty
- Limited to restricted, preannounced areas of taxation

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Letter Rulings (slide 2 of 2)

- Example of Letter Ruling citation
  - Ltr.Rul. 201503010
    - 10th ruling issued in the 3rd week of 2015

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Other Administrative Pronouncements
(slide 1 of 4)

- Treasury Decisions – issued by Treasury Dept. to:
  - Promulgate new or amend existing Regulations
  - Announce position of the Government on selected court decisions
  - Published in the Internal Revenue Bulletin
    - Then transferred to the Cumulative Bulletin

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Other Administrative Pronouncements
(slide 2 of 4)

- Determination Letters
  - Issued by Area Director at taxpayer's request
  - Usually involve completed transactions
  - Not published
    - Made known only to party making the request

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Other Administrative Pronouncements
(slide 3 of 4)

- The IRS also publishes other administrative communications such as
  - Announcements
  - Notices
  - IRs (News Releases)
  - Internal Legal Memoranda (ILMs)
  - Chief Counsel Notices (CC)
  - Prohibited Transaction Exemptions

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Other Administrative Pronouncements
(slide 4 of 4)

- A variety of internal memoranda that constitute the working law of the IRS also are released but not officially published, such as
  - General Counsel Memoranda (GCMs)
  - Technical Advice Memoranda (TAMs)
  - Internal Legal Memoranda (ILMs)
  - Field Service Advice Memoranda (FSAs)
- The IRS indicates that they may not be cited as precedents by taxpayers
  - However, these working documents do explain the IRS's position on various issues

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Federal Judicial System

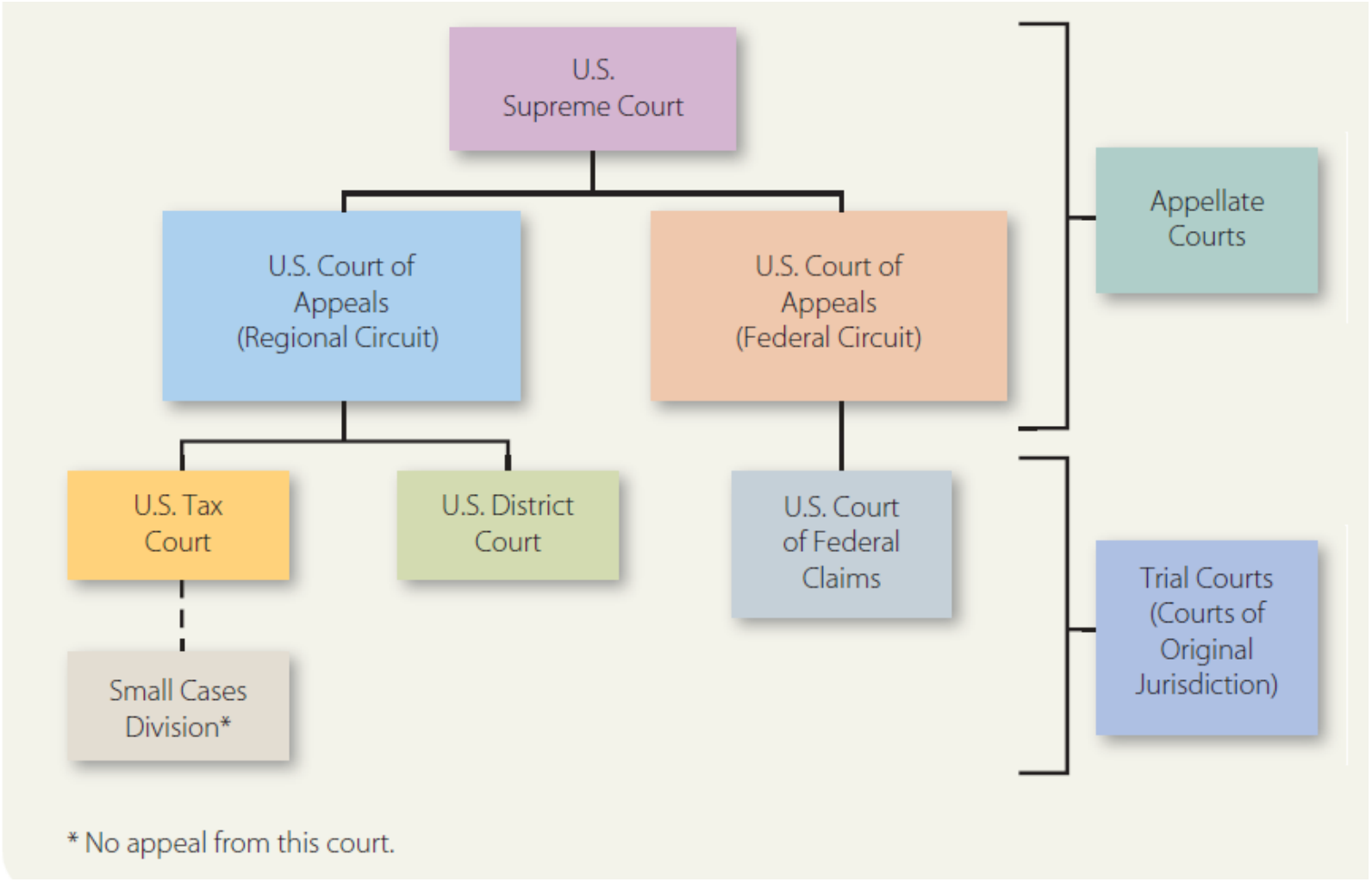


Exhibit 2.4

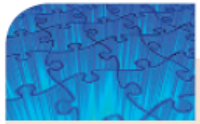
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Judicial Sources (slide 1 of 2)

- There are four courts of original jurisdiction (trial courts)
  - U.S. Tax Court: Regular
  - U.S. Tax Court: Small Cases Division
  - Federal District Court
  - U.S. Court of Federal Claims

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Judicial Sources (slide 2 of 2)



Concept Summary 2.1

Federal Judicial System: Trial Courts

Issue	U.S. Tax Court	U.S. District Court	U.S. Court of Federal Claims
Number of judges per court	19*	Varies	16
Payment of deficiency before trial	No	Yes	Yes
Jury trial available	No	Yes	No
Types of disputes	Tax cases only	Most criminal and civil issues	Claims against the United States
Jurisdiction	Nationwide	Location of taxpayer	Nationwide
IRS acquiescence policy	Yes	Yes	Yes
Appeal route	U.S. Court of Appeals	U.S. Court of Appeals	U.S. Court of Appeals for the Federal Circuit

*Currently, there are also 4 special trial judges and 13 senior judges.

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Appeals Process

- Appeals from District Court or Tax Court go to the U.S. Court of Appeals for circuit where taxpayer resides
- Appeals from Court of Federal Claims is to Court of Appeals for the Federal Circuit
- Appeal to the Supreme Court is by Writ of Certiorari
  - Only granted for those cases it desires to hear

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Courts' Weights As Precedents

- From high to low
  - Supreme Court
  - Circuit Court of Appeals
  - Tax Court (Regular), U.S. Court of Federal Claims, & U.S. District Courts
- Decisions of the Small Cases Division of the Tax Court have no precedential value and cannot be appealed

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Tax Court (slide 1 of 3)

- Issues two types of decisions: Regular and Memorandum
  - Regular decisions involve novel issues not previously resolved by the court
- Regular decisions are published by the U.S. government, for example

Temporary Citation	*MoneyGram International, Inc. and Subsidiaries*, 144 T.C. ___, No. 1 (2015). *Explanation:* Page number left blank because not yet known.
Permanent Citation	*MoneyGram International, Inc. and Subsidiaries*, 144 T.C. 1 (2015). *Explanation:* Page number now available.

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Tax Court (slide 2 of 3)

- Tax Court Memorandum decisions
  - Memorandum decisions deal with situations necessitating only the application of already established principles of law
  - Memorandum decisions were not published by the U.S. Government until recently

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Tax Court (slide 3 of 3)

- Memorandum decisions were – and continue to be – published by several tax services
  - Consider, for example, three different ways that *Nick R. Hughes* can be cited:
    - *Nick R. Hughes*, T.C.Memo. 2009–94
      - The 94th Memorandum decision issued by the Tax Court in 2009
    - *Nick R. Hughes*, 97 TCM 1488
      - Page 1488 of Vol. 97 of the CCH Tax Court Memorandum Decisions
    - *Nick R. Hughes*, 2009 RIA T.C.Memo. ¶2009,094
      - Paragraph 2009,094 of the RIA T.C. Memorandum Decisions

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Examples Of District Court Decision Citations

- *Turner v. U.S.*, 2004–1 USTC ¶60,478 (D.Ct. Tex., 2004) (CCH citation)

- *Turner v. U.S.*, 93 AFTR 2d 2004–686 (D.Ct. Tex., 2004) (RIA citation)

- *Turner v. U.S.*, 306 F.Supp.2d 668 (D.Ct. Tex., 2004)(West citation)

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Supreme Court Decisions

- Examples of citations
  - U.S. v. The Donruss Co., (USSC, 1969)
    - 69-1 USTC ¶9167 (CCH citation)
    - 23 AFTR2d 69-418 (RIA citation)
    - 89 S. CT 501 (West citation)
    - 393 U.S. 297 (U.S. Government citation)
    - 21 L.Ed.2d 495 (Lawyer's Co-operative Publishing Co. citation)

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Tax Treaties

- The U.S. signs tax treaties with foreign countries to:
  - Avoid double taxation
  - Render mutual assistance in tax enforcement
- Neither a tax law nor a tax treaty takes general precedence
  - When there is a direct conflict, the most recent item will take precedence
  - A taxpayer must disclose on the tax return any position where a treaty overrides a tax law
    - There is a $1,000 penalty per failure to disclose for individuals ($10,000 for corporations)

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Tax Research Tools (slide 1 of 2)

- A crucial part of the research process is the ability to locate appropriate sources of the tax law
  - Both electronic and paper-based research tools are available to aid in this search
- Unless the problem is simple (e.g., the Code Section is known, and there is a Regulation on point), the research process should begin with a tax service

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Tax Research Tools (slide 2 of 2)

- A partial list of the available commercial tax services includes:
  - Standard Federal Tax Reporter, CCH
  - CCH IntelliConnect, CCH Internet service
  - United States Tax Reporter, RIA
  - RIA Checkpoint, RIA
  - ATX/Kleinrock Tax Expert, CCH/Wolters Kluwer
  - Tax Management Portfolios, BNA
  - Mertens Law of Federal Income Taxation, Thomson Reuters
  - Westlaw services (including access to Tax Management Portfolios)
  - TaxCenter, LexisNexis
  - Federal Research Library, Tax Analysts

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Tax Research Process

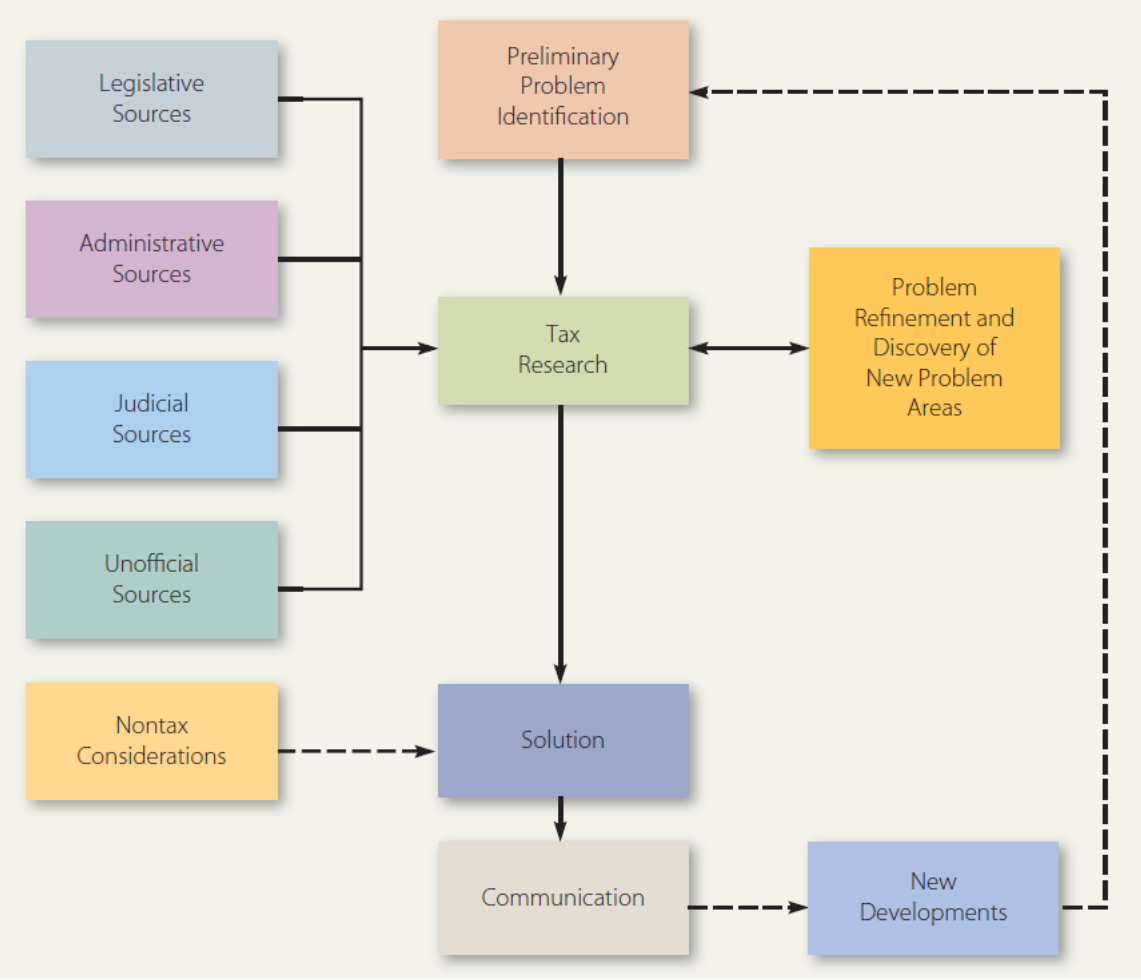


EXHIBIT 2.8

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Tax Research

- Tax research is the method by which an interested party determines the best solution to a tax situation
- Tax research involves:
  - Identifying and refining the problem
  - Locating the appropriate tax law sources
  - Assessing the validity of the tax law sources
  - Arriving at the solution or at alternative solutions with due consideration given to nontax factors

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Assessing The Validity Of Tax Law Sources (slide 1 of 4)

- Regulations
  - IRS agents must give the Code and the Regulations equal weight when dealing with taxpayers and their representatives
  - Proposed Regulations are not binding on IRS or taxpayer
  - Burden of proof is on taxpayer to show Regulation incorrect
  - If the taxpayer loses the challenge, a 20% negligence penalty may be imposed

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Assessing The Validity Of Tax Law Sources (slide 2 of 4)

- Final Regulations tend to be of three types
  - Procedural: housekeeping-type instructions
  - Interpretive: rephrase what is in Committee Reports and the Code
    - Hard to get overturned
  - Legislative: allow the Treasury Department to determine the details of law
    - Congress has delegated its legislative powers and these cannot generally be overturned

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Assessing The Validity Of Tax Law Sources (slide 3 of 4)

- Revenue Rulings
  - Carry less weight than Regulations
  - Not substantial authority in court disputes

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Assessing The Validity Of Tax Law Sources (slide 4 of 4)

- Judicial sources
  - Consider the level of the court and the legal residence of the taxpayer
  - Tax Court Regular decisions carry more weight than Memo decisions
    - Tax Court does not consider Memo decisions to be binding precedents
    - Tax Court reviewed decisions carry even more weight
  - Circuit Court decisions where certiorari has been requested and denied by the U.S. Supreme Court carry more weight than a Circuit Court decision that was not appealed
  - Consider whether the decision has been overturned on appeal

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Tax Law Sources (slide 1 of 2)

- Primary sources of tax law include:
  - The Constitution
  - Legislative history materials
  - Statutes
  - Treaties
  - Treasury Regulations
  - IRS pronouncements
  - Judicial decisions
- In general, the IRS considers only primary sources to constitute substantial authority

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Tax Law Sources (slide 2 of 2)

- Secondary Sources include:
  - Legal periodicals
  - Treatises
  - Legal opinions
  - General Counsel Memoranda
  - Written determinations
- In general, secondary sources are not authority

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Tax Planning

- Consider social, economic, and business goals as well as tax motives
- Tax avoidance is the legal minimization of tax liabilities and one goal of tax planning
- Tax evasion is the illegal minimization of tax liabilities
  - Suggests the use of subterfuge and fraud as a means to tax minimization
  - Can lead to fines and jail

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Taxation on the CPA Examination

- Taxation is included in the 3-hour Regulation section and covers:
  - Federal tax process, procedures, accounting, and planning
  - Federal taxation of property transactions
  - Federal taxation – individuals
  - Federal taxation – entities
- Knowledge is tested using both multiple-choice questions and case studies called simulations

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If you have any comments or suggestions concerning this PowerPoint Presentation for South-Western Federal Taxation, please contact:

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1. For "qualifying widow(er)" filing status, which of the following requirements must be met?

   I. The surviving spouse does not remarry before the end of the current year
   II. The surviving spouse was eligible to file a joint tax return in the year of the spouse's death
   III. The surviving spouse maintains the cost of the principal residence for six months.

   a) I, II, and III
   b) I and II, but not III
   c) I and III, but not II
   d) I only

a) Incorrect. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. Maintaining the cost of the taxpayer's principal residence for six months is not sufficient.
b) **Correct!** A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. Maintaining the cost of the taxpayer's principal residence for six months is not sufficient.
c) Incorrect. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. Maintaining the cost of the taxpayer's principal residence for six months is not sufficient.
d) Incorrect. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. Maintaining the cost of the taxpayer's principal residence for six months is not sufficient.

2. Which of the below prevents a married couple from filing a joint tax return?

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I. The spouses have different accounting methods
II. The spouses have different tax years, provided that both spouses are alive at the end of the year
III. One spouse was a nonresident alien for three months during the year and no proper election was made

a) I and II only
b) II and III only
c) I and III only
d) II only

a) Incorrect. A married couple may file a return as married filing jointly only if they use the same accounting period, although they may use different accounting methods. While a couple generally cannot file a joint return if either is a nonresident alien at any time during the tax year, if a nonresident alien is married to a U.S. citizen or resident alien at the end of the year, the spouses may file jointly.
b) Incorrect. A married couple may file a return as married filing jointly only if they use the same accounting period, although they may use different accounting methods. While a couple generally cannot file a joint return if either is a nonresident alien at any time during the tax year, if a nonresident alien is married to a U.S. citizen or resident alien at the end of the year, the spouses may file jointly.
c) Incorrect. A married couple may file a return as married filing jointly only if they use the same accounting period, although they may use different accounting methods. While a couple generally cannot file a joint return if either is a nonresident alien at any time during the tax year, if a nonresident alien is married to a U.S. citizen or resident alien at the end of the year, the spouses may file jointly.
d) **Correct!** A married couple may file a return as married filing jointly only if they use the same accounting period, although they may use different accounting methods. While a couple generally cannot file a joint return if either is a nonresident alien at any time during the tax year, if a nonresident alien is married to a U.S. citizen or resident alien at the end of the year, the spouses may file jointly.

3. Parker and his wife Marie would have been filing a joint tax return for 2014, how- ever Marie died in October 2014. Parker has not remarried and continues to maintain a home for himself and his two children during 2014, 2015, 2016, and 2017. Parker's filing statuses for 2014, 2015, 2016, and 2017 are as follows:

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	2014	2015	2016	2017
a.	Qualifying widower	Married filing joint return	Qualifying widower	Head of household
b.	Married filing joint return	Married filing joint return	Head of household	Qualifying widower
c.	Married filing joint return	Qualifying widower	Qualifying widower	Head of household
d.	Qualifying widower	Qualifying widower	Head of household	Qualifying widower

a) Incorrect. A couple may file a joint return if they are married as of the end of the tax year or, when one spouse has died during the tax year, if they were married as of the date of death. As a result, Parker would qualify to file a joint return for 2014. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. As a result, Parker will file as a qualifying widower for 2015 and 2016. In 2017, Parker may no longer file as a qualified widower but may file as a head of household, which is an unmarried taxpayer that maintains a home that is the principal residence of a qualifying relative, such as a child.

b) Incorrect. A couple may file a joint return if they are married as of the end of the tax year or, when one spouse has died during the tax year, if they were married as of the date of death. As a result, Parker would qualify to file a joint return for 2014. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. As a result, Parker will file as a qualifying widower for 2015 and 2016. In 2017, Parker may no longer file as a qualified widower but may file as a head of household, which is an unmarried taxpayer that maintains a home that is the principal residence of a qualifying relative, such as a child.

c) **Correct!** A couple may file a joint return if they are married as of the end of the tax year or, when one spouse has died during the tax year, if they were married as of the date of death As a result, Parker would qualify to file a joint return for 2014. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. As a result, Parker will file as a qualifying widower for 2015 and 2016. In 2017, Parker may no

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longer file as a qualified widower but may file as a head of household, which is an unmarried taxpayer that maintains a home that is the principal residence of a qualifying relative, such as a child.

d) Incorrect. A couple may file a joint return if they are married as of the end of the tax year or, when one spouse has died during the tax year, if they were married as of the date of death. As a result, Parker would qualify to file a joint return for 2014. A taxpayer may file a tax return as a qualifying widow or widower for 2 tax years after the year in which a spouse dies provided the couple qualified to file a joint return for the year of death; that the taxpayer provided over 50% of the cost of maintaining the principal residence of a dependent child or stepchild; and that the taxpayer has not remarried as of the end of the current year. As a result, Parker will file as a qualifying widower for 2015 and 2016. In 2017, Parker may no longer file as a qualified widower but may file as a head of household, which is an unmarried taxpayer that maintains a home that is the principal residence of a qualifying relative, such as a child.

4. Which of the following items are included in determining the total support of a dependent?

I. Medical expenditures paid on behalf of the dependent
II. Life insurance premiums paid on behalf of the dependent
III. Fair rental value of dependent's lodging

a) All of the above
b) I and II only
c) I and III only
d) I only

a) Incorrect. To determine if a taxpayer provided over 50% of a qualifying relative's support, or if more than 50% of the support of a qualifying child was provided by that child, Payments for food, lodging, clothing, education, medical and dental care, recreation, transportation, and other necessities are included. Income, social security, and Medicare taxes paid from the individual's own income; life insurance premiums; and funeral expenses are not included.

b) Incorrect. To determine if a taxpayer provided over 50% of a qualifying relative's support, or if more than 50% of the support of a qualifying child was provided by that child, Payments for food, lodging, clothing, education, medical and dental care, recreation, transportation, and other necessities are included. Income, social security, and Medicare taxes paid from the individual's own income; life insurance premiums; and funeral expenses are not included.

c) **Correct!** To determine if a taxpayer provided over 50% of a qualifying relative's support, or if more than 50% of the support of a qualifying child was provided by that child, Payments for food, lodging, clothing, education, medical and dental care, recreation, transportation, and other necessities are included. Income, social security, and Medicare taxes paid from the individual's own income; life insurance premiums; and funeral expenses are not included.

d) Incorrect. To determine if a taxpayer provided over 50% of a qualifying relative's support, or if more than 50% of the support of a qualifying child was provided by that child, Payments for food, lodging, clothing, education, medical and dental care, recreation, transportation, and other necessities are included. Income, social security, and Medicare taxes paid from

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the individual's own income; life insurance premiums; and funeral expenses are not included.

5. Kyle and Elena Smith contributed to the support of their two children, Alexandra and Matthew, and Elena's divorced father, Nick. For 2016, Alexandra, a 22-year-old full-time college student, earned $1,700 from a part-time job. Matthew, a 27-year-old full-time graduate student, earned $23,000 from his job as a teaching assistant. Nick received $12,000 in capital gains income and $7,000 in nontaxable Social Security benefits. Alexandra, Matthew, and Nick are U.S. citizens and were over one-half supported by Kyle and Elena. How many exemptions can Kyle and Elena claim on their 2016 joint income tax return?

   a) 2
   b) 3
   c) 4
   d) 5

   a) Incorrect. Kyle and Elena will be able to claim 3 exemptions, including 2 for themselves, on their joint return. Alexandra is a qualifying child since she is a student under the age of 24, resulting in the third exemption. Matthew, being older than 24, is not a qualifying child. Since Nick has gross income, which includes the $12,000 in capital gains but excludes the nontaxable social security benefits, in excess of the exemption amount, Nick is not a qualifying relative and does not provide an additional exemption.
   b) **Correct!** Kyle and Elena will be able to claim 3 exemptions, including 2 for themselves, on their joint return. Alexandra is a qualifying child since she is a student under the age of 24, resulting in the third exemption. Matthew, being older than 24, is not a qualifying child. Since Nick has gross income, which includes the $12,000 in capital gains but excludes the nontaxable social security benefits, in excess of the exemption amount, Nick is not a qualifying relative and does not provide an additional exemption.
   c) Incorrect. Kyle and Elena will be able to claim 3 exemptions, including 2 for themselves, on their joint return. Alexandra is a qualifying child since she is a student under the age of 24, resulting in the third exemption. Matthew, being older than 24, is not a qualifying child. Since Nick has gross income, which includes the $12,000 in capital gains but excludes the nontaxable social security benefits, in excess of the exemption amount, Nick is not a qualifying relative and does not provide an additional exemption.
   d) Incorrect. Kyle and Elena will be able to claim 3 exemptions, including 2 for themselves, on their joint return. Alexandra is a qualifying child since she is a student under the age of 24, resulting in the third exemption. Matthew, being older than 24, is not a qualifying child. Since Nick has gross income, which includes the $12,000 in capital gains but excludes the nontaxable social security benefits, in excess of the exemption amount, Nick is not a qualifying relative and does not provide an additional exemption.

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APPENDIX E

PRACTICE SET ASSIGNMENTS—COMPREHENSIVE TAX RETURN PROBLEMS

SOLUTIONS TO PROBLEM MATERIALS

PROBLEM 1 SOLUTIONS

1. David is self-employed and reports his business income on Schedule C. Both his consulting fees of $92,800 and his expense reimbursements of $20,420 should be included on line 1. The travel expenses are deducted on line 24a (airfare $8,200 + lodging $5,200 + transportation $920) and $3,050 of meals are deducted online 24b [meals $6,100 – disallowed portion (50% × $6,100)].

2. Given that David is a cash-basis taxpayer, the $4,400 payment received from Sesa Mining in 2015 is also included on Schedule C. This brings the total on line 1 to $117,620 ($92,800 + $4,400 + $20,420). The $5,100 received from Echo will be taxable in 2016. The Cormorant Mining transaction results in neither income (no payment is received) nor a bad debt deduction (no basis exists in the receivable). If H&R Block software is used to complete the tax return, it automatically enters an X on line 32a of Schedule C even though there is no loss reported this year. This can be overriden in the software if desired.

3 The $9,000 contribution to the H.R.10 Keogh retirement plan and the $3,800 of premiums on health insurance are not reported on Schedule C but are listed on Form 1040, page 1, lines 28 and 29, respectively. The remaining expenses are deducted on Schedule C as follows:

Line 8—Advertising		$2,400
Line 18—Office supplies		1,200
Line 22—Supplies		3,200
Line 23—State occupation license		300
Line 27a (and also listed separately on page 2, Part V)		
Business phone and Internet service	$860	
Subscriptions to trade journals	240	
Membership dues to trade associations	180	1,280

4. The home office deduction is computed on Form 8829 (Expenses for Business Use of Your Home). For depreciation purposes, the basis of the residence is the lesser of $450,000 (fair market value) or David's inherited basis of $360,000 under § 1014. The land is not depreciable. Consequently, this amount is entered on line 38 of Form 8829 and multiplied by the business percentage of 20% (line 7) to yield $72,000 (line 39). Referring to Exhibit 8.8 (MACRS Straight-Line Depreciation for Real Property Assuming Mid-Month Convention), the applicable percentage for 39-year nonresidential real property for the recovery period of 2–39 years is 2.564. Thus, the depreciation for 2015 is $1,846 ($72,000 × 2.564%) and is entered on lines 41 and 29. Other data in completing Form 8829 are summarized below.

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Indirect expenses [reported in column (b)]	
Line 10—Deductible mortgage interest	$ 4,400
Line 11—Real estate taxes	3,100
Line 17—Insurance	2,300
Line 19—Repairs and maintenance	2,900
Line 20—Utilities	4,800
Total indirect expenses	$17,500
	× 20%
Business portion	$ 3,500*

*Form 8829 does the calculation for the business portion in two steps. First, it applies 20% to the total of interest ($4,400) and taxes ($3,100) [20% × $7,500] to yield $1,500 (line 13). Second, the 20% is applied to the total of insurance ($2,300), indirect repairs and maintenance ($2,900), and utilities ($4,800) [20% × $10,000] to yield $2,000 (line 23). Thus, the total business portion of the indirect expense is $3,500 ($1,500 + $2,000).

The indirect expenses of $3,500 are added to the direct expense of $1,200 for painting the office and the depreciation of $1,846 for a total of $6,546 (line 35), which is also reported on line 30 of Schedule C.

The special purpose file cabinet is expensed by the use of Form 4562 (Depreciation and Amortization). Use Part I of this form, and when the $4,800 listed on line 12 is combined with the depreciation on the Infiniti SUV (see below), the total is transferred to Schedule C.

5. Depreciation on the Infiniti under the MACRS method is computed as follows:

Cost	$41,000
Second year percentage for five-year property (Exhibit 8.3)	32%
	$13,120
× Business use	90%
	$11,808

However, as the second year recovery limitation (for a vehicle placed in service in 2014) is $5,100, the depreciation claimed cannot exceed $4,590 ($5,100 × 90%). This depreciation, determined by using Part V of Form 4562, is then added to the depreciation on the file cabinet (see item 4), and the total of $9,390 ($4,800 + $4,590) is entered on line 13 of Schedule C.

The actual cost method of calculating the deduction for vehicle expense provides David with a superior result than would the automatic mileage method. Therefore, he elected this method last year when he acquired the SUV, and he will continue to use this method as long as he uses the Infiniti in his business. Under the actual cost method, $5,390 ($4,950 + $440) is deducted as car and truck expenses on line 9 of Schedule C. The $4,950 is the sum of expenses related to the 90% business use of the vehicle—gasoline ($3,300), auto insurance ($1,600), repairs ($240), auto club dues ($180), oil and lubrication ($120), and license and registration ($60). The $440 is all of the toll and parking charges paid by David in the conduct of his business. Note that traffic fines for moving violations are not deductible.

6. As an employee, Sheri will report her expenses using Form 2106 (Employee Business Expenses). Her allowable expenses are as follows:

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Computer [$1,200 × 80% (business use)]	$ 960
Subscriptions and dues	180
Continuing education course	120
Occupational license fee	80
	$1,340

The $1,340 is entered on line 4 and summed on line 10 of Form 2106 and entered on line 21 of Schedule A (Form 1040). The § 179 expense of the business portion of the laptop is computed on Part I of Form 4562.

Sheri uses the Suburban to commute to her work, so she is not permitted to deduct any costs related to the use of the Suburban or for the parking at her work site. No deduction is allowed for the LSAT preparation sessions under § 222 (i.e., tuition and related expenses) because the pursuit of a law degree would qualify Sheri for a new trade or business. The $5,000 contribution to a traditional IRA is deducted on line 32 on page 1 of Form 1040.

Sheri will not receive any tax benefit from her job-related expenses since they do not exceed the 2%-of-AGI floor [$1,340 – $2,104 (2% × $105,175)]. See lines 26 and 27 of Schedule A.

7. Transactions relating to the rental house are reported on Schedule E (Supplemental Income and Loss). Rents received of $28,600 are reported on line 3. Although this represents 13 months of rent, the prepaid rent for January 2016 is taxed to the Johnsons in the year received (i.e., 2015). The operating expenses in connection with the property are reported as follows:

Line 7—Yard maintenance	$1,200
Line 9—Insurance	3,100
Line 14—Repairs	800
Line 16—Property taxes	2,400

Property taxes do not include the $2,400 special street paving assessment, which should be added to the basis of the land.

The line 18 depreciation of $18,205* is computed as follows (use Part III of Form 4562):

Realty—	
Basis: $220,000 (cost) + $80,000 (renovation)	$300,000
Applicable percentage for recovery period of 2–18 years (see Exhibit 8.8 in the text for 27.5-year residential real property)	× 3.636%
Depreciation allowed for 2015	$ 10,908
Personalty—	
Basis: cost (purchase price)	$ 38,000
Applicable percentage for recovery year 3 as to five-year property (see Exhibit 8.3 in the text)	× 19.2%
Depreciation allowed for 2015	$ 7,296

According to Exhibit 8.1 in the text, rental appliances, furniture, carpets, etc., are five-year cost recovery MACRS personalty.

*While the depreciation sums to $18,204, *H&R Block* tax return software rounds this number to $18,205.

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The result reached in Schedule E is summarized below.

Line 3—Income	$28,600
Line 20—Total Expenses	(25,705)
Lines 21 and 26—Profit	$ 2,895

The $2,895 profit is transferred to line 17 of page 1 of Form 1040.

8. Although determining the year in which a corporate stock becomes *entirely* worthless is often problematical, the Johnsons are justified in picking 2015 for the write-off given the fact that the corporation is currently in bankruptcy. The basis of the stock is its value when David received it as payment for services provided, $3,900—the amount David billed for his services. (*Note:* It is assumed that David recognized the $3,900 in 2014.) Worthless securities are deemed sold on the last day of the taxpayer's tax year. Therefore, the worthless Cormorant stock results in a long-term capital loss of $3,900 in Part II of Schedule D.

9. Under § 1015, the basis for gain of property acquired by gift is the donor's basis plus an appropriate portion of any gift tax paid on the transfer. Since no gift tax was incurred (probably due to the application of the unified transfer tax credit), the Johnsons have an income tax basis in the Teton tract of $50,000 (i.e., the father's basis). Thus, the disposition of the property results in a realized gain of $750,000 [$800,000 (value received) – $50,000 (basis of property transferred)]. Because the like-kind exchange rules of § 1031 apply, only $8,000 cash boot is recognized.

   To report the transaction, complete Parts I and III of Form 8824 (Like-Kind Exchanges). The recognized gain of $8,000 on line 22 is then entered on line 11 of Schedule D.

10. David's basis in the antique gun collection is $22,000 based on § 1014 (i.e., fair market value on date of his father's death). The sale of the collection for $29,000 yields a capital gain of $7,000 ($29,000 – $22,000). Because the property is a collectible, the gain requires special tax treatment. The maximum tax rate that can be applied cannot exceed 28% and net short-term capital losses are first applied against collectible gains. The computation of the tax liability can become complex and is facilitated by the use of a *28% Rate Gain Worksheet* provided by the IRS. The result of this worksheet is entered on line 18 of page 2 of Schedule D.

11. Sheri's use of the installment method to report the gain on the Converse County land sale is assumed since the facts do not indicate that she elected out of installment sale treatment under § 453(d). So, her gross profit percentage of 33 1/3% ($25,000/$75,000) means that one-third of every dollar received is taxable gain and two-thirds is a tax-free recovery of basis. Since Sheri owned the land for more than one year and she held the land for investment purposes, the gain is a long-term capital gain. Of the $10,800 Sheri receives in 2015, $4,800 is interest, $2,000 is long-term capital gain ($6,000 × 33 1/3%), and $4,000 is nontaxable.

    The interest of $4,800 is listed in Part 1 of Schedule B. Report the 2015 gain from this past transaction on Form 6252 (Installment Sale Income). Because this is not the year of sale, complete only lines 1 through 4 and Part II (lines 19 through 26). Part I is only filled in during the year the sale occurs. The profit of $2,000 (line 26) is transferred to Schedule D (Part II, line 11).

12. The $4,000 short-term capital loss carried over from 2014 is entered on line 6 of Schedule D. This loss offsets some of the collectible gain when the *28% Rate Gain Worksheet* (see item 10 above) is completed. The net result of this worksheet is $3,000 [$7,000 (collectible gain) – $4,000 (net short-term capital loss)] and is carried to line 18 of Schedule D.

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13. Although Vivian lived for only a few days in 2015, she qualifies as a dependent. As such, her medical expenses can be claimed by the Johnsons. Since the Johnsons are cash-basis taxpayers, the year in which the expenses were incurred is irrelevant—the year they are paid controls. Along with the medical expenses of $7,300 ($4,200 + $3,100), the Johnsons can also claim the $600 church pledge that they paid. (A church pledge is not a binding debt, so the Johnsons will not be treated as satisfying the obligation of another person. Instead, it is treated as a qualifying charitable contribution.) The burial expenses of $4,400 are not deductible for income tax purposes.

    By virtue of § 101(a)(1), the proceeds of life insurance are excluded from income. Thus, the $20,000 Sheri receives is not reported anywhere on the tax return.

14. The $1,900 interest on the City of Cheyenne bonds is nontaxable but is reported on line 8b (page 1 of Form 1040). The $1,100 interest on the CD and the $400 interest on the money market account are separately listed in Part I of Schedule B.

    The garage sale resulted in a realized loss of $850 [$950 – $1,800], which is not recognized because it is a personal loss.

    The $700 qualified dividends are reported in Part II of Schedule B, then entered on line 9b (page 1) of Form 1040.The applicable tax rate is determined by completing the *Schedule D Tax Worksheet*.

    The $420 jury duty fee is income (line 21, page 1 of Form 1040) but none of the expenses relating to the jury duty [$30 (parking), $45 (meals), and use of automobile] are deductible—covered in Chapter 3 of the text.

15. The $3,520 of mortgage interest reported on line 10 of Schedule A is the $4,400 reduced by the $880 claimed as part of the home office deduction (see item 4).

    Charitable contributions of $3,800 are reported on line 16 of Schedule A, the total of $3,200 of the Johnsons' contributions plus the $600 the Johnsons paid on Vivian's pledge.

    The $2,480 of ad valorem taxes reported on line 6 of Schedule is the $3,100 reduced by the $620 claimed as part of the home office deduction (see item 4).

    Medical expenses of $12,197 are reported on line 1 of Schedule A, reflecting the Johnsons' expenses of $4,800, Vivian's medical expenses of $7,300 (see item 12), and medical mileage of $97 (420 miles × 23 cents).

    Since Wyoming does not have a state income tax, the Johnsons will deduct their sales tax on Schedule A. Since the Johnsons do not keep track of their sales taxes, their deduction will be determined based on their $107,075 of adjusted AGI (AGI $105,175 + $1,900 City of Cheyenne interest income) and their five exemptions. Their deductible sales tax is $2,541 (state tax of $753 + local tax of $188 + $1,600 for the sales tax on the camper).

16. Besides two personal exemptions, the Johnsons can claim dependency exemptions for Vivian, Kirby, and Toby. Both Kirby and Toby meet the qualifying child definition, while Vivian is a qualifying relative. Meredith, however, meets neither classification. She is not a qualifying child due to the age test (i.e., not under 19, disabled, or a student), and she is not a qualifying relative due to the gross income test (i.e., income in excess of $3,500).

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17. A brief summary of the Johnsons' tax return for 2015 appears below.

Gross income:	
Salary	$38,000
Schedule B	7,000
Schedule C	70,544
Schedule D	9,100
Schedule E	2,895
Miscellaneous (jury pay)	420
Deductions *for* AGI:	
Deductible self-employment tax	(4,984)
H.R. 10 and IRA	(14,000)
Health insurance premiums	(3,800)
AGI	$105,175
Itemized deductions (deductions *from* AGI)	(14,020)
Personal and dependency exemptions	(20,000)
Taxable income	$ 71,155

Computation of tax liability through use of the *Schedule D Tax Worksheet* yields a liability of $8,734. To this is added the self-employment tax of $9,967 (see Schedule SE) for a total amount due of $18,701. As the Johnsons had paid in $21,250 ($150 overpayment for 2014 + $5,100 Sheri's withholdings + $16,000 quarterly estimated tax payments), the overpayment of $2,549 ($21,250 – $18,701) is applied towards their 2016 tax liability.

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Form **1040** Department of the Treasury—Internal Revenue Service (99) **U.S. Individual Income Tax Return** **2015** OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2015, or other tax year beginning , 2015, ending , 20 See separate instructions.

Your first name and initial	Last name	Your social security number
David R	Johnson	111-11-1112
If a joint return, spouse's first name and initial	Last name	Spouse's social security number
Sheri N	Johnson	123-45-6785

Home address (number and street). If you have a P.O. box, see instructions. Apt. no.
641 Cody Way

▲ Make sure the SSN(s) above and on line 6c are correct.

City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions).
Casper WY 82609

Foreign country name | Foreign province/state/county | Foreign postal code

Presidential Election Campaign
Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund ☐ You ☐ Spouse

Filing Status

Check only one box.

1 ☐ Single
2 ☒ Married filing jointly (even if only one had income)
3 ☐ Married filing separately. Enter spouse's SSN above and full name here. ▶
4 ☐ Head of household (with qualifying person). (See instr.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 ☐ Qualifying widow(er) with dependent child

Exemptions

6a ☒ **Yourself.** If someone can claim you as a dependent, **do not** check box 6a
b ☒ **Spouse**

Boxes checked on 6a and 6b 2
No. of children on 6c who:
- **lived with you** 2
- **did not live with you due to divorce or separation (see instructions)**

Dependents on 6c not entered above 1
Add numbers on lines above ▶ 5

c **Dependents:**

(1) First name	Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) ☒ if child under age 17 qualifying for child tax credit (see instructions)
Kirby	Johnson	123-45-6788	Daughter	
Toby	Johnson	123-45-6789	Son	
Vivian	Olson	123-45-6786	Parent	

If more than four dependents, see instructions and check here ▶ ☐

d Total number of exemptions claimed

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a W-2, see instructions.

7	Wages, salaries, tips, etc. Attach Form(s) W-2		7	38,000
8a	**Taxable** interest. Attach Schedule B if required		8a	6,300
b	**Tax-exempt** interest. **Do not** include on line 8a	8b 1,900		
9a	Ordinary dividends. Attach Schedule B if required		9a	700
b	Qualified dividends	9b 700		
10	Taxable refunds, credits, or offsets of state and local income taxes		10	0
11	Alimony received		11	
12	Business income or (loss). Attach Schedule C or C-EZ		12	70,544
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ ☐		13	9,100
14	Other gains or (losses). Attach Form 4797		14	
15a	IRA distributions	15a	b Taxable amount	15b 0
16a	Pensions and annuities	16a	b Taxable amount	16b 0
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E		17	2,895
18	Farm income or (loss). Attach Schedule F		18	0
19	Unemployment compensation		19	
20a	Social security benefits	20a	b Taxable amount	20b
21	Other income. List type and amount JURY PAY		21	420
22	Combine the amounts in the far right column for lines 7 through 21. This is your **total income** ▶		22	127,959

Adjusted Gross Income

23	Educator expenses	23 0	
24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24 0	
25	Health savings account deduction. Attach Form 8889	25 0	
26	Moving expenses. Attach Form 3903	26 0	
27	Deductible part of self-employment tax. Attach Schedule SE	27 4,984	
28	Self-employed SEP, SIMPLE, and qualified plans	28 9,000	
29	Self-employed health insurance deduction	29 3,800	
30	Penalty on early withdrawal of savings	30 0	
31a	Alimony paid b Recipient's SSN ▶	31a	
32	IRA deduction	32 5,000	
33	Student loan interest deduction	33	
34	Tuition and fees. Attach Form 8917	34	
35	Domestic production activities deduction. Attach Form 8903	35 0	
36	Add lines 23 through 35		36 22,784
37	Subtract line 36 from line 22. This is your **adjusted gross income** ▶		37 105,175

KIA **For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions.** Form **1040** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 1040 (2015) David R Johnson 111-11-1112 Page 2

Tax and Credits	38	Amount from line 37 (adjusted gross income)		38	105,175
	39a	Check if: ☐ You were born before January 2, 1951, ☐ Blind. ☐ Spouse was born before January 2, 1951, ☐ Blind. **Total boxes checked** ▶ 39a 0			
	b	If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ 39b ☐			
Standard Deduction for— • People who check any box on line 39a or 39b **or** who can be claimed as a dependent, see instructions. • All others: Single or Married filing separately, $6,300 Married filing jointly or Qualifying widow(er), $12,600 Head of household, $9,250	40	**Itemized deductions** (from Schedule A) **or** your **standard deduction** (see left margin)		40	14,020
	41	Subtract line 40 from line 38		41	91,155
	42	**Exemptions.** If line 38 is $154,950 or less, multiply $4,000 by the number on line 6d. Otherwise, see instructions		42	20,000
	43	**Taxable income.** Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-		43	71,155
	44	**Tax** (see instructions). Check if any from: a ☐ Form(s) 8814 b ☐ Form 4972 c ☐		44	8,734
	45	**Alternative minimum tax** (see instructions). Attach Form 6251 ▶		45	0
	46	Excess advance premium tax credit repayment. Attach Form 8962		46	
	47	Add lines 44, 45, and 46		47	8,734
	48	Foreign tax credit. Attach Form 1116 if required	0		
	49	Credit for child and dependent care expenses. Attach Form 2441			
	50	Education credits from Form 8863, line 19			
	51	Retirement savings contributions credit. Attach Form 8880	0		
	52	Child tax credit. Attach Schedule 8812, if required			
	53	Residential energy credits. Attach Form 5695			
	54	Other credits from Form: a ☐ 3800 b ☐ 8801 c ☐	0		
	55	Add lines 48 through 54. These are your **total credits**		55	0
	56	Subtract line 55 from line 47. If line 55 is more than line 47, enter -0- ▶		56	8,734
Other Taxes	57	Self-employment tax. Attach Schedule SE		57	9,967
	58	Unreported social security and Medicare tax from Form: a ☐ 4137 b ☐ 8919		58	0
	59	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required		59	0
	60a	Household employment taxes from Schedule H		60a	0
	b	First-time homebuyer credit repayment. Attach Form 5405 if required		60b	0
	61	Health care: individual responsibility (see instructions) Full-year coverage ☒		61	0
	62	Taxes from: a ☐ Form 8959 b ☐ Form 8960 c ☐ Instructions; enter code(s)		62	0
	63	Add lines 56 through 62. This is your **total tax** ▶		63	18,701
Payments If you have a qualifying child, attach Schedule EIC.	64	Federal income tax withheld from Forms W-2 and 1099	5,100		
	65	2015 estimated tax payments and amount applied from 2014 return	16,150		
	66a	**Earned income credit (EIC)**			
	b	Nontaxable combat pay election 66b			
	67	Additional child tax credit. Attach Schedule 8812			
	68	American opportunity credit from Form 8863, line 8			
	69	Net premium tax credit. Attach Form 8962			
	70	Amount paid with request for extension to file			
	71	Excess social security and tier 1 RRTA tax withheld	0		
	72	Credit for federal tax on fuels. Attach Form 4136			
	73	Credits from Form: a ☐ 2439 b ☐ Reserved c ☐ 8885 d ☐	0		
	74	Add lines 64, 65, 66a, and 67 through 73. These are your **total payments** ▶		74	21,250
Refund	75	If line 74 is more than line 63, subtract line 63 from line 74. This is the amount you **overpaid**		75	2,549
	76a	Amount of line 75 you want **refunded to you.** If Form 8888 is attached, check here ▶ ☐		76a	0
Direct deposit? See instructions.	b	Routing number XXXXXXXXX ▶ c Type: ☐ Checking ☐ Savings			
	d	Account number XXXXXXXXXXXXXXXXX			
	77	Amount of line 75 you want **applied to your 2016 estimated tax** ▶	2,549		
Amount You Owe	78	**Amount you owe.** Subtract line 74 from line 63. For details on how to pay, see instructions ▶		78	
	79	Estimated tax penalty (see instructions)	0		

Third Party Designee Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ **Yes.** Complete below ☒ **No**
Designee's name ▶ Phone no. ▶ Personal identification number (PIN) ▶

Sign Here Joint return? See instructions. Keep a copy for your records.
Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number
		Mining Engineer	312-555-0010
Spouse's signature. If a joint return, **both** must sign.	Date	Spouse's occupation	If the IRS sent you an Identity Protection PIN, enter it here (see inst.)
		Paralegal	

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

KIA www.irs.gov/form1040 Form **1040** (2015)

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SCHEDULE A (Form 1040)
Department of the Treasury Internal Revenue Service (99)

Itemized Deductions

▶ Information about Schedule A and its separate instructions is at *www.irs.gov/scheduleA.*
▶ Attach to Form 1040.

OMB No. 1545-0074
2015
Attachment Sequence No. **07**

Name(s) shown on Form 1040: David R Johnson
Your social security number: 111-11-1112

Medical and Dental Expenses		**Caution.** Do not include expenses reimbursed or paid by others.			
	1	Medical and dental expenses (see instructions)	1	12,197	
	2	Enter amount from Form 1040, line 38 . . . 2 105,175			
	3	Multiply line 2 by 10% (.10). But if either you or your spouse was born before January 2, 1951, multiply line 2 by 7.5% (.075) instead	3	10,518	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-			4 1,679
Taxes You Paid	5	State and local **(check only one box):** a. ☐ Income taxes, or b. ☒ General sales taxes	5	2,541	
	6	Real estate taxes (see instructions)	6	2,480	
	7	Personal property taxes	7	0	
	8	Other taxes. List type and amount ▶	8	0	
	9	Add lines 5 through 8			9 5,021
Interest You Paid	10	Home mortgage interest and points reported to you on Form 1098	10	3,520	
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11	0	
Note. Your mortgage interest deduction may be limited (see instructions).	12	Points not reported to you on Form 1098. See instructions for special rules	12	0	
	13	Mortgage insurance premiums (see instructions)	13	0	
	14	Investment interest. Attach Form 4952 if required. (See instructions.)	14		
	15	Add lines 10 through 14			15 3,520
Gifts to Charity If you made a gift and got a benefit for it, see instructions.	16	Gifts by cash or check. If you made any gift of $250 or more, see instructions	16	3,800	
	17	Other than by cash or check. If any gift of $250 or more, see instructions. You **must** attach Form 8283 if over $500	17	0	
	18	Carryover from prior year	18	0	
	19	Add lines 16 through 18			19 3,800
Casualty and Theft Losses	20	Casualty or theft loss(es). Attach Form 4684. (See instructions.)			20 0
Job Expenses and Certain Miscellaneous Deductions	21	Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. (See instructions.) ▶ Form 2106	21	1,340	
	22	Tax preparation fees	22		
	23	Other expenses—investment, safe deposit box, etc. List type and amount ▶	23	0	
	24	Add lines 21 through 23	24	1,340	
	25	Enter amount from Form 1040, line 38 . . . 25 105,175			
	26	Multiply line 25 by 2% (.02)	26	2,104	
	27	Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-			27 0
Other Miscellaneous Deductions	28	Other—from list in instructions. List type and amount ▶			28 0
Total Itemized Deductions	29	Is Form 1040, line 38, over $154,950? ☒ **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40. ☐ **Yes.** Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.			29 14,020
	30	If you elect to itemize deductions even though they are less than your standard deduction, check here ▶ ☐			

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SCHEDULE B (Form 1040A or 1040)

Department of the Treasury Internal Revenue Service (99)

Interest and Ordinary Dividends

▶ Attach to Form 1040A or 1040.

▶ Information about Schedule B and its instructions is a *www.irs.gov/scheduleb*.

OMB No. 1545-0074

2015

Attachment Sequence No. **08**

Name(s) shown on return: David R Johnson

Your social security number: 111-11-1112

Part I Interest

(See instructions for Schedule B, and the instructions for Form 1040A, or Form 1040, line 8a.)

Note: If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

		Amount
1	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see instructions and list this interest first. Also, show that buyer's social security number and address ▶	
	City of Cheyenne	0
	Wells Fargo Bank	1,100
	Bank of America	400
	Local Rancher	4,800
2	Add the amounts on line 1	6,300
3	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815	
4	Subtract line 3 from line 2. Enter the result here and on Form 1040A, or Form 1040, line 8a ▶	6,300

Note: If line 4 is over $1,500, you must complete Part III.

Part II Ordinary Dividends

(See instructions for Schedule B, and the instructions for Form 1040A, or Form 1040, line 9a.)

Note: If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

		Amount
5	List name of payer ▶	
	Meadowlark Corp.	700
6	Add the amounts on line 5. Enter the total here and on Form 1040A, or Form 1040, line 9a ▶	700

Note. If line 6 is over $1,500, you must complete Part III.

Part III Foreign Accounts and Trusts

(See instructions.)

You must complete this part if you **(a)** had over $1,500 of taxable interest or ordinary dividends; **(b)** had a foreign account; or **(c)** received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

		Yes	No
7a	At any time during 2015, did you have a financial interest in or signature authority over a financial account (such as a bank account, securities account, or brokerage account) located in a foreign country? See instructions.		X
	If "Yes," are you required to file FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority? See FinCEN Form 114 and its instructions for filing requirements and exceptions to those requirements		
b	If you are required to file FinCEN Form 114, enter the name of the foreign country where the financial account is located ▶		
8	During 2015, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See instructions.		X

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SCHEDULE C (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Profit or Loss From Business

(Sole Proprietorship)

▶ Information about Schedule C and its separate instructions is at *www.irs.gov/schedulec.*

▶ Attach to Form 1040, 1040NR, or 1041; partnerships generally must file Form 1065.

