

Full-Length Practice Test 7

Instructions: This practice test contains 300 multiple-choice questions divided into three parts. Select the best answer for each question

Part 1: Individuals

1. Married taxpayers must file jointly or separately if living together unless:
 - A. Over 65
 - B. Different incomes
 - C. One is blind
 - D. Legally separated

2. Qualifying surviving spouse status is available for:
 - A. 2 years after spouse's death
 - B. 1 year only
 - C. 3 years maximum
 - D. Permanent

3. Unmarried taxpayers with dependent parents living elsewhere can file as:
 - A. Single
 - B. Qualifying surviving spouse
 - C. Head of household
 - D. Married filing separately

4. Dependents cannot claim:
 - A. Credits
 - B. Personal exemption deduction
 - C. Standard deduction
 - D. Earned income

5. Form W-4 determines:
 - A. Withholding amount
 - B. Tax liability
 - C. Refund amount
 - D. Filing status

6. Nonresident aliens married to U.S. citizens can elect to be taxed as residents if filing:
 - A. Separately

- B. Single
 - C. Head of household
 - D. Joint return
7. Social Security number applications for dependents use Form:
- A. W-7
 - B. W-9
 - C. SS-5
 - D. SS-4
8. Adoption taxpayer identification numbers are used when:
- A. Child is foreign
 - B. SSN not yet available
 - C. Parents unmarried
 - D. Adoption pending
9. Multiple support agreements allow one person to claim exemption when:
- A. Contributing most
 - B. Oldest contributor
 - C. Designated contributor
 - D. Together provide over 50%
10. Divorced parents' exemption follows custody unless:
- A. Noncustodial parent has release form
 - B. Court orders otherwise
 - C. Parents agree verbally
 - D. Income levels differ
11. Wages include:
- A. Tips and bonuses
 - B. Gifts from employer
 - C. Reimbursed expenses
 - D. Nontaxable benefits
12. Fringe benefits taxable unless specifically excluded include:
- A. Health insurance
 - B. Parking over \$315
 - C. Personal use of company car
 - D. Achievement awards over \$1,600

13. Employer-provided dependent care assistance excludable up to:
- A. \$3,000
 - B. \$10,000
 - C. \$2,500
 - D. \$5,000
14. Group term life insurance over what amount creates taxable income:
- A. \$25,000
 - B. \$50,000
 - C. \$100,000
 - D. No limit
15. Cafeteria plans allow employees to choose between cash and:
- A. Raises
 - B. Stock
 - C. Vacation
 - D. Qualified benefits
16. Achievement awards deductible by employer and excludable by employee if:
- A. Tangible personal property
 - B. Cash equivalent
 - C. Gift cards
 - D. Securities
17. Qualified employee discounts for services cannot exceed:
- A. Cost
 - B. 25% of price
 - C. 20% of price charged
 - D. \$1,000
18. Working condition fringe benefits are services or property that would be deductible if:
- A. Required
 - B. Employee paid
 - C. Job-related
 - D. Documented
19. No-additional-cost services are excludable if:
- A. Excess capacity exists
 - B. Same service sold
 - C. Employee discount

D. Normal business

20. Adoption assistance programs exclude up to approximately:

- A. \$5,000
- B. \$10,000
- C. \$16,810
- D. \$18,000

21. Health Savings Account contribution limits for self-only coverage in 2024:

- A. \$3,050
- B. \$4,150
- C. \$4,300
- D. \$5,000

22. Catch-up contributions to HSAs for those 55+ add:

- A. \$500
- B. \$1,000
- C. \$1,500
- D. \$2,000

23. Flexible spending account maximum for 2024 is approximately:

- A. \$3,200
- B. \$2,500
- C. \$5,000
- D. \$1,000

24. Qualified transportation fringes monthly limit for 2024:

- A. \$150
- B. \$280
- C. \$230
- D. \$315

25. Moving expense deduction available only for:

- A. Job change
- B. Distance requirement met
- C. Active duty military
- D. All taxpayers

26. Disaster loss deduction requires loss in:

- A. Any disaster

- B. Federally declared disaster
- C. State emergency
- D. Insurance claim

27. Casualty loss personal property deduction requires loss exceeding 10% of AGI plus:

- A. \$250
- B. \$500
- C. \$1,000
- D. \$100

28. Standard mileage rate for medical and moving (military) for 2024:

- A. 21 cents
- B. 67 cents
- C. 14 cents
- D. 18 cents

29. Charitable mileage rate:

- A. 67 cents
- B. 21 cents
- C. 14 cents
- D. Variable

30. Standard mileage rate for business use for 2024:

- A. 58 cents
- B. 67 cents
- C. 70 cents
- D. 65.5 cents

31. Alimony paid under pre-2019 agreements is:

- A. Deductible by payor
- B. Not deductible
- C. Partially deductible
- D. Credit eligible

32. Child support payments are:

- A. Deductible
- B. Taxable to recipient
- C. Partially deductible
- D. Not deductible

33. Interest on U.S. savings bonds used for education may be:
- A. Fully taxable
 - B. Excluded if income limits met
 - C. Deferred
 - D. Tax credit eligible
34. Dividend income from mutual funds on Form 1099-DIV includes:
- A. Only ordinary dividends
 - B. Interest
 - C. Ordinary and qualified dividends
 - D. Capital gains only
35. Qualified dividends are taxed at:
- A. Ordinary rates
 - B. 28%
 - C. 25%
 - D. Capital gains rates
36. Series I savings bond interest is:
- A. Tax-deferred until redeemed
 - B. Taxed annually
 - C. Tax-exempt
 - D. Subject to AMT
37. Series EE bonds issued after 1989 for education can exclude interest if used for:
- A. Any expense
 - B. Tuition and fees
 - C. Room and board
 - D. Books only
38. Tax-exempt interest must be reported on return even though:
- A. Taxable for AMT
 - B. Not taxed
 - C. Not taxable
 - D. Reduces deductions
39. Kiddie tax applies to unearned income of children under:
- A. 19 or students under 24
 - B. 21
 - C. 18 only

D. 24

40. Net unearned income threshold for kiddie tax in 2024:

- A. \$1,300
- B. \$2,600
- C. \$1,150
- D. \$2,500

41. Capital asset holding period for long-term treatment exceeds:

- A. 6 months
- B. 18 months
- C. 12 months
- D. 24 months

42. Net capital loss deduction limit per year:

- A. \$1,500
- B. \$3,000
- C. \$5,000
- D. Unlimited

43. Capital loss carryforward period:

- A. 5 years
- B. 10 years
- C. 20 years
- D. Indefinite

44. Collectibles capital gain maximum rate:

- A. 28%
- B. 20%
- C. 25%
- D. 15%

45. Section 1250 unrecaptured gain taxed at maximum:

- A. 15%
- B. 20%
- C. 25%
- D. 28%

46. Wash sale rule applies when substantially identical securities purchased within:

- A. 60 days

- B. 30 days before or after
- C. 90 days
- D. 30 days after

47. Constructive sales occur when taxpayer enters offsetting position eliminating:

- A. Risk of loss and opportunity for gain
- B. Basis
- C. Holding period
- D. Cost

48. Mark-to-market election for traders requires annual recognition of:

- A. Realized gains only
- B. Realized losses only
- C. Ordinary income only
- D. Unrealized gains and losses

49. Qualified opportunity fund investment can defer gain until:

- A. Sale of QOF interest
- B. 2030
- C. December 31, 2026
- D. 10 years

50. Installment sale income recognition uses:

- A. Cash method
- B. Gross profit percentage
- C. Accrual method
- D. Fair market value

51. Like-kind exchange treatment under Section 1031 applies to:

- A. Personal property
- B. Securities
- C. Inventory
- D. Real property

52. Boot received in like-kind exchange is:

- A. Taxable
- B. Tax-free
- C. Deferred
- D. Ordinary income

53. Related party exchanges require holding property for:
- A. 1 year
 - B. 6 months
 - C. 2 years
 - D. 3 years
54. Involuntary conversion replacement period for condemned property:
- A. 1 year
 - B. 2 years
 - C. 3 years
 - D. 4 years
55. Home sale exclusion requires ownership and use as principal residence for:
- A. 2 of last 5 years
 - B. 1 of last 3 years
 - C. 3 of last 5 years
 - D. 5 years
56. Home sale exclusion amount for single taxpayers:
- A. \$125,000
 - B. \$500,000
 - C. \$300,000
 - D. \$250,000
57. Married filing jointly home sale exclusion:
- A. \$250,000
 - B. \$300,000
 - C. \$500,000
 - D. \$600,000
58. Partial home sale exclusion available for changes in:
- A. Income
 - B. Employment, health, unforeseen
 - C. Family size
 - D. Market value
59. Rental property converted to personal residence requires use for at least:
- A. 1 year
 - B. 3 years
 - C. 6 months

D. 2 years

60. Self-employment tax rate on net earnings:

- A. 15.3%
- B. 12.4%
- C. 2.9%
- D. 7.65%

61. Self-employment tax Social Security wage base for 2024:

- A. \$147,000
- B. \$160,200
- C. \$168,600
- D. \$200,000

62. Self-employment income includes:

- A. Wages
- B. Net earnings from self-employment
- C. Investment income
- D. Pensions

63. Minister's housing allowance is:

- A. Subject to self-employment tax
- B. Excluded from income tax only
- C. Tax-exempt for all purposes
- D. Subject to FICA

64. Net operating loss carryback for individuals:

- A. 2 years
- B. 3 years
- C. 5 years
- D. Not allowed

65. NOL carryforward limitation is:

- A. 20 years
- B. Indefinite
- C. 10 years
- D. 5 years

66. Excess business loss limitation for 2024 single filers:

- A. \$250,000

- B. \$289,000
- C. \$305,000
- D. \$500,000

67. Alternative minimum tax exemption for 2024 single filers:

- A. \$75,900
- B. \$81,300
- C. \$85,700
- D. \$89,050

68. AMT rate for income above exemption:

- A. 26% and 28%
- B. 24%
- C. 28% only
- D. 20%

69. AMT exemption phase-out begins at approximately for single filers:

- A. \$500,000
- B. \$609,350
- C. \$1,000,000
- D. \$750,000

70. ISO stock option exercise creates AMT preference for:

- A. Exercise price
- B. Fair market value at grant
- C. Spread between FMV and exercise price
- D. Gain on sale

71. Private activity bond interest is:

- A. AMT preference item
- B. Fully taxable
- C. Tax-exempt
- D. Ordinary income

72. Depreciation adjustment for AMT uses:

- A. MACRS
- B. Straight line
- C. Declining balance
- D. 150% declining balance

73. Foreign tax credit is claimed on Form:
- A. 8938
 - B. 1116
 - C. 2555
 - D. 8621
74. Foreign earned income exclusion for 2024 is approximately:
- A. \$100,000
 - B. \$107,600
 - C. \$126,500
 - D. \$150,000
75. Bona fide residence test for foreign earned income exclusion requires residence for:
- A. Full tax year
 - B. 330 days
 - C. 6 months
 - D. 183 days
76. Physical presence test requires presence abroad for:
- A. 365 days
 - B. 183 days
 - C. 11 months
 - D. 330 days in 12 months
77. Foreign housing exclusion applies to amounts exceeding:
- A. Base amount
 - B. \$10,000
 - C. 16% of FEIE
 - D. Housing costs
78. FBAR filing threshold for financial interest in foreign accounts:
- A. \$50,000
 - B. \$10,000
 - C. \$25,000
 - D. \$100,000
79. Form 8938 filing threshold for unmarried taxpayers living in U.S.:
- A. \$25,000
 - B. \$75,000
 - C. \$100,000

D. \$50,000

80. Penalty for failure to file FBAR can reach per violation:

- A. \$10,000 or 50% of account
- B. \$100,000
- C. \$500,000
- D. \$1,000,000

81. Itemized deduction for medical expenses requires exceeding:

- A. 10% of AGI
- B. 2% of AGI
- C. 7.5% of AGI
- D. 5% of AGI

82. Long-term care insurance premium limits are based on:

- A. Policy type
- B. Age
- C. Health status
- D. Income

83. State and local tax deduction limited to:

- A. \$5,000
- B. \$20,000
- C. Unlimited
- D. \$10,000

84. Mortgage interest deduction limited to acquisition debt of:

- A. \$1 million
- B. \$500,000
- C. \$1.5 million
- D. \$750,000

85. Home equity debt interest is deductible if proceeds used to:

- A. Pay personal expenses
- B. Buy car
- C. Improve home
- D. Any purpose

86. Investment interest deduction limited to:

- A. \$3,000

- B. Net investment income
- C. 50% of income
- D. Unlimited

87. Charitable contribution deduction for cash to public charities limited to:

- A. 60% of AGI
- B. 30% of AGI
- C. 50% of AGI
- D. 100% of AGI

88. Charitable contribution of appreciated property held long-term to public charity limited to:

- A. 20% of AGI
- B. 50% of AGI
- C. 60% of AGI
- D. 30% of AGI

89. Qualified charitable distributions from IRAs are limited to:

- A. \$50,000
- B. \$75,000
- C. \$100,000
- D. Unlimited

90. Excess charitable contributions carry forward:

- A. 3 years
- B. 5 years
- C. Indefinitely
- D. 10 years

91. Dependent care credit rate ranges from 20% to:

- A. 30%
- B. 25%
- C. 35%
- D. 50%

92. Child and dependent care credit maximum qualifying expenses for one child:

- A. \$5,000
- B. \$3,000
- C. \$8,000
- D. \$6,000

93. Child tax credit for 2024 is per qualifying child:
- A. \$2,000
 - B. \$3,000
 - C. \$3,600
 - D. \$1,000
94. Additional child tax credit is refundable up to:
- A. \$500
 - B. \$1,000
 - C. \$3,000
 - D. \$1,700
95. Child tax credit phase-out begins for MFJ at:
- A. \$150,000
 - B. \$400,000
 - C. \$200,000
 - D. \$500,000
96. Credit for other dependents is:
- A. \$1,000
 - B. \$2,000
 - C. \$500
 - D. \$1,500
97. Earned income credit maximum number of qualifying children:
- A. 2
 - B. 4
 - C. 5
 - D. 3
98. Premium tax credit reconciliation uses Form:
- A. 8962
 - B. 8965
 - C. 1095-A
 - D. 8941
99. Residential energy credit for qualified expenditures:
- A. 10%
 - B. 26%
 - C. 30%

D. 22%

100. Electric vehicle credit maximum for new vehicles:

- A. \$5,000
- B. \$7,500
- C. \$10,000
- D. \$4,000

Part 2: Businesses

1. Cash method businesses with inventory must account for inventory using:
 - A. Cash method
 - B. Accrual method
 - C. Hybrid method
 - D. Any method

2. Small business taxpayer exemption from inventory accounting applies when average gross receipts don't exceed:
 - A. \$10 million
 - B. \$25 million
 - C. \$29 million
 - D. \$50 million

3. Percentage of completion method applies to:
 - A. Long-term contracts
 - B. Retail sales
 - C. Service businesses
 - D. Manufacturing

4. Completed contract method is generally not allowed except for:
 - A. All contracts
 - B. Retail
 - C. Service
 - D. Small construction contracts

5. Uniform capitalization rules apply to:
 - A. Service providers
 - B. Retailers under \$29 million
 - C. Producers and large retailers
 - D. All businesses

6. UNICAP requires capitalizing:
 - A. Selling expenses
 - B. Direct and indirect production costs
 - C. Administrative costs
 - D. Interest expense

7. Percentage depletion for oil and gas is limited to:
 - A. Cost basis
 - B. 50% of taxable income
 - C. Actual depletion
 - D. 15% of gross income

8. Cost depletion is based on:
 - A. Adjusted basis
 - B. Fair market value
 - C. Replacement cost
 - D. Original cost

9. Section 179 expensing limit for 2024 is approximately:
 - A. \$500,000
 - B. \$1,220,000
 - C. \$2,000,000
 - D. \$3,000,000

10. Section 179 phase-out begins when property placed in service exceeds:
 - A. \$1 million
 - B. \$2 million
 - C. \$3,050,000
 - D. \$5 million

11. Bonus depreciation for 2024 is:
 - A. 0%
 - B. 80%
 - C. 100%
 - D. 60%

12. Luxury auto depreciation first-year limit without bonus depreciation for 2024:
 - A. \$5,000
 - B. \$12,200

- C. \$20,200
- D. \$20,400

13. Heavy SUVs over 6,000 pounds are subject to Section 179 limit of:

- A. \$29,200
- B. Full cost
- C. \$20,200
- D. \$50,000

14. Listed property business use must exceed:

- A. 25%
- B. 75%
- C. 50%
- D. 80%

15. MACRS recovery period for office furniture:

- A. 5 years
- B. 7 years
- C. 10 years
- D. 15 years

16. Residential rental property recovery period:

- A. 27.5 years
- B. 39 years
- C. 31.5 years
- D. 40 years

17. Section 197 intangibles are amortized over:

- A. 5 years
- B. 10 years
- C. 20 years
- D. 15 years

18. Goodwill acquired in business purchase is:

- A. Not amortizable
- B. Expensed
- C. Amortized over 15 years
- D. Depreciated

19. Research and experimentation expenditures for 2024 must be:

- A. Capitalized and amortized
- B. Expensed
- C. Deferred
- D. Credited

20. Startup costs can be deducted up to \$5,000 if total costs don't exceed:

- A. \$10,000
- B. \$50,000
- C. \$100,000
- D. \$25,000

21. Business interest limitation applies when average gross receipts exceed:

- A. \$25 million
- B. \$50 million
- C. \$10 million
- D. \$30 million

22. Business interest deduction limited to 30% of:

- A. Gross income
- B. Net income
- C. Adjusted taxable income
- D. EBITDA

23. Disallowed business interest carries forward:

- A. 5 years
- B. Indefinitely
- C. 20 years
- D. 10 years

24. Meals deduction percentage for 2024:

- A. 50%
- B. 100%
- C. 80%
- D. 75%

25. Entertainment expenses are:

- A. 100% deductible
- B. 50% deductible
- C. Not deductible
- D. Fully deductible if documented

26. Business gifts per recipient limited to:
- A. \$100
 - B. \$50
 - C. \$25
 - D. No limit
27. Hobby loss rule allows deductions only to extent of:
- A. Hobby income
 - B. All income
 - C. Business income
 - D. \$3,000
28. Safe harbor for rental real estate to be trade or business requires:
- A. Rental activity
 - B. 250 hours
 - C. 500 hours
 - D. 100 hours
29. Material participation tests include participating more than:
- A. 250 hours
 - B. 100 hours
 - C. 500 hours
 - D. 750 hours
30. Significant participation activity requires more than 100 hours and all such activities total exceeding:
- A. 250 hours
 - B. 300 hours
 - C. 400 hours
 - D. 500 hours
31. Passive activity loss limitations apply to:
- A. Material participants
 - B. Active businesses
 - C. Portfolio income
 - D. Rental activities and non-material participation
32. Real estate professional status requires more than half of personal services and exceeding:
- A. 750 hours
 - B. 500 hours

- C. 1,000 hours
- D. 250 hours

33. \$25,000 rental loss allowance phases out at AGI between \$100,000 and:

- A. \$125,000
- B. \$200,000
- C. \$150,000
- D. \$175,000

34. Passive activity credits are limited to tax on:

- A. All income
- B. Passive income
- C. Active income
- D. Portfolio income

35. Suspended passive losses are released when:

- A. Activity disposed of
- B. Income generated
- C. 10 years pass
- D. Taxpayer retires

36. At-risk limitations prevent deducting losses exceeding:

- A. Investment
- B. Basis
- C. Income
- D. Amount at risk

37. Qualified nonrecourse financing increases at-risk amount for:

- A. All property
- B. Services
- C. Real property
- D. Personal property

38. Partnership income is reported on:

- A. Form 1065
- B. Form 1120
- C. Form 1120-S
- D. Schedule C

39. Partnership income flows through to partners on:

- A. Form W-2
- B. Schedule K-1
- C. Form 1099
- D. Schedule E

40. Partner basis includes share of partnership:

- A. Assets
- B. Income
- C. Revenue
- D. Liabilities

41. Partner's basis is reduced by:

- A. Income
- B. Contributions
- C. Liabilities assumed
- D. Distributions

42. Guaranteed payments to partners are:

- A. Distributions
- B. Salary equivalent
- C. Ordinary income
- D. Return of capital

43. Special allocations in partnerships must have:

- A. Partner consent
- B. Substantial economic effect
- C. IRS approval
- D. Equal distribution

