

2003

**SPECIAL ENROLLMENT
EXAMINATION**

Part 1

**SPECIAL ENROLLMENT
EXAMINATION BOOKLET**

**September 17, 2003
9:00 A.M. TO 12:00 NOON**

Individuals



IRS

Department of the Treasury
Internal Revenue Service

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Special Enrollment Examination

Part 1

Individuals

Instructions:

The time allotted for this part of the examination is 3 hours. No additional time will be granted. On your answer sheet in the spaces provided you should enter the following:

1. Print your name (First, M.I., Last).
2. Sign your name (First, M.I., Last).
3. Place of examination (City and State).
4. Date of this examination.
5. Print your name (Last, F.I., M.I.) in the boxes provided. Immediately below the boxes darken the oval corresponding to the letter you have printed, as in the sample Name Grid. Darken only one oval in each column below a box in which you have printed a letter. Make no marks in the columns below boxes you have left blank.
6. Enter your candidate number and immediately below, darken the oval corresponding to each number you have entered.
7. Enter your Social Security Number and immediately below, darken the oval corresponding to each number you have entered.

Important:

The answer sheet should not be folded or torn since it will be machine graded.

Read the examination questions carefully. All references are to the Internal Revenue code as amended through December 31, 2002. Unless otherwise stated, all questions relate to the calendar year 2002.

You will be given a No. 2 pencil by the monitor. Darken completely only one oval under the corresponding letter on the answer sheet. In making corrections, erase errors completely.

Scratch paper will be provided, but you may make necessary computations in the questions books. Raise your hand to attract the monitor's attention when you need extra supplies or for permission to leave the room.

!! New procedures!!

All materials must be turned in to the monitor before leaving the room:

Answer sheet: When you finish the examination, your answer sheet must be turned in to the monitor before leaving the room. You must turn in your answer sheet at the end of each test session or your test will not be graded and no credit received. **Answers noted in examination booklets will not be graded.** The examination will be graded in Washington, D.C., by the Office of Professional Responsibility, Internal Revenue Service. You will receive formal notification of your examination results on or about January 31, 2004.

Examination booklets, scratch paper: You must also turn in your examination booklet and scratch paper (used and unused). These materials will be mailed to you after the examination has been administered at all sites.

General Grading Information:

The questions in this examination have been assigned values of 1 to 3 points. All true or false questions have a value of 1 point each; the multiple choice questions in Section B have a value of 2 points each; and the multiple choice questions in Section C have a value of 3 points each.

The examination is graded on the basis of correct answers. If more than one oval is darkened in answering a questions, the answer will be considered incorrect.

The Service will include the answers with your formal notification of examination results. Therefore, you may want to mark your answers in this examination questions book and retain it for purposes of your future comparison.

