TEST BANK: INCOME TAX FUNDAMENTALS, 38TH EDITION, GERALD E. WHITTENBURG, MARTHA ALTUS-BULLER, STEVEN GILL

Chapter 1: The Individual Income Tax Return

1. A corporation is a reporting entity but not a tax-paying entity.
True   False

2. Partnership capital gains and losses are allocated separately to each of the partners.
True   False

3. Married taxpayers may double their standard deduction amount by filing separate returns.
True   False

4. An item is not included in gross income unless the tax law specifies that the item is subject to taxation.
True   False

5. For taxpayers who do not itemize deductions, the standard deduction amount is subtracted from the taxpayer's adjusted gross income.
True   False

6. A taxpayer with self-employment income of $600 must file a tax return.
True   False

7. A dependent child with earned income in excess of the available standard deduction amount must file a tax return.
True   False

8. A single taxpayer, who is not blind and who is under age 65, with income of $8,750 must file a tax return.
True   False

9. If a taxpayer is due a refund, it will be mailed to the taxpayer regardless of whether he or she files a tax return.
True False

10. Taxpayers with self-employment income of $400 or more must file a tax return.
True False

11. If your spouse dies during the tax year and you do not remarry, you must file as single for the year of death.
True False

12. Taxpayers who do not qualify for married, head of household, or qualifying widow or widower filing status must file as single.
True False

13. If an unmarried taxpayer paid more than half the cost of keeping a home which is the principal place of residence of a nephew, who is not her dependent, she may use the head of household filing status.
True False

14. The maximum official individual income tax rate for 2012 is 35 percent.
True False

15. All taxpayers may use the tax rate schedule to determine their tax liability.
True False

16. The head of household tax rates are higher than the rates for a single taxpayer.
True False

17. Most states are community property states.
True False

18. If taxpayers are married and living together at the end of the year, they must file a joint tax return.
True False

19. A taxpayer who maintains a household with an unmarried child may qualify to file as head of household even if the child is not the taxpayer's dependent.
True False

20. A married person with a dependent child may choose to file as head of household if it reduces his or her tax liability.
True False

21. A taxpayer who is living alone and is legally separated from his or her spouse under a separate maintenance decree at year-end should file as single.
True False

22. An individual, age 22, enrolled on a full-time basis at a trade school, is considered a student for purposes of determining whether a dependency exemption is permitted.
True False

23. A dependency exemption may be claimed by the supporting taxpayer in the year of death of a dependent.
True False

24. For 2012, personal and dependency exemptions are $3,800 each.
True False

25. Scholarships received by a student may be excluded for purposes of the support test for determining the availability of the dependency exemption.
True False

26. The two types of exemptions are the personal exemption and the dependency exemption.
True False

27. A child for whom a dependency exemption is claimed on the parents' tax return may also claim a personal exemption on his or her own tax return.
True False

28. If a taxpayer's adjusted gross income exceeds certain threshold amounts, he or she may be required to reduce the amount of the otherwise allowable deductions for itemized deductions and personal and dependency exemptions in 2012.
True False

29. Most taxpayers may deduct the standard deduction amount or the amount of their itemized deductions, whichever is higher.
True False

30. An individual taxpayer with a net capital loss may deduct up to $3,000 per year against ordinary income.
True False

31. Taxpayers can download tax forms from the IRS Internet site.
True False

32. Which of the following is not a goal of the tax law?
A. Encouraging certain social goals such as contributions to charity.
B. Encouraging certain economic goals such as a thriving business community.
C. Encouraging smaller families.
D. Raising revenue to operate the government.
E. None of the above are goals of the tax law.

33. Which one of the following provisions was passed by Congress to meet a social goal of the tax law?
A. The deduction for job hunting expenses
B. The charitable deduction
C. The moving expense deduction for adjusted gross income
D. The deduction for soil and water conservation costs available to farmers
E. None of the above

34. Wesley owns and operates the Cheshire Chicken Ranch in Turpid, Nevada. The income from this ranch is $49,000. Wesley wishes to use the easiest possible tax form. He may file:
A. Form 1040EZ
B. Form 1040A
C. Form 1040
D. Form 1065
E. None of the above.

35. Which of the following forms may be filed by individual taxpayers?
A. Form 1040
B. Form 1041
C. Form 1065
D. Form 1120
E. None of the above

36. Partnerships:
A. Are not taxable entities
B. Are taxed in the same manner as individuals
C. File tax returns on Form 1120
D. File tax returns on Form 1041

37. Which of the following is correct?
A. An individual is a reporting entity but not a taxable entity
B. A partnership is a taxable entity and a reporting entity
C. A corporation is a reporting entity but not a taxable entity
D. A partnership is a reporting entity but not a taxable entity

38. Form 1040 allows a taxpayer to report which of the following items that are not allowed for taxpayers who file form 1040A.
A. Salary income
B. Joint return status
C. Withholding on wages
D. Self-employment income

39. Partnership income is reported on:
A. Form 1040PTR
B. Form 1120S
C. Form 1040X
D. Form 1065

40. Amended returns are filed on:
A. Form 1040X
B. Form 1120S
C. Form 1041
D. Form 1040Amend

41. Depending on the amounts of income and other tax information, some individuals may report their income on:
A. Form 1040A
B. Form 1065
C. Form 1120
D. Form 1041

42. If an individual wishes to amend his individual tax return, he will make the amendment using what form?
A. Form 1040A
B. Form 1040X
C. Form 1120
D. Schedule K-1
E. None of the above

43. Eugene and Velma are married. For 2012, Eugene earned $25,000 and Velma earned $30,000. They have decided to file separate returns and are each entitled to claim one personal exemption. They have no deductions for adjusted gross income. Eugene's itemized deductions are $11,200 and Velma's are $4,000. Assuming Eugene and Velma do not live in a community property state, what is Velma's taxable income?
A. $14,300
B. $20,350
C. $26,000
D. $22,200
E. None of the above

44. An individual is a head of household. What is her standard deduction?
A. $11,900
B. $5,950
C. $14,600
D. $8,700
E. None of the above

45. Eugene and Velma are married. For 2012, Eugene earned $25,000 and Velma earned $30,000. They have decided to file separate returns and are each entitled to claim one personal exemption. They have no deductions for adjusted gross income. Eugene's itemized deductions are $11,200 and Velma's are $4,000. Assuming Eugene and Velma do not live in a community property state, what is Eugene's taxable income?
A. $25,000
B. $13,800
C. $13,600
D. $10,000
E. None of the above

46. Oscar and Mary have no dependents and file a joint income tax return for 2012. They have adjusted gross income of $145,000 and itemized deductions of $32,000. What is the amount of taxable income that Oscar and Mary must report on their 2012 income tax return?
A. $113,000
B. $109,200
C. $125,500
D. $129,300
E. $105,400

47. Which of the following taxpayers does *not* have to file a tax return for 2012?
A. A single taxpayer who is under age 65, with income of $10,000.
B. Married taxpayers (ages 45 and 50 years), filing jointly, with income of $21,000.
C. A student, age 22, with unearned income of $1,200 who is claimed as a dependent by her parents.
D. A qualifying widow (age 67) with a dependent child and income of $14,500.
E. All of the above taxpayers must file a return.

48. In which of the following situations is the taxpayer not required to file an income tax return?
A. When an individual has a 2012 income tax refund and would like to obtain it.
B. When the taxpayer is a single 67-year-old with wages of $9,800 in 2012.
C. When the taxpayer is a 35-year-old head of household with wages of $16,800 in 2012.
D. When the taxpayer is a 79-year-old widow with wages of $16,500 in 2012.
E. When the taxpayers are a married couple with both spouses under 65 years old with wages of $19,800 in 2012.

49. All of the following factors are important in determining whether an individual is required to file an income tax return, *except*:
A. The taxpayer's filing status
B. The taxpayer's gross income
C. The taxpayer's total itemized deductions
D. The availability of the additional standard deduction for taxpayers who are elderly
E. None of the above

50. John, age 25, is a full-time student at a state university. John lives with his sister, Ann, who provides over half of his support. His only income is $4,000 of wages from a part-time job at the college book store. What is Ann's filing status for 2012?
A. Single
B. Head of household
C. Married, filing separately
D. Qualifying widow(er)
E. None of the above

51. Robert is a single taxpayer who has AGI of $145,000 in 2012; his taxable income is $122,000. What is his federal tax liability for 2012?
A. $34,160
B. $27,087
C. $27,621
D. $22,750
E. $42,449

52. William is a divorced taxpayer who provides a home for his dependent child, Edward. What filing status should William indicate on his tax return?
A. Head of household
B. Married, filing separately
C. Single
D. Qualifying widow(er)
E. None of the above.

53. Irma, widowed in 2011, pays all costs related to the home in which she and her unmarried son live. Her son does not qualify as her dependent. What is her filing status for 2012?
A. Single
B. Married, filing separate
C. Head of household
D. Qualifying widow or widower
E. None of the above.

54. Alan, whose wife died in 2010, filed a joint tax return for 2010. He did not remarry and continues to maintain his home in which his four dependent children live. In the preparation of his tax return for 2012, Alan should file as:
A. A single individual
B. Qualifying widow(er)
C. Head of household
D. Married, filing separately
E. None of the above

55. During 2012, Howard maintained his home in which he and his 16-year-old son resided. The son qualifies as his dependent. Howard's wife died in 2011. What is his filing status for 2012?
A. Single
B. Head of household
C. Married, filing separately
D. Qualifying widow or widower
E. None of the above.

56. An unmarried taxpayer who maintains a household for a dependent child and whose spouse died 4 years ago should file as:
A. Single
B. Head of household
C. Qualifying widow or widower
D. Married, filing separately
E. None of the above

57. John, 45 years old and unmarried, contributed $1,000 monthly in 2012 to the support of his parents' household. The parents lived alone and their income for 2012 consisted of $500 from dividends and interest. What is John's filing status and how many exemptions should he claim on his 2012 tax return?
A. Single and 1 exemption
B. Head of household and 1 exemption
C. Single and 3 exemptions
D. Head of household and 3 exemptions
E. None of the above.

58. During 2012, Murray, who is 60 years old and unmarried, provided all of the support of his elderly mother. His mother was a resident of a home for the aged for the entire year and had no income. What is Murray's filing status for 2012, and how many exemptions should he claim on his tax return?
A. Head of household and 2 exemptions
B. Single and 2 exemptions
C. Head of household and 1 exemption
D. Single and 1 exemption
E. None of the above.

59. During 2012, Anita was entirely supported by her three sons, Dudley, Carlton, and Isidore, who provided support for her in the following percentages:

Dudley	8 percent
Carlton	45 percent
Isidore	47 percent

Which of the brothers may be allowed to claim his mother as a dependent, assuming a multiple support agreement exists?
A. Dudley
B. Dudley or Carlton
C. Carlton or Isidore
D. Dudley, Carlton, or Isidore
E. None of the above.

60. Ronald is 92 years old and in poor health. Clever investing earlier in his life has left him with a sizeable income. He is able to support his son Ed. Ed is 67 years old and a bit "confused," so he lives in a nursing home. Ed’s income is less than $2,000. How many exemptions should Ronald claim on his tax return?
A. 1
B. 2
C. 3
D. 4
E. None of the above

61. Which of the following is a true statement with respect to the gross income test for the qualifying relative dependency exemption?
A. The relative must receive less than $3,800 of gross income in order to qualify.
B. The gross income test does not have to be met provided the relative is under age 19 at the end of the tax year.
C. The gross income test does not have to be met provided the relative is under age 24 at the end of the tax year.
D. The gross income test does not have to be met provided the relative is a student.
E. All of the above statements are true.

62. Albert and Louise, ages 66 and 64 respectively, filed a joint return for 2012. They provided all of the support for their blind 19-year-old son, who had no gross income. They also provided the total support of Louise's father, who is a citizen and life-long resident of Peru. How many exemptions may they claim on their 2012 tax return?
A. 2
B. 3
C. 4
D. 5
E. None of the above.

63. Which of the following relatives will not satisfy the relationship test for the dependency exemption?
A. Sister
B. Adopted child
C. Aunt
D. Parent
E. All of the above satisfy the test

64. Which of the following is not a test that must be met for a child to be considered a dependent?
A. Age test
B. Domicile test
C. Citizenship test
D. Relationship test
E. Blood test

65. Mr. and Mrs. Vonce, both age 62, file a joint return for 2012. They provided all the support for their daughter who is 19, legally blind, and who earns no income. Their son, age 21 and a full-time student at a university, had $4,200 of income and provided 70 percent of his own support during 2012. How many exemptions may Mr. and Mrs. Vonce claim on their 2012 tax return?
A. 2
B. 3
C. 4
D. 5
E. None of the above.

66. Taxpayers who are blind get the benefit of:
A. An extra exemption
B. An additional amount added to their standard deduction
C. Two standard deductions
D. None of the above

67. Martin, a 50-year-old single taxpayer, paid the full cost of maintaining his dependent mother in a home for the aged for the entire year. What is the amount of Martin's standard deduction for 2012?
A. $5,950
B. $8,700
C. $9,950
D. $10,600
E. None of the above.

68. Jill is a 16-year-old child who is claimed as a dependent by her parents. Jill's only income is $1,400 from her bank savings account. What is the amount of Jill's standard deduction for 2012?
A. $1,200
B. $950
C. $3,800
D. $5,950
E. None of the above

69. Your standard deduction will be $5,950 in 2012 if you are:
A. Single and 67 years old.
B. Single and 45 years old.
C. Single, 27 years old and blind.
D. A nonresident alien.
E. A married individual filing a separate return and your spouse itemizes his deductions.

70. Brian (60 years old) is single and legally blind. Brian supports his father, who is 88 years old and blind, by paying the rent and other costs of his father’s residence. What is the total standard deduction amount that Brian should claim on his 2012 tax return?
A. $7,250
B. $13,050
C. $10,150
D. $12,050
E. None of the above.

71. Clay purchased Elm Corporation stock 20 years ago for $10,000. In 2012, he sells the stock for $29,000. What is Clay's gain or loss?
A. $19,000 long-term
B. $19,000 short-term
C. $19,000 ordinary
D. $3,000, with the excess carried forward
E. No gain or loss is recognized on this transaction

72. Alexis has a long-term capital loss of $13,000 on the sale of stock in 2012. Her taxable income without this transaction is $60,000. What is her taxable income considering this capital loss?
A. $60,000
B. $57,000
C. $54,000
D. $47,000
E. Some other amount

73. Which of the following is not a capital asset?
A. Inventory
B. Stocks
C. A personal automobile
D. Gold
E. Land

74. Bob owns a rental property that he bought several years ago for $260,000. He has taken depreciation on the house of $37,000 since buying it. He sells it in 2012 for $290,000. His selling expenses were $12,000 for the year. What was Bob's realized gain on the sale?
A. $30,000
B. $55,000
C. $67,000
D. $18,000
E. None of the above.

75. The IRS:
A. has a YouTube video site
B. links to the H & R Block Web site
C. provides information on how to choose a stock
D. has a game page

76. Internet users can sign on to http://www.irs.gov/ and
A. Download tax forms and publications
B. Find links to other useful IRS pages
C. Use a search function to find forms and publications
D. All of the above

77. Electronic filing (e-filing)
A. Reduces the chances that the IRS will make mistakes when inputting tax return information
B. Generally results in a slower refund
C. Can be done only by telephone
D. Requires the services of a professional

78. Electronically filed tax returns:
A. May not be transmitted from a taxpayer’s home computer
B. Constitute more than 90 percent of the returns filed with the IRS
C. Have error rates similar to paper returns
D. Offer faster refunds than paper returns

79. Mark a “Yes” to each of the following if it is an objective of the tax code. Otherwise mark with a “No”.
a. To provide a car to each American
b. To promote giving to charities
c. To encourage taxpayers to send their children to college
d. To raise money to operate the government
e. To promote the use of solar energy

80. List two general objectives of the tax code.

81. Mark each of the following as a taxable entity or as a reporting entity:
a. Individuals
b. Corporations
c. Partnerships

82. List if a form is used for an individual, a corporation, or a partnership tax return.
a. Form 1065
b. Schedule A, Itemized Deductions
c. Form 1040
d. Form 1120
e. Schedule B, Interest and Dividends

83. Barry (age 45) is a single taxpayer. In 2012, he has gross income of $15,000 and itemized deductions of $6,500. If Barry claims one exemption on his 2012 income tax return, calculate the following amounts:

a. His personal exemption amount
b. Barry's taxable income

84. What is the formula for computing taxable income, as summarized in the text?

85. Mary (age 33) is a single taxpayer with adjusted gross income for 2012 of $21,040. Mary maintains a home for two dependent children and has itemized deductions of $3,000. Calculate the following amounts for Mary's 2012 income tax return:

a. The number of exemptions claimed
b. Mary's standard or itemized deduction amount
c. Mary's taxable income

86. Kenzie is a research scientist in Tallahassee, Florida. Her husband Gary stays home to take care of their two young children. Kenzie's total wages for 2012 were $60,000 from which $6,500 of federal income tax was withheld.

Calculate the income tax due with, or refund receivable from, Kenzie and Gary's 2012 individual income tax return. Use the tax formula for individuals and show your work.

87. Betty (age 39) and Steve (age 50) are married with two dependent children. They file a joint return for 2012. Their income from salaries totals $155,400; they receive $1,000 in taxable interest and $2,000 in royalties. Their deductions for adjusted gross income amount to $3,200; they have itemized deductions totaling $40,000. Calculate the following amounts:

a. Gross income
b. Adjusted gross income
c. Itemized deduction or standard deduction amount
d. Deduction for exemptions
e. Taxable income
f. Regular income tax liability from rate schedules

88. Melissa is a 35-year-old single taxpayer with adjusted gross income of $49,000. She uses the standard deduction and has no dependents.

a. Calculate Melissa’s taxable income. Please show your work.
b. When you calculate Melissa’s tax liability, are you required to use the tax tables or the tax rate schedules, or does it matter?
c. What is Melissa’s tax liability?

89. Steven, age 35, is a single commodities broker. His salary for 2012 is $110,000 and he has taxable interest income of $40,000. He has no deductions for adjusted gross income. His itemized deductions are $30,000. Steven does not have any dependents.

a. What is the amount of his adjusted gross income?
b. What are his allowable itemized deductions?
c. What is his deduction for personal exemptions?
d. What is his taxable income?
e. What is his regular tax liability from the tax rate schedules?

90. Nathan is 24 years old and works as an accountant in a salmon cannery in Alaska. His total wages for 2012 were $32,000. Federal income tax of $4,500 was withheld from his wages. His only other income was $210 of interest and he had no deductible expenses.

Calculate the income tax due with, or refund receivable from, Nathan's 2012 individual income tax return. Use the tax formula for individuals and show your work.

91. In 2012, Len has a salary of $40,000 from his job. He also has interest income of $300. Len is single and has no dependents. During the year, Len sold stock held as an investment for a $10,000 loss. Calculate the following amounts for Len.

a. Adjusted gross income
b. Standard deduction
c. Exemption
d. Taxable income
e. Tax liability
f. Explain the tax treatment of the loss from the stock sale.

92. Roger (age 39) and Lucy (age 37) are married taxpayers who file a joint income tax return for 2012. They have gross income of $25,400. Their deductions for adjusted gross income are $550 and they have itemized deductions of $5,300. If Roger and Lucy claim two personal exemptions and no dependency exemptions for 2012, calculate the following amounts:

a. Their adjusted gross income
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

93. Hansel and Gretel are married taxpayers who file a joint income tax return for 2012. They have no dependents. On their 2012 income tax return, they have adjusted gross income of $62,000 and total itemized deductions of $4,000. What is their taxable income?

94. Rod (age 50) and Ann (age 49) are married taxpayers who file a joint return for 2012. They have gross income of $150,000. Their deductions for adjusted gross income are $5,000 and they have itemized deductions of $12,000, consisting of $7,000 in state income taxes and $5,000 in mortgage interest expense. If they claim two personal exemptions and no dependency exemptions for 2012, calculate the following amounts:

a. Their adjusted gross income
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

95. Theodore (age 74) and Maureen (age 59) are married taxpayers with two dependents. Their adjusted gross income for the 2012 tax year is $43,000, and they have itemized deductions of $7,750. Determine the following for Theodore and Maureen's 2012 income tax return:

a. The number of exemptions
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

96. George (age 67) and Linda (age 60) are married taxpayers with two dependent children. Their adjusted gross income for the 2012 tax year is $138,000. They have itemized deductions of $24,000. Determine the following for their joint tax return for 2012:

a. The number of exemptions
b. Exemption deduction amount
c. The amount of their standard deduction or itemized deductions
d. Taxable income

97. Monica is a maid in a San Francisco hotel. Monica received $500 in unreported tips during 2012 and owes Social Security taxes on these tips. Her total income for the year, including tips, is $4,500. Is Monica required to file an income tax return for 2012?

Why?

98. For each of the following situations, indicate whether the taxpayer(s) is(are) required to file a tax return for 2012. Explain your answer.

a. Debra (age 68) and Jerry (age 70) are married and file a joint return. They received $22,000 in interest income from a savings account.
b. Margie is a single taxpayer with wages in 2012 of $8,400 and interest income of $200.
c. Janie (age 30) and Scott (age 28) are married and file a joint tax return. They had $17,000 in earnings from wages.
d. Kim, age 20, is a single college student who is claimed as a dependent by her parents. She earned $2,000 from a part-time job and has $450 in interest income.
e. Stefanie, a 25-year-old single taxpayer, has wages of $1,500, from which $80 of federal income tax was withheld.

99. Norman and Linda are married taxpayers with taxable income of $125,000.

a. When you calculate their tax liability are you required to use the tax tables or the tax rate schedules, or does it matter?
b. What is their tax liability?

100. Curt and Linda were married on December 31, 2012. What are their options for filing status for their 2012 taxes?

101. Madeline is single and supports her 85-year-old parents who live in a senior home paid for by Madeline and have no income. What is Madeline's filing status and why?

102. List each alternative filing status available to unmarried individual taxpayers.

103. Determine from the tax table or the tax rate schedule, whichever is appropriate, the amount of the income tax for each of the following taxpayers for 2012.

Taxpayer(s)	Filing Status	Taxable Income	Income Tax
Macintosh	Single	$35,680	
Hindmarsh	MFS	$62,100	
Kinney	MFJ	$142,000	
Rosenthal	H of H	$91,350	
Wilk	Single	$21,130	

104. Jeri is single and supports her 45-year-old son who has income of $350 from working in a pumpkin patch during October and lives in his own apartment.

a. Can she claim him as a dependent?
b. Can she claim head of household filing status? Why or why not?

105. If Jessica, a 17-year-old guitarist in a successful band, earns $100,000 a year and is completely self-supporting although she lives with her parents, can her parents claim her as a dependent? Why or why not?

106. Karl's father, Vronsky, who is a 60-year-old Russian citizen, lived in Russia for the full year. Karl supported Vronsky while he looked for work. Vronsky had no income. Can Karl claim Vronsky as a dependent?

107. Calculate the amount of the standard deduction the taxpayers should claim on their 2012 income tax returns.

a. Kelly and Glenn are married with one dependent child. They file a joint return, are in good health, and both of them are under 65 years of age. They also support her aging father.
b. Fran is 24 years old, in good health, and single.
c. George and Georgina are married and file a joint return. George is 64 years old and Georgina is 63.
d. Norm is 62, single and blind.
e. Kimberly qualifies for head of household filing status, is 42 years old, and is in good health.
f. Lizzie is 11 years old and her only income is $3,200 of interest on a savings account. She is claimed as a dependent on her parents' tax return.

108. How should a taxpayer decide whether to take the standard deduction or claim itemized deductions?

109. Mike purchased stock in MDH corporation 5 years ago for $15,250. This year he sold it for $12,800 and then paid a $150 sales commission to his broker.
a. What is Mike’s amount realized?
b. What is Mike’s adjusted basis?
c. What is Mike’s *realized* gain or loss?
d. What is Mike’s *recognized* gain or loss?
e. How much of the gain or loss can Mike report in his tax return?

110. Fran bought stock in the FCM corporation 4 years ago at a price of $18,000. She sold it this year for $22,500 and paid her broker $225 from the proceeds of the sale.
a. What is Fran’s amount realized?
b. What is Fran’s adjusted basis?
c. What is Fran’s *realized* gain or loss?
d. What is Fran’s *recognized* gain or loss?
e. How much of the gain or loss should be included in her tax return?

111. Mark a “Yes” to each of the following that can be found on the IRS Web site. If not, mark with a “No”.
a. A list of IRS forms
b. A search function
c. Advice on how to avoid paying taxes
d. Ways to contact the IRS

112. State two reasons why a person would want to e-file their return instead of mailing it.

113. Distinguish between reporting entities and taxable entities and give examples of each.

114. What is the difference between the standard deduction and itemized deductions?

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1. A corporation is a reporting entity but not a tax-paying entity.
FALSE

2. Partnership capital gains and losses are allocated separately to each of the partners.
TRUE

3. Married taxpayers may double their standard deduction amount by filing separate returns.
FALSE

4. An item is not included in gross income unless the tax law specifies that the item is subject to taxation.
FALSE

5. For taxpayers who do not itemize deductions, the standard deduction amount is subtracted from the taxpayer's adjusted gross income.
TRUE

6. A taxpayer with self-employment income of $600 must file a tax return.
TRUE

7. A dependent child with earned income in excess of the available standard deduction amount must file a tax return.
TRUE

8. A single taxpayer, who is not blind and who is under age 65, with income of $8,750 must file a tax return.
FALSE

9. If a taxpayer is due a refund, it will be mailed to the taxpayer regardless of whether he or she files a tax return.
FALSE

10. Taxpayers with self-employment income of $400 or more must file a tax return.
TRUE

11. If your spouse dies during the tax year and you do not remarry, you must file as single for the year of death.
FALSE

12. Taxpayers who do not qualify for married, head of household, or qualifying widow or widower filing status must file as single.
TRUE

13. If an unmarried taxpayer paid more than half the cost of keeping a home which is the principal place of residence of a nephew, who is not her dependent, she may use the head of household filing status.
FALSE

14. The maximum official individual income tax rate for 2012 is 35 percent.
TRUE

15. All taxpayers may use the tax rate schedule to determine their tax liability.
FALSE

16. The head of household tax rates are higher than the rates for a single taxpayer.
FALSE

17. Most states are community property states.
FALSE

18. If taxpayers are married and living together at the end of the year, they must file a joint tax return.
FALSE

19. A taxpayer who maintains a household with an unmarried child may qualify to file as head of household even if the child is not the taxpayer's dependent.
FALSE

20. A married person with a dependent child may choose to file as head of household if it reduces his or her tax liability.
FALSE

21. A taxpayer who is living alone and is legally separated from his or her spouse under a separate maintenance decree at year-end should file as single.
TRUE

22. An individual, age 22, enrolled on a full-time basis at a trade school, is considered a student for purposes of determining whether a dependency exemption is permitted.
TRUE

23. A dependency exemption may be claimed by the supporting taxpayer in the year of death of a dependent.
TRUE

24. For 2012, personal and dependency exemptions are $3,800 each.
TRUE

25. Scholarships received by a student may be excluded for purposes of the support test for determining the availability of the dependency exemption.
TRUE

26. The two types of exemptions are the personal exemption and the dependency exemption.
TRUE

27. A child for whom a dependency exemption is claimed on the parents' tax return may also claim a personal exemption on his or her own tax return.
FALSE

28. If a taxpayer's adjusted gross income exceeds certain threshold amounts, he or she may be required to reduce the amount of the otherwise allowable deductions for itemized deductions and personal and dependency exemptions in 2012.
FALSE

29. Most taxpayers may deduct the standard deduction amount or the amount of their itemized deductions, whichever is higher.
TRUE

30. An individual taxpayer with a net capital loss may deduct up to $3,000 per year against ordinary income.
TRUE

31. Taxpayers can download tax forms from the IRS Internet site.
TRUE

32. Which of the following is not a goal of the tax law?
A. Encouraging certain social goals such as contributions to charity.
B. Encouraging certain economic goals such as a thriving business community.
C. Encouraging smaller families.
D. Raising revenue to operate the government.
E. None of the above are goals of the tax law.

33. Which one of the following provisions was passed by Congress to meet a social goal of the tax law?
A. The deduction for job hunting expenses
B. The charitable deduction
C. The moving expense deduction for adjusted gross income
D. The deduction for soil and water conservation costs available to farmers
E. None of the above

34. Wesley owns and operates the Cheshire Chicken Ranch in Turpid, Nevada. The income from this ranch is $49,000. Wesley wishes to use the easiest possible tax form. He may file:
A. Form 1040EZ
B. Form 1040A
C. Form 1040
D. Form 1065
E. None of the above.

35. Which of the following forms may be filed by individual taxpayers?
A. Form 1040
B. Form 1041
C. Form 1065
D. Form 1120
E. None of the above

36. Partnerships:
A. Are not taxable entities
B. Are taxed in the same manner as individuals
C. File tax returns on Form 1120
D. File tax returns on Form 1041

37. Which of the following is correct?
A. An individual is a reporting entity but not a taxable entity
B. A partnership is a taxable entity and a reporting entity
C. A corporation is a reporting entity but not a taxable entity
D. A partnership is a reporting entity but not a taxable entity

38. Form 1040 allows a taxpayer to report which of the following items that are not allowed for taxpayers who file form 1040A.
A. Salary income
B. Joint return status
C. Withholding on wages
D. Self-employment income

39. Partnership income is reported on:
A. Form 1040PTR
B. Form 1120S
C. Form 1040X
D. Form 1065

40. Amended returns are filed on:
A. Form 1040X
B. Form 1120S
C. Form 1041
D. Form 1040Amend

41. Depending on the amounts of income and other tax information, some individuals may report their income on:
A. Form 1040A
B. Form 1065
C. Form 1120
D. Form 1041

42. If an individual wishes to amend his individual tax return, he will make the amendment using what form?
A. Form 1040A
B. Form 1040X
C. Form 1120
D. Schedule K-1
E. None of the above

43. Eugene and Velma are married. For 2012, Eugene earned $25,000 and Velma earned $30,000. They have decided to file separate returns and are each entitled to claim one personal exemption. They have no deductions for adjusted gross income. Eugene's itemized deductions are $11,200 and Velma's are $4,000. Assuming Eugene and Velma do not live in a community property state, what is Velma's taxable income?
A. $14,300
B. $20,350
C. $26,000
D. $22,200
E. None of the above

44. An individual is a head of household. What is her standard deduction?
A. $11,900
B. $5,950
C. $14,600
D. $8,700
E. None of the above

45. Eugene and Velma are married. For 2012, Eugene earned $25,000 and Velma earned $30,000. They have decided to file separate returns and are each entitled to claim one personal exemption. They have no deductions for adjusted gross income. Eugene's itemized deductions are $11,200 and Velma's are $4,000. Assuming Eugene and Velma do not live in a community property state, what is Eugene's taxable income?
A. $25,000
B. $13,800
C. $13,600
D. $10,000
E. None of the above

46. Oscar and Mary have no dependents and file a joint income tax return for 2012. They have adjusted gross income of $145,000 and itemized deductions of $32,000. What is the amount of taxable income that Oscar and Mary must report on their 2012 income tax return?
A. $113,000
B. $109,200
C. $125,500
D. $129,300
E. $105,400

47. Which of the following taxpayers does *not* have to file a tax return for 2012?
A. A single taxpayer who is under age 65, with income of $10,000.
B. Married taxpayers (ages 45 and 50 years), filing jointly, with income of $21,000.
C. A student, age 22, with unearned income of $1,200 who is claimed as a dependent by her parents.
D. A qualifying widow (age 67) with a dependent child and income of $14,500.
E. All of the above taxpayers must file a return.

48. In which of the following situations is the taxpayer not required to file an income tax return?
A. When an individual has a 2012 income tax refund and would like to obtain it.
B. When the taxpayer is a single 67-year-old with wages of $9,800 in 2012.
C. When the taxpayer is a 35-year-old head of household with wages of $16,800 in 2012.
D. When the taxpayer is a 79-year-old widow with wages of $16,500 in 2012.
E. When the taxpayers are a married couple with both spouses under 65 years old with wages of $19,800 in 2012.

49. All of the following factors are important in determining whether an individual is required to file an income tax return, *except*:
A. The taxpayer's filing status
B. The taxpayer's gross income
C. The taxpayer's total itemized deductions
D. The availability of the additional standard deduction for taxpayers who are elderly
E. None of the above

50. John, age 25, is a full-time student at a state university. John lives with his sister, Ann, who provides over half of his support. His only income is $4,000 of wages from a part-time job at the college book store. What is Ann's filing status for 2012?
A. Single
B. Head of household
C. Married, filing separately
D. Qualifying widow(er)
E. None of the above

51. Robert is a single taxpayer who has AGI of $145,000 in 2012; his taxable income is $122,000. What is his federal tax liability for 2012?
A. $34,160
B. $27,087
C. $27,621
D. $22,750
E. $42,449

52. William is a divorced taxpayer who provides a home for his dependent child, Edward. What filing status should William indicate on his tax return?
A. Head of household
B. Married, filing separately
C. Single
D. Qualifying widow(er)
E. None of the above.

53. Irma, widowed in 2011, pays all costs related to the home in which she and her unmarried son live. Her son does not qualify as her dependent. What is her filing status for 2012?
A. Single
B. Married, filing separate
C. Head of household
D. Qualifying widow or widower
E. None of the above.

54. Alan, whose wife died in 2010, filed a joint tax return for 2010. He did not remarry and continues to maintain his home in which his four dependent children live. In the preparation of his tax return for 2012, Alan should file as:
A. A single individual
B. Qualifying widow(er)
C. Head of household
D. Married, filing separately
E. None of the above

55. During 2012, Howard maintained his home in which he and his 16-year-old son resided. The son qualifies as his dependent. Howard's wife died in 2011. What is his filing status for 2012?
A. Single
B. Head of household
C. Married, filing separately
D. Qualifying widow or widower
E. None of the above.

56. An unmarried taxpayer who maintains a household for a dependent child and whose spouse died 4 years ago should file as:
A. Single
B. Head of household
C. Qualifying widow or widower
D. Married, filing separately
E. None of the above

57. John, 45 years old and unmarried, contributed $1,000 monthly in 2012 to the support of his parents' household. The parents lived alone and their income for 2012 consisted of $500 from dividends and interest. What is John's filing status and how many exemptions should he claim on his 2012 tax return?
A. Single and 1 exemption
B. Head of household and 1 exemption
C. Single and 3 exemptions
D. Head of household and 3 exemptions
E. None of the above.

