

ADVANCED INDIVIDUAL TAXATION

Business 225K – Fall 2017 Online Course

Professor Annette Nellen

Online (at student pace, but with some specified due dates)	September 19 to December 2, 2017 Schedule your time to be sure you have time weekly to watch online video lectures, read, do homework, study. Should work out to about 12 – 16 hours per week (as with a face-to-face class).
Location	Online course: Canvas website log in - https://sjsu.instructure.com/ Final exam in person (see below)
Optional review session	Saturday November 18 from 9 - 11 am at Bunker Hill
Final Exam – at Bunker Hill Classroom	Saturday December 2 from 9 to noon
Office hours	By appointment + available by email or Skype
Office	On campus office is Business Tower 955.
Phone	(408) 924-3508
E-mail	annette.nellen@sjsu.edu NOTE: Use this email to contact Professor Nellen rather than the Canvas website.
Internet	http://www.sjsu.edu/people/annette.nellen/

Course objectives: To gain a deep understanding of the rules on passive activity loss limitation, interest categorization and limitations, individual alternative minimum tax, and individual net operating losses. You will learn the rationale behind these rules, how they interact with other tax provisions, traps, planning opportunities and proposed changes. Rules on self-employment tax, vacation and home office rules, hobby loss, at-risk and flow-through entity rules will also be covered as relevant to passive activity, interest expense, NOL and AMT matters.

The class is designed to give you an opportunity to hone your skills in finding, reading, interpreting and applying the tax law. We will study the IRC provisions along with the legislative histories, regulations and other guidance. From this we will create flowcharts on how the rules work, cautions in dealing with the rules, and identify planning opportunities.

Texts

- Internal Revenue Code (referenced in the presentations slides, Canvas and syllabus)
- Income Tax Regulations tied to IRC sections we'll cover (§§469-X ("X" means each of the sets of 469 regs), 1.163-8T, 1.163-9T, 1.163-10T, 172, 53 - 59) You can obtain the regs from RIA Checkpoint or CCH; the §163 regs are on Canvas as well.
- Reading materials assembled by Professor Nellen and available on the [225K public website](#) or Canvas site for this class.
- Optional – BNA portfolios on course topics (see information in first module on Canvas)

Grading

Research / application exercises (below)	90
Quizzes (online) (7 @ 10 points each)*	60
Check-in via Zoom**	10
Presentation via Brainshark	20
Final Exam (12/2)	<u>120</u>
Total	300

Grades will be assigned based on 90% and above is an A, 80% and above a B and 70% and above is a C, etc. Plus and minus (+/-) will be used as well.

* see Canvas website for due dates; lowest score dropped

** You must participate in one of these two Zoom check-in sessions. The information is posted in the Announcements section of the 225K Canvas site. The purpose is for your instructor to see about student progress and to take a few questions.

1. Friday October 13 from 4 – 5 pm
2. Monday October 16 from 7 – 8 pm

Reading and Assignment Due Dates

Presentation (20 points)

- **Presentation using Brainshark must be completed by 11/13**

You will work with a classmate to create a video on a rule or case you sign up for (every pair of students has a different topic). You will use Brainshark to make the video (I will send you a link for this later in the semester). Details:

- Length – 4 – 6 minutes (so 4 to 6 slides) (any of these topics could be much longer presentations, so you need to hit the highlights in your short video; do not use animation on your slides as it doesn't work well in Brainshark)
- Purpose – explain the rule or case such that your fellow tax practitioners can understand the law, its importance, what type of clients would be affected by the topic. Examples are a good idea, as are referencing the pertinent law.
- Be sure your explanations are clear, the narration and slides are engaging, and correctly explain the law.

To be sure your presentation is technically accurate and clear, you will work on this with a classmate. That is, you'll work together to create and review the slides, as well as prepare a script for recording the slide video presentation. For the narration of the video, it is fine to have just one of you record it provided you were both involved in creating the slides and script. Or, you can both record it, but that requires you both be together at a laptop or computer that has a microphone. You can use the common area at Bunker Hill if you want (generally, Bunker Hill is open 1 hour before classes begin; if unsure, ask Prof. Nellen).

