

# NINJA NOTES

Financial Accounting & Reporting 2026



## Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the FAR Section of the Exam:

Area I	Financial Reporting	30% - 40%
Area II	Select Balance Sheet Accounts	30% - 40%
Area III	Select Transactions	25% - 35%

# Skill Allocation

Remembering and Understanding	5% - 15%
Application	45% - 55%
Analysis	35% - 45%
Evaluation	0% - 0%

# Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
FAR – Core	50%	50%

# Section Time and Question Type

The table below presents the design of the Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
FAR – Core	4 Hours	50	7

# Content

- FAR-1 Fundamentals of Accounting & Conceptual Framework
- FAR-2 Income Statement and Statement of Comprehensive Income
- FAR-3 Balance Sheet
- FAR-4 Statement of Cashflows
- FAR-5 Statement of Changes in Stockholders' Equity
- FAR-6 Notes to Accounts
- FAR-7 SEC Reporting Requirements
- FAR-8 Earnings Per Share
- FAR-9 Ratio Analysis
- FAR-10 Revenue & Expense
- FAR-11 Foreign Currency Transactions
- FAR-12 Accounting Changes, Error Correction & Fair Value Measurement
- FAR-13 Cash and Cash Equivalents & Bank Reconciliation Statement (BRS)
- FAR-14 Accounts Receivable & Notes Receivable
- FAR-15 Inventory
- FAR-16 Property Plant & Equipment (PPE)
- FAR-17 Intangibles
- FAR-18 Investment in Equity Securities
- FAR-19 Investment in Debt Securities
- FAR-20 Business Consolidation and Combination
- FAR-21 Current Liabilities & Contingencies
- FAR-22 Bonds and Troubled Debt Restructuring
- FAR-23 Income & Deferred Taxes

FAR-24 Lease Accounting - Lessee

FAR-25 Equity

FAR-26 Partnership Accounting

FAR-27 Special Purpose Frameworks

FAR-28 Not-for-Profit Accounting

FAR-29 Governmental Accounting

# NINJA NOTES

Financial Accounting & Reporting 2026



**Fundamentals of Accounting & Conceptual Framework**

## **Copyright & Disclaimer**

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

# Fundamentals of Accounting & Conceptual Framework

## Accounting Universe

- Accounting Principles → Accounting Standards → Accounting Books → Financial Statements

## Accounting Principles

- Accrual Principle and Matching Principle
  - Expenses are recorded in the period in which the benefit is received, regardless of when the cash is paid out.
  - Income is recognized when the service or product is provided, irrespective of when the cash is received.
- Monetary Principle
  - Only events that can be denoted in monetary value should be recorded in the financial statements.
- Periodicity Principle
  - Periodicity Principle requires that an entity's life be divided into artificial periods for reporting purposes, such as months, quarters, or years.
- Consistency Principle
  - Consistency Principle mandates the consistent application of accounting policies and principles from one period to the next.
- Conservatism Principle
  - According to Conservatism or the Prudence Principle, all estimated losses should be recorded before they occur, while estimated gains should not be recorded.
- Going Concern Principle
  - Going Concern Principle assumes that a business will continue to operate indefinitely, and assets are not intended to be liquidated in the near term.

## Accounting Standards

- Rules and guidelines set by regulatory bodies to standardize the way financial transactions are recorded and reported.
- Types of Accounting Standards
  - US Generally Accepted Accounting Principles (US GAAP)
  - International Financial Reporting Standards (IFRS)

## Accounting Books

- Journals
- Ledgers
- Trial Balance

## Financial Statements

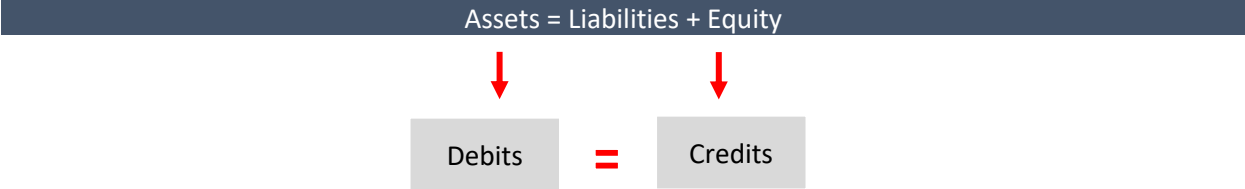
- Income Statement
- Statement of Comprehensive Income
- Balance Sheet
- Cash Flow Statement
- Statement of Changes in Equity
- Notes to Accounts

## Accounting Process

- Journals → Ledger → Unadjusted Trial Balance → Record Adjusting Journal Entries → Adjusted Trial Balance → Financial Statements

# Double Entry Accounting System

- Double-Entry Accounting System requires that for every Financial Transaction, there must be an equal and opposite effect in at least two different accounts.



- In the Double-Entry System, transactions are recorded as Debits and Credits.

Account Type	Balance Type	Increase	Decrease
Assets	Debit	Debit	Credit
Liabilities & Equity	Credit	Credit	Debit
Income & Gains	Credit	Credit	Debit
Expenses & Losses	Debit	Debit	Credit

# NINJA NOTES

Auditing & Attestation 2026



## Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the AUD section of the CPA Exam:

Area I	Ethics, Professional Responsibilities and General Principle	15% - 25%
Area II	Assessing Risk and Developing a Planned Response	25% - 35%
Area III	Performing Further Procedures and Obtaining Evidence	30% - 40%
Area IV	Forming Conclusions and Reporting	10% - 20%

## Skill Allocation

Remembering and Understanding	30% - 40%
Application	30% - 40%
Analysis	15% - 20%
Evaluation	5% - 15%

## Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
AUD – Core	50%	50%

## Section Time and Question Type

The table below presents the design of the CPA Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
AUD – Core	4 Hours	78	7

# Content

AUD-1 Ethics & Professional Responsibilities

AUD-2 Engagement Acceptance

AUD-3 Audit Planning & Supervision

AUD-4 Internal Control

AUD-5 Substantive Procedures & Audit Completion

AUD-6 Audit Reports for Non-Issuers and Issuers

AUD-7 Post-Audit Responsibilities & Audit Quality Control

AUD-8 Audit Sampling

AUD-9 Accounting and Review Services (SSARS)

AUD-10 Attestation Engagements (SSAE)

AUD-11 Audit of Governmental Organizations and Single Audits

AUD-12 Information Technology and Auditing

AUD-13 Audit Data Analytics

AUD-14 Economics

# NINJA NOTES

Auditing & Attestation 2026



**Ethics & Professional Responsibilities**

## **Copyright & Disclaimer**

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

# Ethics & Professional Responsibilities

## Standards for Different Types of Engagement

Engagement Type	Standard	Code of Conduct
Audit of Non-Issuers	<ul style="list-style-type: none"> <li>Generally Accepted Auditing Standards (GAAS) issued by AICPA</li> </ul>	<ul style="list-style-type: none"> <li>AICPA Code of Professional Conduct</li> </ul>
Audit of Issuers	<ul style="list-style-type: none"> <li>PCAOB Auditing Standards + GAAS</li> </ul>	<ul style="list-style-type: none"> <li>AICPA Code of Professional Conduct</li> <li>Securities Exchange Commission</li> <li>Sarbanes-Oxley Act</li> </ul>
International Audits	<ul style="list-style-type: none"> <li>International Standards on Auditing (ISA)</li> </ul>	<ul style="list-style-type: none"> <li>IESBA Code of Conduct</li> </ul>
Governmental Audits	<ul style="list-style-type: none"> <li>Generally Accepted Government Auditing Standards (GAGAS)</li> </ul>	<ul style="list-style-type: none"> <li>AICPA Code of Professional Conduct</li> </ul>
Attestation Engagements	<ul style="list-style-type: none"> <li>Statements on Standards for Attestation Engagements (SSAEs)</li> </ul>	<ul style="list-style-type: none"> <li>AICPA Code of Professional Conduct</li> </ul>
Accounting & Review Services	<ul style="list-style-type: none"> <li>Statements on Standards for Accounting and Review Services (SSARs)</li> </ul>	<ul style="list-style-type: none"> <li>AICPA Code of Professional Conduct</li> </ul>

# AICPA Code of Professional Conduct

- Sets the ethical standards for CPAs and provides a framework for resolving ethical dilemmas.
- Designed to ensure that CPAs carry out their duties with professionalism, integrity, objectivity, and in the best interests of the public.

Part 0 - Principles
Part 1 - Members in Public Practice
Part 2 - Members in Business
Part 3 - All Other Members

- Rules that apply to each member are as follows:

Part 1 - Members in Public Practice	Part 2 - Members in Business	Part 3 - All Other Members
Integrity & Objectivity	Integrity & Objectivity	Integrity & Objectivity
Independence		
General Standards	General Standards	
Compliance with Standards Rule	Compliance with Standards Rule	
Accounting Principles Rule	Accounting Principles Rule	
Confidentiality		
Contingent Fees		
Commission & Referral Fees		
Advertising and Other Solicitation		
Forms of Practices and Names		
Discreditable Acts	Discreditable Acts	Discreditable Acts

- Part 0 – Principles
  - Responsibilities Principle
    - Responsibility to cooperate with each other to improve the art of accounting, maintain the public's confidence, and carry out the profession's high standards.
  - Public Interest
    - Obligation to serve the public interest, honor the public trust, and commit to professionalism.
  - Integrity
    - Should perform all professional responsibilities with the highest sense of integrity.
  - Objectivity Principle
    - Should be impartial, intellectually honest, and free of conflicts of interest.

- Independence Principle
  - Should be independent in fact and appearance.
  - Independence is required for audit and attest services only.
- Due Care
  - Uphold both the technical and ethical standards of the profession
- Scope and Nature of Services
  - Practice should observe each of the above-described principles in determining the scope and nature of services to be provided
- Integrity & Objectivity
  - Applies to:

Part 1	Members in Public Practice
Part 2	Members in Business
Part 3	Other Members
  - Integrity and Objectivity implies the following:
    - Honesty
    - No Conflict of Interest
    - Free from Bias
    - Impartiality
    - No Misrepresentation of Facts
    - Auditors' Judgment

- Independence

- Applies to:

**Part 1** Members in Public Practice

- Independence Required

Engagements Requiring Independence	Engagement Not Requiring Independence
<ul style="list-style-type: none"> <li>• Audit of Financial Statements of Issuers (PCAOB AS)</li> <li>• Audit of Financial Statements of Non-Issuers (GAAS)</li> <li>• Audit of Interim Financial Statements (PCAOB AS / GAAS)</li> <li>• Governmental Audits (GAGAS)</li> <li>• Examination (SSAE)</li> <li>• Review (SSAE)</li> <li>• Agreed-Upon Procedures (SSAE)</li> <li>• Review Services (SSARs)</li> </ul>	<ul style="list-style-type: none"> <li>• Consulting Services</li> <li>• Tax Services</li> <li>• Valuation Services</li> <li>• Accounting Services</li> <li>• Bookkeeping Services</li> <li>• Training Services</li> <li>• Preparation Engagement (SSARs)</li> <li>• Compilation Engagement (SSARs)</li> </ul>

- Covered Members

- Audit Firm
- Audit Team
- All Partners of the Audit Firm Office/Members with an Influencing Position in the Firm
- Partner, Partner Equivalent or Manager Providing More Than 10 Hours of Non-Attest Services to Client
- Employee Benefit Plans of the Audit Firm
- Immediate Family of Covered Members
  - Spouse
  - Related Dependents
  - Unrelated Dependents
- Close Relatives of Covered Member
  - Parents

- Sibling
- Non-Dependent Child
- Duration of Independence
  - Sustained from the date the engagement letter is signed until the professional relationship's termination.
- Threats to Independence
  - Adverse Interest Threat
    - Threat where a member will not act with objectivity because the member's interests are opposed to the client's interests.
  - Advocacy Threat
    - Threat when a member promotes or supports a client's interests or positions to such an extent that the member's objectivity or independence is compromised.
  - Familiarity Threat
    - Threat when a member becomes overly sympathetic to the client's interests or excessively accepting of the client's work or products, which may jeopardize their objectivity.
  - Management Participation Threat
    - Threat when a member takes on the role of client management or assumes management responsibilities.
  - Self-Interest Threat
    - Threat arises when a member, like an auditor, could benefit, either financially or in some other manner, from an interest in, or relationship with, a client or persons associated with the client.
  - Self-Review Threat
    - Threat arises when a member is required to evaluate the results of a previous judgment made or service performed by them or supervised by them.
  - Undue Influence Threat
    - Threat arises when a member's judgment is subordinated or compromised due to external pressures, coercion, or influences.

- Safeguards Against Threats to Independence
  - Profession-Based Safeguards
    - Code of Conduct
    - Continuing Professional Education
    - Legislation
  - Client-Based Safeguards
    - Corporate Governance Structures
    - Internal Audit Function
    - Policies on Hiring Audit Firm Personnel
  - Audit Firm-Based Safeguards
    - Quality Control Standards
    - Peer Reviews
    - Rotation of Audit Partners
    - Policies to Limit Non-Audit Services to Audit Clients

- Independence Impairment
  - Independence Impaired by Financial Relationships

- Direct Financial Relationship

- ⇒ Owning Stocks
      - ⇒ General Partnership in Partnership Interest

	Covered Member's except Close Relatives	Close Relatives
Material	Impairs Independence	Impairs Independence
Immaterial	Impairs Independence	Doesn't Impair Independence

- Indirect Financial Relationship

- ⇒ Shares in Mutual Funds
      - ⇒ Limited Partnership Interest

	Covered Member's except Close Relatives	Close Relatives
Material	Impairs Independence	Impairs Independence
Immaterial	Doesn't Impair Independence	Doesn't Impair Independence

- Independence Impaired by Loans

- Compromised when a member, their firm, or a close relative has a loan or guarantee to or from an audit client.
      - Loans will not impair independence when:
        - ⇒ Grandfathered Loans
        - ⇒ Market Terms and Conditions
        - ⇒ Fully Collateralized
        - ⇒ No Delinquency
        - ⇒ Original Terms and Conditions Remain
      - Following types of loans does not impair Independence:
        - ⇒ Credit Card Debt with balances up to \$10,000 per month.
        - ⇒ FDIC Insured Checking Accounts.

- ⇒ Fully Collateralized Automobile Loans.
- ⇒ Loans fully collateralized by the Cash Surrender Value of an Insurance Policy.
- ⇒ Loans fully collateralized by Cash Deposits at the same Financial institution.
- Independence Impaired by Gifts
  - Gifts are any items or services of more than nominal value.
- Independence Impaired by Employment Relationships
  - Client Employee Joins Audit Firm
    - ⇒ Participates on the audit/attest engagement team.
    - ⇒ In a position to influence the engagement.
    - ⇒ Doesn't disassociate from the client.
  - Audit Firm Member Joins Client
    - ⇒ In a position to influence the CPA firm's operations or financial policies.
    - ⇒ They participate or seem to participate in the firm's business, such as in a consultancy role.
    - ⇒ Move happens within one year of leaving the CPA firm
  - Audit Firm Member Discusses Job Offer with Client
  - Audit Firm Member's Family Employed by Client
  - Simultaneous Employment with Audit Firm and Client.
- Independence Impaired by Unpaid Fees
- Independence Impaired by Unsolicited Financial Interests
  - Acquiring a financial interest through gifts or inheritance can impair independence.
  - Exceptions
    - ⇒ Prompt Disposal
    - ⇒ Engagement Non-participation
    - ⇒ Immaterial Investment

- Independence Impaired by Trusts and Estates
- Independence Impaired by Business Relationships

Business Relationships that Impair Independence	Business Relationships that do not Impair Independence
<ul style="list-style-type: none"> <li>• <b>Roles in Client's Management or Oversight</b> <ul style="list-style-type: none"> <li>○ Serving as a director, officer, employee, promoter, underwriter, voting trustee, or in any managerial position with a client.</li> <li>○ Acting as a trustee for a client's pension or profit-sharing trust.</li> </ul> </li> <li>• <b>Providing Non-Audit Services</b> <ul style="list-style-type: none"> <li>○ Bookkeeping Services.</li> <li>○ Internal Audit Functions.</li> <li>○ Designing or Implementing Internal Controls.</li> <li>○ Certain Consulting Services.</li> <li>○ Supervisory Activities.</li> <li>○ Legal and Valuation Services.</li> </ul> </li> <li>• <b>Financial Relationships</b> <ul style="list-style-type: none"> <li>○ Accepting a contingent fee from a client.</li> <li>○ Engaging in a finance lease agreement with a client.</li> <li>○ Participating in a joint venture with a client.</li> </ul> </li> <li>• <b>Litigation:</b> <ul style="list-style-type: none"> <li>○ Being involved in actual or potential litigation with the client.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Certain Social Memberships:</b> <ul style="list-style-type: none"> <li>○ Membership in a country club client where membership entails obtaining a pro-rata share of equity.</li> </ul> </li> <li>• <b>Honorary Positions:</b> <ul style="list-style-type: none"> <li>○ Serving as an honorary trustee for a not-for-profit client.</li> </ul> </li> <li>• <b>Certain Financial Relationships:</b> <ul style="list-style-type: none"> <li>○ Holding accounts in a financial institution that are fully insured by the appropriate state or federal insurance agency.</li> </ul> </li> <li>• <b>Tax Services for Issuers:</b> <ul style="list-style-type: none"> <li>○ Tax services are permitted if they are pre-approved by the audit committee and disclosed to the SEC. However, tax services related to aggressive tax positions or for corporate officers and their immediate family members are prohibited. Providing tax services to members of the Board of Directors is acceptable.</li> </ul> </li> </ul>

- General Standards

- Applies to:

Part 1	Members in Public Practice
Part 2	Members in Business

- General Standards include the following:

- Professional Competence
    - Due Professional Care
    - Planning and Supervision
    - Sufficient Relevant Data
    - Third-Party Provider

- Compliance with Standards Rule

- Applies to:

Part 1	Members in Public Practice
Part 2	Members in Business

- Must adhere to the standards laid down by the respective governing bodies, as designated by the Council.

Audit of Non-Issuers	Generally Accepted Auditing Standards (GAAS) as issued by the AICPA
Audit of Issuers	Public Company Accounting Oversight Board (PCAOB) Auditing Standards and GAAS
International Audits	International Standards on Auditing (ISA)
Governmental Audits	Generally Accepted Government Auditing Standards (GAGAS)
Attestation Engagements	Statements on Standards for Attestation Engagements (SSAEs)
Accounting & Review Services	Statements on Standards for Accounting and Review Services (SSARs)
Consulting	Statements on Standards for Consulting Services
Financial Planning	Statement on Standards in Personal Financial Planning Services
Valuation	Statement of Standards for Valuation Services
Taxes	Statements on Standards for Tax Services

- Accounting Standards Rule

- Applies to:

- Part 1 Members in Public Practice

- Part 2 Members in Business

- Members in public practice and members in business adhere to the recognized and prevailing accounting

- Confidentiality

- Applies to:

- Part 1 Members in Public Practice

- Confidentiality Rules, members in public practice are required not to disclose any confidential information pertaining to their clients outside of their audit firm.

- Exceptions

- Investigations and Inquiries

- Quality Reviews

- Subpoena or Court Orders

- Contingent Fees

- Applies to:

- Part 1 Members in Public Practice

- Contingent Fees Allowed

- Fees Fixed by Courts

- Representing in Tax Cases

- Contingent Fees Not Allowed

- Audit or Review

- Attestation Services

- Review & Compilation

- Preparing Tax Returns
- Commission & Referral Fees
  - Applies to:
    - Part 1 Members in Public Practice
  - Commission & Referral Fees Rules are allowed for Non-Attest Clients and not allowed for Attest Clients.
- Advertising and Other Solicitation
  - Applies to:
    - Part 1 Members in Public Practice
  - Advertising
    - Allowed, unless
      - False
      - Misleading
      - Deceptive
  - Cannot Claim a Guaranteed Refund
- Forms of Practices and Names
  - Applies to:
    - Part 1 Members in Public Practice
  - Misleading Names Not Allowed
  - Continue in Name of Past Owners
  - Membership in AICPA
    - Can't represent itself as a member of the AICPA unless all of its owners are members of the AICPA.
  - Use of CPA Designation
    - Individuals can use the "CPA" designation after their name, but if they are employed in a position that does not require a CPA license (for instance, in an industry or government position), they must also disclose their employment title.

- Discreditable Acts

- Applies to:

Part 1	Members in Public Practice
Part 2	Members in Business
Part 3	Other Members

- The following Acts are considered Discreditable to Profession:

- Discrimination
    - Tax Compliance
    - Negligence in Work
    - Withholding Client Records
    - Violation of Confidentiality
    - Fraudulent Marketing
    - Solicitation & Disclosure of CPA Exam Questions
    - Question and Answer Sharing of any Professional Education Course Exam
    - Falsifying or misrepresenting attendance at a professional education class
    - Tampering with the administration or grading of any professional education course or material

# Sarbanes-Oxley Act, 2002

- Title I: Public Company Accounting Oversight Board, (PCAOB)
  - Establishment of PCAOB
  - Registration Requirement
    - Auditors for Issuers, i.e., public companies, must register with the PCAOB
  - PCAOB is empowered to establish and adopt standards relating to auditing, attestation, quality control, ethics, and independence.
    - Audit working papers and related documentation to be retained for a period of seven years.
    - An Engagement Quality Control Review (EQCR) to be mandated to ensure quality.
  - Routine Inspections
    - Firms auditing more than 100 issuers: Inspected annually.
    - Firms auditing 100 or fewer issuers: Inspected once every three years.
  - PCAOB holds the authority to conduct investigations.
  - Foreign accounting firms that audit U.S. public companies are also subject to the rules and regulations established by PCAOB.
  - SEC Oversight
- Title II: Auditor Independence
  - Restriction on Non-Audit Services
  - Rotation of Key Audit Personnel
    - Lead (or primary) audit partner and the concurring (or review) partner must rotate off the audit engagement every 5 years.
  - Enhanced Communication with Audit Committees
    - Critical accounting policies used.
    - Alternative accounting treatments discussed with management.
    - Written communications between the auditor and management.