58. During 2012, Murray, who is 60 years old and unmarried, provided all of the support of his elderly mother. His mother was a resident of a home for the aged for the entire year and had no income. What is Murray's filing status for 2012, and how many exemptions should he claim on his tax return?
A. Head of household and 2 exemptions
B. Single and 2 exemptions
C. Head of household and 1 exemption
D. Single and 1 exemption
E. None of the above.

59. During 2012, Anita was entirely supported by her three sons, Dudley, Carlton, and Isidore, who provided support for her in the following percentages:

Dudley	8 percent
Carlton	45 percent
Isidore	47 percent

Which of the brothers may be allowed to claim his mother as a dependent, assuming a multiple support agreement exists?
A. Dudley
B. Dudley or Carlton
C. Carlton or Isidore
D. Dudley, Carlton, or Isidore
E. None of the above.

60. Ronald is 92 years old and in poor health. Clever investing earlier in his life has left him with a sizeable income. He is able to support his son Ed. Ed is 67 years old and a bit "confused," so he lives in a nursing home. Ed's income is less than $2,000. How many exemptions should Ronald claim on his tax return?
A. 1
B. 2
C. 3
D. 4
E. None of the above

61. Which of the following is a true statement with respect to the gross income test for the qualifying relative dependency exemption?
A. The relative must receive less than $3,800 of gross income in order to qualify.
B. The gross income test does not have to be met provided the relative is under age 19 at the end of the tax year.
C. The gross income test does not have to be met provided the relative is under age 24 at the end of the tax year.
D. The gross income test does not have to be met provided the relative is a student.
E. All of the above statements are true.

62. Albert and Louise, ages 66 and 64 respectively, filed a joint return for 2012. They provided all of the support for their blind 19-year-old son, who had no gross income. They also provided the total support of Louise's father, who is a citizen and life-long resident of Peru. How many exemptions may they claim on their 2012 tax return?
A. 2
B. 3
C. 4
D. 5
E. None of the above.

63. Which of the following relatives will not satisfy the relationship test for the dependency exemption?
A. Sister
B. Adopted child
C. Aunt
D. Parent
E. All of the above satisfy the test

64. Which of the following is not a test that must be met for a child to be considered a dependent?
A. Age test
B. Domicile test
C. Citizenship test
D. Relationship test
E. Blood test

65. Mr. and Mrs. Vonce, both age 62, file a joint return for 2012. They provided all the support for their daughter who is 19, legally blind, and who earns no income. Their son, age 21 and a full-time student at a university, had $4,200 of income and provided 70 percent of his own support during 2012. How many exemptions may Mr. and Mrs. Vonce claim on their 2012 tax return?
A. 2
B. 3
C. 4
D. 5
E. None of the above.

66. Taxpayers who are blind get the benefit of:
A. An extra exemption
B. An additional amount added to their standard deduction
C. Two standard deductions
D. None of the above

67. Martin, a 50-year-old single taxpayer, paid the full cost of maintaining his dependent mother in a home for the aged for the entire year. What is the amount of Martin's standard deduction for 2012?
A. $5,950
B. $8,700
C. $9,950
D. $10,600
E. None of the above.

68. Jill is a 16-year-old child who is claimed as a dependent by her parents. Jill's only income is $1,400 from her bank savings account. What is the amount of Jill's standard deduction for 2012?
A. $1,200
B. $950
C. $3,800
D. $5,950
E. None of the above

69. Your standard deduction will be $5,950 in 2012 if you are:
A. Single and 67 years old.
B. Single and 45 years old.
C. Single, 27 years old and blind.
D. A nonresident alien.
E. A married individual filing a separate return and your spouse itemizes his deductions.

70. Brian (60 years old) is single and legally blind. Brian supports his father, who is 88 years old and blind, by paying the rent and other costs of his father's residence. What is the total standard deduction amount that Brian should claim on his 2012 tax return?
A. $7,250
B. $13,050
C. $10,150
D. $12,050
E. None of the above.

71. Clay purchased Elm Corporation stock 20 years ago for $10,000. In 2012, he sells the stock for $29,000. What is Clay's gain or loss?
A. $19,000 long-term
B. $19,000 short-term
C. $19,000 ordinary
D. $3,000, with the excess carried forward
E. No gain or loss is recognized on this transaction

72. Alexis has a long-term capital loss of $13,000 on the sale of stock in 2012. Her taxable income without this transaction is $60,000. What is her taxable income considering this capital loss?
A. $60,000
B. $57,000
C. $54,000
D. $47,000
E. Some other amount

73. Which of the following is not a capital asset?
A. Inventory
B. Stocks
C. A personal automobile
D. Gold
E. Land

74. Bob owns a rental property that he bought several years ago for $260,000. He has taken depreciation on the house of $37,000 since buying it. He sells it in 2012 for $290,000. His selling expenses were $12,000 for the year. What was Bob's realized gain on the sale?
A. $30,000
B. $55,000
C. $67,000
D. $18,000
E. None of the above.

75. The IRS:
A. has a YouTube video site
B. links to the H & R Block Web site
C. provides information on how to choose a stock
D. has a game page

76. Internet users can sign on to http://www.irs.gov/ and
A. Download tax forms and publications
B. Find links to other useful IRS pages
C. Use a search function to find forms and publications
D. All of the above

77. Electronic filing (e-filing)
A. Reduces the chances that the IRS will make mistakes when inputting tax return information
B. Generally results in a slower refund
C. Can be done only by telephone
D. Requires the services of a professional

78. Electronically filed tax returns:
A. May not be transmitted from a taxpayer's home computer
B. Constitute more than 90 percent of the returns filed with the IRS
C. Have error rates similar to paper returns
D. Offer faster refunds than paper returns

79. Mark a "Yes" to each of the following if it is an objective of the tax code. Otherwise mark with a "No".
a. To provide a car to each American
b. To promote giving to charities
c. To encourage taxpayers to send their children to college
d. To raise money to operate the government
e. To promote the use of solar energy

a. No
b. Yes
c. Yes
d. Yes
e. Yes

80. List two general objectives of the tax code.

The tax code promotes social goals and economic goals.

81. Mark each of the following as a taxable entity or as a reporting entity:
a. Individuals
b. Corporations
c. Partnerships

a. Taxable entity
b. Taxable entity
c. Reporting entity

82. List if a form is used for an individual, a corporation, or a partnership tax return.
a. Form 1065
b. Schedule A, Itemized Deductions
c. Form 1040
d. Form 1120
e. Schedule B, Interest and Dividends

a. Partnership
b. Individual
c. Individual
d. Corporation
e. Individual

83. Barry (age 45) is a single taxpayer. In 2012, he has gross income of $15,000 and itemized deductions of $6,500. If Barry claims one exemption on his 2012 income tax return, calculate the following amounts:

a. His personal exemption amount
b. Barry's taxable income

a. $3,800
b. $4,700 = $15,000 - 6,500 - 3,800

84. What is the formula for computing taxable income, as summarized in the text?

Gross income
- <u>Deductions for adjusted gross income</u>
= Adjusted gross income
- Greater of itemized deductions or standard deduction
- <u>Exemptions</u>
= Taxable income

85. Mary (age 33) is a single taxpayer with adjusted gross income for 2012 of $21,040. Mary maintains a home for two dependent children and has itemized deductions of $3,000. Calculate the following amounts for Mary's 2012 income tax return:

a. The number of exemptions claimed
b. Mary's standard or itemized deduction amount
c. Mary's taxable income

a. 3
b. $8,700
c. $940 = $21,040 - 8,700 - 11,400

86. Kenzie is a research scientist in Tallahassee, Florida. Her husband Gary stays home to take care of their two young children. Kenzie's total wages for 2012 were $60,000 from which $6,500 of federal income tax was withheld.

Calculate the income tax due with, or refund receivable from, Kenzie and Gary's 2012 individual income tax return. Use the tax formula for individuals and show your work.

Gross income	$60,000
Deductions for adjusted gross income	-0-
Adjusted gross income	$60,000
Standard deduction	(11,900)
Personal exemptions (4)	(15,200)
Taxable income	$32,900
Gross tax liability (from tax table)	$ 4,069
Tax withheld	(6,500)
Refund due	$(2,431)

87. Betty (age 39) and Steve (age 50) are married with two dependent children. They file a joint return for 2012. Their income from salaries totals $155,400; they receive $1,000 in taxable interest and $2,000 in royalties. Their deductions for adjusted gross income amount to $3,200; they have itemized deductions totaling $40,000. Calculate the following amounts:

a. Gross income
b. Adjusted gross income
c. Itemized deduction or standard deduction amount
d. Deduction for exemptions
e. Taxable income
f. Regular income tax liability from rate schedules

a. $158,400 = $155,400 + $1,000 + $2,000
b. $155,200 = $158,400 - $3,200
c. $40,000
d. $15,200 = 4 ´ $3,800
e. $100,000 = $155,200 - $40,000 - $15,200
f. $17,060 (tax rate schedule: $9,735 + 25% ($100,000 - $70,700)

88. Melissa is a 35-year-old single taxpayer with adjusted gross income of $49,000. She uses the standard deduction and has no dependents.

a. Calculate Melissa’s taxable income. Please show your work.
b. When you calculate Melissa’s tax liability, are you required to use the tax tables or the tax rate schedules, or does it matter?
c. What is Melissa’s tax liability?

a. $39,250 = $49,000 - $5,950 -$3,800
b. Taxpayers with income less than $100,000 must use the tax tables.
c. $5,849

89. Steven, age 35, is a single commodities broker. His salary for 2012 is $110,000 and he has taxable interest income of $40,000. He has no deductions for adjusted gross income. His itemized deductions are $30,000. Steven does not have any dependents.

a. What is the amount of his adjusted gross income?
b. What are his allowable itemized deductions?
c. What is his deduction for personal exemptions?
d. What is his taxable income?
e. What is his regular tax liability from the tax rate schedules?

a. $150,000 = $110,000 + $40,000
b. $30,000
c. $3,800
d. $116,200 = $150,000 - $30,000 - $3,800
e. $25,997 [tax rate schedule: $17,443 + .28 ($116,200 - $85,650)]

90. Nathan is 24 years old and works as an accountant in a salmon cannery in Alaska. His total wages for 2012 were $32,000. Federal income tax of $4,500 was withheld from his wages. His only other income was $210 of interest and he had no deductible expenses.

Calculate the income tax due with, or refund receivable from, Nathan's 2012 individual income tax return. Use the tax formula for individuals and show your work.

Gross income	$32,210
Deductions for adjusted gross income	-0-
Adjusted gross income	$32,210
Standard deduction	(5,950)
Personal exemption	(3,800)
Taxable income	$22,460
Gross tax liability (from tax table)	$ 2,936
Tax withheld	(4,500)
Refund due	$ (1,564)

91. In 2012, Len has a salary of $40,000 from his job. He also has interest income of $300. Len is single and has no dependents. During the year, Len sold stock held as an investment for a $10,000 loss. Calculate the following amounts for Len.

a. Adjusted gross income
b. Standard deduction
c. Exemption
d. Taxable income
e. Tax liability
f. Explain the tax treatment of the loss from the stock sale.

a. $37,300 = $40,000 + $300 - $3,000
b. $5,950
c. $3,800
d. $27,550 = $37,300 - $5,950 - $3,800
e. $3,701 (tax table)
f. Up to $3,000 of capital loss per year can be deducted from ordinary income; any unused portion can be carried forward.

92. Roger (age 39) and Lucy (age 37) are married taxpayers who file a joint income tax return for 2012. They have gross income of $25,400. Their deductions for adjusted gross income are $550 and they have itemized deductions of $5,300. If Roger and Lucy claim two personal exemptions and no dependency exemptions for 2012, calculate the following amounts:

a. Their adjusted gross income
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

a. $24,850 = $25,400 - $550
b. $11,900
c. $5,350 = $24,850 - $11,900 - $7,600

93. Hansel and Gretel are married taxpayers who file a joint income tax return for 2012. They have no dependents. On their 2012 income tax return, they have adjusted gross income of $62,000 and total itemized deductions of $4,000. What is their taxable income?

$42,500 = $62,000 - $11,900 - $7,600

94. Rod (age 50) and Ann (age 49) are married taxpayers who file a joint return for 2012. They have gross income of $150,000. Their deductions for adjusted gross income are $5,000 and they have itemized deductions of $12,000, consisting of $7,000 in state income taxes and $5,000 in mortgage interest expense. If they claim two personal exemptions and no dependency exemptions for 2012, calculate the following amounts:

a. Their adjusted gross income
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

a. $145,000 = $150,000 - $5,000
b. $12,000
c. $125,400 = $145,000 - $12,000 - $7,600

95. Theodore (age 74) and Maureen (age 59) are married taxpayers with two dependents. Their adjusted gross income for the 2012 tax year is $43,000, and they have itemized deductions of $7,750. Determine the following for Theodore and Maureen's 2012 income tax return:

a. The number of exemptions
b. The amount of their standard deduction or itemized deductions
c. Their taxable income

a. 4
b. $13,050 = $11,900 + $1,150
c. $14,750 = $43,000 - $13,050 - $15,200

96. George (age 67) and Linda (age 60) are married taxpayers with two dependent children. Their adjusted gross income for the 2012 tax year is $138,000. They have itemized deductions of $24,000. Determine the following for their joint tax return for 2012:

a. The number of exemptions
b. Exemption deduction amount
c. The amount of their standard deduction or itemized deductions
d. Taxable income

a. 4
b. $15,200 = 4 x $3,800
c. $24,000
d. $98,800 = $138,000 - $24,000 - $15,200

97. Monica is a maid in a San Francisco hotel. Monica received $500 in unreported tips during 2012 and owes Social Security taxes on these tips. Her total income for the year, including tips, is $4,500. Is Monica required to file an income tax return for 2012?

Why?

Yes. Monica must file a return and pay Social Security taxes on the unreported tips.

98. For each of the following situations, indicate whether the taxpayer(s) is(are) required to file a tax return for 2012. Explain your answer.

a. Debra (age 68) and Jerry (age 70) are married and file a joint return. They received $22,000 in interest income from a savings account.
b. Margie is a single taxpayer with wages in 2012 of $8,400 and interest income of $200.
c. Janie (age 30) and Scott (age 28) are married and file a joint tax return. They had $17,000 in earnings from wages.
d. Kim, age 20, is a single college student who is claimed as a dependent by her parents. She earned $2,000 from a part-time job and has $450 in interest income.
e. Stefanie, a 25-year-old single taxpayer, has wages of $1,500, from which $80 of federal income tax was withheld.

a. Yes. The standard deduction of $11,900 plus $7,600 in personal exemptions plus 2 additional standard deductions of $1,150 each add up to $21,800, less than the income of $22,000.
b. No. Income of $8,600 is less than the sum of the $3,800 personal exemption plus the $5,950 standard deduction.
c. No. The income of $17,000 is less than the sum of the $7,600 personal exemptions plus the $11,900 standard deduction.
d. Yes. Gross income is more than the larger of $950 or $2,300 (earned income of $2,000 plus $300).
e. No. Stefanie is not required to file a tax return, but she must file if she wishes to receive a refund of the income tax withheld.

99. Norman and Linda are married taxpayers with taxable income of $125,000.

a. When you calculate their tax liability are you required to use the tax tables or the tax rate schedules, or does it matter?
b. What is their tax liability?

a. Taxpayers with incomes of $100,000 or more must use the tax rate schedules.
b. Tax liability: $23,310 = $9,735 + .25($125,000 - $70,700)

100. Curt and Linda were married on December 31, 2012. What are their options for filing status for their 2012 taxes?

They may file either as married filing joint or married filing separately. Even though they were married on the last day of the year, they must file as if they were married for the full year.

101. Madeline is single and supports her 85-year-old parents who live in a senior home paid for by Madeline and have no income. What is Madeline's filing status and why?

Head of household. Madeline is single, and Madeline's parents meet the tests to qualify as her dependents. Parents are the only exception to the requirement that dependents must live in the same household as the taxpayer to qualify the taxpayer for head of household status.

102. List each alternative filing status available to unmarried individual taxpayers.

Single.
Head of household.
Qualifying widow(er).

103. Determine from the tax table or the tax rate schedule, whichever is appropriate, the amount of the income tax for each of the following taxpayers for 2012.

Taxpayer(s)	Filing Status	Taxable Income	Income Tax
Macintosh	Single	$35,680	
Hindmarsh	MFS	$62,100	
Kinney	MFJ	$142,000	
Rosenthal	H of H	$91,350	
Wilk	Single	$21,130	

Macintosh, $4,949 (tax table)
Hindmarsh, $11,561 (tax table)
Kinney, $27,560 [tax rate schedule: $9,735 + .25($142,000 - $70,700)]
Rosenthal, $17,489 (tax table)
Wilk, $2,734 (tax table)

104. Jeri is single and supports her 45-year-old son who has income of $350 from working in a pumpkin patch during October and lives in his own apartment.

a. Can she claim him as a dependent?
b. Can she claim head of household filing status? Why or why not?

a. Yes, her son qualifies as a dependent
b. No. Her son must live in the same household with Jeri in order for Jeri to be able to file as head of household.

105. If Jessica, a 17-year-old guitarist in a successful band, earns $100,000 a year and is completely self-supporting although she lives with her parents, can her parents claim her as a dependent? Why or why not?

Because Jessica is self-supporting, her parents may not claim her as a dependent. The self-support test is applied to both children and relatives who otherwise qualify, so Jessica is disqualified.

106. Karl's father, Vronsky, who is a 60-year-old Russian citizen, lived in Russia for the full year. Karl supported Vronsky while he looked for work. Vronsky had no income. Can Karl claim Vronsky as a dependent?

Vronsky can not be claimed as a dependent because he is not a U.S. citizen.

107. Calculate the amount of the standard deduction the taxpayers should claim on their 2012 income tax returns.

a. Kelly and Glenn are married with one dependent child. They file a joint return, are in good health, and both of them are under 65 years of age. They also support her aging father.
b. Fran is 24 years old, in good health, and single.
c. George and Georgina are married and file a joint return. George is 64 years old and Georgina is 63.
d. Norm is 62, single and blind.
e. Kimberly qualifies for head of household filing status, is 42 years old, and is in good health.
f. Lizzie is 11 years old and her only income is $3,200 of interest on a savings account. She is claimed as a dependent on her parents' tax return.

a. $11,900
b. $5,950
c. $11,900
d. $7,400. An additional $1,450 is allowed due to blindness.
e. $8,700
f. $950. She is claimed as a dependent on her parents' tax return

108. How should a taxpayer decide whether to take the standard deduction or claim itemized deductions?

A taxpayer should claim the larger of the standard deduction or the total allowed itemized deductions since the amount reduces the taxpayer's income subject to tax.

109. Mike purchased stock in MDH corporation 5 years ago for $15,250. This year he sold it for $12,800 and then paid a $150 sales commission to his broker.
a. What is Mike's amount realized?
b. What is Mike's adjusted basis?
c. What is Mike's *realized* gain or loss?
d. What is Mike's *recognized* gain or loss?
e. How much of the gain or loss can Mike report in his tax return?

a. Amount realized: $12,650 = $12,800 - $150
b. Adjusted basis: $15,250
c. Realized loss: $12,800 - $150 - $15,250 = $2,600
d. Recognized loss: $12,800 - $150 - $15,250 = $2,600
e. $2,600. Up to $3,000 of capital loss can be written off each year.

110. Fran bought stock in the FCM corporation 4 years ago at a price of $18,000. She sold it this year for $22,500 and paid her broker $225 from the proceeds of the sale.
a. What is Fran's amount realized?
b. What is Fran's adjusted basis?
c. What is Fran's *realized* gain or loss?
d. What is Fran's *recognized* gain or loss?
e. How much of the gain or loss should be included in her tax return?

a. Amount realized: $22,275 = $22,500 - $225
b. Adjusted basis: $18,000
c. Realized gain: $22,500 - $225 - $18,000 = $4,275
d. Recognized gain: $22,500 - $225 - $18,000 = $4,275
e. $4,275. There is no limit on the amount of capital gain to be included in tax returns.

111. Mark a "Yes" to each of the following that can be found on the IRS Web site. If not, mark with a "No".
a. A list of IRS forms
b. A search function
c. Advice on how to avoid paying taxes
d. Ways to contact the IRS

a. Yes
b. Yes
c. No
d. Yes

112. State two reasons why a person would want to e-file their return instead of mailing it.

A return that is e-filed has a smaller error rate than paper-filed returns. (Less than 1 percent versus more than 20 percent). E-filing also offers a faster refund by direct depositing the refund into the taxpayer's bank account.

113. Distinguish between reporting entities and taxable entities and give examples of each.

A partnership is an example of a reporting entity. It pays no tax, but must report partnership income or loss and the allocation of income or loss to partners. Individuals, corporations, estates, and trusts are examples of taxable entities whose income is subject to federal income taxation.

114. What is the difference between the standard deduction and itemized deductions?

The standard deduction is a flat amount, varying based on a taxpayer's filing status (single, married, head of household, etc.), age, and vision, which is deducted from adjusted gross income (AGI) along with a taxpayer's exemptions to arrive at taxable income.

Itemized deductions are expenses paid by a taxpayer including medical expenses (over the 7.5 percent of AGI limit), various taxes, home mortgage interest and investment interest, charitable contributions, personal casualty losses and miscellaneous deductions (over the 2 percent of AGI limit). If the total itemized deductions are larger than the taxpayer's standard deduction the taxpayer should complete Schedule A, listing all itemized deductions, and use this amount instead of the standard deduction. By itemizing deductions when they are larger than the standard deduction, taxpayers may reduce their taxable income and pay less tax.

CH 02 Gross Income and Exclusions

1. Noncash items received as income must be included in income at their fair market value.
   a. True
   b. False

ANSWER: True

2. Awards, bonuses, and gifts are all included in gross income.
   a. True
   b. False

ANSWER: False

3. Disability benefits are generally taxable to the individual receiving the amounts.
   a. True
   b. False

ANSWER: False

4. Which of the following must be included in the gross income of the recipient?
   a. Child support payments
   b. Welfare payments
   c. Gifts
   d. Royalties
   e. All of these are included in gross income

ANSWER: d

5. All of the following must be included in gross income, *except*:
   a. Gambling winnings
   b. Partnership income
   c. Accident insurance proceeds
   d. Dividends
   e. Jury duty fees

ANSWER: c

6. All of the following amounts are excluded from gross income, *except*:
   a. Tips and gratuities
   b. Child support payments
   c. Scholarship grants for tuition
   d. Gifts
   e. Veterans' benefits

ANSWER: a

7. Which of the following is generally excluded from gross income?
   a. Dividends
   b. Rewards
   c. Disability benefits
   d. Partnership income

e. None of these

ANSWER: c

8. Which of the following is excluded from gross income?
   a. Prizes
   b. Scholarships for tuition
   c. Hobby income
   d. Rental income
   e. All of these are included in gross income

ANSWER: b

9. Which of the following is classified as nontaxable income?
   a. Unemployment compensation
   b. Dividend income
   c. Income from real estate rental property
   d. Welfare payments
   e. None of these

ANSWER: d

10. In the tax law, the definition of gross income is:
   a. All cash payments received unless excluded by the tax code
   b. All cash payments received for services performed
   c. All income from whatever source derived
   d. All income of any kind unless the income is earned illegally

ANSWER: c

11. Which of the following is *not* taxable income?
   a. Dividends
   b. Hobby income
   c. Interest
   d. Royalties
   e. Welfare benefits

ANSWER: e

12. All of the following amounts are taxable income to the recipient *except*:
   a. Prizes
   b. Unemployment compensation
   c. Salaries
   d. Farm income
   e. Gifts

ANSWER: e

13. Mary received the following items during the current year:

Christmas bonus from her employer	$600
Christmas gift from her father	$100
Unemployment compensation	$35

What is the total amount of the above items that must be included in Mary's current year gross income?

a. $0

b. $100

c. $735

d. $600

e. $635

ANSWER: e

14. As a Christmas thank you for being a good employee, Ed's TV Repair gave 62-year-old Edwina three shares of its stock worth $20 per share. Edwina then received dividends of $1 per share related to the stock. How much should be included in Edwina's gross income?

a. $0

b. $3

c. $60

d. $63

e. None of these

ANSWER: d

15. Which of the following is nontaxable income to the recipient for tax purposes?

a. Salary income

b. Income from real estate rental property

c. Income from tips

d. Inheritances

e. None of these

ANSWER: d

16. Andy landscaped his friend’s house in return for a couch set and an HD television worth $8,000. How much income must Andy report on his tax return for his services?

ANSWER: The noncash payment of $8,000 for services performed is taxable income to Andy. The tax law states that taxable income is “all income from whatever source derived.” There is no exception in the law for noncash items received in exchange for services.

17. Jack is a lawyer and Jeri is a child psychologist. Jack prepares Jeri’s estate planning at no charge and Jeri agrees to counsel Jack’s daughter six times at no charge in return for the estate planning. The value of the estate planning is $1,000 and the value of the therapy sessions is $1,000.

a. How much income does Jack have? Why?
b. How much income does Jeri have? Why?

ANSWER: a. **$1,000**. Taxable income includes “all income from whatever source derived.” The value of the therapy for his child is income to him for the performances of services. There is no taxable income exception in the tax law for “barter income.”
b. **$1,000**. Taxable income includes “all income from whatever source derived.” The value of the estate planning is income to her for the performances of services. There is no taxable income exception in the tax

law for “barter income.”

18. Barry has a successful methamphetamine laboratory. Producing methamphetamine is illegal under federal law. Is Barry required by law to report the income from his lab on his tax return? Why?

ANSWER: Yes. Illegal income is still taxable income since there is no exception excluding it in the tax code. When there is no explicit exception, taxable income is “all income from whatever source derived.”

19. Bonnie receives salary income of $32,000, unemployment compensation of $4,400, and interest income of $1,200 and a gift of $7,000 in cash from her aunt. How much gross income does Bonnie have?

ANSWER: **$37,600** = $32,000 + $1,200 + $4,400

20. Indicate whether each item below would be included in or excluded from the income of the recipient.

a. Payment for laboratory assistant position at University of California State
b. A $1,000 scholarship for tuition
c. College books paid for by grandma and grandpa
d. A $1,000 college loan
e. A scholarship for room and board
f. A new car given to recruit a professional basketball player
g. A scholarship used for supplies and equipment that are required for courses

ANSWER: a. Included
b. Excluded
c. Excluded
d. Excluded
e. Included
f. Included
g. Excluded

Indicate whether each of the items listed below would be (a) included in gross income or (b) excluded from gross income for the 2020 tax year.

a. Included

b. Excluded

21. Receipt of alimony in 2020 from a 2016 divorce

ANSWER: a

22. Lottery winnings

ANSWER: a

23. Life insurance proceeds received upon the death of a family member

ANSWER: b

24. Child support payments

ANSWER: b

25. Reimbursement of hospital expenses from a health insurance plan

ANSWER: b

26. Municipal bond interest

ANSWER: b

27. Unemployment compensation
ANSWER: a

28. Scholarships for tuition and books
ANSWER: b

29. Wages
ANSWER: a

30. Farm income
ANSWER: a

31. Inheritances
ANSWER: b

32. Craig, a single taxpayer, received the following items in 2020: dividends of $450, wages of $32,000, child support from his ex-spouse of $400 per month, a new television worth $1,200 from a door prize at a conference he attended, a gift of $3,000 from Craig's parents, and $200 of interest on bonds issued by the State of Arizona. Craig put $4,000 of his wages into his employer's dependent care flexible spending account (the $4,000 has not been deducted from the $32,000 of wages listed previously). He also receives a reimbursement of $270 per month to pay for public transportation passes each month (the monthly reimbursement of $270 has not been deducted from the $32,000 of wages). Based on the above, what is Craig's gross income in 2020?
ANSWER: Gross income equals
$26,590.

Item	Amount	Explanation
Dividends	$450	Included
Wages	$32,000	Included
Child Support	$0	Excluded
Door Prize	$1,200	Included
Gift	$0	Excluded
Muni Bond Interest	$0	Excluded
Child Care	($4,000)	Excluded up to $5,000
Public Transportation	($3,240)	Excluded up to $270 per month
Gross Income	$26,410	

33. Interest income received by a cash basis taxpayer is generally reported in the tax year it is received.
a. True
b. False
ANSWER: True

34. Interest on US Treasury Bonds is not taxable.
a. True
b. False
ANSWER: False

35. Taxpayers must report interest income on Series EE savings bonds as the interest accrues.
   a. True
   b. False

ANSWER: False

36. A gift received from a financial institution for opening a bank account is not taxable income to the recipient.
   a. True
   b. False

ANSWER: False

37. In 2020, Uriah received the following interest payments:

Interest of $300 on an overpayment of 2019 Federal income taxes
Interest of $400 from his bank certificate of deposit.
Interest of $1,000 on municipal bonds
Interest of $1,500 on US savings bonds (Series HH)

What amount, if any, should Uriah report as taxable interest income on his 2020 individual income tax return?
   a. $400
   b. $700
   c. $2,200
   d. $3,200
   e. None of these

ANSWER: c

38. Elmer received the following distributions from Virginiana Mutual Fund for the calendar year 2020:

Ordinary dividends	$250
Capital gain distributions	$170
Nontaxable distributions	$80

Elsie, Elmer's wife, did not own any of the Virginiana Mutual Fund shares, but she did receive $1,475 in interest on a savings account at the Moss National Bank and $175 in interest on California Municipal Bonds. Elmer and Elsie filed a joint income tax return for 2020. What amount is reportable as taxable *interest* income?
   a. $0
   b. $175
   c. $1,475
   d. $1,650
   e. None of the above

ANSWER: c

39. Elsie received the following distributions from Virginiana Mutual Fund for the calendar year 2020:

Ordinary dividends (nonqualifying)	$250
Capital gain distributions	$170
Nontaxable distributions	$80

Elmer, Elsie's husband, did not own any of the Virginiana Mutual Fund shares, but he did receive $1,600 in interest on a savings account at the Moss National Bank. Elmer and Elsie filed a joint income tax return for 2020. What portion *of the distributions from Virginiana Mutual Fund* is taxable as ordinary income on their 2020 individual income tax return?

a. $0

b. $250

c. $420

d. $500

e. None of these

ANSWER: b

40. Tim, a single taxpayer, receives $500 of qualified dividends from Exxon in the current year. His taxable income before the dividends is $26,000. Tim's tax on the dividends will be:

a. $0

b. $25

c. $50

d. $75

e. $100

ANSWER: a

41. Arthur, age 19, is a full-time student at Gordon College and is a candidate for a bachelor's degree. During 2020, he received the following amounts:

Tuition scholarship	$2,400
Loan from college financial aid office	$1,000
Cash support from parents	$2,000
Ordinary cash dividend	$200
Cash prize awarded from a contest	$300

What is his adjusted gross income for 2020?

a. $300

b. $500

c. $2,300

d. $2,500

e. None of these

ANSWER: b

42. Qualified dividends are given special tax treatment. Describe how they are taxed in 2020.

ANSWER: Qualified dividends are taxed at 0, 15, or 20 percent depending on the taxpayer's filing status. The 0 percent rate applies to taxpayers with incomes below a certain threshold ($40,000 for single and married filing separate, $53,600 for head of household, and $80,000 for married filing jointly. The 15 percent rate applies to taxpayers with income in excess of those amounts up to the 20 percent thresholds of $441,450 (single), $496,600 (MFJ), $248,300 (MFS), and $469,050 (HoH). An additional 3.8 percent Medicare tax may apply for high-income taxpayers.

43. If a taxpayer holding EE bonds makes an election with respect to the taxation of the bonds, how is the interest which accrues on the bonds, but is not paid, taxed each year?

ANSWER: If an election is made, the annual increase in the redemption value of the bond (or interest accrual as it is commonly called) is included in taxable income each year.

CH 02 Gross Income and Exclusions

44. In 2020, what rate would a single taxpayer pay on qualified dividend income:

a. If in the 37 percent bracket?
b. If in the 24 percent bracket?

ANSWER: a. **20 percent**
b. **15 percent**

45. Child support payments are deductible by the spouse making the payments.
a. True
b. False

ANSWER: False

46. If a divorce agreement executed in the 2017 specifies that a portion of the amount of an alimony payment is contingent upon the status of a child, that portion is considered to be a child support payment.
a. True
b. False

ANSWER: True

47. Under a divorce agreement executed before 2018, periodic payments of either cash or property must be made at regular intervals to be deductible as alimony.
a. True
b. False

ANSWER: False

48. Laura and Hung were granted a divorce in 2016. In accordance with the decree, Hung made the following payments to Laura in 2020:

Child support payments contingent on the age of the child	$6,000
Indefinite periodic payments terminating on Laura’s death	$4,000

How much of the payments can he deduct as alimony in 2020?
a. $0
b. $6,000
c. $10,000
d. $4,000
e. None of these

ANSWER: d

49. Jerry and Sally were divorced under an agreement executed July 1, 2020. The terms of the agreement provide that Jerry will transfer to Sally his interest in a rental house worth $250,000 with a tax basis to Jerry of $80,000. What is the amount of the gain that must be recognized by Jerry on the transfer of the property and what is Sally's tax basis in the property after the transfer, respectively?
a. $170,000 and $250,000
b. $0 and $250,000
c. $170,000 and $170,000
d. $0 and $80,000
e. None of these

ANSWER: d

50. Richard and Alice are divorced and under the terms of their written divorce agreement signed on December 30, 2015, Richard was required to pay Alice $1,500 per month of which $600 was designated as child support. He made 12 such payments in 2020. Additionally, Richard voluntarily paid Alice $1,200 per month for 12 months of 2020, no portion of which was designated as child support. Assuming that Alice has no other income, her tax return for 2020 should show gross income of:

a. $0
b. $7,200
c. $10,800
d. $18,000
e. None of these

ANSWER: c

51. Steve and Laura were divorced in 2014. Laura pays Steve alimony of $1,200 a month. The payment amount was agreed upon in the decree of divorce. To save money, Steve and Laura still live together. Are the alimony payments that Steve receives in 2020 included in his income?

a. Yes, the payments meet all alimony payment requirements.
b. Yes, alimony is always taxable.
c. No, only some of it is tax-exempt because Laura pays Steve too much alimony.
d. No, since Steve and Laura still live together, the payments are not considered alimony.
e. Yes, alimony payments are not tax-exempt.

ANSWER: d

52. Roger is required under a 2014 divorce decree to pay $500 of alimony and $200 of child support per month for 12 years. In addition, Roger makes a voluntary payment of $100 per month. How much of the total monthly payment is deductible by Roger?

a. $0
b. $200
c. $500
d. $600
e. None of these

ANSWER: c

53. Laura and Leon were granted a divorce in 2020. In accordance with the decree, Leon made the following payments to Laura in 2020:

Child support payments contingent on the age of the child	$4,000
Annual cash payments, other than child support, specified as alimony in the divorce agreement	$6,000

How much should Laura include in her 2020 taxable income as alimony?

a. $0
b. $4,000
c. $6,000
d. $10,000
e. None of these

ANSWER: a

54. For divorces before 2019, which of the following statements about deductible alimony payments is not correct?
    a. The payments must be in cash and must be received by the spouse (or former spouse).
    b. Divorced or legally separated parties can be members of the same household at the time the payments are made.
    c. The payor must have no liability to make payments for any period following the death of the spouse receiving the payments.
    d. The payments must not be designated in the written agreement as anything other than alimony.

