

Part 2

Section A:

Questions 1-20

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

1. The date a sole proprietorship begins business determines the tax year on which it must file its returns.
2. Ray Johnson operates a retail store using the accrual method of accounting and reporting on Schedule C, Net Profit or Loss from Business. He plans to start a lawn-care service to operate only in the summer months. The lawn-care business must use the accrual method of accounting because he has already elected this method for his other business and all businesses operated by one individual must use the same method of accounting.
3. If a group of trade or business assets is acquired, the purchase price is allocated to the various assets in proportion to their fair market value on the purchase date. The allocation can be made in any order as long as it does not exceed the fair market value of the assets.
4. During 1998, the city changed the street in front of Keith's store into an enclosed mall. Keith and other affected property owners were assessed by the city for the cost of the conversion. Keith can deduct the assessment as a tax expense on his 1998 return.
5. Carol owns a dress shop and employs three people full time. In December 1998, Carol paid bonuses to the three employees in addition to their regular salaries. The bonuses were reasonable and for service performed. She intended the bonuses as additional pay for their services. The bonuses consisted of property and cash. Carol may deduct the entire amount of bonuses paid.
6. The employer provided meals and lodging for 100 employees at the work place for the convenience of the employer and as a condition of employment. The cost can be excluded from the employees' wages and deducted as an expense by the employer.

7. The non-accrual experience method of accounting for bad debts means that income is not accrued by an accrual-basis taxpayer if the taxpayer expects the account receivable to be uncollectible.
8. Dues for membership in a country club that provides meals under circumstances generally considered being conducive to a business discussion are deductible, subject to the 50% limitation.
9. Joe gave one of his customers a ticket to a hockey game. He did not attend the game with the customer. The cost of the ticket can be treated either as a gift expense or an entertainment expense.
10. Michael borrowed \$50,000 to pay his father's medical bills and to purchase a milling machine for his tool and die business. The assets of the business secured the loan. Michael can deduct all the interest on the loan as a business expense.
11. Any amount paid or incurred to demolish a structure or any loss for the undepreciated basis of a demolished structure cannot be deducted.
12. Rob was contracted to construct a swimming pool. There was a clause in the contract that stated if the pool was not finished by June 1, 1998, Rob would have to pay a penalty of \$100 a day until the pool was completed. The pool was completed on July 1, 1998 and Rob paid the penalty on that date. He can deduct this as an expense in 1998.
13. If, in a like-kind exchange, money or unlike property is received in addition to like-kind property, then all of the realized gain becomes taxable.
14. In a nontaxable exchange, if Mary assumes any of John's liabilities, or if John transfers property subject to a liability, John will be treated as if he received cash in the amount of the liability.
15. When like-kind properties are exchanged and no gain or loss is recognized, no report of the transaction should be made on the tax return.
16. Spouses who carry on a business together and share in the profits and losses, but do not have a formal partnership agreement, may report income or loss from the business either on a U. S. Partnership Return of Income (Form 1065) or on separate Schedules C (Form 1040) in the name of each spouse.
17. Members of a family who work together will be recognized as partners only if their invested capital is a material income-producing factor.

18. The rule that neither the partner nor the partnership recognizes a gain or loss when property is contributed to the partnership in exchange for a partnership interest applies only at the time when the partnership is being formed.
19. The adjusted basis of the partnership interest is determined without considering any amount shown in the partnership books as a capital, equity or a similar account.
20. Form 2290 is used to report the excise tax on certain trucks with taxable gross weights of 55,000 pounds or more that are used on public roads.

Section B:

Questions 21 - 45

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

21. Which of the following accounting changes do not require the filing of Form 3115 to request a change in accounting method?

- A. Correction of a math error.
- B. Change from accrual method to cash method.
- C. Change in the method inventory is valued.
- D. Change from cash method to accrual method.

