CHAPTER 3 SYLLABUS  INCOME TAXATION OF THE FAMILY

A. **Introduction**

Several amounts in the chapter have been adjusted for inflation. The 2007 amounts are on h/o 42; make these changes in your casebook. You will not have to compute a taxpayer’s income tax for the course. I will discuss the tax computation using h/o 43-44.

B. **What is Income**

Read 163-170 and h/o 45; do problems 1 and 3 on 169.

C. **Exclusions**

Read 170-179 (omit the last full paragraph on 177-8) and h/o 46-48; do problems 1-3 on 179 and the problem on page 400. Using the facts of the problem on page 400, how much gross income will Neal have if he was married at the time of the sale and sold the home for a $600,000 gain?

D. **Personal Deductions**

Tax Computation and Standard Deduction: Read 180-182.

Alimony: Read h/o 49-50, then 182-184; do the problems on 184.

Charitable Contributions: Read 184 up to the first full paragraph on 187; do problems 1-2 on 188.

Interest: Read 189-191; omit the first full paragraph on 190. Do problem 2 on 191.

Taxes and Medical Expenses

Read 192 up to the first full paragraph on 196. Do problems 2 and 3 on 197; refer to cafeteria plans on 175 and h/o 46 (assigned in section C. above) for problem 3.

Casualty Losses: Read 197-199 and problem 1 on h/o 51.

Phaseout of Itemized Deductions

Read 199. Itemized deductions are phased out by only 2% of the amount that AGI exceeds the threshold amount ($156,400) in 2007 and 1% in 2008-2009. The phaseout ends in 2010.

E. **Personal and Dependent Exemptions**

Read h/o 52-53 and do the handout problems.

F. **Personal Credits**

Child Credit and Dependent Care Credit

Read 203 through the first full sentence on 206 and h/o 55. Do the problem on 207.

Other credits: Read 207-208.

Credit for Hybrid Vehicles and Energy Saving Home Improvements

Buyers of hybrid vehicles can claim a tax credit of up to $3,000, depending on the model of the car. Taxpayers who install specific energy-efficient products in their home, such as windows, insulation, doors, roofs, and air conditioners, can receive a tax credit of up to $500 through 2007.
G. Business Expenses
Read 208-216, paying particular attention to “The 2% Haircut” on 210. Do the problems on 211 and problems 1 and 2 on 214.

H. Depreciation and Depletion
Read 216 to the top of 218 and 220. Skim h/o 56-57; you will not have to calculate depreciation. Read h/o 58 and do problems on 220-221. In problem 1, why is Karen permitted to deduct depreciation if the townhouse will appreciate in value over the years?

I. Basis
Read 221 (bottom) -226; omit the last two full paragraphs on 223 and omit from the fifth line of the first full paragraph on 225 to the end of that paragraph. Read h/o 59 and do the problems on 226-227. The solution to problem 2 is on h/o 60.

J. Sales and Dispositions of Property
Read 227-231; omit: (a) all text after the first seven lines in the last paragraph on 228 and at the top of 229, and (b) the last two full paragraphs on 230. Do problem 3 on h/o 51.

K. Losses
Read 232-236, but omit vacation homes on 235. Do problem 1 on 236.

L. Capital Gains and Losses
Read 237-239, up to ¶ 3,700, and h/o 61. The preferential rates discussed on page 238 have been extended through 2010; note that there will be no tax on long-term capital gains for taxpayers below the 25% bracket in 2008 and 2009. Do problem 1 on 241.

M. Sale of a Sole Proprietorship
Read the last full paragraph on 209, skim 240, read h/o 62, look at problem 3 on 241 and the solution on h/o 63. I will discuss it in class.

N. Taxpaying Entities
Read 241-246. See h/o 64 for an example of the marriage penalty discussed on 242.

The kiddie tax is discussed in the last paragraph on 243. In 2006, Congress raised the age to children under 18. The Small Business Tax Relief Act of 2007 extends the kiddie tax to children who are 18 or who are full-time students over 17 but under age 24. The expanded rule, which becomes effective in 2008, applies only to children whose earned income does not exceed one-half of the amount of their support. Children subject to the kiddie tax will not be able to take advantage of the preferential long-term capital gains rates discussed on casebook page 238. In other words, the capital gains rate for these children will be 15%, regardless of their tax bracket. They will not be able to take advantage of the zero capital gains tax rate for taxpayers in the 10 or 15% brackets.

The income tax rate for trusts discussed at the bottom of 244 are on h/o 43.

O. Assignment of Income
Read 246-247, h/o 65, and do the problems on 247-248.
P. Taxation of Investments

Read 248-256. Omit the following: (1) the computation of the exclusion ratio at the top of 249; (2) the first paragraph on page 250; (3) “Bond Premium” at the bottom of 251-252, and (4) the first two full paragraphs on 254.

To calculate the exclusion ratio of an annuity discussed at 249-250, divide the cost of the annuity by the number of annual payments that will be made. In Bella’s case on 249, she will exclude $10,000 from each $12,000 annual payment ($100,000 cost of the annuity ÷ 10 year life expectancy).

Review ¶ 1,260 on page 40-41 for zero coupon bonds.

Do the problems on 256. For problem 2, only consider the tax consequences of your investments. Does it make a difference if are selecting mutual funds for your personal account or your IRA or 401(k)?

Q. Accounting

Read 257 to the top of 259; do problem 1 on 261.

R. Alternative Minimum Tax

Read 262-263; ignore the computation, but note the deductions listed in the third paragraph that are not deductible for AMT purposes. Read h/o 66-69.