Appendix B

Tax Terms Glossary

§83(b) election a special tax election that employees who receive restricted stock or other property with ownership restrictions can make to accelerate income recognition from the normal date when restrictions lapse to the date when the restricted stock or other property is granted. The election also accelerates the employer's compensation deduction related to the restricted stock or other property.

§1231 assets depreciable or real property used in a taxpayer's trade or business owned for more than one year.

§1231 look-back rule a tax rule requiring taxpayers to treat current year net §1231 gains as ordinary income when the taxpayer has deducted a §1231 loss as an ordinary loss in the five years preceding the current tax year.

§1245 property tangible personal property and intangible property subject to cost recovery deductions.

§1250 property real property subject to cost recovery deductions.

§162(m) limitation the $1 million deduction limit on nonperformance based salary paid to certain key executives.

§179 election an incentive for small businesses that allows them to immediately expense a certain amount of tangible personal property placed in service during the year.

§197 purchased intangibles intangible assets that are purchased that must be amortized over 180 months regardless of their actual useful lives.

§263A Cost (or UNICAP) certain book expenses that must be capitalized into inventory for tax purposes.

§291 depreciation recapture the portion of a corporate taxpayer's gain on real property that is converted from §1231 gain to ordinary income.

§338 election an election by a corporate buyer of 80-percent-or-more of a corporation's stock to treat the acquisition as an asset acquisition and not a stock acquisition.

§338(h)(10) election a joint election by the corporate buyer and corporate seller of the stock of a subsidiary of the seller to treat the acquisition as a sale of the subsidiary's assets by the seller to the buyer.

§481 adjustment a change to taxable income associated with a change in accounting methods.

§7520 rate an interest rate set at 120 percent of the applicable federal midterm rate (published monthly by the Treasury) and used to calculate the value of temporal interests.

12-month rule regulation that allows prepaid business expenses to be currently deducted when the contract does not extend beyond 12 months and the contract period does not extend beyond the end of the tax year following the year of the payment.

704(b) capital accounts partners' capital accounts maintained using the accounting rules prescribed in the Section 704(b) regulations. Under these rules, capital accounts reflect the fair market value of property contributed to and distributed property from partnerships.

A

Accelerated Cost Recovery System (ACRS) the depreciation system enacted by Congress in 1981 that is based on the concept of set recovery periods and accelerated depreciation methods.

Accounting method the procedure for determining the taxable year in which a business recognizes a particular item of income or deduction thereby dictating the timing of when a taxpayer reports income and deductions.

Accounting period a fixed period in which a business reports income and deductions, generally referred to as a tax year.

Accrual method a method of accounting that generally recognizes income in the period earned and recognizes deductions in the period that liabilities are incurred.

Accrued market discount a ratable amount of the market discount at the time of purchase (based on the number of days the bond is held over the number of days until maturity when the bond is purchased) that is treated as interest income when a bond with market discount is sold before it matures.

Accumulated adjustments account (AAA) an account that reflects the cumulative income or loss for the time the corporation has been an S corporation.

Accumulated earnings and profits undistributed earnings and profits from years prior to the current year.

Accumulated earnings tax a tax assessed on corporations that retain earnings without a business reason to do so.

Acquisition subsidiary a subsidiary used by the acquiring corporation in a triangular merger to acquire the target corporation.

Active participant in a rental activity an individual who owns at least 10% of a rental property and participates in the process of making management decisions, such as approving new tenants, deciding on rental terms, and approving repairs and capital expenditures.

Ad valorem tax a tax based on the value of property.

Adjusted basis *see* adjusted tax basis.

Adjusted current earnings (ACE) a version of a corporation's current year earnings that more closely represents a corporation's economic income for the year than do regular taxable income or alternative minimum taxable income.

Adjusted gross estate gross estate reduced by administrative expenses, debts of the decedent, and losses, and state death taxes.

Adjusted tax basis the taxpayer's acquisition basis (for example, cost) plus capital improvements less depreciation or amortization.

Adjusted taxable gifts cumulative taxable gifts from previous years other than gifts already included in the gross estate valued at date of gift values.

Aggregate approach a theory of taxing partnerships that ignores partnerships as entities and taxes partners as if they directly owned partnership net assets.

All-events test requires that income or expenses are recognized when (1) all events have occurred that determine or fix the right to receive the income or liability to make the payments and (2) the amount of the income or expense can be determined with reasonable accuracy.

Allocate as used in the sourcing rules, the process of associating a deduction with a specific item or items of gross income for purposes of computing foreign source taxable income.

Allocation the method of dividing or sourcing nonbusiness income to specific states.

Allowance method bad debt expense is based on an estimate of the amount of the bad debts in accounts receivable at year-end.

Alternative minimum tax a tax on a broader tax base than the base for the "regular" tax; the additional tax paid when the tentative minimum tax (based on the alternative minimum tax base) exceeds the regular tax (based on the regular tax base). The alternative minimum tax is designed to require taxpayers to pay some minimum level of tax even when they have low or no regular taxable income as a result of certain tax breaks in the tax code.

Alternative minimum tax adjustments adjustments (positive or negative) to regular taxable income to arrive at the alternative minimum tax base.

Alternative minimum tax base (AMT base) alternative minimum taxable income minus the alternative minimum tax exemption.

Alternative minimum tax exemption a deduction to determine the alternative minimum tax base that is phased out based on alternative minimum taxable income.

Alternative minimum tax system a secondary or parallel tax system calculated on an *alternative* tax base that more closely reflects economic income than the regular income tax base. The system was designed to ensure that taxpayers generating economic income pay some *minimum* amount of income tax each year.

Alternative valuation date the date nine months after the decedent's date of death.

Amortization the method of recovering the cost of intangible assets over a specific time period.

Amount realized the value of everything received by the seller in a transaction (cash, FMV of other property, and relief of liabilities) less selling costs.

Annual exclusion amount of gifts allowed to be made each year per donee (regardless of the number of donees) to prevent the taxation of relatively small gifts ($14,000 per donee per year in 2014).

Annualized income method a method for determining a corporation's required estimated tax payments when the taxpayer earns more income later in the year than earlier in the year. Requires corporations to base their first and second required estimated tax installments on their income from the first three months of the year, their third installment based on their taxable income from the first six months of the year, and the final installment based on their taxable income from the first nine months of the year.

Applicable tax rate the tax rate or rates used to measure a company's deferred tax asset or liability. In general, it is the enacted tax rate that is expected to apply to taxable income in the period in which the deferred tax asset or liability is expected to be recovered or settled. For U.S. tax purposes, the applicable tax rate is the regular tax rate.