OMB No. 1545-0074

2015

Attachment Sequence No. 09

Name of proprietor: David R Johnson

Social security number (SSN): 111-11-1112

A Principal business or profession, including product or service (see instructions): Engineer, service to mining companies

B Enter code from instructions ▶ 541990

C Business name. If no separate business name, leave blank.

D Employer ID number (EIN), (see instr.)

E Business address (including suite or room no.) ▶ 641 Cody Way
City, town or post office, state, and ZIP code Casper WY 82609

F Accounting method: (1) [X] Cash (2) [ ] Accrual (3) [ ] Other (specify) ▶

G Did you "materially participate" in the operation of this business during 2015? If "No," see instructions for limit on losses . . . [X] Yes [ ] No

H If you started or acquired this business during 2015, check here . . . ▶ [ ]

I Did you make any payments in 2015 that would require you to file Form(s) 1099? (see instructions) . . . [ ] Yes [X] No

J If "Yes," did you or will you file required Forms 1099? . . . [ ] Yes [ ] No

Part I Income

1	Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on form W-2 and the "Statutory employee" box on that form was checked. ▶ [ ]	1	117,620
2	Returns and allowances	2	
3	Subtract line 2 from line 1	3	117,620
4	Cost of goods sold (from line 42)	4	0
5	**Gross profit.** Subtract line 4 from line 3	5	117,620
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	
7	**Gross income.** Add lines 5 and 6 ▶	7	117,620

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8	2,400	18	Office expense (see instructions)	18	1,200
9	Car and truck expenses (see instructions)	9	5,390	19	Pension and profit-sharing plans	19	
10	Commissions and fees	10		20	Rent or lease (see instructions):		
11	Contract labor (see instructions)	11		a	Vehicles, machinery, and equipment	20a	0
12	Depletion	12		b	Other business property	20b	
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13	9,390	21	Repairs and maintenance	21	
14	Employee benefit programs (other than on line 19)	14		22	Supplies (not included in Part III)	22	3,200
15	Insurance (other than health)	15		23	Taxes and licenses	23	300
16	Interest:			24	Travel, meals, and entertainment:		
a	Mortgage (paid to banks, etc.)	16a		a	Travel	24a	14,320
b	Other	16b		b	Deductible meals and entertainment (see instructions)	24b	3,050
17	Legal and professional services	17		25	Utilities	25	
				26	Wages (less employment credits)	26	
				27a	Other expenses (from line 48)	27a	1,280
				b	**Reserved for future use**	27b	

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27a ▶	28	40,530
29	Tentative profit or (loss). Subtract line 28 from line 7	29	77,090
30	Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method (see instructions). **Simplified method filers only:** enter the total square footage of: (a) your home: _____ and (b) the part of your home used for business: _____. Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30	30	6,546
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on both **Form 1040, line 12** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see instructions). Estates and trusts, enter on **Form 1041, line 3.** • If a loss, you **must** go to line 32.	31	70,544
32	If you have a loss, check the box that describes your investment in this activity (see instructions). • If you checked 32a, enter the loss on both **Form 1040, line 12**, (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see the line 31 instructions). Estates and trusts, enter on **Form 1041, line 3.** • If you checked 32b, you **must** attach **Form 6198.** Your loss may be limited.	32a [ ] All investment is at risk. 32b [ ] Some investment is not at risk.	

KIA **For Paperwork Reduction Act Notice, see the separate instructions.** **Schedule C (Form 1040) 2015**

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Schedule C (Form 1040) 2015 David R Johnson 111-11-1112 Page 2

Part III Cost of Goods Sold (see instructions)

33 Method(s) used to value closing inventory: a ☐ Cost b ☐ Lower of cost or market c ☐ Other (attach explanation)

34 Was there any change in determining quantities, costs, or valuations between opening and closing inventory? If "Yes," attach explanation . . . ☐ Yes ☐ No

35	Inventory at beginning of year. If different from last year's closing inventory, attach explanation	35	
36	Purchases less cost of items withdrawn for personal use	36	
37	Cost of labor. Do not include any amounts paid to yourself	37	
38	Materials and supplies	38	
39	Other costs	39	
40	Add lines 35 through 39	40	0
41	Inventory at end of year	41	
42	**Cost of goods sold.** Subtract line 41 from line 40. Enter the result here and on line 4	42	0

Part IV Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 9 and are not required to file Form 4562 for this business. See the instructions for line 13 to find out if you must file Form 4562.

43 When did you place your vehicle in service for business purposes? (month, day, year) ▶ _____

44 Of the total number of miles you drove your vehicle during 2015, enter the number of miles you used your vehicle for:

a Business _____ b Commuting (see instructions) _____ c Other _____

45	Was your vehicle available for personal use during off-duty hours?	☐ Yes	☐ No
46	Do you (or your spouse) have another vehicle available for personal use?	☐ Yes	☐ No
47a	Do you have evidence to support your deduction?	☐ Yes	☐ No
b	If "Yes," is the evidence written?	☐ Yes	☐ No

Part V Other Expenses. List below business expenses not included on lines 8–26 or line 30.

Telephone/Internet	860
Trade Journals	240
Professional Dues	180

48 **Total other expenses.** Enter here and on line 27a . . . 48 1,280

KIA Schedule C (Form 1040) 2015

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SCHEDULE D (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Capital Gains and Losses

► Attach to Form 1040 or Form 1040NR.

► Information about Schedule D and its separate instructions is at *www.irs.gov/scheduled.*

► Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.

OMB No. 1545-0074

2015

Attachment Sequence No. 12

Name(s) shown on return: David R Johnson

Your social security number: 111-11-1112

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 1b	0	0		0
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked	0	0	0	0
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked	0	0	0	0
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked	0	0	0	0

4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824	4	0
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	5	
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your **Capital Loss Carryover Worksheet** in the instructions.	6	(-4,000)
7 **Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the next page	7	-4,000

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b	0	0		0
8b Totals for all transactions reported on Form(s) 8949 with **Box D** checked	0	0	0	0
9 Totals for all transactions reported on Form(s) 8949 with **Box E** checked	0	0	0	0
10 Totals for all transactions reported on Form(s) 8949 with **Box F** checked	29,000	25,900	0	3,100

11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824	11	10,000
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	12	
13 Capital gain distributions. See the instructions	13	0
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your **Capital Loss Carryover Worksheet** in the instructions	14	(0)
15 **Net long-term capital gain or (loss).** Combine lines 8a through 14 in column (h). Then go to Part III on page 2	15	13,100

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Schedule D (Form 1040) 2015 David R Johnson 111-11-1112 Page 2

Part III Summary

16	Combine lines 7 and 15 and enter the result	**16**	9,100
	• If line 16 is a **gain**, enter the amount from line 16 on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 17 below. • If line 16 is a **loss**, skip lines 17 through 20 below. Then go to line 21. Also be sure to complete line 22. • If line 16 is **zero**, skip lines 17 through 21 below and enter -0- on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 22.		
17	Are lines 15 and 16 **both** gains? [X] **Yes.** Go to line 18. [ ] **No.** Skip lines 18 through 21, and go to line 22.		
18	Enter the amount, if any, from line 7 of the **28% Rate Gain Worksheet** in the instructions ▶	**18**	3,000
19	Enter the amount, if any, from line 18 of the **Unrecaptured Section 1250 Gain Worksheet** in the instructions ▶	**19**	0
20	Are lines 18 and 19 **both** zero or blank? [ ] **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). **Do not** complete lines 21 and 22 below. [X] **No.** Complete the **Schedule D Tax Worksheet** in the instructions. **Do not** complete lines 21 and 22 below.		
21	If line 16 is a loss, enter here and on Form 1040, line 13, or Form 1040NR, line 14, the **smaller** of: • The loss on line 16 or • ($3,000), or if married filing separately, ($1,500) **Note.** When figuring which amount is smaller, treat both amounts as positive numbers.	**21**	( )
22	Do you have qualified dividends on Form 1040, line 9b, or Form 1040NR, line 10b? [ ] **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). [ ] **No.** Complete the rest of Form 1040 and Form 1040NR.		

KIA Schedule D (Form 1040) 2015

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Form 8949 (2015) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Name and SSN or taxpayer identification no. not required if shown on Page 1	Social security number or taxpayer identification number
David R Johnson	111-11-1112

Before you check Box D, E, or F below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part II **Long-Term.** Transactions involving capital assets you held more than 1 year are long term. For short-term transactions, see page 1.

Note. You may aggregate all long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 8a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box D, E, *or* F below. Check only one box. If more than one box applies for your long-term transactions, complete a separate Form 8949, page 2, for each applicable box. If you have more long-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

☐ **(D)** Long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)

☐ **(E)** Long-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS

☒ **(F)** Long-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). **See the separate instructions.** (f) Code(s) from instructions	(g) Amount of adjustment	(h) **Gain or (loss).** Subtract column (e) from column (d) and combine the result with column (g)
Cormorant Stock	03/07/14	WORTHLESS	WORTHLESS	3,900		0	-3,900
Antique Gun Collection	inherit	07/10/15	29,000	22,000	C	0	7,000
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
2 **Totals.** Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 8b** (if **Box D** above is checked), **line 9** (if **Box E** above is checked), or **line 10** (if **Box F** above is checked) ▶			29,000	25,900		0	3,100

Note. If you checked Box D above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

KIA Form **8949** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

SCHEDULE E (Form 1040)
Department of the Treasury
Internal Revenue Service (99)

Supplemental Income and Loss

(From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)

▶ Attach to Form 1040, 1040NR, or Form 1041.

▶ Information about Schedule E and its separate instructions is at *www.irs.gov/schedulee.*

OMB No. 1545-0074

2015

Attachment Sequence No. **13**

Name(s) shown on return: David R Johnson

Your social security number: 111-11-1112

Part I Income or Loss From Rental Real Estate and Royalties **Note.** If you are in the business of renting personal property, use **Schedule C** or **C-EZ** (see instructions). If you are an individual, report farm rental income or loss from **Form 4835** on page 2, line 40.

A Did you make any payments in 2015 that would require you to file Form(s) 1099? (see instructions) ☐ Yes ☒ No

B If "Yes," did you or will you file all required Forms 1099? ☐ Yes ☐ No

1a Physical address of each property (street, city, state, ZIP code)

A 4620 Cottonwood Ln Casper WY 82609

B

C

1b Type of Property (from list below)	2 For each rental real estate property listed above, report the number of fair rental and personal use days. Check the **QJV** box only if you meet the requirements to file as a qualified joint venture. See instructions.	Fair Rental Days	Personal Use Days	QJV
A 1	A	365	0	☐
B	B			☐
C	C			☐

Type of Property:
1 Single Family Residence 3 Vacation/Short-Term Rental 5 Land 7 Self-Rental
2 Multi-Family Residence 4 Commercial 6 Royalties 8 Other (describe)

Income: / Properties:		A	B	C
3 Rents received	3	28,600		
4 Royalties received	4	0	0	0
Expenses:				
5 Advertising	5	0		
6 Auto and travel (see instructions)	6	0		
7 Cleaning and maintenance	7	1,200		
8 Commissions	8	0		
9 Insurance	9	3,100		
10 Legal and other professional fees	10	0		
11 Management fees	11	0		
12 Mortgage interest paid to banks, etc. (see instructions)	12	0		
13 Other interest	13	0		
14 Repairs	14	800		
15 Supplies	15	0		
16 Taxes	16	2,400		
17 Utilities	17	0		
18 Depreciation expense or depletion	18	18,205		
19 Other (list) ▶ _____	19	0		
20 Total expenses. Add lines 5 through 19	20	25,705	0	0
21 Subtract line 20 from line 3 (rents) and/or 4 (royalties). If result is a (loss), see instructions to find out if you must file **Form 6198**	21	2,895	0	0
22 Deductible rental real estate loss after limitation, if any, on **Form 8582** (see instructions)	22	(0)	( )	( )

23a Total of all amounts reported on line 3 for all rental properties	23a	28,600	
b Total of all amounts reported on line 4 for all royalty properties	23b	0	
c Total of all amounts reported on line 12 for all properties	23c	0	
d Total of all amounts reported on line 18 for all properties	23d	18,205	
e Total of all amounts reported on line 20 for all properties	23e	25,705	

24 **Income.** Add positive amounts shown on line 21. **Do not** include any losses	24	2,895
25 **Losses.** Add royalty losses from line 21 and rental real estate losses from line 22. Enter total losses here.	25	(0)
26 **Total rental real estate and royalty income or (loss).** Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 40 on page 2 do not apply to you, also enter this amount on Form 1040, line 17, or Form 1040NR, line 18. Otherwise, include this amount in the total on line 41 on page 2	26	2,895

KIA For Paperwork Reduction Act Notice, see the separate instructions. Schedule E (Form 1040) 2015

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SCHEDULE SE (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Self-Employment Tax

▶ Information about Schedule SE and its separate instructions is at *www.irs.gov/schedulese.*
▶ Attach to Form 1040 or Form 1040NR.

OMB No. 1545-0074

2015

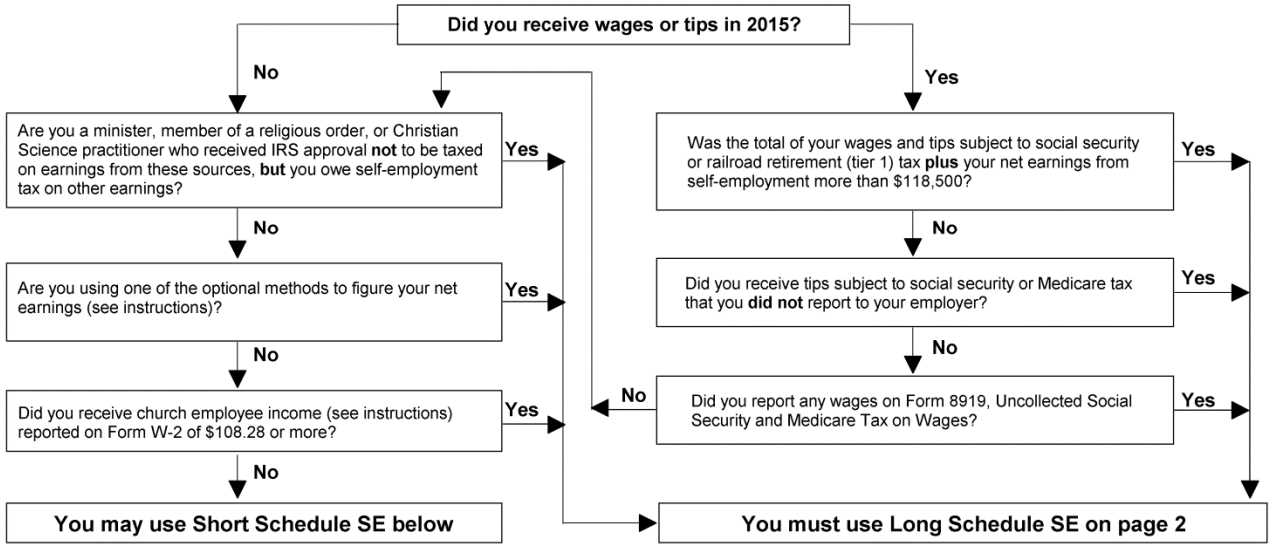
Attachment Sequence No. **17**

Name of person with **self-employment** income (as shown on Form 1040 or Form 1040NR)	Social security number of person with **self-employment** income ▶
David R Johnson	111-11-1112

Before you begin: To determine if you must file Schedule SE, see the instructions.

May I Use Short Schedule SE or Must I Use Long Schedule SE?

Note. Use this flowchart **only if** you must file Schedule SE. If unsure, see *Who Must File Schedule SE* in the instructions.



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

1a	Net farm profit or (loss) from Schedule F, line 34, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A.	1a	0
b	If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4b, or listed on Schedule K-1 (Form 1065), box 20, code Z	1b	(0)
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Ministers and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report	2	70,544
3	Combine lines 1a, 1b, and 2.	3	70,544
4	Multiply line 3 by 92.35% (.9235). If less than $400, you do not owe self-employment tax; **do not** file this schedule unless you have an amount on line 1b ▶	4	65,147
	Note. If line 4 is less than $400 due to Conservation Reserve Program payments on line 1b, see instructions.		
5	**Self-employment tax.** If the amount on line 4 is: • $118,500 or less, multiply line 4 by 15.3% (.153). Enter the result here and on **Form 1040, line 57,** or **Form 1040NR, line 55.** • More than $118,500, multiply line 4 by 2.9% (.029). Then, add $14,694 to the result. Enter the total here and on **Form 1040, line 57,** or **Form 1040NR, line 55.**	5	9,967
6	**Deduction for one-half of self-employment tax.** Multiply line 5 by 50% (.50). Enter the result here and on **Form 1040, line 27,** or **Form 1040NR, line 27**	6	4,984

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Form **6252**

Department of the Treasury
Internal Revenue Service

Installment Sale Income

▶ Attach to your tax return.
▶ Use a separate form for each sale or other disposition of property on the installment method.
▶ Information about Form 6252 and its instructions is at *www.irs.gov/form6252.*

OMB No. 1545-0228

2015

Attachment Sequence No. **79**

Name(s) shown on return: David R Johnson

Identifying number: 111-11-1112

1 Description of property ▶ Converse County Grazing Land

2a Date acquired (mm/dd/yyyy) ▶ 07/12/01 b Date sold (mm/dd/yyyy) ▶ 08/02/14

3 Was the property sold to a related party (see instructions) after May 14, 1980? If "No," skip line 4 . . . . . ☐ Yes ☒ No

4 Was the property you sold to a related party a marketable security? If "Yes," complete Part III. If "No," complete Part III for the year of sale and the 2 years after the year of sale . . . . . ☐ Yes ☐ No

Part I **Gross Profit and Contract Price.** Complete this part for the year of sale only.

5	Selling price including mortgages and other debts. **Do not** include interest whether stated or unstated		5	
6	Mortgages, debts, and other liabilities the buyer assumed or took the property subject to (see instructions)	6		
7	Subtract line 6 from line 5	7	0	
8	Cost or other basis of property sold	8		
9	Depreciation allowed or allowable	9		
10	Adjusted basis. Subtract line 9 from line 8	10	0	
11	Commissions and other expenses of sale	11		
12	Income recapture from Form 4797, Part III (see instructions)	12		
13	Add lines 10, 11, and 12		13	0
14	Subtract line 13 from line 5. If zero or less, **do not** complete the rest of this form (see instructions)		14	0
15	If the property described on line 1 above was your main home, enter the amount of your excluded gain (see instructions). Otherwise, enter -0-		15	0
16	**Gross profit.** Subtract line 15 from line 14		16	0
17	Subtract line 13 from line 6. If zero or less, enter -0-		17	
18	**Contract price.** Add line 7 and line 17		18	

Part II **Installment Sale Income.** Complete this part for the year of sale **and** any year you receive a payment or have certain debts you must treat as a payment on installment obligations.

19	Gross profit percentage (expressed as a decimal amount). Divide line 16 by line 18. For years after the year of sale, see instructions		19	0.3333
20	If this is the year of sale, enter the amount from line 17. Otherwise, enter -0-		20	0
21	Payments received during year (see instructions). **Do not** include interest, whether stated or unstated		21	6,000
22	Add lines 20 and 21		22	6,000
23	Payments received in prior years (see instructions). **Do not** include interest, whether stated or unstated	23		
24	**Installment sale income.** Multiply line 22 by line 19		24	2,000
25	Enter the part of line 24 that is ordinary income under the recapture rules (see instructions)		25	0
26	Subtract line 25 from line 24. Enter here and on Schedule D or Form 4797 (see instructions)		26	2,000

Part III **Related Party Installment Sale Income. Do not** complete if you received the final payment this tax year.

27 Name, address, and taxpayer identifying number of related party

28 Did the related party resell or dispose of the property ("second disposition") during this tax year? . . . . . ☐ Yes ☐ No

29 **If the answer to question 28 is "Yes," complete lines 30 through 37 below unless one of the following conditions is met. Check the box that applies.**

a ☐ The second disposition was more than 2 years after the first disposition (other than dispositions of marketable securities). If this box is checked, enter the date of disposition (mm/dd/yyyy) . . . . . ▶

b ☐ The first disposition was a sale or exchange of stock to the issuing corporation.

c ☐ The second disposition was an involuntary conversion and the threat of conversion occurred after the first disposition.

d ☐ The second disposition occurred after the death of the original seller or buyer.

e ☐ It can be established to the satisfaction of the IRS that tax avoidance was not a principal purpose for either of the dispositions. If this box is checked, attach an explanation (see instructions).

30	Selling price of property sold by related party (see instructions)	30	
31	Enter contract price from line 18 for year of first sale	31	
32	Enter the **smaller** of line 30 or line 31	32	
33	Total payments received by the end of your 2015 tax year (see instructions)	33	
34	Subtract line 33 from line 32. If zero or less, enter -0-	34	
35	Multiply line 34 by the gross profit percentage on line 19 for year of first sale	35	
36	Enter the part of line 35 that is ordinary income under the recapture rules (see instructions)	36	
37	Subtract line 36 from line 35. Enter here and on Schedule D or Form 4797 (see instructions)	37	

KIA **For Paperwork Reduction Act Notice, see page 4.** Form **6252** (2015)

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Form **8582**

Department of the Treasury
Internal Revenue Service (99)

Passive Activity Loss Limitations

▶ See separate instructions.
▶ Attach to Form 1040 or Form 1041.
▶ Information about Form 8582 and its instructions is available at *www.irs.gov/form8582.*

OMB No. 1545-1008

2015

Attachment Sequence No. **88**

Name(s) shown on return: David R Johnson

Identifying number: 111-11-1112

Part I 2015 Passive Activity Loss

Caution: *Complete Worksheets 1, 2 and 3 before completing Part I.*

Rental Real Estate Activities With Active Participation (For the definition of active participation, see **Special Allowance for Rental Real Estate Activities** in the instructions.)

1a	Activities with net income (enter the amount from Worksheet 1, column (a))	1a	2,895	
b	Activities with net loss (enter the amount from Worksheet 1, column (b))	1b	(0)	
c	Prior years unallowed losses (enter the amount from Worksheet 1, column (c))	1c	(0)	
d	Combine lines 1a, 1b, and 1c			1d 2,895

Commercial Revitalization Deductions From Rental Real Estate Activities

2a	Commercial revitalization deductions from Worksheet 2, column (a)	2a	( )	
b	Prior year unallowed commercial revitalization deductions from Worksheet 2, column (b)	2b	( )	
c	Add lines 2a and 2b			2c (0)

All Other Passive Activities

3a	Activities with net income (enter the amount from Worksheet 3, column (a))	3a	0	
b	Activities with net loss (enter the amount from Worksheet 3, column (b))	3b	(0)	
c	Prior years unallowed losses (enter the amount from Worksheet 3, column (c))	3c	(0)	
d	Combine lines 3a, 3b, and 3c			3d 0
4	Combine lines 1d, 2c, and 3d. If this line is zero or more, stop here and include this form with your return; all losses are allowed, including any prior year unallowed losses entered on line 1c, 2b, or 3c. Report the losses on the forms and schedules normally used			4 2,895

If line 4 is a loss and:
- Line 1d is a loss, go to Part II.
- Line 2c is a loss (and line 1d is zero or more), skip Part II and go to Part III.
- Line 3d is a loss (and lines 1d and 2c are zero or more), skip Parts II and III and go to line 15.

Caution: *If your filing status is married filing separately and you lived with your spouse at any time during the year,* ***do not*** *complete Part II or Part III. Instead, go to line 15.*

Part II Special Allowance for Rental Real Estate Activities With Active Participation

Note: *Enter all numbers in Part II as positive amounts. See instructions for an example.*

5	Enter the **smaller** of the loss on line 1d or the loss on line 4			5
6	Enter $150,000. If married filing separately, see instructions	6		
7	Enter modified adjusted gross income, but not less than zero (see instructions)	7		
	Note: *If line 7 is greater than or equal to line 6, skip lines 8 and 9, enter -0- on line 10. Otherwise, go to line 8.*			
8	Subtract line 7 from line 6	8		
9	Multiply line 8 by 50% (.5). **Do not** enter more than $25,000. If married filing separately, see instructions			9
10	Enter the **smaller** of line 5 or line 9			10

If line 2c is a loss, go to Part III. Otherwise, go to line 15.

Part III Special Allowance for Commercial Revitalization Deductions From Rental Real Estate Activities

Note: *Enter all numbers in Part III as positive amounts. See the example for Part II in the instructions.*

11	Enter $25,000 reduced by the amount, if any, on line 10. If married filing separately, see instructions	11	
12	Enter the loss from line 4	12	
13	Reduce line 12 by the amount on line 10	13	
14	Enter the **smallest** of line 2c (treated as a positive amount), line 11, or line 13	14	

Part IV Total Losses Allowed

15	Add the income, if any, on lines 1a and 3a and enter the total	15	
16	**Total losses allowed from all passive activities for 2015.** Add lines 10, 14, and 15. See instructions to find out how to report the losses on your tax return	16	

KIA **For Paperwork Reduction Act Notice, see instructions.** Form **8582** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 8582 (2015) David R Johnson 111-11-1112 Page 2

Caution: *The worksheets must be filed with your tax return. Keep a copy for your records.*

Worksheet 1—For Form 8582, Lines 1a, 1b, and 1c (See instructions.)

Name of activity	Current year		Prior years	Overall gain or loss	
	(a) Net income (line 1a)	(b) Net loss (line 1b)	(c) Unallowed loss (line 1c)	(d) Gain	(e) Loss
4620 Cottonwood Ln C	2,895	0	0	2,895	0
Total. Enter on Form 8582, lines 1a, 1b, and 1c ▶	2,895	0	0		

Worksheet 2—For Form 8582, Lines 2a and 2b (See instructions.)

Name of activity	(a) Current year deductions (line 2a)	(b) Prior year unallowed deductions (line 2b)	(c) Overall Loss
Total. Enter on Form 8582, lines 2a and 2b ▶	0	0	

Worksheet 3—For Form 8582, Lines 3a, 3b, and 3c (See instructions.)

Name of activity	Current year		Prior years	Overall gain or loss	
	(a) Net income (line 3a)	(b) Net loss (line 3b)	(c) Unallowed loss (line 3c)	(d) Gain	(e) Loss
Total. Enter on Form 8582, lines 3a, 3b, and 3c ▶					

Worksheet 4—Use this worksheet if an amount is shown on Form 8582, line 10 or 14 (See instructions.)

Name of activity	Form or schedule and line number to be reported on (see instructions)	(a) Loss	(b) Ratio	(c) Special allowance	(d) Subtract column (c) from column (a)
Total ▶			1.00		

Worksheet 5—Allocation of Unallowed Losses (See instructions.)

Name of activity	Form or schedule and line number to be reported on (see instructions)	(a) Loss	(b) Ratio	(c) Unallowed loss
Total ▶			1.00	

KIA Form **8582** (2015)

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Form **8824**

Department of the Treasury
Internal Revenue Service

Like-Kind Exchanges
(and section 1043 conflict-of-interest sales)

▶ Attach to your tax return.

▶ Information about Form 8824 and its separate instructions is at *www.irs.gov/form8824*.

OMB No. 1545-1190

2015

Attachment Sequence No. **109**

Name(s) shown on tax return	Identifying number
David R Johnson	111-11-1112

Part I Information on the Like-Kind Exchange

Note: *If the property described on line 1 or line 2 is real or personal property located outside the United States, indicate the country.*

1 Description of like-kind property given up:
Teton County Land

2 Description of like-kind property received:
Four Laramie City Lots

3	Date like-kind property given up was originally acquired (month, day, year)	3 03/10/97
4	Date you actually transferred your property to other party (month, day, year)	4 03/04/15
5	Date like-kind property you received was identified by written notice to another party (month, day, year). See instructions for 45-day written identification requirement	5 03/04/15
6	Date you actually received the like-kind property from other party (month, day, year). See instructions	6 03/04/15

7 Was the exchange of the property given up or received made with a related party, either directly or indirectly (such as through an intermediary)? See instructions. If "Yes," complete Part II. If "No," go to Part III . . . . . ☐ Yes ☒ No

Note: *Do not file this form if a related party sold property into the exchange, directly or indirectly (such as through an intermediary); that property became your replacement property; and none of the exceptions in line 11 applies to the exchange. Instead, report the disposition of the property as if the exchange had been a sale. If one of the exceptions on line 11 applies to the exchange, complete Part II.*

Part II Related Party Exchange Information

8 Name of related party	Relationship to you	Related party's identifying number

Address (no., street, and apt., room, or suite no., city or town, state, and ZIP code)

9 During this tax year (and before the date that is 2 years after the last transfer of property that was part of the exchange), did the related party sell or dispose of any part of the like-kind property received from you (or an intermediary) in the exchange? . . . . . ☐ Yes ☐ No

10 During this tax year (and before the date that is 2 years after the last transfer of property that was part of the exchange), did you sell or dispose of any part of the like-kind property you received? . . . . . ☐ Yes ☐ No

If both lines 9 and 10 are "No" and this is the year of the exchange, go to Part III. If both lines 9 and 10 are "No" and this is ***not*** *the year of the exchange, stop here. If either line 9 or line 10 is "Yes," complete Part III and report on this year's tax return the deferred gain or (loss) from line 24* ***unless*** *one of the exceptions on line 11 applies.*

11 If one of the exceptions below applies to the disposition, check the applicable box:

a ☐ The disposition was after the death of either of the related parties.

b ☐ The disposition was an involuntary conversion, and the threat of conversion occurred after the exchange.

c ☐ You can establish to the satisfaction of the IRS that neither the exchange nor the disposition had tax avoidance as one of its principal purposes. If this box is checked, attach an explanation (see instructions).

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 8824 (2015) Page **2**

Name(s) shown on tax return. Do not enter name and social security number if shown on page 1. | **Your social security number**

David R Johnson | 111-11-1112

Part III Realized Gain or (Loss), Recognized Gain, and Basis of Like-Kind Property Received

Caution: *If you transferred* ***and*** *received* ***(a)*** *more than one group of like-kind properties or* ***(b)*** *cash or other (not like-kind) property, see* **Reporting of multi-asset exchanges** *in the instructions.*

Note: *Complete lines 12 through 14* ***only*** *if you gave up property that was not like-kind. Otherwise, go to line 15.*

12	Fair market value (FMV) of other property given up	12		
13	Adjusted basis of other property given up	13		
14	Gain or (loss) recognized on other property given up. Subtract line 13 from line 12. Report the gain or (loss) in the same manner as if the exchange had been a sale		14	0
	Caution: *If the property given up was used previously or partly as a home, see* **Property used as home** *in the instructions.*			
15	Cash received, FMV of other property received, plus net liabilities assumed by other party, reduced (but not below zero) by any exchange expenses you incurred (see instructions)		15	8,000
16	FMV of like-kind property you received		16	792,000
17	Add lines 15 and 16		17	800,000
18	Adjusted basis of like-kind property you gave up, net amounts paid to other party, plus any exchange expenses **not** used on line 15 (see instructions)		18	50,000
19	**Realized gain or (loss).** Subtract line 18 from line 17		19	750,000
20	Enter the smaller of line 15 or line 19, but not less than zero		20	8,000
21	Ordinary income under recapture rules. Enter here and on Form 4797, line 16 (see instructions)		21	0
22	Subtract line 21 from line 20. If zero or less, enter -0-. If more than zero, enter here and on Schedule D or Form 4797, unless the installment method applies (see instructions)		22	8,000
23	**Recognized gain.** Add lines 21 and 22		23	8,000
24	Deferred gain or (loss). Subtract line 23 from line 19. If a related party exchange, see instructions		24	742,000
25	**Basis of like-kind property received.** Subtract line 15 from the sum of lines 18 and 23		25	50,000

Part IV Deferral of Gain From Section 1043 Conflict-of-Interest Sales

Note: *This part is to be used* ***only*** *by officers or employees of the executive branch of the Federal Government or judicial officers of the Federal Government (including certain spouses, minor or dependent children, and trustees as described in section 1043) for reporting nonrecognition of gain under section 1043 on the sale of property to comply with the conflict-of-interest requirements. This part can be used* ***only*** *if the cost of the replacement property is more than the basis of the divested property.*

26	Enter the number from the upper right corner of your certificate of divestiture. (**Do not** attach a copy of your certificate. Keep the certificate with your records.) ▶			
27	Description of divested property ▶			
28	Description of replacement property ▶			
29	Date divested property was sold (month, day, year)		29	
30	Sales price of divested property (see instructions)	30		
31	Basis of divested property	31		
32	**Realized gain.** Subtract line 31 from line 30		32	0
33	Cost of replacement property purchased within 60 days after date of sale	33		
34	Subtract line 33 from line 30. If zero or less, enter -0-		34	0
35	Ordinary income under recapture rules. Enter here and on Form 4797, line 10 (see instructions)		35	
36	Subtract line 35 from line 34. If zero or less, enter -0-. If more than zero, enter here and on Schedule D or Form 4797 (see instructions)		36	0
37	**Deferred gain.** Subtract the sum of lines 35 and 36 from line 32		37	0
38	**Basis of replacement property.** Subtract line 37 from line 33		38	0

KIA Form **8824** (2015)

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Form **2106**

Department of the Treasury
Internal Revenue Service (99)

Employee Business Expenses

▶ **Attach to Form 1040 or Form 1040NR.**

▶ **Information about Form 2106 and its separate instructions is available at *www.irs.gov/form2106*.**

OMB No. 1545-0074

2015

Attachment Sequence No. **129**

Your name	Occupation in which you incurred expenses	Social security number
Sheri N Johnson	Paralegal	123-45-6785

Part I **Employee Business Expenses and Reimbursements**

Step 1 Enter Your Expenses		**Column A** Other Than Meals and Entertainment	**Column B** Meals and Entertainment
1 Vehicle expense from line 22 or line 29. (Rural mail carriers: See instructions.)	1	0	
2 Parking fees, tolls, and transportation, including train, bus, etc., that **did not** involve overnight travel or commuting to and from work	2	0	
3 Travel expense while away from home overnight, including lodging, airplane, car rental, etc. **Do not** include meals and entertainment	3		
4 Business expenses not included on lines 1 through 3. **Do not** include meals and entertainment	4	1,340	
5 Meals and entertainment expenses (see instructions)	5		
6 **Total expenses.** In Column A, add lines 1 through 4 and enter the result. In Column B, enter the amount from line 5	6	1,340	

Note. *If you were not reimbursed for any expenses in Step 1, skip line 7 and enter the amount from line 6 on line 8.*

Step 2 Enter Reimbursements Received From Your Employer for Expenses Listed in Step 1

7 Enter reimbursements received from your employer that were **not** reported to you in box 1 of Form W-2. Include any reimbursements reported under code "L" in box 12 of your Form W-2 (see instructions)	7	0	

Step 3 Figure Expenses To Deduct on Schedule A (Form 1040 or Form 1040NR)

8 Subtract line 7 from line 6. If zero or less, enter -0-. However, if line 7 is greater than line 6 in Column A, report the excess as income on Form 1040, line 7 (or on Form 1040NR, line 8)	8	1,340	0
Note. *If **both columns** of line 8 are zero, you cannot deduct employee business expenses. Stop here and attach Form 2106 to your return.*			
9 In Column A, enter the amount from line 8. In Column B, multiply line 8 by 50% (.50). (Employees subject to Department of Transportation (DOT) hours of service limits: Multiply meal expenses incurred while away from home on business by 80% (.80) instead of 50%. For details, see instructions.)	9	1,340	0
10 Add the amounts on line 9 of both columns and enter the total here. **Also, enter the total on Schedule A (Form 1040), line 21** (or on **Schedule A (Form 1040NR), line 7**). (Armed Forces reservists, qualified performing artists, fee-basis state or local government officials, and individuals with disabilities: See the instructions for special rules on where to enter the total.) ▶	10		1,340

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form **8829**

Department of the Treasury
Internal Revenue Service (99)

Expenses for Business Use of Your Home

► File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year.

► Information about Form 8829 and its separate instructions is at *www.irs.gov/form8829.*

OMB No. 1545-0074

2015

Attachment Sequence No. **176**

Name(s) of proprietor(s): David R Johnson

Your social security number: 111-11-1112

Part I Part of Your Home Used for Business

1	Area used regularly and exclusively for business, regularly for daycare, or for storage of inventory or product samples (see instructions)	1	600
2	Total area of home	2	3,000
3	Divide line 1 by line 2. Enter the result as a percentage	3	20.00 %

For daycare facilities not used exclusively for business, go to line 4. All others, go to line 7.

4	Multiply days used for daycare during year by hours used per day	4	hr.	
5	Total hours available for use during the year (365 days X 24 hrs) (see instructions)	5	8,760	
6	Divide line 4 by line 5. Enter the result as a decimal amount	6		
7	Business percentage. For daycare facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3 ►	7		20.00 %

Part II Figure Your Allowable Deduction

8	Enter the amount from Schedule C, line 29, **plus** any gain derived from the business use of your home, **minus** any loss from the trade or business not derived from the business use of your home (see instructions)				8	77,090
	See instructions for columns (a) and (b) before completing lines 9-21.		**(a)** Direct expenses	**(b)** Indirect expenses		
9	Casualty losses (see instructions)	9				
10	Deductible mortgage interest (see instructions)	10		4,400		
11	Real estate taxes (see instructions)	11		3,100		
12	Add lines 9, 10, and 11	12	0	7,500		
13	Multiply line 12, column (b) by line 7			13 1,500		
14	Add line 12, column (a) and line 13				14	1,500
15	Subtract line 14 from line 8. If zero or less, enter -0-				15	75,590
16	Excess mortgage interest (see instructions)	16				
17	Insurance	17		2,300		
18	Rent	18				
19	Repairs and maintenance	19	1,200	2,900		
20	Utilities	20		4,800		
21	Other expenses (see instructions)	21	0	0		
22	Add lines 16 through 21	22	1,200	10,000		
23	Multiply line 22, column (b) by line 7			23 2,000		
24	Carryover of prior year operating expenses (see instructions)			24 0		
25	Add line 22, column (a), line 23, and line 24				25	3,200
26	Allowable operating expenses. Enter the **smaller** of line 15 or line 25				26	3,200
27	Limit on excess casualty losses and depreciation. Subtract line 26 from line 15				27	72,390
28	Excess casualty losses (see instructions)			28 0		
29	Depreciation of your home from line 41 below			29 1,846		
30	Carryover of prior year excess casualty losses and depreciation (see instructions)			30 0		
31	Add lines 28 through 30				31	1,846
32	Allowable excess casualty losses and depreciation. Enter the **smaller** of line 27 or line 31				32	1,846
33	Add lines 14, 26, and 32				33	6,546
34	Casualty loss portion, if any, from lines 14 and 32. Carry amount to **Form 4684** (see instructions)				34	0
35	**Allowable expenses for business use of your home.** Subtract line 34 from line 33. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions ►				35	6,546

Part III Depreciation of Your Home

36	Enter the **smaller** of your home's adjusted basis or its fair market value (see instr.)	36	400,000
37	Value of land included on line 36	37	40,000
38	Basis of building. Subtract line 37 from line 36	38	360,000
39	Business basis of building. Multiply line 38 by line 7	39	72,000
40	Depreciation percentage (see instructions)	40	2.5640 %
41	Depreciation allowable (see instructions). Multiply line 39 by line 40. Enter here and on line 29 above	41	1,846

Part IV Carryover of Unallowed Expenses to 2016

42	Operating expenses. Subtract line 26 from line 25. If less than zero, enter -0-	42	0
43	Excess casualty losses and depreciation. Subtract line 32 from line 31. If less than zero, enter -0-	43	0

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Form **4562**
Department of the Treasury
Internal Revenue Service (99)

Depreciation and Amortization
(Including Information on Listed Property)
▶ Attach to your tax return.
▶ Information about Form 4562 and its separate instructions is at *www.irs.gov/form4562.*

OMB No. 1545-0172
2015
Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
David R Johnson	SCH C 1	111-11-1112

Part I **Election To Expense Certain Property Under Section 179**
Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	500,000
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	2,000,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	0
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	500,000

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost
	File Cabinet	4,800	4,800

7	Listed property. Enter the amount from line 29	7	0
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	4,800
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	4,800
10	Carryover of disallowed deduction from line 13 of your 2014 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	500,000
12	Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12	4,800
13	Carryover of disallowed deduction to 2016. Add lines 9 and 10, less line 12 ▶	13	0

Note: Do not use Part II or Part III below for listed property. Instead, use Part V.

Part II **Special Depreciation Allowance and Other Depreciation (Do not** include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	0
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III **MACRS Depreciation (Do not** include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2015	17	
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2015 Tax Year Using the General Depreciation System

	(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a	3-year property						
b	5-year property						
c	7-year property		0	7.00	HY	200DB	0
d	10-year property						
e	15-year property						
f	20-year property						
g	25-year property			25 yrs.		S/L	
h	Residential rental property			27.5 yrs.	MM	S/L	
				27.5 yrs.	MM	S/L	
i	Nonresidential real property			39 yrs.	MM	S/L	
					MM	S/L	

Section C—Assets Placed in Service During 2015 Tax Year Using the Alternative Depreciation System

20a	Class life					S/L	
b	12-year			12 yrs.		S/L	
c	40-year			40 yrs.	MM	S/L	

Part IV **Summary** (See instructions.)

21	Listed property. Enter amount from line 28	21	4,590
22	**Total.** Add amounts from line 12, lines 14 through 17, line 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	9,390
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

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Form 4562 (2015) David R Johnson 111-11-1112 Page 2

Part V **Listed Property** (Include automobiles, certain other vehicles, certain aircraft, certain computers, and property used for entertainment, recreation, or amusement.)

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete **only** 24a, 24b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A—Depreciation and Other Information (Caution: See the instructions for limits for passenger automobiles.**)**

24a Do you have evidence to support the business/investment use claimed? [X] Yes [ ] No **24b** If "Yes," is the evidence written? [X] Yes [ ] No

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Special depreciation allowance for qualified listed property placed in service during the tax year and used more than 50% in a qualified business use (see instructions)						**25**	0	
26 Property used more than 50% in a qualified business use:								
Infiniti	02/04/14	90 %	41,000	36,900	5.00	200DB HY	4,590	
		%						
		%						
27 Property used 50% or less in a qualified business use:								
		%				S/L -		
		%				S/L -		
		%				S/L -		
28 Add amounts in column (h), lines 25 through 27. Enter here and on line 21, page 1						**28**	4,590	
29 Add amounts in column (i), line 26. Enter here and on line 7, page 1							**29**	0

Section B—Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle 1		(b) Vehicle 2		(c) Vehicle 3		(d) Vehicle 4		(e) Vehicle 5		(f) Vehicle 6	
30 Total business/investment miles driven during the year (**do not** include commuting miles)	13,050											
31 Total commuting miles driven during the year	1,450											
32 Total other personal (noncommuting) miles driven	0											
33 Total miles driven during the year. Add lines 30 through 32	14,500		0		0		0		0		0	
	Yes	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
34 Was the vehicle available for personal use during off-duty hours?	X											
35 Was the vehicle used primarily by a more than 5% owner or related person?	X											
36 Is another vehicle available for personal use?	X											

Section C—Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who **are not** more than 5% owners or related persons (see instructions).

	Yes	**No**
37 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		
38 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See the instructions for vehicles used by corporate officers, directors, or 1% or more owners		
39 Do you treat all use of vehicles by employees as personal use?		
40 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		
41 Do you meet the requirements concerning qualified automobile demonstration use? (See instructions)		

Note: If your answer to 37, 38, 39, 40, or 41 is "Yes," do not complete Section B for the covered vehicles.

Part VI **Amortization**

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 2015 tax year (see instructions):					
43 Amortization of costs that began before your 2015 tax year				**43**	
44 **Total.** Add amounts in column (f). See the instructions for where to report				**44**	0

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Form **4562**
Department of the Treasury
Internal Revenue Service (99)

Depreciation and Amortization
(Including Information on Listed Property)
▶ Attach to your tax return.
▶ Information about Form 4562 and its separate instructions is at *www.irs.gov/form4562.*

OMB No. 1545-0172
2015
Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
David R Johnson	Form 2106	111-11-1112

Part I **Election To Expense Certain Property Under Section 179**
Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	500,000
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	2,000,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	0
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	500,000

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost

7	Listed property. Enter the amount from line 29	7	960
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	960
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	960
10	Carryover of disallowed deduction from line 13 of your 2014 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	500,000
12	Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12	960
13	Carryover of disallowed deduction to 2016. Add lines 9 and 10, less line 12 ▶	13	0

Note: Do not use Part II or Part III below for listed property. Instead, use Part V.

Part II **Special Depreciation Allowance and Other Depreciation (Do not** include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III **MACRS Depreciation (Do not** include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2015	17	
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2015 Tax Year Using the General Depreciation System

	(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a	3-year property						
b	5-year property						
c	7-year property						
d	10-year property						
e	15-year property						
f	20-year property						
g	25-year property			25 yrs.		S/L	
h	Residential rental property			27.5 yrs.	MM	S/L	
				27.5 yrs.	MM	S/L	
i	Nonresidential real property			39 yrs.	MM	S/L	
					MM	S/L	

Section C—Assets Placed in Service During 2015 Tax Year Using the Alternative Depreciation System

20a	Class life					S/L	
b	12-year			12 yrs.		S/L	
c	40-year			40 yrs.	MM	S/L	

Part IV **Summary** (See instructions.)

21	Listed property. Enter amount from line 28	21	0
22	**Total.** Add amounts from line 12, lines 14 through 17, line 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	960
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

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Form 4562 (2015) David R Johnson 111-11-1112 Page **2**

Part V **Listed Property** (Include automobiles, certain other vehicles, certain aircraft, certain computers, and property used for entertainment, recreation, or amusement.)

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete **only** 24a, 24b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A—Depreciation and Other Information (Caution: See the instructions for limits for passenger automobiles.**)**

24a Do you have evidence to support the business/investment use claimed? [X] Yes [ ] No **24b** If "Yes," is the evidence written? [X] Yes [ ] No

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Special depreciation allowance for qualified listed property placed in service during the tax year and used more than 50% in a qualified business use (see instructions)					**25**		0	
26 Property used more than 50% in a qualified business use:								
Laptop	03/12/15	80 %	1,200	0	5.00	200DB HY	0	960
		%						
		%						
27 Property used 50% or less in a qualified business use:								
		%				S/L -		
		%				S/L -		
		%				S/L -		
28 Add amounts in column (h), lines 25 through 27. Enter here and on line 21, page 1					**28**		0	
29 Add amounts in column (i), line 26. Enter here and on line 7, page 1							**29**	960

Section B—Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle 1		(b) Vehicle 2		(c) Vehicle 3		(d) Vehicle 4		(e) Vehicle 5		(f) Vehicle 6	
30 Total business/investment miles driven during the year (**do not** include commuting miles) .												
31 Total commuting miles driven during the year												
32 Total other personal (noncommuting) miles driven												
33 Total miles driven during the year. Add lines 30 through 32	0		0		0		0		0		0	
	Yes	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
34 Was the vehicle available for personal use during off-duty hours?												
35 Was the vehicle used primarily by a more than 5% owner or related person?												
36 Is another vehicle available for personal use?												

Section C—Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who **are not** more than 5% owners or related persons (see instructions).

	Yes	**No**
37 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		
38 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See the instructions for vehicles used by corporate officers, directors, or 1% or more owners		
39 Do you treat all use of vehicles by employees as personal use?		
40 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		
41 Do you meet the requirements concerning qualified automobile demonstration use? (See instructions)		

Note: If your answer to 37, 38, 39, 40, or 41 is "Yes," do not complete Section B for the covered vehicles.

Part VI **Amortization**

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 2015 tax year (see instructions):					
43 Amortization of costs that began before your 2015 tax year				**43**	
44 **Total.** Add amounts in column (f). See the instructions for where to report				**44**	0

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PROBLEM 2 SOLUTIONS

1. As noted in the problem, Carrie uses the hybrid method of accounting for her business as required by Reg § 1.446–1(c)(2)(i). On Schedule C, line F, the Other box should be checked and "hybrid method" should be entered on the line that follows. Carrie's major business activities (i.e., hair styling, rental of workstations, sales of beauty supplies and hairpieces) are reported on a single Schedule C. Gross income reported on line 1 (Part I) is:

Services income earned from her own stations	$ 44,000
Rental of operating stations	68,000
Sale of beauty products and wigs ($48,000 + $69,000)	117,000
Total	$229,000

2. Sales of beauty products and wigs have already been reported on line 1. In the Cost of Goods Sold section of Schedule C (Part III), indicate that lower of cost or market is being used (check box b on line 33). Enter beginning inventory of $22,100 on line 35 ($11,400 + $10,700); purchases of $56,600 on line 36 ($26,100 + $30,500); and final inventory of $22,500 on line 41 ($9,900 + $12,600). The resulting cost of goods sold of $56,200 [($22,100 + $56,600) – $22,500] is reported on line 42 (Part III) and line 4 (Part I). Gross profit (line 5) and gross income (line 7) are $172,800 ($229,000 – $56,200).

   Expenses related to the business are reported on Schedule C as follows:

Line 25—Utilities $12,900 + Water $2,200	$15,100
Line 23—Property taxes ($1,800 + $4,200) + License $1,500	7,500
Line 22—Styling supplies	5,700
Line 15—Fire and casualty insurance $4,100 + Liability insurance $4,000	8,100
Line 17—Accounting services $3,800 + Legal fees $600 (see note 5)	4,400
Line 21—Sewage/garbage $2,300 + Janitorial services $2,400 + Repainting $8,000 (see note 4) + Repairs $1,900 (see note 4)	14,600
Line 27a—Waiting room supplies $1,300 + Business gifts $795 (see note 8) + Professional expenses $320 (see note 18)	2,415

3. The $10,400 spent on new waiting room furnishings is fully deductible by making a § 179 election to expense, which is done by completing Part I of Form 4562 (Depreciation and Amortization).

4. Depreciation of the shop building is also reported on line 17, Part III of Form 4562. The depreciation of $7,692 [$300,000 × 2.564% (see Exhibit 8.8)] carries forward onto line 13 of Schedule C (see Example 30 in Chapter 8 of the text).

   The repainting and repairs of $9,900 ($8,000 + $1,900) are reported on line 21 Repairs and maintenance on Schedule C (see note 2 above).

   Mortgage interest of $10,400 is deducted on line 16a of Schedule C. It is assumed that the prepayment penalty of $4,400 on the mortgage payoff is not for a specific service performed or cost incurred in connection with the mortgage. As such, the $4,400 is deductible along with the regular interest paid of $6,000.

5. The $500 fine is not deductible, but the legal expenses incurred in contesting the penalty are. They are combined with the accounting fees and deducted on line 17 of Schedule C (see note 2). (See Chapter 6 of the text.)

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6. Since the purpose of the Reading trip was to investigate the possible acquisition of the same type of business as Carrie's Coiffures, a deduction is available (see Chapter 6 of the text). These investigation expenses should be reported on Schedule C as follows:

   - Line 24a—$360 of Travel includes $140 (car rental) + $220 (motel)
   - Line 24b—$195 Deductible meals and entertainment is [50% × ($110 + $280)]

   Note that the meals and entertainment are subject to the 50% cutback adjustment (see Chapter 9 of the text). One final note—If H&R Block software is used to complete the tax return, it automatically enters an X on line 32a of Schedule C even though there is no loss reported this year. This can be overriden in the software if desired.

7. It is doubtful that Carrie loaned the $7,000 to Joan Myers for purposes of making a profit, nor was it intended as a gift. Thus, the noncollectibility of the loan should be classified as a nonbusiness bad debt. Under § 166(d)(1)(B), nonbusiness bad debts are classified as short-term capital losses. If you are not using a tax program, enter the $7,000 in parentheses in column (f) on line 1, Part I of Schedule D. If you are using *H&R Block* tax return software, the nonbusiness bad debt must be forced into the STCG section of Schedule D by leaving column (b) (Date acquired) blank. On Schedule D, Part I, line 1, enter the name of the debtor and "statement attached" in column (a). Then the attached statement should contain:

   - A description of the debt (the amount of the loan, the provision for interest, the date it became due, etc.);
   - The name of the debtor, listing any business or family relationship with the debtor;
   - A description of the efforts made to collect the debt; and
   - An explanation of why the debt is considered worthless (e.g., the borrower is in bankruptcy; legal action against the borrower would probably not result in payment, etc.)

   No deduction is allowed for the unpaid interest as Carrie has a zero basis in the unrealized receivable.

8. The gifts to Carrie's customers and her stylist colleagues are considered business gifts. The deduction for these gifts is capped at $25 per gift. However, incidental costs like gift wrapping and delivery charges are not subject to the $25 cap. As such, Carrie may deduct $525 for the customer gifts [35 customers × $15 ($12 wholesale cost + $3 gift wrapping)] and $270 for the gifts to the stylists [9 stylists × $30 ($25 limitation + $5 shipping)]. Enter $795 ($525 + $270) on line 27 of Schedule C and explain the entry on line 48 of page 2.

