



51A Middle Street Newburyport MA 01950  
Phone: 800-588-7039 Fax: 877-902-4284  
[contact@bhfe.com](mailto:contact@bhfe.com) [www.bhfe.com](http://www.bhfe.com)

## Course Information

---

**Course Title:** *Tax Guide to Business Entities #490319*

**Recommended CPE credit hours for this course**

In accordance with the standards of the National Registry of CPE Sponsors and the IRS, CPE credits have been granted based on a 50-minute hour.

**CPA 3.5** (All states)

National Registry of CPE Sponsors ID Number: 107615.

Sponsor numbers for states requiring sponsor registration:

Florida Division of Certified Public Accountancy: 4761 (Ethics #11467)

Hawaii Board of Public Accountancy: 14003

New York State Board of Accountancy: 002146

Ohio State Board of Accountancy: M0021

Pennsylvania Board of Accountancy: PX178025

Texas State Board of Accountancy: 009349

**EA/OTRP 3** (All States) IRS: Qualified Sponsor number: *FWKKO*.

IRS Course Number: FWKKO-T-00066-13-S

**CLU, ChFC Professional Recertification 3**

**Course Description**

This course describes and compares sole proprietorships, partnerships, limited liability companies, "C" corporations and "S" corporations. It examines their advantages and disadvantages, permitting the participant to properly select the right business entity for their tax and liability needs.

**Program Delivery Method:** Self-Study (NASBA QAS Self-Study/interactive)

**Subject Codes/Field of Study**

NASBA (CPA): Taxes.

IRS (EA, OTRP): Federal Tax Law.

NAPFA: Taxes

### **Course Level, Prerequisites, and Advance Preparation Requirements**

Program Level: NASBA/CPA, IRS: Overview.

This program is appropriate for professionals at all organizational levels.

Prerequisites: Basic familiarity with federal taxation

Advance Preparation: None

### **Course Content**

Publication/Revision Date: 3/15/2019.

Author: Danny Santucci, J.D.

Final exam (online): Twenty questions (multiple-choice).

### **Instructions for taking this course**

You must complete this course within one year of the date of purchase (if you do not complete the course within one year, contact us to determine whether an updated edition of the course is available, in which case we will provide you with a PDF of the updated course and the online exam at no charge).

A passing grade of at least 70% is required on the final exam for this course. You may retake the exam if you do not pass it on the first attempt (no charge).

Complete the course by following the learning objectives listed on the following page, studying the text, and studying the review questions at the end of each major section (or at the end of the course). Once you have completed studying the course and you are confident that the learning objectives have been met, answer the final exam questions (online).

### **Instructions for Taking the Final Exam Online**

- Login to your account online at [www.bhfe.com](http://www.bhfe.com).
- The exam may be started, stopped, then resumed at a later date.
- The exam is "open book," it is not timed, and it may be retaken if not passed on the first attempt (no charge).
- Results (correct, incorrect answers) and certificate appear immediately upon passing the exam.
- EA credits are reported weekly.

**Have a question?** Call us at 800-588-7039 or email us at [contact@bhfe.com](mailto:contact@bhfe.com).

# Learning Assignment & Objectives

---

As a result of studying the assigned materials, you should be able to meet the objectives listed below.

## **ASSIGNMENT**

At the start of the materials, participants should identify the following topics for study:

- \* Advantages and disadvantages of sole proprietorships
- \* Taxes for self-employed individuals
- \* Definition of partnership
- \* Partnership tax return & year taxable
- \* Contributed property, assets & services
- \* Sales & exchanges of partnership interests
- \* Limited liability companies
- \* C corporations & PSC corporations
- \* Inventories
- \* S corporations

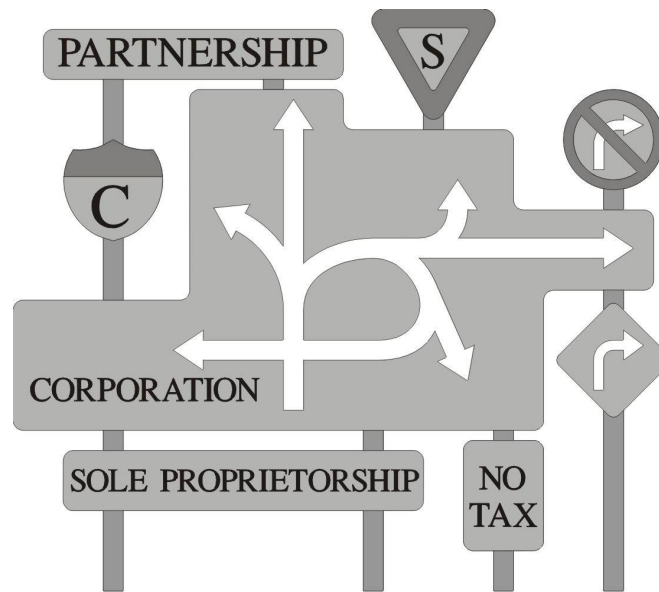
## **Learning Objectives**

After reading the materials, participants will be able to:

1. Cite the central differences among business entities and the advantages and disadvantages associated with basic business entity types.
2. Recognize the tax attributes sole proprietorships, partnerships, LLCs, S corporations and C corporations and how each entity can be used to enhance tax and financial purposes and objectives.
3. Specify the unique (e.g., self-employment) and general taxes applicable to particular entities and the tax forms that may be required.
4. Identify the basic deductions that are permissible for each entity type and the conditions under which they are allowed.
5. Determine the tax years, accounting methods and valuation methods that each entity type may use, and how the entities can be terminated.
6. Specify for different entity types the basis and the tax effect of sales, exchanges, transfers, contributions, and distributions.