- Title III: Corporate Responsibility
  - Independent Audit Committee
  - Audit Committee Financial Expert
  - Audit Committee Responsibilities
    - Oversight of External Auditors.
    - Handling of Complaints
  - Corporate Responsibility for Financial Reports
  - Prohibition on Improper Influence on Conduct of Audits
  - Forfeiture of Certain Bonuses and Profits
- Title IV—Enhanced Financial Disclosures
  - Disclosures in Periodic Reports
    - Material Corrections Identified by the Auditor
    - Off-Balance Sheet Transactions
    - Pro Forma Financial Information
  - Prohibition on Personal Loans to Executives
  - Disclosure Requirements for Directors, Officers, and Principal Stockholders
  - Management's Assessment of Internal Controls
  - Each issuer shall disclose in its periodic reports whether they have adopted a code of ethics for senior financial officers.
  - Real-Time Issuer Disclosures
- Title V: Analysis Conflict of Interest
- Title VI: SEC Resources & Authority
- Title VII: Studies & Reports

- Title VIII—Corporate and Criminal Fraud Accountability
  - Criminal Penalties for Altering Documents.
  - Criminal Penalties for the Destruction of Audit Records
  - Statute of Limitations
    - Violations of security laws may be brought within two years after the discovery of the facts constituting the violation; or five years after the violation, whichever event is earlier.
  - Whistle-Blower Protection
  - Criminal Penalties for Defrauding Shareholders
- Title IX—White Collar Crime Penalty Enhancements
  - Elevating the status of attempt and conspiracy to the same level as a completed action.
  - Penalty for those corporate officers who fail to certify corporate financial reports are:
    - Misstatement: \$1 Million or Imprisoned up to 10 Years or both
    - Willful Default: \$5 Million or Imprisoned up to 20 Years or both
- Title X: Corporate Tax Returns
- Title XI—Corporate Fraud Accountability
  - Tampering
    - Shall be fined or imprisoned for not more than 20 years, or both.
  - Prohibit Persons from Serving as Officers/Directors
  - Can be fined or imprisoned for not more than 10 years, or both for Retaliation Against Informants

## Other Laws and Regulations

- Private Securities Litigation Reform Act of 1995
  - Enacted to curb perceived abuses in securities class action lawsuits.
  - Key provisions include:
    - Enhanced Auditor Procedures
      - Related Party Transactions
      - Illegal Acts
      - Going Concern Issues
    - Reporting of Illegal Acts
      - Investigate the act promptly.
      - Notify the management about the act.
      - Notify the Audit Committee (or, in its absence, the Board of Directors) is adequately informed.
- Dodd-Frank Wall Street Reform and Consumer Protection Act
  - It aimed to reduce risks in the U.S. financial system through a myriad of reforms.
  - Key provisions of Dodd-Frank Act include:
    - No Integrated Audit for Non-Accelerated Filers
- Jumpstart Our Business Startups Act (JOBS Act)
  - Its primary goal was to ease various securities regulations to encourage the funding of small businesses in the United States.

- Securities and Exchange Commission (SEC)
  - Key responsibilities of SEC include:
    - Oversight & Enforcement Authority over PCAOB
    - Approval of PCAOB Rules/Pronouncements
    - Sanction Authority
    - Censure or Impose Limitations
    - Removal of PCAOB Members
    - SEC Regulation S-K
- Department of Labor (DOL)
  - Responsible for ensuring the welfare of wage-earning workers, job seekers, and retirees.
  - Key provisions of the DOL include:
    - The DOL establishes specific guidelines to ensure that CPAs who audit Employee Benefit Plans are independent and free from any conflicts of interest.
      - They must not have any financial interests in the plan or the plan sponsor that would be considered material.
      - They also shouldn't have any direct business relationships with the plan or plan sponsor outside of the audit engagement.
- Governmental Accountability Office (GAO)
  - The Governmental Accountability Office (GAO) is an independent, non-partisan agency that works for the U.S. Congress.
  - Its primary function is to audit federal agencies to ensure the effective, efficient, and transparent use of public funds.
  - Additionally, the GAO investigates how the federal government spends taxpayer dollars.

# NINJA NOTES

Regulation 2026



## Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the REG section of the Exam:

Area I	Ethics, Professional Responsibilities and Federal Tax Procedures	10% - 20%
Area II	Business Law	15% - 25%
Area III	Federal Taxation of Property Transactions	5% - 15%
Area IV	Federal Taxation of Individuals	22%-32%
Area V	Federal Taxation of Entities	23%-33%

## Skill Allocation

Remembering and Understanding	25% - 35%
Application	35% - 45%
Analysis	25% - 35%
Evaluation	0% - 0%

## Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
REG - Core	50%	50%

## Section Time and Question Type

The table below presents the design of the Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
REG - Core	4 Hours	72	8

# Content

REG-1 Individual Taxation

REG-2 Property Taxation

REG-3 C-Corporation Taxation

REG-4 S-Corporation Taxation

REG-5 Partnership Taxation

REG-6 Limited Liability Companies (LLC) Taxation

REG-7 Tax-Exempt Organization Taxation

REG-8 State and Local Tax Issues

REG-9 Tax Compliance & Ethics and Responsibilities in Tax Preparation and Practice

REG-10 Federal Taxation Process

REG-11 Professional and Legal Responsibilities

REG-12 Contracts

REG-13 Sale of Goods

REG-14 Agency

REG-15 Secured Transactions

REG-16 Bankruptcy

REG-17 Suretyship

REG-18 Business Structures

REG-19 Other Laws and Regulations

# NINJA NOTES

Regulation 2026



**Individual Taxation**  
(July 1, 2025 – June 30, 2026 Exams)

## **Copyright & Disclaimer**

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

# Individual Taxation

## Overview of Individual Taxation

- Filing Requirements of Form 1040
  - Who must file Form 1040?
    - Income is greater than the standard deduction
    - Net self-employment income of \$400 or more
  - When to file Form 1040?
    - Form 1040 must be filed by April 15
- Overview of Form 1040

Gross Income
<Adjustments>
<b>Adjusted Gross Income (AGI)</b>
<Standard Deduction>
or
<Itemized Deductions>
<b>Taxable Income Before Qualified Business Income Deduction</b>
<Qualified Business Income Deduction>
<b>Taxable Income</b>
x Tax Rate
<b>Federal Income Tax</b>
< Tax Credits >
Alternative Minimum Tax
Self-Employment Tax
< Estimated Payments / Withholdings >
<b>Tax Due</b>

- Tax Accounting Basis: Cash & Accrual
  - Cash Basis: Cash Basis is allowed for small businesses that have average annual gross receipts of \$31 Million or less (for 2025) during the preceding 3 Years.
  - Accrual Basis: Accrual Basis is mandatory for businesses that have average annual gross receipts of more than \$31 Million (for 2025) during the preceding 3 Years.

## Qualifying Child and Qualifying Relative

- Qualifying Child and a Qualifying Relative are terms used by the IRS to determine if a person can be claimed as a dependent on your federal income tax return.
- Claiming a dependent can provide certain tax benefits, such as advantageous filing status, deductions, or credits.
- Qualifying Child
  - Son, daughter, stepchild, foster child, brother, sister, half-brother, half-sister, stepbrother, stepsister, or a descendant of any of these (e.g., grandchild, niece, or nephew).
  - The child must be under age 19 at the end of the tax year or under age 24 if they are a full-time student.
  - The child must not have provided more than half of their own support during the tax year
  - The child must have lived with you for more than half of the tax year.
  - Citizen of United States or Resident of United States, Mexico, or Canada
  - No income limit for the dependent to be claimed as a qualifying child
  - The child must not be filing a joint return for the tax year.
- Qualifying Relative
  - Not a Qualifying Child:
  - The person must either live with you all year as a member of your household or be related to you as a child, sibling, parent, grandparent, niece, nephew, aunt, uncle, or in-law
  - There is no age limit for a dependent to be claimed as a qualifying relative
  - Taxpayer must provide more than half of the person's total support for the tax year
  - Citizen of United States or Resident of United States, Mexico, or Canada
  - The person's gross income for the tax year must be less than the annual exemption amount (\$5,200 for tax year 2025; this amount may change in subsequent years)
  - The relative must not be filing a joint return for the tax year.

## Filing Status

- Single
  - Unmarried
  - Married but legally separated as of year-end
- Married Filing Jointly (MFJ)
  - Married and not divorced or legally separated as of year-end
  - Both spouses file one single joint return (Form 1040)
  - Neither spouse is a non-resident alien
  - Tax year is the same for both spouses
- Married Filing Separately (MFS)
  - Married couples who file separate tax returns, reporting their individual income, deductions, and credits.
- Head of Household
  - Unmarried or Considered Unmarried
  - Maintaining a Household
    - The taxpayer must have paid more than half the cost of maintaining a home for the tax year.
  - Must have a qualifying person, such as a dependent child, parent, or relative:
    - Qualifying Child
      - Meets the criteria of a Qualifying Child
    - Qualifying Relative other than Parent
      - Meets the criteria of a Qualifying Relative
      - Actually Related
      - Lives with the taxpayer for more than half the year (not the whole year)
    - Qualifying Relative who is a Parent
      - Meets the criteria of a Qualifying Relative

- Actually Related
- Need not live with the taxpayer
- Surviving Spouse (SS) / Qualifying Widow(er)
  - Spouse passed away in the last two years
  - Not Remarried
  - Qualifying Child
  - Principle Residence for the Qualifying Child for the whole year

## Gross Income

- Various types of gross income should be reported on U.S. tax forms:

Type of Income	Relevant Form(s)
Wages and Salaries (Salary Income)	Form W-2
Interest & Dividend (Portfolio Income)	Schedule B
Business Income or Loss (Business Income)	Schedule C
Capital Gains & Losses	Schedule D
Passive Income (Income from Pass-thru entities)	Schedule E
Farming Income	Schedule F
Other Miscellaneous Income	Schedule 1

- Wages and Salaries (Form W-2)

Taxable	Non-Taxable
<p><b>Cash &amp; Property</b></p> <ul style="list-style-type: none"> <li>• Include receipts in cash and FMV of property</li> </ul> <p><b>Tips</b></p> <ul style="list-style-type: none"> <li>• Tips &gt; \$20: Report to employer by 10th of next month: Included in month reported</li> <li>• Tips &lt; \$20: No need to report to the employer: Included in the month received</li> </ul> <p><b>Cancellation of Debt</b></p> <ul style="list-style-type: none"> <li>• Debt cancellation by employer should be included in gross income.</li> </ul> <p><b>Bargain Purchase</b></p> <ul style="list-style-type: none"> <li>• Include the difference between FMV and Purchase Price</li> </ul>	<p><b>Insurance Premiums</b></p> <ul style="list-style-type: none"> <li>• Group-term life insurance premiums for the first \$50,000 of coverage are excluded from taxable income</li> </ul> <p><b>Proceeds on Life Insurance</b></p> <ul style="list-style-type: none"> <li>• Proceeds from a life insurance policy are generally excluded from beneficiaries' gross income</li> </ul> <p><b>Medical/Health/Accident Insurance Premiums</b></p> <ul style="list-style-type: none"> <li>• Employer-paid medical, health, dental, vision, or accident insurance premiums are not part of the employee's taxable income</li> </ul>

### Guaranteed Payments

- Guaranteed payments received by a partner without regard to the partnership income are included in gross income and are subject to self-employment tax.

### Taxable Fringe Benefits

- Include FMV of fringe benefits in gross income (e.g., personal use of company car, moving expense reimbursements, non-qualified bicycle commuting)

### Insurance Premiums

- Include premiums paid for coverage above \$50,000

### Stock Options

Stock Options that have a readily determinable Fair Market Value:

- **Granted:** Ordinary Income = FMV of Options on Grant Date – Cost
- **Exercised:** No Tax on Exercise.  
Basis of Stock = Exercise Price + Income Recognized on Options on Grant Date
- **Sold:** Capital Gain or Loss = Sales Price – Basis of Stock
- **Lapsed:** Capital Loss = Income Recognized on Options on Grant Date.

Stock Options that do not have a readily determinable Fair Market Value:

- **Granted:** No Tax on Grant
- **Exercised:** Ordinary Income = FMV of Stock at Exercise Date – Exercise Price
- **Sold:** Capital Gain or Loss = Sales Price - FMV of Stock at Exercise Date.
- **Lapsed:** No Deduction on Lapse.

### Qualified Medical Expenses Reimbursement

- Reimbursements for qualified medical expenses are generally not taxable

### HSA and MSA Contributions

- Employer contributions to HSA and MSA accounts are not part of the employee's taxable income

### Contributions to Flexible Spending Arrangements (FSAs)

- Contributions to an FSA lower an employee's taxable income, providing tax savings. The dollar limitation on voluntary employee salary reductions for contributions to FSA is \$3,300 (for 2025).

### Dependent Care Benefits

- Employer-provided Dependent Care Benefits are not taxable up to a certain limit (\$5,000 per year for most taxpayers)

### Qualified Adoption Expenses

- Employer-provided financial assistance for adoption-related expenses is not taxable up to \$17,280 (for 2025)

### Workers' Compensation

- Workers' compensation in the form of wage replacement and medical benefits to employees who are injured or become ill as a direct result of their job is not taxable income for the employee.

### Employee Achievement Award

- Employee Achievement Award is not taxable if the value does not exceed \$400 and is not cash or cash equivalent

### De Minimis Fringe Benefits

- Low-value benefits are not considered taxable income

### Meals in Employer-Operated Facilities

- Meals provided on the employer's premises are generally not taxable

**Lodging (Required for the Job)**

- Lodging provided on the employer's premises as a job requirement is generally not taxable

**Transit Passes & Parking Benefits**

- Employer-provided transit passes up to \$325/month (for 2025) and parking benefits up to \$325/month (for 2025) are not taxable, helping offset commuting costs

**Qualified Employee Discounts**

- Discounts on merchandise or services are not taxable:
  - Merchandise discounts: If the discount is less than the employer's gross profit percentage (Discount % < Gross Profit %; Not Taxable)
  - Service Discounts If Discount is less than 20% of FMV of service (Discount % < 20%; Not Taxable)

**Educational Expenses**

- Educational assistance up to \$5,250 per year for undergraduate or graduate-level education provided by the employer is not taxable

**Contributions to the Pension Plan**

- Employer contributions to SEP or SIMPLE plans are not taxable

**Qualified Tuition Reductions**

- Qualified tuition reductions for educational institution employees are not taxable. If for a graduate degree, should be engaged in teaching (even if in a different institution) and should receive pay for that.

- Interest & Dividend (Schedule B)
  - Interest Income (Part I of Schedule B)

Taxable	Non-Taxable
Interest on U.S. Federal bonds, U.S. Treasury bills, and other U.S. obligations.	Interest earned on State, Municipal, and U.S. Possession Bonds are not taxable.
Interest in Industrial Development Bonds and Corporate Bonds.	Series EE & Series I Savings Bonds: Interest earned is not taxed upon redemption if used for qualified higher education expenses (tuition and fees, not room and board) for the taxpayer, their spouse, or their dependents.
Interest paid by Federal or State Government on late payment of tax refund.	
The Interest portion of the Installment Sale proceeds.	

- Dividend Income (Part II of Schedule B)

Taxable	Non-Taxable
<p><b>Qualified Dividends</b></p> <ul style="list-style-type: none"> <li>• Taxed at lower rates as they meet specific criteria set by the IRS</li> </ul> <p><b>Ordinary Dividends</b></p> <ul style="list-style-type: none"> <li>• Dividends that do not meet the criteria to be considered qualified dividends. Taxed at the taxpayer's ordinary income tax rate</li> </ul>	<p><b>Return of Capital</b></p> <ul style="list-style-type: none"> <li>• Non-taxable distribution representing a return on the shareholder's initial investment.</li> </ul> <p><b>Stock Splits</b></p> <ul style="list-style-type: none"> <li>• A corporate action dividing existing shares into multiple shares.</li> </ul> <p><b>Stock Dividends</b></p> <ul style="list-style-type: none"> <li>• Stock dividends to common stockholders allocate the original basis to the increased number of stocks held. Non-taxable when there is no option to receive cash dividends.</li> </ul> <p><b>Mutual Funds Invested in Tax-Free Bonds</b></p> <ul style="list-style-type: none"> <li>• Dividends from mutual funds invested in tax-free bonds are not taxable.</li> </ul> <p><b>Life Insurance</b></p> <ul style="list-style-type: none"> <li>• Non-taxable return of premium/capital from life insurance.</li> </ul> <p><b>S-Corp Dividend</b></p> <ul style="list-style-type: none"> <li>• S-Corp Income flows through to Schedule E of S-Corp shareholders and is not taxable as dividends.</li> </ul>

- Business Income (Schedule C)
  - Applicability
    - Self-Employed Individuals
    - Sole Proprietors
    - Single-Member LLCs
    - Income from a Hobby
    - Husband and Wife Joint Venture
    - Statutory Employees
  - Overview of Schedule C

Gross Receipts	Total amount received from sales and services provided during the tax year.
Sales Returns	Sales Returns represent the value of Sales returned by the customer.
Net Receipts	Net Receipts = Gross Receipts – Sales Return. (If cash basis, net receipts equals cash received.)
Cost of Goods Sold or Cost of Services	<p>Cost of Goods Sold (COGS) = Opening Inventory + Cost of Goods Manufactured - Ending Inventory</p> <p><b>Inventory</b></p> <ul style="list-style-type: none"> <li>• <b>Small Businesses with average annual gross receipts of \$31 Million (for 2025) or less during the preceding three Years:</b> <ul style="list-style-type: none"> <li>○ <u>If Using Accrual Basis of Accounting:</u> <ul style="list-style-type: none"> <li>▪ Inventory is valued at a Lower Cost or Market Value</li> <li>▪ May use, specific identification, FIFO, or LIFO Rule. (Must follow LIFO Conformity Rule)</li> </ul> </li> <li>○ <u>If Using Cash Basis of Accounting:</u> <ul style="list-style-type: none"> <li>▪ Treat Inventory as non-incidental material and supplies</li> <li>▪ Conform to taxpayer’s financial accounting treatment of inventories.</li> </ul> </li> </ul> </li> <li>• <b>Businesses with average annual gross receipts of \$31 Million (for 2025) or more during the preceding three Years:</b> <ul style="list-style-type: none"> <li>○ Must use UNICAP Rules for Inventory</li> </ul> </li> </ul>
Gross Profit	Gross Profit = Net Receipts – COGS
Other income	Other Income may include:

	<ul style="list-style-type: none"> <li>• Federal and State Gasoline Tax Credit</li> <li>• Royalties</li> <li>• Rental Income (if part of business operations)</li> <li>• Interest on business accounts</li> <li>• Gains from the sale of business assets</li> </ul>
<b>Gross Income</b>	Gross Income = Gross Profit + Other Income
<Total Expenses>	
<b>Net Profit/Loss</b>	Gross Income – Total Expenses – Expenses for Business Use of Home

○ Deductible Business Expenses

- Salaries
- State and Local Taxes and Federal Payroll Taxes
- Office Expenses
- Transportation Expenses
- Business Meals up to 50%
- Business Travel
- Interest on Business Loan
- Fringe Benefits Paid to Employee
- Legal & Professional Services and Fees
- Business Bad Debts
- Depreciation and Amortization
- Business Start-Up Cost
  - Businesses can deduct up to \$5,000 in start-up costs during the first year of operation. However, this \$5,000 limit is reduced dollar-for-dollar for start-up expenses exceeding \$50,000. If your start-up costs exceed the deductible limit the remaining balance will be amortized over 180 months (15 years), beginning with the month your business starts operating.

- Non-Deductible Expenses
  - Salaries to Owner
  - Entertainment Expense
  - Federal Income Taxes
  - Fines & Penalties
  - Personal Expense
  - Expenses for Illegal Business
  - Transportation Benefits Provided to an Employee for Travel Between Home Location and Office
- Uniform Capitalization (UNICAP) Rules
  - Applies to
    - Produced for Use: Example, Building constructed for own use
    - Produced for Sale: Example, Manufacturer's Inventory
    - Acquired for Resale: Example, Retailer's Inventory
  - Capitalized Costs
    - Pre-Production Costs
    - Production Costs
      - ⇒ Direct Materials
      - ⇒ Direct Labor
      - ⇒ Direct & Indirect Production Costs (Factory Overheads)
    - Pre-Sale Costs
  - Non-Capitalized Costs
    - Advertising, Selling, and Distribution Expenses
    - Income Taxes
    - Strike Expenses

- Warranty Expenses
- General and Administrative (G&A) Expenses
- Applicability
  - Businesses with average annual gross receipts of more than \$31 million (for 2025) during each of the preceding three tax years.
- Net Operating Loss (NOL)
  - Sources of NOL
    - Business Loss from a Sole Proprietorship reported on Schedule C
    - Share of Business Loss from a Partnership or S-Corporation reported on Schedule E
    - Farming Business Loss reported on Schedule F

- NOL Calculation

Component	Amount \$
Loss Sources:	
Schedule C Business Loss	(XXX)
Schedule F Farming Business Loss	(XXX)
Schedule E Partnership/S-Corp Loss	(XXX)
Income Sources:	
Wages & Salaries Income (Form W-2)	XXX
Business Income (Schedule C)	XXX
Passive Income (Schedule E)	XXX
Farming Income (Schedule F)	XXX
<b>Net Operating Loss (NOL)</b>	<b>(XXX)</b>

- Excess Business Losses (Business Losses in excess of Business Income) can be deducted against other sources of income unto \$626,000 for MFJ and \$313,000 for other taxpayers (for 2025) and the balance is carried forward as NOL.
- NOL Treatment
  - Businesses can now carry forward Net Operating Losses (NOLs) indefinitely but can only use NOL carryforwards to offset up to 80% of their taxable income in a given year, with any remaining NOLs continuing to be carried forward indefinitely.

- Capital Gains & Losses (Schedule D)
  - Calculation of Capital Gains and Losses

Proceeds	Cash received Property received (FMV) Services received (FMV) Cancellation of Debt Selling Expenses
<Adjusted Basis of Assets Sold>	
<b>Capital Gain or Loss Realized</b>	Holding Period > 1 Year (Long-Term Capital Gain or Loss) Holding Period < 1 Year (Short-Term Capital Gain or Loss)

- Netting Process for Capital Gains and Losses
  - Step 1: Net Short-Term Gains and Losses together, and Long-Term Gains and Losses together

Short-Term Capital Gain
(Short-Term Capital Loss)
Net Short-Term Capital Gain / (Net Short-Term Capital Loss)

Long-Term Capital Gain
(Long-Term Capital Loss)
Net Long-Term Capital Gain / (Net Long-Term Capital Loss)

- Step 2: Net Short-Term Gains and Losses with Long-Term Gains and Losses if opposite signs or else no netting.
  - If one is a net gain and the other is a net loss, net them together. This will result in either a single net Short-Term Capital Gain/Loss or a Single Net Long-Term Capital Gain/Loss.

Net Short-Term Capital Gain
(Net Long-Term Capital Loss)
Net Short-Term Capital Gain

(Net Short-Term Capital Loss)
Net Long-Term Capital Gain
Net Short-Term Capital Loss

Net Long-Term Capital Gain
(Net Short-Term Capital Loss)
Net Long-Term Capital Gain

(Net Long-Term Capital Loss)
Net Short-Term Capital Gain
Net Long-Term Capital Loss

- If both are gains or both are losses, do not net them together. In this case, you will have either:
  - ⇒ Net Short-Term Capital Gain and Net Long-Term Capital Gain.
  - ⇒ Net Short-Term Capital Loss and Net Long-Term Capital Loss.