9. The additional $340 state tax assessment resulting from the audit is added to state tax payments made in 2015 (see note 18 below) and claimed as an itemized deduction *from* AGI on Schedule A.

10. Under § 104(a)(2), the $200,000 Carrie received for personal injury is excluded from her gross income. The direct payment of the medical expenses by the delivery company does not affect Carrie's tax situation as she was not involved in these transfers.

11. Under § 1014, Carrie's basis in the York County property is $140,000—its value on the day her father died. Consequently, she has a realized gain of $18,000 ($158,000 proceeds – $140,000 basis). Because the condemnation qualifies as an involuntary conversion, Carrie can avoid recognizing any gain if she reinvests in like-kind property within a certain period of time (see Chapter 13 of the text). As she has chosen not to make use of § 1033, she recognizes the $18,000 realized gain on the sale as a long-term capital gain per § 1223(9)(B) (property acquired from a decedent is deemed held for more than one year). Enter this sale on line 8, Part II of Schedule D.

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12. Under § 101(a)(1), the proceeds of life insurance are excluded from gross income. However, the interest of $1,500 is taxable. Report it on line 1, Part I of Schedule B.

13. The sale of Grosbeak stock results in a realized and recognized short-term capital loss of $12,000 ($28,000 selling price – $40,000 basis).

The results of Schedule D are summarized as follows:

STCL (bad debt), item 7	($ 7,000)
STCL (stock loss), item 13	(12,000)
LTCG (condemnation), item 11	18,000
Excess capital loss, lines 16 and 21, Part III of Schedule D and line 13, page 1 of Form 1040	($ 1,000)

14. The $1,000 reimbursement of Carrie's insurance deductible is a nontaxable return of capital. The tax benefit rule does not apply to generate income since the $1,000 was never deducted and, therefore, never generated a tax benefit.

15. The installation of the elevator is a deductible medical expense to the extent its cost exceeds the increase in the value of the residence. Thus, Carrie may deduct $7,000 ($12,000 cost – $5,000 increase in FMV of home) along with the $300 increase in utility bills to run the elevator under § 213. The appraisal fee of $400 is deductible under § 212 and will be subject to the 2%-of-AGI limitation. (See Chapter 10 of the text.)

16. No deduction is allowed for the contribution of services to a qualified charity. Thus, it does not matter what Carrie would charge for the time she spent. (See Chapter 10 of the text.)

17. The interest from the City of Lancaster bonds is nontaxable under § 103. However, the $490 must be listed on line 8b, page 1 of Form 1040. The interest from the money market account ($340) and the CD ($900) is listed in Part I of Schedule B, and along with the interest from the insurance company of $1,500 (see item 12), the $2,740 total is carried over to line 8a, page 1 of Form 1040.

The qualified dividends require special treatment, and the result is determined by completing a special worksheet (see item below). The total amount of $850 ($470 + $380), however, is entered on line 9b of page 1, Form 1040. The state income tax refund of $205 is taxable under the tax benefit rule (i.e., state income taxes were deducted in 2014). It is shown as income on line 10, page 1 of Form 1040. A refund of Federal income taxes has no effect on Federal taxable income.

18. Carrie's contribution to a pension plan is a deduction for AGI and should be reported on line 28 of Form 1040. Medical insurance premiums of a self-employed taxpayer are deductions *for* AGI and the $4,800 is claimed on line 29, page 1 of Form 1040.

The $1,914 of deductible medical expenses is the excess of the $8,700 ($7,300 from item 15 + $1,400 of dental bills) over $6,786 (10% × $67,861 AGI).

Deductible state and local income taxes of $3,540 include the additional assessment of $340 (see item 9) and the estimated tax payments for 2015 of $3,200 [$2,400 state + $800 local (see item 19)]. *Note:* It does not matter what year was involved with respect to the assessment of state tax; the year of payment controls the timing of the deduction since Carrie is a cash-basis taxpayer. The deductible income taxes of $3,540 are reported on line 5, and the deductible real estate taxes of $3,800 are reported on line 6 of Schedule A.

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Interest on home mortgage of $3,200 is claimed on line 10 of Schedule A.

The professional expenses (dues of $140 and journal subscriptions of $180) are deducted on Schedule C since Carrie is self-employed (see note 2 above).

The appraisal fee of $400 (see item 15) is reported on line 23 of Schedule A. However, no deduction will result because this expenditure does not exceed $1,357 (2% of $67,863 of AGI).

19. In determining taxable income, Carrie can claim a personal exemption for herself and a dependency exemption for her mother, for a total of $8,000 ($4,000 × 2).

20. A brief summary of Carrie's Federal income tax status for 2015 appears below.

Gross income:	
Schedule B	$ 3,590
State income tax refund	205
Schedule C	85,938
Schedule D	(1,000)
Deductions *for* AGI:	
Deductible self-employment tax	(6,072)
§ 401(k) retirement plan contribution	(10,000)
Medical insurance premiums	(4,800)
AGI	$67,861
Deductions *from* AGI	(12,454)
Personal and dependency exemptions	(8,000)
Taxable income	$47,407

Carrie's income tax liability is $6,329, calculated using the *Qualified Dividends and Capital Gain tax Worksheet – Line 44* since qualified dividends ($850) are taxed at a preferential rate. Carrie's total tax liability is $18,472, which is the sum of her $6,329 income tax and her self-employment tax of $12,143. Since she has prepaid $20,800, Carrie is entitled to a refund of $2,328.

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Form **1040** Department of the Treasury—Internal Revenue Service (99) **U.S. Individual Income Tax Return** **2015** OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2015, or other tax year beginning , 2015, ending , 20 See separate instructions.

Your first name and initial	Last name	Your social security number
Carrie A	Morgan	111-11-1112
If a joint return, spouse's first name and initial	Last name	Spouse's social security number

Home address (number and street). If you have a P.O. box, see instructions. Apt. no.
426 Grouse Avenue

▲ Make sure the SSN(s) above and on line 6c are correct.

City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions).
Allentown PA 18105

Foreign country name | Foreign province/state/county | Foreign postal code

Presidential Election Campaign
Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund ☐ You ☐ Spouse

Filing Status Check only one box.

1 ☐ Single
2 ☐ Married filing jointly (even if only one had income)
3 ☐ Married filing separately. Enter spouse's SSN above and full name here. ▶
4 ☒ Head of household (with qualifying person). (See instr.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 ☐ Qualifying widow(er) with dependent child

Exemptions

6a ☒ **Yourself.** If someone can claim you as a dependent, **do not** check box 6a
b ☐ **Spouse**

c **Dependents:** (1) First name / Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) ☒ if child under age 17 qualifying for child tax credit (see instructions)
Mildred Morgan	123-45-6789	Parent	

If more than four dependents, see instructions and check here ▶ ☐

Boxes checked on 6a and 6b: 1
No. of children on 6c who:
• lived with you:
• did not live with you due to divorce or separation (see instructions):
Dependents on 6c not entered above: 1
Add numbers on lines above ▶: 2

d Total number of exemptions claimed

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a W-2, see instructions.

7	Wages, salaries, tips, etc. Attach Form(s) W-2		7	0
8a	**Taxable** interest. Attach Schedule B if required		8a	2,740
b	**Tax-exempt** interest. **Do not** include on line 8a	8b 490		
9a	Ordinary dividends. Attach Schedule B if required		9a	850
b	Qualified dividends	9b 850		
10	Taxable refunds, credits, or offsets of state and local income taxes		10	205
11	Alimony received		11	
12	Business income or (loss). Attach Schedule C or C-EZ		12	85,938
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ ☐		13	-1,000
14	Other gains or (losses). Attach Form 4797		14	
15a	IRA distributions	15a b Taxable amount	15b	0
16a	Pensions and annuities	16a b Taxable amount	16b	0
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E		17	
18	Farm income or (loss). Attach Schedule F		18	0
19	Unemployment compensation		19	
20a	Social security benefits	20a b Taxable amount	20b	
21	Other income. List type and amount		21	0
22	Combine the amounts in the far right column for lines 7 through 21. This is your **total income** ▶		22	88,733

Adjusted Gross Income

23	Educator expenses	23		
24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24	0	
25	Health savings account deduction. Attach Form 8889	25	0	
26	Moving expenses. Attach Form 3903	26	0	
27	Deductible part of self-employment tax. Attach Schedule SE	27	6,072	
28	Self-employed SEP, SIMPLE, and qualified plans	28	10,000	
29	Self-employed health insurance deduction	29	4,800	
30	Penalty on early withdrawal of savings	30	0	
31a	Alimony paid b Recipient's SSN ▶	31a		
32	IRA deduction	32	0	
33	Student loan interest deduction	33		
34	Tuition and fees. Attach Form 8917	34		
35	Domestic production activities deduction. Attach Form 8903	35	0	
36	Add lines 23 through 35		36	20,872
37	Subtract line 36 from line 22. This is your **adjusted gross income** ▶		37	67,861

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Form 1040 (2015) Carrie A Morgan 111-11-1112 Page 2

Tax and Credits	38	Amount from line 37 (adjusted gross income)		38	67,861
	39a	Check if: ☐ **You** were born before January 2, 1951, ☐ Blind. ☐ **Spouse** was born before January 2, 1951, ☐ Blind. **Total boxes checked** ▶ 39a	0		
	b	If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ 39b ☐			
Standard Deduction for— • People who check any box on line 39a or 39b **or** who can be claimed as a dependent, see instructions. • All others: Single or Married filing separately, $6,300; Married filing jointly or Qualifying widow(er), $12,600; Head of household, $9,250	40	**Itemized deductions** (from Schedule A) **or** your **standard deduction** (see left margin)		40	12,454
	41	Subtract line 40 from line 38		41	55,407
	42	**Exemptions.** If line 38 is $154,950 or less, multiply $4,000 by the number on line 6d. Otherwise, see instructions		42	8,000
	43	**Taxable income.** Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-		43	47,407
	44	**Tax** (see instructions). Check if any from: a ☐ Form(s) 8814 b ☐ Form 4972 c ☐		44	6,329
	45	**Alternative minimum tax** (see instructions). Attach Form 6251 ▶		45	0
	46	Excess advance premium tax credit repayment. Attach Form 8962		46	
	47	Add lines 44, 45, and 46		47	6,329
	48	Foreign tax credit. Attach Form 1116 if required	0		
	49	Credit for child and dependent care expenses. Attach Form 2441			
	50	Education credits from Form 8863, line 19			
	51	Retirement savings contributions credit. Attach Form 8880	0		
	52	Child tax credit. Attach Schedule 8812, if required			
	53	Residential energy credits. Attach Form 5695			
	54	Other credits from Form: a ☐ 3800 b ☐ 8801 c ☐	0		
	55	Add lines 48 through 54. These are your **total credits**		55	0
	56	Subtract line 55 from line 47. If line 55 is more than line 47, enter -0- ▶		56	6,329
Other Taxes	57	Self-employment tax. Attach Schedule SE		57	12,143
	58	Unreported social security and Medicare tax from Form: a ☐ 4137 b ☐ 8919		58	0
	59	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required		59	0
	60a	Household employment taxes from Schedule H		60a	0
	b	First-time homebuyer credit repayment. Attach Form 5405 if required		60b	0
	61	Health care: individual responsibility (see instructions) Full-year coverage ☒		61	0
	62	Taxes from: a ☐ Form 8959 b ☐ Form 8960 c ☐ Instructions; enter code(s)		62	0
	63	Add lines 56 through 62. This is your **total tax** ▶		63	18,472
Payments	64	Federal income tax withheld from Forms W-2 and 1099	0		
	65	2015 estimated tax payments and amount applied from 2014 return	20,800		
If you have a qualifying child, attach Schedule EIC.	66a	**Earned income credit (EIC)**			
	b	Nontaxable combat pay election 66b			
	67	Additional child tax credit. Attach Schedule 8812			
	68	American opportunity credit from Form 8863, line 8			
	69	Net premium tax credit. Attach Form 8962			
	70	Amount paid with request for extension to file			
	71	Excess social security and tier 1 RRTA tax withheld	0		
	72	Credit for federal tax on fuels. Attach Form 4136			
	73	Credits from Form: a ☐ 2439 b ☐ Reserved c ☐ 8885 d ☐	0		
	74	Add lines 64, 65, 66a, and 67 through 73. These are your **total payments** ▶		74	20,800
Refund	75	If line 74 is more than line 63, subtract line 63 from line 74. This is the amount you **overpaid**		75	2,328
	76a	Amount of line 75 you want **refunded to you.** If Form 8888 is attached, check here ▶ ☐		76a	2,328
Direct deposit? See instructions.	b	Routing number XXXXXXXXX ▶ c Type: ☐ Checking ☐ Savings			
	d	Account number XXXXXXXXXXXXXXXXX			
	77	Amount of line 75 you want **applied to your 2016 estimated tax** ▶	0		
Amount You Owe	78	**Amount you owe.** Subtract line 74 from line 63. For details on how to pay, see instructions ▶		78	
	79	Estimated tax penalty (see instructions)	0		

Third Party Designee Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ **Yes.** Complete below ☒ **No**
Designee's name ▶ Phone no. ▶ Personal identification number (PIN) ▶

Sign Here Joint return? See instructions. Keep a copy for your records.
Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number
		Hairstylist	312-555-0100
Spouse's signature. If a joint return, **both** must sign.	Date	Spouse's occupation	If the IRS sent you an Identity Protection PIN, enter it here (see inst.)

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

KIA www.irs.gov/form1040 Form **1040** (2015)

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SCHEDULE A (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Itemized Deductions

▶ Information about Schedule A and its separate instructions is at *www.irs.gov/schedulea.*

▶ Attach to Form 1040.

OMB No. 1545-0074

2015

Attachment Sequence No. **07**

Name(s) shown on Form 1040: Carrie A Morgan

Your social security number: 111-11-1112

Medical and Dental Expenses		**Caution.** Do not include expenses reimbursed or paid by others.			
	1	Medical and dental expenses (see instructions)	1	8,700	
	2	Enter amount from Form 1040, line 38 . . . 2 67,861			
	3	Multiply line 2 by 10% (.10). But if either you or your spouse was born before January 2, 1951, multiply line 2 by 7.5% (.075) instead	3	6,786	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-			4 1,914
Taxes You Paid	5	State and local **(check only one box):** a. [X] Income taxes, or b. [ ] General sales taxes	5	3,540	
	6	Real estate taxes (see instructions)	6	3,800	
	7	Personal property taxes	7	0	
	8	Other taxes. List type and amount ▶	8	0	
	9	Add lines 5 through 8			9 7,340
Interest You Paid	10	Home mortgage interest and points reported to you on Form 1098	10	3,200	
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11	0	
Note. Your mortgage interest deduction may be limited (see instructions).	12	Points not reported to you on Form 1098. See instructions for special rules	12	0	
	13	Mortgage insurance premiums (see instructions)	13	0	
	14	Investment interest. Attach Form 4952 if required. (See instructions.)	14		
	15	Add lines 10 through 14			15 3,200
Gifts to Charity If you made a gift and got a benefit for it, see instructions.	16	Gifts by cash or check. If you made any gift of $250 or more, see instructions	16		
	17	Other than by cash or check. If any gift of $250 or more, see instructions. You **must** attach Form 8283 if over $500	17		
	18	Carryover from prior year	18		
	19	Add lines 16 through 18			19
Casualty and Theft Losses	20	Casualty or theft loss(es). Attach Form 4684. (See instructions.)			20 0
Job Expenses and Certain Miscellaneous Deductions	21	Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. (See instructions.) ▶	21	0	
	22	Tax preparation fees	22		
	23	Other expenses—investment, safe deposit box, etc. List type and amount ▶ OTHER	23	400	
	24	Add lines 21 through 23	24	400	
	25	Enter amount from Form 1040, line 38 . . . 25 67,861			
	26	Multiply line 25 by 2% (.02)	26	1,357	
	27	Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-			27 0
Other Miscellaneous Deductions	28	Other—from list in instructions. List type and amount ▶			28 0
Total Itemized Deductions	29	Is Form 1040, line 38, over $154,950? [X] **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40. [ ] **Yes.** Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.			29 12,454
	30	If you elect to itemize deductions even though they are less than your standard deduction, check here ▶ [ ]			

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SCHEDULE B (Form 1040A or 1040)

Department of the Treasury Internal Revenue Service (99)

Interest and Ordinary Dividends

▶ Attach to Form 1040A or 1040.

▶ Information about Schedule B and its instructions is a *www.irs.gov/scheduleb*.

OMB No. 1545-0074

2015

Attachment Sequence No. 08

Name(s) shown on return: Carrie A Morgan

Your social security number: 111-11-1112

Part I Interest

(See instructions for Schedule B, and the instructions for Form 1040A, or Form 1040, line 8a.)

Note: If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

			Amount
1	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see instructions and list this interest first. Also, show that buyer's social security number and address ▶		
	Falcon Life Insurance		1,500
	Allentown State Bank		340
	Scranton First National Bank		900
	City of Lancaster Bonds		0
		1	
2	Add the amounts on line 1	2	2,740
3	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815	3	
4	Subtract line 3 from line 2. Enter the result here and on Form 1040A, or Form 1040, line 8a ▶	4	2,740

Note: If line 4 is over $1,500, you must complete Part III.

Part II Ordinary Dividends

(See instructions for Schedule B, and the instructions for Form 1040A, or Form 1040, line 9a.)

Note: If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

			Amount
5	List name of payer ▶		
	General Electric		470
	AT&T Common		380
		5	
6	Add the amounts on line 5. Enter the total here and on Form 1040A, or Form 1040, line 9a ▶	6	850

Note. If line 6 is over $1,500, you must complete Part III.

Part III Foreign Accounts and Trusts

(See instructions.)

You must complete this part if you **(a)** had over $1,500 of taxable interest or ordinary dividends; **(b)** had a foreign account; or **(c)** received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

		Yes	No
7a	At any time during 2015, did you have a financial interest in or signature authority over a financial account (such as a bank account, securities account, or brokerage account) located in a foreign country? See instructions.		X
	If "Yes," are you required to file FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority? See FinCEN Form 114 and its instructions for filing requirements and exceptions to those requirements		
b	If you are required to file FinCEN Form 114, enter the name of the foreign country where the financial account is located ▶		
8	During 2015, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See instructions.		X

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SCHEDULE C (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Profit or Loss From Business

(Sole Proprietorship)

▶ Information about Schedule C and its separate instructions is at *www.irs.gov/schedulec.*

▶ Attach to Form 1040, 1040NR, or 1041; partnerships generally must file Form 1065.

OMB No. 1545-0074

2015

Attachment Sequence No. 09

Name of proprietor: Carrie A Morgan	Social security number (SSN): 111-11-1112
A Principal business or profession, including product or service (see instructions): Beauty Salon, Personal Services	B Enter code from instructions ▶ 812112
C Business name. If no separate business name, leave blank.: Carrie's Coiffures	D Employer ID number (EIN), (see instr.)
E Business address (including suite or room no.) ▶ 480 Laurel Street City, town or post office, state, and ZIP code: Allentown PA 18105	
F Accounting method: (1) ☐ Cash (2) ☐ Accrual (3) ☒ Other (specify) ▶ Hybrid Method	
G Did you "materially participate" in the operation of this business during 2015? If "No," see instructions for limit on losses	☒ Yes ☐ No
H If you started or acquired this business during 2015, check here ▶	☐
I Did you make any payments in 2015 that would require you to file Form(s) 1099? (see instructions)	☐ Yes ☒ No
J If "Yes," did you or will you file required Forms 1099?	☐ Yes ☐ No

Part I Income

1	Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on form W-2 and the "Statutory employee" box on that form was checked. ▶ ☐	1	229,000
2	Returns and allowances	2	
3	Subtract line 2 from line 1	3	229,000
4	Cost of goods sold (from line 42)	4	56,200
5	**Gross profit.** Subtract line 4 from line 3	5	172,800
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	
7	**Gross income.** Add lines 5 and 6 ▶	7	172,800

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8		18	Office expense (see instructions)	18	
9	Car and truck expenses (see instructions)	9	0	19	Pension and profit-sharing plans	19	
10	Commissions and fees	10		20	Rent or lease (see instructions):		
11	Contract labor (see instructions)	11		a	Vehicles, machinery, and equipment	20a	0
12	Depletion	12		b	Other business property	20b	
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13	18,092	21	Repairs and maintenance	21	14,600
14	Employee benefit programs (other than on line 19)	14		22	Supplies (not included in Part III)	22	5,700
15	Insurance (other than health)	15	8,100	23	Taxes and licenses	23	7,500
16	Interest:			24	Travel, meals, and entertainment:		
a	Mortgage (paid to banks, etc.)	16a	10,400	a	Travel	24a	360
b	Other	16b		b	Deductible meals and entertainment (see instructions)	24b	195
17	Legal and professional services	17	4,400	25	Utilities	25	15,100
				26	Wages (less employment credits)	26	
				27a	Other expenses (from line 48)	27a	2,415
				b	**Reserved for future use**	27b	

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27a ▶	28	86,862
29	Tentative profit or (loss). Subtract line 28 from line 7	29	85,938
30	Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method (see instructions). **Simplified method filers only:** enter the total square footage of: (a) your home: _____ and (b) the part of your home used for business: _____. Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30	30	0
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on both **Form 1040, line 12** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see instructions). Estates and trusts, enter on **Form 1041, line 3.** • If a loss, you **must** go to line 32.	31	85,938
32	If you have a loss, check the box that describes your investment in this activity (see instructions). • If you checked 32a, enter the loss on both **Form 1040, line 12**, (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see the line 31 instructions). Estates and trusts, enter on **Form 1041, line 3.** • If you checked 32b, you **must** attach **Form 6198.** Your loss may be limited.	32a ☐ All investment is at risk. 32b ☐ Some investment is not at risk.	

KIA **For Paperwork Reduction Act Notice, see the separate instructions.** **Schedule C (Form 1040) 2015**

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Schedule C (Form 1040) 2015 Carrie A Morgan 111-11-1112 Page 2

Part III Cost of Goods Sold (see instructions)

33 Method(s) used to value closing inventory: a ☐ Cost b ☒ Lower of cost or market c ☐ Other (attach explanation)

34 Was there any change in determining quantities, costs, or valuations between opening and closing inventory? If "Yes," attach explanation . . . ☐ Yes ☒ No

35	Inventory at beginning of year. If different from last year's closing inventory, attach explanation	35	22,100
36	Purchases less cost of items withdrawn for personal use	36	56,600
37	Cost of labor. Do not include any amounts paid to yourself	37	
38	Materials and supplies	38	
39	Other costs	39	
40	Add lines 35 through 39	40	78,700
41	Inventory at end of year	41	22,500
42	**Cost of goods sold.** Subtract line 41 from line 40. Enter the result here and on line 4	42	56,200

Part IV Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 9 and are not required to file Form 4562 for this business. See the instructions for line 13 to find out if you must file Form 4562.

43 When did you place your vehicle in service for business purposes? (month, day, year) ▶ _____

44 Of the total number of miles you drove your vehicle during 2015, enter the number of miles you used your vehicle for:

a Business _____ b Commuting (see instructions) _____ c Other _____

45	Was your vehicle available for personal use during off-duty hours?	☐ Yes	☐ No
46	Do you (or your spouse) have another vehicle available for personal use?	☐ Yes	☐ No
47a	Do you have evidence to support your deduction?	☐ Yes	☐ No
b	If "Yes," is the evidence written?	☐ Yes	☐ No

Part V Other Expenses. List below business expenses not included on lines 8–26 or line 30.

Waiting Room Supplies	1,300
Business Gifts	795
Professional Dues	140
Journal Subscriptions	180

48 **Total other expenses.** Enter here and on line 27a . . . 48 2,415

KIA Schedule C (Form 1040) 2015

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SCHEDULE D (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Capital Gains and Losses

► Attach to Form 1040 or Form 1040NR.

► Information about Schedule D and its separate instructions is at *www.irs.gov/scheduled.*

► Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.

OMB No. 1545-0074

2015

Attachment Sequence No. **12**

Name(s) shown on return: Carrie A Morgan

Your social security number: 111-11-1112

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 1b	0	0		0
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked	28,000	40,000	0	-12,000
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked	0	0	0	0
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked	0	7,000	0	-7,000

4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824	**4**	0
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	**5**	
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your **Capital Loss Carryover Worksheet** in the instructions.	**6**	(0)
7 **Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the next page	**7**	-19,000

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b	0	0		0
8b Totals for all transactions reported on Form(s) 8949 with **Box D** checked	0	0	0	0
9 Totals for all transactions reported on Form(s) 8949 with **Box E** checked	158,000	140,000	0	18,000
10 Totals for all transactions reported on Form(s) 8949 with **Box F** checked	0	0	0	0

11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824	**11**	0
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	**12**	
13 Capital gain distributions. See the instructions	**13**	0
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your **Capital Loss Carryover Worksheet** in the instructions	**14**	(0)
15 **Net long-term capital gain or (loss).** Combine lines 8a through 14 in column (h). Then go to Part III on page 2	**15**	18,000

KIA **For Paperwork Reduction Act Notice, see your tax return instructions.** **Schedule D (Form 1040) 2015**

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Schedule D (Form 1040) 2015 Carrie A Morgan 111-11-1112 Page 2

Part III Summary

16	Combine lines 7 and 15 and enter the result • If line 16 is a **gain**, enter the amount from line 16 on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 17 below. • If line 16 is a **loss**, skip lines 17 through 20 below. Then go to line 21. Also be sure to complete line 22. • If line 16 is **zero**, skip lines 17 through 21 below and enter -0- on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 22.	16	-1,000
17	Are lines 15 and 16 **both** gains? ☐ **Yes.** Go to line 18. ☐ **No.** Skip lines 18 through 21, and go to line 22.		
18	Enter the amount, if any, from line 7 of the **28% Rate Gain Worksheet** in the instructions ▶	18	
19	Enter the amount, if any, from line 18 of the **Unrecaptured Section 1250 Gain Worksheet** in the instructions ▶	19	
20	Are lines 18 and 19 **both** zero or blank? ☐ **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). **Do not** complete lines 21 and 22 below. ☐ **No.** Complete the **Schedule D Tax Worksheet** in the instructions. **Do not** complete lines 21 and 22 below.		
21	If line 16 is a loss, enter here and on Form 1040, line 13, or Form 1040NR, line 14, the **smaller** of: • The loss on line 16 or • ($3,000), or if married filing separately, ($1,500) **Note.** When figuring which amount is smaller, treat both amounts as positive numbers.	21	(1,000)
22	Do you have qualified dividends on Form 1040, line 9b, or Form 1040NR, line 10b? ☒ **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). ☐ **No.** Complete the rest of Form 1040 and Form 1040NR.		

KIA Schedule D (Form 1040) 2015

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Form **8949**

Department of the Treasury
Internal Revenue Service

Sales and Other Dispositions of Capital Assets

► **Information about Form 8949 and its separate instructions is at *www.irs.gov/form8949***

► **File with your Schedule D to list your transactions for lines 1b, 2, 3, 8b, 9, and 10 of Schedule D.**

OMB No. 1545-0074

2015

Attachment Sequence No. **12A**

Name(s) shown on return	Social security number or taxpayer identification number
Carrie A Morgan	111-11-1112

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I **Short-Term.** Transactions involving capital assets you held 1 year or less are short-term. For long-term transactions, see page 2.

Note. You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box A, B, *or* C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- [X] **(A)** Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- [ ] **(B)** Short-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- [ ] **(C)** Short-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions. (f) Code(s) from instructions	(g) Amount of adjustment	(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
1000 Grosbeak Exploration	03/04/15	12/23/15	28,000	40,000		0	-12,000
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
2 **Totals.** Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 1b** (if **Box A** above is checked), **line 2** (if **Box B** above is checked), or **line 3** (if **Box C** above is checked) ►			28,000	40,000		0	-12,000

Note. If you checked Box A above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

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Form 8949 (2015) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Name and SSN or taxpayer identification no. not required if shown on Page 1	**Social security number or taxpayer identification number**
Carrie A Morgan	111-11-1112

Before you check Box D, E, or F below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part II **Long-Term.** Transactions involving capital assets you held more than 1 year are long term. For short-term transactions, see page 1.

Note. You may aggregate all long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 8a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box D, E, *or* F below. Check only one box. If more than one box applies for your long-term transactions, complete a separate Form 8949, page 2, for each applicable box. If you have more long-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

☐ **(D)** Long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)

☒ **(E)** Long-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS

☐ **(F)** Long-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions. (f) Code(s) from instructions	(g) Amount of adjustment	(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
York County Land	inherit	07/25/15	158,000	140,000		0	18,000
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
2 **Totals.** Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 8b** (if **Box D** above is checked), **line 9** (if **Box E** above is checked), or **line 10** (if **Box F** above is checked) ▶			158,000	140,000		0	18,000

Note. If you checked Box D above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

KIA Form **8949** (2015)

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Form **8949**

Department of the Treasury
Internal Revenue Service

Sales and Other Dispositions of Capital Assets

► **Information about Form 8949 and its separate instructions is at *www.irs.gov/form8949***

► **File with your Schedule D to list your transactions for lines 1b, 2, 3, 8b, 9, and 10 of Schedule D.**

OMB No. 1545-0074

2015

Attachment Sequence No. **12A**

Name(s) shown on return	Social security number or taxpayer identification number
Carrie A Morgan	111-11-1112

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I **Short-Term.** Transactions involving capital assets you held 1 year or less are short-term. For long-term transactions, see page 2.

Note. You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box A, B, *or* C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- ☐ **(A)** Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- ☐ **(B)** Short-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- ☒ **(C)** Short-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions. (f) Code(s) from instructions	(g) Amount of adjustment	(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
Loan to friend		12/31/15	0	7,000		0	-7,000
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
2 **Totals.** Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 1b** (if **Box A** above is checked), **line 2** (if **Box B** above is checked), or **line 3** (if **Box C** above is checked) ►			0	7,000		0	-7,000

Note. If you checked Box A above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

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SCHEDULE SE (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Self-Employment Tax

► Information about Schedule SE and its separate instructions is at *www.irs.gov/schedulese.*
► Attach to Form 1040 or Form 1040NR.

OMB No. 1545-0074

2015

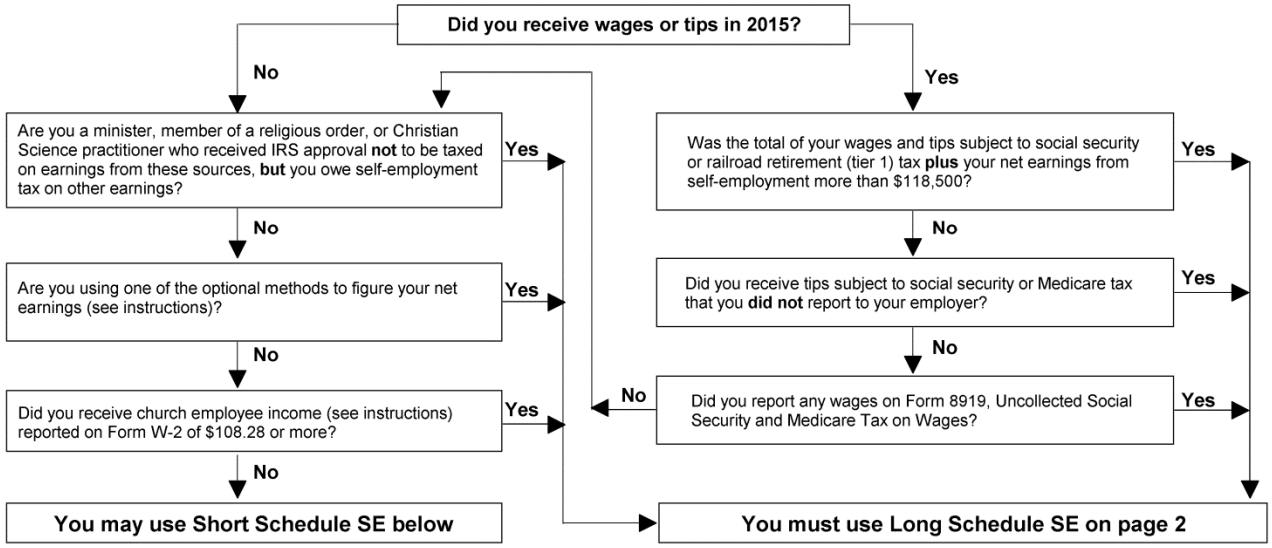
Attachment Sequence No. **17**

Name of person with **self-employment** income (as shown on Form 1040 or Form 1040NR)	Social security number of person with **self-employment** income ►
Carrie A Morgan	111-11-1112

Before you begin: To determine if you must file Schedule SE, see the instructions.

May I Use Short Schedule SE or Must I Use Long Schedule SE?

Note. Use this flowchart **only if** you must file Schedule SE. If unsure, see *Who Must File Schedule SE* in the instructions.



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

1a	Net farm profit or (loss) from Schedule F, line 34, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A.	**1a**	0
b	If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4b, or listed on Schedule K-1 (Form 1065), box 20, code Z	**1b**	(0)
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Ministers and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report	**2**	85,938
3	Combine lines 1a, 1b, and 2.	**3**	85,938
4	Multiply line 3 by 92.35% (.9235). If less than $400, you do not owe self-employment tax; **do not** file this schedule unless you have an amount on line 1b ►	**4**	79,364
	Note. If line 4 is less than $400 due to Conservation Reserve Program payments on line 1b, see instructions.		
5	**Self-employment tax.** If the amount on line 4 is: • $118,500 or less, multiply line 4 by 15.3% (.153). Enter the result here and on **Form 1040, line 57,** or **Form 1040NR, line 55.** • More than $118,500, multiply line 4 by 2.9% (.029). Then, add $14,694 to the result. Enter the total here and on **Form 1040, line 57,** or **Form 1040NR, line 55.**	**5**	12,143
6	**Deduction for one-half of self-employment tax.** Multiply line 5 by 50% (.50). Enter the result here and on **Form 1040, line 27,** or **Form 1040NR, line 27**	**6**	6,072

KIA **For Paperwork Reduction Act Notice, see your tax return instructions.** **Schedule SE (Form 1040) 2015**

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Form **4562**
Department of the Treasury
Internal Revenue Service (99)

Depreciation and Amortization
(Including Information on Listed Property)
▶ Attach to your tax return.
▶ Information about Form 4562 and its separate instructions is at *www.irs.gov/form4562.*

OMB No. 1545-0172
2015
Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
Carrie A Morgan	SCH C 1	111-11-1112

Part I **Election To Expense Certain Property Under Section 179**
Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	500,000
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	2,000,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	0
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	500,000

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost
	Furniture	10,400	10,400

7	Listed property. Enter the amount from line 29	7	0
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	10,400
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	10,400
10	Carryover of disallowed deduction from line 13 of your 2014 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	500,000
12	Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12	10,400
13	Carryover of disallowed deduction to 2016. Add lines 9 and 10, less line 12 ▶	13	0

Note: Do not use Part II or Part III below for listed property. Instead, use Part V.

Part II **Special Depreciation Allowance and Other Depreciation (Do not** include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	0
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III **MACRS Depreciation (Do not** include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2015	17	7,692
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2015 Tax Year Using the General Depreciation System

	(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a	3-year property						
b	5-year property						
c	7-year property		0	7.00	HY	200DB	0
d	10-year property						
e	15-year property						
f	20-year property						
g	25-year property			25 yrs.		S/L	
h	Residential rental property			27.5 yrs.	MM	S/L	
				27.5 yrs.	MM	S/L	
i	Nonresidential real property			39 yrs.	MM	S/L	
					MM	S/L	

Section C—Assets Placed in Service During 2015 Tax Year Using the Alternative Depreciation System

20a	Class life					S/L	
b	12-year			12 yrs.		S/L	
c	40-year			40 yrs.	MM	S/L	

Part IV **Summary** (See instructions.)

21	Listed property. Enter amount from line 28	21	0
22	**Total.** Add amounts from line 12, lines 14 through 17, line 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	18,092
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

KIA **For Paperwork Reduction Act Notice, see separate instructions.** Form **4562** (2015)

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PROBLEM 3 SOLUTIONS

Form **1120**
Department of the Treasury
Internal Revenue Service

U.S. Corporation Income Tax Return

For calendar year 2015 or tax year beginning _____, ending _____
▶ Information about Form 1120 and its separate instructions is at *www.irs.gov/form1120*.

OMB No. 1545-0123
2015

A Check if:
1a Consolidated return (attach Form 851) ☐
b Life/nonlife consolidated return ☐
2 Personal holding co. (attach Sch. PH) ☐
3 Personal service corp. (see instructions) ☐
4 Schedule M-3 attached ☒

TYPE OR PRINT

Name: Pet Kingdom, Inc.
Number, street, and room or suite no. If a P.O. box, see instructions.: 1010 Northwest Parkway
City or town: Dallas | State: TX | ZIP code: 75225
Foreign country name | Foreign province/state/county | Foreign postal code

B Employer identification number: 11-1111111
C Date incorporated: 11/1/2006
D Total assets (see instructions): $ 13,802,727

E Check if: (1) ☐ Initial return (2) ☐ Final return (3) ☐ Name change (4) ☐ Address change

Income	1a	Gross receipts or sales	1a	5,750,000	
	b	Returns and allowance	1b	200,000	
	c	Balance. Subtract line 1b from line 1a			1c 5,550,000
	2	Cost of goods sold (attach Form 1125-A)			2 2,300,000
	3	Gross profit. Subtract line 2 from line 1c			3 3,250,000
	4	Dividends (Schedule C, line 19)			4 43,750
	5	Interest			5 20,000
	6	Gross rents			6
	7	Gross royalties			7
	8	Capital gain net income (attach Schedule D (Form 1120))			8
	9	Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797)			9
	10	Other income (see instructions—attach statement)			10
	11	**Total income.** Add lines 3 through 10 ▶			11 3,313,750
Deductions (See instructions for limitations on deductions.)	12	Compensation of officers (see instructions—attach Form 1125-E) ▶			12 525,000
	13	Salaries and wages (less employment credits)			13 725,000
	14	Repairs and maintenance			14 140,000
	15	Bad debts			15
	16	Rents			16 109,000
	17	Taxes and licenses			17 238,000
	18	Interest			18 207,000
	19	Charitable contributions			19 38,000
	20	Depreciation from Form 4562 not claimed on Form 1125-A or elsewhere on return (attach Form 4562)			20 136,000
	21	Depletion			21
	22	Advertising			22 58,000
	23	Pension, profit-sharing, etc., plans			23
	24	Employee benefit programs			24 60,000
	25	Domestic production activities deduction (attach Form 8903)			25
	26	Other deductions (attach statement)			26
	27	**Total deductions.** Add lines 12 through 26 ▶			27 2,236,000
	28	Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11			28 1,077,750
	29a	Net operating loss deduction (see instructions)	29a		
	b	Special deductions (Schedule C, line 20)	29b	30,625	
	c	Add lines 29a and 29b			29c 30,625
Tax, Refundable Credits, and Payments	30	**Taxable income.** Subtract line 29c from line 28 (see instructions)			30 1,047,125
	31	Total tax (Schedule J, Part I, line 11)			31 356,023
	32	Total payments and refundable credits (Schedule J, Part II, line 21)			32 360,000
	33	Estimated tax penalty (see instructions). Check if Form 2220 is attached ▶ ☐			33
	34	**Amount owed.** If line 32 is smaller than the total of lines 31 and 33, enter amount owed			34 0
	35	**Overpayment.** If line 32 is larger than the total of lines 31 and 33, enter amount overpaid			35 3,977
	36	Enter amount from line 35 you want: **Credited to 2016 estimated tax** ▶ **Refunded** ▶			36 3,977

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of officer | Date | Title

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
	SELF-PREPARED RETURN			

Firm's name ▶ | Firm's EIN ▶
Firm's address ▶ | Phone no.
City | State | ZIP code

For Paperwork Reduction Act Notice, see separate instructions. Form **1120** (2015)
HTA

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Form 1120 (2015) Pet Kingdom, Inc. 11-1111111 Page **2**

Schedule C **Dividends and Special Deductions** (see instructions)

		(a) Dividends received	(b) %	(c) Special deductions (a) × (b)
1	Dividends from less-than-20%-owned domestic corporations (other than debt-financed stock)	43,750	70	30,625
2	Dividends from 20%-or-more-owned domestic corporations (other than debt-financed stock)		80	0
3	Dividends on debt-financed stock of domestic and foreign corporations		see instructions	0
4	Dividends on certain preferred stock of less-than-20%-owned public utilities		42	0
5	Dividends on certain preferred stock of 20%-or-more-owned public utilities		48	0
6	Dividends from less-than-20%-owned foreign corporations and certain FSCs		70	0
7	Dividends from 20%-or-more-owned foreign corporations and certain FSCs		80	0
8	Dividends from wholly owned foreign subsidiaries		100	0
9	**Total.** Add lines 1 through 8. See instructions for limitation			30,625
10	Dividends from domestic corporations received by a small business investment company operating under the Small Business Investment Act of 1958		100	0
11	Dividends from affiliated group members		100	0
12	Dividends from certain FSCs		100	0
13	Dividends from foreign corporations not included on lines 3, 6, 7, 8, 11, or 12			
14	Income from controlled foreign corporations under subpart F (attach Form(s) 5471)			
15	Foreign dividend gross-up			
16	IC-DISC and former DISC dividends not included on lines 1, 2, or 3			
17	Other dividends			
18	Deduction for dividends paid on certain preferred stock of public utilities			
19	**Total dividends.** Add lines 1 through 17. Enter here and on page 1, line 4 ▶	43,750		
20	**Total special deductions.** Add lines 9, 10, 11, 12, and 18. Enter here and on page 1, line 29b ▶			30,625

Form **1120** (2015)

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Form 1120 (2015) Pet Kingdom, Inc. 11-1111111 Page 3

Schedule J Tax Computation and Payment (see instructions)

Part I–Tax Computation

1	Check if the corporation is a member of a controlled group (attach Schedule O (Form 1120)) ▶ ☐					
2	Income tax. Check if a qualified personal service corporation (see instructions) ▶ ☐			2	356,023	
3	Alternative minimum tax (attach Form 4626)			3		
4	Add lines 2 and 3			4	356,023	
5a	Foreign tax credit (attach Form 1118)	5a				
b	Credit from Form 8834 (see instructions)	5b				
c	General business credit (attach Form 3800)	5c				
d	Credit for prior year minimum tax (attach Form 8827)	5d				
e	Bond credits from Form 8912	5e				
6	**Total credits.** Add lines 5a through 5e			6	0	
7	Subtract line 6 from line 4			7	356,023	
8	Personal holding company tax (attach Schedule PH (Form 1120))			8		
9a	Recapture of investment credit (attach Form 4255)	9a				
b	Recapture of low-income housing credit (attach Form 8611)	9b				
c	Interest due under the look-back method—completed long-term contracts (attach Form 8697)	9c				
d	Interest due under the look-back method—income forecast method (attach Form 8866)	9d				
e	Alternative tax on qualifying shipping activities (attach Form 8902)	9e				
f	Other (see instructions—attach statement)	9f				
10	**Total.** Add lines 9a through 9f			10	0	
11	**Total tax.** Add lines 7, 8, and 10. Enter here and on page 1, line 31			11	356,023	

Part II–Payments and Refundable Credits

12	2014 overpayment credited to 2015			12		
13	2015 estimated tax payments			13	360,000	
14	2015 refund applied for on Form 4466			14	( )	
15	Combine lines 12, 13, and 14			15	360,000	
16	Tax deposited with Form 7004			16		
17	Withholding (see instructions)			17		
18	**Total payments.** Add lines 15, 16, and 17			18	360,000	
19	Refundable credits from:					
a	Form 2439	19a				
b	Form 4136	19b				
c	Form 8827, line 8c	19c				
d	Other (attach statement—see instructions)	19d				
20	**Total credits.** Add lines 19a through 19d			20	0	
21	**Total payments and credits.** Add lines 18 and 20. Enter here and on page 1, line 32			21	360,000	

Schedule K Other Information (see instructions)

		Yes	No
1	Check accounting method: a ☐ Cash b ☒ Accrual c ☐ Other (specify) ▶		
2	See the instructions and enter the:		
a	Business activity code no. ▶ 453910		
b	Business activity ▶ Retail Trade		
c	Product or service ▶ Pet and Pet Supplies Store		
3	Is the corporation a subsidiary in an affiliated group or a parent-subsidiary controlled group?		X
	If "Yes," enter name and EIN of the parent corporation ▶		
4	At the end of the tax year:		
a	Did any foreign or domestic corporation, partnership (including any entity treated as a partnership), trust, or tax-exempt organization own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote? If "Yes," complete Part I of Schedule G (Form 1120) (attach Schedule G)		X
b	Did any individual or estate own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote? If "Yes," complete Part II of Schedule G (Form 1120) (attach Schedule G)	X	

Form **1120** (2015)

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Form 1120 (2015) Pet Kingdom, Inc. 11-1111111 Page 4

Schedule K **Other Information** *continued* (see instructions)

		Yes	No
5	At the end of the tax year, did the corporation:		
a	Own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of stock entitled to vote of any foreign or domestic corporation not included on **Form 851,** Affiliations Schedule? For rules of constructive ownership, see instructions . . If "Yes," complete (i) through (iv) below.		X

(i) Name of Corporation	(ii) Employer Identification Number (if any)	(iii) Country of Incorporation	(iv) Percentage Owned in Voting Stock

b	Own directly an interest of 20% or more, or own, directly or indirectly, an interest of 50% or more in any foreign or domestic partnership (including an entity treated as a partnership) or in the beneficial interest of a trust? For rules of constructive ownership, see instructions . . If "Yes," complete (i) through (iv) below.		X

(i) Name of Entity	(ii) Employer Identification Number (if any)	(iii) Country of Organization	(iv) Maximum Percentage Owned in Profit, Loss, or Capital

6	During this tax year, did the corporation pay dividends (other than stock dividends and distributions in exchange for stock) in excess of the corporation's current and accumulated earnings and profits? (See sections 301 and 316.) . . . If "Yes," file **Form 5452,** Corporate Report of Nondividend Distributions. If this is a consolidated return, answer here for the parent corporation and on Form 851 for each subsidiary.		X
7	At any time during the tax year, did one foreign person own, directly or indirectly, at least 25% of **(a)** the total voting power of all classes of the corporation's stock entitled to vote or **(b)** the total value of all classes of the corporation's stock? . . . For rules of attribution, see section 318. If "Yes," enter: **(i)** Percentage owned ► _____ and **(ii)** Owner's country ► _____ **(c)** The corporation may have to file **Form 5472,** Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Enter the number of Forms 5472 attached ► _____		X
8	Check this box if the corporation issued publicly offered debt instruments with original issue discount . . . ► ☐ If checked, the corporation may have to file **Form 8281,** Information Return for Publicly Offered Original Issue Discount Instruments.		
9	Enter the amount of tax-exempt interest received or accrued during the tax year ► $ 15,000		
10	Enter the number of shareholders at the end of the tax year (if 100 or fewer) ► 2		
11	If the corporation has an NOL for the tax year and is electing to forego the carryback period, check here . . . ► ☐ If the corporation is filing a consolidated return, the statement required by Regulations section 1.1502-21(b)(3) must be attached or the election will not be valid.		
12	Enter the available NOL carryover from prior tax years (do not reduce it by any deduction on line 29a.) ► $		
13	Are the corporation's total receipts (page 1, line 1a, plus lines 4 through 10) for the tax year **and** its total assets at the end of the tax year less than $250,000? . . . If "Yes," the corporation is not required to complete Schedules L, M-1, and M-2. Instead, enter the total amount of cash distributions and the book value of property distributions (other than cash) made during the tax year. ► $		X
14	Is the corporation required to file Schedule UTP (Form 1120), Uncertain Tax Position Statement (see instructions)? . . . If "Yes," complete and attach Schedule UTP.		X
15a	Did the corporation make any payments in 2015 that would require it to file Form(s) 1099? . . .	X	
b	If "Yes," did or will the corporation file required Forms 1099? . . .	X	
16	During this tax year, did the corporation have an 80% or more change in ownership, including a change due to redemption of its own stock? . . .		X
17	During or subsequent to this tax year, but before the filing of this return, did the corporation dispose of more than 65% (by value) of its assets in a taxable, non-taxable, or tax deferred transaction? . . .		X
18	Did the corporation receive assets in a section 351 transfer in which any of the transferred assets had a fair market basis or fair market value of more than $1 million? . . .		X

Form **1120** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 1120 (2015) Pet Kingdom, Inc. 11-1111111 Page **5**

Schedule L Balance Sheets per Books

Assets	Beginning of tax year (a)	Beginning of tax year (b)	End of tax year (c)	End of tax year (d)
1 Cash		1,200,000		1,037,750
2a Trade notes and accounts receivable	2,062,500		2,147,000	
b Less allowance for bad debts	( )	2,062,500	( )	2,147,000
3 Inventories		2,750,000		3,030,000
4 U.S. government obligations				
5 Tax-exempt securities (see instructions)		375,000		375,000
6 Other current assets (attach statement)		400,000		403,977
7 Loans to shareholders				
8 Mortgage and real estate loans				
9 Other investments (attach statement)		1,125,000		1,125,000
10a Buildings and other depreciable assets	5,455,000		5,455,000	
b Less accumulated depreciation	(606,000)	4,849,000	(712,000)	4,743,000
11a Depletable assets				
b Less accumulated depletion	( )	0	( )	0
12 Land (net of any amortization)		812,500		812,500
13a Intangible assets (amortizable only)				
b Less accumulated amortization	( )	0	( )	0
14 Other assets (attach statement)		140,000		128,500
15 Total assets		13,714,000		13,802,727
Liabilities and Shareholders' Equity				
16 Accounts payable		2,284,000		1,975,000
17 Mortgages, notes, bonds payable in less than 1 year				
18 Other current liabilities (attach statement)		175,000		155,000
19 Loans from shareholders				
20 Mortgages, notes, bonds payable in 1 year or more		4,625,000		4,575,000
21 Other liabilities (attach statement)				
22 Capital stock: a Preferred stock				
b Common stock	2,500,000	2,500,000	2,500,000	2,500,000
23 Additional paid-in capital				
24 Retained earnings—Appropriated (attach statement)				
25 Retained earnings—Unappropriated		4,130,000		4,597,727
26 Adjustments to shareholders' equity (attach statement)				
27 Less cost of treasury stock		( )		( )
28 Total liabilities and shareholders' equity		13,714,000		13,802,727

Schedule M-1 Reconciliation of Income (Loss) per Books With Income per Return

Note: The corporation may be required to file Schedule M-3 (see instructions).

1 Net income (loss) per books		7 Income recorded on books this year not included on this return (itemize): Tax-exempt interest $	
2 Federal income tax per books			
3 Excess of capital losses over capital gains			
4 Income subject to tax not recorded on books this year (itemize):			0
	0	8 Deductions on this return not charged against book income this year (itemize):	
5 Expenses recorded on books this year not deducted on this return (itemize):		a Depreciation $	
a Depreciation $		b Charitable contributions $	
b Charitable contributions $			
c Travel and entertainment $			0
	0	9 Add lines 7 and 8	0
6 Add lines 1 through 5	0	10 Income (page 1, line 28)—line 6 less line 9	0

Schedule M-2 Analysis of Unappropriated Retained Earnings per Books (Line 25, Schedule L)

1 Balance at beginning of year	4,130,000	5 Distributions: a Cash	250,000
2 Net income (loss) per books	717,727	b Stock	
3 Other increases (itemize):		c Property	
		6 Other decreases (itemize):	
	0	7 Add lines 5 and 6	250,000
4 Add lines 1, 2, and 3	4,847,727	8 Balance at end of year (line 4 less line 7)	4,597,727

Form **1120** (2015)

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Form **1125-A**
(Rev. December 2012)
Department of the Treasury
Internal Revenue Service

Cost of Goods Sold

▶ **Attach to Form 1120, 1120-C, 1120-F, 1120S, 1065, or 1065-B.**
▶ **Information about Form 1125-A and its instructions is at *www.irs.gov/form1125a.***

OMB No. 1545-2225

Name	Employer identification number
Pet Kingdom, Inc.	11-1111111

1	Inventory at beginning of year	1	2,750,000	
2	Purchases	2	2,580,000	
3	Cost of labor	3		
4	Additional section 263A costs (attach schedule)	4		
5	Other costs (attach schedule)	5		
6	**Total.** Add lines 1 through 5	6	5,330,000	
7	Inventory at end of year	7	3,030,000	
8	**Cost of goods sold.** Subtract line 7 from line 6. Enter here and on Form 1120, page 1, line 2 or the appropriate line of your tax return (see instructions)	8	2,300,000	

9 a Check all methods used for valuing closing inventory:
- *(i)* ☐ Cost
- *(ii)* ☒ Lower of cost or market
- *(iii)* ☐ Other (Specify method used and attach explanation.) ▶

b Check if there was a writedown of subnormal goods ▶ ☐

c Check if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970) ▶ ☐

d If the LIFO inventory method was used for this tax year, enter amount of closing inventory computed under LIFO — 9d

e If property is produced or acquired for resale, do the rules of section 263A apply to the entity (see instructions)? ☐ Yes ☒ No

f Was there any change in determining quantities, cost, or valuations between opening and closing inventory? If "Yes," attach explanation ☐ Yes ☒ No

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SCHEDULE G (Form 1120)
(Rev. December 2011)
Department of the Treasury
Internal Revenue Service

Information on Certain Persons Owning the Corporation's Voting Stock

▶ Attach to Form 1120.
▶ See instructions on page 2.