Part 1
Section A:
Questions 1– 20

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

1. Generally, if an unmarried dependent child, John, earns \$4,200 wages during the summer, has no tips, has \$200 in interest/dividends, and no income tax withheld, he would not be required to file a tax return for 2002.
2. Mary's husband died in 1999. Her son Bob is her dependent and has lived in her house since his birth in 1992. In 2002, Mary may file as qualifying widow because she has not remarried.
3. Peter's unmarried daughter lived with him in his house for the entire year 2002. Peter owns the home and pays all the costs of upkeep for that home. His ex-wife did not live in the home at any time during the year. Peter can file as head of household in the year 2002.
4. If a taxpayer files his 2002 Form 1040 by January 31, 2003 and pays the balance due with the return; he will not receive an underpayment of estimated tax penalty for the fourth quarter estimated tax payment that was due on January 15, 2003.
5. Ted is an ordained minister. He owns his own home and receives a housing allowance that is less than the fair rental value of the home. Because he owns his home, the must include the housing allowance as income for income tax and self-employment tax purposes.
6. A regulated investment company (mutual fund) or real estate investment trust (REIT) declares a dividend in November 2002 payable to shareholders of record on November 15. If the dividends are actually paid on January 5, 2003, the dividends are taxable in 2002.
7. There is no difference in the tax treatment of short-term capital gains, dividends, and long-term capital gains on your federal return.
8. Rosemary's home is used exclusively as her residence all year except for 10 days. During this time, Rosemary rents out her home to alumni while the local college has its homecoming celebration. The rent does not need to be included in income.
9. Cory owns an apartment building. In addition to providing the utilities for his tenants, he also cleans the halls and utility room and picks up the trash. Because of these added services, Cory must report the rentals on Schedule C, Profit or Loss from Business instead of reporting them on the Schedule E. (He is not a real estate professional.)
10. A property received as a gift has a basis greater than its fair market value. Generally, if it is sold at a loss, the fair market value becomes the basis for computing the loss.
11. Fred bought ten shares of stock on October 1, 2001. He sold them for a \$20 loss on October 1, 2002. This is a short term capital loss.
12. Derek is a self-employed carpenter and is also an employee of Krispy, Inc. His self-employment net income is \$35,000, and he received a W-2 for salaries and wages of \$25,000. He is covered by his employer's pension plan. Derek is not eligible to take a deduction for an IRA but he can deduct 50% of his self-employment tax and 70% of his health insurance premiums for 2002.
13. Jim files his tax return as married filing separately. He has not lived with his wife for two years. In tax year 2002, by court order, he paid her \$500 per month as separate maintenance. He will be able to deduct \$6,000 as alimony.
14. Carleen paid \$1,000 U. S. dollar equivalent in Deutsche Marks to Germany on income earned while working there. She qualified for the income earned abroad exclusion on the \$40,000 wages she earned. She can take a credit or a deduction for the foreign tax paid to Germany.
15. Generally, those claiming earned income credit cannot have investment income greater than \$2,550 for tax year 2002.
16. George and Jean, a married couple living together, have no income other than their wages. George earned \$12,000 and Jean earned \$9,000. They have two minor children and have decided to file married filing separate tax returns, each claiming one child as a dependent. This way they will both qualify for the earned income credit.

17. To qualify for the earned income credit, the taxpayer must have a dependent child.
18. Anthony, filing single, has one household employee, and attaches Schedule H to his individual tax return for reporting. He may use his W-2 withholdings to offset the Schedule H tax liabilities.
19. Two years ago, Mark sold property (basis of \$250,000) for \$500,000. He received a down payment of \$50,000 plus regular monthly payments of principal and interest until 10 months ago. The buyer failed to make further payments resulting in Mark repossessing the property. Mark may have a tax consequence as a result of repossessing the property.
20. The President and CEO of Online, Inc., who had no direct or indirect ownership interest in Online, Inc., personally advanced \$50,000 to the corporation as a temporary loan. Online, Inc. declared bankruptcy and was discharged from bankruptcy without repaying the \$50,000. This should be treated as a non-business bad debt.

Turn to the next page for Part 1, Section B.

Part 1
Section B:
Questions 21 - 45

The following questions are multiple choice. Select the most appropriate answer and darken the oval under the corresponding letter on the answer sheet.

21. Form 4868, Application for Automatic Extension of Time to File U. S. Individual Income Tax Return, will provide the individual taxpayer with the following:
- A. An automatic extension of 2 months for taxpayers out of the country on April 15th.
 - B. An automatic extension of 4 months to pay the taxes due.
 - C. An automatic extension of 4 months to file the return.
 - D. An automatic extension of 6 months to file the return.
22. The following statements about dividends received from a dividend reinvestment plan are correct **except**:
- A. Reinvested dividends are not taxable if not removed from the account.
 - B. Reinvested dividends are not taxable until the related stock is sold.
 - C. Reinvested dividends automatically receive capital gains treatment when received.
 - D. Reinvested dividends are treated as normal dividends on Schedule B.
23. An individual taxpayer has capital gain distributions only, and no other capital gains. Which of the following satisfies the reporting requirements:
- A. All capital gain distributions must be entered on Schedule B.
 - B. No Schedule D is required and the amount is entered directly on Form 1040.
 - C. Dividends and capital gains distributions are totaled on Schedule B and carried to the front page of Form 1040.
 - D. If there are no other capital gains, capital gain distributions must be combined with interest on the Schedule B.
24. Tom, a single taxpayer, determines that he has both a short term capital loss of \$2,000 and a non-taxable distribution of \$1,000 from an investment. The following statements are correct, **except**:
- A. The basis of the investment is reduced by the non-taxable distribution.
 - B. Non-taxable distribution is a return of capital.
 - C. The short term capital loss can be used to offset capital gains (if any) for the year.
 - D. Any unused short term capital loss may be carried back three years.
25. During the year 2002, Dan had these expenses for his rental house:
- 1. Replaced a screen in the storm door.
 - 2. Replaced the heating system.
 - 3. Sowed grass seed in some bare spots on the lawn.
 - 4. Built a detached two-car garage.
 - 5. Installed a new dishwasher.
 - 6. Bought a welcome mat for the front stoop.
- Which of these items must be depreciated rather than deducted as an expense on his Schedule E?
- A. 1, 3, 4, and 5.
 - B. 2, 4, 5, and 6.
 - C. 2, 4, and 5.
 - D. 3, 4, and 6.
26. Jeremy owns a duplex. He lives in one half and rents out the other half at fair rental value. He wants to take depreciation on the building, the appliances, and major remodeling in the bathroom on the rental side. What depreciation may be taken?
- A. 27.5 year MACRS on both sides of the duplex, 7 year MACRS on the appliances and remodeling.
 - B. 27.5 year MACRS on the rental side, 0 on the personal side, and 7 year MACRS on the appliances and remodeling.
 - C. 27.5 year MACRS on both sides of the duplex, 5 year MACRS on the appliances and remodeling.
 - D. 27.5 year MACRS on the rental and remodeling, 5 year MACRS on the appliances, and no depreciation on the personal side.
27. Which of the following is the depreciable basis in rental property that is placed in service after receiving it as a gift, if the donor's basis was more than the fair market value of the property?
- A. The fair market value on the date of the gift, plus or minus any required adjustments to basis.
 - B. The fair market value of the property on the date you converted it to rental property.
 - C. The donor's basis of the property plus or minus any required adjustments to basis.
 - D. All of the above.