## **Notice**

This course and test have been adapted from materials and information contained in the above text and any supplemental material provided. This course is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional advice and assumes no liability whatsoever in connection with its use. Since laws are constantly changing, and are subject to differing interpretations, we urge you to do additional research and consult appropriate experts before relying on the information contained in this course to render professional advice.



## Tax Guide to Business Entities

By

**Danny C. Santucci**

The author is not engaged by this text, any accompanying electronic media, or lecture in the rendering of legal, tax, accounting, or similar professional services. While the legal, tax, and accounting issues discussed in this material have been reviewed with sources believed to be reliable, concepts discussed can be affected by changes in the law or in the interpretation of such laws since this text was printed. The accuracy and completeness of this information and the author's opinions based thereon cannot be guaranteed. In addition, state or local tax laws and procedural rules may have a material impact on the general discussion. As a result, the strategies suggested may not be suitable for every individual. Before taking any action, all references and citations should be checked and updated accordingly.

*This publication is designed to provide accurate and authoritative information in regard to the subject matter covered. It is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional service. If legal advice or other expert advice is required, the services of a competent professional person should be sought.*

*—From a Declaration of Principles jointly adopted by a committee of the American Bar Association and a Committee of Publishers and Associations.*

**Copyright March, 2019**

**Danny Santucci**

# Table of Contents

<b>The Great Business Entity Tax Divide .....</b>	<b>1</b>
Passthrough Entities - 20% Deduction .....	1
Limitations.....	1
Deduction Amount .....	2
Qualified Trade Or Business.....	2
Corporations - 21% Rate .....	3
<b>Sole Proprietorship .....</b>	<b>3</b>
Introduction.....	3
Advantages .....	4
Disadvantages .....	4
Formation.....	4
Withdrawals.....	4
Schedule C .....	5
Not-For-Profit Activities - §183.....	5
Deduction & Loss Limit.....	5
Profit Presumption - 3/5 .....	6
Schedule C-EZ.....	6
Self-Employment Tax - SECA .....	6
Estimated Tax.....	7
Sale of a Business .....	7
Classification of Assets .....	8
Income Splitting .....	8
<b>Partnerships .....</b>	<b>8</b>
Definition of Partnership.....	9
Section 761(a).....	9
Co-tenancies.....	9
Partnership Agreement .....	9
Modifications .....	9
Partner’s Share of Tax Items.....	9
Limited Partners.....	10
Family Partnerships - §704(e).....	10
Advantages .....	11
Disadvantages .....	11
Partners Taxed as Individuals.....	11
Individual Returns & Schedules K-1.....	12
Separately Treated Items.....	12
Character of Items & Limitations.....	13
Deduction of Losses.....	13
Outside Basis Limitation - §704(d).....	13
Loss Ultimately Deductible .....	14

Effect of Losses on Outside Basis - §705 .....	14
Partnership Tax Return .....	16
Filing Requirements .....	16
Due Date of Return.....	16
Failure to File.....	17
Failure to Furnish Copies to Partners.....	17
Special Allocations - §704(b).....	17
Economic Effect.....	17
“Substantial Effect” .....	17
Year Taxable - §706(a).....	18
Limitation on Choice of Taxable Year .....	18
Closing of Partnership Year.....	18
Events That Terminate Partnership - §708(b) .....	19
Discontinuance of Business.....	19
Winding Up.....	19
Sale of 50% or More Interest - Repealed.....	19
Transactions between Partner & Partnership.....	20
Treating Partner as Stranger - §707(a).....	20
Guaranteed Payments - §707(c) .....	20
Certain Losses Disallowed - §707(b) .....	20
Two Partnerships.....	21
Sales at Gain .....	21
Contributions of Property - §721 .....	21
Contribution vs. Sale or Exchange .....	21
Disguised Sale - §707(a).....	21
Property Distribution to Contributing Partner - §737.....	22
Contributed Property Distribution to Another Partner - §704(c).....	22
Inside Basis of Contributed Assets - §723.....	22
Allocation of Precontribution Gain or Loss - §704(c) .....	23
Character of Subsequent Gain.....	23
Taint On Contribution- §724.....	23
Character of Subsequent Loss - §724(c).....	23
Contribution of Services .....	23
Basis of Partner’s Interest - Outside Basis .....	24
Original Basis - §722.....	24
Adjustments to Basis - §705(a) .....	24
Effect of Liabilities - §752.....	25
Sales & Exchanges of Partnership Interests .....	25
Hot Assets - §751 .....	25
Liabilities of Partnership - §752.....	26
Basis of Partnership Assets after Transfer of Interest.....	26
General Rule - §743(a) .....	26
Special Basis Adjustment - §§743, 754 .....	26
Partnership Distributions - §731 .....	26
Exceptions to General Rule .....	27
Partnership Liquidations .....	27
Types of Liquidating Distributions .....	27
Liquidating Distributions of Money - §736 .....	28
Section 736(a) Payments.....	28
Section 736(b) Payments.....	28

