

Part 3

Section A:

Questions 1 – 20

The following statements are either true or false. Select the most appropriate answer and darken the box under A for true or under B for false.

- 1.** If a business entity formed before 1997 was taxed as a corporation, it will generally be taxed as a corporation for tax years after 1996?
- 2.** The Internal Revenue Service will grant a request for a six month extension of time to file a corporation's income tax return if the corporation properly completes, and files, Form 7004, Application for Automatic Extension of Time to File Corporation Income Tax Return, but does not pay any balance due by the due date of the return for which the extension applies.
- 3.** For a transfer of property to a corporation to qualify as a nontaxable exchange, it must be a transfer of property for stock and the transferors must be in control of the transferee corporation immediately after the transfer.
- 4.** J. Hancock, a furniture retailer, incorporates his sole proprietorship by transferring cash, accounts receivable, inventory, fixtures, transportation equipment and a building for 100% of the B shares (non voting) stock in the new corporation. At the same time, his new co-owner, T. Jefferson received 100% of the A shares (voting) stock in the corporation for his transfer of \$100,000. Each will have to report a taxable transaction.
- 5.** In 1999, Bill Jones, an attorney, provided all the legal services for the incorporation of MindTech, a newly formed corporation. In exchange for these services, Bill received a check for \$3,000 and stock of MindTech valued at \$ 10,000. With respect to the above transaction, attorney Bill Jones will have to report only ordinary income in 1999.
- 6.** The Crane Partnership and the Blair Partnership formed a corporation to do joint research for a new high tech product line. Crane contributed property and equipment worth \$60,000 in exchange for 60% of the common stock. Blair contributed cash, secret formulas and process knowledge worth \$40,000 for the remaining 40% of the common stock. Both must recognize gain on the transfer of property because only individuals are subject to the provisions of Section 351, nontaxable nontaxable transfer to controlled corporation.
- 7.** Generally, if a shareholder transfers a liability to a corporation along with the property, and the transferred liability exceeds the adjusted basis in the property transferred to the corporation, gain is recognized up the amount of the difference between the adjusted basis of the properties and the FMV of the liabilities assumed.
- 8.** The corporation's basis in the property received in a taxable exchange is the FMV of the property received, which may generally be measured by the adjusted basis of the property in the hands of the transferor, plus any gain recognized by the transferor.

- 9.** An S corporation's items of income, loss, deductions, etc., are allocated to the shareholder on an annual basis, according to the number of shares of stock held by the shareholder on the last day of the tax year of the S corporation.
- 10.** If an S corporation election is revoked by the consent of shareholders, the revocation may specify a revocation date that is on or after the date the revocation is filed.
- 11.** Funeral expenses of the decedent may be deducted on Form 1040, U. S. Individual Income Tax return, for the year of death.
- 12.** The executor of an estate must use the same tax year (calendar or fiscal), for filing a Form 1041, U.S. Income Tax Return for Estates and Trusts, as that used by the decedent on the decedent's most recently filed Form 1040.
- 13.** There is no provision for an extension of time to pay the tax liability associated with Form 706, United States Estate Tax Return.
- 14.** The gross estate includes only property which was owned and in the possession of the decedent at the time of death.
- 15.** The executor or personal administrator of an estate always has the option to use alternate valuation in determining the gross value of estate assets.
- 16.** The decedent, a sole proprietor, suffered an operating loss in his final year of business in 1999. After first carrying back the allowable amount, the executor may carry over any unused net operating loss to the estate's income tax return on Form 1041.
- 17.** A married couple may not file a joint gift tax return.
- 18.** Contributions made directly to and for the benefit of qualified political organizations may be used as a credit against any gift tax liability incurred in the same year as the contribution.
- 19.** Withholding of tax is required on a domestic corporation's cash distribution made on its stock in the ordinary course of business to foreign shareholders; even though it may be later determined that part or all of the distribution is a return of capital or gain from the sale or exchange of property.
- 20.** A trust must pay income tax on the beneficiary's distributive share of income.