ANSWER: b

55. Under a divorce agreement executed in 2015, Bob is required to pay his ex-wife, Carol, $3,000 a month until their youngest daughter is 21 years of age. At that time, the required payments are reduced to $2,000 per month.

a. How much of each $3,000 payment may be deducted as alimony by Bob?
b. How much of each $3,000 payment must be included in Carol's taxable income?

ANSWER: a. **$2,000**
b. **$2,000**

The amount over the continuing alimony payment is not treated as alimony for tax purposes.

56. Under the terms of a property settlement executed during the current year, Cindy transferred a house worth $350,000 to her ex-husband, Carl. The property has a tax basis to Cindy of $300,000.

a. How much taxable gain or loss must be recognized by Cindy at the time of the transfer?
b. What is Carl's tax basis in the property he received from Cindy?

ANSWER: a. **$0**
b. **$300,000**

57. Peter is required by his 2020 divorce agreement to pay alimony of $4,000 a month and child support of $6,000 a month to his ex-wife Stella. What is the tax treatment of these two payments?
To Peter?
To Stella?

ANSWER: Post-2018 divorce:
Peter cannot deduct the alimony or the child support.
Stella will not report the alimony or the child support as income.

58. As part of the property settlement related to their 2020 divorce, Stella must give Peter the house that they have been living in, while she gets 100 percent of their savings accounts. The house was purchased in Texas 15 years ago for $100,000 and is now worth $110,000. How much gain must Stella recognize on the transfer of the house to Peter? What is Peter’s tax basis in the house for calculating any future sale of the house?

ANSWER: No gain is taxable to Stella on the transfer of the house since it is part of a property settlement related to a divorce. Peter has a basis of $100,000 in the house for calculating tax on any future sale of the house.

59. An auto that is received as a prize should be included in the taxpayer's income at its list price rather than its fair market value.
    a. True

b. False

ANSWER: False

60. Basketball superstar Kawhi Leonard's outstanding player award is not includible in income, since the award is in recognition of his outstanding performance.

a. True

b. False

ANSWER: False

61. Marie had a good year. She received the following prizes and awards:
- an iPad from The Famous Daytime Talk Show with a fair market value of $500
- lottery winnings of $1,000 received in cash
- a plaque worth $25 plus $100 of Godiva chocolate in recognition for 100 days on the job without an accident
- a $10,000 cash prize from American Idol

How much of her prizes and awards should Marie report on her tax return?

a. None, they are all excluded from income

b. $11,000; only cash prizes and awards are included

c. $11,500; the award from her job is excluded

d. $11,600; the plaque may be excluded

e. $11,625; everything is included at the highest amount

ANSWER: c

62. Which of the following gifts or prizes would be considered taxable income to the person receiving the gift?

a. $5,000 given to the taxpayer by his friend

b. A mobile home given to the taxpayer by his mother

c. A ski boat won by the taxpayer on the Price is Right game show

d. A Mustang GT given to the taxpayer by his brother

e. None of the above would be considered taxable

ANSWER: c

63. Rob is 8 years old and won a sports car valued at $30,000 in a drawing at Disneyland this year. How much income, if any, must Rob report on his tax return for this year? Why?

ANSWER: **$30,000**. Prizes are taxable income, valued at fair market value.

64. State whether each of the following is taxable or nontaxable.

a. Susan won a jackpot of $50,000 gambling at a casino.
b. Sarah received a Christmas ham from her employer.
c. Jonathan won a car in a supermarket raffle valued at $25,000.
d. Gary received a scholarship for tuition of $5,000 a year.
e. Eric is given lodging valued at $1,000 a month on the oil rig where he is employed since it is impossible for Eric to go home during the period of time he is assigned to work on the rig.

ANSWER: a. Taxable
b. Nontaxable
c. Taxable
d. Nontaxable

e. Nontaxable

65. If an annuitant, whose annuity starting date was January 1, 2008, dies before recovering his or her investment in the annuity, any unrecovered investment is recognized as a miscellaneous itemized deduction on the annuitant's tax return for the year of death.

a. True

b. False

ANSWER: True

66. Payments made to a qualified retirement plan by an employer are considered part of the employee's investment in the contract for calculation of the annuity exclusion ratio.

a. True

b. False

ANSWER: False

67. When calculating the exclusion ratio for an annuity, the ratio should be revised when there is a significant change in the taxpayer's status or health.

a. True

b. False

ANSWER: False

68. Richard, who retired on April 30, 2020, receives a monthly employee annuity benefit of $1,400 payable for life, beginning May 1, 2020. During his years of employment, Richard contributed $29,400 to the company's plan. Richard's age on May 1 is 66. Using the simplified method, how much of the $11,200 annuity payment received during 2020 may Richard exclude from gross income?

a. $427

b. $1,120

c. $1,680

d. $11,200

e. None of these

ANSWER: b

69. Martin retired in May 2020. His pension is $1,000 per month from a qualified retirement plan to which he contributed $42,000, and to which his employer contributed $12,000. Martin was 67 when the plan payments started. During 2020, he received 8 months of payment for a total of $8,000 from the plan.

a. Using the simplified method, calculate Martin's taxable income for 2020 from the retirement plan distributions.
b. If Martin's contributions to the plan had been $25,200, instead of $42,000, using the simplified method, how much taxable income would he have to report in 2020 from the plan distributions?

ANSWER: a. **$6,400.** $42,000 ÷ 210 (factor for age 67) = $200 × 8 months = $1,600. $8,000 − $1,200 = $6,400

b. **$7,040.** $25,200 ÷ 210 = $120 × 8 months = $960. $8,000 − $960 = $7,040

CH 02 Gross Income and Exclusions

70. Cynthia, age 64, retired in June. Starting in July, Cynthia received $2,000 per month from an annuity. She has contributed $260,000 to the annuity. Her life expectancy is 20 years. How much is excluded from income using the simplified method? Use 260 as the factor to divide by.

1. Enter total amount received this year
2. Enter cost in plan at the annuity starting date
3. Factor at annuity starting date 260
4. Divide line 2 by line 3
5. Multiply line 4 by the number of monthly payments this year
6. Amount, if any, recovered tax free in prior years
7. Subtract line 6 from line 2
8. Enter the smaller of line 5 or 7
9. Taxable amount this year. Subtract line 8 from line 1

ANSWER: $6,000 is excluded from income. See calculation below.

1. Enter total amount received this year: $12,000
2. Enter cost in plan at the annuity starting date: $260,000
3. Factor at annuity starting date: 260
4. Divide line 2 by line 3: $1,000
5. Multiply line 4 by the number of monthly payments this year: $6,000
6. Amount, if any, recovered tax free in prior years: $0
7. Subtract line 6 from line 2: $260,000
8. Enter the smaller of line 5 or 7: $6,000
9. Taxable amount this year. Subtract line 8 from line 1: $6,000

71. If a life insurance policy is transferred to the insured's partnership for valuable consideration, the insurance proceeds are taxable when received by the partnership.

a. True

b. False

ANSWER: False

72. Sam died on January 15, 2012 and left his wife, Terry, an insurance policy with a face value of $100,000. Terry elected to receive the proceeds over a 10-year period ($10,000 plus interest each year). This year Terry receives $11,500 ($10,000 proceeds plus $1,500 interest) from the insurance company. How much income must Terry report from this payment?

a. $0

b. $500

c. $1,500

d. $11,500

e. None of these

ANSWER: c

73. Seymore named his wife, Penelope, the beneficiary of a $100,000 insurance policy on his life. The policy provided that, upon his death, the proceeds would be paid at a rate of $4,000 per year plus interest over a 25-year period. Seymore died June 25 of last year, and in the current year Penelope received a payment of $5,200 from the insurance company. What amount should she include in her gross income for the current year?

a. $200

b. $1,200

c. $4,000
d. $5,200
e. None of these

ANSWER: b

74. Which of the following would result in life insurance proceeds that are taxable to the recipient?
a. A life insurance policy transferred to a creditor in payment of a debt
b. A life insurance policy in which the insured is the daughter of the taxpayer and the beneficiary is the taxpayer
c. A life insurance policy transferred by a shareholder to a corporation
d. A life insurance policy purchased by a taxpayer insuring his or her business partner
e. A life insurance policy purchased by a corporation insuring an officer.

ANSWER: a

75. Toby transfers to Jim a life insurance policy with a face value of $25,000 and a cash value of $5,000 in payment of a personal debt. Jim continues to make premium payments on the policy until Toby's death. At that time, Jim had paid $1,500 in premiums.

a. How much income must Jim report when he receives the $25,000 in proceeds?
b. Would your answer be different if Toby and Jim were partners in a partnership? Why?

ANSWER: a. **$18,500** = $25,000 − $5,000 − $1,500.
b. **Yes**. Transfers to a partner, even for valuable consideration, result in nontaxable proceeds.

76. Tracy transfers to Glen a life insurance policy with a face value of $40,000 and a cash value of $8,000 in payment of a personal debt. Glen continues to make premium payments on the policy until Tracy's death. At that time, Glen had paid $3,500 in premiums.

a. How much income must Glen report when he receives the $40,000 in proceeds?
b. Would your answer be different if Tracy were a shareholder and CEO of a corporation to which the policy was transferred? Why?

ANSWER: a. **$28,500** = $40,000 − $8,000 − $3,500
b. **Yes**. Transfers to corporation by a shareholder and officer of a corporation, even if for valuable consideration, result in nontaxable proceeds.

77. Van is sick and tired of his job. His doctor certifies that his health may be compromised if he continues to work at his current job. He sells his life insurance policy to Life Settlements, Inc. for $50,000 so he can take a break from work. He has paid $10,000 so far for the policy. How much of the $50,000 must Van include in his taxable income?

ANSWER: He must pay tax on the $40,000 gain on the sale of the policy. Van has not met the requirement for an accelerated death benefit or a viatical settlement.

78. Helga receives a $300,000 life insurance payment when her boyfriend Andy dies. How much of the payment is taxable to Helga?

ANSWER: None of the payment is taxable. Life insurance proceeds received upon the death of the insured are generally considered to be tax-free and specifically excluded from taxable income.

79. Ordinarily life insurance proceeds are excluded from gross income. Why would they be taxable if the policy had been transferred for valuable consideration, prior to the death of the insured?

ANSWER: If a policy is transferred for valuable consideration, it takes on the nature of an investment for the new owner. Generally, the excess of the amount realized on disposal of an investment over the cost of the investment is subject to taxation.

80. To promote business activity, the tax rules generally are very liberal in treating business gifts as tax-free income to the recipient.

a. True

b. False

ANSWER: False

81. The receipt of an inheritance is excluded from the taxable income of the recipients.

a. True

b. False

ANSWER: True

82. Dividend income arising from stock received as a gift is excluded from gross income since the dividends are considered part of the gift.

a. True

b. False

ANSWER: False

83. In June of the current year, Rob's wealthy stepmother died and left him a stock portfolio worth $600,000. Before she died, she gave him a gift of $20,000 in cash. How much of these amounts, if any, are taxable to Rob? Why?

ANSWER: $0

Inheritances and gifts are not taxable to the recipient.

84. In June of the current year, a wealthy aunt gave Janie a stock portfolio worth $150,000. During the year, she collects $4,000 in dividends. How much of these amounts, if any, should Janie include in gross income for the current year? Why?

ANSWER: **$4,000**. The gift of stock is not classified as income, but earnings on the stock are income.

85. Geoff is a company president who has had a very good year at work. The owner of the company is pleased and gives him a gift of $50,000 at the end of the year. The owner writes "gift" in the memo section of the check. How much of the gift is taxable to Geoff?

ANSWER: The full $50,000 is taxable. The gift is clearly bonus income in a business setting so it does not qualify for tax-free gift treatment, even if Geoff's employer calls the payment a gift.

86. Tim receives a $25,000 gift from his parents for a down payment on a house. They know he cannot buy a house without their help. They write "gift" in the memo line of the check. How much of the gift is taxable to Tim?

ANSWER: None of the gift is taxable. Gifts are excluded from the taxable income of the person receiving the gift.

87. Elmore receives a rental property as an inheritance from his grandmother. The rental property is worth $500,000 and Elmore collected rental income of $24,000 during the year.

For the year, how much is Elmore's gross income as a result of the inheritance?

ANSWER: **$24,000**, the amount of the rental income.

88. Amounts received as scholarships for books and tuition may be excluded from the recipient's taxable income.

a. True

b. False

ANSWER: True

89. A scholarship for room and board is fully taxable to the recipient.

a. True

b. False

ANSWER: True

90. Nicole is a student at USB Law School; she receives a $52,000 scholarship. Of the $52,000, $40,000 is used for tuition, $5,000 is used for books, and $7,000 is used for room and board. How much of the scholarship is excluded from taxable income for Nicole?

a. $5,000

b. $7,000

c. $45,000

d. $47,000

e. $52,000

ANSWER: c

91. To pay for college, Henry received the following:
$1,000 scholarship from the Thespian Club to pay for books
$4,000 scholarship from the Elks Lodge for tuition
$5,000 worth of room and board as a dorm supervisor through a work-study program

How much income must Henry report on his tax return?

a. $0

b. $4,000

c. $5,000

d. $6,000

e. $10,000

ANSWER: c

92. Karina receives a scholarship of $10,000 to a college. She is also given a job which pays $5,000 a year to help with her expenses. $7,000 of the scholarship is earmarked for tuition and $3,000 is for room and board. How much of the money from the scholarship and the job are taxable to Karina?

ANSWER: $8,000. The $5,000 earnings from the job are taxable, as is $3,000 of the scholarship. There is no exclusion for payments made for room and board. $7,000 is not taxable, since scholarships for tuition are specifically excluded from taxable income.

93. Kim earned $30,000 from Pfizer before she was laid off. She then collected $7,000 of unemployment benefits. Finally, Kim received a $12,500 scholarship for tuition so she could return to college to earn a microbiology degree. How much does Kim need to report as income on her tax return?

ANSWER: Kim needs to report $37,000 on her tax return: $30,000 from her employment at Pfizer and $7,000 from unemployment benefits received. The $12,500 scholarship is excluded from income.

94. Amounts received by an employee as reimbursement for medical expenses under a policy provided by the taxpayer's employer are excluded from gross income.

a. True

b. False

ANSWER: True

95. If an employer claims a business deduction for group health insurance premiums paid on behalf of his employees, the amount must be included in the employees' gross income.

a. True

b. False

ANSWER: False

96. Payments made by an employer for health insurance on behalf of an employee are considered income to the employee at the time the payments are made.

a. True

b. False

ANSWER: False

97. Robert works for American Motors. American Motors pays a $1,200 premium on Robert’s health insurance in 2020. Robert has an operation on his big toe in 2020 that cost $7,200. The insurance company paid for $6,800 of it. Which one of the following is true for 2020?

a. Robert must claim the $1,200 premium paid by his employer as income.

b. Robert must claim the $6,800 paid by the insurance company for the operation as income.

c. Robert must claim the $1,200 premium and the $6,800 insurance payment as income.

d. None of these events are taxable on his 2020 return.

ANSWER: d

98. Which of the following may be excluded from income?

a. Payment for the loss of an arm

b. Premiums for health insurance paid by the employer

c. Reimbursement from the insurance company for a physical examination

d. All of the above are excluded from gross income

e. None of these are excluded from gross income

ANSWER: d

99. Joey is a single taxpayer. Joey's employer pays $1,800 per year for his health insurance. During the year, Joey had medical expenses of $2,500 and the insurance company reimbursed him for the full $2,500. How much of the above amounts, if any, must be included in Joey's gross income? Why?

ANSWER: **None.** The health insurance premiums paid by the employer are not income to Joey and the reimbursement of medical expense by the insurance company is not income to Joey.

100. Marco and his family are covered by his company’s health insurance plan. The health insurance costs his company $8,500 a year. During the year, Marco’s daughter is diagnosed with a serious illness and the health insurance pays $25,000 for treatment. How much of the insurance and treatment costs are taxable to Marco?

ANSWER: None of the cost of the family insurance or amounts paid by the insurance company for treatment are taxable to Marco. These amounts are specifically excluded from taxable income under the tax law.

101. Cash allowances for meals or lodging generally must be included in the employee's income.

a. True

b. False

ANSWER: True

102. The value of lodging provided to a professor to enable him to live on the campus is excluded from gross income.

a. True

b. False

ANSWER: False

103. Anthony is a marine biologist who spends months living on a boat in the ocean studying the impact of runoff water a hundred miles off the coast as a part of his job. Which of the following sentences is the most accurate?

a. Lodging is included in his income.

b. He may exclude meals from his income.

c. The fuel used to power the boat is excluded from his income.

d. b & c are correct, not a.

e. All are correct.

ANSWER: d

104. In which of the following cases may the employee exclude the meals and/or lodging:

a. A taxpayer lives rent-free at the property she manages even though the owner does not require the manager to live on site.

b. A headmaster at a boarding school is required to be on campus all night.

c. A president of a major film studio receives a cash allowance to live in Beverly Hills.

d. An employee has an option of dining in an all-expense paid employer-sponsored cafeteria or dining out of the office.

ANSWER: b

105. Bob is a machinist in a remote Alaskan crab-freezing plant. The plant is accessible only by boat or airplane and has no available lodging for rent. Bob's employer provides him with lodging at the plant and pays for all of his electricity, gas, and other utilities, valued at $700 per month. Is the value of the lodging taxable to Bob? Explain.

ANSWER: **No**. The lodging costs paid by the employer are not taxable to the employee because the lodging is on the business premises and must be accepted as a requirement for employment.

106. As a new benefit to employees, the Acme Company is providing a dining allowance every Tuesday for use in one of the twenty restaurants that they own around town. Should this benefit be included in the wages of the employees?

ANSWER: Yes. The meals are not being provided for the convenience of the employer. Therefore, the value of the meals should be included in the wages of the employees.

107. Interest earned on bonds issued by a state government is fully taxable.

a. True

b. False

ANSWER: False

108. An investor is comparing the following two bonds: a bond from ABC Corp which pays an interest rate of 9 percent per year and a municipal bond which pays an interest rate of 7.9 percent per year. The investor is in the 22 percent tax bracket. Which bond will give the investor a higher ***after-tax*** interest rate and for which reason?

a. The ABC bond because it pays a 9 percent interest rate, while the municipal bond only pays 7.9 percent.

b. The ABC bond because it pays an equivalent after-tax rate of 11.5 percent, while the municipal bond pays out an equivalent after-tax rate of 10.1 percent.

c. The municipal bond because it pays an equivalent after-tax rate of 7.9 percent, while the ABC bond pays out an after-tax 7.02 percent interest rate.

d. The municipal bond because it pays an equivalent after-tax rate of 7.9 percent, while the ABC bond pays out an equivalent after-tax rate of 2.0 percent.

e. None of these is correct.

ANSWER: c

109. Which taxpayer would benefit the most from a tax-free municipal bond compared to a taxable bond?

a. A taxpayer whose only income is from Social Security

b. A taxpayer who won a mega-million-dollar lottery

c. The average low income worker

d. They would all equally benefit from the tax-free municipal bond

ANSWER: b

110. A taxpayer in the 33 percent tax bracket invests in a New York City Bond paying 5 percent interest. What taxable interest rate would provide the same after-tax return?

ANSWER: **7.46%** = 5% / (1 − 0.33)

111. Mable is a wealthy widow who has come to you for tax advice. She is in the 35 percent tax bracket. She has a choice between investing in a high-quality municipal bond paying 3.5 percent or a high-quality corporate bond paying 7 percent. From a tax standpoint, which investment would you advise her to make and why?

ANSWER: She should invest in the corporate bond. At the 35 percent tax bracket, the after-tax equivalent rate on the corporate bond is 4.55 percent or 7 percent times (1 − 0.35), which is greater than the 3.5 percent rate of return on the municipal bond.

112. A taxpayer in the 32 percent tax bracket invests in a City of San Diego bond paying 8 percent interest. What taxable interest rate would provide the same after-tax return?

ANSWER: **11.76 percent** = 8 percent / (1 − 0.32)

113. Unemployment compensation is fully taxable to the individual receiving the compensation.

a. True

b. False

ANSWER: True

114. Steve worked as a tech supervisor for a computer company. In September of this year, he was laid off. He was paid unemployment compensation for the rest of the year totaling $7,000. Which of the following is true?

a. Steve will have to report all $7,000 of the unemployment compensation as income.

b. Steve will have to report $4,600 of the unemployment compensation as income.

c. Unemployment compensation is never taxable.

d. As long as the unemployment compensation payments are less than the taxpayer’s previous salary, they are not taxable.

e. None of these is true.

ANSWER: a

CH 02 Gross Income and Exclusions

115. Susie received unemployment benefits in the current year.
   a. All of the unemployment benefits are taxable.
   b. All of the unemployment benefits are nontaxable.
   c. Half of the unemployment benefits are taxable and half are nontaxable.
   d. The taxability of the unemployment benefits depends upon other income received for the year.

ANSWER: a

116. Jim, a single individual, was unemployed for a few months during the current year. During the year, he received $3,600 in unemployment compensation payments. How much of his unemployment compensation payments must be included in gross income?

ANSWER: **$3,600**. Unemployment compensation is included in gross income.

117. Group term life insurance premiums paid by an employer for insurance amounts less than $50,000 must be included in the employee's income.
   a. True
   b. False

ANSWER: False

118. A "no-additional-cost" service includes only those services in the major line of business in which the employee is employed.
   a. True
   b. False

ANSWER: True

119. Employer-provided spending accounts:
   a. May be set up for tax-free vacation savings
   b. Are not allowed for dependent care
   c. Do not require that the employee provide receipts for the expenses incurred
   d. Allow qualifying expenses to be treated as tax-free reductions in the employees' salaries

ANSWER: d

120. Indicate which of the following statements is true.
   a. Dependent care plans can *only* be used to cover the costs of caring for a dependent child.
   b. Health care flexible spending accounts can be used to cover dentist fees.
   c. Public transportation may be covered by an employer-provided spending account, but parking cannot be covered.
   d. Dependent care accounts may include day care but not preschool.

ANSWER: b

121. Which of the following is correct?
   a. Employee discounts are always included in gross income.
   b. Employee discounts of up to 20 percent may be taken on personal property held for investment.
   c. Employee discounts are not tax-free if they exceed the employer's gross markup for merchandise.
   d. Tax-free employee discounts include discounts in lines of business in which the employee does not work.

ANSWER: c

122. Which of the following fringe benefits is taxable to the employee receiving the benefit?
   a. A subscription to a tax journal provided by the employer to a corporation's tax accountant
   b. A small discount on toys granted to the salesperson for a toy store
   c. Incidental use of the company's copier by an office worker
   d. A 15 percent discount on investment real estate granted to the employee of a real estate developer
   e. All of the above are tax-free

ANSWER: d

123. William, a single taxpayer, works for the men's clothing division of a large corporation. During the year, William received the following fringe benefits:

	Value
20 percent discount on men's clothing (the usual markup is 40 percent)	$350
15 percent discount on toys from the toy division of the company (the usual markup is 25 percent)	$100
Personal copies on the company's copier	$15
A subscription to *Men's Clothing Weekly*	$35
Use of the company's athletic facilities	$50

As a result of receiving the above fringe benefits, what amount must William include in his current year gross income?

ANSWER: **$100**, the discount on toys from the toy division.

124. Curt’s tax client, Terry, is employed at a large company that offers health care flexible spending accounts to its employees. Terry must decide at the beginning of the year whether he wants to put as much as $2,750 of his salary into the medical flexible spending account. Terry has excellent insurance through the company and is very healthy. He does not expect to have any medical expenses during the year. Terry does not itemize deductions. Should Curt recommend that Terry put the maximum in his health care flexible spending account? Why or why not?

ANSWER: No. Terry will be better off keeping his salary $2,750 higher and paying tax on the salary, since he will likely have no medical costs to reimburse from a health care spending account during the year. If Terry has no medical expenses, he could lose all or part of the $2,750 in the account after the end of the year.

125. The amount of excludable employee reimbursement in 2020 for parking and mass transit costs are each $270 per month.
   a. True
   b. False

ANSWER: True

126. Which of the following are **not** excludable as an employee fringe benefit?
   a. Employee deductions of $4,200 for dependent childcare expenses
   b. Premiums for up to $50,000 of group term life insurance
   c. An employee discount that permits the sale of merchandise to employees for just over cost
   d. Public transportation costs of $130 per month provided by the employer
   e. All of these are excludable as an employee fringe benefit

ANSWER: e

127. In some cases, Social Security benefits may be partially taxable.
   a. True
   b. False

ANSWER: True

128. In regards to Social Security benefits:

a. The Social Security inclusion formula is the same amount for each filing status.

b. Social Security benefits are always excluded because wages are subject to Social Security tax when earned.

c. Tax-free interest income must be included in the formula used to determine if Social Security is included in taxable income.

d. Up to 100 percent of Social Security benefits received may be included in taxable income.

ANSWER: c

129. For the current year, the maximum percentage of Social Security benefits which might be included in a taxpayer's gross income is?

a. 0%

b. 50%

c. 65%

d. 85%

e. 100%

ANSWER: d

130. Answer the following questions regarding the taxability of Social Security payments.

a. Will a taxpayer with no income other than Social Security have to include the Social Security in taxable income?

b. Will a taxpayer with a large amount of municipal bond income, but no taxable income, likely have to pay tax on part of his or her Social Security?

c. What is the maximum percentage of Social Security benefits which may be subject to tax on an individual’s tax return?

ANSWER: a. No. The taxpayer’s income is below the threshold amount used in the formula to determine whether Social Security is taxable.

b. Yes. Tax-free municipal bond income is added to AGI in the formula to determine the amount of taxable Social Security.

c. 85 percent. High-income taxpayers must include 85 percent of Social Security receipts in taxable income.

131. During the tax year, Thomas and Yolanda received $24,000 in Social Security benefits. The amount of their adjusted gross income for the year was $2,000 and they received no tax-exempt interest income.

Calculate the amount of the Social Security benefits that Thomas and Yolanda must include in their gross income for the year.

ANSWER: **$0**. Their modified adjusted gross income is less than the base amount required to have taxable Social Security.

132. During the current year, Margaret and John received $24,000 in Social Security benefits. The amount of their adjusted gross income for the year before any Social Security income was $140,000 and they received $19,000 in tax-exempt income.

Explain the treatment of their Social Security income for tax purposes and the likely percentage of the Social Security income that will be taxable to Margaret and John.

ANSWER: Social Security income is partially taxed based on the taxpayer's modified adjusted gross income. Modified adjusted gross income includes adjusted gross income plus tax exempt interest plus half of the Social Security received. For low income taxpayers, no Social Security income is taxable. Higher income taxpayers must include 50 to 85 percent of the Social Security receipts in income. Given the high level of income reported by Margaret and John, it is safe to say they would have to include 85 percent of the Social Security payments in taxable income. To be certain, the IRS Social Security worksheet should be used to calculate the taxable amount.

133. Mary Lou took an $8,000 distribution from her educational savings account and used $6,000 to pay for qualified higher education expenses. The remaining balance of $2,000 was used to purchase clothes. On the date of the distribution, her educational savings account had a $25,000 balance including the $20,000 she had contributed. How much of the $8,000 distribution is tax-free?

a. $0

b. $6,000

c. $7,600

d. $7,625

e. $8,000

ANSWER: c

134. Charlie is a single taxpayer with income of $107,000 which includes $22,500 of interest income. Contributions to Coverdell educational savings accounts are phased out between $95,000 and $110,000. What is the maximum contribution Charlie can make to an educational savings account?

a. $400

b. $1,600

c. $2,000

d. $2,500

e. $0

ANSWER: a

135. Which of the following is correct for Qualified Tuition Programs?

a. Contributions are deductible and qualified educational expense distributions are tax-free.

b. Contributions are not deductible and qualified educational expense distributions are tax-free.

c. Contributions are deductible and qualified educational expense distributions are taxable.

d. Contributions are not deductible and qualified educational expense distributions are taxable.

ANSWER: b

136. Jennie receives $12,000 (of which $2,000 is earnings) from a Qualified Tuition Program. She uses the funds to pay for new furniture for her apartment. What amount is taxable to Jennie?

a. $12,000

b. $10,000

c. $3,000

d. $2,000

e. $0

ANSWER: d

137. Which of the following is true with respect to an education incentive?

a. Contributions to Qualified Tuition Programs (Section 529 plans) are deductible.

b. Contributions to education savings accounts (Coverdell ESAs) are deductible.

c. Tuition paid by a taxpayer earning $300,000 of income is deductible.

d. Married taxpayers at any income level may contribute to a Qualified Tuition Program (Section 529 plan).

ANSWER: d

138. For married taxpayers filing a joint return in 2020, at what AGI level does the phase-out limit for contributions to Qualified Tuition Programs (Section 529 plans) start?

a. $150,500

b. $190,000

c. $220,000

d. $400,000

e. There is no phase-out limit on Qualified Tuition Program contributions.

ANSWER: e

139. Geoffrey receives $20,000 from a qualified tuition program created by his grandmother. The program had accumulated $6,000 in earnings. He used the full $20,000 to pay for qualified higher education expenses. Calculate the amount of earnings subject to taxation.

ANSWER: **$0**. Both the original contributions and the earnings were used to pay for qualified higher education expenses.

140. Phillip, a single parent, would like to contribute $1,800 to a Coverdell educational savings account for his 10-year-old son. His AGI is $98,000. Calculate the amount of the contribution he can make.

ANSWER: **$1,600**. His contribution is limited because of his AGI. ($110,000 − $98,000) / $15,000 × $2,000 is $1,600. $15,000 is the range between the upper and lower phase-out limits.

141. Melissa took a $1,500 distribution from her educational savings account and used $1,200 to pay for qualified education expenses. Before the distribution, Melissa's account balance was $4,000, of which $1,000 was earnings. Calculate the following:

a. The tax-free return of capital
b. Her new adjusted basis for her savings account
c. Distribution of earnings *potentially* subject to tax
d. The excludable portion of the earnings
e. The taxable portion of her earnings

ANSWER: a. **$1,125.** 75 percent of the account balance before the distribution was from Melissa's contributions; therefore, 75 percent of the amount distributed is a return of her capital.
b. **$1,875.** $3,000 basis before distribution less tax-free return of capital of $1,125.
c. **$375.** The total distribution of $1,500 less the $1,125 return of capital.
d. **$300.** The potential amount subject to tax, $375, times the ratio of the amount used to pay for qualified education expenses, $1,200, to the full distribution, $1,500, equals the excludable portion.
e. **$75.** The potential amount subject to tax, $375, times the ratio of the amount not used to pay for qualified education expenses, $300, to the full distribution, $1,500, equals the taxable portion.

142. All taxpayers may deduct up to $4,000 of higher education tuition expenses.

a. True

b. False

ANSWER: False

143. Toni and Beyonze are married and file jointly. During 2020, they paid tuition for their daughter's college in the amount of $23,000. If their AGI was $142,000, what is the amount of tuition deduction they are eligible for?
   a. $0
   b. $2,000
   c. $4,000
   d. $23,000
   e. None of these

ANSWER: b

144. In all community property states, income from community property is community income.
   a. True
   b. False

ANSWER: True

145. New York is a community property state.
   a. True
   b. False

ANSWER: False

146. Most states are community property states.
   a. True
   b. False

ANSWER: False

147. Molly and Steve are married and live in Texas. Molly earns a salary of $50,000 and Steve owns a rental property that gives him $35,000 of income. If they filed separate tax returns, what amount of income would Steve report?
   a. $35,000
   b. $85,000
   c. $42,500
   d. $60,000
   e. None of these

ANSWER: c

148. Which one of the following conditions must be satisfied in order for a married taxpayer to be taxed on only his income if he resides in a community property state?
   a. The husband and wife must live apart for the entire year.
   b. The husband and wife must live apart for more than half the year.
   c. The husband and wife must be in the process of filing for a divorce.
   d. Only one of the spouses can be working and earning an income.
   e. None of these.

ANSWER: a

149. Which of the following is *not* a true statement regarding community property law?

a. For a married couple living in California, income derived from separate property is taxable to the owner of the property.
b. For a married couple living in Texas, income derived from separate property produces community income.
c. In all community property states, the salary of married spouses is allocated one-half to each spouse.
d. Colorado, Ohio, and Florida are community property states.
e. Property acquired before marriage in a community property state continues to be separate property.

ANSWER: d

150. Lee and Pat are married taxpayers living in Louisiana. Lee earns wages of $40,000 and has $5,000 of dividend income from separate property. Lee and Pat have interest income from community property of $10,000. If Lee and Pat file separate income tax returns, what amount of income must be included on Lee's separate tax return?

a. $50,000
b. $30,000
c. $27,500
d. $25,000
e. None of these

ANSWER: c

151. Patricia and Cliff are married but file separate tax returns. Patricia received a salary of $42,000 and Cliff received $15,000 of dividends from a stock portfolio that is his own separate property.

a. If Patricia and Cliff live in a common law state, what income should Patricia show on her separate return?
Salary
Dividends

b. If they live in California (a community property state), what income should Patricia show on her separate return?
Salary
Dividends

ANSWER: a. Salary: **$42,000**
Dividends: **$0**
b. Salary: **$21,000**
Dividends: **$0**

152. Rachel and Rob are married and living together in California. Their income is:

Rob’s salary	$120,000
Rachel’s net income from her business	130,000
Interest (Rob’s separate property investments)	4,000
Interest (Rachel’s separate property investments)	2,000
Dividends (community property)	5,000

Total income is $261,000
a. If Rachel files a separate return, how much income should she report?
b. If Rob and Rachel live in Texas, what should Rachel report as income?

ANSWER: a. 50% of Rob’s salary, $60,000, plus 50% of Rachel’s net business income, $65,000, plus 100% of Rachel’s interest income on her property, $2,000, plus 50% of the dividends on community property, $2,500, for a total of **$129,500**.

b. 50% of Rob's salary, $60,000, plus 50% of Rachel's net business income, $65,000, plus 50% of Rachel's interest income on her property, $1,000, plus 50% of Rob's interest income on his property, $2,000, plus 50% of the dividends on community property, $2,500, for a total of **$130,500**.