22. All of the following "Section 197 intangibles" acquired after August 10, 1993, must be amortized over 15 years **except**:

- A. A covenant not to compete entered in connection with the acquisition of an interest in a trade or business.
- B. A patent that you created, but not in connection with the acquisition of assets constituting a trade or business or a substantial part of a trade or business.
- C. A fast food franchise.
- D. A governmental license including renewals.

23. All of the following items decrease the basis of property **except**:

- A. Casualty or theft loss deductions and insurance reimbursements.
- B. The cost of defending and perfecting a title.
- C. Section 179 deduction.
- D. The exclusion from income of subsidies for energy conservation measures.

24. Peter is an auto mechanic. On Nov. 25, 1998, he made some major auto repairs on Harry's Mercedes. Harry is an attorney. In exchange for the service, Harry is going to draft Peter's will and represent him when he settles on his new house. Harry will perform all of these services in 1999. The repair bill for the Mercedes came to \$1,200. Both Peter and Harry are cash basis taxpayers. How do they report this income?

- A. Both report \$1,200 income in 1998.
- B. Both report \$1,200 income in 1999.
- C. Harry reports \$1,200 in 1998 and Peter reports \$1,200 in 1999.
- D. Peter reports \$1,200 in 1998 and Harry reports \$1,200 in 1999.

25. In which one of the following business situations do the uniform capitalization rules for capitalizing direct and indirect cost of production or resale not apply?

- A. Automobile dealership sells automobiles, average annual gross receipts more than \$10 million
- B. Create baskets and woven crafts for sale; average annual gross \$10 million or less.
- C. Sell office supplies purchased wholesale; average annual gross receipts \$10 million or less.
- D. Produce instructional videos for computer training; average annual gross receipts \$10 million or less.

26. All of the following statements about fringe benefits for 1998 are correct **except**:

- A. An employer can exclude qualified transportation fringe benefits from an employee's wages even if they are provided in place of pay.
- B. An employer cannot use the vehicle cents-per-mile rule to figure the value of an employee's use of an automobile first made available to the employee for personal use in 1998, if the fair market value of the automobile is more than \$15,600.
- C. Employee wages do not include the value of any property or service that has so little value that accounting for it would be unreasonable or administratively impracticable.
- D. An employer can treat all meals furnished to employees on their premises as furnished for the employer's convenience if half of these employees are furnished the meals for a substantial nonpay business reason.

27. Under MACRS the cost of depreciable property is recovered using:
- A. The applicable depreciation method.
 - B. The applicable recovery period.
 - C. The applicable convention.
 - D. All of the above.
28. Which is not a true statement regarding business bad debts?
- A. The debt does not have to be due to be worthless.
 - E. A bad debt can result from a loan to a supplier.
 - C. Cash-basis taxpayers can take a deduction for amounts never received or collected.
 - D. A debt can arise from the guarantee of a debt that becomes worthless.
29. Which of the following statements about deductible travel expenses when attending a convention is true?
- A. The convention agenda does not have to deal specifically with the official duties and responsibilities of your position.
 - B. Appointment or election as a delegate to a convention is sufficient in itself to make that delegates travel expense deductible.
 - C. The daily limit on the amount that can be deducted for a convention held on a cruise ship is the highest federal per diem rate allowable at the time of travel.
 - D. Travel expense for attendance at a conference on investments is deductible if the taxpayer is seeking advice on suitable investments for the production of taxable income.
30. Expenses for travel outside the United States are not allocated between business and personal days when:
- A. A personal vacation was not a major consideration.
 - B. The trip was not more than seven consecutive days.
 - C. At least 75% of the time was spent on business.
 - D. All of the above.

31. All of the following statements about the 50% limit on business-related meal and entertainment expenses are true **except**:

- A. Employees are not subject to the 50% limit if the employer reimburses the employees under an accountable plan and does not treat the reimbursement as wages.
- B. A self-employed accountant is not subject to the 50% limit if he/she was reimbursed and provided the payer with adequate records of the expenses.
- C. The cost of a package deal that includes a ticket to a regular season professional baseball game is not subject to the 50% limit.
- D. A Pizza Parlor's cost in providing free slices of pizza to the public, as a form of advertisement, is not subject to the 50% limit.