Apportion as used in the sourcing rules, the process of calculating the amount of a deduction that is associated with a specific item or items of gross income for purposes of computing foreign source taxable income.

Apportionment the method of dividing business income of an interstate business among the states where nexus exists.

Arm's-length amount price in transactions among unrelated taxpayers, where each transacting party negotiates for his or her own benefit.

Arm's-length transaction transactions among unrelated taxpayers, where each transacting party negotiates for his or her own benefit.

Articles of incorporation a document, filed by a corporation's founders with the state describing the purpose, place of business, and other details of the corporation.

Articles of organization a document, filed by a limited liability company's founders with the state, describing the purpose, place of business, and other details of the company.

Asset and liability approach the approach taken by ASC Topic 740 that focuses on computing a company's current taxes payable (refundable) and deferred tax assets and liabilities on the balance sheet. The income tax provision recorded on the income statement is the amount needed to adjust the beginning of the year balance sheet amounts to the end of the year balance sheet amounts.

Assignment of income doctrine the judicial doctrine holding that earned income is taxed to the taxpayer providing the service, and that income from property is taxed to the individual who owns the property when the income accrues.

At-risk amount an investor's risk of loss in a worst-case scenario. In a partnership, an amount generally equal to a partner's tax basis exclusive of the partner's share of nonrecourse debt.

At-risk rules tax rules limiting losses flowing through to partners or S corporation shareholders to their at-risk amount.

B

Bargain element (of stock options) the difference between the fair market value of the employer's stock and the amount employees pay to acquire the employer's stock.

Beneficiary person for whom trust property is held and administered.

Bonus depreciation additional depreciation allowed in the acquisition year for new tangible personal property with a recovery period of 20 years or less.

Book equivalent of taxable income a company's pretax income from continuing operations adjusted for permanent differences.

Book or financial reporting income the income or loss corporations report on their financial statements using applicable financial accounting standards.

Book–tax difference a difference in the amount of an income item or deduction item taken into account for book purposes compared to the amount taken into account for the same item for tax purposes.

Boot property given or received in an otherwise nontaxable transaction such as a like-kind exchange that may trigger gain to a party to the transaction.

Branch an unincorporated division of a corporation.

Bright line tests technical rules found in the tax law that provide the taxpayer with objective tests to determine the tax consequences of a transaction.

Brother-sister controlled group a form of controlled group consisting of two or more corporations if five or fewer individuals collectively own more than 50 percent of the voting power or stock value of the corporation on the last day of the year.

Built-in gain the difference between the fair market value and tax basis of property owned by an entity when the fair market value exceeds the tax basis.

Built-in gains tax a tax levied on S corporations that were formerly C corporations. The tax applies to net unrealized built-in gains at the time the corporation converted from a C corporation to the extent the gains are recognized during the built-in gains tax recognition period. The applicable tax rate is 35 percent.

Built-in gains tax recognition period the first 5 years a corporation operates as an S corporation after converting from a C corporation for asset sales in 2011, 2012, and 2013 (first 7 years for asset sales in 2009 and 2010; first 10 years for assets sales in other years).

Built-in loss the difference between the fair market value and tax basis of property owned by an entity when the tax basis exceeds the fair market value.

Business activity a profit-motivated activity that requires a relatively high level of involvement or effort from the taxpayer to generate income.

Business income income derived from business activities.

Business purpose doctrine the judicial doctrine that allows the IRS to challenge and disallow business expenses for transactions with no underlying business motivation.

Business tax credits nonrefundable credits designed to provide incentives for taxpayers to hire certain types of individuals or to participate in certain business activities.

Bypass provision a provision in the will of a deceased spouse that transfers property to nonspousal beneficiaries to maximize the value of the decedent's unified credit.

Bypass trust a trust used in lieu of a bypass provision to transfer property to nonspousal beneficiaries to maximize the value of the unified credit of the first spouse to die.

C

C corporation a corporate taxpaying entity with income subject to taxation. Such a corporation is termed a "C" corporation because the corporation and its shareholders are subject to the provisions of subchapter C of the Internal Revenue Code.

Capital account an account reflecting a partner's share of the equity in a partnership. Capital accounts are maintained using tax accounting methods or other methods of accounting, including GAAP, at the discretion of the partnership.

Capital asset in general, an asset other than an asset used in a trade or business or an asset such as an account or note receivable acquired in a business from the sale of services or property.

Capital gain property any asset that would have generated a long-term capital gain if the taxpayer had sold the property for its fair market value.

Capital interest an economic right attached to a partnership interest giving a partner the right to receive cash or property in the event the partnership liquidates. A capital interest is synonymous with the liquidation value of a partnership interest.

Capital loss carryback the amount of a corporation's net capital loss from one year that it uses to offset net capital gains in any of the three preceding tax years.

Capital loss carryover the amount of a corporation's or an individual's net capital loss from one year that it may use to offset net capital gains in future years.

Capitalization recording an expenditure as an asset on the balance sheet rather than expensing it immediately.

Carryover basis the basis of an asset the transferee takes in property received in a nontaxable exchange. The basis of the asset carries over from the transferor to the transferee.

Cash method the method of accounting that recognizes income in the period in which cash, property, or services are received and recognizes deductions in the period paid.

Cash surrender value the amount, if any, the owner of a life insurance policy receives when the policy is cashed in before the death of the insured individual.

Cash tax rate the tax rate computed by dividing a company's taxes paid during the year by its pretax income from continuing operations.

Certificate of deposit an interest-bearing debt instrument offered by banks and savings and loans. Money removed from the CD before maturity is subject to a penalty.

Certificate of limited partnership a document limited partnerships must file with the state to be formerly recognized by the state. The document is similar to articles of incorporation or articles or organization.

Character of income determines the rate at which income will be taxed. Common income characters (or types of income) include tax-exempt, ordinary, and capital.

Charitable contribution deduction modified taxable income taxable income for purposes of determining the 10% of taxable income deduction limitation for corporate charitable contributions. Computed as taxable income before deducting (1) any charitable contributions, (2) the dividends received deduction, (3) net operating loss carrybacks, and (4) the domestic production activities deduction.

Combined controlled group a form of a controlled group consisting of three or more corporations each of which is a member of either a parent-subsidiary or brother-sister controlled group and one of the corporations is the parent in the parent-subsidiary controlled group and also is in a brother-sister controlled group.