44. Partnership distributions of cash exceeding basis create:

- A. Ordinary income
- B. No gain
- C. Deferred gain
- D. Capital gain

45. Section 736 payments for deceased partner's interest can be:

- A. Ordinary income
- B. Capital gain
- C. Ordinary or capital depending on type
- D. Tax-free

46. Partnership merger results in continuing partnership when partners own more than:

- A. 50%
- B. 80%
- C. 25%
- D. 75%

47. Partnership technical termination was eliminated for years after:

- A. 2016
- B. 2018
- C. 2020
- D. 2017

48. Partnership tax year must generally conform to:

- A. Calendar year
- B. Majority partners
- C. Principal partners
- D. Fiscal year

49. LLC taxed as partnership files:

- A. Form 1120
- B. Form 1065
- C. Form 1040
- D. Form 1120-S

50. Single-member LLC is by default:

- A. Disregarded entity
- B. Partnership
- C. Corporation
- D. Trust

51. S corporation shareholders are limited to:

- A. 50
- B. 75
- C. 150
- D. 100

52. S corporation stock ownership by partnerships is:

- A. Allowed
- B. Not permitted

- C. Limited
- D. Conditional

53. S corporation can have only one class of stock but voting rights can:

- A. Differ
- B. Be identical only
- C. Vary by shares
- D. Change annually

54. S corporation built-in gains tax applies to gains recognized within:

- A. 10 years
- B. 3 years
- C. 5 years
- D. 7 years

55. Excess net passive income tax applies when passive income exceeds 25% of gross receipts and corporation has:

- A. No E&P
- B. C corporation E&P
- C. Losses
- D. Accumulated adjustments

56. S corporation loses election if passive income exceeds 25% for:

- A. 1 year
- B. 3 consecutive years
- C. 2 years
- D. 5 years

57. S corporation shareholder basis includes:

- A. Entity liabilities
- B. Guaranteed debt
- C. Direct loans only
- D. All debt

58. AAA represents S corporation:

- A. Earnings and profits
- B. Taxable income
- C. Distributions
- D. Accumulated income not distributed

59. S corporation distributions first come from AAA, then from:

- A. Capital
- B. Basis
- C. Loans
- D. E&P if any

60. QSub election treats subsidiary as:

- A. Separate corporation
- B. Division of parent
- C. Partnership
- D. Disregarded entity

61. C corporation capital losses can offset:

- A. Capital gains only
- B. Operating income
- C. Any income
- D. Ordinary income limited

62. Corporate capital loss carryback period:

- A. None
- B. 2 years
- C. 3 years
- D. 5 years

63. Corporate charitable contribution carryforward is:

- A. Indefinite
- B. 10 years
- C. 20 years
- D. 5 years

64. Dividends received deduction for 80% or more ownership:

- A. 50%
- B. 100%
- C. 65%
- D. 80%

65. Personal service corporation tax rate:

- A. Graduated
- B. 35%
- C. 21%

D. 15%

66. Personal holding company tax rate:

- A. 20%
- B. 21%
- C. 35%
- D. 15%

67. Accumulated earnings tax applies at rate of:

- A. 15%
- B. 20%
- C. 25%
- D. 21%

68. Schedule M-1 reconciles book income to:

- A. Cash flow
- B. Retained earnings
- C. Financial income
- D. Taxable income

69. Controlled group brother-sister requires common ownership exceeding:

- A. 50%
- B. 80%
- C. 25%
- D. 75%

70. Parent-subsidiary controlled group requires ownership of:

- A. 50%
- B. 100%
- C. 80%
- D. 75%

71. Affiliated group requirements for consolidation include:

- A. 50% ownership
- B. 100% ownership
- C. 51% ownership
- D. 80% ownership

72. Consolidated return election is made by filing consolidated Form:

- A. 1120-C

- B. 1120
- C. 1065
- D. 1120-S

73. Intercompany dividends in consolidated group are:

- A. Eliminated
- B. Taxed
- C. Deferred
- D. Partially taxed

74. Corporate formation under Section 351 requires transferors to own:

- A. 51%
- B. 100%
- C. 80%
- D. 50%

75. Boot received in Section 351 exchange is taxable up to:

- A. Fair market value
- B. Basis
- C. Amount received
- D. Gain realized

76. Section 1244 stock ordinary loss treatment applies to:

- A. All stock
- B. Small business stock
- C. Publicly traded stock
- D. Preferred stock

77. Organizational costs are amortized over:

- A. 60 months
- B. 84 months
- C. 180 months
- D. 15 years

78. Corporate liquidation under Section 331 creates:

- A. Capital gain or loss
- B. Ordinary income
- C. Dividend
- D. No recognition

79. Parent liquidating 80% owned subsidiary under Section 332 results in:

- A. Taxable gain
- B. No gain or loss
- C. Ordinary income
- D. Deferred gain

80. Section 338 election treats stock purchase as:

- A. Stock acquisition
- B. Asset acquisition
- C. Merger
- D. Consolidation

81. Employment taxes include FICA and:

- A. FUTA
- B. State income tax
- C. Sales tax
- D. Property tax

82. FICA tax rate for 2024:

- A. 15.3%
- B. 12.4%
- C. 7.65%
- D. 6.2%

83. FUTA tax rate after credit:

- A. 6%
- B. 5.4%
- C. 1.5%
- D. 0.6%

84. FUTA wage base for 2024:

- A. \$10,000
- B. \$7,000
- C. \$168,600
- D. \$5,000

85. Form W-2 must be provided to employees by:

- A. January 15
- B. February 15
- C. January 31

D. April 15

86. Form 941 is filed:

- A. Quarterly
- B. Monthly
- C. Annually
- D. Semi-annually

87. Employer mandate for health coverage applies to employers with at least:

- A. 25 employees
- B. 100 employees
- C. 10 employees
- D. 50 employees

88. Independent contractor classification depends on:

- A. Written agreement
- B. Common law factors
- C. Hourly pay
- D. Part-time status

89. Form 1099-NEC reports:

- A. Nonemployee compensation
- B. Employee wages
- C. Interest
- D. Dividends

90. Backup withholding rate:

- A. 10%
- B. 24%
- C. 28%
- D. 15%

91. Information return penalties vary based on when filed, with lowest penalty for filing within:

- A. 15 days
- B. 60 days
- C. 90 days
- D. 30 days

92. Intentional disregard of information return filing has minimum penalty of:

- A. \$100

- B. \$580
- C. \$250
- D. \$1,000

93. Form 1099-K reports payment card and third-party network transactions exceeding:

- A. \$5,000
- B. \$20,000
- C. \$600
- D. \$10,000

94. Employers must verify employee work authorization using Form:

- A. I-9
- B. W-4
- C. I-94
- D. SS-59

95. Fringe benefit taxation requires including value on Form W-2 by:

- A. Cost to employer
- B. Fair market value
- C. Employee's price
- D. Wholesale value

96. Accountable plan requirements include business connection, substantiation, and:

- A. Monthly reporting
- B. Return of excess
- C. Annual election
- D. Employer approval

97. Nonaccountable plan reimbursements are treated as:

- A. Nontaxable
- B. Deductible by employee
- C. Loans
- D. Wages

98. Cafeteria plan nondiscrimination testing ensures benefits don't favor:

- A. Full-time employees
- B. Management
- C. Highly compensated
- D. Long-term employees

99. Educational assistance exclusion applies to:
- A. Undergraduate only
 - B. Graduate only
 - C. Job-related only
 - D. Both graduate and undergraduate
100. Qualified retirement plan nondiscrimination testing ensures coverage of:
- A. All employees
 - B. Rank-and-file employees
 - C. Officers
 - D. Owners

Part 3: Representation, Practices, And Procedures

1. Circular 230 violations can result in censure, suspension, or:
- A. Fine
 - B. Criminal charges
 - C. License revocation
 - D. Disbarment
2. Enrolled agents must renew enrollment every:
- A. 5 years
 - B. 2 years
 - C. 3 years
 - D. Annually
3. Continuing education for enrolled agents requires minimum per year of:
- A. 24 hours
 - B. 16 hours
 - C. 12 hours
 - D. 72 hours
4. Ethics CE requirement for enrolled agents is:
- A. 6 hours per cycle
 - B. 4 hours per cycle
 - C. 10 hours per cycle
 - D. 2 hours per year
5. Practitioner suspension from IRS practice can be for:
- A. Specific period

- B. Indefinite period
 - C. Permanent
 - D. One year only
6. Best practices under Circular 230 include establishing facts through:
- A. Client statement
 - B. Affidavit
 - C. Reasonable inquiry
 - D. Written agreement
7. Solicitation is prohibited if it involves:
- A. Advertising
 - B. Coercion
 - C. Marketing
 - D. Networking
8. Contingent fees are permitted for services in connection with:
- A. Original returns
 - B. Routine advice
 - C. Preparation services
 - D. IRS examinations
9. Tax return positions must have at least reasonable basis and be disclosed if lacking:
- A. Substantial authority
 - B. More likely than not
 - C. Any support
 - D. Court approval
10. Covered opinions require practitioner to reach conclusion at confidence level of:
- A. Reasonable basis
 - B. More likely than not
 - C. Should
 - D. Substantial authority
11. Former government employees cannot represent on matters they participated in:
- A. At any time
 - B. Within 5 years
 - C. Personally and substantially
 - D. As supervisor

12. Confidential client information can be disclosed with:
- A. IRS request
 - B. Verbal consent
 - C. Implied consent
 - D. Written consent
13. Return of client records must occur:
- A. After payment
 - B. Within 30 days
 - C. At end of engagement
 - D. Upon request
14. Practitioner must advise client of noncompliance and:
- A. File corrected return
 - B. Consequences
 - C. Report to IRS
 - D. Withdraw immediately
15. Diligence requires practitioner to make reasonable inquiry when information appears:
- A. Complete
 - B. Accurate
 - C. Incorrect
 - D. Documented
16. Practice before IRS includes:
- A. Filing returns only
 - B. Correspondence only
 - C. Representation and advocacy
 - D. Administrative tasks
17. Limited practice allows unenrolled preparers to represent on returns they:
- A. Filed
 - B. Reviewed
 - C. Signed
 - D. Prepared and signed
18. AFSP participants can represent before revenue agents on returns they:
- A. Reviewed
 - B. Filed
 - C. Prepared and signed

D. Supervised

19. Form 2848 authorizes representative to:

- A. Receive information only
- B. Represent and receive information
- C. File returns
- D. Sign agreements

20. Form 8821 allows designated person to:

- A. Represent taxpayer
- B. Inspect and receive information
- C. Sign returns
- D. Negotiate settlements

21. CAF retention period for Form 2848 is:

- A. 1 year
- B. 5 years
- C. Permanent
- D. 3 years

22. Power of attorney can be revoked by:

- A. IRS
- B. Representative
- C. Taxpayer written notice
- D. Automatic expiration

23. Centralized Authorization File number is assigned to:

- A. Taxpayer
- B. Representative
- C. IRS office
- D. Return

24. Declaration of representative requires practitioner to state they are:

- A. Licensed
- B. Experienced
- C. Certified
- D. Authorized and eligible

25. Multiple representatives can act:

- A. Only jointly

- B. Only one at a time
- C. Independently unless specified
- D. With IRS approval

26. Third-party designee authority terminates:

- A. When return processed
- B. After 1 year
- C. Never
- D. When refund issued

27. PTIN must be obtained:

- A. From state
- B. From IRS
- C. Annually
- D. Once

28. Annual PTIN renewal is required by:

- A. December 31
- B. October 15
- C. April 15
- D. June 30

29. Preparer tax identification number is required for:

- A. All preparers
- B. Volunteers
- C. Paid preparers
- D. Family members

30. Tax return preparer includes anyone who prepares for:

- A. Free
- B. Family
- C. Compensation
- D. Friends

31. Signing preparer is person with primary responsibility for:

- A. Filing
- B. Overall accuracy
- C. Signature
- D. Payment

32. Nonsigning preparer prepares substantial portion meaning entry affects:
- A. Any amount
 - B. Filing status only
 - C. \$10,000 or 20% of gross income
 - D. Refund only
33. Due diligence requirements apply to EITC, CTC, AOTC, ACTC, and:
- A. LLC
 - B. Saver's Credit
 - C. Foreign Tax Credit
 - D. HOH
34. Form 8867 must be completed for each return claiming:
- A. Any credit
 - B. EITC only
 - C. Covered credits
 - D. Refund
35. Due diligence records must be retained for:
- A. 1 year
 - B. 3 years
 - C. 5 years
 - D. Permanently
36. Knowledge standard for due diligence is knew or reasonably:
- A. Might know
 - B. Could know
 - C. Would know
 - D. Should have known
37. Unreasonable position penalty is greater of \$1,000 or:
- A. 25% of income
 - B. \$5,000
 - C. 50% of income
 - D. 100% of income
38. Willful or reckless conduct penalty is greater of \$5,000 or:
- A. 75% of income
 - B. 50% of income
 - C. \$10,000

D. 100% of income

39. Failure to furnish copy to taxpayer penalty is:

- A. \$100 per return
- B. \$50 per return
- C. \$250 per return
- D. \$500 per return

40. Disclosure or use of return information penalty is \$250 per disclosure up to:

- A. \$5,000
- B. \$25,000
- C. No limit
- D. \$10,000 per year

41. Aiding and abetting understatement penalty for corporate returns is:

- A. \$1,000
- B. \$5,000
- C. \$10,000
- D. \$50,000

42. Promoting abusive tax shelter penalty is 50% or 75% of:

- A. Gross income from activity
- B. Tax benefit
- C. Shelter investment
- D. Fees charged

43. Assessment statute of limitations is generally:

- A. 2 years
- B. 5 years
- C. 6 years
- D. 3 years

44. Statute extends to 6 years if gross income omission exceeds:

- A. \$10,000
- B. 25% of gross income
- C. \$5,000
- D. 50% of tax

45. Fraud has no statute of limitations but requires proof of intent to:

- A. Delay

- B. Underpay
- C. Evade
- D. Defer

46. Refund claim must be filed within the later of 3 years from filing or:

- A. 1 year from payment
- B. 4 years from payment
- C. 6 months from payment
- D. 2 years from payment

47. Collection statute is generally 10 years from:

- A. Filing
- B. Assessment
- C. Notice
- D. Payment

48. Statute can be suspended during IRS collection action including offer in compromise and:

- A. Appeals
- B. Installment agreement request
- C. Litigation
- D. Audit

49. Financial status audit examines ability to pay and focuses on:

- A. Income sources
- B. Deductions
- C. Lifestyle and assets
- D. Prior returns

50. Correspondence audit is conducted by:

- A. Mail
- B. Office visit
- C. Field visit
- D. Phone

51. Office examination requires taxpayer to appear at:

- A. Home
- B. Business
- C. Practitioner's office
- D. IRS office

52. Field audit occurs at taxpayer's home or:
- A. IRS office
 - B. Place of business
 - C. Attorney's office
 - D. Any location
53. Examination changes are proposed on:
- A. Notice of Deficiency
 - B. 30-day letter
 - C. Audit report
 - D. Assessment notice
54. Taxpayer who disagrees with examination can request conference with:
- A. Examiner
 - B. Manager
 - C. IRS Counsel
 - D. Appeals
55. Statutory notice of deficiency gives taxpayer 90 days to:
- A. Pay
 - B. Respond
 - C. File amended return
 - D. Petition Tax Court
56. Failure to respond to notice of deficiency results in:
- A. Default judgment
 - B. Criminal referral
 - C. Assessment
 - D. Collection
57. Tax Court petition must be filed within:
- A. 30 days
 - B. 90 days
 - C. 60 days
 - D. 6 months
58. Small case Tax Court procedures apply to disputes of \$50,000 or less and decisions are:
- A. Not appealable
 - B. Appealable
 - C. Precedential

D. Published

59. Tax Court regular decisions are:

- A. Not published
- B. Memorandum only
- C. Published
- D. Summary

60. Appeals from Tax Court go to:

- A. District Court
- B. Supreme Court
- C. Court of Federal Claims
- D. Circuit Court

61. District Court jurisdiction requires:

- A. Petition
- B. Payment first
- C. Appeal
- D. Notice

62. Court of Federal Claims hears tax cases where taxpayer has paid and seeks refund and has jurisdiction:

- A. Limited to \$10,000
- B. Nationwide
- C. State-specific
- D. Regional

63. Appeals from District Court go to:

- A. Tax Court
- B. Supreme Court
- C. Court of Federal Claims
- D. Circuit Court

64. Golsen rule requires Tax Court to follow:

- A. Prior Tax Court decisions
- B. Supreme Court
- C. Appellate court for taxpayer's residence
- D. IRS position

65. Whistleblower awards are paid for information resulting in collection exceeding:

- A. \$1 million
- B. \$2 million
- C. \$5 million
- D. \$10 million

66. Whistleblower award percentage ranges from:

- A. 5–10%
- B. 10–20%
- C. 25–50%
- D. 15–30%

67. John Doe summons requires court approval showing investigation of:

- A. Individual
- B. Ascertainable group
- C. Specific person
- D. Named party

68. Third-party recordkeeper summons notice gives taxpayer right to petition to quash within:

- A. 10 days
- B. 30 days
- C. 20 days
- D. 14 days

69. Summons enforcement requires IRS to show legitimate purpose and:

- A. Court order
- B. Relevance
- C. Necessity
- D. Urgency

70. Taxpayer may claim privilege for communications with enrolled agent regarding:

- A. Tax return preparation
- B. All communications
- C. Tax advice in noncriminal proceedings
- D. Audit matters

71. Federally authorized tax practitioner privilege applies to communications made to obtain or provide tax advice in matters before IRS or court relating to:

- A. Any matter
- B. Nontax issues
- C. Tax matters

D. Criminal matters

72. Privilege does NOT apply to written communications regarding tax shelters or:

- A. Audits
- B. Appeals
- C. Criminal matters
- D. Collections

73. Summons may be issued to examine books and records or to compel:

- A. Payment
- B. Settlement
- C. Filing
- D. Testimony

74. Levy is IRS collection action that seizes:

- A. Real property only
- B. Wages only
- C. Property and rights to property
- D. Bank accounts only

75. Notice of intent to levy must be given at least 30 days before levy and provides right to collection:

- A. Waiver
- B. Extension
- C. Appeal
- D. Due process hearing

76. Property exempt from levy includes certain amounts of wages, unemployment, and:

- A. All retirement accounts
- B. Luxury items
- C. Principal residence without approval
- D. Investment accounts

77. Federal tax lien arises automatically when IRS assesses tax and taxpayer fails to pay and IRS files:

- A. Notice of Federal Tax Lien
- B. Levy
- C. Warrant
- D. Judgment

78. Federal tax lien notice is filed with:

- A. Tax Court

- B. IRS
- C. Appropriate government office
- D. Employer

79. Lien priority is generally determined by:

- A. Amount
- B. Type of tax
- C. Date filed
- D. First in time

80. Certificate of release of federal tax lien must be issued within 30 days of satisfaction or becoming unenforceable and taxpayer can request if not issued within:

- A. 60 days
- B. 90 days
- C. 6 months
- D. 1 year

81. Offer in compromise based on doubt as to collectibility requires detailed financial statement on Form:

- A. 433-A or 433-B
- B. 656
- C. 8857
- D. 9465

82. OIC application fee is:

- A. \$50
- B. \$500
- C. \$205
- D. \$100

83. Effective tax administration OIC applies when collection would create economic hardship or be unfair due to:

- A. Insolvency
- B. Inability to pay
- C. Exceptional circumstances
- D. Disputed liability

84. Installment agreement user fee varies but can be as low as \$31 for:

- A. Any agreement
- B. Direct debit low-income

- C. Standard agreement
- D. High-balance agreement

85. Currently not collectible status means IRS determines taxpayer cannot pay any amount because it would create:

- A. Delay
- B. Difficulty
- C. Hardship
- D. Inconvenience

86. Innocent spouse relief under Section 6015(b) requires understatement attributable to erroneous item of:

- A. Both spouses
- B. Either spouse
- C. Requesting spouse
- D. Other spouse

87. Separation of liability relief under 6015(c) requires requestor be no longer married or be:

- A. Legally separated
- B. Living apart
- C. Divorced
- D. Separated or living apart 12 months

88. Equitable relief considers all facts and circumstances including whether requesting spouse knew of understatement and whether they would suffer:

- A. Any burden
- B. Economic hardship
- C. Inconvenience
- D. Delayed refund

89. Injured spouse allocation is filed on Form 8379 when joint refund offset for other spouse's:

- A. Current taxes
- B. Underpayment
- C. Separate debt
- D. Business taxes

90. Injured spouse differs from innocent spouse because injured spouse claims share of refund while innocent spouse seeks relief from:

- A. Filing requirement
- B. Payment

- C. Liability
- D. Penalties

91. Collection due process hearing is requested within 30 days of notice of intent to levy or notice of lien and is held by:
- A. IRS Counsel
 - B. Revenue Officer
 - C. Settlement Officer
 - D. Appeals Officer
92. CDP hearing allows challenge to collection action including raising defenses and proposing:
- A. Payment plan
 - B. Collection alternatives
 - C. Dismissal
 - D. Extension
93. Equivalent hearing is available for those who miss CDP deadline and provides similar review but no:
- A. Appeals rights
 - B. Payment plan
 - C. Court review
 - D. Settlement
94. Taxpayer Advocate Service assists when taxpayer experiencing economic harm or significant hardship and can issue:
- A. Refund
 - B. Ruling
 - C. Assessment
 - D. Taxpayer Assistance Order
95. TAS is independent organization within IRS headed by:
- A. Commissioner
 - B. Treasury Secretary
 - C. Appeals Officer
 - D. National Taxpayer Advocate
96. Low Income Taxpayer Clinics provide free or low-cost representation for taxpayers whose income is below certain level and are funded by:
- A. State
 - B. Private donations
 - C. IRS grants

D. Court fees

97. LITC also provides education and advocacy on behalf of taxpayers with limited English proficiency or who speak English as second language, demonstrating need for language access in tax:
- A. Forms
 - B. Administration
 - C. Court
 - D. Returns
98. Fast Track Settlement provides expedited resolution using Appeals personnel while case remains in:
- A. Examination
 - B. Collection
 - C. Appeals
 - D. Litigation
99. Fast Track Mediation provides expedited resolution after examination using Appeals mediator and is voluntary program for:
- A. All cases
 - B. Small cases only
 - C. Willing parties
 - D. Appeals cases
100. Arbitration in Appeals is binding resolution of factual issues when regular Appeals process cannot resolve dispute and is available for issues involving:
- A. Law
 - B. Policy
 - C. Facts
 - D. All issues

Answer Explanations - Practice Test 7

Part 1: Individuals

1. Correct Answer: D (Legally separated)

Married taxpayers must file jointly or separately if living together unless they are legally separated under a decree of divorce or separate maintenance. Being over 65, having different incomes, or one spouse being blind does not eliminate the requirement to file as married. Legal separation under a divorce decree or

separate maintenance agreement allows taxpayers to file as single or head of household if they qualify, even before the divorce is finalized.