32. Which of the following insurance premiums are generally not deductible by a sole proprietorship?

- A. Liability insurance.
- B. Workers' compensation insurance.
- C. Life insurance.
- D. Merchandise and inventory insurance.

33. With respect to Net Operating Losses occurring in 1998, which of the following statements is true?

- A. An NOL attributable to a farming business can be carried back 5 years only if it is attributable to a Presidential declared disaster
- B. If you elect to forgo the carryback period you can carry forward the NOL for 20 years.
- C. The election to forgo the carryback period has no effect on the alternative minimum tax NOL.
- D. All of the above.

34. Ron wants to transfer a table used in his business for another asset and have the exchange qualify as non-taxable to him. Which circumstances will qualify the transaction?

- A. Use the table as a down payment on a business vehicle.
- B. Trade the table for a desk to be used in the business office.
- C. Apply the table as a payment on the rent for the business office space.
- D. Give the table to an employee in lieu of salary.

35. Qualified small business stock, for purposes of applying rollover and exclusion rules, is stock that meets all the following tests except:

- A. Stock in a C corporation.
- B. Originally issued after August 10, 1993.
- C. Acquired by original issue in exchange for money or other property or as pay for services.
- D. Total gross assets of \$100,000,000 or less at all times after August 10, 1993 and before it issued the stock.

36. Which of the following is not section 1245 property?

- A. Computer.
- B. Office building.
- C. Display shelving.
- D. Covenant not to compete.

37. Which of the following dispositions of depreciable property would trigger recapture?

- A. Installment sale.
- B. Gift.
- C. Transfer at death.
- D. Tax-free exchange where no money or unlike property is received.

38. For purposes of the estimated tax for qualified farmers, all of the following statements are true except:

- A. A qualified farmer does not have to make any estimated payments if he files by the first day of the third month after the close of the tax year and pays 100% of the previous year's taxes with the return.
- B. You are a qualified farmer if at least two-thirds of your previous year's gross income is from farming.
- C. The required annual payment is due on the 15th day after the close of the tax year.
- D. The required annual payment is two-thirds of your current year's tax or 100% of the previous year's tax.

39. Which of the following organizations formed after 1996 cannot be classified as a partnership?

- A. An insurance company.
- B. A tax-exempt organization.
- C. A real estate investment trust.
- D. All of the above.

40. Rose and Irene each have a 50% interest in a partnership that started business on July 1. Rose uses a calendar year while Irene has a fiscal year ending November 30. Which of the following is correct?

- A. The partnership may also use the calendar year because at least 50% is owned by a calendar year taxpayer.
- B. The partnership must use the fiscal year ending November 30 because it results in a deferral of 11 months.
- C. The partnership must use the fiscal year ending November 30 because it results in a deferral of 1 month.
- D. The partnership may use either the calendar year or fiscal year ending November 30 because each partner owns an equal percentage.

41. Maggie and Simon each have a 50% interest in a partnership that started business October 1. Maggie uses a calendar year while Simon has a fiscal year ending November 30. Which of the following is correct?

- A. The partnership may use the fiscal year ending September 30 provided a section 444 election and payment are made.
- B. The partnership may use the fiscal year ending November 30th as that results in the least deferral.
- C. The partnership may use the calendar year.
- D. A & B above are both correct.

42. Ted and Jane form a cash basis general partnership with cash contributions of \$20,000 each. They share all partnership profits and losses equally. They borrow \$60,000 and purchase depreciable business equipment. Jane, however, is required to pay the creditor if the partnership defaults. Which of the following is correct?

- A. Ted and Jane each have a basis of \$80,000 in the partnership.
- B. Ted has a basis of \$50,000, and Jane has a basis of \$80,000.
- C. Ted and Jane each have a basis of \$50,000 in the partnership.
- D. Ted has a basis of \$20,000 and Jane has a basis of \$80,000 in the partnership.

43. Which of the following statements about the effect of a sale or exchange of a partner's interest in a partnership is correct?