**Limited Liability Companies.....31**

Introduction ..... 31  
LLC Benefits ..... 31  
Advantages of LLCs over C Corporation..... 32  
    Double Tax ..... 32  
    Basis Adjustment ..... 32  
    Special Allocations..... 32  
    Contributions ..... 32  
    Liquidation..... 32  
    Unreasonable Compensation..... 33  
    Non-Tax Benefits..... 33  
Advantages of LLCs over S Corporations..... 33  
Advantages of LLCs over Limited Partnerships..... 34  
    Outside Basis & Debt Share Advantage ..... 34  
        Substantial Economic Effect Rules - §704(b) ..... 35  
        Discharge of Indebtedness Income..... 35  
Advantages of LLCs over General Partnerships..... 35  
Disadvantages..... 36

**Corporations .....37**

Corporation Defined ..... 37  
    Corporate Characteristics..... 37  
        Check-the-Box Regulations ..... 37  
C Corporations ..... 38  
    Advantages ..... 38  
    Disadvantages ..... 38  
PSC Corporations - §441, §448, §469..... 38  
    Testing Period - §441 ..... 39  
    Personal Services - §441..... 39  
    Principal Activity & Substantial Performance - §441 ..... 39  
    Employee-Owner - §441..... 40  
    Passive Loss Limitations - §469(a)(2)..... 40  
    Qualified Personal Service Corporation - §448..... 40  
Incorporation - §351 ..... 41  
    Basic Requirements..... 41  
        Corporate Nonrecognition..... 41  
    Control..... 41  
    Property Basis - §362 ..... 42  
    Stock Basis ..... 42  
Section 1244 Stock ..... 42  
    Maximum Ordinary Loss ..... 43  
    Original Issuance..... 43  
        Distributed Stock..... 43  
    General Requirements ..... 43  
Start-Up Expenses - §195..... 43  
    Covered Expenses ..... 44  
        Amortization ..... 44  
Organizational Expenses - §248 ..... 45  
    Definition..... 45  
    Stock Issuance & Syndication Expenses ..... 45

Amortization .....	45
Corporate Income Tax Rates .....	46
Tax Tables .....	46
Current Rate - 21% .....	46
Tax Return & Filing .....	46
Alternative Minimum Tax Repealed.....	47
Capital Gains & Losses - §1212 .....	47
Net Capital Loss Carryovers .....	47
Dividends Received Deduction - §243.....	48
Dividends from Domestic Corporations .....	48
65% Exception .....	48
Charitable Contributions - §170 .....	50
Limitation .....	50
Personal Holding Companies - §541.....	51
Penalty Tax .....	51
Accumulated Earnings Tax Trap .....	51
Computation.....	51
Accumulated Earnings Credit .....	52
Accounting Periods & Methods.....	52
Accounting Periods .....	52
Accounting Methods .....	53
Methods Available .....	53
Inventories - §446.....	53
Identification Methods.....	54
Specific Identification Method.....	54
FIFO Method .....	54
LIFO Method .....	54
Valuation Methods .....	55
Cost Method.....	55
Uniform Capitalization Rules - §263A.....	55
Lower of Cost or Market Method.....	56
Corporate Liquidations & Distributions.....	56

**S Corporations .....57**

Introduction .....	57
Advantages .....	57
Disadvantages .....	58
Becoming an S Corporation .....	59
S Corporation Status.....	59
Number of Shareholders .....	59
One Class of Stock .....	60
Domestic Corporation.....	60
Election Requirement .....	60
Making the Election .....	60
Form 2553 .....	60
S Corporation Termination.....	61
Ceasing to Qualify.....	61
Passive Income - §1362.....	61
Taxation of S Corporations .....	62
Built-In Gain - §1374 .....	62



Taxable Year.....	63
Fringe Benefits .....	63
Answers to Review Questions: page 66	
Glossary and Index: page 73	

### **Learning Objectives**

After reading the materials, participants will be able to:

1. Cite the central differences among business entities and the advantages and disadvantages associated with basic business entity types.
2. Recognize the tax attributes sole proprietorships, partnerships, LLCs, S corporations and C corporations and how each entity can be used to enhance tax and financial purposes and objectives.
3. Specify the unique (e.g., self-employment) and general taxes applicable to particular entities and the tax forms that may be required.
4. Identify the basic deductions that are permissible for each entity type and the conditions under which they are allowed.
5. Determine the tax years, accounting methods and valuation methods that each entity type may use, and how the entities can be terminated.
6. Specify for different entity types the basis and the tax effect of sales, exchanges, transfers, contributions, and distributions.