Commercial domicile the state where a business is headquartered and directs operations; this location may be different from the place of incorporation.

Commercial traveler exception a statutory exception that exempts nonresidents from U.S. taxation of compensation from services if the individual is in the United States 90 days or less and earns compensation of $3,000 or less.

Common-law states the 41 states that have not adopted community property laws.

Community-property states nine states (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin) that automatically equally divide the ownership of property acquired by either spouse during a marriage.

Community property systems systems in which state laws dictate how the income and property is legally shared between a husband and a wife.

Complex trust a trust that is not required by the trust instrument to distribute income currently.

Conglomerate a group of corporations in different businesses under common ownership.

Consolidation the combining of the assets and liabilities of two or more corporations into a new entity.

Constructive dividend a payment made by a corporation to a shareholder that is recharacterized by the IRS or courts as a dividend even though it is not characterized as such by the corporation.

Constructive ownership rules that cause stock not owned by a taxpayer to be treated as owned by the taxpayer for purposes of meeting certain stock ownership tests.

Constructive receipt doctrine the judicial doctrine that provides that a taxpayer must recognize income when it is actually or constructively received. Constructive receipt is deemed to have occurred if the income has been credited to the taxpayer's account or if the income is unconditionally available to the taxpayer, the taxpayer is aware of the income's availability, and there are no restrictions on the taxpayer's control over the income.

Continuity of business enterprise (COBE) a judicial (now regulatory) requirement that the acquiring corporation continue the target corporation's historic business or continue to use a "significant" portion of the target corporation's historic business assets to be tax-deferred.

Continuity of interest (COI) a judicial (now regulatory) requirement that the transferors of stock in a reorganization collectively retain a continuing ownership (equity) interest in the target corporation's assets or historic business to be tax-deferred.

Contribution to capital a shareholder's or other person's contribution of cash or other property to a corporation without receipt of an additional equity interest in the corporation.

Controlled foreign corporation a foreign corporation that is more than 50 percent owned by U.S. shareholders.

Controlled group a group of corporations owned by the same individual shareholders; it can either be brother-sister corporations or parent-subsidiary corporations.

Corporation business entities recognized as separate entities from their owners under state law.

Corpus the principal or property transferred to fund a trust or accumulated in the trust.

Cost depletion the method of recovering the cost of a natural resource that allows a taxpayer to estimate or determine the number of units that remain in the resource at the beginning of the year and allocate a pro rata share of the remaining basis to each unit of the resource that is extracted or sold during the year.

Cost recovery the method by which a company expenses the cost of acquiring capital assets. Cost recovery can take the form of depreciation, amortization, or depletion.

Coupon rate the interest rate expressed as a percentage of the face value of the bond.

Covenant not to compete a contractual promise to refrain from conducting business or professional activities similar to those of another party.

Current earnings and profits a year-to-year calculation maintained by a corporation to determine if a distribution is a dividend. Earnings and profits is computed for the current year by adjusting taxable income to make it more closely resemble economic income.

Current gifts gifts completed during the calendar year that are not already exempted from the gift tax.

Current income tax expense or benefit the amount of taxes paid or payable (refundable) in the current year.

Current tax liability or asset the amount of taxes payable or refundable in the current year.

D

Debt basis the outstanding principal of direct loans from an S corporation shareholder to the S corporation. Once taxpayers deduct losses to the extent of their stock basis, they may deduct losses to the extent of their debt basis. When the debt basis has been reduced by losses, it is restored by income/gain allocations.

Deductible temporary differences book-tax differences that will result in tax deductible amounts in future years when the related deferred tax asset is recovered.

Deferral items, deferred income, or deferrals realized income that will be taxed as income in a subsequent year.

Deferral method recognizes income from advance payments for goods by the earlier of (1) when the business would recognize the income for tax purposes if it had not received the *advance* payment or (2) when it recognizes the income for financial reporting purposes.

Deferred like-kind exchange a like-kind exchange where the taxpayer transfers like-kind property before receiving the like-kind property in exchange. The property to be received must be identified within 45 days and received within 180 days of the transfer of the property given up.

Deferred tax asset the expected future tax benefit attributable to deductible temporary differences and carryforwards.

Deferred tax liability the expected future tax cost attributable to taxable temporary differences.

Defined benefit plan employer-provided qualified plans that spell out the specific benefit employees will receive on retirement.

Defined contribution plan employer-provided qualified plans that specify the maximum annual contributions employers and/or employees may contribute to the plan.

Definitely related deductions deductions that are associated with the creation of a specific item or items of gross income.

Depletion the cost recovery method to allocate the cost of natural resources as they are removed.

Depreciation the cost recovery method to allocate the cost of tangible personal and real property over a specific time period.

Depreciation recapture the conversion of §1231 gain into ordinary income on a sale (or exchange) based on the amount of accumulated depreciation on the property at the time of sale or exchange.

Direct conversion when a taxpayer receives noncash property as a replacement for property damaged or destroyed in an involuntary conversion rather than a cash payment.

Direct write-off method required method for deducting bad debts for tax purposes. Under this method, businesses deduct bad debt only when the debt becomes wholly or partially worthless.

Disproportionate distributions partnership distributions that change the partners' relative ownership of hot assets.

Disregarded entities unincorporated entities with one owner that are treated as flow-through entities for U.S. income tax purposes.

Dividends distributions to shareholders of money or property from the corporation's earnings and profits.

Dividends received deduction a corporate deduction for part or all of a dividend received from other taxable, domestic corporations.

Document perfection program a program under which all tax returns are checked for mathematical and tax calculation errors.

Domestic production activities deduction (DPAD) a deduction for businesses that manufacture goods in the United States.

Donee person receiving a gift.

Donor person making a gift.

Double taxation the tax burden when an entity's income is subject to two levels of tax. Income of C corporations is subject to double taxation. The first level of tax is at the corporate level and the second level of tax on corporate income occurs at the shareholder level. Income of flow-through entities is generally not subject to double taxation.

DRD modified taxable income taxable income for purposes of applying the taxable income limitation for the dividends received deduction. Computed as the dividend receiving corporation's taxable income before deducting the dividends received deduction, any net operating loss deduction, the domestic production activities deduction, and capital loss carrybacks.

E

Earnings and profits a measure of a corporation's earnings that is similar to its economic earnings. Corporate dividends are taxable to shareholders to the extent they come from earnings and profits.

Economic nexus the concept that businesses without a physical presence in the state may establish income tax nexus in the state through an economic presence there.

Enacted tax rate the statutory tax rate that will apply in the current or a future period.