- A. The entire transaction is always treated as the sale of a capital asset.
- B. The partnership may make an election for an optional adjustment to the basis of partnership assets in the year the interest is transferred.
- C. The exchange of a partnership interest generally qualifies for like-kind exchange treatment.
- D. The gain on the sale of a partnership interest may not be reported on the installment basis.

44. Which of the following statements about payments made to a retiring partner or successor in interest of a deceased partner that are not made in exchange for an interest in the partnership property is correct?

- A. Payments made within five years of the partner's retirement or death are always treated as made in exchange for an interest in the partnership property.
- B. Payments made within five years of the partner's retirement or death are always treated as distributive shares of partnership income.
- C. If the amount of the payment is based on partnership income, the payment is taxable as a distributive share of partnership income.
- D. If the amount of the payment is based on partnership income, the payment is treated as a guaranteed payment.

45. Which type of income is not subject to self-employment tax?

- A. Wages, salaries, and tips received as an employee.
- B. Non-employee compensation.
- C. Net profits from sole proprietorship.
- D. Distributive share of partnership income.

Section C:

Questions 46 - 80

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

46. John is a cash basis taxpayer. He received the following items of income in Dec. 1998:

1. The loan on his truck was forgiven because he performed some accounting work for the dealer. He owed \$2,000 at the time.
2. He received a retainer of \$500 from a new client to guarantee that his services would be available in February when the client would need help preparing financial statements.
3. He finally received the \$800 for work he completed in Nov. of 1997.

How much of this income must John include on his 1998 tax return?

- A. \$ 500
- B. \$1,300
- C. \$2,500
- D. \$3,300

47. Williams Manufacturing has the following account information at year-end. Compute ending inventory.

Physical inventory at 12-31 at cost, all accounts	\$ 300,000
Reserve for estimated depreciation of inventory	\$ 15,000
Stock shipped FOB destination 12-30	\$ 5,000
Raw materials ordered 12-20, invoiced and payable (Not yet received)	\$ 10,000

- A. \$300,000
- B. \$305,000
- C. \$310,000
- D. \$315,000

48. Jack Roston operates a small manufacturing business as a sole proprietorship. His business, Roston Rubber, manufactures industrial rubber seals and also makes rubber bands used in packaging. He uses the accrual method of accounting. He incurred the following expenses during 1998. What was his cost of goods sold? (Disregard uniform capitalization rules for this computation.)

Beginning inventory, raw materials	\$ 14,000
Beginning inventory, work in process	\$ 20,000
Beginning inventory, finished goods	\$ 100,000
Ending inventory, raw materials	\$ 15,000
Ending inventory, work in process	\$ 12,000
Ending inventory, finished goods	\$ 110,000
Purchases	\$2,000,000
Salaries, factory	\$ 200,000
Salaries, sales	\$ 50,000
Chemicals used in manufacturing process	\$ 10,000
Office supplies	\$ 5,000
Freight-in on raw material purchases	\$ 3,000

- A. \$2,210,000
- B. \$2,207,000
- C. \$2,268,000
- D. \$2,265,000

49. On July 1, 1998, Mel leased property for 2 years for \$700 a month. On September 30, 1998, the owner of the property told him if he paid the total in advance for the remainder of the lease the rent would be reduced to \$675 a month. Mel accepted his offer and on October 1, 1998, he paid the owner \$14,175. How much can Mel deduct as rental expense in 1998?