Part 3

Section B

Questions 21-45

21. If a corporation's tax year ends December 31, it generally must file its income tax return:
- A. By June 15th of the following year.
 - B. By April 15th of the following year.
 - C. By March 15th of following year.
 - D. By October 15th of the following year.
22. Generally, if a new corporation is filing a short-period return with a tax year ending on July 31st, when must it file its income tax return:
- A. By October 15th.
 - B. By November 15th.
 - C. By December 15th.
 - D. January 31st of the following year.
23. David Shea transfers real estate with a basis of \$ 40,000 and a FMV of \$90,000 to a controlled corporation in return for stock in the corporation. Just before the transfer, David obtains a loan secured by the real estate and uses the \$ 10,000 loan proceeds to buy a new motorcycle. Along with the real estate, the mortgage is transferred to the corporation. Which of the following are true with regard to the tax consequences to David?
- A. The mortgage assumed by the corporation does not exceed his basis in this particular property transferred but because the liability is considered boot, David has to report a gain.
 - B. No bona fide business purpose exists for the corporation to assume David's loan.
 - C. Using the proceeds for personal purposes is like the corporation distributing cash, which would be taxed as boot under normal circumstances.
 - D. All of the above.
24. All of the following can be amortized as organizational expenditures for a newly formed corporation except:
- A. Organizational meeting expenses of the corporate directors.
 - B. Organizational meeting expenses of stockholders.
 - C. Fees paid to attorney for legal expenses in conjunction with creation of corporation.
 - D. Commissions to investment banker for initial public offering of stock.
25. Which of the following statements is **not** true?
- A. A controlled group of corporations must file a consolidated return.
 - B. In addition to regular income tax, a corporation may be liable for accumulated earnings tax if it accumulates profits instead of distributing them to shareholders.
 - C. In addition to regular income tax, a corporation may be liable for personal holding company tax if a significant portion of its income is dividends, interest, rents, and royalties.
 - D. Generally, a personal service corporation is one that furnishes personal services performed by employee-owners.

26. Sincere Inc., a C corporation, overestimated how successful it would be in the 1999 tax year. Final calculations show it will have an NOL for 1999 and owe no taxes. It had overpaid its estimated taxes for the year by \$ 700. Sincere Inc. wants its tax refund as soon as possible. What should it do?
- A. File a Form 1120, U.S. Corporation Income Tax Return, as quickly as possible before the 15th day of the third month after its year ended and wait for the money.
 - B. File Form 7004, Application for Automatic Extension of Time to File Corporation Income Tax Return, as quickly as possible and state on the form that it had overestimated its tax and wishes a quick refund as quickly as possible.
 - C. File Form 4466, Corporation Application for a Quick Refund, before the 16th day of the third month after its year end, and use it as a worksheet to show that it had overpaid its estimates by \$ 700.
 - D. Write a letter to the appropriate IRS Service Center and ask for a quick refund of overpaid corporate tax estimates.
27. Collander Corporation is preparing Schedule M-1 of its Form 1120, U. S. Corporation Income Tax Return. Which of the following statements is **incorrect** with regard to the preparation of Collander's Schedule M-1.
- A. The starting point is net income per books and the ending point is taxable income before the NOL and dividends- received deductions.
 - B. Life insurance proceeds paid on the death of a key employee is a negative adjustment to book income to arrive at taxable income.
 - C. Federal income taxes on book income are added back to net book income to arrive at taxable income.
 - D. The premiums paid on the key employee life insurance policy are a negative adjustment to book income to arrive at taxable income.
28. James Williams is the sole shareholder of Crystal Ball Enterprises, Inc. He received a \$100 dividend distribution from his corporation in 1999. Current earnings of Crystal Ball were \$1,000. What reporting requirements apply to this distribution?
- A. No reporting requirements apply because the distribution is less than \$600.
 - B. No reporting requirements apply because the distribution is not taxable.
 - C. Form 1099-DIV should be filed because the distribution is a dividend and is at least \$10.
 - D. Form 1099-MISC should be filed to report miscellaneous income.
29. Rand Corporation distributes land to a shareholder. The fair market value of the land exceeds its basis to the corporation. Which of the following statements is true with regard to this transaction?
- A. Rand Corporation must recognize gain on this distribution.
 - B. Rand Corporation realizes but does not recognize gain on this distribution.
 - C. Rand Corporation has neither a realized nor a recognized gain on this distribution.
 - D. The stockholder has a recognized loss on this distribution.