CHAPTER 3

BUSINESS INCOME AND EXPENSES Part I

Group 1 - Multiple Choice Questions

1.	**B**	7.	**C**	13.	**E**	19.	**D**
2.	**D**	8.	**D**	14.	**B**	20.	**A**
3.	**E**	9.	**D**	15.	**B**	21.	**C**
4.	**D**	10.	**C**	16.	**C**	22.	**E**
5.	**A**	11.	**D**	17.	**C**		
6.	**D**	12.	**A**	18.	**C**		

Group 2 – Problems

1. **See Attached Schedule C**

2. **See Attached Schedule C**

3. Margaret should show $40,032.24 net income on her Schedule C.

Gross Income:	**$50,000.00**
Expenses:	
Travel	1,000.00
Contribution to Presidential Election Campaign	100.00
Transportation 7,680 miles using standard mileage method (6,144 x 54 cents/mile)	3,317.76
Entertainment (4,400 x 50%)	2,200.00
Eight gifts at $50 each (Only $25 is allowed so 8 x $25)	200.00
Rent and Utilities for apartment in total 30% is used for a home office (10,500 x 30%)	3,150.00
Total Expenses	**$9,967.76**
Taxable Business Income	**$40,032.24**

4. a. Ending inventory **$26,500**

Cost of goods sold **$41,500**

b. Ending inventory **$24,500**

Cost of goods sold **$43,500**

5.

Part III **Cost of Goods Sold** (see instructions)

33 Method(s) used to value closing inventory: a ☑ Cost b ☐ Lower of cost or market c ☐ Other (attach explanation)

34 Was there any change in determining quantities, costs, or valuations between opening and closing inventory? If "Yes," attach explanation ☐ Yes ☑ No

35	Inventory at beginning of year. If different from last year's closing inventory, attach explanation	35	67,000
36	Purchases less cost of items withdrawn for personal use	36	608,220
37	Cost of labor. Do not include any amounts paid to yourself	37	
38	Materials and supplies	38	
39	Other costs	39	
40	Add lines 35 through 39	40	675,220
41	Inventory at end of year	41	77,200
42	**Cost of goods sold.** Subtract line 41 from line 40. Enter the result here and on line 4	42	598,020

6. See attached Publication 538 on Inventories

7. See attached Cost of Goods Schedule page 2 of Schedule C (F1040)

8. a. $5,994

b. $5,874

c. Since the deduction is larger using the standard mileage method, Teresa should deduct that amount.

9. $7,500
10. $2,160
11. $1,158
12. a. April - $124 November - $91

b. March - $123 December - $131

c. June - $125 September - $125
13. $1,150 course fees
 117 ($354 x 50% cost of meals)
$1,267 total amount that Bob can deduct on his Schedule C

14. Grace may claim $3,000 in the current year. She should use Schedule C to claim the deduction

15. a. $,1522

b. Club dues and personal use are non-deductible.

16. a. No, Loren's educational expenses are not deductible since the program leads to a new tradeor business, the practice of law.

    b. Yes, Alice may deduct educational expenses because she is improving her existing skills.

    c. No, Joan's educational expenses are not deductible since the program leads to a new trade or business. This may be for her education but does not retain to the job she currently has.

17. $1,670

18. $290

19.

Donee	Amount	Amount Allowed
Ms. Sears	$35, plus $4 shipping	$ 25.00
Mr. Williams	55	0
Mr. Sample	22	22.00
Mrs. Sample	20	20.00
Various customers	300	300.00
Mr. Shiver	175	175.00
Total business gift deduction		$ 542.00

20. a. $3,000

    b. The remaining amount can be carried forward as a short term loss and deducted in future years, subject to $3000 annual limitation

21. Yes. Because that's considered as Business bad debts. Deductible business bad debts are debts that became worthless in the year they were to be deducted. However, requirements for the business bad debt should be met. They should incur in the taxpayer's trade or business, or were debts created or acquired in such trade or business. Business bad debts would be deductible on Schedule C.

22. This is a non-business bad debt. Carrie may claim a $3,000 short-term capital loss in the current year and carry forward any remaining amount.

23. a.

Income	**$ 4,400.00**
Less: Depreciation	500.00
Sub total	3,900.00
Less: Real Estate taxes and Mortgage interest	825.00

Sub total	3,075.00
Less: Utilities	500.00
Total deduction	**$ 2,575.00**

b.

Income	**$ 2,600.00**
Less: Depreciation	500.00
Sub total	2,100.00
Less: Real Estate taxes and Mortgage interest	825.00
Sub total	1,275.00
Less: Utilities	500.00
Total deduction	**$ 775.00**

24.

Rent (9,600 x 25%)	$2,400
Utilities other than phone (2,500 x 25%)	625
Total home expenses	**$3,025**

25. $1,600 x 20% = 320 $3,400 – 820 = **$3,080 Randi's home office deduction**

300
200
820

26. 200/1000 = 20%

$6,000	x	20%	=	$1,200
$1,000	x	20%	=	200
$200	x	20%	=	40
				1,440
				800
				$2,240 Ann's home office deduction

27. Carl's net operating loss of $80,000 can be used as a deduction in another tax year as per deduction for NOL's allowed by law.

28. She could elect out of the carry back period.

29. a. The IRS presumes that an activity is carried on for profit if it makes a profit during at least three of the last five tax years, including the current year — at least two of the last seven years for activities that consist primarily of breeding, showing, training or racing horses.

If an activity is not for profit, losses from that activity may not be used to offset other income. An activity produces a loss when related expenses exceed income. The limit on not-for-profit losses applies to individuals, partnerships, estates, trusts, and S corporations. It does not apply to corporations other than S corporations.

b. $6,500

c. $5,000

CHAPTER 4 - BUSINESS INCOME AND EXPENSES, PART II

Group 1 - Multiple Choice Questions

1. E (LO 4.1)
2. D $\$4,000 - \frac{30 \text{ days}}{40 \text{ days}} (\$5,000 + \$600 + \$900 + \$3,500) = \$3,500$ loss (LO 4.1)
3. B $140,000 – $100,000 = $40,000; $25,000 – (50% x $40,000) = $5,000 (LO 4.2)
4. B (LO 4.2)
5. A (LO 4.2)
6. A (LO 4.2)
7. D (LO 4.2)
8. A (LO 4.2)
9. C (LO 4.2)
10. B (LO 4.3)
11. D (LO 4.3)
12. D (LO 4.4)
13. D (LO 4.4)
14. E (LO 4.5)
15. A (LO 4.6)
16. E (LO 4.6)
17. C $\frac{\$127,000 - \$113,800}{\$15,000} \times \$5,500 = \$4,840$ (LO 4.6)
18. B (LO 4.6)
19. A (LO 4.6)
20. A (LO 4.6)
21. A (LO 4.6)
22. B (LO 4.7)
23. B (LO 4.8)
24. D (LO 4.8)
25. D (LO 4.8)
26. B (LO 4.8)
27. A (LO 4.9)
28. C (LO 4.9)

29. A (LO 4.9)

ITEMIZED DEDUCTIONS AND OTHER INCENTIVES

Group 1 - Multiple Choice Questions

1.	C	(Section 5.1)	10.	C	(Section 5.3)	18.	E	(Section 5.8)
2.	B	(Section 5.1)	11.	D	(Section 5.4)	19.	E	(Section 5.9)
3.	D	(Section 5.1)	12.	B	(Section 5.4)	20.	C	(Section 5.10)
4.	E	(Section 5.2)	13.	D	($5,000 + 30% of $35,000) (Section 5.4)	21.	C	(Section 5.10)
5.	A	(Section 5.2)				22.	D	(Section 5.10)
6.	D	(Section 5.2)	14.	A	(Section 5.4)	23.	B	(Section 5.10)
7.	C	(Section 5.3)	15.	D	(Section 5.4)	24.	B	(Section 5.10)
8.	E	(Section 5.3)	16.	C	(Section 5.6)	25.	D	(Section 5.10)
9.	B	(Section 5.3)	17.	D	(Section 5.7)	26.	D	(Section 5.10)

Group 2 - Problems

1. $8,000 = $20,000 - 5,000 - 7,000. Since the pool was prescribed, it qualifies as a medical expense. The increase in value of $7,000 on the house and the reimbursement of $5,000 from the insurance company must be deducted from total expenditures. Although the expenditure is for a capital asset, it can be deduct-
ed in full in the year paid for, subject to the deduction of 7.5% of adjusted gross income. (Section 5.1)

2.

Medical and		Caution. Do not include expenses reimbursed or paid by others.					
	1	Medical and dental expenses (see page A-1)			1	4,260	
Dental Expenses	2	Enter amount from Form 1040, line 38	2	25,000			
	3	Multiply line 2 by 7.5% (.075)			3	1,875	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-				4	2,385

(Section 5.1)

3. The medical deduction for the elevator is the amount by which the $10,000 expenditure exceeds the increase in value of the property. Therefore, $10,000 is deductible in the current year as an expense before the 7.5% AGI limitation. For medical purposes such capital expenses are not required to be depreciated. (Section 5.1)

4. $1,800. The $200 refund is picked up in gross income on the tax return. (Section 5.2)

5.

	Regular years	Leap years (2004, 2008, etc.)
Mike:	$623 = $2,500 x 91/365	$628 = $2,500 x 92/366
Jane:	$1,877 = $2,500 x 274/365	$1,872 = $2,500 x 274/366

(Section 5.2)

6.

Taxes You	5	State and local income taxes	5	4,150		
Paid	6	Real estate taxes (see page A-5)	6	1,600		
(See	7	Personal property taxes	7	380		
page A-2.)	8	Other taxes. List type and amount ©	8			
	9	Add lines 5 through 8			9	6,130

(Section 5.2)

not
allowed due to the adjusted gross income limitation is carried forward for as long as five years until there is sufficient income to take the deduction. (Section 5.4)

charges	$5,100	
Travel during the move	900	
Lodging during move	600	
	$6,600	(Section 5.8)

28. See Form 3903 on page 113. (Section 5.8)

29. $11,500; Tuition, room and board, and books. (Section 5.8)

30. See the answer to Problem 28. (Section 5.8)

31. Sherry is allowed to claim the costs of moving her household goods and the travel to the new city for a total moving expense deduction of $5,300. The costs of her first month's rent and restaurant meals while apartment hunting are considered personal and non-deductible. (Section 5.8)

32. a. The IRS will consider (1) whether the activity is conducted like a business, (2) the expertise of the taxpayer, (3) the time and effort expended, (4) previous success of the taxpayer in similar activities, (5) income and loss history from the activity, (6) relationship of income to losses in the activity, (7) financial status of the taxpayer, and (8) the elements of personal recreation in the activity.

b. $6,500 loss = $5,000 - 10,000 - 1,500.

c. $5,000, loss is limited to the amount of income from the hobby. Of course, the $5,000 of bonsai sales would have to be included in gross income while the $5,000 of expenses would be miscellaneous itemized deductions subject to the 2 percent of AGI limitation. (Section 5.9)

33. $0; All distributions are used for qualifying expenses. (Section 5.10)

CHAPTER 6

CREDITS AND SPECIAL TAXES

Group 1 - Multiple Choice Questions

1.	D	(Section 6.1)	11.	C	(Section 6.4)
2.	C	(Section 6.1)	12.	C	($100,000/300,000 x $90,000) (Section 6.5)
3.	C	(Section 6.2)			
4.	D	(Section 6.3)	13.	C	(Section 6.6)
5.	C	(Section 6.4)	14.	A	(Section 6.6)
6.	B	(Section 6.4)	15.	C	(Section 6.6)
7.	E	(Section 6.4)	16.	C	(Section 6.6)
8.	A	(Section 6.4)	17.	E	(Section 6.8)
9.	C	(Section 6.4)	18.	E	$35,000 each (Section 6.10)
10.	D	(Section 6.4)	19.	B	(Section 6.10)

Group 2 - Problems

1. a. $750. $79,600 – $75,000 = $4,600 ÷ 1,000 = 4.6, which is rounded up to 5; 5 x $50 = $250 of $1,000 child credit is phased out due to AGI limits.
   b. $2,000. The income is less than the phase out range for married taxpayers, so two child credits are allowed at $1,000 each.
   c. $1,450. $120,400 – $110,000 = $10,400 ÷ 1,000 = 10.4, which is rounded up to 11; 11 x $50 = $550 of the $2,000 child credit is phased out due to AGI limits. $2,000 – $550 = $1,450 (Section 6.1)

2. The earned income credit is designed to provide financial relief to low income taxpayers. Taxpayers may receive a refund for the credit even though the credit exceeds their tax liability. (Section 6.2)

3. Earned income credit:

Amount from Earned Income Credit Table for earned income of $16,100		$5,028
Amount from Earned Income Credit Table for AGI of $16,600		4,985
Lesser of two amounts	**$4,985**	

   Diane must compute the credit using both earned income and AGI because her AGI exceeds the threshhold amount of $16,420. (Section 6.2)

4. Earned income credit
   See Schedule EIC on page 137. (Section 6.2)

5. A taxpayer may have a maximum of $3,100 of investment income in 2009 and still claim the earned income credit. The likely reason for the investment income limit is that the government intends the earned income credit to give a helping hand to the working poor. If a low income worker has investment income over $2,950 they have savings that indicate to the government that the taxpayer may not need a helping hand as badly as other taxpayers. (Section 6.2)

6. a. **$653** = $2,250 (student income limitation) x 29%.
   b. **$1,260** = $6,000 (income limitation) x 21%.
   c. **$1,800** = $6,000 x 30%. (Section 6.3)

7.

Qualified expenses	$3,000
For two dependents, lesser of $6,000 maximum or actual	$3,000
Credit percentage from table	33%
Credit allowed	**$ 990**

(Section 6.3)

8. See the answer to Problem 7. The purpose of this problem is to familiarize the students with the "Fill-in Forms" available from the IRS on the Internet. As of the date of this book, the forms do not do calculations, so students should be told to have a calculator handy. After the form is filled in, it can be saved to
a computer by using the "document rights" feature. (Section 6.3)

9. None. The credit is intended to help taxpayers who work at income-earning jobs. Therefore, since John doesn't earn income (though many would argue that he has a very difficult job caring for two young children and deserves a respite), no credit is allowed. (Section 6.3)

10. $600, or 20% of $3,000 (Section 6.3)

11. $900. Jean gets credit for $500 a month of earned income while she attends school for 9 months, or $4,500 of earned income for the year. Therefore, the maximum qualifying expenses for their dependents are limited to $4,500. The credit is calculated as $4,500 (which is less than the $6,000 maximum costs allowed for two children, and less than the $10,000 actually paid) x 20% = $900. (Section 6.3)

12. The American Opportunity credit and lifetime learning credit are in the tax law to give assistance to low and middle income students and/or their parents in paying for education. As discussed in Chapter 1, the tax law is used to encourage certain activities, and a well-educated, skilled and competitive workforce is obviously the goal of these credits. Congress hopes to encourage students in pursuing college and ongoing lifetime education. (Section 6.4)

13. The American Opportunity credit covers only the first 4 years of post-secondary education with at least a half-time course load, so it encourages students to continue their education after high school. The lifetime learning credit may be claimed for any year of college or graduate school, and may also
be claimed for educational courses taken during any stage of life, so it encourages lifelong ongoing education. The education is not required to be at the more than half-time level so includes students who take a class occasionally. (Section 6.4)

14. a. $1,250; Janie's total American Opportunity credit will be 100% of $2,000 plus 25% of $2,000, or $2,500. Because her parents have AGI over $160,000 the credit is phased out partially: the credit is reduced by the following amount $2,500 x ($190,000 – $160,000)/ $20,000 = $1,250. Therefore, the credit is $2,500 – $1,250 = $1,250.
    b. $2,500. Janie's parents have AGI below the phase-out range so they qualify for the full American Opportunity credit. (Section 6.4)

15. a. Jasper's income is too high to qualify for the lifetime learning credit. The ceiling for claiming

    any part of the credit for single taxpayers is $60,000. If Jasper were married and supporting a non-working wife, however, he would qualify for the full credit since the credit begins to phase-out
    for married taxpayers at $100,000. If he were married, his credit would be $400, or 20% of $2,000.
    b. Jasper qualifies for the full credit of $400, or 20% of $2,000. (Section 6.4)

16. Martha and Lew should claim the credit. If they deduct the taxes, they will have a $100 tax benefit ($400 deduction at a 25% tax rate). If they claim the $400 credit, they will have a full $400 tax benefit. (Section 6.5)

17. a.

	Paul	Cindy
Paul's salary (50% each)	$22,500	$22,500
Dividends on Paul's stock	4,000	0
Cindy's salary (50% each)	13,500	13,500
Interest income (50% each)	750	750
Total income	**$40,750**	**$36,750**

b.

	Paul	Cindy
Paul's salary (50% each)	$22,500	$22,500
Dividends on Paul's stock (50% each)	2,000	2,000
Cindy's salary (50% each)	13,500	13,500
Interest income (50% each)	750	750
Total income	**$38,750**	**$38,750**

(Section 6.10)

18. a. They may claim the maximum credit of $12,150 in 2009 since that is the year the adoption was finalized and their expenses exceed the amount of the credit.
    b. If the adoption is never finalized, no credit is allowed, since it is a foreign adoption.
    c. Carl and Jenny have income in the phase-out range for the adoption credit. The phase-out is calculated as follows: ($200,500 – $182,180)/$40,000 x $12,150 = $5,565. Only $6,585 of the credit is allowed ($12,150 – $5,565). (Section 6.6)

19. a. Mike's credit would be $750, 30% of the cost.
    b. **$1,500**. This is the maximum credit allowed for qualified water heaters, heat pumps and central air conditioners. (Section 6.7)

20. a. 30%, up to a maximum credit of $1,500 in 2009 and 2010.
    b. $1,500 – 30% of $5,000 up to $1,500. (Section 6.7)

21. a. **$5,244**
    b. **$11,531** = 26% x ($80,300 + 67,500 – 25,000 – 7,500 – 70,950)
    c. **$11,531**, the larger of the regular tax or the alternative minimum tax. (Section 6.8)

22. Some of the most common deductions allowed for regular tax and not for AMT are:
    - The standard deduction
    - Personal and dependency exemptions
    - State income taxes, property taxes, and all other taxes deducted on Schedule A
    - Miscellaneous itemized deductions taken on Schedule A
    - The interest deduction for up to $100,000 of home equity debt which is not used to purchase or improve part of a principal residence
    - Medical expenses are limited to 10% of AGI for AMT rather than 7.5% as used for regular tax purposes (Section 6.8)

23. In computing the AMT, deductions for personal and dependency exemptions are not allowed, and state income taxes and real estate property taxes are also not allowed. The elimination of these two kinds of deductions when calculating AMT may be enough to cause a taxpayer to pay AMT instead of the regular income tax. (Section 6.8)

24. Because of the reduction in regular tax rates in recent years that has not been matched by a reduction in AMT tax rates and AMT exemptions that have not been indexed for inflation, many more taxpayers are now paying AMT than in the past. Most of these taxpayers are not the people the AMT originally targeted, as they do not have complex tax shelters designed to reduce their taxable income. Instead, normal deductions such as personal and dependency exemptions, state income and property taxes and miscellaneous deductions are causing taxpayers to pay AMT. (Section 6.8)

25. 26% and 28% (Section 6.8)

26. Regular Taxable Income (before exemptions and standard deductions)

+ – Plus or minus AMT tax preferences and adjustments
= Equals Alternative Minimum Taxable Income (AMTI)
– Less AMT exemption (phased out to zero as AMTI increases)
= Equals amount subject to AMT
x Multiplied by the AMT tax rate(s)
= Equals tentative minimum tax
– Less regular tax
= Equals amount of AMT due with tax return (if it is a positive amount) (Section 6.8)

27. The provision is designed to prevent taxpayers from transferring income-earning assets to a minor child in order to take advantage of the child's lower tax rate. Assuming the child has a relatively small amount of taxable income, the child's tax rate will be lower due to the progressive tax rate structure. (Section 6.9)

28. a. **$2,600** = $4,500 – 950 (greater of standard deduction of $950 or investment expenses of $250) – 950.
    b. **$390** = $7,359 (tax on $52,000 + 2,600) – $6,969 (tax on $52,000)
    c. **$485** = $390 + 95 (tax at an assumed rate of 10 percent on regular taxable income of $950). Regular taxable income is $950 ($4,500 – 950 (standard deduction) – 2,600 (net unearned income)). (Section 6.9)

29. a. **$1,440** = $6,000/10,000 x $2,400.
    b. **$960** = $4,000/10,000 x $2,400. (Section 6.9)

30. The kiddie tax may be computed on Form 8615, which shows the income of the parents and provides
a calculation of the child's tax at the parents' tax rates. This form is attached to the child's separate tax return. Alternatively, parents may elect to include the child's income with their own return. To make this election, the child's unearned income must be more than $950 and less than $9,500 and consist only of interest and dividends. In this case, the parents must attach Form 8814 to their tax return showing the child's income that is taxed in their tax return.
(The basic answer is that either the child or the parent may report the unearned income and pay the tax.) (Section 6.9)

31. No, the kid's tax does not apply to wages earned by minors. The purpose of the tax is only to prevent investment income shifting from the generally higher tax rates of parents to the lower rates of the child. Wages earned by minors are taxed at the child's separate low income tax rates. (Section 6.9)

32. Publication 555, Community Property, is the source the student should find. (Section 6.10)

CHAPTER 7

ACCOUNTING PERIODS AND METHODS AND DEPRECIATION

Group 1 – Multiple Choice Questions

1. D (LO 7.1)
2. D (LO 7.1)
3. D (LO 7.2)
4. B (LO 7.2)
5. C ($100,000 x 1.364%) (LO 7.4)
6. B (20% x $25,000) (LO 7.4)
7. C $40,000 x 50% Bonus = $20,000. $20,000 x 20% MACRS = $4,000. (LO 7.4)
8. B ($14,000 x 7.14%) (LO 7.4)
9. C (LO 7.4)
10. A (LO 7.4)
11. A (LO 7.4, 7.6)
12. C (LO 7.5)
13. C (LO 7.6)
14. D (LO 7.8)
15. D (LO 7.8)
16. D The related party loss is disallowed. (LO 7.9)
17. A (LO 7.2, 7.9)
18. C (LO 7.2, 7.9)
19. C (40% + 35%) (LO 7.9)

Group 2 – Problems

1.

Step 1: Annualize the income	$24,000 x 12/3 = $96,000
Step 2: Tax on the annualized income	15% x $50,000 = $ 7,500
	25% x $25,000 = $ 6,250
	34% x $21,000 = $ 7,140
	Total $20,890
Step 3: Short period tax	$20,890 x 3/12 = **$ 5,223**
(LO 7.1)	

2.

Sales income	$66,000
Expenses:	
Other than rent and interest	(40,000)
Rent ($45,000 x 1/18)	(2,500)
Interest	(0)
Net Income	**$23,500**
(LO 7.2)	

3.

Income:	
Other than rental	$220,000
Rental	21,000
Expenses:	
Other than rental	(170,000)
Rental ($9,000 / 6)	(1,500)
Net Income	**$ 69,500**
(LO 7.2)	

4. a. Even though the contribution is paid in cash in 2018, it is deductible in 2017 if it is designated as a contribution for 2017 and paid by April 15, 2018.
   b. If an election has been made, the increase in value of savings bonds is included in income each year even though no cash is received.
   c. The half-year prepayment of interest for 2018 is not allowed as a deduction on her 2017 tax return.
   d. All of the standard business expenses which have already been invoiced and are paid at year-end are deductible in 2017.
   e. Even though the work was performed in 2017, the income is not recognized until it is received in cash in 2018. (LO 7.2)

5. Land is not allowed to be depreciated. It is held on the taxpayer's books at its cost basis. Under U.S. tax law, land is considered to be an asset that is not subject to obsolescence. (LO 7.3)

6. Yes, the tax law allows a taxpayer to take tax depreciation on a residential rental building no matter what happens to its fair value in the market. Even if the value of the building doubles or triples, the depreciation is allowed and remains the same regardless of fluctuations up and down in value. The term depreciation does not necessarily mean physical deterioration or loss of value of the asset, though this is usually true of the asset. The depreciation of computers, office furniture, automobiles, etc. often follows the decline in value of the assets reasonably well. (LO 7.3)

7. a. **$5,200** = $39,000 / 60 months x 8 months.
   b. **$3,900** = $39,000 x 10%. The taxpayer must use the annual percentage rates from the optional straight-line table (Table 7.3).
   c. **$23,400** = $19,500 ($39,000 x 50%) bonus depreciation plus $3,900 ($19,500 x 20%) of MACRS (Table 7.2). (LO 7.4)
   d. **$39,000.** All $39,000 can be deducted under the immediate expensing election. (LO 7.4)

8. a. **$22,883** = ($800,000 x 2.576%) + ($500,000 x 0.455%.)
   b. **$47,268** = ($800,000 x 3.636%) + ($500,000 x 3.636%.) (LO 7.4)

9. a. 5 years
   b. 7 years
   c. 5 years
   d. 27.5 years
   e. 39 years
   f. Indefinite life, no depreciation allowed. (LO 7.4)

10. When a taxpayer acquires more than 40% of its MACRS depreciable property (other than real estate) during the last quarter of the year, the taxpayer must use the mid-quarter convention in calculating depreciation rather than the half-year convention. There are separate MACRS tables for the mid-quarter depreciation convention. This treatment requires all assets purchased in any quarter of the year to be treated as purchased in the middle of that quarter. (LO 7.4)

11. a. 1.667% x $200,000 = **$3,334**
    b. 32% x $2,500 = **$800** (Bonus depreciation of $2,500 was allowed in 2016 reducing the depreciable basis to $2,500)
    c. 10% x $2,800 = **$280**
    d. 17.49% x $8,000 = **$1,399** (LO 7.4)

12. Election to expense $6,500
    Depreciation on automobile:
    Regular depreciation of $21,500 x 20%, but limited to $3,160 3,160
    Total depreciation **$9,660**

    For 2017, the automobile is 5-year recovery property; however, the depreciation deduction is subject to the annual automobile depreciation expense limitations. (LO 7.4, 7.5, 7.6, 7.7)

13. **$448** = $2,800 x 20% x 80%. The total depreciation on the computer must be divided between the business use, $448, and personal use, $0. Straight-line depreciation is not required on this listed property due to the greater than 50% business use. (LO 7.4, 7.6)

14. a. **$8,370.** Bonus depreciation of $43,000 x 50% x 75% = $16,125
    MACRS depreciation of $21,500 x 20% x 75% = $3,225
    Total depreciation = $19,350
    Limit $11,160 x 75% = $8,370
    b. **$3,825** = Limit of $5,100 x 75%; limit is less than actual of $8,311 (Remaining basis of $34,630 ($43,000 – $8,370) multiplied by business use of 75% x 32% depreciation factor). (LO 7.4, 7.6, 7.7)

15. See Form 4562 on pages 151 and 152. Convention test:

    4th quarter $3,800 ÷ total personal property $82,800 = 5%; thus half-year convention

Assets	Recovery Period
Manufacturing Equipment	7-year
Office Furniture	7-year
Office Computer	5-year

Auto depreciation $35,600 x 90% x 20% = $6,408 but limited to $3,160 x 90% = $2,844. (LO 7.4, 7.6, 7.7)

16. See Form 4562 on pages 153 and 154.
    Bonus Depreciation on Line 14: ($38,000 + $5,400 + $3,800) x 50% = $23,600
    Bonus Depreciation on Line 25: $35,600 x 50% = $17,800 limited to $11,160 x 90% or $10,044
    Auto Depreciable Basis on Line 26e: ($35,600 x 90%) – $10,044 = $21,996 (LO 7.4, 7.6, 7.7)

17. Tom should expense the machine under the Section 179 election to expense. Under the election to expense he can write off the entire cost of the machine in 2017 and bring his taxable income down to $75,000. If Tom does not elect to expense the machine, he must depreciate it over a life of 7 years, and will deduct bonus depreciation and only a small amount of MACRS depreciation from the purchase. (LO 7.5)

18. Even though a car has a 5-year life under MACRS, the depreciation allowed for the car is limited to the amounts allowed under the luxury auto rules. The car is allowed $11,160, $5,100 and $3,050 of depreciation in the first 3 years and then $1,875 a year thereafter. The car will be fully depreciated in 10 years using this schedule:

Year 1	$11,160
Year 2	$ 5,100
Year 3	$ 3,050
Years 4–9	$ 1,875
Year 10	$ 1,440
Total	$32,000 (LO 7.4, 7.7)

19. a. **$105,000** = $50,000 + $55,000
    b. **$3,500** deductible for 2016. $105,000/15 x (6/12) months. (LO 7.8)

20. The purchased goodwill and going-concern value of $54,000 should be amortized over 15 years at $300 a month as a Section 197 intangible asset. (LO 7.8)

21. a. **36%** = 20% + (80% x 20%)
    b. **60%** = 30% + 30%
    c. **60%** = 30% + 30%
    d. **$0** Brian owns more than 50% of JBC Corporation, directly or indirectly. (LO 7.9)

22. Section 267(a) is not reproduced here. (LO 7.9)

Group 3 – Writing Assignment

Ethics Solution:

Unless otherwise restricted by law, taxpayers can elect to use either the cash or accrual method. As long as cash receipts are recorded as income when received and cash payments are deducted as expenses when paid, Charlie is obeying the law. The ability to postpone income and accelerate expenses is good tax planning. It is not unethical or illegal.

Group 4 – Comprehensive Problems

1. See pages 155 through 158.

   2017 depreciation on property placed in service in prior years:

Cash register	$9,800 x 19.20% =	$1,881.60
Fixtures	$4,500 x 38.00% =	$1,710.00
Furniture	$3,600 x 38.00% =	$1,368.00
Total		$4,959.60

2. See pages 159 through 165.

Group 5 – Cumulative Software Problem

The solution to the Cumulative Software Problem is posted on the website for the textbook at *www.cengage.com/login*.

Group 2: Problem 15

Form **4562** — Department of the Treasury, Internal Revenue Service (99)

Depreciation and Amortization

(Including Information on Listed Property)

▶ Attach to your tax return.

▶ Go to *www.irs.gov/Form4562* for instructions and the latest information.

OMB No. 1545-0172 — **2017** — Attachment Sequence No. 179

Name(s) shown on return	Business or activity to which this form relates	Identifying number
Palo Fiero	Manufacturing	

Part I Election To Expense Certain Property Under Section 179

Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost

7	Listed property. Enter the amount from line 29	7	
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	
10	Carryover of disallowed deduction from line 13 of your 2016 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	
12	Section 179 expense deduction. Add lines 9 and 10, but don't enter more than line 11	12	
13	Carryover of disallowed deduction to 2018. Add lines 9 and 10, less line 12 ▶	13	

Note: Don't use Part II or Part III below for listed property. Instead, use Part V.

Part II Special Depreciation Allowance and Other Depreciation (Don't include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III MACRS Depreciation (Don't include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2017	17	
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2017 Tax Year Using the General Depreciation System

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a 3-year property						
b 5-year property		3,800	5 yrs	HY	200 DB	760
c 7-year property		43,400	7 yrs	HY	200 DB	6,202
d 10-year property						
e 15-year property						
f 20-year property						
g 25-year property			25 yrs.		S/L	
h Residential rental property			27.5 yrs.	MM	S/L	
			27.5 yrs.	MM	S/L	
i Nonresidential real property	04/23/17	170,000	39 yrs.	MM	S/L	3,092
				MM	S/L	

Section C—Assets Placed in Service During 2017 Tax Year Using the Alternative Depreciation System

20a Class life					S/L	
b 12-year			12 yrs.		S/L	
c 40-year			40 yrs.	MM	S/L	

Part IV Summary (See instructions.)

21	Listed property. Enter amount from line 28	21	2,844
22	**Total.** Add amounts from line 12, lines 14 through 17, lines 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	12,898
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 12906N Form **4562** (2017)

Group 2: Problem 15, cont.

Form 4562 (2017) Page **2**

Part V **Listed Property** (Include automobiles, certain other vehicles, certain aircraft, certain computers, and property used for entertainment, recreation, or amusement.)

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete **only** 24a, 24b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A—Depreciation and Other Information (Caution: See the instructions for limits for passenger automobiles.**)**

24a Do you have evidence to support the business/investment use claimed? ☒ **Yes** ☐ **No** **24b** If "Yes," is the evidence written? ☒ **Yes** ☐ **No**

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Special depreciation allowance for qualified listed property placed in service during the tax year and used more than 50% in a qualified business use (see instructions) .						**25**		
26 Property used more than 50% in a qualified business use:								
Passenger automobile	05/31/17	90 %	35,600	32,040	5 yrs	200DB HY	2,844	0
		%						
27 Property used 50% or less in a qualified business use:								
		%				S/L –		
		%				S/L –		
		%				S/L –		
28 Add amounts in column (h), lines 25 through 27. Enter here and on line 21, page 1 .						**28**	2,844	
29 Add amounts in column (i), line 26. Enter here and on line 7, page 1							**29**	

Section B—Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle 1		(b) Vehicle 2		(c) Vehicle 3		(d) Vehicle 4		(e) Vehicle 5		(f) Vehicle 6	
30 Total business/investment miles driven during the year (**don't** include commuting miles) .												
31 Total commuting miles driven during the year												
32 Total other personal (noncommuting) miles driven												
33 Total miles driven during the year. Add lines 30 through 32												
	Yes	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
34 Was the vehicle available for personal use during off-duty hours?												
35 Was the vehicle used primarily by a more than 5% owner or related person? . .												
36 Is another vehicle available for personal use?												

Section C—Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who **aren't** more than 5% owners or related persons (see instructions).

	Yes	**No**
37 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		
38 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See the instructions for vehicles used by corporate officers, directors, or 1% or more owners . .		
39 Do you treat all use of vehicles by employees as personal use?		
40 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		
41 Do you meet the requirements concerning qualified automobile demonstration use? (See instructions.) . . .		

Note: If your answer to 37, 38, 39, 40, or 41 is "Yes," don't complete Section B for the covered vehicles.

Part VI **Amortization**

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 2017 tax year (see instructions):					
43 Amortization of costs that began before your 2017 tax year				**43**	
44 **Total.** Add amounts in column (f). See the instructions for where to report				**44**	

Form **4562** (2017)

Group 2: Problem 16

Form **4562** — Department of the Treasury, Internal Revenue Service (99)

Depreciation and Amortization
(Including Information on Listed Property)
▶ Attach to your tax return.
▶ Go to *www.irs.gov/Form4562* for instructions and the latest information.

OMB No. 1545-0172 — **2017** — Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number
Palo Fiero	Manufacturing	

Part I Election To Expense Certain Property Under Section 179
Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost

7	Listed property. Enter the amount from line 29	7	
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	
10	Carryover of disallowed deduction from line 13 of your 2016 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	
12	Section 179 expense deduction. Add lines 9 and 10, but don't enter more than line 11	12	
13	Carryover of disallowed deduction to 2018. Add lines 9 and 10, less line 12 ▶	13	

Note: Don't use Part II or Part III below for listed property. Instead, use Part V.