- A. \$2,025
- B. \$4,050
- C. \$4,125
- D. \$16,300

50. Juliet bought and placed in service computer equipment in 1998. She paid \$10,000 and received a \$2,000 trade-in allowance for her old computer equipment. She had an adjusted basis of \$3,000 in the old computer equipment. Juliet used both the old and new equipment 90% for business and 10% for personal purposes. Her allowable Section 179 expense deduction is:

- A. \$12,000
- B. \$10,800
- C. \$10,000
- D. \$ 9,000

51. Several years ago Nia paid \$160,000 to have her home built on a lot that cost her \$10,000. Before changing the property to rental use last year, she paid \$20,000 for permanent improvements to the house and claimed a \$2,000 casualty loss deduction for damage to the house. On the date of change in use, her property has an FMV of \$180,000, of which \$30,000 is for the land and \$150,000 is for the house. Her depreciable basis for the house is:

- A. 180,000
- B. 178,000
- C. 160,000
- D. 150,000

52. In 1997, the Hydrangea Company (a sole proprietorship) had gross income of \$158,000, a bad debt deduction of \$3,500, and other allowable deductions of \$49,437. The business reported on the accrual method of accounting and used the specific charge-off method for bad debts. The entire bad debt deduction reduced the taxable income on the 1997 return. In 1998, the business recovered \$2,000 of the \$3,500 deducted in 1997. How should the recovery be treated?

- A. Include \$2,000 in income on the 1998 return.
- B. Include \$3,500 in income on the 1998 return.
- C. Amend the 1997 return to add the \$2,000.
- D. None of the above.

53. Basil Company, a cash basis taxpayer, had the following activity during 1998:

Sales-1998, uncollected	\$ 40,000
Sales-1998, collected	\$1,000,000
Total Sales - 1998	\$1,040,000
Collections on 1997 bad debt	\$ 50,000

What is the correct amount of income to be reported for 1998?

- A. \$1,040,000
- B. \$1,000,000
- C. \$1,050,000
- D. \$1,090,000

54. Lisa traveled from Philadelphia to New York on a business trip for her employer. She is not reimbursed for the travel expenses. Lisa spends two days in business meetings and one day on vacation. Lisa's meals cost \$90 (\$30 per day), lodging costs \$360 (\$120 per day), and train fare costs \$102. What is the total amount of Lisa's business related travel expense?

- A. \$366
- B. \$372
- C. \$507
- C. \$552

55. On New Year's Eve, Hal sent three bottles of champagne to the three owners of the Day & Night Cleaners to thank them for their business during the year. Each bottle of champagne cost \$75. Each of the owners took the champagne home. Earlier in the year, Hal had given a video game to the son of one of the owners. The value of the game was \$50. To show his appreciation to another customer for his business, Hal took the customer to a football game. The value of the tickets was \$100. What is the total amount Hal can deduct as business gifts?

- A. \$375
- B. \$100
- C. \$125
- D. \$ 75

56. Manuel paid the following amounts in 1998 for interest:

1. \$1,000 interest on a loan used to buy a new computer used 80% for business.
2. \$2,000 interest on a construction loan for his new business location, to be completed in May 1999.
3. \$10,000 interest on a 2nd mortgage on his home. The original loan amount was \$100,000; \$50,000 was used to make improvements to his home, \$25,000 was spent on a new truck for the business and the remainder was invested in tax-exempt bonds.

Compute Manuel's business interest deduction for 1998.

- A. \$3,300
- B. \$5,300
- C. \$5,800
- D. \$7,800

57. Sam Sheffield operates a café and files his returns on a calendar-year basis. He bought a fire insurance policy on the café building effective October 1, 1997 and paid a premium of \$3,600 for 2 years of coverage. On Sam's 1998 return, how much of the premium can he deduct for 1998?

- A. \$0
- B. \$3,150
- C. \$2,400
- D. \$1,800

58. Ida is engaged in a not-for-profit activity. The income and expenses of the activity are as follows:

Gross income.....	\$3,200
Less expenses:	
Real estate tax.....	\$700
Home mortgage interest.....	900
Insurance.....	400
Utilities.....	700
Maintenance.....	200
Depreciation on an automobile.....	600
Depreciation on a machine.....	<u>200</u>
Total expenses	<u>\$3,700</u>
Loss	\$ 500