2. Correct Answer: A (2 years after spouse's death)

Qualifying surviving spouse (formerly called qualifying widow/widower) status is available for 2 years following the year of the spouse's death. To qualify, the taxpayer must have a dependent child living with them, have been eligible to file jointly in the year of death, not have remarried, and pay over half the cost of maintaining the home. This filing status provides the same standard deduction and tax rates as married filing jointly, easing the financial transition after a spouse's death.

3. Correct Answer: C (Head of household)

Unmarried taxpayers with dependent parents who do not live with them can still qualify for head of household filing status. The parent does not need to live with the taxpayer—they can maintain their own residence. The taxpayer must pay over half the cost of maintaining the parent's home and be able to claim the parent as a dependent. This exception recognizes taxpayers who support parents in separate households.

4. Correct Answer: B (Personal exemption deduction)

Dependents cannot claim a personal exemption for themselves on their own tax return if they can be claimed as a dependent by another taxpayer. The Tax Cuts and Jobs Act suspended personal exemptions for 2018-2025, setting the amount to zero, but the rule remains that dependents cannot claim their own exemption. Dependents can still claim credits, take the standard deduction (limited for dependents), and report earned income.

5. Correct Answer: A (Withholding amount)

Form W-4, Employee's Withholding Certificate, determines the amount of federal income tax withheld from an employee's wages. Employees complete W-4 to indicate filing status, dependents, other income, deductions, and additional withholding. Employers use this information to calculate withholding using IRS tax tables or formulas. The form doesn't determine actual tax liability, refund amount, or filing status—it only affects withholding to approximate the final tax liability.

6. Correct Answer: D (Joint return)

Nonresident aliens married to U.S. citizens or residents can elect to be treated as U.S. residents for tax purposes if they file a joint return. This election (made on the joint return) subjects the nonresident alien's worldwide income to U.S. taxation but allows the couple to use joint filing rates and standard deductions. Once made, the election remains in effect for all subsequent years unless terminated or revoked.

7. Correct Answer: C (SS-5)

Social Security number applications for dependents (and all individuals) use Form SS-5, Application for a Social Security Card. Parents typically apply for SSNs for newborns at the hospital or shortly after birth.

Form W-7 is for ITINs (Individual Taxpayer Identification Numbers), Form W-9 requests taxpayer identification information, and Form SS-4 applies for Employer Identification Numbers.

8. Correct Answer: B (SSN not yet available)

Adoption Taxpayer Identification Numbers (ATINs) are used when a child in a domestic adoption doesn't yet have a Social Security number and cannot obtain one in time for tax filing. The adoptive parents apply using Form W-7A. ATINs are temporary—once the adoption is finalized and an SSN obtained, the SSN must be used for future tax returns. ATINs allow parents to claim the child as a dependent during the adoption process.

9. Correct Answer: D (Together provide over 50%)

Multiple support agreements allow one person to claim a dependency exemption when no single person provides over 50% of support but together a group provides more than 50%. The person claiming the exemption must provide over 10% of support, and others who provided over 10% must sign Form 2120 agreeing not to claim the dependent. This situation commonly arises when siblings support a parent.

10. Correct Answer: A (Noncustodial parent has release form)

In divorces, the custodial parent (the parent with whom the child lived for the greater number of nights) generally claims the dependency exemption. However, the noncustodial parent can claim the exemption if the custodial parent releases the claim using Form 8332 or a substantially similar statement. Court orders alone don't transfer the exemption—the release form is required. Verbal agreements and income differences don't affect the rule.

11. Correct Answer: A (Tips and bonuses)

Wages include all compensation for services, including regular pay, tips, bonuses, commissions, vacation pay, sick pay, and severance. Tips must be reported to employers if they total \$20 or more per month. Bonuses are wages even if discretionary. Gifts from employers are generally taxable unless they qualify as de minimis fringe benefits. Properly reimbursed expenses under accountable plans and specifically excluded fringe benefits are not wages.

12. Correct Answer: C (Personal use of company car)

Personal use of a company car is a taxable fringe benefit that must be included in wages. Employers must value the personal use (using various IRS methods) and include it in income. Health insurance premiums paid by employers, qualified parking up to \$315 monthly, and achievement awards up to \$1,600 (qualified plan awards) are excludable fringe benefits. The personal use value represents compensation for services.

13. Correct Answer: D (\$5,000)

Employer-provided dependent care assistance is excludable up to \$5,000 per year (\$2,500 for married filing separately). The assistance must be provided under a written, nondiscriminatory program. Amounts excluded reduce expenses eligible for the dependent care credit dollar-for-dollar. The exclusion helps

employees pay for care for children under 13 or disabled dependents while working. Amounts over \$5,000 are taxable wages.

14. Correct Answer: B (\$50,000)

Group term life insurance coverage provided by employers is excludable up to \$50,000 of coverage. Coverage exceeding \$50,000 results in taxable income calculated using the IRS Uniform Premium Table based on the employee's age. The cost is imputed income reported on Form W-2. The \$50,000 threshold recognizes reasonable employer-provided life insurance while limiting the tax benefit for excessive coverage.

15. Correct Answer: D (Qualified benefits)

Cafeteria plans (Section 125 plans) allow employees to choose between cash compensation and qualified benefits such as health insurance, dependent care assistance, adoption assistance, and contributions to HSAs or FSAs. The ability to choose benefits allows customization while the pre-tax nature reduces both income and FICA taxes. Plans must be written and cannot discriminate in favor of highly compensated employees.

16. Correct Answer: A (Tangible personal property)

Employee achievement awards are excludable (within limits) only if they consist of tangible personal property (not cash, cash equivalents, gift cards, securities, or vacations) given for length of service or safety achievement. The award must be presented as part of a meaningful presentation. Cash, gift cards, and securities are always taxable. The exclusion limits are \$400 for non-qualified plans and \$1,600 for qualified plans.

17. Correct Answer: C (20% of price charged)

Qualified employee discounts for services provided to employees cannot exceed 20% of the price charged to customers. For property, the discount cannot exceed the employer's gross profit percentage. The exclusion applies to services or property offered to customers in the ordinary course of the employer's business in which the employee works. Discounts exceeding these limits create taxable income equal to the excess.

18. Correct Answer: B (Employee paid)

Working condition fringe benefits are property or services provided to employees that would be deductible as business expenses under Section 162 or 167 if the employee paid for them. Examples include job-related education, professional subscriptions, business use of employer-provided vehicles, and tools required for work. The exclusion recognizes that these benefits facilitate work rather than providing personal compensation.

19. Correct Answer: A (Excess capacity exists)

No-additional-cost services are excludable when the employer provides services to employees in the employer's line of business where excess capacity exists and the service doesn't create substantial additional cost. Examples include airline employees flying standby, hotel employees using vacant rooms, or phone company employees using excess network capacity. The exclusion applies when the employee's use doesn't prevent customer sales or create meaningful cost.

20. Correct Answer: C (\$16,810)

Adoption assistance programs under Section 137 allow employers to exclude from employee income up to approximately \$16,810 (for 2024, adjusted annually for inflation) for qualified adoption expenses. This exclusion applies to employer-provided adoption assistance benefits for each child. Qualified expenses include adoption fees, court costs, attorney fees, traveling expenses, and other directly related costs. The exclusion amount is the same as the adoption credit amount. The exclusion phases out for taxpayers with modified AGI between approximately \$252,150 and \$292,150 (for 2024), providing meaningful support for employees adopting children while targeting benefits to lower and middle-income families.

21. Correct Answer: B (\$4,150)

Health Savings Account contribution limits for self-only coverage in 2024 are approximately \$4,150 (adjusted annually for inflation). For family coverage, the limit is approximately \$8,300. Individuals age 55 or older can contribute an additional \$1,000 catch-up contribution. To qualify for HSA contributions, taxpayers must be covered by a high-deductible health plan (HDHP) with minimum deductibles of \$1,600 (self-only) or \$3,200 (family) and maximum out-of-pocket expenses of \$8,050 (self-only) or \$16,100 (family) for 2024. HSA contributions are deductible (or excluded if employer-contributed), earnings grow tax-free, and distributions for qualified medical expenses are tax-free.

22. Correct Answer: B (\$1,000)

HSA catch-up contributions for individuals age 55 or older add \$1,000 to the annual contribution limit. This additional amount is not indexed for inflation and has remained \$1,000 since HSAs were created. The catch-up allows older individuals approaching Medicare eligibility to build additional health savings. Both spouses can make catch-up contributions if both are 55+ with separate HSAs.

23. Correct Answer: A (\$3,200)

The health care flexible spending arrangement (FSA) maximum contribution for 2024 is approximately \$3,200 (adjusted annually for inflation). FSAs are "use it or lose it" accounts, though employers may offer either a \$640 carryover to the next year or a 2.5-month grace period. FSA contributions reduce both income and FICA taxes. Unlike HSAs, FSAs don't require high-deductible health plans and funds are available immediately.

24. Correct Answer: D (\$315)

Qualified transportation fringe benefits for 2024 have a monthly limit of \$315 for transit passes and vanpooling, and a separate \$315 monthly limit for qualified parking (amounts adjusted annually). These

amounts can be excluded from employee income. Employers can provide these benefits pre-tax, though the Tax Cuts and Jobs Act eliminated employer deductions for transportation fringe benefits. Bicycle commuting benefits were suspended through 2025.

25. Correct Answer: C (Active duty military)

Moving expense deductions are available only for members of the Armed Forces on active duty who move pursuant to military orders for a permanent change of station. The Tax Cuts and Jobs Act suspended the moving expense deduction for other taxpayers for 2018-2025. Military members can deduct reasonable moving expenses for transporting household goods and traveling to the new home. Civilian moving expenses are not deductible during the suspension period.

26. Correct Answer: B (Federally declared disaster)

Personal casualty and theft loss deductions require losses occurring in a federally declared disaster area. The Tax Cuts and Jobs Act suspended personal casualty loss deductions for 2018-2025 except for losses in federally declared disaster areas. The loss must exceed \$500 per casualty (indexed), and total losses must exceed 10% of AGI. State emergencies or insurance claims alone don't qualify without federal disaster declaration.

27. Correct Answer: D (\$100)

Personal casualty and theft losses (deductible only for federally declared disasters for tax years 2018-2025) are subject to a two-part floor: (1) each casualty event must exceed \$100 per event, and (2) the total of all casualty losses for the year (after applying the \$100 reduction to each event) must exceed 10% of adjusted gross income. Only the amount exceeding both floors is deductible. For example, if a taxpayer with \$80,000 AGI has a casualty loss of \$10,000, the deductible amount is \$1,900: $\$10,000 - \$100 = \$9,900$, minus 10% of AGI ($\$8,000$) = $\$1,900$. The \$100 per-event floor prevents deducting very small losses, while the 10% of AGI floor ensures only significant losses relative to income are deductible.

28. Correct Answer: A (21 cents)

The standard mileage rate for medical and moving (military only) purposes for 2024 is 21 cents per mile. This rate is lower than the business rate because it only covers actual costs without profit margin. Medical mileage is deductible as a medical expense (subject to 7.5% AGI floor). Military moving mileage is deductible by active duty members moving under orders. The rate is set annually by the IRS.

29. Correct Answer: C (14 cents)

The charitable mileage rate is 14 cents per mile and is set by statute, not IRS regulation, so it rarely changes. This rate applies when using a car for charitable volunteer work. Unlike business and medical rates, the charitable rate has remained 14 cents for many years. Taxpayers can deduct this amount plus parking fees and tolls related to charitable use.

30. Correct Answer: B (67 cents)

The standard business mileage rate for 2024 is 67 cents per mile (adjusted annually). This rate includes all vehicle operating costs: gas, oil, repairs, insurance, depreciation, and lease payments. Taxpayers using the standard mileage rate cannot also deduct actual vehicle expenses. Business parking fees and tolls are separately deductible in addition to the mileage rate. The rate can be used instead of actual expense method.

31. Correct Answer: A (Deductible by payor)

Alimony paid under divorce or separation agreements executed before January 1, 2019, is deductible by the payor and taxable to the recipient. The Tax Cuts and Jobs Act eliminated the alimony deduction for agreements executed after December 31, 2018. Pre-2019 agreements retain the old rules unless modified to adopt new treatment. The deduction is taken as an adjustment to income on Schedule 1.

32. Correct Answer: D (Not deductible)

Child support payments are not deductible by the payor and not taxable to the recipient. This treatment differs from pre-2019 alimony. Child support is a legal obligation to support children and doesn't represent income to the recipient or a deductible expense to the payor. Payments designated as child support in divorce agreements are never deductible, regardless of when the agreement was executed.

33. Correct Answer: B (Excluded if income limits met)

Interest on U.S. Series EE or I savings bonds issued after 1989 may be excluded from income if the bonds are used to pay qualified higher education expenses and the taxpayer meets income limits. The exclusion phases out at higher income levels (approximately \$96,800-\$111,800 for single filers in 2024). The bonds must be issued to a taxpayer age 24 or older. Qualified expenses include tuition and fees, not room and board.

34. Correct Answer: C (Ordinary and qualified dividends)

Form 1099-DIV reports both ordinary dividends and qualified dividends from mutual funds and other investments. It also reports capital gain distributions, nondividend distributions, federal and state tax withheld, foreign taxes paid, and investment expenses. Ordinary dividends are taxed at ordinary income rates, while qualified dividends receive preferential capital gains tax rates. Interest income is reported on Form 1099-INT, not 1099-DIV.

35. Correct Answer: D (Capital gains rates)

Qualified dividends are taxed at the same preferential rates as long-term capital gains: 0%, 15%, or 20%, depending on the taxpayer's taxable income. To qualify, dividends must be paid by U.S. corporations or qualified foreign corporations, and the taxpayer must meet the holding period requirement (more than 60 days during the 121-day period beginning 60 days before the ex-dividend date). This favorable treatment encourages equity investment.

36. Correct Answer: A (Tax-deferred until redeemed)

Series I savings bond interest accrues but is tax-deferred until the bonds are redeemed or mature, whichever comes first. Alternatively, taxpayers can elect to report the interest annually as it accrues. Most taxpayers use the tax-deferral method, reporting all accrued interest in the year of redemption. Series I bonds earn interest for 30 years and protect against inflation through adjustable rates.

37. Correct Answer: B (Tuition and fees)

Series EE bonds issued after 1989 can qualify for interest exclusion if used for qualified higher education expenses: tuition and fees for the taxpayer, spouse, or dependent at an eligible institution. Room and board don't qualify. The taxpayer must be age 24 or older when the bonds were issued. The exclusion phases out at higher income levels. Expenses must be reduced by tax-free scholarships and education credits claimed.

38. Correct Answer: C (Not taxable)

Tax-exempt interest (such as from municipal bonds) must be reported on the tax return even though it's not taxed. It's reported for informational purposes and because it affects other tax calculations including Social Security taxation, alternative minimum tax, and various phase-outs and credits. The reporting ensures the IRS can verify income levels for these purposes even though the interest itself remains tax-exempt.

39. Correct Answer: A (19 or students under 24)

The kiddie tax applies to unearned income of children under age 19, or full-time students under age 24 (who don't provide over half their own support). The kiddie tax taxes the child's unearned income above a threshold (\$2,500 for 2024) at the parent's marginal tax rate if higher than the child's rate. This prevents income-shifting to children to take advantage of lower brackets.

40. Correct Answer: D (\$2,500)

Net unearned income for kiddie tax purposes in 2024 is unearned income exceeding \$2,500 (twice the standard deduction for dependents, which is \$1,300). The first \$1,300 of unearned income is offset by the dependent's standard deduction, the next \$1,300 is taxed at the child's rate (typically 10%), and amounts above \$2,500 are potentially taxed at the parent's marginal rate under the kiddie tax rules.

41. Correct Answer: C (12 months)

Capital assets must be held for more than 12 months (more than one year) to qualify for long-term capital gain treatment. Assets held 12 months or less are short-term. The holding period begins the day after acquisition and includes the day of sale. Long-term capital gains receive preferential tax rates (0%, 15%, or 20%), while short-term gains are taxed at ordinary income rates.

42. Correct Answer: B (\$3,000)

Net capital losses can be deducted against ordinary income up to \$3,000 per year (\$1,500 if married filing separately). Capital losses first offset capital gains. Excess losses beyond the \$3,000 annual limit carry

forward indefinitely to future tax years, retaining their character as short-term or long-term losses. This limitation prevents excessive use of capital losses against ordinary income.

43. Correct Answer: D (Indefinite)

Capital loss carryforwards are indefinite—they never expire. Unused capital losses can be carried forward to offset capital gains in future years or deducted against ordinary income (\$3,000 per year) until fully used. The losses retain their character (short-term or long-term) when carried forward. Long-term capital loss carryforwards can offset long-term gains, while short-term losses offset short-term gains.

44. Correct Answer: A (28%)

Collectibles (art, antiques, gems, stamps, coins, etc.) held more than one year are subject to a maximum capital gains rate of 28%, higher than the normal long-term capital gains rates of 0%, 15%, or 20%. This higher rate recognizes that collectibles may have special characteristics not shared by regular investment assets. The actual tax depends on the taxpayer's ordinary income bracket—if below 28%, the lower rate applies.

45. Correct Answer: C (25%)

Section 1250 unrecaptured gain (depreciation recapture on real property) is taxed at a maximum rate of 25%. This applies to the portion of gain attributable to straight-line depreciation on real property. The 25% rate is higher than the 0%, 15%, or 20% long-term capital gains rates but lower than ordinary income rates. Any gain exceeding depreciation is taxed at regular capital gains rates.

46. Correct Answer: B (30 days before or after)

The wash sale rule disallows losses when substantially identical securities are purchased within 30 days before or after the sale (a 61-day window). The disallowed loss is added to the basis of the replacement securities, deferring the loss recognition. This prevents taxpayers from recognizing tax losses while maintaining the same investment position. The rule applies to stocks, bonds, and options on those securities.