Entity approach a theory of taxing partnerships that treats partnerships as entities separate from partners.

Estate fiduciary legal entity that comes into existence upon a person's death and is empowered by the probate court to gather and transfer the decedent's real and personal property.

Excess net passive income net passive investment income × passive investment income in excess of 25% of the S corporation's gross receipts divided by its passive investment income.

Excess net passive income tax a tax levied on an S corporation that has accumulated earnings and profits from years in which it operated as a C corporation if the corporation reports excess net passive income.

Exchanged basis the basis of an asset received in a nontaxable exchange. An exchanged basis is generally the basis of the asset given up in a nontaxable exchange. Exchanged basis may also be referred to as a *substituted basis.*

Executor the person who takes responsibility for collecting the assets of the decedent, paying the decedent's debts, and distributing the remaining assets to the rightful heirs.

Exemption equivalent the amount of cumulative taxable transfers a taxpayer can make without exceeding the unified credit.

Exercise date the date employees use their stock options to acquire employer stock at a discounted price.

Exercise price the price at which holders of stock options may purchase stock in the corporation issuing the option.

F

Family limited partnership a partnership designed to save estate taxes by dividing a family business into various ownership interests representing control of operations and future income and appreciation of the assets.

Favorable book-tax difference a book-tax difference that requires a subtraction from book income in determining taxable income.

Federal/state adjustments amounts added to or subtracted from federal taxable income when firms compute taxable income for a particular state.

Federal short-term interest rate the quarterly interest rate used to determine the interest charged for tax underpayments (federal short-term rate plus 3 percent).

Fiduciary a person or legal entity that takes possession of property for the benefit of beneficiaries.

Fiduciary duty a requirement that a fiduciary act in an objective and impartial manner and not favor one beneficiary over another.

FIFO *see* first-in, first-out (FIFO) method.

Fiscal year a year that ends on a day other than December 31.

First-in, first-out (FIFO) method an accounting method that values the cost of assets sold under the assumption that the assets are sold in the order purchased (i.e., first purchased, first sold).

Fixed and determinable, annual or periodic income U.S. source passive income earned by a nonresident.

Flat tax a tax in which a single tax rate is applied throughout the tax base.

Flexible spending account a plan that allows employees to contribute before-tax dollars that may be used for unreimbursed medical expenses or dependent care.

Flipping a term used to describe the real estate investment practice of acquiring a home, repairing or remodeling the home, and then immediately, or soon thereafter, selling it (presumably at a profit).

Floor limitation a minimum amount that an expenditure (or credit or other adjustment to taxable income) must meet before any amount is allowed.

Flow-through entities legal entities like partnerships, limited liability companies, and S corporations that do not pay income tax. Income and losses from flow-through entities are allocated to their owners.

Foreign joint venture a 50 percent or less owned foreign entity.

Foreign personal holding company income a category of foreign source passive income that includes interest, dividends, rents, royalties, and gains from sale of assets.

Foreign subsidiary a more than 50 percent owned foreign corporation.

Foreign tax credit a credit for income taxes paid to a foreign jurisdiction.

Foreign tax credit limitation the limit put on the use of creditable foreign taxes for the current year.

Form 1065 the form partnerships file annually with the IRS to report partnership ordinary income (loss) and separately stated items for the year.

Form 1120S the form S corporations file annually with the IRS to report S corporation ordinary income (loss) and separately stated items for the year.

Form 7004 the form C corporations, partnerships, and S corporations file to receive an automatic extension to file their annual tax return.

Forward triangular merger an acquisition in which the acquired (target) corporation merges into an acquisition subsidiary of the acquiring corporation, after which the acquired corporation becomes part of the acquisition subsidiary of the acquiring corporation.

FTC basket a category of income that requires a separate FTC limitation computation.

Full-inclusion method the method for accounting for advance payments for goods that requires that businesses immediately recognize advance payments as taxable income.

Full-month convention a convention that allows owners of intangibles to deduct an entire month's amortization in the month of purchase and month of disposition.

Functional currency the currency of the primary economic environment in which an entity operates (that is the currency of the jurisdiction in which an entity primarily generates and expends cash).

Future interest the right to receive property in the future.

G

GAAP capital accounts partners' capital accounts maintained using generally accepted accounting principals.

General category income foreign source income that is not considered passive category income for foreign tax credit purposes (generally income from an active trade or business).

General partnership a partnership with partners who all have unlimited liability with respect to the liabilities of the entity.

Generation-skipping tax (GST) supplemental transfer tax designed to prevent the avoidance of estate and gift taxes through transfers that skip a generation of recipients.

Gift a transfer of property where no, or inadequate, consideration is paid for the property.

Golsen rule the rule that states that the U.S. Tax Court will abide by the circuit court's rulings that has appellate jurisdiction for a case.

Goodwill the value of an acquired business in excess of the fair market value of identifiable assets.

Grantor person creating a trust.

Gross estate property owned by the decedent at death and certain property transfers taking effect at death.

Gross income realized income reduced for any excluded or deferred income.

Gross receipts (for purposes of net passive investment income tax calculation) the total amount of revenues (including passive investment income) received or accrued under the corporation's accounting method, not reduced by returns, allowances, cost of goods sold, or deductions. Gross receipts include net capital gains from the sales or exchanges of capital assets and gains from the sales or exchanges of stock or securities (losses do not offset gains).

Group-term life insurance term life insurance provided by an employer to a group of employees.

Guaranteed payments payments made to partners or LLC members that are guaranteed because they are not contingent on partnership profits or losses. They are economically similar to shareholder salary payments.

H

Half-year convention a depreciation convention that allows owners of tangible personal property to take one-half of a year's worth of depreciation in the year of purchase and in the year of disposition regardless of when the asset was actually placed in service or sold.

Heirs persons who inherit property from the deceased.

Hot assets unrealized receivables or inventory items defined in §751(a) that give rise to ordinary gains and losses. The exact definition of hot assets depends on whether it is in reference to dispositions of a partnership interest or distributions.

Hybrid entity an entity for which an election is available to choose the entity's tax status for U.S. tax purposes.

I

Impermissible accounting method an accounting method prohibited by tax laws.

Indirect conversion the receipt of money or other property as a replacement for property that was destroyed or damaged in an involuntary conversion.

Inheritance a transfer of property when the owner is deceased (the transfer is made by the decedent's estate).

Initial public offering the first sale of stock by a company to the public.

Inside tax basis the tax basis of an entity's assets and liabilities.