OMB No.1545-0123

Name	Employer identification number (EIN)
Pet Kingdom, Inc.	11-1111111

Part I **Certain Entities Owning the Corporation's Voting Stock.** (Form 1120, Schedule K, Question 4a). Complete columns (i) through (v) below for any foreign or domestic corporation, partnership (including any entity treated as a partnership), trust, or tax-exempt organization that owns directly 20% or more, or owns, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote (see instructions).

(i) Name of Entity	(ii) Employer Identification Number (if any)	(iii) Type of Entity	(iv) Country of Organization	(v) Percentage Owned in Voting Stock

Part II **Certain Individuals and Estates Owning the Corporation's Voting Stock.** (Form 1120, Schedule K, Question 4b). Complete columns (i) through (iv) below for any individual or estate that owns directly 20% or more, or owns, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote (see instructions).

(i) Name of Individual or Estate	(ii) Identifying Number (if any)	(iii) Country of Citizenship (see instructions)	(iv) Percentage Owned in Voting Stock
Janet Morton	123-45-6789	United States	50.000%
Kim Wong	987-65-4321	United States	50.000%

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1833

Schedule G (Form 1120) (Rev. 12-2011)

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SCHEDULE M-3 (Form 1120)
Department of the Treasury
Internal Revenue Service

Net Income (Loss) Reconciliation for Corporations With Total Assets of $10 Million or More

▶Attach to Form 1120 or 1120-C. ▶Information about Schedule M-3 (Form 1120) and its separate instructions is available at *www.irs.gov/form1120*.

OMB No. 1545-0123

2015

Name of corporation (common parent, if consolidated return)	Employer identification number
Pet Kingdom, Inc.	11-1111111

Check applicable box(es): (1) [X] Non-consolidated return (2) [ ] Consolidated return (Form 1120 only)
(3) [ ] Mixed 1120/L/PC group (4) [ ] Dormant subsidiaries schedule attached

Part I Financial Information and Net Income (Loss) Reconciliation (see instructions)

1a Did the corporation file SEC Form 10-K for its income statement period ending with or within this tax year?
[ ] **Yes.** Skip lines 1b and 1c and complete lines 2a through 11 with respect to that SEC Form 10-K.
[X] **No.** Go to line 1b. See instructions if multiple non-tax-basis income statements are prepared.

b Did the corporation prepare a certified audited non-tax-basis income statement for that period?
[ ] **Yes.** Skip line 1c and complete lines 2a through 11 with respect to that income statement.
[X] **No.** Go to line 1c.

c Did the corporation prepare a non-tax-basis income statement for that period?
[X] **Yes.** Complete lines 2a through 11 with respect to that income statement.
[ ] **No.** Skip lines 2a through 3c and enter the corporation's net income (loss) per its books and records on line 4a.

2a Enter the income statement period: Beginning 1/1/2015 Ending 12/31/2015

b Has the corporation's income statement been restated for the income statement period on line 2a?
[ ] **Yes.** (If "Yes," attach an explanation and the amount of each item restated.)
[X] **No.**

c Has the corporation's income statement been restated for any of the five income statement periods immediately preceding the period on line 2a?
[ ] **Yes.** (If "Yes," attach an explanation and the amount of each item restated.)
[X] **No.**

3a Is any of the corporation's voting common stock publicly traded?
[ ] **Yes.**
[X] **No.** If "No," go to line 4a.

b Enter the symbol of the corporation's primary U.S. publicly traded voting common stock . . . . . [ ]

c Enter the nine-digit CUSIP number of the corporation's primary publicly traded voting common stock . . . . . [ ]

4a	Worldwide consolidated net income (loss) from income statement source identified in Part I, line 1	**4a**	717,727
b	Indicate accounting standard used for line 4a (see instructions): (1)[X] GAAP 2)[ ] IFRS 3)[ ] Statutory (4)[ ] Tax-basis (5)[ ] Other (specify) _____		
5a	Net income from nonincludible foreign entities (attach statement)	**5a**	( )
b	Net loss from nonincludible foreign entities (attach statement and enter as a positive amount)	**5b**	
6a	Net income from nonincludible U.S. entities (attach statement)	**6a**	( )
b	Net loss from nonincludible U.S. entities (attach statement and enter as a positive amount)	**6b**	
7a	Net income (loss) of other includible foreign disregarded entities (attach statement)	**7a**	
b	Net income (loss) of other includible U.S. disregarded entities (attach statement)	**7b**	
c	Net income (loss) of other includible entities (attach statement)	**7c**	
8	Adjustment to eliminations of transactions between includible entities and nonincludible entities (attach statement)	**8**	
9	Adjustment to reconcile income statement period to tax year (attach statement)	**9**	
10a	Intercompany dividend adjustments to reconcile to line 11 (attach statement)	**10a**	
b	Other statutory accounting adjustments to reconcile to line 11 (attach statement)	**10b**	
c	Other adjustments to reconcile to amount on line 11 (attach statement)	**10c**	
11	**Net income (loss) per income statement of includible corporations.** Combine lines 4 through 10	**11**	717,727

Note: Part I, line 11, must equal Part II, line 30, column (a) or Schedule M-1, line 1 (see instructions).

12 Enter the total amount (not just the corporation's share) of the assets and liabilities of all entities included or removed on the following lines.

		Total Assets	Total Liabilities
a	Included on Part I, line 4 ▶	13,802,727	6,705,000
b	Removed on Part I, line 5 ▶		
c	Removed on Part I, line 6 ▶		
d	Included on Part I, line 7 ▶		

For Paperwork Reduction Act Notice, see the Instructions for Form 1120. **Schedule M-3 (Form 1120) 2015**
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Schedule M-3 (Form 1120) 2015 Page **2**

Name of corporation (common parent, if consolidated return)	Employer identification number
Pet Kingdom, Inc.	11-1111111

Check applicable box(es): (1) ☐ Consolidated group (2) ☐ Parent corp (3) ☐ Consolidated eliminations (4) ☐ Subsidiary corp (5) ☐ Mixed 1120/L/PC group

Check if a sub-consolidated: (6) ☐ 1120 group (7) ☐ 1120 eliminations

Name of subsidiary (if consolidated return)	Employer identification number

Part II **Reconciliation of Net Income (Loss) per Income Statement of Includible Corporations With Taxable Income per Return** (see instructions)

	Income (Loss) Items (Attach statements for lines 1 through 12)	(a) Income (Loss) per Income Statement	(b) Temporary Difference	(c) Permanent Difference	(d) Income (Loss) per Tax Return
1	Income (loss) from equity method foreign corporations				
2	Gross foreign dividends not previously taxed				
3	Subpart F, QEF, and similar income inclusions				
4	Section 78 gross-up				
5	Gross foreign distributions previously taxed				
6	Income (loss) from equity method U.S. corporations				
7	U.S. dividends not eliminated in tax consolidation	43,750			43,750
8	Minority interest for includible corporations				
9	Income (loss) from U.S. partnerships				
10	Income (loss) from foreign partnerships				
11	Income (loss) from other pass-through entities				
12	Items relating to reportable transactions				
13	Interest income (see instructions)	35,000		(15,000)	20,000
14	Total accrual to cash adjustment				
15	Hedging transactions				
16	Mark-to-market income (loss)				
17	Cost of goods sold (see instructions)	(2,300,000)			(2,300,000)
18	Sale versus lease (for sellers and/or lessors)				
19	Section 481(a) adjustments				
20	Unearned/deferred revenue				
21	Income recognition from long-term contracts				
22	Original issue discount and other imputed interest				
23a	Income statement gain/loss on sale, exchange, abandonment, worthlessness, or other disposition of assets other than inventory and pass-through entities				
b	Gross capital gains from Schedule D, excluding amounts from pass-through entities				
c	Gross capital losses from Schedule D, excluding amounts from pass-through entities, abandonment losses, and worthless stock losses				
d	Net gain/loss reported on Form 4797, line 17, excluding amounts from pass-through entities, abandonment losses, and worthless stock losses				
e	Abandonment losses				
f	Worthless stock losses (attach statement)				
g	Other gain/loss on disposition of assets other than inventory				
24	Capital loss limitation and carryforward used				
25	Other income (loss) items with differences (attach statement)				
26	**Total income (loss) items.** Combine lines 1 through 25	(2,221,250)	0	(15,000)	(2,236,250)
27	**Total expense/deduction items** (from Part III, line 38)	(756,023)	(30,000)	405,023	(381,000)
28	Other items with no differences	3,695,000			3,695,000
29a	Mixed groups, see instructions. All others, combine lines 26 through 28	717,727	(30,000)	390,023	1,077,750
b	PC insurance subgroup reconciliation totals				
c	Life insurance subgroup reconciliation totals				
30	**Reconciliation totals.** Combine lines 29a through 29c	717,727	(30,000)	390,023	1,077,750

Note: Line 30, column (a), must equal Part I, line 11, and column (d) must equal Form 1120, page 1, line 28.

Schedule M-3 (Form 1120) 2015

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Schedule M-3 (Form 1120) 2015 Page 3

Name of corporation (common parent, if consolidated return)	Employer identification number
Pet Kingdom, Inc.	11-1111111

Check applicable box(es): (1) ☐ Consolidated group (2) ☐ Parent corp (3) ☐ Consolidated eliminations (4) ☐ Subsidiary corp (5) ☐ Mixed 1120/L/PC group
Check if a sub-consolidated: (6) ☐ 1120 group (7) ☐ 1120 eliminations

Name of subsidiary (if consolidated return)	Employer identification number

Part III **Reconciliation of Net Income (Loss) per Income Statement of Includible Corporations With Taxable Income per Return—Expense/Deduction Items** (see instructions)

	Expense/Deduction Items	(a) Expense per Income Statement	(b) Temporary Difference	(c) Permanent Difference	(d) Deduction per Tax Return
1	U.S. current income tax expense	356,023		(356,023)	
2	U.S. deferred income tax expense				
3	State and local current income tax expense				
4	State and local deferred income tax expense				
5	Foreign current income tax expense (other than foreign withholding taxes)				
6	Foreign deferred income tax expense				
7	Foreign withholding taxes				
8	Interest expense (see instructions)	216,000		(9,000)	207,000
9	Stock option expense				
10	Other equity-based compensation				
11	Meals and entertainment				
12	Fines and penalties				
13	Judgments, damages, awards, and similar costs				
14	Parachute payments				
15	Compensation with section 162(m) limitation				
16	Pension and profit-sharing				
17	Other post-retirement benefits				
18	Deferred compensation				
19	Charitable contribution of cash and tangible property	38,000			38,000
20	Charitable contribution of intangible property				
21	Charitable contribution limitation/carryforward				
22	Domestic production activities deduction				
23	Current year acquisition or reorganization investment banking fees				
24	Current year acquisition or reorganization legal and accounting fees				
25	Current year acquisition/reorganization other costs				
26	Amortization/impairment of goodwill				
27	Amortization of acquisition, reorganization, and start-up costs				
28	Other amortization or impairment write-offs				
29	Reserved				
30	Depletion				
31	Depreciation	106,000	30,000		136,000
32	Bad debt expense				
33	Corporate owned life insurance premiums	40,000		(40,000)	
34	Purchase versus lease (for purchasers and/or lessees)				
35	Research and development costs				
36	Section 118 exclusion (attach statement)				
37	Other expense/deduction items with differences (attach statement)				
38	**Total expense/deduction items.** Combine lines 1 through 37. Enter here and on Part II, line 27, reporting positive amounts as negative and negative amounts as positive	756,023	30,000	(405,023)	381,000

Schedule M-3 (Form 1120) 2015

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Form **1125-E**
(Rev. December 2013)
Department of the Treasury
Internal Revenue Service

Compensation of Officers

▶ **Attach to Form 1120, 1120-C, 1120-F, 1120-REIT, 1120-RIC, or 1120S**
▶ **Information about Form 1125-E and its separate instructions is at *www.irs.gov/form1125e.***

OMB No. 1545-2225

Name: Pet Kingdom, Inc.
Employer identification number: 11-1111111

Note. Complete Form 1125-E only if total receipts are $500,000 or more. See instructions for definition of total receipts.

(a) Name of officer	(b) Social security number	(c) Percent of time devoted to business	Percent of stock owned (d) Common	Percent of stock owned (e) Preferred	(f) Amount of compensation
1 Janet Morton	123-45-6789	100.00%	50.00%	%	262,500
Kim Wong	987-65-4321	100.00%	50.00%	%	262,500
		%	%	%	
		%	%	%	
		%	%	%	
		%	%	%	
		%	%	%	
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		%	%	%	
		%	%	%	
		%	%	%	
		%	%	%	
		%	%	%	

2	Total compensation of officers	2	525,000
3	Compensation of officers claimed on Form 1125-A or elsewhere on return	3	
4	Subtract line 3 from line 2. Enter the result here and on Form 1120, page 1, line 12 or the appropriate line of your tax return	4	525,000

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Form **8916-A**

Department of the Treasury
Internal Revenue Service

Supplemental Attachment to Schedule M-3

▶ Attach to Schedule M-3 for Form 1065, 1120, 1120-L, 1120-PC, or 1120S.
▶ Information about Form 8916-A and its instructions is at *www.irs.gov/form1120.*

OMB No. 1545-0123

2015

Name of common parent: Pet Kingdom, Inc.
Employer identification number: 11-1111111

Name of subsidiary
Employer identification number

Part I Cost of Goods Sold

Cost of Goods Sold Items	(a) Expense per Income Statement	(b) Temporary Difference	(c) Permanent Difference	(d) Deduction per Tax Return
1 Amounts attributable to cost flow assumptions				
2 Amounts attributable to:				
a Stock option expense				
b Other equity based compensation				
c Meals and entertainment				
d Parachute payments				
e Compensation with section 162(m) limitation				
f Pension and profit sharing				
g Other post-retirement benefits				
h Deferred compensation				
i Reserved				
j Amortization				
k Depletion				
l Depreciation				
m Corporate owned life insurance premiums				
n Other section 263A costs				
3 Inventory shrinkage accruals				
4 Excess inventory and obsolescence reserves				
5 Lower of cost or market write-downs				
6 Other items with differences (attach statement)				
7 Other items with no differences	2,300,000			2,300,000
8 **Total cost of goods sold.** Add lines 1 through 7 in columns a, b, c, and d. Enter totals on the applicable Schedule M-3. See instructions	2,300,000	0	0	2,300,000

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Form 8916-A (2015) Pet Kingdom, Inc. 11-1111111 Page 2

Part II Interest Income

	Interest Income Item	(a) Income (Loss) per Income Statement	(b) Temporary Difference	(c) Permanent Difference	(d) Income (Loss) per Tax Return
1	Tax-exempt interest income	15,000		-15,000	
2	Interest income from hybrid securities				
3	Sale/lease interest income				
4a	Intercompany interest income — From outside tax affiliated group				
4b	Intercompany interest income — From tax affiliated group				
5	Other interest income	20,000			20,000
6	Total interest income. Add lines 1 through 5 in columns a, b, c, and d. Enter total on the applicable Schedule M-3. See instructions.	35,000	0	-15,000	20,000

Part III Interest Expense

	Interest Expense Item	(a) Expense per Income Statement	(b) Temporary Difference	(c) Permanent Difference	(d) Deduction per Tax Return
1	Interest expense from hybrid securities				
2	Lease/purchase interest expense				
3a	Intercompany interest expense — Paid to outside tax affiliated group				
3b	Intercompany interest expense — Paid to tax affiliated group				
4	Other interest expense	216,000		-9,000	207,000
5	Total interest expense. Add lines 1 through 4 in columns a, b, c, and d. Enter total on the applicable Schedule M-3. See instructions.	216,000	0	-9,000	207,000

Form **8916-A** (2015)

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Pet Kingdom, Inc. 11-1111111

Line 6, Sch L (1120) - Other Current Assets

			Beginning		End
1	Certificates of Deposit	1	400,000		400,000
2	Federal Income Tax Refund Due	2			3,977
3	Total other current assets	3	400,000		403,977

Line 9, Sch L (1120) - Other Investments

			Beginning		End
1	Stock Investments	1	1,125,000		1,125,000
2	Total other investments	2	1,125,000		1,125,000

Line 14, Sch L (1120) - Other Assets

			Beginning		End
1	Other Assets	1	140,000		128,500
2	Total other assets	2	140,000		128,500

Line 18, Sch L (1120) - Other Current Liabilities

			Beginning		End
1	Other Current Liabilities	1	175,000		155,000
2	Total other current liabilities	2	175,000		155,000

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PROBLEM 4 SOLUTIONS

Form **1120**
Department of the Treasury
Internal Revenue Service

U.S. Corporation Income Tax Return

For calendar year 2015 or tax year beginning _____, ending _____
▶ Information about Form 1120 and its separate instructions is at *www.irs.gov/form1120*.

OMB No. 1545-0123
2015

A Check if:
1a Consolidated return (attach Form 851) ☐
b Life/nonlife consolidated return ☐
2 Personal holding co. (attach Sch. PH) ☐
3 Personal service corp. (see instructions) ☐
4 Schedule M-3 attached ☐

TYPE OR PRINT

Name: Kingfisher Corporation
Number, street, and room or suite no. If a P.O. box, see instructions.: 1717 Main Street
City or town: Ely | State: MN | ZIP code: 55731
Foreign country name | Foreign province/state/county | Foreign postal code

B Employer identification number: 11-1111111
C Date incorporated: 2/12/2003
D Total assets (see instructions): $ 2,564,100

E Check if: (1) ☐ Initial return (2) ☐ Final return (3) ☐ Name change (4) ☐ Address change

Income	1a	Gross receipts or sales	1a	2,408,000	
	b	Returns and allowance	1b	80,000	
	c	Balance. Subtract line 1b from line 1a			1c 2,328,000
	2	Cost of goods sold (attach Form 1125-A)			2 920,000
	3	Gross profit. Subtract line 2 from line 1c			3 1,408,000
	4	Dividends (Schedule C, line 19)			4 12,000
	5	Interest			5 10,000
	6	Gross rents			6
	7	Gross royalties			7
	8	Capital gain net income (attach Schedule D (Form 1120))			8
	9	Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797)			9
	10	Other income (see instructions—attach statement)			10
	11	**Total income.** Add lines 3 through 10 ▶			11 1,430,000
Deductions (See instructions for limitations on deductions.)	12	Compensation of officers (see instructions—attach Form 1125-E) ▶			12 320,000
	13	Salaries and wages (less employment credits)			13 290,000
	14	Repairs and maintenance			14 56,000
	15	Bad debts			15
	16	Rents			16 68,000
	17	Taxes and licenses			17 85,000
	18	Interest			18 12,000
	19	Charitable contributions			19 15,000
	20	Depreciation from Form 4562 not claimed on Form 1125-A or elsewhere on return (attach Form 4562)			20 40,000
	21	Depletion			21
	22	Advertising			22 6,000
	23	Pension, profit-sharing, etc., plans			23
	24	Employee benefit programs			24 24,000
	25	Domestic production activities deduction (attach Form 8903)			25
	26	Other deductions (attach statement)			26
	27	**Total deductions.** Add lines 12 through 26 ▶			27 916,000
	28	Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11			28 514,000
	29a	Net operating loss deduction (see instructions)	29a		
	b	Special deductions (Schedule C, line 20)	29b	8,400	
	c	Add lines 29a and 29b			29c 8,400
Tax, Refundable Credits, and Payments	30	**Taxable income.** Subtract line 29c from line 28 (see instructions)			30 505,600
	31	Total tax (Schedule J, Part I, line 11)			31 171,904
	32	Total payments and refundable credits (Schedule J, Part II, line 21)			32 175,000
	33	Estimated tax penalty (see instructions). Check if Form 2220 is attached ▶ ☐			33
	34	**Amount owed.** If line 32 is smaller than the total of lines 31 and 33, enter amount owed			34 0
	35	**Overpayment.** If line 32 is larger than the total of lines 31 and 33, enter amount overpaid			35 3,096
	36	Enter amount from line 35 you want: **Credited to 2016 estimated tax** ▶ **Refunded** ▶			36 3,096

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of officer | Date | Title

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
	SELF-PREPARED RETURN			

Firm's name ▶ | Firm's EIN ▶
Firm's address ▶ | Phone no.
City | State | ZIP code

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Form 1120 (2015) Kingfisher Corporation 11-1111111 Page **2**

Schedule C **Dividends and Special Deductions** (see instructions)

		(a) Dividends received	(b) %	(c) Special deductions (a) × (b)
1	Dividends from less-than-20%-owned domestic corporations (other than debt-financed stock)	12,000	70	8,400
2	Dividends from 20%-or-more-owned domestic corporations (other than debt-financed stock)		80	0
3	Dividends on debt-financed stock of domestic and foreign corporations		see instructions	0
4	Dividends on certain preferred stock of less-than-20%-owned public utilities		42	0
5	Dividends on certain preferred stock of 20%-or-more-owned public utilities		48	0
6	Dividends from less-than-20%-owned foreign corporations and certain FSCs		70	0
7	Dividends from 20%-or-more-owned foreign corporations and certain FSCs		80	0
8	Dividends from wholly owned foreign subsidiaries		100	0
9	**Total.** Add lines 1 through 8. See instructions for limitation			8,400
10	Dividends from domestic corporations received by a small business investment company operating under the Small Business Investment Act of 1958		100	0
11	Dividends from affiliated group members		100	0
12	Dividends from certain FSCs		100	0
13	Dividends from foreign corporations not included on lines 3, 6, 7, 8, 11, or 12			
14	Income from controlled foreign corporations under subpart F (attach Form(s) 5471)			
15	Foreign dividend gross-up			
16	IC-DISC and former DISC dividends not included on lines 1, 2, or 3			
17	Other dividends			
18	Deduction for dividends paid on certain preferred stock of public utilities			
19	**Total dividends.** Add lines 1 through 17. Enter here and on page 1, line 4 ▶	12,000		
20	**Total special deductions.** Add lines 9, 10, 11, 12, and 18. Enter here and on page 1, line 29b ▶			8,400

Form **1120** (2015)

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Form 1120 (2015) Kingfisher Corporation 11-1111111 Page 3

Schedule J Tax Computation and Payment (see instructions)

Part I–Tax Computation

1	Check if the corporation is a member of a controlled group (attach Schedule O (Form 1120)) ▶ ☐					
2	Income tax. Check if a qualified personal service corporation (see instructions) ▶ ☐			2	171,904	
3	Alternative minimum tax (attach Form 4626)			3		
4	Add lines 2 and 3			4	171,904	
5a	Foreign tax credit (attach Form 1118)	5a				
b	Credit from Form 8834 (see instructions)	5b				
c	General business credit (attach Form 3800)	5c				
d	Credit for prior year minimum tax (attach Form 8827)	5d				
e	Bond credits from Form 8912	5e				
6	**Total credits.** Add lines 5a through 5e			6	0	
7	Subtract line 6 from line 4			7	171,904	
8	Personal holding company tax (attach Schedule PH (Form 1120))			8		
9a	Recapture of investment credit (attach Form 4255)	9a				
b	Recapture of low-income housing credit (attach Form 8611)	9b				
c	Interest due under the look-back method—completed long-term contracts (attach Form 8697)	9c				
d	Interest due under the look-back method—income forecast method (attach Form 8866)	9d				
e	Alternative tax on qualifying shipping activities (attach Form 8902)	9e				
f	Other (see instructions—attach statement)	9f				
10	**Total.** Add lines 9a through 9f			10	0	
11	**Total tax.** Add lines 7, 8, and 10. Enter here and on page 1, line 31			11	171,904	

Part II–Payments and Refundable Credits

12	2014 overpayment credited to 2015			12		
13	2015 estimated tax payments			13	175,000	
14	2015 refund applied for on Form 4466			14	( )	
15	Combine lines 12, 13, and 14			15	175,000	
16	Tax deposited with Form 7004			16		
17	Withholding (see instructions)			17		
18	**Total payments.** Add lines 15, 16, and 17			18	175,000	
19	Refundable credits from:					
a	Form 2439	19a				
b	Form 4136	19b				
c	Form 8827, line 8c	19c				
d	Other (attach statement—see instructions)	19d				
20	**Total credits.** Add lines 19a through 19d			20	0	
21	**Total payments and credits.** Add lines 18 and 20. Enter here and on page 1, line 32			21	175,000	

Schedule K Other Information (see instructions)

		Yes	No
1	Check accounting method: a ☐ Cash b ☒ Accrual c ☐ Other (specify) ▶		
2	See the instructions and enter the:		
a	Business activity code no. ▶ 451110		
b	Business activity ▶ Retail Sporting Goods		
c	Product or service ▶ Fishing Tackle		
3	Is the corporation a subsidiary in an affiliated group or a parent-subsidiary controlled group?		X
	If "Yes," enter name and EIN of the parent corporation ▶		
4	At the end of the tax year:		
a	Did any foreign or domestic corporation, partnership (including any entity treated as a partnership), trust, or tax-exempt organization own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote? If "Yes," complete Part I of Schedule G (Form 1120) (attach Schedule G)		X
b	Did any individual or estate own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote? If "Yes," complete Part II of Schedule G (Form 1120) (attach Schedule G)	X	

Form **1120** (2015)

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Form 1120 (2015) Kingfisher Corporation 11-1111111 Page 4

Schedule K Other Information *continued* (see instructions)

		Yes	No
5	At the end of the tax year, did the corporation:		
a	Own directly 20% or more, or own, directly or indirectly, 50% or more of the total voting power of all classes of stock entitled to vote of any foreign or domestic corporation not included on **Form 851,** Affiliations Schedule? For rules of constructive ownership, see instructions . . If "Yes," complete (i) through (iv) below.		X

(i) Name of Corporation	(ii) Employer Identification Number (if any)	(iii) Country of Incorporation	(iv) Percentage Owned in Voting Stock

b	Own directly an interest of 20% or more, or own, directly or indirectly, an interest of 50% or more in any foreign or domestic partnership (including an entity treated as a partnership) or in the beneficial interest of a trust? For rules of constructive ownership, see instructions . . If "Yes," complete (i) through (iv) below.		X

(i) Name of Entity	(ii) Employer Identification Number (if any)	(iii) Country of Organization	(iv) Maximum Percentage Owned in Profit, Loss, or Capital

6	During this tax year, did the corporation pay dividends (other than stock dividends and distributions in exchange for stock) in excess of the corporation's current and accumulated earnings and profits? (See sections 301 and 316.) . . . If "Yes," file **Form 5452,** Corporate Report of Nondividend Distributions. If this is a consolidated return, answer here for the parent corporation and on Form 851 for each subsidiary.		X
7	At any time during the tax year, did one foreign person own, directly or indirectly, at least 25% of **(a)** the total voting power of all classes of the corporation's stock entitled to vote or **(b)** the total value of all classes of the corporation's stock? . . . For rules of attribution, see section 318. If "Yes," enter: **(i)** Percentage owned ► _____ and **(ii)** Owner's country ► _____ **(c)** The corporation may have to file **Form 5472,** Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Enter the number of Forms 5472 attached ► _____		X
8	Check this box if the corporation issued publicly offered debt instruments with original issue discount . . . ► ☐ If checked, the corporation may have to file **Form 8281,** Information Return for Publicly Offered Original Issue Discount Instruments.		
9	Enter the amount of tax-exempt interest received or accrued during the tax year ► $ 14,000		
10	Enter the number of shareholders at the end of the tax year (if 100 or fewer) ► 2		
11	If the corporation has an NOL for the tax year and is electing to forego the carryback period, check here . . . ► ☐ If the corporation is filing a consolidated return, the statement required by Regulations section 1.1502-21(b)(3) must be attached or the election will not be valid.		
12	Enter the available NOL carryover from prior tax years (do not reduce it by any deduction on line 29a.) ► $		
13	Are the corporation's total receipts (page 1, line 1a, plus lines 4 through 10) for the tax year **and** its total assets at the end of the tax year less than $250,000? . . . If "Yes," the corporation is not required to complete Schedules L, M-1, and M-2. Instead, enter the total amount of cash distributions and the book value of property distributions (other than cash) made during the tax year. ► $		X
14	Is the corporation required to file Schedule UTP (Form 1120), Uncertain Tax Position Statement (see instructions)? . . . If "Yes," complete and attach Schedule UTP.		X
15a	Did the corporation make any payments in 2015 that would require it to file Form(s) 1099? . . .	X	
b	If "Yes," did or will the corporation file required Forms 1099? . . .	X	
16	During this tax year, did the corporation have an 80% or more change in ownership, including a change due to redemption of its own stock? . . .		X
17	During or subsequent to this tax year, but before the filing of this return, did the corporation dispose of more than 65% (by value) of its assets in a taxable, non-taxable, or tax deferred transaction? . . .		X
18	Did the corporation receive assets in a section 351 transfer in which any of the transferred assets had a fair market basis or fair market value of more than $1 million? . . .		X

Form **1120** (2015)

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Form 1120 (2015) Kingfisher Corporation 11-1111111 Page **5**

Schedule L Balance Sheets per Books

Assets	Beginning of tax year (a)	Beginning of tax year (b)	End of tax year (c)	End of tax year (d)
1 Cash		380,000		335,524
2a Trade notes and accounts receivable	308,400		480,280	
b Less allowance for bad debts	( )	308,400	( )	480,280
3 Inventories		900,000		1,012,000
4 U.S. government obligations				
5 Tax-exempt securities (see instructions)		160,000		160,000
6 Other current assets (attach statement)				3,096
7 Loans to shareholders				
8 Mortgage and real estate loans				
9 Other investments (attach statement)		440,000		440,000
10a Buildings and other depreciable assets	240,000		240,000	
b Less accumulated depreciation	(88,800)	151,200	(128,800)	111,200
11a Depletable assets				
b Less accumulated depletion	( )	0	( )	0
12 Land (net of any amortization)		20,000		20,000
13a Intangible assets (amortizable only)				
b Less accumulated amortization	( )	0	( )	0
14 Other assets (attach statement)		3,600		2,000
15 Total assets		2,363,200		2,564,100
Liabilities and Shareholders' Equity				
16 Accounts payable		300,000		299,104
17 Mortgages, notes, bonds payable in less than 1 year				
18 Other current liabilities (attach statement)		80,300		40,000
19 Loans from shareholders				
20 Mortgages, notes, bonds payable in 1 year or more		210,000		200,000
21 Other liabilities (attach statement)				
22 Capital stock: a Preferred stock				
b Common stock	500,000	500,000	500,000	500,000
23 Additional paid-in capital				
24 Retained earnings—Appropriated (attach statement)				
25 Retained earnings—Unappropriated		1,272,900		1,524,996
26 Adjustments to shareholders' equity (attach statement)				
27 Less cost of treasury stock		( )		( )
28 Total liabilities and shareholders' equity		2,363,200		2,564,100

Schedule M-1 Reconciliation of Income (Loss) per Books With Income per Return

Note: The corporation may be required to file Schedule M-3 (see instructions).

1 Net income (loss) per books	332,096	7 Income recorded on books this year not included on this return (itemize): Tax-exempt interest $ 14,000	14,000
2 Federal income tax per books	171,904		
3 Excess of capital losses over capital gains			
4 Income subject to tax not recorded on books this year (itemize):	0	8 Deductions on this return not charged against book income this year (itemize):	
5 Expenses recorded on books this year not deducted on this return (itemize):		a Depreciation $	
a Depreciation $		b Charitable contributions $	
b Charitable contributions $			
c Travel and entertainment $			
State Bond Interest Expense 8,000			0
Life Insurance Premiums 16,000	24,000	9 Add lines 7 and 8	14,000
6 Add lines 1 through 5	528,000	10 Income (page 1, line 28)—line 6 less line 9	514,000

Schedule M-2 Analysis of Unappropriated Retained Earnings per Books (Line 25, Schedule L)

1 Balance at beginning of year	1,272,900	5 Distributions: a Cash	80,000
2 Net income (loss) per books	332,096	b Stock	
3 Other increases (itemize):		c Property	
		6 Other decreases (itemize):	
	0	7 Add lines 5 and 6	80,000
4 Add lines 1, 2, and 3	1,604,996	8 Balance at end of year (line 4 less line 7)	1,524,996

Form **1120** (2015)

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Form **1125-A** (Rev. December 2012)
Department of the Treasury
Internal Revenue Service

Cost of Goods Sold

▶ **Attach to Form 1120, 1120-C, 1120-F, 1120S, 1065, or 1065-B.**
▶ **Information about Form 1125-A and its instructions is at *www.irs.gov/form1125a.***

OMB No. 1545-2225

Name	Employer identification number
Kingfisher Corporation	11-1111111

1	Inventory at beginning of year	1	900,000	
2	Purchases	2	1,032,000	
3	Cost of labor	3		
4	Additional section 263A costs (attach schedule)	4		
5	Other costs (attach schedule)	5		
6	**Total.** Add lines 1 through 5	6	1,932,000	
7	Inventory at end of year	7	1,012,000	
8	**Cost of goods sold.** Subtract line 7 from line 6. Enter here and on Form 1120, page 1, line 2 or the appropriate line of your tax return (see instructions)	8	920,000	

9 **a** Check all methods used for valuing closing inventory:
- *(i)* ☐ Cost
- *(ii)* ☒ Lower of cost or market
- *(iii)* ☐ Other (Specify method used and attach explanation.) ▶

b Check if there was a writedown of subnormal goods ▶ ☐

c Check if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970) ▶ ☐

d If the LIFO inventory method was used for this tax year, enter amount of closing inventory computed under LIFO — 9d

e If property is produced or acquired for resale, do the rules of section 263A apply to the entity (see instructions)? ☐ Yes ☒ No

f Was there any change in determining quantities, cost, or valuations between opening and closing inventory? If "Yes," attach explanation ☐ Yes ☒ No

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SCHEDULE G (Form 1120)
(Rev. December 2011)
Department of the Treasury
Internal Revenue Service

Information on Certain Persons Owning the Corporation's Voting Stock

▶ Attach to Form 1120.
▶ See instructions on page 2.

OMB No.1545-0123

Name	Employer identification number (EIN)
Kingfisher Corporation	11-1111111

Part I **Certain Entities Owning the Corporation's Voting Stock.** (Form 1120, Schedule K, Question 4a). Complete columns (i) through (v) below for any foreign or domestic corporation, partnership (including any entity treated as a partnership), trust, or tax-exempt organization that owns directly 20% or more, or owns, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote (see instructions).

(i) Name of Entity	(ii) Employer Identification Number (if any)	(iii) Type of Entity	(iv) Country of Organization	(v) Percentage Owned in Voting Stock

Part II **Certain Individuals and Estates Owning the Corporation's Voting Stock.** (Form 1120, Schedule K, Question 4b). Complete columns (i) through (iv) below for any individual or estate that owns directly 20% or more, or owns, directly or indirectly, 50% or more of the total voting power of all classes of the corporation's stock entitled to vote (see instructions).

(i) Name of Individual or Estate	(ii) Identifying Number (if any)	(iii) Country of Citizenship (see instructions)	(iv) Percentage Owned in Voting Stock
Nancy Trout	123-45-6789	United States	50.000%
Delores Lake	987-65-4321	United States	50.000%

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1833

Schedule G (Form 1120) (Rev. 12-2011)

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Form **1125-E**
(Rev. December 2013)
Department of the Treasury
Internal Revenue Service

Compensation of Officers

▶ **Attach to Form 1120, 1120-C, 1120-F, 1120-REIT, 1120-RIC, or 1120S**
▶ **Information about Form 1125-E and its separate instructions is at *www.irs.gov/form1125e.***

OMB No. 1545-2225

Name: Kingfisher Corporation
Employer identification number: 11-1111111

Note. Complete Form 1125-E only if total receipts are $500,000 or more. See instructions for definition of total receipts.

(a) Name of officer	(b) Social security number	(c) Percent of time devoted to business	Percent of stock owned (d) Common	Percent of stock owned (e) Preferred	(f) Amount of compensation
1 Nancy Trout	123-45-6789	100.00%	50.00%	%	160,000
Delores Lake	987-65-4321	100.00%	50.00%	%	160,000
		%	%	%	
		%	%	%	
		%	%	%	
		%	%	%	
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		%	%	%	
		%	%	%	
		%	%	%	

2	Total compensation of officers	2	320,000
3	Compensation of officers claimed on Form 1125-A or elsewhere on return	3	
4	Subtract line 3 from line 2. Enter the result here and on Form 1120, page 1, line 12 or the appropriate line of your tax return	4	320,000

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Kingfisher Corporation 11-1111111

Line 6, Sch L (1120) - Other Current Assets

			Beginning		End
1	Federal Income Tax Refund Due	1			3,096
2	Total other current assets	2	0		3,096

Line 9, Sch L (1120) - Other Investments

			Beginning		End
1	Certificates of Deposit	1	140,000		140,000
2	Stock Investments	2	300,000		300,000
3	Total other investments	3	440,000		440,000

Line 14, Sch L (1120) - Other Assets

			Beginning		End
1	Other Assets	1	3,600		2,000
2	Total other assets	2	3,600		2,000

Line 18, Sch L (1120) - Other Current Liabilities

			Beginning		End
1	Other Current Liabilities	1	80,300		40,000
2	Total other current liabilities	2	80,300		40,000

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PROBLEM 5 SOLUTIONS

- When preparing page 1 of Form 1065, the payment for the partners' services is deducted on line 10 as a guaranteed payment.

- When preparing Schedule K–1, the net earnings from self-employment (line 14a) equals the combination of lines 1 and 4 on the K–1. This is Ryan's 1/4 share of the partnership's ordinary income plus his guaranteed payment for services.

- Ryan Ross's "current year increase/decrease" in item L of the Schedule K–1 is computed as follows: $840,000 (book income) ÷ 4 = $210,000. This amount consists of the following items on the K–1:

Line 1, Ordinary business income (loss)	$244,800
Plus: Line 5, Interest income	400
Less: Line 8, Net short-term capital gain (loss)	(5,000)
Plus: Line 9a, Net long-term capital gain (loss)	6,000
Less: Line 12, Section 179 deduction	(5,000)
Less: Line 13a, Charitable contributions	(7,000)
Plus: Line 18 (Code A), Tax-exempt interest income	800
Less: Line 18 (Code C), Nondeductible expenses	(25,000)
Line L, current year increase (decrease)	$210,000

- On Schedules K and K–1, no amount is shown for net investment income on line 20, Code Y, because all components of net investment income are readily identifiable (e.g., interest income). An amount would have been shown, for example, if some or all of the guaranteed payments had been for use of the members' capital.

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Form **1065**
Department of the Treasury
Internal Revenue Service

U.S. Return of Partnership Income

For calendar year 2015, or tax year beginning _____, ending _____.
▶ Information about Form 1065 and its separate instructions is at *www.irs.gov/form1065.*

OMB No. 1545-0123
2015

A Principal business activity: Musican Agents/Mgrs	Name of partnership: ROCK the Ages LLC	**D** Employer identification number: 55-5555555
B Principal product or service: Agent Services	Number, street, and room or suite no. If a P.O. box, see the instructions.: 6102 Wilshire Boulevard, Suite 2100	**E** Date business started: 1/1/2004
C Business code number: 711410	City or town: Los Angeles; State: CA; ZIP code: 90036	**F** Total assets (see the instructions): $ 800,000
	Foreign country name; Foreign province/state/county; Foreign postal code	

Type or Print

G Check applicable boxes: (1) ☐ Initial return (2) ☐ Final return (3) ☐ Name change (4) ☐ Address change (5) ☐ Amended return
(6) ☐ Technical termination - also check (1) or (2)

H Check accounting method: (1) ☒ Cash (2) ☐ Accrual (3) ☐ Other (specify) ▶

I Number of Schedules K-1. Attach one for each person who was a partner at any time during the tax year ▶ 4

J Check if Schedules C and M-3 are attached ☐

Caution. *Include* ***only*** *trade or business income and expenses on lines 1a through 22 below. See the instructions for more information.*

Income	1a	Gross receipts or sales	1a	4,800,000	
	b	Returns and allowances	1b		
	c	Balance. Subtract line 1b from line 1a		1c	4,800,000
	2	Cost of goods sold (attach Form 1125-A)		2	
	3	Gross profit. Subtract line 2 from line 1c		3	4,800,000
	4	Ordinary income (loss) from other partnerships, estates, and trusts (attach statement)		4	
	5	Net farm profit (loss) (attach Schedule F (Form 1040))		5	
	6	Net gain (loss) from Form 4797, Part II, line 17 (attach Form 4797)		6	
	7	Other income (loss) (attach statement)		7	
	8	**Total income (loss).** Combine lines 3 through 7		8	4,800,000
Deductions (see the instructions for limitations)	9	Salaries and wages (other than to partners) (less employment credits)		9	1,000,000
	10	Guaranteed payments to partners		10	1,400,000
	11	Repairs and maintenance		11	
	12	Bad debts		12	
	13	Rent		13	80,000
	14	Taxes and licenses		14	92,000
	15	Interest		15	10,000
	16a	Depreciation (if required, attach Form 4562)	16a		
	b	Less depreciation reported on Form 1125-A and elsewhere on return	16b	16c	0
	17	Depletion **(Do not deduct oil and gas depletion.)**		17	
	18	Retirement plans, etc.		18	
	19	Employee benefit programs		19	
	20	Other deductions (attach statement)		20	1,238,800
	21	**Total deductions.** Add the amounts shown in the far right column for lines 9 through 20		21	3,820,800
	22	**Ordinary business income (loss).** Subtract line 21 from line 8		22	979,200

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than general partner or limited liability company member manager) is based on all information of which preparer has any knowledge.

▶ _____ Signature of general partner or limited liability company member manager ▶ _____ Date

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature: SELF-PREPARED RETURN	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	
City	State		ZIP code	

For Paperwork Reduction Act Notice, see separate instructions. Form **1065** (2015)

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Form 1065 (2015) ROCK the Ages LLC 55-5555555 Page 4

Schedule K	Partners' Distributive Share Items		Total amount
Income (Loss)	1 Ordinary business income (loss) (page 1, line 22)	1	979,200
	2 Net rental real estate income (loss) (attach Form 8825)	2	
	3a Other gross rental income (loss) 3a		
	b Expenses from other rental activities (attach statement) 3b		
	c Other net rental income (loss). Subtract line 3b from line 3a	3c	0
	4 Guaranteed payments	4	1,400,000
	5 Interest income	5	1,600
	6 Dividends: a Ordinary dividends	6a	
	b Qualified dividends 6b		
	7 Royalties	7	
	8 Net short-term capital gain (loss) (attach Schedule D (Form 1065))	8	-20,000
	9a Net long-term capital gain (loss) (attach Schedule D (Form 1065))	9a	24,000
	b Collectibles (28%) gain (loss) 9b		
	c Unrecaptured section 1250 gain (attach statement) 9c		
	10 Net section 1231 gain (loss) (attach Form 4797)	10	
	11 Other income (loss) (see instructions) Type ▶	11	
Deductions	12 Section 179 deduction (attach Form 4562)	12	20,000
	13a Contributions	13a	28,000
	b Investment interest expense	13b	
	c Section 59(e)(2) expenditures: (1) Type ▶ (2) Amount ▶	13c(2)	
	d Other deductions (see instructions) Type ▶	13d	
Self-Employment	14a Net earnings (loss) from self-employment	14a	2,379,200
	b Gross farming or fishing income	14b	
	c Gross nonfarm income	14c	4,800,000
Credits	15a Low-income housing credit (section 42(j)(5))	15a	
	b Low-income housing credit (other)	15b	
	c Qualified rehabilitation expenditures (rental real estate) (attach Form 3468, if applicable)	15c	
	d Other rental real estate credits (see instructions) Type ▶	15d	
	e Other rental credits (see instructions) Type ▶	15e	
	f Other credits (see instructions) Type ▶	15f	
Foreign Transactions	16a Name of country or U.S. possession ▶		
	b Gross income from all sources	16b	
	c Gross income sourced at partner level	16c	
	Foreign gross income sourced at partnership level		
	d Passive category ▶ e General category ▶ f Other ▶	16f	
	Deductions allocated and apportioned at partner level		
	g Interest expense ▶ h Other ▶	16h	
	Deductions allocated and apportioned at partnership level to foreign source income		
	i Passive category ▶ j General category ▶ k Other ▶	16k	
	l Total foreign taxes (check one): ▶ Paid ☐ Accrued ☐	16l	
	m Reduction in taxes available for credit (attach statement)	16m	
	n Other foreign tax information (attach statement)		
Alternative Minimum Tax (AMT) Items	17a Post-1986 depreciation adjustment	17a	
	b Adjusted gain or loss	17b	
	c Depletion (other than oil and gas)	17c	
	d Oil, gas, and geothermal properties—gross income	17d	
	e Oil, gas, and geothermal properties—deductions	17e	
	f Other AMT items (attach statement)	17f	
Other Information	18a Tax-exempt interest income	18a	3,200
	b Other tax-exempt income	18b	
	c Nondeductible expenses	18c	100,000
	19a Distributions of cash and marketable securities	19a	1,000,000
	b Distributions of other property	19b	
	20a Investment income	20a	1,600
	b Investment expenses	20b	
	c Other items and amounts (attach statement)		

Form 1065 (2015)

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Form 1065 (2015) ROCK the Ages LLC 55-5555555 Page **5**

Analysis of Net Income (Loss)

1	Net income (loss). Combine Schedule K, lines 1 through 11. From the result, subtract the sum of Schedule K, lines 12 through 13d, and 16l	1	2,336,800

2 Analysis by partner type:	(i) Corporate	(ii) Individual (active)	(iii) Individual (passive)	(iv) Partnership	(v) Exempt Organization	(vi) Nominee/Other
a General partners		1,034,200				
b Limited partners		2,336,800				

Schedule L Balance Sheets per Books

Assets	Beginning of tax year (a)	Beginning of tax year (b)	End of tax year (c)	End of tax year (d)
1 Cash		444,000		380,000
2a Trade notes and accounts receivable				
b Less allowance for bad debts		0		0
3 Inventories				
4 U.S. government obligations				
5 Tax-exempt securities		120,000		120,000
6 Other current assets (attach statement)				
7a Loans to partners (or persons related to partners)				
b Mortgage and real estate loans				
8 Other investments (attach statement)		436,000		300,000
9a Buildings and other depreciable assets	960,000		980,000	
b Less accumulated depreciation	960,000	0	980,000	0
10a Depletable assets				
b Less accumulated depletion		0		0
11 Land (net of any amortization)				
12a Intangible assets (amortizable only)				
b Less accumulated amortization		0		0
13 Other assets (attach statement)				
14 Total assets		1,000,000		800,000
Liabilities and Capital				
15 Accounts payable				
16 Mortgages, notes, bonds payable in less than 1 year				
17 Other current liabilities (attach statement)		200,000		160,000
18 All nonrecourse loans				
19a Loans from partners (or persons related to partners)				
b Mortgages, notes, bonds payable in 1 year or more				
20 Other liabilities (attach statement)				
21 Partners' capital accounts		800,000		640,000
22 Total liabilities and capital		1,000,000		800,000

Schedule M-1 Reconciliation of Income (Loss) per Books With Income (Loss) per Return

Note. The partnership may be required to file Schedule M-3 (see instructions).

1	Net income (loss) per books	840,000	6	Income recorded on books this year not included on Schedule K, lines 1 through 11 (itemize):	
2	Income included on Schedule K, lines 1, 2, 3c, 5, 6a, 7, 8, 9a, 10, and 11, not recorded on books this year (itemize):	0	a	Tax-exempt interest $ 3,200	3,200
3	Guaranteed payments (other than health insurance)	1,400,000	7	Deductions included on Schedule K, lines 1 through 13d, and 16l, not charged against book income this year (itemize):	
4	Expenses recorded on books this year not included on Schedule K, lines 1 through 13d, and 16l (itemize):		a	Depreciation $	0
a	Depreciation $		8	Add lines 6 and 7	3,200
b	Travel and entertainment $ 100,000	100,000	9	Income (loss) (Analysis of Net Income (Loss), line 1). Subtract line 8 from line 5	2,336,800
5	Add lines 1 through 4	2,340,000			

Schedule M-2 Analysis of Partners' Capital Accounts

1	Balance at beginning of year	800,000	6	Distributions: a Cash	1,000,000
2	Capital contributed: a Cash			b Property	
	b Property		7	Other decreases (itemize):	
3	Net income (loss) per books	840,000			
4	Other increases (itemize):	0	8	Add lines 6 and 7	1,000,000
5	Add lines 1 through 4	1,640,000	9	Balance at end of year. Subtract line 8 from line 5	640,000

Form **1065** (2015)

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Form **8949**

Department of the Treasury
Internal Revenue Service

Sales and Other Dispositions of Capital Assets

► Information about Form 8949 and its separate instructions is at *www.irs.gov/form8949.*
► File with your Schedule D to list your transactions for lines 1b, 2, 3, 8b, 9, and 10 of Schedule D.

OMB No. 1545-0074
2015
Attachment Sequence No. **12A**

Name(s) shown on return	Social security number or taxpayer identification number
ROCK the Ages LLC	55-5555555

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I **Short-Term.** Transactions involving capital assets you held 1 year or less are short term. For long-term transactions, see page 2.

Note: You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box A, B, *or* C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- [X] **(A)** Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- [ ] **(B)** Short-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- [ ] **(C)** Short-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions. (f) Code(s) from instructions	(g) Amount of adjustment	(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
Tech, Inc. - 1,000 Shares	6/15/2015	12/15/2015	80,000	100,000			-20,000
2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 1b** (if **Box A** above is checked), line 2 (if **Box B** above is checked), or **line 3** (if **Box C** above is checked) ►			80,000	100,000		0	-20,000

Note: If you checked Box A above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

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Form 8949 (2015) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Name and SSN or taxpayer identification no. not required if shown on other side	**Social security number or taxpayer identification number**
ROCK the Ages LLC	55-5555555

Before you check Box D, E, or F below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part II **Long-Term.** Transactions involving capital assets you held more than 1 year are long term. For short-term transactions, see page 1.

Note: You may aggregate all long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 8a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box D, E, *or* F below. Check only one box. If more than one box applies for your long-term transactions, complete a separate Form 8949, page 2, for each applicable box. If you have more long-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- [X] **(D)** Long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- [ ] **(E)** Long-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- [ ] **(F)** Long-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	**Adjustment, if any, to gain or loss.** If you enter an amount in column (g), enter a code in column (f). **See the separate instructions.** (f) Code(s) from instructions	(g) Amount of adjustment	(h) **Gain or (loss).** Subtract column (e) from column (d) and combine the result with column (g)
BioLabs, Inc. - 2,000 Shares	3/15/2014	12/15/2015	160,000	136,000			24,000
2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 8b** (if **Box D** above is checked), **line 9** (if **Box E** above is checked), or **line 10** (if **Box F** above is checked) ▶			160,000	136,000		0	24,000

Note: If you checked Box D above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

Form **8949** (2015)

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SCHEDULE D (Form 1065)

Department of the Treasury
Internal Revenue Service

Capital Gains and Losses

▶ Attach to Form 1065 or Form 8865.
▶ Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.
▶ Information about Schedule D (Form 1065) and its separate instructions is at *www.irs.gov/form1065.*

OMB No. 1545-0123

2015

Name of partnership: ROCK the Ages LLC

Employer identification number: 55-5555555

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

See instructions for how to figure the amounts to enter on the lines below.
This form may be easier to complete if you round off cents to whole dollars.

	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 1b				0
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked	80,000	100,000		-20,000
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked				0
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked				0

4 Short-term capital gain from installment sales from Form 6252, line 26 or 37	4	
5 Short-term capital gain or (loss) from like-kind exchanges from Form 8824	5	
6 Partnership's share of net short-term capital gain (loss), including specially allocated short-term capital gains (losses), from other partnerships, estates, and trusts	6	
7 **Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). Enter here and on Form 1065, Schedule K, line 8 or 11; or Form 8865, Schedule K, line 8 or 11	7	-20,000

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

See instructions for how to figure the amounts to enter on the lines below.
This form may be easier to complete if you round off cents to whole dollars.

	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b				0
8b Totals for all transactions reported on Form(s) 8949 with **Box D** checked	160,000	136,000		24,000
9 Totals for all transactions reported on Form(s) 8949 with **Box E** checked				0
10 Totals for all transactions reported on Form(s) 8949 with **Box F** checked				0

11 Long-term capital gain from installment sales from Form 6252, line 26 or 37	11	
12 Long-term capital gain or (loss) from like-kind exchanges from Form 8824	12	
13 Partnership's share of net long-term capital gain (loss), including specially allocated long-term capital gains (losses), from other partnerships, estates, and trusts	13	
14 Capital gain distributions	14	
15 **Net long-term capital gain or (loss).** Combine lines 8a through 14 in column (h). Enter here and on Form 1065, Schedule K, line 9a or 11; or Form 8865, Schedule K, line 9a or 11	15	24,000

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651113

☐ Final K-1 ☐ Amended K-1 OMB No. 1545-0123

Schedule K-1 (Form 1065) 2015

Department of the Treasury
Internal Revenue Service

For calendar year 2015, or tax year beginning _____, 2015 ending _____, 20 ____

Partner's Share of Income, Deductions, Credits, etc. ▶ See back of form and separate instructions.