○ Tax Treatment of Capital Gains and Losses

Type	Tax Treatment
Net Short-Term Capital Gain	<ul style="list-style-type: none"> <li>• Short-Term Capital Gains are taxed at ordinary income tax rates</li> </ul>
Net Short-Term Capital Loss	<ul style="list-style-type: none"> <li>• Set off Net Short-Term Capital Loss from other sources of income up to \$3,000 (MFJ &amp; Single) and \$1,500 (MFS) every year.</li> <li>• Excess carried forward indefinitely</li> </ul>
Net Long-Term Capital Gain	<ul style="list-style-type: none"> <li>• Long-Term Capital Gains are taxed at capital gain tax rates (0%, 15%, 20%)</li> </ul>
Net Long-Term Capital Loss	<ul style="list-style-type: none"> <li>• Set off Net Long-Term Capital Loss from other sources of income up to \$3,000 (MFJ &amp; Single) and \$1,500 (MFS) every year.</li> <li>• Excess carried forward indefinitely</li> </ul>

- Passive Income (Schedule E)

- Passive Activities include the following:

- Income from Rental Real Estate Activities
- Income from Royalties
- Income from Closely Held C-Corporations and Personal Service Corporations
- Income from Schedule K-1 (Pass-through Income)
  - Partnerships and Limited Liability Companies (LLCs)
  - S-Corporations
  - Estates and Trusts

○ Income from Rental Real Estate Activities

▪ Rental Income: Active vs. Passive

	Income Type	Reporting Form
Materially Participating & Real Estate Professional	Active	Schedule C (Form 1040)
No Material Participation or Non-Real Estate Professional	Passive	Schedule E (Form 1040)

▪ Rental Income: Calculation

Gross Rental Income	<ul style="list-style-type: none"> <li>• Gross Rental Income includes               <ul style="list-style-type: none"> <li>○ Rent Payments taxpayers receive from tenants during the tax year.</li> <li>○ Other payments from tenants, such as:                   <ul style="list-style-type: none"> <li>▪ Reimbursement for utilities</li> <li>▪ Other property-related expenses</li> </ul> </li> </ul> </li> <li>• Cash Basis: Rent Received &amp; Accrual Basis: Rent Earned</li> </ul>
Prepaid Rental Income	<ul style="list-style-type: none"> <li>• Prepaid Rental Income is always included, even on an accrual basis.</li> <li>• Rental income is taxed earlier than received or earned.</li> </ul>
Lease Cancellation Payment	<ul style="list-style-type: none"> <li>• Payments received for lease cancellation are included in the calculation of Net Rental Income.</li> </ul>
Lease Improvement In-lieu-of Rent	<ul style="list-style-type: none"> <li>• Payments received for lease improvements in place of rent are included in the calculation of Net Rental Income.</li> </ul>
<Rental Expenses>	<ul style="list-style-type: none"> <li>• Rental Expenses include:               <ul style="list-style-type: none"> <li>○ Mortgage interest</li> <li>○ Property taxes</li> <li>○ Insurance</li> <li>○ Depreciation</li> <li>○ Repairs and Maintenance</li> <li>○ Utilities</li> <li>○ Property Management Fees</li> <li>○ Advertising Costs</li> <li>○ Legal and Professional Fees</li> </ul> </li> </ul>
<b>Net Rental Income or Loss</b>	

- Home Is Rented Out and also used as a Personal Residence

	Rental Income	Rental Expenses
<p>Treated as Personal Residence:</p> <ul style="list-style-type: none"> <li>Used as a Home: Higher of 15 Days or 10% of Rented Days. and</li> <li>Rented for less than 15 days during the year.</li> </ul>	Not Included	<p>Not Deducted on Schedule E.</p> <p><b>Mortgage Interest &amp; Property Taxes:</b></p> <ul style="list-style-type: none"> <li>Allowed as an Itemized Deduction on Schedule A.</li> </ul> <p><b>Property Expenses:</b></p> <ul style="list-style-type: none"> <li>Property expenses such as utilities, insurance, and depreciation are not deductible.</li> </ul>
<p>Treated as Personal and Rental Residence:</p> <ul style="list-style-type: none"> <li>Used as a Home: Higher of 15 Days or 10% of Rented Days. and</li> <li>Rented for 15 or more days during the year.</li> </ul>	Included	<p>Proportionate Reductions for Rental Expenses are allowed on Schedule E.</p> <p><b>Mortgage Interest &amp; Property Taxes:</b></p> <ul style="list-style-type: none"> <li>Mortgage Interest &amp; Property Taxes allocated between Personal and Rental Use <ul style="list-style-type: none"> <li>Deductible for the Period Rented on Schedule E (Months Rented / 12)</li> <li>Allowed as an Itemized Deduction on Schedule A for the period used as a personal residence. (Months used as a Personal Residence / 12)</li> </ul> </li> </ul> <p><b>Property Expenses:</b></p> <ul style="list-style-type: none"> <li>Property Expenses such as utilities, insurance, and depreciation are allocated proportionately between Personal and Rental Use. <ul style="list-style-type: none"> <li>Deductible for the Period Rented on Schedule E.</li> <li>Not Deductible for Period used as a personal residence.</li> </ul> </li> </ul>

- **Passive Activity Loss Offset Rules**

- Passive Activity Losses (PAL) can generally be offset against passive income only.
- Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed of.
- Exceptions:

⇒ Active Participation

AGI Range	Offset Limitation
\$100,000 or less	\$25,000
Between \$100,000 and \$150,000	\$25,000 - 50% x (AGI - \$100,000)
\$150,000 or more	\$0

⇒ Material Participation

- Rental losses are fully deductible against all types of income without any limitations.

- **Income from Royalties**

Gross Royalty Income	<ul style="list-style-type: none"> <li>• Gross Royalty Income includes               <ul style="list-style-type: none"> <li>○ Upfront Payments</li> <li>○ Ongoing Royalties based on Sales or Usage,</li> <li>○ Other Relevant Payments</li> </ul> </li> </ul>
<Royalty Expenses>	<ul style="list-style-type: none"> <li>• Royalty Expenses include:               <ul style="list-style-type: none"> <li>○ Legal Fees.</li> <li>○ Agent Fees.</li> <li>○ Other Costs directly associated with generating the Royalty Income.</li> </ul> </li> </ul>
<b>Net Royalty Income or Loss</b>	

- **Income from Closely Held C-Corporations and Personal Service Corporations**

- This has been discussed along with C-Corporation Taxation.

- **Income from Schedule K-1 (Pass-through Income): Partnerships, Limited Liability Companies (LLCs), S-Corporations, Estates, and Trusts.**

- This has been discussed along with Entities Taxation.

- Farming Income (Schedule F)

- Accounting Methods Used to Report Farming Income

Accounting Method	Description
Cash Basis	Income is reported in the year it is received, and expenses are deducted in the year they are paid.
Accrual Basis	Income is reported in the year it is earned, and expenses are deducted in the year they are incurred, regardless of when cash is received or paid.
Crop Basis	Expenses for producing the crop are deducted in the year income is realized from the sale of the crop.

- Farming Income: Calculation

Farming Income	Farming Income includes: <ul style="list-style-type: none"> <li>• Sales of livestock, produce, grains, etc.</li> <li>• Agricultural program payments.</li> <li>• Crop insurance proceeds and disaster payments.</li> <li>• Cooperative distributions.</li> <li>• Custom hire (machine work) income.</li> <li>• Other farming-related income.</li> </ul>
<Farming Expenses>	Farming Expenses include: <ul style="list-style-type: none"> <li>• Vehicle expenses.</li> <li>• Chemicals, conservation, and depreciation.</li> <li>• Employee benefits and feed for livestock.</li> <li>• Fertilizers, freight, and fuel expenses.</li> <li>• Insurance, interest, and labor costs.</li> <li>• Rent or lease, repairs, and seeds/plants.</li> <li>• Taxes, utilities, and veterinary expenses.</li> <li>• Other farming-related expenses.</li> </ul>
<b>Net Farming Profit or Loss</b>	

- Net Operating Loss Related to Farming

- Net Operating Losses (NOL) related to farming can still be carried back for two years and carried forward for 20 years.

- Other Items of Inclusions in Gross Income

- Alimony Received

Divorces finalized prior to January 1, 2019	<ul style="list-style-type: none"> <li>• <b>Alimony Received:</b> Taxable</li> <li>• <b>Alimony Paid:</b> Deductible</li> </ul>
Divorces finalized on or after January 1, 2019	<ul style="list-style-type: none"> <li>• <b>Alimony Received:</b> Not Taxable</li> <li>• <b>Alimony Paid:</b> Not Deductible</li> </ul>

- Social Security Benefits

- Taxation of Social Security benefits depends on the beneficiary's provisional income.
- 0% - 85% of Social Security Benefits are taxable based on the provisional income level.

- Distributions from Individual Retirement Account (IRA)

	Traditional IRA	Roth IRA	Non-Deductible IRA	Coverdell IRA
Contribution	Deductible	Non-Deductible	Non-Deductible	Non-Deductible
Distributions: Principal	Taxable	Not taxable	Not taxable	Not taxable
Distributions: Interest	Taxable	Not taxable	Taxable	Not taxable
Distribution Age Limits	Distributions can occur after age 59 ½.	Distributions can occur after age 59 ½. and the account has been open for 5 years	Distributions can occur after age 59 ½.	No Age limit on Distribution. However, Funds should be used by the beneficiary before age 30.
Penalty on Early Withdrawal	10% Penalty + Income Tax on the amount withdrawn in case of early withdrawal	10% Penalty + Income Tax on the Earnings Portion in case of early withdrawal	10% Penalty + Income Tax on the Earnings Portion in case of early withdrawal	10% Penalty + Income Tax on the Leftover Funds
Required Minimum Distributions (RMDs)	RMDs must begin by April 1 of the year following the year that you turn 73	No RMDs.	RMDs must begin by April 1 of the year following the year that you turn 73	No RMDs.

○ Income from Pensions and Annuities

	Qualified Pension and Retirement Plans	Non-Qualified Pension and Retirement Plans
Contributions	Deductible	Non-Deductible
Distributions: Principal	Taxable	Non-Taxable
Distributions: Interest	Taxable	Taxable

○ State and Local Tax Refunds

Situation	Taxability of State and Local Tax Refunds
Itemized Deductions	Taxable up to the benefit received from the deduction
Standard Deduction	Not Taxable

○ Unemployment Compensation

○ Debt Cancellation

○ Gambling Winnings

○ Jury Duty Fees

○ Prizes and Awards

- Prizes and awards are taxable
- Exceptions:
  - Selection without any action on the recipient's part.
  - Services not required of the recipient.
  - Charity or government gets the payment as assigned by the recipient.

○ Punitive Damages

○ Scholarships and Grants

- Non-Degree Students: Taxable
- Degree Students: Non-Taxable to the extent used for tuition and fees, books, supplies, and equipment.

○ Income Earned by Decedent

- Exclusions from Gross Income
  - Foreign Earned Income Exclusion
  - Alimony Received for divorce or separation agreements executed or modified on or after January 1, 2019.
  - Inheritance and Gifts
  - Life Insurance Policy
  - Medical Benefits

## Adjustments (Above the Line Deductions)

- Contributions to HSA: Health Savings Account / MSA: Medical Savings Account Deduction

	HSA: Health Savings Account / MSA: Medical Savings Account Deduction
Contribution	<ul style="list-style-type: none"> <li>Deductible</li> <li>\$4,300 (Individual) &amp; \$8,550 (Family) (for 2025)</li> <li>Additional \$1,000 Contribution allowed for Individuals aged 55 and above</li> </ul>
Distributions	<ul style="list-style-type: none"> <li>Non-Taxable if used for Qualified Medical Expenses</li> </ul>
Penalty on Non-Qualified Use	<ul style="list-style-type: none"> <li>20% Penalty + Income Tax if the distribution is not used for medical expenses.</li> </ul>

- Contributions Individual Retirement Account (IRA)

Retirement Account	Deductibility	Contribution Limit	Additional Contribution	Retirement Savings Contribution Credit
Traditional IRA	Deductible	Lesser of <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony).</li> </ul>	An additional \$1,000 is allowed for Individuals aged 50 and above	Allows Retirement Savings Contribution Credit for up to 50% on \$2,000 Contributions for Low-Income Groups
Roth IRA	Non-Deductible	Lesser of <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony).</li> </ul>	An additional \$1,000 is allowed for Individuals aged 50 and above	Allows Retirement Savings Contribution Credit for up to 50% on \$2,000 Contributions for Low-Income Groups
Non-Deductible IRA	Non-Deductible	Lesser of <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony).</li> </ul>	An additional \$1,000 is allowed for Individuals aged 50 and above	N/A
Coverdell IRA (ESA)	Non-Deductible	\$2,000	N/A	N/A

- Alimony Paid

Divorces finalized prior to January 1, 2019	<ul style="list-style-type: none"> <li><b>Alimony Received:</b> Taxable</li> <li><b>Alimony Paid:</b> Deductible</li> </ul>
Divorces finalized on or after January 1, 2019	<ul style="list-style-type: none"> <li><b>Alimony Received:</b> Not Taxable</li> <li><b>Alimony Paid:</b> Not Deductible</li> </ul>

- Withdrawal of Savings Penalty

- Educator Expenses
  - Educators in primary and secondary schools can deduct up to \$300 (for 2025) of unreimbursed qualified teaching expenses
- Student Loan Interest Deduction
  - Individuals can deduct the lesser of \$2,500 or the amount of interest paid on a student loan for the tax year for themselves, spouse, or dependents.
- Moving Expenses for Members of the Armed Forces
- Legal Fees for Discrimination Suit
- Jury Duty Fees Paid to Your Employer
- Deductions for Self-Employed
  - Self-Employment Taxes
    - Self-employed individuals are allowed to deduct the employer's portion of self-employment taxes (7.65%) paid by them which is 50% of total Self-Employment Taxes paid.
  - Self-Employment Health Insurance Deduction
  - Self-Employed Retirement Plans

	Qualified Pension and Retirement Plans	Non-Qualified Pension and Retirement Plans
Contributions	Deductible	Non-Deductible
Distributions: Principal	Taxable	Non-Taxable
Distributions: Interest	Taxable	Taxable

## Standard Deduction

- Standard Deduction Limits (for 2025)

Filing Status	Standard Deduction
Single/Married Filing Separately	\$15,000
Married Filing Jointly/Qualifying Widow(er)	\$30,000
Head of Household	\$22,500

- Additional Standard Deduction (for 2025)

	Single	Married Filing Jointly
Single / Only 1 Spouse Qualify		
65 or Blind	\$2,000	\$1,600
65 and Blind	\$4,000	\$3,200
Both Spouses Qualify		
Each 65 or Blind	-	\$3,200
Both 65 and Blind	-	\$6,400

- Standard Deduction – Individuals Claimed as Dependents
  - For dependents of others, the standard deduction is the greater of \$1,350 or earned income + \$450 for 2025 but must not exceed the regular standard deduction.

## Itemized Deductions

- Medical Expenses (In Excess of 7.5% of AGI)
  - Qualified Medical Expenses for Self, Spouse and Dependents
    - To claim someone as a dependent for Medical Expenses, they must meet the following criteria:
      - Taxpayer must provide more than half of the person's total support for the tax year
      - The person must either live with the taxpayer all year as a member of taxpayer's household or be related to taxpayer as a child, sibling, parent, grandparent, niece, nephew, aunt, uncle, or in-law
      - Citizen of United States or Resident of United States, Mexico, or Canada
    - However, they are not required to meet the Gross Income (Gross Income less than \$5,050 for 2025) or Joint Return (No Joint Return) criteria which is required to meet the definition of Qualifying Relative.

o Qualified and Non-Qualified Medical Expenses

Qualified Medical Expenses	Non-Qualified Medical Expenses
<ul style="list-style-type: none"> <li>Prescribed drugs and medicines.</li> </ul>	<ul style="list-style-type: none"> <li>Over-the-counter drugs not prescribed by a physician</li> </ul>
<ul style="list-style-type: none"> <li>Fees paid to medical practitioners, including doctors, dentists, and surgeons.</li> </ul>	<ul style="list-style-type: none"> <li>General health costs, like Gym Memberships and Health Club Membership, that aren't prescribed by a physician for a specific health condition</li> </ul>
<ul style="list-style-type: none"> <li>Travel Costs for Medical Care (Actual Costs or Standard Mileage Rate of \$0.21/mile for 2025)</li> </ul>	<ul style="list-style-type: none"> <li>Personal hygiene items and ordinary personal care expenses.</li> </ul>
<ul style="list-style-type: none"> <li>Meals and Lodging provided by a hospital or similar institution during medical treatment.</li> </ul>	<ul style="list-style-type: none"> <li>Household help.</li> </ul>
<ul style="list-style-type: none"> <li>Stop-Smoking Programs</li> </ul>	<ul style="list-style-type: none"> <li>Illegal operations or treatments.</li> </ul>
<ul style="list-style-type: none"> <li>Weight-Loss Programs (only if the purpose is to treat obesity or other disease)</li> </ul>	<ul style="list-style-type: none"> <li>Cosmetic surgery purely for aesthetic reasons.</li> </ul>
<ul style="list-style-type: none"> <li>Surgery including plastic/cosmetic surgery done to cure the disfiguring injury, illness, or birth defects.</li> <li>LASIK surgery</li> </ul>	<ul style="list-style-type: none"> <li>The Medicare portion of Social Security and Self-Employment Taxes.</li> </ul>
<ul style="list-style-type: none"> <li>Insurance Premiums for Medical, Dental, Hospital care, and Qualifying Long-Term Care Policies</li> </ul>	<ul style="list-style-type: none"> <li>Insurance premiums for Accident, Disability, and Life Insurance.</li> </ul>
<ul style="list-style-type: none"> <li>Medical Equipment and devices like eyeglasses, hearing aids, false teeth, etc.</li> </ul>	<ul style="list-style-type: none"> <li>Funeral and Burial Expenses.</li> </ul>
<ul style="list-style-type: none"> <li>Costs to install medically prescribed facilities or remove structural barriers at home for physically handicapped such as swimming pool, elevator, etc.</li> </ul> <p>⇒ Deduction = Cost of Home Improvement – Increase in FMV</p>	

o Calculation of Deductible Medical Expenses

Qualified Medical Expense	XXX
<Insurance/Employer Reimbursement>	(XXX)
<b>Medical Expense Paid</b>	<b>XXX</b>
<7.5% of AGI>	(XXX)
<b>Deductible Medical Expenses</b>	<b>XXX</b>

- State/Local/Foreign Taxes (SALT) paid (up to \$10,000)

Deductible Taxes	Non-Deductible Taxes
<ul style="list-style-type: none"> <li>• State and Local Income Taxes or State and Local Sales Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Federal Income Tax</li> </ul>
<ul style="list-style-type: none"> <li>• State and Local Personal and Real Property Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Federal, State, and Local Estate or Gift Taxes</li> </ul>
<ul style="list-style-type: none"> <li>• Foreign Income Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Social Security and Self-Employment Taxes</li> </ul>
	<ul style="list-style-type: none"> <li>• Business Taxes.</li> </ul>
	<ul style="list-style-type: none"> <li>• Foreign Sales Tax, Real Property Tax, and Personal Property Tax</li> </ul>

- Interest Expense

Deductible Interest	Non-Deductible Interest
<ul style="list-style-type: none"> <li>• Home Mortgage Interest for loans up to \$750,000</li> </ul>	<ul style="list-style-type: none"> <li>• Personal Consumer Interest</li> </ul>
<ul style="list-style-type: none"> <li>• Investment Interest Expense limited to net investment income</li> </ul>	<ul style="list-style-type: none"> <li>• Education Loan Interest</li> </ul>
<ul style="list-style-type: none"> <li>• Home Equity Loans</li> </ul>	<ul style="list-style-type: none"> <li>• Prepaid Interest</li> </ul>

- Charitable Contributions

- Allowed as an itemized deduction on Schedule A up to 60% of AGI.
- Deductible and Non-Deductible Charitable Contribution

Deductible Charitable Contribution	Non-Deductible Charitable Contribution
<ul style="list-style-type: none"> <li>• Charitable Contributions to Qualified Domestic Organizations for religious, charitable, scientific, literary, or educational purposes.</li> </ul>	<ul style="list-style-type: none"> <li>• Contributions to individuals or non-qualified organizations civic leagues, social clubs, foreign organizations, political organizations, communist organizations, chambers of commerce, and labor unions.</li> </ul>
<ul style="list-style-type: none"> <li>• Out-of-pocket costs incurred while doing work for a charitable organization.</li> </ul>	<ul style="list-style-type: none"> <li>• Cannot deduct the value of taxpayer's time or services that taxpayer donates to a charitable organization.</li> </ul>
<ul style="list-style-type: none"> <li>• \$50 per student per month for every completed month of an unrelated student staying in a taxpayer's home on agreement with a qualified organization.</li> </ul>	<ul style="list-style-type: none"> <li>• Cannot deduct the value of the use of a property that the taxpayer allows to a charitable organization.</li> </ul>
	<ul style="list-style-type: none"> <li>• Cannot deduct the value of Blood Donation</li> </ul>

- Charitable Contribution Deduction Calculation

Charitable Contribution	XXX
<Benefits Received>	(XXX)
<b>Charitable Contribution Deduction</b>	<b>XXX</b>

- Charitable Contribution Limits

Contribution Type	Deduction	Deduction Limit
Cash	Amount Contributed	Up To 60% of Adjusted Gross Income (AGI)
Short-Term Property	Lower of Basis or FMV of Property	Up To 50% of Adjusted Gross Income (AGI)
Long-Term Property	FMV of Property	Up To 30% of Adjusted Gross Income (AGI)

- Casualty Losses (In Excess of 10% of AGI)

- Deductible and Non-Deductible Casualty Losses

Deductible Casualty Losses	Non-Deductible Casualty Losses
<ul style="list-style-type: none"> <li>● Personal Property Losses that occurred due to a Federally Declared Disaster</li> </ul>	<ul style="list-style-type: none"> <li>● Business Property Losses that occurred due to a Federally Declared Disaster</li> </ul>
	<ul style="list-style-type: none"> <li>● Progressive Damage that happens over time, such as wear and tear or deterioration.</li> </ul>
	<ul style="list-style-type: none"> <li>● Casualty Insurance Premiums for insurance coverage</li> </ul>
	<ul style="list-style-type: none"> <li>● Incidental Expenses such as temporary housing, meals, and transportation costs incurred due to a casualty or disaster, but not directly related to the damage or destruction of property, are not deductible as a casualty loss.</li> </ul>

- Casualty Loss Deduction Calculation

Drop in FMV (Limited to Tax Basis of the Asset)	XXX
<Insurance/Government Reimbursement>	(XXX)
<\$100 per event>	(\$100)
<b>Loss Eligible for Deduction</b>	<b>XXX</b>
<10% of AGI>	(XXX)
<b>Deductible Casualty Loss</b>	<b>XXX</b>

- Other Itemized Deductions

- Gambling Losses

- Taxes for Decedent

## Qualified Business Income (QBI) Deduction

- QBI Deduction Calculation
  - Step 1: Calculate Tentative QBI Deduction
    - Tentative QBI Deduction = QBI x 20%
  - Step 2: Apply Phase-Out (Wage and Property Limitation) (for 2025)

	Taxable Income		QTB	SSTB
	Single	MFJ		
<b>Below Threshold</b>	\$197,300	\$394,600	Full 20% Deduction	Full 20% Deduction
<b>Between Threshold</b>	\$197,300- \$247,300	\$394,600- \$494,600	QBI Deduction - [(QBI Deduction - W-2 Wage & Property Limitation) x Phase-in Percentage]	[(1 - Phase-in %) x QBI Deduction] - {[(1 - Phase-in %) x QBI Deduction]} - [(1 - Phase-in %) x W-2 Wage & Property Limitation]} x Phase-in Percentage Used up
<b>Above Threshold</b>	\$247,300	\$494,600	QBI Deduction Limited to W-2 Wage & Property Limitation	No QBI Deduction

- Step 3: Apply Overall Limitation
  - The final QBI deduction would be limited to an overall limitation calculated as 20% of (Taxable Income – Capital Gain) of the taxpayer.

