Subject code: FIN 1114

Date: May 14, 2016

Room: 2C323

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Major: ACC 3

Homework Chapter 6

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Discussion Questions:

1. Discuss the definition of trade or business. Why does it matter whether a taxpayer is classified as an employee or as self-employed?

Answer:

Neither the tax law nor the regulations directly define the term trade or business. However, the term is used quite frequently in various code sections, particularly when addressing the deductibility of expense. The general consensus of the relevant tax authority is that a “trade or business” is any activity that is engaged in for profit. The profit motive is necessary, and the activity should be engaged in with continuity and regularity. Thus sporadic activity or hobby activities are not considered trade or business activity.

The income from a sole proprietorship is netted with related ordinary and necessary business expenses to determine the increase (or decrease if a net loss results) in AGI.

(张雨薇，Viki Zhang , 5201434301, P.209 Paragraph 2, line 3. checked by Michelle Wang, 5201434319, on May 14, 2016)

2. Discuss the concepts of ordinary, necessary, and reasonable in relation to trade or business expense.

Answer:

For an expense to be deductible, it must be “ordinary” and “necessary.” For an expense to be ordinary, it must be customary or usual in the taxpayer’s particular business. The necessary criterion refers to an expense that is appropriate and helpful rather than one is essential to the taxpayer’s business. The courts have added a third standard:”reasonableness.” The courts have held that a trade or business expense must not only be ordinary and necessary but also reasonable in amount and reasonable in relation to its purpose.

(张雨薇，Viki Zhang , 5201434301, P.215 Paragraph 1, line 1. Checked by Michelle Wang, 5201434319, on May 14, 2016)

3. On what form is depreciation reported, and how does it relate to other forms such as Schedules C, E, F, and Form 2106?

Answer:

For each activity that uses depreciable assets, a taxpayer must complete Form 4562 to report depreciation.

The depreciation allowance (commonly called cost recovery) is the expense allowed for the wear or loss of usefulness of a business asset. Depreciation is a material noncash expense on the tax return that provides a large cash flow savings in terms of a tax reduction. Depreciation is allowed for every tangible asset (except land) used in a trade or business or for the production of income. Thus deprecation is calculated for Schedule C (trades or business- discussed in this chapter), Schedule E (rents and royalties-Chapter8), and Form 2106 (unreimbursed employee business expense-Chapter5).

(张雨薇，Viki Zhang , 5201434301, P.216, checked by Michelle Wang, 5201434319, on May 14, 2016)

4. On what type of property is depreciation allowed?

Answer:

Depreciation is allowed for every tangible asset (except land) used in a trade or business or for the production of income. For depreciation to be allowed, the property must be used in a business or held for the production of income (such as rental property) and not be inventory or investment property.

(王舒艺，Michelle Wang, 5201434319, P.216, checked by Viki Zhang, 5201434301, on May 14, 2016)

5. Discuss the word basis in relation to the financial accounting term book value. What is meant by the term adjusted basis?

Answer:

Basis is a concept similar to book value on a financial accounting balance sheet. Typically the depreciable basis of property is its initial cost.

Adjusted basis is the cost basis less any accumulated depreciation.
(王舒艺，Michelle Wang, 5201434319, P.216-217, checked by Viki Zhang, 5201434301, on May 14, 2016)

6. Discuss the difference between personal property and real property. Give examples of each.

Answer:

Personal property includes equipment, furniture, and fixtures or anything else that is not classified as real property. Real property consists of land and buildings as well as any other structural components attached to land. Personal properties usually have shorter useful lives, and real properties have longer.
(王舒艺，Michelle Wang, 5201434319, P.218, checked by Viki Zhang, 5201434301, on May 14, 2016)

7. What is a depreciation convention? What conventions are available under MACRS?

Answer:

A depreciation convention is a concept which is used to determine the amount of a partial year allowed in the depreciation calculation.

Available conventions include the half-year convention, the mid-quarter convention, and the mid-month convention.
(金雅馨，Samantha Jin, 5201434317, P.218, checked by Anny Xie, 5201434325, on May 14, 2016)

8. When calculating depreciation for personal property (assuming the half-year convention) using the IRS depreciation tables, does the taxpayer need to multiply the first year table depreciation percentage by one-half? What about in the year of disposal, assuming the property is disposed of prior to the end of its recovery period?

Answer:

The half-year convention for the first year is built into the depreciation tables issued by the IRS.