The amount of allowable depreciation for the automobile is

- A. 600
- B. 300
- C. 225
- D. None of the above

59. Paula owns and operates a small flower shop that generated a \$5,000 loss in 1998. She sold some of the land she uses for the business at a \$2,000 gain and some stock she had inherited at a \$1,000 loss. She also earned \$1,225 from her part time job as an usher at the local Movie Theater. Her bank personal savings account earned \$425 in interest in 1998. Paula files as single and claims the standard deduction. Her exemptions and standard deduction amounts for 1998 are \$2,700 and \$4,250 respectively. Her net operating loss for 1998 is:

- A. \$1,775
- B. \$2,350
- C. \$5,000
- D. \$9,300

60. Charlie Croker exchanged real estate held for investment that had an adjusted basis of \$8,000 for other real estate that he will hold for investment. The property given up was subject to a \$3,000 mortgage. The real estate he received had a fair market value of \$10,000. Charlie also received \$1,000 in cash from which he paid \$500 in exchange expenses. He realized a gain on the exchange. How much of the gain is taxable?

- A. \$5,500
- B. \$6,000
- C. \$4,000
- D. \$3,500

61. Maria Mordant acquired all of the original stock of The Diamond, Inc., a Section 1244 small business, on January 10, 1994 for \$10,000. She contributed another \$9,000 to capital before selling all of her stock on June 30, 1998 for \$10,000. How much loss should Maria report on her 1998 return and is the loss capital or ordinary?

- A. Deduct \$4,737 as ordinary loss and \$4,263 as capital loss subject to limitations.
- B. Deduct \$3,000 of her loss on Schedule D as a capital loss and carryover the remainder.
- C. Deduct her \$9,000 loss as an ordinary loss.
- D. None of the above.

62. Sam files a calendar year return. In February 1996, he purchased and placed in service for 100% use in his business a light-duty truck (5-year property) for a cost of \$10,000. He used the half-year convention and figured his MACRS deductions for the truck were \$2,000 in 1996 and \$3,200 in 1997. He did not take the section 179 deduction on it. He sold the truck in May 1998 for \$7,000. The MACRS deduction in 1998, the year of sale, is \$960 (1/2 of \$1,920). How much of the gain will be treated as ordinary income in 1998?

- A. \$3,160
- B. \$2,200
- C. \$3,840
- D. None of the above

63. Gwen owned a duplex and lived in one-half. The other half was rental property. The cost of the property was \$80,000, of which \$70,000 was allocated to the building and \$10,000 to the land. She added an improvement to the half she lived in that cost \$10,000. In 1998, the property was condemned by the city. Up to that time she had allowed/allowable depreciation of \$23,000. The city paid Gwen \$90,000, and she bought another duplex for \$85,000. Gwen lived in one-half and the other half is a rental. What is the basis of the replacement property?

- A. \$73,000
- B. \$62,000
- C. \$60,000
- D. \$55,000

64. Josh is a cattle farmer who uses the cash method of accounting. He files his returns on a calendar year basis. Normally, he sells 100 head of beef cattle a year; however, as a result of drought he had to sell 135 head during 1998. He realized \$35,100 from the sale. On August 9, 1998, due to the drought, Josh's area was declared eligible for federal assistance. How much of the income from the sale of the cattle can Josh defer until 1999?

- A. None
- B. \$9,100
- C. \$26,000
- D. \$35,100

65. Betsy is a dairy cow raised on Ronald's Dairy Farm. On Dec. 26, 1998, Ronald sold Betsy for \$3,800. He incurred \$300 in transportation expenses that were included in the sales price. Ronald estimates that Betsy cost \$2,000 for food and other expenses to raise her. He deducted these expenses. What is Ronald's gain from the sale of Betsy.

- A. \$1,500
- B. \$1,800
- C. \$3,500
- D. \$3,800

66. ABC is a calendar year partnership with three partners, Alan, Bob and Cathy. The profits and losses are shared in proportion to each partner's contributions. On January 1, the ratio was 90% for Alan, 5% for Bob, and 5% for Cathy. On December 1, Bob and Cathy each contributed additional amounts and the new profit and loss sharing ratios were 30% for Alan, 35% for Bob, and 35% for Cathy. For its tax year ended December 31, the partnership had a loss of \$1,200. This loss occurred equally over the partnership's tax year. How is the loss allocated?