47. Correct Answer: A (Risk of loss and opportunity for gain)

Constructive sales occur when a taxpayer enters into an offsetting position that substantially eliminates both the risk of loss and opportunity for gain on an appreciated financial position. Examples include short sales against the box, certain options, or forward contracts. Constructive sales trigger immediate gain recognition as if the asset were sold, preventing indefinite deferral of gains while hedging positions.

48. Correct Answer: D (Unrealized gains and losses)

Mark-to-market election for securities traders requires annual recognition of unrealized gains and losses—all positions are treated as sold at fair market value on the last business day of the year. This election converts capital gains and losses to ordinary income and losses, allowing full deduction of trading losses

against ordinary income without the \$3,000 limitation. The election must be made by the due date of the prior year's return.

49. Correct Answer: C (December 31, 2026)

Qualified opportunity fund investments allow deferral of capital gains until December 31, 2026, or the earlier sale or exchange of the QOF investment. Taxpayers must invest the gain amount (not the entire proceeds) within 180 days of recognizing the gain. Holding the QOF investment for at least 5 years excludes 10% of the deferred gain; 7 years excludes 15%. Holding 10 years allows exclusion of appreciation on the QOF investment itself.

50. Correct Answer: B (Gross profit percentage)

Installment sale income recognition uses the gross profit percentage—the ratio of gross profit to contract price. This percentage is applied to each payment received to determine the taxable gain. The method spreads gain recognition over the payment period, matching taxation with cash receipt. Interest on deferred payments is separately taxable. The installment method is not available for dealer dispositions or publicly traded securities.

51. Correct Answer: D (Real property)

Like-kind exchange treatment under Section 1031 applies only to real property (real estate) after the Tax Cuts and Jobs Act. Before 2018, personal property qualified, but TCJA eliminated personal property exchanges from Section 1031. The real property must be held for investment or use in a trade or business. Primary residences, inventory, securities, and partnership interests don't qualify. Both properties must be located in the United States.

52. Correct Answer: A (Taxable)

Boot (cash or other property received that doesn't qualify for like-kind treatment) in a like-kind exchange is taxable to the extent of realized gain. If boot received is less than realized gain, the boot amount is taxed. If boot exceeds realized gain, only the gain is taxed. Boot received reduces the amount of gain that can be deferred. The basis in the new property is adjusted for boot received and gain recognized.

53. Correct Answer: C (2 years)

Related party like-kind exchanges require both parties to hold the exchanged properties for at least 2 years after the exchange to avoid having the gain recognized. If either party disposes of the property within 2 years (other than by death, involuntary conversion, or non-tax-avoidance transactions), both parties must recognize the deferred gain. This prevents related parties from using exchanges to shift basis without economic substance.

54. Correct Answer: B (2 years)

Involuntary conversions (such as condemnation) require replacement property to be acquired within 2 years after the close of the first tax year in which any gain is realized (generally 2 years from the date of

condemnation). For condemned property held for business or investment, this allows time to find and purchase replacement property. The replacement period can be extended to 3 years for certain condemned real property.

55. Correct Answer: A (2 of last 5 years)

The home sale exclusion requires ownership and use of the property as a principal residence for at least 2 years (24 months, not necessarily consecutive) during the 5-year period ending on the date of sale. Temporary absences for vacation or seasonal use count as use. The ownership and use tests don't need to overlap—a taxpayer could rent before buying or rent after buying and still meet both tests.

56. Correct Answer: D (\$250,000)

Single taxpayers can exclude up to \$250,000 of gain from the sale of a principal residence if they meet the ownership and use tests. The exclusion can be used repeatedly, but not more frequently than once every 2 years. Gain exceeding the exclusion is taxed as long-term capital gain (if held over one year). The exclusion significantly reduces or eliminates tax on most home sales.

57. Correct Answer: C (\$500,000)

Married couples filing jointly can exclude up to \$500,000 of gain on the sale of a principal residence if either spouse meets the ownership test, both meet the use test, and neither used the exclusion in the prior 2 years. For surviving spouses, the \$500,000 exclusion is available if the home is sold within 2 years of the spouse's death. The larger exclusion recognizes the higher cost of housing for families.

58. Correct Answer: B (Employment, health, unforeseen)

Partial home sale exclusion is available when the sale occurs due to a change in employment, health, or unforeseen circumstances, even if the 2-year ownership/use tests aren't met. The exclusion is prorated based on the time the tests were met. Examples include job relocation, doctor-recommended move for health, divorce, or multiple births. IRS provides safe harbors for qualifying changes. Changes in income, family size, or market value alone don't qualify.

59. Correct Answer: D (2 years)

Rental property converted to a principal residence requires use as a principal residence for at least 2 years to qualify for the home sale exclusion. However, gain attributable to periods of non-qualified use (such as rental periods after 2008) doesn't qualify for exclusion. Depreciation taken on the property is subject to 25% recapture even if the property qualifies for the exclusion. The conversion must involve actual residence use, not just ownership.

60. Correct Answer: A (15.3%)

Self-employment tax rate on net earnings from self-employment is 15.3%, consisting of 12.4% for Social Security (on earnings up to \$168,600 for 2024) and 2.9% for Medicare (on all earnings). Self-employed

individuals pay both the employer and employee portions of FICA taxes. An additional 0.9% Medicare tax applies to self-employment income exceeding \$200,000 (single) or \$250,000 (married filing jointly).

61. Correct Answer: C (\$168,600)

The Social Security wage base for 2024 is \$168,600. Self-employment income up to this amount is subject to the 12.4% Social Security portion of self-employment tax. Earnings exceeding this threshold are subject only to the 2.9% Medicare portion (plus 0.9% additional Medicare tax if applicable thresholds are exceeded). The wage base is indexed annually for inflation.

62. Correct Answer: B (Net earnings from self-employment)

Self-employment income includes net earnings from self-employment—income from a trade or business operated as a sole proprietor or independent contractor, minus expenses. It includes Schedule C income, partnership distributive share (for general partners), and farming income. Wages, investment income (interest, dividends, capital gains), and pensions are not self-employment income. Only earned income from business activities is subject to self-employment tax.

63. Correct Answer: A (Subject to self-employment tax)

Ministers' housing allowance is excluded from income tax but subject to self-employment tax. The exclusion is limited to the lesser of the amount designated as housing allowance, actual housing expenses, or fair rental value of the home plus furnishings and utilities. Ministers can elect out of self-employment tax on ministerial earnings by filing Form 4361, but only if conscientiously opposed to public insurance on religious grounds.

64. Correct Answer: D (Not allowed)

Net operating loss carryback is generally not allowed for individuals for losses arising after 2017. The Tax Cuts and Jobs Act eliminated NOL carrybacks (except for farming losses and certain casualty losses). The CARES Act temporarily restored 5-year carrybacks for 2018-2020 losses, but the general rule prohibits carrybacks. NOLs carry forward indefinitely but can offset only 80% of taxable income.

65. Correct Answer: B (Indefinite)

NOL carryforwards for individuals are indefinite—they never expire. Losses can be carried forward to offset future income without time limitation. However, the NOL deduction is limited to 80% of taxable income (before the NOL deduction) in the carryforward year, ensuring taxpayers pay some tax even with NOL carryforwards. This limitation applies to losses arising after 2017.

66. Correct Answer: C (\$305,000)

The excess business loss limitation for 2024 is approximately \$305,000 for single filers (\$610,000 for married filing jointly), adjusted annually for inflation. Business losses exceeding these amounts cannot offset non-business income (wages, investment income) in the current year. Excess losses are treated as

net operating loss carryforwards to future years. This limitation prevents high-income taxpayers from using large business losses to shelter other income.

67. Correct Answer: C (\$85,700)

The Alternative Minimum Tax exemption for single filers in 2024 is approximately \$85,700 (adjusted annually for inflation). For married filing jointly, the exemption is approximately \$133,300, and for married filing separately it's approximately \$66,650. The exemption phases out at a rate of 25 cents per dollar when alternative minimum taxable income (AMTI) exceeds \$609,350 for single filers and \$1,218,700 for married filing jointly. The AMT applies when tentative minimum tax (26% on AMTI up to approximately \$232,600, then 28% above that, reduced by the exemption amount) exceeds regular tax. The exemption reduces AMTI before calculating tentative minimum tax, providing significant relief for moderate-income taxpayers while targeting AMT to higher-income taxpayers using preference items and adjustments.

68. Correct Answer: A (26% and 28%)

AMT rates are 26% on the first \$220,700 of alternative minimum taxable income (2024, MFS uses half) and 28% on amounts above that threshold. These rates are lower than the top ordinary income rates but higher than preferential capital gains rates. AMT is calculated separately from regular tax, and taxpayers pay the higher of the two. The two-tier rate structure provides some progressivity within the AMT system.

69. Correct Answer: B (\$609,350)

The AMT exemption phase-out for single filers begins at approximately \$609,350 for 2024 (adjusted annually). The exemption is reduced by 25 cents for each dollar of alternative minimum taxable income exceeding this threshold. For married filing jointly, the phase-out begins at approximately \$1,218,700. The phase-out ensures high-income taxpayers pay AMT by reducing or eliminating their exemption.

70. Correct Answer: C (Spread between FMV and exercise price)

Incentive stock option (ISO) exercise creates an AMT preference equal to the spread (bargain element) between the fair market value of the stock at exercise and the exercise price. This preference increases alternative minimum taxable income, potentially triggering AMT. The spread is not included in regular taxable income at exercise. If the stock is later sold in a disqualifying disposition, the previously reported AMT preference is removed through an AMT adjustment.

71. Correct Answer: A (AMT preference item)

Private activity bond interest is an AMT preference item that increases alternative minimum taxable income, even though it's excluded from regular taxable income. Private activity bonds are issued by state or local governments for certain private projects like airports, student loans, or affordable housing. The AMT preference treatment limits the tax benefit of these bonds for high-income taxpayers subject to AMT.

72. Correct Answer: D (150% declining balance)

For AMT purposes, depreciation on personal property placed in service before 1999 uses the 150% declining balance method rather than the 200% (double) declining balance method used for regular tax. This slower depreciation creates a positive AMT adjustment. Property placed in service after 1998 generally uses the same depreciation for both regular tax and AMT, eliminating this adjustment for newer property.

73. Correct Answer: B (1116)

The foreign tax credit is claimed on Form 1116, Foreign Tax Credit (Individual, Estate, or Trust). The form calculates the credit for income taxes paid to foreign countries, preventing double taxation of foreign-source income. Separate Forms 1116 may be required for different categories of income (passive, general, etc.). The credit is limited to the U.S. tax on foreign-source income, preventing foreign taxes from offsetting U.S. tax on U.S.-source income.

74. Correct Answer: C (\$126,500)

The foreign earned income exclusion for 2024 is approximately \$126,500 (adjusted annually for inflation). Qualifying taxpayers can exclude this amount of foreign earned income from U.S. taxation if they meet the bona fide residence test or physical presence test. The exclusion applies only to earned income (wages, self-employment income), not to passive income (interest, dividends, capital gains). A separate housing exclusion or deduction may also be available.

75. Correct Answer: A (Full tax year)

The bona fide residence test for the foreign earned income exclusion requires being a bona fide resident of a foreign country for an uninterrupted period that includes an entire tax year (January 1 through December 31 for calendar year taxpayers). The test focuses on intent and facts showing establishment of foreign residence. Once established for a full year, qualification continues as long as bona fide residence continues, even if brief trips are made to the U.S.

76. Correct Answer: D (330 days in 12 months)

The physical presence test requires being physically present in a foreign country or countries for at least 330 full days during any 12-month consecutive period. The 330 days don't need to be consecutive. The 12-month period can begin on any day, not just January 1. Physical presence is easier to prove than bona fide residence but requires careful day-counting to meet the 330-day threshold.

77. Correct Answer: C (16% of FEIE)

The foreign housing exclusion applies to qualified housing expenses exceeding the base amount, which is 16% of the foreign earned income exclusion. For 2024, the base amount is approximately 16% of \$126,500, or about \$20,240. Expenses above this base (up to a limit, generally 30% of FEIE) can be excluded. The exclusion recognizes that housing costs abroad often exceed U.S. housing costs.

78. Correct Answer: B (\$10,000)

The FBAR (Report of Foreign Bank and Financial Accounts, FinCEN Form 114) filing requirement is triggered when a U.S. person has a financial interest in or signature authority over foreign financial accounts with an aggregate value exceeding \$10,000 at any time during the calendar year. The \$10,000 threshold is based on the combined total of all foreign accounts—not per account. For example, if a taxpayer has three foreign accounts with balances of \$4,000, \$5,000, and \$2,000, the aggregate value is \$11,000, requiring FBAR filing even though no single account exceeds \$10,000. FBAR is filed electronically with FinCEN (not with tax returns) by April 15 with automatic extension to October 15. Penalties for willful failure to file can be severe, including criminal penalties for intentional violations.

79. Correct Answer: D (\$50,000)

Form 8938, Statement of Specified Foreign Financial Assets, has a filing threshold for unmarried taxpayers living in the U.S. of \$50,000 on the last day of the year or \$75,000 at any time during the year. Higher thresholds apply to married couples and those living abroad. Form 8938 is filed with the tax return and reports foreign financial assets, overlapping but not duplicating FBAR requirements. Penalties for non-filing can be substantial.

80. Correct Answer: A (\$10,000 or 50% of account)

Penalties for willful failure to file FBAR can reach the greater of \$100,000 or 50% of the account balance per violation. Non-willful violations face penalties up to \$10,000 per violation. Criminal penalties can include fines up to \$250,000 and imprisonment. The severe penalties reflect the government's emphasis on detecting offshore tax evasion. Penalties can be mitigated through voluntary disclosure programs.

81. Correct Answer: C (7.5% of AGI)

Medical expense deductions require total expenses to exceed 7.5% of adjusted gross income. Only the amount exceeding this floor is deductible. Qualified medical expenses include payments for diagnosis, cure, mitigation, treatment, or prevention of disease, and for treatments affecting body structure or function. Insurance premiums (if not paid pre-tax), prescription drugs, and medical devices qualify. The 7.5% floor significantly limits the deduction for most taxpayers.

82. Correct Answer: B (Age)

Long-term care insurance premium deduction limits are based on the insured's age at the end of the year. For 2024, limits range from approximately \$470 (age 40 or younger) to \$5,880 (over age 70), adjusted annually for inflation. Only qualified long-term care insurance contracts qualify. Premiums are deductible as medical expenses subject to the 7.5% of AGI floor (or as self-employed health insurance deduction if applicable).

83. Correct Answer: D (\$10,000)

State and local tax (SALT) deductions are limited to \$10,000 per year (\$5,000 for married filing separately) for tax years 2018-2025 under the Tax Cuts and Jobs Act. The limit is a combined total for

state and local income taxes (or sales taxes if elected) plus property taxes. This limitation significantly affects taxpayers in high-tax states and is one of the most controversial provisions of TCJA.

84. Correct Answer: D (\$750,000)

The mortgage interest deduction is limited to acquisition debt of \$750,000 for married filing jointly (\$375,000 for married filing separately) for loans taken out after December 15, 2017. Acquisition debt is debt used to buy, build, or substantially improve the principal residence or second home, secured by that home. Loans taken out on or before December 15, 2017, are grandfathered under the old \$1 million limit (\$500,000 married filing separately). The reduced limit was part of the Tax Cuts and Jobs Act. Interest on home equity debt used for purposes other than improving the home (such as paying off credit cards or college tuition) is no longer deductible. Only interest on the qualified loan amount up to the limit is deductible.

85. Correct Answer: C (Improve home)

Home equity debt interest is deductible only if the loan proceeds are used to buy, build, or substantially improve the taxpayer's home that secures the loan. Interest on home equity debt used for personal expenses, buying a car, or paying credit cards is not deductible under current law (2018-2025). The total of acquisition and home equity debt is subject to the \$750,000 limit (\$1 million for pre-2018 loans).

86. Correct Answer: B (Net investment income)

Investment interest expense is deductible only to the extent of net investment income (investment income minus investment expenses). Investment income includes interest, dividends (unless claimed at capital gains rates), annuities, and royalties from passive activities. Capital gains can be included if the taxpayer elects to give up preferential rates. Disallowed interest carries forward indefinitely to future years when investment income is available.

87. Correct Answer: A (60% of AGI)

Charitable contribution deductions for cash donations to public charities are limited to 60% of adjusted gross income (increased from 50% by the Tax Cuts and Jobs Act). Contributions to private foundations and certain other organizations are limited to 30% of AGI. Contributions exceeding these limits can be carried forward for 5 years. The higher limit for cash to public charities encourages direct giving to operating charities.

88. Correct Answer: D (30% of AGI)

Charitable contributions of appreciated capital gain property held long-term to public charities are limited to 30% of adjusted gross income. Alternatively, taxpayers can elect to deduct the property's basis (rather than fair market value) and use the 60% limit. For contributions to private foundations, appreciated property is limited to 20% of AGI and generally must be reduced to basis. The lower limits for property donations reflect the larger tax benefit from deducting fair market value.

89. Correct Answer: C (\$100,000)

Qualified charitable distributions (QCDs) from IRAs allow taxpayers age 70½ or older to transfer up to \$100,000 annually directly from IRAs to qualified charities. The distribution is excluded from income and counts toward required minimum distributions but doesn't generate a charitable deduction. This provides tax benefits even for taxpayers who don't itemize. QCDs must go directly from the IRA to the charity.

90. Correct Answer: B (5 years)

Excess charitable contribution carryforwards are allowed for 5 years. Contributions exceeding the AGI limitations carry forward and retain their character (cash vs. property, public charity vs. private foundation). Carryforwards are used after current year contributions of the same type. Unused carryforwards expire after 5 years. The carryforward allows taxpayers to benefit from large charitable gifts over multiple years.

91. Correct Answer: C (35%)

The dependent care credit rate ranges from 20% to 35% of qualifying expenses, depending on adjusted gross income. The maximum rate of 35% applies to taxpayers with AGI up to \$15,000. The rate decreases by 1% for each \$2,000 of AGI above \$15,000, until reaching the minimum rate of 20% at AGI of \$43,000 or more. The sliding scale targets benefits to lower-income taxpayers.

92. Correct Answer: B (\$3,000)

The child and dependent care credit maximum qualifying expenses are \$3,000 for one qualifying individual or \$6,000 for two or more. These limits haven't been indexed for inflation and have remained unchanged for many years. The credit percentage (20%-35%) is applied to qualifying expenses to determine the credit. The American Rescue Plan temporarily increased limits for 2021 only, but they returned to \$3,000/\$6,000 for subsequent years.

93. Correct Answer: A (\$2,000)

The child tax credit for 2024 is \$2,000 per qualifying child under age 17. The American Rescue Plan temporarily increased the credit to \$3,000/\$3,600 for 2021, but it returned to \$2,000 for 2022 and later years. The credit phases out at higher income levels: \$200,000 for single filers, \$400,000 for married filing jointly. Up to \$1,700 is refundable as the additional child tax credit.

94. Correct Answer: D (\$1,700)

The additional child tax credit (refundable portion) for 2024 is up to \$1,700 per qualifying child (adjusted annually for inflation). This allows taxpayers with little or no tax liability to receive a refund based on the child tax credit. The refundable amount is the lesser of the unused child tax credit or 15% of earned income exceeding \$2,500. The additional child tax credit helps low-income working families.

95. Correct Answer: B (\$400,000)

The child tax credit begins phasing out at \$400,000 modified AGI for married filing jointly (\$200,000 for other filers). The credit is reduced by \$50 for each \$1,000 (or fraction thereof) of modified AGI exceeding

the threshold. The phase-out can eliminate the credit for high-income taxpayers. The threshold has increased over time, expanding credit availability to middle- and upper-middle-class families.

96. Correct Answer: C (\$500)

The credit for other dependents is \$500 per qualifying dependent who doesn't qualify for the child tax credit. This includes dependents age 17 or older, dependents who don't have Social Security numbers, and other qualifying relatives. The credit is nonrefundable—it can reduce tax to zero but not create a refund. It's subject to the same income phase-outs as the child tax credit.

97. Correct Answer: D (3)

The earned income credit maximum number of qualifying children is 3. Credit amounts increase with each qualifying child up to three children, then plateau. For 2024, the maximum EITC is approximately \$7,830 for three or more children, \$6,960 for two children, \$4,213 for one child, and \$632 for no children. Qualifying children must meet age, relationship, and residency tests. The EITC is fully refundable.

98. Correct Answer: A (8962)

Premium tax credit reconciliation uses Form 8962, Premium Tax Credit. The form reconciles advance premium tax credits received during the year with the actual premium tax credit based on final household income. If advance credits exceeded the allowable credit, taxpayers must repay the excess (subject to caps for lower-income taxpayers). If actual credit exceeds advance credits, taxpayers receive the difference as a refund. Form 1095-A provides information needed for Form 8962.