Part II Special Depreciation Allowance and Other Depreciation (Don't include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	23,600
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III MACRS Depreciation (Don't include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2017	17	
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2017 Tax Year Using the General Depreciation System

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a 3-year property						
b 5-year property		1,900	5 yrs	HY	200 DB	380
c 7-year property		21,700	7 yrs	HY	200 DB	3,101
d 10-year property						
e 15-year property						
f 20-year property						
g 25-year property			25 yrs.		S/L	
h Residential rental property			27.5 yrs.	MM	S/L	
			27.5 yrs.	MM	S/L	
i Nonresidential real property	04/23/17	170,000	39 yrs.	MM	S/L	3,092
				MM	S/L	

Section C—Assets Placed in Service During 2017 Tax Year Using the Alternative Depreciation System

20a Class life					S/L	
b 12-year			12 yrs.		S/L	
c 40-year			40 yrs.	MM	S/L	

Part IV Summary (See instructions.)

21	Listed property. Enter amount from line 28	21	10,044
22	**Total.** Add amounts from line 12, lines 14 through 17, lines 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	40,217
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 12906N Form **4562** (2017)

Group 2: Problem 16, cont.

Form 4562 (2017) Page **2**

Part V **Listed Property** (Include automobiles, certain other vehicles, certain aircraft, certain computers, and property used for entertainment, recreation, or amusement.)

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete **only** 24a, 24b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A—Depreciation and Other Information (Caution: See the instructions for limits for passenger automobiles.**)**

24a Do you have evidence to support the business/investment use claimed? ☒ **Yes** ☐ **No** **24b** If "Yes," is the evidence written? ☒ **Yes** ☐ **No**

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Special depreciation allowance for qualified listed property placed in service during the tax year and used more than 50% in a qualified business use (see instructions) . **25**							10,044	
26 Property used more than 50% in a qualified business use:								
Passenger automobile	05/31/17	90 %	35,600	21,996	5 yrs	200DBHY	0	0
		%						
27 Property used 50% or less in a qualified business use:								
		%				S/L –		
		%				S/L –		
		%				S/L –		
28 Add amounts in column (h), lines 25 through 27. Enter here and on line 21, page 1 . **28**							10,044	
29 Add amounts in column (i), line 26. Enter here and on line 7, page 1 . . . **29**								

Section B—Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle 1		(b) Vehicle 2		(c) Vehicle 3		(d) Vehicle 4		(e) Vehicle 5		(f) Vehicle 6	
30 Total business/investment miles driven during the year (**don't** include commuting miles) .												
31 Total commuting miles driven during the year												
32 Total other personal (noncommuting) miles driven												
33 Total miles driven during the year. Add lines 30 through 32												
	Yes	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
34 Was the vehicle available for personal use during off-duty hours?												
35 Was the vehicle used primarily by a more than 5% owner or related person?												
36 Is another vehicle available for personal use?												

Section C—Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who **aren't** more than 5% owners or related persons (see instructions).

	Yes	**No**
37 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		
38 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See the instructions for vehicles used by corporate officers, directors, or 1% or more owners		
39 Do you treat all use of vehicles by employees as personal use?		
40 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		
41 Do you meet the requirements concerning qualified automobile demonstration use? (See instructions.)		

Note: If your answer to 37, 38, 39, 40, or 41 is "Yes," don't complete Section B for the covered vehicles.

Part VI **Amortization**

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 2017 tax year (see instructions):					
43 Amortization of costs that began before your 2017 tax year . . .				**43**	
44 **Total.** Add amounts in column (f). See the instructions for where to report . . .				**44**	

Form **4562** (2017)

Comprehensive Problem 1

SCHEDULE C (Form 1040)
Department of the Treasury
Internal Revenue Service (99)

Profit or Loss From Business
(Sole Proprietorship)

▶ Go to *www.irs.gov/ScheduleC* for instructions and the latest information.
▶ Attach to Form 1040, 1040NR, or 1041; partnerships generally must file Form 1065.

OMB No. 1545-0074
2017
Attachment Sequence No. 09

Name of proprietor: Sherry Hopson
Social security number (SSN): 123 45 6789

A Principal business or profession, including product or service (see instructions): Retail Family Clothing Store
B Enter code from instructions ▶ 4 4 8 1 4 0

C Business name. If no separate business name, leave blank.: Hopson Retail
D Employer ID number (EIN) (see instr.): 9 5 1 2 3 4 3 2 1

E Business address (including suite or room no.) ▶ 4321 Heather Drive
City, town or post office, state, and ZIP code: Henderson, NV 89002

F Accounting method: (1) ☐ Cash (2) ☒ Accrual (3) ☐ Other (specify) ▶

G Did you "materially participate" in the operation of this business during 2017? If "No," see instructions for limit on losses . ☒ Yes ☐ No

H If you started or acquired this business during 2017, check here ▶ ☐

I Did you make any payments in 2017 that would require you to file Form(s) 1099? (see instructions) ☐ Yes ☒ No

J If "Yes," did you or will you file required Forms 1099? ☐ Yes ☐ No

Part I Income

1	Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked ▶ ☐	1	351,700
2	Returns and allowances	2	4,000
3	Subtract line 2 from line 1	3	347,700
4	Cost of goods sold (from line 42)	4	110,000
5	**Gross profit.** Subtract line 4 from line 3	5	237,700
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	
7	**Gross income.** Add lines 5 and 6 ▶	7	237,700

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8	2,100	18	Office expense (see instructions)	18	750
9	Car and truck expenses (see instructions)	9		19	Pension and profit-sharing plans	19	
10	Commissions and fees	10		20	Rent or lease (see instructions):		
11	Contract labor (see instructions)	11		a	Vehicles, machinery, and equipment	20a	
12	Depletion	12		b	Other business property	20b	23,800
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13	35,975	21	Repairs and maintenance	21	
				22	Supplies (not included in Part III)	22	
				23	Taxes and licenses	23	3,440
				24	Travel, meals, and entertainment:		
14	Employee benefit programs (other than on line 19)	14		a	Travel	24a	
15	Insurance (other than health)	15	1,500	b	Deductible meals and entertainment (see instructions)	24b	
16	Interest:			25	Utilities	25	1,850
a	Mortgage (paid to banks, etc.)	16a		26	Wages (less employment credits)	26	37,200
b	Other	16b		27a	Other expenses (from line 48)	27a	
17	Legal and professional services	17	2,800	b	**Reserved for future use**	27b	

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27a ▶	28	109,415
29	Tentative profit or (loss). Subtract line 28 from line 7	29	128,285
30	Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method (see instructions). **Simplified method filers only:** enter the total square footage of: (a) your home: ______ and (b) the part of your home used for business: ______ . Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30	30	
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on both **Form 1040, line 12** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see instructions). Estates and trusts, enter on **Form 1041, line 3.** • If a loss, you **must** go to line 32.	31	128,285

32 If you have a loss, check the box that describes your investment in this activity (see instructions).
• If you checked 32a, enter the loss on both **Form 1040, line 12,** (or **Form 1040NR, line 13**) and on **Schedule SE, line 2.** (If you checked the box on line 1, see the line 31 instructions). Estates and trusts, enter on **Form 1041, line 3.**
• If you checked 32b, you **must** attach **Form 6198.** Your loss may be limited.

32a ☐ All investment is at risk.
32b ☐ Some investment is not at risk.

Comprehensive Problem 1, cont.

Schedule C (Form 1040) 2017 Sherry Hopson 123-45-6789 Page **2**

Part III **Cost of Goods Sold** (see instructions)

33 Method(s) used to value closing inventory: **a** [X] Cost **b** [ ] Lower of cost or market **c** [ ] Other (attach explanation)

34 Was there any change in determining quantities, costs, or valuations between opening and closing inventory? If "Yes," attach explanation . . . [ ] **Yes** [X] **No**

35	Inventory at beginning of year. If different from last year's closing inventory, attach explanation	35	84,300
36	Purchases less cost of items withdrawn for personal use	36	100,700
37	Cost of labor. Do not include any amounts paid to yourself	37	
38	Materials and supplies	38	
39	Other costs	39	
40	Add lines 35 through 39	40	185,000
41	Inventory at end of year	41	75,000
42	**Cost of goods sold.** Subtract line 41 from line 40. Enter the result here and on line 4	42	110,000

Part IV **Information on Your Vehicle.** Complete this part **only** if you are claiming car or truck expenses on line 9 and are not required to file Form 4562 for this business. See the instructions for line 13 to find out if you must file Form 4562.

43 When did you place your vehicle in service for business purposes? (month, day, year) ▶ / /

44 Of the total number of miles you drove your vehicle during 2017, enter the number of miles you used your vehicle for:

a Business ______ **b** Commuting (see instructions) ______ **c** Other ______

45 Was your vehicle available for personal use during off-duty hours? . . . [ ] **Yes** [ ] **No**

46 Do you (or your spouse) have another vehicle available for personal use?. . . [ ] **Yes** [ ] **No**

47a Do you have evidence to support your deduction? . . . [ ] **Yes** [ ] **No**

b If "Yes," is the evidence written? . . . [ ] **Yes** [ ] **No**

Part V **Other Expenses.** List below business expenses not included on lines 8–26 or line 30.

48 Total other expenses. Enter here and on line 27a	48

Schedule C (Form 1040) 2017

Comprehensive Problem 1, cont.

Form **4562** — Department of the Treasury, Internal Revenue Service (99)

Depreciation and Amortization

(Including Information on Listed Property)

▶ Attach to your tax return.

▶ Go to *www.irs.gov/Form4562* for instructions and the latest information.

OMB No. 1545-0172 — 2017 — Attachment Sequence No. 179

Name(s) shown on return	Business or activity to which this form relates	Identifying number
Sherry Hopson	Retail family clothing store	123-45-6789

Part I Election To Expense Certain Property Under Section 179

Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	

6	(a) Description of property	(b) Cost (business use only)	(c) Elected cost

7	Listed property. Enter the amount from line 29	7	
8	Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	
9	Tentative deduction. Enter the **smaller** of line 5 or line 8	9	
10	Carryover of disallowed deduction from line 13 of your 2016 Form 4562	10	
11	Business income limitation. Enter the smaller of business income (not less than zero) or line 5 (see instructions)	11	
12	Section 179 expense deduction. Add lines 9 and 10, but don't enter more than line 11	12	
13	Carryover of disallowed deduction to 2018. Add lines 9 and 10, less line 12 ▶	13	

Note: Don't use Part II or Part III below for listed property. Instead, use Part V.

Part II Special Depreciation Allowance and Other Depreciation (Don't include listed property.**)** (See instructions.)

14	Special depreciation allowance for qualified property (other than listed property) placed in service during the tax year (see instructions)	14	26,250
15	Property subject to section 168(f)(1) election	15	
16	Other depreciation (including ACRS)	16	

Part III MACRS Depreciation (Don't include listed property.**)** (See instructions.)

Section A

17	MACRS deductions for assets placed in service in tax years beginning before 2017	17	4,960
18	If you are electing to group any assets placed in service during the tax year into one or more general asset accounts, check here ▶ ☐		

Section B—Assets Placed in Service During 2017 Tax Year Using the General Depreciation System

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (business/investment use only—see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
19a 3-year property						
b 5-year property		17,750	5 yrs	HY	200 DB	3,550
c 7-year property		8,500	7 yrs	HY	200 DB	1,215
d 10-year property						
e 15-year property						
f 20-year property						
g 25-year property			25 yrs.		S/L	
h Residential rental property			27.5 yrs.	MM	S/L	
			27.5 yrs.	MM	S/L	
i Nonresidential real property			39 yrs.	MM	S/L	
				MM	S/L	

Section C—Assets Placed in Service During 2017 Tax Year Using the Alternative Depreciation System

20a Class life					S/L	
b 12-year			12 yrs.		S/L	
c 40-year			40 yrs.	MM	S/L	

Part IV Summary (See instructions.)

21	Listed property. Enter amount from line 28	21	
22	**Total.** Add amounts from line 12, lines 14 through 17, lines 19 and 20 in column (g), and line 21. Enter here and on the appropriate lines of your return. Partnerships and S corporations—see instructions	22	35,975
23	For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	23	

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 12906N Form **4562** (2017)

Comprehensive Problem 1, cont.

Form 4562 (2017) Sherry Hopson 123-45-6789 Page **2**

Part V **Listed Property** (Include automobiles, certain other vehicles, certain aircraft, certain computers, and property used for entertainment, recreation, or amusement.)

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete **only** 24a, 24b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A—Depreciation and Other Information (Caution: See the instructions for limits for passenger automobiles.**)**

24a Do you have evidence to support the business/investment use claimed? ☐ Yes ☐ No **24b** If "Yes," is the evidence written? ☐ Yes ☐ No

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Special depreciation allowance for qualified listed property placed in service during the tax year and used more than 50% in a qualified business use (see instructions) .						**25**		
26 Property used more than 50% in a qualified business use:								
		%						
		%						
		%						
27 Property used 50% or less in a qualified business use:								
		%				S/L –		
		%				S/L –		
		%				S/L –		
28 Add amounts in column (h), lines 25 through 27. Enter here and on line 21, page 1 .						**28**		
29 Add amounts in column (i), line 26. Enter here and on line 7, page 1							**29**	

Section B—Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle 1		(b) Vehicle 2		(c) Vehicle 3		(d) Vehicle 4		(e) Vehicle 5		(f) Vehicle 6	
30 Total business/investment miles driven during the year (**don't** include commuting miles) .												
31 Total commuting miles driven during the year												
32 Total other personal (noncommuting) miles driven												
33 Total miles driven during the year. Add lines 30 through 32												
	Yes	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
34 Was the vehicle available for personal use during off-duty hours?												
35 Was the vehicle used primarily by a more than 5% owner or related person? . .												
36 Is another vehicle available for personal use?												

Section C—Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who **aren't** more than 5% owners or related persons (see instructions).

	Yes	**No**
37 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		
38 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See the instructions for vehicles used by corporate officers, directors, or 1% or more owners . .		
39 Do you treat all use of vehicles by employees as personal use?		
40 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		
41 Do you meet the requirements concerning qualified automobile demonstration use? (See instructions.) . . .		

Note: If your answer to 37, 38, 39, 40, or 41 is "Yes," don't complete Section B for the covered vehicles.

Part VI **Amortization**

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 2017 tax year (see instructions):					
43 Amortization of costs that began before your 2017 tax year				**43**	
44 **Total.** Add amounts in column (f). See the instructions for where to report				**44**	

Form **4562** (2017)

Comprehensive Problem 2

Form **1040** Department of the Treasury—Internal Revenue Service (99) **U.S. Individual Income Tax Return** **2017** OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2017, or other tax year beginning , 2017, ending , 20 See separate instructions.

Your first name and initial: Warner	Last name: Robins	Your social security number: 798 09 8526
If a joint return, spouse's first name and initial: Augustine	Last name: Robins	Spouse's social security number: 445 81 1423
Home address (number and street). If you have a P.O. box, see instructions.: 638 Russell Parkway	Apt. no.	▲ Make sure the SSN(s) above and on line 6c are correct.
City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions).: Macon, GA 31207		**Presidential Election Campaign** Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund. [X] You [X] Spouse
Foreign country name	Foreign province/state/county	Foreign postal code

Filing Status Check only one box.

1 ☐ Single
2 [X] Married filing jointly (even if only one had income)
3 ☐ Married filing separately. Enter spouse's SSN above and full name here. ▶
4 ☐ Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 ☐ Qualifying widow(er) (see instructions)

Exemptions

6a [X] **Yourself.** If someone can claim you as a dependent, **do not** check box 6a
b [X] **Spouse**

Boxes checked on 6a and 6b: 2

c **Dependents:**

(1) First name Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) ✓ if child under age 17 qualifying for child tax credit (see instructions)
			☐
			☐
			☐
			☐

If more than four dependents, see instructions and check here ▶ ☐

No. of children on 6c who:
• lived with you
• did not live with you due to divorce or separation (see instructions)
Dependents on 6c not entered above
Add numbers on lines above ▶ 2

d Total number of exemptions claimed

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a W-2, see instructions.

7	Wages, salaries, tips, etc. Attach Form(s) W-2	7	151,900
8a	**Taxable** interest. Attach Schedule B if required	8a	450
b	**Tax-exempt** interest. **Do not** include on line 8a — 8b		
9a	Ordinary dividends. Attach Schedule B if required	9a	
b	Qualified dividends — 9b		
10	Taxable refunds, credits, or offsets of state and local income taxes	10	
11	Alimony received	11	
12	Business income or (loss). Attach Schedule C or C-EZ	12	
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ ☐	13	0
14	Other gains or (losses). Attach Form 4797	14	
15a	IRA distributions 15a — b Taxable amount	15b	
16a	Pensions and annuities 16a — b Taxable amount	16b	
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17	
18	Farm income or (loss). Attach Schedule F	18	
19	Unemployment compensation	19	
20a	Social security benefits 20a — b Taxable amount	20b	
21	Other income. List type and amount	21	
22	Combine the amounts in the far right column for lines 7 through 21. This is your **total income** ▶	22	152,350

Adjusted Gross Income

23	Educator expenses	23			
24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24			
25	Health savings account deduction. Attach Form 8889	25			
26	Moving expenses. Attach Form 3903	26			
27	Deductible part of self-employment tax. Attach Schedule SE	27			
28	Self-employed SEP, SIMPLE, and qualified plans	28			
29	Self-employed health insurance deduction	29			
30	Penalty on early withdrawal of savings	30	320		
31a	Alimony paid **b** Recipient's SSN ▶	31a			
32	IRA deduction	32	11,000		
33	Student loan interest deduction	33			
34	Reserved for future use	34			
35	Domestic production activities deduction. Attach Form 8903	35			
36	Add lines 23 through 35			36	11,320
37	Subtract line 36 from line 22. This is your **adjusted gross income** ▶			37	141,030

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions. Cat. No. 11320B Form **1040** (2017)

Comprehensive Problem 2, cont.

Form 1040 (2017) Page **2**

	38	Amount from line 37 (adjusted gross income)			38	141,030
Tax and Credits	39a	Check if: ☐ **You** were born before January 2, 1953, ☐ Blind. ☐ **Spouse** was born before January 2, 1953, ☐ Blind. **Total boxes checked** ▶ **39a**				
	b	If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ **39b** ☐				
Standard Deduction for— • People who check any box on line 39a or 39b **or** who can be claimed as a dependent, see instructions. • All others: Single or Married filing separately, $6,350 Married filing jointly or Qualifying widow(er), $12,700 Head of household, $9,350	40	**Itemized deductions** (from Schedule A) **or** your **standard deduction** (see left margin)			40	89,589
	41	Subtract line 40 from line 38			41	51,441
	42	**Exemptions.** If line 38 is $156,900 or less, multiply $4,050 by the number on line 6d. Otherwise, see instructions			42	8,100
	43	**Taxable income.** Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-			43	43,341
	44	**Tax** (see instructions). Check if any from: **a** ☐ Form(s) 8814 **b** ☐ Form 4972 **c** ☐			44	5,566
	45	**Alternative minimum tax** (see instructions). Attach Form 6251			45	
	46	Excess advance premium tax credit repayment. Attach Form 8962			46	
	47	Add lines 44, 45, and 46 ▶			47	5,566
	48	Foreign tax credit. Attach Form 1116 if required	48			
	49	Credit for child and dependent care expenses. Attach Form 2441	49			
	50	Education credits from Form 8863, line 19	50			
	51	Retirement savings contributions credit. Attach Form 8880	51			
	52	Child tax credit. Attach Schedule 8812, if required	52			
	53	Residential energy credit. Attach Form 5695	53			
	54	Other credits from Form: **a** ☐ 3800 **b** ☐ 8801 **c** ☐	54			
	55	Add lines 48 through 54. These are your **total credits**			55	
	56	Subtract line 55 from line 47. If line 55 is more than line 47, enter -0- ▶			56	5,566
Other Taxes	57	Self-employment tax. Attach Schedule SE			57	
	58	Unreported social security and Medicare tax from Form: **a** ☐ 4137 **b** ☐ 8919			58	
	59	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required			59	
	60a	Household employment taxes from Schedule H			60a	
	b	First-time homebuyer credit repayment. Attach Form 5405 if required			60b	
	61	Health care: individual responsibility (see instructions) Full-year coverage ☒			61	
	62	Taxes from: **a** ☐ Form 8959 **b** ☐ Form 8960 **c** ☐ Instructions; enter code(s)			62	
	63	Add lines 56 through 62. This is your **total tax** ▶			63	5,566
Payments	64	Federal income tax withheld from Forms W-2 and 1099	64	8,000		
If you have a qualifying child, attach Schedule EIC.	65	2017 estimated tax payments and amount applied from 2016 return	65			
	66a	**Earned income credit (EIC)**	66a			
	b	Nontaxable combat pay election **66b**				
	67	Additional child tax credit. Attach Schedule 8812	67			
	68	American opportunity credit from Form 8863, line 8	68			
	69	Net premium tax credit. Attach Form 8962	69			
	70	Amount paid with request for extension to file	70			
	71	Excess social security and tier 1 RRTA tax withheld	71			
	72	Credit for federal tax on fuels. Attach Form 4136	72			
	73	Credits from Form: **a** ☐ 2439 **b** Reserved **c** ☐ 8885 **d** ☐	73			
	74	Add lines 64, 65, 66a, and 67 through 73. These are your **total payments** ▶			74	8,000
Refund	75	If line 74 is more than line 63, subtract line 63 from line 74. This is the amount you **overpaid**			75	2,434
	76a	Amount of line 75 you want **refunded to you.** If Form 8888 is attached, check here ▶ ☐			76a	2,434
Direct deposit? See instructions.	▶ b	Routing number ▶ **c** Type: ☐ Checking ☐ Savings				
	▶ d	Account number				
	77	Amount of line 75 you want **applied to your 2018 estimated tax** ▶	77			
Amount You Owe	78	**Amount you owe.** Subtract line 74 from line 63. For details on how to pay, see instructions ▶			78	
	79	Estimated tax penalty (see instructions)	79			

Third Party Designee
Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ **Yes.** Complete below. ☐ **No**
Designee's name ▶ Phone no. ▶ Personal identification number (PIN) ▶

Sign Here
Joint return? See instructions. Keep a copy for your records.

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	Daytime phone number
		Company President	
Spouse's signature. If a joint return, **both** must sign.	Date	Spouse's occupation	If the IRS sent you an Identity Protection PIN, enter it here (see inst.)
		Homemaker	

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

Comprehensive Problem 2, cont.

SCHEDULE A (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Itemized Deductions

▶ Go to *www.irs.gov/ScheduleA* for instructions and the latest information.
▶ Attach to Form 1040.

OMB No. 1545-0074
2017
Attachment Sequence No. 07

Name(s) shown on Form 1040	Your social security number
Warner and Augustine Robins	798-09-8526

Medical and Dental Expenses		**Caution:** Do not include expenses reimbursed or paid by others.				
	1	Medical and dental expenses (see instructions)	1	14,122 (a)		
	2	Enter amount from Form 1040, line 38 [2] 141,030				
	3	Multiply line 2 by 10% (0.10)	3	14,103		
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-			4	19
Taxes You Paid	5	State and local **(check only one box):** a ☒ Income taxes, **or** b ☐ General sales taxes	5	3,970		
	6	Real estate taxes (see instructions)	6	5,650		
	7	Personal property taxes	7			
	8	Other taxes. List type and amount ▶	8			
	9	Add lines 5 through 8			9	9,620
Interest You Paid	10	Home mortgage interest and points reported to you on Form 1098	10	34,800		
Note: Your mortgage interest deduction may be limited (see instructions).	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11			
	12	Points not reported to you on Form 1098. See instructions for special rules	12			
	13	Reserved	13			
	14	Investment interest. Attach Form 4952 if required. See instructions.	14			
	15	Add lines 10 through 14			15	34,800
Gifts to Charity	16	Gifts by cash or check. If you made any gift of $250 or more, see instructions	16	10,600		
If you made a gift and got a benefit for it, see instructions.	17	Other than by cash or check. If any gift of $250 or more, see instructions. You **must** attach Form 8283 if over $500	17	34,550		
	18	Carryover from prior year	18			
	19	Add lines 16 through 18			19	45,150
Casualty and Theft Losses	20	Casualty or theft loss(es). Attach Form 4684. See instructions			20	
Job Expenses and Certain Miscellaneous Deductions	21	Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. See instructions. ▶	21			
	22	Tax preparation fees	22	750		
	23	Other expenses—investment, safe deposit box, etc. List type and amount ▶ Safe Deposit Box Rental	23	300		
	24	Add lines 21 through 23	24	1,050		
	25	Enter amount from Form 1040, line 38 [25] 141,030				
	26	Multiply line 25 by 2% (0.02)	26	2,821		
	27	Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-			27	0
Other Miscellaneous Deductions	28	Other—from list in instructions. List type and amount ▶			28	
Total Itemized Deductions	29	Is Form 1040, line 38, over $156,900? ☒ **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40. ☐ **Yes.** Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.			29	89,589
	30	If you elect to itemize deductions even though they are less than your standard deduction, check here ▶ ☐				

For Paperwork Reduction Act Notice, see the Instructions for Form 1040. Cat. No. 17145C **Schedule A (Form 1040) 2017**

(a) $14,122 = $10,400 + ($6,720 – $3,100) + (300 miles x 2 x $0.17)

Comprehensive Problem 2, cont.

SCHEDULE B (Form 1040A or 1040)
Department of the Treasury Internal Revenue Service (99)

Interest and Ordinary Dividends

▶ Attach to Form 1040A or 1040.
▶ Go to *www.irs.gov/ScheduleB* for instructions and the latest information.

OMB No. 1545-0074
2017
Attachment Sequence No. 08

Name(s) shown on return: Warner and Augustine Robins
Your social security number: 798-09-8526

Part I Interest

(See instructions and the instructions for Form 1040A, or Form 1040, line 8a.)

Note: If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

			Amount
1	List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see the instructions and list this interest first. Also, show that buyer's social security number and address ▶	1	
	Georgia National Bank		450 *
2	Add the amounts on line 1	2	450
3	Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815	3	
4	Subtract line 3 from line 2. Enter the result here and on Form 1040A, or Form 1040, line 8a ▶	4	450

Note: If line 4 is over $1,500, you must complete Part III.

Part II Ordinary Dividends

(See instructions and the instructions for Form 1040A, or Form 1040, line 9a.)

Note: If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

			Amount
5	List name of payer ▶	5	
6	Add the amounts on line 5. Enter the total here and on Form 1040A, or Form 1040, line 9a ▶	6	

Note: If line 6 is over $1,500, you must complete Part III.

Part III Foreign Accounts and Trusts

(See instructions.)

You must complete this part if you **(a)** had over $1,500 of taxable interest or ordinary dividends; **(b)** had a foreign account; or **(c)** received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

		Yes	No
7a	At any time during 2017, did you have a financial interest in or signature authority over a financial account (such as a bank account, securities account, or brokerage account) located in a foreign country? See instructions		X
	If "Yes," are you required to file FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority? See FinCEN Form 114 and its instructions for filing requirements and exceptions to those requirements		
b	If you are required to file FinCEN Form 114, enter the name of the foreign country where the financial account is located ▶		
8	During 2017, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See instructions		X

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 17146N **Schedule B (Form 1040A or 1040) 2017**

* Because interest is less than $1,500, Schedule B is not required.

Comprehensive Problem 2, cont.

SCHEDULE D (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Capital Gains and Losses

► Attach to Form 1040 or Form 1040NR.
► Go to *www.irs.gov/ScheduleD* for instructions and the latest information.
► Use Form 8949 to list your transactions for lines 1b, 2, 3, 8b, 9, and 10.

OMB No. 1545-0074
2017
Attachment Sequence No. 12

Name(s) shown on return: Warner and Augustine Robins

Your social security number: 798-09-8526

Part I **Short-Term Capital Gains and Losses—Assets Held One Year or Less**

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part I, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
1a Totals for all short-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 1b .				
1b Totals for all transactions reported on Form(s) 8949 with **Box A** checked				
2 Totals for all transactions reported on Form(s) 8949 with **Box B** checked				
3 Totals for all transactions reported on Form(s) 8949 with **Box C** checked				

4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824 .	4	
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	5	
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your **Capital Loss Carryover Worksheet** in the instructions	6	( )
7 **Net short-term capital gain or (loss).** Combine lines 1a through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the back	7	

Part II **Long-Term Capital Gains and Losses—Assets Held More Than One Year**

See instructions for how to figure the amounts to enter on the lines below. This form may be easier to complete if you round off cents to whole dollars.	(d) Proceeds (sales price)	(e) Cost (or other basis)	(g) Adjustments to gain or loss from Form(s) 8949, Part II, line 2, column (g)	(h) Gain or (loss) Subtract column (e) from column (d) and combine the result with column (g)
8a Totals for all long-term transactions reported on Form 1099-B for which basis was reported to the IRS and for which you have no adjustments (see instructions). However, if you choose to report all these transactions on Form 8949, leave this line blank and go to line 8b .				
8b Totals for all transactions reported on Form(s) 8949 with **Box D** checked				
9 Totals for all transactions reported on Form(s) 8949 with **Box E** checked				
10 Totals for all transactions reported on Form(s) 8949 with **Box F** checked.	75,000	160,000	Related Party Loss Disallowed 85,000	0

11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824	11	
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	12	
13 Capital gain distributions. See the instructions	13	
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your **Capital Loss Carryover Worksheet** in the instructions	14	( )
15 **Net long-term capital gain or (loss).** Combine lines 8a through 14 in column (h). Then go to Part III on the back	15	0

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 11338H **Schedule D (Form 1040) 2017**

Comprehensive Problem 2, cont.

Form **8949**

Department of the Treasury
Internal Revenue Service

Sales and Other Dispositions of Capital Assets

▶ Go to *www.irs.gov/Form8949* for instructions and the latest information.

▶ File with your Schedule D to list your transactions for lines 1b, 2, 3, 8b, 9, and 10 of Schedule D.

OMB No. 1545-0074

2017

Attachment Sequence No. **12A**

Name(s) shown on return: Warner and Augustine Robins

Social security number or taxpayer identification number: 798-09-8526

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I **Short-Term.** Transactions involving capital assets you held 1 year or less are short term. For long-term transactions, see page 2.

Note: You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box A, B, *or* C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

☐ **(A)** Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
☐ **(B)** Short-term transactions reported on Form(s) 1099-B showing basis **wasn't** reported to the IRS
☐ **(C)** Short-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). **See the separate instructions.** (f) Code(s) from instructions	(g) Amount of adjustment	(h) **Gain or (loss).** Subtract column (e) from column (d) and combine the result with column (g)
2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 1b** (if **Box A** above is checked), **line 2** (if **Box B** above is checked), or **line 3** (if **Box C** above is checked) ▶							

Note: If you checked Box A above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

Comprehensive Problem 2, cont.

Form 8949 (2017) Attachment Sequence No. **12A** Page **2**

Name(s) shown on return. Name and SSN or taxpayer identification no. not required if shown on other side: Warner and Augustine Robins

Social security number or taxpayer identification number: 798-09-8526

Before you check Box D, E, or F below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part II **Long-Term.** Transactions involving capital assets you held more than 1 year are long term. For short-term transactions, see page 1.

Note: You may aggregate all long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 8a; you aren't required to report these transactions on Form 8949 (see instructions).

You *must* check Box D, E, *or* F below. Check only one box. If more than one box applies for your long-term transactions, complete a separate Form 8949, page 2, for each applicable box. If you have more long-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

☐ **(D)** Long-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see **Note** above)
☐ **(E)** Long-term transactions reported on Form(s) 1099-B showing basis **wasn't** reported to the IRS
☒ **(F)** Long-term transactions not reported to you on Form 1099-B

1 (a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold or disposed of (Mo., day, yr.)	(d) Proceeds (sales price) (see instructions)	(e) Cost or other basis. See the **Note** below and see *Column (e)* in the separate instructions	Adjustment, if any, to gain or loss. If you enter an amount in column (g), enter a code in column (f). **See the separate instructions.** (f) Code(s) from instructions	(g) Amount of adjustment	(h) **Gain or (loss).** Subtract column (e) from column (d) and combine the result with column (g)
Land	1/1/12	1/1/17	75,000	160,000	L	85,000	0
2 Totals. Add the amounts in columns (d), (e), (g), and (h) (subtract negative amounts). Enter each total here and include on your Schedule D, **line 8b** (if **Box D** above is checked), **line 9** (if **Box E** above is checked), or **line 10** (if **Box F** above is checked) ▶			75,000	160,000		85,000	0

Note: If you checked Box D above but the basis reported to the IRS was incorrect, enter in column (e) the basis as reported to the IRS, and enter an adjustment in column (g) to correct the basis. See *Column (g)* in the separate instructions for how to figure the amount of the adjustment.

Form **8949** (2017)

Key Number Tax Return Summary

Chapter 7

Comprehensive Problem 1

Schedule C, Gross Income (Line 7)	237,700
Form 4562, Depreciation on 5-Year Property (Line 19b)	3,550
Schedule C, Depreciation (Line 13)	35,975
Schedule C, Total Expenses (Line 28)	109,415
Schedule C, Net Profit or Loss (Line 31)	128,285

Comprehensive Problem 2

Adjusted Gross Income (Line 37)	141,030
Itemized Deductions (Line 40)	89,589
Exemptions (Line 42)	8,100
Total Tax (Line 63)	5,566
Amount Overpaid (Line 75)	2,434

Chapter 8: Capital Gains and Losses

Student: ____

1. An artist's painting is *not* a capital asset when held by the artist.

   True False

2. A taxpayer's personal automobile is a capital asset.

   True False

3. Accounts receivable are capital assets.

   True False

4. The first day a capital asset, acquired on August 31, 2013, may be sold for long-term capital gain or loss treatment is September 1, 2014.

   True False

5. If a capital asset acquired on October 27, 2001 is sold on April 30, 2013 for a gain, the gain is a long-term capital gain.

   True False

6. If a capital asset acquired August 5, 2013 is sold on February 6, 2014, any gain is a short-term capital gain.

   True False

7. The basis of property received as an inheritance is generally equal to the fair market value at the date of death.

   True False

8. If property is received from a decedent, the taxpayer who inherits the property has the same basis in the property as the decedent.

   True False

9. If a taxpayer is relieved of a liability on the disposition of property, the amount of the liability should be included in the amount realized on the sale or other disposition.

   True False

10. Net short-term capital gains may be offset by net long-term capital losses.

True False

11. For 2013, long-term capital gains are *not* afforded preferential tax treatment.

True False

12. Taxpayers are allowed to offset net short-term capital losses with net long-term capital gains.

True False

13. There is no limit on the amount of capital losses that an individual may deduct against ordinary income.

True False

14. Cows used in a farming business are Section 1245 property.

True False

15. The depreciation recapture provisions are designed to prevent taxpayers from converting capital gains into ordinary income.