- 30.** Which of the following statements regarding corporate distributions is false?
- A.** Under no circumstances may a distribution, whether in cash or property, generate a deficit in Earnings and Profits.
 - B.** Under no circumstances may a distribution, whether in cash or property, add to a deficit in Earnings and Profits.
 - C.** In a corporate distribution, the Earnings and Profits account is reduced by the amount of money distributed.
 - D.** In a corporate distribution, the Earnings and Profits account is reduced by the lesser of the FMV or the adjusted basis of the property distributed.
- 31.** One of the following statements with regard to stock dividends and stock rights is false. Which one is false?
- A.** If stock dividends are not taxable, there is no reduction in the corporation's Earnings and Profits account.
 - B.** If stock dividends are taxable, the distribution is treated by the distributing corporation in the same manner as any other taxable property dividend.
 - C.** A disproportionate distribution of stock rights is not includable in gross income.
 - D.** If stock rights are taxable; basis to the shareholder-distributee is the FMV of the rights.
- 32.** A stock redemption is the acquisition by a corporation of its stock from a shareholder. A stockholder who owns all of the stock of a corporation sells back one half of his stock for cash. Which of the following statements is true with regard to this stock redemption? Assume current Earnings and Profits greater than redemption amount.
- A.** This sale back to the corporation of one half will cause no percentage change in the shareholder's ownership.
 - B.** After the redemption the shareholder will own all of the stock in the corporation.
 - C.** The stock redemption resembles a dividend distribution and will be taxed accordingly.
 - D.** A, B, and C are all true.
- 33.** A corporation may elect to be an S corporation if it meets the following tests:
- A.** It is a domestic corporation.
 - B.** It has no more than 75 shareholders. A husband and wife (and their estates) are treated as one shareholder for this requirement. All other persons are treated as separate shareholders.
 - C.** It has only one class of stock.
 - D.** All of the above.

34. Bob and Dianne are merchants. They decided to combine their businesses and start a mail-order business. They also decided that the corporate structure would be in their best interest. On January 1, 1999, they formed the B. & D. Corporation, but they did not file Form 2553 (Election by a Small Business Corporation) when they formed the corporation. Bob and Dana filed an 1120S return at the end of the 1999 calendar tax year, and reported their respective shares of earnings on their individual tax returns. All of following statements are true except:

- A.** Bob and Dianne have until March 15, 2000, to make a valid election for 1999.
- B.** Bob and Dianne were not permitted to file an 1120S return because they did not make a valid election for 1999.
- C.** Bob & Dianne should have filed Form 1120, U. S. Corporation Income Tax Return, and should not report earnings and losses on their individual tax returns.
- D.** Both Bob and Dianne are required to consent to the election.

35. The Emerson Corporation may elect to be an S corporation if it meets all of the following conditions **except**:

- A.** Its only shareholders are individuals.
- B.** It has no more than 75 shareholders.
- C.** It has only one class of stock, 50% with voting rights and 50% with non-voting rights.
- D.** It is a domestic international sales corporation.

36. Which of the following is **not** eligible to be a shareholder of an S corporation?

- A.** A domestic partnership
- B.** Individuals who are not nonresident aliens.
- C.** Estates
- D.** An exempt organizations described in section 401 (a) or 501(c)(3).

37. Which of the following are considered separately stated items for Form 1120S shareholders?

- A.** Net income or loss from rental real estate activities.
- B.** Interest income.
- C.** Royalty Income.
- D.** All of the above.

38. Which of the following are considered separately stated items for Form 1120S shareholders:

- A.** Charitable contributions.
- B.** Low-income housing credit.
- C.** Section 179 expense deduction.
- D.** All of the above.

39. All of the following events would cause an S Corporation to cease qualifying as an S Corporation **except**:

- A.** Having more than 75 shareholders.
- B.** The transfer of its stock to a corporation
- C.** The transfer of its stock to a nonresident alien.
- D.** Failure of the passive income test for two consecutive years.

40. All of the following events would cause an S Corporation to cease qualifying as an S corporation **except**:

- A.** Having a total of 65 shareholders.
- B.** The transfer of its stock to a corporation
- C.** The transfer of its stock to a nonresident alien.
- D.** The election is revoked with the consent of shareholders that, at the time the revocation is made, had 55% of the stock.

41. All of the following events would cause an S Corporation to cease qualifying as an a S corporation **except**:

- A.** Having more than 75 shareholders.
- B.** The transfer of its stock to a corporation.
- C.** The transfer of its stock to a nonresident alien.
- D.** The election is revoked with the consent of shareholders that, at the time the revocation is made, had 40% of the stock.