99. Correct Answer: C (30%)

The residential energy credit for qualified expenditures (solar electric, solar water heating, fuel cells, wind energy, biomass fuel, geothermal heat pumps) is 30% of costs for property placed in service through 2032. The credit then decreases to 26% (2033) and 22% (2034), expiring after 2034. The credit has no annual or lifetime dollar limit for most technologies (except fuel cells). Battery storage technology was added to qualifying property in recent years.

100. Correct Answer: B (\$7,500)

The electric vehicle credit maximum for new qualified plug-in electric vehicles is \$7,500. The credit has two components: \$3,750 for meeting battery component requirements and \$3,750 for meeting critical mineral requirements. Vehicles must meet MSRP limits (\$80,000 for vans, SUVs, trucks; \$55,000 for other vehicles) and buyer income limits (\$300,000 MFJ, \$225,000 HOH, \$150,000 single). Starting in 2024, the credit can be transferred to dealers as a point-of-sale rebate.

Part 2: Businesses

1. Correct Answer: B (Accrual method)

Cash method businesses with inventory must account for inventory using the accrual method, even if they use the cash method for other income and expenses. This requirement ensures proper matching of costs with related sales. However, small business taxpayers (average annual gross receipts of \$29 million or less) are exempt from inventory accounting requirements and can use the cash method throughout, treating inventory as non-incidental materials and supplies.

2. Correct Answer: C (\$29 million)

The small business taxpayer exemption from inventory accounting and other complex accounting rules applies when average annual gross receipts for the prior three tax years don't exceed \$29 million (2024, adjusted for inflation). Qualifying businesses can use the cash method, avoid UNICAP, and treat inventory as non-incidental materials and supplies (deductible when paid). This simplification reduces compliance burdens for smaller businesses.

3. Correct Answer: A (Long-term contracts)

The percentage of completion method applies to long-term contracts—generally contracts not completed within the same tax year they begin. Under this method, income is recognized based on the percentage of the contract completed during the year, determined by comparing costs incurred to total estimated costs. This method better matches revenue with costs than waiting until contract completion. Exceptions exist for small construction contracts and home construction contracts.

4. Correct Answer: D (Small construction contracts)

The completed contract method (deferring all income and costs until contract completion) is generally not allowed except for small construction contracts—contracts estimated to be completed within 2 years by taxpayers meeting the small business taxpayer exception (\$29 million gross receipts test). Home construction contracts can also use the completed contract method. Large contractors and long-term contracts must use the percentage of completion method.

5. Correct Answer: C (Producers and large retailers)

Uniform capitalization (UNICAP) rules apply to producers of real or tangible personal property and resellers with average annual gross receipts exceeding \$29 million. UNICAP requires capitalizing direct costs and allocable indirect costs into inventory or self-constructed assets. Small businesses (\$29 million or less average gross receipts) are exempt. Service providers are generally exempt regardless of size because they don't produce or resell tangible property.

6. Correct Answer: B (Direct and indirect production costs)

UNICAP requires capitalizing both direct costs (materials, labor directly involved in production) and allocable indirect costs (overhead, storage, purchasing, handling, administrative). Selling expenses are never capitalized. General and administrative expenses are capitalized only to the extent allocable to production. Interest expense may require capitalization under separate rules for self-constructed property or long production period property. The capitalized costs become part of inventory or asset basis.

7. Correct Answer: D (15% of gross income)

Percentage depletion for oil and gas producers is limited to 15% of gross income from the property. Independent producers can use percentage depletion instead of cost depletion. Percentage depletion can exceed the property's basis (unlike cost depletion, which cannot). The deduction is further limited to 65% of taxable income (computed without depletion). Integrated oil companies cannot use percentage depletion—they must use cost depletion.

8. Correct Answer: A (Adjusted basis)

Cost depletion is based on the adjusted basis of the natural resource property divided by the estimated recoverable units, determining a per-unit depletion amount. This per-unit amount is multiplied by units sold during the year. Cost depletion cannot exceed the property's adjusted basis—once basis is fully recovered, no more cost depletion is allowed. Percentage depletion, where available, can exceed basis.

9. Correct Answer: B (\$1,220,000)

The Section 179 expensing limit for 2024 is approximately \$1,220,000 (adjusted annually for inflation). This allows businesses to immediately expense (rather than depreciate) qualifying property placed in service. Qualifying property includes tangible personal property, certain improvements to nonresidential real property, and computer software. The limit is reduced dollar-for-dollar when total qualifying property placed in service exceeds the phase-out threshold.

10. Correct Answer: C (\$3,050,000)

Section 179 expensing begins phasing out when the total cost of qualifying property placed in service exceeds approximately \$3,050,000 for 2024 (adjusted annually). The \$1,220,000 limit is reduced dollar-for-dollar by the excess. When property placed in service reaches \$4,270,000, the deduction is completely phased out. This phase-out targets the benefit to smaller businesses with limited equipment purchases.

11. Correct Answer: D (60%)

Bonus depreciation under Section 168(k) for property placed in service during 2024 is 60%. After being 100% for property placed in service from September 28, 2017, through December 31, 2022, bonus depreciation is phasing down on the following schedule: 80% for 2023, 60% for 2024, 40% for 2025, 20% for 2026, and 0% for 2027 and later years. Bonus depreciation applies to qualified property with a MACRS recovery period of 20 years or less, including most tangible personal property and qualified improvement property. The gradual phase-down encourages capital investment while transitioning away from the temporary 100% expensing benefit.

12. Correct Answer: B (\$12,200)

The luxury automobile depreciation first-year limit without bonus depreciation for passenger automobiles placed in service in 2024 is approximately \$12,200 (adjusted annually for inflation). With bonus depreciation (60% for 2024), an additional amount of approximately \$20,000 can be claimed in the first year, bringing the total first-year limit to around \$32,200. These limits apply to passenger automobiles

(vehicles with gross vehicle weight of 6,000 pounds or less). Trucks and vans have slightly higher limits. Vehicles over 6,000 pounds are exempt from luxury auto limits but face Section 179 limitations for vehicles between 6,000 and 14,000 pounds.

13. Correct Answer: A (\$29,200)

Heavy SUVs and trucks with gross vehicle weight over 6,000 pounds are exempt from luxury auto depreciation limits but Section 179 expensing is limited to approximately \$29,200 (2024, adjusted for inflation). Amounts exceeding this limit must be depreciated. Bonus depreciation (if available) applies without limit to these vehicles. The limit prevents businesses from fully expensing very expensive heavy vehicles in year one.

14. Correct Answer: C (50%)

Listed property business use must exceed 50% to qualify for regular depreciation methods (MACRS with accelerated depreciation), bonus depreciation, and Section 179 expensing. If business use is 50% or less, the property must use the straight-line method over the ADS recovery period, and no Section 179 or bonus depreciation is allowed. Listed property includes passenger automobiles, computers (unless at regular business establishment), and certain other property.

15. Correct Answer: B (7 years)

Office furniture and fixtures have a MACRS recovery period of 7 years (using 200% declining balance method with half-year convention). This classification includes desks, chairs, file cabinets, and similar items. The 7-year class also includes office equipment not otherwise classified. Computers and peripheral equipment are 5-year property. Most other personal property used in business falls into 5-year or 7-year classes.

16. Correct Answer: A (27.5 years)

Residential rental property (apartments, rental houses) has a MACRS recovery period of 27.5 years using the straight-line method and mid-month convention. "Residential rental property" means buildings where 80% or more of gross rental income is from dwelling units. Single-family rentals, duplexes, and apartment buildings qualify. The longer recovery period reflects real estate's longer useful life and slower obsolescence compared to personal property.

17. Correct Answer: D (15 years)

Section 197 intangibles (goodwill, going concern value, workforce in place, business books and records, customer lists, patents, copyrights, licenses, permits, franchises, trademarks, trade names, and certain other intangibles) acquired in connection with acquiring a trade or business must be amortized over 15 years using the straight-line method, regardless of actual useful life. This mandatory amortization period simplifies taxation and prevents disputes over useful lives.

18. Correct Answer: C (Amortized over 15 years)

Goodwill acquired in a business purchase is a Section 197 intangible amortized over 15 years. Goodwill represents the excess of purchase price over the fair market value of identifiable assets acquired. Self-created goodwill is not amortizable—only purchased goodwill qualifies. The 15-year amortization period is mandatory regardless of whether the business expects the goodwill to last longer or shorter than 15 years.

19. Correct Answer: A (Capitalized and amortized)

Research and experimentation (R&E) expenditures for 2024 must be capitalized and amortized over 5 years (U.S. research) or 15 years (foreign research), beginning with the midpoint of the tax year. This requirement began in 2022 under the Tax Cuts and Jobs Act. Previously, R&E costs could be currently expensed or amortized at the taxpayer's election. The mandatory capitalization generated significant revenue but is controversial because it reduces incentives for innovation.

20. Correct Answer: B (\$50,000)

Startup costs can be deducted up to \$5,000 in the year business begins, but this amount is reduced dollar-for-dollar when total startup costs exceed \$50,000. When startup costs reach \$55,000, the first-year deduction is completely phased out. Startup costs exceeding the first-year deduction are amortized over 180 months. Startup costs include investigating creating/acquiring a business, creating an active business, and pre-opening activities.

21. Correct Answer: D (\$30 million)

The business interest limitation applies to taxpayers (other than small businesses) with average annual gross receipts exceeding \$30 million for the prior three tax years (2024, adjusted for inflation). The limitation restricts business interest deductions to the sum of business interest income plus 30% of adjusted taxable income. Disallowed interest carries forward indefinitely. Small businesses (\$30 million or less) are exempt from this limitation.

22. Correct Answer: C (Adjusted taxable income)

Business interest deduction is limited to business interest income plus 30% of adjusted taxable income (ATI). For 2024 and later, ATI is computed without deductions for depreciation, amortization, or depletion (similar to EBITDA minus those items). Before 2022, ATI was computed before depreciation/amortization (similar to EBITDA). The change to excluding depreciation/amortization from ATI tightened the limitation, reducing allowable interest deductions.

23. Correct Answer: B (Indefinitely)

Disallowed business interest carries forward indefinitely—there's no time limit. The carryforward can be used in future years when the 30% limitation allows. The indefinite carryforward ensures businesses eventually get the deduction. However, the carryforward doesn't increase the 30% limitation in future years—it's only available to the extent the current year limitation isn't fully used by current year interest.

24. Correct Answer: A (50%)

Meals expenses are deductible at 50% for 2024. The deduction covers meals provided to employees, meals while traveling on business, and meals with business associates when there's a direct business purpose. The 50% limitation recognizes the personal benefit component of meals. Certain exceptions exist: employee meals on employer premises for employer's convenience (100% before 2026, then 50%), company cafeterias for employees, and meals at conferences (typically 50%).

25. Correct Answer: C (Not deductible)

Entertainment expenses are not deductible after the Tax Cuts and Jobs Act. This includes tickets to sporting events, concerts, theater, golf outings, and similar entertainment, even when conducted with clients or employees and even when business is discussed. The elimination of entertainment deductions simplifies recordkeeping and reduces disputes over what constitutes entertainment versus meals. Meals separate from entertainment remain 50% deductible.

26. Correct Answer: C (\$25)

Business gifts are limited to \$25 per recipient per tax year under Section 274(b). This limit has remained unchanged since 1962. Gifts to a husband and wife count as gifts to one recipient unless each has an independent business relationship with the donor. Incidental costs like engraving, packaging, and mailing don't count toward the \$25 limit. Items costing \$4 or less with the business name permanently imprinted (such as pens, calendars, or keychains) are not considered gifts and aren't subject to the limit. The low \$25 threshold reflects longstanding concern about disguising entertainment or personal expenses as business gifts, though inflation has made this limit increasingly restrictive over the decades.

27. Correct Answer: A (Hobby income)

Hobby loss rules allow deductions only to the extent of hobby income. For 2018-2025, hobby expenses are not deductible at all due to suspension of miscellaneous itemized deductions. Before 2018, hobby expenses were deductible as miscellaneous itemized deductions subject to 2% of AGI floor, but only to the extent of hobby income. Hobbies are distinguished from businesses by lack of profit motive—if no profit in 3 of 5 years (2 of 7 for horse activities), rebuttable presumption of hobby exists.

28. Correct Answer: B (250 hours)

The safe harbor for rental real estate to qualify as a trade or business for QBI purposes requires 250 or more hours of rental services annually. Services include advertising, negotiating leases, tenant screening, rent collection, repairs, and maintenance. Contemporaneous records must be maintained. The safe harbor (Revenue Procedure 2019-38) provides certainty for rental property owners seeking to claim the Section 199A qualified business income deduction without proving Section 162 trade or business status.

29. Correct Answer: C (500 hours)

Material participation tests include several alternatives, one of which is participating in the activity for more than 500 hours during the year. This is the simplest and most commonly used test. Other tests include: substantially all participation, more than 100 hours with no one else participating more,

significant participation activities totaling over 500 hours, material participation in 5 of prior 10 years, personal service activity with material participation in 3 prior years, or facts and circumstances showing regular, continuous, substantial involvement.

30. Correct Answer: D (500 hours)

The significant participation test requires participating more than 100 hours in each of multiple activities (significant participation activities), with total participation in all such activities exceeding 500 hours. This test recognizes that multiple part-time activities can collectively demonstrate material participation. Each activity must involve over 100 hours, and together they must exceed 500 hours for the year. This test helps taxpayers with several businesses avoid passive loss limitations.

31. Correct Answer: D (Rental activities and non-material participation)

Passive activity loss limitations apply to (1) rental activities (generally passive regardless of participation, unless real estate professional) and (2) business activities in which the taxpayer doesn't materially participate. Passive losses can offset only passive income—they cannot offset active income (wages, business income from material participation activities) or portfolio income (interest, dividends). Material participation makes business activities active, avoiding passive loss limitations.

32. Correct Answer: A (750 hours)

Real estate professional status requires (1) more than half of personal services performed during the year in real property trades or businesses and (2) performing more than 750 hours in real property trades or businesses. Meeting these tests allows rental real estate activities to avoid automatic passive classification and be tested for material participation. Without real estate professional status, rental activities are automatically passive regardless of participation level.

33. Correct Answer: C (\$150,000)

The \$25,000 rental loss allowance for active participation in rental real estate phases out when AGI exceeds \$100,000, with complete phase-out at \$150,000. The allowance is reduced by 50 cents for each dollar of AGI over \$100,000. Active participation is easier to meet than material participation—it requires making management decisions (tenant approval, repairs, rental terms) but not regular, continuous, substantial involvement. The allowance helps small landlords offset rental losses against other income.

34. Correct Answer: B (Passive income)

Passive activity credits (such as low-income housing credit, rehabilitation credit, or credits from passive investments) can only offset tax attributable to passive income—they cannot reduce tax on active or portfolio income. Unlike passive losses (which can offset any income when the activity is fully disposed of), passive credits remain limited to passive income even at disposition. Unused passive credits carry forward indefinitely.

35. Correct Answer: A (Activity disposed of)

Suspended passive losses are fully released and can offset any income (active or portfolio) when the activity is fully disposed of in a fully taxable transaction to an unrelated party. The disposition must be complete—selling part of an activity doesn't release losses. Gifting or transferring at death doesn't release suspended losses. The release provision prevents permanent loss of deductions when the taxpayer exits the passive activity.

36. Correct Answer: D (Amount at risk)

At-risk limitations prevent deducting losses exceeding the amount the taxpayer has at risk—the amount the taxpayer could actually lose. Amount at risk includes cash and property contributed, recourse debt (where the taxpayer is personally liable), and qualified nonrecourse financing for real property. Losses exceeding the at-risk amount are suspended until the at-risk amount increases through additional contributions, income, or assumption of recourse debt.

37. Correct Answer: C (Real property)

Qualified nonrecourse financing increases at-risk basis only for real property activities. The financing must be from a qualified lender (not sellers or related parties), secured only by the real property, and represent arm's-length terms. This exception recognizes that nonrecourse financing is standard and economically sound for real estate. Personal property or service activities cannot increase at-risk basis with nonrecourse debt.

38. Correct Answer: A (Form 1065)

Partnership income is reported on Form 1065, U.S. Return of Partnership Income. Form 1065 is an information return—partnerships don't pay income tax. The form reports partnership income, gains, losses, deductions, and credits, which flow through to partners on Schedule K-1. Form 1120 is for C corporations, Form 1120-S for S corporations, and Schedule C for sole proprietors.

39. Correct Answer: B (Schedule K-1)

Partnership income flows through to partners on Schedule K-1 (Form 1065), Partner's Share of Income, Deductions, Credits, etc. Each partner receives a K-1 showing their distributive share of partnership items. Partners report these amounts on their individual returns. The K-1 separately states items that might receive special tax treatment (capital gains, Section 1231 gains, charitable contributions, foreign taxes, etc.).

40. Correct Answer: D (Liabilities)

Partner basis includes the partner's share of partnership liabilities. Increases in partnership liabilities increase partner basis; decreases in liabilities decrease basis. This treatment recognizes that partners are at risk for partnership debt and may be called upon to satisfy it. Recourse debt is allocated to partners who bear the economic risk of loss. Nonrecourse debt is generally allocated according to profit-sharing ratios.

41. Correct Answer: D (Distributions)

Partner basis is reduced by distributions received from the partnership (cash or property). Distributions first reduce basis; distributions exceeding basis create taxable gain (usually capital gain). Basis is increased by the partner's share of income (including tax-exempt income) and contributions. Basis is decreased by the partner's share of losses and deductions, nondeductible expenses, and distributions. Proper basis tracking is essential for determining loss limitations and tax consequences of distributions.

42. Correct Answer: C (Ordinary income)

Guaranteed payments to partners are compensation for services or use of capital, paid without regard to partnership income. They're treated as ordinary income to the receiving partner and are deductible by the partnership (or capitalized if appropriate). Guaranteed payments are reported separately on Schedule K-1 and are subject to self-employment tax if for services. They differ from distributive shares, which are allocations of partnership income.

43. Correct Answer: B (Substantial economic effect)

Special allocations in partnerships (allocations different from ownership percentages) must have substantial economic effect to be respected for tax purposes. This requires (1) allocation reflected in capital accounts, (2) liquidation based on capital accounts, and (3) partners with deficit capital account balances must restore them. The substantial economic effect requirement prevents tax-motivated allocations that don't reflect economic reality. Allocations lacking substantial economic effect are reallocated based on partners' interests in the partnership.

44. Correct Answer: D (Capital gain)

Partnership distributions of cash exceeding the partner's basis create capital gain (usually long-term if the partnership interest was held long-term). Distributions at or below basis are tax-free returns of investment. Property distributions generally don't create gain unless basis is reduced below zero. This treatment recognizes that distributions exceeding basis represent recoveries exceeding the partner's investment, similar to sales proceeds exceeding basis.

45. Correct Answer: C (Ordinary or capital depending on type)

Section 736 payments for a deceased or retired partner's interest can be treated as either (1) Section 736(b) payments (for the partner's share of partnership property, treated as distributions creating capital gain if exceeding basis) or (2) Section 736(a) payments (for goodwill and unrealized receivables in certain partnerships, treated as distributive share or guaranteed payments, generally ordinary income). The classification depends on what's being paid for and the partnership's characteristics (capital vs. service partnership).

46. Correct Answer: A (50%)

In a partnership merger, the continuing partnership is the one whose partners owned more than 50% of the capital and profits in the resulting partnership immediately after the merger. Partners of the terminated partnership are treated as contributing assets to the continuing partnership. The continuing partnership

retains its EIN and tax year. This determination affects when partnerships are deemed to continue versus terminate.

47. Correct Answer: D (2017)

The partnership technical termination rule was eliminated for partnership years beginning after December 31, 2017, by the Tax Cuts and Jobs Act. Previously, partnerships terminated for tax purposes when 50% or more of total interests in capital and profits changed hands within 12 months. Eliminating this rule reduced compliance complexity—partnerships no longer terminate and require new EINs due to sales or exchanges of partnership interests. The partnership continues until it legally dissolves.

48. Correct Answer: B (Majority partners)

Partnership tax years must generally conform to the tax year of partners owning a majority interest (over 50% of capital and profits). If there's no majority interest tax year, the partnership uses the tax year of all principal partners (those owning 5% or more). If principal partners have different years, the partnership uses the year resulting in the least aggregate deferral. Partnerships can also elect a fiscal year using Section 444 (3-month deferral maximum) with required payments.