Installment sale a sale for which the taxpayer receives payment in more than one period.

Institutional shareholder an entity with large amounts to invest in corporate stock, such as investment companies, mutual funds, brokerages, insurance companies, pension funds, investment banks, and endowment funds.

Intangible assets assets that do not have physical characteristics. Examples include goodwill, covenants not to compete, organizational expenditures, and research and experimentation expenses.

Interstate commerce business conducted between parties in two or more states.

Intervivos transfers gifts made by a donor during his or her lifetime.

Inventory items (for sale of partnership interest purposes) classic inventory defined as property held for sale to customers in the ordinary course of business, but also assets that are not capital assets or §1231 assets, which would produce ordinary income if sold by the entity. There are actually two definitions of inventory items in §751. §751(a) inventory items are defined in §751(d) to include all inventory items. The §751(b) definition includes only substantially appreciated inventory.

Investment interest expense interest paid on borrowings or loans that are used to fund portfolio investments. Individuals are allowed an itemized deduction for qualified investment interest paid during the year.

Involuntary conversion a direct or indirect conversion of property through natural disaster, government condemnation, or accident that allows a taxpayer to defer realized gain if certain requirements are met.

J

Joint tenancy with the right of survivorship title to property that provides the co-owners with equal rights to it and that automatically transfers to the survivor at the death of a co-owner.

L

Last will and testament the document that directs the transfer of ownership of the decedent's assets to the heirs.

Least aggregate deferral an approach to determine a partnership's required year-end if a majority of the partners don't have the same year-end and if the principal partners don't have the same year-end. As the name implies, this approach minimizes the combined tax deferral of the partners.

Life estate the right to possess property and/or collect income from property for the duration of someone's life.

Life insurance trust a trust funded with an irrevocable transfer of a life insurance policy and that gives the trustee the power to re-designate beneficiaries.

LIFO last-in, first-out method; an accounting method that values the cost of assets sold under the assumption that assets are sold in the reverse order in which they are purchased (i.e., last purchased, first sold).

LIFO recapture amount the excess of a C corporation's inventory basis under the FIFO method in excess of the inventory basis under the LIFO method in its final tax year as a C corporation before it becomes an S corporation.

LIFO recapture tax a tax levied on a C corporation that elects to be taxed as an S corporation when it is using the LIFO method for accounting for inventories.

Like-kind exchange a nontaxable (or partially taxable) trade or exchange of assets that are similar or related in use.

Limited liability company (LLC) a type of flow-through entity for federal income tax purposes. By state law, the owners of the LLC have limited liability with respect to the entity's debts or liabilities. Limited liability companies are taxed as partnerships for federal income tax purposes.

Limited partnership a partnership with at least one general partner with unlimited liability for the entity's debts and at least one limited partner with liability limited to the limited partner's investment in the partnership.

Liquidating distributions a distribution that terminates an owner's interest in the entity.

Liquidation value the amount a partner would receive if the partnership were to sell all its assets, pay its debts, and distribute its remaining assets to the partners in exchange for their partnership interests.

Listed property business assets that are often used for personal purposes. Depreciation on listed property is limited to the business use portion of the asset.

Long-term capital gain property property that would generate long-term capital gain if it were sold. This includes capital assets held for more than a year.

Long-term capital gains or losses gains or losses from the sale of capital assets held for more than 12 months.

Luxury automobile an automobile on which the amount of annual depreciation expense is limited because the cost of the automobile exceeds a certain threshold. The definition excludes vehicles with gross vehicle weight exceeding 6,000 pounds.

M

M adjustments *see* Schedule M adjustments.

Majority interest taxable year the common tax year of a group of partners who jointly hold greater than 50% of the profits and capital interests in the partnership.

Marital deduction the deduction for transfers of qualified property to a spouse.

Medicare tax the Medical Health Insurance (MHI) tax. This tax helps pay medical costs for qualifying individuals. The Medicare tax rate for employees is 1.45% on salary or wages up to $200,000 ($125,000 for married filing separate; $250,000 of combined salary or wages for married filing joint) and is 2.35% on salary or wages in excess of $200,000 ($125,000 for married filing separate; $250,000 of combined salary or wages for married filing joint). For employers, the Medicare tax rate is 1.45% of employee salary or wages, regardless of the amount of salary or wages. Self-employed taxpayers pay both the employee and employer Medicare tax.

Merger the acquisition by one (acquiring) corporation of the assets and liabilities of another (target) corporation. No new entity is created in the transaction.

Mid-month convention a convention that allows owners of real property to take one-half of a month's depreciation during the month when the property was placed in service and in the month it was disposed of.

Mid-quarter convention a depreciation convention for tangible personal property that allows for one-half of a quarter's worth of depreciation in the quarter of purchase and in the quarter of disposition. This convention must be used when more than 40% of tangible personal property is placed into service in the fourth quarter of the tax year.

Minimum tax credit credit available in certain situations for the alternative minimum tax paid. The credit can be used only when the regular tax exceeds the tentative minimum tax.

Modified Accelerated Cost Recovery System (MACRS) the current tax depreciation system for tangible personal and real property. Depreciation under MACRS is calculated by finding the depreciation method, the recovery period, and the applicable convention.

N

Negative basis adjustment (for special basis adjustment purposes) the sum of the recognized loss and the amount of the basis increase made by an owner receiving the distribution.

Net long-term capital gain the net gain resulting when taxpayers combine long-term capital gains and losses for the year.

Net long-term capital loss the net loss resulting when taxpayers combine long-term capital gains and losses for the year.

Net operating loss (NOL) the excess of allowable deductions over gross income.

Net operating loss carryback the amount of a current year net operating loss that is carried back to offset income in a prior year.

Net operating loss carryover the amount of a current year net operating loss that is carried forward for up to 20 years to offset taxable income in those years.

Net passive investment income passive investment income less any expenses connected with producing it.

Net short-term capital gain the net gain resulting when taxpayers combine short-term capital gains and losses for the year.

Net short-term capital loss the net loss resulting when taxpayers combine short-term capital gains and losses for the year.

Net unearned income unearned income in excess of a specified threshold amount of a child under the age of 19 or under the age of 24 if a full-time student.

Net unrealized built-in gain the net gain (if any) an S corporation that was formerly a C corporation would recognize if it sold each asset at its fair market value. It is measured on the first day of the corporation's first year as an S corporation.

Nexus the connection between a business and a tax jurisdiction sufficient to subject the business to the tax jurisdiction's tax system. Also, the connection that is required to exist between a jurisdiction and a potential taxpayer such that the jurisdiction asserts the right to impose a tax.