## Tax Rates (2025)

Tax Rate	Single	Head of Household	Married MFJ / QW	MFS
10%	Up to \$11,925	Up to \$17,000	\$0 to \$23,850	Up to \$11,925
12%	\$11,926 to \$48,475	\$17,001 to \$64,850	\$23,851 to \$96,950	\$11,926 to \$48,475
22%	\$48,476 to \$103,350	\$64,851 to \$103,350	\$96,951 to \$206,700	\$48,476 to \$103,350
24%	\$103,351 to \$197,300	\$103,351 to \$197,300	\$206,701 to \$394,600	\$103,351 to \$197,300
32%	\$197,301 to \$250,525	\$197,301 to \$250,500	\$394,601 to \$501,050	\$197,301 to \$250,525
35%	\$250,526 to \$626,350	\$250,501 to \$626,350	\$501,051 to \$751,600	\$250,526 to \$375,800
37%	\$626,351 or more	\$626,351 or more	over \$751,601	\$375,801 or more

## Tax Credits

Tax Credit	Description	Credit Amount
<b>Refundable Credit</b>		
Child Tax Credit	Aids taxpayers with qualifying dependent children	Up to \$2,000 per qualifying child
American Opportunity Tax Credit	Education credit for qualified expenses in the first 4 years of college	Up to \$2,500 per eligible student
Earned Income Credit	Assistance for low-to-moderate-income individuals and families with earned income	Maximum credit amounts based on the number of qualifying children
Premium Tax Credit	Helps low-income individuals and families afford health insurance coverage.	Depending upon the taxpayer's income, the cost of coverage in the taxpayer's area, and the size of the taxpayer's household,
<b>Non-Refundable Credit</b>		
Adoption Credit	Helps with expenses incurred for adopting a child under 18 years of age	Limited to \$17,280 per child (for 2025)
Lifetime Learning Credit	Education credit for qualified expenses beyond the first 4 years of college	Up to \$2,000 per taxpayer
Dependent and Child Care Credit	Provides assistance for child and dependent care expenses	Percentage of qualifying expenses, up to \$3,000 for one dependent or \$6,000 for multiple dependents
Elderly and Disabled Credit	Credit for individuals over 65 years or permanently disabled	15% of Eligible Income
Credit for Other Dependents	Credit for eligible dependents that do not qualify for the Child Tax Credit	Up to \$500 per eligible dependent
Retirement Savings Contribution Credit	Credit for contributions to retirement savings accounts	Percentage of eligible contributions, up to \$2,000
Foreign Tax Credit	Credit for foreign income taxes paid to a foreign government	Actual foreign taxes paid, subject to foreign tax credit limitation
General Business Credits	Various credits available to businesses for qualifying activities	Varies depending on the type of credit
Residential Energy Credit	Credit for taxpayers who make energy-efficient improvements to their homes.	<ul style="list-style-type: none"> <li>Residential Clean Energy Credit: 30% of Qualified Energy-Efficient Improvements.</li> <li>Energy Efficient Home Improvement Credit: 10% of Qualified Energy-Efficient Improvements</li> </ul>
Credit for Electric Vehicles	Credit for taxpayers who purchase qualified Electric Vehicles.	Up to \$7,500.

## Other Taxes

- Federal Insurance Contributions Act (FICA) Tax & Self-Employment Tax

- Employee

	Employer's FICA Contribution	Employee's FICA Contribution	Total
FICA Social Security	6.2%	6.2%	12.4%
FICA Medicare	1.45%	1.45%	2.9%
<b>Total Contribution</b>	<b>7.65%</b>	<b>7.65%</b>	<b>15.3%</b>

- Withhold employees' shares from Wages
    - Employer's FICA Share is Deductible as a business expense.

- Self Employed Individuals

- Self-Employed Individuals are required to pay both Employee's and Employers' share of FICA which is equal to 15.3%.
    - Allowed to deduct the employer's portion of self-employment taxes (7.65%) paid by them which is 50% of total Self-Employment Taxes paid.

- Kiddie Tax

- The Kiddie Tax is a tax that applies to the unearned income of children
  - Applies to children under the age of 19 and certain full-time students under the age of 24.
  - A child is subject to kiddie tax if the following conditions are met:
    - Have net unearned income above \$2,700 (threshold amount for 2025).
    - The child did not pay for more than one-half of the support.

- Kiddie Tax Calculation

Child's Unearned Income	
(\$2,600)	
<b>Net Unearned Minor Income</b>	→ Taxed at Parent's Marginal Tax Rates

- Net Investment Income Tax
  - The Net Investment Income Tax (NIIT) is a 3.8% tax that applies to certain net investment income of individuals, estates, and trusts with income above the statutory threshold amounts.
  - Net Investment Income Tax Calculation
    - Net Investment Income Tax (NIIT) applies to the lesser of:
      - Net Investment Income
      - Amount by which Modified Adjusted Gross Income exceeds the thresholds:  
Modified Adjusted Gross Income - \$200,000 (Single) / \$250,000 (MFJ) / \$125,000 (MFS)

## Estimated Payments & Withholdings

- Estimated Payments
  - Estimated tax payments are typically due in four equal installments as follows:
    - 1st payment: April 15.
    - 2nd payment: June 15.
    - 3rd payment: September 15.
    - 4th payment: January 15 of the following year.
  - Penalty for Failure to Make Estimated Tax Payments
    - Penalty for underpayment of Estimated Taxes will not apply in the following circumstances:
      - Taxpayer owes less than \$1,000 on the tax return due date (April 15).
      - Estimated Tax Payments are equal to the lesser of:
        - ⇒ Withholding and Estimated Tax Payments is at least 90% of the Current Year Tax Liability.
        - ⇒ Withholding and Estimated Tax Payments are at least 100% of the Prior Year's Tax Liability (Withholding and Estimated Tax Payments are at least 110% of the Prior Year's Tax Liability if the Prior Year AGI was more than \$150,000)
      - Zero tax liability in the Prior Year.
- Withholdings
  - Income taxes that are withheld and paid directly by an individual's employer on their behalf.

# NINJA NOTES

## Tax Compliance & Planning 2026



### Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the TCP section of the Exam:

Area I	Tax Compliance and Planning for Individuals and Personal Financial Planning	30% - 40%
Area II	Entity Tax Compliance	30% - 40%
Area III	Entity Tax Planning	10% - 20%
Area IV	Property Transactions (disposition of assets)	10% - 20%

## Skill Allocation

Remembering and Understanding	5% - 15%
Application	55% - 65%
Analysis	25% - 35%
Evaluation	0% - 0%

## Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
TCP - Discipline	50%	50%

## Section Time and Question Type

The table below presents the design of the Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
TCP - Discipline	4 Hours	68	7

# Content

TCP-1 Individual Taxation & Planning

TCP-2 Property Taxation

TCP-3 C-Corporation Taxation

TCP-4 S-Corporation Taxation

TCP-5 Partnership Taxation

TCP-6 Comparison of Taxation of Business Entities

TCP-7 Gift Taxation

TCP-8 Trust Taxation

TCP-9 Tax-Exempt Organization Taxation

TCP-10 State and Local Tax Issues

# NINJA NOTES

## Tax Compliance & Planning 2026



## Individual Taxation & Planning

(July 1, 2025 – June 30, 2026 Exams)

## Copyright & Disclaimer

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

# Individual Taxation & Planning

## Overview of Individual Taxation

Gross Income
<Adjustments>
<b>Adjusted Gross Income (AGI)</b>
<Standard Deduction>
or
<Itemized Deductions>
<b>Taxable Income Before Qualified Business Income Deduction</b>
<Qualified Business Income Deduction>
<b>Taxable Income</b>
x Tax Rate
<b>Federal Income Tax</b>
< Tax Credits >
Alternative Minimum Tax
Self-Employment Tax
< Estimated Payments / Withholdings >
<b>Tax Due</b>

## Gross Income

Type of Income	Relevant Form(s)
Wages and Salaries (Salary Income)	Form W-2
Interest & Dividend (Portfolio Income)	Schedule B
Business Income or Loss (Business Income)	Schedule C
Capital Gains & Losses	Schedule D
Passive Income (Income from Pass-thru entities)	Schedule E
Farming Income	Schedule F
Other Miscellaneous Income	Schedule 1

## Stock Options

Type of Stock Options	Taxation
Qualified Stock Options	<p>Taxable when Sold:</p> <ul style="list-style-type: none"> <li>• <b>Sold:</b> Sales Price – Exercise Price</li> </ul>
Non-Qualified Stock Options	<p>Stock Option have Readily Determinable Fair Market Value:</p> <ul style="list-style-type: none"> <li>• <b>Granted:</b> Ordinary Income = FMV of Options on Grant Date – Cost</li> <li>• <b>Exercised:</b> No Tax on Exercise. Basis of Stock = Exercise Price + Income Recognized on Options on Grant Date</li> <li>• <b>Sold:</b> Capital Gain or Loss = Sales Price – Basis of Stock</li> <li>• <b>Lapsed:</b> Capital Loss = Income Recognized on Options on Grant Date.</li> </ul> <p>Stock Option that does not have Readily Determinable Fair Market Value:</p> <ul style="list-style-type: none"> <li>• <b>Granted:</b> No Tax on Grant</li> <li>• <b>Exercised:</b> Ordinary Income = FMV of Stock at Exercise Date – Exercise Price</li> <li>• <b>Sold:</b> Capital Gain or Loss = Sales Price - FMV of Stock at Exercise Date.</li> <li>• <b>Lapsed:</b> No Deduction on Lapse.</li> </ul>

## Restricted Stock, Restricted Stock Units and Stock Appreciation Rights

Type of Stock Rights	Taxation
Restricted Stock	<ul style="list-style-type: none"> <li>• <b>Granted:</b> No Tax on Grant (If an 83(b) election is made, the employee recognizes Ordinary Income equal to the FMV of the stock on the Grant Date)</li> <li>• <b>Vesting Date:</b> Ordinary Income = FMV of Options on Vesting Date</li> <li>• <b>Sold:</b> Capital Gain or Loss = Sales Price – Basis of Stock</li> <li>• <b>Forfeited:</b> No Tax Consequence on Forfeiture</li> </ul>
Restricted Stock Units (RSUs)	<ul style="list-style-type: none"> <li>• <b>Granted:</b> No Tax on Grant</li> <li>• <b>Vesting Date:</b> Ordinary Income = FMV of Options on Vesting Date</li> <li>• <b>Sold:</b> Capital Gain or Loss = Sales Price – Basis of Stock</li> <li>• <b>Forfeited:</b> No Tax Consequence on Forfeiture</li> </ul>
Stock Appreciation Rights (SARs)	<ul style="list-style-type: none"> <li>• <b>Granted:</b> No Tax on Grant</li> <li>• <b>Vesting Date:</b> Ordinary Income = FMV on Exercise Date – FMV on Grant Date</li> <li>• <b>Sold:</b> Capital Gain or Loss = Sales Price – FMV on Exercise Date</li> <li>• <b>Forfeited:</b> No Tax Consequence on Forfeiture</li> </ul>

## Imputed Interest on Below Market Rate Loan

- If a taxpayer makes a loan to someone with little or no interest, the IRS treats it as if the taxpayer had charged Market Rate Interest and then gifted the value of that interest back to the borrower.
- The difference between the interest the taxpayer should have charged at the AFR and the interest the taxpayer actually charged is the Imputed Interest. This Imputed Interest is considered income to the lender, even though they never received it.
  - $\text{Imputed Interest Income} = \text{Principal Amount} \times (\text{AFR} - \text{Interest Rate})$

## Compensation Earned while Employed Outside US

- IRS imposes taxes on the worldwide income of U.S. citizens and resident aliens, regardless of where they live or work.
- To mitigate the risk of double taxation the IRS provides some relief in the form of the Foreign Earned Income Exclusion up to \$130,000 (for 2025) of their foreign earned income from U.S. taxation.
  - Requirements
    - The taxpayer must have foreign earned income.
    - The taxpayer must have a tax home in a foreign country.
    - The taxpayer must meet either the Bona Fide Residence Test or the Physical Presence Test.
      - Bona Fide Residence Test
        - ⇒ A Taxpayer is a bona fide resident of a foreign country if the taxpayer resides in that country for an uninterrupted period that includes an entire tax year.
      - Physical Presence Test
        - ⇒ Taxpayers meet this test if they are physically present in a foreign country (or countries) for at least 330 full days during a 12-month period.
  - In addition to the Foreign Earned Income Exclusion, U.S. taxpayers may also qualify for the Foreign Housing Exclusion or Deduction. This can exclude or deduct certain amounts for household expenses that occur as a consequence of living abroad.

## Passive Activity Loss Limitations

- Passive Activities include the following:
  - Income from Rental Real Estate Activities
  - Income from Royalties
  - Income from Closely Held C-Corporations and Personal Service Corporations
  - Income from Schedule K-1 (Pass-through Income)
    - Partnerships and Limited Liability Companies (LLCs)
    - S-Corporations
    - Estates and Trusts

- Income from Rental Real Estate Activities

- Rental Income: Active vs. Passive

	Income Type	Reporting Form
Materially Participating & Real Estate Professional	Active	Schedule C (Form 1040)
No Material Participation or Non-Real Estate Professional	Passive	Schedule E (Form 1040)

- Passive Activity Loss Offset Rules

- Passive Activity Losses (PAL) can generally be offset against passive income only.
    - Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed of.
    - Exceptions:

- Active Participation

AGI Range	Offset Limitation
\$100,000 or less	\$25,000
Between \$100,000 and \$150,000	$\$25,000 - 50\% \times (\text{AGI} - \$100,000)$
\$150,000 or more	\$0

- Material Participation

- ⇒ Rental losses are fully deductible against all types of income without any limitations.

- Income from S-Corporations (Loss Limitations)

- Income, deductions, and credits from S Corporations are reported on Schedule E of Form 1040.

- Passive Activity Losses (PAL) from S-Corporation can be offset against passive income only. Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed.

- Shareholder's Stock Basis in S-Corporation

$$\text{Stock Basis} = \text{Contributions} + \text{Income} - \text{Distributions} - \text{Deductions and Losses}$$

- Shareholder's Debt Basis in S-Corporation

$$\text{Debt Basis} = \text{Loans made by a Shareholder to S-Corporation}$$

- Shareholder's Tax Basis (At-Risk Basis) in S-Corporation

$$\text{Tax Basis} = \text{Stock Basis} + \text{Debt Basis}$$

- Shareholder's At-Risk Basis in S-Corporation

$$\text{At-Risk Basis} = \text{Tax Basis}$$

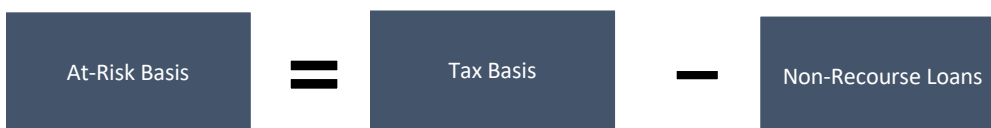
- S-Corporation Shareholders Limitations on Loss Deduction
  - Tax Basis Limitation
    - Shareholder can only claim a loss to the extent of their Tax Basis in their S-Corporation which is the sum of Stock and Debt basis.
    - Tax Basis Limitation will apply even in case of Material Participation.
    - Excess Loss is suspended and carried forward to future years.
    - Suspended Losses due to Tax Basis Limitation are no longer deductible once the activity is disposed of.
  - At-Risk Basis
    - At-Risk Basis further limit the amount of loss a shareholder can claim.
    - At-Risk Limitation will apply even in case of Material Participation.
    - Excess Loss is suspended and carried forward to future years.
    - Suspended Losses due to At-Risk Limitation will reduce Gain from Sale when the activity is disposed of.
  - Passive Activity Loss (PAL) Limitation
    - Passive Activity Loss are limited to Passive Activity Income.
    - Passive Activity Loss Limitation will not apply in case of Material Participation.
    - Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed.
    - Suspended Passive Activity Losses is deductible from all other sources of Income in the year of disposal.
  - Excess Business Loss Limitation
    - An Excess Business Loss is calculated as the amount by which the Total Deductions from all trades or businesses exceed the Total Gross Income from those trades or businesses over the threshold amount.
    - For 2025, the threshold limit is \$313,000 for single filers and \$626,000 for married filing jointly.
    - Any loss in excess of these amounts is treated as a Net Operating Loss Carryforward.
    - Excess Business Loss Limitation will apply even in case of Material Participation.

- Income from Partnerships (Loss Limitations)

- Partnerships are pass-through entities. Income, deductions, and credits from Partnerships are reported on Schedule E of Form 1040.
- Passive Activity Losses (PAL) from Partnerships can be offset against passive income only. Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed.
- Partner's Tax Basis in Partnership



- Partner's At-Risk Basis in Partnership



- Partner's Limitations on Loss Deduction

- Tax Basis Limitation

- Partners can only claim a loss to the extent of their Tax Basis in their Partnership.
    - Tax Basis Limitation will apply even in case of Material Participation.
    - Excess Loss is suspended and carried forward to future years.
    - Suspended Losses due to Tax Basis Limitation are no longer deductible once the activity is disposed of.

- At-Risk Basis

- At-Risk Basis further limit the amount of loss a Partner can claim.
    - At-Risk Limitation will apply even in case of Material Participation.
    - Excess Loss is suspended and carried forward to future years.
    - Suspended Losses due to At-Risk Limitation will reduce Gain from Sale when the activity is disposed of.

- Passive Activity Loss (PAL) Limitation
  - Passive Activity Loss are limited to Passive Activity Income.
  - Passive Activity Loss Limitation will not apply in case of Material Participation.
  - Excess Passive Activity Losses (PAL) are carried forward indefinitely or until the activity is disposed.
  - Suspended Passive Activity Losses is deductible from all other sources of Income in the year of disposal.
  
- Excess Business Loss Limitation
  - An Excess Business Loss is calculated as the amount by which the Total Deductions from all trades or businesses exceed the Total Gross Income from those trades or businesses over the threshold amount.
  - For 2025, the threshold limit is \$313,000 for single filers and \$626,000 for married filing jointly.
  - Any loss in excess of these amounts is treated as a Net Operating Loss Carryforward.
  - Excess Business Loss Limitation will apply even in case of Material Participation.

## Standard Deduction & Itemized Deductions

- Standard Deduction

- Standard Deduction Limits (for 2025)

Filing Status	Standard Deduction
Single/Married Filing Separately	\$15,000
Married Filing Jointly/Qualifying Widow(er)	\$30,000
Head of Household	\$22,500

- Additional Standard Deduction (for 2025)

	Single	Married Filing Jointly
<b>Single / Only 1 Spouse Qualify</b>		
65 or Blind	\$2,000	\$1,600
65 and Blind	\$4,000	\$3,200
<b>Both Spouses Qualify</b>		
Each 65 or Blind	-	\$3,200
Both 65 and Blind	-	\$6,400

- Standard Deduction – Individuals Claimed as Dependents

- For dependents of others, the standard deduction is the greater of \$1,350 or earned income + \$450 for 2025 but must not exceed the regular standard deduction.