Selecting a partner – look at the “people” link on Canvas to see if you know someone to work with. If you want Prof Nellen to help you pair up, let her know by September 21.

Your video will be posted to the course website to be viewed by your fellow students. These videos will also be tested on the final exam.

Topics to select from (let Professor Nellen know your top 3 choices by 9/29 or earlier; also let Prof Nellen know who your partner is):

- A. *Stanley v. U.S.*, (DC AR) 116 AFTR 2d 2015-6766 (11/12/2015)
- B. Home office deduction for both self-employed and employee
- C. Kiddie Tax and its application to taxable portion of a scholarship
- D. Alimony and child support payments
- E. Charitable contribution of cash and used kitchen equipment (blender, etc.) and used clothes
- F. Charitable contribution of cash or stock (whether appreciated or not); documentation and AGI limits

- G. "Donation" to enter a charitable organization's raffle (see Rev. Rul. 67-246, *Patterson*, TC Memo 1987-252 and other pertinent guidance)
- H. Donation of an individual's used auto to a charity (like you have likely seen ads for on television and billboards)
- I. Casualty loss involving a house damaged by flood
- J. Hobby loss rules of §183 as applied to a concert activity, including the regs and how to report on return (the taxpayer occasionally plays her violin at weddings of friends and family and gets paid \$100/hour, but only has a few gigs per year)
- K. Treatment of gambling winnings and losses by someone who is not a professional gambler, including how to handle winnings and losses while playing at a slot machine (how to net)
- L. Federal and California income tax reporting for California registered domestic partners
- M. *Garcia*, TC Memo 2016-21 (2/16/16) – charitable donation problems and how to avoid
- N. *Hickam*, TC Summary Opinion 2017-66 – §469(c)(7) real estate professional
- O. *Hailstock*, TC Memo 2016-146 – material participation test

Reading and Instructor Presentations

The table below lists the sequence of topics. These topics will be covered through a combination of reading (mostly primary authorities), online video presentations with accompanying Powerpoint files you can download (and print if you wish), quizzes on the video presentations, research/application questions, and a project where you explain a particular individual provision and provide examples and planning ideas for it (the "Brainshark" assignment).

You will email your homework assignments to your instructor using annette.nellen@sjsu.edu. If it formats in a legible manner, you can just paste your homework into your email to your instructor (no need to attach as a word doc). (Do not use Canvas to submit homework.)

Topics	OBJECTIVES - The goal of this lesson is to be able to explain the answers to the following questions and understand the significance of the rules in practice and theory:	Reading
1	Course Overview <ul style="list-style-type: none"> ▪ Learning objectives for this course ▪ Relevance of the topics to individual taxpayers 	Introductory quiz (no value) and audio file [the quiz is for your benefit; no need to turn it in]
2	Review of Itemized Deduction Rules	Complete the IRS Advanced Menu tutorial on Itemized Deductions and Complete Homework #1 Be sure to click the links in the lessons so you don't miss anything!

3	<p>Interest Expense Limitations for Individuals</p> <ul style="list-style-type: none"> • What is interest expense? • How do the interest tracing rules of Reg. §163-8T work and why? • What is personal interest? Why is it non-deductible? What about §221? • What is investment interest expense and what limitations apply to it? • Introduction to home mortgage interest rules 	<p>Read (see Canvas):</p> <ul style="list-style-type: none"> - TRA '86 legislative history on interest expense limitations - §163 and §221 - §1.163-8T - §1.163-9T - Notice 89-35 and FSA 200011025 - Revenue rulings on §163(d) <p>Review: Form 4952 and instructions</p>
	<p>Home Mortgage Interest Limitations</p> <ul style="list-style-type: none"> • What is home mortgage interest? • What limitations apply to home mortgage interest? • What is the tax treatment of points? • What issues can arise from refinancings? • What planning opportunities arise from the home mortgage interest rules? • What recordkeeping is needed to comply with all of the interest expense rules for individuals? <p>Tax-exempt interest income and related interest expense</p>	<p>Read (225K Canvas site):</p> <ul style="list-style-type: none"> - §163(h) - §1.163-10T - Form 1098 - Rev Rul. 87-22 - Rev Proc 87-15 - Rev Rul 92-91 - §265 and §1.265-2 - cases listed on Canvas
4	<p>Passive Activity Loss Limitation Rules</p> <p>Introduction</p> <ul style="list-style-type: none"> • Why do we have §469? • What does §469 entail? • Is §469 a method of accounting? • What is the basic rule of §469? • Who is subject to §469? • What is a passive activity? (§1.469-1(e)) • What is a rental activity? (§1.469-1(e)(3)) • What is a trade or business? • What is material participation and the 7 tests? (§1.469-5) • What form is used to report and track PALs and PACs? 	<p>Read (225K Canvas site):</p> <ul style="list-style-type: none"> - TRA '86 legislative history - IRS Pub 925 - §469 <p>Skim: Form 8582</p>