49. Correct Answer: B (Form 1065)

Multi-member LLCs taxed as partnerships file Form 1065, U.S. Return of Partnership Income. This is the default classification for multi-member LLCs—they're automatically treated as partnerships unless they elect corporate treatment. The LLC provides legal liability protection while the partnership taxation provides flow-through treatment and flexibility in allocations. Members receive Schedule K-1s reporting their shares of income, deductions, and credits.

50. Correct Answer: A (Disregarded entity)

Single-member LLCs are treated by default as disregarded entities—the LLC has no separate tax existence and income/expenses are reported on the owner's return (Schedule C for businesses, Schedule E for rentals). The LLC provides legal liability protection without creating a separate tax entity. Single-member LLCs can elect to be treated as corporations by filing Form 8832, Check-the-Box election.

51. Correct Answer: D (100)

S corporations are limited to 100 shareholders maximum. Family members (up to 6 generations) can elect to be treated as one shareholder for this count. Spouses are automatically counted as one shareholder. This limit distinguishes S corporations from publicly traded C corporations and ensures they remain closely held. Exceeding 100 shareholders terminates the S election, converting the corporation to C status.

52. Correct Answer: B (Not permitted)

S corporation stock ownership by partnerships is not permitted. Eligible S corporation shareholders are limited to individuals (U.S. citizens or residents), certain estates, certain trusts (grantor trusts, testamentary trusts, QSSTs, ESBTs), and certain tax-exempt organizations (401(k) plans, charitable organizations).

Corporations and partnerships cannot be S corporation shareholders. This restriction maintains the single level of taxation principle.

53. Correct Answer: A (Differ)

S corporations can have only one class of stock, meaning all shares must confer identical rights to distributions and liquidation proceeds. However, differences in voting rights are permitted and don't create a second class of stock. An S corporation can have voting and non-voting common stock as long as distribution and liquidation rights are identical. This flexibility allows family business planning while maintaining S status.

54. Correct Answer: C (5 years)

The S corporation built-in gains tax applies to gains recognized within 5 years after converting from C to S corporation (reduced from 10 years). When appreciated assets are sold during this recognition period, the S corporation pays corporate-level tax (21%) on the built-in gain (appreciation at conversion). This tax prevents C corporations from converting to S status solely to avoid corporate tax on appreciated assets. After the recognition period expires, the built-in gains tax no longer applies.

55. Correct Answer: B (C corporation E&P)

The excess net passive income tax applies to S corporations when (1) passive investment income (interest, dividends, rents, royalties, annuities) exceeds 25% of gross receipts AND (2) the corporation has accumulated earnings and profits from C corporation years. The tax is imposed at the highest corporate rate (21%) on the excess net passive income. If this situation continues for three consecutive years, the S election automatically terminates. S corporations without accumulated E&P are not subject to this tax, even if passive income exceeds 25%.

56. Correct Answer: B (3 consecutive years)

S corporation election terminates if passive investment income exceeds 25% of gross receipts for 3 consecutive years AND the corporation has accumulated earnings and profits from C corporation years at the end of each year. This rule prevents S corporations from being used as personal holding companies. The termination is automatic without IRS action. Corporations can avoid termination by distributing E&P or restructuring to reduce passive income.

57. Correct Answer: C (Direct loans only)

S corporation shareholder basis includes stock basis (capital contributions plus income minus losses and distributions) plus debt basis from direct loans from the shareholder to the corporation. Unlike partnerships, S corporation entity liabilities don't increase shareholder basis—only direct shareholder loans create debt basis. Guarantees of corporate debt don't create basis. This limitation makes loss deductions more restricted for S corporations than partnerships.

58. Correct Answer: D (Accumulated income not distributed)

The Accumulated Adjustments Account (AAA) represents the S corporation's cumulative undistributed income that has been taxed to shareholders. AAA increases for income items (except tax-exempt income) and decreases for losses, deductions, and distributions. AAA can be negative from losses but distributions cannot reduce it below zero. It's tracked on Schedule M-2 and is crucial for determining the tax treatment of distributions—distributions from AAA are tax-free returns of previously taxed income.

59. Correct Answer: D (E&P if any)

For S corporations with accumulated earnings and profits from C corporation years, distributions follow this ordering: (1) first from AAA (tax-free), (2) then from accumulated E&P (taxable as dividends), (3) then from remaining stock basis (tax-free), and (4) finally as capital gain. For S corporations without accumulated E&P, distributions come from AAA first, then from stock basis, then create capital gain. The E&P layer in the middle (for former C corporations) ensures that pre-S corporation earnings are taxed as dividends when distributed.

60. Correct Answer: B (Division of parent)

A qualified Subchapter S subsidiary (QSub) election treats a subsidiary corporation as a division of the parent S corporation rather than a separate corporation. The subsidiary must be 100% owned by the parent S corporation. The QSub isn't treated as a separate corporation for tax purposes—its assets, liabilities, income, and deductions are treated as belonging to the parent. This allows affiliated S corporation structures while maintaining S status.

61. Correct Answer: A (Capital gains only)

Corporate capital losses can offset only capital gains—they cannot offset ordinary income. This is more restrictive than individual treatment (where \$3,000 can offset ordinary income annually). Corporations must carefully time capital asset sales to ensure capital gains are available to absorb losses. Unused capital losses carry back 3 years and forward 5 years, but expire if not used within that window.

62. Correct Answer: C (3 years)

Corporate capital loss carryback period is 3 years. Losses are carried back to the earliest year first, then forward if not fully absorbed. Carrybacks can create refund claims for taxes paid in prior years. After exhausting the 3-year carryback, unused losses carry forward 5 years. The carryback and carryforward provide an 8-year window to use capital losses, but the window is much more limited than the indefinite carryforward for individuals.

63. Correct Answer: D (5 years)

Corporate charitable contribution carryforwards are allowed for 5 years. Contributions exceeding the 10% of taxable income limitation carry forward and retain their character. Current year contributions are deducted before carryforwards. Carryforwards expire after 5 years if not used. The carryforward helps corporations benefit from large charitable gifts over multiple years when the 10% annual limit restricts current deductions.

64. Correct Answer: B (100%)

The dividends received deduction for corporations owning 80% or more of another corporation's stock is 100% of dividends received. This full deduction prevents triple taxation as income passes through corporate chains. For ownership of 20% to under 80%, the DRD is 65%. For ownership under 20%, the DRD is 50%. The 100% DRD recognizes affiliated corporation status and encourages corporate group structures.

65. Correct Answer: C (21%)

Personal service corporations are taxed at the flat 21% corporate rate, the same as all other C corporations after the Tax Cuts and Jobs Act. Previously, PSCs were taxed at a flat 35% (the highest rate), eliminating the benefit of graduated rates. A PSC is a corporation where substantially all activities involve performing services in health, law, accounting, engineering, architecture, actuarial science, performing arts, or consulting, and substantially all stock is owned by employees performing the services.

66. Correct Answer: A (20%)

The personal holding company tax rate is 20%. This penalty tax applies to undistributed personal holding company income when a corporation qualifies as a PHC (more than 50% of stock value owned by 5 or fewer individuals AND 60% or more of adjusted ordinary gross income is PHC income like dividends, interest, rents, royalties). The tax encourages distribution of passive income rather than accumulation in corporations to avoid shareholder taxation.

67. Correct Answer: B (20%)

The accumulated earnings tax is imposed at 20% on accumulated taxable income (income retained beyond reasonable business needs). The tax applies to corporations formed or availed of to avoid shareholder income tax through accumulation rather than distribution. Reasonable accumulations (\$250,000 for most corporations, \$150,000 for service corporations) are presumed. The tax is in addition to regular corporate income tax and encourages dividend distributions.

68. Correct Answer: D (Taxable income)

Schedule M-1 (or Schedule M-3 for larger corporations) reconciles book income (net income per financial statements) to taxable income. The reconciliation identifies temporary and permanent differences between book and tax accounting, such as tax-exempt interest (book income, not taxable), nondeductible expenses (book expense, not deductible), depreciation differences, and meals and entertainment limitations. This helps IRS verify accurate tax reporting and identify potential issues.

69. Correct Answer: A (50%)

Brother-sister controlled groups require the same five or fewer individuals, estates, or trusts to own more than 50% of the voting power or value of stock in each corporation. Additionally, they must own at least 80% counted only to the extent ownership is identical. The 50% test ensures common control. Controlled

groups must share certain tax benefits (Section 179 limits, accumulated earnings credit, etc.) as if they were one corporation.

70. Correct Answer: C (80%)

Parent-subsiary controlled groups require one corporation (parent) to own stock possessing at least 80% of voting power or value of another corporation (subsidiary). Chains of ownership can create controlled groups if 80% ownership exists at each level (excluding parent's interest). The 80% threshold is lower than the 100% required for QSub election but higher than the 50% voting stock required for consolidated returns filing.

71. Correct Answer: D (80% ownership)

Affiliated groups eligible to file consolidated returns require the common parent to own at least 80% of voting power and 80% of value of stock of includible corporations. All tiers of the affiliated group must meet the 80% test. The common parent must be an includible corporation. Certain corporations (foreign corporations, tax-exempt organizations, insurance companies) cannot be included. The 80% test is lower than 100% ownership but ensures substantial control.

72. Correct Answer: B (1120)

A consolidated return election is made by filing a consolidated Form 1120, U.S. Corporation Income Tax Return, that includes the income of all group members. All members must consent (evidenced by joining the consolidated return). Once the election is made, the group must continue filing consolidated returns unless composition changes or permission is obtained to deconsolidate. Form 1120-C doesn't exist; 1065 is for partnerships; 1120-S is for S corporations.

73. Correct Answer: A (Eliminated)

Intercompany dividends in consolidated groups are eliminated—they don't create income to the recipient or a deduction to the payor. This treatment recognizes that dividends within a consolidated group are transfers within a single economic unit. The elimination prevents dividends from affecting consolidated taxable income. Without elimination, intercompany dividends would create artificial income and corresponding DRD deductions.

74. Correct Answer: C (80%)

Section 351 nonrecognition on corporate formation requires transferors of property to own at least 80% of voting stock and 80% of each class of nonvoting stock immediately after the exchange. If this control requirement is met, transferors recognize no gain or loss on property transferred for stock. Boot (cash or property other than stock) received triggers gain recognition to the extent of boot or realized gain, whichever is less.

75. Correct Answer: D (Gain realized)

Boot received in a Section 351 exchange is taxable up to the amount of gain realized. If boot is less than realized gain, the boot amount is recognized. If boot exceeds realized gain, only the realized gain is recognized. This rule prevents taxpayers from fully avoiding gain recognition through tax-free exchanges while receiving significant non-qualifying property (boot). The basis in stock received is adjusted for boot and gain recognized.

76. Correct Answer: B (Small business stock)

Section 1244 stock is small business stock meeting specific requirements: domestic C corporation, total capitalization under \$1 million when stock is issued, active business (not passive investments), and issued for money or property (not services). Losses from Section 1244 stock are treated as ordinary losses (not capital losses) up to \$50,000 per year (\$100,000 MFJ). This favorable treatment helps small business investors by allowing ordinary loss deductions when businesses fail.

77. Correct Answer: C (180 months)

Organizational costs are amortized over 180 months (15 years), with up to \$5,000 deductible in the first year if total costs don't exceed \$50,000. The \$5,000 first-year deduction phases out dollar-for-dollar when costs exceed \$50,000. Organizational costs include legal fees, state incorporation fees, accounting fees, and organizational meeting costs. Costs must be incurred before the business begins and relate to creating the corporation.

78. Correct Answer: A (Capital gain or loss)

Corporate liquidations under Section 331 create capital gain or loss to shareholders. The shareholder's gain or loss equals the difference between liquidating distributions received and stock basis. The gain or loss is capital (long-term if stock held over one year). The corporation recognizes gain or loss on property distributed as if sold to shareholders at fair market value. This creates potential double taxation.

79. Correct Answer: B (No gain or loss)

Under Section 332, a parent corporation liquidating an 80%-or-more owned subsidiary recognizes no gain or loss on the liquidation. The parent must own at least 80% of voting power and 80% of value of subsidiary stock. The liquidation must be completed under a plan within 3 years. The parent takes a carryover basis in the subsidiary's assets (the subsidiary's basis transfers to the parent). The parent also inherits the subsidiary's tax attributes including net operating losses, earnings and profits, and capital loss carryforwards. This nonrecognition treatment prevents corporate-level tax on reorganizations within a controlled group while maintaining tax attributes at carryover basis.

80. Correct Answer: B (Asset acquisition)

A Section 338 election treats a qualified stock purchase (80% or more of target corporation stock acquired in 12-month period) as an asset acquisition for tax purposes. The target is treated as selling all assets at fair market value, recognizing gain or loss. The buyer gets a stepped-up basis in the assets equal to the

purchase price (allocated among assets). This election is rarely made because it triggers significant gain to the target, but it provides stepped-up basis.

81. Correct Answer: A (FUTA)

Employment taxes include FICA (Federal Insurance Contributions Act, covering Social Security and Medicare) and FUTA (Federal Unemployment Tax Act). FICA includes 6.2% Social Security (on wages up to \$168,600 for 2024) and 1.45% Medicare (on all wages) paid by both employer and employee. FUTA is 6% (0.6% after credits) on first \$7,000 of wages, paid only by employers. State income tax, sales tax, and property tax are not employment taxes.

82. Correct Answer: C (7.65%)

The FICA tax rate is 7.65% each for employer and employee (total 15.3%), consisting of 6.2% Social Security tax on wages up to \$168,600 (2024) and 1.45% Medicare tax on all wages. An additional 0.9% Medicare tax applies to wages exceeding \$200,000 (employee portion only). Self-employed individuals pay the entire 15.3% as self-employment tax (but can deduct half as a business expense).

83. Correct Answer: D (0.6%)

The FUTA tax rate after the standard credit is 0.6%. The gross FUTA rate is 6.0% on the first \$7,000 of each employee's wages, but employers receive a credit of up to 5.4% for state unemployment taxes paid, reducing the net federal rate to 0.6%. In states with outstanding federal unemployment loan balances, the credit is reduced, increasing the effective FUTA rate. FUTA is paid entirely by employers.

84. Correct Answer: B (\$7,000)

The FUTA wage base for 2024 is \$7,000 per employee. FUTA tax applies only to the first \$7,000 of each employee's annual wages. This wage base has not been indexed for inflation and has remained \$7,000 for decades. Once an employee's wages exceed \$7,000, no additional FUTA tax is owed for that employee for the year. The low wage base significantly limits FUTA tax liability.

85. Correct Answer: C (January 31)

Employers must provide Form W-2 to employees by January 31 of the year following the year for which wages were paid. For example, 2024 wages require W-2s by January 31, 2025. If January 31 falls on a weekend or holiday, the due date is the next business day. Employers must also file copies with the Social Security Administration by January 31 (previously the deadline was later, but it was moved up to reduce tax fraud).

86. Correct Answer: A (Quarterly)

Form 941, Employer's Quarterly Federal Tax Return, is filed quarterly to report income tax withholding and FICA taxes (Social Security and Medicare). The quarters are January-March (due April 30), April-June (due July 31), July-September (due October 31), and October-December (due January 31). Very small

employers (annual tax liability under \$1,000) can file annually on Form 944. Large employers must deposit taxes semi-weekly or monthly, even though reporting is quarterly.

87. Correct Answer: D (50 employees)

The employer mandate for health coverage (Affordable Care Act employer shared responsibility) applies to applicable large employers—those with an average of at least 50 full-time equivalent employees during the prior calendar year. Employers meeting this threshold must offer minimum essential coverage that's affordable and provides minimum value to full-time employees (30+ hours/week average) or potentially pay penalties. The mandate doesn't require covering part-time employees.

88. Correct Answer: B (Common law factors)

Independent contractor classification depends on common law factors examining the degree of control and independence in the relationship. Factors include behavioral control (who directs work), financial control (who provides tools, how payment is made), and relationship type (contracts, benefits, permanency). No single factor is determinative—all facts are considered. Written agreements, hourly pay, and part-time status alone don't determine classification. Proper classification affects employment tax obligations.

89. Correct Answer: A (Nonemployee compensation)

Form 1099-NEC, Nonemployee Compensation, reports payments of \$600 or more to independent contractors for services. Previously reported on Form 1099-MISC, nonemployee compensation was moved to separate Form 1099-NEC starting in 2020. The form is due to recipients by January 31 and to the IRS by January 31 (or March 31 if filed electronically). It covers payments to non-corporate service providers.

90. Correct Answer: B (24%)

Backup withholding applies at a rate of 24% to reportable payments (interest, dividends, nonemployee compensation, rents, royalties, etc.) when the payee fails to provide a correct taxpayer identification number (TIN), the IRS notifies the payer that the TIN is incorrect, the payee fails to certify they're not subject to backup withholding, or the IRS notifies the payer to start backup withholding due to underreporting. The 24% rate matches typical withholding rates and creates incentive for payees to provide correct TINs. Withheld amounts are credited to the payee's account when they file their return.

91. Correct Answer: D (30 days)

Information return filing penalties vary based on how late returns are filed. The lowest penalty applies if filed within 30 days of the due date: \$60 per return (2024). If filed after 30 days but by August 1, the penalty is \$120. If filed after August 1 or not filed, the penalty is \$310. Intentional disregard has a higher penalty of at least \$580 per return with no annual maximum.

92. Correct Answer: B (\$580)

Intentional disregard of information return filing requirements results in a minimum penalty of \$580 per return (2024, adjusted for inflation) with no annual maximum. If the amount required to be reported exceeds this minimum, the penalty can be 5% or 10% of that amount. "Intentional disregard" includes knowing or reckless failures. The unlimited nature of this penalty (no cap) makes intentional violations very costly.

93. Correct Answer: C (\$600)

Form 1099-K reports payment card transactions (credit/debit cards) and third-party payment network transactions (PayPal, Venmo, etc.). For 2024, the threshold for third-party network reporting has been lowered to \$600 (from \$20,000 and 200 transactions previously), though implementation has been delayed. Payment card transactions are reported regardless of amount. Form 1099-K helps IRS identify unreported business income from electronic payments.

94. Correct Answer: A (I-9)

Employers must verify employee work authorization using Form I-9, Employment Eligibility Verification. Employees must complete Section 1 on their first day, attesting to work authorization status. Employers must examine original documents establishing identity and work authorization within 3 business days and complete Section 2. Form I-9 is not filed with the government but must be retained for 3 years after hire or 1 year after termination, whichever is later.

95. Correct Answer: B (Fair market value)

Fringe benefits are valued at fair market value for inclusion in employee wages. Fair market value is the price a willing buyer would pay a willing seller in an arm's-length transaction. Special valuation rules exist for certain fringe benefits (automobile lease value tables, cents-per-mile rates, commuting valuation, etc.). The FMV standard ensures employees are taxed on the actual value of compensation received.

96. Correct Answer: B (Return of excess)

Accountable plan requirements are (1) business connection (expenses must be business-related), (2) substantiation (employees must adequately account for expenses within a reasonable time, generally 60 days), and (3) return of excess advances (amounts exceeding substantiated expenses must be returned within a reasonable time, generally 120 days). Reimbursements under accountable plans are not included in employee wages and are not subject to withholding or employment taxes.

97. Correct Answer: D (Wages)

Nonaccountable plan reimbursements are treated as wages—they're included in employee's income on Form W-2, subject to income tax withholding and FICA taxes. Nonaccountable plans are those that don't meet all accountable plan requirements. Employees cannot deduct business expenses (except business expenses by statutory employees and certain others) for 2018-2025 due to suspension of miscellaneous itemized deductions, making nonaccountable plans particularly unfavorable.

98. Correct Answer: C (Highly compensated)

Cafeteria plan nondiscrimination testing ensures benefits don't favor highly compensated employees (those earning over approximately \$155,000 in 2024, or officers, 5% owners, or spouses/dependents of these). Plans must benefit a reasonable classification of employees and cannot discriminate in favor of highly compensated employees as to eligibility or benefits. Discriminatory plans result in highly compensated employees recognizing income for their plan benefits.

99. Correct Answer: D (Both graduate and undergraduate)

The employer educational assistance exclusion (Section 127) applies to both graduate and undergraduate education. Employers can exclude up to \$5,250 per year of education benefits for job-related or non-job-related courses. This includes tuition, fees, books, supplies, and equipment. Starting in 2020, the \$5,250 can also include employer student loan repayment assistance (through 2025). Amounts over \$5,250 are taxable unless they qualify as working condition fringe benefits.