42. All of the following events would cause an S Corporation to cease qualifying as an S corporation **except**:

- A.** Having more than 75 shareholders.
- B.** The transfer of its stock to a corporation.
- C.** The transfer of its stock to a resident alien.
- D.** The election is revoked with the consent of shareholders who, at the time the revocation is made, had 55% of the stock.

43. Which of the following statements is false?

- A.** The beneficiary of an estate or trust may be taxed on money required to be distributed whether actually distributed or not.
- B.** Money distributed to a beneficiary from an estate is taxed twice – on the estate return and on the beneficiary's return.
- C.** Tax-exempt interest distributed to a beneficiary is not taxable to the beneficiary.
- D.** Losses of estates and trusts are generally not deductible by the beneficiaries.

44. Mr. Alexis died April 30, 1999. His gross estate totaled \$1.5 million dollars. Assuming no extension is granted, the executor must file Form 706, United States Estate Tax Return, on or before:

- A.** April 15, 2000.
- B.** August 15, 1999.
- C.** January 30, 2000.
- D.** October 31, 1999.

45. Mary Smith made only the following transfers of interest in personal property during the 1999 tax year:

- \$40,000 cash to the Democratic Party, a political organization (as defined in section 527(e)(1))
- \$25,000 cash to Good Care Health, Inc. for medical care (as defined in section 213(d)) of her ailing resident father
- 100 shares of common stock of ABC Inc. with a basis to Mary of \$5,00 and a fair market value (FMV) of \$10,000 to Save the Walnut Foundation, a section 501(c)(3) organization.

What is the total amount of gifts that must be reported on Mary's gift tax return for 1999?

- A.** \$75,000
- B.** \$70,000
- C.** \$50,000
- D.** Mary does not need to File Form 709 for the 1999 tax year

Part 3

Section C:

Questions 46-80

The following questions may require some computation. Select the most appropriate answer and darken completely the box under the corresponding letter on the answer sheet.

46. Mario and Jim are considering incorporating their pizza shop. If Mario and Jim incorporate, they would transfer the following assets to the corporation in exchange for 100% of the stock.

	Basis		FMV	
	<u>Mario</u>	<u>Jim</u>	<u>Mario</u>	<u>Jim</u>
Cash	\$ 5,000	\$ 4,000	\$ 5,000	\$ 4,000
Equipment	\$10,000	\$31,000	\$ 30,000	\$30,000
Furniture and fixtures	\$ 1,000	\$ -0-	\$ 12,000	\$ 1,000
Building	<u>\$40,000</u>	<u>\$ -0-</u>	<u>\$100,000</u>	<u>\$ -0-</u>
Totals	\$56,000	\$35,000	\$147,000	\$35,000

If they went forward with the incorporation, how much gain/loss would Mario have to report on his individual tax return for the year of transfer?

- A. \$ 91,000
 - B. \$ -0-
 - C. \$ 91,000 loss
 - D. None of the above
47. Frank and his son, Kyle, form a corporation with the transfer of property valued at \$50,000 and \$ 25,000 respectively. In return for this property, Frank and Kyle each receive 50% of the corporation's stock. Which of the following statements is false regarding the transaction?
- A. A nontaxable exchange has taken place and neither Frank nor Kyle will have a gain on the transfer.
 - B. The stock received is not proportionate to the value of the property transferred.
 - C. Frank will be deemed to have made a gift to his son of \$ 12,500 and Frank's basis in his stock will be the adjusted basis of the property that he transferred to the corporation less the basis of the property deemed to be a gift to Kyle.
 - D. Kyle's basis in his stock will be the adjusted basis of the property that he transferred to the corporation plus the FMV of the property transferred by Frank that is deemed to be a gift to him.

48. Sam transfers assets with an adjusted tax basis to him of \$ 50,000 to Zarus Corp., a C-corporation, in exchange for special business equipment worth \$ 5,000 and 100 % of all the stock in Zarus worth \$ 100,000. How much gain does Sam realize and how much gain must he recognize on the transfer?

- A.** \$ 0 realized, \$ 0 recognized.
- B.** \$ 55,000 realized, \$ 0 recognized.
- C.** \$ 55,000 realized, \$ 55,000 recognized
- D.** \$ 55,000 realized, \$ 5,000 recognized.

49. The Jones Corporation was formed on December 1, 1999. Qualifying organizational expenditures were incurred and paid as follows:

Incurred and paid in December of 1999	\$10,000
Incurred in December, 1999 but paid in January, 2000	5,000
Incurred and paid in February, 2000	3,000

Assume that Jones Corp. makes a timely election under IRC Section 248 to amortize organizational expenditures over a period of 60 months. What amount may be amortized in the corporation's first tax year if it adopts a calendar year and the accrual basis of accounting for tax purposes ?