Part I Information About the Partnership

A Partnership's employer identification number
55-5555555

B Partnership's name, address, city, state, and ZIP code
ROCK the Ages LLC
6102 Wilshire Boulevard, Suite 2100
Los Angeles, CA 90036

C IRS Center where partnership filed return
e-file

D ☐ Check if this is a publicly traded partnership (PTP)

Part II Information About the Partner

E Partner's identifying number Partner: 1
111-11-1112

F Partner's name, address, city, state, and ZIP code
Ryan Ross
15520 West Earlson Street
Pacific Palisades, CA 90272

G ☒ General partner or LLC member-manager ☐ Limited partner or other LLC member

H ☒ Domestic partner ☐ Foreign partner

I1 What type of entity is this partner? Active Individual

I2 If this partner is a retirement plan (IRA/SEP/Keogh/etc.), check here ☐

J Partner's share of profit, loss, and capital (see instructions):

	Beginning	Ending
Profit	25.000000%	25.000000%
Loss	25.000000%	25.000000%
Capital	25.000000%	25.000000%

K Partner's share of liabilities at year end:
Nonrecourse . . . . . $ _____
Qualified nonrecourse financing . . $ _____
Recourse . . . . . $ 40,000

L Partner's capital account analysis:
Beginning capital account . . . . $ 200,000
Capital contributed during the year . . $ _____
Current year increase (decrease) . . $ 210,000
Withdrawals & distributions . . . . $ (250,000)
Ending capital account . . . . . $ 160,000

☒ Tax basis ☐ GAAP ☐ Section 704(b) book
☐ Other (explain)

M Did the partner contribute property with a built-in gain or loss?
☐ Yes ☒ No
If "Yes," attach statement (see instructions)

Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items

1	Ordinary business income (loss) 244,800	15	Credits
2	Net rental real estate income (loss)		
3	Other net rental income (loss)	16	Foreign transactions
4	Guaranteed payments 800,000		
5	Interest income 400		
6a	Ordinary dividends		
6b	Qualified dividends		
7	Royalties		
8	Net short-term capital gain (loss) -5,000		
9a	Net long-term capital gain (loss) 6,000	17	Alternative minimum tax (AMT) items
9b	Collectibles (28%) gain (loss)		
9c	Unrecaptured section 1250 gain		
10	Net section 1231 gain (loss)	18	Tax-exempt income and nondeductible expenses
11	Other income (loss)	A	800
		C	25,000
		19	Distributions
12	Section 179 deduction 5,000	A	250,000
13	Other deductions	20	Other information
A	7,000	A	400
14	Self-employment earnings (loss)		
A	1,044,800		
C	1,200,000		

*See attached statement for additional information.

For IRS Use Only

For Paperwork Reduction Act Notice, see Instructions for Form 1065. IRS.gov/form1065 Schedule K-1 (Form 1065) 2015
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Ryan Ross 111-11-1112

K-1 Statement (Sch K-1, Form 1065)

Line 13 - Deductions

A	Code A - Cash contributions (50%)	**A**	7,000

Line 14 - Self-Employment

A	Code A - Net earnings (loss) from self-employment	**A**	1,044,800
C	Code C - Gross non-farm income	**C**	1,200,000

Line 18 - Tax-Exempt Income and Nondeductible Expenses

A	Code A - Tax-exempt interest income	**A**	800
C	Code C - Nondeductible expenses	**C**	25,000

Line 19 - Distributions

A	Code A - Cash and marketable securities	**A**	250,000

Line 20 - Other Information

A	Code A - Investment income	**A**	400

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Form **4562**

Department of the Treasury
Internal Revenue Service (99)

Depreciation and Amortization
(Including Information on Listed Property)

▶ Attach to your tax return.
▶ Information about Form 4562 and its separate instructions is at *www.irs.gov/form4562*.

OMB No. 1545-0172
2015
Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
ROCK the Ages LLC	1065 - Musican Agents/Mgrs	55-5555555

Part I Election To Expense Certain Property Under Section 179

Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	500,000
2	Total cost of section 179 property placed in service (see instructions)	2	20,000
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	2,000,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	0
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	500,000

6 (a) Description of property	(b) Cost (business use only)	(c) Elected cost
Furniture and Fixtures	20,000	20,000

7	Listed property. Enter the amount from line 29	7		
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8		20,000
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9		20,000
10	Carryover of disallowed deduction from line 13 of your 2014 Form 4562.	10		
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11		500,000
12	Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12		20,000
13	Carryover of disallowed deduction to 2016. Add lines 9 and 10, less line 12 ▶	13	0	

Note: Do not use Part II or Part III below for listed property. Instead, use Part V.

Part II Special Depreciation Allowance and Other Depreciation (Do not include listed property.) (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III MACRS Depreciation (Do not include listed property.) (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2015	17	
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B - Assets Placed in Service During 2015 Tax Year Using the General Depreciation System

	(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19	a 3-year property						
	b 5-year property						
	c 7-year property						
	d 10-year property						
	e 15-year property						
	f 20-year property						
	g 25-year property			25 yrs.		S/L	
	h Residential rental property			27.5 yrs.	MM	S/L	
				27.5 yrs.	MM	S/L	
	i Nonresidential real property			39 yrs.	MM	S/L	
					MM	S/L	

Section C - Assets Placed in Service During 2015 Tax Year Using the Alternative Depreciation System

20	a Class life					S/L	
	b 12-year			12 yrs.		S/L	
	c 40-year			40 yrs.	MM	S/L	

Part IV Summary (See instructions.)

21	Listed property. Enter amount from line 28	21	
22	**Total.** Add amounts from line 12, lines 14 through 17, lines 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	0
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

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ROCK the Ages LLC 55-5555555

Line 15 (1065) - Interest Expense

1	Interest expense on line of credit	1	10,000
2	Total interest expense	2	10,000

Line 20 (1065) - Other Deductions

1	Travel, Meals and Entertainment				
	a Travel			1a	320,000
	b Meals and entertainment, subject to 50% limit	1b	200,000		
	d Less disallowed	1d	100,000		
	e Subtract line d from lines b and c			1e	100,000
2	Insurance			2	52,000
3	Laundry and cleaning			3	132,000
4	Office expenses			4	200,000
5	Utilities			5	54,800
6	Advertising			6	380,000
7	Total other deductions			7	1,238,800

Line 13a, Sch K (1065) - Contributions

A	Code A - Cash contributions (50%)	A	28,000
	Total contributions	13a	28,000

Line 8, Sch L (1065) - Other Investments

			Beginning		Ending
1	Marketable Securities	1	436,000		300,000
2	Total other investments	2	436,000		300,000

Line 17, Sch L (1065) - Other Current Liabilities

			Beginning		Ending
1	Operating Line of Credit	1	200,000		160,000
2	Total other current liabilities	2	200,000		160,000

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ROCK the Ages LLC 55-5555555

Line 9 (1065) - Salaries and Wages

1	Salaries	1	1,000,000	
2	Wages	2		
3		3		
4	Total salaries and wages			4 1,000,000
	Salaries and wages reported elsewhere on return:			
5	Amounts included in Cost of Goods Sold	5	0	
6	Elective contributions to a section 401(k) cash or deferred arrangement, or amounts contributed under a salary reductions SEP agreement or a SIMPLE IRA plan	6		
7	Total salaries and wages reported elsewhere on return			7 0
	Less employment credits:			
8	From Form 5884 - Work Opportunity Credit	8	0	
9	From Form 8844 - Empowerment Zone Employment Credit	9		
10	From Form 8845 - Indian Employment Credit	10	0	
11		11		
12		12		
13		13		
14	Total employment credits			14 0
15	Reduction of expenses for offsetting credits			15
16	Total salaries and wages less employment credits and expense reductions			16 1,000,000

Line 10 (1065) - Guaranteed Payments to Partners

1	Guaranteed payments to partners	1	1,400,000
2	Medical insurance payments for partners, partners' spouses or dependents	2	
3		3	
4		4	
5	Total guaranteed payments to partners	5	1,400,000

Line 14 (1065) - Taxes and Licenses

1	Payroll tax	1	92,000
2	Sub Total	2	92,000
3	Total taxes and licenses	3	92,000

Lines 5, 6a and 6b, Sch K (1065) - Interest and Dividends

Interest income (line 5)

1	Bank	1	1,600
2	Total interest income	2	1,600

Line 18c, Sch K (1065) - Nondeductible Expenses

C	Code C - Nondeductible expenses		
	Nondeductible portion of meals, travel and entertainment expenses		100,000
	Total nondeductible expenses	18c	100,000

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PROBLEM 6 SOLUTIONS

Form **1120S**

Department of the Treasury
Internal Revenue Service

U.S. Income Tax Return for an S Corporation

▶ **Do not file this form unless the corporation has filed or is attaching Form 2553 to elect to be an S corporation.**

▶ **Information about Form 1120S and its separate instructions is at *www.irs.gov/form1120s.***

OMB No. 1545-0123

2015

For calendar year 2015 or tax year beginning , ending

A S election effective date: 1/15/2009	Name: Premium, Inc.	**D** Employer identification number: 11-1111111
B Business activity code number (see instructions): 311300	TYPE OR PRINT — Number, street, and room or suite no. If a P.O. box, see instructions.: 1005 16th Street	**E** Date incorporated: 1/15/2009
C Check if Sch. M-3 attached ☐	City or town: Cut and Shoot; State: TX; ZIP code: 77303	**F** Total assets (see instructions): $ 844,422
	Foreign country name; Foreign province/state/county; Foreign postal code	

G Is the corporation electing to be an S corporation beginning with this tax year? ☐ Yes ☐ No If "Yes," attach Form 2553 if not already filed

H Check if: **(1)** ☐ Final return **(2)** ☐ Name change **(3)** ☒ Address change **(4)** ☐ Amended return **(5)** ☐ S election termination or revocation

I Enter the number of shareholders who were shareholders during any part of the tax year ▶ 2

Caution: Include **only** trade or business income and expenses on lines 1a through 21. See the instructions for more information.

Income	1a	Gross receipts or sales	1a	2,410,000	
	b	Returns and allowances	1b		
	c	Balance. Subtract line 1b from line 1a		1c	2,410,000
	2	Cost of goods sold (attach Form 1125-A)		2	736,741
	3	Gross profit. Subtract line 2 from line 1c		3	1,673,259
	4	Net gain (loss) from Form 4797, line 17 (attach Form 4797)		4	
	5	Other income (loss) (see instructions—attach statement)		5	
	6	**Total income (loss).** Add lines 3 through 5 ▶		6	1,673,259
Deductions (see instructions for limitations)	7	Compensation of officers (see instructions — attach Form 1125-E)		7	150,000
	8	Salaries and wages (less employment credits)		8	442,103
	9	Repairs and maintenance		9	206,106
	10	Bad debts		10	
	11	Rents		11	40,000
	12	Taxes and licenses		12	65,101
	13	Interest		13	35,222
	14	Depreciation not claimed on Form 1125-A or elsewhere on return (attach Form 4562)		14	15,254
	15	Depletion **(Do not deduct oil and gas depletion.)**		15	
	16	Advertising		16	20,000
	17	Pension, profit-sharing, etc., plans		17	
	18	Employee benefit programs		18	
	19	Other deductions (attach statement)		19	59,899
	20	**Total deductions.** Add lines 7 through 19 ▶		20	1,033,685
	21	**Ordinary business income (loss).** Subtract line 20 from line 6		21	639,574
Tax and Payments	22a	Excess net passive income or LIFO recapture tax (see instructions)	22a		
	b	Tax from Schedule D (Form 1120S)	22b		
	c	Add lines 22a and 22b (see instructions for additional taxes)		22c	0
	23a	2015 estimated tax payments and 2014 overpayment credited to 2015	23a		
	b	Tax deposited with Form 7004	23b		
	c	Credit for federal tax paid on fuels (attach Form 4136)	23c		
	d	Add lines 23a through 23c		23d	0
	24	Estimated tax penalty (see instructions). Check if Form 2220 is attached ▶ ☐		24	
	25	**Amount owed.** If line 23d is smaller than the total of lines 22c and 24, enter amount owed		25	0
	26	**Overpayment.** If line 23d is larger than the total of lines 22c and 24, enter amount overpaid		26	0
	27	Enter amount from line 26 **Credited to 2016 estimated tax** ▶ **Refunded** ▶		27	0

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

▶ Signature of officer — Date — ▶ Title

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature: SELF-PREPARED RETURN	Date	Check ☐ if self-employed / PTIN
Firm's name ▶			Firm's EIN ▶
Firm's address ▶			Phone no.
City	State		ZIP code

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Form 1120S (2015) Premium, Inc. 11-1111111 Page 2

Schedule B Other Information (see instructions)

		Yes	No
1	Check accounting method: a ☐ Cash b ☒ Accrual c ☐ Other (specify) ▶		
2	See the instructions and enter the: a Business activity ▶ Food Processing b Product or service ▶ Candy		
3	At any time during the tax year, was any shareholder of the corporation a disregarded entity, a trust, an estate, or a nominee or similar person? If "Yes," attach Schedule B-1, Information on Certain Shareholders of an S Corporation		X
4	At the end of the tax year, did the corporation:		
a	Own directly 20% or more, or own, directly or indirectly, 50% or more of the total stock issued and outstanding of any foreign or domestic corporation? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (v) below		X

(i) Name of Corporation	(ii) Employer Identification Number (if any)	(iii) Country of Incorporation	(iv) Percentage of Stock Owned	(v) If Percentage in (iv) is 100%, Enter the Date (if any) a Qualified Subchapter S Subsidiary Election Was Made

b	Own directly an interest of 20% or more, or own, directly or indirectly, an interest of 50% or more in the profit, loss, or capital in any foreign or domestic partnership (including an entity treated as a partnership) or in the beneficial interest of a trust? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (v) below		X

(i) Name of Entity	(ii) Employer Identification Number (if any)	(iii) Type of Entity	(iv) Country of Organization	(v) Maximum Percentage Owned in Profit, Loss, or Capital

5 a	At the end of the tax year, did the corporation have any outstanding shares of restricted stock? If "Yes," complete lines (i) and (ii) below.		X
	(i) Total shares of restricted stock ▶		
	(ii) Total shares of non-restricted stock ▶		
b	At the end of the tax year, did the corporation have any outstanding stock options, warrants, or similar instruments? If "Yes," complete lines (i) and (ii) below.		X
	(i) Total shares of stock outstanding at the end of the tax year ▶		
	(ii) Total shares of stock outstanding if all instruments were executed ▶		
6	Has this corporation filed, or is it required to file, **Form 8918,** Material Advisor Disclosure Statement, to provide information on any reportable transaction?		X
7	Check this box if the corporation issued publicly offered debt instruments with original issue discount ▶ ☐ If checked, the corporation may have to file **Form 8281,** Information Return for Publicly Offered Original Issue Discount Instruments.		
8	If the corporation: **(a)** was a C corporation before it elected to be an S corporation **or** the corporation acquired an asset with a basis determined by reference to the basis of the asset (or the basis of any other property) in the hands of a C corporation **and (b)** has net unrealized built-in gain in excess of the net recognized built-in gain from prior years, enter the net unrealized built-in gain reduced by net recognized built-in gain from prior years (see instructions) ▶ $		
9	Enter the accumulated earnings and profits of the corporation at the end of the tax year. $		
10	Does the corporation satisfy **both** of the following conditions?		
a	The corporation's total receipts (see instructions) for the tax year were less than $250,000		X
b	The corporation's total assets at the end of the tax year were less than $250,000		X
	If "Yes," the corporation is not required to complete Schedules L and M-1.		
11	During the tax year, did the corporation have any non-shareholder debt that was canceled, was forgiven, or had the terms modified so as to reduce the principal amount of the debt?		X
	If "Yes," enter the amount of principal reduction $		
12	During the tax year, was a qualified subchapter S subsidiary election terminated or revoked? If "Yes," see instructions		X
13 a	Did the corporation make any payments in 2015 that would require it to file Form(s) 1099?	X	
b	If "Yes," did the corporation file or will it file required Forms 1099?	X	

Form **1120S** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 1120S (2015) Premium, Inc. 11-1111111 Page 3

Schedule K	Shareholders' Pro Rata Share Items		Total amount
Income (Loss)	1 Ordinary business income (loss) (page 1, line 21)	1	639,574
	2 Net rental real estate income (loss) (attach Form 8825)	2	
	3a Other gross rental income (loss) 3a		
	b Expenses from other rental activities (attach statement) 3b		
	c Other net rental income (loss). Subtract line 3b from line 3a	3c	0
	4 Interest income	4	100,000
	5 Dividends: a Ordinary dividends	5a	
	b Qualified dividends 5b		
	6 Royalties.	6	
	7 Net short-term capital gain (loss) (attach Schedule D (Form 1120S))	7	
	8a Net long-term capital gain (loss) (attach Schedule D (Form 1120S))	8a	
	b Collectibles (28%) gain (loss) 8b		
	c Unrecaptured section 1250 gain (attach statement) 8c		
	9 Net section 1231 gain (loss) (attach Form 4797)	9	
	10 Other income (loss) (see instructions) Type ▶	10	
Deductions	11 Section 179 deduction (attach Form 4562)	11	
	12a Charitable contributions	12a	20,000
	b Investment interest expense	12b	
	c Section 59(e)(2) expenditures (1) Type ▶ (2) Amount ▶	12c(2)	
	d Other deductions (see instructions) Type ▶	12d	
Credits	13a Low-income housing credit (section 42(j)(5))	13a	
	b Low-income housing credit (other)	13b	
	c Qualified rehabilitation expenditures (rental real estate) (attach Form 3468, if applicable)	13c	
	d Other rental real estate credits (see instructions) Type ▶	13d	
	e Other rental credits (see instructions) Type ▶	13e	
	f Biofuel producer credit (attach Form 6478)	13f	
	g Other credits (see instructions) Type ▶	13g	
Foreign Transactions	14a Name of country or U.S. possession ▶		
	b Gross income from all sources	14b	
	c Gross income sourced at shareholder level	14c	
	Foreign gross income sourced at corporate level		
	d Passive category	14d	
	e General category	14e	
	f Other (attach statement)	14f	
	Deductions allocated and apportioned at shareholder level		
	g Interest expense	14g	
	h Other	14h	
	Deductions allocated and apportioned at corporate level to foreign source income		
	i Passive category	14i	
	j General category	14j	
	k Other (attach statement)	14k	
	Other information		
	l Total foreign taxes (check one): ▶ ☐ Paid ☐ Accrued	14l	
	m Reduction in taxes available for credit (attach statement)	14m	
	n Other foreign tax information (attach statement)		
Alternative Minimum Tax (AMT) Items	15a Post-1986 depreciation adjustment	15a	
	b Adjusted gain or loss	15b	
	c Depletion (other than oil and gas)	15c	
	d Oil, gas, and geothermal properties—gross income	15d	
	e Oil, gas, and geothermal properties—deductions	15e	
	f Other AMT items (attach statement)	15f	
Items Affecting Shareholder Basis	16a Tax-exempt interest income	16a	
	b Other tax-exempt income	16b	
	c Nondeductible expenses	16c	15,000
	d Distributions (attach statement if required) (see instructions)	16d	100,000
	e Repayment of loans from shareholders	16e	

Form 1120S (2015)

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Form 1120S (2015) Premium, Inc. 11-1111111 Page **4**

Schedule K	Shareholders' Pro Rata Share Items (continued)		Total amount
Other Information	17a Investment income	17a	100,000
	b Investment expenses	17b	
	c Dividend distributions paid from accumulated earnings and profits	17c	
	d Other items and amounts (attach statement)		
Reconciliation	18 **Income/loss reconciliation.** Combine the amounts on lines 1 through 10 in the far right column. From the result, subtract the sum of the amounts on lines 11 through 12d and 14l	18	719,574

Schedule L Balance Sheets per Books	Beginning of tax year		End of tax year	
Assets	(a)	(b)	(c)	(d)
1 Cash		47,840		612,410
2a Trade notes and accounts receivable	93,100		123,104	
b Less allowance for bad debts		93,100		123,104
3 Inventories		9,607		3,467
4 U.S. government obligations				
5 Tax-exempt securities (see instructions)				
6 Other current assets (attach statement)		8,333		17,582
7 Loans to shareholders				
8 Mortgage and real estate loans				
9 Other investments (attach statement)				
10a Buildings and other depreciable assets	138,203		185,348	
b Less accumulated depreciation	84,235	53,968	99,489	85,859
11a Depletable assets				
b Less accumulated depletion		0		0
12 Land (net of any amortization)		2,000		2,000
13a Intangible assets (amortizable only)				
b Less accumulated amortization		0		0
14 Other assets (attach statement)				
15 Total assets		214,848		844,422
Liabilities and Shareholders' Equity				
16 Accounts payable		42,500		72,300
17 Mortgages, notes, bonds payable in less than 1 year		4,500		2,100
18 Other current liabilities (attach statement)				
19 Loans from shareholders				
20 Mortgages, notes, bonds payable in 1 year or more		26,700		24,300
21 Other liabilities (attach statement)				
22 Capital stock		30,000		30,000
23 Additional paid-in capital				
24 Retained earnings		111,148		715,722
25 Adjustments to shareholders' equity (attach statement)				
26 Less cost of treasury stock				
27 Total liabilities and shareholders' equity		214,848		844,422

Form **1120S** (2015)

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Form 1120S (2015) Premium, Inc. 11-1111111 Page **5**

Schedule M-1 **Reconciliation of Income (Loss) per Books With Income (Loss) per Return**

Note: The corporation may be required to file Schedule M-3 (see instructions)

1	Net income (loss) per books	704,574	5	Income recorded on books this year not included on Schedule K, lines 1 through 10 (itemize):	
2	Income included on Schedule K, lines 1, 2, 3c, 4, 5a, 6, 7, 8a, 9, and 10, not recorded on books this year (itemize):		a	Tax-exempt interest $	0
3	Expenses recorded on books this year not included on Schedule K, lines 1 through 12 and 14l (itemize):		6	Deductions included on Schedule K, lines 1 through 12 and 14l, not charged against book income this year (itemize):	
a	Depreciation $		a	Depreciation $	0
b	Travel and entertainment $				
	Payroll Penalties 15,000	15,000	7	Add lines 5 and 6	0
4	Add lines 1 through 3	719,574	8	Income (loss) (Schedule K, line 18). Line 4 less line 7	719,574

Schedule M-2 **Analysis of Accumulated Adjustments Account, Other Adjustments Account, and Shareholders' Undistributed Taxable Income Previously Taxed** (see instructions)

		(a) Accumulated adjustments account	(b) Other adjustments account	(c) Shareholders' undistributed taxable income previously taxed
1	Balance at beginning of tax year	111,148		
2	Ordinary income from page 1, line 21	639,574		
3	Other additions	100,000		
4	Loss from page 1, line 21			
5	Other reductions	35,000		
6	Combine lines 1 through 5	815,722	0	0
7	Distributions other than dividend distributions	100,000		
8	Balance at end of tax year. Subtract line 7 from line 6	715,722	0	0

Form **1120S** (2015)

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671113

☐ Final K-1 ☐ Amended K-1 OMB No. 1545-0123

Schedule K-1 (Form 1120S)
Department of the Treasury
Internal Revenue Service

2015

For calendar year 2015, or tax year beginning _____, 2015
ending _____, 20____

Shareholder's Share of Income, Deductions, Credits, etc.
▶ See back of form and separate instructions.

Part I Information About the Corporation

A Corporation's employer identification number
11-1111111

B Corporation's name, address, city, state, and ZIP code
Premium, Inc.
1005 16th Street
Cut and Shoot, TX 77303

C IRS Center where corporation filed return
e-file

Part II Information About the Shareholder

D Shareholder's identifying number Shareholder: 1
123-45-6781

E Shareholder's name, address, city, state, and ZIP code
John Parsons
5607 20th Street
Cut and Shoot, TX 77303

F Shareholder's percentage of stock ownership for tax year 70.000000%

For IRS Use Only

Part III Shareholder's Share of Current Year Income, Deductions, Credits, and Other Items

1	Ordinary business income (loss) 447,702	13	Credits
2	Net rental real estate income (loss)		
3	Other net rental income (loss)		
4	Interest income 70,000		
5a	Ordinary dividends		
5b	Qualified dividends	14	Foreign transactions
6	Royalties		
7	Net short-term capital gain (loss)		
8a	Net long-term capital gain (loss)		
8b	Collectibles (28%) gain (loss)		
8c	Unrecaptured section 1250 gain		
9	Net section 1231 gain (loss)		
10	Other income (loss)	15	Alternative minimum tax (AMT) items
11	Section 179 deduction	16	Items affecting shareholder basis
		C	10,500
12	Other deductions		
A	14,000	D	70,000
		17	Other information
		A	70,000

* See attached statement for additional information.

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John Parsons 123-45-6781

K-1 Statement (Sch K-1, Form 1120S)

Line 12 - Deductions

A	Code A - Cash contributions (50%)	**A**	14,000

Line 16 - Items affecting shareholder basis

C	Code C - Nondeductible expenses	**C**	10,500
D	Code D - Distributions	**D**	70,000

Line 17 - Other Information

A	Code A - Investment income	**A**	70,000

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671113

☐ Final K-1 ☐ Amended K-1 OMB No. 1545-0123

Schedule K-1 (Form 1120S)
Department of the Treasury
Internal Revenue Service

2015

For calendar year 2015, or tax year beginning _____, 2015 ending _____, 20_____

Shareholder's Share of Income, Deductions, Credits, etc. ▶ See back of form and separate instructions.

Part I Information About the Corporation

A Corporation's employer identification number
11-1111111

B Corporation's name, address, city, state, and ZIP code

Premium, Inc.
1005 16th Street
Cut and Shoot, TX 77303

C IRS Center where corporation filed return
e-file

Part II Information About the Shareholder

D Shareholder's identifying number Shareholder: 2
123-45-6782

E Shareholder's name, address, city, state, and ZIP code

George Smith
5607 20th Street
Cut and Shoot, TX 77303

F Shareholder's percentage of stock ownership for tax year 30.000000%

For IRS Use Only

Part III Shareholder's Share of Current Year Income, Deductions, Credits, and Other Items

1	Ordinary business income (loss) 191,872	13	Credits
2	Net rental real estate income (loss)		
3	Other net rental income (loss)		
4	Interest income 30,000		
5a	Ordinary dividends		
5b	Qualified dividends	14	Foreign transactions
6	Royalties		
7	Net short-term capital gain (loss)		
8a	Net long-term capital gain (loss)		
8b	Collectibles (28%) gain (loss)		
8c	Unrecaptured section 1250 gain		
9	Net section 1231 gain (loss)		
10	Other income (loss)	15	Alternative minimum tax (AMT) items
11	Section 179 deduction	16	Items affecting shareholder basis C 4,500
12	Other deductions A 6,000	D	30,000
		17	Other information A 30,000

* See attached statement for additional information.

For Paperwork Reduction Act Notice, see Instructions for Form 1120S. IRS.gov/form1120s **Schedule K-1 (Form 1120S) 2015**
HTA

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George Smith 123-45-6782

K-1 Statement (Sch K-1, Form 1120S)

Line 12 - Deductions

A	Code A - Cash contributions (50%)	**A**	6,000

Line 16 - Items affecting shareholder basis

C	Code C - Nondeductible expenses	**C**	4,500
D	Code D - Distributions	**D**	30,000

Line 17 - Other Information

A	Code A - Investment income	**A**	30,000

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Form **1125-A**
(Rev. December 2012)
Department of the Treasury
Internal Revenue Service

Cost of Goods Sold

▶ **Attach to Form 1120, 1120-C, 1120-F, 1120S, 1065, or 1065-B.**
▶ **Information about Form 1125-A and its instructions is at *www.irs.gov/form1125a*.**

OMB No. 1545-2225

Name	Employer identification number
Premium, Inc.	11-1111111

1	Inventory at beginning of year	1	9,607	
2	Purchases	2	278,143	
3	Cost of labor	3	203,102	
4	Additional section 263A costs (attach schedule)	4		
5	Other costs (attach schedule)	5	249,356	
6	**Total.** Add lines 1 through 5	6	740,208	
7	Inventory at end of year	7	3,467	
8	**Cost of goods sold.** Subtract line 7 from line 6. Enter here and on Form 1120, page 1, line 2 or the appropriate line of your tax return (see instructions)	8	736,741	

9 a Check all methods used for valuing closing inventory:
- *(i)* [X] Cost
- *(ii)* [ ] Lower of cost or market
- *(iii)* [ ] Other (Specify method used and attach explanation.) ▶

b Check if there was a writedown of subnormal goods ▶ [ ]

c Check if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970) ▶ [ ]

d If the LIFO inventory method was used for this tax year, enter amount of closing inventory computed under LIFO — 9d

e If property is produced or acquired for resale, do the rules of section 263A apply to the entity (see instructions)? [ ] Yes [ ] No

f Was there any change in determining quantities, cost, or valuations between opening and closing inventory? If "Yes," attach explanation [ ] Yes [ ] No

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Premium, Inc. 11-1111111

Line 19 (1120S) - Other Deductions

1	Other Deductions	1	59,899
2	Total other deductions	2	59,899

Line 12a, Sch K (1120S) - Contributions

A	Code A - Cash contributions (50%)	A	20,000
	Total contributions	12a	20,000

Line 16d, Schedule K (1120S) - Distributions

A.	Cash	100,000

B. Property

Description	Date Acquired	Date Distributed	FMV on date of distribution	Basis in property

	Total property	0
C.	Other	
	Total distributions	100,000

Line 6, Sch L (1120S) - Other Current Assets

			Beginning		End
1	Prepaid expenses	1	8,333		17,582
2	Total other current assets	2	8,333		17,582

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PROBLEM 7 SOLUTIONS

A summary of the determination of the gift tax liability appears below.

	James	Ella
Condominium in Conroe	$1,900,000	$1,900,000
Office building in Round Rock	2,300,000	2,300,000
Vacation home in Bandera	1,300,000	1,300,000
Father's bypass operation(1)	41,000	41,000
Daughter's wedding(2)	–0–	–0–
Graduation present(3)	21,000	21,000
Total gifts for 2015	$5,562,000	$5,562,000
Less annual exclusion (5 × $14,000)	(70,000)	(70,000)
Taxable gifts for 2015	$5,492,000	$5,492,000
Add prior taxable gifts	–0–	–0–
Total of current and prior taxable gifts	$5,492,000	$5,492,000
Tax on current and past taxable gifts— $345,800 + 40%($5,492,000 – $1,000,000)	$2,142,600	$2,142,600
Less: Unified transfer tax credit for 2015	(2,117,800)	(2,117,800)
Gift tax due for 2015	$ 24,800	$ 24,800

FOOTNOTES

(1) No taxable gift would have resulted had the providers of the medical care (e.g., physicians, hospital) been paid directly [§ 2503(e)(2)(B)].

(2) Paying for a child's wedding constitutes satisfying an obligation of support and is not a gift.

(3) The niece is not a dependent of the Polks. Thus, the obligation of support (see Footnote 2) does not exist.

Completed Forms 709 for the Polks follow.

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Form **709**

Department of the Treasury
Internal Revenue Service

United States Gift (and Generation-Skipping Transfer) Tax Return

▶ Information about Form 709 and its separate instructions is at *www.irs.gov/form709*.

(For gifts made during calendar year 2015)
▶ See instructions.

OMB No. 1545-0020

2015

1 Donor's first name and middle initial	2 Donor's last name	3 Donor's social security number
James A.	Polk	123-45-6789

4 Address (number, street, and apartment number)	5 Legal residence (domicile)
13319 Taylorcrest Street	USA
6 City or town, state or province, country, and ZIP or foreign postal code	**7** Citizenship (see instructions)
Houston, TX 77079	USA

Part 1—General Information

		Yes	No
8	If the donor died during the year, check here ▶ ☐ and enter date of death _____, _____.		
9	If you extended the time to file this Form 709, check here ▶ ☐		
10	Enter the total number of donees listed on Schedule A. Count each person only once ▶		
11a	Have you (the donor) previously filed a Form 709 (or 709-A) for any other year? If "No," skip line 11b		✓
b	Has your address changed since you last filed Form 709 (or 709-A)?		
12	**Gifts by husband or wife to third parties.** Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (see instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. **If the answer is "No," skip lines 13–18.**)	✓	
13	Name of consenting spouse **Ellen R. Polk** **14** SSN **123-45-6788**		
15	Were you married to one another during the entire calendar year? (see instructions)	✓	
16	If 15 is "No," check whether ☐ married ☐ divorced or ☐ widowed/deceased, and give date (see instructions) ▶		
17	Will a gift tax return for this year be filed by your spouse? (If "Yes," mail both returns in the same envelope.)	✓	
18	**Consent of Spouse.** I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.		
	Consenting spouse's signature ▶ **Date ▶**		
19	Have you applied a DSUE amount received from a predeceased spouse to a gift or gifts reported on this or a previous Form 709? If "Yes," complete Schedule C		

Part 2—Tax Computation

1	Enter the amount from Schedule A, Part 4, line 11	1	5,492,000
2	Enter the amount from Schedule B, line 3	2	
3	Total taxable gifts. Add lines 1 and 2	3	5,492,000
4	Tax computed on amount on line 3 (see *Table for Computing Gift Tax* in instructions)	4	2,142,600
5	Tax computed on amount on line 2 (see *Table for Computing Gift Tax* in instructions)	5	
6	Balance. Subtract line 5 from line 4	6	2,142,600
7	Applicable credit amount. If donor has DSUE amount from predeceased spouse(s), enter amount from Schedule C, line 4; otherwise, see instructions	7	2,117,800
8	Enter the applicable credit against tax allowable for all prior periods (from Sch. B, line 1, col. C)	8	
9	Balance. Subtract line 8 from line 7. Do not enter less than zero	9	2,117,800
10	Enter 20% (.20) of the amount allowed as a specific exemption for gifts made after September 8, 1976, and before January 1, 1977 (see instructions)	10	
11	Balance. Subtract line 10 from line 9. Do not enter less than zero	11	2,117,800
12	Applicable credit. Enter the smaller of line 6 or line 11	12	2,117,800
13	Credit for foreign gift taxes (see instructions)	13	
14	Total credits. Add lines 12 and 13	14	2,117,800
15	Balance. Subtract line 14 from line 6. Do not enter less than zero	15	24,800
16	Generation-skipping transfer taxes (from Schedule D, Part 3, col. H, Total)	16	
17	Total tax. Add lines 15 and 16	17	24,800
18	Gift and generation-skipping transfer taxes prepaid with extension of time to file	18	
19	If line 18 is less than line 17, enter **balance due** (see instructions)	19	24,800
20	If line 18 is greater than line 17, enter **amount to be refunded**	20	

Attach check or money order here.

Sign Here

Under penalties of perjury, I declare that I have examined this return, including any accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than donor) is based on all information of which preparer has any knowledge.

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Signature of donor _____ Date _____

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see the instructions for this form. Cat. No. 16783M Form **709** (2015)

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Form 709 (2015) Page **2**

SCHEDULE A **Computation of Taxable Gifts** (Including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation . . . . . Yes ☐ No ☐

B ☐ ◄ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1—Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusions. (see instructions)

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1	**Condo in Conroe to children**		1,200,000	2015	1,900,000	950,000	950,000
	Office building in Round Rock to children		1,800,000	2015	2,300,000	1,150,000	1,150,000
	Vacation home to children		900,000	2015	2,600,000	1,300,000	1,300,000
	BMW automobile to niece		42,000	2015	42,000	21,000	21,000
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							
	Condo in Conroe to children		1,200,000	2015	1,900,000	950,000	950,000
	Office building in Round Rock to children		900,000	2015	2,300,000	1,150,000	1,150,000
	Reimbursement of expenses for father		82,000	2015	82,000	41,000	41,000

Total of Part 1. Add amounts from Part 1, column H . . . . . ► **5,562,000**

Part 2—Direct Skips. Gifts that are direct skips and are subject to both gift tax and generation-skipping transfer tax. You must list the gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(b) election out	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1							
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							

Total of Part 2. Add amounts from Part 2, column H . . . . . ►

Part 3—Indirect Skips. Gifts to trusts that are currently subject to gift tax and may later be subject to generation-skipping transfer tax. You must list these gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(c) election	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1							
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							

Total of Part 3. Add amounts from Part 3, column H . . . . . ►

(If more space is needed, attach additional statements.) Form **709** (2015)

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Form 709 (2015) Page 3

Part 4—Taxable Gift Reconciliation

1	Total value of gifts of donor. Add totals from column H of Parts 1, 2, and 3		1	5,562,000	
2	Total annual exclusions for gifts listed on line 1 (see instructions)		2	70,000	
3	Total included amount of gifts. Subtract line 2 from line 1		3	5,492,000	
Deductions (see instructions)					
4	Gifts of interests to spouse for which a marital deduction will be claimed, based on item numbers _____ of Schedule A	4			
5	Exclusions attributable to gifts on line 4	5			
6	Marital deduction. Subtract line 5 from line 4	6			
7	Charitable deduction, based on item nos. _____ less exclusions	7			
8	Total deductions. Add lines 6 and 7		8		
9	Subtract line 8 from line 3		9	5,492,000	
10	Generation-skipping transfer taxes payable with this Form 709 (from Schedule D, Part 3, col. H, Total)		10		
11	**Taxable gifts.** Add lines 9 and 10. Enter here and on page 1, Part 2—Tax Computation, line 1		11	5,492,000	

Terminable Interest (QTIP) Marital Deduction. (see instructions for Schedule A, Part 4, line 4)

If a trust (or other property) meets the requirements of qualified terminable interest property under section 2523(f), and:

a. The trust (or other property) is listed on Schedule A, and

b. The value of the trust (or other property) is entered in whole or in part as a deduction on Schedule A, Part 4, line 4,

then the donor shall be deemed to have made an election to have such trust (or other property) treated as qualified terminable interest property under section 2523(f).

If less than the entire value of the trust (or other property) that the donor has included in Parts 1 and 3 of Schedule A is entered as a deduction on line 4, the donor shall be considered to have made an election only as to a fraction of the trust (or other property). The numerator of this fraction is equal to the amount of the trust (or other property) deducted on Schedule A, Part 4, line 6. The denominator is equal to the total value of the trust (or other property) listed in Parts 1 and 3 of Schedule A.

If you make the QTIP election, the terminable interest property involved will be included in your spouse's gross estate upon his or her death (section 2044). See instructions for line 4 of Schedule A. If your spouse disposes (by gift or otherwise) of all or part of the qualifying life income interest, he or she will be considered to have made a transfer of the entire property that is subject to the gift tax. See *Transfer of Certain Life Estates Received From Spouse* in the instructions.

12 Election Out of QTIP Treatment of Annuities

☐ ◀Check here if you elect under section 2523(f)(6) **not** to treat as qualified terminable interest property any joint and survivor annuities that are reported on Schedule A and would otherwise be treated as qualified terminable interest property under section 2523(f). See instructions. Enter the item numbers from Schedule A for the annuities for which you are making this election ▶ _____

SCHEDULE B Gifts From Prior Periods

If you answered "Yes," on line 11a of page 1, Part 1, see the instructions for completing Schedule B. If you answered "No," skip to the Tax Computation on page 1 (or Schedules C or D, if applicable). Complete Schedule A before beginning Schedule B. See instructions for recalculation of the column C amounts. Attach calculations.

A Calendar year or calendar quarter (see instructions)	B Internal Revenue office where prior return was filed	C Amount of applicable credit (unified credit) against gift tax for periods after December 31, 1976	D Amount of specific exemption for prior periods ending before January 1, 1977	E Amount of taxable gifts
1 Totals for prior periods	1			

2	Amount, if any, by which total specific exemption, line 1, column D is more than $30,000	2	
3	Total amount of taxable gifts for prior periods. Add amount on line 1, column E and amount, if any, on line 2. Enter here and on page 1, Part 2—Tax Computation, line 2	3	

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James A. Polk — 123-45-6789

Schedule A – Form 709, page 2 –Tax Year 2015

Part 1: Gifts made by taxpayer

A	B	C	D	E	F	G	H
1	Benjamin, Michael, Olivia Polk; children; condo; Conroe (TX)		1,200,000	2015	1,900,000	950,000	950,000
2	Benjamin, Michael, Olivia Polk; children; office building; Round Rock (TX)		1,800,000	2015	2,300,000	1,150,000	1,150,000
3	Benjamin, Michael, Olivia Polk; children; vacation home; Bandera (TX)		900,000	2015	2,600,000	1,300,000	1,300,000
4	Carol Polk; niece; BMW auto		42,000	2015	42,000	21,000	21,000

Part 1: Gifts made by spouse

5	Benjamin, Michael, Olivia Polk; children; condo; Conroe (TX)		1,200,000	2015	1,900,000	950,000	950,000
6	Benjamin, Michael, Olivia Polk; children; office building; Round Rock (TX)		1,800,000	2015	2,300,000	1,150,000	1,150,000
7	Alan Roberts; father; reimbursement for expenses	8	42,000	2015	82,000	41,000	41,000

Total of Part 1	**5,562,000**

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Form **709**

Department of the Treasury
Internal Revenue Service

United States Gift (and Generation-Skipping Transfer) Tax Return

▶ Information about Form 709 and its separate instructions is at *www.irs.gov/form709*.

(For gifts made during calendar year 2015)
▶ See instructions.

OMB No. 1545-0020

2015

1 Donor's first name and middle initial	2 Donor's last name	3 Donor's social security number
Ella R.	Polk	123-45-6788
4 Address (number, street, and apartment number)		**5** Legal residence (domicile)
13319 Taylorcrest Street		USA
6 City or town, state or province, country, and ZIP or foreign postal code		**7** Citizenship (see instructions)
Houston, TX 77079		USA

Part 1—General Information

		Yes	No
8	If the donor died during the year, check here ▶ ☐ and enter date of death _____ , _____.		
9	If you extended the time to file this Form 709, check here ▶ ☐		
10	Enter the total number of donees listed on Schedule A. Count each person only once ▶		
11a	Have you (the donor) previously filed a Form 709 (or 709-A) for any other year? If "No," skip line 11b		✓
b	Has your address changed since you last filed Form 709 (or 709-A)?		
12	**Gifts by husband or wife to third parties.** Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (see instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. **If the answer is "No," skip lines 13–18.**)	✓	
13	Name of consenting spouse **James A. Polk** **14** SSN **123-45-6789**		
15	Were you married to one another during the entire calendar year? (see instructions)	✓	
16	If 15 is "No," check whether ☐ married ☐ divorced or ☐ widowed/deceased, and give date (see instructions) ▶		
17	Will a gift tax return for this year be filed by your spouse? (If "Yes," mail both returns in the same envelope.)	✓	
18	**Consent of Spouse.** I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.		
	Consenting spouse's signature ▶ **Date ▶**		
19	Have you applied a DSUE amount received from a predeceased spouse to a gift or gifts reported on this or a previous Form 709? If "Yes," complete Schedule C		

Part 2—Tax Computation

1	Enter the amount from Schedule A, Part 4, line 11	1	5,492,000
2	Enter the amount from Schedule B, line 3	2	
3	Total taxable gifts. Add lines 1 and 2	3	5,492,000
4	Tax computed on amount on line 3 (see *Table for Computing Gift Tax* in instructions)	4	2,142,600
5	Tax computed on amount on line 2 (see *Table for Computing Gift Tax* in instructions)	5	
6	Balance. Subtract line 5 from line 4	6	2,142,600
7	Applicable credit amount. If donor has DSUE amount from predeceased spouse(s), enter amount from Schedule C, line 4; otherwise, see instructions	7	2,117,800
8	Enter the applicable credit against tax allowable for all prior periods (from Sch. B, line 1, col. C)	8	
9	Balance. Subtract line 8 from line 7. Do not enter less than zero	9	2,117,800
10	Enter 20% (.20) of the amount allowed as a specific exemption for gifts made after September 8, 1976, and before January 1, 1977 (see instructions)	10	
11	Balance. Subtract line 10 from line 9. Do not enter less than zero	11	2,117,800
12	Applicable credit. Enter the smaller of line 6 or line 11	12	2,117,800
13	Credit for foreign gift taxes (see instructions)	13	
14	Total credits. Add lines 12 and 13	14	2,117,800
15	Balance. Subtract line 14 from line 6. Do not enter less than zero	15	24,800
16	Generation-skipping transfer taxes (from Schedule D, Part 3, col. H, Total)	16	
17	Total tax. Add lines 15 and 16	17	24,800
18	Gift and generation-skipping transfer taxes prepaid with extension of time to file	18	
19	If line 18 is less than line 17, enter **balance due** (see instructions)	19	24,800
20	If line 18 is greater than line 17, enter **amount to be refunded**	20	

Attach check or money order here.

Sign Here

Under penalties of perjury, I declare that I have examined this return, including any accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than donor) is based on all information of which preparer has any knowledge.

May the IRS discuss this return with the preparer shown below (see instructions)? ☐ Yes ☐ No

Signature of donor _____ Date _____

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see the instructions for this form. Cat. No. 16783M Form **709** (2015)

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Form 709 (2015) Page **2**

SCHEDULE A **Computation of Taxable Gifts** (Including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation . . . . . Yes ☐ No ☐

B ☐ ◄ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1—Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusions. (see instructions)

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1	**Condo in Conroe to children**		1,200,000	2015	1,900,000	950,000	950,000
	Office building in Round Rock to children		1,800,000	2015	2,300,000	1,150,000	1,150,000
	Reimbursement of expenses for father		82,000	2015	82,000	41,000	41,000
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							
	Condo in Conroe to children		1,200,000	2015	1,900,000	950,000	950,000
	Office building in Round Rock to children		900,000	2015	2,300,000	1,150,000	1,150,000
	Vacation home to children		1,800,000	2015	2,600,000	1,300,000	1,300,000
	BMW automobile to niece		42,000	2015	42,000	21,000	21,000
Total of Part 1. Add amounts from Part 1, column H . . . . . ►							5,562,000

Part 2—Direct Skips. Gifts that are direct skips and are subject to both gift tax and generation-skipping transfer tax. You must list the gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(b) election out	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1							
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							
Total of Part 2. Add amounts from Part 2, column H . . . . . ►							

Part 3—Indirect Skips. Gifts to trusts that are currently subject to gift tax and may later be subject to generation-skipping transfer tax. You must list these gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(c) election	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter ½ of column F	H Net transfer (subtract col. G from col. F)
1							
Gifts made by spouse —*complete* ***only*** *if you are splitting gifts with your spouse and he/she also made gifts.*							
Total of Part 3. Add amounts from Part 3, column H . . . . . ►							

(If more space is needed, attach additional statements.) Form **709** (2015)

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Form 709 (2015) Page 3

Part 4—Taxable Gift Reconciliation

1	Total value of gifts of donor. Add totals from column H of Parts 1, 2, and 3	1	5,562,000	
2	Total annual exclusions for gifts listed on line 1 (see instructions)	2	70,000	
3	Total included amount of gifts. Subtract line 2 from line 1	3	5,492,000	
Deductions (see instructions)				
4	Gifts of interests to spouse for which a marital deduction will be claimed, based on item numbers _____ of Schedule A	4		
5	Exclusions attributable to gifts on line 4	5		
6	Marital deduction. Subtract line 5 from line 4	6		
7	Charitable deduction, based on item nos. _____ less exclusions	7		
8	Total deductions. Add lines 6 and 7	8		
9	Subtract line 8 from line 3	9	5,492,000	
10	Generation-skipping transfer taxes payable with this Form 709 (from Schedule D, Part 3, col. H, Total)	10		
11	**Taxable gifts.** Add lines 9 and 10. Enter here and on page 1, Part 2—Tax Computation, line 1	11	5,492,000	

Terminable Interest (QTIP) Marital Deduction. (see instructions for Schedule A, Part 4, line 4)

If a trust (or other property) meets the requirements of qualified terminable interest property under section 2523(f), and:

a. The trust (or other property) is listed on Schedule A, and

b. The value of the trust (or other property) is entered in whole or in part as a deduction on Schedule A, Part 4, line 4,

then the donor shall be deemed to have made an election to have such trust (or other property) treated as qualified terminable interest property under section 2523(f).

If less than the entire value of the trust (or other property) that the donor has included in Parts 1 and 3 of Schedule A is entered as a deduction on line 4, the donor shall be considered to have made an election only as to a fraction of the trust (or other property). The numerator of this fraction is equal to the amount of the trust (or other property) deducted on Schedule A, Part 4, line 6. The denominator is equal to the total value of the trust (or other property) listed in Parts 1 and 3 of Schedule A.

If you make the QTIP election, the terminable interest property involved will be included in your spouse's gross estate upon his or her death (section 2044). See instructions for line 4 of Schedule A. If your spouse disposes (by gift or otherwise) of all or part of the qualifying life income interest, he or she will be considered to have made a transfer of the entire property that is subject to the gift tax. See *Transfer of Certain Life Estates Received From Spouse* in the instructions.

12 Election Out of QTIP Treatment of Annuities

☐ ◀ Check here if you elect under section 2523(f)(6) **not** to treat as qualified terminable interest property any joint and survivor annuities that are reported on Schedule A and would otherwise be treated as qualified terminable interest property under section 2523(f). See instructions. Enter the item numbers from Schedule A for the annuities for which you are making this election ▶ _____

SCHEDULE B Gifts From Prior Periods

If you answered "Yes," on line 11a of page 1, Part 1, see the instructions for completing Schedule B. If you answered "No," skip to the Tax Computation on page 1 (or Schedules C or D, if applicable). Complete Schedule A before beginning Schedule B. See instructions for recalculation of the column C amounts. Attach calculations.

A Calendar year or calendar quarter (see instructions)	B Internal Revenue office where prior return was filed	C Amount of applicable credit (unified credit) against gift tax for periods after December 31, 1976	D Amount of specific exemption for prior periods ending before January 1, 1977	E Amount of taxable gifts
1 Totals for prior periods	1			

2	Amount, if any, by which total specific exemption, line 1, column D is more than $30,000	2	
3	Total amount of taxable gifts for prior periods. Add amount on line 1, column E and amount, if any, on line 2. Enter here and on page 1, Part 2—Tax Computation, line 2	3	

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Ella R. Polk — 123-45-6788

Schedule A – Form 709, page 2 –Tax Year 2015

Part 1: Gifts made by taxpayer

A	B	C	D	E	F	G	H
1	Benjamin, Michael, Olivia Polk; children; condo; Conroe (TX)		1,200,000	2015	1,900,000	950,000	950,000
2	Benjamin, Michael, Olivia Polk; children; office building; Round Rock (TX)		1,800,000	2015	2,300,000	1,150,000	1,150,000
3	Alan Roberts; father; reimbursement for expenses		82,000	2015	82,000	41,000	41,000

Part 1: Gifts made by spouse

4	Benjamin, Michael, Olivia Polk; children; vacation home; Bandera (TX)		900,000	2015	2,600,000	1,300,000	1,300,000
5	Benjamin, Michael, Olivia Polk; children; condo; Conroe (TX)		1,200,000	2015	1,900,000	950,000	950,000
6	Benjamin, Michael, Olivia Polk; children; office building; Round Rock (TX)		1,800,000	2015	2,300,000	1,150,000	1,150,000
7	Carol Polk; niece; BMW auto		42,000	2015	42,000	21,000	21,000

Total of Part 1	**5,562,000**

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PROBLEM 8 SOLUTIONS

A summary of the determination of estate tax liability follows.

John Harper Trust (Schedule F, Note 1)		$2,100,000
Insurance on Harriet's life (Schedule D)		100,000
Insurance on the lives of others (Schedule F, Note 2)		80,000
Tract of undeveloped land (Schedule A, Note 3)		1,000,000
Beach cottages (Schedule A)		1,200,000
Vacation lodge (Schedule E, Note 4)		700,000
Personal residence (Schedule A)		800,000
Lawsuit settlement (Schedule F, Note 5)		700,000
Cash—checking account ($18,000), income tax refund ($4,000)—(Schedule C)		22,000
Municipal bonds (Schedule B)		205,000
Personal and household effects (Schedule F)		60,000
Gross estate		$6,967,000
Funeral and administration expenses (Schedule J):		
Funeral	$ 9,000	
Attorney's fees	24,000	
Accounting fees	10,000	
Appraisal fees and court costs	6,000	(49,000)
Debts of the decedent (Schedule K):		
Credit card debt and household bills	$21,000	
Federal income tax (1/1 – 6/6/15)	27,000	(48,000)
Mortgage (Schedule K)		(200,000)
Charitable contribution (Schedule O, Note 6)		(40,000)
Taxable estate		$6,630,000
Tax on taxable estate of $6,630,000— $345,800 + 40%($6,630,000 – $1,000,000)		$2,597,800
Less: Unified transfer tax credit for 2015		(2,117,800)
Estate tax due		$ 480,000

NOTES

(1) Under § 2044, the QTIP election made by her husband's executor forces the inclusion of the trust in Harriet's gross estate.