- Itemized Deductions

- Medical Expenses (In Excess of 7.5% of AGI)

- Qualified and Non-Qualified Medical Expenses

Qualified Medical Expenses	Non-Qualified Medical Expenses
<ul style="list-style-type: none"> <li>• Prescribed drugs and medicines.</li> </ul>	<ul style="list-style-type: none"> <li>• Over-the-counter drugs not prescribed by a physician</li> </ul>
<ul style="list-style-type: none"> <li>• Fees paid to medical practitioners, including doctors, dentists, and surgeons.</li> </ul>	<ul style="list-style-type: none"> <li>• General health costs, like Gym Memberships and Health Club Membership, that aren't prescribed by a physician for a specific health condition</li> </ul>
<ul style="list-style-type: none"> <li>• Travel Costs for Medical Care (Actual Costs or Standard Mileage Rate of \$0.21/mile for 2025)</li> </ul>	<ul style="list-style-type: none"> <li>• Personal hygiene items and ordinary personal care expenses.</li> </ul>
<ul style="list-style-type: none"> <li>• Meals and Lodging provided by a hospital or similar institution during medical treatment.</li> </ul>	<ul style="list-style-type: none"> <li>• Household help.</li> </ul>

<ul style="list-style-type: none"> <li>• Stop-Smoking Programs</li> </ul>	<ul style="list-style-type: none"> <li>• Illegal operations or treatments.</li> </ul>
<ul style="list-style-type: none"> <li>• Weight-Loss Programs (only if the purpose is to treat obesity or other disease)</li> </ul>	<ul style="list-style-type: none"> <li>• Cosmetic surgery purely for aesthetic reasons.</li> </ul>
<ul style="list-style-type: none"> <li>• Surgery including plastic/cosmetic surgery done to cure the disfiguring injury, illness, or birth defects.</li> <li>• LASIK surgery</li> </ul>	<ul style="list-style-type: none"> <li>• The Medicare portion of Social Security and Self-Employment Taxes.</li> </ul>
<ul style="list-style-type: none"> <li>• Insurance Premiums for Medical, Dental, Hospital care, and Qualifying Long-Term Care Policies</li> </ul>	<ul style="list-style-type: none"> <li>• Insurance premiums for Accident, Disability, and Life Insurance.</li> </ul>
<ul style="list-style-type: none"> <li>• Medical Equipment and devices like eyeglasses, hearing aids, false teeth, etc.</li> </ul>	<ul style="list-style-type: none"> <li>• Funeral and Burial Expenses.</li> </ul>
<ul style="list-style-type: none"> <li>• Costs to install medically prescribed facilities or remove structural barriers at home for physically handicapped such as swimming pool, elevator, etc. ⇒ Deduction = Cost of Home Improvement – Increase in FMV</li> </ul>	

▪ Calculation of Deductible Medical Expenses

Qualified Medical Expense	XXX
<Insurance/Employer Reimbursement>	(XXX)
<b>Medical Expense Paid</b>	<b>XXX</b>
<7.5% of AGI>	(XXX)
<b>Deductible Medical Expenses</b>	<b>XXX</b>

○ State/Local/Foreign Taxes (SALT) paid (up to \$10,000)

Deductible Taxes	Non-Deductible Taxes
<ul style="list-style-type: none"> <li>• State and Local Income Taxes or State and Local Sales Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Federal Income Tax</li> </ul>
<ul style="list-style-type: none"> <li>• State and Local Personal and Real Property Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Federal, State, and Local Estate or Gift Taxes</li> </ul>
<ul style="list-style-type: none"> <li>• Foreign Income Tax</li> </ul>	<ul style="list-style-type: none"> <li>• Social Security and Self-Employment Taxes</li> </ul>
	<ul style="list-style-type: none"> <li>• Business Taxes.</li> </ul>
	<ul style="list-style-type: none"> <li>• Foreign Sales Tax, Real Property Tax, and Personal Property Tax</li> </ul>

o Interest Expense

Deductible Interest	Non-Deductible Interest
<ul style="list-style-type: none"> <li>Home Mortgage Interest for loans up to \$750,000</li> </ul>	<ul style="list-style-type: none"> <li>Personal Consumer Interest</li> </ul>
<ul style="list-style-type: none"> <li>Investment Interest Expense limited to net investment income</li> </ul>	<ul style="list-style-type: none"> <li>Education Loan Interest</li> </ul>
<ul style="list-style-type: none"> <li>Home Equity Loans</li> </ul>	<ul style="list-style-type: none"> <li>Prepaid Interest</li> </ul>

o Charitable Contributions

- Allowed as an itemized deduction on Schedule A up to 60% of AGI.
- Deductible and Non-Deductible Charitable Contribution

Deductible Charitable Contribution	Non-Deductible Charitable Contribution
<ul style="list-style-type: none"> <li>Charitable Contributions to Qualified Domestic Organizations for religious, charitable, scientific, literary, or educational purposes.</li> </ul>	<ul style="list-style-type: none"> <li>Contributions to individuals or non-qualified organizations civic leagues, social clubs, foreign organizations, political organizations, communist organizations, chambers of commerce, and labor unions.</li> </ul>
<ul style="list-style-type: none"> <li>Out-of-pocket costs incurred while doing work for a charitable organization.</li> </ul>	<ul style="list-style-type: none"> <li>Cannot deduct the value of taxpayer's time or services that taxpayer donates to a charitable organization.</li> </ul>
<ul style="list-style-type: none"> <li>\$50 per student per month for every completed month of an unrelated student staying in a taxpayer's home on agreement with a qualified organization.</li> </ul>	<ul style="list-style-type: none"> <li>Cannot deduct the value of the use of a property that the taxpayer allows to a charitable organization.</li> </ul>
	<ul style="list-style-type: none"> <li>Cannot deduct the value of Blood Donation</li> </ul>

- Charitable Contribution Deduction Calculation

Charitable Contribution	XXX
<Benefits Received>	(XXX)
Charitable Contribution Deduction	XXX

- Charitable Contribution Limits

Contribution Type	Deduction	Deduction Limit
Cash	Amount Contributed	Up To 60% of Adjusted Gross Income (AGI)
Short-Term Property	Lower of Basis or FMV of Property	Up To 50% of Adjusted Gross Income (AGI)
Long-Term Property	FMV of Property	Up To 30% of Adjusted Gross Income (AGI)

- Casualty Losses (In Excess of 10% of AGI)

- Deductible and Non-Deductible Casualty Losses

Deductible Casualty Losses	Non-Deductible Casualty Losses
<ul style="list-style-type: none"> <li>• Personal Property Losses that occurred due to a Federally Declared Disaster</li> </ul>	<ul style="list-style-type: none"> <li>• Business Property Losses that occurred due to a Federally Declared Disaster</li> </ul>
	<ul style="list-style-type: none"> <li>• Progressive Damage that happens over time, such as wear and tear or deterioration.</li> </ul>
	<ul style="list-style-type: none"> <li>• Casualty Insurance Premiums for insurance coverage</li> </ul>
	<ul style="list-style-type: none"> <li>• Incidental Expenses such as temporary housing, meals, and transportation costs incurred due to a casualty or disaster, but not directly related to the damage or destruction of property, are not deductible as a casualty loss.</li> </ul>

- Casualty Loss Deduction Calculation

Drop in FMV (Limited to Tax Basis of the Asset)	XXX
<Insurance/Government Reimbursement>	(XXX)
<\$100 per event>	(\$100)
<b>Loss Eligible for Deduction</b>	<b>XXX</b>
<10% of AGI>	(XXX)
<b>Deductible Casualty Loss</b>	<b>XXX</b>

- Other Itemized Deductions

- Gambling Losses
  - Taxes for Decedent

- Itemized Deductions or Standard Deduction

Itemized Deductions < Standard Deductions	Standard Deduction
Itemized Deductions > Standard Deductions	Itemized Deduction

- The Taxpayer Should Take the Standard Deduction
  - Standard Deduction is Greater than Itemized Deductions
  - Simplicity
- The Taxpayer Should Itemize Deductions
  - Itemized Deductions are Greater than Standard Deduction
  - State Tax Considerations
  - Married Filing Separately
    - If a taxpayer is married and files separately, and if one spouse itemizes deductions, then the other spouse must also itemize their deductions.
  - Qualifying for a Mortgage or Other Loan
    - Some financial institutions may request to see itemized deductions as part of the process for qualifying for a mortgage or other type of loan.

## Alternative Minimum Tax (AMT)

- The Alternative Minimum Tax (AMT) is a separate tax system in the United States that operates parallel to the regular income tax system.
- It is designed to ensure that high-income individuals, corporations, and certain taxpayers with substantial deductions or tax preferences pay at least a minimum amount of tax.
- AMT Calculation

<b>Regular Taxable Income</b>
Add/Less: Adjustments
Add: Preferences
<b>Alternative Minimum Taxable Income (AMTI)</b>
<AMT Exemptions>
<b>AMT Tax Base</b>
x Tax Rate (26% to 28%)
<b>Tentative AMT</b>
<Regular Tax>
<b>AMT</b>

- Adjustments (Increases or Decreases AMTI)

Adjustments	Explanation
Recalculate Losses	<ul style="list-style-type: none"> <li><b>Passive Activity Losses:</b> Recalculate for AMT purposes.</li> <li><b>Net Operating Losses:</b> Recalculate according to AMT rules.</li> </ul>
Adjust Accounting Methods	<ul style="list-style-type: none"> <li><b>Long-Term Contracts:</b> Adjust for the difference between percentage-of-completion for AMT and other methods for regular tax purposes.</li> <li><b>Installment Sales:</b> Adjust for the difference between full accrual for AMT and installment sales revenue for regular tax purposes.</li> </ul>
Adjust Depreciation on Post-1986 Property	<ul style="list-style-type: none"> <li><b>Real Property:</b> Adjust the difference between straight-line depreciation (40-year life) for AMT and other methods used for regular tax purposes.</li> <li><b>Personal Property:</b> Adjust the difference between 150% declining balance depreciation for AMT and other methods used for regular tax purposes.</li> </ul>
Add-back Standard and Certain Itemized Deductions	<ul style="list-style-type: none"> <li><b>Taxes:</b> Add-back non-deductible state and local taxes under AMT rules.</li> <li><b>Standard Deduction:</b> Add-back if claimed for regular tax purposes</li> </ul>
Incentive Stock Options (ISOs)	<ul style="list-style-type: none"> <li>Taxed upon exercise for AMT purposes. Carryforward AMT tax to be deducted in the year of ISOs sale.</li> </ul>

- Preferences (Increases AMTI)

Preferences	Explanation
Depreciation on Pre-1987 Property	<ul style="list-style-type: none"> <li>Add back excess accelerated depreciation over straight-line depreciation.</li> </ul>
Interest on Private Activity Bonds	<ul style="list-style-type: none"> <li>Add back tax-exempt interest from private activity bonds.</li> </ul>
Percentage Depletion	<ul style="list-style-type: none"> <li>Add back excess depletion deductions over the property's adjusted basis.</li> </ul>

- AMT Exemptions

	Single	Married filing jointly	Married filing separately
Exemption Amount	\$88,100	\$137,000	\$68,650
Income at which exemption begins to phase out	\$626,350	\$1,252,700	\$626,350

- o AMT Exemption for 2025 will be calculated as follows:

- For MFJ taxpayers, the exemption is  $\$137,000 - 25\% \times (\text{AMTI before exemption} - \$1,252,700)$ .
  - For Single taxpayers, the exemption is  $\$88,100 - 25\% \times (\text{AMTI before exemption} - \$626,350)$ .

- AMT Tax Rates

Filing Status	26%	28%
MFJ / Single	\$0 - \$239,100	plus 28% on the excess >\$239,100

## Taxes on Investment Income

- Kiddie Tax

- The Kiddie Tax is a tax that applies to the unearned income of children.
- Applies to children under the age of 19 and certain full-time students under the age of 24.
- A child is subject to kiddie tax if the following conditions are met:
  - Have net unearned income above \$2,700 (threshold amount for 2025).
  - The child did not pay for more than one-half of the support.
- Kiddie Tax Calculation



- Net Investment Income Tax

- The Net Investment Income Tax (NIIT) is a 3.8% tax that applies to certain net investment income of individuals, estates, and trusts with income above the statutory threshold amounts.
- Net Investment Income Tax Calculation
  - Net Investment Income Tax (NIIT) applies to the lesser of:
    - Net Investment Income
    - Amount by which Modified Adjusted Gross Income exceeds the thresholds:  
Modified Adjusted Gross Income - \$200,000 (Single) / \$250,000 (MFJ) / \$125,000 (MFS)

## Estimated Payments

- Estimated Payments
  - Estimated tax payments are typically due in four equal installments as follows:
    - 1st payment: April 15.
    - 2nd payment: June 15.
    - 3rd payment: September 15.
    - 4th payment: January 15 of the following year.
  - Penalty for Failure to Make Estimated Tax Payments
    - Penalty for underpayment of Estimated Taxes will not apply in the following circumstances:
      - Taxpayer owes less than \$1,000 on the tax return due date (April 15).
      - Estimated Tax Payments are equal to the lesser of:
        - Withholding and Estimated Tax Payments is at least 90% of the Current Year Tax Liability.
        - Withholding and Estimated Tax Payments are at least 100% of the Prior Year's Tax Liability (Withholding and Estimated Tax Payments are at least 110% of the Prior Year's Tax Liability if the Prior Year AGI was more than \$150,000)
      - Zero tax liability in the Prior Year.

## Impact of Changing Tax Rates and Legislation

- Impact of Changes in Tax Rates
  - Tax Rates to Increase in the Future
    - Accelerating Income
      - Offer Early Payment Incentives
      - Close Deals Before Year-End
    - Delaying Expenses
      - Deferring Purchases
      - Deferring Charitable Donations

- Tax Rates to Decrease in Future
  - Deferring Income
    - Delay Billing
    - Defer Bonuses
  - Accelerating Expenses
    - Prepay Deductible Expenses
    - Accelerate Purchases
    - Contribute to Retirement Accounts
    - Charitable Donations
- Impact of Changes in Tax Legislation

	Income	Expenses
Taxes Increase	Accelerate	Defer
Taxes Decrease	Defer	Accelerate

## Tax Planning for Individuals

- Medical Expense Planning
  - Flexible Spending Account (FSA)
    - Definition
      - Flexible Spending Arrangements (FSAs) are tax-advantaged accounts offered by employers to help employees pay for qualified medical or dependent care expenses.
    - Tax-Deductible
 

Contributions	Deductible
Withdrawal	Non-Taxable
    - How does an FSA Work?
      - Flexible Spending Account (FSA) is usually set up through an employer's benefits program.
      - Employees decide how much money they want to contribute to the FSA for the upcoming plan year.

- Employees make tax-deductible contributions to Flexible Spending Account (FSA)
- When employees have eligible expenses, they can use the funds in their FSA to pay for them.
- FSAs generally operate on a "use-it-or-lose-it" basis, meaning taxpayers need to use all the money in the FSA within the plan year or forfeit the remaining balance.
- Types of FSAs
  - Healthcare FSA
  - Dependent Care FSA
- Contributions Limits
  - Healthcare FSA
    - ⇒ Individuals: \$3,300 (for 2025)
    - ⇒ Families: \$6,600 (for 2025)
  - Dependent Care FSA
    - ⇒ Single & MFJ: \$5,000 (for 2025)
    - ⇒ MFS: \$2,500 (for 2025)
- Health Savings Account (HSA)
  - Definition
    - Health Savings Accounts (HSA) are tax-advantaged accounts designed to help employees save for and cover qualified medical expenses.
  - Eligibility
    - Covered under a High Deductible Health Plan (HDHP)
    - No Other Health Coverage
    - Not Enrolled in Medicare
    - Not Claimed as a Dependent

- Tax-Deductible

Contributions	Deductible
Withdrawal	Non-Taxable

- How does an HSA Work?
  - HSAs can be set up through a qualified HSA trustee, which could be a bank, an insurance company, or any company approved by the IRS,
  - Contributions to an HSA can be made by the individual, the individual's employer, or both, up to the maximum annual limit set by the IRS.
  - The funds in an HSA can be used tax-free for qualified medical expenses.
  - HSAs are portable, meaning that they stay with the individual even if they change employers or leave the workforce.
  - Unused funds in an HSA rollover from year to year, providing an opportunity to save for future medical expenses.
- Contributions Limits
  - Individuals: \$4,300 (for 2025)
  - Families: \$8,550 (for 2025)

- Retirement Planning

- Steps in Retirement Planning

- Set Retirement Goals
- Assess Current Financial Situation
- Estimate Retirement Income Needs
- Choose Retirement Savings Vehicles
  - Traditional IRA
  - Non-Deductible IRA
  - Roth IRA
  - Simplified Employee Pension (SEP) IRA
  - Savings Incentive Match Plan for Employees (SIMPLE) IRA

- 401(k)s
- Defined Benefit Plans
- Manage Investment Portfolio.
- Monitor and Adjust
- Social Security Optimization
- Traditional IRA
  - How Does a Traditional IRA Work?
    - Establishment
      - ⇒ Choosing a Provider
      - ⇒ Opening an Account
      - ⇒ Selecting Investments
      - ⇒ Contributions
    - Deductible Contributions
      - ⇒ Contribution Limits
        - Contribution Limit is Lesser of:
          - ✓ \$7,000 (Single) & \$14,000 (MFJ) (for 2025)
          - ✓ Earned Income (Wage, Business & Alimony)
          - ✓ An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.
      - ⇒ Tax Credit on Contribution
        - Contribution to IRA allows Retirement Savings Contribution Credit for up to 50% on \$2,000 Contribution for Low-Income Groups
    - Distributions
      - ⇒ Distribution
        - Principal: Taxable
        - Interest: Taxable

⇒ Distributions can occur after the individual reaches the age 59 ½ without incurring a penalty.

⇒ Penalties on Early Withdrawal

- 10% Penalty in addition to Income Tax would apply on early withdrawal.
- No Penalty would apply on Qualified Early Withdrawal to meet the following expenses:
  - ✓ Medical Expenses in excess of 7.5% of AGI
  - ✓ Medical Insurance for 12 Weeks Unemployed
  - ✓ Disability
  - ✓ Higher Education Qualified Expenses for Individuals, Spouses, Children, or Grandchildren.
  - ✓ First-time Home Purchase.

⇒ Required Minimum Distributions (RMDs)

- Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.

○ Non-Deductible IRA

▪ How Does a Non-Deductible IRA Work?

➤ Establishment

⇒ Choosing a Provider

⇒ Opening an Account

⇒ Selecting Investments

➤ Contribution

⇒ Non-Deductible Contributions

⇒ Contribution Limits

- Contribution Limit is Lesser of:
  - ✓ \$7,000 (Single) & \$14,000 (MFJ) (for 2025)

- ✓ Earned Income (Wage, Business & Alimony)
- ✓ An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.

➤ Distribution

⇒ Distribution

- Principal: Non-Taxable
- Interest: Taxable

⇒ Distribution Age Limits

- Distributions can occur after the individual reaches the age 59 ½ without incurring a penalty.

⇒ Penalties on Early Withdrawal

- A 10% Penalty and Income Tax on Earnings would apply on early withdrawal.
- No Penalty and Taxes would apply on Qualified Early Withdrawal to meet the following expenses:
  - ✓ Medical Expenses in excess of 7.5% of AGI
  - ✓ Medical Insurance for 12 Weeks Unemployed
  - ✓ Disability
  - ✓ Higher Education Qualified Expenses for Individuals, Spouses, Children, or Grandchildren.
  - ✓ First-time Home Purchase.

⇒ Required Minimum Distributions (RMDs)

- Individuals must start taking RMDs from Non-Deductible IRA by April 1 of the year following the year in which they turn 73.

- Roth IRA
  - How does a Roth IRA Work?
    - Establishment
      - ⇒ Determine Eligibility
        - To contribute to a Roth IRA, Income must be below the following level for 2025:
          - ✓ Single/Head of Household: \$165,000
          - ✓ Married Filing Jointly/Surviving Spouse: \$246,000
      - ⇒ Choosing a Provider
      - ⇒ Opening an Account
      - ⇒ Selecting Investments
    - Contribution
      - ⇒ Non-Deductible Contributions
      - ⇒ Contribution Limits
        - Contribution Limit is Lesser of:
          - ✓ \$7,000 (Single) & \$14,000 (MFJ) (for 2025)
          - ✓ Earned Income (Wage, Business & Alimony)
          - ✓ An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.
      - ⇒ Tax Credit on Contribution
        - Contribution to IRA allows Retirement Savings Contribution Credit for up to 50% on \$2,000 Contribution for Low-Income Groups
    - Distribution
      - ⇒ Distribution
        - Principal: Non-Taxable
        - Interest: Non-Taxable

⇒ Distribution Age Limits

- Qualified withdrawals from a Roth IRA are tax-free.
  - ✓ Must occur at least five years after the first contribution to the Roth IRA
  - ✓ Distribution occurs after you've reached age 59 ½.

⇒ Penalties on Early Withdrawal

- 10% Penalty and Income Tax on Earnings would apply on early withdrawal.
- No Penalty and Taxes would apply on Qualified Early Withdrawal to meet the following expenses:
  - ✓ Medical Expenses in excess of 7.5% of AGI
  - ✓ Medical Insurance for 12 Weeks Unemployed
  - ✓ Disability
  - ✓ Higher Education Qualified Expenses for Individuals, Spouses, Children, or Grandchildren.
  - ✓ First-time Home Purchase.

⇒ No Required Minimum Distributions (RMDs)

○ Simplified Employee Pension (SEP) IRA

▪ Definition

- A Simplified Employee Pension (SEP) IRA is a retirement savings plan established by employers including self-employed individuals for the benefit of their employees.
- Employers can contribute up to 25% of an employee's compensation or \$70,000 (whichever is less) each year.

▪ How does a SEP IRA Work?

➤ Establishment

- ⇒ Adopt a Written Agreement
- ⇒ Choose a Financial Institution
- ⇒ Set Up SEP IRAs

⇒ Provide Information to Employees

⇒ Employee Controls the Investment

➤ Contributions

⇒ Deductible Contributions

⇒ Contribution Limits:

Contribution Limit for each employee is Lesser of:

✓ 25% of Employee's Compensation

✓ \$70,000 (for 2025)

⇒ Equal Percentage

If an employer chooses to contribute in a given year, they must contribute an equal percentage of salary for each eligible employee.

⇒ Immediate Vesting

➤ Distributions

⇒ Distribution

Principal: Taxable

Interest: Taxable

⇒ Distribution Age Limits

Distributions can occur after the individual reaches the age 59 ½ without incurring a penalty.

⇒ Penalties on Early Withdrawal

10% Penalty in addition to Income Tax would apply on early withdrawal.

No Penalty would apply on Qualified Early Withdrawal to meet the following expenses:

✓ Medical Expenses in excess of 7.5% of AGI

✓ Medical Insurance for 12 Weeks Unemployed

✓ Disability

- ✓ Higher Education Qualified Expenses for Individuals, Spouses, Children, or Grandchildren.
- ✓ First-time Home Purchase.

⇒ Required Minimum Distributions (RMDs)

- Individuals must start taking RMDs from SEP IRA by April 1 of the year following the year in which they turn 73.

○ Savings Incentive Match Plan for Employees (SIMPLE) IRA

▪ Definition

- A Savings Incentive Match Plan for Employees (SIMPLE) IRA is a retirement savings plan that small businesses with 100 or fewer employees can set up.

▪ How does a SIMPLE IRA Work?

➤ Establishment

⇒ Eligibility

- A business can use a SIMPLE IRA plan if it has 100 or fewer employees.

⇒ Adopt a Written Agreement

⇒ Choose a Financial Institution

⇒ Set Up SIMPLE IRAs

⇒ Employee Controls the Investment

➤ Contributions

⇒ Deductible Contributions

⇒ Contribution Limits

- Employees

- ✓ Employees can contribute up to a maximum of \$16,500 (for 2025).
- ✓ An additional \$3,000 Contribution is allowed for Individuals aged 50 and above.

- Employers
  - ✓ Match Contributions up to 3% of an Employee's Compensation.
  - or
  - ✓ Non-Elective Contributions up to 2% of an Employee's Compensation
- ⇒ Immediate Vesting
- Distributions
  - ⇒ Distribution
    - Principal: Taxable
    - Interest: Taxable
  - ⇒ Distribution Age Limits
    - Distributions can occur after the individual reaches age 59 ½ without incurring a penalty.
  - ⇒ Penalties on Early Withdrawal
    - 10% Penalty in addition to Income Tax would apply on early withdrawal.
    - No Penalty would apply on Qualified Early Withdrawal to meet the following expenses:
      - ✓ Medical Expenses in excess of 7.5% of AGI
      - ✓ Medical Insurance for 12 Weeks Unemployed
      - ✓ Disability
      - ✓ Higher Education Qualified Expenses for Individuals, Spouses, Children, or Grandchildren.
      - ✓ First-time Home Purchase.
  - ⇒ Required Minimum Distributions (RMDs)
    - Individuals must start taking RMDs from SIMPLE IRA by April 1 of the year following the year in which they turn 73.