Nonbusiness income all income except for business income—generally investment income and rental income.

Nondeductible terminable interests transfers of property interests to a spouse that do not qualify for a marital deduction, because the interest of the spouse terminates when some event occurs or after a specified amount of time and the property is then transferred to another person.

Nondomiciliary business a business operating in a state other than its commercial domicile.

Nonperformance based compensation compensation paid to an employee that does not depend on the employee's performance or the corporation's performance or success. It usually is straight salary.

Nonqualified deferred compensation compensation provided for under a nonqualified plan allowing employees to defer compensation to a future period.

Nonqualified stock option a type of stock option requiring employees to treat the bargain element from options exercised as ordinary income in the tax year options are exercised. Correspondingly, employers may deduct the bargain element as compensation expense in the tax year options are exercised.

Nonrecaptured net §1231 losses a net §1231 loss that is deducted as an ordinary loss in one year and has not caused subsequent §1231 gain to be taxed as ordinary income.

Nonrecognition provisions tax laws that allow taxpayers to permanently exclude income from taxation or to defer recognizing realized income until a subsequent period.

Nonrecognition transaction a transaction where at least a portion of the realized gain or loss is not currently recognized.

Nonrecourse debt debt for which no partner bears any economic risk of loss. Mortgages on real property are a common form of nonrecourse debt.

Nonresident alien an individual who does not meet the criteria to be treated as a resident for U.S. tax purposes.

Nonservice partner a partner who receives a partnership interest in exchange for property rather than services.

Nontaxable fringe benefit an employer provided benefit that may be excluded from an employee's income.

Not definitely related deductions deductions that are not associated with a specific item or items of gross income in computing the foreign tax credit limitation.

O

Operating distributions payments to the owners from an entity that represent a distribution of entity profits. Distributions generally fall into the category of operating distributions when the owners continue their interests in the entity after the distribution.

Ordinary asset an asset created or used in a taxpayer's trade or business (e.g., accounts receivable or inventory) that generates ordinary income (or loss) on disposition.

Ordinary business income (loss) a partnership's or S corporation's remaining income or loss after separately stated items are removed. It is also referred to as nonseparately stated income (loss).

Ordinary income property property that if sold would generate income taxed at ordinary rates.

Ordinary and necessary an expense that is normal or appropriate and that is helpful or conducive to the business activity.

Organization costs costs associated with legally forming a partnership (such as attorneys' and accountants' fees).

Organizational expenditures expenses that are (1) connected directly with the creation of a corporation or partnership, (2) chargeable to a capital account, and (3) generally amortized over 180 months (limited immediate expensing may be available).

Outbound transaction a transaction conducted outside the United States by a U.S. person that is subject to U.S. taxation.

Outside tax basis an investor's tax basis in the stock of a corporation or the interest in a partnership or LLC.

P

PAL an acronym for "passive activity loss." Losses allocated to partners who are not material participants in the partnership are passive activity losses.

Parent-subsidiary controlled group a form of controlled group consisting of one corporation that owns at least 80% of the voting power or stock value of another corporation on the last day of the year.

Partial liquidation a distribution made by a corporation to shareholders that results from a contraction of the corporation's activities.

Partnership agreement an agreement among the partners in a partnership stipulating the partners' rights and responsibilities in the partnership.

Partnership interest an intangible asset reflecting the economic rights a partner has with respect to a partnership including the right to receive assets in liquidation of the partnership called a capital interest and the right to be allocated profits and losses called a profits interest.

Passive activity an activity in which the taxpayer does not materially participate.

Passive activity income or loss income or loss from an activity in which the taxpayer does not materially participate.

Passive activity loss rules tax rules designed to limit taxpayers' ability to deduct losses from activities in which they don't materially participate against income from other sources.

Passive category income foreign source personal holding company income such as interest, dividends, rents, royalties, annuities, and gains from sale of certain assets that is combined in computing the FTC limitation.

Passive investment income (PII) royalties, rents, dividends, interest (including tax exempt interest), annuities, and gains from the sales or exchanges of stock or securities.

Passive investments direct or indirect investments (other than through a C corporation) in a trade or business or rental activity in which the taxpayer does not materially participate.

Payment liability liabilities of accrual method businesses for which economic performance occurs when the business actually *pays* the liability for, among others: worker's compensation; tort; breach of contract or violation of law; rebates and refunds; awards, prizes, and jackpots; insurance, warranties, and service contracts provided *to* the business; and taxes.

Percentage depletion a method of recovering the cost of a natural resource that allows a taxpayer to recover or expense an amount based on a statutorily determined percentage.

Permanent book-tax differences items of income or deductions for either book purposes or for tax purposes during the year but not both. Permanent differences do not reverse over time so over the long run the total amount of income or deduction for the item is different for book and tax purposes.

Permanent establishment generally, a fixed place of business through which an enterprise carries out its business. Examples include a place of management, a branch, an office, and a factory.

Permissible accounting method accounting method allowed under the tax law. Permissible accounting methods are adopted the first time a taxpayer uses the method on a tax return.

Person an individual, trust, estate, partnership, association, company, or corporation.

Personal expenses expenses incurred for personal motives. Personal expenses are not deductible for tax purposes.

Personal holding companies closely held corporations generating primarily investment income.

Personal holding company tax penalty tax on the undistributed income of a personal holding company.

Personal property all tangible property other than real property.

Positive basis adjustment (for special basis adjustment purposes) the sum of the gain recognized by the owners receiving distributed property and the amount of any required basis reduction.

Post-termination transition period (PTTP) the period that begins on the day after the last day of a corporation's last taxable year as an S corporation and generally ends on the later of (a) one year after the last S corporation day, or (b) the due date for filing the return for the last year as an S corporation (including extensions).

Present interest right to presently enjoy property or receive income from the property.

Principal partner a partner having a 5% interest or more in partnership capital or profits.

Private activity bond a bond issued by a municipality but proceeds of which are used to fund privately owned activity.

Probate the process in the probate court of gathering property possessed by or titled in the name of a decedent at the time of death, paying the debts of the decedent and transferring the ownership of any remaining property to the decedent's heirs.

Probate estate property possessed by or titled in the name of a decedent at the time of death.

Procedural regulations regulations that explain Treasury Department procedures as they relate to administering the Code.

Production of income a for-profit activity that doesn't rise to the level of a trade or business.