(2) Because these insurance policies have not matured, their value is not the face amount. They are included in the gross estate under § 2033, not § 2042.

(3) The mortgage on this property is deducted separately.

(4) As Harriet contributed one-half of the purchase price, only one-half of the value is included under § 2040.

(5) The lawsuit settlement was not cash (Schedule C) as of the date of death. It is uncertain when the income tax refund was received (i.e., before or after Harriet's death).

(6) The church pledge could have been reported as a debt of the decedent (Schedule K).

On Form 706, line 5, page 2, an estimate must be given as to how much the major heirs of the estate will receive. The estimate was determined by using the taxable estate of $6,630,000, subtracting the estate tax of $480,000, and dividing by two to arrive at $3,075,000 for each heir (Travis and Hannah). Completed Form 706 follows.

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Form **706** (Rev. August 2013)

Department of the Treasury
Internal Revenue Service

United States Estate (and Generation-Skipping Transfer) Tax Return

▶ **Estate of a citizen or resident of the United States (see instructions). To be filed for decedents dying after December 31, 2012.**
▶ **Information about Form 706 and its separate instructions is at *www.irs.gov/form706.***

OMB No. 1545-0015

Part 1—Decedent and Executor

1a Decedent's first name and middle initial (and maiden name, if any) **Harriet C.**	**1b** Decedent's last name **Harper**		**2** Decedent's social security no. **123 45 6781**
3a City, town, or post office; county; state or province; country; and ZIP or foreign postal code. **1520 Marlin Drive** **Clearwater,FL 33758**	**3b** Year domicile established **xxxx**	**4** Date of birth **xx/xx/1941**	**5** Date of death **06/06/2015**
6a Name of executor (see instructions) **Travis Harper and Hannah Baker**	**6b** Executor's address (number and street including apartment or suite no.; city, town, or post office; state or province; country; and ZIP or foreign postal code) and phone no.		
6c Executor's social security number (see instructions) **123 45 6782**	Phone no.		

6d If there are multiple executors, check here ☐ and attach a list showing the names, addresses, telephone numbers, and SSNs of the additional executors.

7a Name and location of court where will was probated or estate administered **Probate Court, X County, Florida**		**7b** Case number
8 If decedent died testate, check here ▶ ☑ and attach a certified copy of the will.	**9** If you extended the time to file this Form 706, check here ▶ ☐	
10 If Schedule R-1 is attached, check here ▶ ☐	**11** If you are estimating the value of assets included in the gross estate on line 1 pursuant to the special rule of Reg. section 20.2010-2T(a) (7)(ii), check here ▶ ☐	

Part 2—Tax Computation

1	Total gross estate less exclusion (from Part 5—Recapitulation, item 13)			1	6,967,000
2	Tentative total allowable deductions (from Part 5—Recapitulation, item 24)			2	337,000
3a	Tentative taxable estate (subtract line 2 from line 1)			3a	6,630,000
b	State death tax deduction			3b	
c	Taxable estate (subtract line 3b from line 3a)			3c	6,630,000
4	Adjusted taxable gifts (see instructions)			4	
5	Add lines 3c and 4			5	6,630,000
6	Tentative tax on the amount on line 5 from Table A in the instructions			6	2,597,800
7	Total gift tax paid or payable (see instructions)			7	
8	Gross estate tax (subtract line 7 from line 6)			8	2,597,800
9a	Basic exclusion amount	9a	5,430,000		
9b	Deceased spousal unused exclusion (DSUE) amount from predeceased spouse(s), if any (from Section D, Part 6—Portability of Deceased Spousal Unused Exclusion)	9b			
9c	Applicable exclusion amount (add lines 9a and 9b)	9c	5,430,000		
9d	Applicable credit amount (tentative tax on the amount in 9c from Table A in the instructions)	9d	2,117,800		
10	Adjustment to applicable credit amount (May not exceed $6,000. See instructions.)	10			
11	Allowable applicable credit amount (subtract line 10 from line 9d)			11	2,117,800
12	Subtract line 11 from line 8 (but do not enter less than zero)			12	480,000
13	Credit for foreign death taxes (from Schedule P). (Attach Form(s) 706-CE.)	13			
14	Credit for tax on prior transfers (from Schedule Q)	14			
15	Total credits (add lines 13 and 14)			15	
16	Net estate tax (subtract line 15 from line 12)			16	480,000
17	Generation-skipping transfer (GST) taxes payable (from Schedule R, Part 2, line 10)			17	
18	Total transfer taxes (add lines 16 and 17)			18	480,000
19	Prior payments (explain in an attached statement)			19	
20	Balance due (or overpayment) (subtract line 19 from line 18)			20	480,000

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than the executor is based on all information of which preparer has any knowledge.

Sign Here

▶ Signature of executor ▶ Date

▶ Signature of executor ▶ Date

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

For Privacy Act and Paperwork Reduction Act Notice, see instructions. Cat. No. 20548R Form **706** (Rev. 8-2013)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

Part 3—Elections by the Executor

Note. For information on electing portability of the decedent's DSUE amount, including how to opt out of the election, see Part 6—Portability of Deceased Spousal Unused Exclusion.
Note. Some of the following elections may require the posting of bonds or liens.

Please check "Yes" or "No" box for each question (see instructions).

			Yes	No
1	Do you elect alternate valuation?	1		✓
2	Do you elect special-use valuation? If "Yes," you must complete and attach Schedule A-1	2		✓
3	Do you elect to pay the taxes in installments as described in section 6166? If "Yes," you must attach the additional information described in the instructions. **Note. By electing section 6166 installment payments, you may be required to provide security for estate tax deferred under section 6166 and interest in the form of a surety bond or a section 6324A lien.**	3		✓
4	Do you elect to postpone the part of the taxes due to a reversionary or remainder interest as described in section 6163?	4		✓

Part 4—General Information

Note. Please attach the necessary supplemental documents. **You must attach the death certificate.** (See instructions)

Authorization to receive confidential tax information under Reg. section 601.504(b)(2)(i); to act as the estate's representative before the IRS; and to make written or oral presentations on behalf of the estate:

Name of representative (print or type)	State	Address (number, street, and room or suite no., city, state, and ZIP code)

I declare that I am the ☐ attorney/ ☐ certified public accountant/ ☐ enrolled agent (check the applicable box) for the executor. I am not under suspension or disbarment from practice before the Internal Revenue Service and am qualified to practice in the state shown above.

Signature	CAF number	Date	Telephone number

1 Death certificate number and issuing authority (attach a copy of the death certificate to this return).

2 Decedent's business or occupation. If retired, check here ▶ ☐ and state decedent's former business or occupation.

3a Marital status of the decedent at time of death:
☐ Married ☐ Widow/widower ☐ Single ☐ Legally separated ☐ Divorced

3b For all prior marriages, list the name and SSN of the former spouse, the date the marriage ended, and whether the marriage ended by annulment, divorce, or death. Attach additional statements of the same size if necessary.

4a Surviving spouse's name	**4b** Social security number	**4c** Amount received (see instructions)

5 Individuals (other than the surviving spouse), trusts, or other estates who receive benefits from the estate (do not include charitable beneficiaries shown in Schedule O) (see instructions).

Name of individual, trust, or estate receiving $5,000 or more	Identifying number	Relationship to decedent	Amount (see instructions)
Travis Harper	**123-45-6782**	**Son**	**3,075,000**
Hannah Baker	**123-45-6783**	**Daughter**	**3,075,000**
All unascertainable beneficiaries and those who receive less than $5,000 ▶			
Total			

If you answer "Yes" to any of the following questions, you must attach additional information as described.			Yes	No
6	Is the estate filing a protective claim for refund? If "Yes," complete and attach two copies of Schedule PC for each claim.			✓
7	Does the gross estate contain any section 2044 property (qualified terminable interest property (QTIP) from a prior gift or estate)? (see instructions)			✓
8a	Have federal gift tax returns ever been filed? If "Yes," attach copies of the returns, if available, and furnish the following information:			
b	Period(s) covered	**c** Internal Revenue office(s) where filed		
9a	Was there any insurance on the decedent's life that is not included on the return as part of the gross estate?			✓
b	Did the decedent own any insurance on the life of another that is not included in the gross estate?			✓

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper — **Decedent's social security number:** 123 45 6781

Part 4—General Information *(continued)*

	If you answer "Yes" to any of the following questions, you must attach additional information as described.	Yes	No
10	Did the decedent at the time of death own any property as a joint tenant with right of survivorship in which **(a)** one or more of the other joint tenants was someone other than the decedent's spouse, and **(b)** less than the full value of the property is included on the return as part of the gross estate? If "Yes," you must complete and attach Schedule E	✓	
11a	Did the decedent, at the time of death, own any interest in a partnership (for example, a family limited partnership), an unincorporated business, or a limited liability company; or own any stock in an inactive or closely held corporation?		✓
b	If "Yes," was the value of **any** interest owned (from above) discounted on this estate tax return? If "Yes," see the instructions on reporting the total accumulated or effective discounts taken on Schedule F or G		✓
12	Did the decedent make any transfer described in sections 2035, 2036, 2037, or 2038? (see instructions) If "Yes," you must complete and attach Schedule G		✓
13a	Were there in existence at the time of the decedent's death any trusts created by the decedent during his or her lifetime?		✓
b	Were there in existence at the time of the decedent's death any trusts not created by the decedent under which the decedent possessed any power, beneficial interest, or trusteeship?	✓	
c	Was the decedent receiving income from a trust created after October 22, 1986, by a parent or grandparent?		✓
	If "Yes," was there a GST taxable termination (under section 2612) on the death of the decedent?		✓
d	If there was a GST taxable termination (under section 2612), attach a statement to explain. Provide a copy of the trust or will creating the trust, and give the name, address, and phone number of the current trustee(s).		
e	Did the decedent at any time during his or her lifetime transfer or sell an interest in a partnership, limited liability company, or closely held corporation to a trust described in lines 13a or 13b?		✓
	If "Yes," provide the EIN for this transferred/sold item. ▶		
14	Did the decedent ever possess, exercise, or release any general power of appointment? If "Yes," you must complete and attach Schedule H		✓
15	Did the decedent have an interest in or a signature or other authority over a financial account in a foreign country, such as a bank account, securities account, or other financial account?		✓
16	Was the decedent, immediately before death, receiving an annuity described in the "General" paragraph of the instructions for Schedule I or a private annuity? If "Yes," you must complete and attach Schedule I		✓
17	Was the decedent ever the beneficiary of a trust for which a deduction was claimed by the estate of a predeceased spouse under section 2056(b)(7) and which is not reported on this return? If "Yes," attach an explanation		✓

Part 5—Recapitulation. Note. If estimating the value of one or more assets pursuant to the special rule of Reg. section 20.2010-2T(a)(7)(ii), enter on both lines 10 and 23 the amount noted in the instructions for the corresponding range of values. (See instructions for details.)

Item no.	Gross estate		Alternate value	Value at date of death
1	Schedule A—Real Estate	1		3,000,000
2	Schedule B—Stocks and Bonds	2		205,000
3	Schedule C—Mortgages, Notes, and Cash	3		22,000
4	Schedule D—Insurance on the Decedent's Life (attach Form(s) 712)	4		100,000
5	Schedule E—Jointly Owned Property (attach Form(s) 712 for life insurance)	5		700,000
6	Schedule F—Other Miscellaneous Property (attach Form(s) 712 for life insurance)	6		2,940,000
7	Schedule G—Transfers During Decedent's Life (att. Form(s) 712 for life insurance)	7		
8	Schedule H—Powers of Appointment	8		
9	Schedule I—Annuities	9		
10	Estimated value of assets subject to the special rule of Reg. section 20.2010-2T(a)(7)(ii)	10		
11	Total gross estate (add items 1 through 10)	11		6,967,000
12	Schedule U—Qualified Conservation Easement Exclusion	12		
13	Total gross estate less exclusion (subtract item 12 from item 11). Enter here and on line 1 of Part 2—Tax Computation	13		

Item no.	Deductions		Amount
14	Schedule J—Funeral Expenses and Expenses Incurred in Administering Property Subject to Claims	14	49,000
15	Schedule K—Debts of the Decedent	15	48,000
16	Schedule K—Mortgages and Liens	16	200,000
17	Total of items 14 through 16	17	297,000
18	Allowable amount of deductions from item 17 (see the instructions for item 18 of the Recapitulation)	18	
19	Schedule L—Net Losses During Administration	19	
20	Schedule L—Expenses Incurred in Administering Property Not Subject to Claims	20	
21	Schedule M—Bequests, etc., to Surviving Spouse	21	
22	Schedule O—Charitable, Public, and Similar Gifts and Bequests	22	40,000
23	Estimated value of deductible assets subject to the special rule of Reg. section 20.2010-2T(a)(7)(ii)	23	
24	Tentative total allowable deductions (add items 18 through 23). Enter here and on line 2 of the Tax Computation	24	337,000

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

SCHEDULE A—Real Estate

- For jointly owned property that must be disclosed on Schedule E, see instructions.
- Real estate that is part of a sole proprietorship should be shown on Schedule F.
- Real estate that is included in the gross estate under sections 2035, 2036, 2037, or 2038 should be shown on Schedule G.
- Real estate that is included in the gross estate under section 2041 should be shown on Schedule H.
- If you elect section 2032A valuation, you must complete Schedule A and Schedule A-1.

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(*7*)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last three columns.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1	**Land in Pinellas County, Florida**			**1,000,000**
	Beach cottage in Destin, Florida			**1,200,000**
	Residence at 1520 Marlin Drive, Clearwater, Florida			**800,000**
	Total from continuation schedules or additional statements attached to this schedule . . .			
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 1.)			**3,000,000**

(If more space is needed, attach the continuation schedule from the end of this package or additional statements of the same size.)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper	Decedent's social security number 123 45 6781

SCHEDULE B—Stocks and Bonds

(For jointly owned property that must be disclosed on Schedule E, see instructions.)

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last four columns.

Item number	Description, including face amount of bonds or number of shares and par value for identification. Give CUSIP number. If trust, partnership, or closely held entity, give EIN.	CUSIP number or EIN, where applicable	Unit value	Alternate valuation date	Alternate value	Value at date of death
1	**State of Georgia municipal bonds**					**205,000**
	Total from continuation schedules (or additional statements) attached to this schedule . . .					
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 2.)					**205,000**

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Schedule B—Page 10

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

SCHEDULE C—Mortgages, Notes, and Cash

(For jointly owned property that must be disclosed on Schedule E, see instructions.)

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last three columns.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1	**Dunedin State Bank checking account**			**18,000**
	Federal income tax refund			**4,000**
	Total from continuation schedules (or additional statements) attached to this schedule . .			
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 3.)			**22,000**

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper	Decedent's social security number 123 45 6781

SCHEDULE D—Insurance on the Decedent's Life

You must list all policies on the life of the decedent and attach a Form 712 for each policy.

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last three columns.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1	**Falcon Assurance policy on Harriet**			100,000
	Total from continuation schedules (or additional statements) attached to this schedule . .			
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 4.)			100,000

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

SCHEDULE E—Jointly Owned Property

(If you elect section 2032A valuation, you must complete Schedule E and Schedule A-1.)

PART 1. Qualified Joint Interests—Interests Held by the Decedent and His or Her Spouse as the Only Joint Tenants (Section 2040(b)(2))

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last three columns.

Item number	Description. For securities, give CUSIP number. If trust, partnership, or closely held entity, give EIN.	CUSIP number or EIN, where applicable	Alternate valuation date	Alternate value	Value at date of death
1					
	Total from continuation schedules (or additional statements) attached to this schedule				
1a	Totals		1a		
1b	Amounts included in gross estate (one-half of line 1a)		1b		

PART 2. All Other Joint Interests

2a State the name and address of each surviving co-tenant. If there are more than three surviving co-tenants, list the additional co-tenants on an attached statement.

	Name	Address (number and street, city, state, and ZIP code)
A.		
B.		
C.		

Item number	Enter letter for co-tenant	Description (including alternate valuation date if any). For securities, give CUSIP number. If trust, partnership, or closely held entity, give EIN	CUSIP number or EIN, where applicable	Percentage includible	Includible alternate value	Includible value at date of death
1		**Vacation lodge in Union, South Carolina**		**50%**		**700,000**
		Total from continuation schedules (or additional statements) attached to this schedule				
2b		Total other joint interests		2b		
3		**Total includible joint interests** (add lines 1b and 2b). Also enter on Part 5—Recapitulation, page 3, at item 5		3		**700,000**

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Schedule E—Page 13

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper	Decedent's social security number 123 45 6781

SCHEDULE F—Other Miscellaneous Property Not Reportable Under Any Other Schedule

(For jointly owned property that must be disclosed on Schedule E, see instructions.)
(If you elect section 2032A valuation, you must complete Schedule F and Schedule A-1.)

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entries in the last three columns.

		Yes	No
1	Did the decedent own any works of art, items, or any collections whose artistic or collectible value at date of death exceeded $3,000? . . . . . If "Yes," submit full details on this schedule and attach appraisals.		✓
2	Has the decedent's estate, spouse, or any other person received (or will receive) any bonus or award as a result of the decedent's employment or death? . . . . . If "Yes," submit full details on this schedule.		✓
3	Did the decedent at the time of death have, or have access to, a safe deposit box? . . . . . If "Yes," state location, and if held jointly by decedent and another, state name and relationship of joint depositor. If any of the contents of the safe deposit box are omitted from the schedules in this return, explain fully why omitted.		✓

Item number	Description. For securities, give CUSIP number. If trust, partnership, or closely held entity, give EIN	CUSIP number or EIN, where applicable	Alternate valuation date	Alternate value	Value at date of death
1	**Household effects**				**60,000**
	Life insurance policy on Travis Harper				**40,000**
	Life insurance policy on Hannah Baker				**40,000**
	John Harper QTIP trust				**2,100,000**
	Lawsuit settlement claim				**700,000**
	Total from continuation schedules (or additional statements) attached to this schedule . .				
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 6.)				**2,940,000**

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

SCHEDULE J—Funeral Expenses and Expenses Incurred in Administering Property Subject to Claims

► **Use Schedule PC to make a protective claim for refund due to an expense not currently deductible. For such a claim, report the expense on Schedule J but without a value in the last column.**

Note. Do not list expenses of administering property not subject to claims on this schedule. To report those expenses, see instructions.

If executors' commissions, attorney fees, etc., are claimed and allowed as a deduction for estate tax purposes, they are not allowable as a deduction in computing the taxable income of the estate for federal income tax purposes. They are allowable as an income tax deduction on Form 1041, U.S. Income Tax Return for Estates and Trusts, if a waiver is filed to forgo the deduction on Form 706 (see Instructions for Form 1041).

	Yes	No
Are you aware of any actual or potential reimbursement to the estate for any expense claimed as a deduction on this schedule?		✓
If "Yes," attach a statement describing the expense(s) subject to potential reimbursement. (see instructions)		

Item number	Description	Expense amount	Total amount
	A. Funeral expenses:		
1	**Funeral home and cemetery charges**		9,000
	Total funeral expenses ►		9,000

B. Administration expenses:

1	Executors' commissions—amount estimated/agreed upon/paid. (Strike out the words that do not apply.)	
2	Attorney fees—amount estimated/agreed upon/paid. (Strike out the words that do not apply.)	24,000
3	Accountant fees—amount estimated/agreed upon/paid. (Strike out the words that do not apply.)	10,000

	4 Miscellaneous expenses:	Expense amount	
	Appraisal fees and court costs		6,000
	Total miscellaneous expenses from continuation schedules (or additional statements) attached to this schedule		
	Total miscellaneous expenses ►		6,000
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 14.) ►		49,000

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper

Decedent's social security number: 123 45 6781

SCHEDULE K—Debts of the Decedent, and Mortgages and Liens

▶ **Use Schedule PC to make a protective claim for refund due to a claim not currently deductible. For such a claim, report the expense on Schedule K but without a value in the last column.**

	Yes	No
Are you aware of any actual or potential reimbursement to the estate for any debt of the decedent, mortgage, or lien claimed as a deduction on this schedule?		✓
If "Yes," attach a statement describing the items subject to potential reimbursement. (see instructions)		
Are any of the items on this schedule deductible under Reg. section 20.2053-4(b) and Reg. section 20.2053-4(c)?		
If "Yes," attach a statement indicating the applicable provision and documenting the value of the claim.		

Item number	Debts of the Decedent—Creditor and nature of debt, and allowable death taxes	Amount
1	**Credit card balances**	**21,000**
	Income tax liability	**27,000**
	Total from continuation schedules (or additional statements) attached to this schedule	
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 15.)	**48,000**

Item number	Mortgages and Liens—Description	Amount
1	**Mortgage on land in Pinellas County, Florida**	**200,000**
	Total from continuation schedules (or additional statements) attached to this schedule	
	TOTAL. (Also enter on Part 5—Recapitulation, page 3, at item 16.)	**200,000**

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

Form 706 (Rev. 8-2013)

Estate of: Harriet C. Harper | **Decedent's social security number** 123 45 6781

SCHEDULE O—Charitable, Public, and Similar Gifts and Bequests

Note. If the value of the gross estate, together with the amount of adjusted taxable gifts, is less than the basic exclusion amount and the Form 706 is being filed solely to elect portability of the DSUE amount, consideration should be given as to whether you are required to report the value of assets eligible for the marital or charitable deduction on this schedule. See the instructions and Reg. section 20.2010-2T (a)(7)(ii) for more information. If you are not required to report the value of an asset, identify the property but make no entry in the last column.

		Yes	No
1a	If the transfer was made by will, has any action been instituted to contest or have interpreted any of its provisions affecting the charitable deductions claimed in this schedule? If "Yes," full details must be submitted with this schedule.		✓
b	According to the information and belief of the person or persons filing this return, is any such action planned? If "Yes," full details must be submitted with this schedule.		✓
2	Did any property pass to charity as the result of a qualified disclaimer? If "Yes," attach a copy of the written disclaimer required by section 2518(b).		✓

Item number	Name and address of beneficiary	Character of institution	Amount
1	**Church pledge**		40,000
	Total from continuation schedules (or additional statements) attached to this schedule		
3	Total	**3**	40,000
4a	Federal estate tax payable out of property interests listed above **4a**		
b	Other death taxes payable out of property interests listed above **4b**		
c	Federal and state GST taxes payable out of property interests listed above **4c**		
d	Add items 4a, 4b, and 4c	**4d**	
5	Net value of property interests listed above (subtract 4d from 3). Also enter on Part 5—Recapitulation, page 3, at item 22	**5**	40,000

(If more space is needed, attach the continuation schedule from the end of this package or additional statements of the same size.)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

PROBLEM 9 SOLUTIONS

The Green Trust is a complex trust. It accumulated the $25,000 corpus capital gain, and it pays $4,473 entity-level tax on this amount. Marcus receives a $40,000 check and pays tax on $28,771: $23,587 taxable interest income and $5,184 qualified dividend income.

Five-step procedure for computing solution (as illustrated in Exhibit 28.5): Steps 1–4

Item	Totals	Accounting Income	Taxable Income	Distributable Net Income/Distribution Deduction
Dividend income	$10,000	$10,000	$10,000	
Taxable interest income	50,000	50,000	50,000	
Exempt interest income	20,000	20,000		
Net long-term capital gain	25,000		25,000	
Fiduciary fees	6,000		(4,500)	6,000 × (60/80)
Personal exemption			(100)	
Accounting income/Taxable income before the distribution deduction		$80,000 ***STEP 1***	$80,400 ***STEP 2***	$80,400
Exemption				100
Corpus capital gain/loss				(25,000)
Net exempt income				18,500
Distributable net income			***Taxable portion*** $74,000 −18,500 $55,500	$74,000
Distribution deduction			(55,500) ***STEP 3***	Lesser of $80,000 distributed or $55,500 taxable DNI distributed
Entity taxable income			$24,900 ***STEP 4***	

Proof of Entity TI: Capital gain accumulated $25,000 – Exemption $100 = $24,900

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STEP 5: Allocate DNI

STEP 5: Beneficiary Taxation	Amount Received	DNI Received	Income Type		
			Interest Income	Exempt Interest	Dividend Income
Totals	$80,000	$74,000	$45,500▼	$18,500■	$10,000
Marcus	$40,000	$38,364●	$23,587	$9,591	$5,184▲
Ellen	$40,000	$35,636	$21,913	$8,909	$4,816

NOTES

- DNI received

	Marcus		Ellen	Total
First tier		$25,000	$ –0–	$25,000
Second tier	(15/55 distributions × $49,000 remaining DNI) =	13,364	35,636	49,000
Totals		$38,364●	$35,636	$74,000

- Schedule K–1, Marcus:

  Interest income: $45,500 × ($38,364/$74,000) = $23,587
  Dividend income: $10,000 × ($38,364/$74,000) = $5,184▲
  Exempt income: $18,500 × ($38,364/$74,000) = $9,591

- Net exempt income = $20,000 – $1,500 disallowed fiduciary fees = $18,500■
- Net taxable interest = $50,000 – $4,500 deductible fiduciary fees = $45,500▼

Entity tax:

Tax on net long-term capital gain				
$ 2,500	×	0%	=	$ –0–
9,800	×	15%	=	1,470
12,600	×	20%	=	2,520
$ 24,900				$3,990
Tax on undistributed net investment income				
$25,000 – $12,300	×	3.8%	=	483
Total				$4,473

Completed Form 1041 for the Green Trust, and Schedule K–1 for Marcus White, follow.

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Form **1041** Department of the Treasury—Internal Revenue Service
U.S. Income Tax Return for Estates and Trusts
2015 OMB No. 1545-0092

▶ Information about Form 1041 and its separate instructions is at *www.irs.gov/form1041.*

A Check all that apply:
- ☐ Decedent's estate
- ☐ Simple trust
- ☑ Complex trust
- ☐ Qualified disability trust
- ☐ ESBT (S portion only)
- ☐ Grantor type trust
- ☐ Bankruptcy estate-Ch. 7
- ☐ Bankruptcy estate-Ch. 11
- ☐ Pooled income fund

For calendar year 2015 or fiscal year beginning , 2015, and ending , 20

Name of estate or trust (If a grantor type trust, see the instructions.)
GREEN TRUST

C Employer identification number
11-1111111

Name and title of fiduciary
WISCONSIN STATE NATIONAL BANK

D Date entity created
12/14/1953

Number, street, and room or suite no. (If a P.O. box, see the instructions.)
3100 EAST WISCONSIN AVENUE

E Nonexempt charitable and split-interest trusts, check applicable box(es), see instructions.
- ☐ Described in sec. 4947(a)(1). Check here if not a private foundation . . . ▶ ☐
- ☐ Described in sec. 4947(a)(2)

City or town, state or province, country, and ZIP or foreign postal code
MILWAUKEE, WI 53201

B Number of Schedules K-1 attached (see instructions) ▶

F Check applicable boxes: ☐ Initial return ☐ Final return ☐ Amended return ☐ Net operating loss carryback ☐ Change in trust's name ☐ Change in fiduciary ☐ Change in fiduciary's name ☐ Change in fiduciary's address

G Check here if the estate or filing trust made a section 645 election . . . . . ▶ ☐ Trust TIN ▶

Income	1	Interest income	1	50,000
	2a	Total ordinary dividends	2a	10,000
	b	Qualified dividends allocable to: (1) Beneficiaries _____ (2) Estate or trust _____		
	3	Business income or (loss). Attach Schedule C or C-EZ (Form 1040)	3	
	4	Capital gain or (loss). Attach Schedule D (Form 1041)	4	25,000
	5	Rents, royalties, partnerships, other estates and trusts, etc. Attach Schedule E (Form 1040)	5	
	6	Farm income or (loss). Attach Schedule F (Form 1040)	6	
	7	Ordinary gain or (loss). Attach Form 4797	7	
	8	Other income. List type and amount _____	8	
	9	**Total income.** Combine lines 1, 2a, and 3 through 8 ▶	9	85,000
Deductions	10	Interest. Check if Form 4952 is attached ▶ ☐	10	
	11	Taxes	11	
	12	Fiduciary fees	12	4,500
	13	Charitable deduction (from Schedule A, line 7)	13	
	14	Attorney, accountant, and return preparer fees	14	
	15a	Other deductions **not** subject to the 2% floor (attach schedule)	15a	
	b	Net operating loss deduction (see instructions)	15b	
	c	Allowable miscellaneous itemized deductions subject to the 2% floor	15c	
	16	Add lines 10 through 15c ▶	16	4,500
	17	Adjusted total income or (loss). Subtract line 16 from line 9 . . . 17		
	18	Income distribution deduction (from Schedule B, line 15). Attach Schedules K-1 (Form 1041)	18	55,500
	19	Estate tax deduction including certain generation-skipping taxes (attach computation)	19	
	20	Exemption	20	100
	21	Add lines 18 through 20 ▶	21	55,600
Tax and Payments	22	Taxable income. Subtract line 21 from line 17. If a loss, see instructions	22	24,900
	23	**Total tax** (from Schedule G, line 7)	23	4,473
	24	**Payments: a** 2015 estimated tax payments and amount applied from 2014 return	24a	4,000
	b	Estimated tax payments allocated to beneficiaries (from Form 1041-T)	24b	
	c	Subtract line 24b from line 24a	24c	4,000
	d	Tax paid with Form 7004 (see instructions)	24d	
	e	Federal income tax withheld. If any is from Form(s) 1099, check ▶ ☐	24e	
		Other payments: f Form 2439 _____ ; g Form 4136 _____ ; Total ▶	24h	
	25	**Total payments.** Add lines 24c through 24e, and 24h ▶	25	
	26	Estimated tax penalty (see instructions)	26	
	27	**Tax due.** If line 25 is smaller than the total of lines 23 and 26, enter amount owed	27	473
	28	**Overpayment.** If line 25 is larger than the total of lines 23 and 26, enter amount overpaid	28	
	29	Amount of line 28 to be: **a Credited to 2016 estimated tax** ▶ ; **b Refunded** ▶	29	

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of fiduciary or officer representing fiduciary | Date | EIN of fiduciary if a financial institution

May the IRS discuss this return with the preparer shown below (see instr.)? ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

For Paperwork Reduction Act Notice, see the separate instructions. Cat. No. 11370H Form **1041** (2015)

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Form 1041 (2015) Page 2

Schedule A **Charitable Deduction.** Do not complete for a simple trust or a pooled income fund.

1	Amounts paid or permanently set aside for charitable purposes from gross income (see instructions)	1	
2	Tax-exempt income allocable to charitable contributions (see instructions)	2	
3	Subtract line 2 from line 1	3	
4	Capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes	4	
5	Add lines 3 and 4	5	
6	Section 1202 exclusion allocable to capital gains paid or permanently set aside for charitable purposes (see instructions)	6	
7	**Charitable deduction.** Subtract line 6 from line 5. Enter here and on page 1, line 13	7	

Schedule B **Income Distribution Deduction**

1	Adjusted total income (see instructions)	1	80,500
2	Adjusted tax-exempt interest	2	18,500
3	Total net gain from Schedule D (Form 1041), line 19, column (1) (see instructions)	3	
4	Enter amount from Schedule A, line 4 (minus any allocable section 1202 exclusion)	4	
5	Capital gains for the tax year included on Schedule A, line 1 (see instructions)	5	
6	Enter any gain from page 1, line 4, as a negative number. If page 1, line 4, is a loss, enter the loss as a positive number	6	-25,000
7	**Distributable net income.** Combine lines 1 through 6. If zero or less, enter -0-	7	74,000
8	If a complex trust, enter accounting income for the tax year as determined under the governing instrument and applicable local law — 8: 80,000		
9	Income required to be distributed currently	9	25,000
10	Other amounts paid, credited, or otherwise required to be distributed	10	55,000
11	Total distributions. Add lines 9 and 10. If greater than line 8, see instructions	11	80,000
12	Enter the amount of tax-exempt income included on line 11	12	18,500
13	Tentative income distribution deduction. Subtract line 12 from line 11	13	61,500
14	Tentative income distribution deduction. Subtract line 2 from line 7. If zero or less, enter -0-	14	55,500
15	**Income distribution deduction.** Enter the smaller of line 13 or line 14 here and on page 1, line 18	15	55,500

Schedule G **Tax Computation** (see instructions)

1	**Tax:** a Tax on taxable income (see instructions)	1a	3,990		
	b Tax on lump-sum distributions. Attach Form 4972	1b			
	c Alternative minimum tax (from Schedule I (Form 1041), line 56)	1c			
	d **Total.** Add lines 1a through 1c ▶			1d	3,990
2a	Foreign tax credit. Attach Form 1116	2a			
b	General business credit. Attach Form 3800	2b			
c	Credit for prior year minimum tax. Attach Form 8801	2c			
d	Bond credits. Attach Form 8912	2d			
e	**Total credits.** Add lines 2a through 2d ▶			2e	
3	Subtract line 2e from line 1d. If zero or less, enter -0-			3	483
4	Net investment income tax from Form 8960, line 21			4	
5	Recapture taxes. Check if from: ☐ Form 4255 ☐ Form 8611			5	
6	Household employment taxes. Attach Schedule H (Form 1040)			6	
7	**Total tax.** Add lines 3 through 6. Enter here and on page 1, line 23 ▶			7	4,473

	Other Information	Yes	No
1	Did the estate or trust receive tax-exempt income? If "Yes," attach a computation of the allocation of expenses. Enter the amount of tax-exempt interest income and exempt-interest dividends ▶ $ 20,000	✓	
2	Did the estate or trust receive all or any part of the earnings (salary, wages, and other compensation) of any individual by reason of a contract assignment or similar arrangement?		✓
3	At any time during calendar year 2015, did the estate or trust have an interest in or a signature or other authority over a bank, securities, or other financial account in a foreign country?		✓
	See the instructions for exceptions and filing requirements for FinCEN Form 114. If "Yes," enter the name of the foreign country ▶		
4	During the tax year, did the estate or trust receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the estate or trust may have to file Form 3520. See instructions		✓
5	Did the estate or trust receive, or pay, any qualified residence interest on seller-provided financing? If "Yes," see the instructions for required attachment		✓
6	If this is an estate or a complex trust making the section 663(b) election, check here (see instructions) ▶ ☐		
7	To make a section 643(e)(3) election, attach Schedule D (Form 1041), and check here (see instructions) ▶ ☐		
8	If the decedent's estate has been open for more than 2 years, attach an explanation for the delay in closing the estate, and check here ▶ ☐		
9	Are any present or future trust beneficiaries skip persons? See instructions		✓

Form **1041** (2015)

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661113

☐ Final K-1 ☐ Amended K-1 OMB No. 1545-0092

Schedule K-1 (Form 1041)
Department of the Treasury
Internal Revenue Service

2015

For calendar year 2015,
or tax year beginning _____, 2015,
and ending _____, 20 _____

Beneficiary's Share of Income, Deductions, Credits, etc.

▶ See back of form and instructions.

Part I Information About the Estate or Trust

A Estate's or trust's employer identification number

11-1111111

B Estate's or trust's name

GREEN TRUST

C Fiduciary's name, address, city, state, and ZIP code

WISCONSIN STATE NATIONAL BANK, TRUSTEE
3100 EAST WISCONSIN AVENUE
MILWAUKEE, WI 53201

D ☐ Check if Form 1041-T was filed and enter the date it was filed

_____

E ☐ Check if this is the final Form 1041 for the estate or trust

Part II Information About the Beneficiary

F Beneficiary's identifying number

123-45-6789

G Beneficiary's name, address, city, state, and ZIP code

MARCUS WHITE
9880 EAST NORTH AVENUE
SHOREWOOD, WI 53211

H ☒ Domestic beneficiary ☐ Foreign beneficiary

Part III Beneficiary's Share of Current Year Income, Deductions, Credits, and Other Items

1	Interest income: 23,587	11	Final year deductions
2a	Ordinary dividends: 5,184		
2b	Qualified dividends: 5,184		
3	Net short-term capital gain		
4a	Net long-term capital gain		
4b	28% rate gain	12	Alternative minimum tax adjustment
4c	Unrecaptured section 1250 gain		
5	Other portfolio and nonbusiness income		
6	Ordinary business income		
7	Net rental real estate income	13	Credits and credit recapture
8	Other rental income		
9	Directly apportioned deductions		
		14	Other information
		A	9,591
10	Estate tax deduction	E	28,771

*See attached statement for additional information.

Note. A statement must be attached showing the beneficiary's share of income and directly apportioned deductions from each business, rental real estate, and other rental activity.

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CHAPTER 7

DEDUCTIONS AND LOSSES: CERTAIN BUSINESS EXPENSES AND LOSSES

SOLUTIONS TO PROBLEM MATERIALS

DISCUSSION QUESTIONS

1. (LO 1) An account receivable can give rise to a bad debt deduction if income arising from the creation of the account receivable was previously included in gross income.

2. (LO 1) Ron has no bad debt deduction because he is a cash basis taxpayer. Rather, Ron has $70,000 of income.

3. (LO 1) A loss is deductible only in the year of total worthlessness for a nonbusiness bad debt and is classified as a short-term capital loss.

4. (LO 1) The business bad debt is treated as an ordinary loss; hence, the fact that the business has long-term capital gains has no relevance.

5. (LO 1) Jack should be concerned with the following issues:

   - Should this be treated as a worthless security?
   - Should this be treated as a theft loss?
     - Does the theft loss create an NOL?
     - Can the NOL be carried back three years?
   - Is it § 1244 stock?

6. (LO 2) Sean cannot take the loss as a business bad debt because a bond is a security. Sean cannot take the loss as a worthless security because losses are allowed only when the security is completely worthless.

7. (LO 2) The gain on the sale of § 1244 stock is treated as a capital gain.

8. (LO 3, 4) Some courts have held that termite damage over periods of up to 15 months after infestation constituted a sudden event and was, therefore, deductible as a casualty loss. However, the current position of the IRS is that termite damage is not deductible (it is not considered a sudden event).

9. (LO 3, 4) Casualty losses are not allowed for a decline in the value of the property. Losses are allowed only for actual damage.

10. (LO 4) Generally, a theft loss is deducted in the year of discovery. However, no theft loss is permitted if a reimbursement claim with a reasonable prospect of full recovery exists. If the taxpayer has a partial claim of recovery, only part of the loss can be claimed in the year of discovery, and the remainder is deducted in the year the claim is settled.

11. (LO 4) The cost of repairs can be used as a method for measuring the amount of a casualty loss if the repairs are necessary to restore the property to its condition before the casualty, the amount spent for the

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repairs is not excessive, and the repairs do not extend beyond the damage suffered. In addition, the value of the property after the repairs must not, as a result of the repairs, exceed the value of the property immediately before the casualty.

12. (LO 4) If the painting is treated as personal use property, the amount of the loss is limited to $20,000 and is subject to the $100 and 10%-of-AGI floors. However, if the painting is treated as investment property, the loss is $20,000 and is treated as an other miscellaneous itemized deduction and is not subject to the 2%-of-AGI floor. Hence, all of the $20,000 could be taken as a deduction.

13. (LO 4) Kelly should be concerned with the following issues:

- Is this a theft loss?
- What is the amount of the loss?
- In which year can the loss be taken?

14. (LO 3, 4) The tax issues for John are as follows:

- Is the loss a theft loss or an investment loss?
- Is the loss subject to either the personal loss limits ($100 floor and 10%-of-AGI floor) or the limits on itemized deductions (2%-of-AGI floor)?
- How is the amount of the loss determined?
- What year can the loss be taken?

15. (LO 5) Research and experimental expenditures are usually amortized rather than expensed when a company does not have sufficient income to offset the expenses.

16. (LO 6) The tax issues for Silver, Inc., are as follows:

- Is the extraction and processing of silver ore a manufacturing activity?
- Can the deduction be taken for prior years?
- What laws will apply for prior years?

17. (LO 6) DPAD is a deduction that is determined in a unique manner. Unlike most deductions that are generated by expenditures, DPAD is based on income. If certain production activities produce a profit, DPAD is a percentage of that profit (but cannot exceed 50% of specified wages). Consequently, the larger the profit, the larger the deduction. Of course, the profit increases the income tax, whereas the deduction reduces the income tax.

18. (LO 7) Individual Retirement Account deductions and alimony paid deductions are deductions *for* AGI. However, they are treated as nonbusiness deductions in computing an individual's NOL.

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COMPUTATIONAL EXERCISES

19. (LO 1) Jane must include the $10,000 in gross income of the current tax year, but only to the extent of the tax benefit in the previous year. Because Jane had capital gains of $5,000 in the previous year, $8,000 of the $50,000 bad debt would have been deducted last year ($5,000 + $3,000). Hence, Jane would have to include $8,000 of the $10,000 received in gross income in the current year.

20. (LO 1) Bob has no bad debt deduction. Rather, he has income of $12,000 [$60,000 − $48,000 (basis in the account receivable)].

21. (LO 2) It is possible to receive an ordinary loss deduction if the loss is sustained on small business stock (§ 1244 stock). Only individuals who acquired the stock from the corporation are eligible to receive ordinary loss treatment under § 1244. The ordinary loss treatment is limited to $50,000 ($100,000 for married individuals filing jointly) per year. Losses on § 1244 stock in excess of the statutory limits receive capital loss treatment.

    Therefore, Calvin's total loss of $61,750 ($68,750 − $7,000) is treated as follows: $50,000 is ordinary loss, and the remaining $11,750 ($61,750 − $50,000) is long-term capital loss.

22. (LO 4) Mary should include the recovery as gross income in her 2016 tax return, but only to the extent of the tax benefit in the prior year. Mary's deduction in the prior year would have been $3,900 computed as follows:

Amount of loss	$ 8,000
Less: $100 floor	(100)
10% × 40,000	(4,000)
Deduction	$ 3,900

    Therefore, Mary must include $3,900 in gross income in 2016.

23. (LO 4) The amount of the loss is $600,000, the lesser of the decline in FMV $600,000 ($800,000 − $200,000) or basis of $650,000.

24. (LO 4) For partial or complete destruction of personal use property, the loss is the lesser of the following:

    - The adjusted basis of the property.
    - The difference between the fair market value of the property before the event and the fair market value immediately after the event.

    Any insurance recovery reduces the loss. The amount of the loss for personal use property must be further reduced by a $100-per-event floor and a 10%-of-AGI aggregate floor. The $100 floor applies separately to each casualty loss. The loss is then reduced by 10% of the taxpayer's AGI. The resulting loss is the taxpayer's itemized deduction for casualty and theft losses.

    Belinda's casualty loss deduction is $200 [$14,000 basis − $10,000 insurance recovery − $100 floor – $3,700 (10% × $37,000 AGI)]. The $200 casualty loss is an itemized deduction (from AGI).

25. (LO 4) A taxpayer who has both gains and losses for the taxable year must first net (offset) the personal casualty gains and personal casualty losses. If the gains exceed the losses, the gains and losses are treated as gains and losses from the sale of capital assets. The capital gains and losses are short-term or long-term, depending on the period the taxpayer held each of the assets.

    In the netting process, personal casualty and theft gains and losses are not netted with the gains and losses on business and income-producing property.

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Tucker has a net casualty gain of $1,050 ($1,500 + $750 − $1,200). Therefore, he treats all of the gains and losses as capital gains and losses:

Long-term capital loss (Asset 1) $ 1,200.
Short-term capital gain (Asset 2) $750.
Long-term capital gain (Asset 3) $1,500.

Note: If personal casualty losses exceed personal casualty gains, all gains and losses are treated as ordinary items. The gains—and the losses to the extent of gains—are treated as ordinary income and ordinary loss in computing AGI. Losses in excess of gains are deducted as itemized deductions to the extent the losses exceed 10% of AGI.

26. (LO 5) Research and experimental expenditures may be deferred and amortized if the taxpayer makes an election. Under the election, research and experimental expenditures are amortized ratably over a period of not less than 60 months. A deduction is allowed beginning with the month in which the taxpayer first realizes benefits from the experimental expenditure. The election is binding, and a change requires permission from the IRS.

Because the benefits from the project will be realized starting in July 2017, Sandstorm Corporation has no deduction prior to July 2017, the month benefits from the project begin to be realized. The deduction for 2017 is $12,750, computed as follows:

($85,000 + $30,000 + $12,500 = $127,500).
$127,500 × 6 months /60 months = $12,750.

27. (LO 6) The formula is 9% × Lesser of (1) Qualified production activities income (QPAI) or (2) Taxable (or modified adjusted gross) income or alternative minimum taxable income. In addition, the amount of the DPAD cannot exceed 50% of certain W–2 wages paid by the taxpayer during the tax year.

The DPAD is computed as follows:

9% of the lesser of $4,500,000 or $3,100,000 or 9% × $3,100,000 = $279,000. However, the $279,000 is subject to the 50% of W–2 wages limitation or $107,000 (50% × $214,000). Therefore, the deduction for 2016 is only $107,000.

PROBLEMS

28. (LO 1)

Hoffman, Maloney, Raabe, & Young, CPAs
5191 Natorp Boulevard
Mason, OH 45040

January 29, 2017

Mr. John Johnson
100 Tyler Lane
Erie, PA 16563

Dear Mr. Johnson:

This letter is to inform you of the possibility of taking a bad debt deduction.

Your loan to Sara is a business bad debt; therefore, you are allowed to take a bad debt deduction for partial worthlessness. You will be able to take a bad debt deduction in the current year of $25,000 [($30,000 − $1,000) − $4,000].

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Should you need more information or need to clarify anything, please contact me.

Sincerely,

John J. Jones, CPA
Partner

TAX FILE MEMORANDUM

DATE: January 29, 2017

FROM: John J. Jones

SUBJECT: Bad Debt Deduction

John Johnson's $30,000 loan to Sara is a business bad debt. Therefore, a bad debt deduction is allowed for partial worthlessness. John will be able to claim a bad debt deduction in the current year of $25,000 [($30,000 − $1,000) − $4,000].

29. (LO 1) Monty must include up to $10,000 in gross income, but only to the extent of a tax benefit in a prior year. Because the debt is a nonbusiness bad debt, the $11,000 would have been reported as a short-term capital loss. Last year, Monty had capital gains of $4,000 and taxable income of $20,000. Therefore, $7,000 of the $11,000 loss produced a tax benefit ($4,000 + $3,000). Hence, only $7,000 would be included in Monty's gross income this year.

30. (LO 1) Sally has no bad debt deduction. Sally has income of $5,000 ($65,000 − $60,000) because she collected more than her basis in the receivable.

31. (LO 1, 2)

Salary		$120,000
§ 1244 ordinary loss (limit of $100,000)		(100,000)
Short-term capital gain on § 1244 stock	$ 20,000	
Short-term capital loss (nonbusiness bad debt)	(19,000)	
Net short-term capital gain	$ 1,000	
Net long-term capital loss (remaining § 1244 loss)	(5,000)	
Net capital loss (limited to $3,000; $1,000 LTCL carryover)		(3,000)
Adjusted gross income		$ 17,000

32. (LO 2, 8) Sell all of the stock in the current year:

Current year's AGI		
Salary		$ 80,000
Ordinary loss (§ 1244 limit)		(50,000)
Long-term capital gain	$ 8,000	
Long-term capital loss ($80,000 − $50,000)	(30,000)	
Long-term capital loss (limited to $3,000; $19,000 LTCL carryover)		(3,000)
AGI		$ 27,000
Next year's AGI		
Salary		$ 90,000
Long-term capital gain	$ 10,000	
Long-term capital loss carryover ($30,000 − $11,000)	(19,000)	
Long-term capital loss (limited to $3,000; $6,000 LTCL carryover)		(3,000)
AGI		$ 87,000

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Total AGI	
Current year	$ 27,000
Next year	87,000
Total	$114,000

Sell half of the stock this year and half next year:

Current year's AGI	
Salary	$ 80,000
Ordinary loss (§ 1244 stock)	(40,000)
Long-term capital gain	8,000
AGI	$ 48,000

Next year's AGI	
Salary	$ 90,000
Ordinary loss (§ 1244 stock)	(40,000)
Long-term capital gain	10,000
AGI	$ 60,000

Total AGI	
Current year	$ 48,000
Next year	60,000
Total	$108,000

Mary's combined AGI for the two years is lower if she sells half of her § 1244 stock this year and half next year.

33. (LO 3, 4, 8) The amount of the loss before the 10%-of-AGI limitation is computed as follows:

Home ($350,000 − $280,000)	$70,000
Auto ($30,000 − $20,000)	10,000
Total loss	$80,000
Less: $100	(100)
Loss before 10% of AGI	$79,900

Because the President declared the area a disaster area, Olaf and Anna could claim the loss on last year's return (2015) or on the current year's return (2016).

Amount of loss on last year's return:	
Loss	$ 79,900
Less: 10% of AGI (10% × $180,000)	(18,000)
Total loss	$ 61,900

Amount of loss on current year's return:	
Loss	$ 79,900
Less: 10% of AGI (10% × $300,000)	(30,000)
Total loss	$ 49,900

If Olaf and Anna apply the loss to 2015, the benefit of the loss will be at a rate of 25% because taxable income will be $78,100 ($140,000 − $61,900) and the loss falls entirely within the 25% tax bracket. If the loss is applied to 2016, the benefit will be at a rate of 28% because taxable income will be $165,100 ($215,000 − $49,900) and the loss falls entirely within the 28% tax bracket. The tax savings will be $15,475 (25% × $61,900) if the loss is taken in 2015 and $13,972 (28% × $49,900) if the loss is taken in 2016. Therefore, Olaf and Anna should include the loss on their 2015 return, because the tax savings is $1,503 ($15,475 − $13,972) greater.

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34. (LO 3, 4)

	Total	Business Portion (40%)	Personal Portion (60%)
Cost	$ 800,000	$ 320,000	$480,000
Depreciation	(100,000)	(100,000)	(–0–)
Adjusted basis	$ 700,000	$ 220,000	$480,000
Loss on building:			
Loss ($900,000 − $200,000)	$ 700,000	$ 220,000*	$420,000
Less: Insurance reimbursement	$ 600,000	(240,000)	(360,000)
Loss (gain)		($ 20,000)	$ 60,000
Business contents loss			$220,000
Less: Insurance recovery			(175,000)
Loss			$ 45,000
Personal casualty gain—contents ($65,000 insurance proceeds − $50,000 adjusted basis)			$ 15,000
Personal casualty loss—building			($ 60,000)
AGI before effects of accident			$100,000
Business gain—building			20,000
Business loss—contents			(45,000)
Personal casualty gain			15,000
Personal casualty loss to extent of gain			(15,000)
AGI			$ 75,000
Personal casualty loss—building ($60,000 − $15,000 − $100)			($ 44,900)
Less: 10%-of-AGI floor (10% × $75,000)			7,500
Itemized deduction			($ 37,400)

*Adjusted basis is less than the decline in FMV of $280,000 ($700,000 × 40%).

35. (LO 3, 4)

Hoffman, Maloney, Raabe, & Young, CPAs
5191 Natorp Boulevard
Mason, OH 45040

January 26, 2017

Mr. Sam Smith
450 Colonel's Way
Warrensburg, MO 64093

Dear Mr. Smith:

This letter is to inform you of the tax and cash flow consequences of filing a claim versus not filing a claim with your insurance company for reimbursement for damages to your business use car.

If an insurance claim is filed, you will have a taxable gain of $2,000 computed as follows:

Insurance recovery	$ 12,000
Less: Lesser of adjusted basis of $10,000 or decline of FMV of $12,000	(10,000)
Gain	$ 2,000

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This will produce a net cash flow of $11,300 computed as follows:

Insurance reimbursement received	$12,000
Less: Tax on gain (35% × $2,000)	(700)
Net cash flow	$11,300

If no insurance claim is filed, you will have a deductible loss of $10,000, which will reduce your tax liability by $3,500 (35% × $10,000); see Concept Summaries 7.3 and 7.4.

The net cash benefit resulting from filing an insurance reimbursement claim would be $7,800 ($11,300 − $3,500).

Should you need more information or need to clarify anything, please contact me.

Sincerely,

John J. Jones, CPA
Partner

TAX FILE MEMORANDUM

DATE: January 26, 2017

FROM: John J. Jones

SUBJECT: Tax consequences for Sam Smith if he does not file an insurance claim for reimbursement for damages to his business use car

If an insurance claim is filed, Sam will have a taxable gain of $2,000 computed as follows:

Insurance recovery	$ 12,000
Less: Lesser of adjusted basis of $10,000 or decline of FMV of $12,000	(10,000)
Gain	$ 2,000

This will produce a net cash flow of $11,300 computed as follows:

Insurance reimbursement received	$12,000
Less: Tax on gain (35% × $2,000)	(700)
Net cash flow	$11,300

If no insurance claim is filed, Sam will have a deductible loss of $10,000, which will reduce his tax liability by $3,500 (35% × $10,000); see Concept Summaries 7.3 and 7.4.

In my correspondence with Sam, I pointed out that the net cash benefit from filing an insurance reimbursement claim would be $7,800 ($11,300 − $3,500).

36. (LO 5)

a.

2016	
Salaries	$500,000
Materials	90,000
Insurance	8,000
Utilities	6,000
Equipment depreciation	15,000
Total expenses	$619,000

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Cost of inspection of materials for quality control ($7,000), promotion expenses ($11,000), and cost of market survey ($8,000) are not included as research and experimental expenditures.