100. Correct Answer: B (Rank-and-file employees)

Qualified retirement plan nondiscrimination testing ensures coverage and benefits don't discriminate in favor of highly compensated employees and that rank-and-file employees (non-highly compensated employees) receive meaningful benefits. Tests include minimum coverage tests (percentage test and ratio test) and nondiscrimination tests for contributions and benefits. Safe harbor designs automatically satisfy testing. Discriminatory plans lose qualified status, resulting in adverse tax consequences.

Part 3: Representation, Practices, And Procedures

1. Correct Answer: D (Disbarment)

Circular 230 sanctions for practitioner misconduct include censure (public or private reprimand), suspension (prohibition from practice for a specified period), and disbarment (indefinite prohibition from practice before the IRS unless successfully petitioning for reinstatement). Monetary penalties can also be imposed. Criminal charges and license revocation are separate matters handled outside Circular 230. The sanctions are imposed by the IRS Office of Professional Responsibility after proceedings before Administrative Law Judges.

2. Correct Answer: C (3 years)

Enrolled agents must renew their enrollment every 3 years (each enrollment cycle). Renewal requires filing Form 8554 and certifying completion of continuing education requirements (72 hours per enrollment cycle, including 2 hours of ethics annually). The enrollment cycle begins on the date enrollment is granted or renewed. Failure to renew results in loss of enrolled agent status and the ability to represent clients before the IRS.

3. Correct Answer: B (16 hours)

Enrolled agents must complete a minimum of 16 hours of continuing education per year, totaling 72 hours per 3-year enrollment cycle. The annual 16-hour minimum prevents clustering all CE in one year of the cycle. At least 2 hours annually (6 per cycle) must cover ethics. The remaining hours must cover federal tax law, procedures, or related topics. Failure to meet CE requirements makes EAs ineligible for renewal.

4. Correct Answer: D (2 hours per year)

The ethics continuing education requirement for enrolled agents is 2 hours per year, totaling 6 hours per 3-year enrollment cycle. Ethics CE must cover Circular 230 (regulations governing practice before the IRS) and professional responsibilities. The annual ethics requirement ensures EAs maintain current knowledge of professional standards and obligations. Ethics courses must be specifically designated as ethics CE.

5. Correct Answer: A (Specific period)

Practitioner suspension from IRS practice is for a specific period stated in the suspension order (such as 6 months, 2 years, or 5 years). After the suspension period expires, the practitioner can resume practice. This differs from disbarment, which is indefinite and requires successful petition for reinstatement. Suspensions are imposed for serious violations but those not warranting permanent exclusion from practice.

6. Correct Answer: C (Reasonable inquiry)

Best practices under Circular 230 Section 10.33 include establishing facts and circumstances through reasonable inquiry. This means asking appropriate questions, reviewing relevant documents, and verifying information when warranted. Other best practices include communicating clearly about engagement terms, advising clients of implications of noncompliance, and exercising due diligence. Best practices are aspirational—they're not mandatory and violations don't result in discipline.

7. Correct Answer: B (Coercion)

Solicitation is prohibited under Circular 230 if it involves false or misleading communications, coercion, overreaching, or harassing conduct. Truthful advertising and marketing are permitted. Professional solicitation through networking, advertising, targeted marketing, and public speaking is acceptable if communications are accurate and not coercive. The prohibition aims to prevent unprofessional or deceptive solicitation while allowing legitimate marketing.

8. Correct Answer: D (IRS examinations)

Contingent fees are generally prohibited under Circular 230 but are permitted for services in connection with IRS examinations or audits of original tax returns, claims for refund or credit (except preparing original returns), and judicial proceedings. The exception recognizes that these services involve disputes over existing liabilities where contingent arrangements are appropriate. Contingent fees for preparing original returns are prohibited.

9. Correct Answer: A (Substantial authority)

Tax return positions must have at least a reasonable basis. If a position lacks substantial authority (approximately 40% likelihood of success), it must be disclosed to avoid penalties. Reasonable basis is approximately 20% likelihood. Positions without even reasonable basis should not be taken. More likely than not (over 50%) is required for tax shelter opinions. The substantial authority standard balances aggressive tax planning with professional responsibility.

10. Correct Answer: B (More likely than not)

Covered opinions under Circular 230 Section 10.35 (opinions on listed transactions, principal purpose transactions, and certain other tax-motivated transactions) require practitioners to reach conclusions at the "more likely than not" confidence level (greater than 50% likelihood of success) or higher, or clearly state they cannot reach that level. The opinion must address all significant tax issues, consider all relevant facts, relate law to facts, and not assume favorable resolution of significant issues. Lower confidence levels like "reasonable basis" (approximately 20%), "substantial authority" (approximately 40%), or "should" (approximately 70-80%) are insufficient for covered opinions. The heightened "more likely than not" standard prevents abusive tax shelter opinions lacking proper analysis.

11. Correct Answer: C (Personally and substantially)

Former government employees cannot represent clients before the IRS on matters in which they personally and substantially participated as government employees. The restriction is permanent for those specific matters. "Personal and substantial participation" means direct involvement in the matter through decision-making, approval, recommendation, investigation, or similar active roles. Former employees can represent clients on other matters not involving their personal substantial participation.

12. Correct Answer: D (Written consent)

Confidential client information can be disclosed with the client's informed written consent. Other permitted disclosures include those pursuant to court orders, to comply with Circular 230 requirements, in response to IRS inquiries, for quality or peer reviews, in investigations of practitioner misconduct, for conflict checks, and as otherwise provided by law. Verbal or implied consent is insufficient—explicit written consent is required for voluntary disclosures.

13. Correct Answer: D (Upon request)

Practitioners must return client records upon client request, regardless of fees owed for work performed. Circular 230 prohibits holding client records hostage for unpaid fees. "Client records" include records originally provided by the client and records that must be provided for the client to comply with federal tax obligations. Practitioners can retain work papers and internal documents. The rule protects clients' ability to comply with tax obligations.

14. Correct Answer: B (Consequences)

When a practitioner becomes aware of client noncompliance or errors on returns or submissions to the IRS, they must promptly advise the client of the noncompliance and the consequences of the

noncompliance. The practitioner doesn't file corrected returns without client authorization or report the issue to the IRS—the duty runs to the client. The practitioner advises on corrective measures, but the client decides whether to correct.

15. Correct Answer: C (Incorrect)

Diligence as to accuracy requires practitioners to make reasonable inquiries when information appears incorrect, inconsistent, or incomplete. Practitioners cannot ignore red flags or obvious errors. The standard is reasonableness—not perfection or auditing, but appropriate inquiry based on the circumstances. When information appears incorrect, the practitioner must ask questions, request clarification, and verify if warranted.

16. Correct Answer: C (Representation and advocacy)

Practice before the IRS includes all matters connected with presentations to the IRS relating to a client's rights, privileges, or liabilities under laws or regulations administered by the IRS. This encompasses representation, advocacy, correspondence, preparing documents, advising on tax matters, and appearing before IRS personnel. Simply filing returns is not "practice," but representing taxpayer positions during examinations, appeals, or collection matters is practice.

17. Correct Answer: D (Prepared and signed)

Limited practice authority allows unenrolled return preparers to represent taxpayers before revenue agents, customer service representatives, and similar IRS employees, but only on returns or claims they prepared and signed. The representation is limited to these specific returns and cannot extend to Appeals, Collection, or Tax Court. The preparer must have actually prepared and signed the return to qualify for limited practice.

18. Correct Answer: C (Prepared and signed)

Annual Filing Season Program (AFSP) participants who complete the required continuing education can represent taxpayers before revenue agents, customer service representatives, and similar IRS employees on returns they prepared and signed. This limited representation is similar to unenrolled preparer rights but recognizes AFSP participants' additional education. AFSP participants cannot represent before Appeals, Collection, or Tax Court.

19. Correct Answer: B (Represent and receive information)

Form 2848, Power of Attorney and Declaration of Representative, authorizes the representative to represent the taxpayer before the IRS and receive confidential tax information for the matters and years specified. The representative can advocate positions, negotiate, sign certain forms, and generally act on the taxpayer's behalf. The form doesn't automatically authorize signing returns or binding the taxpayer to settlements unless specifically stated.

20. Correct Answer: B (Inspect and receive information)

Form 8821, Tax Information Authorization, allows designated individuals to inspect and receive confidential tax information for specified matters and years. It does NOT grant authority to represent the taxpayer, advocate positions, or bind the taxpayer. It's purely an information disclosure authorization, useful for allowing accountants, family members, or others to obtain tax information without representation authority. The authorization can be limited to specific forms or years.

21. Correct Answer: D (3 years)

The Centralized Authorization File (CAF) retains Form 2848 (Power of Attorney) for 3 years from the date it's recorded in the system. After 3 years, the authorization expires and representatives must submit new Forms 2848 to represent taxpayers. Taxpayers can check CAF status online and revoke authorizations at any time. The 3-year retention balances accessibility with the need for current authorizations.

22. Correct Answer: C (Taxpayer written notice)

Powers of attorney can be revoked by the taxpayer providing written notice to the IRS. The notice should identify the specific Form 2848 being revoked or state that all previously filed Forms 2848 are revoked. Filing a new Form 2848 for the same matters automatically revokes prior authorizations unless the retention box is checked. Representatives can also withdraw by notifying both the IRS and the taxpayer in writing.

23. Correct Answer: B (Representative)

The Centralized Authorization File (CAF) number is assigned to representatives, not taxpayers. Each practitioner receives a unique CAF number when they first appear on a Form 2848. The CAF number links all authorizations for that practitioner, allowing the IRS to manage representation authority centrally. Practitioners provide their CAF number on subsequent Forms 2848 to link to their existing CAF record.

24. Correct Answer: D (Authorized and eligible)

The Declaration of Representative section on Form 2848 requires practitioners to declare under penalties of perjury that they're currently eligible to practice before the IRS, authorized to represent the taxpayer, and not under suspension or disbarment. This certification protects taxpayers and the IRS by ensuring only qualified, authorized practitioners represent taxpayers. False declarations can result in sanctions.

25. Correct Answer: C (Independently unless specified)

Form 2848 allows multiple representatives who can act independently by default—any appointed representative can act alone unless the form specifies joint authority (all must act together) or sequential authority (designated order of representation). Independent authority is most common and efficient, allowing any representative to handle matters without coordinating with others. The designation should match the actual representation arrangement.

26. Correct Answer: A (When return processed)

The third-party designee authority (checkbox on Form 1040) terminates when the return is processed or on the due date of the return, whichever is later. This limited authority allows the IRS to contact the designee about processing questions, math errors, and return completion, but doesn't authorize representation or advocacy. It's intended for short-term assistance with return preparation and filing issues.

27. Correct Answer: B (From IRS)

Preparer Tax Identification Numbers (PTINs) must be obtained from the IRS by all paid tax return preparers. PTINs are obtained online at IRS.gov or by filing Form W-12. Every paid preparer must have a PTIN regardless of whether they're enrolled agents, attorneys, CPAs, or unenrolled preparers. PTINs identify preparers on returns and are used for IRS compliance and enforcement efforts.

28. Correct Answer: A (December 31)

PTINs must be renewed annually, with the renewal period opening in mid-October and PTINs expiring December 31. Preparers renew online at IRS.gov, paying a renewal fee. Without a valid PTIN, preparers cannot prepare returns for compensation. The annual renewal ensures current contact information and allows the IRS to suspend or revoke PTINs for practitioners who are ineligible due to misconduct.

29. Correct Answer: C (Paid preparers)

PTINs are required for all paid tax return preparers—anyone who prepares all or substantially all of a return or claim for refund for compensation. Volunteers preparing returns for free (such as through VITA or TCE programs) don't need PTINs. Family members preparing returns for free for relatives don't need PTINs. The PTIN requirement applies only when compensation is received for preparation services.

30. Correct Answer: C (Compensation)

A tax return preparer is anyone who prepares all or substantially all of a return or claim for refund for compensation. "Compensation" is broadly defined and includes direct or indirect payment. Even nominal compensation creates preparer status. Preparing returns for free for friends or family doesn't create preparer status for penalty purposes. The determination focuses on whether any form of compensation was received.

31. Correct Answer: B (Overall accuracy)

The signing preparer is the person with primary responsibility for the overall substantive accuracy of the return. Only one signing preparer exists per return. The signing preparer must manually or electronically sign the return and include their PTIN. When multiple preparers work on a return, the most experienced or senior preparer typically serves as signing preparer and takes responsibility for the overall return accuracy.

32. Correct Answer: C (\$10,000 or 20% of gross income)

A nonsigning preparer prepares a "substantial portion" when the schedule or entry they prepare affects tax liability (or refund or credit) of at least the lesser of \$10,000 or 20% of the gross income shown on the

return. For individual returns, the test is typically \$10,000 or 20% of gross income. For business returns (corporations, partnerships), the threshold is \$400,000 or 20% of gross income or total receipts. Preparing a substantial portion subjects the nonsigning preparer to preparer penalties under Sections 6694 and 6695, creating accountability for preparers who work on significant portions of returns even if they don't sign them.

33. Correct Answer: D (HOH)

Preparer due diligence requirements apply to returns claiming the Earned Income Tax Credit (EITC), Child Tax Credit (CTC), Additional Child Tax Credit (ACTC), American Opportunity Tax Credit (AOTC), and Head of Household (HOH) filing status. These items are subject to significant improper claims, requiring heightened preparer diligence. Form 8867, Paid Preparer's Due Diligence Checklist, must be completed for each applicable item and retained for 3 years.

34. Correct Answer: C (Covered credits)

Form 8867, Paid Preparer's Due Diligence Checklist, must be completed for each return claiming covered credits: EITC, CTC, ACTC, AOTC, or HOH filing status. The form documents the preparer's efforts to comply with due diligence requirements: determining eligibility, completing computation worksheets, asking additional questions when information appears inconsistent, and documenting inquiries. Separate checklists are completed for each credit or HOH claimed.

35. Correct Answer: B (3 years)

Due diligence records, including Form 8867 and supporting documentation of inquiries and client responses, must be retained for 3 years from the later of the return due date or the date the return was filed. This matches the general preparer recordkeeping requirement. The records document compliance with due diligence requirements and protect preparers from penalties when proper procedures were followed.

36. Correct Answer: D (Should have known)

The knowledge standard for due diligence is that the preparer knew or reasonably should have known that information was incorrect, inconsistent, or incomplete. This is an objective standard—what a competent preparer in similar circumstances should know based on information provided and reasonable inquiries. Preparers cannot turn a blind eye to obvious issues or rely on information they should know is questionable.

37. Correct Answer: C (50% of income)

The unreasonable position penalty under Section 6694(a) is the greater of \$1,000 or 50% of the income derived by the preparer from preparing the return. The penalty applies when positions lack substantial authority (or reasonable basis with adequate disclosure). The penalty is assessed per return, potentially accumulating to large amounts for preparers with many returns. Reasonable cause defenses may be available.

38. Correct Answer: A (75% of income)

The willful or reckless conduct penalty under Section 6694(b) is the greater of \$5,000 or 75% of the income derived from preparing the return. This higher penalty (compared to 50% for unreasonable positions) reflects greater culpability for willful attempts to understate tax or reckless/intentional disregard of rules. The penalty applies instead of, not in addition to, the unreasonable position penalty. No reasonable cause defense exists.

39. Correct Answer: B (\$50 per return)

The penalty for failure to furnish a copy of the return to the taxpayer is \$50 per return, up to a maximum of \$27,000 per calendar year (amounts adjusted for inflation). Tax return preparers must provide complete copies of returns to taxpayers no later than presenting the return for signature. This ensures taxpayers can review returns before signing. The per-return penalty encourages systematic compliance.

40. Correct Answer: D (\$10,000 per year)

The penalty for unauthorized disclosure or use of tax return information is \$250 per disclosure or use, with a maximum of \$10,000 per calendar year. The annual cap limits total civil penalties, but each unauthorized disclosure creates a separate violation. Criminal penalties (up to \$1,000 fine and 1 year imprisonment) can also apply. The penalties protect taxpayer privacy and deter preparers from misusing client information.

41. Correct Answer: C (\$10,000)

The penalty for aiding and abetting understatement of tax liability is \$1,000 for individual returns or \$10,000 for corporate returns, per taxpayer per document. This penalty applies to those who aid or assist in preparing or presenting tax documents (including those who are not return preparers) with knowledge that the documents will result in tax understatement. The higher corporate penalty reflects larger tax amounts typically involved.

42. Correct Answer: A (Gross income from activity)

The penalty for promoting abusive tax shelters is 50% of gross income derived from the activity (or 75% if the person makes fraudulent statements or fails to adequately disclose that tax benefits are not IRS-approved). Gross income includes all fees, commissions, and other compensation related to organizing, selling, or participating in organizing or selling the tax shelter. This severe penalty deters tax shelter promotion.

43. Correct Answer: D (3 years)

The assessment statute of limitations is generally 3 years from the later of the return due date or the date the return was filed. The IRS generally cannot assess additional tax after this period expires. Exceptions extend the statute: 6 years if gross income is understated by more than 25%, indefinitely for fraud or failure to file, and by agreement (consent to extend). The statute starts when a valid return is filed.

44. Correct Answer: B (25% of gross income)

The statute of limitations extends to 6 years (instead of 3) when gross income is omitted exceeding 25% of gross income shown on the return. This extended period gives the IRS additional time to discover and assess tax on substantial omissions. The 6-year statute applies to omissions, not overstatements of deductions (except certain basis overstatements). The extension recognizes the difficulty of detecting large omissions.

45. Correct Answer: C (Evade)

Fraud has no statute of limitations. The IRS can assess tax at any time if fraud is proven. Fraud requires proving the taxpayer intended to evade tax through intentional wrongdoing. The burden of proof is on the IRS, and fraud must be proven by clear and convincing evidence (higher than normal "preponderance" standard). Because fraud opens the statute indefinitely, the IRS carefully evaluates fraud assertions.

46. Correct Answer: D (2 years from payment)

Refund claims must be filed within the later of 3 years from the date the return was filed or 2 years from the date the tax was paid. Returns filed before the due date are deemed filed on the due date. This dual statute ensures taxpayers have adequate time whether they filed early or paid late. The refund amount is limited based on which period is used for the claim.

47. Correct Answer: B (Assessment)

The collection statute of limitations is 10 years from the date of assessment. The IRS generally cannot collect tax after 10 years from assessment. The statute can be suspended during certain events: offers in compromise, collection due process hearings, bankruptcy, innocent spouse cases, military service in combat zones, and requests for installment agreements. Each suspension extends the collection period by the suspension duration plus additional time.

48. Correct Answer: B (Installment agreement request)

The collection statute is suspended during pending installment agreement requests, offers in compromise, collection due process hearings, bankruptcy proceedings, innocent spouse relief requests, and certain other events. During litigation in Tax Court, the statute is also suspended. Each suspension adds the duration of the suspension plus additional time (typically 30-90 days) to the 10-year collection period, potentially allowing collection beyond 10 years after assessment.

49. Correct Answer: C (Lifestyle and assets)

Financial status audits (also called economic reality audits) examine the taxpayer's lifestyle, expenditures, assets, and liabilities to determine if reported income is sufficient to support the lifestyle. The IRS analyzes bank deposits, asset acquisitions, and living expenses to reconstruct income. These audits are used when the IRS suspects unreported income, often in cash businesses. The audits can result in income reconstruction based on bank deposits or net worth increases.

50. Correct Answer: A (Mail)

Correspondence audits are conducted entirely by mail. The IRS sends a letter requesting specific documentation or information to verify return items. The taxpayer responds by mail with explanations and supporting documents. No in-person meeting occurs. Correspondence audits are the most common type, typically involving straightforward issues like substantiation of deductions, credits, or income items. They're less burdensome than office or field audits.

51. Correct Answer: D (IRS office)

Office examinations require the taxpayer (or authorized representative) to appear at an IRS office with requested records and documents. The examination occurs at the IRS facility, not the taxpayer's location. Office audits are more complex than correspondence audits but less extensive than field audits. They typically involve multiple issues or items requiring detailed review but don't warrant the resources of a field audit.

52. Correct Answer: B (Place of business)

Field audits occur at the taxpayer's home, place of business, or representative's office—wherever the taxpayer's books and records are maintained. Revenue agents conduct field audits, which are the most comprehensive type of examination. Field audits typically involve businesses, complex returns, or situations where examining records at their location is more efficient. Taxpayers can often negotiate the field audit location.