28. Connor purchased Flora stock in 1996 and sold it in 2002. In 2002, he also traded in a copy machine that he had been using in his business since 1998 for a new model. On December 15, 2002, he inherited 35 shares of Fauna Laboratories stock. What is the holding period for these properties?
- All short term.
 - Flora stock long term, copy machine and Fauna stock short term.
 - Flora and Fauna stock long term; copy machine short term.
 - All long term.
29. James sells stock that he purchased in 1990, to his brother John for a \$500 loss. He also sells a truck, purchased in 2000, to ABC Corporation, his 100% owned C corporation, for a profit of \$800, including \$500 of depreciation recapture. What is the effect of these transactions on James's 2002 tax return?
- A loss of \$500 on the stock and no gain on the truck.
 - A disallowed loss on the stock, \$500 ordinary gain and \$300 long-term capital gain on the truck.
 - A loss of \$500 on the stock and \$800 ordinary gain on the truck.
 - A disallowed loss on the stock and \$800 ordinary gain on the truck.
30. Generally, if you own stock in a small corporation that meets the requirements of Section 1244 (small business) stock and you sell that stock at a loss, the loss is reported as:
- Short term loss on Schedule D limited to \$3,000.
 - Ordinary loss on Form 4797 limited to \$25,000 for a single individual and limited to \$50,000 for those filing a joint return.
 - Long term loss on Schedule D limited to \$3,000.
 - Ordinary loss on Form 4797 limited to \$50,000 for a single individual and limited to \$100,000 for those filing a joint return.
31. David is an interstate truck driver subject to Department of Transportation hours of service, but is not an employee. In 2002, he is allowed to deduct what percent of his meals he had while working as an interstate truck driver?
- 0%.
 - 50%.
 - 65%.
 - 80%.
32. Generally, which of the following expenses paid by Kathy, a salesperson, are deductible as **entertainment** expenses?
- Chamber of Commerce dues.
 - Cover charges and cost of meals for taking a client to a nightclub.
 - Country club dues where she entertains clients.
 - Weekly meals with business associates at local restaurants (they take turns paying).
33. In order to qualify as an accountable plan for reimbursement of travel expenses, the employer plan must satisfy all of the following **except**:
- The expenses have a business connection.
 - The employee must make an adequate and timely accounting to the employer.
 - The employer must pay a per diem for meals.
 - The employee must timely return any excess reimbursements.
34. Generally, the taxpayer may deduct the cost of medical expenses on Schedule A for which of the following:
- Doctor prescribed birth control pills.
 - Controlled substances like marijuana that are in violation of federal law.
 - Trips for general health improvement.
 - Marriage counseling.
35. To qualify for a medical expense deduction as your dependent, a person must be your dependent either at the time the medical services were provided or at the time you paid the expenses. A person **generally** qualifies as your dependent for purposes of the medical expense deduction if:
- The person would qualify as a dependent except for the amount of gross income.
 - The person was a foreign student staying briefly at your home.
 - The person is your sibling's unmarried adult child.
 - The person is the unrelated caregiver for your elderly parents.