- 401(k)s
  - Definition
    - A 401(k) plan is an employer-sponsored defined-contribution retirement savings plan that allows employees to contribute a portion of their pre-tax salary to the plan.
  - How does a 401(k) Work?
    - Establishment
      - ⇒ Choose a Plan Type
        - Traditional 401(k)
        - Safe Harbor 401(k),
        - SIMPLE 401(k)
        - Roth 401(k).
      - ⇒ Select a Plan Provider
      - ⇒ Create a Written Plan Document
      - ⇒ Set Up a Trust for the Plan's Assets
      - ⇒ Provide Plan Information to Employees
    - Contributions
      - ⇒ Deductible Contributions
      - ⇒ Contribution Limits
        - Employees
          - ✓ Employees can contribute up to a maximum of \$23,500 (for 2025). An additional \$7,500 Contribution is allowed for Individuals aged 50 and above.
        - Employers
          - ✓ Employers are not required to make matching contributions to 401(k) plans, but many employers do.
      - ⇒ Based on Vesting Schedule

➤ Distributions

⇒ Distribution

- Principal: Taxable
- Interest: Taxable

⇒ Distribution Age Limits

- Distributions can occur after the individual reaches age 59 ½ without incurring a penalty.

⇒ Penalties on Early Withdrawal

- 10% Penalty in addition to Income Tax would apply on early withdrawal.
- No Penalty would apply on Qualified Early Withdrawal to meet the following expenses:
  - ✓ Medical Expenses in excess of 7.5% of AGI
  - ✓ Medical Insurance for 12 Weeks Unemployed
  - ✓ Disability

⇒ Required Minimum Distributions (RMDs)

- Individuals must start taking RMDs from 401(k) IRA by April 1 of the year following the year in which they turn 73.

- Defined Benefit Plans
  - Definition
    - Defined Benefit Plans, also known as Pension Plans, are employer-sponsored retirement plans that promise a specified monthly benefit to employees upon their retirement.
  - Characteristics
    - Employer Funding
    - Guaranteed Retirement Benefit
    - Investment Responsibility
    - Actuarial Assumptions
    - Vesting and Retirement Age
    - Annuity Payments

- Annuities
  - Annuities are long-term, tax-advantaged contracts where earnings accumulate on a Tax-Deferred Basis.
  - Immediate Annuities
    - An Immediate Annuity is purchased with a lump-sum payment, and in exchange, the taxpayer begins receiving income almost immediately, typically within 30 days or no later than one year.
  - Deferred Annuities
    - Deferred Annuities have two distinct phases
      - ⇒ Accumulation Phase
        - During this phase, premiums (or contributions) are made into the annuity, which grows on a tax-deferred basis.
      - ⇒ Payout Phase
        - Income payments begin in the payout phase.
  - Tax Treatment of Annuity Payments
    - Fixed Period Annuity Payments
      - ⇒ A Fixed Period Annuity provides payments for a set period of time, such as 10 or 20 years.
        - $\text{Exclusion Ratio} = \text{Original Investment} / \text{Total Expected Value of Annuity Payments}$
        - $\text{Non-Taxable Portion} = \text{Monthly Payment} \times \text{Exclusion Ratio}$
        - $\text{Taxable Portion} = \text{Monthly Payment} - \text{Non-Taxable Portion}$
    - Life Annuity Payments
      - ⇒ In a Life Annuity, the exact number of payments the taxpayer will receive is unknown because it depends on how long the taxpayer lives.
        - $\text{Non-Taxable Portion} = \text{Original Investment} / \text{IRS Life Expectancy Factor}$

	Traditional IRA	Non-Deductible IRA	Roth IRA	SEP IRA	SIMPLE IRA	401(k)s
Contributions Deductible	Yes	No	No	Yes	Yes	Yes
Contribution Limits	<p>Lesser of:</p> <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony)</li> </ul> <p>An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.</p>	<p>Lesser of:</p> <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony)</li> </ul> <p>An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.</p>	<p>Lesser of:</p> <ul style="list-style-type: none"> <li>\$7,000 (Single) &amp; \$14,000 (MFJ) (for 2025)</li> <li>Earned Income (Wage, Business &amp; Alimony)</li> </ul> <p>An additional \$1,000 Contribution is allowed for Individuals aged 50 and above.</p>	<p>Lesser of:</p> <ul style="list-style-type: none"> <li>25% of Employee's Compensation</li> <li>\$70,000 (for 2025)</li> </ul>	<p><b>Employees:</b> Employees can contribute up to a maximum of \$16,500 (for 2025). An additional \$3,500 Contribution is allowed for Individuals aged 50 and above.</p> <p><b>Employers:</b> Employers can contribute either through a match or a non-elective contribution.</p> <ul style="list-style-type: none"> <li>Match Contributions up to: 3% of an Employee's Compensation</li> <li>Non-Elective Contributions up to: 2% of an Employee's Compensation</li> </ul>	<p><b>Employees:</b> Employees can contribute up to a maximum of \$23,500 (for 2025). An additional \$7,500 Contribution is allowed for Individuals aged 50 and above.</p> <p><b>Employers:</b> Employers are not required to make matching contributions to 401(k) plans, but many employers do. If an employer does make matching contributions, they are typically made on a dollar-for-dollar basis, up to a certain percentage of the employee's salary.</p>
Distributions	<p><b>Principal:</b> Taxable</p> <p><b>Interest:</b> Taxable</p>	<p><b>Principal:</b> Non-Taxable</p> <p><b>Interest:</b> Taxable</p>	<p><b>Principal:</b> Non-Taxable</p> <p><b>Interest:</b> Non-Taxable</p>	<p><b>Principal:</b> Taxable</p> <p><b>Interest:</b> Taxable</p>	<p><b>Principal:</b> Taxable</p> <p><b>Interest:</b> Taxable</p>	<p><b>Principal:</b> Taxable</p> <p><b>Interest:</b> Taxable</p>
Distribution Age Limits	Distribution occurs after you've reached age 59 ½.	Distribution occurs after you've reached age 59 ½.	<p>Must occur at least five years after the first contribution to the Roth IRA</p> <p>Distribution occurs after you've reached age 59 ½.</p>	Distribution occurs after you've reached age 59 ½.	Distribution occurs after you've reached age 59 ½.	Distribution occurs after you've reached age 59 ½.

Penalties on Early Withdrawal	10% Penalty in addition to Income Tax on Principal and Earnings portion of Withdrawal	10% Penalty in addition to Income Tax on Earnings portion of Withdrawal	10% Penalty in addition to Income Tax on Earnings portion of Withdrawal	10% Penalty in addition to Income Tax on Principal and Earnings portion of Withdrawal	10% Penalty in addition to Income Tax on Principal and Earnings portion of Withdrawal	10% Penalty in addition to Income Tax on Principal and Earnings portion of Withdrawal
Qualified Early Withdrawal	No Penalty would apply on Qualified Early Withdrawal.	No Penalty would apply on Qualified Early Withdrawal.	No Penalty would apply on Qualified Early Withdrawal.	No Penalty would apply on Qualified Early Withdrawal.	No Penalty would apply on Qualified Early Withdrawal.	No Penalty would apply on Qualified Early Withdrawal.
Required Minimum Distributions (RMDs):	Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.	Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.	No RMD Requirements	Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.	Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.	Individuals must start taking RMDs from Traditional IRA by April 1 of the year following the year in which they turn 73.
Penalty for Failing to Take RMD	25% of the amount that was not withdrawn as required	25% of the amount that was not withdrawn as required	No RMD Requirements	25% of the amount that was not withdrawn as required	25% of the amount that was not withdrawn as required	25% of the amount that was not withdrawn as required

- Education Planning
  - Coverdell Education Savings Account (ESA)
    - Definition
      - A Coverdell Education Savings Account (ESA), formerly known as an Education IRA, is a tax-advantaged investment account in the United States designed to encourage savings to cover future education expenses.
    - How does a Coverdell ESA Work?
      - Establishment
        - ⇒ Determine Eligibility
        - ⇒ Choosing a Provider
        - ⇒ Opening an Account
        - ⇒ Selecting Investments
      - Contribution
        - ⇒ Non-Deductible Contributions
        - ⇒ Contribution Limits
          - Maximum Contribution to Coverdell IRA is \$2,000 per beneficiary.
      - Distribution
        - ⇒ Distribution
          - Principal: Non-Taxable
          - Interest: Non-Taxable
        - ⇒ Distribution Age Limits
          - Funds should be used by the beneficiary before age 30.
        - ⇒ Penalties on Non-Withdrawal
          - A 10% Penalty and Income Tax on Earnings would apply to any leftover funds.
        - ⇒ No Required Minimum Distributions (RMDs)

- Qualified Tuition Programs (529 Plans)
  - Definition
    - A qualified tuition program (QTP), also known as a 529 plan, is a tax-advantaged savings plan designed to encourage saving for future education expenses.
  - Types of Tuition Programs (529 Plans)
    - Education Savings Plans
      - ⇒ These plans allow one to contribute funds that are then invested in various investment options, such as stocks, mutual funds, etc.
    - Prepaid Tuition Plans
      - ⇒ These plans allow one to purchase credits or units at today's prices to be used in the future for tuition and, in some cases, other qualified expenses.
  - How Does a 529 Plan Work?
    - Establishment
      - ⇒ Account Setup
      - ⇒ Investment Options
    - Contribution
      - ⇒ Non-Deductible Contributions
      - ⇒ Contribution Limits
        - Each 529 plan sets its own maximum contribution limits.
    - Distribution
      - ⇒ Distribution
        - Principal: Non-Taxable
        - Interest: Non-Taxable
      - ⇒ Penalties on Non-Qualified Expenses
        - 10% Penalty and Income Tax would apply on the Earnings portion if funds were used for Non-Qualified Expenses.

⇒ Beneficiary Changes Allowed

○ Student Loans

▪ Types of Student Loans

➤ Federal Student Loans

⇒ Stafford Loans

⇒ Parent Loans for Undergraduate Students (PLUS)

➤ Private Student Loans

▪ Free Application for Federal Student Aid (FAFSA)

➤ The Free Application for Federal Student Aid (FAFSA) is the first step in applying for federal student loans.

➤ The FAFSA determines your eligibility for federal financial aid programs, including grants and loans.

▪ Student Loan Interest Deduction

➤ Individuals can deduct the lesser of \$2,500 or the amount of interest paid on a student loan for the tax year for themselves, a spouse, or dependents.

- Grants & Scholarships
  - Grants and Scholarships are financial aid awards that do not need to be repaid. They are typically awarded based on financial need, academic merit, or other specific criteria.
  - There are various Grant Programs available at the Federal, State, and Institutional Levels.
    - Federal Pell Grant
    - Federal Supplemental Educational Opportunity Grant (FSEOG)
  - Types of Grants
    - Need-Based Grants & Scholarships
    - Merit-Based Grants & Scholarships
  - Taxability of Scholarships and Grants
    - Non-Degree Students
      - ⇒ Taxable
    - Degree Students
      - ⇒ Not Taxable if they are used to pay for qualified education expenses.
  - Employer-Provided Educational Assistance
    - Employers can provide tax-free educational assistance to their employees up to \$5,250 per year.
- US Series EE Savings Bond
  - Interest income from U.S. Series EE Savings Bonds issued after 1989 may be excluded from taxable income if the bond proceeds are used to pay for Qualified Higher Education Expenses.

- Education Credits

- American Opportunity Tax Credit

- American Opportunity Tax Credit is available for qualified expenses for the first 4 years of college.
- The American Opportunity Tax Credit provides a maximum credit of up to \$2,500 per eligible student per year calculated as:
  - ⇒ American Opportunity Tax Credit = 100% of the first \$2,000 spent on qualified expenses + 25% of the next \$2,000 spent on qualified expenses.
- The Refundable amount is 40% of the credit. As such, the maximum refundable amount is \$1,000, which is 40% of \$2,500.
- A Taxpayer cannot claim the American Opportunity Tax Credit & Lifetime Learning Credit for the same student in the same year, but they can claim both credits for different students in the same year.

- Lifetime Learning Credit

- The Lifetime Learning Credit is an education credit available to eligible taxpayers who are pursuing higher education or acquiring new skills.
- The Credit is Limited up to \$2,000 per taxpayer, i.e., 20% of the first \$10,000 paid on behalf of all family members together.
- The Taxpayer cannot claim the American Opportunity Tax Credit & Lifetime Learning Credit for the same student in the same year but can claim credits for different students in the same year.

- Investment Planning
  - Equity
    - Risks
      - Market Risk
      - Company Risk
      - Sector Risk
      - Volatility Risk
      - Liquidity Risk
    - Returns
      - Potential for Capital Appreciation
      - Dividend Income
    - Advantages
      - Tax Efficiency: Capital Gains are subject to Lower Tax Rates
      - Potential for Higher Returns
    - Disadvantages
      - Market Volatility
      - Lack of Fixed Income
  - Treasury Securities
    - Risk
      - Interest Rate Risk
      - Inflation Risk
    - Returns
      - Fixed Income
      - Return of Principal

- Advantages
  - Credit Quality
  - Liquidity
- Disadvantages
  - Lower Yields
  - Interest Rate Risk
- Corporate Bonds
  - Risks
    - Credit Risk
    - Interest Rate Risk
    - Inflation Risk
  - Returns
    - Fixed Income
    - Return of Principal
  - Advantages
    - Income Generation
    - Diversification
  - Disadvantages
    - Credit Risk
    - Interest Rate Risk
- Municipal Bonds
  - Risks
    - Credit Risk
    - Interest Rate Risk
    - Inflation Risk

- Returns
  - Fixed Income
  - Return of Principal
  - Tax-Exempt Income
- Advantages
  - Tax Benefits
  - Potential for Fixed Income
- Disadvantages
  - Credit Risk
  - Limited Availability
- Mutual Funds
  - Risks
    - Market Risk
    - Manager Risk
  - Returns
    - Capital Appreciation
    - Dividend and Interest Income
  - Advantages
    - Professional Management
    - Diversification
  - Disadvantages
    - Fees and Expenses

- Insurance Planning
  - Life Insurance
    - Life Insurance provides financial support to the insured's beneficiaries upon the insured's death.
  - Health Insurance
    - Health Insurance assists in covering medical expenses, such as doctor visits, hospital stays, and prescription medications.
  - Long-Term Care Insurance
    - Long-Term Care Insurance covers services that are not usually covered by regular health insurance, such as assistance with daily activities like bathing, dressing, or eating.
  - Disability Insurance
    - Disability Insurance provides income replacement if an individual becomes unable to work due to a disability.
  - Homeowners Insurance
    - Homeowners Insurance offers protection for a person's home and possessions against damage resulting from incidents like fire, theft, and other perils.
  - Auto Insurance
    - Auto Insurance, required by law in most states, helps cover the costs related to vehicular damage and the property of others in the event of an accident.
  - Umbrella Insurance
    - Umbrella Insurance is a type of personal liability insurance that goes above and beyond the coverage limits of an individual's other insurance policies, like homeowners or auto insurance.

- Estate Planning
  - Legal Ownership of Assets
    - Sole Ownership
    - Joint Ownership
    - Trust Ownership
  - Beneficiary Designations
    - Types of Beneficiaries
      - Primary Beneficiaries
      - Contingent Beneficiaries
    - Allocation of Asset on Death of Beneficiary
      - Per Capita
        - ⇒ With per capita distribution, allocation is equal to each person or each beneficiary.
      - Per Stirpes
        - ⇒ With per stirpes distribution, allocation is equal at the level of the first generation.

# NINJA NOTES

Business Analysis & Reporting 2026



## Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the BAR section of the CPA Exam:

Area I	Business Analysis	40% - 50%
Area II	Technical Accounting and Reporting	35% - 45%
Area III	State and Local Governments	10% - 20%

# Skill Allocation

Remembering and Understanding	10% - 20%
Application	45% - 55%
Analysis	30% - 40%
Evaluation	-

# Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
BAR - Discipline	50%	50%

# Section Time and Question Type

The table below presents the design of the Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
BAR - Discipline	4 Hours	50	7

# Content

- BAR-1 Strategic Planning & Budgeting
- BAR-2 Cost Accounting
- BAR-3 Breakeven Analysis, Decision Analysis & Pricing
- BAR-4 Operations Management & Performance Measurement
- BAR-5 Financial Management
- BAR-6 Financial Risk Management
- BAR-7 Ratio Analysis
- BAR-8 Economics
- BAR-9 Enterprise Risk Management Framework
- BAR-10 Revenue Recognition
- BAR-11 SEC Reporting Requirements and Segment Reporting
- BAR-12 Share-Based Compensation
- BAR-13 Intangibles
- BAR-14 Financial Statements of Employee Benefit Plans
- BAR-15 Derivatives and Derivative Accounting
- BAR-16 Business Consolidation and Combination
- BAR-17 Foreign Currency Financial Statements
- BAR-18 Lease Accounting – Lessor
- BAR-19 Governmental Accounting

# NINJA NOTES

Business Analysis & Reporting 2026



**Strategic Planning & Budgeting**

## **Copyright & Disclaimer**

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

# Strategic Planning & Budgeting

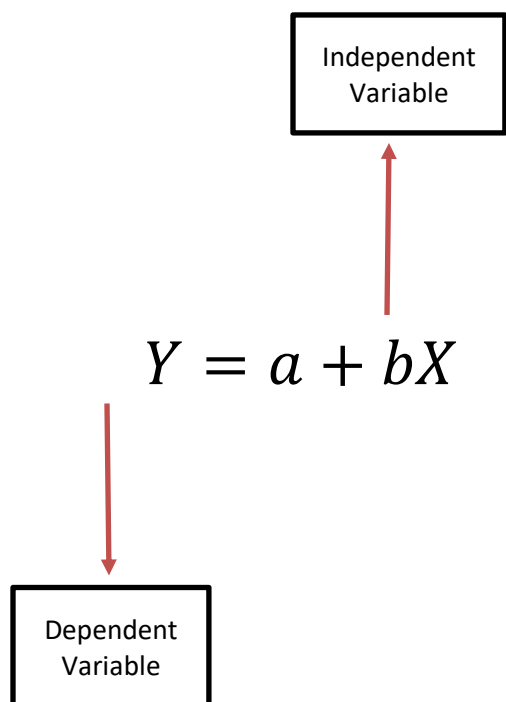
## Strategy

- Levels of Strategy
  - Corporate Strategy
    - The corporate strategy addresses issues facing the whole company.
    - The corporate strategy helps an organization decide the industries and businesses it should operate to maximize profitability.
  - Business Strategy
    - Business strategy involves decision-making processes to determine how a business segment operates and succeeds within its industry.
  - Functional Strategy
    - Every business division has different functions like marketing, operations, finance, sales, human resources, etc.
    - Functional-level strategy develops plans, objectives, and guidelines for each of these departments and functions, such as to maximize the effectiveness and efficiency of operations.
- Long-term Mission and Goals
  - Vision
    - The vision statement is the organization's objectives expressed in terms of contribution to society.
    - For example, Tesla's vision statement is: "To accelerate the world's transition to sustainable energy."
  - Mission
    - The mission statement refers to how an organization intends to create value for its stakeholders.
    - The mission statement is based on the vision statement and explains how an organization will achieve its vision.
    - For example, Tesla's mission statement is, "To create the most compelling car company of the 21st century by driving the world's transition to electric vehicles."

- Goals
  - Strategic Goals
    - Strategic goals are long-term in nature and deal with the entity's strategic policies.
    - For example, "Acquire 30% market share of United States automobile industry by 2030."
  - Tactical Goals
    - Tactical goals, on the other hand, are short-term in nature, and these ensure the achievement of strategic goals.
    - For example, "Increase production capacity by 20%."
- Objectives
  - Objectives are the plan of actions and should be specific, measurable, attainable, realistic, and timely (SMART).
  - For example, "Purchase additional machinery that would increase production capacity in the next 6-months."

## Forecasting Techniques

- Regression Analysis
  - Regression analysis is a mathematical technique used to predict the value of the dependent variable based upon the value of the independent variable.
  - Regression Equation



- Multiple R
  - Coefficient of Correlation (R)
  - Measures the degree of linearity in the relationship between two variables
  - Between +1 and -1
    - Perfect Positive Correlation = 1
    - Perfect Negative Correlation = -1
    - No Correlation = 0
- R-Square
  - Coefficient of Determination
  - Square of Coefficient of Correlation (R<sup>2</sup>)

- Measures the effect of changes in one independent variable on another dependent variable
- Between 1 and 0
  - Higher the value, Higher the explaining power of independent variable
- Standard Error
  - Measures the accuracy and precision of predictions made using regression equation
- T-Stat
  - Relationship of independent variable relative to dependent variable
    - Substantial and Long-Term Relationship
    - T-Stat of 2 or More is Significant, while 3 or More is Preferred
- Advantages of Regression Analysis
  - Simplicity
  - Multiple Data Points
- Disadvantages of Regression Analysis
  - Effect of Outliers
  - Assumption of Linearity
- Learning Curve Analysis
  - Graphic representation of relationship between productivity and experience
  - Useful for forecasting & budgeting labor costs
  - Learning Curve represents that people are much slower at performing a task for the first time, than they would be performing it for the 100th time
  - Cumulative Average-Time Learning Model
    - Learning curve applies at the average time taken to manufacture the product
    - Average time declines as production doubles
  - Advantages of Learning Curve Analysis
    - Accuracy

- Planning
- Disadvantages of Learning Curve Analysis
  - Constant Learning Rate
  - Relevance
- Expected Value Analysis
  - Prediction technique using the probability distribution
  - Allows Managers to make Decisions Resulting in Highest Expected Profit or Lowest Expected Loss
  - *Expected Value* =  $\Sigma X \times P(X)$
  - Advantages of Expected Value Analysis
    - Multiple Scenarios
    - Simplicity
  - Disadvantages of Expected Value Analysis
    - Based on Estimates
    - Not the Most Likely Outcome
- Other Forecasting Tools
  - Sensitivity Analysis
    - Analysis of What-If Scenarios to Evaluate Possible Outcomes
    - Financial Estimate of Sensitivity of Scenarios to Change in Circumstances
    - Use of Probability Theory
      - Firms can Prepare for the Worst Case, Best Case & Most Likely Scenario
  - Time Series Analysis and Smoothing
    - Time Series Analysis
      - Trend Analysis
      - Measures Variables against Time

- Time is the Independent Variable
- Smoothing
  - Part of Time Series Analysis
  - Smoothing out random & uncertain fluctuations from the irregular components of a time series
- Decision Tree Analysis
  - Allows managers to choose outcome with highest expected payoff
  - Each Possible Outcomes = Branches of a Tree
  - Expected Payoff = Possible Payoff x Probability
- Monte-Carlo Simulations
  - Computer-Based Statistical Technique
  - Runs multiple simulations and generates values for a random variable at various probability distribution

## Budgeting Methodologies

- A Budget may be defined as a plan for future operations expressed in dollars or units, or both.
- Master Budgets
  - A Master Budget provides a blueprint for the organization.
  - A Master Budget is divided into two parts (Operating Budgets and Financial Budgets), which include all of the following budgets from various functions:

Operating Budgets	Financial Budgets
Sales Budget	Cash Budget
Production Budget	Capital Budget
Direct Materials Budget	
Direct Labor Budget	
Overhead Budget	
Cost of Goods Sold Budget	
Selling and Administrative Expense Budget	

- Flexible Budgeting

- Flexible Budgets

- Based on Actual Level of Output
- Provides for Better Comparison with Actual Costs

- Preparation

- Budgeted Rates x Actual Level of Activity

- Example

- Direct Materials Budget with 100,000 Units at a Standard Cost of \$2 per Unit. Actual Production was 80,000 units at of \$2.1 per unit

	Static Budget	Flexible	Actual
Units	100,000 units	80,000 units	80,000 units
Cost per Unit	\$2	\$2	\$2.1
Total Direct Material Cost	\$200,000	\$160,000	\$168,000

- Benefits

- Allows Estimation of Income at More than One Level of Output
- As an Evaluation Tool allows for Fair Comparison
- As an Evaluation Tool allows for Easy Variance Analysis

- Continuous (Rolling) Budgeting

- Additional period added at the end of each budgeting period

- Ensure sufficient number of periods planned
- Constantly updates budget to the constantly changing operating environment

- Benefits of Continuous Budgeting

- Allows for Increased Alignment of Short-Term Goals with Long-Term Strategy
- More relevant and updated budgets, increases the effectiveness of operations
- Budgeting is broken into smaller, more manageable parts

- Zero-Based Budgeting
  - Starts from Scratch
  - Forward-Looking
  - Focused on Constant Cost Justification
  - Classifies Budget Requests on the Basis of Benefits Arising from Each activity
- Incremental Budgeting
  - Incremental changes made to prior period's budget
  - Changes are based on preceding year's results & future year's expectations
- Activity-Based Budgeting
  - Budgeting Technique
    - Budgets are prepared using activity-based costing
    - Overhead allocation using multiple cost drivers
  - Advantages
    - Increased Budget Accuracy
    - Judicious Consumption of Common Resources
  - Disadvantages
    - Expensive
    - Estimation Errors
- Project Budgeting
  - Budgeting for specific projects or assignments
  - Treated as a separate entity
  - All costs are tracked independently from rest of the organization
- Life-Cycle Budgeting
  - Life-Cycle Budgeting focuses on individual products and attempts to budget the costs of the product over the entire life cycle from research and development to customer support.