Profits interest an interest in a partnership giving a partner the right to share in future profits but not the right to share in the current value of a partnership's assets. Profits interests are generally not taxable in the year they are received.

Public Law 86-272 federal law passed by Congress that provides additional protection for sellers of tangible personal property against income tax nexus.

Publicly state traded corporations corporations whose stock is publicly traded on a stock exchange.

Q

Qualified moving expense reimbursement a nontaxable fringe benefit that allows employers to pay moving-related expenses on behalf of employees.

Qualified nonrecourse financing nonrecourse debt secured by real property from a commercial lender unrelated to the borrower.

Qualified production activities income (QPAI) the *net* income from selling or leasing property that was manufactured in the United States.

Qualified replacement property property acquired to replace property damaged or destroyed in an involuntary conversion. It must be of a similar or related use to the original property even if the replacement property is real property (rental real estate for rental real estate).

Qualified retirement plans employer-sponsored retirement plans that meet government-imposed funding and anti-discrimination requirements.

R

Real property land and structures permanently attached to land.

Real property tax a tax on the fair market value of land and structures permanently attached to land.

Realization gain or loss that results from an exchange of property rights in a transaction.

Realization principle the proposition that income only exists when there is a transaction with another party resulting in a measurable change in property rights.

Realized gain or loss the difference between the amount realized and the adjusted basis of an asset sold or otherwise disposed of.

Reasonable in amount an expenditure is reasonable when the amount paid is not extravagant nor exorbitant.

Recognition gain or loss included in the computation of taxable income.

Recourse debt debt held by a partnership for which at least one partner has economic risk of loss.

Recovery period a length of time prescribed by statute in which business property is depreciated or amortized.

Remainder the right to ownership of a property that transfers to a new owner, the remainderman, following a temporary interest.

Remainderman the person entitled to a remainder interest.

Reorganization a tax-deferred transaction (acquisition, disposition, recapitalization, or change of name or place of incorporation) that meets one of the seven statutory definitions found in §368(a)(1).

Research and experimentation costs expenses for research including costs of research laboratories (salaries, materials, and other related expenses). Taxpayers can elect to amortize research and development costs over not less than 60 months from the time benefits are first derived from the research.

Residence-based jurisdiction taxation of income based on the taxpayer's residence.

Resident alien an individual who is not a U.S. citizen but is treated as a resident for U.S. tax purposes.

Reverse hybrid entity a "check-the-box" entity owned by multiple persons for which corporation status is elected.

Reverse triangular merger an acquisition in which an acquisition subsidiary of the acquiring corporation merges into the acquired (target) corporation, after which the acquired corporation becomes a subsidiary of the acquiring corporation.

Reversion terms by which ownership of property returns to the original owner following a temporary interest.

S

S corporation a corporation under state law that has elected to be taxed under the rules provided in subchapter S of the Internal Revenue Code. Under subchapter S, an S corporation is taxed as a flow-through entity.

Sales tax a tax imposed on the retail sales of goods (plus certain services). Retailers are responsible for collecting and remitting the tax; typically sales tax is collected at the point of sale.

Schedule C a schedule on which a taxpayer reports the income and deductions for a sole-proprietorship.

Schedule K a schedule filed with a partnership's annual tax return listing its ordinary income (loss) and its separately stated items.

Schedule M adjustments book-tax differences that corporations report on the Schedule M-1 or M-3 of Form 1120 as adjustments to book income to reconcile to taxable income.

Schedule M-1 a schedule on Form 1120 that reconciles book income to taxable income before special deductions. Book-tax differences are reported in a general way.

Schedule M-3 a schedule on Form 1120 that reconciles book income to taxable income for corporations and partnerships with total assets of $10 million or more. The schedule M-3 includes much more detail than the Schedule M-1, including identifying whether each book-tax difference is a temporary difference or a permanent book-tax difference.

Security a financial instrument including an equity interest in business organizations and creditor interests such as savings accounts, notes, and bonds.

Self-employment taxes Social Security and Medicare taxes paid by the self-employed on a taxpayer's net earnings from self-employment. For self-employed taxpayers, the terms "self-employment tax" and "FICA tax" are synonymous.

Separate tax return a state tax return methodology requiring that each related entity with nexus files a separate tax return.

Separately stated items income, expenses, gains, losses, credits, and other items that are excluded from a partnership's or S corporation's operating income (loss) and disclosed to partners in a partnership or shareholders of an S corporation separately because their tax effects may be different for each partner or shareholder.

Serial gift transfer tax strategy that uses the annual exclusion to convert a potentially large taxable transfer into a tax-exempt transfer by dividing it into multiple intervivos gifts spread over several periods or donees.

Service partner partners who receive their partnership interest by contributing services rather than cash or property.

Single member LLC a limited liability company with only one member. Single member LLCs with individual owners are taxed as sole proprietorships and as disregarded entities otherwise.

Sole proprietorship a business entity that is not legally separate from the individual owner of the business. The income of a sole proprietorship is taxed and paid directly by the owner.

Solicitation selling activities or activities ancillary to selling that are protected under Public Law 86-272.

Source-based jurisdiction taxation of income based on where the income is earned.

Special allocations allocations of income, gain, expense, or loss, etc., that are allocated to the owners of an entity in a manner out of proportion with the owners' interests in the entity. Special allocations can be made by entities treated as partnerships for federal income tax purposes.

Special basis adjustment an optional (sometimes mandatory) election to adjust the entity asset bases as a result of an owner's disposition of an interest in the entity or of distributions from the entity to its owners.

Specific identification method an elective method for determining the cost of an asset sold. Under this method, the taxpayer specifically chooses the assets that are to be sold.

Split-gift election election that allows spouses to treat all gifts made in a year as if each spouse made one-half of each gift.

Spot rate the foreign currency exchange rate on a specific day.

Start-up costs expenses that would be classified as business expenses except that the expenses are incurred before the business begins. These costs are generally capitalized and amortized over 180 months, but limited immediate expensing may be available.

State tax a tax imposed by one of the 50 U.S. states.

Stock dividend a dividend made by a corporation of its own stock.

Stock-for-stock acquisition an exchange of solely voting stock by the acquiring corporation in exchange for stock of the target corporation, after which the acquiring corporation controls (owns 80-percent-or-more of) the target corporation. Often referred to as a "Type B reorganization."

Stock redemption a property distribution made to shareholders in return for some or all of their stock in the distributing corporation that is not in partial or complete liquidation of the corporation.

Stock split a stock redemption in which a corporation exchanges a ratio of shares of stock (e.g., 2 for 1) for each share held by the shareholder.