53. Correct Answer: B (30-day letter)

Examination changes are initially proposed in the 30-day letter (also called the examination report or Revenue Agent's Report). This letter explains the proposed changes, provides the basis for the adjustments, and gives taxpayers 30 days to either agree with the changes, disagree and request an Appeals conference, or do nothing. The 30-day letter is not the statutory notice of deficiency—it's the preliminary proposal that gives taxpayers opportunity to resolve disputes through Appeals before formal deficiency procedures begin. If taxpayers don't respond or can't reach agreement in Appeals, the IRS then issues a statutory notice of deficiency (90-day letter).

54. Correct Answer: D (Appeals)

Taxpayers who disagree with examination results can request a conference with the IRS Independent Office of Appeals. Appeals provides independent administrative review of disputes. Appeals Officers are separate from examination personnel and can consider hazards of litigation in reaching settlements. Most cases settle in Appeals, avoiding litigation. Requesting Appeals is typically done in response to the 30-day letter.

55. Correct Answer: D (Petition Tax Court)

The statutory notice of deficiency (90-day letter) gives taxpayers 90 days (150 days if addressed outside the United States) to petition the U.S. Tax Court to contest the proposed deficiency. Filing a timely petition is the only way to obtain prepayment judicial review—it allows taxpayers to challenge the deficiency in

court before paying any tax. The 90-day period is jurisdictional—Tax Court lacks jurisdiction if petitions are filed late. If no petition is filed within 90 days, the IRS can assess the deficiency and pursue collection, and the taxpayer's only remaining option is to pay the tax and sue for refund in District Court or Court of Federal Claims.

56. Correct Answer: C (Assessment)

Failure to petition Tax Court within 90 days of the notice of deficiency results in the IRS assessing the deficiency. Once assessed, the amount becomes due and the IRS can pursue collection through levies and liens. The taxpayer loses the opportunity for prepayment judicial review in Tax Court. The only option after assessment is to pay the tax and file a refund suit in District Court or Court of Federal Claims.

57. Correct Answer: B (90 days)

Tax Court petitions must be filed within 90 days of the date of the statutory notice of deficiency (150 days if the notice is addressed to someone outside the United States). The petition must be postmarked by the 90th day or filed electronically by the deadline. This deadline is jurisdictional—missing it means Tax Court lacks jurisdiction and the case is dismissed. The 90-day period cannot be extended.

58. Correct Answer: A (Not appealable)

Small case procedures in Tax Court apply to disputes of \$50,000 or less per year. The decisions are final and not appealable—neither the taxpayer nor the IRS can appeal small case decisions. This trade-off provides simplified procedures, relaxed evidence rules, informal hearings, and faster resolution in exchange for finality. Small case elections cannot be changed once made, and decisions have no precedential value.

59. Correct Answer: C (Published)

Tax Court regular decisions are published in the official United States Tax Court Reports and have precedential value—they establish binding authority that the Tax Court and lower courts follow. Regular decisions are reserved for cases involving novel or important legal issues. They are distinguished from memorandum decisions (which apply established law and are published commercially but not officially) and summary opinions (small case decisions that are not appealable and have no precedential value). The published, precedential nature of regular decisions makes them important for tax law development and authoritative interpretation.

60. Correct Answer: D (Circuit Court)

Appeals from Tax Court decisions go to the U.S. Court of Appeals (Circuit Court) for the circuit where the taxpayer resides. This is the same circuit that the Golsen rule requires Tax Court to follow when deciding cases. From the Circuit Court, decisions can potentially be appealed to the Supreme Court through certiorari (though the Supreme Court accepts very few tax cases). Appeals don't go to District Court (which is trial-level), Court of Federal Claims (a separate trial court), or directly to the Supreme Court (which requires intermediate appellate review first).

61. Correct Answer: B (Payment first)

District Court jurisdiction for tax cases requires the taxpayer to first pay the tax and file a refund claim. After the claim is denied or deemed denied (6 months without action), the taxpayer can sue in District Court for refund. This "pay first" requirement distinguishes District Court from Tax Court (which has prepayment jurisdiction). District Court is the only tax forum offering jury trials. Geographic jurisdiction is in the district where the taxpayer resides or where the return was filed.

62. Correct Answer: B (Nationwide)

The U.S. Court of Federal Claims has nationwide jurisdiction for tax refund suits. Like District Court, it requires payment first. The Court of Federal Claims sits in Washington, D.C., but has jurisdiction over cases throughout the country. Cases are heard by judges (no jury option). The court handles large refund cases and provides an alternative to District Court when the taxpayer prefers the specialized tax expertise of the Court of Federal Claims judges.

63. Correct Answer: D (Circuit Court)

Appeals from District Court tax decisions go to the U.S. Court of Appeals for the circuit where the District Court sits. The circuit courts review both legal and factual determinations, giving deference to factual findings (clearly erroneous standard) but reviewing legal conclusions de novo. The circuit split (different circuits reaching different conclusions on the same issue) can create geographic disparities until the Supreme Court resolves the split.

64. Correct Answer: C (Appellate court for taxpayer's residence)

The Golsen rule requires Tax Court to follow the precedent of the Court of Appeals for the circuit where the taxpayer resides (and where the case would be appealed if appealed). This prevents the futility of Tax Court ruling contrary to controlling appellate authority. The Golsen rule can create different Tax Court results for identical facts depending on taxpayer residence, reflecting circuit splits in tax law. Tax Court follows its own prior decisions except when reversed by the appellate court.

65. Correct Answer: B (\$2 million)

Mandatory whistleblower awards under Section 7623(b) with awards ranging from 15-30% apply when the tax, penalties, interest, and other amounts in dispute exceed \$2 million AND the taxpayer's gross income exceeds \$200,000 (for individuals). Cases not meeting these thresholds may qualify for discretionary awards up to 15% under Section 7623(a). The \$2 million threshold targets mandatory awards to significant cases involving substantial tax noncompliance. The IRS Whistleblower Office determines the specific award percentage within the 15-30% range based on the quality and value of information provided.

66. Correct Answer: D (15-30%)

Whistleblower awards for cases meeting the mandatory award thresholds (over \$2 million in dispute, taxpayer gross income over \$200,000) range from 15% to 30% of collected proceeds. The IRS Whistleblower Office determines the percentage based on factors including the value and significance of the information provided, the whistleblower's contribution to the case, and other factors. Awards for smaller cases are discretionary and capped at 15%.

67. Correct Answer: B (Ascertainable group)

John Doe summonses allow the IRS to obtain information about unknown taxpayers who are members of an ascertainable group or class. The IRS must obtain court approval by demonstrating: (1) the summons relates to investigation of an ascertainable group, (2) reasonable basis exists that the group may have failed to comply with tax laws, and (3) the information sought isn't readily available from other sources. John Doe summonses help identify noncompliant taxpayers when names are unknown.

68. Correct Answer: C (20 days)

Third-party recordkeeper summonses (issued to banks, accountants, attorneys, etc., for records regarding taxpayers) require giving notice to the taxpayer whose records are summoned. The taxpayer has the right to petition to quash the summons within 20 days of the notice (not 14, 30, or 10 days). If no petition is filed within 20 days, the recordkeeper must comply with the summons. The notice protects taxpayers' rights to challenge summonses for their records.

69. Correct Answer: B (Relevance)

Summons enforcement requires the IRS to establish the Powell requirements: (1) investigation conducted for a legitimate purpose, (2) inquiry is relevant to that purpose, (3) information sought is not already in the IRS's possession, and (4) required administrative steps have been followed. The burden then shifts to the taxpayer to show the summons is issued for improper purpose, in bad faith, or constitutes harassment. Relevance is a key requirement.

70. Correct Answer: C (Tax advice in noncriminal proceedings)

The federally authorized tax practitioner privilege under Section 7525 applies to confidential communications between taxpayers and federally authorized practitioners (attorneys, CPAs, enrolled agents) regarding tax advice in noncriminal tax matters before the IRS or federal courts. The privilege does NOT apply to return preparation, all communications generally, or routine audit matters—only to tax advice. The privilege is narrower than attorney-client privilege and excludes criminal proceedings, state matters, and written communications regarding tax shelters.

71. Correct Answer: C (Tax matters)

The federally authorized tax practitioner privilege under Section 7525 applies to communications made to obtain or provide tax advice in matters before the IRS or federal courts relating to tax matters (nontax advice is not covered). The privilege protects confidential tax advice communications between taxpayers

and authorized practitioners (EAs, attorneys, CPAs) but only in noncriminal proceedings. The limitation to tax matters ensures the privilege doesn't extend beyond its intended scope of federal tax advice.

72. Correct Answer: C (Criminal matters)

The federally authorized practitioner privilege does NOT apply to written communications regarding tax shelters OR criminal tax matters. Other exclusions include return preparation (the mechanical act of preparing returns isn't protected), state proceedings (only federal matters are covered), and communications not related to tax advice. The exclusion for criminal matters recognizes the government's strong interest in prosecuting tax crimes and prevents the privilege from shielding criminal tax evasion or fraud. The tax shelter exclusion addresses abusive tax avoidance schemes.

73. Correct Answer: D (Testimony)

Summonses may be issued to examine books, records, and other data, and to compel testimony under oath regarding tax liabilities. The summons power is broad and extends to both documents and testimony. Taxpayers and third parties can be summoned. Refusal to comply can result in court enforcement through contempt proceedings. The summons power is essential for IRS information gathering during examinations and investigations.

74. Correct Answer: C (Property and rights to property)

Levy is an IRS collection action that seizes property and rights to property, including wages, bank accounts, accounts receivable, vehicles, real estate, and other assets. Levies on wages are continuous (applying to future wages until released), while bank levies are one-time seizures. Certain property is exempt from levy (necessary clothing, household goods up to limits, unemployment benefits, certain pension benefits, etc.). Notice of intent to levy must generally be given 30 days before levy.

75. Correct Answer: D (Due process hearing)

Notice of intent to levy (Form 1058 or Letter 1058) must be given at least 30 days before levy and provides the right to a Collection Due Process (CDP) hearing. The CDP hearing allows the taxpayer to challenge collection actions, propose collection alternatives (installment agreements, offers in compromise), and raise defenses. The hearing is conducted by an Appeals Settlement Officer independent from the collection function. Requesting CDP suspends levy action during the hearing process.

76. Correct Answer: C (Principal residence without approval)

Property exempt from levy includes certain amounts of wages (based on filing status and dependents, similar to standard deductions), unemployment benefits, workers' compensation, welfare payments, certain annuity and pension payments, disability payments, and specified amounts of household goods, personal effects, books, and tools of trade. The principal residence cannot be levied without written approval from a U.S. District Court judge or magistrate, providing special protection for homes.

77. Correct Answer: A (Notice of Federal Tax Lien)

A federal tax lien arises automatically when the IRS assesses tax, the taxpayer fails to pay, and the IRS makes demand for payment. However, the lien is not effective against certain third parties (purchasers, secured creditors, judgment lien holders) until the IRS files a Notice of Federal Tax Lien with the appropriate government office (usually county recorder). Filing the notice provides public notice of the government's claim against the taxpayer's property.

78. Correct Answer: C (Appropriate government office)

The Notice of Federal Tax Lien is filed with the appropriate government office, typically the county recorder's office where the taxpayer's real property is located or the Secretary of State for personal property. The filing location depends on state law. Filing provides public notice of the lien, protecting the government's priority against subsequent creditors and purchasers. The lien attaches to all the taxpayer's property and rights to property.

79. Correct Answer: D (First in time)

Federal tax lien priority is generally determined by the "first in time, first in right" rule—the first perfected interest has priority. The federal tax lien arises upon assessment and demand, but is not effective against certain parties until notice is filed. Competing interests (mortgages, judgment liens, etc.) are prioritized based on when they were perfected. The priority rules are complex and can determine whether the IRS or other creditors are paid from proceeds of property sales.

80. Correct Answer: A (60 days)

A Certificate of Release of Federal Tax Lien must be issued by the IRS within 30 days after the liability is fully satisfied, becomes legally unenforceable (statute expires), or a bond is accepted. If the IRS fails to issue the certificate within this 30-day period, taxpayers can request the release. If the IRS doesn't respond to the request within 60 days, the taxpayer can bring a civil action for damages in federal district court. The 60-day period gives the IRS reasonable time to respond to the taxpayer's request before legal action is available. Failure to timely release liens can result in civil damages against the United States, protecting taxpayers' credit and property interests.

81. Correct Answer: A (433-A or 433-B)

Offers in compromise based on doubt as to collectibility require detailed financial statements on Form 433-A (individuals) or Form 433-B (businesses) showing assets, income, expenses, and liabilities. The IRS uses these forms to calculate reasonable collection potential—the amount the IRS could collect through other means. The offer must exceed the RCP to be acceptable. The detailed financial disclosure is essential to the doubt as to collectibility analysis.

82. Correct Answer: C (\$205)

The offer in compromise application fee is \$205 (subject to adjustment). Low-income taxpayers meeting certain thresholds are exempt from the application fee. The fee is submitted with Form 656, Offer in Compromise. The fee is non-refundable even if the offer is rejected, withdrawn, or returned. The fee

partially covers IRS costs of processing and investigating offers. Offers are complex and require significant IRS resources to evaluate.

83. Correct Answer: C (Exceptional circumstances)

Effective tax administration (ETA) offers in compromise apply when collection wouldn't create economic hardship but would be unfair or create exceptional circumstances due to public policy or equity considerations. ETA offers are rare and require showing that collection, while possible, would be inequitable or contrary to effective tax administration. Examples include serious long-term illness, elderly taxpayers with limited income, or situations where strict collection would undermine tax compliance norms.

84. Correct Answer: B (Direct debit low-income)

Installment agreement user fees vary based on agreement type and payment method, ranging from \$31 (for direct debit agreements by low-income taxpayers) to \$225 (for non-direct-debit agreements by taxpayers not qualifying for reduced fees). Direct debit agreements (automatic bank withdrawals) receive reduced fees because they're more reliable and reduce IRS costs. Low-income taxpayers receive additional fee reductions. The fees can be reimbursed if certain low-income criteria are met.

85. Correct Answer: C (Hardship)

Currently not collectible (CNC) status applies when the IRS determines that collecting any amount would create economic hardship—the taxpayer cannot pay reasonable basic living expenses if required to pay the tax. While in CNC status, the IRS temporarily suspends collection, but interest and penalties continue accruing and the statute of limitations continues running. The IRS periodically reviews CNC accounts to determine if financial status has improved sufficiently to resume collection.

86. Correct Answer: D (Other spouse)

Innocent spouse relief under Section 6015(b) requires the understatement to be attributable to erroneous items of the other spouse (the spouse from whom relief is sought). The requesting spouse must not have known or had reason to know of the understatement when signing the return. Relief is from liability for tax attributable to the other spouse's errors. The requesting spouse isn't responsible for their own errors.

87. Correct Answer: D (Separated or living apart 12 months)

Separation of liability relief under Section 6015(c) requires the requesting spouse to be either (1) divorced or legally separated from the other spouse, or (2) not living in the same household as the other spouse for the 12-month period ending on the date relief is requested. This relief allocates liability between spouses based on their separate returns as if they had filed separately. The allocation limits each spouse's liability to their own items.

88. Correct Answer: B (Economic hardship)

Equitable relief under Section 6015(f) is available when traditional innocent spouse or separation of liability relief doesn't apply but it would be inequitable to hold the requesting spouse liable. Factors considered include whether the requesting spouse knew or should have known of the understatement, whether they would suffer economic hardship if relief is denied, whether they benefited from the understated tax, and whether significant marital discord existed when the return was signed. The IRS considers all facts and circumstances.

89. Correct Answer: C (Separate debt)

Injured spouse allocation (Form 8379) applies when a joint refund is offset (applied) to satisfy the other spouse's separate debt—past-due federal taxes, state taxes, child or spousal support obligations, or federal non-tax debts like student loans. The injured spouse requests allocation of the refund based on each spouse's contributions (income, withholding, payments, credits). The injured spouse receives their allocated portion of the refund. This differs from innocent spouse relief (which addresses liability).

90. Correct Answer: C (Liability)

Injured spouse allocation seeks to recover the injured spouse's portion of a joint refund that was offset to pay the other spouse's separate debt. The injured spouse is not seeking relief from liability (that's innocent spouse relief)—they're seeking return of their share of a refund that was taken to pay the other spouse's debt. The distinction is critical: injured spouse involves refund allocation; innocent spouse involves liability relief.

91. Correct Answer: D (Appeals Officer)

Collection Due Process hearings are conducted by Appeals Settlement Officers (also called Appeals Officers or Hearing Officers) who are independent from the IRS collection function. The hearing is held by the IRS Independent Office of Appeals, not by IRS collection personnel, counsel, or revenue officers. The independence ensures impartial review of collection actions. Settlement Officers can consider collection alternatives, verify proper procedure, and weigh hazards of litigation in appropriate cases.

92. Correct Answer: B (Collection alternatives)

CDP hearings allow taxpayers to challenge the underlying liability (if they didn't previously have an opportunity to dispute it), raise collection defenses (such as innocent spouse relief, statute of limitations), and propose collection alternatives (installment agreements, offers in compromise, currently not collectible status, or bonds). The hearing provides a forum to resolve collection disputes before the IRS proceeds with levies or liens.

93. Correct Answer: C (Court review)

Equivalent hearings are available for taxpayers who miss the 30-day deadline to request a CDP hearing. Equivalent hearings provide similar review by Appeals as CDP hearings and allow proposing collection alternatives. However, equivalent hearings do NOT provide the right to judicial review in Tax Court—

that right exists only for timely requested CDP hearings. This distinction makes timely CDP requests valuable even when equivalent hearings are available.

94. Correct Answer: D (Taxpayer Assistance Order)

The Taxpayer Advocate Service can issue Taxpayer Assistance Orders (TAOs) when taxpayers are experiencing significant hardship or the IRS hasn't responded to their problems. TAOs can order the IRS to cease actions causing hardship, release levied property, or take specific actions to resolve issues. TAOs are binding on the IRS and provide emergency relief from IRS actions that would cause irreparable harm to taxpayers.

95. Correct Answer: D (National Taxpayer Advocate)

The Taxpayer Advocate Service is an independent organization within the IRS headed by the National Taxpayer Advocate. The NTA reports directly to Congress as well as the IRS Commissioner, maintaining independence. The NTA submits annual reports to Congress on the most serious problems facing taxpayers and TAS recommendations. TAS has Local Taxpayer Advocates in each state helping taxpayers resolve issues with the IRS.

96. Correct Answer: C (IRS grants)

Low Income Taxpayer Clinics (LITCs) provide free or low-cost representation to low-income taxpayers (generally those with income below 250% of federal poverty guidelines) in disputes with the IRS. LITCs also provide education and advocacy on behalf of taxpayers with limited English proficiency. LITCs are independent organizations (often operated by law schools, legal aid societies, or nonprofits) funded by IRS grants authorized by Congress. The grant funding ensures LITC independence from the IRS.

97. Correct Answer: B (Administration)

LITCs provide representation, education, and advocacy demonstrating the need for language access in tax administration. Many LITCs focus on serving taxpayers with limited English proficiency or who speak English as a second language. The language access work includes educating taxpayers about their rights, preparing materials in multiple languages, and advocating for improved IRS language access. This addresses barriers to tax compliance and dispute resolution for non-English speakers.

98. Correct Answer: A (Examination)

Fast Track Settlement provides expedited resolution using Appeals personnel while the case remains in the examination phase (before referral to Appeals). Both the taxpayer and examination team must agree to participate. An Appeals employee acts as mediator to help reach settlement. Fast Track Settlement resolves cases faster than the traditional Appeals process and reduces the backlog of examination cases going to Appeals.

99. Correct Answer: C (Willing parties)

Fast Track Mediation (FTM) is a voluntary program available after a case has been referred to Appeals. Both the taxpayer and the IRS/Appeals must agree to participate—it's not mandatory or automatic. FTM uses an Appeals mediator to facilitate resolution between the parties, typically within 40-120 days. The voluntary nature ensures both parties are willing to negotiate in good faith toward settlement. FTM is available for most cases in Appeals (not just small cases), but participation requires mutual agreement. The structured mediation process helps parties reach agreement while maintaining their control over settlement terms.

100. Correct Answer: C (Facts)

Arbitration in Appeals provides binding resolution of factual issues when the regular Appeals process cannot resolve a dispute and both parties agree to arbitration. Arbitration is limited to factual determinations—not legal or policy issues. An arbitrator (typically a neutral expert) hears evidence and makes a binding determination on the factual issue. The arbitration provides finality on disputed facts, allowing the case to proceed to resolution without protracted factual disputes.