In the year of disposal, the table percentage must be multiplied by 0.5 for the half-year convention and by the appropriated months for mid-quarter and mid-month conventions.
(金雅馨，Samantha Jin, 5201434317, P.218-220, checked by Anny Xie, 5201434325, on May 14, 2016)

9. Discuss the concept of electing § 179 expense. Does the election allow a larger expense deduction in the year of asset acquisition?

Answer:

The taxpayer can elect to expense a certain portion of personal property purchased during the year (real property is excluded).

The maximum Section 179 for 2013 is $500,000. The § 179 deduction is designed to benefit small business by permitting them to expense the cost of the assets in the year of purchase rather than over time. The expense is allowed in full only if the total of personal property purchases is less than $2,000,000 in 2013 in aggregate cost. The expense election is phased out dollar-for-dollar for purchases in excess of $2,000,000. Thus the expense election is completely eliminated when asset purchases reach $2,500,000($2,000,000+500,000)

(谢诗怡，Anny Xie, 5201434325, P.222, checked by Samantha Jin, 5201434317, on May 14, 2016)

10. Discuss the concept of listed property.

Answer:

Listed property consists of the following:

- Any passenger automobile.
- Any other property used as a means of transportation (not include are vehicles that constitute a trade or business, such as taxis).
- Any property of a type generally used for entertainment, recreation, or amusement (such as a boat).
- Any computer or peripheral equipment.
- Any cellular telephone or other telecommunications equipment.

(谢诗怡，Anny Xie, 5201434325, P.224, checked by Samantha Jin, 5201434317, on May 14, 2016)

11. Distinguish between travel and transportation expenses.

Answer:

Travel expenses are different from transportation expenses because travel involves an overnight stay for business purposes. The basic travel requirement is that the trip requires sleep or rest.

(谢诗怡，Anny Xie, 5201434325, P.232, checked by Samantha Jin, 5201434317, on May 14, 2016)

12. When can a taxpayer use the standard mileage rate? Is the standard mileage rate better than actual auto costs?

Answer:

A taxpayer can use the standard mileage rate if

- The taxpayer owns the vehicle and uses the standard mileage rate for the first year it was placed in service.
- The taxpayer leases the auto and uses the standard mileage for the entire lease period.

No, it isn’t. Because the standard mileage rate cannot be used in the following instances:

- The auto has claimed depreciation (other than straight-line), § 179, or bonus depreciation.
- The auto is for hire (taxis).
- The taxpayer operates five or more cars simultaneously in business operations.

(陈海培，Linda Chen，5201434316，P.231, checked by Carina Xie, 5201434340, on May 14, 2016)

13. Discuss the limits on meals and entertainment. Are meals and entertainment expenses always limited to 50%?

Answer:

In general, any business meals and entertainment expenditures are limited to 50% of the amount incurred. The 50% limit pertains to any expense for food or beverage and any expense with respect to an activity that is generally considered to constitute entertainment, amusement, or recreation. To qualify for any deduction, meals and entertainment expenses must be both ordinary and necessary business expenses as well as be either "directly related" to or "associated with 'business.'" Directly related or associated with business primarily means that the activity took place in a business setting or the entertainment directly preceded or followed business discussions.

(陈海培，Linda Chen，5201434316，P.234, checked by Carina Xie, 5201434340, on May 14, 2016)

14. Discuss the limits on home office expense deductibility.

Answer:

Home office expenses that are not otherwise deductible (such as insurance, utilities, and depreciation) are limited to the gross income from the business use of the home. Gross income is first reduced by the amount of regular trade or business expenses (non-home related) and home office expenses that would be deductible in any event (mortgage interest and property taxes). If any positive income remains, the business use portions of insurance, utilities, and depreciation (note that depreciation is late) can be deducted. Even though one-half of the utilities, insurance, repairs, and depreciation are for the exclusive use of the home office, they are limited to $1,500. The excess is indefinitely carried over (assuming continued home office use) to the following tax year and deducted, subject to the limit in that year.

(陈海培，Linda Chen，5201434316，P.236, checked by Carina Xie, 5201434340, on May 14, 2016)

15. Why were the hobby loss rules established? What factors determine whether an activity is a trade or business or a hobby? Is any one factor controlling?

Answer:

1) To limit deductible losses from activities that are primarily for personal pleasure instead of a trade or business, Congress established the hobby loss rules.