- A. Alan \$720, Bob \$240, Cathy \$240
- B. Alan \$360, Bob \$420, Cathy \$420.
- C. Alan \$1,020; Bob \$90; Cathy \$90.
- D. Alan \$1080, Bob \$60, Cathy \$60.

67. David and Robert form an equal partnership. David contributed \$10,000 cash to the partnership and Robert contributed depreciable property with a fair market value of \$10,000 and an adjusted basis of \$4,000. What is the partnership's basis for depreciation of the property and how is the depreciation deduction allocated among the partners (assuming the depreciation rate is 10% per year)?

<u>Partnership's Basis for Depreciation</u>	<u>Annual Depreciation Deduction</u>	
	<u>David's Share</u>	<u>Robert's Share</u>
A. \$4,000	\$200	\$200
B. \$4,000	\$400	\$0
C. \$4,000	\$0	\$400
D. \$10,000	\$500	\$500

68. Doug sold 50% of his business to his son, Ben. The resulting partnership had a profit of \$60,000. Capital is a material income-producing factor. Doug performed services worth \$24,000, which is reasonable compensation, and Ben performed no services. What is the maximum amount of profit that Ben can report from the partnership for the tax year?

- A. \$30,000
- B. \$36,000
- D. \$12,000
- E. \$18,000

69. Andrew is a 40% partner in the ABC Partnership, in which capital is a material income-producing factor. He gives one-half of his interest to his brother, John. During the current year, Andrew performs services for the partnership, for which reasonable compensation is \$65,000, but for which he accepts no pay. Andrew and John are each credited with a \$100,000 distributive share of the partnership's ordinary income. How much should Andrew report?

- A. \$132,500
- B. \$100,000
- C. \$67,500
- D. \$105,000

70. In 1998, Barb and Bet Partnership sold land having a \$45,000 basis to the PTA Partnership for \$35,000. Pat has a 55% capital and profits interest in the PTA Partnership, and his sister owns 60% of Barb & Bet Partnership. In 1999 the PTA Partnership sells the land to an unrelated individual for \$47,000. How much gain or loss should Barb and Bet Partnership recognize on the subsequent sale of the land?

- A. 1998: \$ -0- 1999: \$2,000 gain
- B. 1998: \$10,000 loss 1999: \$- 0 -
- C. 1998: \$ -0- 1999 \$12,000 gain
- D. 1998: \$ -0- 1999 \$ - 0 -

71. Ted owns a 60% interest in Alpha Partnership and a 55% interest in Beta Partnership. In August 1998, Alpha sold land to Beta for \$85,000. The land had a basis to Alpha of \$100,000. In September 1998, Beta sold the land to an unrelated individual for \$125,000. How much gain or loss must Beta recognize for 1998?

- A. \$15,000 loss
- B. \$ -0-
- C. \$25,000 gain
- D. \$40,000 gain

72. Dianne owns 10% interest in DJJ Partnership and 20% of the outstanding stock of PAD Corporation. Her son, Nick, owns 60% of the outstanding shares of shares of PAD Corporation. The PAD Corporation owns 50% interest in the DJJ Partnership. Dianne's sister, Dolores, owns 40% interest in the DJJ Partnership. Using the constructive ownership rules for partnerships, Dianne is considered to own how much of DJJ Partnership?

- A. 80%
- B. 50%
- C. 90%
- D. 20%

73. Arthur is to receive 30% of partnership income, but not less than \$5,000. The partnership has net income of \$10,000 before any allocation. How much income should the partners report?

	Arthur Guaranteed Payment	Other partners total Distributive Share	Distributive share
A.	\$5,000	\$1,500	\$3,500
B.	\$5,000	\$3,000	\$2,000
C.	\$ -0-	\$3,000	\$7,000
D.	\$2,000	\$3,000	\$5,000

74. In return for a 20% partnership interest, Kathy contributed land having a \$60,000 fair market value and a \$30,000 basis to the partnership. The partnership assumes Kathy's \$15,000 liability arising from her purchase of the land. The partnership's liabilities arising from its purchases of assets is \$4,000 immediately prior to the contribution. What is Kathy's basis in her partnership interest?