	<p>Passive Activity Loss Limitation – More definitions and special rules</p> <ul style="list-style-type: none"> • What is an “activity”? • Details – passive activity income, passive activity deduction, passive activity credit • Recharacterization rules – when might income not be PAI? (§1.469-2(f)) • What special rules apply to rental real estate with active participation? • What special rules apply to real estate professionals? • What is the self-charged interest rule? 	<p>Read (225K Canvas site):</p> <ul style="list-style-type: none"> - 1993 legislative history - §469 regulations (-1, -2, -3, -4, -7, -9) - Rev. Proc. 2011-34 - Article (on Canvas) – "Working with the Passive Activity Loss Groupings," April 2012, <i>Practical Tax Strategies/Taxation for Accountants</i> (WG&L) - other materials posted to Canvas
	<p>Passive Activity Loss Limitation – special rules</p> <ul style="list-style-type: none"> • What happens to suspended PALs and PACs upon disposition of a passive activity? • What does “disposition” mean? • How does §469 interact with other IRC sections and rules? • How does §469 apply to passthrough entities? • How does §469 apply to publicly-traded partnerships? • Cautions in dealing with §469 • Reporting PALs and related recordkeeping 	<p>Read (225K Canvas site):</p> <ul style="list-style-type: none"> - §469 regulations (-10 and review -5 and -5T) - Rev Rul 92-92 - Notice 2008-64 - Form 8582 and instructions
5	<p>Individual Alternative Minimum Tax (AMT)</p> <ul style="list-style-type: none"> • What is AMT? • Why do we have AMT? • Which individuals owe AMT? • How is AMT computed for an individual? • How can AMT be avoided? • What is the minimum tax credit (MTC) and how is it computed and used? • What recordkeeping is needed for AMT? • What issues currently exist for the AMT? 	<p>Read (225K Canvas site):</p> <p>IRC §§53, 55 – 59</p> <p>Review Form 6251 and instructions</p>
6	<p>Special topics related to course topics</p> <ul style="list-style-type: none"> • Student videos – be sure to watch them all • Rental of residences • Comprehensive federal tax reform • Legislative outlook • Net Investment Income Tax (§1411) and §469 	<p>See materials on Canvas</p>

7	<p>Net Operating Losses (NOLs) of Individuals</p> <ul style="list-style-type: none"> • What is an NOL? • How is an NOL computed for individuals? • What are the carryover rules? • What recordkeeping is needed? 	Read §172 and 225K Website materials (includes pages in BNA portfolio)
Dec 3	<p>Final Exam – December 2 from 9 am to noon at the Bunker Hill classroom.</p> <p>You may bring one page of notes (front and back) to use on the exam.</p>	180 minutes

Research/Application Questions

Be sure to explain all of your answers and provide the citations to the relevant primary authority.