- A.** \$ 300
- B.** \$ 250
- C.** \$3,600
- D.** None of the above.

50. Joseph Jackson had previously incorporated his sole proprietorship by transferring property to his newly formed corporation in exchange for 100% of the stock. These assets, if sold, would produce a gain of \$ 100,000. A week after incorporation, Joseph sells other assets for cash to the corporation that produce a loss of \$ 20,000. Joseph is attempting to avoid Section 351 on the transfer of the loss assets in order to recognize the loss for tax purposes. Which statement best explains the tax consequences to him?

- A.** Joseph has a recognized loss of \$ 20,000 to report.
- B.** Joseph has a recognized gain of \$ 100,000 and a recognized loss of \$ 20,000 to report.
- C.** Joseph has neither a recognized gain nor recognized loss to report.
- D.** Joseph has only a recognized gain of \$ 100,000 to report.

51. Big and Bold, Inc. is a C corporation, which constructs billboards for advertising. During 1999 its books reflect the following:

Income:
 Net income from sales of billboards \$35,000
 Interest income \$ 1,500

Deductions:
 Charitable contributions paid in 1999 \$ 4,000
 Truck expense \$ 28,000
 Office, utility and telephone expense \$ 500

Compute the tax on the taxable income. The following information is provided for your convenience:

Taxable Income Over	But not Over	Pay	% on excess	of the amount Over
0 --	\$ 50,000	0	plus 15	0
50,000	75,000	7,500	plus 25	50,000

Taxable income of certain personal service corporations is taxed at a flat rate of 35%.

- A. \$ 600
- B. \$2,520
- C. \$1,080
- D. None of the above.

52. Pipe Dreams, Inc. is a C corporation which provides plumbing repair services to individual homeowners. During 1999, it had the following income:

Income from plumbing services \$49,000
 Interest Income 2,000
 Net short term capital gain 3,000
 Net long term capital loss (54,000)

Compute the tax on the taxable income. The following information is provided for your convenience:

Taxable Income Over	But not Over	Pay	% on excess	of the amount Over
0 --	\$ 50,000	0	plus 15	0
50,000	75,000	7,500	plus 25	50,000

Taxable income of certain personal service corporations is taxed at a flat rate of 35%.

- A. \$7,750
- B. \$ 0
- C. \$7,350
- D. \$17,850

53. Copper Corporation had the following income and expenses during its calendar year of 1999:

Income from operations	\$250,000
Expenses from operations	175,000
Qualifying dividends from domestic corporations (10% ownership)	15,000

What is Copper Corporation's dividends-received deduction for 1999?

- A.** \$15,000
- B.** \$10,500
- C.** \$12,000
- D.** None of the above

54. Dooly Corp. incurred net short-term capital gains of \$40,000 and net long-term capital losses of \$90,000 during 1999. Taxable income from other sources was \$500,000. How are the capital gains and losses treated on the 1999 tax return, Form 1120 ?

- A.** \$3,000 of the excess net long-term capital losses are deducted currently and the \$47,000 remainder is carried forward indefinitely.
- B.** None of the excess net long-term capital losses are currently deductible, but may be carried back to the three preceding years and then forward five years as short-term capital losses.
- C.** Excess net long-term capital losses are fully deductible in 1999.
- D.** Excess net long-term capital losses of \$50,000 are carried back two years and then carried forward 20 years as short-term capital losses.

55. Mr. Fred Wall bought a house that cost \$50,000 for an unrelated friend, Gloria Wilson, in 1999. Mrs. Wall made no gifts in 1999. In filing their gift tax returns for 1999, Mr. and Mrs. Wall should file Form 709, United States Gift Tax Return, as follows:

- A.** Mr. Wall should file a gift tax return reporting the \$50,000 gift and taking a \$10,000 annual exclusion.
- B.** File one joint gift tax return reporting the \$50,000 gift and taking a \$10,000 annual exclusion for each spouse, or a \$20,000 exclusion.
- C.** File two gift tax returns, one for Mr. Wall and one for Mrs. Wall, with each spouse signing the consent section of the other's gift tax return signifying that the spouse agrees to treat all gifts as made one-half by each spouse. A \$10,000 annual exclusion may be taken on each return.
- D.** Either A or C.