36. Which of the following costs are deductible on Form 1040, Schedule A as taxes?
1. Personal property tax on an airplane.
 2. Garbage pickup itemized on the real estate bill.
 3. Real estate tax on property owned in Canada.
 4. Sales tax paid on the purchase of your personal car.
- A. None of the above.
 - B. 1 and 3.
 - C. 2 and 4.
 - D. All of the above.
37. Some contributions may be limited to 50% of the taxpayer's adjusted gross income. Deductions to the following organizations are subject to the 50% limitation on deductible contributions:
- A. Churches and conventions of organizations of churches and educational organizations with regular faculty and curriculum and regularly enrolled students.
 - B. Hospitals and certain medical research organizations associated with these hospitals.
 - C. Kiwanis, Rotary, and Lions Club who raise money for public causes.
 - D. Both A and B.
38. Which of the following organizations qualify for deductible contributions (not dues)?
- A. A Public Library in your city.
 - B. Salvation Army.
 - C. Churches.
 - D. All of the above.
39. In 2002, the U. S. President declared a federal disaster due to the flooding in Minnesota. Lisa lives in that area and lost her home in the flood. What choice does she have regarding when she can claim the loss on her tax return?
- A. It must be claimed in 2001 if the return has not been filed by the date of the loss.
 - B. It must be claimed in 2002 if the loss is greater than the modified adjusted gross income.
 - C. It may be claimed in 2003 if an election is filed with the 2002 return.
 - D. It may be claimed in 2001 or 2002.
40. Which of the following will qualify for an educational deduction on Schedule A?
- A. The employer reimburses your expenses under a tuition reimbursement (nontaxable) program.
 - B. The education maintains or improves skills needed in your present work.
 - C. The education is required by your employer or the law to keep your present salary, status, or job. The required education must serve a bona fide business purpose of your employer.
 - D. Both B and C.
41. Which of the following expenses are deductible, but subject to the 2% limitation on Form 1040, Schedule A, Job Expenses and Most Other Miscellaneous Itemized Deductions?
- A. License of a self-employed plumber.
 - B. Appraisal fees on the sale of your personal residence.
 - C. Uniforms for a UPS delivery person.
 - D. The cost of hauling tools to work in the trunk of your car.
42. Carol, an individual taxpayer, received a Form 1099-Div from her global mutual fund that showed dividend income of \$500 and foreign taxes withheld of \$67. This is the only foreign source income she received for the year. Her income tax before any credits is \$4,320. On which of the following forms may Carol elect to claim a **credit** for the foreign tax paid?
- A. Form 1040, Line 68, Other Payments, with a disclosure statement.
 - B. Directly on Form 1040, Tax and Credits, Foreign Tax Credit.
 - C. Form 1040, Schedule A, Itemized Deductions, Line 8, "Other Taxes."
 - D. Form 1040, Schedule B, by electing to reduce the dividend income by \$134 ($\67×2).
43. Hollie filed as head of household and would like to take the child tax credit for Amanda in 2002. Which of the following statements is **incorrect** regarding the child tax credit?
- A. Amanda must be under 18 at the end of the tax year.
 - B. Hollie must claim Amanda as a dependent.
 - C. All or part of the child tax credit may be refundable.
 - D. If Hollie's adjusted gross income is above \$75,000, her credit will be reduced or eliminated.

44. Elton declared bankruptcy in the current year. Included in the liabilities discharged in the bankruptcy was a \$15,000 personal loan Elton had received from his friend, Edward two years ago. How would **Edward** treat this for tax purposes?
- A. Ordinary loss on Form 4797.
 - B. Long-term capital loss on Schedule D.
 - C. Short-term capital loss on Schedule D.
 - D. Investment expense subject to 2% miscellaneous itemized deduction limitation.
45. Which of the following is earned income for earned income tax credit purposes?
- A. Unemployment compensation.
 - B. Alimony.
 - C. The wages of a minister who has an exemption from self-employment tax.
 - D. The wages of an inmate working in the prison laundry.

Turn to the next page for Part 1, Section C.