## Operating Budget

- Sales Budget
  - The first step in the budgeting process (given the goals and policies of operation) is to forecast the level of sales for the budget period.
  - Sales budget is calculated: Forecasted Units x Forecasted Price
  - Example
    - Ninja Company, which is preparing the upcoming quarter budget (January-March), projected the following sales figures. Prepare the sales budget:

Month	Forecasted Units	Forecasted Sales Price (\$)	Budgeted Sales (\$)
December	10,000	\$50	\$500,000
January	12,000	\$50	\$600,000
February	15,000	\$50	\$750,000
March	18,000	\$60	\$1,080,000
April	20,000	\$60	\$1,200,000
May	22,000	\$60	\$1,320,000

Budgeted Sales (January, February & March)	\$2,430,000
--	-------------

- Production Budget

- The production budget calculates the number of units required to be produced to meet the expected sales targets, usually determined by the sales or marketing departments.

	Units
Opening Inventory	XXX
<b>Add: Production</b>	<b>XXX</b>
Less: Cost of Goods Sold	(XXX)
Ending Inventory	XXX

- Example

- Ninja Company's policy is to maintain finished goods inventory levels at 30% of the following month's budgeted sales units. Prepare the production budget:

Month	Budgeted Sales Units	Ending inventory (30% of Next Month's COGS)	Opening Inventory (Last Month's Ending Inventory)
December	10,000	3,600	-
January	12,000	4,500	3,600
February	15,000	5,400	4,500
March	18,000	6,000	5,400
April	20,000	6,600	6,000
May	22,000	0	6,600

	January	February	March	April
Opening Inventory	3,600	4,500	5,400	6,000
<b>Add: Production (Balancing Figure)</b>	12,900	15,900	18,600	20,600
Less: Units Sold	(12,000)	(15,000)	(18,000)	(20,000)
Ending Inventory	4,500	5,400	6,000	6,600

Budgeted Production (January, February & March)	47,400 units
---	--------------

- Direct Materials Budget

- Direct Materials Usage Budget

- Based on the production budget, the company first determines the units and cost of direct material required for production. This is done using the Direct Material Usage Budget.

- Direct Materials Usage Budget = Units to be Produced x No. of pounds per Finished Good x Cost per Pound

- Example

- Ninja Company requires 2 pounds of direct material to produce 1 unit of finished goods. Each unit of direct material costs \$5. Prepare a direct material usage budget.

	January	February	March	April
Production	12,900 units	15,900 units	18,600 units	20,600 units
No. of pounds per Finished Good	2	2	2	2
Pounds of Direct Material Required	25,800	31,800	37,200	41,200
Cost per Pound	\$5	\$5	\$5	\$5
Direct Material Cost	\$129,000	\$159,000	\$186,000	\$206,000

Budgeted Direct Materials Usage Cost (January, February & March)	\$474,000
--	-----------

- Direct Materials Purchase Budget

- Once the direct material requirement is established, the company determines the number of units of direct materials to be purchased.

	Units
Opening DM Inventory	XXX
Add: Purchase (a)	XXX
Less: Transfers to Production	(XXX)
Ending DM Inventory	XXX
Cost per Pound (b)	XXX
Direct Material Purchase Cost (a x b)	XXX

- Example

- Ninja Company's policy is to maintain direct material inventory levels at 20% of the following month's budgeted production units. Prepare the direct material purchase budget.

Month	Direct Material Required (Transfer to Production)	Ending inventory (20% of Next Month's Requirement)	Opening Inventory (Last Month's DM Ending Inventory)
January	25,800 pounds	6,360 pounds	5,160 pounds
February	31,800 pounds	7,440 pounds	6,360 pounds
March	37,200 pounds	8,240 pounds	7,440 pounds
April	41,200 pounds	-	8,240 pounds

	January	February	March
Opening DM Inventory	5,160	6,360	7,440
Add: Purchase (a)	27,000	32,880	38,000
Less: Transfers to Production	(25,800)	(31,800)	(37,200)
Ending DM Inventory	6,360	7,440	8,240
Cost per Pound (b)	\$5	\$5	\$5
Direct Material Purchase Cost (a x b)	\$135,000	\$164,400	\$190,000

Budgeted Direct Materials Purchase Cost (January, February & March)	\$489,400
---	-----------

- Direct Labor Budget

- The production budget will be used to prepare the direct labor budget.
- This budget indicates the hours and cost of direct labor needed to meet production requirements.

- Example

- Ninja Company estimates that it takes 1 hour of labor to assemble a table. The labor rate is \$8 per hour. Prepare the direct labor budget.

	January	February	March
Production	12,900 units	15,900 units	18,600 units
Hours Required per unit	1 Hour	1 Hour	1 Hour
Total Hours Required	12,900 Hours	15,900 Hours	18,600 Hours
Cost per Hour	\$8	\$8	\$8
Direct Labor Cost	\$103,200	\$127,200	\$148,800

Budgeted Direct Labor Cost (January, February & March)	\$379,200
--	-----------

- Overhead Budget

- Overhead Budget is usually divided into Fixed and Variable Costs.
- Overheads can be allocated based on direct labor hours/machine hours or applied using activity-based costing.

- Example

- Ninja Company applies variable overheads based on direct labor hours at the rate of \$3 per hour. The fixed overhead rate is \$100,000 per month. Prepare the overhead budget.

	January	February	March
<b>Variable Overhead</b>			
Total Hours Required	12,900 Hours	15,900 Hours	18,600 Hours
Variable Overhead Rate per DL Hour	\$3	\$3	\$3
Total Variable Overhead	\$38,700	\$47,700	\$55,800
<b>Fixed Overhead</b>			
Total Fixed Overhead	\$100,000	\$100,000	\$100,000
Total Overhead	\$138,700	\$147,700	\$155,800

Budgeted Overhead (January, February & March)	\$442,200
---	-----------

- Cost of Goods Sold Budget

- Cost of Goods Sold Budget presents the total cost of producing the product sold for a period.

		\$\$
Opening Finished Goods Inventory (Given)		XXX
Add: Direct Materials (From Direct Material Usage Budget)		
Add: Direct Labor (From Direct Labor Budget)	XXX	
Add: Overheads (From Overheads Budget)	XXX	
<b>Cost of Goods Manufactured</b>		<b><u>XXX</u></b>
<b>Cost of Goods Available for Sale</b>		<b>XXX</b>
Less: Ending Finished Goods Inventory (Calculated)		<u>(XXX)</u>
<b>Cost of Goods Sold</b>		<b>XXX</b>

- Example

- Ninja Company's opening finished goods inventory was valued at \$68,000. Prepare the cost of goods sold budget.

(January – March)		\$\$
Opening Finished Goods Inventory (Given)		\$68,000
Add: Direct Materials (From Direct Material Usage Budget)	\$474,000	
Add: Direct Labor (From Direct Labor Budget)	\$379,200	
Add: Overheads (From Overheads Budget)	<u>\$442,200</u>	
<b>Cost of Goods Manufactured</b>		<b><u>\$1,295,400</u></b>
<b>Cost of Goods Available for Sale</b>		<b>\$1,363,400</b>
Less: Ending Finished Goods Inventory (Calculated)		<u>(\$162,000)</u>
<b>Cost of Goods Sold</b>		<b>\$1,201,400</b>

- Ending finished goods inventory can be calculated as follows:
  - Total cost of goods manufactured = \$1,295,400
  - Units manufactured (12,900 + 15,900 + 18,600) = 47,400 units
  - Cost per unit = \$27
  - Ending finished goods inventory (6,000 units x \$27) = \$162,000

- Selling, General, and Administrative (SG&A) Expense Budget
  - Selling, General, and Administrative (SG&A) expense refers to period costs expensed in the period incurred.
  - These are non-manufacturing expenses that could be both fixed or variable.
  - Example
    - Prepare Ninja Company's SG&A Expense Budget.

	\$\$
Salaries	\$200,000
Insurance	\$200,000
Rent	\$50,000
Advertising	<u>\$100,000</u>
Total Selling, General & Administrative (SG&A) Expense	\$550,000

- Pro Forma Income Statement
  - Budgeted Income Statement
  - Prepared Based on Sales Budget, Production Budget, Direct Materials Budget, Direct Labor Budget, Overhead Budget and Selling, General and Administrative Expenses Budget
  - Analyzed by top Management to Determine the Alignment with Objectives and Goals
  - Example

Sales (From Sales Budget)	\$2,430,000
Less: Cost of Goods Sold (From Cost of Goods Sold Budget)	(\$1,201,400)
Gross Profit	\$1,228,600
Less: SG&A Expense (From SG&A Budget)	<u>(\$550,000)</u>
Operating Profit	\$678,600
Less: Taxes (30%)	(\$203,580)
Net Income	\$475,020

- Cash Budget
  - Calculates the effect of all budgets on Cash
  - Prepared for the near future
  - Forecasts the Cash Outflows and Inflows of a Firm
  - Useful in the planning process for determining
    - Expected Sources and Uses of Funds
    - Availability of Funds for Investment Purposes
    - Need for External Financing
    - Availability of Funds for the Repayment of Debt
    - Availability of Funds for Distribution to Owners
  - Example
    - 30% is Cash sales, and Balance is Credit Sales. Cash Collection for Credit Sales is as follows:
      - 30% in Month of Sale
      - 40% in the month following the Month of Sale
      - 25% in the Second Month following the Month of Sale
      - 5% is uncollectible
    - 50% is Cash Purchases, and Balance is Credit Purchases. Cash Payment for Credit Purchase is as follows:
      - 60% in Month of Purchase
      - 40% in the month following the Month of Purchases
    - Operating Expenses, 80% of Operating Expenses are cash expenses and are paid in arrears.
    - Sales, Purchase and Operating Expenses information is given below:

	November	December	January	February	March
Sales	\$100,000	\$110,000	\$120,000	\$130,000	\$140,000
Purchase	\$40,000	\$50,000	\$60,000	\$70,000	\$80,000
Operating Expense	\$30,000	\$40,000	\$50,000	\$60,000	\$70,000
Insurance					\$30,000

- Using this information prepare Cash Budget

	January	February	March
Total Sales	\$120,000	\$130,000	\$140,000
Cash Sales (30% of Total Sales) (a)	\$36,000	\$39,000	\$42,000
Credit Sales (70% of Total Sales)	\$84,000	\$91,000	\$98,000
Cash Collection:			
30% in the Month of Sales (b)	\$25,200	\$27,300	\$29,400
40% in Month following the Month of Sale (c)	\$30,800	\$33,600	\$36,400
25% in the Second Month following the Month of Sale (d)	\$17,500	\$19,250	\$21,000
<b>Total Cash Receipts (A) = (a) + (b) + (c) + (d)</b>	<b>\$109,500</b>	<b>\$119,150</b>	<b>\$128,800</b>
Total Purchases	\$60,000	\$70,000	\$80,000
Cash Purchases (50% of Total Purchases) (a)	\$30,000	\$35,000	\$40,000
Credit Purchases (50% of Total Purchases)	\$30,000	\$35,000	\$40,000
Cash Payment:			
60% in the Month of Purchase (b)	\$18,000	\$21,000	\$24,000
40% in Month following the Month of Purchase (c)	\$10,000	\$12,000	\$14,000
Operating Expense (d)	\$32,000	\$40,000	\$48,000
Insurance (e)			\$30,000
<b>Total Cash Receipts (B) = (a) + (b) + (c) + (d) + (e)</b>	<b>\$90,000</b>	<b>\$108,000</b>	<b>\$156,000</b>
<b>Cash Surplus (Deficit) (A) – (B)</b>	<b>\$19,500</b>	<b>\$11,150</b>	<b>(\$27,200)</b>

- Pro Forma Balance Sheet
  - Calculates the estimated Financial Position of a company
  - Illustrates the effect of budgeting on components of Balance Sheet
- Pro Forma Statement of Cash Flows
  - Last Budget to be Prepared
  - Converts accrual-based Budgeted Income Statement and Balance Sheet into cash-based Information.

# NINJA NOTES

Information Systems & Control 2026



## Introduction

# Content Area Allocation

The following table summarizes the content areas and the allocation of content tested in the ISC section of the Exam:

Area I	Information Systems and Data Management	35% - 45%
Area II	Security, Confidentiality and Privacy	35% - 45%
Area III	Considerations for System and Organization Controls (SOC) Engagements	15% - 25%

## Skill Allocation

Remembering and Understanding	55% - 65%
Application	20% - 30%
Analysis	10% - 20%
Evaluation	0% - 0%

## Scoring Weight

The table below presents the scoring weight of MCQs and TBSs

	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
ISC - Discipline	60%	40%

## Section Time and Question Type

The table below presents the design of the Exam by section time and question type.

	Section Time	Multiple-Choice Questions (MCQs)	Tasked-Based Simulations (TBSs)
ISC - Discipline	4 Hours	82	6

# Content

ISC-1 IT Infrastructure & Cloud Computing

ISC-2 IT Systems & Business Processes

ISC-3 Data

ISC-4 Emerging Technologies

ISC-5 Outsourcing

ISC-6 Change Management

ISC-7 Systems Availability

ISC-8 Regulation, Standards and Frameworks

ISC-9 Cybersecurity Risks and Mitigation of Cybersecurity Risks

ISC-10 Data Confidentiality and Privacy

ISC-11 Data Breach and Incident Response

ISC-12 System and Organization Controls (SOC)

# NINJA NOTES

Information Systems & Control 2026



**IT Infrastructure & Cloud Computing**

## **Copyright & Disclaimer**

This book contains material copyrighted © 1953 through 2026 by the American Institute of Certified Public Accountants, Inc., and is used or adapted with permission.

Material from the Uniform CPA Examination Questions and Unofficial Answers, copyright © 1976 through 2026, American Institute of Certified Public Accountants, Inc., is used or adapted with permission.

This book is written to provide accurate and authoritative information concerning the covered topics for the Uniform CPA Examination and is to be used solely for studying for the Uniform CPA Examination and for no other purpose.

© 2026 NINJA CPA Review, LLC. All Rights Reserved.

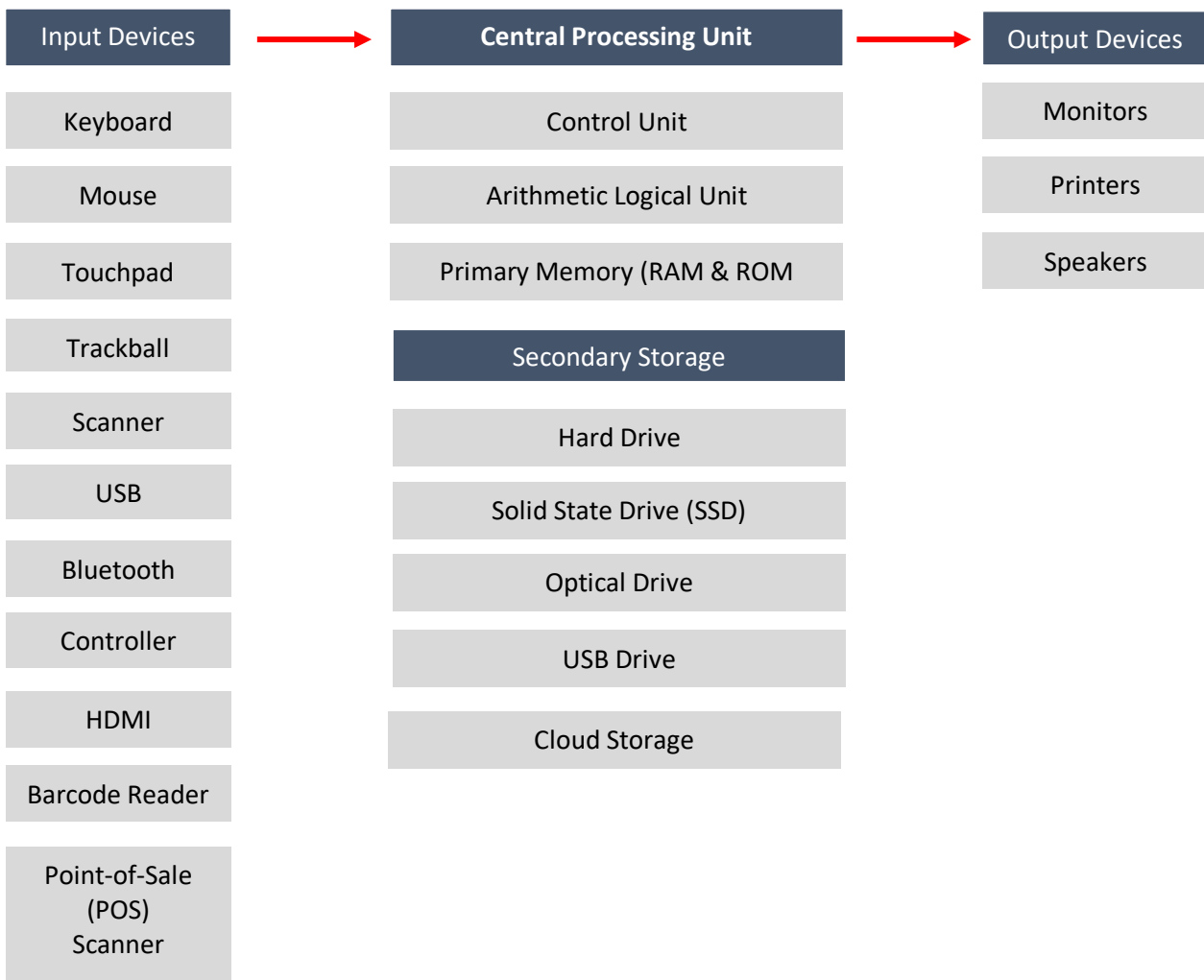
# IT Infrastructure & Cloud Computing

## IT Infrastructure

- Types of Computers
  - Supercomputers
    - Supercomputers are among the fastest computers currently available and are employed for specialized applications that require immense amounts of mathematical calculations
    - They are very expensive and are used for applications such as weather forecasting, scientific simulations, graphics, fluid dynamic calculations, nuclear energy research, electronic design, and analysis of geological data in petrochemical prospecting
  - Mainframe Computers
    - Mainframe Computers are very large and expensive computers capable of simultaneously supporting hundreds or even thousands of users
    - They were originally called mainframe computers because they contained the central processor unit in a large cabinet, but the term has come to encompass any large computer that is used for mainframe-type applications
  - Minicomputer
    - Minicomputers are larger and more powerful than a personal computer, but smaller and less powerful than a mainframe computer
    - These computers are typically used by small and medium-sized businesses and organizations for tasks such as file and print serving, database management, and application hosting
  - Microcomputers
    - Microcomputers, also known as Personal Computers (PCs), are small, relatively inexpensive computers that are designed for an individual user
    - They include desktops and laptops and are based on microprocessor technology, which enables manufacturers to put an entire CPU on one chip
  - Tablets
    - Tablets are portable computers that are small enough to be held in one's hand
    - They are convenient to carry and can be used instead of a laptop due to their processing power and on-screen keyboard

- Smartphones
  - Like a Tablet, but smaller
  - Advantages vs Tablet
    - Portability and Cell Service (many tablets are Wi-Fi only)
  - Disadvantages vs Tablet
    - Screen is too small for most business functions

- Hardware

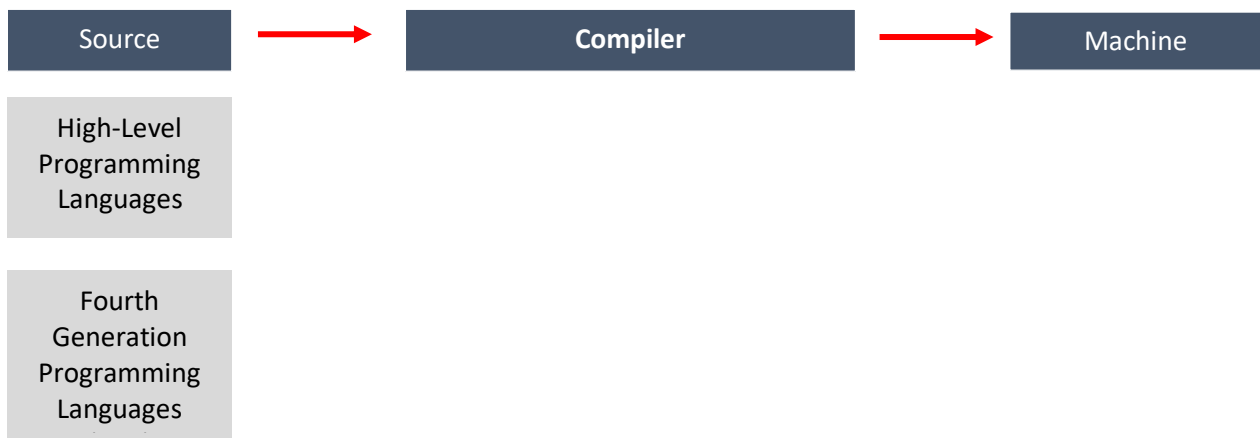


- Software
  - Software is a set of instructions that tells a computer what to do and how to do it. It is a collection of programs and data that enables a computer to perform specific tasks.
  - There are two main types of software: System Software and Application Software.
  - System Software
    - System Software is software that manages and controls the hardware and other system resources of a computer.
    - Operating System
      - Operating System is the most important type of system software.
      - The Operating System manages the Hardware and Software resources of a computer and provides a platform for running application software.
    - Utility Programs
      - Utility Programs are a type of system software that are designed to perform specific tasks, such as virus scanning, disk defragmentation, and data backup.
        - ⇒ Antivirus Software
        - ⇒ Disk Defragmenter
        - ⇒ Backup Software
        - ⇒ System Monitoring Software
        - ⇒ Disk Cleanup Utility
  - Application Software
    - Application Software is software that is designed to perform specific tasks, such as word processing, spreadsheet management, and photo editing.
    - Productivity Software
      - Examples include word processors, spreadsheet programs, and presentation software.
    - Graphics Software
      - Examples include photo editing software, illustration software, and 3D modeling software.