True False

16. The amount of ordinary income recognized on the sale of a Section 1245 asset is limited to the total gain realized on the sale.

True False

17. A net long-term gain from the theft of a Section 1231 asset is treated as a Section 1231 gain.

True False

18. Assuming a taxpayer has no other gains or losses for the year, a loss from the theft of a Section 1231 asset is treated as a capital loss.

True False

19. A taxpayer eligible to use the installment method for reporting gain on the sale of an asset must use the installment method unless he or she elects out of the provision.

True False

20. If the proceeds from the sale of property will be collected over a period of more than one year, a taxpayer is required to use the installment method.

True False

21. The exchange of inventory does *not* qualify for like-kind exchange treatment.

True False

22. The exchange of shares of stock does *not* qualify for like-kind exchange treatment.

True False

23. In a like-kind exchange, relief from a liability is treated as boot.

True False

24. To have the like-kind exchange provisions apply, a taxpayer must make an election.

True False

25. If insurance proceeds exceed the taxpayer's basis in property destroyed by fire and the proceeds are not invested in similar property, the taxpayer may be required to recognize a gain.

True False

26. The taxpayer generally has only 1 year to replace involuntarily converted property in order to postpone the recognition of gain.

True False

27. The condemnation of property is *not* an involuntary conversion, since it is done pursuant to a government decree.

True False

28. The exclusion of gain on the sale of a personal residence may be elected only by a taxpayer who has owned three or more residences.

True False

29. If not entirely used in one sale, the unused portion of the $250,000 exclusion on the sale of a taxpayer's principal residence may be used to reduce the recognized gain on the sale of the taxpayer's next residence.

True False

30. In 2013, the basis of a taxpayer's replacement residence is equal to the cost of the replacement residence less the gain which was deferred on the sale of the old residence.

True False

31. If a taxpayer sells his personal residence and purchases a new residence, realized gain may be recognized.

True False

32. Which of the following is a capital asset?

A. A literary work held by the author
B. Real estate held by a developer
C. A taxpayer's personal automobile
D. A truck used in a taxpayer's business
E. None of the above

33. Which of the following is a capital asset?

A. Inventory held by a manufacturer
B. Accounts receivable held by a dentist
C. All property owned by a taxpayer other than property specifically noted in the law as an exception
D. Depreciable property and real estate used in a trade or business

34. Which one of the following is a capital asset?

A. Accounts receivable
B. Copyright held by the author
C. Securities
D. Inventories
E. All of the above are capital assets

35. Sol purchased land as an investment on January 12, 2004 for $85,000. On January 31, 2013, Sol sold the land for $90,000 cash. What is the nature of the gain or loss?

A. Long-term capital loss
B. Long-term capital gain
C. Short-term capital gain
D. Short-term capital loss
E. None of the above

36. Which of the following is *not* true about capital assets?

A. Real property used in a trade or business is not a capital asset.
B. Capital losses may be carried back for 3 years to offset capital gains in those years.
C. For 2013, net long-term capital gains are granted preferential tax treatment.
D. Individual taxpayers may deduct net capital losses of up to $3,000 per year.
E. Shares of stock held for investment are capital assets.

37. Which of the following sales results in a short-term gain/loss?

A. A capital asset bought on June 30, 2012 and sold June 20, 2013.
B. A capital asset bought on July 25, 2012 and sold August 19, 2013.
C. A capital asset bought on September 12, 2006 and sold August 19, 2013.
D. A capital asset bought on August 15, 2012 and sold August 16, 2013.
E. All of the above are long-term gains/losses.

38. If property is inherited by a taxpayer,

A. To the recipient, the basis for the property is the same as the basis to the decedent.
B. At sale date, the basis of the property to the recipient differs depending on whether the property was sold at a gain or a loss.
C. At sale date, the recipient will not have a gain or loss even if the recipient has held the property for more than a year.
D. In general, the basis to the recipient is the fair market value at the decedent's date of death.

39. Sol purchased land as an investment on January 12, 2004 for $85,000. On January 31, 2013, Sol sold the land for $20,000 cash. In addition, the purchaser assumed the mortgage of $70,000 on the land. What is the amount of the realized gain or loss on the sale?

A. $65,000 loss
B. $15,000 loss
C. $5,000 gain
D. $90,000 gain
E. None of the above

40. An asset has an original basis of $25,000 and depreciation has been claimed for the asset in the amount of $20,000. If the asset's adjusted basis is $15,000, what is the amount of capital improvements that have been made to the asset?

A. $5,000
B. $10,000
C. $20,000
D. $30,000
E. None of the above

41. Carlos bought a building for $111,000 in 2009. He built an addition to the building for $24,000. In 2013, he sold it for $190,000. What was his long-term capital gain?

A. $190,000
B. $55,000
C. $79,000
D. $175,000
E. $59,000

42. An asset's adjusted basis is computed as:

A. Original basis + capital improvements - accumulated depreciation.
B. Original basis - capital improvements + accumulated depreciation.
C. Original basis + capital improvements + accumulated depreciation.
D. Original basis + capital improvements + gain or loss realized.
E. None of the above.

43. The adjusted basis of an asset may be determined by the:

A. Selling price + gain realized.
B. Selling price - gain realized.
C. Selling price + capital improvements - accumulated depreciation.
D. Original basis + capital improvements - selling price.
E. None of the above.

44. Bennett purchased a tract of land for $20,000 in 2004 when he heard that a new highway was going to be constructed through the property and the land would soon be worth $200,000. The highway project was abandoned in 2013 and the value of the land fell to $15,000. Bennett can claim a loss in 2013 of:

A. $0
B. $5,000
C. $165,000
D. $180,000
E. None of the above

45. Sol purchased land as an investment on January 12, 2004, for $85,000. On January 31, 2013, Sol sold the land for $20,000 cash. In addition, the purchaser assumed the mortgage of $70,000 on the land. What is the amount realized (not gain realized) on the sale of the land?

A. $5,000
B. $20,000
C. $70,000
D. $90,000
E. None of the above

46. For purposes of determining the adjusted basis of a capital asset at the time of its sale,

A. Capital improvements are added to the basis.
B. Ordinary repairs reduce the adjusted basis.
C. Accumulated depreciation is added to the basis.
D. The basis does not include costs such as title insurance and escrow fees related to the initial purchase.

47. Which of the following is *true* about capital gains?

    A. Short-term capital gains are *not* netted with other capital gains and losses.
    B. For 2013, long-term capital gains are subject to special tax treatment.
    C. Long-term capital gains are never taxed.
    D. Net short-term capital gains are *not* netted with net long-term capital losses.
    E. None of the above.

48. For the year 2013, Susan had salary income of $19,000. In addition she reported the following capital transactions during the year:

Long-term capital gain	$ 7,000
Short-term capital gain	$ 3,000
Long-term capital loss	$(2,000)
Short-term capital loss	$(4,000)

    There were no other items includable in her gross income. What is the amount of her adjusted gross income for 2013?

    A. $19,000
    B. $21,400
    C. $23,000
    D. $26,000
    E. None of the above

49. In December, 2013, Ben and Jeri (married, filing jointly) have a long-term capital gain of $55,000 on the sale of stock held for 4 years. They have no other capital gains and losses for the year. After standard deduction and personal exemptions, their ordinary income for the year, before the capital gain, is $72,500, making their total income for the year $127,500, ($72,500 + $55,000). In 2013, married taxpayers pay tax of $9,983 at 10 percent and 15 percent rates (from the tax table) on the first $72,500 of ordinary taxable income and 25 percent on ordinary taxable income up to $146,400. What is their total tax liability?

    A. $9,983
    B. $23,733
    C. $18,233
    D. $13,750

50. Robert and Becca are in the 25 percent tax bracket. They have a long-term capital gain of $27,000 and a long-term capital loss of $18,000 on sales of stock in 2013. What will their capital gains tax be in 2013?

    A. $4,050
    B. $6,750
    C. $1,350
    D. $9,000
    E. None of the above is correct

51. For purposes of taxation of capital gains:

    A. Short-term capital gains are taxed at 5 percent.
    B. Ordinary income tax rates are applied to gains on collectibles.
    C. Gains on Section 1231 assets may be treated as long-term capital gains, while losses in some cases may be deducted as ordinary losses.
    D. Under the provisions of Section 1245, any gain recognized on the disposition of a Section 1245 asset will be classified as a capital gain.

52. Martha has a net capital loss of $20,000 and other ordinary taxable income of $45,000 for the current year. What is the amount of Martha's capital loss carryforward?

    A. $0
    B. $10,000
    C. $14,000
    D. $17,000
    E. None of the above

53. In 2013, Paul, a single taxpayer, has taxable income of $30,000 exclusive of capital gains and losses. Paul incurred a $1,000 short-term capital loss and a $5,000 long-term capital loss. What is the amount of his long-term capital loss carryover to 2014?

    A. $0
    B. $2,000
    C. $3,000
    D. $5,000
    E. None of the above

54. For the 2013 tax year, Morgan had $25,000 of ordinary income. In addition, he had an $1,800 long-term capital loss and a $1,500 short-term capital loss. What will be the amount of Morgan's capital loss carryforward to 2014?

    A. $0
    B. $300
    C. $500
    D. $3,000
    E. $3,300

55. Martha has a net capital loss of $20,000 and other ordinary taxable income of $45,000 for the current tax year. What is the amount of Martha's taxable income after deducting the allowed capital loss?

    A. $25,000
    B. $35,000
    C. $42,000
    D. $45,000
    E. None of the above

56. In 2013, Marc, a single taxpayer, has ordinary income of $35,000. In addition, he has $3,000 in short-term capital gains, short-term capital losses of $6,000, and long-term capital gains of $4,000. What is Marc's adjusted gross income (AGI) for 2013?

A. $32,000
B. $39,000
C. $36,000
D. $34,000

57. Which of the following assets is *not* a Section 1231 asset?

A. Equipment used in a business
B. The unharvested crops of a farmer
C. Timber
D. Inventory
E. All of the above are Section 1231 assets

58. Which one of the following is true about Section 1231 assets?

A. Section 1231 assets are treated like capital assets when they produce losses on sale.
B. Business property held 1 year or less is considered a Section 1231 asset.
C. Section 1231 assets include company stock.
D. Section 1231 asset losses must be netted against 1231 asset gains before tax treatment is determined.
E. All of the above are false.

59. On December 31, 2013, Henry, a sole proprietor, sold for $65,000 a machine that was used in his business. The machine had been purchased in 2003 for $50,000, and when it was sold, it had accumulated depreciation of $20,000 and an adjusted basis of $30,000. For the year 2013, how should this gain be treated?

A. Ordinary income of $35,000
B. Section 1231 gain of $35,000
C. Section 1231 gain of $20,000 and ordinary income of $15,000
D. Section 1231 gain of $15,000 and ordinary income of $20,000
E. None of the above

60. Ben purchased an apartment building on January 1, 1994, for $200,000. The building has been depreciated over the appropriate recovery period using the straight-line method. On December 31, 2013, the building was sold for $220,000, when the accumulated depreciation was $62,500. Ben is in the highest tax bracket; on his 2013 tax return, he should report:

A. Section 1231 gain of $20,000 and ordinary income of $62,500
B. Section 1231 gain of $62,500 and ordinary income of $20,000
C. Ordinary income of $82,500
D. Section 1231 gain of $20,000 and "unrecaptured depreciation" taxed at 25 percent of $62,500
E. None of the above

61. In 2013, Tim sells Section 1245 property for $28,000 that he had purchased in 2007. Tim has claimed $5,000 in depreciation on the property and originally purchased it for $15,000. How much of the gain is taxable as ordinary income?

A. $5,000
B. $8,000
C. $18,000
D. $13,000
E. None of the above is correct

62. Sally acquired an apartment building in 1998 for $150,000 and sold it for $400,000 in 2013. At the time of the sale, there is $55,000 of accumulated straight-line depreciation on the apartment building. Assuming Sally is in the 35 percent tax bracket for ordinary income, how much of her gain is taxed at 15 percent?

A. None
B. $55,000
C. $250,000
D. $305,000
E. $400,000

63. Casualty gains and losses from business or investment property:

A. May be treated differently depending on whether the property has been held 1 year or less or has been held over 1 year.
B. Are treated the same as casualty gains and losses from personal property.
C. Are subject to the 10 percent of adjusted gross income limitation.
D. Are not subject to the depreciation recapture provisions.

64. Terry has a casualty gain of $1,000 and a casualty loss of $5,400, before the $100 floor and before the adjusted gross income limitation. The gain and loss were the result of two separate casualties occurring during 2013 and both properties were personal-use assets. If Terry itemizes deductions on her 2013 return and has adjusted gross income of $25,000, what is Terry's gain or net itemized deduction as a result of these casualties?

A. $5,300 itemized deduction, $1,000 capital gain
B. $4,300 itemized deduction
C. $1,800 itemized deduction
D. $2,800 itemized deduction, $1,000 capital gain
E. None of the above

65. Simon sold investment property 2 years ago for $750. Simon's basis in the property was $300. Simon is receiving $150 per year from the buyer. Simon reports this income on the installment method. If Simon collects $150 in principal during the current year, how much gain should he report from the sale for the year?

A. $0
B. $75
C. $90
D. $150
E. None of the above

66. Perry acquired raw land as an investment in 1996. The land cost $60,000. In 2013, the land is sold for a total sales price of $120,000, consisting of $10,000 cash and the buyer's note for $110,000. If Perry elects to recognize the entire gain in the year of sale, what is his recognized gain in 2013?

A. $50,000
B. $60,000
C. $100,000
D. $110,000
E. None of the above

67. Perry acquired raw land as an investment in 1996. The land cost $60,000. In 2013, the land is sold for a total sales price of $120,000, consisting of $10,000 cash and the buyer's note for $110,000. Assume that Perry uses the installment method to recognize the gain and receives only the $10,000 down payment in the year of sale. How much gain should Perry recognize in 2013?

A. $5,000
B. $5,833
C. $7,000
D. $9,000
E. None of the above

68. Tim sells land to Brad for $75,000. Tim originally purchased the land for $50,000. Brad agrees to pay Tim five annual installments of $15,000 each. In year three, Brad makes his third installment of $15,000. How much taxable gain will Tim have in year three?

A. $30,000
B. $20,000
C. $5,000
D. $10,000
E. All the taxable gain should be recognized in year one

69. Which one of the following qualifies as a like-kind exchange?

A. A chicken held by a farmer exchanged for medical services.
B. A home owned and lived in by a taxpayer exchanged for a new personal residence.
C. IBM stock exchanged for Exxon stock.
D. A Dodge Ram pickup truck used in business traded in for a new Ford 250 pickup truck also intended for business use.
E. None of the above are like-kind property.

70. In January 2013, Keyaki Construction Company exchanged an old truck, which cost $54,000 and had accumulated depreciation of $18,000, for a new truck having a fair market value of $65,000. In connection with the exchange, Keyaki paid $35,000 in cash. What is the tax basis of the new truck?

A. $54,000
B. $65,000
C. $71,000
D. $89,000
E. None of the above

71. Which of the following is true of a like-kind exchange:

A. There must be no cash exchanged to qualify.
B. The properties exchanged cannot be personal residences.
C. Office furniture can be exchanged for computers.
D. A new holding period for capital gains treatment starts on the day the exchange is completed.

72. Joseph exchanged land (tax basis of $36,000), that he had held for 4 years as an investment, for similar land valued at $40,000 which was owned by Adrian. In connection with this transaction, Adrian assumed Joseph's $12,000 mortgage. As a result of this transaction Joseph should report a long-term capital gain of:

A. $0
B. $4,000
C. $12,000
D. $16,000
E. None of the above

73. Which of the following statements is correct with respect to the deferral provisions of the Tax Code?

A. The like-kind exchange provision is elective.
B. The involuntary conversion provision is elective.
C. The exclusion of gain on the sale of a personal residence is elective.
D. Both the like-kind exchange and the involuntary conversion provisions are elective.
E. None of the above.

74. Johnny owned a gas station with an adjusted basis of $300,000. After it was destroyed in a fire, he received $600,000 from the insurance company. Within the next year, he bought a new gas station for $480,000. What is Johnny's taxable gain and what is the basis in the new building?

A. $120,000; $300,000
B. $180,000; $300,000
C. $120,000; $480,000
D. $120,000; $600,000
E. $180,000; $480,000

75. Jerry bought his home 15 years ago for $60,000. Three years ago Jerry married Debbie and she moved into the same house and has lived there since. If they sell Jerry's house in December, 2013 for $340,000, what is their taxable gain on a joint tax return?

A. $0
B. $280,000
C. $155,000
D. $30,000

76. On August 8, 2013, Sam, single, age 62, sold for $210,000 his principal residence, which he has lived in for 10 years, and which had an adjusted basis of $60,000. On November 1, 2013, he purchased a new residence for $80,000. For 2013, Sam should recognize a gain on the sale of his residence of:

A. $0
B. $25,000
C. $50,000
D. $130,000
E. None of the above

77. Which of the following statements is true?

A. A taxpayer's personal residence qualifies for a like-kind exchange.
B. A taxpayer who sells a personal residence may always exclude the realized gain from taxable income.
C. A one-time election is available to taxpayers 55 years of age or older which allows them to sell their personal residences and to exclude all of the realized gain.
D. None of the above are true.
E. All of the above are true.

78. Simonne, a single taxpayer, bought her home in La Jolla 25 years ago for $45,000. She has lived continuously in the home since she purchased it. In December, 2013, she sells her home for $405,000. What is Simonne's taxable gain on the sale?

A. $0
B. $360,000
C. $235,000
D. $110,000

79. If the following are capital assets, mark with a "Yes." If they are not capital assets, mark with a "No."

a. A taxpayer's personal jet ski ______
b. Ford Motor Credit Company bond held by an investor ______
c. A baseball for sale at Sports.com ______
d. J.K. Rowling's personal copy of her original manuscript of Harry Potter and the Sorcerer's Stone ______
e. An antique grandfather clock inherited from the taxpayer's aunt ______

80. The following are owned by Robert. Mark which are capital assets.

a. Rental property at 123 Main Street ______
b. Tables and chairs sold in his furniture business ______
c. The cash register used in his furniture business ______
d. A 1972 Porsche 916 ______
e. The rights to Weezer's song, "The Good Life" ______

81. Indicate whether a gain or loss realized in each of the following situations would be long-term or short-term by putting an "X" on the appropriate blank line:

Date Acquired	Date Sold	Long-term	Short-term
a. June 6, 2008	January 20, 2013	________	________
b. April 18, 2013	July 13, 2013	________	________
c. May 14, 2012	May 9, 2013	________	________
d. July 12, 2012	August 15, 2013	________	________
e. January 6, 2012	June 20, 2013	________	________

82. Emily sold the following investments during the year:

Stock	Date Purchased	Date Sold	Sales Price	Cost Basis
a. 1,000 shares Dot Com Co.	03-21-2002	02-04-2013	$20,000	$ 5,000
b. 500 shares Big Box Store	05-19-2012	01-22-2013	$ 8,200	$ 7,500
c. 300 shares Lotta Fun, Inc.	10-02-2012	09-21-2013	$ 3,000	$ 4,500
d. 700 shares Local Gas Co.	06-17-2012	11-11-2013	$14,000	$17,000

For each stock, calculate the amount and the nature of the gain or loss.

83. Nick received a gift of stock from his father. Nick's father had purchased the stock 2 years earlier and his father's basis in the stock was $30,000. On the date of the gift, the stock had a fair market value of $25,000.

a. If Nick sells the stock for $23,000, calculate the amount of Nick's gain or loss on the transaction.
b. If Nick sells the stock for $32,000, calculate the amount of Nick's gain or loss on the transaction.
c. If Nick sells the stock for $27,000, calculate the amount of Nick's gain or loss on the transaction.

84. Bev owns an apartment complex she purchased 10 years ago for $500,000 with a $100,000 cash down payment accompanied by a $400,000 loan. Bev has made $75,000 of capital improvements on the complex and her depreciation claimed on the building to date is $120,000. Calculate Bev's adjusted basis in the building.

85. Karen received a stock portfolio upon the death of her grandmother. The stock originally cost her grandmother $32,000, but was worth $300,000 when she died. What is Karen's tax basis in the stock portfolio? Explain.

86. At the end of 2013, Falstaff sold for $5,000 General Martin stock that was purchased 5 months ago for $4,000. He also sold Cedar stock for $6,000 at the same time. The Cedar stock cost $4,000, 2 years ago. In addition, Falstaff has a short-term capital loss of $500 on the sale of silver.

a. Calculate the amount of Falstaff's net short-term and net long-term capital gain or loss.
b. If Falstaff has a net capital gain, what is the maximum rate at which the gain will be taxed?

87. In October of the current year, Mike sold a share of Berkshire-Hathaway for $73,000. He had acquired it several years ago at a cost of $38,000. He also sold Microsoft stock he had held for 3 years at a gain of $17,000. He had a short-term $2,000 loss on the sale of stock of a start-up technical company. He has $85,000 in taxable income before capital transactions are taken into account.

What is the amount of Mike's tax on the capital transactions?

88. In 2013, Estes has net short-term capital losses of $3,000, a net long-term capital loss of $45,000, and taxable income from wages of $35,000.

a. Calculate the amount of Estes' deduction for capital losses for 2013.
b. Calculate the amount and nature (short-term or long-term) of his capital loss carryforward.
c. For how many years may Estes carry the unused loss forward?

89. During 2013, William sold the following capital assets:

Description	Date Purchased	Date Sold	Sales Price	Cost Basis
ABC Stock	05-05-2009	08-03-2013	$ 500	$9,000
123 Bond Fund	11-07-2012	02-25-2013	$2,000	$6,000
Dune buggy	06-12-2008	09-29-2013	$2,400	$4,600
Antique chair	10-09-2000	04-21-2013	$4,000	$3,000

Calculate the following:

a. Total short-term capital gain/loss realized for tax purposes
b. Total long-term capital gain/loss realized for tax purposes
c. Deductible capital gain/loss
d. The amount and nature (short-term or long-term) of his capital loss carryforward
e. Assuming that William has no capital gain or loss for 2014, how much can he deduct in 2014 and what is the amount and nature of any carryforward to 2015?

90. Elmer sold machinery used in his business for $20,000. The machinery originally cost $75,000 and had $40,000 of accumulated depreciation at the time of the sale.

a. What is the gain or loss on the sale of the machinery?
b. Is the gain or loss treated as capital or ordinary? Explain.

91. After 4 years of life in the slow lane, Doug decided to give up his goat ranch and move back to the big city. He sold the goat milking machine for $1,000. The machine originally cost $1,200 and had $920 of accumulated depreciation at the time of sale.

a. What is the total gain or loss on the sale of the goat milking machine?
b. Is the gain or loss treated as capital or ordinary? Explain.

92. In 2013, Helen sold Section 1245 property for $6,000. The property cost $25,000 when it was purchased 5 years ago. The depreciation claimed on the property was $23,000.

a. Calculate the adjusted basis of the property.
b. Calculate the amount of ordinary income under Section 1245.
c. Calculate the Section 1231 gain.

93. Robert acquired his rental property in November 2003 for $100,000 and sold it in October 2013 for $225,000. The accumulated straight-line depreciation on the property at the time of the sale was $20,000. Robert is in the 35 percent tax bracket for ordinary income.

a. What is Robert's gain on the sale of his rental property?
b. How is the gain taxed? (i.e., What tax bracket is the gain subject to)?

94. Rod had the following personal casualty in 2013:

	Decrease in fair market value due to casualty	Adjusted basis	Insurance reimbursement	Holding period
Rod's antique furniture was vandalized.	$2,500	$500	$1,700	20 years

Calculate the amount and nature of Rod's gain or loss as a result of this casualty.

95. Rod had the following loss on business-use property:

	Decrease in fair market value due to casualty	Adjusted basis	Insurance reimbursement	Holding period
Rod's storage shed was partially destroyed by fire.	$300	$700	$100	2 years

Calculate the amount and nature of Rod's gain or loss as a result of this casualty.

96. Dan acquired rental property in June 2003 for $380,000 and sold it in October, 2013. $30,000 in straight-line depreciation has been taken on the house. A run-up in housing prices in San Diego allowed him to sell the house for $570,000. In the year of sale, Dan received $170,000 when the buyer sold some investments, an additional $200,000 when the buyer closed a loan from the bank, and took a $200,000 note from the buyer, payable on the anniversary of the sale date in 10 installments of $20,000 each plus interest on the unpaid balance.

Using the installment method, calculate his taxable gain in the year of sale.

97. Verlin sells a commercial building and receives $50,000 in cash and a note for $50,000 at 10 percent interest. Verlin's adjusted basis in the building on the date of sale is $40,000 and he collects only the $50,000 down payment in the year of the sale.

a. If Verlin elects to recognize the total gain on the property in the year of sale, calculate the taxable gain.
b. Assuming Verlin uses the installment sale method, calculate the taxable gain he must report for the year of the sale.
c. Assuming Verlin collects $10,000 (not including interest) of the note principal in the year following the year of sale, calculate the amount of income recognized under the installment sale method.

98. During 2013, Ethel exchanges a machine for another machine in a like-kind exchange. Ethel's adjusted basis in the machine given up is $8,000, and she receives a machine worth $12,000 plus $2,000 cash.

a. Calculate the amount of gain realized by Ethel on the exchange.
b. Calculate the amount of the gain that must be recognized by Ethel on the transaction.
c. Calculate Ethel's basis in the new machine.

99. The owner of M&N Milling exchanged a milling machine used in his business for a new one. M&N Milling's basis in the machine was $20,000 and the owner still owes $6,000 related to the purchase of the machine. The other party to the exchange, M. Grinding, assumed the liability along with the machine and transferred a newer and smaller machine worth $30,000 to M&N Milling.

a. Calculate M&N Milling's
1. Realized gain on the exchange. $__________
2. Recognized gain on the exchange. $__________
b. Calculate the adjusted basis of the newer machine. $__________

100.In 2013, Penny exchanges an investment property in Santa Barbara with a mountain view for a lot with an ocean view in a qualifying like-kind exchange. Penny's basis in the land given up is $100,000 and the property has a fair market value of $250,000. In exchange for her property, Penny receives land with a fair market value of $200,000 and cash of $20,000. In addition, the other party to the exchange assumes a mortgage loan on Penny's property of $30,000.

a. Calculate Penny's realized gain, if any, on the exchange.
b. Calculate Penny's recognized gain, if any, on the exchange.
c. Calculate Penny's basis in the property received.

101.During 2013, an office desk used by Pat in his business was completely destroyed by a fire. The adjusted basis of the desk was $900 (original cost of $1,500 less accumulated depreciation of $600). Pat received $500 from his insurance company, but he did not replace the desk.

a. What is the amount of Pat's recognized gain or loss (deduction) as a result of the casualty?
b. Assuming this is Pat's only casualty gain or loss for 2013, what is the nature of the gain or loss?

102. Lorreta has a manufacturing business. In 2013, her storage building is completely destroyed by fire and she receives $300,000 from her insurance company. She purchased the building for $295,000 in 1994 and has claimed depreciation of $80,000 using the straight-line method. In 2014, she purchases a new storage building at a cost of $285,000.

a. Calculate Lorreta's realized gain or loss.
b. Assuming Lorreta makes an election under the involuntary conversion provision, calculate Lorreta's recognized gain or loss?
c. Assuming Lorreta makes an election under the involuntary conversion provision, what is Lorreta's basis in the new building?

103. The office building Donna owned and used for her desk-top publishing business was destroyed by a hurricane. Although the basis of the building was $80,000, Donna carried replacement cost insurance and received $160,000 from the insurance company after it was determined that the building was a complete loss. It cost her $152,000 to rebuild the store in 2014.

a. Calculate Donna's recognized gain, assuming an election under the involuntary conversion provision is made. $__________

b. Calculate Donna's basis in the replacement building. $__________

104. Russell purchased a house 1 year ago for $150,000 and, due to an employment-related move, sold the house this year for $200,000. What is Russell's taxable gain?

105. Stewart, age 44, sells his personal residence of 4 years on June 14, 2013, for $185,000. The expenses of sale are $15,000 and he has paid for capital improvements of $3,000. Stewart purchased the residence for $100,000. On February 2, 2014, Stewart purchases and occupies a new residence at a cost of $200,000.

a. Calculate the gain realized on the sale of Stewart's residence.
b. How much gain must be recognized on the sale of Stewart's residence?
c. Calculate Stewart's basis in the new residence.

106. In November, 2013, 70 year-old Jeanette sells her personal residence of the last 40 years for $350,000. Jeanette's basis in her residence is $60,000. The expenses associated with the sale of her home total $20,000. Jeanette decides to move in with her daughter rather than purchase a new residence. Calculate Jeanette's realized gain and recognized gain on the sale of her residence.

a. Realized gain
b. Recognized gain

107. What are capital assets?

108. What is the treatment given to personal casualty gains and losses?

Chapter 8: Capital Gains and Losses Key

1. TRUE

2. TRUE

3. FALSE

4. TRUE

5. TRUE

6. TRUE

7. TRUE

8. FALSE

9. TRUE

10. TRUE

11. FALSE

12. TRUE

13. FALSE

14. TRUE

15. FALSE

16. TRUE

17. TRUE

18. FALSE

19. TRUE

20. FALSE

21. TRUE

22. TRUE

23. TRUE

24. FALSE

25. TRUE

26. FALSE

27. FALSE

28. FALSE

29. FALSE

30. FALSE

31. TRUE

32. C

33. C

34. C

35. B

36. B

37. A

38. D

39. C

40. B

41. B

42. A

43. B

44. A

45. D

46. A

47. B

48. C

49. C

50. C

51. C

52. D

53. C

54. B

55. C

56. C

57. D

58. D

59. D

60. D

61. A

62. C

63. A

64. C

65. C

66. B

67. A

68. C

69. D

70. C

71. B

72. C

73. B

74. A

75. A

76. A

77. D

78. D

79. a. Yes
b. Yes
c. No
d. No
e. Yes

80. a. Rental property at 123 Main Street
d. A 1972 Porsche 916
e. The rights to Weezer's song, "The Good Life"

81. a. Long-term
b. Short-term
c. Short-term
d. Long-term
e. Long-term

82. a. $15,000 long-term gain
b. $700 short-term gain
c. $1,500 short-term loss
d. $3,000 long-term loss

83.
a. **$2,000 loss** = $25,000 - 23,000.
b. **$2,000 gain** = $32,000 - 30,000.
c. **$0**. No gain or loss is recognized since the property is sold at a price that falls between the donor's basis for gain and basis for loss.

84. **$455,000** = $500,000 + $75,000 - $120,000

85. **$300,000**. If property is received from a decedent, the basis to the recipient is usually the fair market value at the decedent's date of death.

86.
a. Net short-term capital gain of $500 and a net long-term capital gain of $2,000.
b. Net capital gains (net long-term capital gains in excess of net short-term capital losses) are subject to tax rates up to 28%, depending on the nature of the asset sold. In this instance, the sale of stock is subject to a maximum capital gains rate of 20% (0% if Falstaff is in the 10% or 15% tax bracket or 15% if Falstaff is in the 25% to 35% tax brackets). The net short-term capital gain will be taxed at ordinary income rates, which range up to 39.6%. High-income taxpayers also incur the 3.8% ACA Medicare surtax.

87. Based on his other taxable income, Mike has a capital gains tax rate of 15 percent. $50,000 of net capital gains ($35,000 + $17,000 - $2,000), taxed at 15 percent results in **$7,500 of tax**.

88.
a. **$3,000**
b. **$45,000** net long-term capital loss. Short-term capital losses are deducted first.
c. Unused capital losses may be carried forward indefinitely

89. a. $4,000 short-term loss ($2,000 - $6,000)
b. $7,500 long-term loss ($500 - $9,000) + ($4,000 - $3,000). Since the dune buggy is a personal asset, the loss is not allowed for tax purposes.
c. $3,000. $4,000 + $7,500 = $11,500, limited to $3,000.
d. $1,000 short-term capital loss carryforward ($4,000 - $3,000)
$7,500 long-term capital loss carryforward.
e. $3,000 capital loss may be deducted on William's 2014 tax return, and he has a $5,500 long-term capital loss carryforward to 2015.

90.
a. **$15,000 loss** = $20,000 - ($75,000 - $40,000)
b. **Ordinary loss**. Depreciable property used in a trade or business is Section 1231 property.

91. a. **$720 gain.** $1,000 - ($1,200 - $920)
b. **Ordinary Section 1245 depreciation recapture.** The machine is Section 1231 property. The gain is all attributable to depreciation previously taken.

92.
a. **$2,000** = $25,000 - $23,000
b. **$4,000** = $6,000 sales price - $2,000 adjusted basis
c. **$0**. The gain recognized did not exceed the amount of the potential Section 1245 recapture

93. a. **$145,000.** Calculated as $225,000 - ($100,000 - $20,000).
b. **$20,000** of the gain is attributable to unrecaptured depreciation which is taxed at 25 percent, while the remaining **$125,000** gain is taxed at the 15 percent long-term capital
gain rate.

94. **$1,200 long-term capital gain** due to casualty. $1,700 insurance reimbursement less $500 (lesser of adjusted basis or decrease in fair market value).

95. **$200 long-term loss.** The loss is a Section 1231 loss which is treated as an ordinary (not capital) loss. The basis of the shed is adjusted to $400 ($700 - $300).

96. $570,000 - ($380,000 - $30,000) = $220,000 profit.

$220,000 / $570,000 = a profit percentage of 38.6%.

$370,000 collected in the year of sale times the profit percentage of 38.6 = a **taxable gain of $142,820** in the year of the sale. The taxable gain may also be calculated as **$142,807,** if the profit percentage is not rounded.

97.
a. **$60,000** = $50,000 + $50,000 - $40,000
b. **$30,000** = $50,000 ´ ($60,000/$100,000)
c. **$6,000** = $10,000 ´ 60% gain rate

98.
a. **$6,000** = $12,000 + 2,000 - 8,000.
b. **$2,000**, the lesser of the gain realized or the boot received.
c. **$8,000** = $8,000 - 2,000 + 2,000.

99. a. 1. Value of new machine, $30,000, plus the liability assumed by M. Grinding, $6,000, less the basis of $20,000 equals a **$16,000 gain**.
2. **$6,000** of the gain, the amount equal to the boot received, is recognized as taxable gain.
b. Basis of $20,000 for the property given up less $6,000 boot received plus gain recognized of $6,000 equals the **new basis of $20,000**. Note that $16,000 of gain was realized, but only $6,000 of boot was received, and this limits the amount of the realized gain to be recognized.