Part 1

Section C:

Questions 46 - 80

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

- 46.** Jill and John, married filing jointly, have provided more than 50% of the support for two minor children and Jill's mother. The children each had interest income of less than \$700. Jill's mother received a taxable pension of \$2,500, dividends of \$1,500 and interest of \$1,000. How many exemptions can the taxpayers claim, including themselves, on their 2002 tax return?
- A.** 3.
 - B.** 5.
 - C.** 4.
 - D.** 2.
- 47.** In meeting the "Gross Income" test for claiming his father as a dependent, the taxpayer had to consider the income received by his father. This income included gross rents of \$4,000 (expenses were \$2,000), mutual fund municipal bond interest of \$1,200, corporate bond interest of \$1,000, dividends of \$1,400, wages of \$2,000 and Social Security of \$4,000. What is the father's gross income for dependency test purposes?
- A.** \$2,000.
 - B.** \$8,400.
 - C.** \$9,600.
 - D.** \$11,600.
- 48.** A taxpayer had adjusted gross income of \$98,000 and a total tax liability in 2001 of \$20,000. In 2002, the taxpayer has a tax liability of \$25,000. The taxpayer's withholding was increased to \$23,500. He will file his tax return for 2002 on April 10, 2003. To **avoid** the underpayment of estimated tax penalty, the taxpayer must:
- A.** Pay the additional \$1,500 due by April 15, 2003.
 - B.** Pay an additional \$1,500 by January 15, 2003.
 - C.** File an annualized estimated tax computation.
 - D.** Do nothing, as he has satisfied the minimum tax payment requirements.
- 49.** Sandy received the following income in 2002:
- | | |
|--|----------|
| Wages (Box 1 of W-2) | \$50,000 |
| Money won at weekly poker games | \$1,000 |
| Christmas ham (fair market value) | \$22 |
| Dependent care benefits (Box 10 of W-2)
(Spent \$3,000 for childcare) | \$2,000 |
| Group term life insurance
(\$40,000 death benefit) | \$50 |
- How much gross income must be reported by Sandy for tax year 2002?
- A.** \$50,022.
 - B.** \$53,000.
 - C.** \$51,000.
 - D.** \$53,072.
- 50.** Susan is a waitress and earned \$15,000 in wages, not including any tips she received in 2002. She received tips of \$17 in March, which she did not report to her employer. Because she became ill in February and did not return to work until late March, she also forgot to report the \$58 for tips that she received in February. She did report the \$7,000 she received as tips for the rest of the year. How much income must she report as wages, tips and other compensation for tax year 2002?
- A.** \$22,185.
 - B.** \$22,075.
 - C.** \$15,260.
 - D.** \$15,183.
- 51.** Scott and Marie, husband and wife, are equal partners in a law firm. They had gross receipts of \$120,000, less expense of \$40,000 resulting in net income of \$80,000 for the law firm. Marie received an inheritance of \$20,000. In addition, they had municipal bond interest of \$3,000 and savings account interest of \$2,000. What is their adjusted gross income on a married filing joint return?
- A.** \$105,000.
 - B.** \$142,000.
 - C.** \$ 82,000.
 - D.** \$102,000.
- 52.** Maria had municipal bond interest of \$6,000, certificate of deposit interest of \$4,000, reinvested corporate bond interest of \$2,000, mutual fund municipal bond interest of \$7,000 and savings account interest of \$1,000. What is Maria's taxable interest?
- A.** \$3,000.
 - B.** \$7,000.
 - C.** \$20,000.
 - D.** \$16,000.