56. In 1999, Panda Corp. has passive losses of \$ 250,000 from a rental activity. Its active business income is \$ 150,000 and its portfolio income is \$ 50,000. What is Panda Corp.'s 1999 taxable income if a) Panda is a closely held corporation and b) Panda is a personal service corporation?

- A.** a.) \$ 50,000, b.) \$200,000
- B.** a.) \$ 50,000 loss, b.) \$200,000
- C.** a.) \$ 50,000, b.) \$50,000
- D.** a.) \$200,000, b.) \$50,000

57. The X Corporation, a calendar-year taxpayer, estimates at the end of March 1999 that its federal income tax for 1999 will be \$800,000. Accordingly, it pays \$200,000 (25% of \$800,000 x 100%) by April 15, 1999. At the end of August 1999, a recalculation shows that its 1999 tax is expected to be \$1,000,000. Assuming that there is no later change in the estimated tax, what should be the estimated tax installment for September?

- A. \$0
- B. \$200,000
- C. \$350,000
- D. \$400,000

58. The following information is available from the books of ABC Corporation. Determine what taxable income should be reported on Form 1120.

Federal income tax accrued for the tax year	\$ 55,000
Net income per books, after tax	\$148,000
Life insurance premiums (not deductible on return)	\$ 17,000
Tax exempt interest income	\$ 15,000

- A. \$150,000
- B. \$201,000
- C. \$205,000
- D. \$220,000

59. Morris Corporation has \$ 100,000 positive current E&P to cover any distributions. It distributes land with a fair market value of \$ 30,000 and adjusted basis of \$ 10,000 to its sole shareholder, Mary, who has \$70,000 basis in her Morris Corp. stock. This is not a liquidation or redemption. Which statement below best describes the tax consequences to the Morris Corporation and to stockholder, Mary?

- A. Morris will recognize gain of \$20,000 and Mary a taxable dividend of \$20,000.
- B. Morris will recognize gain of \$20,000 and Mary a taxable dividend of \$30,000.
- C. Morris will recognize gain of \$20,000 and Mary will have a non-taxable return of capital reducing her basis by \$30,000.
- D. None of the above.

60. Buffalo Properties, Inc. owned and displayed a collection of watercolors in its main office. When the 75% owner retired, he was presented with his choice from the collection. He selected a painting with a fair market value of \$250,000. Buffalo Properties' basis in the painting was \$150,000. Current year earnings and profits were \$500,000. No other distributions were made during the year. What amount of dividend must the retiring owner report for the year that he received the painting?

- A. \$0
- B. \$150,000
- C. \$250,000
- D. \$100,000

61. Buffalo Properties, Inc. owned and displayed a collection of watercolors in its main office. When the 75% owner retired, he was presented with his choice from the collection. He selected a painting with a fair market value of \$250,000. Buffalo Properties' basis in the painting was \$150,000. How should the distribution be reported on the return of Buffalo Properties?

- A.** No reporting required.
- B.** \$150,000 distribution reduces assets on the balance sheet but no effect on tax.
- C.** \$100,000 taxable gain.
- D.** \$250,000 taxable gain.

62. Philly Corp. distributed an office building to its 60% shareholder. The fair market value of the building on the date of the distribution was \$300,000. Philly's basis in the building was \$200,000. The shareholder assumed the mortgage on the building that had a principal balance of \$100,000 on the date of distribution. Current year earnings and profits of Philly Corp. were \$400,000. No other distributions were made during the year. What should the shareholder report on his tax return for the year of the distribution?

- A.** \$0; distributions to shareholders result in no gain or loss to the shareholder.
- B.** \$300,000 dividend.
- C.** \$200,000 dividend.
- D.** \$100,000 dividend.

63. Arena, Inc. decided to distribute shares of its own stock to its employees at year-end as a reward for a profitable year. Each employee was to receive 10 shares with a fair market value of \$100 per share. Employees were offered a choice of cash or the stock dividend. What is the tax effect to the employees of this distribution?

- A.** \$0; distributions of stock dividends and stock rights are tax-free to shareholders.
- B.** \$1,000 taxable income to the employees who chose to receive cash and no effect on the employees who received stock.
- C.** \$1,000 taxable income to each employee.
- D.** None of the above.

64. Larry, Jane, Robert and Mary each own 250 shares of XYZ, Inc. for which they paid \$100 each. They started their corporation this year. Current earnings and profits are \$40,000. Which of the following is most correct?