100.
a. **$150,000** = ($200,000 + $20,000 +$30,000) - $100,000
b. **$50,000**, the sum of the cash received and the loan assumed
c. **$100,000** = $100,000 - $50,000 + $50,000

101.
a. **$400 loss** = $900 - $500
b. **Ordinary loss**

102.
a. **$85,000 gain realized** = $300,000 - ($295,000 - $80,000).
b. **$15,000 recognized gain** = $300,000 - $285,000.
c. **$215,000** = $285,000 - ($85,000 - $15,000), purchase price less unrecognized gain of $70,000.

103. a. A gain of $80,000 was realized, but only **$8,000 (the amount not reinvested)** was recognized.
b. Although the new building cost $152,000, $72,000 of realized gain was deferred (not recognized) and the building cost minus the deferred gain results in a **basis of $80,000** for the replacement building.

104. **$0.** The $250,000 exclusion is pro-rated in the case of the employment-related move. $125,000 exclusion = (1 year / 2 years ´ $250,000)

105.
a. **$67,000** = $185,000 - $15,000 - $3,000 - $100,000.
b. **$0.** Up to $250,000 of gain is excluded from taxable income.
c. **$200,000**.

106.
a. **$270,000** = $350,000 - $60,000 - $20,000
b. **$20,000** = $270,000 - $250,000 exclusion

107. A capital asset is any property whether or not used in a trade or business except for assets specifically excluded by tax law. Examples of assets not considered to be capital assets are inventory, depreciable property used in a trade or business, and accounts and notes receivable.

108. Personal casualty gains and losses are first netted. If, after applying the $100 floor to each casualty loss but before the 10 percent of adjusted gross income limitation, the net amount is a gain, it is treated as a capital gain. If it is a loss, it is treated as a casualty loss and is an itemized deduction, subject to the 10 percent of adjusted gross income limitation.

CHAPTER 9

WITHHOLDING, ESTIMATED PAYMENTS, AND PAYROLL TAXES

BRIEF TOPICAL OUTLINE

A. Learning Objectives and Overview
B. Withholding Methods
   1. Withholding allowances and Form W-4
   2. Computing withholding
      - Percentage method
      - Wage bracket method
   3. Pension and deferred income
   4. Tip reporting
   5. Backup withholding
C. Estimated Payments
   1. Requirements for filing
   2. Underpayment of estimated tax
   3. Avoiding the underpayment penalty
D. The FICA Tax
   1. Two parts, the Social Security tax and the Medicare tax
   2. Paid by employee and employer
   3. Applicable rates
      - Social Security rate
      - Medicare rate
   4. Maximum base amounts
      - Social Security tax maximum base amount
      - No Medicare tax maximum base amount
   5. Overpayment of FICA taxes
E. Federal Tax Deposit System
   1. Frequency of deposits
   2. How deposits are made
   3. Filing Form 941
F. Employer Reporting Requirements
   1. Form W-2
      - Wages and tips reported on Form W-2
      - Other compensation, including reimbursements
   2. Other Forms W-2
   3. Information returns—Forms 1099
G. Self-Employment Tax
   1. Comprised of two parts, the Social Security tax and the Medicare tax
   2. Applicable rates
      - Social Security rate
      - Medicare rate
   3. Maximum base amounts
      - Social security tax maximum base amount
      - No Medicare tax maximum base amount
   4. Net earnings from self-employment
   5. Calculation of self-employment tax

H. The FUTA Tax
   1. Rates
      - Federal
      - State
   2. Maximum base amount
   3. Filing Form 940

I. The Nanny Tax
   1. Threshold for reporting
   2. Employee-employer relationship
   3. Schedule H

J. The 0.9 Percent Medicare Surtax for High-Income Taxpayers
   1. Definition of "high-income"
   2. Calculation of surtax for employees and self-employed taxpayers

SUGGESTED MINIMUM ASSIGNMENT:

Problems 1, 3, 4, 5, 6, 7, 9, 13 and 16
Optional: Writing assignment
Comprehensive problem

Chapter 10: Partnership Taxation

Student: ____

1. If Margo and Bruce purchase and operate an ice cream store, for tax purposes they have formed a partnership.

   True False

2. Income from a partnership is taxed to the partner only if the partner receives the income as a distribution during the year.

   True False

3. Because a partnership does not pay taxes, a partnership is *not* recognized as a legal entity under civil law.

   True False

4. In general, income is recognized by the partner when a partnership interest is received in exchange for services rendered to the partnership.

   True False

5. The holding period of property contributed to a partnership includes the period of time that the contributor has held the property.

   True False

6. The basis of a partner's interest in a partnership is increased by losses of the partnership allocated to the partner.

   True False

7. A partnership may deduct a single personal exemption in calculating ordinary taxable income or loss.

   True False

8. A partnership reports its income on Form 1040.

   True False

9. Partnership losses that are not used because a partner's basis in the partnership interest is zero may *not* be carried forward and are lost by the partner.

   True False

10. Partnership income is taxed at the same tax rates as the income of corporations.

True False

11. A partnership must separately report Section 1231 gains and losses rather than including them in ordinary taxable income.

True False

12. A partnership may *not* show a loss as a result of deducting guaranteed payments made to the partners.

True False

13. Guaranteed payments made by a partnership must be made to individuals other than partners in the partnership.

True False

14. A partnership tax year will close if the partnership ceases to carry on any business activity.

True False

15. The tax year of a partnership generally closes upon entry of a new 20% partner.

True False

16. A partnership generally must adopt the same tax year as its majority partners.

True False

17. Guaranteed payments received from a partnership are included in the income of the partner receiving the payments on a cash basis, without regard to the partnership's tax year.

True False

18. Ownership of a partnership interest by a taxpayer's brother is considered indirect ownership by the taxpayer.

True False

19. If a partner has a more than 50 percent interest in a partnership, a capital gain resulting from the sale of property to the partnership will be taxed as ordinary income to the partner, provided the property is not a capital asset to the partnership.

True False

20. Losses on transactions between a partnership and its partners are always disallowed.

True False

21. Losses are disallowed for transactions between a partnership and a partner who has a 50 percent interest in the partnership.

True False

22. The "at-risk" rule acts to prevent tax shelters from generating large losses for their investors while exposing them to little personal risk.

True False

23. The "at-risk" rule applies, with limited exceptions, to all taxable activities.

True False

24. The “at-risk” rule does *not* apply to activities involving real estate.

True False

25. There is no general partner required in a limited liability company (LLC).

True False

26. Limited liability companies may operate in more than one state.

True False

27. Which one of the following is *not* true about partnerships?

A. There must be two or more owners.
B. General partners assume more risk of legal liability than limited partners.
C. An LLC limits certain liability risks.
D. A partnership is taxed like a corporation.
E. All of the above are true.

28. Which of the following statement is true about partnerships?

A. The formation of a partnership must be documented in writing.
B. An LLC is generally treated as a partnership for tax law purposes.
C. General partners have no liability for partnership obligations beyond their capital contributions.
D. When Sue and Billy Bob invest in land together, they are considered to have formed a partnership.

29. On July 1, 2013, Bertram acquired a 30 percent interest in Sycamore Company, a partnership, by contributing property with an adjusted basis of $6,000 and a fair market value of $12,000. The property was subject to a mortgage of $8,000, which was assumed by Sycamore Company. What is Bertram's basis in his partnership interest in Sycamore Company immediately after the partnership contribution?

A. $400
B. $3,600
C. $6,400
D. $8,400
E. None of the above

30. On July 1, 2013, Ambrose was admitted to partnership in the firm of Ambrose and Nectar. His contribution to capital consisted of 500 shares of stock in Paniculata Corporation, which he bought in 1985 for $10,000 and which had a fair market value of $50,000 on July 1, 2013. Ambrose's interest in the partnership's capital and profits is 25 percent. On July 1, 2013, the fair market value of the partnership's net assets (after Ambrose was admitted) was $200,000. What is Ambrose's taxable gain in 2013 on the exchange of stock for his partnership interest?

A. $0 gain or loss
B. $40,000 ordinary income
C. $40,000 long-term capital gain
D. $40,000 Section 1231 gain
E. None of the above

31. During 2013, Norman contributed investment property held for over one year to the Mary Ann Partnership for a 40 percent interest in partnership capital and profits. His tax basis in the property contributed was $8,000, and the property had a fair market value of $10,000 on the date of the contribution to the partnership. What gain or loss should Norman report as a result of the contribution of the property to the partnership in exchange for the 40 percent partnership interest?

A. No gain or loss
B. $2,000 long-term capital gain
C. $2,000 ordinary income
D. $10,000 long-term capital gain
E. None of the above

32. Leslie contributes a building worth $88,000, with an adjusted basis of $38,000, to a partnership in exchange for a 50 percent interest in the partnership's capital and profits. What is the amount of Leslie's basis in her partnership interest immediately after the contribution?

A. $38,000
B. $44,000
C. $50,000
D. $88,000
E. None of the above

33. An equal partnership is formed by Rita and Gerry. Rita contributes cash of $10,000 and a building with a fair market value of $150,000, adjusted basis of $55,000, and subject to a liability of $60,000. Gerry contributes cash of $100,000. What amount of gain must Rita recognize as a result of this transaction?

A. $95,000
B. $35,000
C. $5,000
D. $0
E. None of the above

34. An equal partnership is formed by Rita and Gerry. Rita contributes cash of $10,000 and a building with a fair market value of $150,000, adjusted basis of $55,000, and subject to a liability of $60,000. Gerry contributes cash of $100,000. What is Rita's basis in her partnership interest immediately after formation of the partnership?

A. $25,000
B. $35,000
C. $65,000
D. $70,000
E. None of the above

35. An equal partnership is formed by Rita and Gerry. Rita contributes cash of $10,000 and a building with a fair market value of $150,000, adjusted basis of $55,000 and subject to a liability of $60,000. Gerry contributes cash of $100,000. What is the partnership's basis in the building contributed by Rita?

A. $55,000
B. $60,000
C. $90,000
D. $150,000
E. None of the above

36. Loretta contributes property to a partnership in exchange for a 25 percent partnership interest. The property contributed has a fair market value of $45,000 and a basis of $35,000 on the date of the contribution to the partnership. In addition, Loretta receives a 10 percent partnership interest, valued at $18,000, in exchange for services rendered to the partnership. What is Loretta's basis in her partnership interest, immediately after these transactions?

A. $35,000
B. $45,000
C. $53,000
D. $63,000
E. None of the above

37. A partner's interest in a partnership is decreased by:

A. Capital gains of the partnership.
B. Distributions from the partnership.
C. Taxable income of the partnership.
D. Additional contributions by the partner.
E. None of the above.

38. Sabrina contributes a building with an adjusted basis of $40,000 to a partnership. The fair market value of the building is $100,000 on the date of the contribution. What is Sabrina's basis in her partnership interest immediately after the contribution?

A. $0
B. $40,000
C. $80,000
D. $100,000
E. None of the above

39. Jamie decides to contribute cash and property to a partnership she and her friends started. She contributes a building worth $260,000 that she purchased for $100,000 and she also contributes $40,000 in cash. What is her basis in the partnership?

A. $300,000
B. $100,000
C. $260,000
D. $140,000
E. None of the above is correct

40. Which of the following statements about partnerships is true?

A. Partnerships must file their tax returns on a calendar year basis.
B. No gain or loss is ever recognized in transactions between partners and a partnership.
C. Gain is never recognized by a partner on a contribution of property to a partnership.
D. A partner's original basis in a partnership interest is equal to the basis of the property transferred (plus cash contributed) to the partnership, adjusted for any gain recognized on the transfer and reduced for liabilities assumed by the other partners.
E. The partnership's basis in property contributed by a partner is equal to the fair market value of the property on the date of the transfer.

41. The partnership of Truman and Hanover realized the following items of income during the year ended December 31, 2013:

Net income from operations	$62,000
Dividends from domestic corporations	$ 4,000
Interest on corporate bonds	$ 3,000
Net long-term capital gains	$ 5,000
Net short-term capital gains	$ 1,000

Both the partners are on a calendar year basis. What is the total income which should be reported as ordinary income from business activities of the partnership for 2013?

A. $62,000
B. $65,000
C. $69,000
D. $70,000
E. None of the above

42. Which of the following items must be reported separately from ordinary income or loss on a partnership return?

A. Capital losses
B. Miscellaneous income
C. Cost of goods sold
D. Sales income
E. None of the above

43. For tax purposes, in computing the ordinary income of a partnership, a deduction is allowed for:

A. Payments to partners, determined without regard to the income of the partnership, for services provided to the partnership.
B. The net operating loss deduction.
C. Contributions to charitable organizations.
D. Personal exemptions of the partners.
E. None of the above.

44. Which one of the following is *not* true about partnerships and their income-reporting process?

A. The partnership must file a Form 1065.
B. The partner's share of income/loss is presented on Schedule K-1.
C. A partner's deductible loss is limited to his basis in the partnership.
D. The partnership pays income tax.
E. All of the above are true.

45. The partnership of Felix and Oscar had the following items of income during the tax year ended December 31, 2013:

Income from operations	$156,000
Tax-exempt interest income	$ 8,000
Dividend income	$ 6,000

What is the total ordinary income from business activities passed through by the partnership for the 2013 tax year?

A. $156,000
B. $157,000
C. $162,000
D. $170,000
E. None of the above

46. Nash and Ford are partners who share profits and losses equally. For the year ended December 31, 2013, the partnership had book income of $80,000 which included the following deductions:

Guaranteed payments to partners:	
Nash	$35,000
Ford	$25,000
Charitable contributions	$ 5,000

What amount should be reported as ordinary income on the partnership return for 2013?

A. $80,000
B. $85,000
C. $140,000
D. $145,000
E. None of the above

47. Phil and Bill each own a 50 percent interest in P&B Interests. P&B Interests has ordinary income for the year of $35,000 before guaranteed payments to Phil. If Phil receives guaranteed payments of $25,000 during the tax year, what is the total income or loss that should be reported by Phil from the partnership for this tax year?

A. $5,000 income
B. $17,500 income
C. $25,000 income
D. $30,000 income
E. None of the above

48. Barbara receives a current distribution consisting of $2,000 cash plus other property with an adjusted basis to the partnership of $2,300 and a fair market value on the date of the distribution of $7,000. Barbara has a 10 percent interest in the partnership and her basis in her partnership interest, immediately prior to the distribution, is $5,000. What is Barbara's basis in the non-cash property received in the current distribution?

A. $2,000
B. $2,300
C. $3,000
D. $7,000
E. None of the above

49. Jim's basis in his partnership is $200,000. His share of the 2013 income is $60,000. The partnership gave him a $75,000 distribution in 2013. What is his new basis in the partnership and what is his taxable income?

A. $200,000; $75,000
B. $200,000; $60,000
C. $140,000; $60,000
D. $185,000; $60,000
E. $125,000; $75,000

50. Salix Associates is a partnership with an October 31 year-end. For the fiscal year ended October 31, 2013, Salix Associates reported ordinary income of $100,000, after deducting guaranteed payments. Max, a calendar year taxpayer, is a 30 percent partner in the partnership and received $2,000 monthly as a guaranteed payment for the calendar year 2012, and $2,100 monthly for the calendar year 2013. What is the total income from the partnership that Max should report on his 2013 individual income tax return?

A. $30,000
B. $54,200
C. $55,000
D. $55,200
E. None of the above

51. Jordan files his income tax return on a calendar-year basis. He is the principal partner of a partnership reporting on a June 30 fiscal year end basis. Jordan's share of the partnership's ordinary income was $24,000 for the fiscal year ended June 30, 2013, and $72,000 for the fiscal year ended June 30, 2014. How much should Jordan report on his 2013 individual income tax return as his share of taxable income from the partnership?

A. $24,000
B. $36,000
C. $48,000
D. $72,000
E. None of the above

52. Under which of the following circumstances would a partnership terminate and close its tax year?

A. Divorce of a partner
B. Sale of an interest in a partnership by a partner who holds a 60 percent capital and profits interest
C. Entry of a new partner
D. Distribution of property to a 10 percent partner in complete termination of the partner's interest in the partnership
E. None of the above

53. Kitty is a 60 percent partner of Tabby Associates. Kitty sells a building to the partnership for $75,000. If the building had an adjusted basis to Kitty of $95,000, how much gain or loss does Kitty recognize on this transaction?

A. $95,000 loss
B. $20,000 loss
C. $0 gain or loss
D. $20,000 gain
E. None of the above

54. Barry owns a 50 percent interest in B&B Interests, a partnership. His brother, Benny, owns a 35 percent interest in that same partnership, and the remaining 15 percent is owned by an unrelated individual. During 2013, Barry sells a rental property with a basis of $60,000 to B&B Interests for $100,000. The partnership intends to hold the rental as inventory for resale. What is the amount and nature of Barry's gain or loss on this transaction?

A. $40,000 long-term capital loss
B. $0 gain or loss
C. $40,000 long-term capital gain
D. $40,000 ordinary income
E. None of the above

55. Owen owns 60 percent of the Big Time partnership. He sells to the partnership a machine for $70,000 that has a $45,000 basis. What would the taxable income be for Owen and what is the partnership's basis in the machine?

A. $25,000; $45,000
B. $0; $45,000
C. $25,000; $70,000
D. None of the above is correct

56. Wallace and Pedersen have equal interests in the capital and profits of the partnership of Wallace and Pedersen, but are otherwise unrelated. On August 1, 2013, Wallace sold 100 shares of Kalmia Mining Corporation to the partnership for its fair market value of $7,000. Wallace had bought the stock in 1998 at a cost of $10,000. What is Wallace's deductible loss for 2013 as a result of the sale of this stock?

A. $0
B. $1,500 long-term capital loss
C. $3,000 long-term capital loss
D. $3,000 ordinary loss
E. None of the above

57. Which of the following liabilities would be considered nonrecourse?

A. A bank loan for which the taxpayer is personally liable.
B. Credit card debt.
C. A $20,000 real estate loan which allows the bank to take the real estate if the taxpayer stops making payments on the loan.
D. All of the above are nonrecourse liabilities.

58. At the beginning of the year, Joe's basis in his partnership interest was $5,000. During the year, Joe contributed $10,000 in cash to the partnership and signed a bank loan to be personally liable for the partnership's debt of $25,000. For the current year, the partnership allocated a loss of $60,000 to Joe. In the following year, Joe's portion of the partnership income is $30,000. Which of the following is accurate?

A. In the following year, Joe's reportable taxable income from the partnership is $10,000.
B. Joe's basis in his partnership at the end of the year is $15,000.
C. Joe may deduct all of the $60,000 loss in the current year.
D. Joe may carry over a $45,000 loss to the following year.

59. Which of the following is *true* about an LLC (Limited Liability Company)?

A. An LLC is always treated like a corporation for tax purposes.
B. An LLC must have at least two members.
C. An LLC is always taxed like a partnership.
D. An LLC's limited liability is similar to a corporation's.
E. All of the above are false.

60. Which of the following is a *disadvantage* of an LLC?

A. For security law purposes, an ownership interest in an LLC is not necessarily a security.
B. There is no general partner requirement.
C. Taxable income and losses pass through to the owners.
D. The states are not uniform in their treatment of limited liability companies.

61. For the following separate, independent situations indicate with a "Yes" if a partnership return needs to be filed. Mark with a "No" if a partnership return is not required.

a. Tony and Gina form a joint venture to import goods from South Korea.
b. Nancy decided to start her own private investigative business.
c. Uncle Pennybag's estate assets are pooled together until they can be distributed to the beneficiaries.
d. Howie, Dewey, and Cheatem form an LLC.
e. Flora, Fauna, and Merryweather start a child care business. No official documents are drawn up.

62. Jack and Jill decided to pool their money and start a water delivery business. Since they trust each other so much, they did not draw up any legal documents for the business. During the first year of business, they earned $50,000 which was net of $10,000 paid to Jill as a guaranteed payment. During the second year of business, they decided to limit their liability exposure by forming an LLP.

a. Was a partnership formed during the first year?
b. If a partnership was formed, how much income will the partnership pay tax on?
c. For the second year, do they need to file a partnership tax return?

63. Cooke and Thatcher form the C&T Partnership. Cooke contributes equipment with a fair market value of $80,000 and a basis of $35,000, in exchange for an 80 percent interest in the partnership capital and profits. Thatcher performs services worth $20,000 for the partnership in exchange for a 20 percent interest in capital and profits.

a. What is the amount of Cooke's recognized gain or loss (if any) as a result of the contribution to the partnership in exchange for the partnership interest?
b. What is Cooke's basis in his partnership interest immediately after the contribution?
c. What is the amount of Thatcher's recognized income or loss (if any) on the contribution to the partnership?
d. What is Thatcher's basis in her partnership interest immediately after the contribution?
e. What is C&T Partnership's basis in the equipment received from Cooke?

64. Oscar and Frank form an equal partnership, the O and F Partnership. Oscar contributes land with an adjusted basis of $45,000, subject to a mortgage of $100,000, in exchange for a partnership interest worth $250,000. Frank contributes cash of $100,000 and performs services for the partnership in exchange for a partnership interest worth $250,000.

a. What is the amount of Oscar's recognized gain or loss (if any) as a result of the contribution to the partnership in exchange for the partnership interest?
b. What is Oscar's basis in his partnership interest immediately after the contribution?
c. What is the amount of Frank's recognized income or loss (if any) as a result of the receipt of the partnership interest in exchange for the cash and services?
d. What is the partnership's basis in the land received from Oscar?

65. Jennifer has a 25 percent interest in the Aspen Aircraft partnership. Her basis in her partnership interest is $10,000 at the beginning of 2013. The partnership reported the following activity for 2013:

Ordinary income	$40,000
Section 1231 gain	$10,000
Charitable contribution	$12,000
Total distributions to partners	$20,000

What is Jennifer's basis in her partnership interest at the end of 2013?

66. J. Bean and D. Counter formed a partnership. During the current year, the partnership had the following income and expenses:

Gross income from operations	$135,000
Gain on sale of antique abacus (a business asset)	$ 5,000
Interest income from business bank account	$ 100

Deductions:

Salaries to employees	$ 65,000
Payroll taxes	$ 5,000
Rent	$ 7,000
Depreciation	$ 3,500
Contribution to United Way charity	$ 2,000
Foreign tax paid on overseas business deals	$ 3,000

Distributions to the partners $ 40,000

a. Calculate the net ordinary income.
b. List all of the other items that need to be separately reported.
c. If the partnership is on a calendar year tax basis, when is the partnership tax return due?

67. Please answer the following questions:

a. What form is used to report income and expenses from a partnership?
b. If a partner's basis at the beginning of the year is $1,000 and the partnership allocates $7,000 of loss to the partner: how much of the loss is deductible in the current year; what is his new basis in the partnership; and what happens to any excess loss not deducted?
c. What is the exemption amount for a partnership?

68. Lucky's original contribution to the Boxwood Partnership was land with a basis of $5,000 and a market value of $55,000. Her share of the taxable income from the partnership since her original contribution has been $95,000 and Lucky has received $50,000 in cash distributions from the partnership. Lucky did not recognize any gains as a result of the distributions. Calculate Lucky's current basis in her partnership interest.

69. Cypress Road is a partnership with two partners, Saul, a 60 percent partner, and Robbie, a 40 percent partner. The partnership has income for the year of $100,000 before guaranteed payments to Robbie. Guaranteed payments of $50,000 are paid to Robbie for his management services during the year. Calculate the amount of income that should be reported by Saul and Robbie from the partnership for the year.

Saul should report income of $__________.
Robbie should report income of $__________.

70. Lilac Designs is a partnership with a tax year that ends November 30, 2013. During that year, William, a partner, received $5,000 per month as a guaranteed payment and his share of partnership income after guaranteed payments was $20,000. For December of 2013, William received a guaranteed payment of $10,000. Calculate the amount of income from the partnership that William should report for his tax year ended December 31, 2013.

71. Jerry receives cash of $15,000 and a building with a fair market value of $50,000 (adjusted basis of $30,000) in a current distribution.

a. Assuming his basis in his partnership interest was $50,000, what amount of gain must Jerry recognize as a result of the current distribution?
b. Assuming his basis in his partnership interest was $10,000, what amount of gain must Jerry recognize as a result of the current distribution?

72. Debbie and Betty operate the D & B partnership. Betty, a 50 percent partner, receives a guaranteed payment of $10,000 for her services in operating the partnership. The partnership has income before the guaranteed payment of $5,000. What is the taxable income Debbie and Betty must each report from the partnership for the year?

Debbie should report income of $__________.
Betty should report income of $__________.

73. In December of 2013, Miss Havisham and Pip form a wedding planning business. Each of them own 50 percent of the partnership. The partnership establishes a September 30th year-end since most weddings are during the summer. Therefore, the partnership year-end is September 30, 2014. For the month of December 2013, the partnership made $3,000 after Miss Havisham's guaranteed payment of $1,000. From January through September of 2014, the partnership made a net income of $65,000 after a $1,500 per month guaranteed payment to Miss Havisham.

   a. How much income should Miss Havisham report for 2013?
   b. How much income should Miss Havisham report for 2014?

74. Assuming that a partnership normally has a calendar year-end, what should the tax year-end be in the following independent cases?

   a. Jim, a 70 percent partner, sells his partnership interest to Fred on August 10th.
   b. On July 13th, the partnership sells its office building and moves its business across town.
   c. June buys a 15 percent interest in the partnership on May 14th.
   d. The partnership goes out of business on February 26th.

75. Rochelle owns 40 percent of a partnership and her brother owns the remaining 60 percent interest. During the current tax year, Rochelle sold a building to the partnership for $180,000, to be used for the partnership's office. She had held the building for 3 years at the time of the sale.

a. Assuming Rochelle's basis in the building was $200,000, what is the amount and nature of her gain or loss?
b. Assuming Rochelle's basis in the building was $150,000, what is the amount and nature of her gain or loss?

76. Mario and Luigi are brothers and they are equal partners in Pipes of Your Dreams Plumbing. Mario sells his fancy sports car to the business for $40,000. Mario's basis in the car is $45,000.

a. What is the amount of Mario's recognized gain or loss on this transaction, and what is the nature of the gain or loss?
b. If the partnership later sells the sports car for $55,000, how much of the gain is recognized?

77. During 2013, Jay is a partner in an automobile dealership. Jay's amount at risk at the beginning of the year is $90,000, and during 2013 Jay's share of the dealership's ordinary loss is $120,000.

a. What is the amount of the loss from the automobile dealership that Jay may deduct in 2013?
b. If the dealership has a profit of $63,000 in 2014, how much of the 2014 income is taxable to Jay?

78. Michael invests in Buxus Interests, a partnership. Michael's capital contribution to the partnership consists of $10,000 cash and equipment with an adjusted basis of $120,000 (fair market value of $150,000) subject to a nonrecourse liability of $60,000.

a. Calculate the amount that Michael is at-risk in the activity after making the above contribution?
b. If Michael's share of the partnership loss in the year after he makes the contribution is $150,000, how much of the loss may be deducted in that year (before considering the limitations on passive losses)? Assume the partnership had no other transactions.
c. If Michael has any nondeductible loss in part b, what may Michael do with the nondeductible loss?

79. List three advantages of an LLC.

80. A partner contributes assets with a basis of $50,000 and a fair market value of $80,000 to a partnership. What is the basis of the property to the partnership and what is the general rule for the basis of appreciated property contributed to a partnership?

81. A distribution of cash to a partner was greater than his basis in the partnership. How would this distribution be treated by the partner, assuming the distribution is not a liquidating distribution?

Chapter 10: Partnership Taxation Key

1. TRUE

2. FALSE

3. FALSE

4. TRUE

5. TRUE

6. FALSE

7. FALSE

8. FALSE

9. FALSE

10. FALSE

11. TRUE

12. FALSE

13. FALSE

14. TRUE

15. FALSE

16. TRUE

17. FALSE

18. TRUE

19. TRUE

20. FALSE

21. FALSE

22. TRUE

23. TRUE

24. FALSE

25. TRUE

26. TRUE

27. D

28. B

29. A

30. A

31. A

32. A

33. D

34. B

35. A

36. C

37. B

38. B

39. D

40. D

41. A

42. A

43. A

44. D

45. A

46. B

47. D

48. B

49. D

50. C

51. A

52. B

53. C

54. D

55. C

56. C

57. C

58. A

59. D

60. D

61. a. **Yes**
b. **No**
c. **No**
d. **Yes**
e. **Yes**

62. a. **Yes.**
b. **$0.** There is no tax at the partnership level. The partnership income and other items are passed through to the partners and taxed at the individual level.
c. **Yes.** An LLP is still generally treated as a partnership for tax law purposes.

63.
a. **$0**.
b. **$35,000**, the same as the basis of the property contributed to the partnership.
c. **$20,000**, since services do not qualify as property.
d. **$20,000**, the income recognized.
e. **$35,000**, the same as the partner's basis in the property contributed.

64.
a. **$5,000 gain** = ($100,000 ´ 50%) - $45,000.
b. **$0** = $45,000, basis of the property contributed, + $5,000, gain recognized, - $50,000, liability assumed by the other partner through the partnership.
c. **$150,000**, since services do not qualify as property.
d. **$50,000** = $45,000 + $5,000.

65. **$14,500** = $10,000 + 25% ´ ($40,000 + $10,000 - $12,000 - $20,000)

66. a. Ordinary income:

Gross income from operations		$135,000
Less:		
Salaries to employees	65,000	
Payroll taxes	5,000	
Rent	7,000	
Depreciation	3,500	
Net ordinary income	$ 54,500	

b. Items that need to be separately reported:

Gain on sale of antique abacus	$ 5,000
Interest income	$ 100
Contribution to United Way charity	$ 2,000
Foreign tax paid	$ 3,000
Distributions to the partners	$ 40,000

c. It is due on April 15 of the year following the end of the tax year.

67. a. Partnership income and expenses are reported on Form 1065.
b. The partner may deduct $1,000 of the loss; the partner's new basis is zero; and the excess loss of $6,000 is carried forward to future years when there is partnership basis available to be deduct the loss.
c. There are no exemption amounts for partnerships.

68. **$50,000** = $5,000 + $95,000 - $50,000

69. **Saul: $30,000** = 60% ´ ($100,000 - $50,000)
Robbie: $70,000 = $50,000 + 40% ´ ($100,000 - $50,000)

70. **$80,000** = $20,000 + (12 ´ $5,000)

71.
a. **$0**. He still has a $5,000 basis in his partnership interest.
b. **$5,000** = $15,000 cash - $10,000 basis

72. **Debbie: $2,500 loss** = 50% ´ ($5,000 - $10,000)
Betty: $7,500 income = $10,000 + 50% ´ ($5,000 - $10,000)

73.
a. Since the partnership's year-end is September 30, 2014, Miss Havisham does not report any income in 2013.
b. In 2014, Miss Havisham reports a total income of $48,500, calculated as
50% x ($3,000 + $65,000) + $1,000 + $1,500 x 9 months.

74. a. The partnership's tax year-end is August 10th and then December 31st.
b. The partnership's tax year-end is December 31st.
c. The partnership's tax year-end is December 31st.
d. The partnership's tax year-end is February 26th.

75.

a. **$0.** The potential $20,000 loss is disallowed as a related-party transaction.

b. **$30,000 gain.** It is an ordinary gain since the building is a Section 1231 asset, not a capital asset, to the partnership.

76. a. **$0.** The $5,000 loss is disallowed since Mario is deemed to own more than 50 percent of the partnership.

b. **$10,000.** The partnership can use Mario's $5,000 loss which was disallowed to offset the $15,000 gain.

77.

a. **$90,000**, the at-risk amount.

b. **$33,000** = $63,000 - $30,000.

78.

a. **$70,000** = $10,000 + $120,000 - $60,000.

b. **$70,000**, the at-risk amount.

c. The loss may be carried forward by the partner for an indefinite period, subject to similar limitations in the carryover years.

79. A student may list any of the following as advantages of an LLC:

1. An LLC for tax purposes is generally treated like a partnership. Taxable income and losses pass through to the owners, thereby avoiding double taxation.
2. There is no general partnership requirement as in a limited partnership. All partners therefore have limited liability.
3. An LLC is not subject to the security laws.
4. All members in an LLC may participate in management.
5. There is no limit on the number or kind of owners who may have an interest in an LLC.
6. Tax attributes of an LLC transaction pass through to the owners.
7. There can be a single member LLC.

80. The basis to the partnership is $50,000, the same as the basis to the partner who contributed the property. The contribution is not a taxable event, i.e., the contributing partner does not recognize a gain on the contribution. The partnership generally has a basis in appreciated property equal to the contributing partner's basis. If the partner is required to recognize gain on the contribution due to a liability in excess of basis, the partner's gain is added to the partnership's basis in the asset.

81. The portion equal to the partner's basis is return of investment and is not taxable. The excess would be treated as a gain, subject to taxation. The partner's basis in its partnership interest would be reduced to zero.

Chapter 11: The Corporate Income Tax

Student: ____

1. Corporations pay a flat 30 percent federal income tax.

   True False

2. The corporate tax rates favor large corporations.

   True False

3. Corporations are granted favorable tax treatment for short-term capital losses.

   True False

4. A corporation may carry forward capital losses for an indefinite period.

   True False

5. Capital losses of a corporation must be used to offset capital gains and net capital losses may not be deducted from the ordinary income of a corporation.

   True False

6. If a corporation is unable to deduct a capital loss against capital gains for a particular tax year, it loses the tax benefit since the loss may not be carried to other tax years.

   True False

7. Corporations may deduct without limitation any amount of charitable contributions providing the amounts are paid to qualified organizations.

   True False

8. Corporations are *not* allowed to amortize the costs of organizing the corporation.

   True False

9. A corporation may elect to take a credit for dividends paid in lieu of claiming a dividends received deduction.

   True False

10. A corporation owning 80 percent or more of the stock of another corporation has a dividends received deduction of 100 percent.

True False

11. Brokers' fees incurred in the issuance of a corporation's stock are considered organizational expenditures.

True False

12. To prevent triple taxation, a corporation is entitled to deduct 50 percent of the dividends received from other domestic corporations.

True False

13. A regular corporation with excess charitable contributions may carry the excess forward to the 5 succeeding tax years.

True False

14. Corporations can elect to deduct up to $5,000 of organizational costs in the year they begin business, assuming their total organizational expenses do not exceed $50,000.

True False

15. A corporation must reconcile, to the IRS's satisfaction, the differences between net income as shown on the company's books and taxable income (before special deductions and net operating losses) as shown on the tax return.

True False

16. Schedule M-1 on Form 1120 shows the reconciliation of a corporation's tax liability to the tax expense on the corporation's books.

True False

17. An S corporation files a Form 1120S.

True False

18. If the shareholders of an S corporation voluntarily revoke the corporation's S corporation status in the sixth month of the tax year and the revocation does not specify a prospective revocation date, the corporation is a regular corporation for that tax year.