53. Paul owns a second home at the lake. During 2002, he spent three weeks (21 days) at the lake home, rented it to his daughter for three three-day weekends for a total of \$220, and rented it to friends for ten weeks (70 days) at fair rental value of \$300 per week. His expenses for the year include:
- | | |
|-------------------|---------|
| Depreciation | \$2,000 |
| Insurance | \$ 100 |
| Mortgage interest | \$1,000 |
| Real estate taxes | \$2,000 |
| Utilities | \$1,000 |
- What amount may he deduct for expenses on his Schedule E, Rental Income?
- A. \$2,100.
 B. \$3,000.
 C. \$3,220.
 D. \$4,620.
54. Cyril, who is 68 years of age, received Social Security benefits of \$12,000, wages of \$5,000, interest and dividends of \$4,000, unemployment compensation of \$3,000 and municipal bond interest of \$1,500. Calculate Cyril's adjusted gross income.
- A. \$22,200.
 B. \$25,500.
 C. \$19,200.
 D. \$12,000.
55. John and Mary, a married couple, have a wide variety of investments and are cash basis taxpayers. Because their self-employment earnings are considerable, they reinvested the following: \$4,000 of mutual fund dividends and \$5,000 of certificate of deposit interest. They also earned dividends on corporate stock of \$12,000 that they received and spent. Interest of \$2,000 that had accrued on a loan to a friend was not paid until the following year. What is the amount of interest and dividends currently taxable to them?
- A. \$21,000.
 B. \$14,000.
 C. \$16,000.
 D. \$23,000.
56. A taxpayer purchases real estate rental property for \$150,000. She pays \$25,000 cash and obtains a mortgage for \$125,000. She pays closing costs of \$8,000, which includes \$4,000 in points on the mortgage and \$4,000 for bank fees and title costs. The basis in the property is:
- A. \$33,000 depreciation, \$125,000 amortization.
 B. \$158,000, depreciation only.
 C. \$154,000 depreciation, \$4,000 amortization.
 D. \$150,000 depreciation, \$8,000 amortization.
57. Sandra joins Sam in forming a partnership. Sandra invests \$50,000 in cash. Sam will work for \$70,000 a year as a guaranteed payment to partner. Of the \$70,000 payment, \$50,000 will be retained by the partnership. Assuming the partnership had zero net income and expenses, Sam's basis in the partnership and taxable income at the end of the year are:
- A. Sam's basis in the partnership is \$50,000 and taxable income is \$20,000.
 B. Sam's taxable income is \$50,000 and his basis in the partnership is \$20,000.
 C. Sam's taxable income is \$70,000 and his basis is \$50,000.
 D. Sam's basis in the partnership is \$70,000 and taxable income of \$70,000.
58. Charles gave his daughter, Jane, a residential house. He had purchased the house for \$250,000 in 1990. The fair market value on the date of the gift was \$300,000. Charles had added a \$25,000 roof the year before he gave it to Jane. Jane converts the house to a residential rental property within one year of the gift. Jane's basis in the property is:
- A. \$300,000.
 B. \$250,000.
 C. \$225,000.
 D. \$275,000.
59. Sue gave Jennifer a rental house. Sue had purchased the property in 1993 for \$60,000 and has taken \$17,000 in depreciation. Just before the transfer she also paid \$5,000 for a room addition. Gift tax of \$18,200, attributed to the increased value, was paid. The fair market value of the rental house on the day of transfer was \$90,000. Jennifer's **basis** in the property will be:
- A. \$90,000.
 B. \$60,000.
 C. \$66,200.
 D. \$42,000.
60. Nature Corporation declared and distributed a stock dividend of 1 share for each 10 shares held by stockholders. Donna had 100 shares (\$5.50 per share basis) and received 10 additional shares with a fair market value of \$6.00 per share. Which of the following is most applicable to the stock dividend?
- A. 100 shares at \$5.50 per share basis and 10 shares at zero basis per share.
 B. 110 shares at \$5 per share basis and \$55 taxable income.
 C. 110 shares at \$5 per share.
 D. 100 shares at \$5 per share basis and 10 shares at \$6 per share basis.

61. Rose has the following transactions during the year of 2002:

Sale of ACB stock (basis \$400)	\$800
Commission paid on sale of ACB stock.	\$50
Received 200 extra shares of DEF in stock split (fair market value)	\$800
Decrease in value of GHI mutual Fund.	\$600
JKL stock declared worthless (basis \$700). (no stock value)	\$ 0

What is the net gain or loss Rose will claim on her Schedule D?

- A. \$350 loss.
B. \$1,000 gain.
C. \$300 gain.
D. \$650 loss.
62. Clyde, a single person, sold his principal residence for \$700,000. He purchased his home in 1995 for \$150,000 and lived there until he sold it. He paid for capital improvements of \$75,000, paid real estate commissions of \$36,000 and other settlement costs of \$4,000. How much taxable gain must Clyde report?
- A. None
B. \$185,000
C. \$435,000
D. \$225,000
63. Robert purchased his home for \$150,000 in 1992. He sold it for \$350,000 (including \$100,000 for the land) in 2002. This was his primary residence until it was sold. However, Robert claimed one-fifth of his home as an office for his self-employed business. He claimed a total of \$6,000 depreciation over the years. The \$150,000 purchase was assessed at \$90,000 building and \$60,000 land. Calculate Robert's taxable income as a result of the sale of this primary residence.
- A. \$6,000.
B. \$38,000.
C. \$200,000.
D. None.