Itemized Deductions (DUE October 2) [10 points]

1. The IRS VITA training site has many tutorials you may find of interest (<http://apps.irs.gov/app/vita/sitemap.jsp>). Complete the Advanced tutorial on Itemized Deductions. Answer these questions:
 - a. How long did it take you to complete the tutorial?
 - b. Was it useful to you? Why or why not (be specific)?
 - c. Why might an amount listed on a property tax bill not be deductible on Schedule A?
 - d. Are investment related expenses deductions (such as a subscription to the *Wall Street Journal*)? If yes, how?
 - e. What questions should you ask an individual client to be sure they are entitled to charitable contributions made in cash to the Red Cross and of used household goods and clothes made to the Salvation Army? Consider the basic rules learned in the IRS tutorial and a preparer's due diligence obligations as laid out in Circular 230:

Circular 230, §10.34(d) - *Relying on information furnished by clients*

- “A practitioner advising a client to take a position on a tax return, document, affidavit or other paper submitted to the Internal Revenue Service, or preparing or signing a tax return as a preparer, generally may rely in good faith without verification upon information furnished by the client. The practitioner may not, however, ignore the implications of information furnished to, or actually known by, the practitioner, and must make reasonable inquiries if the information as furnished appears to be incorrect, inconsistent with an important fact or another factual assumption, or incomplete.”

Interest Expense (DUE by October 23) [30 points]

1. In 2016, Jane borrowed \$25,000 using half of the funds to buy Disney stock and half to buy tax-exempt bonds. Assuming she paid \$1,600 of interest in 2016, how does she report it on her tax return?
2. Would Jane have obtained a better result if she had borrowed the \$25,000 as home equity debt? explain including what the tax treatment is in this scenario.
3. The Greens plans to remodel their home. They already have acquisition debt of \$1 million and home equity debt of \$40,000. They borrow \$120,000 secured by their home to make the improvements. What is the tax treatment of the interest on this debt? Explain.
4. Agnes borrowed \$700,000 + used \$400,000 of her savings to build a home to use as her principal residence. Construction began on 4/1/15 and the home was completed on 7/1/17. Where possible, the debt is secured by the land and construction.
 - a. May Agnes deduct the interest incurred during the construction period? Explain. Hint: Does she have a qualified residence? Do any special rules apply?
 - b. On 7/21/17, Agnes borrowed \$100,000 secured by her new home. What type of debt is this? Explain.
5. The Smiths have the following debt on their principal residence:

Refinanced acquisition debt	\$700,000	interest rate is 5%
Debt for home improvements	\$400,000	interest rate is 6%
Home equity debt	\$ 75,000	interest rate is 7%

Assuming simple interest, how much interest expense can the Smiths deduct in 2017? Explain.

Passive Activities (DUE by November 20) – 40 points

1. In 2015, Sarah started some web-based activities. She started selling her stamp and coin collections via eBay. In addition, she has some ads on her rare stamps and coins blog. Sarah spends about 6 hours per week selling stamps and coins plus another 5 hours on the blog.
 - a. Under the §469 regulations, how many activities does Sarah have? Explain.
 - b. Assume Sarah pays Third Party Z to post the coins and stamps online and Third Party X handles the payment arrangements. Both of these third parties spend about 100 hours per year on their work for Sarah. Sarah spends about 150 hours per year finding more coins and stamps to sell and handling business strategy. Is Sarah a material participant? Explain.

2. Henry has the following activities

Activity	Type	Date acquired	2016 income (loss)	# hours
A	Rental – single family residence	2008	(\$7,000)	200
B	Movie theater operated through a partnership	2013	(\$6,000)	-0-
C	Graphic design business operated as sole proprietorship, no employees	2009	34,000	400
D	Car stereo installation business with two employees who each work about 30 hours per week	2012	\$5,000	270
E	Publicly-traded partnership	2008	\$7,000	-0-

- a. How much income or loss will Henry report on his 2017 Form 1040 if his AGI before considering any of the items in the above table is \$100,000? Explain how each item is treated and why.
 - b. If Henry’s graphic design business had one employee who worked 900 hours per year, how would your answer to (a) change?
 - c. If Henry worked 1,600 hours per year as a real estate broker, along with the hours in the chart above and no other work, would any of your answers to (a) change? Explain.
3. Larry is a partner in a CPA partnership. He rents a building he owns to the partnership and charges fair rental of \$4,000 per month, generating net rental income for himself. Is this a "rental activity" under §469 for Larry? Does it produce PAI for him? Explain.