- Multimedia Software
  - Examples include audio editors, video editors, and music production software.
- Communication Software
  - Examples include email clients, chat programs, and video conferencing software.
- Games
- Heuristic Software
  - Heuristic Software is software that uses heuristic algorithms or methods to solve problems or make decisions.

- Programming Language

- A Programming Language is a set of instructions, rules, and conventions that are used to create and execute Software Programs.
- It is a way of communicating with a computer and giving it specific instructions to perform a task.



- Machine Language
  - Machine language, also known as machine code or assembly language, is a set of instructions that are written in a form that can be directly executed by a computer's Central Processing Unit (CPU).
  - Machine language consists of a series of binary digits (ones and zeros) that represent the instructions and data that the computer is to process.

- Source Program

- A Source Program is a set of instructions written in a programming language that is intended to be compiled or interpreted by a computer.
- The Source Program is written in High-Level Programming Languages or Fourth Generation Programming Languages (4GL).
- High-Level Programming Languages
  - High-level Programming Languages are programming languages that are designed to be more human-readable and easier to use than machine language.
  - They are closer to natural human language and are less detailed and more abstract than Machine Language.
    - ⇒ C
    - ⇒ C++
    - ⇒ Java
    - ⇒ Python
    - ⇒ JavaScript
- Fourth Generation Programming Languages (4GL)
  - Fourth-Generation Programming Languages (4GLs) are a type of High-Level Programming Language that is designed to be more user-friendly and easier to use than Traditional Programming Languages.
  - 4GLs are characterized by their use of English-like statements and commands, which make them easier to read and understand than traditional programming languages.

- Compiler

- A Compiler is a type of software that converts source code written in a programming language into machine code that can be executed by a computer.

- Network
  - A Network allows devices to connect and communicate with each other, enabling the exchange of data and information.
  - Types of Networks – Based on Geographical Coverage
    - Personal Area Network (PAN)
      - A Personal Area Network (PAN) is a type of network that connects devices and other personal computing devices that are close to a person, typically within a range of a few meters.
    - Local Area Network (LAN)
      - A Local Area Network (LAN) is a network that connects devices within a limited geographic area, such as a home, office, or school.
    - Wireless Local Area Network (WLAN)
      - A Wireless Local Area Network (WLAN) is a type of LAN that uses wireless technology, such as Wi-Fi, to connect devices.
    - Value-Added Network (VAN)
      - A Value-Added Network (VAN) is a type of network that provides value-added services, such as data storage and secure transmission, to businesses and organizations.
    - Wide Area Network (WAN)
      - A Wide Area Network (WAN) is a network that connects devices over a large geographic area, such as a city, country, or the entire world.
      - The Internet is the largest WAN, connecting millions of devices worldwide.
  - Types of Networks – Based on Ownership
    - Private Networks
      - Private Networks are networks that are owned and operated by a single organization or entity and are typically used to connect devices within that organization.
      - Advantages
        - ⇒ Increased Security
        - ⇒ Flexibility
        - ⇒ Better Performance

- Disadvantages
  - ⇒ Higher Cost
  - ⇒ Limited Access
  - ⇒ Limited Scalability

- Public Networks

- Public Networks, on the other hand, are networks that are owned and operated by third-party companies and leased to users on a usage basis.

- Advantages

- ⇒ Lower Cost
- ⇒ Wider Availability
- ⇒ Scalability

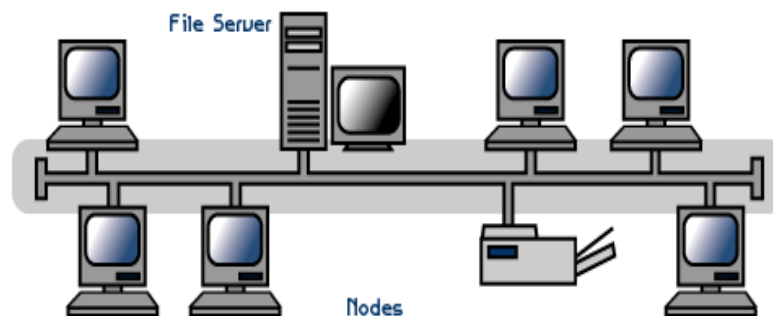
- Disadvantages

- ⇒ Lower Security
- ⇒ Lower Performance
- ⇒ Limited Control

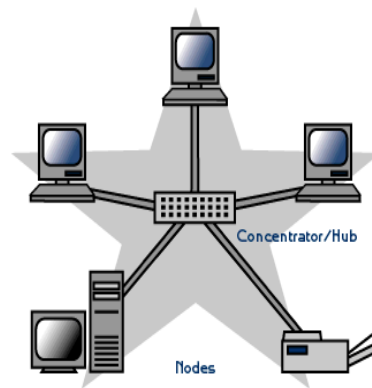
- Network Topology

- Network Topology refers to the shape or layout of a network and determines how devices on the network are connected to each other and how they communicate.

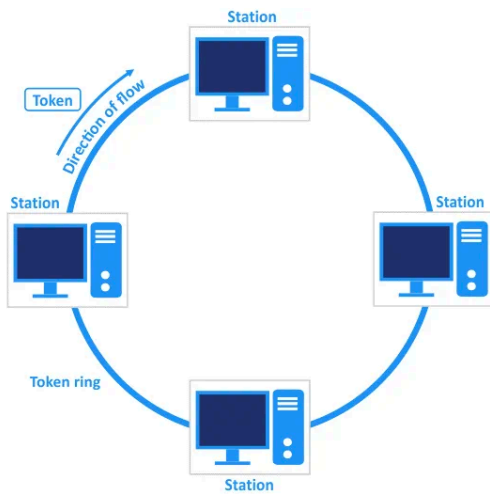
- Bus Topology



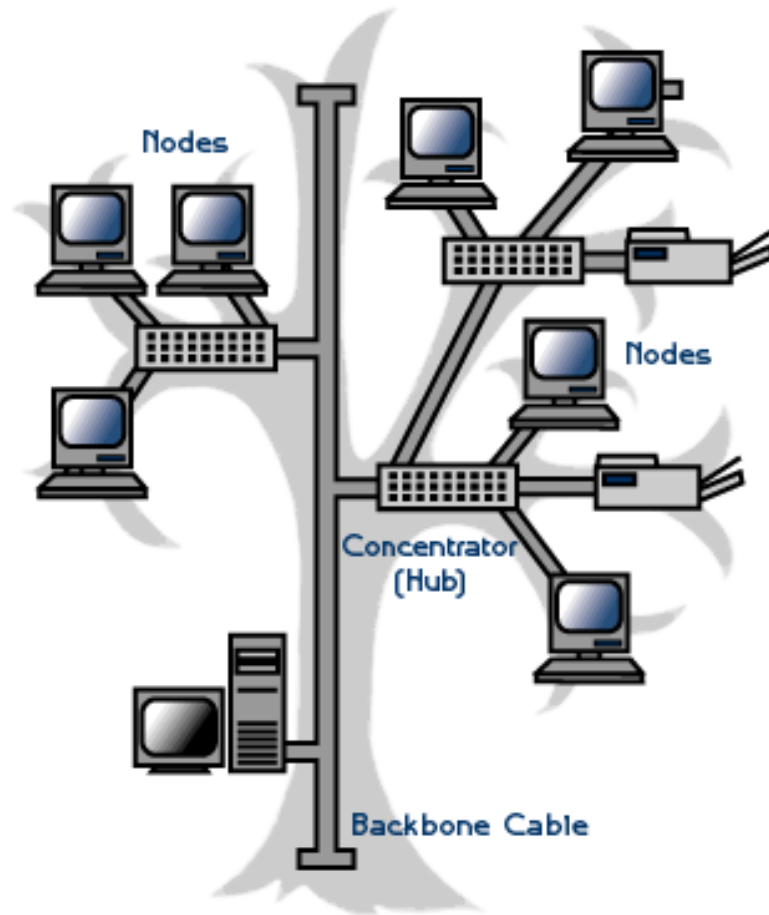
- Star Topology



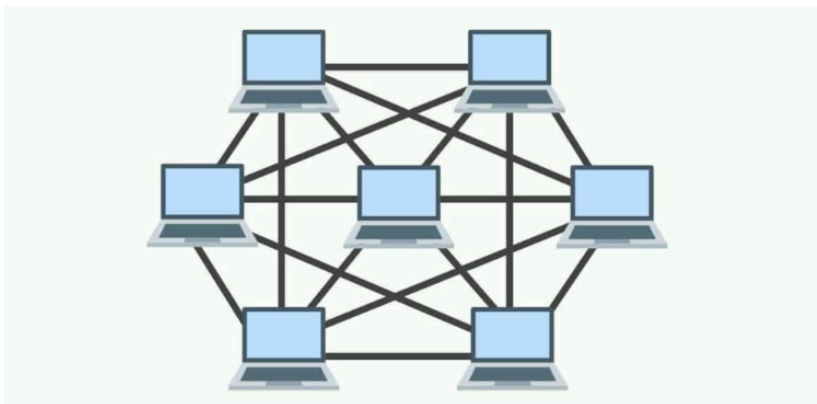
- Ring Topology



- Tree Topology



- Mesh Topology



- Client-Server Architecture
  - In Computer Networking, the Client-Server Architecture is a standard model of communication where one device (The Server) is responsible for providing a specific service to other devices (The Clients).
  - The client sends a request to the server, which then performs a specific task and sends a response back to the client. This model is commonly used for applications such as email, file sharing, and web services. The client-server architecture can be implemented on a local area network (LAN) or over the Internet.
  - Client
    - In a Client-Server Architecture, clients are typically individual computers or workstations that are used by users to access the resources provided by the server.
  - Server
    - The Server is a high-capacity computer that contains the necessary software and hardware to provide a variety of services to the clients.
- Internet
  - The Internet is a global network of interconnected computers and servers that communicate with each other.
  - Internet Related Terminologies
    - Intranet
      - An Intranet is a private network that is used by an organization to share information and resources among its employees, members, or departments.
    - Extranet
      - An Extranet is a private network that shares part of an organization's information or operations with suppliers, vendors, partners, customers, or other businesses.
    - World Wide Web
      - The World Wide Web (WWW or Web) is a vast network of interconnected documents and other resources, linked by hyperlinks and URLs.
      - It is the primary platform for information-sharing on the Internet and is used by billions of people every day to access information, communicate, and conduct business.

- Hyper-Text Transfer Protocol (HTTP)
  - HTTP is a protocol used for transferring data over the Internet.
- Transmission Control Protocol/Internet Protocol
  - TCP/IP stands for Transmission Control Protocol/Internet Protocol, and it is the basic communication protocol of the Internet.
  - TCP is responsible for ensuring that data is transmitted reliably and in the correct order, while IP is responsible for routing data packets to their destination.
- Internet Service Provider (ISP)
  - An Internet Service Provider (ISP) is a company that provides customers with access to the Internet.
- Uniform Resource Locator (URL)
  - A Uniform Resource Locator (URL) is a unique string of characters that identifies a specific webpage or resource on the Internet.
  - A URL is often called a web address, and it is used to locate and retrieve a specific resource, such as a webpage, image, or video.
- Web Servers
  - Web Servers are specialized computers that store and manage webpages, images, videos, and other types of data on the Internet.
- Web Browser
  - A Web Browser is a software application that allows users to access and navigate the World Wide Web.
- Router
  - A Router is a connection point between a home or office network and the Internet.
- Gateway
  - A Gateway is a networking device that connects two different networks together, allowing them to communicate with each other.
- Bridge
  - A Bridge is a networking device that connects two separate LANs (Local Area Networks) together, allowing them to communicate with each other as if they were a single network.

- Switch
  - A Switch is a networking device that connects multiple devices together on a computer network and forwards data packets between them.
  
- Proxy Server
  - A Proxy Server is a server that acts as an intermediary between a client and a server in a network.
  - It forwards requests from clients to servers and returns the responses back to the clients.
  
- Killer Application
  - A Killer Application, also known as a "killer app", is a software program that is so useful and in demand that it drives the sales of a particular hardware platform or operating system
  - For example, a spreadsheet program like Microsoft Excel or Google Sheets can be considered as a Killer application for personal computers, as it is so widely used and necessary for many businesses and individuals.
  
- HTML (Hypertext Markup Language)
  - HTML (Hypertext Markup Language) is a markup language used to create the structure and layout of a webpage.
  
- XML (eXtensible Markup Language)
  - XML (eXtensible Markup Language) is a markup language used to store and transport data.
  - XML (eXtensible Markup Language) is similar to HTML in that it is a markup language used to structure and organize data.
  
- XBRL (eXtensible Business Reporting Language)
  - XBRL (eXtensible Business Reporting Language) is a standard for electronic communication of business and financial data.
  - XBRL allows companies to tag financial data in their reports using a standardized set of tags, called taxonomies, which define the meaning of the data.
  - This makes it possible for financial software and other applications to automatically extract and analyze the data, reducing the need for manual data entry and increasing the accuracy of the analysis.

- Security Threats on Internet

- Virus

- A Virus is a type of malware (malicious software) that attaches itself to a legitimate program or file and is designed to replicate and spread itself to other computers.

- Trojan Horse

- A Trojan horse is a type of malware that disguises itself as a legitimate program or file, but once executed, it can cause damage or steal information from the infected computer.

- Worm

- A Worm is a type of malware that is similar to a virus in that it replicates itself and can spread to other computers, but it does not need to attach itself to a legitimate program or file to do so.

- Hoax Virus

- A Hoax Virus is a message that is circulated through email or social media warning users of a virus that does not actually exist.

- Phishing

- Phishing is a type of social engineering attack that is used to trick users into providing sensitive information, such as passwords, credit card numbers, or personal details.

- Protection against Security Threats on Internet

- Firewall

- A Firewall is a security system that is used to control incoming and outgoing network traffic by analyzing data packets and determining whether they should be allowed through or not.

- Firewalls can be Network Firewall and Application Firewall:

- Network Firewall

- ⇒ A Network Firewall is implemented at the network level, which means it controls all the traffic that flows in and out of the network.

- ⇒ It uses security algorithms and router communications protocols to prevent outsiders from accessing the corporate database and e-mail systems.

- Application Firewall

- ⇒ An Application Firewall, on the other hand, is implemented at the application level.

⇒ It controls the traffic that flows in and out of specific programs or applications.

- Antivirus Software
  - Antivirus Software is a program or set of programs that are designed to prevent, detect, and remove malware from a computer or mobile device.
- Virtual Private Network (VPN)
  - A Virtual Private Network (VPN) is a technology that allows users to securely connect to a private network over the Internet.

## Cloud Computing

- Cloud Computing is the delivery of computing services—including servers, storage, databases, networking, software, analytics, and intelligence—over the Internet (“The Cloud”) to offer faster innovation, flexible resources, and economies of scale.
- Examples of Cloud Computing providers include Amazon Web Services (AWS), Microsoft Azure, and Google Cloud Platform (GCP).
- Types of Cloud
  - Private Cloud
    - A Private Cloud is a cloud computing environment that is dedicated to a single organization.
  - Community Cloud
    - A Community Cloud is a type of cloud computing environment that is shared by a specific group of organizations with similar requirements and concerns.
  - Public Cloud
    - A Public Cloud is a type of cloud computing environment where resources, such as servers, storage, and applications, are made available to the general public over the Internet.
    - Public Clouds are owned and operated by third-party companies, such as Amazon Web Services (AWS), Microsoft Azure, and Google Cloud Platform (GCP).
  - Hybrid Cloud
    - A Hybrid Cloud is a type of cloud computing environment that combines the benefits of both public and private clouds.

- Cloud Computing Service Models
  - Cloud Computing Service Models are categorized based on the type of access and ownership of the underlying infrastructure
  - Infrastructure as a Service (IaaS)
    - Infrastructure as a Service (IaaS) is a type of cloud computing service model that provides virtualized computing resources, such as servers, storage, and networking, over the Internet.
    - Examples of IaaS providers include Amazon Web Services (AWS), Microsoft Azure, and Google Cloud Platform (GCP).
  - Software as a Service (SaaS)
    - Software as a Service (SaaS) is a type of cloud computing service model that provides software applications over the Internet, which can be accessed on demand.
    - SaaS is a delivery model where software vendors host and maintain their software applications and make them available to customers over the Internet.
    - Examples of SaaS providers include Office 365, Salesforce, Zoom, G-Suite, Adobe Creative Cloud, Slack, and many more.
  - Platform as a Service (PaaS)
    - Platform as a Service (PaaS) is a type of cloud computing service model that provides a platform for developing, running, and managing applications without the need for users to worry about the underlying infrastructure.
    - Examples of PaaS providers include Heroku, Salesforce App Cloud, Google App Engine, AWS Elastic Beanstalk, and Azure App Service.
- Roles and Responsibilities of Cloud Service Providers
  - Infrastructure Management
    - Cloud Service Providers are responsible for setting up, maintaining, and managing the physical infrastructure required to deliver cloud services.
  - Resource Provisioning
    - One of the primary responsibilities of a Cloud Service Provider is to provide on-demand computing resources, such as processing power, memory, storage, and networking.
  - Service Reliability and Availability
    - Cloud Service Providers must ensure that their services are reliable and available to their customers.

- Security and Compliance
  - Cloud Service Providers are responsible for implementing robust security measures to protect their customers' data and applications.
- Platform and Software Management
  - In the case of PaaS and SaaS offerings, cloud Service Providers are responsible for managing the underlying platforms and software applications, respectively.
- Customer Support and Service
  - Cloud Service Providers are responsible for providing customer support and assistance, which may include technical support, documentation, training, and consulting services.
- Billing and Cost Management
  - Cloud Service Providers offer flexible, pay-as-you-go pricing models, which require them to monitor and track customers' resource usage accurately.
- Service-Level Agreements (SLAs)
  - Cloud Service Providers establish Service-Level Agreements (SLAs) with their customers, outlining the performance, availability, and support standards they commit to.
- Innovation and Scalability
  - Cloud Service Providers must continuously innovate and improve their services to stay competitive in the rapidly evolving cloud computing landscape.
- Cloud Computing Governance
  - Cloud Computing Governance refers to the process of establishing and implementing a set of policies, procedures, and guidelines to ensure that an organization's cloud computing resources are effectively managed, secure, compliant, and aligned with its overall business objectives.
  - Cloud Computing Governance encompasses several key elements, including:
    - Strategy and Goals
      - Defining the organization's cloud computing strategy, aligning it with business objectives, and setting clear goals for cloud adoption, migration, and management
    - Risk Management
    - Policies and Procedures

- Establishing and documenting cloud-specific policies, procedures, and guidelines that cover areas like data management, security, privacy, and vendor management
  - Roles and Responsibilities
    - Defining and assigning roles and responsibilities for cloud governance within the organization.
  - Compliance and Legal Requirements
    - Ensuring that the organization's cloud computing activities comply with relevant laws, regulations, and industry standards, such as GDPR, HIPAA, and SOC 2.
  - Vendor Management
  - Performance Measurement and Monitoring
  - Training and Awareness
  - Incident Management and Response
- Role of COSO Frameworks in Cloud Computing Governance
    - Role of COSO Internal Control Framework in Cloud Computing Governance
      - Control Environment
        - Establish a strong Control Environment for cloud computing by setting a tone at the top that emphasizes the importance of cloud security, compliance, and risk management.
      - Risk Assessment
        - Conduct a comprehensive Risk Assessment to identify and prioritize cloud-related risks, such as data security, privacy, vendor management, regulatory compliance, and operational risks.
      - Control Activities
        - Implement cloud-specific control activities to mitigate identified risks, such as access controls, data classification, encryption, intrusion detection and prevention systems, and incident response plans.
      - Information and Communication
        - Develop effective communication channels to share relevant information about cloud governance, such as policies, procedures, and risk assessments, both within the organization and with external stakeholders.

- Monitoring Activities
  - Establish a Monitoring program to evaluate the effectiveness of cloud governance efforts, including the performance of control activities and the organization's adherence to cloud-related policies and procedures.
- Role of COSO Enterprise Risk Management Framework in Cloud Computing Governance
  - Governance and Culture
    - Establish a strong risk culture for cloud computing by setting a tone at the top that emphasizes the importance of cloud security, compliance, and risk management.
    - Define clear roles and responsibilities for managing cloud resources and embed risk awareness throughout the organization.
    - Develop risk appetite and tolerance statements specific to cloud computing and ensure they are aligned with the organization's overall risk appetite and strategic objectives.
  - Strategy and Objective Setting
    - Integrate cloud computing risks and opportunities into the organization's strategy-setting process.
  - Performance
    - Identify, assess, and prioritize cloud-related risks and opportunities, such as data security, privacy, vendor management, regulatory compliance, and operational risks.
    - Establish risk tolerances, risk response strategies, and performance metrics to monitor risk management effectiveness for cloud computing.
  - Review and Revision
    - Continuously evaluate and improve the organization's cloud computing governance and risk management practices, identifying and addressing deficiencies and gaps, learning from past events, and enhancing risk management capabilities.
  - Information, Communication, and Reporting
    - Ensure that relevant and timely risk-related information for cloud computing is identified, captured, and communicated within the organization and to external parties.
    - Enable all personnel to understand their risk management responsibilities, adhere to cloud governance requirements, and make informed decisions.
    - Develop information systems and communication channels that support the flow of information, both vertically and horizontally, across the organization.