2) Nine factors are used in the hobby determination.

a. Manner in which the taxpayer carries on the activity.
b. Expertise of the taxpayer or his or her advisers.
c. Time and effort expended by the taxpayer in carrying on the activity.
d. Expectations that assets used in the activity can appreciate in value
e. Success of the taxpayer in carrying on other similar or dissimilar activities.
f. Taxpayer's history of income or losses with respect to the activity.
g. Amount of occasional profits, if any, that are earned.

h. Taxpayer's financial status.
i. Elements of personal pleasure or recreation.

3) No, it isn’t. The regulations note that taxpayers are to take all of the facts and circumstances into account and that no one factor is controlling in the hobby determination.
(谢雨琪,Carina Xie, 5201434340, P.241, checked by Linda Chen, 5201434316, on May 14, 2016)

16. What are the two components of the self-employment tax? Is either component limited?

Answer:
1) Self-employment tax consists of two parts: (1) the social security tax (2) the Medicare tax.
2) The tax base for the social security tax is limited. The tax base for the Medicare tax, on the other hand, is not limited.
(谢雨琪,Carina Xie, 5201434340, P.242-243, checked by Linda Chen, 5201434316, on May 14, 2016)

Questions:

Professor Dave Jaye, please further explain questions

a) P.257. Question 3. (Viki Zhang)
b) P.261. Question 30 & P.262. Question 35. (Samantha Jin)

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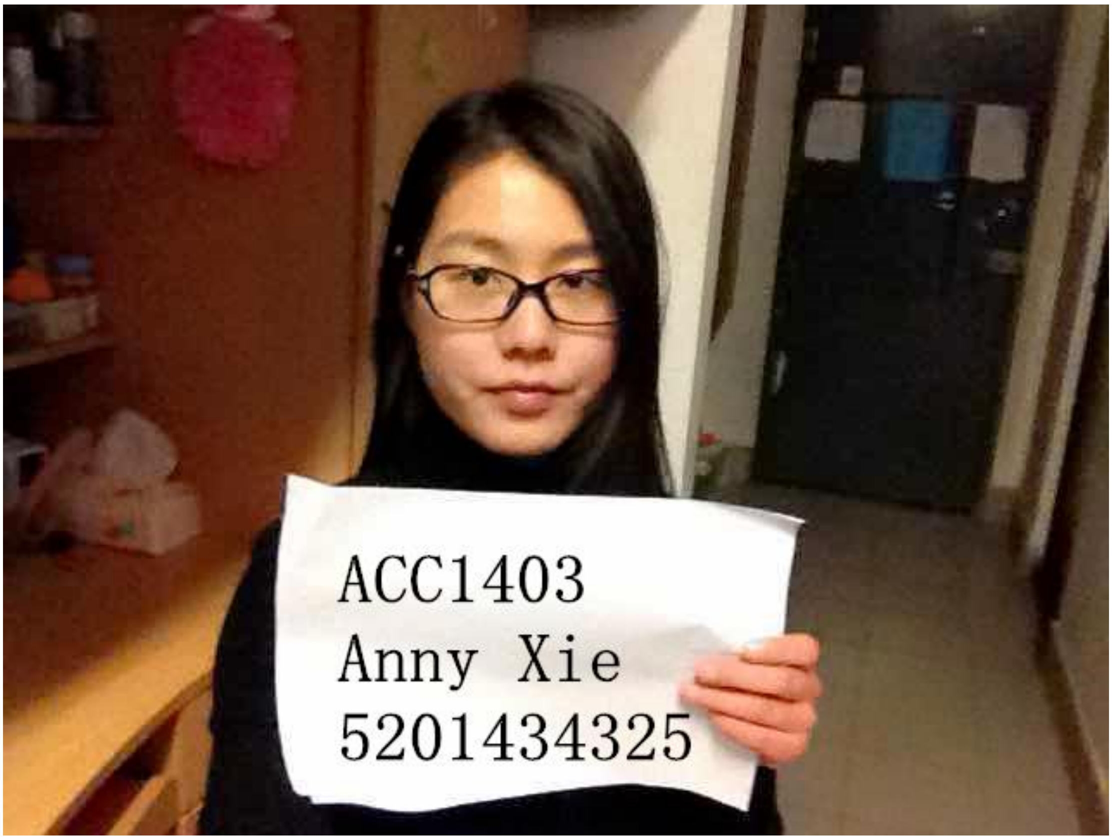

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