64. Emma's brother purchased 100 shares of Clockwork, Inc. stock for \$10 per share on December 30, 2001. Emma inherited the shares of Clockwork stock from her brother on September 15, 2002 when it had a fair market value of \$15 per share. On December 20, 2002, she sold the stock for \$20 per share. What is the amount and character of her gain?

- A. The gain of \$1,000 is short-term capital gain.
B. The gain of \$1,000 is long-term capital gain.
C. The gain of \$500 is long-term capital gain.
D. The gain of \$500 is short-term capital gain.

65. Albina purchased 1,000 shares of Global Tech Growth mutual fund on February 15, 2002 for \$15 per share. On January 31, 2003, she sold the 1,000 of Global Tech Growth mutual fund for \$4.50 per share. Albina had no other capital transactions in 2003. Which of the following is correct?

- A. Albina has a short-term capital loss of \$10,500 on her 2003 tax return and she will be allowed to offset \$10,500 of her earnings.
B. Albina has a short-term capital loss of \$3,000 on her 2003 tax return and no carryover.
C. Albina has a short-term capital loss of \$10,500 in 2003 and will deduct \$3,000 on her tax return. She will carry-forward a short-term loss of \$7,500 to 2004.
D. Albina has a short-term capital loss of \$10,500 in 2003 and will deduct \$3,000 on her tax return. She will carry forward a long-term loss of \$7,500 to 2004.

66. During the year 2002, Ted drives his car 5,000 miles to visit clients, 10,000 miles to get to his office, and 500 miles to attend business-related seminars. He also spent \$300 for airfare to another business seminar and \$200 for parking at his office. Using 36.5 cents per mile, what is his deductible transportation expense?

- A. \$300.
B. \$2,308.
C. \$2,508.
D. \$5,958.

- 67.** Bernie is a self-employed accountant in 2002. He reported net income of \$50,000 on his Schedule C for 2002. During the year Bernie paid the following: \$5,200 child support, \$5,000 in alimony, \$6,000 in medical insurance premiums, self-employment tax of \$7,065 and \$2,000 to his IRA plan. What amounts are deductible in arriving at adjusted gross income for 2002?
- A. \$19,933.
 - B. \$40,267.
 - C. \$14,733.
 - D. \$25,265.
- 68.** In 2002, Gene is 85 years of age and single. He received Social Security payments totaling \$14,000 (this includes Medicare premium of \$600), dividend and interest income of \$21,000, a pension of \$30,000 and a taxable IRA benefits of \$16,000. What is Gene's adjusted gross income for 2002?
- A. \$80,400.
 - B. \$78,900.
 - C. \$78,390.
 - D. \$67,000.
- 69.** A taxpayer is a cash basis taxpayer. During the year, he paid the following medical expenses for himself and his daughter, Johanna, whom he claims as a dependent on his tax return.
- \$310 for glasses for Johanna and \$290 for himself;
 - \$650 for a dental root canal procedure for him;
 - \$900 for hospital emergency services; of which \$700 was paid by insurance in the same year;
 - \$1,250 for Johanna's braces which he charged to his credit card in December and paid in January of the next year;
 - \$500 for prescriptions for allergies
 - \$2,200 cosmetic plastic surgery
- The taxpayer's medical expense deduction before limitations is:
- A. \$6,100.
 - B. \$4,150.
 - C. \$3,200.
 - D. \$5,400.
- 70.** George had the following income and expenses:
- Interest and dividend income of \$8,000.
 - Gross wages of \$100,000
 - Margin interest of \$10,000
 - Mortgage interest of \$6,000
 - Interest on a mobile home used as a second home \$3,000
 - Credit card interest of \$2,000.
- How much interest can George deduct on Schedule A?
- A. \$21,000.
 - B. \$18,000.
 - C. \$17,000.
 - D. \$19,000.
- 71.** Chester and Mary, a married couple, have interest and dividends (investment income) of \$14,000. They have margin interest of \$16,000, home mortgage interest of \$12,000, equity loan interest of \$3,000 on a \$50,000 loan, credit card interest of \$4,500 and automobile loan interest of \$2,000. They have no tax-exempt investments. What amount can they take as interest deductions after limitations?
- A. \$29,000.
 - B. \$52,500.
 - C. \$31,000.
 - D. \$37,500.
- 72.** If the taxpayer makes a contribution by cash, check, credit card or payroll deduction to a qualified organization, what record of the contribution is the taxpayer required to obtain from the organization?
- A. If the amount is for some item or service, like a charity dinner, and over \$100, the taxpayer must have a separate acknowledgement for each contribution.
 - B. For annual payroll deductions over \$250, the taxpayer must have a separate acknowledgement for each contribution.
 - C. Weekly contributions of \$50 to the taxpayer's church must have a separate acknowledgement for each contribution.
 - D. For contributions under \$250, the taxpayer must keep an account, statement, receipt or other reliable written record.