True False

19. The income of an S corporation is computed in much the same manner as that of a partnership.

True False

20. Charitable contributions made by an S corporation are not deductible by the corporation; therefore, the shareholders receive no tax benefit from the contributions.

    True False

21. S corporations pay taxes at a higher rate than do regular corporations.

    True False

22. If a corporation's status as an S corporation is involuntarily terminated in the middle of the tax year, the corporation must file as an S corporation for the first half of the tax year and a regular corporation for the second half of the tax year.

    True False

23. As a general rule, the transfer of property to a corporation in exchange for stock does not result in a taxable transaction.

    True False

24. The accumulated earnings tax will *not* be imposed on accumulations that can be shown to be necessary to meet the reasonable needs of the business.

    True False

25. The accumulated earnings tax is designed to prevent shareholders from avoiding the individual income tax.

    True False

26. A corporation may be found subject to both the accumulated earnings tax and the personal holding company tax in the same year.

    True False

27. The original due date for a tax return of a corporation with a calendar tax year-end falls before the original due date of a return for an individual taxpayer with the same tax year.

    True False

28. The corporate alternative minimum tax rate is 28 percent.

    True False

29. Corporations may be subject to the alternative minimum tax.

    True False

30. For 2013, what is the maximum tax rate for personal service corporations?

    A. 25 percent
    B. 28 percent
    C. 34 percent
    D. 35 percent
    E. None of the above

31. Which of the following companies is taxed at a flat rate of 35 percent?

    A. An auto parts manufacturing corporation with taxable income of $73,000.
    B. A consulting corporation of owner-employee CPAs with taxable income of $1,000,000.
    C. A family-owned shoe store with earnings of $224,000 in 2013.
    D. All of the above are taxed at a flat rate of 35 percent.

32. In 2013, Apricot Corporation had taxable income of $120,000. Included in taxable income was a $10,000 capital gain. The $120,000 of taxable income does not include a $15,000 capital loss carryforward available from the previous year. What is Apricot Corporation's 2013 income tax liability before any tax credits?

    A. $24,200
    B. $26,150
    C. $28,550
    D. $30,050
    E. None of the above

33. Which of the following statements is true of corporations?

    A. Income of all corporations is taxed in the same way that income of partnerships is taxed.
    B. A corporation's charitable contribution deduction is limited to 25 percent of the corporation's taxable income.
    C. Capital losses of a corporation may be deducted from ordinary income, subject to an annual limitation.
    D. If a corporation has a long-term capital loss that is carried back, it is treated as a short-term capital loss.
    E. A corporation may deduct organizational expenditures as they are incurred.

34. Which of the following is true with respect to capital gains and losses of a corporation?

    A. A corporation can offset ordinary income with capital losses.
    B. A corporation pays 15 percent long-term capital gains rate, just like an individual.
    C. A corporation can carry a capital loss back 5 years.
    D. A corporation can carry a capital loss forward 5 years.

35. For 2013, the Beech Corporation has net income on its books of $60,000, including the following items:

Net capital losses	$10,000
Federal income tax expense	$25,000

Federal tax depreciation exceeds the depreciation deducted on the books by $5,000. What is the corporation's taxable income?

A. $70,000
B. $85,000
C. $90,000
D. $100,000
E. None of the above

36. The Nandina Corporation was formed and began operations on July 1, 2013, and incurred the following expenses during the year:

State fees for incorporation	$ 800
Legal and accounting fees incident to organization	$1,500
Legal fees for the issuance of stock	$ 600
Temporary directors' fees	$1,000

If the corporation chooses not to expense but rather amortizes organizational costs over 180 months, what is the amount of its amortization expense for 2013?

A. $0
B. $110
C. $130
D. $220
E. None of the above

37. ABC Company owns 40 percent of JMT Company and 95 percent of DEM Company. JMT pays a $100,000 dividend to ABC and DEM pays a $40,000 dividend to ABC in 2013. Assuming that ABC has $1,000,000 of taxable income, calculate ABC's dividends received deduction for 2013.

A. $120,000
B. $132,000
C. $140,000
D. $112,000
E. None of the above is correct

38. The F. Repens Corporation has taxable income of $250,000 for 2013, including dividends of $50,000 received from 30 percent-owned domestic corporations. How much is the F. Repens Corporation's dividends received deduction for 2013?

A. $0
B. $40,000
C. $50,000
D. $170,000
E. None of the above

39. The Bay Fig Corporation has $350,000 of taxable income from operations for 2013, and dividends of $100,000 received from 30 percent-owned domestic corporations. How much is the Bay Fig Corporation's dividends received deduction for 2013?

A. $35,000
B. $40,000
C. $70,000
D. $80,000
E. None of the above

40. In 2013, Parvifolia, Inc. had $400,000 of revenue from operations and $160,000 of dividends from non-affiliated 15 percent-owned domestic corporations. The corporation's deductible operating expenses totaled $410,000. What is Parvifolia, Inc.'s dividends received deduction for 2013?

A. $105,000
B. $112,000
C. $120,000
D. $128,000
E. None of the above

41. Ficus, Inc. began business on April 1, 2013, and elected to file its income tax return on a calendar-year basis. The corporation incurred $600 in organizational expenditures. Assuming the corporation does not elect to expense but chooses to amortize the costs over 180 months, the maximum allowable deduction for amortization of organizational expenditures in 2013 is:

A. $20
B. $21.67
C. $30
D. $40
E. None of the above

42. For the year ended December 31, 2013, Prunus, Inc., reported net income before federal income tax expense of $900,000 per the corporation's books. This figure included the following items:

Interest income on tax-exempt municipal securities	$30,000
Loss on sale of land acquired in 1985 as an investment	$40,000
Interest expense on loan to purchase tax-exempt municipal securities	$16,000

What is the taxable income of Prunus, Inc. for 2013?

A. $886,000
B. $900,000
C. $918,000
D. $926,000
E. None of the above

43. Which of the following items is *not* generally a schedule M-1 adjustment?

A. Net capital losses
B. Interest on tax-exempt bonds
C. Federal income tax expense
D. Interest expense on a loan to purchase municipal bonds
E. All of the above are M-1 adjustments

44. In general, estimated payments for calendar-year corporations are due on:

A. March 15, June 15, September 15, and December 15.
B. March 15, June 15, September 15, and January 15 of the following year.
C. April 15, June 15, September 15, and December 15.
D. April 15, June 15, September 15, and January 15 of the following year.

45. Which of the following is *false* in regards to filing requirements?

A. Corporations file their tax returns on Form 1120.
B. An automatic 6-month extension can be obtained by a corporation by filing Form 7004.
C. Filing Form 7004 provides a 6-month extension for paying the corporation's tax due. A corporation can wait to pay its tax liability without penalty when the return is filed.
D. None of the above is false.

46. For its year ended December 31, 2013, Cupressa Corporation, an S corporation, had net income of \$216,000 which included \$180,000 of ordinary income from operations and a \$36,000 net long-term capital gain. During 2013, a total of \$90,000 was distributed to the corporation's nine equal shareholders, all of whom are on a calendar-year tax basis. For 2013, each shareholder should report:

A. \$10,000 ordinary income
B. \$20,000 ordinary income
C. \$20,000 ordinary income and \$4,000 net long-term capital gain
D. \$24,000 ordinary income
E. None of the above

47. Which of the following corporations is allowed to make an S corporation election?

A. A small U.S. owned and operated company with two individual owners.
B. A U.S. corporation owned by a Brazilian corporation.
C. A U.S. owned and operated corporation with 7,000 separate shareholders.
D. None of the above could be an S corporation.

48. Which of the following statements is *not* true of S corporations?

A. S corporations are corporations that receive tax treatment similar to that given partnerships.
B. Section 1231 gains and losses pass through separately to stockholders of an S corporation.
C. The amount of losses that a shareholder of an S corporation may report on his or her tax return is limited to the basis of the stock plus any loans made by the shareholder to the corporation.
D. If a taxpayer purchases stock in an S corporation from another shareholder during the year, the new shareholder may report the entire amount of any loss for the year attributable to the shares purchased.
E. If a shareholder acquires 40 percent of the stock of an S corporation, the new shareholder cannot cause the corporation to lose its S corporation election.

49. Which of the following is *not* a requirement for qualification as an S corporation?

A. The corporation must be a domestic corporation.
B. The corporation must have 25 or fewer shareholders.
C. The corporation must have only one class of stock outstanding.
D. The shareholders of the corporation must not be nonresident aliens.
E. None of the above.

50. Rob, Bill, and Steve form Big Company. Rob performs $45,000 of services for his shares of the company. Bill transferred property with a basis of $5,000 for $75,000 of stock. Steve contributes cash of $100,000 for his shares. Which of the three must recognize income in the year of the formation?

A. Rob
B. Rob, Bill, Steve
C. Bill
D. Steve, Bill
E. Steve, Rob

51. On July 1, 2013, Grey formed Arucaria Corporation. On that same date, Grey contributed $100,000 cash and transferred property with an adjusted basis of $50,000 to Arucaria in exchange for 3,000 shares of the corporation's common stock. The property transferred had a fair market value of $85,000 on the date of the transfer. Arucaria Corporation had no other shares of common stock outstanding on July 1, 2013. As a result of this transaction, Grey's basis in the stock and Arucaria Corporation's basis in the property (other than the cash), respectively, are:

A. $150,000 and $50,000
B. $150,000 and $85,000
C. $185,000 and $50,000
D. $185,000 and $85,000
E. None of the above

52. Terry forms the Camphor Corporation during 2013. She transfers property with a value of $700,000 to Camphor Corporation in exchange for 100 percent of the stock in the corporation. Terry's basis in the property transferred was $350,000 and the corporation assumed a $250,000 mortgage on the property. If the fair market value of the stock received by Terry is $450,000, what is the corporation's basis in the property received from Terry?

A. $100,000
B. $250,000
C. $350,000
D. $450,000
E. $700,000

53. Roberta and Sally formed the Alder Corporation on October 1, 2013. On the same date, Roberta paid $75,000 cash to Alder Corporation for 750 shares of the corporation's common stock. Simultaneously, Sally received 100 shares of Alder Corporation's stock for services rendered. How much should Sally include in her taxable income for 2013, and what will be the basis of her Alder Corporation stock?

Taxable Income	Basis of Stock
A. $0	$0
B. $0	$10,000
C. $10,000	$0
D. $10,000	$10,000
E. None of the above	

54. On July 1, 2013, Robert forms the Yew Corporation. In exchange for 100 percent of the corporation's stock, Robert contributes land with a fair market value of $100,000. Robert acquired the land 5 years ago at a cost of $30,000. At the date of the contribution, the land is subject to a $10,000 mortgage which the corporation assumes. What is the basis of the land to Yew Corporation?

A. $20,000
B. $30,000
C. $90,000
D. $100,000
E. None of the above

55. Harry forms the Nectarine Corporation during the 2013 tax year. To form the corporation, Harry transfers assets having a fair market value of $650,000 to Nectarine Corporation for 100 percent of the corporation's stock. Harry's adjusted basis in the assets transferred was $350,000 and Nectarine Corporation assumed a $200,000 mortgage on the assets. If the fair market value of the stock received by Harry is $450,000, what is his basis in the stock received from the corporation?

A. $150,000
B. $200,000
C. $350,000
D. $450,000
E. None of the above

56. The Sapote Corporation is a manufacturing corporation. The corporation has accumulated earnings of $450,000 and the corporation cannot establish a reasonable business need for any of that amount. What is the amount of the accumulated earnings tax, if any, that will be imposed on the corporation?

A. $45,000
B. $30,000
C. $50,000
D. $76,000
E. None of the above

57. What is the maximum amount of accumulated earnings that a corporation is allowed to accumulate, without regard to business needs, before the accumulated earnings tax is imposed?

A. $150,000 for all corporations
B. $150,000 for nonservice corporations only
C. $250,000 for all corporations
D. $250,000 for nonservice corporations only
E. None of the above

58. The accumulated earnings tax, which is imposed on corporations for the accumulation of earnings in excess of reasonable business needs, does not apply to:

A. Closely-held corporations.
B. Widely-held corporations.
C. Corporations subject to the personal holding company tax.
D. Both b. and c.
E. All of the above.

59. Which of the following is *not* an adjustment or tax preference item for the corporate alternative minimum tax?

A. Certain tax-exempt bond intererest
B. Organization cost amortization
C. Accelerated depreciation on personal property
D. Percentage depletion in excess of the property's adjusted basis

60. Choose the correct statement:

A. The corporate alternative minimum tax applies to all corporations including S corporations.
B. The exemption amount is phased out at a rate of $1.00 for every $1.00 by which the corporation's alternative minimum taxable base exceeds $210,000.
C. The alternative minimum tax is imposed at 26 percent on the alternative minimum tax base up to $150,000 and 28 percent on the AMT base that is greater than $150,000.
D. The alternative minimum tax base is equal to the corporation's regular taxable income increased or decreased for certain adjustments, increased by tax preference items, and decreased by the exemption amount.

61. For the year ended June 30, 2013, the Rosaceae Corporation, a regular C corporation, has a long-term capital loss of $25,000.

a. Assuming that in addition to the capital loss, the corporation has taxable income, before capital gains and losses, of $20,000 for 2013, calculate the corporation's tax liability before any credits.
b. Assuming that in addition to the long-term capital loss of $25,000 the corporation has taxable income, before capital gains and losses, of $100,000 and a short-term capital gain of $10,000 for 2013, calculate the corporation's tax liability before any credits.

62. During 2013, the Squamata Corporation, a regular C corporation, has $25,000 in ordinary income, a long-term capital loss of $20,000, and a short-term capital gain of $10,000.

a. Calculate the Squamata Corporation's tax liability for 2013.
b. Explain the nature and amount of any carrybacks or carryforwards that the corporation is entitled to use.

63. Calculate the corporate tax liability in each of the following circumstances:

a. X Corporation has taxable income of $250,000 for its 2013 calendar tax year.
b. Y Corporation has $1,500,000 in taxable income for 2013.
c. Z Corporation has taxable income of $100,000, before capital gains and losses, a short-term capital loss of $30,000, and a long-term capital gain of $10,000 in 2013.

64. During 2013, the Melaleuca Corporation received dividends from 50-percent-owned domestic corporations in the amount of $100,000.

a. Assuming that in addition to the dividend income the corporation has gross income from operations of $250,000 and deductible operating expenses of $210,000, calculate the amount of the corporation's dividends received deduction for 2013.
b. If, instead of $250,000 in gross income from operations, the corporation has $200,000 in gross income from operations and the same amount of dividends and expenses, calculate the amount of the corporation's dividends received deduction for 2013.

65. The Lagerstroemia Corporation was formed on January 1, 2013. Calculate the Lagerstroemia Corporation's taxable income or loss for 2013 given the following information:

Gross receipts	$250,000
Cost of goods sold	$150,000
Dividend income (from 10 percent-owned domestic corporation)	$ 35,000
Interest income	$ 15,000
Business expenses (other than organizational costs and charitable contributions)	$125,000
Charitable contributions	$ 5,000
Organizational costs expensed	$ 5,000
Taxable income/(loss)	$______

66. The Peach Corporation is a regular corporation that contributes $25,000 cash to qualified charitable organizations during 2013. The corporation has net taxable income of $200,000 before deducting the contributions.

a. What is the amount of Peach Corporation's allowable deduction for charitable contributions for the current year?
b. What may the corporation do with any excess amount of contributions?

67. The Guava Corporation has book net income of $90,000 for 2013. Included in this figure are the following items which are reported on the corporation's Schedule M-1, Reconciliation of Income (Loss) per Books with Income per Return.

1.	Federal income tax expense	$22,000
2.	Depreciation deducted on books, not deductible for tax purposes	$ 5,000
3.	Deduction for 50 percent of meals and entertainment expense not allowed for tax purposes	$ 3,000
4.	Deduction for payroll tax penalties not allowed for tax purposes	$ 2,000
5.	Tax exempt interest income included in book income but not in tax return income	$10,000

Based on the above information, calculate the Guava Corporation's taxable income for the year. Show your calculations.

68. The Cat Corporation had $20,000 of book income in the current year. The following is a list of differences between federal and book income and expenses:

Federal income tax expense deducted for books	$ 4,400
Depreciation deducted on books	$ 3,000
Depreciation deducted on tax return	$14,000
50 percent of meals expense not allowed as an expense for taxes	$ 2,000
Charitable contributions carried over from prior years and deducted on the current year tax return	$ 2,300
Current year taxable gain on an installment sale which was reported on the books in a previous year	$ 5,000
Prepaid interest not deductible in the current year for tax purposes but claimed as a deduction for book income purposes	$10,000
Nondeductible club dues	$ 1,000

Based on the above information, calculate the Cat Corporation's federal taxable income for the year. Show your calculations.

69. Avocado Corporation paid $3,000 in estimated tax payments for the calendar year ended December 31, 2013. The corporation has an actual tax liability of $4,000 for the year.

a. If no extension is requested, when is the tax return due?
b. If an extension of time to file is requested and approved, when is the tax return due?
c. If an extension of time to file is requested and approved, when is the additional $1,000 of the 2013 tax due?

70. XYZ Corporation has a December 31 year-end.

    a. When is XYZ Corporation's tax return due?
    b. When does XYZ Corporation need to make its estimated tax payments?
    c. Assuming that XYZ Corporation owes $5,000 on the original tax return due date and it files for an extension and is granted an automatic extension to file tax returns, what is the extended tax return date and when should taxes be paid?

71. During the current year, The Jupiter Company, which is an S corporation, had the following items of income and expenses:

Gross income from operations	$135,000
Gain on sale of business assets	$ 5,000
Qualified dividend income from investments	$ 100
Deductions:	
Salaries to employees	$ 65,000
Payroll taxes	$ 5,000
Rent	$ 7,000
Depreciation	$ 3,500
Contributions to United Way charity	$ 2,000
Foreign tax paid on overseas business deals	$ 3,000
Distributions to the shareholders	$ 40,000

    a. Calculate the net ordinary income.
    b. List all the other items which must be separately reported.
    c. If the S corporation is on a calendar year, when is the corporation's tax return due?

72. Rex and Marsha each own 50 percent of the Grandiflora Corporation, an S corporation with a calendar tax year. At the beginning of the tax year, Marsha and Rex both have a basis in the stock of the corporation of $25,000. On June 30, 2013, Rex sells his interest in the corporation to George for $200,000, and for 2013 the Grandiflora Corporation has a loss of $90,000.

a. Calculate the amount of the corporation's loss that may be deducted by Rex on his 2013 tax return.
b. Calculate the amount of the corporation's loss that may be deducted by George on his 2013 tax return.
c. Calculate the amount of the corporation's loss that may be deducted by Marsha on her 2013 tax return.

73. Fran, George, and Helen form FGH Corporation. In exchange for 300 shares of stock of the corporation, Fran contributes property with a basis of $15,000, fair market value of $50,000 and subject to a liability of $20,000 which the corporation assumed. George contributes property with a basis of $20,000, fair market value of $30,000 in exchange for 250 shares of stock of the corporation with a value of $25,000 plus $5,000 cash. Helen performs services for the corporation and receives $2,000 worth of stock (20 shares) in exchange for the services.

a. What is the amount of Fran's recognized gain or loss on the transaction?
b. What is Fran's basis in the stock of the corporation?
c. What is the corporation's basis in the property received from Fran?
d. What is the amount of George's recognized gain or loss on the transaction?
e. What is George's basis in the stock of the corporation?

74. Robert, Kim, Tony, and Sharon decided to form the Cash Cow Corporation. In exchange for 40 percent of the stock, Robert contributed an apartment building with a fair market value of $700,000 and subject to a liability of $300,000. Robert's basis in the apartment building is $225,000. Kim contributed warehouse storage units worth $450,000 in exchange for 40 percent of the stock plus $50,000 in cash from the corporation. Her basis in the warehouse is $125,000. Tony contributed $100,000 cash for 10 percent of the stock. Sharon is performing services worth $100,000 for 10 percent of the stock.

    a. What is the recognized gain or recognized income for:
        1. Robert
        2. Kim
        3. Tony
        4. Sharon
    b. What is the basis in the stock for:
        1. Robert
        2. Kim
        3. Tony
        4. Sharon
    c. What is the corporation's basis in:
        1. The apartment building
        2. The warehouse

75. The Heal Yourself Health Care Corporation, a service corporation, has accumulated earnings of $375,000 and the corporation can establish a reasonable need for $125,000. Calculate the amount of the accumulated earnings tax, if any, that will be imposed on the corporation.

76. The Great Gumball Corporation is a gumball producer. The corporation has accumulated earnings of $425,000 and it can establish a reasonable need for $360,000. Calculate the amount of the accumulated earnings tax, if any, that will be imposed on the corporation.

77. The Birch Corporation has regular taxable income of $85,000 and a regular tax liability of $17,150. The corporation also has $45,000 of tax preference items. Calculate Birch Corporation's alternative minimum tax liability. Assume that the Birch Corporation is not a "small corporation."

78. Ashwood Corporation has been in business for 20 years. For the previous 3 years, Ashwood Corporation had annual gross receipts of $3.3 million, $4.2 million and $5.4 million, respectively. For alternative minimum tax purposes, is Ashwood Corporation a small corporation? Give your reasoning and/or the calculation that you based your answer on. Also, why does it matter if they are a small corporation?

79. Is it correct to state that the maximum corporate tax rate is 35 percent? Please describe the structure of the corporate tax rate schedule in your answer.

80. What is the purpose of Schedule M-1?

Chapter 11: The Corporate Income Tax Key

1. FALSE
2. FALSE
3. FALSE
4. FALSE
5. TRUE
6. FALSE
7. FALSE
8. FALSE
9. FALSE
10. TRUE
11. FALSE
12. FALSE
13. TRUE
14. TRUE
15. TRUE
16. FALSE
17. TRUE
18. FALSE
19. TRUE
20. FALSE
21. FALSE
22. TRUE
23. TRUE
24. TRUE
25. TRUE
26. FALSE
27. TRUE
28. FALSE
29. TRUE
30. D

31. B

32. B

33. D

34. D

35. C

36. B

37. A

38. B

39. D

40. A

41. C

42. D

43. E

44. C

45. C

46. C

47. A

48. D

49. B

50. A

51. A

52. C

53. D

54. B

55. A

56. B

57. D

58. C

59. B

60. D

61.
a. **$3,000** = 15% ´ $20,000
b. **$22,250**, the tax on $100,000, taken from the table

62.
a. **$3,750** = 15% ´ $25,000.
b. **$10,000** long-term capital loss. It becomes a short-term capital loss and can be carried back 3 years and forward 5 years to offset capital gains in those years.

63.
a. **$80,750** = $22,250 + 39% ´ ($250,000 - $100,000)
b. **$510,000** = $113,900 + 34% ´ ($1,500,000 - $335,000)
c. **$22,250** on taxable income of $100,000

64.
a. **$80,000** = $100,000 ´ 80%
b. **$72,000** = Lessor of: 80% ´ ($200,000 - $210,000 + $100,000) or $100,000 x 80%

65.

Gross receipts	$ 250,000
Cost of goods sold	(150,000)
Gross profit	$ 100,000
Dividend income	35,000
Interest income	15,000
Total income	$ 150,000
Business expenses	$(125,000)
Organizational costs	(5,000)
Income before charitable contribution deduction	$ 20,000
Charitable contribution deduction (10% x $20,000)	(2,000)
Income before dividends received deduction	$ 18,000
Dividends received deduction (70% x $35,000 = $24,500)	(24,500)
Taxable income/(loss)	**$ (6,500)**

66.
a. **$20,000** = 10% ´ $200,000.
b. The excess may be **carried forward** to the 5 succeeding tax years, again subject to the 10 percent limitation.

67. **$112,000** = $90,000 + $22,000 + $5,000 + $3,000 + $2,000 - $10,000

68. **$29,100** = $20,000 + $4,400 + $3,000 - $14,000 + $2,000 - $2,300 + $5,000 + $10,000 + $1,000

69.
a. **March 15, 2014** (Note that when the filing date falls on a Saturday or a Sunday, the actual filing date is the next business day).
b. **September 15, 2014** (Note that when the filing date falls on a Saturday or a Sunday, the actual filing date is the next business day).
c. **March 15, 2014** (Note that when the filing date falls on a Saturday or a Sunday, the actual filing date is the next business day).

70. a. March 15 of the following year.
b April 15, June 15, September 15, and December 15
c. The extended tax due date is September 15 of the following year, but the taxes owed should be paid by March 15 after the year end.

71. a. Ordinary income:

Gross income from operations		$135,000
Less:		
Salaries	$(65,000)	
Payroll taxes	$ (5,000)	
Rent	$ (7,000)	
Depreciation	$ (3,500)	
Net ordinary income		$ 54,500

b. Items which need to be separately reported:

Gain on sale of business assets	$ 5,000
Dividend income	$ 100
Charitable contributions to United Way	$ 2,000
Foreign tax paid	$ 3,000
Distributions to the shareholders	$40,000

c. March 15 of the following year

72.

a. **$22,192** = $45,000 ´ 180 days/365 days. (Leap year: **$22,254** = $45,000 ´ 181/366)

b. **$22,808** = $45,000 ´ 185 days/365 days. (Leap year: **$22,746** = $45,000 ´ 185/366)

c. **$25,000**. Marsha's share of the corporation's loss is $45,000; however, her deductible loss is limited to her $25,000 basis in the corporation's stock.

73.

a. **$5,000** gain = $20,000 - $15,000

b. **$0** = $15,000 + $5,000 - $20,000

c. **$20,000** = $15,000 + $5,000

d. **$5,000**, boot received

e. **$20,000** = $20,000 - $5,000 + $5,000

74. a. The gain recognized is as follows:
   1. Robert's recognized gain is **$75,000** ($300,000 - $225,000).
   2. Kim's recognized gain is **$50,000** (the cash received as boot).
   3. Since Tony paid cash for his stock, he has **no recognized gain.**
   4. Since Sharon is performing services, she needs to recognize income of **$100,000**, the value of her stock.

b. The basis in the stock is as follows:
   1. Robert's stock basis is **$0** ($225,000 - $0 + $75,000 - $300,000).
   2. Kim's stock basis is **$125,000** ($125,000 - $50,000 + $50,000 - $0).
   3. Tony's stock basis is **$100,000** ($100,000 - $0 + $0 - $0).
   4. Sharon's stock basis is **$100,000**, the amount of her services.

c. The corporation's basis is as follows:
   1. Apartment building: **$300,000** ($225,000 + $75,000).
   2. Warehouse storage units: **$175,000** ($125,000 + $50,000).

75. **$33,750** = 15% x ($375,000 - $150,000)

76. **$9,750** = 15% x ($425,000 - $360,000)

77. **$850**, calculated as [20% x ($85,000 + $45,000 - $40,000)] - $17,150

78. Yes, since their average gross receipts for the previous 3 years is less than $7.5 million, they are considered a "small corporation." Since they are a small corporation, Ashwood Corporation is not subject to the corporate alternative minimum tax.

79. For income between $100,000 and $335,000 the effective rate is 39 percent, that is, 34 percent plus the 5 percent surcharge. For income between $15,000,000 and $18,333,333 the effective rate is 38 percent, that is, 35 percent plus the 3 percent surcharge. The higher effective rates within these dollar limits are sometimes referred to as the "bubble" rates.

The higher bubble rates represent a phaseout of the benefit of the lower corporate rates on lower amounts of corporate income. Although there are marginal rates higher than 35 percent on some corporate income, the effective tax rate on corporate income does not exceed 35 percent of the total income of a corporation.

80. Schedule M-1 is included in corporate tax returns and is used to reconcile corporate book income to taxable income. Schedule M-1 provides a summary of the items of income and expense which are treated differently for purposes of calculating book income and tax income.

CHAPTER 12

TAX ADMINISTRATION AND TAX PLANNING

Group 1 - Multiple Choice Questions

1. E (LO 12.1)
2. B (LO 12.2)
3. A (LO 12.2)
4. E (LO 12.3)
5. A (LO 12.4)
6. D (LO 12.4)
7. D (LO 12.5)
8. C (LO 12.5)
9. A (LO 12.5)
10. C (LO 12.5)
11. E (LO 12.5)
12. D (LO 12.5)
13. A (LO 12.6)
14. D (LO 12.6)
15. D (LO 12.6)
16. D (LO 12.6)
17. D (LO 12.6)
18. B (LO 12.6)
19. D ($10,875 – $8,375) / ($60,000 – $50,000) (LO 12.7)
20. B ($6,113 – $5,863) / ($41,000 – $40,000) (LO 12.7)
21. D ($2,000 – (30% x $1,800)) (LO 12.7)

Group 2 -Problems

1. **True.**(LO 12.1)
   False. See Figure 12.1 (LO 12.1)
   False. Most individual returns are processed at one of the IRS Campus Processing Sites. (LO 12.1)
   False. Taxpayers should contact other offices for tax information. (LO 12.1)
   False. The IRS may issue a summons for a taxpayer's records which are in the possession of third parties, such as CPAs. (LO 12.1)
   True. Taxpayer audits are also conducted at the office of the taxpayer or at the IRS office. (LO 12.2)

2. **False.** In a field audit, the IRS agent reviews a taxpayer's books and records at the taxpayer's place of business or at the office of the taxpayer's accountant. (LO 12.2)
   False. A low DIF score decreases the possibility that a return will be selected for audit. (LO 12.2)
   False. The IRS pays interest on overpayments of taxes, except for overpayments of current year taxes. (LO 12.3)
   True. (LO 12.3)
   True. (LO 12.3)
   False. The fraud penalty is only applied when a tax return has been filed. (LO 12.3)

3. a. **$7.00** = $700 x 0.5% x 2 months.
   b.

Failure to pay penalty	
(0.5% x $750 x 5 months)	$ 18.75
Failure to file penalty	
(5% x $750 x 5 months)	$187.50
Less the failure to pay penalty	(18.75)
Net failure to file penalty	168.75
Total penalties	**$187.50**

   c. **$0**. If the taxpayer is entitled to a refund, there is no penalty. (LO 12.3)

4. **$0**. None of the amounts are deductible since (1) the interest is considered consumer interest which is 100 percent disallowed, (2) federal income taxes are not deductible and (3) fines and penalties are not allowed as deductions. (LO 12.3)

5. a. Negligence penalty (20% x $4,000) = **$800**
   b. Fraud penalty (75% x $4,000) = **$3,000** (LO 12.3)

6. a. Filing a frivolous tax return; **$5,000**
   b. Bad check; **$25,** since the check is less than $1,250.
   c. Accuracy-related penalty, substantial understatement; **$2,000** = $10,000 x 20%. (LO 12.3)

7. **True.** (LO 12.3)
   False. The statute of limitations is normally 3 years from the date the tax return was filed or the date it was due, whichever is later. (LO 12.4)
   True. (LO 12.4)
   False. Enrolled agents are tax practitioners who have passed an exam. They are allowed to represent taxpayers in proceedings before the IRS. (LO 12.5)
   False. Only enrolled agents, CPAs, and attorneys may represent their clients in IRS proceedings. (LO 12.5)
   False. The IRS must schedule audits at a reasonable time and place. (LO 12.6)

8. a. **Never**
   b. **May 19, 2018**
   c. **April 15, 2018**
   d. **April 15, 2021** (LO 12.4)

9. a. **$1,000 or more** (the greater of $1,000 or 50 percent of the income derived by the tax preparer for
   an undisclosed unrealistic position)
   b. **$50**
   c. **$1,000**, for each separate return or document, etc.
   d. **$500** (LO 12.5)

10. **True.**
    True.
    False. The marginal tax rate represents the rate of tax that will be applied to the "next" dollar of income.
    True.
    True. (LO 12.7)

11. Information about the commissioner of the IRS will change from time to time, so it is not reproduced here. The purpose of this problem is to familiarize the students with some of the nontechnical information available from the IRS Internet site.

12. Information in the Tax Pro News and Events will change regularly so it is not reproduced here; it would not be current by the time students are assigned this problem.

Question 1

The statute of limitations for a tax return generally is 3 years.

Selected Answer: False

Question 2

If a taxpayer makes all of his income from his job and various investments, which office of the IRS would likely investigate his return if it were audited?

Selected Answer: a.
Wage & Investment Division (W&I)

Question 3

All paid tax return preparers must sign up with the IRS, pay a fee, and obtain a preparer tax identification number.

Selected Answer: True

Question 4

A "correspondence audit" by the IRS is conducted through the mail.

Selected Answer: True

Question 5

Which of the following is *not* a characteristic around which tax planning is organized:

Selected Answer: c.
Entity

Question 6

A tax return with a large casualty loss would be most likely selected for audit through:

Selected Answer: a.
The Discriminant Function System

Question 7

Mike deducts a bad debt on his 2014 tax return. How many years is the statute of limitations for the bad debt deduction?

Selected Answer: d.
7 years

Question 8

Tax return preparers must enter the annual filing season program (AFSP).

Selected Answer: True

Response Feedback: Rationale:
AFSP is voluntary.

Question 9

Taxpayers are required by law to maintain records to facilitate an IRS audit.

Selected Answer: True

Question 10

If a taxpayer has too much income tax withheld from his salary during the tax year, the IRS will pay interest on the excess amount.

Selected Answer: False

Response Feedback: Rationale:
A taxpayer is not paid interest on a refund arising from an overpayment of taxes during the current tax year.

Question 11

Patricia has taxable income of $40,000 on which she pays income tax of $5,856. If Patricia's taxable income increases by $2,000, she will pay an additional tax of $500. What is Patricia's marginal tax rate?

Selected Answer: d.
25.00 percent

Response Feedback: Rationale:
$500 / $2,000

Question 12

Which category of tax preparers may represent their clients in only the most limited situations in front of the IRS?

Selected Answer: c.
Enrolled Agents

Question 13

Tax returns selected for most audits are selected by the Discriminant Function System.

Selected Answer: True

Question 14

Which of the following is the most common type of audit for an individual taxpayer?

Selected Answer: a.
Office audit

Question 15

Which of the following is *false* regarding the return audit process?

Selected Answer: c.
50 percent of taxpayers are audited every year.

Question 16

Which of the following types of audits was suspended due to protests from taxpayers and lawmakers?

Selected Answer: b.
Taxpayer Compliance Measurement Program selected audit

Question 17

Tax penalties are *not* deductible by taxpayers.

Selected Answer: True

Question 18

Tax returns are processed at the IRS national office in Washington, D.C.

Selected Answer: False

Response Feedback: Rationale:
Tax returns are processed at the IRS Campus Processing Sites.

Question 19

The tax law contains a penalty for filing a "frivolous" tax return.

Selected Answer: True

Question 20

Which of the following is the *best* definition of tax planning?

Selected Answer: b.
Planning taxpayers' financial affairs in an effort to minimize tax liability