- A. \$18,800
- B. \$30,000
- C. \$15,000
- E. \$15,800

75. Earl acquired a 20% interest in a partnership by contributing property that had an adjusted basis to him of \$8,000 and that was subject to a mortgage of \$12,000. Which of the following results is correct?

<u>Capital Gain Recognized</u>	<u>Basis of Partnership Interest</u>
A. \$1,600	\$1,600
B. - 0 -	(\$1,600)
C. \$4,000	\$8,000
D. \$1,600	- 0 -

76. The adjusted basis of Stan's partnership interest is \$15,000. He receives a distribution of cash of \$6,000 and property with an adjusted basis to the partnership of \$11,000. (This was not a distribution in liquidation.) What is the basis of the distributed property in Stan's hands?

- A. \$ 9,000
- B. \$11,000
- C. \$ 5,000
- D. \$17,000

77. On January 1, 1998, Ruth had a basis in her partnership interest of \$55,000. Thereafter, in liquidation of her entire interest, she received an apartment house and

an office building. The apartment house has an adjusted basis to the partnership of \$5,000 and a fair market value of \$40,000. The office building has an adjusted basis to the partnership of \$10,000 and a fair market value of \$10,000. What is Ruth's basis in each property after the distribution?

- A. Apartment house, \$40,000, Office building, \$15,000
- B. Apartment house, \$44,000, Office building, \$11,000
- C. Apartment house, \$25,000, Office building, \$30,000
- D. Apartment house, \$45,000, Office building, \$10,000

78. Scott became a limited partner in the S&N Partnership with a \$10,000 contribution on the formation of the partnership. The adjusted basis of his partnership interest at the end of the current year is \$20,000, which includes his \$15,000 share of partnership liabilities. He had been paid his share of the partnership income for the year. There are no unrealized receivables or inventory items. Scott sells his interest in the partnership for \$10,000. Which of the following is correct?

- A. \$5,000 ordinary income
- B. \$5,000 capital gain
- C. \$10,000 ordinary loss
- D. \$25,000 capital gain

79. Tracy has a one-fourth interest in the TANY Partnership. The adjusted basis of his interest at the end of the current year is \$30,000. He sells his interest in the TANY Partnership to Roy for \$50,000 cash. There was no agreement between Tracy and Roy for any allocation of the sales price. The basis and fair market value of the partnership's assets (there are no liabilities) are as follows:

<u>Assets</u>	<u>Basis</u>	<u>Fair Market Value</u>
Cash	\$40,000	\$40,000
Unrealized Receivables	\$ - 0 -	\$36,000
Inventory	\$40,000	\$92,000
Land	<u>\$40,000</u>	<u>\$32,000</u>
Total	\$120,000	\$200,000

What is the amount and character of Tracy's gain or loss?

- A. \$ - 0 - ordinary income, \$ - 0 - capital gain
- B. \$20,000 ordinary income, \$ -0- capital gain
- C. \$10,000 ordinary income, \$10,000 capital gain
- D. \$22,000 ordinary income, \$2,000 capital loss

80. Michael operates his health food store as a sole proprietorship out of a building he owns. Based on the following information regarding 1998, compute his net self-employment income (for SE tax purposes) for 1998.

Gross receipts	\$100,000
Cost of Goods Sold	\$ 49,000
Utilities	\$ 6,000
Real estate taxes	\$ 1,000
Gain on sale of business truck	\$ 2,000
Depreciation expense	\$ 5,000
Section 179 expense	\$ 1,000
Mortgage interest on building	\$ 7,000
Contributions to Keogh retirement plan	\$ 2,000
Net operating loss from 1997	\$ 10,000

- A. \$14,000
- B. \$16,000
- C. \$24,000
- D. \$31,000