- A.** If XYZ cancels (redeems) 25 shares of each shareholder's stock, the \$2,500 paid to each owner will be taxable as a dividend.
- B.** If Robert redeems all of his stock (and Larry, Jane and Mary and Joe redeem none), the \$25,000 Robert receives will not be taxed as a dividend.
- C.** Both A & B are true.
- D.** Neither A nor B is true.

65. Chandler Corporation has 500 shares of common stock outstanding. Scott owns 150 shares, Scott's mother, Mabel, owns 50 shares, his brother, Ted, owns 40 shares, and Scott's son, Fred, owns 60 shares. Borus Corporation owns 50 shares of Chandler Corporation and Scott owns 70% of the stock in Borus Corporation. How many shares does Scott own in Chandler Corporation, applying the rules of ownership attribution, for purposes of determining whether a loss on the sale or trade of property between related parties is deductible?

- A.** 335 shares
- B.** 295 shares
- C.** 350 shares
- D.** None of the above.

66. What is the non-separately stated income amount of a calendar year S corporation operating on an accrual basis with the following items?

Gross receipts	\$300,000
Interest income	\$ 25,000
Royalty Income	\$ 10,000
Salary paid to shareholder	\$ 20,000

- A.** \$ 300,000
- B.** \$ 55,000
- C.** \$ 320,000
- D.** \$ 280,000

67. What is the total amount of separately stated income of a calendar year S corporation operating on an accrual basis with the following items:

Gross receipts	\$ 300,000
Interest income	\$25,000
Royalty Income	\$10,000
Salary paid to shareholder	\$20,000

- A.** \$300,000
- B.** \$ 55,000
- C.** \$ 35,000
- D.** \$320,000

68. What is the total amount of separately stated income items of a calendar year S corporation operating on an accrual basis with the following information:

Net income of rental real estate activities	\$ 300,000
Interest income	\$25,000
Royalty Income	\$10,000
Section 1231 Gain (from equipment sale)	\$20,000
Gross receipts	\$700,000

- A.** \$ 355,000
- B.** \$1,055,000
- C.** \$ 300,000
- D.** \$ 720,000

69. Quantum Leap Industries, an S corporation, has \$10,000 in accumulated earnings and profits. In 1999, Quantum Leap Industries distributed property with a fair market value of \$75,000 and an adjusted basis of \$62,000 to Edward, its sole shareholder. After recognizing his share of any corporate gain or loss, his adjusted basis in Quantum Leap Industries' stock at the end the year was \$60,000. How should the distribution be handled by Edward?

- A.** \$60,000 as return of capital and \$15,000 is non-taxable distributions.
- B.** \$10,000 as ordinary Income, \$60,000 as return to capital and \$5,000 is taxable capital gain.
- C.** \$60,000 as return to capital and \$2,000 as taxable capital gain.
- D.** \$70,000 is a non taxable distribution.

70. Lebeck Industries, a qualified S corporation, has no accumulated earnings and profits. In 1999, Lebeck Industries distributed property to Bob, its sole shareholder. It had a fair market value of \$75,000 and an adjusted basis of \$62,000. After recognizing his share of any corporate gain or loss, his adjusted basis in Lebeck Industries' stock at the end the year was \$60,000. How should the distribution be handled by Bob?

- A.** \$60,000 as return of capital and \$15,000 is non-taxable distributions.
- B.** \$60,000 as return to capital and \$2,000 is taxable capital gain.
- C.** \$60,000 as return to capital and \$15,000 as taxable capital gain.
- D.** \$60,000 is a non taxable distribution.

71. On January 1, 1999, Bob purchased 50% of the stock of Lebeck Industries, an S corporation, for \$100,000, and Bob also loaned the corporation \$20,000. At the end of the 1999, Lebeck Industries incurred in ordinary loss of \$180,000. How much of the loss can Bob deduct on his personal income tax return for 1999?

- A.** \$ 90,000
- B.** \$180,000
- C.** \$ -0-
- D.** \$120,000

72. Ms. Smith, a cash method taxpayer, died on September 30, 1999. Subsequent to her death, but prior to December 31, 1999, her beneficiary received the following:

Rental income	\$ 1,500
Proceeds from a life insurance policy	\$20,000
Dividend declared on September 27, 1999	\$ 6,000

What amount is considered income in respect of a decedent?