2017	
Salaries	$600,000
Materials	70,000
Insurance	11,000
Utilities	8,000
Equipment depreciation	14,000
Total expenses	$703,000

Cost of inspection of materials for quality control ($6,000), advertising ($20,000), and promotion expenses ($18,000) are not included as research and experimental expenditures.

2018
No deduction based on data provided.

b. The research and experimental expenditures are amortized over a 60-month period beginning with the month in which the taxpayer first realizes benefits from the experimental expenditures (i.e., July 2018 for Blue Corporation). The monthly amortization is $22,033 ($1,322,000 ÷ 60).

2016
No deduction for research and experimental expenditures.

2017
No deduction for research and experimental expenditures.

2018
Deduction for research and experimental expenditures:
$22,033 × 6 months = $132,198

37. (LO 6) Sarah's DPAD is $30,000 [9% × $350,000 (the smaller of $350,000 modified AGI or $400,000 QPAI)] [not to exceed $30,000 (50% × $60,000 of W–2 wages)].

38. (LO 6) Barbara's DPAD is $45,000 [9% × $500,000 (the smaller of $500,000 AGI and $550,000 QPAI)].

39. (LO 6) Red Corporation's taxable income for the year is $1,200,000 ($2,000,000 − $800,000 NOL). This is not less than the QPAI ($1,000,000); hence, the QPAD is $90,000 (9% × $1,000,000). This assumes that the QPAD is not limited by W–2 wages.

40. (LO 6) The QPAI for a skirt is $6 ($12 − $5 − $1). The QPAI for a blouse is a negative $1 ($10 − $6 − $5). Green must net the two items to arrive at the QPAI of $5 ($6 − $1).

41. (LO 6)
a. The DPAD is $200,000 (50% × $400,000 associated W–2 wages), which is less than $270,000 (9% × $3,000,000).

b. Because the wage base limits the deduction, Rose may want to outsource less of its work.

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42. (LO 1, 3)

Salary		$50,000
Interest income		3,000
Business bad debt		(2,000)
Nonbusiness bad debt (short-term capital loss)	($6,000)	
Short-term capital loss	(3,000)	
Total short-term capital loss	($9,000)	
Long-term capital gain	4,000	
Net short-term capital loss	($5,000)	
Capital loss limit		(3,000)
Adjusted gross income		$48,000

43. (LO 1, 4)

Salary		$50,000
Interest income		3,000
Business bad debt		(2,000)
Nonbusiness bad debt	($ 6,000)	
Short-term capital loss	(3,000)	
Total short-term capital loss	($ 9,000)	
Short-term capital gain*	10,000	
Net short-term capital gain		1,000
Long-term capital gain	$ 4,000	
Long-term capital loss*	(1,000)	
Net long-term capital gain		3,000
Adjusted gross income		$55,000

*Personal casualty gains exceed personal casualty losses ($10,000 − $1,000 = $9,000); therefore, all personal casualty items are treated as capital gains and losses.

CUMULATIVE PROBLEMS

44. *Part 1—Tax Computation*

Salary and bonus ($100,000 + $1,000)			$101,000
Typing service business net receipts ($20,000 − $24,580)			(4,580)
Interest income (Note 1)			700
Life insurance proceeds (Note 2)			–0–
Gift (Note 3)			–0–
Bingo prize			100
Alimony			10,000
Nonbusiness bad debt (Note 4)			(2,100)
Adjusted gross income			$105,120
Less: Itemized deductions			
Home mortgage interest		$9,500	
Charitable contributions		2,500	
Sales taxes		946	
Property taxes		1,100	
Silverware loss: Lesser of adjusted basis of $14,000 or FMV of $15,000	$14,000		
Less: Insurance proceeds	(1,500)		
Less: $100	(100)	$12,400	
Auto: Lesser of decline in FMV ($7,000) or adjusted basis ($52,000)	$ 7,000		
Less: Insurance proceeds if claim filed	(2,000)		
Less: $100	(100)	4,900	

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Total	$17,300		
Less: 10% of AGI	(10,512)	6,788	
Total itemized deductions			(20,834)
Less: Personal exemption			(4,000)
Taxable income			$ 80,286
Tax on taxable income (from Tax Table)			$ 15,863
Less: Federal income tax withheld and estimated tax payments ($16,000 + $1,000)			(17,000)
Net tax payable (or refund due) for 2015			($ 1,137)

See the tax return solution beginning on p. 7-19 of the Solutions Manual.

Notes

(1) The $800 interest on the City of Boca Raton bonds is tax-exempt.

(2) Life insurance proceeds of $60,000 payable as the result of the death of Jane's sister are excludible from gross income.

(3) The $5,000 gift from Jane's aunt is excludible from gross income.

(4) The $2,100 loss on the loan to her friend, Joan Jensen, is deductible as a nonbusiness bad debt (i.e., short-term capital loss). The loan is a bona fide loan.

Part 2—Tax Planning

Salary and bonus			$ 101,000
Gross receipts from business		$26,000	
Less:			
Office rent	$7,000		
Supplies	4,840		
Utilities and telephone	5,148		
Wages	5,500		
Payroll taxes	550		
Equipment rentals	3,300	(26,338)	
Net business income			(338)
Interest income			700
Alimony			10,000
Adjusted gross income			$ 111,362
Less:			
Itemized deductions		$14,046	
Personal exemption		4,050	(18,096)
Taxable income			$ 93,266
Tax on $93,266 [$18,558.75 + .28($93,266 − $91,150)]			$ 19,151
Less: Federal income tax withheld			(16,000)
Net tax payable (or refund due)			$ 3,151

Jane would need to make estimated tax payments of $3,151 for 2016 because the Federal income tax withholdings are expected to be less than the tax liability.

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Hoffman, Maloney, Raabe, & Young, CPAs
5191 Natorp Boulevard
Mason, OH 45040

January 26, 2016

Ms. Jane Smith
2020 Oakcrest Road
Boca Raton, FL 33431

Dear Ms. Smith:

This letter is in response to your request concerning the minimum amount of estimated tax you must pay for 2016 so that you will not have to pay any additional tax upon filing your 2016 Federal income tax return.

Based on the 2016 estimates you provided to us, we have determined that your estimated tax payments for the 2016 calendar year should total $3,151. This estimate is based on the following computation.

Salary and bonus			$101,000
Gross receipts from business		$26,000	
Less:			
Office rent	$7,000		
Supplies	4,840		
Utilities and telephone	5,148		
Wages	5,500		
Payroll taxes	550		
Equipment rentals	3,300	(26,338)	
Net business income			(338)
Interest income			700
Alimony			10,000
Adjusted gross income			$111,362
Less:			
Itemized deductions		$14,046	
Personal exemption		4,050	(18,096)
Taxable income			$ 93,266
Tax on $93,266			$ 19,151
Less: Federal income tax withheld			(16,000)
Net tax payable (or refund due)			$ 3,151

Should you need more information or want to clarify anything, please contact me.

Sincerely yours,

John J. Jones, CPA
Partner

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TAX FILE MEMORANDUM

DATE: January 10, 2016

FROM: John J. Jones

SUBJECT: Jane Smith's 2016 estimated tax

Today I talked with Jane Smith concerning her 2016 estimated tax. She wanted to know the minimum amount of estimated tax she would have to pay for the calendar year 2016 so that she would not have to pay any additional tax upon filing her 2016 Federal income tax return.

In addition to the gross receipts from her typing business increasing to $26,000 (from $20,000 in 2015), the following projections for 2016 were provided by Jane Smith:

(1) Items remaining unchanged from 2015:

	2015	2016
Salary	$100,000	$100,000
Christmas bonus	$1,000	$1,000
Itemized deductions	$14,046	$14,046
Interest income	$700	$700
Alimony	$10,000	$10,000
Office rent expense	$7,000	$7,000

(2) Business expenses expected to increase by 10% from 2015 to 2016:

	2015	2016
Supplies	$4,400	$4,840
Utilities and telephone	$4,680	$5,148
Wages	$5,000	$5,500
Payroll taxes	$500	$550
Equipment rentals	$3,000	$3,300

(3) The following 2015 items will not recur in 2016: life insurance proceeds ($60,000), gift ($5,000), bingo winnings ($100), bad debt ($2,100), stolen silverware, auto accident.

Based on this estimated information for 2016, Jane Smith should make 2016 estimated tax payments totaling $3,151. The determination was made as follows:

Salary and bonus			$101,000
Gross receipts from business		$26,000	
Less:			
Office rent	$7,000		
Supplies	4,840		
Utilities and telephone	5,148		
Wages	5,500		
Payroll taxes	550		
Equipment rentals	3,300	(26,338)	
Net business income			(338)
Interest income			700
Alimony			10,000
Adjusted gross income			$111,362
Less:			
Itemized deductions		$14,046	
Personal exemption		4,050	(18,096)
Taxable income			$ 93,266
Tax on $93,266			$ 19,151
Less: Federal income tax withheld			(16,000)
Net tax payable (or refund due)			$ 3,151

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45.

Salary			$140,000
Rental income		$60,000	
Less: Rental expenses		(33,000)	27,000
Casualty loss on rental property			(10,000)
Bad debt on uncollected rent (Note 1)			(–0–)
Rent collected from prior year (Note 2)			6,000
Ordinary loss on § 1244 stock (Note 3)			(100,000)
Short-term capital loss—limit (Note 4)			(3,000)
AGI			$ 60,000
Less: Itemized deductions			
Personal casualty loss	$20,000		
Less: $100 floor	(100)		
Less: 10% AGI	(6,000)		(13,900)
Loss on investment property (painting)			(8,000)
Loss on computer	$ 5,000		
Less: 2% AGI	(1,200)		(3,800)
Other itemized deductions			(18,000)
Less: Personal exemptions (2 × $4,050)			(8,100)
Taxable income			$ 8,200
Tax on $8,200 (Note 5)			$ 820
Income tax withholdings			(3,000)
Net tax payable (or refund due) for 2016			($ 2,180)

Notes

(1) No bad debt deduction on uncollected rents can be taken because Mason and Ruth are cash basis taxpayers.

(2) Rent collected from prior year must be included in gross income because Mason and Ruth are cash basis taxpayers.

(3) The loss of up to $100,000 on the § 1244 stock is classified as ordinary loss.

(4) The additional $5,000 loss on § 1244 stock is short-term capital loss. Only $3,000 of the loss can be used to offset ordinary income.

(5) Mason and Ruth's filing status is married filing jointly.

Tax on $8,200: $8,200 × 10% = $820

RESEARCH PROBLEMS

1. This fact pattern is similar to *Clifford L. Brody and Barbara J. De Clerk*, T.C. Summary Opinion, 2004–149. In this case, the petitioners were not allowed to claim their payment of the portion of the loan that they contend was the responsibility of the corporation as a bad debt deduction under § 166. The record indicated that the loan was a personal loan between the bank and petitioners and not a loan from petitioners to the corporation. In addition, it appeared likely that the corporation was capable of eventually paying its alleged share of the debt if necessary.

2. The fact pattern in this situation is similar to the fact pattern in *Mark D. Ambrose and Jennifer L. Ambrose v. The United States*, 2012–2 USTC ¶50,518 (Ct. Cl., 2012). In this case, the Court held that taxpayers were not barred from claiming a casualty loss deduction for damage to their home due to fire despite their insurance company's denial of their recovery for failure to provide timely proof of loss. The Regulations clearly distinguish between the claim requirement under Code § 165(h)(5)(E) and the proof a policy required as a precondition to recovery.

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3. The key is to determine in which year the casualty was sustained. Reg. § 1.165–1(a) provides that a casualty or theft loss is deductible in the year the loss was "actually sustained" but does not clarify what "actually sustained" means. Thus, we look to case law for additional guidance. In *Oregon Mesabi Corp. v. CIR*, 39 BTA 1033 (1939), appeal dismissed, *Com'r v. Oregon Mesabi Corporation*, 24 AFTR 458 (109 F2d 1014) (CA 9, 1940), fire killed trees in 1933. However, the timber was rendered worthless when attacked by insects and fungi in 1934 and 1935. The court determined that a loss deduction was not necessarily taken in the year of the fire, but in the years, as shown by the evidence, that worthlessness occurred. As a result, Esther's loss is deductible in 2016, the year in which the trees died from disease. Despite the fact that the trees were weakened by the hurricane, they were not worthless until they died of disease.

Research Problems 4 and 5

The Internet Activity research problems require that students utilize online resources to research and answer the questions. As a result, solutions may vary among students and courses. You should determine the skill and experience levels of the students before assigning these problems, coaching where necessary. Encourage students to explore all parts of the Web in this research process, including tax research databases, as well as the websites of the IRS, newspapers, magazines, businesses, tax professionals, other government agencies, and political outlets. Students should also work with resources such as blogs, Twitter feeds, and other interest-oriented technologies to research their answers.

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CHECK FIGURES

19. $8,000.
20. No bad debt deduction; gain of $12,000.
21. $50,000 ordinary loss; $11,750 long-term capital loss.
22. $3,900.
23. $600,000.
24. $200.
25. $1,050 personal casualty gain.
26. 2016 $0; 2017 $12,750.
27. $107,000.
28. In the year of partial worthlessness.
29. Include $7,000 in gross income.
30. No bad debt deduction; gain of $5,000.
31. $17,000.
32. Mary should sell half each year.
33. $79,900 loss should be taken in prior year.
34. AGI of $75,000; $37,400 itemized deduction.
35. Net cash benefit of $7,800 of filing an insurance claim.
36.a. 2016 $619,000; 2017 $703,000; 2018 $0.
36.b. 2016 $0; 2017 $0; 2018 $132,198.
37. $30,000.
38. $45,000.
39. $90,000.
40. $5 ($6 − $1).
41.a. $200,000.
42. $48,000.
43. $55,000.
44. Refund due for 2015 $1,137.
45. Refund due for 2016 $2,180.

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SOLUTION TO ETHICS & EQUITY FEATURE

Is Policy Cancellation an Escape Hatch? (p. 7-11). Section 165(h)(5)(E), enacted in 1986, states that "[a]ny loss of an individual described in subsection (c)(3) to the extent covered by insurance shall be taken into account under this section only if the individual files a timely insurance claim with respect to such loss."

Prior to the enactment of § 165(h)(5)(E), a number of courts considered whether under § 165(a) a taxpayer's election not to file an insurance claim for a loss precluded him or her from deducting the loss. In these cases, which involved casualty or theft losses, the IRS argued that the loss in question derived not from the casualty or theft itself, but from the taxpayer's intervening decision not to file an insurance claim. It contended that as a result of the latter decision, the deduction did not correspond to a loss "sustained . . . and not compensated for by insurance or otherwise," as required by § 165(a). *See* Rev.Rul. 78–141, 1978 C.B. 57 (1978).

While this argument met some initial success (see, for example, *Kentucky Utilities Co. v. Glenn*, 394 F.2d 631 (6th Cir. 1968), ultimately it was soundly rejected by the courts—first by the specialized U.S. Tax Court and then by various appellate decisions affirming the decisions of that tax tribunal. See *Miller v. Comm.*, 733 F.2d 399 (6th Cir. 1984), *aff'g*, 42 T.C.M. (CCH) 665 (1981); *Hills v. Comm.*, 691 F.2d 997 (11th Cir. 1982), *aff'g*, 76 T.C. 484 (1981).

In these cases, the taxpayers were allowed to deduct casualty losses under § 165 even though they failed to file insurance claims.

In the Tax Reform Act of 1986, Congress intervened, denying a loss deduction under § 163(c)(3) for any loss covered by insurance unless "the individual files a timely insurance claim with respect to such loss." Citing *Hills* and *Miller*, the accompanying House Committee Report noted that "[c]ertain courts have ruled that a taxpayer whose loss was covered by an insurance policy could nevertheless deduct the loss if the taxpayer decided not to file a claim under the terms of the insurance policy." H.R. Rep. No. 99–426, at 658 (1985). It then continues with the following rationale for § 165(h)(5)(E):

The deduction for personal casualty losses should be allowed only when a loss is attributable to damages to property that is caused by one of the specified types of casualties. Where the taxpayer has the right to receive insurance proceeds that would compensate for the loss, the loss suffered by the taxpayer is not damage to property caused by the casualty. Rather, the loss results from the taxpayer's personal decision to forego [*sic*] making a claim against the insurance company. The committee believes that losses resulting from a personal decision of the taxpayer should not be deductible as a casualty loss.

Under the bill, a taxpayer is not permitted to deduct a casualty loss for damages to property . . . unless the taxpayer files a timely insurance claim with respect to damages to that property.

As a result, Noah's casualty loss deduction will be disallowed by the IRS.

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SOLUTIONS TO ROGER CPA REVIEW QUESTIONS

Detailed answer feedback for Roger CPA Review questions is available on the instructor companion site (www.cengage.com/login).

1. a
2. a
3. b
4. c
5. d

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44.

Form **1040** Department of the Treasury—Internal Revenue Service (99) **U.S. Individual Income Tax Return** **2015** OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2015, or other tax year beginning , 2015, ending , 20 See separate instructions.

Your first name and initial	Last name	Your social security number
JANE	SMITH	123-45-6789
If a joint return, spouse's first name and initial	Last name	Spouse's social security number

Home address (number and street). If you have a P.O. box, see instructions. Apt. no.
2020 OAKCREST

▲ Make sure the SSN(s) above and on line 6c are correct.

City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions).
BOCA RATON FL 33431

Foreign country name | Foreign province/state/county | Foreign postal code

Presidential Election Campaign
Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund [X] You [ ] Spouse

Filing Status Check only one box.

1 [X] Single
2 [ ] Married filing jointly (even if only one had income)
3 [ ] Married filing separately. Enter spouse's SSN above and full name here. ▶
4 [ ] Head of household (with qualifying person). (See instr.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 [ ] Qualifying widow(er) with dependent child

Exemptions

6a [X] **Yourself.** If someone can claim you as a dependent, **do not** check box 6a
b [ ] **Spouse**

c **Dependents:** (1) First name Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) X if child under age 17 qualifying for child tax credit (see instructions)

If more than four dependents, see instructions and check here ▶ [ ]

d Total number of exemptions claimed

Boxes checked on 6a and 6b: 1
No. of children on 6c who:
• lived with you
• did not live with you due to divorce or separation (see instructions)
Dependents on 6c not entered above
Add numbers on lines above ▶: 1

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a W-2, see instructions.

7	Wages, salaries, tips, etc. Attach Form(s) W-2		7	101,000
8a	**Taxable** interest. Attach Schedule B if required		8a	700
b	**Tax-exempt** interest. **Do not** include on line 8a	8b 800		
9a	Ordinary dividends. Attach Schedule B if required		9a	0
b	Qualified dividends	9b 0		
10	Taxable refunds, credits, or offsets of state and local income taxes		10	0
11	Alimony received		11	10,000
12	Business income or (loss). Attach Schedule C or C-EZ		12	-4,580
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ [ ]		13	-2,100
14	Other gains or (losses). Attach Form 4797		14	
15a	IRA distributions 15a	b Taxable amount	15b	0
16a	Pensions and annuities 16a	b Taxable amount	16b	0
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E		17	
18	Farm income or (loss). Attach Schedule F		18	0
19	Unemployment compensation		19	
20a	Social security benefits 20a	b Taxable amount	20b	
21	Other income. List type and amount GAMBLING		21	100
22	Combine the amounts in the far right column for lines 7 through 21. This is your **total income** ▶		22	105,120

Adjusted Gross Income

23	Educator expenses	23 0		
24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24 0		
25	Health savings account deduction. Attach Form 8889	25 0		
26	Moving expenses. Attach Form 3903	26 0		
27	Deductible part of self-employment tax. Attach Schedule SE	27 0		
28	Self-employed SEP, SIMPLE, and qualified plans	28 0		
29	Self-employed health insurance deduction	29		
30	Penalty on early withdrawal of savings	30 0		
31a	Alimony paid b Recipient's SSN ▶	31a		
32	IRA deduction	32 0		
33	Student loan interest deduction	33		
34	Tuition and fees. Attach Form 8917	34		
35	Domestic production activities deduction. Attach Form 8903	35 0		
36	Add lines 23 through 35		36	0
37	Subtract line 36 from line 22. This is your **adjusted gross income** ▶		37	105,120

KIA **For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions.** Form **1040** (2015)

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Access Complete Solutions Manual for South-Western Federal Taxation 2017 Comprehensive 40th Hoffman

44. continued

Form 1040 (2015) JANE SMITH 123-45-6789 Page 2

Tax and Credits	38	Amount from line 37 (adjusted gross income)		38	105,120
	39a	Check if: ☐ **You** were born before January 2, 1951, ☐ Blind. ☐ **Spouse** was born before January 2, 1951, ☐ Blind. **Total boxes checked** ▶ 39a 0			
	b	If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ 39b ☐			
Standard Deduction for— • People who check any box on line 39a or 39b **or** who can be claimed as a dependent, see instructions. • All others: Single or Married filing separately, $6,300 Married filing jointly or Qualifying widow(er), $12,600 Head of household, $9,250	40	**Itemized deductions** (from Schedule A) **or** your **standard deduction** (see left margin)		40	20,834
	41	Subtract line 40 from line 38		41	84,286
	42	**Exemptions.** If line 38 is $154,950 or less, multiply $4,000 by the number on line 6d. Otherwise, see instructions		42	4,000
	43	**Taxable income.** Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-		43	80,286
	44	**Tax** (see instructions). Check if any from: a ☐ Form(s) 8814 b ☐ Form 4972 c ☐		44	15,863
	45	**Alternative minimum tax** (see instructions). Attach Form 6251 ▶		45	0
	46	Excess advance premium tax credit repayment. Attach Form 8962		46	
	47	Add lines 44, 45, and 46		47	15,863
	48	Foreign tax credit. Attach Form 1116 if required	0		
	49	Credit for child and dependent care expenses. Attach Form 2441			
	50	Education credits from Form 8863, line 19			
	51	Retirement savings contributions credit. Attach Form 8880	0		
	52	Child tax credit. Attach Schedule 8812, if required			
	53	Residential energy credits. Attach Form 5695			
	54	Other credits from Form: a ☐ 3800 b ☐ 8801 c ☐	0		
	55	Add lines 48 through 54. These are your **total credits**		55	0
	56	Subtract line 55 from line 47. If line 55 is more than line 47, enter -0- ▶		56	15,863
Other Taxes	57	Self-employment tax. Attach Schedule SE		57	0
	58	Unreported social security and Medicare tax from Form: a ☐ 4137 b ☐ 8919		58	0
	59	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required		59	0
	60a	Household employment taxes from Schedule H		60a	0
	b	First-time homebuyer credit repayment. Attach Form 5405 if required		60b	0
	61	Health care: individual responsibility (see instructions) Full-year coverage ☒		61	0
	62	Taxes from: a ☐ Form 8959 b ☐ Form 8960 c ☐ Instructions; enter code(s)		62	0
	63	Add lines 56 through 62. This is your **total tax** ▶		63	15,863
Payments	64	Federal income tax withheld from Forms W-2 and 1099	16,000		
	65	2015 estimated tax payments and amount applied from 2014 return	1,000		
If you have a qualifying child, attach Schedule EIC.	66a	**Earned income credit (EIC)**			
	b	Nontaxable combat pay election 66b			
	67	Additional child tax credit. Attach Schedule 8812			
	68	American opportunity credit from Form 8863, line 8			
	69	Net premium tax credit. Attach Form 8962			
	70	Amount paid with request for extension to file			
	71	Excess social security and tier 1 RRTA tax withheld	0		
	72	Credit for federal tax on fuels. Attach Form 4136			
	73	Credits from Form: a ☐ 2439 b ☐ Reserved c ☐ 8885 d ☐	0		
	74	Add lines 64, 65, 66a, and 67 through 73. These are your **total payments** ▶		74	17,000
Refund	75	If line 74 is more than line 63, subtract line 63 from line 74. This is the amount you **overpaid**		75	1,137
	76a	Amount of line 75 you want **refunded to you.** If Form 8888 is attached, check here ▶ ☐		76a	1,137
Direct deposit? See instructions.	b	Routing number XXXXXXXXX ▶ c Type: ☒ Checking ☐ Savings			
	d	Account number XXXXXXXXXXXXXXXXX			
	77	Amount of line 75 you want **applied to your 2016 estimated tax** ▶	0		
Amount You Owe	78	**Amount you owe.** Subtract line 74 from line 63. For details on how to pay, see instructions ▶		78	
	79	Estimated tax penalty (see instructions)			

Third Party Designee Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ **Yes.** Complete below ☒ **No**
Designee's name ▶ Phone no. ▶ Personal identification number (PIN) ▶

Sign Here Joint return? See instructions. Keep a copy for your records.
Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number
		LEGAL SECRETARY	
Spouse's signature. If a joint return, **both** must sign.	Date	Spouse's occupation	If the IRS sent you an Identity Protection PIN, enter it here (see inst.)

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

KIA www.irs.gov/form1040 Form **1040** (2015)

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44. continued

SCHEDULE A (Form 1040) — Department of the Treasury, Internal Revenue Service (99)

Itemized Deductions

▶ Information about Schedule A and its separate instructions is at *www.irs.gov/scheduleа.*

▶ Attach to Form 1040.

OMB No. 1545-0074

2015

Attachment Sequence No. **07**

Name(s) shown on Form 1040: JANE SMITH

Your social security number: 123-45-6789

Medical and Dental Expenses		**Caution.** Do not include expenses reimbursed or paid by others.			
	1	Medical and dental expenses (see instructions)	1	0	
	2	Enter amount from Form 1040, line 38 . . . 2 105,120			
	3	Multiply line 2 by 10% (.10). But if either you or your spouse was born before January 2, 1951, multiply line 2 by 7.5% (.075) instead	3	10,512	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-			4 0
Taxes You Paid	5	State and local a. ☐ Income taxes, or b. ☒ General sales taxes	5	946	
	6	Real estate taxes (see instructions)	6	0	
	7	Personal property taxes	7	1,100	
	8	Other taxes. List type and amount ▶	8	0	
	9	Add lines 5 through 8			9 2,046
Interest You Paid	10	Home mortgage interest and points reported to you on Form 1098	10	9,500	
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11	0	
Note. Your mortgage interest deduction may be limited (see instructions).	12	Points not reported to you on Form 1098. See instructions for special rules	12	0	
	13	Mortgage insurance premiums (see instructions)	13	0	
	14	Investment interest. Attach Form 4952 if required. (See instructions.)	14		
	15	Add lines 10 through 14			15 9,500
Gifts to Charity If you made a gift and got a benefit for it, see instructions.	16	Gifts by cash or check. If you made any gift of $250 or more, see instructions	16	2,500	
	17	Other than by cash or check. If any gift of $250 or more, see instructions. You **must** attach Form 8283 if over $500	17		
	18	Carryover from prior year	18		
	19	Add lines 16 through 18			19 2,500
Casualty and Theft Losses	20	Casualty or theft loss(es). Attach Form 4684. (See instructions.)			20 6,788
Job Expenses and Certain Miscellaneous Deductions	21	Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. (See instructions.) ▶	21	0	
	22	Tax preparation fees	22		
	23	Other expenses—investment, safe deposit box, etc. List type and amount ▶	23	0	
	24	Add lines 21 through 23	24	0	
	25	Enter amount from Form 1040, line 38 . . . 25 105,120			
	26	Multiply line 25 by 2% (.02)	26	2,102	
	27	Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-			27 0
Other Miscellaneous Deductions	28	Other—from list in instructions. List type and amount ▶			28 0
Total Itemized Deductions	29	Is Form 1040, line 38, over $154,950? ☒ **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40. ☐ **Yes.** Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.			29 20,834
	30	If you elect to itemize deductions even though they are less than your standard deduction, check here ▶ ☐			

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44. continued

SCHEDULE C (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Profit or Loss From Business

(Sole Proprietorship)

▶ Information about Schedule C and its separate instructions is at *www.irs.gov/schedulec.*

▶ Attach to Form 1040, 1040NR, or 1041; partnerships generally must file Form 1065.

OMB No. 1545-0074

2015

Attachment Sequence No. **09**

Name of proprietor: JANE SMITH	Social security number (SSN): 123-45-6789
A Principal business or profession, including product or service (see instructions): TYPING SERVICES	B Enter code from instructions ▶ 561410
C Business name. If no separate business name, leave blank.: TYPING SERVICES	D Employer ID number (EIN), (see instr.)
E Business address (including suite or room no.) ▶ 2020 OAKCREST City, town or post office, state, and ZIP code: BOCA RATON FL 33431	

F Accounting method: (1) [X] Cash (2) [ ] Accrual (3) [ ] Other (specify) ▶

G Did you "materially participate" in the operation of this business during 2015? If "No," see instructions for limit on losses . . . [X] Yes [ ] No

H If you started or acquired this business during 2015, check here . . . ▶ [ ]

I Did you make any payments in 2015 that would require you to file Form(s) 1099? (see instructions) . . . [ ] Yes [X] No

J If "Yes," did you or will you file required Forms 1099? . . . [ ] Yes [ ] No

Part I Income

1	Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on form W-2 and the "Statutory employee" box on that form was checked. ▶ [ ]	1	20,000
2	Returns and allowances	2	
3	Subtract line 2 from line 1	3	20,000
4	Cost of goods sold (from line 42)	4	0
5	**Gross profit.** Subtract line 4 from line 3	5	20,000
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	
7	**Gross income.** Add lines 5 and 6 ▶	7	20,000

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8		18	Office expense (see instructions)	18	
9	Car and truck expenses (see instructions)	9	0	19	Pension and profit-sharing plans	19	
10	Commissions and fees	10		20	Rent or lease (see instructions):		
11	Contract labor (see instructions)	11		a	Vehicles, machinery, and equipment	20a	3,000
12	Depletion	12		b	Other business property	20b	7,000
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13	0	21	Repairs and maintenance	21	
14	Employee benefit programs (other than on line 19)	14		22	Supplies (not included in Part III)	22	4,400
15	Insurance (other than health)	15		23	Taxes and licenses	23	500
16	Interest:			24	Travel, meals, and entertainment:		
a	Mortgage (paid to banks, etc.)	16a		a	Travel	24a	
b	Other	16b		b	Deductible meals and entertainment (see instructions)	24b	0
17	Legal and professional services	17		25	Utilities	25	4,680
				26	Wages (less employment credits)	26	5,000
				27a	Other expenses (from line 48)	27a	0
				b	**Reserved for future use**	27b	

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27a ▶	28	24,580
29	Tentative profit or (loss). Subtract line 28 from line 7	29	-4,580
30	Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method (see instructions). **Simplified method filers only:** enter the total square footage of: (a) your home: _____ and (b) the part of your home used for business: _____. Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30	30	0
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on both **Form 1040, line 12** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see instructions). Estates and trusts, enter on **Form 1041, line 3.** • If a loss, you **must** go to line 32.	31	-4,580
32	If you have a loss, check the box that describes your investment in this activity (see instructions). • If you checked 32a, enter the loss on both **Form 1040, line 12,** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see the line 31 instructions). Estates and trusts, enter on **Form 1041, line 3.** • If you checked 32b, you **must** attach **Form 6198.** Your loss may be limited.	32a [X] All investment is at risk. 32b [ ] Some investment is not at risk.	

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44. continued

SCHEDULE D (Form 1040)
Department of the Treasury Internal Revenue Service (99)

Capital Gains and Losses

► Attach to Form 1040 or Form 1040NR.
► Information about Schedule D and its separate instructions is at *www.irs.gov/scheduled.*
► Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.

OMB No. 1545-0074
2015
Attachment Sequence No. **12**

Name(s) shown on return: JANE SMITH
Your social security number: 123-45-6789

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 1b	0	0		0
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked	0	0	0	0
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked	0	0	0	0
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked	0	2,100	0	-2,100

4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824	**4**	0
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	**5**	
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your **Capital Loss Carryover Worksheet** in the instructions.	**6**	(0)
7 **Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the next page	**7**	-2,100

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b	0	0		0
8b Totals for all transactions reported on Form(s) 8949 with **Box D** checked	0	0	0	0
9 Totals for all transactions reported on Form(s) 8949 with **Box E** checked	0	0	0	0
10 Totals for all transactions reported on Form(s) 8949 with **Box F** checked	0	0	0	0

11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824	**11**	0
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	**12**	
13 Capital gain distributions. See the instructions	**13**	0
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your **Capital Loss Carryover Worksheet** in the instructions	**14**	(0)
15 **Net long-term capital gain or (loss).** Combine lines 8a through 14 in column (h). Then go to Part III on page 2	**15**	0

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44. continued

Schedule D (Form 1040) 2015 JANE SMITH 123-45-6789 Page 2

Part III Summary

16	Combine lines 7 and 15 and enter the result	**16**	-2,100
	• If line 16 is a **gain**, enter the amount from line 16 on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 17 below. • If line 16 is a **loss**, skip lines 17 through 20 below. Then go to line 21. Also be sure to complete line 22. • If line 16 is **zero**, skip lines 17 through 21 below and enter -0- on Form 1040, line 13, or Form 1040NR, line 14. Then go to line 22.		
17	Are lines 15 and 16 **both** gains? ☐ **Yes.** Go to line 18. ☐ **No.** Skip lines 18 through 21, and go to line 22.		
18	Enter the amount, if any, from line 7 of the **28% Rate Gain Worksheet** in the instructions ▶	**18**	
19	Enter the amount, if any, from line 18 of the **Unrecaptured Section 1250 Gain Worksheet** in the instructions ▶	**19**	
20	Are lines 18 and 19 **both** zero or blank? ☐ **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). **Do not** complete lines 21 and 22 below. ☐ **No.** Complete the **Schedule D Tax Worksheet** in the instructions. **Do not** complete lines 21 and 22 below.		
21	If line 16 is a loss, enter here and on Form 1040, line 13, or Form 1040NR, line 14, the **smaller** of: • The loss on line 16 or • ($3,000), or if married filing separately, ($1,500) **Note.** When figuring which amount is smaller, treat both amounts as positive numbers.	**21**	(2,100)
22	Do you have qualified dividends on Form 1040, line 9b, or Form 1040NR, line 10b? ☐ **Yes.** Complete the **Qualified Dividends and Capital Gain Tax Worksheet** in the instructions for Form 1040, line 44 (or in the instructions for Form 1040NR, line 42). ☒ **No.** Complete the rest of Form 1040 and Form 1040NR.		

KIA Schedule D (Form 1040) 2015

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44. continued

Form **8949**

Department of the Treasury
Internal Revenue Service

Sales and Other Dispositions of Capital Assets

▶ **Information about Form 8949 and its separate instructions is at *www.irs.gov/form8949***

▶ **File with your Schedule D to list your transactions for lines 1b, 2, 3, 8b, 9, and 10 of Schedule D.**

OMB No. 1545-0074

2015

Attachment Sequence No. **12A**

Name(s) shown on return	Social security number or taxpayer identification number
JANE SMITH	123-45-6789

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I **Short-Term.** Transactions involving capital assets you held 1 year or less are short-term. For long-term transactions, see page 2.

Note. You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box A, B, *or* C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

- ☐ **(A)** Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
- ☐ **(B)** Short-term transactions reported on Form(s) 1099-B showing basis was **not** reported to the IRS
- ☒ **(C)** Short-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). See the separate instructions. (f) Code(s) from instructions	(g) Amount of adjustment	(h) Gain or (loss). Subtract column (e) from column (d) and combine the result with column (g)
NONBUSINESS BAD DEBT - JENSE		08/15/15	0	2,100		0	-2,100
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
							0
2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 1b** (if **Box A** above is checked), **line 2** (if **Box B** above is checked), or **line 3** (if **Box C** above is checked) . ▶			0	2,100		0	-2,100

Note. If you checked Box A above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

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44. continued

Form **4684**
Department of the Treasury
Internal Revenue Service

Casualties and Thefts

► Information about Form 4684 and its separate instructions is at *www.irs.gov/form4684.*
► Attach to your tax return.
► Use a separate Form 4684 for each casualty or theft.

OMB No. 1545-0177
2015
Attachment Sequence No. **26**

Name(s) shown on tax return: JANE SMITH
Identifying number: 123-45-6789

SECTION A—Personal Use Property (Use this section to report casualties and thefts of property **not** used in a trade or business or for income-producing purposes.)

1 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft.
Property **A** SILVERWARE HOME 07/01/06
Property **B**
Property **C**
Property **D**

		Properties A	B	C	D
2 Cost or other basis of each property	2	14,000			
3 Insurance or other reimbursement (whether or not you filed a claim) (see instructions)	3	1,500			
Note: *If line 2 is **more** than line 3, skip line 4.*					
4 Gain from casualty or theft. If line 3 is **more** than line 2, enter the difference here and skip lines 5 through 9 for that column. See instructions if line 3 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year	4	0	0	0	0
5 Fair market value **before** casualty or theft	5	15,000			
6 Fair market value **after** casualty or theft	6	0			
7 Subtract line 6 from line 5	7	15,000	0	0	0
8 Enter the **smaller** of line 2 or line 7	8	14,000	0	0	0
9 Subtract line 3 from line 8. If zero or less, enter -0-	9	12,500	0	0	0

10 Casualty or theft loss. Add the amounts on line 9 in columns A through D	10	12,500
11 Enter the **smaller** of line 10 or $100	11	100
12 Subtract line 11 from line 10	12	12,400
Caution: *Use only one Form 4684 for lines 13 through 18.*		
13 Add the amounts on line 12 of all Forms 4684	13	17,300
14 Add the amounts on line 4 of all Forms 4684	14	0
15 • If line 14 is **more** than line 13, enter the difference here and on Schedule D. **Do not** complete the rest of this section (see instructions). • If line 14 is **less** than line 13, enter -0- here and go to line 16. • If line 14 is **equal** to line 13, enter -0- here. **Do not** complete the rest of this section.	15	0
16 If line 14 is **less** than line 13, enter the difference	16	17,300
17 Enter 10% of your adjusted gross income from Form 1040, line 38, or Form 1040NR, line 37. Estates and trusts, see instructions	17	10,512
18 Subtract line 17 from line 16. If zero or less, enter -0-. Also enter the result on Schedule A (Form 1040), line 20, or Form 1040NR, Schedule A, line 6. Estates and trusts, enter the results on the "Other deductions" line of your tax return	18	6,788

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44. continued

Form 4684 (2015) Attachment Sequence No. **26** Page **2**

Name(s) shown on tax return. Do not enter name and identifying number if shown on first page of this form. JANE SMITH | **Identifying number** 123-45-6789

SECTION B—Business and Income-Producing Property

Part I Casualty or Theft Gain or Loss (Use a separate Part I for each casualty or theft.)

19 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft. **See instructions if claiming a loss due to a Ponzi-type investment scheme and Section C is not completed.**

Property **A** _____

Property **B** _____

Property **C** _____

Property **D** _____

			Properties			
			A	**B**	**C**	**D**
20	Cost or adjusted basis of each property	20				
21	Insurance or other reimbursement (whether or not you filed a claim). See the instructions for line 3	21				
	Note: *If line 20 is **more** than line 21, skip line 22.*					
22	Gain from casualty or theft. If line 21 is **more** than line 20, enter the difference here and on line 29 or line 34, column (c), except as provided in the instructions for line 33. Also, skip lines 23 through 27 for that column. See the instructions for line 4 if line 21 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year	22	0	0	0	0
25	Fair market value **before** casualty or theft	23				
24	Fair market value **after** casualty or theft	24				
25	Subtract line 24 from line 23	25	0	0	0	0
26	Enter the **smaller** of line 20 or line 25	26	0	0	0	0
	Note: *If the property was totally destroyed by casualty or lost from theft, enter on line 26 the amount from line 20.*					
27	Subtract line 21 from line 26. If zero or less, enter -0-	27	0	0	0	0

28	Casualty or theft loss. Add the amounts on line 27. Enter the total here and on line 29 **or** line 34 (see instructions).	28	0

Part II Summary of Gains and Losses (from separate Parts I)

(a) Identify casualty or theft	**(b)** Losses from casualties or thefts: *(i)* Trade, business, rental or royalty property	**(b)** Losses from casualties or thefts: *(ii)* Income-producing and employee property	**(c)** Gains from casualties or thefts includible in income
Casualty or Theft of Property Held One Year or Less			
29	(0)	(0)	0
	(0)	(0)	0
30 Totals. Add the amounts on line 29	(0)	(0)	0

31	Combine line 30, columns (b)(i) and (c). Enter the net gain or (loss) here and on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions	31	0
32	Enter the amount from line 30, column (b)(ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040), line 28, or Form 1040NR, Schedule A, line 14, and enter the amount from property used as an employee on Schedule A (Form 1040), line 23, or Form 1040NR, Schedule A, line 9. Estates and trusts, partnerships, and S corporations, see instructions	32	0
	Casualty or Theft of Property Held More Than One Year		
33	Casualty or theft gains from Form 4797, line 32	33	0
34	(0) (0)		0
	(0) (0)		0
35	Total losses. Add amounts on line 34, columns (b)(i) and (b)(ii) (0) (0)		
36	Total gains. Add lines 33 and 34, column (c)	36	0
37	Add amounts on line 35, columns (b)(i) and (b)(ii)	37	0
38	If the loss on line 37 is **more** than the gain on line 36:		
a	Combine line 35, column (b)(i) and line 36, and enter the net gain or (loss) here. Partnerships (except electing large partnerships) and S corporations, see the note below. All others, enter this amount on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions	38a	0
b	Enter the amount from line 35, column (b)(ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040), line 28, or Form 1040NR, Schedule A, line 14, and enter the amount from property used as an employee on Schedule A (Form 1040), line 23, or Form 1040NR, Schedule A, line 9. Estates and trusts, enter on the "Other deductions" line of your tax return. Partnerships (except electing large partnerships) and S corporations, see the note below. Electing large partnerships, enter on Form 1065-B, Part II, line 11	38b	0
39	If the loss on line 37 is **less** than or **equal** to the gain on line 36, combine lines 36 and 37 and enter here. Partnerships (except electing large partnerships), see the note below. All others, enter this amount on Form 4797, line 3	39	0
	Note: *Partnerships, enter the amount from line 38a, 38b, or line 39 on Form 1065, Schedule K, line 11. S corporations, enter the amount from line 38a or 38b on Form 1120S, Schedule K, line 10.*		

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44. continued

Form 4684 (2015) Page 3

Name(s) shown on tax return. JANE SMITH

Identifying number 123-45-6789

SECTION C—Theft Loss Deduction for Ponzi-Type Investment Scheme Using the Procedures in Revenue Procedure 2009-20 (Complete this section in lieu of Appendix A in Revenue Procedure 2009-20. See instructions.)

Part I Computation of Deduction

40	Initial investment	40			
41	Subsequent investments (see instructions)	41			
42	Income reported on your tax returns for tax years prior to the discovery year (see instructions)	42			
43	Add lines 40, 41, and 42	43	0		
44	Withdrawals for all years (see instructions)	44			
45	Subtract line 44 from line 43. This is your total qualified investment	45	0		
46	Enter .95 (95%) if you have no potential third-party recovery. Enter .75 (75%) if you have potential third-party recovery	46			
47	Multiply line 46 by line 45	47			0
48	Actual recovery	48			
49	Potential insurance/Securities Investor Protection Corporation (SIPC) recovery	49			
50	Add lines 48 and 49. This is your total recovery.	50			0
51	Subtract line 50 from line 47. This is your deductible theft loss. Include this amount on line 28 of Section B, Part I. Do not complete lines 19-27 for this loss. Then complete Section B, Part II	51			0

Part II Required Statements and Declarations (See instructions.)

- I am claiming a theft loss deduction pursuant to Revenue Procedure 2009-20 from a specified fraudulent arrangement conducted by the following individual or entity.

  Name of individual or entity _____

  Taxpayer identification number (if known) _____

  Address _____
- I have written documentation to support the amounts reported in Part I of this Section C.
- I am a qualified investor as defined in section 4.03 of Revenue Procedure 2009-20.
- If I have determined the amount of my theft loss deduction using .95 on line 46 above, I declare that I have not pursued and do not intend to pursue any potential third-party recovery, as that term is defined in section 4.10 of Revenue Procedure 2009-20.
- I agree to comply with the conditions and agreements set forth in Revenue Procedure 2009-20 and this Section C.
- If I have already filed a return or amended return that does not satisfy the conditions in section 6.02 of Revenue Procedure 2009-20, I agree to all adjustments or actions that are necessary to comply with those conditions. The tax year(s) for which I filed the return(s) or amended return(s) and the date(s) on which they were filed are as follows:

_____

_____

_____

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44. continued

Form **4684**
Department of the Treasury
Internal Revenue Service

Casualties and Thefts

► Information about Form 4684 and its separate instructions is at *www.irs.gov/form4684.*
► Attach to your tax return.
► Use a separate Form 4684 for each casualty or theft.

OMB No. 1545-0177
2015
Attachment Sequence No. **26**

Name(s) shown on tax return JANE SMITH

Identifying number 123-45-6789

SECTION A—Personal Use Property (Use this section to report casualties and thefts of property **not** used in a trade or business or for income-producing purposes.)

1 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft.

Property **A** AUTOMOBILE
Property **B** HOME
Property **C** 01/01/12
Property **D**

		Properties			
		A	**B**	**C**	**D**
2 Cost or other basis of each property	2	52,000			
3 Insurance or other reimbursement (whether or not you filed a claim) (see instructions)	3	2,000			
Note: *If line 2 is **more** than line 3, skip line 4.*					
4 Gain from casualty or theft. If line 3 is **more** than line 2, enter the difference here and skip lines 5 through 9 for that column. See instructions if line 3 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year	4	0	0	0	0
5 Fair market value **before** casualty or theft	5	45,000			
6 Fair market value **after** casualty or theft	6	38,000			
7 Subtract line 6 from line 5	7	7,000	0	0	0
8 Enter the **smaller** of line 2 or line 7	8	7,000	0	0	0
9 Subtract line 3 from line 8. If zero or less, enter -0-	9	5,000	0	0	0

10	Casualty or theft loss. Add the amounts on line 9 in columns A through D	10	5,000
11	Enter the **smaller** of line 10 or $100	11	100
12	Subtract line 11 from line 10	12	4,900
	Caution: *Use only one Form 4684 for lines 13 through 18.*		
13	Add the amounts on line 12 of all Forms 4684	13	
14	Add the amounts on line 4 of all Forms 4684	14	
15	• If line 14 is **more** than line 13, enter the difference here and on Schedule D. **Do not** complete the rest of this section (see instructions). • If line 14 is **less** than line 13, enter -0- here and go to line 16. • If line 14 is **equal** to line 13, enter -0- here. **Do not** complete the rest of this section.	15	
16	If line 14 is **less** than line 13, enter the difference	16	
17	Enter 10% of your adjusted gross income from Form 1040, line 38, or Form 1040NR, line 37. Estates and trusts, see instructions	17	
18	Subtract line 17 from line 16. If zero or less, enter -0-. Also enter the result on Schedule A (Form 1040), line 20, or Form 1040NR, Schedule A, line 6. Estates and trusts, enter the results on the "Other deductions" line of your tax return	18	

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44. continued

Form 4684 (2015) Attachment Sequence No. **26** Page **2**

Name(s) shown on tax return. Do not enter name and identifying number if shown on first page of this form. JANE SMITH | **Identifying number** 123-45-6789

SECTION B—Business and Income-Producing Property

Part I Casualty or Theft Gain or Loss (Use a separate Part I for each casualty or theft.)

19 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft. **See instructions if claiming a loss due to a Ponzi-type investment scheme and Section C is not completed.**

Property **A** _____

Property **B** _____

Property **C** _____

Property **D** _____

			Properties			
			A	**B**	**C**	**D**
20	Cost or adjusted basis of each property	20				
21	Insurance or other reimbursement (whether or not you filed a claim). See the instructions for line 3	21				
	Note: *If line 20 is **more** than line 21, skip line 22.*					
22	Gain from casualty or theft. If line 21 is **more** than line 20, enter the difference here and on line 29 or line 34, column (c), except as provided in the instructions for line 33. Also, skip lines 23 through 27 for that column. See the instructions for line 4 if line 21 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year	22	0	0	0	0
25	Fair market value **before** casualty or theft	23				
24	Fair market value **after** casualty or theft	24				
25	Subtract line 24 from line 23	25	0	0	0	0
26	Enter the **smaller** of line 20 or line 25	26	0	0	0	0
	Note: *If the property was totally destroyed by casualty or lost from theft, enter on line 26 the amount from line 20.*					
27	Subtract line 21 from line 26. If zero or less, enter -0-	27	0	0	0	0

28 Casualty or theft loss. Add the amounts on line 27. Enter the total here and on line 29 **or** line 34 (see instructions). **28** 0

Part II Summary of Gains and Losses (from separate Parts I)

(a) Identify casualty or theft	**(b)** Losses from casualties or thefts: *(i)* Trade, business, rental or royalty property	**(b)** Losses from casualties or thefts: *(ii)* Income-producing and employee property	**(c)** Gains from casualties or thefts includible in income
Casualty or Theft of Property Held One Year or Less			
29	( )	( )	
	( )	( )	
30 Totals. Add the amounts on line 29 — 30	( )	( )	
31 Combine line 30, columns (b)(i) and (c). Enter the net gain or (loss) here and on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions — 31			
32 Enter the amount from line 30, column (b)(ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040), line 28, or Form 1040NR, Schedule A, line 14, and enter the amount from property used as an employee on Schedule A (Form 1040), line 23, or Form 1040NR, Schedule A, line 9. Estates and trusts, partnerships, and S corporations, see instructions — 32			
Casualty or Theft of Property Held More Than One Year			
33 Casualty or theft gains from Form 4797, line 32 — 33			
34	( )	( )	
	( )	( )	
35 Total losses. Add amounts on line 34, columns (b)(i) and (b)(ii) — 35	( )	( )	
36 Total gains. Add lines 33 and 34, column (c) — 36			
37 Add amounts on line 35, columns (b)(i) and (b)(ii) — 37			
38 If the loss on line 37 is **more** than the gain on line 36:			
a Combine line 35, column (b)(i) and line 36, and enter the net gain or (loss) here. Partnerships (except electing large partnerships) and S corporations, see the note below. All others, enter this amount on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions — 38a			
b Enter the amount from line 35, column (b)(ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040), line 28, or Form 1040NR, Schedule A, line 14, and enter the amount from property used as an employee on Schedule A (Form 1040), line 23, or Form 1040NR, Schedule A, line 9. Estates and trusts, enter on the "Other deductions" line of your tax return. Partnerships (except electing large partnerships) and S corporations, see the note below. Electing large partnerships, enter on Form 1065-B, Part II, line 11 — 38b			
39 If the loss on line 37 is **less** than or **equal** to the gain on line 36, combine lines 36 and 37 and enter here. Partnerships (except electing large partnerships), see the note below. All others, enter this amount on Form 4797, line 3 — 39			
Note: *Partnerships, enter the amount from line 38a, 38b, or line 39 on Form 1065, Schedule K, line 11. S corporations, enter the amount from line 38a or 38b on Form 1120S, Schedule K, line 10.*			

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44. continued

Form 4684 (2015) Page 3

Name(s) shown on tax return. JANE SMITH | Identifying number 123-45-6789

SECTION C—Theft Loss Deduction for Ponzi-Type Investment Scheme Using the Procedures in Revenue Procedure 2009-20 (Complete this section in lieu of Appendix A in Revenue Procedure 2009-20. See instructions.)

Part I Computation of Deduction

40	Initial investment	40			
41	Subsequent investments (see instructions)	41			
42	Income reported on your tax returns for tax years prior to the discovery year (see instructions)	42			
43	Add lines 40, 41, and 42	43	0		
44	Withdrawals for all years (see instructions)	44			
45	Subtract line 44 from line 43. This is your total qualified investment	45	0		
46	Enter .95 (95%) if you have no potential third-party recovery. Enter .75 (75%) if you have potential third-party recovery	46			
47	Multiply line 46 by line 45	47			0
48	Actual recovery	48			
49	Potential insurance/Securities Investor Protection Corporation (SIPC) recovery	49			
50	Add lines 48 and 49. This is your total recovery.	50			0
51	Subtract line 50 from line 47. This is your deductible theft loss. Include this amount on line 28 of Section B, Part I. Do not complete lines 19-27 for this loss. Then complete Section B, Part II	51			0

Part II Required Statements and Declarations (See instructions.)

- I am claiming a theft loss deduction pursuant to Revenue Procedure 2009-20 from a specified fraudulent arrangement conducted by the following individual or entity.

  Name of individual or entity _____

  Taxpayer identification number (if known) _____

  Address _____
- I have written documentation to support the amounts reported in Part I of this Section C.
- I am a qualified investor as defined in section 4.03 of Revenue Procedure 2009-20.
- If I have determined the amount of my theft loss deduction using .95 on line 46 above, I declare that I have not pursued and do not intend to pursue any potential third-party recovery, as that term is defined in section 4.10 of Revenue Procedure 2009-20.
- I agree to comply with the conditions and agreements set forth in Revenue Procedure 2009-20 and this Section C.
- If I have already filed a return or amended return that does not satisfy the conditions in section 6.02 of Revenue Procedure 2009-20, I agree to all adjustments or actions that are necessary to comply with those conditions. The tax year(s) for which I filed the return(s) or amended return(s) and the date(s) on which they were filed are as follows:

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NOTES

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CHAPTER 2

WORKING WITH THE TAX LAW

LECTURE NOTES

OVERVIEW

Federal tax law is a mixture of statutory provisions, administrative pronouncements, and court decisions.