Strike price *see* exercise price.

Structural tax rate the tax rate computed by dividing a company's income tax provision adjusted for nonrecurring permanent differences by its pretax income from continuing operations.

Subchapter K the portion of the Internal Revenue Code dealing with partnerships tax law.

Subchapter S the portion of the Internal Revenue Code containing tax rules for S corporations and their shareholders.

Subpart F income income earned by a controlled foreign corporation that is not eligible for deferral from U.S. taxation.

Substantial basis reduction negative basis adjustment of more than $250,000 resulting from a distribution from an entity taxed as a partnership to its owners.

Substantial built-in loss exists when a partnership's adjusted basis in its property exceeds the property's fair market value by more than $250,000 when a transfer of an interest occurs.

Substantially appreciated inventory (for partnership disproportionate distributions purposes) inventory with a fair market value that exceeds its basis by more than 120%.

Substituted basis the transfer of the tax basis of stock or other property given up in an exchange to stock or other property received in return.

Syndication costs costs partnerships incur to promote the sale of partnership interests to the public. Syndication expenses must be capitalized and are not amortizable.

T

Tacks the adding on of the transferor's holding period of property to the transferee in a tax-deferred exchange.

Tax a payment required by a government that is unrelated to any specific benefit or service received from the government.

Tax accounting balance sheet a balance sheet that records a company's assets and liabilities at their tax bases instead of their financial accounting bases.

Tax base the item that is being taxed (e.g., purchase price of a good, taxable income, etc.).

Tax basis the amount of a taxpayer's unrecovered cost of or investment in an asset. *See also* adjusted tax basis.

Tax bracket a range of taxable income taxed at a specified rate.

Tax capital accounts partners' capital accounts initially determined using the tax basis of contributed property and maintained using tax accounting income and expense recognition principles.

Tax carryforwards tax deductions or credits that cannot be used on the current year tax return and that can be carried forward to reduce taxable income or taxes payable in a future year.

Tax contingency reserve a company's reserve for taxes it has not paid, but it may pay in the future, for uncertain tax positions taken on the current and prior year income tax returns.

Tax shelter an investment or other arrangement designed to produce tax benefits without any expectation of economic profits.

Tax year a fixed period in which a business reports income and deductions, generally referred to as an accounting period.

Taxable estate adjusted gross estate reduced by the marital deduction and the charitable deduction.

Taxable fringe benefit a noncash fringe benefit provided by employers to an employee that is included in taxable income (e.g., auto allowance or group-term life over $50,000).

Taxable gifts the amount left after adjusting current gifts for gift splitting, annual exclusions, the marital deduction, and the charitable deduction.

Taxable temporary differences book-tax differences that will result in taxable amounts in future years when the related deferred tax liability is settled.

Temporary book-tax differences book-tax differences that reverse over time such that, over the long-term, corporations recognize the same amount of income or deductions for the items on their financial statements as they recognize on their tax returns.

Tenancy by the entirety ownership by husband and wife similar to joint tenancy with right of survivorship.

Tenancy in common ownership in which owners hold divided rights to property and have the ability to transfer these rights during their life or upon their death.

Tentative minimum tax the tax on the AMT tax base under the alternative minimum tax system.

Terminable interest a right to property that terminates at a specified time or upon the occurrence of a specified event, such as a life estate.

Testamentary transfers transfers that take place upon the death of the donor.

Third-party intermediaries people or organizations that facilitate the transfer of property between taxpayers in a like-kind exchange. Typically, the intermediary receives the cash from selling the property received from the taxpayer and uses it to acquire like-kind property identified by the taxpayer.

Throwback rule the rule that sales into a state without nexus are included with sales from the state the property was shipped from.

Trade show rule a rule that permits businesses to have physical presence at conventions and trade shows, generally up to two weeks a year, without creating nexus.

Traditional 401(k) a popular type of defined contribution plan with before-tax employee and employer contributions and taxable distributions.

Transfer taxes taxes on the transfer of wealth from one taxpayer to another. The estate and gift taxes are two examples of transfer taxes.

Travel expenses expenditures incurred while "away from home overnight," including the cost of transportation, meals, lodging, and incidental expenses.

Triple i agreement a 10-year agreement filed with the IRS in which the taxpayer agrees to notify the IRS that he or she has acquired a prohibited interest after waiving the family attribution rules in a complete redemption.

Trust fiduciary entity created to hold and administer the property for other persons according to the terms of a trust instrument.

Trustee the person responsible for administering a trust.

U

Uncertain tax positions a tax return position for which a corporation does not have a high degree of certainty as to its tax consequences.

Unfavorable book-tax difference any book-tax difference that requires an add back to book income in computing taxable income. This type of adjustment is unfavorable because it increases taxable income relative to book income.

Unified credit amount of credit based on the exemption equivalent designed to prevent transfer taxation of smaller cumulative transfers.

Uniform cost capitalization rules (UNICAP rules) specify that inventories must be accounted for using full absorption rules to allocate the indirect costs of productive activities to inventory.

Unitary tax return a state tax return methodology requiring the activities of a group of related entities to be reported on a single tax return. The criteria for determining whether a group of entities must file a unitary tax return are functional integration, centralization of management, and economies of scale.

Unrealized receivables any rights to receive payment for (1) goods delivered, or to be delivered, or (2) services rendered, or to be rendered. Unrealized receivables also include other assets to the extent that they would produce ordinary income if sold for their fair market value.

Unrecaptured §1250 gain a gain from the sale of real estate held by a noncorporate taxpayer for more than one year in a trade or business or as rental property attributable to tax depreciation deducted at ordinary tax rates. This gain is taxable at a maximum 25% capital gains rate.

Unrecognized tax benefit a reserve for tax benefits related to a tax position for which the corporation does not have a high degree of certainty as to its sustainability on audit or in a court of law.

Use tax a tax imposed on the retail price of goods owned, possessed, or consumed within a state that were *not* purchased within the state.

V

Valuation allowance the portion of a deferred tax asset for which management determines it is more likely than not that a tax benefit will not be realized on a future tax return.

Vest to become legally entitled to receive a particular benefit without risk of forfeiture; to gain ownership.

Vesting date the date on which the taxpayer becomes legally entitled to receive a particular benefit without risk of forfeiture.

Vesting period period of employment over which employees earn the right to own and exercise stock options.

W

Willing-buyer, willing-seller rule the guideline for determining fair market value as "the price at which such property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell, and both have reasonable knowledge of the relevant facts."