AMT (DUE by November 27) 10 points

1. Information for Mr. and Mrs. Gehry for 2017 is listed below. They have three dependent children and claimed dependency exemptions for them. The deduction and income items listed below have already been used to calculate their \$220,000 of taxable income. They itemized their deductions (all of their itemized deductions are listed below) and had no capital gains or losses.
 - a. Calculate their 2017 AMT (if any) (show the details of your calculation).
 - b. Which of the items that affect AMT will create a minimum tax credit for the Gehry's?

Taxable income	\$220,000
Mortgage interest on debt to acquire principal residence; debt balance is below \$1 million.	\$29,000
Mortgage interest on home equity debt; balance is under \$100,000.	\$8,000
Property taxes on residence	\$16,000
State income taxes	\$27,500
Charitable contributions	\$6,000
Miscellaneous itemized deductions claimed on Schedule A	\$3,400
Spread on exercise of ISO	\$73,000
Private activity bond interest on bonds purchased in 2005	\$4,100

University Policies

Academic integrity

Students should know the University's Academic Integrity Policy that is available at <http://www.sjsu.edu/senate/docs/F15-7.pdf>. Your own commitment to learning, as evidenced by your enrollment at San Jose State University and the University's integrity policy, require you to be honest in all your academic course work. Faculty members are required to report all infractions to the office of Student Conduct and Ethical Development. The website for Student Conduct and Ethical Development is available at <http://www.sjsu.edu/studentconduct/>.

Instances of academic dishonesty will not be tolerated. Cheating on exams or plagiarism (presenting the work of another as your own, or the use of another person's ideas without giving proper credit) will result in a failing grade and sanctions by the University. For this class, all assignments are to be completed by the individual student unless otherwise specified. If you would like to include in your assignment any material you have submitted, or plan to submit for another class, please note that SJSU's Academic Policy F06-1 requires approval of instructors.

Be sure to read the following additional information on academic integrity and avoiding plagiarism from Professor Nellen at:

<http://www.sjsu.edu/people/annette.nellen/website/ClassInfo.html#Integrity>

All work you do must be your own work. If your work includes anything you are representing as your own which is not your own, you will receive zero points for the assignment and a referral to Judicial Affairs will be required. Be sure to read the SJSU Academic Integrity Policy and do the right thing. When in doubt, ask your instructor.

Do not discuss quiz questions or answers with classmates. You are all taking these quizzes at different times because they are online and are taken within a window rather than at a set time.

Do not share quiz questions or answers with anyone else. If someone offers to give you quiz questions, do not take them as doing so is a violation of academic integrity for both parties and you'll fail the class (and risk expulsion from the program).

Campus Policy in Compliance with the American Disabilities Act

If you need course adaptations or accommodations because of a disability, or if you need to make special arrangements in case the building must be evacuated, please make an appointment with me as soon as possible, or see me during office hours. Presidential Directive 97-03 requires that students with disabilities requesting accommodations must register with the DRC (Disability Resource Center) to establish a record of their disability.

Consent for Recording of Class and Public Sharing of Instructor Material

University Policy S12-7, <http://www.sjsu.edu/senate/docs/S12-7.pdf>, requires students to obtain instructor's permission to record the course.

- Common courtesy and professional behavior dictate that you notify someone when you are recording him/her. You must obtain the instructor's permission to make audio or video recordings in this class. Such permission allows the recordings to be used for your private, study purposes only. The recordings are the intellectual property of the instructor; you have not been given any rights to reproduce or distribute the material.”
- Course material developed by the instructor is the intellectual property of the instructor and cannot be shared publicly without his/her approval. You may not publicly share or upload instructor generated material for this course such as exam questions, lecture notes, or homework solutions without instructor consent.
- You may request permission, either in writing or orally, at any time during the semester.
- If students or guests may be on the recording, permission of those students or guests should be obtained as well.