SUMMARY OF CHANGES IN THE CHAPTER

The following are notable changes in the chapter from the 2016 Edition. For major changes, see the Preface to the Instructor's Edition of the text.

- Updated references and citations throughout the chapter.
- Added a new Ethics & Equity feature on tax fraud.
- Updated materials on administrative tax law sources and commercial tax services.

THE BIG PICTURE

The Big Picture discussion in Chapter 2 introduces the introductory tax student to the idea that answers to tax questions will not always be found in the tax textbook and that research often needs to be undertaken to answer the question.

The discussion in Section 2-3 of the chapter takes the student through the answer to the research questions posed. Depending on the research services available, the instructor might ask the students to formulate keyword searches and then demonstrate what happens when those searches are undertaken in the research service. The instructor could also demonstrate the index feature of the research services to look up topics related to dependents or dependency exemptions. Alternatively, the instructor could ask the students to see if they could verify the correctness of the textbook conclusion or change one of the key facts (e.g., change the relationship between the taxpayers so that the qualifying relative test applies) and ask the student to determine how the conclusion would change, if at all.

TAX SOURCES

Statutory Sources of the Tax Law

1. Statutory sources of law include the Constitution (Article I, Sections 7, 8, and 10), tax treaties, and the Internal Revenue Code.

2. Origin of the Internal Revenue Code.

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a. Constitution. The source of the Federal taxing authority is the U.S. Constitution: "The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defense and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States." (Art. I, § 8, Cl. 1)

b. Sixteenth Amendment. The Sixteenth Amendment is the foundation of our Federal income tax: "The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration."

3. Internal Revenue Code. The Code generally is supreme in the Federal tax area, unless a U.S. tax treaty is in direct conflict. In this case, TAMRA of 1988 provides that neither a tax law nor a tax treaty takes general precedence. Instead, the most recent item will take precedence.

a. Role of Congress. Unless a *constitutional* issue is involved, Congress can override a U.S. Supreme Court decision by amending the Code.

(1) Code supremacy. This Court supremacy is not the case when the Internal Revenue Code is concerned (i.e., Congress can change the law).

b. Congressional Committee Reports. Congressional Committee Reports may be helpful in interpreting the Code.

(1) Congressional intent. Such reports reflect the intent of Congress in implementing or changing the tax law.

(2) *Cumulative Bulletins*. The Committee Reports usually are conveniently available in special volumes of the *Cumulative Bulletins* as well as online, on the committee's web page (e.g., http://waysandmeans.house.gov/).

c. Public and closed congressional hearings. Congress holds both public and closed hearings on tax proposals.

(1) After public hearings before the House Ways and Means Committee, the public may be excluded in a closed session.

(2) Tax bills may be debated under a closed rule before the full House with approval by the Rules Committee.

(3) Under this closed rule, amendments are not allowed on the House floor unless approved by the House Ways and Means Committee.

(4) The full Senate, however, does not have a closed rule process.

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d. Organization of the Code. The Code is organized into Subtitles, Chapters, and Subchapters. See Figure 2-1 in these Lecture Notes.

e. Interrelation of Code provisions. Tying the various Code provisions together to reach the total result is important.

(1) For example, consider why there are three separate sections dealing with alimony.

(2) Section 71 (in the gross income sequence) makes it taxable to the payee; § 215 (in the deduction sequence) makes it deductible to the payor; while § 62(a)(10) classifies the deduction (as a deduction for AGI) for the payor.

f. Subpart designations. The designation given to the subparts of a Code section will vary.

(1) The usual approach has been to use (a), (b), etc. [e.g., § 162(a)].

(2) On occasion, however, the designation is (1), (2), etc. [e.g., § 212(1)].

g. Code section numbers. Section numbers do not repeat in the same title of the Code. Some Code section numbers contain a capital letter (e.g., a numerical designation such as §§ 453A, 453B).

(1) The reason is that certain numerical sequences in the Code have no space for expansion.

(2) Since there exists a § 453 and a § 454, how else would the two intervening provisions be designated?

h. Recodification. The Internal Revenue Code has been recodified twice.

(1) Internal Revenue Codes of 1939 and 1954. The first was in 1939 and the second was in 1954.

(2) Internal Revenue Code of 1986. Although Congress did not codify and rearrange the law in the Tax Reform Act of 1986, the radical changes did provide some rationale for renaming the entire tax law in the Internal Revenue Code of 1986.

i. General explanation of the act. Upon the completion of major tax legislation, the staff of the Joint Committee on Taxation (in consultation with the staffs of the House Ways and Means and Senate Finance Committees) often will prepare a general explanation of the act.

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(1) Bluebook: no legal effect. Commonly known as the "bluebook" because of the color of its cover, the IRS will not accept this detailed explanation as having legal effect (except for purposes of the accuracy-related penalty in § 6662).

(2) Bluebook: temporary guidance. The "bluebook," however, does provide valuable guidance to tax advisers and taxpayers until Regulations are issued, and some letter rulings and general counsel memoranda of the IRS cite such explanations.

4. The legislative process.

a. Evolution of tax law. Some provisions in the tax law take years to become law (e.g., H.R. 10 or Keogh plans).

(1) This process means that with each new Congress the measure had to be reintroduced until it finally gained the required support.

(2) An example of a provision that currently seems to be going through this process is the provision to tax carried interest at ordinary income rather than capital gains tax rates.

b. Deadwood bills. On occasion Congress will enact deadwood bills. The purpose of such legislation is to "clean up" provisions that are obsolete and possess no continuing validity.

c. Origin of a tax bill. Tax legislation normally originates in the House Ways and Means Committee of the House of Representatives because the U.S. Constitution mandates that revenue raising bills begin in the House. A tax bill might originate in the Senate when it is attached to other legislative proposals.

(1) The Tax Equity and Fiscal Responsibility Act of 1982 originated in the Senate, and its constitutionality was unsuccessfully challenged in the courts.

(2) The Senate version of the Deficit Reduction Act of 1984 was attached as an amendment to the Federal Boat Safety Act.

d. Naming tax legislation. Some tax provisions are commonly referred to by the number the bill received in the House when first proposed or by the name of the member of Congress sponsoring the legislation. For example, the Self-Employed Individuals Tax Retirement Act of 1962 is popularly known as H.R. 10 (House of Representatives Bill No. 10) or as the Keogh Act (Keogh being one of the members of Congress sponsoring the bill). The Roth IRA is named after Senator William Roth, an influential sponsor. Coverdell Education Savings Accounts

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(first called education IRAs) are named after the late Senator Paul Coverdell (R–GA).

e. Beginning in 1997, the president was supposed to be able to cancel provisions from enacted tax legislation under the Line Item Veto Act. President Clinton, on August 11, 1997, did strike two provisions from TRA of 1997 and one nontax provision from the Balanced Budget Act. Congress did not override these cancellations, but the constitutionality of the Line Item Veto Act was challenged in the court system and the Supreme Court held it unconstitutional.

f. Tax legislation is referred from the Senate Finance Committee to the entire Senate. If the House and Senate tax bills disagree, the Joint Conference Committee resolves the differences. (See Exhibits 2.1 and 2.2 in the text.)

5. Arrangement of the Code. The Internal Revenue Code of 1986 is found in Title 26 of the U.S. Code. In working with the Code, it helps to understand the format. The key is usually the section number. For example, in citing Section 2(a), it is unnecessary to include Subtitle A, Chapter 1, Subchapter A, Part I. Mentioning Section 2(a) is sufficient. (See "Citing the Code" in the text.)

Administrative Sources of the Tax Law (See Exhibit 2.3 in the text.)

6. Treasury Department Regulations. The Treasury Department under § 7805(a) has a duty to issue rules and regulations to explain and interpret the Code.

a. Treasury decisions. Final Regulations are issued as Treasury Decisions (TDs) in the *Federal Register*. Regulations carry considerable authority as the official interpretation of tax statutes. They are arranged in the same sequence as the Internal Revenue Code and have the force and effect of law.

b. Types of regulations issued:

(1) Legislative Regulations.

(2) Interpretative Regulations.

(3) Procedural Regulations.

(4) Temporary Regulations may be cited as precedent and are found in the *Federal Register*, *Internal Revenue Bulletin*, and *Cumulative Bulletin*. They are also concurrently issued as Proposed Regulations (in order to become Final Regulations) and automatically expire within three years after the date of issuance.

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ETHICS & EQUITY

Reporting Tax Fraud. Would you turn in someone you knew wasn't paying all their taxes? The IRS certainly tries to encourage tax fraud reporting by offering a portion of the resulting collections to the whistleblower. You can use this Ethics & Equity feature to spark a discussion with your class. What would motivate your students to turn someone in: the satisfaction of getting back at someone they didn't like, the need to adhere to a private moral code, or something else? Would the size of the monetary reward from the IRS affect your students' decisions? And is it ethical of the IRS to pay people to tattle on their tax-dodging literal and metaphorical neighbors, or should justice be its own reward?

c. Validity of a Regulation. One way courts assess the validity of a Regulation is by the legislative reenactment doctrine. A Regulation is considered to have received congressional approval if the Regulation was finalized many years earlier and during the interim period Congress has not amended the relevant statutory language.

d. Information in *Cumulative Bulletins* and *Internal Revenue Bulletins*. The I.R.B.s for a six-month period are gathered together and published in a bound volume designated as a C.B.

7. Revenue Rulings and Revenue Procedures. The C.B.s and I.R.B.s include a variety of administrative sources, including Revenue Rulings and Revenue Procedures.

a. Revenue Rulings are official pronouncements of the National Office of the IRS and provide guidance to both IRS personnel and taxpayers in handling routine tax matters. They usually deal with more restricted problems than Regulations and do not carry the same legal force and effect as Regulations.

b. Revenue Procedures are issued in the same manner as Revenue Rulings, but they deal with the internal management practices and procedures of the IRS. Revenue Procedures do not carry the same legal force and effect as Regulations.

c. Other materials included in the I.R.B and C.B.:

(1) Announcements of Proposed Regulations as well as the related public hearings.

(2) Treasury decisions.

(3) Executive orders.

(4) Tax conventions (i.e., international treaties).

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(5) Legislation (including Committee Reports).

(6) Certain court decisions.

(7) Announcements of court decisions to which the IRS acquiesces or does not acquiesce.

(8) Punitive action (e.g., disbarment, suspension) taken against persons (e.g., attorneys, CPAs) practicing before the IRS.

8. Letter rulings. Letter rulings and determination letters have in common the fact that they apply only to the person who requested the ruling or letter. Note that neither is published by the IRS, but made available to private publishers.

a. Letter ruling. A letter ruling is a statement issued by the National Office of the IRS in response to a taxpayer's request, which applies the tax law to a proposed transaction. Revenue Rulings can result from a taxpayer request for a letter ruling.

b. Determination letter. A determination letter is a statement issued by the Area Director in response to a taxpayer, which applies the tax law to a completed transaction.

9. Other administrative pronouncements. These sources are not the same.

a. Technical Memoranda (TMs) are memoranda from the IRS Commissioner to the Assistant Secretary of the Treasury for Tax Policy. They are drafted by the Legislation and Regulation Division of the Office of Chief Counsel and relate to proposed Treasury Decisions or Regulations.

b. Technical Advice Memoranda (TAMs) are furnished by the National Office of the IRS upon request of an Area Director or an Appeals Officer of the IRS in response to any technical or procedural question (e.g., a completed transaction).

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ADDITIONAL LECTURE RESOURCE

Provider of the Tax Law Source

Internal Revenue Code	Congress/President
Regulations	U.S. Treasury Department
Revenue Ruling	National Office of IRS
Letter Ruling	National Office of IRS
Notices and Announcements	National Office of IRS
Determination Letter	Area Director of IRS
Technical Advice Memorandum	National Office of IRS
Treasury Decision	U.S. Treasury Department
Revenue Procedure	National Office of IRS
General Counsel Memorandum	General Counsel's Office of IRS
Action on Decision	Office of Chief Counsel of IRS
Field Service Advice	Office of Chief Counsel of IRS

Judicial Sources of the Tax Law

10. Precedential value. American law, following English common law, is frequently "made" by judicial decisions. Under the doctrine of *stare decisis*, each decision has precedential value for future decisions with the same controlling set of facts.

11. The judicial process in general. After a taxpayer has exhausted some or all of the remedies available within the IRS, the dispute can be taken to the Federal courts. A taxpayer chooses the route to pursue a tax conflict from among four alternatives (as illustrated in Exhibit 2.4 and Concept Summary 2.1 in the text).

    a. U.S. Court of Federal Claims (hears tax and other monetary claims against the Federal government). This court formerly was called the U.S. Claims Court. There is only one U.S. Court of Federal Claims. The court meets most often in Washington, D.C. Decisions are appealed to the U.S. Court of Appeals (Federal Circuit).

    b. U.S. Tax Court (hears only tax cases). Taxpayer does not pay the deficiency before trial. Decisions are appealed to the U.S. Court of Appeals (Regional Circuit).

    c. Small Cases Division of the U.S. Tax Court (hears only tax cases). No appeal available. The broken line between the U.S. Tax Court and the Small Cases Division in Exhibit 2.4 in the text indicates that there is no appeal from the Small Cases Division.

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(1) $50,000 or less. This court hears cases involving disputed amounts of $50,000 or less.

(2) No written record. The proceedings are informal, and there was no written record of such cases before 2002. Some of the more recent cases can now be found on the U.S. Tax Court website or in online research services.

(3) Informal proceedings.

(a) No necessity for the taxpayer to be represented by a lawyer or other tax adviser.

(b) Special trial judges, rather than Tax Court judges, preside over the proceedings.

(c) Decisions are not precedent for any other court and are not reviewable by any higher court.

d. U.S. District Court (hears tax as well as nontax cases). A jury trial is available. Decisions are appealed to the U.S. Court of Appeals (Regional Circuit). See Exhibit 2.4 in the text.

12. Trial Courts. (See Concept Summary 2.2 in the text.) The differences among the various trial courts can be summarized as follows:

- Number of courts.
- Number of judges.
- Location.
- Jurisdiction of the Court of Federal Claims.
- Jurisdiction of the Tax Court and District Courts.
- Jury trial.
- Payment of deficiency.
- Termination of running of interest.
- Appeals.
- Bankruptcy.

13. Appellate courts. The two appellate courts are the Circuit Courts of Appeal (11 geographical circuits, the circuit for the District of Columbia, and the Federal Circuit) and the Supreme Court (see Exhibit 2.4 in the text).

a. All courts must follow the decisions of the U.S. Supreme Court.

b. A particular Court of Appeals need not follow the decisions of another Court of Appeals.

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c. District Courts, the Tax Court, and the Court of Federal Claims must abide by the precedents set by the Court of Appeals of the relevant jurisdiction.

ADDITIONAL LECTURE RESOURCE

Jurisdiction of the Courts of Appeal

First
Maine
Maryland
Massachusetts
New Hampshire
Rhode Island
Puerto Rico

Second
Connecticut
New York
Vermont

Third
Delaware
New Jersey
Pennsylvania
Virgin Islands

District of Columbia
Washington, D.C.

Fourth
Arkansas
North Carolina
South Carolina
Virginia
West Virginia

Fifth
Canal Zone
Louisiana
Mississippi
Texas

Sixth
Kentucky
Michigan
Ohio
Tennessee

Seventh
Illinois
Indiana
Wisconsin

Eighth
Colorado
Iowa
Minnesota
Missouri
Nebraska
North Dakota
South Dakota

Ninth
Alaska
Arizona
California
Hawaii
Idaho
Montana
Nevada
Oregon
Washington
Guam

Tenth
Kansas
New Mexico
Oklahoma
Utah
Wyoming

Eleventh
Alabama
Florida
Georgia

Federal
U.S. Court of Federal Claims

d. Bankruptcy court. In certain situations, a bankruptcy court may have jurisdiction over tax matters. Since the filing of a bankruptcy petition prevents creditors from filing a claim against a person, a tax dispute may be settled by the bankruptcy court.

e. Locating court cases. Tax cases can be found in a variety of different official and unofficial sources. The instructor can utilize Figure 2-2 in these Lecture Notes to explain the different sources in which tax cases are published.

14. The appellate process. The role of the appellate court is limited to a review of the trial record compiled by the trial court. The appellate process usually involves a determination of whether the trial court applied the proper law in arriving at its decision.

a. Bound by findings of facts unless they are clearly erroneous.

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b. The appellate court may approve (affirm) or disapprove (reverse) the lower court's findings, or it may send the case back for further consideration (remand).

c. District Courts, the Tax Court, and the Court of Federal Claims must abide by the precedents set by the Court of Appeals of jurisdiction.

d. All courts must follow the decision of the U.S. Supreme Court.

e. Since the *Golsen* decision [*Jack E. Golsen*, 54 T.C. 742 (1970)], the Tax Court decides a case as it believes the law should be applied only if the Court of Appeals has not passed on the issue.

f. The U.S. Supreme Court grants certiorari to resolve a conflict among the Courts of Appeals or where the tax issue is extremely important.

(1) The granting of a Writ of Certiorari indicates that at least four of the nine members of the Supreme Court believe that the issue is of sufficient importance to be heard by the full Court.

15. Judicial citations. Judicial citations usually follow a standard pattern: case name, volume number, reporter series, page or paragraph number, court, and year of the decision.

a. U.S. Court of Federal Claims. Prior to October 1, 1982, the Claims Court was called the Court of Claims. Beginning on October 29, 1992, the Claims Court underwent a further name change. The new designation, U.S. Court of Federal Claims, begins with Volume 27 of the former *Cl.Ct.* (West citation) now abbreviated as *Fed.Cl*. Claims Court and Court of Federal Claims decisions are now appealable to the Federal Circuit, whereas they were previously appealable only to the Supreme Court.

(1) *Court of Claims Reporter*. The *Court of Claims Reporter* series, published by the U.S. Government Printing Office, is the primary source of these former Court of Claims cases.

(2) *Federal Reporter and Claims Court Reporter*. Court of Claims cases from 1929 to 1932 and from 1960 to September 1982 can be found in the *Federal Reporter*, published by West. Beginning in October 1982, these Claims Court decisions are published in West's *Claims Court Reporter*.

(3) *Federal Claims Reporter*. Beginning with Volume 27 on October 30, 1992, the name of the reporter is changed to the *Federal Claims Reporter*.

b. U.S. Tax Court. Often called the "poor person's court" because a taxpayer does not have to pay the proposed deficiency in order to bring a case before the court.

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(1) Organization and authority. In 1969, the Tax Court transitioned from an administrative court to a judicial court. Nineteen regular judges produce both "regular decisions" and so-called "memorandum decisions."

(2) Tax Court decisions. Regular Tax Court decisions are published by the U.S. Government Printing Office as the *Tax Court of the United States Reports*.

c. Memorandum decisions. Memorandum decisions are reproduced by the government in mimeograph form only. However, RIA publishes RIA (formerly Prentice-Hall) T.C. Memorandum Decisions and Commerce Clearing House makes them available as Tax Court Memorandum Decisions.

Other Sources of the Tax Law

16. Tax treaties. Tax legislation enacted in 1988 provided that neither a tax law nor a tax treaty takes general precedence. If there is a conflict between the Code and a treaty, the most recent item takes precedence.

17. Tax periodicals.

a. Can shorten the research time needed to resolve a tax issue.

WORKING WITH THE TAX LAW—TAX RESEARCH TOOLS

Commercial Tax Services

18. Loose leaf tax services. A number of publishers provide loose leaf (or other currently supplemented) tax services for practitioners. Some of the major services include:

a. Research Institute of America's (RIA) *United States Tax Reporter* (formerly P-H's *Federal Taxes*).

b. Commerce Clearing House's (CCH) *Standard Federal Tax Reporter*.

c. RIA's *Federal Tax Coordinator 2d.*

d. *Mertens Law of Federal Income Taxation* (Clark, Boardman, Callaghan).

e. *Federal Income, Gift, and Estate Taxation* (Warren, Gorham and Lamont).

f. Bureau of National Affair's (BNA) *Tax Management Portfolios*.
Many of these services are also available electronically.

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19. Assessing tax services. In terms of assessing the major tax services, the following points are relevant:

    a. Except for arrangement of the subject matter, there is not much difference between CCH's *Standard Federal Tax Reporter* and RIA's *United States Tax Reporter*.

    b. RIA's editorial content is generally more detailed than CCH's editorial content. The RIA editorial materials also contain more detailed tax-planning discussions. However, many practitioners feel that rule coverage and case law background are more extensive in CCH.

    c. Mertens is an excellent source if the emphasis is on background material for in-depth research. Mertens is, however, difficult reading due to its legalistic style. Also, updating is less frequent than most other services and not as accessible.

    d. BNA's *Tax Management Portfolios* (TMPs) comprise a series of monographs on various subjects. As the treatment of a subject usually is exhaustive, a portfolio can serve as a convenient means of familiarizing the reader with the material. Note that portfolios are generally updated on a three-year cycle.

    e. In summary, the day-to-day, all-purpose services are CCH and RIA. Mertens and the TMPs are useful for more extensive research and background.

Using Online Tax Services

20. RIA's *Checkpoint* and CCH's *Intelliconnect* are commonly used online tax research services. (Westlaw and Lexis are more commonly used by law firms.) Both services provide access to primary and secondary sources of tax law.

21. Internet. See Exhibits 2.6 and 2.7 in the text.

22. Key ways to use an online tax service.

    a. Choose keywords for the search carefully.

    b. Take advantage of connectors.

    c. Be selective in choosing a database.

    d. Use a table of contents, index, or citation approach.

Noncommercial Online Tax Services

23. Search Home pages.

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24. Search news groups.

WORKING WITH THE TAX LAW—TAX RESEARCH

25. Definition of research. Tax research is the method whereby one determines the best available solution to a situation that possesses tax consequences. In other words, it is the process of finding a professional conclusion to a tax problem. The problem might originate either from completed or proposed transactions. Tax research involves the following procedures (see Exhibit 2.8 in the text):

    a. Identifying and refining the problem.

    b. Locating the appropriate tax law sources.

    c. Assessing the validity of the tax law sources.

    d. Arriving at the solution or at alternative solutions with due consideration given to nontax factors.

    e. Effectively communicating the solution to the taxpayer or the taxpayer's representative. See Exhibits 2.9, 2.10, and 2.11 in the text.

        (1) A short review of the fact pattern that raises the issue.

        (2) A clear statement of the research question/issue.

        (3) A review of the pertinent tax law sources (e.g., Code, administrative sources, judicial authority).

        (4) Any assumptions made in arriving at the conclusion.

        (5) The conclusion recommended and the logic or reasoning supporting it.

        (6) The references consulted in the research process.

    f. Following up on the solution in the light of new developments.

Identifying the Problem

26. Problem identification must start with a compilation of the relevant facts involved. In other words, all of the facts that may have a bearing on the problem must be gathered.

Refining the Problem

27. Use new facts to refine the tax problem.

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Locating the Appropriate Tax Law Sources

28. Once the problem is clearly defined, we index the volume of a hard copy tax service or a keyword search on an online tax service.

Assessing the Validity of the Tax Law Sources

29. Once a source has been located, the next step is to assess it in light of the problem at hand. Proper assessment involves careful interpretation of the tax law with consideration given to its relevance and validity.

30. Interpreting the Internal Revenue Code. This is the greatest challenge for the IRS. The language of the Code is difficult to comprehend fully.

31. Assessing the validity of a Treasury Regulation.

    a. Give the Code equal weight when dealing with taxpayers and their representatives.

    b. Proposed Regulations are not binding.

    c. The burden of proof is on the taxpayer.

    d. If the taxpayer loses the challenge, then a 20% negligence penalty may be imposed.

    e. Final Regulations provide instructions about internal management.

    f. Interpretive Regulations are hard and solid and almost impossible to overturn.

    g. In some Code sections, Congress has given the Treasury Secretary the authority to prescribe Regulations to carry out the details of administration.

    h. Apply the legislative reenactment doctrine.

32. Assessing the validity of other administration sources of the tax law. In any dispute with the IRS on the interpretation of tax law.

33. Assessing the validity of judicial sources of the tax law.

    a. The higher the level of the court that issued a decision, the greater the weight accorded to that decision.

    b. More reliance is placed on decisions of courts that have jurisdiction in the area where the taxpayer's legal residence is located.

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c. A Tax Court Regulator decision carries more weight than a memorandum decision, because the Tax Court does not consider memorandum decisions to be binding.

d. A Circuit Court decision where certiorari has been requested and denied by the U.S. Supreme Court carries more weight than a Circuit Court decision that was not appealed.

e. A decision that is supported by cases from other courts carries more weight than a decision that is not supported by other cases.

f. The weight of a decision also can be affected by its status on appeal.

34. Assessing the validity of other sources.

a. In Notice 90-20, the IRS expanded the list of substantial authority for purposes of the accuracy-related penalty in § 6662 to include a number of secondary materials.

Arriving at the Solution or at Alternative Solutions

Communicating Tax Research

35. A good tax research communication should contain:
- A clear statement of the issue.
- A short review of the facts that raise the issue.
- A review of the pertinent tax law source.
- Any assumptions made in arriving at the solution.
- The solution recommended and the logic or reasoning supporting it.
- The references consulted in the research process.
- It should tell the audience what was researched, the results of the research, and the justification for the recommendation made. (See Exhibits 2.9 and 2.10 in the text.)

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Table 1
Primary and Secondary Tax Law Sources

	Primary	Secondary
16th Amendment to Constitution	X	
Tax Treaty	X	
Internal Revenue Code Section	X	
U.S. Supreme Court Decision	X	
U.S. Circuit Court of Appeals Decision	X	
Tax Court Memorandum Decision	X	
Tax Court Regular Decision	X	
U.S. District Court Decision	X	
U.S. Court of Federal Claims Decision	X	
Small Cases Division of U.S. Tax Court	X**	
Final Regulation	X	
Temporary Regulation	X*	
Proposed Regulation	X***	
Revenue Ruling	X	
Revenue Procedure	X	
Senate Finance Committee Report	X	
Bluebook		X
Letter Ruling		X
Technical Advice Memorandum		X
Actions on Decisions		X
Determination Letter		X
Harvard Law Review article		X
Field Service Advice		X
General Counsel Memorandum		X

* Can be outstanding for three years at most.

The categorization of a tax law source as a primary or a secondary source is not black and white. All of the sources categorized as primary in the above table are so categorized because all can be relied on to defend against the application of penalties by the IRS. However, note the following:

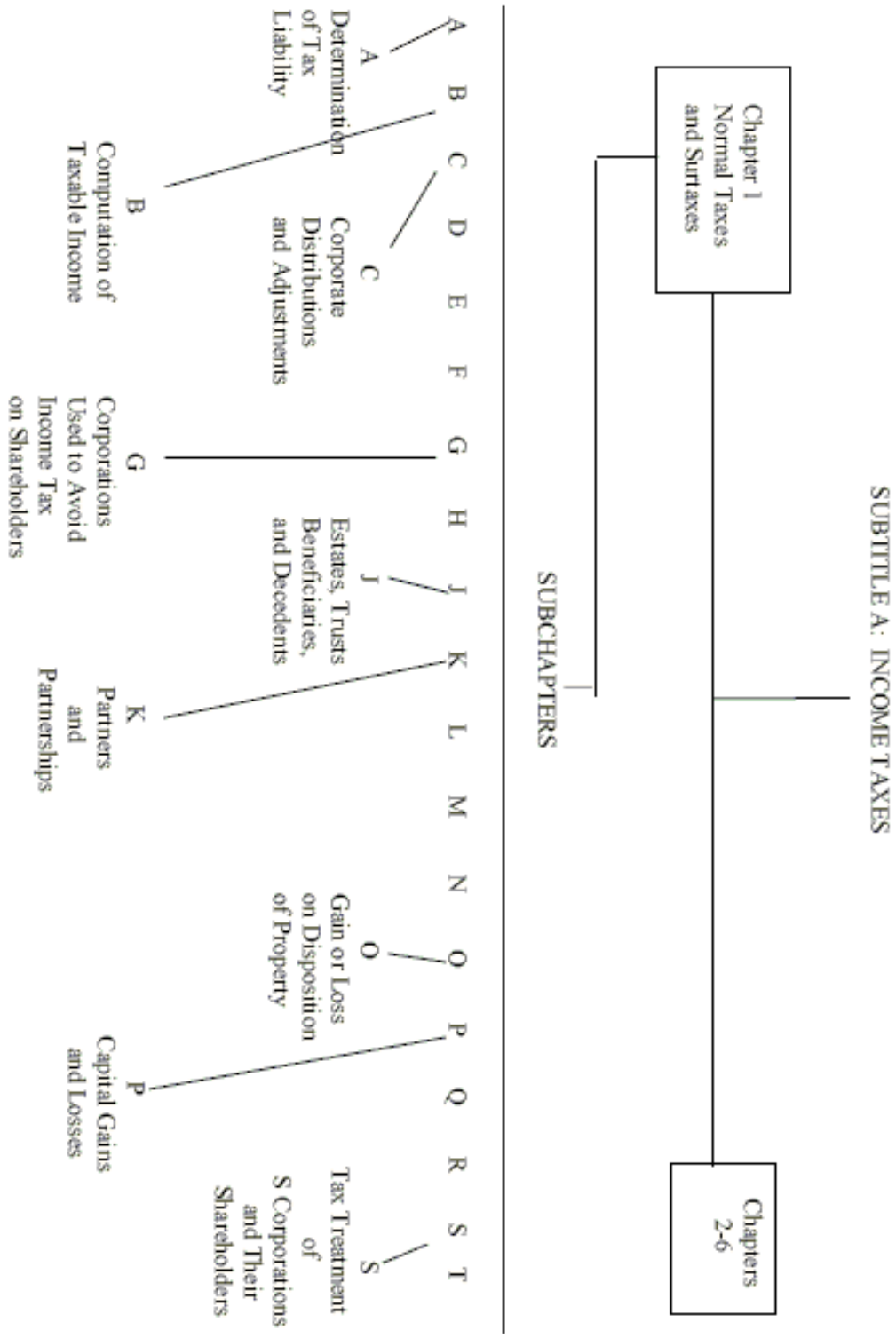
** The Tax Court indicates that Small Cases Division opinions should not be used or cited as precedent. As such, these decisions could be categorized as secondary sources.

*** Proposed Regulations are not binding. That is, a taxpayer is not required to follow the guidance in the proposed Regulation unless (or until) the Regulation becomes final. This could lead to the categorization of a proposed Regulation as a secondary source.

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Figure 2-1



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Figure 2-2
Location of Judicial Sources

	USTC Series	AFTR Series	F.Supp. Series	F.3d Series	Cls.Ct. Series	S.Ct. Series[a]
U.S. District Courts (tax cases)	Yes	Yes	Yes	No	No	No
U.S. Tax Court[b]	No[c]	No[c]	No	No	No	No
U.S. Court of Federal Claims[d] (tax cases)	Yes	Yes	No[e]	Yes[e]	Yes[e]	No
U.S. Courts of Appeal (tax cases)	Yes	Yes	No	Yes	No	No
U.S. Supreme Ct. (tax cases)	Yes	Yes	No	No	No	Yes
U.S. District Courts[f] (all cases)	No	No	Yes	No	No	No
U.S. Courts of Appeal (all cases)	No	No	No	Yes	No	No
U.S. Supreme Court (all cases)	No	No	No	No	No	Yes

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Notes for Figure 2-2:

a Answers also apply to the *United States Supreme Court Reports* (abbreviated U.S.) and to the *United States Reports, Lawyers Edition* (abbreviated L.Ed.).

b Regular (not memorandum) decisions are published by the U.S. Government Printing Office (GPO) in *Tax Court of the United States Reports*.

c Both CCH and RIA (formerly P-H) have separate reporters for Regular, Memorandum, and Small Cases Division decisions of the U.S. Tax Court.

d All decisions (both tax and nontax) of the U.S. Court of Federal Claims are published by the U.S. GPO in the *Claims Court Reporter Series*. From 1960 to October 1, 1982, Court of Claims decisions were published in the *Court of Claims Reporter Series*.

e From 1932 to 1960, the Court of Claims decisions were published in the *F.Supp. Series*. Beginning October 1982, the Claims Court decisions are published in the *Claims Court Reporter*. Beginning on October 30, 1992, the Claims Court underwent a further name change. The new designation, U.S. Court of Federal Claims, begins with Volume 27 of the former *Cl.Ct.* (West citation) now abbreviated as *Fed.Cl.*

f "All cases" has reference to nontax as well as tax decisions. Thus, it would include such varied issues as interstate transportation of stolen goods, civil rights violations, and anti-trust suits.

WORKING WITH THE TAX LAW—TAX PLANNING

36. Tax research and tax planning are inseparable.
- The primary purpose of effective tax planning is to reduce the taxpayer's total tax bill.
- The secondary objective of effective tax planning is to reduce or defer the tax in the current tax year.

Nontax Considerations

37. Tax considerations may impair the exercise of sound business judgment by the taxpayer. The goal should be a balance that recognizes the significance of taxes, but not beyond the point where planning detracts from the exercise of good business judgment.

Components of Tax Planning

38. Avoid the recognition of income.

39. Defer the recognition of income.

40. Convert the classification of income.

41. Choose the business entity with the desired tax attributes.

42. Preserve formalities by generating and maintaining supporting documentation.

43. Act in a manner consistent with the intended objective.

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Tax Avoidance and Tax Evasion

44. Avoidance versus evasion. There is a fine line between legal tax planning and illegal tax planning—tax avoidance versus tax evasion. However, the consequences of the two are as vast as the difference between a lightning bug and lightning.

    a. Tax avoidance. Tax avoidance is merely tax minimization through legal techniques. In this sense, tax avoidance becomes the proper objective of all tax planning.

    b. Evasion. Evasion, while also aimed at the elimination or reduction of taxes, connotes the use of subterfuge and fraud as a means to an end.

Follow-Up Procedures

Tax Planning—A Practical Application

TAXATION ON THE CPA EXAMINATION

45. The CPA examination has changed from a paper-and-pencil exam to a computer-based exam with increased emphasis on information technology and general business knowledge. The 14-hour exam has four sections, and taxation is included in the three-hour Regulations section.

46. Each exam section includes multiple-choice questions and two other sections that have short task-based simulation questions. The Regulations section is 60% Taxation and 40% Law & Professional Responsibilities.

47. Candidates can learn more about the CPA examination at www.cpa-exam.org. This online tutorial site's topics include:
    - Common tools.
    - Navigation.
    - Form completion.
    - Numeric entry.
    - Research questions.
    - Authoritative literature search.
    - Written communication.

RESEARCH PROBLEMS

Solutions to end-of-chapter Research Problems are located in the Solutions Manual.

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IN-CLASS EXERCISES

Q1. The shareholders of Red Corporation and Green Corporation want assurance that the consolidation of the corporation into Blue Corporation will be a nontaxable reorganization.

Solution:
The proper approach is to request that the National Office of the IRS issue a letter ruling concerning the income tax effect of the proposed transaction.

Q2. Chris operates a barbershop in which he employs eight barbers. To comply with the rules governing income tax and payroll tax withholding, Chris wants to know whether the barbers working for him are employees or independent contractors.

Solution:
The proper procedure is to request a determination letter on their status from the appropriate Area Director.

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CHAPTER 1

AN INTRODUCTION TO TAXATION AND UNDERSTANDING THE FEDERAL TAX LAW

SOLUTIONS TO PROBLEM MATERIALS

DISCUSSION QUESTIONS

1. (LO 1)
   a. By becoming a dealer, any gains and losses John has are converted from capital to ordinary classification.

   b. Theresa has become self-employed. Now she will be subject to self-employment tax and will have to make quarterly installment payments of estimated income and payroll taxes.

   c. Due to the home mortgage interest deduction and property tax deduction, most new home-owners will itemize their deductions *from* AGI. Thus, Paul probably will no longer claim the standard deduction on his income tax return.

2. (LO 1) The income tax consequences that result are Marvin's principal concern. Any rent he receives is taxed as income, but operating expenses and depreciation will generate deductions that offset some or all of the income or even yield a loss. Marvin must also consider the effect of other taxes. Because the property is being converted from residential to commercial use, he can expect an increase in the ad valorem property taxes levied by the local (and perhaps even the state) taxing authorities. Besides the real estate taxes, personal property taxes could be imposed on the furnishings.

3. (LO 2) The statement is only partly correct. The Federal income tax on corporations was not a problem as it had previously been sanctioned by the Supreme Court. What had been declared unconstitutional was the tax on individuals as it applied to the income *from property*.

4. (LO 2) To finance our participation in World War II, the scope of the income tax was expanded considerably—from a limited coverage of 6% to over 74% of the population. Hence, the description of the income tax as being a "mass tax" became appropriate.

5. (LO 2) For wage earners, the tax law requires employers to withhold a specified dollar amount from wages paid to the employee to cover income taxes and payroll taxes. Persons with nonwage income generally are required to make quarterly payments to the IRS for estimated taxes. Both procedures ensure that taxpayers will be financially able to meet their annual tax liabilities. That is, the amounts withheld are meant to prepay the employee's income taxes and payroll taxes related to the wages earned.

6. (LO 3) As to Adam Smith's canon on *economy*, the Federal income tax yields a mixed result. From the standpoint of the IRS, economy exists as collection costs are nominal (when compared with revenue generated). The government's cost of collecting Federal taxes amounts to less than one-half of 1 percent of the revenue collected. Economy is not present, however, if one looks to the compliance effort and costs expended by taxpayers. According to recent estimates, about 56% of individual taxpayers who file a return pay a preparer, and one-third purchase tax software.

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7. (LO 3) A tax is *proportional* if the rate of tax remains constant for any given income level. The tax is *progressive* if a higher rate of tax applies as the tax base increases.

8. (LO 4)
   a. The parsonage probably was not listed on the property tax rolls because it was owned by a tax-exempt church. Apparently, the taxing authorities are not aware that ownership has changed.

   b. Ethan should notify the authorities of his purchase. This will force him to pay back taxes but will eliminate *future* interest and penalties.

9. (LO 4) Although the Baker Motors bid is the lowest, from a long-term financial standpoint, it is the best. The proposed use of the property by the state and the church probably will make it exempt from the school district's ad valorem tax. This would hardly be the case with a car dealership. In fact, commercial properties (e.g., car dealerships) often are subject to higher tax rates.

10. (LO 4)
   a. In this case, the "tax holiday" probably concerns exemption from ad valorem taxes. "Generous" could involve an extended period of time (e.g., 10 years) and include both realty and personalty.

   b. The school district could be affected in two ways. First, due to the erosion of the tax base, less revenue would be forthcoming. Second, new workers would mean new families and more children to educate.

11. (LO 4) A possible explanation could be that Sophia made capital improvements (e.g., added a swimming pool) to her residence and her parents became retirees (e.g., reached age 65).

12. (LO 4) Presuming that the dockage facilities are comparable in Massachusetts, the Morgans may be trying to avoid ad valorem taxes. Taxes on nonbusiness personalty vary from one state to another and are frequently avoided.

13. (LO 4) Until recently, it appeared that Federal excise taxes had declined significantly as to the number of transactions covered. Taxes on the sale of jewelry, leather goods, cosmetics, and admission to entertainment events are no longer taxed by the Federal government. But the enactment of the gas guzzler tax and the tax on tanning salons, in addition to the increase in the tax on tobacco products, seems to indicate an expansion of excise taxes at the Federal level.

14. (LO 4) Herman could have been overcharged, but at least part of the excess probably is attributable to a hotel occupancy tax and a car rental tax. In major cities, these types of excise taxes have become a popular way of financing capital improvements such as sports arenas and stadiums. Consequently, the amount of the taxes could be significant.

15. (LO 4) An *excise tax* is limited to a particular transaction (e.g., sale of gasoline), while a general *sales tax* covers a multitude of transactions (e.g., sale of all nonfood goods).

   a. The following states *do not* impose a general sales tax: Alaska, Delaware, Montana, New Hampshire, and Oregon.

   b. There is no Federal general sales tax.

16. (LO 4)
   a. Jackson County must be in a state that imposes a lower (or *no*) sales tax. With certain major purchases (i.e., big-ticket items), any use tax imposed by the state of the Grays' residence could come into play.

   b. In some states, the sales tax rate varies depending on the county and/or city.

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17. (LO 4) Earl probably purchased his computer out of state through a catalog or via the Internet. In such cases, state collection of the sales (use) tax is not likely.

18. (LO 4) If the tax is imposed on the right to pass property at death, it is classified as an estate tax. If it taxes the right to receive property from a decedent, it is termed an inheritance tax.

    a. Some states impose both an estate tax and an inheritance tax. Some states (e.g., Florida and Texas) levy neither tax.

    b. The Federal government imposes an estate tax.

19. (LO 4) Jake either has a severe misunderstanding as to the rules regarding transfer taxes or is lying to Jessica to delay any parting with his wealth. The marital deduction allows interspousal transfers (whether by gift or at death) free of any tax (either gift or estate). There is no tax reason, therefore, in the case of spousal transfers to prefer transfers at death over lifetime gifts.

20. (LO 4)
    a. The purpose of the unified transfer tax credit is to eliminate the tax on all but substantial gifts and estates.

    b. Yes. The credit for 2016 is $2,125,800; for 2015, it is $2,117,800.

    c. Yes. The credit is available to cover transfers by gift or by death (or both), but the amount can be used only once.

21. (LO 4) $532,000. 19 donees (5 married children + 5 spouses + 9 grandchildren) × $14,000 (annual exclusion for 2016) × 2 donors (Elijah and Anastasia) = $532,000.

22. (LO 4) Both taxes are progressive in nature, but the corporate income tax does not make any distinction as to deductions—only business deductions are allowed. Nor does it require the computation of adjusted gross income (AGI) or provide for the standard deduction and personal and dependency exemptions.

23. (LO 4)
    a. For state income tax purposes, "piggyback" means making use of what was done for Federal income tax purposes. By "decoupling," a state decides not to allow a particular Federal provision (e.g., exclusion, deduction, credit) for state income tax purposes.

    b. A diminishing number of states allow a deduction for Federal income taxes paid.

    c. Most states allow their residents some form of tax credit for income taxes paid to other states.

24. (LO 4) What happened here likely is not a coincidence. The IRS probably notified the state of California regarding Hernando's omission of income. Thus, California followed up with its own audit.

25. (LO 4) If Mike is drafted by a team in one of the listed states, he will escape state income tax on income earned within that state (e.g., training camp, home games). He will not, however, escape the income tax (state and local) imposed by jurisdictions where he plays away games. Called the "jock tax," it is applied to out-of-state athletes and entertainers.

26. (LO 4, 5)
    a. This type of question has no relevance to the state income tax, but is a less than subtle way of encouraging taxpayers to pay any use tax due on Internet and mail-order purchases.

    b. As the preparer of the state income tax return, you should not leave questions unanswered unless there is a good reason for doing so. It appears that Harriet has no justifiable reason.

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27. (LO 4) The checkoff boxes add complexity to the return and mislead taxpayers into presuming that they are not paying for the donation.

28. (LO 4)
a. They uncover taxpayers who were previously unknown to the taxing authority.

b. Amnesty provisions can apply to other than income taxes (e.g., sales, franchise, severance).

c. As of yet, no general amnesty program has been offered for the Federal income tax.

29. (LO 4)
a. FICA offers some measure of retirement security, and FUTA provides a modest source of income in the event of loss of employment.

b. FICA is imposed on both employer and employee, while FUTA is imposed only on the employer.

c. FICA is administered by the Federal government. FUTA, however, is handled by both the Federal and state government.

d. This applies only to FUTA. The merit system rewards employers who have low employee turnover, because this reduces the payout of unemployment benefits.

30. (LO 4)
a. Unlike the Social Security portion of FICA, there is no dollar limit on the imposition of the Medicare tax.

b. The .9% Medicare addition applies to taxpayers with wages or net self-employment income in excess of $200,000 ($250,000 for married filing jointly).

31. (LO 4) Only children under age 18 are excluded from FICA. Other family members, including spouses, must be covered.

32. (LO 4)
a. Severance taxes are transaction taxes that are based on the notion that the state has an interest in its natural resources. The tax is imposed on the extraction of minerals.

b. Franchise taxes are levied on the right to do business in the state. Typically, they are imposed on corporations and are based on their capitalization.

c. Occupational fees are applicable to trades or businesses and are licenses to practice. Most are not significant revenue producers, and the amounts collected are utilized to defray the cost of regulating the profession.

d. Customs duties are taxes on the importation of certain foreign goods. They are imposed by the Federal government and are not found at the state and local level.

e. Export duties are taxes imposed on the export of certain commodities (e.g., oil, coffee). They are common to less-developed nations and are not levied by the United States.

33. (LO 4)
a. The United States is the only country in the OECD (Organization of Economic Cooperation and Development) that does not have a value added tax (VAT). Approximately 80 countries use a VAT. In spite of its extensive use by other countries, the adoption of a VAT by the United States appears doubtful. Instead, the U.S. places high reliance on the income tax as its major revenue source.

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b. A VAT taxes the increment in value as goods move through the production and manufacturing stages to the marketplace. Although the tax is paid by the producer, it is reflected in the selling price of the goods. Therefore, a VAT is a tax on consumption.

c. Because it is an effective generator of revenue, the VAT has been criticized as leading to more government spending.

34. (LO 4)

a. Both the national sales tax and the VAT are taxes on consumption. Both taxes impose more of a burden on low-income taxpayers who must spend a larger proportion of their incomes on essential purchases. Thus, the taxes are regressive in effect.

b. At least in the case of a national sales tax, the regressive effect might be partly remedied by granting some sort of credit, rebate, or exemption to low-income taxpayers.

35. (LO 4, 5)

a. Due to the location of the business and the fact that the employees are "itinerant," Serena may be hiring undocumented aliens. Needless to say, this could cause serious nontax problems involving employment and immigration laws. As to tax problems, is Serena complying with the FICA and income tax withholding rules? Because of the high labor turnover Serena probably has, FUTA costs could be severe.

b. Very high. First, Serena is self-employed. Second, she operates on a cash basis. Third, the opportunity to understate income and/or overstate expenses is extremely high.

36. (LO 5)

a. A correspondence audit is probably involved. These audits involve a limited number of issues (i.e., taxpayer failed to report some dividend income) and most often are easily resolved.

b. What is described is an office audit.

c. The revenue agent's report (RAR) accepts the taxpayer's return as filed.

d. When a special agent becomes involved, this usually means that fraud is suspected.

37. (LO 5) In many unresolved audit disagreements at the agent level, the taxpayer should consider an appeal to the Appeals Division. Although it is part of the IRS, it is authorized to resolve audit disputes. It has greater settlement authority than does the agent. In many cases, a compromise reached at the Appeals Division can avoid a costly and time-consuming judicial proceeding.

38. (LO 5) The purpose of a statute of limitations is to preclude parties from prosecuting stale claims. The passage of time makes the defense of such claims difficult because witnesses and other evidence may no longer be available. In the Federal tax area, statutes of limitations cover additional assessments by the IRS and the pursuit of refund claims by taxpayers.

39. (LO 5)

a. The normal three-year statute of limitations will begin to run on April 15, 2016. When the return is filed early, the regular filing date controls.

b. Now the statute of limitations starts to run on the filing date. If the date of filing controlled (see part a. above), the taxpayer could shorten the assessment period by filing late.

c. If a return that is due is not filed, the statute of limitations does not start to run. It does not matter that the failure to file was due to an innocent error on the part of the taxpayer or adviser.

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d. Regardless of the fact that an innocent misunderstanding was involved, there is no statute of limitations when a return is not filed.

40. (LO 5) No. Interest is not paid if the refund is made within 45 days of when the return was filed. However, a return is not considered filed until its due date. Thus, the period from April 15 to May 28 does not satisfy the 45-day requirement.

41. (LO 5, 6)

a. Normally, the three-year statute of limitations applies to additional assessments the IRS can make. However, if a substantial omission from gross income is made, the statute of limitations is increased to six years. A substantial omission is defined as omitting in excess of 25% of the gross income reported on the return.

b. No, it would not. The proper procedure would be to advise Andy to disclose the omission to the IRS. Absent the client's consent, do not make the disclosure yourself.

c. If Andy refuses to make the disclosure and the omission has a material carryover effect to the current year, you should withdraw from the engagement.

42. (LO 5) $4,000, determined as follows:

Failure to pay penalty [.5% × $40,000 × 2 months]		$ 400
Plus:		
Failure to file penalty [5% × $40,000 × 2 months]	$4,000	
Less failure to pay penalty for the same period	(400)	3,600
Total penalties		$4,000

43. (LO 5)

a. $100,000 (20% × $500,000).

b. $375,000 (75% × $500,000). The answer presumes that civil (not criminal) fraud is involved.

44. (LO 5, 6)

a. No. Because no return was filed, the statute of limitations never runs. But even if a return had been filed, the three-year period for the 2012 tax return would not expire until April 15, 2016, three years after the normal due date for filing.

b. Although you can only recommend that the return be filed, you cannot force him to do so. However, you should not undertake the engagement for 2013 through 2015 if you cannot correctly reflect the tax liability due to the omission for 2012.

45. (LO 5, 6) The practice of outsourcing the preparation of tax returns is ethical if three steps are taken.

- Maintain client confidentiality.
- Verify the accuracy of the work done.
- Notify the client, preferably in writing, of the outsourcing.

46. (LO 7)

a. This is the ideal approach to handling a tax cut—for every dollar lost, a new dollar is gained.

b. Pay-as-you-go is another way of describing revenue neutrality. Thus, tax cuts should not result in an overall loss of revenue.

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c. All the sunset provision does is reinstate the law as it existed prior to the tax cut. Here, the possibility exists that Congress will rescind (or postpone) the sunset provision before it takes effect.

d. Indexation is a procedure whereby the IRS makes annual adjustments to certain key tax components to take into account inflation. Some of the more important components that are adjusted include tax brackets, standard deduction, and personal and dependency exemptions.

47. (LO 7)

a. To encourage pension plans is to stimulate saving (economic consideration). Also, it provides security from the private sector for retirement to supplement rather meager public programs (social considerations).

b. To make education more widely available is to promote a socially desirable objective. A better educated workforce also serves to improve the country's economic capabilities. Thus, education tax incentives can be justified on both social and economic grounds.

c. The encouragement of home ownership can be justified on both social and economic grounds.

48. (LO 7, 8)

a. Social considerations explain the credit. It is socially desirable to encourage parents to provide care for their children while they work.

b. These deductions raise the issue of preferential tax treatment for homeowners—taxpayers who rent their personal residences do not receive comparable treatment. Even so, the encouragement of home ownership can be justified on economic and social grounds.

c. The joint return procedure came about to equalize the position of married persons living in common law states with those residing in community property jurisdictions. Political and equity considerations caused this result.

d. Social considerations dictate that the tax law should not be used to encourage certain activities that are deemed to be contrary to public policy.

e. The NOL carryback provision is an equity consideration that is designed to mitigate the effect of the annual accounting period concept.

f. The installment method of reporting gain is consistent with the wherewithal to pay concept—the seller is taxed when the payments are made by the purchaser.

g. The exclusion from Federal income taxation of interest from state and local bonds can be justified largely on political considerations. Political goodwill is generated by allowing state and local jurisdictions to secure financing at a lower cost (i.e., interest rate) due to favorable Federal income tax treatment.

h. The treatment of prepaid income is justified under the wherewithal to pay concept. It also eases the task of the IRS as to administration of the tax law.

49. (LO 7)

a. Mia's realized gain from the condemnation is $320,000 [$400,000 (amount of award) − $80,000 (cost basis of the warehouse)]. However, her recognized gain is limited to $120,000—the amount received that was not reinvested.

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b. None of the gain is recognized because Mia reinvested the full amount of the condemnation award.

c. As none of the gain was reinvested, the full $320,000 is recognized as income.

d. The involuntary conversion provision can be justified under the wherewithal to pay concept and the notion that the taxpayer's economic position has not changed. In part b., for example, Mia has retained none of the award and has reinvested in property similar to that taken by the city.

50. (LO 8) If the collection is worth more than $1,000, the mother has probably made a gift of the excess value to the daughter. Quite possibly the transaction could result in the imposition of a gift tax. Sales or other transactions between related parties are subject to the arm's length test. In this case, for example, would the mother have made this sale for $1,000 if the purchaser had been an unrelated third party?

SOLUTION TO ETHICS & EQUITY FEATURE

Making Good Use of Out-of-State Relatives (p. 1-10). Who is the true purchaser of the bracelet? If the aunt really made the purchase with her funds and then gave the bracelet to Marcus, no sales or use tax evasion has occurred. More likely, the purchase was made by Marcus indirectly through his aunt—the aunt being reimbursed by Marcus or using funds provided by him. If such is the case, Marcus owes a sales tax on the purchase. Presuming the matter comes to light—the jewelry store might be the weak link—Marcus could be subject to prosecution for tax evasion.

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