- A.** \$ 1,500
- B.** \$ 7,500
- C.** \$ 3,000
- D.** \$27,500

73. Mr. Jones died on November 30, 1999. After his death, but prior to December 31, 1999, his estate received the following cash receipts:

Life insurance proceeds	\$50,000
Social Security death benefits	\$ 250
Redeemed Certificate of Deposit of which \$100 was accrued interest	\$10,100
Mutual fund dividend distribution	\$ 200

Assuming that none of the beneficiaries are nonresident alien individuals and the executor of the estate adopted a calendar year for the estate, Form 1041 will need to be filed on or before:

- A.** March 15, 2000.
- B.** April 17, 2000 (April 15, 2000 falls on a Saturday).
- C.** August 30, 2000.
- D.** Form 1041 does not need to be filed for the 1999 tax year.

74. Ms. Brown died on June 30, 1998. During 1999, her estate received the following:

Interest income	\$2,500
Dividend income	\$5,000
Long Term Capital Gain	\$2,500

Pursuant to her will, 50% of all income was to be distributed to a specific qualifying charitable organization. The executor complied with the provision in a timely manner. Assuming all income was accumulated, what is the estate's taxable income for 1999?

- A.** \$10,000
- B.** \$ 2,500
- C.** \$ 5,000
- D.** \$ 4,400

75. The Mrs. Flame passed away on March 15, 1999. The assets, included in her estate, were properly valued as follows:

	3-15-99	7-15-99	9-15-99
Personal Residence	\$ 500,000	\$600,000	\$700,000
Stocks held	\$1,000,000	\$700,000	\$750,000

The executor sold the home on July 15, 1999 for \$600,000. The alternate valuation date was properly elected. What is the value of the estate reported for estate tax purposes?

- A.** \$1,450,000
- B.** \$1,500,000
- C.** \$1,350,000
- D.** \$1,300,000

- 76.** On June 30, 1999, John Smith made a gift of \$2,000 to his daughter. John will need to file a gift tax return (Form 709 or 709A) on or after January 1, 2000, but no later than:
- A.** March 15, 2000
 - B.** April 17, 2000 (April 15 falls on a Saturday)
 - C.** March 31, 3000
 - D.** John will not have to file Form 709 or 709A for year ending 12-31-1999

77. Mrs. A died on June 30, 1999. According to the terms of her will, \$20,000 was paid to each of her three children prior to the end of the year. Additionally, the estate was to pay from earnings, \$20,000 to each child in 1999. In 1999, the estate had net earnings of \$30,000.

Assuming no charitable contributions were made, how much income will each child report?

- A.** \$30,000 ordinary income.
 - B.** \$40,000 ordinary income.
 - C.** \$10,000 ordinary income.
 - D.** \$0.
- 78.** Given the following information, what is the distributable net income for the simple trust established by Mr. Bill?

Dividend Income	\$20,000
Taxable Interest Income	\$25,000
Tax Exempt Interest Income	\$10,000
Long Term Capital Gains	\$20,000
(Capital Gains are allocable to Corpus)	
Fiduciary Fees	\$ 5,000

- A.** \$70,000
- B.** \$60,000
- C.** \$50,000
- D.** \$40,000

79. Van and Floyd formed a corporation in 1999. In exchange for one-half of the outstanding shares of the corporation's voting stock, which had a total par value of \$400,000, Van contributed property with a fair market value of \$200,000 for which he had paid \$300,000 in a prior year. Floyd contributed property with a fair market value of \$200,000 for which he had paid \$100,000 in a prior year and received the other one-half of the outstanding stock. How much gain or loss will Van and Floyd recognize on the transfer of property?

- A.** Van will recognize \$100,000 loss; Floyd will recognize \$100,000 gain
- B.** No gain or loss to either Van or Floyd
- C.** Van will recognize \$0 loss; Floyd will recognize \$100,000 gain
- D.** None of the above

- 80.** Foster's RV Sales, Inc. is an S corporation with the following activity during 1999:
- \$500,000 gross sales of RV's and campers
 - \$300,000 operating expenses
 - \$ 1,000 interest income
 - \$ 3,000 charitable contributions
 - \$ 10,000 Section 179 expense

How much ordinary income from trade or business activities will be reported on Schedule K, Shareholders' Shares of Income, Credits, Deductions, etc.?

- A.** \$188,000
- B.** \$190,000
- C.** \$198,000
- D.** \$200,000