73. Alona is a student, and her personal car was stolen in May, 2002. It was found several days later severely damaged. The decrease in fair market value (less than her adjusted basis) was \$3,500. In addition, a personal lap top computer in the car at the time was never recovered (fair market value \$500, also less than her adjusted basis). What is the amount and treatment of the casualty loss after considering the \$100 minimum floor, but before the AGI limitation?
- Schedule A loss of \$3,800 for the car and computer.
 - Schedule D loss of \$3,500 for the car and a Schedule A loss of \$500 for the computer.
 - Schedule A loss of \$3,900 for the car and the computer.
 - Schedule D loss of \$4,000 for the car and the computer.
74. During the year, Ron paid \$85 to have his tax return prepared. He also paid a lawyer \$215 to prepare his will. At work, he paid union dues of \$650, bought safety boots for \$200, and contributed \$75 to collections for sick co-workers. What is Ron's miscellaneous deduction on his Schedule A, before the 2% limitation?
- \$935.
 - \$1,010.
 - \$1,150.
 - \$1,225.
75. Paula won \$5,000 in the lottery in 2002. She also won \$200 playing bingo at her lodge hall. She is not a professional gambler. She kept meticulous records of the \$6,550 she spent on gambling expenses. How much may she deduct on her Schedule A, as a miscellaneous deduction not subject to the 2% limitation.
- \$0.
 - \$200.
 - \$5,200.
 - \$6,550.
76. Zach and Myra have four children ranging in age from two to ten. Zach has wages of \$80,000 and Myra \$25,000. Two of the children went to Child Nursery School, Inc. at a total cost of \$8,000. The two older children attended a qualified after-school program that costs \$2,500. What amount of childcare expenses can be used to determine the credit on their 2002 return?
- \$10,500.
 - \$2,500.
 - \$4,800.
 - \$6,000.
77. Ruth had wages of \$34,000 and her husband John's wages were \$27,000. They have three children ages 3, 6 and 9. They paid a total of \$6,000 to Creative Child Care School, Inc. Assuming a 20% credit rate, what will be their child care **credit**?
- \$960.
 - \$1,200.
 - \$6,000.
 - \$4,800.
78. Liz has adjusted gross income of \$65,000, no foreign source income and a tax before credits of more than \$3,000. Her dependents include her son Ben, who turned 17 in September 2002, her daughter, Sheila, who is 12 and her niece, Abigail, who is 6. All of the children are U.S. citizens and lived with her all year. What is the amount of child tax credit she may claim on her 2002 return filed April 15, 2003?
- 0.
 - \$600.
 - \$1,200.
 - \$1,800.
79. Jerry has two dependent children, Greg and Mandy, who are attending an accredited college in 2002. Greg is a senior who spent \$7,000 for tuition and fees. Mandy, a freshman with no prior post-secondary education, had tuition expenses of \$4,000. Jerry meets all the income and filing status requirements for the education credits. There is no tax-free assistance to pay these expenses. Jerry's tax liability before credits equals \$14,000. What is the maximum credit that Jerry may claim on his 2002 tax return?
- \$2,200 Lifetime Learning Credit.
 - \$3,000 Hope Credit.
 - \$1,500 Hope Credit and \$1,000 Lifetime Learning Credit.
 - \$1,500 Hope Credit and \$1,400 Lifetime Learning Credit.
80. Mildred and John purchased 40 acres of undeveloped land in 1960 for \$120,000. They paid personal real estate taxes of \$50,000, which they elected to add to the property's basis. They sold the property for \$600,000, having total settlement costs of \$70,000. The settlement costs are allowable as an expense of sale. Mildred and John received a down payment of \$100,000 with the balance to be paid over 15 years. What is their gross profit percentage?
- 60%
 - 72%
 - 68.33%
 - 82%

